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Dear Peter,

"I tell you in all confidence that the Egyptian economy is not in an intensive care unit." With this rather dramatic statement president Mubarak opened the fourth annual National Democratic Party congress a few days ago. The NDP was founded by president Sadat in 1978 and possesses a virtual monopoly on political representation in Egypt. Political manoeuvring and clever election rules have kept the opposition parties reduced to a small - but growing - presence.

No one expected the congress to be anything more than a ritualistic gathering of party faithfuls. Its program had been prepared and announced in advance. The 4,500 attending NDP delegates obligingly raised their hands in approval of the various programs announced by the party leadership. A few foreign delegations attended the congress. Even the opposition parties had been invited to observe the proceedings. As far as I could see, none had taken the opportunity to do so.

As Mubarak's opening statement suggested, the central theme of the conference was the state of the Egyptian economy. The president was remarkably candid, almost refreshingly and often painfully so. This candidness has been Mubarak's trademark for the last few months. It seems as if after five years in office he has finally started to chart his own path. With his conservative pinstripe suite and silk tie he looked very much like a hardworking technocrat - an image he is trying to foster. There were no public adulation ceremonies of the kind Nasser and Sadat engaged in. Just business and, as Mubarak hinted at, not very pleasant business at that.

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By now I have attended about a dozen meetings within several ministries. The docility of the people participating in those meetings has always struck me. No arguments about proposed guidelines, no eruptions of anger. Especially no challenging of people higher up on the ladder. The same thing occurred at the NDP congress. The whole affair seemed carefully orchestrated, the "august gathering" (as al-Ahram called it) participating in a carefully designed show. Things might have been different within the committees where more concrete issues were discussed. Unfortunately no foreign journalists or academics were allowed to participate. But judging from conversations I had with people afterwards, I doubt there was any real difference here.

Despite these disparaging remarks the convention was an important event. The current five-year plan is in its final year and a new one has been announced. The congress was thus in part a stocktaking of Egypt's recent achievements, and in part the charting of a new course for the next five years and beyond.

Egypt's current economic position was summarized by Mubarak in his opening statement. The picture is bleak. Egypt's debt to foreign banks and governments stands at \$32.5 billion. The repayment schedule gobbles up almost one fourth of the country's yearly income. The public sector shows little signs of improvement. Productivity is often less than one percent. A new cement plant at Helwan, built at a cost of more than \$100 million, has already lost several million this year. And this in a country with a critical shortage of cement!! The agricultural sector continues to struggle along at growth rates of two percent. The population meanwhile continues to grow at 2.8% annually.

These are only some quick indications of where Egypt stands. Paradoxically, the country seems to have made progress these last years. For the first time telephones work more or less normally. International lines are becoming commonplace. At the Mugamma - where most tourists have to extend their visas - service has improved dramatically. Red tape has been cut. On a recent visit I only spent forty minutes getting my extension granted. I had been warned about spending hours at the place, having to run from office to office.

Consumer goods are in abundant supply at downtown stores. Even Cairo's legendary busses are less crowded. The government has introduced a number of "micro busses" that guarantee a seat and charge according to distance travelled. Perhaps the best news concerns a tentative indication that increasing numbers of well-educated Egyptians are coming (or staying) home. It is still too early to obtain hard figures, but Egypt's brain drain could be slowing down.¹

¹ During my visits to the General Organization for Physical Planning (where I have been working on some upcoming reports concerning Cairo's urban problems) I was struck by the large number of young male and female Ph.Ds and engineers. Many obtained their degrees in the United States. Several had deliberately chosen to work within government offices, despite

Many of these improvements, however, are only the icing on a cake that has gone stale. Many entrepreneurs are indeed making good money importing western goods. But as my telephone repairman observed, "just wait a couple of years until things start breaking down. Then Cairo will be where it was before." Perhaps not, but his comment hits upon some grain of truth. There is a level of mercantile economic activity going in Egypt that seems to indicate economic progress and that provides amenities to a greater number of consumers than ever before. Nevertheless, that group remains tiny in comparison with the total population. And beneath the growing consumption some of the lingering problems show little sign of improvement.

Mubarak's candor alone - no matter how refreshing - will not get the Egyptian economy back on its feet. Planning Minister Ganzoury recently said that Egypt needs four rigorous Five Year Plans that will bring the country into the 21st century as a regional economic powerhouse. How far Egypt will go toward that goal depends not only on local measures. Cooperation from the West, particularly the United States, will to a large extent determine how successful Egypt will be.

I have written in my first report on the economic legacy of Nasser and Sadat. It needs no repeating here. Until now I paid little attention to what one high USAID official described to me as the "passive nature" of the economy. He referred to the fact that Egypt's economy depends to a large extent on revenues that contribute little to the country's productive capacity: oil revenues, receipts from the Suez Canal, money earned by Egyptians working in the rest of the Middle East, and tourism.

In 1980 these four sources of income provided more than half of Egypt's revenues. Since then the situation has changed dramatically. This year's oil revenues will be at least \$1.2 billion lower than last year's. Tourist receipts have plummeted. Official estimates of earnings from Egyptians working outside Egypt were \$3 billion in 1984. Unofficial estimates run 2-3 times as high. At that time an estimated 3 million Egyptians worked outside the country. As many as 2.2 million may return

more lucrative offers in the private sector or outside Egypt. One reason was the security of government employee benefits and pensions. I talked to one young woman for example, whose salary within GOPP was half of what she had made previously in a private sector company. I found this rather puzzling. She explained that the government job would provide her with employment for the rest of her life, subsidized transportation, and a number of other social provisions. Working for the private sector company she enjoyed none of the latter and could be fired at any time. In complete contrast to the entrepreneurship so glorified in the United States, she asked "Why not take what you're sure of, even if you make less money?"

Another explanation for the greater number of Egyptian professionals staying home is the decreased demand for their services throughout the Middle East and the Persian Gulf. A third reason - admittedly the least prevalent in my very small sample - was a genuine desire to help Egypt overcome its economic difficulties.

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over the next five years, victims of reduced development budgets or of infrastructures that are now finished within the host countries. It may mean an annual loss of \$2-8 billion, depending on whose figures you use. Projections for the Suez Canal show only small increases over the next few years.

It is clear that if the government is to continue with the economic philosophy it now embraces - and there are no indications so far of any change of mind - then the economy will need some particularly painful adjustments (see, for example, DJV-2 on subsidies). Although Sadat's infitah continues in name, there is now a major difference: The price of the economic experiment of the 1970s will have to be paid. Consumerism will have to yield to substantive economic change. Faced with both these old and more recent problems, Egypt cannot turn the tide by itself. The situation is simply too desperate. The country may not be in the intensive care unit. But it will need careful monitoring of its economic pulse.

Who the doctors will be also seems reasonably clear: the IMF and the small cluster of western banks from whom Egypt will need to borrow more money. Three interrelated problems are now being discussed. How much money will be channeled to Egypt? Under what rules and stipulations will the money be handed over? Finally, for what projects will the new capital be put to use? On all three questions the Egyptian government and the Western creditors disagree so far.

Mubarak's advisors dished up some tentative solutions at the NDP congress. But it is clear that Egypt finds itself in an extremely weak position to make demands. In several ways the two weeks leading up to the NDP congress had already set the parameters of any eventual bargaining between Egypt and the West. Claude Cheysson, the EEC Commissioner for Mediterranean Policy, had arrived in Cairo for a three day visit. The message he brought could not be misconstrued. Europe was willing to continue its extensive aid program to Egypt. Egypt, however, would need to take drastic action to bring its economy in line with IMF demands. Coming at the eve of the renewal of the third Egyptian-European financial protocol in October this year, the call for action carried extra weight. There was also the added problem that Egypt had requested greater access to IMF facilities and needed European support to do so.

Europe was obviously worried about the slow reforms taking place in Egypt, and about some of the lingering problems I mentioned earlier. The message was seemingly worrisome enough to persuade president Mubarak to undertake an unscheduled 36 hour whirlwind tour of the four most important European capitals.² The message from Italy, France, Britain, and Germany was unanimous. Europe fully understands the difficult situation Egypt finds itself. It considers Egypt a valuable partner within the Middle

² Al-Ahram initially called the Mubarak visit "unscheduled." Two days later, when the opposition papers had started to talk about "caving in to foreign pressure" it reported that it had been "planned long in advance."

East. But Egypt will have to push more forcefully for changes within its own economy...

Since that time a certain uneasiness existed among Egyptian officials. Both Mubarak and his advisors consider IMF loans indispensable to get Egypt over what they consider a short-term economic crisis. But they are also aware of the political ramifications of rapid economic reforms.

The position of the United States was thus crucial to Egypt. Not only could it facilitate access to IMF funds, but the US could extend bilateral aid to provide a cushion against the demands of the Europeans. For these reasons the visit by Vice President George Bush was eagerly (but anxiously) looked forward to by officials here. For a few weeks the capital was full of rumors concerning his upcoming talks with president Mubarak. In some of my interviews these last weeks the person being interviewed often turned the tables around, asking me what I thought Bush would have to say?

The Bush visit was expected to resolve three problems: A statement on the whole IMF question, the future of the USAID program in Egypt, and the future of the Egyptian military debt to the United States. All three are closely interrelated.

It was clear from the beginning that the IMF issue would not be addressed. No agreement had yet been reached with the Europeans. The USAID problem is a particularly vexing one. Since the Camp David accords in 1979, the United States has annually given almost \$1 billion to Egypt.³ Most of it comes with strings attached. The Egyptian government has consistently asked that the US would simply hand over the money - as it does to Israel - and let the Egyptians decide how it should be used. The US has been reluctant to do so. One angry Egyptian official once asked me "Why should we be saddled with 150 USAID officials who tell us what to do while Israel has only one person to guide their program?"

The rescheduling of Egypt's military debt was perhaps the most pressing issue. It had been one of the major topics when a top level Egyptian delegation visited Washington a couple of months ago. Egypt owes the United States \$4.6 billion for purchases of military hardware. Most of this was bought during the middle and late seventies when interest rates were high. It is now repaying the loans at rates of 12-14%, plus a 4% penalty for being a year behind schedule. This year Egypt needs to come up with \$554 million, most of it for interest payments.

The Egyptian government has asked the US to turn over this debt to commercial banks. There it could be refinanced at rates perhaps as low as 7%. This would save Egypt several hundred million dollars. Washington has been reluctant to consider the proposal. A commercial refinancing of this kind is a precedent-setting arrangement. Officials are worried about Sudan, Morocco, and a number of other countries asking for similar settlements. Nevertheless, Egypt's leadership hoped that Bush would have a positive answer to relay to them.

I attended Bush's press conference, also hoping to hear some news on

³ I will write in greater detail on USAID in DJV-5.

these three issues. It was a disappointing event. The vice president was primarily interested in reaching an agreement on Taba, the disputed sliver of Sinai that remains a bone of contention between Egypt and Israel. The press conference was even delayed for a couple of hours in the hope that he would be able to announce the breakthrough.

In any event the economic issues were barely raised. The United States was "interested in Egypt's solvency" and in this "most urgent economic situation" Bush said. But there had been no progress on the military debt rescheduling or any other economic issues.

Egyptian reaction ranged from "disappointment" in the official press to downright outrage in the opposition papers. The latter declared - not completely without foundation - that the vice president had used the trip as a piece of propaganda in his run for the presidency.

It is perhaps still too early to draw any hard conclusions from the visit. Many of the statements may be modified as the vice president confers with president Reagan and State Department officials. A couple of issues are nonetheless clear. A consensus has been reached within the US about what Egypt should do concerning its economy. That consensus coincides closely with the European one Claude Cheysson laid out during his visit, and with some of the conditions contained within IMF guidelines. The Egyptian economy will have to be streamlined.

Secondly, I detect no long-term US strategy to deal with Egypt's economic problems. For once I agree with Planning Minister Ganzouri that Egypt desperately needs a strategy until the end of this century - and that the strategy will require large sums of money. This is an extremely sticky point between Egypt and its creditors. Boutrus Boutros-Ghali, Minister of State for Foreign Affairs and Esmat Abdel-Meguid, Foreign Minister, have repeatedly called for a Marshall plan for Egypt and the Middle East. Washington rightly points out that the US has spent twice that amount in Egypt since 1975.

If the US is really interested in Egypt as a regional ally, however, it has little choice but to spend even more money. Ganzouri, Boutros-Ghali and Abdel-Meguid are at least correct in pointing out that solving Egypt's ills will take many years, enormous amounts of money, and active involvement by the United States.

Egypt faces a number of problems it seems unlikely to solve by itself. The country is just at the beginning of a battle for efficient use of water. It shares the Nile with nine other African countries. By the year 2,000 there will not be enough water to support Egypt's population (which will at a minimum be 70 million) and those of the other countries. Under a 1959 Sudan-Egyptian agreement Egypt is allotted 55.5 billion cubic meters annually. Until now it has used substantially more, in part because Sudan has not drawn its share. This is now coming to an end. There are further worries that Libya's efforts to channel water from its southern desert is lowering groundwater levels in Egypt. Water may well be Egypt's greatest challenge in the years ahead. It is a challenge that can only be solved through regional cooperation, and one that may well need an international sponsor.

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A prominent leftist intellectual I conducted several interviews with remarked bitterly: "The United States accuses us of running from crisis to crisis. But what do they do? Do they have a strategy to deal with Egypt beyond the yearly USAID hand-outs? Have you noticed any commitment to this country's long-term interests? If we're such an important regional ally as they claim, why are we treated like this?"

But concerns about Egypt's future have an internal dimension as well. For most poor and middle-class Egyptians the question is not how well the economy has done (or will do) as a whole, but how it affects their lives directly. And here the picture is remarkably more murky. I have mentioned some economic aspects of this in my first two reports. The political aspects are equally important. The type of economic actions the West is expecting Egypt to take will hurt the lower income groups, and political turmoil will undoubtedly take place from time to time.

Mubarak calls himself committed to democracy, but it a democracy in which tapped telephone lines are still largely present and where opposition papers have no access to the daily television reviews of the press. Despite his assertions that the NDP is firmly in control, the cooperation between muslim fundamentalists and the New Wafd may well be more of a threat than Mubarak admits. The fundamentalists have slowly invaded the other parties. There is a gradual acceptance of a greater level of "muslim identity" within Egypt's political life. Even Adil Hussein, editor of the influential leftist As-Shaab now claims that Islam and socialism can develop side by side.

The specter of radical fundamentalism^{however,} has largely disappeared in Egypt. It was debatable whether it ever existed at all - except on the frontpages of news hungry western newspapers. The idea of a Khomeyni-style take-over in Egypt remains extremely remote. Even those who actively subscribe to the so-called radical Islamic position in Egypt see little point in the type of action taken by Islambouli when he assassinated Sadat. For a short while Sheikh Salama or the blind Sheikh Abdulhamid Kishk were thrown up as possible candidates for such a role. But since that time events have clearly shown that neither men possessed the stature to lead a mass movement. And Umar Tlismani of the Muslim Brotherhood, perhaps the only group that could seriously challenge the government, has been replaced by a new leader who also stresses a non-confrontational approach.

If February's rioting of conscripts of the central security forces reiterated one thing, it is that the army remains the power-broker in Egypt. Abdul Halim Abu Ghazala is currently the heir apparent. He is known to be both a canny and ambitious politician, and recently turned down the post of vice-president which would have removed him from the defense ministry. The power of the army is further attested by the amenities it is provided with. Never in its history has the Egyptian army been so well dressed and so well fed, not to speak of the subsidized housing and duty-free facilities it now enjoys. And, perhaps because of the bad state of the economy, the army is increasingly used by the government as contractors for infrastructure projects within the country..

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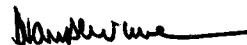
While the security forces are being revamped, Mubarak has little choice but to rely on Ghazala and the army if further disturbances take place. Whether or not they do occur will depend largely on what happens to the economy. Until now president Mubarak has been careful to "pay off" different groups whenever disturbances occurred. In the last three months labor disturbances at Mahalla al-Kubra and a machinists' strike in Cairo were settled by meeting some of the demands of the strikers. But how long can the government afford to do this?

An enormous amount of money will be needed if Mubarak can continue to be successful. Fortunately he is less tainted by connections to infatih riches than Sadat was. The removal of a number of Sadat's more notorious ministers from government was a good sign. But if his call for a renewal of Egypt's agriculture, for example, is to be even partially successful, economic assistance will be needed. The same goes for transportation and housing. The challenge for the United States and Europe will undoubtedly be to put extremely large amounts of money to good use in a region that will continue to be desperately short of capital.

I am not very optimistic that this large task can be carried out. I think there is something to the charge made by the leftist intellectual that donors as well as receivers hobble from crisis to crisis. I am particularly dismayed by the cynicism and pessimism of many of those responsible for carrying out the programs that now provide Egypt with much of its foreign aid. George Bush's visit was one more small indication, perhaps not even a relevant one, of how problems are tackled.

Not surprisingly, little was accomplished at the NDP convention. Hemmed in on all sides, Ganzouri, Mubarak, and Prime Minister Lutfi were waiting for a clear message from the United States. That message still has not arrived.

All the best,

A handwritten signature in black ink, appearing to read "Dan P. ...", written in a cursive style.

Received in Hanover 8/20/86