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INFITAH AND THE MODERNIZATION OF EGYPT

CHRIS MONSON*

Introduction

At the secondary school, I came to realize for the first time what city dwellers were and what class officers meant. . . . My classmates were naturally better dressed than I was but I never suffered because of this. Many of my friends came from wealthy families and lived in luxurious houses, yet I cannot recall ever wishing to possess what they had.

--Anwar el-Sadat

This early memory, in contrast later with Sadat's aggressive wish for foreign investment, is characteristic of the change that not only influenced the career of the late President Sadat, but also the change of a country. This change became known as infitah. The term infitah (Arabic) means reaching upward and outward. It became the term commonly used for the "1974 October paper" in which Sadat offered an economic cure for the ills of Egypt. Infitah--the Open Door Policy--described a post-socialist policy, an opening up of the Egyptian economy to direct private investment. This paper does not try to reconstruct the policy in detail, but rather

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it focuses on the effects of such a policy—more specifically, the impact of infitah on the modernization and economic development of Egypt during Sadat's Open Door Policy era of 1974-1981.

Development can be very difficult to define precisely. However, in focusing this discussion, the following definitions are offered as a guide to the reader: Development is defined as the capacity to stimulate demands and to solve problems based on the effective use of new technology, skill, and functionality. Modernization, a subset of development, is the actual formation of new adaptive roles in a system to prevent a population—that has tasted the fruits of development (technology, skill, and functionality)—from slipping backwards.

Once modernization has begun, it tends to become a pervasive, disruptive, and painful process. As a result, those who lead out and push for modernization often lose the ability to control and regulate this process. The intent of this paper is to illustrate the inability of the Egyptian government to change to new adaptive roles to assimilate and properly absorb the great influx of technology and industrialization resulting from infitah.

Because of the broad nature of this topic, discussion has been limited to three general sectors: effects upon (1) agricultural development, (2) industrial/manufacturing development, and (3) trade and financial development. A basic assumption is made that most of the economic influence during the period of 1974-1981 has come from the West, although other influences certainly have been present from Arab and Eastern Bloc countries. It is not the purpose of this paper to discuss the political nature of leadership, the Camp David Peace Treaty, or the sale of military arms.
Background

The formal adoption of the Open Door Policy (infitah) was not forced upon Egypt by capitalistic investors nor by international Western creditors. The Policy was chosen in light of internal economic and external political factors. Sadat's own words best describe the seriousness of some of these factors:

So that I can give you an idea of what the opening is all about, I must go back to the fourth of Ramadan of last year [October 1, 1973], six days before the battle. I invited to this same house in which we are now seated the members of the National Security Council . . . and I laid before them the situation and asked them to advance their own opinions. . . . We debated for a long time. There were some who advocated fighting, and others who said we were not ready. . . . At the end I said that I wanted to tell them one thing only, that as of that day we had reached the "zero stage" economically in every sense of the term. What this meant in concrete terms was that I could not have paid a penny toward our debt installments falling due on January 1 [1974]; nor could I have bought a grain of wheat in 1974. There wouldn't have been bread for the people, that's the least one can say. . . .

In addition to these problems, Egypt was at that time, and still is, plagued by a serious population explosion. Every 20 seconds an Egyptian baby is born; 180 every hour; 4,320 every day. There are currently over 46 million people in Egypt. Current fertility rates continue to grow at 3 percent per year, and it is estimated
that by the year 2000 there will be over 76 million. Sadat undoubtedly understood the magnitude of such a problem and realized that foreign investment and aid were the best alternatives. The announcement of the Open Door Policy in 1974 provided relief from the country's failure to achieve a truly socialist economy.

External political factors also added pressure to change and to open up to outside investment. Egypt could not afford another war and Western aid remained tied to promoting a peaceful dialogue with Israel. Thus we see the Camp David accords emerging as a partial result of the need for (the Open Door Policy). Western aid and investment.

Now that a brief setting has been established for infitah, an outline of what the policy actually is will be helpful.

Infitah--The Open Door Policy

a. Law No. 43 of 1974

• provision for opening the Egyptian economy to foreign and Arab direct investment in almost every field.

• provision against nationalization and confiscation.

• tax exemption that lasts for five years, and which may extend to eight years "if warranted by public interest"; and a 10-year tax exemption, which may extend to 15 years, for reconstruction projects.

• companies established under this law are considered private companies.
b. The new import-export law of 1975

- provides for the importation of certain goods to be open to the private sector as well as to the public sector.

- machinery, equipment and raw materials—the basic items of any investment program or development plan—are now imported by the private sector.

c. Foreign Exchange Law No. 97 of 1976

- provides for the liberalization of foreign exchange transactions outside of Egypt.

- freedom to keep the foreign exchange acquired from any source whatever.

d. The own-import system

- provides for anyone who has foreign exchange resources to use them to import directly, without having to go through the Egyptian banking system.

e. Phasing out of bilateral trade agreements to allow market forces to dominate in shaping the foreign trade picture.

f. Restructuring the public sector so that public organizations are abolished to make way for private enterprise capitalism.
Agriculture

The Open Door Policy has caused some drastic changes in the Egyptian agricultural sector. When investment regulations relaxed for many of the sectors of the Egyptian economy, both foreign and domestic investors shifted to those areas that would bring them the highest return. This caused both public and private investment in agriculture to fall from about 25 percent in the mid-1960s to an estimated 7 percent in 1977. Agricultural investment did not actually decrease in dollar amount; it just did not get a very large share of the millions as compared to other sectors. This was far from the mid-point projected goal of 13 percent to be invested in agriculture (according to Egypt's 10-year plan, 1973-1982). World Bank average annual growth rate indicators reveal the effects of this change in another way: From 1960-1969 the growth rate for agricultural production was 2.9 percent, contrasting a drop to 2.7 percent for the period of 1970-1979. The slide in Egyptian agriculture became apparent in 1974, when the government was forced to embark on a major food importation program.

Although the total amount of agricultural investment as a percentage had dropped, as just mentioned, the total dollar amount still increased significantly. But the Western-invested increase yielded lower production. Chiefly to blame was the low agricultural investment level. The Open Door Policy lured investors away from agriculture and into the more profitable sectors of tourism and industry.

To meet the demands of over 45 million people, Egypt has had to increase both food imports and food subsidy aid from Western countries. The pressure on farmers for results is very real: Self-sufficient less than 10 years ago, Egypt now has to import half of its food, at an
estimated cost in 1983 of almost $4 billion. As well as injecting more funds, the government has recently raised producer prices for corn, rice, and wheat, thus reversing a years-old policy of forcing farmers to sell their crops at less than market prices to provide city dwellers with cheap food.

However, such innovations have come a little too late to provide incentive for the struggling farmer. For example, government subsidies provide a price monopoly controlled by the government that forces farmers to keep their prices competitive. In a recent 10-year period (1971-1980), profits decreased substantially for farmers raising crops that were heavily subsidized to the public. The net effect has been that some farmers have turned to more profitable crops like fruits, vegetables, and animal fodder (clover), while other farmers have given up and migrated to the urban centers for different employment. Over a period of 10 years (1971-1980), animal fodder alone replaced wheat in crop area as much as 32 percent.

The mechanization of farms has also had both good and bad effects. Since 1973, the Open Door Policy has caused tractor imports to quadruple. Some areas have almost completely done away with old methods. In the Sharqiyya province, land preparation and threshing are almost entirely mechanized; plowing is over 85 percent mechanized and irrigation pumping nearly 75 percent. There is no question that such technical change brings about important benefits; yet, statistics show that land yield has not increased.

The impressive mechanization statistics do not account for the lack of spare parts, mechanics, and repair shops in rural areas. There is a general shortage of spare parts, and local manufacturers do not maintain an inventory of parts, but manufacture them on demand. As a result,
farmers often wait three to six months for repairs. Farm animals continue to provide a kind of insurance for equipment. In addition, the working of dairy animals reduces the yield on dairy products that mechanization had hoped to increase.

Yield gains as much as 15 percent were expected from deeper and better ground tillage from mechanization. However, at the present, farmers plough no deeper with tractor ploughs than they do with animal ploughs. Furthermore, mechanization was to intensify the timing of crop planting to obtain the ultimate yield, but low price policies currently push 25 percent of crop production later than its optimal planting time in order for farmers to get the best price return for their crops.

The severity of these facts is intensified by the fact that Egypt's population has more than tripled in this century alone, yet the area of cultivated land has remained by and large the same. In many areas prime farmland continues to lose out to urban and village sprawl. Still to be resolved is the argument of whether to concentrate on traditional farming lands along the Nile and in the Delta, or to broaden into costly land reclamation. A report submitted by the Ministry of Agriculture and Food Security in 1982 concluded that agricultural output could be tripled by the year 2000 through better use of traditional lands; many senior planners, however, seem reluctant to relinquish the Sadat Administration's dream of massive desert conversion. In the 1960s more than 900,000 feddan (934,200 acres) were reclaimed—at an average cost of $4,000 per feddan—but much of this has reverted to barren desert. What remains constitutes 13 percent of cultivated land, but accounts for only 2 percent of total output.

The Egyptian Ministry of Planning estimated that more than a million extra tons of wheat and
over half a million extra tons of rice and maize would be needed per year by the mid-1980s. This is expected to increase demand for imports from the West. It has been estimated that grain production alone fell about 4 percent per capita during the 1970s, while grain consumption rose per capita almost 9 percent. Unless this trend can be contained, mechanization will be plagued by the increased pressure of the one million new mouths to feed every eight months. Whatever the answer—and it is not likely to be self-sufficiency—time is not on the Egyptian farmer's side.

Industry/Manufacturing

Western influence on industry and manufacturing grew to new heights when Open Door Policy Law 43 was passed in 1974. This new policy allows foreign firms to bring in equipment without having to pay a tariff. Other incentives under Law 43 include customs yields and 10-year tax holiday concessions to foreign firms that link up with Egyptian partners. By 1980, new foreign private investment (majority Western) reached about $400 million a year, compared with $100 million just three years earlier. In addition to private investment, economic assistance by governments and international organizations have played a significant role. For example, in 1980 the United States contributed $1.2 billion, the World Bank fund donated $450 million, West Germany contributed $150 million, and Japan funded $170 million. This aid, totalling nearly $2 billion per year, has given rise to a rapid industrial-manufacturing boom overlapping into all the economic sectors of the country. The soaring investment and aid have produced impressive production indicators. The average annual growth rate for industry has risen from 5.4 percent in 1960-1969 to 6.8 percent in 1970-1979. Manufacturing has even greater results: 4.8 percent in 1960-1969 to an average annual growth
rate of 8 percent in 1970-1979. The growth in industry also has a considerable effect on labor statistics. By 1980, industry and manufacturing were employing over 30 percent of the Egyptian working population. That amounts to over eight million jobs.

In addition to this, over 1,000 new projects are scheduled to go into operation by 1984, employing an additional 160,000 Egyptians. More than 200 American companies have a corporate presence in Egypt, with an addition of 50 firms per year.

Despite all this, however, the payoff from the Open Door Policy hasn't been as large as Sadat would have liked. Although the midpoint goal for private investment under Egypt's 10-year plan ($400 million) has been realized, many companies are beginning to be frightened off by bureaucratic bottlenecks. Realizing this potential bureaucratic paralysis, Sadat created the Investment Authority to encourage foreign investment by coordinating intra-government efforts. But the task has often become insurmountable. The government has over 20 ministries whose functions overlap. This creates occasional inability of government organizations to honor commitments because of unclear lines of authority and competing inter-agency interests and policy claims.

Such power struggles are extremely damaging to the government's credibility in foreign eyes. For example, one large U.S. company considering a tomato processing joint venture was told by Agriculture Ministry officials that the public sector was the only avenue open to the company. Government policy, it was later discovered, favored private sector joint ventures. The Agricultural Ministry had taken the initiative to promote a public joint venture that was to its advantage, leaving the investor with misplaced directives.
Another critical area of bureaucratic paralysis in which the battle is not yet won—or even properly engaged—is with the customs authority. Approximately 90 percent of the country's imports arrive through the port city of Alexandria. There are three competing bureaucracies governing the import and export of goods: the Finance Ministry, which formulates tariffs and is responsible for classification; the Investment Authority, which negotiates Law 43 exemptions; and the Customs Service, which often ignores both the Finance Ministry and the Investment Authority, and interprets the regulations as it sees fit. Although Law 43 specifically states that foreign firms may bring in plant equipment without paying any tariff whatsoever, customs officers have been known to routinely say: "I do not recognize that interpretation; those who do not pay the required fee will see their equipment collect dust on the pier."  

The greatest problem the potential investor meets is finding a clear authority with which to deal. The General Authority for Investment and Free Zones, under the supervision of the Ministry of Economy, is supposed to have the last word on conditions under which foreign companies operate in Egypt. However, the foreign company must also have its project approved by the ministry directly involved in its activity. For example, the Ministry of Industry competes constantly with the Ministry of Economy for decision-making power. Although there continues to be more coordination at the cabinet level, these two ministries and others continue to pull in different directions when it comes to deciding how and with whom a foreign company should operate.

The Egyptian ministries have to deal not only with pure industrial assembly line companies—such as Ford, Xerox, and Coca-Cola—but also with the even more imposing growth in the closely related tourism and construction indus-
tries. Statistics reveal that although pure industry and manufacturing annual growth levels are impressive, growth in the service sector (tourism) is the highest of all. Service sector production for 1960-1969 was 4.7 percent, while in 1970-1979 it rose to 11 percent—the largest growth rate of all sectors. It came as no surprise that Western investment sought out the most financially attractive projects. By 1977, over 25 percent of foreign investment was in housing, tourism, and construction—well above any percentage for industry. It was argued that luxury housing was an essential means of attracting foreign currency (tourism). However, the surge by the West in luxury construction has had some far-reaching side effects.

First, powerful developers have obtained priority on building materials and have absorbed the already-low supply of materials for their luxury projects. Regular housing project developers, who were assured by the government that luxury construction would not be importing most of their supplies, are continually cut out of business because of the shortage. Thus, luxury construction for the few is built at the expense of regular or economic housing projects for the many. Second, large-scale building projects have caused substantial price increases for middle-income housing, creating a greater shift toward demand on rent-controlled housing for the poor. Both these factors compound a serious housing shortage for Egypt's urban population explosion. A walk through the streets and hotel lobbies of Cairo reveal the seriousness of the housing shortage. For example, an early-morning departure from a Cairo hotel will discover the sleeping bodies of homeless porters, busboys, clerks, and cooks strewn across the lobby floor.

Lack of skill and the inability to adapt to modern manufacturing methods is another problem resulting from rapid modernization. A look at the
Egyptian textile industry provides a clear example of this dilemma. Egypt's long-time staple, cotton, is of very high quality and is exported for its use in high-quality fabric at an extremely favorable rate for the economy. The main input for Egypt's textile factories is the same high-quality cotton. Domestic textile plants as of yet have not been able to manufacture more than a course-grade product. Western technology has been hampered by the low training capacity of laborers. Textile manufacturers also suffer from excess waste during the production of combed yarn: as much as 20 percent per year is lost because of incompetent laborers, though inadequate supervision and negligence on the part of management have also been blamed.

An additional problem the newly developing Egyptian economy has to battle is inappropriate technology. Relaxed import rules from the Open Door Policy have brought thousands of goods into Egypt that are too sophisticated for the average consumer. This problem has brought about the creation of Egypt's Engineering and Industrial Design Development Centre (EIDDC). EIDDC redesigns products to find a balance between sophisticated, imported Western technology, Egyptian industry, and local demand. The head of Egypt's EIDDC, Yusef Mazhar, gives the following useful example:

... take the fully automatic washing machine found in most Western homes. In Egypt, this machine is impractical. It costs $1,000, a sum probably equivalent to the annual salary of a typical middle-class worker. Coupled with the drawback of high initial cost, are the inevitable problems of improper maintenance and scarcity of spare parts generally found in developing countries. These mean that the
washing machine is likely to remain idle for long periods of time.

More significant, however, is the fact that the fully automatic washing machine is too sophisticated for the Egyptian market. The Egyptian housewife does not have the problem of trying to save time and effort like her Western counterpart. Very few need a washing machine that they can turn on when they leave home in the morning and empty out when they return home.

Instead, with time to spare and different life-styles... the washing machine designed by EIDDC... carries out the same cleaning functions as its Western equivalent. But nothing on it, including the water supply, is automated. It doesn't matter that a maid has to pour water into our washing machine with a bucket. It achieves the same result... at less than one-fifth the initial cost.26

Another example illustrates this point in yet another way. A large Egyptian firm assembling buses under license from a West German company wanted to subcontract seats locally rather than have the seats imported. The design called for more than 350 individual parts. However, the bus firm could not find anyone in Cairo capable of the task. EIDDC took the plans and came back with specifications reduced to 60 parts. The seat was then able to be produced locally as were other parts.27 Although these examples shine light on the problem of inappropriate technology, they are but a small dent in the vast amount of potential products that could be manufactured in Egypt.

Just before his death, President Sadat expressed the dream that he would live to see the day when every product sold locally bore the
label "Made in Egypt." The late President's dream still remains, on a large scale, highly unreachable in the near future. Ironically, President Sadat's Open Door Policy fuelled consumption and encouraged imports to the point of discouraging the possibilities of large-scale local production. Goods and products manufactured in highly-skilled foreign markets were more profitable for investors.

Trade and Finance

This section will highlight some of the dilemmas not previously discussed and then bring together the two main arguments against liberalization of trade.

The implementors of the Open Door Policy have realized by now that they are involved in a far more difficult and sophisticated process than originally anticipated. For example, the exchange rate policy, designed earlier to shelter industrial development and to protect consumer prices, had to be changed to clarify price signalling. Interest rate policies, which had been tailored to direct resources toward favored economic sectors, needed reconstructing to promote domestic savings and to distribute capital more competitively. Tax policies had to be revamped to provide necessary equity protection during changing economic incentives. The interrelationships of public and private sector investments became more complex as the private sector was stimulated toward direct competition with the already-defensive public sector.

The ability of Egyptian economic leaders to manage this transition has also been inhibited by inflation, lack of training and background, and pressure from the lack of infrastructure development in the past. The government has sought to protect the public from inflation to the greatest
possible extent using price controls. However, the steep rise in the costs of goods, and the increased demand for them, has placed a great burden on the Egyptian budget. For example, subsidies for basic commodities--less than $300 million in 1973--reached over $1,500 million in the 1980-1981 budget. (This exceptional rise in budgetary outlays for subsidies was also affected by a 56 percent devaluation of the exchange rate in 1979.)

While this huge subsidy outlay has partially helped the public, it has created large budget deficits and important increases in the money supply. This in turn has led to inflation in prices of non-subsidized goods. Official price indexes show inflation at about 15 percent, but most observers estimate that prices of non-subsidized goods have increased by about 30 percent annually.

However, one factor has given Egypt more flexibility in managing the economy: an improvement in foreign exchange. Debt servicing costs were eased by Arab nations and at the same time disbursement from the West provided more of a cushion. Earnings from foreign workers, Suez Canal revenues, and tourism have provided a surplus in the balance of trade for the first time in two decades. Egypt's trade balance went from a deficit of $1.5 billion in 1976 to a slight surplus in 1980.

Although the trade statistics offer hope to Egypt's economy, the two basic problems of trade liberalization resulting from the Open Door Policy have taken their toll. First, Open Door trade has had an impact on national industry and massive consumption. Second, Egypt has been reduced to a country with debts and deficits subordinate to the dictates of others, such as the International Monetary Fund (IMF).
In reference to the first problem, the new laws resulting from the Open Door Policy have had drastic effects on the consumption of local products. The intervention of the government in the national tire industry is a perfect illustration of this problem with trade liberalization. Local tire industries in Egypt had previously met the requirements of domestic consumption and had a decent volume of exports when surpluses materialized from new import laws in the mid-1970s. The public sector became overstocked with tires. The new capitalist doctrine of the Open Door Policy further tempted government ministries, looking out for their self interests, to use foreign loans to buy imported tires (in this case from Japan). Thus, in 1978, only one-half of the local tire production was sold.

Consumption has been tampered with to the detriment of Egypt's economy as well. Products imported under the new trade concessions were largely of the type motivated by high profits. These products would include more of the luxury type than the necessary. To state this another way, a highly developed country may indeed agree to a trade relationship with a poor country, whereby the poor country buys a much-needed commodity (such as wheat), or may even be offered such a commodity as a free gift. But this would be attractive for the developed country only if the poor country proves to be a "good customer" and is ready to buy large quantities of a commodity the seller finds advantageous (beer, automobiles, cigarettes, tires, etc.). This situation is like a store that offers free a useful but cheap item if customers would buy a certain quantity of a much less useful but expensive item. It would be foolish in such a situation to expect to get the free gift without accepting the other part of the transaction.

The impact of the second problem, a country with deficits being subjected to the power of its
creditors, has had its far-reaching effects. Indebtedness has reached a disturbing level in Egypt. In 1982 alone, the external debt grew by 18.6 percent. This figure is dangerously high for a country that has a debt/export ratio above 200 percent.

To manage their debt problems, Egypt has had to trim unnecessary imports and expenditures. The following example provides a good illustration of how pressure from creditors (like the IMF) to cut expenses can be very hard on a country: By 1980, one of Egypt's major expenses was the food subsidy program. The program cost $1.7 billion—an amount equal to Egypt's 1979 budget deficit, or over 10 percent of the GNP. To make any small change was extremely difficult. Even with the food subsidies, most Egyptian families spend between 70 and 80 percent of their income on food. In January, 1977, the government attempted to reduce subsidies (raise prices) on flour and some other foods because of pressure from the International Monetary Fund (IMF), the U.S. government, and private American banks to demonstrate financial responsibility. Immediately the streets erupted in violent riots, killing 80 people and wounding over 1,000.

Conclusions

In contrast to his early days as a poor village schoolboy, Sadat rose upward and outward from his submissive attitudes toward wealth. Infitah—upward and outward—became the symbol for a national struggle: the economic development and modernization of Egypt.

Egypt is in the process of important and dynamic change. It has set out on a course of fundamental restructuring of its economic future. While important steps are being taken with some positive results, much remains to be done. Egypt
has discovered that this change is often painful and disruptive. It is always easier to generate change than to absorb it.

The most serious problems are internal: inefficient bureaucracy, inappropriate technology, lack of incentives for agricultural production, population explosion, etc. It can be assumed that there will always be a gap between the demands that accompany modernization and the political system's ability to satisfy those demands. Egypt certainly has this gap and must resolve many critical issues if progress is to be maintained and intensified. By allowing or encouraging the society to wholeheartedly take on capitalistic values and consumption habits without adjusting them socially and economically will likely lead to cultural impoverishment.

By defining development in terms of a capacity to stimulate demands and solve problems, Egypt's Open Door Policy has not been effective. Egypt needs to change to new adaptive roles to assimilate and properly absorb the great influx of technology and industrialization resulting from infitah.
ENDNOTES


9 Ikram, p. 208.


11 Ibid., p. 416.


16 World Bank, p. 112.

17 Ibid., p. 146.


20 Ibid., p. 74.


22 World Bank, p. 112.


24 Observations from a personal trip by the author, Chris Monson, to Cairo in February 1982.


27 Ibid., p. 37.


30 Ibid.


32 Tinnin, p. 74.


35 Thurgood, p. 28.

36 Bednar, p. 9.
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