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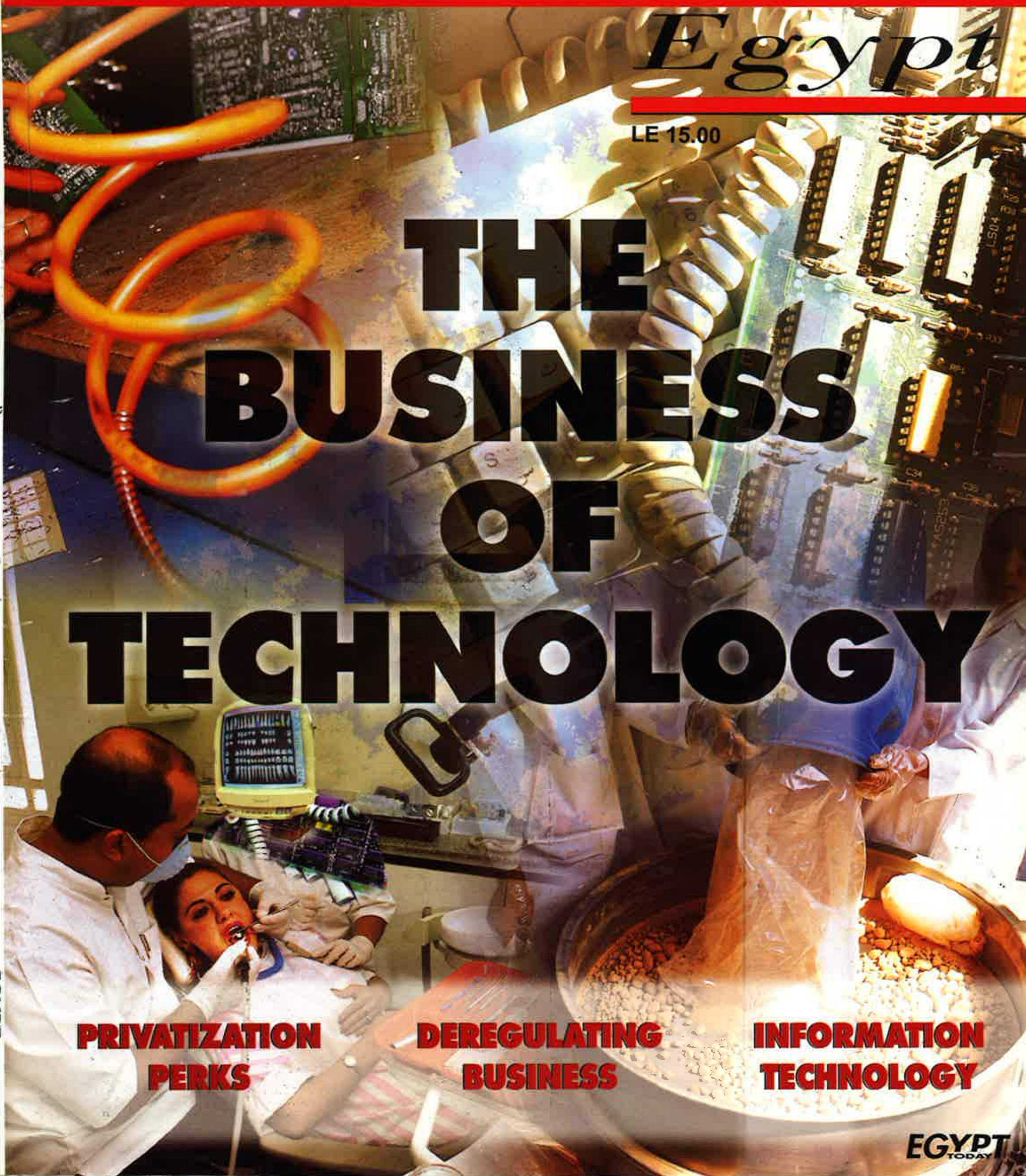

THE BUSINESS OF TECHNOLOGY

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EGYPT TODAY

Coming Up with the Goods

Can privatization create a sound industrial base

by Dr. Khaled Fouad Sherif

Since the late 1970s, Egypt's economy has been slowly unraveling. Economic decline has been marked by growing unemployment, disguised unemployment, mounting public sector failures and falling productivity. Today the Egyptian government confronts the twin difficulties of a sizeable budget deficit and an inability to finance additional public sector inefficiency. In an attempt to streamline this overburdened economy, the government has invited Egypt's private sector back into the forefront of development efforts.

Private sector development is no longer a choice, but a necessity in order to reduce state expenditure — the government's first priority. The decision to allow it, however, provokes three underlying questions: 1) Can the private sector play as large a role in development as the government envisions? 2) Can the new private sector really flourish in an environment that continues to support public sector failure? 3) Can the private sector truly emerge as a force able to export and create wealth in a more liberal free trade environment? Here are some of my own opinions in answering these key questions.

Can the private sector play as large a role in development as the government envisions?

The private sector's role in development clearly depends upon a number of extremely complex factors. Egypt will only retain a competitive edge and create a vibrant private sector if two specific conditions are met: avoiding high volume products and standardization, characteristics of present public sector industries; and investing in relatively smaller, more specialized ventures producing high-value, precision-engineered goods that are customized to meet the needs of a particular market. Such high tech ventures use evolving technologies.

Examples include high value segments of more traditional industries like chemicals, machine tools, and automobile components. If Egypt's private sector can infiltrate these areas, it will be better able to adapt to the evolving international economy.

Unfortunately, at present, Egypt is ill-prepared for such adaptation. For too long the government has sought stability in a declining public sector with mass production-based industries. Egypt now needs a private sector and a labor force that is capable of operating in more flexible systems of production, geared toward change, instability and innovation. For the next stage of economic evolution, the government's role in industry must decline dramatically.

Can Egypt's private sector reall[y] [de]velop and flourish in an enviro[nment] that continues to support public s[ector] failure?

This is a difficult question to a[...]
Even though some recent chan[...]
popular attitudes are encoura[...]
schism seems to exist between E[...]
public sector industrial culture a[...]
vate business. Yet we now have [...]
ber of success stories in the pri[...]
tor that clearly contradict this no[...]
Oriental Carpet Weavers, for exa[...]

One major concern though is [...]
or not continued public secto[...]
will prevent a significant porti[...]
industrial base from reorgani[...]
responding to new developm[...]
lenges. Sadly, this could hap[...]
all, the public and private s[...]
share the same resources a[...]
partner consumes a large [...]
them inefficiently, the other [...]
directly or indirectly be affe[...]

For example, assume a h[...]
case in which a public ind[...]
an industry that started [...]
and whose technology is [...]
obsolete or is on the declin[...]
ernment, through overr[...]
considerations prevents it [...]
bankrupt, the consequen[...]
severe, reaching all other s[...]
economy. Further, assu[...]
public enterprise loses L[...]
per year yet is kept open [...]
proximately 6,000 peopl[...]

the dire consequences of unemployment. What is the impact of this LE 300 million burden on the rest of the population? Simply expressed, potential public or private investors lose the chance to invest LE 300 million in new ventures. Assuming LE one million generates, directly and indirectly, 200 jobs, the annual losses of this failing state-owned firm costs the country 60,000 jobs. To preserve 6,000 jobs, 60,000 young graduates remain unemployed. In short, there is neither economic nor social justification to keep failing public industries alive. Thus public sector failure has adverse consequences because the "social logic" of preserving 6,000 jobs clearly does not outweigh the potential harm to society as a whole if 60,000 young graduates remain unemployed. And furthermore, keeping people in jobs that, for economic purposes, no longer exist, represents a significant cost to the industry itself.

Dr. Sherif maintains that the protection of public sector jobs in uneconomic industries is counterproductive.

John Samples

Can the private sector truly emerge as a force able to export and create wealth in a more liberal, free trade environment?

With over 200,000 university graduates entering the white-collar labor market every year and 200,000 technical school graduates looking for blue-collar jobs, domestic job creation becomes a considerable challenge to both the public and private sector. It also underlines the cost of public sector failure on future job creation.

Historically, for fear of redundancy or just a basic unwillingness to accept change, Egypt does not allow public businesses to fail. We attempt to maintain short-term paper profits in public industries through various legal and financial maneuvers. This maneuvering includes either restructuring the financial portfolios of public firms to avoid showing them as a failure or merging different public firms to make them appear viable. Such efforts, while feasible in the short run, merely rearrange public industrial assets without enhancing their competitiveness or changing their underlying orientation. Protection from imports — in the form of tariffs, quotas and subsidies — that has existed since the mid-1960s, has made public firms even less competitive. In addition, import protection has not only distorted public investment, making unprofitable ventures seem economically sound, but it has also led a large number of private ventures to try unsuccessfully to compete on the international market. Auto industry joint venture projects are, in my opinion, one such example.

Protectionism has in many cases encouraged domestic public and private investors to avoid international competition rather than to meet it. Not surprisingly, for over 20 years our public sector engineering industries have exported nothing! The cost of their products, on average, is about 20 percent higher than the border prices of imported substitutes. They can sell in the domestic market only because of import tariffs. Why should a typical consumer pay 20 percent more for a refrigerator or television set than his European or American counterpart? Consumers should not suffer if the overriding concern is to preserve jobs that would not exist in a free trade environment.

But what kinds of jobs are we protecting? Primarily, they are dead-end jobs in propped up, uneconomic industries that are showing paper profits. If we assume that such ventures are justified because they maintain over 30,000 jobs, one should ask a more pertinent question. Does providing 30,000 jobs outweigh the social cost of making over 30 million consumers pay too much for a wide variety of goods? Perhaps not, because in the end you make things more expensive for a thousand times more people.

Egypt should not have an industrial sector that is a burden on the pocketbooks of Egyptian consumers. We need change and, more importantly, we need to learn some key lessons from our experience of public sector failure. We must not repeat these mistakes during the era of private sector led growth. We need an industrial sector led by private initiative that can export and compete in world markets.

Egypt needs an industrial base that will generate more wealth and not one that will deprive domestic consumers of theirs. ■

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