Can Egypt Afford to Meet Its Creditors' Demands?

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CAIRO — The Egyptian government is now deeply immersed in detailed negotiations with the World Bank which it hopes will lead to an agreement opening the way for soft loans to the tune of $800 million. At the same time, this month a whole series of fresh negotiations begins with the International Monetary Fund (IMF).

Egypt has had difficulty in convincing the World Bank and the IMF that it should receive additional credits, primarily because the government has not been keen to implement a number of structural adjustment reforms recommended by the two institutions over the past five years.

Both the World Bank and the IMF perceive the government as being too cautious about reform. The gradualist policy followed in the structural adjustment process has often meant that reforms came too late or were imprecisely timed with other reforms.

The World Bank is not happy with the progress the government has made in restructuring electricity and energy prices and is still concerned that little is being done to remedy the chronic problems facing Egyptian state-owned enterprises.

On the other hand, the IMF is displeased with Egypt's monetary policies and is calling for additional interest rate and exchange rate adjustments which the government has been reluctant to implement.

Most of the problems between the government and the IMF are linked to the state's very cautious stand toward economic reform and its very gradualist style.

There are major differences over the pace at which each side feels the reforms should be carried out. For example, the World Bank disagrees with Cairo over how quickly energy and electricity subsidies should be eliminated. The government agrees that they should be dropped but feels that this cannot be done overnight.

Similarly, Cairo is thoroughly convinced that exchange rates must be unified but disagrees with the IMF over how quickly this should take place.

Yet the World Bank and the IMF are arguing that excessive caution in undertaking reforms may create additional burdens on the economy that will make future adjustment even more difficult. For

A Point Of View

example, if price differentials for basic commodities imported and sold domestically continue to grow in real terms because of slow price adjustments, subsidies will only become larger. Then the dependence of the population on such subsidies will in turn become greater, making it more difficult for the government to do away with them. Who is right? The IMF and the World Bank, or the government? Is the government really being too cautious about implementing economic reform? This is a question the government must now answer.

In any case, the IMF is pushing the government into a corner by offering to help Egypt reschedule its outstanding loans due over the next 36 months only if the government accepts the interest rate and exchange rate proposals submitted by the IMF.

Of course, accepting these proposals means accepting a rigid timetable for implementation of these reforms.

In this case, Egypt would have to drop its gradualist attitude and adopt policies likely to result in greater inflation.

How will the public react to substantial inflationary pressures, with the prices of major imported commodities going up at the same time as credit becomes tighter? This question will also have to be answered by the government.

If the government declines to accept the IMF's monetary proposals, Egypt can probably forget about debt rescheduling. For Egypt, this would be a nightmare.

It would find itself in the middle of a foreign exchange crisis that would likely lead to shortages across the board.

Consumers would find a lower number of commodities on the store shelves and industrial establishments would be hard pressed to obtain the foreign currency they need to import raw materials, making it more difficult to turn out products.

How would the public react to such shortages? No one knows for sure. Thus, an agreement with the World Bank and the IMF requiring immediate reforms will likely lead to problems.

No agreement will lead to other problems. A gradualist approach toward reform, even if the world lending bodies are forced to accept it, will lead to yet other problems.

Is there any way out? For an economy that has been threatened by one economic crisis after another since the 1967 war, the upcoming wave of structural adjustment reforms is a major test which will determine how the general public will react to change.

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