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CHAPTER ONE

INTRODUCTION: BACKGROUND

1.1. Background of the Economic Reform

Several years prior to the eruption of the 2011 Egyptian Revolution, the common perception was that Egypt's emerging economy is on its way on the road of progressive economic development and more profound integration into the global economy. Yet the multiple shocks brought about by the food, energy and financial crises at the advent of the millennium imposed a heavy toll on the rent-dependent Egyptian economy. Diminishing foreign direct investment, declining expatriates' remittances, deteriorating Suez Canal revenue and decreasing tourism proceeds caused a significant slide in real GDP growth from 7.2 percent in 2008 to 5.4 percent in 2010 (Reviewed in Abdel Baki, 2011). Furthermore, for the first time since the 1980s, Egypt suffered from inflation that peaked at 23.7 percent in August 2008 to remain at double-digit levels ever since (Abdel Baki, 2011).¹

In the past decade, particularly when Nazif administration came to power, the Government of Egypt (GOE) has embarked on a comprehensive program of economic, social and political reform. The reforms are widespread and diverse and are not confined to achieving macroeconomic stability. They include new policies to reform the financial sector and state-owned enterprises, revise fiscal and monetary systems and policies in order to have an enhanced allocation of public resources. The importance of this reform originates from the

¹ Figures from The Central Bank of Egypt in 2011

need to raise and sustain economic growth in different sectors of the economy, and guarantee that the poor contribute to and gain from the economic growth process. It also brings to light a new role of the Egyptian state in which it can no longer be regarded as the main provider of jobs, goods and subsidies for its citizens. This initiative implies a new 'social contract' where the role of the state is to administer the public interest rather than controlling it and to protect the poor and vulnerable in an economy that is primarily and mainly led by the private sector (World Bank, 2005).

It is perceived that the multiple serious predicaments that threaten stability and living standards in Egypt are attributed to the escalating population growth and the increasing wave of urbanization. Besides, the conditional loans of the International Monetary Fund and the massive privatization scheme raised the level of unemployment, which had reached 9.6 percent by December 2010 (Abdel Baki, 2011)². Not only that but also being the second largest importer of wheat in the world, the uncontrollable 2007/2008 rise in food prices has negatively affected the living standards of lower income groups to such an extent that many economic analysts attribute the triggers of the Egyptian Revolution to food insecurity (Reviewed in Abdel Baki, 2011).

Within this framework, the attempts for reform by GOE were driven primarily by the high levels of poverty despite of the augmented levels of social spending by the government in the year 2000 (World Bank, 2005). The food subsidy reform in particular became inevitable due to the inefficiencies of the food subsidy programs as a result of the ineffective targeting mechanisms, their large contribution to the government budget deficit, price distortions that were associated with price controls set by the government, controlled processing, marketing

² United Nations Development Program in 2010

and distribution systems, misallocation of agricultural production toward products regardless of their comparative advantage, inflationary pressures (due to monetizing the debt incurred in financing imports), smuggling, shortages, black marketing (due to dual exchange rate mechanisms to support imports), and rent-seeking by producers and distributors (World Bank 1999 and Adams 2000).

Generally, consumer subsidies are a common element of safety net programs in many developing countries. In Egypt, the subsidy program is more extensive than other programs in other developing countries but still all of those programs share common features and create the same problems (Harik, 1992)

Since these programs often represent a considerable share of government budget spending, many developing countries have introduced reforms to decrease inefficiencies and escalating fiscal costs, but with limited success. In most cases, only minor adjustments have been made, and those countries that launched food subsidy reform (e.g., Algeria, Egypt, Jordan, and Tunisia) have done so with varying degrees of success. (World Bank, 1999)

The main objective of almost all food subsidy programs among countries is to improve the food security of households especially the poorer ones. In some countries, food subsidies are planned to improve the nutritional level of some vulnerable groups who are specifically targeted by those programs such as pregnant mothers or school children. While in other countries food subsidies are intended to elevate the income and enhance nutritional condition of a larger and -may be more poor targeted- groups such as the general populace of the poor (Adams, 2000)

In general, subsidy programs aim to stabilize the prices of necessary goods regardless of the fluctuations of the market price of those food items. The main objectives of such programs are (1) contributing to alleviating poverty by providing cheaper food to the poor, (2) redistributing income and protecting the purchasing power and nutritional status of the poor; (3) providing a safety net to the population in general; and (3) achieving political and social stability by contributing to protecting the poor from economic shocks and enhancing their well being. (World Bank, 1999)

In my thesis I focus on one aspect of state provisions in Egypt represented in food subsidy particularly the rationing scheme or the ration cards. I explore the latest reform that was done in the rationing system in 2008 which is the introduction of the smart ration cards. I explore the response of the target beneficiaries to the introduction of the smart cards as the culmination of a series of reforms in the system that has taken place over the past four decades. I also derive implications from my qualitative analysis about the shortcomings of the rationing system and conclude with possible policy options to address the problems of the rationing system.

1.2. Objectives/Research Questions

GOE has passed through a series of reforms in the rationing system over the past few decades ending with one reform represented in the smart card system. My goals in writing about this topic are multiple folds: 1) to highlight the major operations of the Egyptian food subsidy system represented in the rationing scheme.2) to examine the efficiency of the system, whether or not it reaches its intended beneficiaries at a reasonable cost on the government's budget, and to explore its advantages and shortcomings.3) to get a preliminary reaction of the public sentiments regarding a certain policy change which is the introduction of the smart subsidy cards as a part of

an e-government initiative. 4) Last but not least, to derive some possible alternative policy options that could be applied consecutively in the long run.

1.3. Hypothesis

Smart cards as a technological advancement tool in the administration of the rationing system could be working well in itself. However, the real problems inherent in the system's administration are not yet addressed. I will argue that despite the introduction of smart cards for better administration of the rationing system, the reform is not sufficient to solve the several problems intrinsic in the system that still needs more intervention.

1.4. Methodology and Manner of Obtaining Data

The basic tool that I employed was in-depth interviews, the research thus being of a qualitative nature rather than a quantitative one. The main purpose for the interviews is multiple folds. The general purpose was to examine the reaction of the stakeholders in the rationing system, mainly the end users and the ration shops' owners, to a certain policy reform which is the introduction of the smart cards in 2008. The more specific reasons that I tried to capture from the interviews were as follows: 1) to examine the shortcomings of the paper system and whether or not these problems were addressed in the new smart system, 2) To test the effectiveness of the smart cards in enhancing the administration and the distribution of rations, 3) To examine the system's ways of inclusion/exclusion from the ration cards, 4) to test the relative importance of certain goods that are distributed through the rationing system with respect to the households who use the cards as well as the end users' level of satisfaction with regards to the quality of the rationed commodities, 5) to explore different ways of enhancing the distribution and the administration of

the rations from the point of view of the end users. All interviews were conducted in Arabic. The interviews were recorded and translated and transcribed immediately after the interviews were done. The interviews were mainly conducted in the poor suburbs of two prime metropolitan cities in Egypt; Cairo and Alexandria. Interviews were conducted in Matariya, hadayek el Qobba, Abdeen, El Mosky, El Nahda and Victoria neighborhoods. In my choice of the different neighborhoods, aside from poverty, my criteria were to diversify geographically as much as possible given the available resources. In other words, since I was working alone I couldn't extend my pilot study to cover different governorates as I also mentioned in the limitation to the research. However, I chose Matariya, Hadayek El Qobba as two poor neighborhoods surrounding the upscale district Heliopolis located in the Eastern part of Cairo. El Mosky and Abdeen are another two poor neighborhoods located down town. In addition, El Nahda is a neighborhood that is located near El Obour city which, I thought, could give a different perspective than the other old Cairo neighborhoods mentioned above. As for Alexandria, it is the second largest city of Egypt and the country's larger seaport which gives its population different characteristics than Cairo. This was an attempt to examine the reactions of a certain population with different characteristics and trying to extract the similarities and/or the differences than interviewees from Cairo. As I was going through the interviewing process, I tried to extract main themes that I could use in my study. In order to do that, I had to keep interviewing people from different neighborhoods until a certain pattern emerged from all the interviews that I used in my analysis.

The target group for interviews was the end users of the smart cards as well as the ration shop owners (*tamween* shop owners). In each neighborhood, in-depth interviews were conducted. Each interview lasted about three to four hours. Some of the interviews were group interviews

and others were one-on-one interviews. I had a group of open-ended questions but ensured that the interviews expand beyond those questions where interviewees open up and bring up issues beyond the scope of the original questions. I made sure to make them comfortable to talk freely and ask new questions based on the information that they say during the interview. This was critical to my research since I was trying to measure the reaction of the beneficiaries to a certain policy change. In all interviews, I was accompanied by a community agent for facilitation and guidance to the *tamween* shops and designated households. The community agents were comprised of individuals from the different neighborhoods who I either knew from within my social circle or to whom I had been led to by others.

In some interviews, I visited the ration shops to talk to the owner or the responsible person for the distribution of the rations who deals with the clients. Simultaneously, I interviewed the customers who came to take their rations on a time span of two to three hours. The interviewees (end users) were eager to share their experiences and talk about the advantages and disadvantages of the system. The *tamween* shop owners showed some skepticism in the beginning of the interviews but then they started to talk with more freedom. One *tamween* shop owner from Al Mosky area didn't want me to record the interview nor reveal his identity in my research.

A worth mentioning observation is that even very simple, ignorant daily workers had a good vision and well thought profound understanding of the problems of the system as well as the advantages and the disadvantages of the smart cards. This was intriguing in many ways and also encouraging and supportive to my proposed approach in this study of community participation and bottom up approach for development.

In addition, snowball sampling was employed as an additional technique to find more participants from the different neighborhoods other than the identified ones by the community agents. Snowball sampling technique is a non-probability sampling technique where existing study subjects recommend future subjects from among their relatives, neighbors or acquaintances. More respondents could be recruited using this technique until enough data is gathered and certain themes could be identified from the interviews. One advantage of this sampling technique is that it is very useful in case of hidden populations which are difficult for researchers to access and identify.

In order to complement my qualitative analysis, I also used secondary statistical data from previous nationwide studies done by the World Bank and the World Food Program.

1.5. Chapter Outline

My goals in writing about this topic are multiple folds, first to highlight the major operations of the Egyptian food subsidy system represented in the rationing scheme, its advantages and shortcomings. Second, to get a preliminary reaction of the public sentiments regarding a certain policy change, represented in, the introduction of the smart subsidy cards. Third, to introduce some policy options that could be applied in the next period under a new president and a new government.

My thesis will be divided into seven chapters including the conclusion. The first chapter will be the introduction that includes the background, the research objective, hypothesis, methodology and manner of obtaining data and limitations for the research. The second chapter will provide the literature review. This includes the theoretical background and a political economy analysis for the need for state intervention in social provision. This gives the necessary background to

understand the underlying elements that connects both political and economic spheres with subsidy schemes. This includes cases of market failure; political patronage and implicit social contract; and welfare systems. This chapter concludes with using New Institutional Economics theory as the conceptual framework for my analysis. Then I proceed to the case of Egypt in the third chapter highlighting specifically how Egypt adopted a planned economy and how subsidy was a part of both a case of an implicit social contract and political patronage. The fourth chapter provides a detailed historical record of consumer subsidies and their objectives. It also explains the evolution of the Egyptian food subsidy system and the rationing scheme since World War II. In addition, it includes a section of the various reforms done in the rationing system in the past few decades culminating with the smart cards and the opportunities for further reform.

The fifth chapter examines the target beneficiaries' response to the change in policy. It is the chapter that contains the analysis of my field work and qualitative analysis. The data generated from the in-depth interviews will be analyzed thematically and content analysis will be done with reference to both subjective and objective categories of analysis. A series of interviews has been done until certain themes emerged and some conclusions could be derived. The first section addresses the respondents' views supporting the smart system. The second section addresses the respondents' views opposing the smart system. The third section addresses the commodity preferences of the consumers and whether or not they are well addressed in the system. The fourth section looks at the loopholes in the system, which still exists regardless of the multiple reforms. The fifth section puts forward the suggestion of transferring the in-kind subsidy to cash transfers and examines the respondents' reactions.

The sixth chapter is a look at the policy implications and the possible alternative approaches that future governments could adopt in order to address the most eminent loopholes in the system

which are the leakage of the subsidy benefits away from the poor and the lack of a definitive targeting mechanism that ensures the subsidies goes to the needy and the poorest quintiles of the population and then I will conclude with the final chapter.

1.6. Limitations of the Research

One limitation to my research was the issue of whether I was compatible to my research topic or not. In other words, especially in the beginning of the interviews, interviewees looked a bit suspicious not knowing why I would be interested in the subject matter. I attempted to overcome this obstacle first by having one community agent with me in each interview which helped to break the ice and second by being friendly, simple and humble during the interviews. After starting the interviews and talking with the subjects they felt more at ease and felt comfortable opening up about their problems. Indeed, as the interviews progressed the respondents became increasingly enthusiastic about sharing their experiences and problems and persuaded me to communicate their concerns and problems to whoever can help them. One important policy implication, based on the eagerness of people to share their problems and to brainstorm regarding solutions, is the community based approach that calls for greater participation of the poor themselves in suggesting alternative solutions to their problems.

Interviewees felt more comfortable after knowing that the interviews are done for the purpose of academic research and not for a governmental agency or a foreign entity. The fact that this research is done for academic purposes seemed to make them more comfortable and relaxed. Some respondents didn't want the interviews to be recorded or their names to be mentioned in the research.

Another limitation to the research is that my study was confined to poor neighborhoods that were selected randomly in two prime metropolitan cities Cairo and Alexandria. Due to the lack of human resources and since I was working alone in collecting the data, the research could not be a nationwide research. I attempted to overcome this obstacle by backing up my qualitative analysis with quantitative data collected from nationwide surveys done by the World Food Program. It is important to note that the results of this study cannot speak of the Egyptian society as a whole and is not meant to be a comprehensive analysis that could be applied to the whole country. Nevertheless my study provides some indicators regarding the community response to a certain policy measure and their different viewpoints regarding change and enhancement of the service provided and the policy implications that could be derived as a result of this study. It only gives a preliminary reaction and quick glimpse which provides some groundwork and direction for further extensive research.

CHAPTER TWO

LITERATURE REVIEW AND CONCEPTUAL FRAMEWORK

2.1 Literature Review

In this study I will use the political economy approach in order to analyze the nature of social and welfare policies and the role of the state in them. Political economy is the best discipline to study subsidies and the nature of state intervention in the welfare of the citizens since it studies the dialectical relationship between the economic and political fields and takes into consideration the interactions between economic and political variables that affect a certain subject (Soliman, 2011).

Political economy perspective provides a number of tools that enables the analysis of the role of the state in social provision and the nature of the welfare systems. It also explains how the western welfare states managed to stay intact despite the widely discussed crisis of the well established welfare states such as the United Kingdom. In addition, in recent years, there has been a major regression in the dogmatic neoliberal ideology regarding the role of the state. This calls for a more broad perspective of studying the political forces that affect the role of the state in social provision. Integrating the political approaches with the economic factors is essential for the intellectual debate regarding the social provision and also for evaluating the feasibility of alternative modes of provision. The essence of using a combination of economic and political analysis in welfare provision analysis can be best described by Haggard and Webb (1993: 162) in (Mwabu, Ugaz, White 2001) that “while prescriptive analysis by economists aims to identify policies which are optimal according to a set of specified objectives, positive political analysis is often concerned with why optimal policies are not adopted”. The separation between the economic and political factors affecting a certain subject is clearly illogical and the significance

of political analysis has been clearly demonstrated in guiding the design of economic reform programs by specifying the political character and the ramifications of various reform options and seeking to incorporate these into the design of policies themselves. In other words, political factors such as power, interest, institution and ideology need to be integrated in policy analysis whenever possible. The complexity and the diversity of these variables provide new perspective on different concepts. For instance, the rise of institutions could not be attributed to some process of coherent adaptation but rather through the interaction of the former four political variables. In addition, a new perspective is also applied to the state where it cannot be perceived as a static nest for rent seekers rather it is perceived to embody the dynamic ever changing patterns of social interests and institutional systems that has significant policy outcomes. Civil society cannot be regarded as a form of philanthropy or as a perfect territory of altruism without highlighting the conflicts and the insecurities that it entails. Moreover the market, is not just a mechanism of enhancing efficiency but could also be a mechanism that fosters power and pressure of some interest groups that might shift welfare policies to unintended directions (Mwabu, Ugaz, & White, 2001).

Since the subsidy system needs to be studied within a framework of the state's social policy and the relationship between the market, the state and the poor. Since the issue of the state versus market has lied in the core of the economic development discourse for so many years. For the purpose of this thesis and in order to put forward an adequate theoretical framework for the subject matter, I will focus on the literature concerning the relationship between the market and the state, the state and the citizens and the right mix between the state and the market forces. Given that, I will cover the literature that answers one prime question: *Why state intervention is needed for social provision?*

For that purpose, the following sections will cover the literature basis for this which explains the need for state intervention in case of market failure, welfare systems, and political patronage. I will conclude this chapter by the conceptual framework. I am going to use New Institutional Economics theory as the theoretical framework for my analysis. I find it the most suitable theory for my study since it addresses the institutional component in the study of the welfare discipline and emphasizes the diverse social, political, economic and ideological forces that affect decision makers regarding these policies. In addition, there is a growing trend towards a more targeted provision through various actors, including but not limited to, civil organizations and an intense reliance on informal institutions such as extended family networks in providing fundamental guarantees of income security during periods of economic or social stress.

2.2 The need for social provision and state intervention

2.2.1 The state of market failure

The market is considered a key ingredient of resource allocation mechanism. The market can simply be defined as an institution that makes available to interested parties the opportunity to negotiate courses of actions. The market mechanism can be defined as the resource allocation mechanism in which the state restricts its activities in the socio economic area to facilitating the operation of private markets. The state plays this role using different tools. Among these is developing and enforcing commercial laws, protecting private property rights and so forth. Yet under the terms of the social contract the state is obliged to do more than merely sustain the market mechanism (Dasgupta, 1993).

Market mechanism allocates resources to the most profitable areas and hence achieves the highest satisfaction with a certain distribution of purchasing power. It does not question the

original distribution of purchasing power, its equity or desirability. It functions best when price mechanism works fully. Competition is its driving force. It can then work best to produce the demanded goods cheapest. It is the best instrument to connect supply and demand with the smallest effort for the largest result. It is an efficient machine but only as far as it presumes the given starting point and destination. Since market mechanism assumes certain supply & demand, it does not concern itself with the spread of them. The spread of the effective demand is the ultimate condition to determine our life. This task should not be left to the market mechanism that is rather inclined towards competition and efficiency (Tsukada, 2002).

In fact this problem is created by the market mechanism itself. The urge of competition promotes efficiency (investment) more, and equity (profit-wage distribution) and human fellowship (social welfare) less. The solution to this problem would not be sufficiently provided by the good intentions of individual entrepreneurs trapped in this mechanism, for every resource in the producers' hands is ordered to be invested for higher competitiveness and less and less towards the employees and the disadvantaged. This market rule creates conflict between profit and wages, rich and poor, productive goods and consumption goods, and supply and demand. Sporadic charity does not solve these serious problems including poverty. Hence, it is critical to find a complimenting tool to the market mechanism (Tsukada 2002).

The Welfare State is the balancing-measure to such a danger of the market economy. Such state usually declares the public welfare of the people as the most important goal of state policies. It often has a clear goal of realizing and raising the minimum welfare level of all citizens. It then endorses relevant laws and institutions to realize this goal such as labor laws, various social

welfare provisions and so on. The main goal is to assist the disadvantaged and regain the balance between efficiency, equity and human fellowship (Tsukada, 2002).

State intervention is mainly needed for the social welfare function. In a market economy the volatility of life because of the rise and fall of firms and jobs nurtures an inclination to earn and save for one self, thus creating a hurdle to the full expression of natural human fellowship in an apparently contradictory affluent society. The common ambiguity of market transactions lies behind this anxiety and saving tendency. The Welfare state with the institutionalized redistribution of income becomes necessary to counterbalance this unnatural instability of human fellowship (Tsukada, 2002).

Mishra (1990) states that, the relationship between the market and the state is a complimentary one. The capitalist market economy aims to maximize efficiency and profit through competition, through which the economy becomes imbalanced and amoral. The counter movement is formed through the movement of the majority of people for political right and economic security. This has been materialized in the state laws and policies. Hence the responsibility for rectifying this trend rests with the state. There are some main state interventions necessary to balance the market mechanism. First is equalizing the bargaining power of labor and the second is creating a safety net for the needy. Labor laws target the protection of the bargaining power of the employees in order to realize fair contracts. High employment policy also helps achieve this goal by creating insufficiency of labor and thus strengthening labor's bargaining power. Safety net was originally established to save the neediest of people without job or money and has grown gradually to cover a larger number of people and a higher standard of living, yet with significant differences in its levels among different countries (Tsukada, 2002).

One by product of state intervention policies is their effect toward adjusting demand and supply. The redistribution of income among the rich and the poor adjusts the total supply and demand. As the market mechanism has the affinity to over produce by its mere compulsion toward investment for higher productivity under competitive pressures, this function is particularly effective when the gap widens in a depression period of a business cycle (Tsukada, 2002).

Much of the social policy is concerned with the public provision of goods and services. Particular interventions are intended to (1) guarantee access to a range of goods and services to improve welfare and achieve socially defined objectives. This may be achieved through numerous mechanisms such as direct state provision, publicly financed payment systems, and government mandates to other organizations to provide services; and (2) reduce insecurity or insure against risk in order to deal with household or individual shocks, such as, serious illness, disability or unemployment and to smooth consumption and income.

The conventional economic rationale for public interventions in the production or financing of certain goods and services is to support efficiency in the presence of market imperfections or failures. Market failures in the provision of social welfare goods arise in part because of the characteristics of these goods (public goods or externalities) or because of imperfect information and uncertainty. Even with well functioning markets there may, nonetheless, exist too much poverty or inequality according to established social norms. This provides a strong distributional or equity rationale for government intervention. Hence, we are not only concerned with those goods where the market mechanism generally fails to guarantee adequate provision –public goods, quasi public goods, and merit goods for example- but also with private goods which increase security or welfare but where markets fall short to ensure an adequate distribution.

Many public interventions to achieve equity or welfare goals fall into this category of the public provision of private goods (Mwabu, Ugaz, & White, 2001).

Thus, the question is not one of either state or market, but one of how much state intervention, what kind and by what means. Generally, markets must be allowed to function where price signals clearly work in achieving efficiency. State intervention becomes necessary when markets fail or where they cannot perform efficiently or when there is too much inequality and poverty. The most important factor for determining the right mix is that of comparative efficiency. In other words, it is necessary to create a matrix of activities in the economy and the kind of intervention that is required for each activity and in what form it should occur. Forms of intervention can be either market-driven or state-controlled. The strength of intervention also needs to be determined. With limited resource availability, government should reallocate resources more in areas where it has a comparative advantage over the market and give up those where it has less of an advantage. The critical test is not ideology but what works best under a given set of circumstance (Rangarajan, 2000)

2.2.2 Welfare systems

Welfare State is considered the most prominent form of state where the government puts the public welfare as the ultimate goal of its policies. The welfare system is one that enables the state to ensure a decent living standard for its citizens and provides security to those citizens in major areas such as health care, old age pensions, and support for low income citizens (Tsukada 2002)

Welfare systems could be regarded as a form of contract between the state and the citizens where the state is committed to providing certain goods and services in return for the high taxes paid by the citizens. Also, much of the state's political legitimacy originates from the provision of these

goods and services. In numerous developed countries, in the decades after World War II, the welfare system has reached a relative level of maturity. At the time, most western industrialized democracies have adopted policies of income security and have provided their citizens with free or subsidized services in many areas such as education, health, housing and employment. Those countries continued to increase their level of spending as a percentage of their national product over the next half of the twentieth century (Spiro & Yuchtman-Yaar, 1983).

One way of analysis of the welfare state depends primarily on the changes in social structure and the emergence of new groups and new interests during periods of democratizations or political change. From a Marxist perspective, welfare programs can be defined as a result of class concession on part of the bourgeoisie in order to avoid intense class conflict, of the rise of political power of inferior classes which is primarily driven by the wider proliferation of democracy, or a combination of both. It also emphasizes the significance of class relations as political forces which shape institutions and determine strategic policy agendas.

In some cases, the rise of welfare states is traced to the emergence of an industrial working classes and patterns of political alliance between them and other interest groups who want to gain from welfare state expansion. Some analysts emphasize the importance of the role of the industrial working class in this process while others stress the role of the middle class and sometimes they extend it to the industrial bourgeoisie. Those groups find a way of expression through political parties of interest groups. Hence this approach is used to explain the emergence or the development of welfare state in developing or transitional societies (Mwabu, Ugaz, & White, 2001)

Since the inception of the welfare state, its activities tend to be in five major areas. First the large size of the public sector that mainly includes major heavy industries such as coal, steel, railways, gas and electricity supply and others. This type of public sector or government ownership to major industries prevailed in countries like the United Kingdom and the United States in the twentieth century as well as in other developing countries where it was mainly referred to as “socialism”. Second, the state acts as a macroeconomic manager or macroeconomic regulator. Governments often change their taxing and spending systems as well as use their control over money supply to achieve macroeconomic objectives such as full employment, stabilizing prices and controlling the balance of payments. This type of macroeconomic management is usually associated with Keynesian economic policies. Third, state is also involved in controlling some details pertaining to economic activity. For instance, in the United States there are a number of federal agencies that are concerned with regulating things like railway rates and water pollution. These agencies include the Food & Drug Administration, the Consumer Product Safety Commission and others. This type of regulations are intended to cover diverse objectives such as product safety, price fixing, maintenance of adequate public services, and protection of the rights of minorities (Spiro & Yuchtman-Yaar, 1983).

Fourth, governments or welfare states have become heavily engaged now in social engineering. In other words, states are concerned of bringing about desired changes in the structure of the society. These changes include but not limited to: the elimination of poverty, racism, sexism, crime, the creation of more egalitarian societies and so forth. In order to achieve this objective governments have changed tax policies, expanded educational systems, issued laws against sex and racial discrimination (Spiro & Yuchtman-Yaar, 1983).

This function of welfare state is often encouraged by the neoliberals who classify social expenditure as investment in people. Consequently the allocation of a portion of the government budget for social provisions is not regarded as a cost rather than a benefit. The rationale behind this is that since the poor are already costly the money is better spent on equipping them with useful skills (Blau, 1989).

Finally, the state in almost every country has emerged as the guarantor of minimum standard of living to its citizens. In other words the state has become involved in the business of welfare provision. Governments protect their populations from a number of unfavorable conditions such as sickness, accidents, unemployment and old age. They can be the major suppliers of health care like in the case of Britain's National Health Service. They intervene heavily in the housing market. They are in most countries the major provider of education (Spiro & Yuchtman-Yaar, 1983).

In many countries social welfare goals entails extensive food subsidy programs which are generally accompanied by widespread social safety net spending often arising from a socialist ideology. This is the case for countries like China, Egypt, Mexico, Sri Lanka, and for several African countries where this ideology is prevalent. For instance, in Egypt, Nasser as the leader of a nationalist and socialist revolution has led a state that adopted a policy of a redistribution of income and opportunities. Embedded in this policy was the role of the state as a provider of food subsidies through government control of wheat prices and marketing, along with other rationed goods.

Similarly, though more populist, inclinations toward social justice account for the emergence of subsidy programs in Argentina, Mexico, and Sri Lanka. In Sri Lanka, socialist-oriented governments in the 1950s and 1960s adamantly defended subsidies as a major policy apparatus

for social justice. Consequently, socialist origins, more often, lead to widespread food subsidy programs which bring about major government involvement in the production and marketing of food commodities. They reflect strong political support for goals of income redistribution, social solidarity, and economic development. They usually follow major shifts toward socialist and even revolutionary leadership (Hopkins 1988)

2.2.3 Political patronage

Neo-patrimonialism is a term used to describe political regimes where authority is exercised through patronage networks rather than through bureaucratic policies or conventions. In these types of regimes, government institutions are heavily politicized through these networks, to a massive extent that some parts of these institutions have come to be privately controlled and have become major tools for the accumulation of wealth and power for individuals and their networks. Thus these corrupted networks control the distribution of public resources among themselves rather than being fairly distributed among all citizens.

Based on Max Weber, the term is also defined “as a system of rule in which all governmental authority and the corresponding economic rights tend to be treated as privately appropriated economic advantages and where governmental powers and the associated advantages are treated as private rights” (Titeca, 2006)

In a Weberian sense patronage challenges the modern concept of representation which entails a system of public rights, a public discourse on what should be perceived as rights and what should be enjoyed in practice as entitlements, and a competitive system for establishing rights and priorities and for controlling their execution according to public laws.

From this perspective patronage is shown to counteract the system of representation, of assignment of rights, by placing friends in the strategic positions of authority and power. This

approach is often contradicting to the institutionalization of public accountability and therefore stands in opposition to a politics open to participation and to a rhetoric aimed at the protection of individual and collective liberties and rights (Roniger, 1994)

This type of patronage systems is often used by authoritarian regimes to guarantee the loyalty of some interest groups that would also help to sustain their regimes. In Egypt, few years before the 2011 revolution, this Weberian approach of patronage was heavily utilized by the ousted autocratic regime to the extent that Egypt was perceived to suffer from a “resource curse” where as the totalitarian Mubarak regime and its cronies embezzled the country’s resources for their own private interest. This led to further increasing the gap between the richest quintile of the Egyptian society and the poorest one as the corrupt politicians and their business associates got richer at the expense of the poor due to these patronage networks (Abdel Baki, 2011)

Nevertheless, putting aside the corrupt patronage networks, at a minimum, government leadership needs sufficient support from various sectors and groups to enable the performance of the fundamental government functions. Given that, government leaders are certainly occupied with the calculations of the opportunity costs of different uses of financial resources in terms of the support, sustainability and legitimacy of the regime.

Among the different uses of the public resources, leaders are occupied with the allocation of resources for subsidies provision. Subsidies, particularly explicit food subsidies through rationing or fixed prices, are not only an element of political patronage. Subsidies comprise an implicit social contract between citizens and the state in many developing countries. Hence, any changes in them or attempts for reduction becomes a source of social unrest and political upheaval. This is attributed to the fact that citizens regard any reduction in the level of subsidies

or price increases for certain commodities as a negative indication. In other words, changes in subsidies are almost always regarded as the advent of a series of other unfavorable changes regarding the government's commitment for social provision. Government food subsidies appear to constitute this kind of implicit contract in countries like Egypt and Sri Lanka, and probably in Bangladesh, India, Mexico, Morocco, Pakistan, Tunisia, and Zambia (Hopkins, 1988).

The rhetoric of food subsidies takes place within a framework of expectations that are part of the general political formula for a society (Reviewed in Hopkins, 1988). One expectation of the public could be referred to as "a right to food". Indeed, when a subsidy takes on the quality of being a right, this can be very influential and can negatively affect the legitimacy of a certain government. The right's particular meaning may be embodied in something quite specific such as: the one-piaster price for a loaf of balady bread in Egypt or the rice ration in Sri Lanka (Hopkins 1988).

When food subsidies are considered an economic right of the public as in Egypt and in other countries, governments need to obtain public approval for any alterations in the system. Failure to obtain consent through advance warning, public discussion, and compensation payments for those most harmed groups may be the main reasons for failures of planned changes in countries such as Egypt, Liberia, Morocco, and Tunisia. On the other hand, when subsidies are regarded by the beneficiaries as a kind of donation or endowment of the government with no special commitment, amending them involves only normal political bargaining, without affecting the legitimacy of the regime's hegemony.

Food subsidies are considered a political right in many countries of Asia, Africa, and unquestionably Egypt, although the extent to which subsidies play a prime role in politics differs

from one country to another. Some countries in Asia, such as Pakistan, have slashed their subsidy costs without experiencing instability or any hazardous consequences to legitimacy. Indeed, a number of countries have reduced the size of the cost borne either by the government or by the agricultural sector without grave political price (Reviewed in Hopkins, 1988). In Egypt, it has been feasible to shift the cost of paying for subsidies in some measure away from the farmer and to expand the accessibility of the subsidies in the rural sector, but the right of the government to regulate the subsidies substantially has not been demonstrated (Hopkins, 1988).

Calculations of the political advantages of subsidy provision to certain interest groups often represent an important task for decision makers. In many developing countries, the identification of these interest groups is a rough and hard undertaking. This is due to the fact that these interest groups tend to be weak and Often the most powerful groups are civil servants, the military, urban labor, and sometimes industrial interests (Hopkins 1988).

Basically, if subsidies are targeted to the poorest groups, they go to a group whose political power is relatively unimportant and thus would not represent the best allocation for resources as far as patronage is concerned. In this case subsidies may exist nevertheless the government would not commit to its provision due to uncertainty and lack of information regarding the necessary groups needed to support the power of the existing regime. With improved information, a government can decide to target or to abandon a subsidy program. For instance, in 1953, the Sri Lankan government eliminated the rice subsidy, producing a 280 percent increase in rice prices. This has caused the eruption of nationwide strikes that were lead by organized labor. After several deaths, the prime minister resigned, and the subsidy cuts were partially discarded. In 1956, a socialist government came into power and reinstated the low price of rice,

cutting the existing market price almost by half. Another attempt to reduce subsidies took place in the 1960s, which also fueled a big wave of protests. As a result, subsidies became the major issue of the 1970 campaign, and the party that supported the largest subsidy programs came to power and brought back the weekly ration. On the contrary of these developments, and after the 1977 elections, the new Sri Lankan government calculated that it needed less support from the urban poor. Hence, it adopted a policy of slashing subsidies more vigorously than earlier governments, which had calculated that subsidy beneficiaries were in the winning coalition (Hopkins 1988). Similarly, in Jamaica, when the conservative government had strong support in the early 1980s, it reduced benefits for groups not critical to its power. So, in cases of ambiguity about the necessary winning groups, subsidies are likely to be more universal and less targeted, since more groups are deemed potential candidates for the minimum coalition required for effective rule. On the other hand, patronage can be a very powerful tool when the information is available and when the right groups are identified. So the government or the regime in power strives to win by sharing the fruits of its victory in different ways among them are subsidies when carefully targeted to the right coalition or group.

Indeed, patronage imposes a predicament for leaders since it is easier to shift the subsidies away from the neediest groups than it is to withdraw them from politically influential or potentially unstable groups. (Hopkins 1988).

In addition, subsidy schemes offer a way to support political organizations and political parties especially those who strive for electoral support. Political entrepreneurs realize the benefit of targeted programs that can be utilized as a reward for loyalty. Accordingly, leaders use such projects or organizations to distribute food and to gain support rather than mechanisms that yield

no political advantages. In addition, provision of food subsidies creates a form of dependency between the provider and the beneficiaries that promote general political stability. Thus subsidy systems are considered prime sources of patronage in many countries. Generally subsidy schemes improve the image of the government as the provider of food.

A secondary benefit to subsidizing food is the licensing of shops to distribute subsidized food. If a shop is licensed as a ration shop, there is natural incentive for customers to shop there and purchase a variety of non-rationed commodities as well. Hence, by including the owners of these shops in the winning coalition political leaders widen their support base.

In general, examining the political aspect of subsidies widens its analysis and unleashes further benefits and costs that were not readily uncovered in economic and nutritional status measures. Benefits to the government of helping the poor through food subsidies are not confined to possible efficiencies compared to money transfers and their cost effectiveness as nutrition-oriented tools. Indeed their political benefits to leaders could be of prime significance and perhaps adequate to sustain those leaders when other redistribution programs are discontinued (Hopkins 1988)

2.2. Conceptual framework: New Institutional Economics Theory

The existing models of welfare policy and social provision has proven to be limited and there has been a dire need for alternative approaches that address the institutional component of the welfare arena and the diverse social, political, economic and ideological forces that affect decision makers. There is a growing approach towards a more targeted provision through various actors with a greater role for civil organizations and an intense reliance on private family or

kinship networks in providing fundamental guarantees of livelihood security during periods of economic or social stress. NIE offers a broader theoretical framework for analyzing the public provision of welfare goods. **In particular, its analysis of micro-level behavior sheds light on the reactions of stake holders or intended beneficiaries to certain policy interventions.**

NIE explains the behavioral responses that cannot be explained through conventional rational-actor models. For instance, existing social norms may either activate or hinder certain programs depending whether or not there is a stigma attached to this program. A good example, is self-targeting, sometimes used in subsidy programs, where this stigma could be used to exclude the upper-middle or middle classes from benefiting from such programs so that only the poorest participate (Mwabu, Ugaz, & White, 2001). For example, an upper middle class Egyptian would not want to be seen in a queue in-front of a bakery that distributes subsidized bread. In this case, social acceptability as an institution will be the incentive for self -targeting.

In addition, in my research, it is essential to understand the local institutional context in order to comprehend the reactions of the target beneficiaries to a certain policy change. The existence of informal institutions such as marriage, remittances or extended family support which are intrinsic to our Egyptian society affects the behavior of the respondents. To illustrate this point, if a household partially depends on the support of a family member who works abroad, this will affect the standpoint of this household to subsidy provisions. Again, social acceptability will play a role where these families would like to be regarded as non-needy of assistance. They might as well stop using their ration cards or start complaining about the quality of the commodities which they perceive as non-satisfactory.

Moreover, the support of extended family could be used as one determinant of poverty –among other factors- or the lack thereof. For instance, as I propose later in the research using proxy

means testing to identify the poorest quintile of the Egyptian society could use indicators such as the existence of extended family support. This kind of indicators is more of local institutions that are somewhat unique in the Egyptian society which are worthwhile examining.

This focus on the significance of institutions lies at the heart of NIE and closer attention to the institutional arena within which policy interventions are received may emphasize ways to enhance policy.

Two key courses of thinking within NIE focus on distinct but related aspects of the economics of information, market imperfections or failures. First the historical transaction cost school based on the work on the theory of the firm and social cost. This approach highlights market imperfections stemming from the costs of transactions in the presence of ill-defined property rights. Costly transactions include the costs associated with the acquisition of information, coordination and monitoring and the enforcement of contracts. The development of institutions such as legal rules and regulations, property rights, and contracts reflect a rational response by actors aiming to decrease the costs and uncertainties associates with such transactions. (Mwabu, Ugaz, White 2001)

The second line of thought within NIE associated particularly with the work of Stiglitz (for example 1989, 1985, 1974) focuses on problems arising from imperfect or asymmetric information. It points to areas where markets are prone to fail, and thus helps to recognize potential areas for government intervention in markets. Like conventional economics, it does not essentially accept an automatic role for the state in cases where markets fail or function imperfectly. There has to be a strong justification for intervention that would rest also on the capacity of the state to provide services in an efficiency enhancing manner (Mwabu, Ugaz,& White, 2001)

This branch of NIE has received considerable momentum from the study of development economics. In developing countries, market imperfections and failures tend to be more invasive, information more costly and regulation often less effective than in more industrialized market economies (Reviewed in Mwabu, Ugaz, & White 2001). In the presence of such factors such as risk, uncertainties, and market imperfections, an extensive range of seemingly “irrational” institutional arrangements or behaviors are observed; NIE interprets this as the result of efforts to compensate for markets’ inadequacy. Empirical testing of the formal approaches of NIE has been mainly through micro economic studies of village and household level institutional arrangements, and their role in buffering risk and providing insurance. Institutional arrangements examined this way have included markets for productive assets such as marriage, migration, and remittances (Reviewed in Mwabu, Ugaz, & White 2001), and mutual insurance agreements such as farmers’ cooperatives and credit associations (Reviewed in Mwabu, Ugaz, & White 2001). Whereas many observed arrangements were formerly found hard to reconcile with the assumption of rational behavior, the focus on the institutional perspective of economic activity allows them to be viewed as a rational response to information problems and imperfect markets.

New Institutional Economics also provides an important approach for the legitimacy and the operation of social welfare policies. NIE is concerned with institutions, defined as the formal and informal rules that influence human individual behavior as well as his interaction with others. NIE is also concerned with the relationship between those institutions, transaction costs, incentives, economic behavior and outcomes. NIE emphasizes the importance of the role of institutions in welfare social policy provisions. This is due to two main reasons, first the nature

of the goods involved are often those where markets are subject to major imperfections. Second is that the most needy individuals, households and groups are those who are most likely to be marginalized and not included in the markets. As Bates observes, NIE is used by some as a validation for interventionist benefits, as well as by those seeking a middle way between state and market **as ‘justification for basing development efforts on community action and civic engagement’** (1995:27) (Mwabu, Ugaz, White 2001)

NIE also provides insights for understanding relatively new pluralist patterns of welfare provision. A transfer towards greater privatization of welfare services has paved the way for the different existing institutional arrangements involved in informal welfare provision, and their versatility and resilience. Numerous publicly provided welfare goods are in fact jointly produced and financed, for example, by households and communities in addition to the state. In addition, in response to the fairly polarized rhetoric on the role of the market versus state, there has been a growing focus on the role of civic society organizations in the provision of welfare goods and services. The expansion of the role of the civil society in welfare provision has generally been interpreted as a response to the malfunction of both market and state provision (Reviewed in Mwabu, Ugaz, White 2001), although the opposite argument that public actions is a response to failures in the voluntary sector, has also been argued. Despite this pluralism is sometimes viewed as a new approach to welfare provision, **in fact households and communities have long been involved in providing social and economic security through a range of informal and semi-formal mechanisms. However, the extent to which these activities are regarded as forming an important component of a formal system of welfare provision which the state can compliment, sustain, and promote, is relatively new.** Moreover, in contrast to neoclassical economics, NIE facilitates the analysis of relationships and possible tensions between this

market and non market institutions in satisfying welfare needs. As Davis and Hossain remark, the institutional approach has been influential in redrawing the map of relations between levels and types of institutions (state, civil society, market, family) and their objectives (1997:13) (Mwabu, Ugaz, White 2001)

NIE explains how institutional arrangements mediate between the formal system of welfare provisions and the actual outcomes and impact on individuals and households. Not only that it focuses on the roles of untraditional actors in service provisions but **also it emphasizes the recent ideological shifts of having a pluralist multiple actor society that is involved in social provision.** For instance, civic organizations which are heavily involved in their communities can play a prime role as the mediator between the formal system of welfare provisions (the government) and the actual impact on individuals and households (target beneficiaries). In addition, NGOs can help in implementing studies relevant to public policy with their capability to better reach respondents from their local communities. Some recent studies have shown that NGOs can play a crucial role in managing surveys and collecting data from their beneficiaries. Those NGOs had a direct access and wide networks in their local communities that extended among different socioeconomic classes as well as various ethnic and ideological positions in the society. In a particular study, this led to a response rate of 75.6 percent which entails that NGOs were quite successful in reaching and convincing respondents to participate in this survey (Abdel Baki, 2011)

CHAPTER THREE

CASE OF EGYPT: BACKGROUND OF THE EGYPTIAN ECONOMIC SYSTEM AND FOOD SUBSIDY SCHEME

In order to understand the importance of the food subsidy system in the Egyptian economy and its significance for the Egyptian people, it is important to look at the historical development of the role of the state in the Egyptian economic system as well as the role of the subsidies in the Egyptian economic and social system over the years. In particular, in this chapter, I will highlight briefly the political economy of the food subsidy in Egypt in the past few decades. In the first section I will discuss the clientelist state started under Nasser and continuing under his successors then I will move to structural adjustment policies that the country adopted in the early nineties then the third section will describe the problems with the existing food rationing system.

3.1. Egypt: Clientelist state and rentier economy

Existing literature has shown that the main role of the state in any economic system can be narrowed down to three major functions. (1) The role of the producer of goods and services, (2) the role of the regulator of the system and (3) the role of the supplier of public goods or social goods like primary education and health (Rangarajan 2000)

Different countries shuffled between the different roles of the state in order to obtain the right mix at different stages of development and at different points of time. This was also true for most developing countries in the past 60 years where different degrees of state intervention in the process of economic development were adopted.

The 1950s and 1960s of the last century marked an era of an immense state intervention in many countries. The success of command economies in a lot of European countries has led to the birth of planned economies in many developing countries. The main premise of planned economies was primarily manifested in the total control of the state on the allocation of resources and in the distribution of the national product. The system emphasized the state's guidance in the process of economic planning and involved setting the targets by the state for industry and other activities based on what is considered to be an optimal allocation of resources (Rangarajan 2000). Gerschenkron 1962 and Hirschman 1971 in Barkey & Parikh 1991 confirmed this argument by stating that policy makers in developing countries during that period of time believed that planned economies and sustained state intervention were the prime way to achieve economic development and to compete in the world markets.

In Egypt, the political order under the revolution of 1952 had led to state's intervention in almost every aspect of every citizen's life. Under Nasser's regime the state was the main provider for the masses and the main business entrepreneur. The state played a central and a controlling role in the national economy. Nasser created a clientelist state, where the state controlled all resources and was the only distributor of these resources to certain sectors of the population. Thus creating an evident form of political patronage where the state controls these groups through various grants and guarantees their loyalty to the regime. These grants ranged from subsidizing certain commodities to providing health care benefits and most importantly appointment in certain positions in the government apparatus.

It is argued that the clientelist state is the other side of the coin to the rentier state. In other words, the rentier revenues being totally controlled by the state gives more power to the state and makes it the sole distributor of benefits thus strengthening the state's political authority. This

provides some explanation to the total dependence of the state on rentier revenues and the escalating deterioration of the economy's most productive sectors. These revenues helped the state to maintain power through full control of the economy's resources (Soliman, 2011)

It is argued by some researchers that the Nasserist regime instituted some kind of an unwritten contract between the Egyptian people and the state which stipulates the provision of services to the population in return for full domination by the regime, total submission to the state policies, and the abandonment of political rights and political participation. No wonder the regime used excessive force against any labor movements' actions and in the same time gave social rights to workers. The state took the responsibility of the provision of economic and social rights which strengthened it even further and lead to a growing influence of bureaucracy. This form of state managed to keep the political regime in power

Among the various means that the state relied upon to control the economy and to control the masses were subsidies. Subsidies started in Egypt, even before Nasser's era, as a way to provide a support system for consumers especially for the urban poor. By time subsidies have played another strategic role in the economy. It became a monetary mechanism to adjust wages and prices. Starting with Nasser and continuing under his successors the role of subsidies has changed from being a tool in an efficient welfare system to a fake instrument to maintain balance between wages and prices. This has resulted in many distortions such as decreased productivity of the labor force, low wages, elevated level of unemployment especially disguised unemployment, and the inability of the economy to compete in either regional or international trade (Harik, 1992)

Since Nasser's era, the state has made explicit its mandate to guarantee the provision of basic food supplies for all Egyptians. Over time, Egypt's provision of subsidized bread in particular has become one authoritative tool of the government and a significant symbol of the broader social contract between the government and the population, in order to ensure the legitimacy of the regime and to maintain a political system of limited political participation.

As Singerman (1995) has noted, "The Egyptian Government's policies of political exclusion have gone hand in hand with their public commitment to provide for the basic needs of the population....(T)he government maintains its legitimacy by providing goods and services to the population." (Gutner, 1999)

As a result, food subsidies in Egypt, especially those for bread and flour, have been juxtaposed with promoting political stability. Indeed, sharp increases in the price of food staples and other products in 1977 resulted in regime threatening riots in Egypt. The riots left a legacy of government caution and gradualism on any change in food subsidy strategies (Gutner, 1999)

The few favorable economic growth results that were achieved in Egypt under its planned economy were counter balanced by the mammoth economic losses incurred. Public enterprises instead of generating surpluses for the state for investment had to look for budgetary support from the government. The inefficiency of the public sector enterprises could not be adequately explained other than that their structure and the accountability system were not conducive to promote efficiency. The widespread control mechanism by the state has led to a collapse of the productive capacity and a reduction in competition.

For instance, the widespread price controls that were set by the government on producers whether being public or private have deprived them of earnings necessary for investment and renovations, hence curtailing growth. By those price controls, the government shifts the cost of

the subsidies to the producer whether he is a public producer or a private one. When this happens, the value of the subsidy never appears in the government records, yet this cost that is borne by the producer causes major disincentives to producers, decreases their production levels, deteriorates the quality of their products and decreases the overall productivity and efficiency (Harik, 1992)

In addition, rentier revenues, especially foreign aid, were one of the main pillars of the state resources not only during Nasser ruling but also during Sadat and Mubarak eras. The Egyptian rentier state expanded under Sadat's ruling in the 1970's. At the time, the country experienced massive flows from external revenues from abroad such as workers' remittances and foreign aid which were considered the main drivers of the Egyptian economy (Soliman, 2011). For instance, in the years following 1973 war new sources of external income have emerged. These sources included workers' remittances from abroad, foreign aid given generously to Egypt based on its embarking on a series of economic reforms, oil revenues due to the increase in the international prices after 1973 war and in 1979 after the Iranian revolution, revenues from Suez canal after its reopening in 1975, and also increasing proceeds from tourism. This was a period when Egypt experienced a very high rate of growth in GDP that reached 8 percent (Amin, 2004).

Undoubtedly Sadat and his cabinet managed to mobilize external resources and allow for an increasing cash inflow from the rentier revenues but this was not really a mere coincidence or depending only on a long lasting economic vision of Sadat. Indeed, one major reason for this was to escape the fiscal crisis that faced Sadat after 1973 war. The increasing dependence on external revenues had managed to maintain the stability of the regime for good ten years but resulted in an inflated state that was inherited by Sadat's successor Mubarak and who was faced with an

augmented fiscal crisis that kept building up over the preceding decades to his ruling (Soliman 2011).

By 1989 Egypt's debt service obligations were approximately 40 per cent of total foreign exchange revenues. The economy's condition was moving from bad to worse and was progressively characterized by stagflation and the failure of the state to provide even the minimum services in both health and education sectors. The economy's condition was deteriorating and the state inadequacy to maintain the basic infrastructure was augmenting (Bromely and Bush 1994)

Having this mentioned, the economic problems kept surmounting and the capital output ratio kept rising till the 1980s and the early 1990s which compelled the need for a better efficient use of capital and pushed policy makers to re-evaluate the nature of the mix of state and market and the kind of instruments to be used to stimulate a reform in the existing system.

3.2. Structural Adjustment Program (SAP)

The period of the late 1980s and the 1990s witnessed the adoption of a new system of economic growth in order to overcome the deficiencies of planned economies that were adopted by several developing countries in the preceding period. Structural adjustment programs and liberalization policies using trade and fiscal and monetary instruments were the new adopted policies that attempted to reorganize production and decrease the role of the state as a producer of goods and services and as a provider of welfare systems. It promoted greater integration of the domestic economies into the global one with a focus of the national policies on reduction of external debt and stimulating growth with a limited emphasis on the reduction of poverty (Roy, 1997)

The main Bretton Woods institutions –IMF and the World Bank- have exerted pressures on most developing countries that suffered from accumulated external debts to restrain the ideology of planning in the development process. Instead they put forward the ideology of reducing the role of the state to more intelligent regulation and allow the market forces to steer the development process.

In Egypt in 1991, the growing belief among state bureaucracy that a reform has to take place together with the changing international environment has led to the GOE signing a Stand-by Agreement with IMF in May 1991 followed by a Structural Adjustment Loan (SAL) in October 1991. The IMF agreement focused on regaining the macroeconomic stability of the country through decreasing inflation, eliminating ceilings on interest rates, decontrolling the foreign exchange market and reducing the government's budget deficit. While SAL agreement necessitated the government to undergo major privatization efforts and to undertake radical reforms in both the financial and the trade sectors. These measures were seen as crucial by the Bretton Woods Institutions to counterbalance forty years of invasive state intervention into the affairs of the Egyptian citizens. According to those institutions, Egypt's political economy is at best characterized by state inefficiency and at worst by state corruption which have resulted in major disincentives to the private sector investment and led to incurable macro-economic imbalances such as budget deficit representing 10 percent of the GDP and inflation reaching 20 percent. It was argued that among the main reasons that led to the weak economic performance in the beginning of the 90s is the scale of the public sector enterprises with its guarantee of employment; subsidies for public services, energy and basic food stuffs; price controls; and trade restrictions (Bromely and Bush, 1994)

Alan Richards (1991) summarized Egypt's economic predicament in terms of three major areas. (1) unemployment and the need to generate jobs for the youth, (2) increase exports in order to bring the necessary foreign currency into the country in order to be used for importing food commodities, (3) curbing inflation and attracting local savings into investment by providing incentives to the private sector. Furthermore, Richards believes that the only way to achieving this is shifting the resources and decision making from the state to the private sector and by greater openness to the international economy.

In general, the major problems with SAP policies is that they did not take into account the historical forces which have shaped the socio-economic structure of developing countries and thus leading to a greater complication in those countries' situation and an additional marginalization of the poor who had to adapt to the harsh adjustment programs that did not provide any support for the underprivileged or the vulnerable groups.

Reduction of external debts has exerted a tremendous pressure on most of these countries' economies in terms of debt servicing (external debts as a percentage of exports) due to the falling terms of trade in the agricultural sector of those countries. This in addition to the reduction in public expenditures –including social welfare-as advised by SAP policies, which in turn has augmented levels of unemployment, reduced real incomes and thus purchasing power of individuals especially in the urban sector. Moreover devaluation policies has led to increased levels of inflation reinforcing the poverty of the unemployed and those on low or falling income.

Thus the impact of liberalization on poverty has been acknowledged and the need to address the social aspect of development became eminent. This has caused the Bretton Wood institutions to put forward poverty alleviation strategies and various forms of safety nets. These strategies

included redirecting social expenditure, direct transfers to the poor, targeted employment programs, and food subsidies and nutrition. The main emphasis of these measures was on creating special 'social funds' in order to temporarily reduce the economic burden on those who cannot share in the adjustment driven growth process. However, those measures proved to have limited impact on poverty reduction in the long run. They only served as emergency measures to protect the poor from the negative effect of adjustment (Roy, 1997)

As a result there are multiple lessons learned from the structural adjustment reform experience in developing countries that includes: (1) the state's role as a regulator for the market is essential in order to function more efficiently in line with the goals of growth and poverty reduction. The state's intervention should be market complimentary and not market excluding (Rangarajan, 2000) (2) the role of the state as a provider of welfare benefits is essential as a part of clear vision of safety net policies to protect the poor especially in the early stages of reform and to include them in the economic growth process

3.3 Background for Food Subsidy and the Rising Need for new Subsidy Reforms in Egypt

In order to tackle the subsidy reform issue we need to emphasize the historical evolution of the subsidy scheme. Egypt provides a case of a country with an extensive food subsidy program that has been moderately effective as a social safety net, yet a program that exerts a lot of pressure on the government budget and is unsuccessfully targeted to the poor. Policy discussions about reform strategies to improve the system's performance run into the extreme political sensitivity of the issue of food subsidies in Egypt. Egypt is therefore a country that represents a typical

example of the dilemmas facing policymakers contemplating food subsidy reform in developing countries (Gutner, 1999).

The ration scheme in Egypt was introduced as early as during World War II in order to ensure a supply of indispensable goods such as edible oil, sugar, tea and kerosene to the population at relatively low prices. The cost of subsidizing those goods i.e. food subsidies remained relatively small during the 1950s and 1960s. During the 1970s the food subsidy system was expanded to include more food items such as beans, lentils, meat and chicken. The system kept expanding until it reached almost 20 food items which were accessible on monthly quota basis to all Egyptians who had ration cards. Since the majority of Egyptians had ration cards, subsidized food items were almost available for all Egyptians. This expansion in the food subsidy system was not without cost. By 1975, food subsidies alone accounted for 16.9 percent of total government expenditure (Adams, 2000)

It is worth mentioning that this food subsidy system was a part of a larger welfare program for consumers- which was not essentially directed to the poor- that included explicit subsidies for items like food and implicit subsidies for items like water and electricity (Adams, 2000)

In 1983 GOE was suffering from a persistent budget deficit, increasing inflation rates and high levels of foreign borrowing. The cost of subsidies was seen as a major contributor to the budget deficit. Accordingly, a gradual and slow subsidy reform system was adopted in order to avoid political upheaval and social unrest. This reform included measures like better targeting of the ration card system, reduction in the number of the subsidized food items, reduction in the number of people on the ration card system and also gradually reducing the quantity of particular food items (Ahmed & Bouis & Gutner & Löfgren, 2001)

GOE spending on the safety net and subsidy systems is significant. In 1996/97, the absolute cost of the food subsidy was 3.7 billion Egyptian pounds. This expenditure roughly corresponds to total earnings from tourism, or 58 percent of the revenue generated by the Suez Canal in the same year (Ahmed & Bouis & Gutner & Löfgren 2001).

In 2004 approximately 10.8 percent of GDP was spent on the safety net and the subsidy programs. This accounts to more than 30 percent of the public expenditure. Food subsidy is considered the main component of the Egyptian safety net. In 2005, the financial cost of the food subsidies alone was estimated to be 2 percent of the GDP.

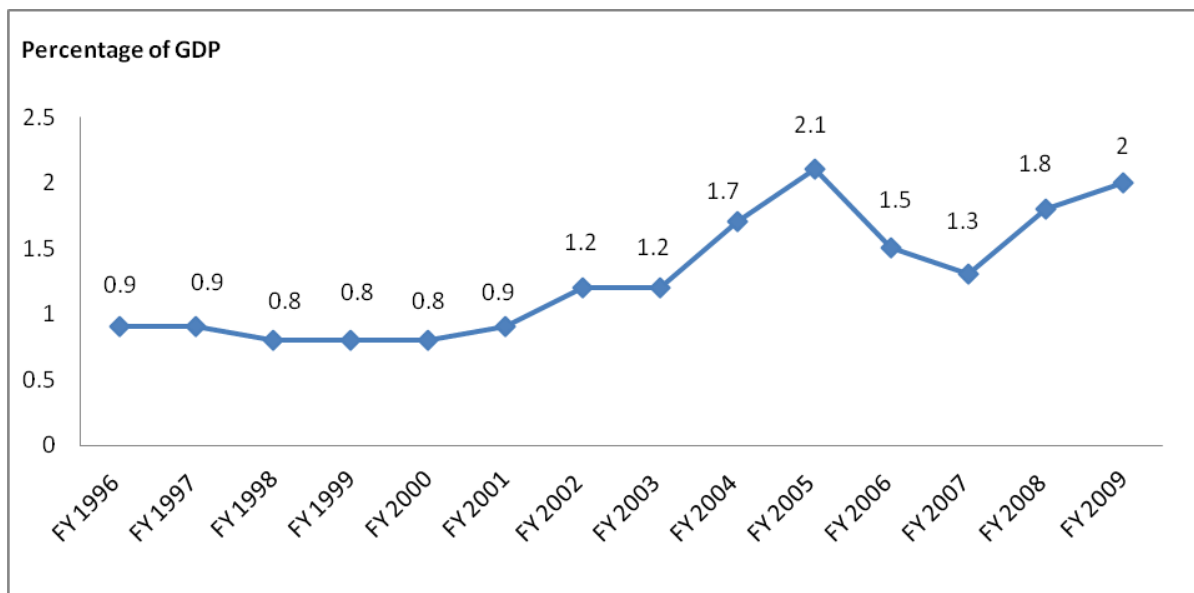


Figure (1) Fiscal Budget Cost of Food Subsidies³

One argument could be that the relative spending on food subsidies as a percentage of GDP might not be very high. However, the problem under discussion is not the absolute or the relative

³ Calculated by the authors using Ministry of Finance budget. Egypt's Food Subsidies: Benefit Incidence and Leakages. Social and Economic Development Group, Middle East and North Africa Region, The World Bank (September 2010)

value of the spending on food subsidies. The main problem is that, the system is ineffective, as one-quarter to one-third of the poor do not benefit from it. In addition to being ineffective, the system is highly inefficient, spending significantly more to deliver benefits to the poor than most comparable programs in other countries. The main reason for this high cost is the inadequate targeting of food subsidies, much of which goes to non-needy households (World Bank, 2005).

In addition based on the data from a vulnerability analysis survey implemented by the World Food Program in 2008, the middle class has the highest percentage of ration card holders (84 percent) while the very high and the very low vulnerable households have the lowest percentage of ration card holders (76 percent). This indicates that about one quarter of the highly vulnerable households is excluded from the ration card system. One explanation for this could be due to the fact that the very high vulnerable groups are most likely illiterate who work in the informal sector. Accordingly they don't have the necessary documents to apply for ration cards. This data indicates the high leakage of the subsidy program resources to the less needy and the least vulnerable and thus calls for better targeting in order to optimally benefit from the subsidy provided

Indeed, one major prerequisite to the efficacy of food subsidy programs is the degree to which they are able to deliver subsidized food to their intended target group. This in turn requires identification of a certain mechanism by which the general population can be screened in order to determine which individuals should receive food subsidies and which should not (Adams, 2000)

Moreover, a significant proportion of the poor and vulnerable are not reached by any of the food subsidies. Poor targeting combined with system leakage leads to only about one-third of the

subsidy going to the needy. This untargeted system permitted all consumers to benefit but it is a very expensive method of improving the food security and nutrition of the poor. Sugar and cooking oil subsidies are not well targeted. About 71 percent of households in the top three quintiles carry the high subsidy green ration cards. In other words, a big percentage of the wealthy families gain large benefits from the food subsidy program. Those richer households receive about 62 percent of the rationed subsidy benefits. Meanwhile, about 10 percent of the neediest households hold the low-subsidy red cards, and about 14 percent of poor households do not have any ration cards (Ahmed & Bouis & Gutner & Löfgren, 2001)

Another study by the World Bank (2005) confirmed this argument. The study showed that many poor households are not reached by any of the existing subsidy programs. The study attributed this to the geographical distribution of the poor, who mostly live in Upper Egypt and to the eligibility criteria for ration cards. Moreover, much of the resources of the food-subsidy system go to households that are not poor or vulnerable. Indeed, the wealthiest Egyptians (the top quintile) receive 21 percent of the value of baladi bread subsidies, nearly three-quarters of 10-piaster bread subsidies and 20 percent of ration item subsidies. These findings were also confirmed by the Ministry of Supply and Internal Trade/ World Food Program (MOSIT/WFP) “Vulnerability and Subsidy Study Phase II.”

Another finding of the same study was that almost 83 percent of the value of food subsidies goes to non-poor households. This means the subsidy program benefits the better off Egyptian families more than the poor ones. It also entails that the current subsidy program wastes a tremendous amount of public resources to the wrong stratum of the Egyptian population. These resources –if optimally targeted- would be available to reduce poverty and assist the most

vulnerable target groups. The same study also concluded that the poverty-reduction impact of food subsidies is very small – only 5 percent of the population is lifted out of poverty as a result of transfers through subsidies.

In response to these findings, the GOE has resorted to adopting a new subsidy reform, based mainly on better targeting in order to avoid leakage of the subsidies' benefit to the non needy or the rich Egyptians. The new system entails better geographic targeting with regards to bread and flour subsidies in order to reach the poorest parts of Egypt and also a revision of the eligibility criteria for high-subsidy ration cards so that they reach the poor as well as reducing the transfers associated with the low-subsidy ration cards (World Bank, 2005)

This is also should be accompanied by other social safety net measures such as the cash transfers for the needy provided by the Ministry of Social Solidarity as well as the Social Fund for Development aiming at alleviating the negative effects of globalization on poor families. This is all part of a new social contract between the government and its citizens for a revised welfare state that is based on a pro-poor vision which favors the poorer half of the society (Egypt HDR, 2005)

CHAPTER FOUR

EGYPTIAN FOOD SUBSIDY SYSTEM AND REFORMS OF THE RATIONING SYSTEM

In Egypt, the food subsidy program is indispensable for a lot of poor households since it provides essential commodities at cheaper prices than the regular market prices. Consequently it frees a portion of these households' income to be spent on other crucial needs such as education and health care (World Food Program, 2008)

The Egyptian government involvement in the food subsidy system started following World War I. The government responded to rising food prices by importing large quantities of wheat and flour from Australia and selling it at a loss in government owned shops in 1919/20.

Nevertheless the food rationing system began as a response to the rising food prices after World War II in an attempt to help Egyptians cope with the scarcity and inflation resulting from the war. The preliminary system was initiated to provide all the population with necessary commodities such as kerosene, sugar, edible oil and tea (Reviewed in Ahmed, Bouis, Gutner and Lofgren 2001). Since World War II, Egypt's food subsidy system has gone through several phases. Among those phases there were two main ones, the first one is the expansion stage of the system in 1960s and 1970s until it reached unsustainable levels in the early 1980s. The second phase is the reduction phase of the system till its contemporary levels.

The food subsidy system expanded in the 1960 and 1970s, representing a part of larger set of consumer welfare policies that also subsidized transport, housing, energy, water, health, education and some non-food consumer products such as cigarettes and soap. These policies

were the government's attempt to hold down and stabilize consumer prices in the face of urbanization and rapid population growth (Ahmed, Bouis, Gutner and Lofgren, 2001)

In the mid 60s ration cards were introduced. In the beginning the cards did not involve price subsidies, but were designed as a quantity rationing system to ensure that all Egyptians received a reasonable quantity of essential food items and that they will be protected from the rising domestic prices and the food shortages. Despite the socialist orientation of the country under President Nasser, (dates 1953- 1970), spending on food subsidies remained a modest percentage of the government's budget, and the primary role of food subsidy policies was to ensure the supply of essential food items. (Ahmed, Bouis, Gutner and Lofgren, 2001)

4.1 Expansion of Food Subsidies

The food subsidy system considerably expanded both in scope and cost during President Anwar Sadat's period of ruling starting in 1970. The number of subsidized food items has increased to include commodities like beans, lentils, frozen fish, meat, and chicken, as well as rice and yellow maize. The system kept growing to reach almost 18 food items.

In 1972 the international wheat prices increased dramatically from \$60 to \$250 per ton. Since Egypt is a major wheat importer, this increased the cost of Egypt imports from \$147 million to \$400 million (Reviewed in Ahmed, Bouis, Gutner and Lofgren 2001). As a result, the expenditures on food subsidies increased from LE 3 million in 1970/71 (only 0.2 percent of total government expenditure) to LE 1.4 billion in 1980/81, which accounted for 14 percent of total government expenditure (Reviewed in Ahmed, Bouis, Gutner and Lofgren 2001). The system was in crisis.

4.2 The 1977 Riots & food subsidies in the context of being a “right” not a “privilege”

Among President Sadat’s attempts to liberalize the Egyptian economy was his endeavor to cut subsidies on some food items in January 1977. The subsidy cuts resulted from negotiations between the Government of Egypt and the International Monetary Fund (IMF) in 1976 over a package of economic reforms for the Egyptian economy. This resulted in major riots known as “Bread Riots” since Egyptians were very angry from the government as they were promised that Sadat’s Open Door Policy will result in prosperity and better living conditions for the Egyptian people and that food subsidy will not be negatively affected by the new model of a more liberal economy. (Gutner, Gomaa, and Nasser 1998 in Ahmed, Bouis, Gutner and Lofgren 2001)

Price increases were announced mainly for fino bread (50 percent) and for 72 percent extraction flour from which fino bread is made (67 percent), as well as for regulated sugar (4 percent), rationed rice (20 percent), tea (subsidy canceled), butagas, the butane gas used for cooking, (46 percent), gasoline (26–31 percent), and cigarettes (different amounts) (Alderman 1986 in Ahmed, Bouis, Gutner and Lofgren 2001).

The riots were violent ones concentrated mainly in Cairo and Alexandria governorates. They didn’t stop until the government announced the cancellation of its plans to cut the subsidies.

The impact of those riots surpassed being drastic. After which Sadat further expanded the subsidy system to increase the value of existing subsidies and to extend the distribution of flour from urban areas to rural areas (Sadowski 1991 in Ahmed, Bouis, Gutner and Lofgren 2001). This major change in his policy was an attempt to counter the criticism against his government regarding social equity. Food subsidies came to be seen as both a safety net to protect the poor

and an important tool in the promotion of social equity (Ahmed, Bouis, Gutner and Lofgren 2001).

The 1977 January riots are one major evidence of how food subsidies represented a major form of patronage in Egypt. At the time the cabinet decided to cut down the government budget and decided that subsidies are the least relatively important item when compared to other budget items like military, investment and debt service. This judgment, according to one analyst, "overlooked the use of a subsidy program as a form of material incentive to secure mass loyalty to the regime" (Baker, 1978 in Hopkins 1988). Indeed, these Egyptian political leaders were not myopic; they knew well the feelings of military, industrial, and financial leaders yet they did not realize the sufferings of the urban poor (Hopkins 1988).

In addition, the riots left a legacy of the government's extreme caution in any economic reform. The riots illustrated all of the strategies policymakers should avoid in reforming food subsidy policy, which is, high, sharp price increases in a political context where the public perceives the changes to be inequitable (Seddon 1986 in Ahmed, Bouis, Gutner and Lofgren 2001).

Since the failure of Sadat's attempt to slash food subsidies in 1977, several trials took place to get the cabinet to approve subsidy changes without success. Shortly after Mubarak came to power following Sadat's assassination, a package of economic reforms was rejected. Instead gradual and less noticeable steps to reduce subsidies were planned in the first half of 1983. Yet, the cabinet was becoming increasingly anxious regarding the enormous liability of subsidies on the government budget and their inevitable growth if prices remained fixed in nominal terms (Hopkins, 1988)

Surprisingly other countries such as Sri Lanka was able to cut down food subsidies dramatically between 1978 and 1980, whereas Egyptian efforts attempted towards slashing subsidy costs were deemed unsuccessful, despite that, for both countries, subsidies were regarded as a right by the citizens.

The failure of the Egyptian case compared to the Sri Lankan one could be attributed to three main reasons. First, the Egyptian government decisions were neither well prepared for nor preceded by a public discourse that could have promoted public consent eventually. Second, the Egyptian government itself was divided over the issue. And third, the Egyptian government was less legitimate than was the Sri Lankan government. In 1977 the government provided almost no preparation for the anticipated changes. Although the magnitude of the subsidy changes was smaller than those announced in Sri Lanka, the Egyptian government has made the mistake of decreasing subsidies without advance warning which was not the case in Sri Lanka. Thus the January 1977 riots were triggered by surprise and instant anger, although the context was almost the same in which growing resentment over the dismantling of Nasserite socialism was common among left-wing trade union officials and intellectuals.

The second reason compares the standpoint towards the issue in Sri Lanka and in Egypt. There was more unity over the issue in the Sri Lankan case. On the other hand, the announced reductions in subsidies in Egypt were the result of a cabinet concession. The debate inside the cabinet was polarized between the progressive economic reformers who perceived the cuts in subsidies as inadequate and recommended more cuts, and the traditional political hands who warned against any modifications in the inherited on-going subsidy scheme. It is worth mentioning that in 1977 the major food subsidy on wheat and bread was not touched; only

subsidies on rice, sugar, and butane gas for cooking were targeted. Thus, certainly the political tactic used to carry out subsidy reductions was poor (Hopkins 1988)

4.3 Reduction Phase

It is common knowledge among policymakers in developing countries that expanding consumer subsidy programs is always politically easier than reducing them. One main problem that often faces policy makers in this case is the poor performance of the system at its far end to provide a safety net for the truly needy. In the same time, it exerts a significant pressure on the government budget. External donor actors, such as the International Monetary Fund (IMF), are often one of the key sources of pressure for food subsidy reform, proposed within broader structural adjustment programs. The impasse often facing policymakers with large food subsidy programs –as in the case of Egypt- is whether, when, and how these programs can be reformed without sparking political turmoil. It is also an issue of concern to donors looking to encourage food subsidy reform in recipient countries, as well as scholars seeking to understand the political and economic factors that contribute to the success or failure of policy reform in developing countries. (Gutner 1999)

When President Hosni Mubarak took office in 1981, he was faced with the daunting task of easing the acute economic burden imposed by the food subsidy system. The rising subsidy costs were seen as a major reason behind the deficit problem. In 1982, he initiated a process of reforming the food subsidy system. During this period, and over the next decade, Mubarak's advisers developed several strategies to gradually reform the subsidy system. The main approach they adopted was a slow transformation of the system as a means to avoid political unrest. This

approach, according to senior Egyptian officials involved in its development, was based on the hypothesis that the most important impediment to subsidy reduction was public perception, a lesson learned from 1977 riots, and if change were introduced gradually, people would not perceive that their living standards were being negatively affected (Sadowski 1991 in Ahmed, Bouis, Gutner and Lofgren, 2001).

The government's specific strategies since the early 1980s have included the following:

1. Attempts to better target the ration card system by introducing in 1981 red ration cards, which offer a lower subsidy on commodities such as sugar, cooking oil, tea, and rice than the existing green card. The red cards are intended for people in higher-income jobs.

2. A reduction in the number of subsidized foods. Meat, chicken, fish, and other foods mainly consumed by higher-income groups were removed from the subsidy program. Subsidies on meat were removed in 1990/91, those on fish and tea in 1991/92, and those on rice in October 1992.

3. Reductions in the number of people on the ration card system. These were cut back from 99 percent in the early 1980s to around 70 percent in 1998. In 1989, MOTS stopped adding newborns to the ration card system. Other reduction strategies included canceling cards owned by people who had died or moved abroad.

4. A slow reduction in subsidies through various techniques, such as gradually reducing the quantity of a particular subsidized food, in some cases gradually replacing it with a more expensive version. An example of this is the increase in the price of bread from 1 piaster to 2 piasters in 1984, without protest or agitating the people. The government's strategy was to introduce a higher-quality 2 piaster loaf alongside the 1 piaster loaf. Over time, the old loaf became harder to find and its quality had deteriorated. Finally, the 1 piaster loaf was no longer produced, but most people switched to the widely available 2 piaster version without complaint.

Using the same strategy, the government further increased bread prices to 5 piasters in 1989, also without stimulating the public or causing any political unrest. Other examples of this quiet reform process for baladi bread include decreases in loaf size (from 168 grams to 160 grams in 1984 and to 130 grams in 1991), and more recently, the addition of maize flour in some areas. The government also ended subsidies on fino bread and 72 percent-extraction flour in 1992 and on shami bread and 76 percent-extraction flour in 1996 (Ahmed, Bouis, Gutner and Lofgren 2001)

The result of these policy steps has been a significant reduction in the number of subsidized foods and a decline in subsidy costs in real terms from a peak of almost LE 6.0 billion in 1981/82 to LE 2.5 billion in 1996/97 in constant 1991/92 prices. In addition, the explicit cost of food subsidies has fallen from 13.9 percent of total government expenditures in 1980/81 to 5.6 percent of such expenditures in 1996/97. Before the exchange rate was unified in Egypt in 1991/92, explicitly subsidized foods also received large implicit subsidies, because the government imported food and other commodities at an overvalued exchange rate. According to World Bank calculations, implicit food subsidies accounted for 39.4 percent of total food subsidies (explicit plus implicit) and 2.8 percent of the gross domestic product (GDP) in 1989/90 (Ahmed, Bouis, Gutner and Lofgren 2001)⁴.

Gradual liberalization of wheat input and output markets since 1987 has resulted in a dramatic increase of domestic wheat production, which tripled between the early 1980s and 1995. While Egypt is still one of the world's largest importers of wheat, its self-sufficiency has improved significantly in the past decade, to just under 50 percent by 1995. Despite these improvements,

⁴ Figures from the World Bank in 1995

there is still significant scope for further improvement in the food subsidy system, particularly by improving targeting and reducing leakage. (Ahmed, Bouis, Gutner and Lofgren 2001)

Currently, the food subsidy system has two major components: 1) ration cards, which offer a predetermined monthly quota of essential food commodities (rice, sugar, tea and cooking oil) to households based on the number of individuals registered on each ration card, and 2) subsidized bread which is available to everybody without certain rationing or pre-defined quota. (World Food Program, 2008)

Ration cards are basically issued by GOE for poor households in order to enable them to purchase basic food necessities at reduced affordable prices. Until 2007, approximately 40 million citizens were benefiting from the ration cards. In 2008 GOE had to increase the number of people registered on the ration card system as a response to the increase in the international food prices. This move included additional 22 million people in the rationing system to reach about 62 million beneficiaries. In addition, the rations for rice have been doubled for card holders.

Figure (2) illustrates that the expenditure on subsidies for the rationed commodities has increased from EGP 0.8 billions in 2002/2003 to EGP 9.4 billions in 2010/2011 with an average annual increase of almost 134%. One of the main reasons for this increase is opening the window for addition of individuals who were born between (1988-2005) to the rationing system. Those beneficiaries were excluded in the reduction phase –as mentioned above- when the Ministry of Trade and Supply stopped adding the new-borns in 1988 to the ration card system. Despite that, my research showed that even with this policy some of the respondents expressed their discontent that they couldn't add their children to the ration cards either due to the difficulty in

the procedure or due to the short period of time specified for addition of beneficiaries who were born between 1988-2005. Another important reason for the increase in the subsidy expenditure on ration cards is changing all the partial subsidy red cards to full subsidy green ration cards in 2008. This increased the total number of full subsidy ration cards to be 11.8 million.

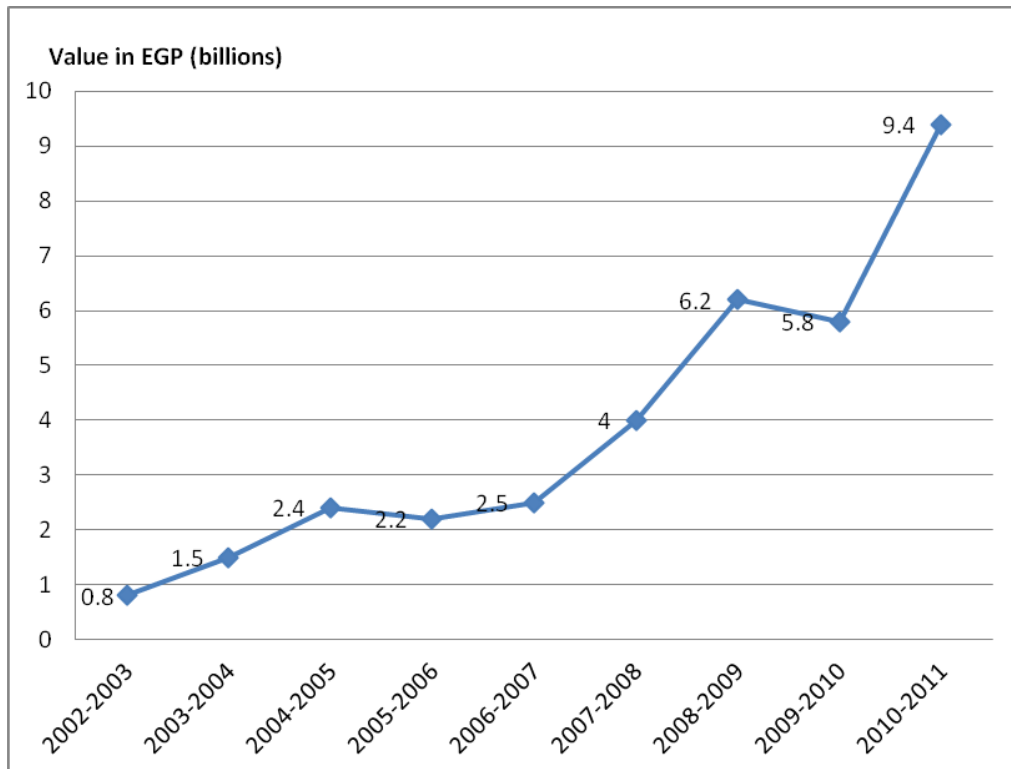


Figure (2) Expenditure on Subsidies for Rationed Commodities⁵

While ration cards provide underprivileged households with significant amount of the most needed foodstuffs, there is still a great opportunity of abuse that take place either by designated grocery stores (Tamween shops) or by the card holders themselves. It is worth mentioning that the majority of households with ration cards are not among the most vulnerable households.

⁵ Source: The Egyptian Cabinet: Information and Decision Support Center (March 2012)

They are literate, permanent employees in the government or the public sector. Highly vulnerable households are less likely to register all their members on ration cards due to improper documentation required for registration (WFP, October 2008).

The ration card system has recently been upgraded to a new smart system. The ragged paper ration cards, that used to be available to all Egyptians to purchase preset quantities of basic foodstuffs, have been replaced recently by more resilient, better looking plastic smart cards, in an attempt to ensure the subsidized foodstuff reaches its target groups of the limited income Egyptian citizens. The new smart cards contain embedded chips that are programmed and fed with the necessary data on the monthly quota of subsidized commodities for each household that owns a ration card. This new electronic card system is meant to enhance the rationing system and to allow officials to better track the distribution and consumption of subsidized goods. It is also planned that the smart cards will be used for other services including healthcare, education and pensions (Omar, 2008).

It is worth mentioning that despite the upward curve in figure (1) representing the absolute value of government spending on ration cards, the percentage of spending on rationed commodities as a percentage to the total spending on subsidies has a less steep curve which signifies an increase also in the total spending on subsidies specifically between the years 2007 and 2009 as a result of the increase in the international commodity prices.

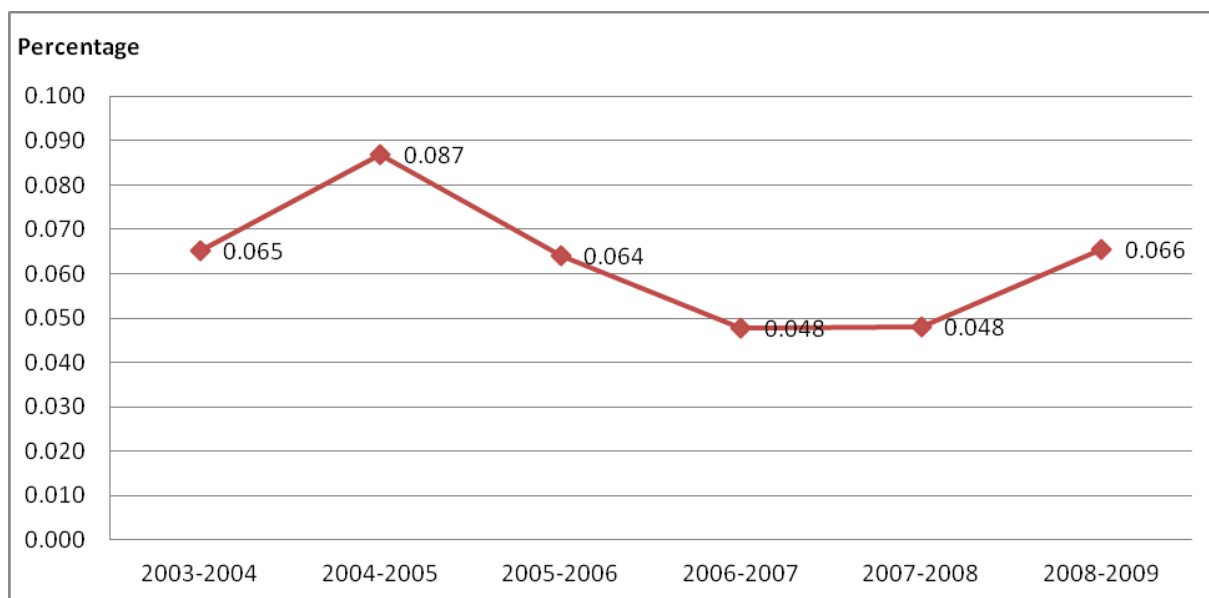


Figure (3) Spending on Ration Cards as a Percentage of Total Spending on Subsidies⁶

⁶ Calculated by the author using Ministry of Finance budget

CHAPTER FIVE

ANALYSIS OF INTERVIEWS & RESEARCH FINDINGS

Before getting into the analysis of the interviews I would like to highlight few points regarding the degree of the ration cards coverage nationwide as well as the administrative details of the old paper cards and the smart ones.

5.1. Ration cards ownership by geographical location

The data presented in this table shows that ration cards ownership are widespread in Egypt throughout its different governorates. Almost 80 percent of the households in Egypt have ration cards. The table shows a comparison of ration card ownership between 2005 and 2008 and indicates that possession of ration cards increased by 1.7 percentage points. Lower Egypt has the highest increment in the percentage of ration card ownership between the two surveys.

The table also shows that ownership of ration cards in metropolitan areas such as Cairo, Alexandria and Port Said (71 percent) is considerably less than in Upper Egypt (77 percent) and in Lower Egypt (87 percent). If broken down by urban and rural sampling units, the data shows that rural households (86 percent) are more likely to own ration cards than those in urban areas (73 percent). In this study each household that owned a ration card was asked whether or not it was a full subsidy ration card or partial subsidy. Generally, 94 percent of ration cards are full ration cards. The survey data showed that 90 percent or above of the ration cards owned in all governorates are full ration cards.

	2005	2008
Total Sample	77.50	79.20
Governorate		
Cairo	70.90	70.90
Alexandria	68.80	71.20
Port Said	73.50	73.50
Dakahliya	81.20	84.10
Gharbeya	81.20	87.70
Giza	60.10	63.30
Fayoum	79.90	87.30
Minia	83.60	84.70
Assiut	79.30	77.70
Sohag	77.80	75.40
Matrouh	50.30	54.50
Region		
Metropolitan	70.40	71.00
Upper Egypt	77.00	77.30
Lower Egypt	81.90	87.40
Zone		
Urban	71.40	73.40
Rural	82.40	85.70

⁷**Ration cards ownership by geographical location (governorates, regions and zones)**

The old ration card system depended heavily on the commitment of shopkeepers to keep accurate ledgers. To receive their monthly allotment of subsidized goods, citizens were required to purchase their goods at designated groceries, where their names and quotas were kept on a

⁷ Vulnerability Analysis and Review of the Food Subsidy Program in Egypt, World Food Program, October 2008

ledger. The individual would sign for goods received on the ledger, while the shopkeeper would sign on the recipient's ration card (Omar, 2008). As mentioned above, the ledger system created opportunities for abuse. One common scenario was for grocery clerks to sell unclaimed subsidized goods on the black market at the end of the month. If a citizen came late to purchase their quota, the shopkeeper would claim that the unclaimed goods had been returned to the local supply office. It would be difficult for the citizen to prove otherwise. The main problem with old system is that it was impossible to know what was left in stock at the grocery, and whether goods had actually been distributed to the citizens according to their quotas, or sold by the groceries on the black market. The new cards identify which citizen purchased the goods, and record the time and location of the transaction, enabling officials to better track the distribution of subsidized commodities (Omar, 2008).

The new subsidy smart cards system is being implemented under a public-private partnership (PPP) between the government and a consortium of private companies handling the project's technical application. The government had a bid and it was specified in the request for proposals that the company that wins the bid for this project would bear the cost of building the entire infrastructure for the project such as the connection of the groceries to the supply offices.

In return, the private partner makes a profit from each smart card transaction. Every time a citizen puts their subsidy smart card in a point-of-sale machine, the government credits the firm approximately LE 2 for the transaction. Moreover the government credits the groceries LE 1 for each transaction made for every smart card that passes through their point of sale machine. This decision was taken based on the low profit that the groceries make from selling the subsidized commodities so this was kind of an additional compensation from the government to the ration

shops (Omar, 2008).

5.2. Target beneficiaries response to policy change

End users had different views with regards to the usage of smart cards as opposed to the paper ones. Their opinions varied from supporting the change to smart cards to opposing it to being a bit indifferent. Yet, more importantly are the issues that came up during the interviews concerning the operation and the administration of the system. As we will see in the following sections, these issues were independent of the smart cards and originally existed in the system but not yet addressed till now.

Views Supporting the New Smart System-Advantages of the New System

Respondents' views that supported the smart cards included the tighter measures on the ration shops to decrease fraud, better price controls and better monitoring on the ration shops from the government. Am Salah who is a simple man who doesn't have a stable job (he sells things in the street and his monthly income is around L.E 200) has a unique opinion regarding the smart system, "I like the new system. I like the new computerized system since it has created a commitment from the grocery shops towards us and has regulated the process of distribution to us. Now the grocery shop owners can't cheat or sell to us with higher prices"

An evident theme that emerges here is that the new smart system has imposed tighter measures on the ration shops (tamween shops) for the benefit of the consumers. Am Salah was particularly impressed with these measures. He says that he used to be with a tamween shop before where the shop owner manipulated the system. Sometimes when Am Salah went to take his rations, the grocery shop owner used to tell him that he didn't not have cooking oil or that he did not have

sugar ...etc. Consequently, Am Salah sees the old system as one that gave the opportunity to some grocery shop owners to misuse the system and use the subsidized commodities for their own benefit. “Let me give you an example regarding the old paper system” he says, “if I have four month worth of rations and I go to take them from the tamween shop, he gives me 2 months only and register in the records that I took four months and this is how they used to manipulate the system”.

Supporting the same argument, Adel who is a tamween grocery shop owner mentions that the new system has imposed tighter supervision on the grocery shop owners. “With the new system, I have to report every month via the electronic system to the authorities about the number of cards that got their rations each month. For instance, if I am assigned 200 cards and 150 families only came and took their assigned rations then I have left overs of rations for 50 cards/families. When I report this to the authorities by the end of the month, they cancel the commodities assigned for these 50 cards from my share of commodities of the following month. In the past with the paper system, the method of reporting depended mainly on the grocery shop owner hand writing this information in the books. So a ration shop owner can easily manipulate the records if he wants to. For example, he can write that everybody got their rations (while this is not true) and uses the left over commodities and sells them in the black market with higher prices for his own profit”

Another consumer (an old man who has his own small private shop for ironing clothes) likes the smart cards new system. He believes that one advantage of the new system is having well defined prices of the commodities since it also appear in the receipts that they take from the groceries. The receipts have the quantities and the prices of the commodities specified for a certain card per month. This was not clear in the old paper ration system. In the old system he

used to pay different prices for the same commodities each month. “One month I pay a certain amount of money and the following month I pay a different amount. One month I pay LE 48, another month I pay LE50 something for the same amounts of the same commodities. The prices were not constant per month although they are the same rations of the same commodities” he thinks that the prices are better controlled in the new scheme and that there is no manipulation of prices in the new system like it used to be in the old one. He also thinks that the new system is better than the old one since the accumulation of months before used to make problems. For instance, if someone accumulated 3 months and then he went to claim them the grocery may start negotiating with him and tells him that he can give him only 2 months instead of 3 for whatever reason and that if he has a problem with that then he can file a complaint against him. So the old system gave the grocery shop owners a lot of power over the consumers. “Now I have 30 days to claim my rations from the beginning of the month till the end” he says, “I can go any day during the month whenever is more convenient for me. It is easier now this way”

Views Opposing the New Smart System-Disadvantages of the New System

The target beneficiaries agreed that since they started using the smart cards they have to take their rations regularly each month. Most of them regarded this as a drawback of the new system. The period specified for each month is from the beginning till the end of the same month. If they missed taking their rations during any month then they can't take it the following month which was allowed before when the paper cards were in use.

One interviewee who is a government employee and whose monthly income is between L.E 700-1000 said: “Restricting the time period to take our rations of a certain month to be during the same month only in the new system is suffocating us. It means that if I missed one month then I

can't take my ration later or during the following month like what used to happen in the old system. This means that my kids will starve for this month"

Another woman who is a housewife, her husband works in the informal sector (manual labor) and who has four children and they are all on the same ration card said: "I don't like this new regulation since sometimes I don't have enough money at the time when I have to go and get my rations. Specifying the time period makes my life more difficult since I need to have the money at a certain time of the month otherwise I will lose my right to take my rations for that month"

Commenting on the same point some interviewees said that they live far away from the tamween grocery shops that they should travel a long distance to get their rations. It was more convenient for them to get their rations every 3 or 4 months when they were using the paper cards. The old system enabled them to have a reduced number of trips to get their rations.

The interviews also rendered a serious drawback in the old system which was not addressed in the new system. The problem is that grocery shop owners need to pay the government in advance for the rations and then they collect the money from the consumers. The cash problem is exacerbated with the tight measures of the new system where the grocery shop owners need to get all their rations month by month.

Adel (tamween shop owner from Matariya) mentioned that the new system has posed a cash problem on the grocery shop owners especially with the increasing prices of the commodities. He explains that, for example, in the past when one kilo sugar costed him L.E. 0.6 he used to buy 2 tons for about L.E. 1200 but now he buys the 2 tons with LE 2500 since the prices are doubled. The same goes for the cooking oil, one ton used to cost him LE 1000 since one kilo was for one pound. Now he buys the ton and pay LE 3000. Consequently, there is a problem with his

resources as a shop owner. In the old system, he used to buy the commodities of the low prices first and sells them and then uses the cash to buy commodities with higher prices. This facilitated his work. With the new system he needs to buy everything within the period of one month which imposes a big financial problem for him. If he didn't have enough money to buy his rations within one month he cannot buy it later and so he loses those rations and thus the consumer loses his rations as well.

Another ration shop owner from Victoria neighborhood affirms the cash problem for ration shops but the explanation is different. He mentioned that the problem is that with the increasing quantities of the rationed goods (For details regarding the additional rations, see Appendix C, Table 1) and with their augmenting prices, now he can't take all the rations for all the families that he is assigned for at one time. He has to go to the warehouse several times per month and pays for the transportation each time which imposes an additional cash burden on him particularly that the government does not pay for the transportation of the goods. He calls it "Mashal".

Adel adds that there is a problem in the availability of the commodities at the government distribution centers (Supply offices). Sometimes there is a shortage in some commodities such as rice for several months. "In the past three months I didn't take all my portions from the rice. Accordingly some of the consumers didn't get their ration from rice and also they could not get it later (in the following month) according to the new system. Thus they lost their rations from rice for these months".

On the other hand, interviewees from another area in Cairo (Hadayek El Qobba) said that in case of a shortage of a certain commodity for one month or more the tamween grocery shop that they

deal with takes notes of the consumers who didn't take their rations as a result of the shortage and then gives them their rations at later months when this commodity is available.

The commodity preferences/tastes of the consumers, are they well addressed in the rationing system?

Interviewees agreed that the four commodities (cooking oil, sugar, rice and tea) are important. The least important is the tea. They also mentioned that there has been a shortage in rice since they started using the smart cards especially in the period following the Egyptian revolution. When asked about the most essential commodities that are most needed for them and that they want to include in the ration cards, they answered that they would like to include macaroni and ghee in the ration cards. They said it is very expensive to get ghee from the market without subsidies.

Based on a nationwide study implemented by the WFP Egypt in 2008, generally ration cards are used by most households who are registered in the system. However, ration cards are more crucial for poorer households where they represent a safety net that improves their food security and may contribute to overall livelihood security by freeing a portion of these households income to be spent on other basic needs such as health and education.

Before 2006 four goods were offered at a subsidized rate. Almost every household uses the ration card to purchase sugar and oil and over 90 percent purchase their entire rations each month except tea where only 54 percent use it. In July 2006 and then in June 2008 households were allowed to buy additional quantities of sugar, oil and rice at lower subsidized rates (See Appendix D, Table 1). 92 percent of households use their additional quotas from sugar and oil and 71 percent uses their additional quotas from rice. An interesting finding of this survey is that

the less vulnerable households purchase additional quotas more regularly which is not a desired result concerning the distribution of benefits from the subsidies.

In addition, the study shows that 45 percent of respondents consider sugar as the most important commodity distributed through ration cards. However for the least vulnerable groups oil is considered the most important commodity.

A qualitative survey implemented in 2005 measuring the food item preferences showed that sugar, oil and rice are the three most preferred commodities distributed by the ration cards. It showed that preference for some items such as ghee, lentils and beans is relatively low. The results also show that the quality of the commodities is inconsistent especially for the beans. Despite that the majority of households continue to use their full commodity ration cards and the inclusion of beans and lentils is an important contribution to the household diet. These results implicate that future policy options regarding the food subsidy system should consider the quality of commodities as a determining factor for inclusion/exclusion of certain commodities (World Food Program, 2008)

An interesting finding from my interviews is that the government pushes for a self targeted subsidy scheme in a subtle way. In other words, with the deterioration of the quality of the subsidized food items, the richer households consume less from these items, thus the low quality subsidized foods become inferior goods and the poorer households consume more of these goods in both relative and absolute terms.

When the interviewees were asked about their level of satisfaction concerning the quality of the commodities that they purchase with the ration cards, their answer was that despite that commodities are not of the best quality they believe that they can't afford to complain. "Those people who complain about the quality must be the ones who earn higher incomes and they are

saying this because they can afford to say it”, says the man who works in the public sector, “As for us we are so squashed, we can’t even be categorized as people with limited income because we can’t even aspire to be in the category of limited income people. We are in a lower category than that. I am a government employee at the Authority of the Buses of Greater Cairo and my whole income is L.E.700 per month including all the bonuses and everything” he adds in a frustrated tone.

System of administration of the rations, Better or Worse? Loopholes innate in the system.

In a trial to know if there are any changes that took place in the administration of the system as a result of the introduction of the smart cards the research yielded information about other problems inherent in the system that are not related to the smart cards such as the cards coverage, registration problems, and the systems of inclusion/exclusion from the subsidy system.

The old system was better for consumers in case there is a shortage in commodities since consumers could get their rations by accumulating several months. Consequently when there is a shortage in one commodity in one month they can get the rations of this month and the following month together. In the new system when there is a shortage in one commodity in one month, there is no guarantee that the consumer is going to have his rations from that particular commodity when it is available. It depends on the grocery shop owner and whether he will keep notes of the people who did not take their rations from one month to another. One interviewee mentioned that this will depend on the relationship between the ration shop owner and his customers. If it is a good relationship then he will take notes and give the customers whatever is missing in the following month. If it is not then there is no guarantee that the clients will take all their shares.

Having this mentioned, one evident loophole comes to the forefront of the discussion and which is not addressed in the new technological smart system. This loophole is that when the citizens put their card in the machine they don't enter the pin codes themselves which corresponds to their rations from each commodity. They give the card to the merchant together with the pin code and he does the transaction for them. So, there is no tracking system that proves whether the commodities reflected in the customers' receipts are actually purchased by them. The consumers don't even take their receipts from the merchant. In addition, the new system can't indeed stop the conspiracy that could take place between the ration shop owners and the customers.

Another thing that came out of the interviews that interviewees were very unhappy that the grocery shop owners charge them about L.E2-4 each month as an additional charge to pay for the transportation of the commodities from the distribution centers to the grocery shop. They called it "Mashal". "The grocery tells us to take it or leave it. If you don't want to pay for the mashal you can go to another grocery shop or file a complaint against me" says Saadiyya, a widow who has 3 married children.

Problems of registration in the system: An inadequate database for ration card beneficiaries

Based on all the interviews there are no limits to the number of family members who benefit from each family card. Some families have up to three generations on the same card. The respondents mentioned that there is a law that was issued in 2009 limiting the number of family members on the family cards to be 4 members. This law applies on the new ration cards that are issued since 2009 but the old ones have no limits regarding the number of family members covered.

Another finding of the interviews is that within the same family there are some members who are not covered by the family ration cards. On the other hand, other families have a family card that includes three generations

The government employee says (in an angry tone) “I have 3 kids who I can’t include in my family card the eldest of them is in the sixth grade. My family card covers only two people, myself and my wife. The kids are: Maha who is in the sixth grade, Menna who is in the third grade and Mohamed who is 2.5 year old. Even the smallest kid could not be added to the family card. I asked several times at the tamween office but they told me it is still not opened and that my request can’t be processed now”

Saadiyya says that she managed to add one of her grandchildren to her smart card. The grand child is 10 years old. She managed to do this when the government allowed the addition of the family members born between 1989 and 2005.

Wafaa who is a widow and have 4 children says that her ration card includes her and one of her daughters only. She just managed to add her daughter when the government allowed the addition of the individuals born between 1989-2005 while she couldn’t manage to add her other two daughters or her son. When she was asked why her children were not originally covered by her ration card she said that when they were born she was not allowed to add them and even now.

Another theme that emerged is the issue of separation of the married sons and daughters from the original parents’ family card . Most of the subjects interviewed confirmed that their married sons and daughters could not get separate ration cards for themselves and their new families. So they stayed with the parents’ original cards. One woman talked about her case and the case of a friend of hers. She said that her friend had a son who got married and so she dropped him from her

ration card but he couldn't do a new family card for himself and his wife. They told him at the Supply Office (*maktab el tamween*) that they cannot yet process his request and they keep pushing the date back, come in July, come in September ... and so on.

Am Salah narrated the story of his son who is married and has 3 kids, he said that when the government announced that people should apply for the smart cards, he applied for his son and his family to have a separate ration card and he removed them from his. As a result of that his son currently does not take his rations. At the supply office (*maktab el tamween*) they told him they cannot currently issue a separate ration card for his son since his son does not exist in their database and the papers have been sitting at *maktab el tamween* for five months with no action till the moment this interview was done.

“The government said that we should do separate family cards for married sons and daughters so I dropped my son from my card since I was told to do that and when I applied for my son and his family to have his own family card, they told me to wait until the new smart cards are issued” he says. Am Salah claims that before the introduction of the smart cards it was possible to separate the married children from their parents' cards and have new cards issued for them. He believes that the government is doing this now together with the introduction of the smart cards in order to impose tighter measures on the number of people who have ration cards. “At *maktab el tamween* they said that they are going to issue new smart cards for the sons and daughters who get married but they didn't say when or how this will be implemented”.

Samia (Um Mohamed) tells the story of her son in law who tried to separate from the ration card of his parents. Samia's husband is from the daily labor (*arzo2y*) and her smart card is in the name of her husband. They are 9 family members benefiting from the card, Samia and her husband and

7 children, 5 of them are married. Her son in law tried to separate from his parents and make a separate smart card for him and his family. He went to the Supply Office at ElKhosous to do the necessary procedures since 4 months (4 month before the time when the interview was conducted) but nothing happened. Samia tried to add her grand children to her smart card but could not since they are young (5 years old and 3 years old). She was told that they are too young to be added to the smart cards. She was told that she can add children starting age 10 or older. “I wish my children separate from me and manage to do their own ration cards with their families”, she says, “The rations that I have on my card are not sufficient for everybody. If they manage to separate and have their own ration cards, the rations will be sufficient for them and their children”, she adds

The difficulty in the separation of the married sons and daughters from their parents ration cards could be regarded as a way of controlling subsidies and excluding more people from the system. This can be explained as follows: The maximum additional commodity rations on each family card are the same whether this family card has 4 individuals or 20 individuals. The maximum additional rations on each family card are as follows: 4 kilos of sugar, 4 bottles of cooking oil, 8 kilos of rice. This amount is the same whether the family ration card has 4 individuals or 20 individuals. There is a minimum of this additional rations and a maximum. For instance, if a family card has two individuals then the additional rations that they are entitled to will be 2 kilos of sugar, 2 bottles of cooking oil and 4 kilos of rice. If a family card has 4 individuals then the additional rations will be 4 kilos of sugar, 4 bottles of cooking oil, 8 kilos of rice. If a family card has 20 individuals then the additional rations will be 4 kilos of sugar, 4 bottles of cooking oil, 8 kilos of rice. We are talking here about the additional rations but if we are talking about the primary rations each individual is entitled to 1 kilo of sugar and half kilo of

cooking oil. This is the reason for the separation dilemma. The government wants to control the rations and not increase them. For instance, if a family card has 20 individuals and those individuals were separated then we will have about 5 separate ration cards with 4 individuals each. These five new ration cards will have 20 kilos of additional sugar, 20 kilos of additional cooking oil and 40 kilos of additional rice instead of 4 kilos of additional sugar, 4 kilos of additional cooking oil and 8 kilos of additional rice when they were all included in one ration card. The beneficiaries pay the same price for the primary rations and the additional ones. So if the ministry opened a window of the families to separate then they will need to supply the grocery shops with larger amounts of the commodities and it will constitute an additional burden on the government.

The problem in registration is affirmed by the study made by the World Food Program in 2008.

In the survey households that did not have ration cards were asked about the reasons for not being registered in the system. The data shows that 38 percent of households mentioned that they have information about ration cards but could not register, 22 percent of households mentioned that they didn't have enough information about the system and 17 percent of households mentioned that they were late for re-registration. At the regional level, the data differs from one region to another. About one third of metropolitan households who didn't own ration cards mentioned they didn't have enough information about the system. This percentage decreases to 14 percent in Lower Egypt region. Moreover, 47 percent of households in Upper Egypt who did not have ration cards mentioned they have information about the system but could not register. This figure decreased to 29 percent among metropolitan households. The figures also differ from one governorate to another. For example, 71 percent of households in Giza who didn't have ration card mentioned that they had information but could not register, on the other hand 25

percent of households in Dakahliya mentioned this reason. Also, only 11 percent of households who didn't have ration cards in Gharbeya mentioned that they didn't have enough information about the system. This percentage increased to 36 percent among households in Cairo.

The survey also collected data about reasons for not having ration cards by household characteristics. The data shows that the most vulnerable groups are more likely to mention that they have information about the system but could not register than the least vulnerable groups (World Food Program, 2008)

Interviewees agreed that the procedure of issuing smart cards was simple. They went to the tamween office with their old paper ration cards, national IDs and birth certificates of the young children. They said that they could not add new individuals to the smart cards at the time. So the same number of individuals who were on the old paper ration cards were transmitted to the new smart ones.

One woman said that the government allowed a window of one month in the beginning of 2010 for people to add new individuals to their ration cards. She said that her ration card originally included 5 individuals and she managed to add her grandchildren to the family ration card but in the same time her son and his family could not separate from her ration card and issue a new one for them.

Enhancing the rationing system or cash transfers?

When asked about their suggestions for a better rationing system, the beneficiaries said they wanted to add more commodities to the cards like lentils, pasta, ghee and tomato paste. They said that these commodities used to be part of the ration cards before and they would like to reinstate them.

Am Salah suggested that private companies can help the government to subsidize the essential commodities to the poor as part of their corporate social responsibility. Those companies can provide their commodities to the poor at subsidized prices.

They all agreed that it would be better if all prices of the rations decreased in addition to increasing the availability of the commodities. They complained from not finding the commodities that they need each month. They also suggested that they would like the additional rations to be increased at lower prices.

When asked about their opinion regarding substituting in-kind subsidies to cash transfers interviewees didn't like the idea and thought that this would be only a trap or a tactic used by the government to camouflage a policy of subsidy removal. They think that in-kind subsidy is better since it secures the basic needs of the family each month. There is also a sense of security about being sure of getting their rationed commodities each month. They thought that whatever the amount of cash transfers that they would receive as a substitute for the rations would not be enough to buy the commodities from the market without subsidy and that inflation is always ahead of them and they will never be able to keep up with the price increases. One advantage about the existing system is that prices are fixed within the subsidy system. They didn't advocate the idea even if the compensation is double or triple the subsidy that they are currently taking.

CHAPTER SIX

ALTERNATIVE APPROACHES

Our qualitative analysis has indicated that the smart cards are a good technological advancement but there are other problems that are inherent in the system that has not been addressed and that still cause a lot of inefficiency. The prime problem is the lack of a well targeted database of beneficiaries. The various reforms undertaken by the government have led to a sporadic and inconsistent system of identification of beneficiaries which in turn led to many inclusion and exclusion errors. The identification of beneficiaries is still not well specified depending on certain criteria like means testing for example. There is a sporadic system of identifying very poor people and issuing new cards for them by social researchers from the Ministry of Social Affairs. Having this mentioned, I propose some policy options that could be implemented in the long term for modification of the subsidy system based primarily on minimizing the errors of exclusion of the poor and an accurate identification of the beneficiaries.

Proxy Means Testing

Geographical targeting has proved to be insufficient to accurately target the poor in many developing countries. In order to achieve better accuracy in targeting means-testing is usually utilized. In Egypt, a proxy means test has been already developed by MOSS using 2004/05 data, however it needs to be updated and brought together in a national framework with adequate information and administrative systems in place (Worldbank, 2010)

As mentioned earlier, the Egyptian subsidy system has numerous inclusion errors that include non-needy individuals and households which in part due to weaknesses in targeting mechanisms.

It is a common problem among many developing countries that identification of the poor is often flawed as many public safety net programs rely on selection criteria that are neither observable nor verifiable (Reviewed in Sharif, 2009).

Proxy Means Tests is a system of targeting that entails using easily recognizable and verifiable household or individual characteristics in a formal algorithm to proxy household welfare. These variables are selected based on their ability to envisage welfare as measured by, for instance, consumption expenditure of households. Such a scheme is often preferred for its transparent process and objective criteria, cost efficiency and its potential capacity to minimize to some extent elite capture. The administrative difficulties juxtaposed with sophisticated means tests, and the imprecision of the results due to the problems with measuring income also provide a strong basis for employing proxy means tests. Similar to means tests, proxy means tests can be costly relative to other forms of household level targeting (e.g. community-based targeting methods). Nevertheless, they tend to produce the lowest errors of inclusions and hence are considered good investments (Sharif, 2009)

In order to maximize the benefit from proxy means testing civic engagement is much desirable in the execution of such methods. Implementation details extremely matter to distributive outcomes, as is evidenced by the significant success of Bangladeshi nongovernment organizations (NGOs) and microfinance institutions (MFIs) in their ability to reach the poor with services that merge safety net type interventions with microfinance products. Their success in targeting the poor could be attributed to their profound presence on the local level and knowledge as well as efficient management information systems funded by donors (Sharif, 2009)⁸.

⁸ World Bank 2007

Academic evidence and practical experience both recommend using proxies for consumption expenditure and predict that it can target the poor with a realistic level of accuracy. For example, some studies use regression analysis to point to a set of variables that are able to proxy for welfare levels (Reviewed in Sharif 2009)⁹. There is also successful practical experience from Latin American countries like Chile which have been using a PMT based targeting system since the 1980s, and from other countries such as Colombia, Costa Rica and Mexico who have implemented this targeting system more recently in the late 90s. In all of these cases, the PMT based targeting system managed to achieve very good targeting results (Reviewed in Sharif 2009). For instance, between 80-90 percent of the benefits of proxy-means tested programs in Chile and Mexico are received by the poorest 40 percent of the households in those countries. The effectiveness of proxy means testing has also been documented in an earlier comparative study which found that among all targeting mechanisms proxy means tests tend to produce the best incidence outcomes in developing countries. Proxy means tests are known to especially distinguish chronic poverty well which makes it an appropriate targeting option in countries of severe and extensive poverty (Sharif 2009)

However, Proxy Means Tests is plagued with inherent inaccuracies especially when targeting the poorest of the poor. Grosh and Baker (1995) find that proxy means tests have significant levels of errors of exclusion when trying to target the bottom 10 to 20 percent of the population. Yet they minimize errors of inclusion when compared to no targeting or universal provision systems. There is also recent evidence from Pakistan that is consistent with the above view. Such evidence suggests caution when using a PMT based household targeting system for safety net programs, and calls for designing PMT models that would minimize these targeting errors. For instance,

⁹ Also in (Glewwe and Kanaan, 1989; Grosh and Baker, 1995; Narayan et al, 2005; Ahmed and Bouis, 2002)

combining the PMT with geographic or community level outreach and validation where appropriate and practical can enhance accuracy (Reviewed in Sharif, 2009). Moreover, existing international experience suggests that PMT based targeting systems take time (at least 18 months) to design, pilot and implement on a large scale. So having the institutional set up to implement the targeting system is just as important as having a strong workable PMT formula. For instance, there is a need to have an adequate data collection strategy and reliable management systems to ensure the accuracy of household assessment mechanisms as well as appropriate monitoring and evaluation mechanisms to guarantee transparency, accountability and control of fraud (Sharif 2009)

Community Based Targeting

Despite of the importance of social safety nets in developing countries, this has not been translated into successful action because of the failure of traditional social welfare ministries to effectively target and engage the poor. Given this fact, experimentation with new bottom-up service delivery options and poverty alleviation mechanisms have come to the forefront scene.

Such mechanisms should actively engage the poor and their communities in program design, implementation and monitoring. Examples include reforms that decentralize the delivery of public services to local governments, community management of forests and other natural resources, and group-based microcredit programs. In addition, demand-driven social funds that aim by design to extract community involvement have become progressively more popular with governments and donors, and international organizations such as the World Bank now make

community participation an explicit criterion for funding approval for a growing list of projects (Reviewed in Conning and Kevane, 2000)¹⁰.

There is considerable evidence that advocates community participation and proposes that it can lead to improved project performance and better targeting (Reviewed in Conning & Kevane 2000)¹¹. For instance, a study of India's Integrated Rural Development Project found that Indian states which employed village councils to select beneficiaries had a much smaller proportion of non-poor participating households. A large recent survey of dozens of country experiences with social safety nets conducted by Subbarao et al. (1997, p. 87) for the World Bank contends that programs that engage communities, local groups, and NGOs can realize enhanced targeting outcomes (Conning & Kevane 2000). Generally, the design of any social service or benefit delivery program faces the difficulty of obtaining reliable and accurate information in order to determine beneficiary eligibility.

In theory social safety net could be administered via a single central income tax office that would make transfers based on self reported income or other household or individual attributes. In practice all programs depend on welfare agents to assess eligibility and deliver benefits. The reason for this is that even in well developed industrialized countries where the income tax base is broad, self-reported data is not very reliable and a welfare program generates incentives for dissimulation. Given the cost and difficulty of audits, benefit eligibility tends to be conditioned on personal or household characteristics or 'tags' that are believed to be easily observable, measurable and less manipulable. These tags include but not limited to employment status, age,

¹⁰ Worldbank 1996 & World Food Program 1998

¹¹ Also in Baland and Platteau (1996), La Ferrara (1999), Narayan et al. (1997), Wade (1988), Isham et al. (1995)

gender, and number of dependents (Akerlof 1978, Besley and Coate 1995, Boadway and Keen 1999 in Conning & Kevane 2000). Tagging is an even more important mechanism for targeting social spending in developing countries where income tax systems are often weak or non-existent, and where information asymmetries can be relentless.

There are several reasons as to why community based targeting is considered an effective targeting mechanism. First, local community agents often have better information on household characteristics, needs and recent events upon which to stipulate beneficiary eligibility. This is an advantage that they have over any outside welfare agents who have to count on unsophisticated and outdated proxy indicators (Cremer, Estache and Seabright 1996 in Conning & Kevane 2000). Thus, this leads to a significant reduction in targeting errors of inclusion or exclusion. In addition, better information may also significantly reduce administration costs compared to other programs administered by less informed welfare agents. As the latter must rely on screening and monitoring devices such as costly audits and indirect incentive systems that hinders the quantity and the quality of benefits delivered. (Conning & Kevane 2000)

Second local community targeting can help avoid a major hindrance in targeting which is corruption and misinformation. Community agents will be intertwined in widespread and dense networks of social interaction, thus, reducing the cost of cooperation and coordination.

If we think of the allocation of benefits as the result of the continuous interaction between local intermediary agents and members of the community, the more the agent overlaps with local community members who might strike back in other dimensions of social interaction, the less likely the agent is to cheat in any one dimension. In other words, local social capital of accountability, can make a difference when it comes to community based targeting. So if

performance in one arena is closely related to results in other arenas, such as multi-issue local politics, cooperation and accountability are more likely (Conning & Kevane 2000).

Third, by raising the rewards to participation, community targeting could connect and strengthen social capital and community organizations, with positive externalities.

Particularly in countries that have a strong legacy of planned economies and heavy state intervention in almost every aspect of citizens' lives, community based targeting mechanisms may help to crowd-in rather than crowd-out new civic society groups and private safety nets.

The basic idea is that by giving communities ownership over new local public goods projects, and/or by insisting on community co-responsibilities requirements, incentives can be generated for members to organize private energies and resources for the common good. Indeed, there is considerable subjective evidence that community-based targeting increases local social capital.

There is evidence from indigenous communities in Mexico, where waves of decentralization in provision of public goods and services, followed by crackdowns of control expanded the reach and capacity of local social institutions (Reviewed in Conning & Kevane 2000)

To empower marginalized groups community-based targeting may need to integrate some of the lessons of the social fund approach, and adopt a demand-driven approach that widens the diversity of participating community agents. The local community could then include semi-formal or informal village councils, school boards and mosques, organized NGOs, or perhaps ethnic groups and traditional leaders, assisted perhaps by institutional organizers. Each of these community institutions will vary in terms of their access to information, embeddedness in monitoring institutions, willingness to engage in rent-seeking, and their propensity to be responsive to the poor.

Moreover, in many cases there is strong likelihood that the prevailing stronger community groups will tend to rule out weaker groups, one possible way to target excluded groups is to explicitly use categorical targeting or quotas. For example, in the state of Karnataka in India the composition of the mandal panchayat (group of villages) reserves a quarter of all seats for women, and 18 percent for members of scheduled caste (Conning & Kevane 2000)

Grameen bank is one example of an organization that has achieved relatively good targeting results based partially on categorical targeting such as targeting women and imposing wealth ceiling eligibility requirements (Conning & Kevane 2000).

Step 1: Integrating proxy means testing with community based framework

In order to develop a proxy means test formula (PMTF), a weighted combination of “proxy” variables or indicators have to be compiled which together can identify whether a household is poor or not. In order to identify an appropriate set of variables and weights data has to be collected on income and expenditures of households. This household welfare data is used as a benchmark for calculations on the incidence of poverty (Sharif 2009)

As New Institutional Economics emphasizes the role of institutions in social provision and in order to achieve a better reach to the most needy individuals, households and groups who are mostly marginalized and not included or registered in the official databases, a community based framework needs to be adopted in the collection of the survey data, inclusion of the opinions of the poor and in the monitoring, evaluation and follow up.

In 2008 shortly before the Egyptian revolution a study was conducted in order to identify the main sources of the socioeconomic discontent of the economically deprived members of the

Egyptian society. Over 3000 questionnaires were sent to NGOs and were distributed among vulnerable households in 20 governorates in both urban and rural Egypt. Participants were divided into stratified samples and were randomly selected from the beneficiaries of these NGOs. Those NGOs had a direct access and wide networks in their local communities that extended among different socioeconomic classes as well as various ethnic and ideological positions in the society. The response rate was 75.6 percent which entails that NGOs were quite successful in reaching and convincing respondents to participate.

A series of regression models were run afterwards in order to unleash what Egyptians perceived as the root causes of their poverty. Based on this data a composite indicator of poverty based on societal welfare preferences was established (Abdel Baki, 2011)

Following the same approach, a similar study can be conducted nationwide where data collection is managed by community agents or local NGOs who have a deep and extensive presence in their communities. The study should aim to collect information regarding the current household demographics and socioeconomic conditions as well as the beneficiaries' subjective identification of the root causes behind their poverty (Abdel Baki, 2011). The data collected from this study should be used as the major welfare proxy indicators to be entered in the formal means testing algorithm.

This kind of survey or study can help to face one of the main challenges that could face future governments which is to establish a mechanism of mediating between individual groups that are divided by vast religious, cultural and educational differences. This challenge is exacerbated by the absence of democratic political institutions which will require joint efforts on both the individuals' and governmental parts. After collecting adequate data from individual groups and engaging them in national-scale discussions, policymakers could coordinate viewpoints in order

to make optimal decisions and then transform them into procedures, policies and laws. (Abdel Baki, 2011)

However, there are two critical factors for the success of such a framework. First, it is vital to strengthen communication channels and to increase the occurrence and level of intensity of discourse and interaction between members of the society. Second, the transition from one stage to another needs to be improved by ethical commitments. The installation of a strong ethical leadership draws the inspiration of individuals and enables a higher level of commitment, cooperation, trust, and shared values among members of the society.

Furthermore surveys need to be updated frequently in order to monitor the changes in societal preferences. Any changes in the socio-political circumstances, age structure, the level of education and the extent of gender participation impacts individuals' choices thus, surveys need to be conducted frequently to update the policymakers' awareness of societal changing perceptions. (Abdel Baki, 2011)

The final choice of variables should be made based on several criteria among which that those variables are easily recognizable and measurable, cannot be manipulated easily by households in order to minimize errors, and that they are not politically sensitive. There are often trade-offs when choosing variables based on these criteria and in the end a pilot testing of the variables on the ground is recommended to ensure that the final choice of the model is robust.

Following the PMT model in Bangladesh, the variables that have been found to be highly correlated with poverty fell broadly into four categories: (1) household demographics and characteristics of household head; (2) ownership of easily verifiable assets; (3) housing quality,

access to facilities and remittances, and participation in anti-poverty programs; and (4) location variables (Sharif 2009)

Cost effectiveness of the proposed approach

The proposed approach for targeting uses multiple targeting methods and in order to ensure cost effectiveness the same targeting system should be used for multiple programs. The same database that will be created using this approach should also be used for any social assistance benefits, health subsidies, cash or in-kind assistance.

Colombia is a good example to illustrate this argument. It first developed its proxy means test to target subsidized health insurance, and later used it for targeting hospital fee waivers and its CCT, public works, youth training, and social pension programs. In addition, other countries like Armenia, Chile and Jamaica also use their proxy means test for several programs. There is also an additional benefit from this approach since it does not only provide for economies of scale in the targeting system, but can also lead to a more integrated package of support for households that can provide better risk management and more effective assistance for moving them out of poverty which should be the ultimate goal for assistance programs.

Furthermore, the use of multiple targeting methods within a single program generally produces more accurate targeting results than the use of one approach (Worldbank 2010).

Also, the smart card is an exceptional innovation that can be effectively used for poverty targeting. Yet it must be understood that a targeted system is not a utopian one where it will be the best solution with no problems. For instance, in India the Public Distribution System (PDS)

was reformed to be the targeted PDS (TPDS) in 1997. Some recent studies show that the TPDS has high exclusion error (excluding poor). This is attributed to fine targeting that increased the probability of excluding the needy. Moreover, some asymmetries in the information could exist depending on how targeting information is collected. To sum up, the experience in India shows that shifting the primary mode of intervention is possible, however, there is a chance of emerging new problems, making program modifications an incessant process (Worldbank 2010)

Step 2: Shift from in-kind transfers to conditional cash transfers

The rhetoric of the shift from in-kind transfers to cash transfers has been very controversial. One argument states that the idea of substituting in-kind support for cash transfers would create inflation in the economy. Moreover, our qualitative data from the interviews showed that almost all respondents resisted the move to cash transfers out of fear from the uncontrolled prices as well as mistrusting the government that this would be only a transition step towards eliminating subsidies altogether. Since my interviews were limited geographically to only two governorates, further research should be done in order to test the feasibility of the shift to cash transfers and whether or not this shift in policy would gain public consent.

Indeed Egypt can benefit from other countries' experiences; we have successful experiences from Latin America of shifting from universal subsidy provision of tortillas and milk to conditional cash transfers. It is worth mentioning that the shift to cash transfers can solve one of the prime two drawbacks inherent in the food subsidy system which is the leakage of the subsidy benefits between the ration shops and the consumers. The same argument is confirmed by Marzaban, Consultant in the World Food Program, who believes that cash transfers could contribute to reducing leakage of the food subsidy benefits which is estimated to be between

15% to 20% annually. He adds that this also would give the consumer more freedom of choice regarding the commodities purchased. In addition, cash transfers would eliminate one prime problem of the rationing system which is the existence of multiple markets for the same commodities which creates a big chance for manipulation and selling rationed goods in the black market with higher prices (Gab Allah, 2007).

I have chosen one experience that links cash transfers to education, health and nutrition which is the Mexican experience. The reason for choosing this successful experience is that it is argued that poverty is not an economic state rather than a state of mind and a state of affairs. In other words, in order to alleviate poverty first the dependency relationship between the government and the needy has to be broken. I am not arguing that the government abandon social safety measures altogether but I am advocating an empowerment approach that helps to break the intergenerational cycles of poverty in the long run. This cannot be achieved with in-kind or cash transfers alone but government assistance has to be linked to other programs with greater emphasis on integrating the poor into the economy so that they may eventually rise out of poverty through their own efforts (Sanders, 1990)

Lessons from the Mexican experience: Oportunidades

Oportunidades was first created in 1997 under the name Progresá before it was changed to its current name in 2002 under the new government in Mexico. The objectives of Oportunidades are to empower poor households in Mexico in order to break the intergenerational cycle of poverty. The program's main mechanism in achieving its objectives is through an integrated approach which targets poor households with children. The program is based primarily on the concept of "co-responsibilities" and households have to comply with certain conditions in order to be

eligible to the cash transfers. The eligible households should enroll and regularly send their children to school and attend regular health talks/workshops and health care appointments. If households abide by these conditions, mothers receive a cash transfer every two months which supports household income. In addition, they also receive education grants for the children and nutrition supplements, and further income support for the elderly and for household energy expenses. (See Appendix B for program components)

It is worth mentioning that the strength of this program lies in its design around two essential pillars. First the cash transfers are conditional depending on the idea of co-responsibility of the beneficiaries. It is like a contract where each party has to fulfill its role in order to reap the gains. Co-responsibilities are based on the understanding that families are active in their own development thus breaking the concept of total dependency upon the donor-government in this case. Therefore, in order to receive the income transfer, children must attend school regularly and families must visit the health centers as required. The second pillar is that Oportunidades transfers the income and therefore the responsibility to meet the conditional requirements, to the mother of the family. The objective is to empower women through strengthening their position in the family and the community (Holmes & Slater, 2007)

The impact of Oportunidades has been very positive on education, health and nutrition based on several evaluations done on both rural and urban areas between 1997 and 2003 for rural areas, and between 2002 and 2004 for urban areas (Reviewed in Holmes & Slater, 2007).

With regards to education, Oportunidades increased the enrolment for the transition from primary and secondary school, and higher secondary school, particularly for girls. It also

decreased school drop outs, increased school realization, and encouraged parents to support the continued education of their children and the achievement of their school obligations.

With regards to health, Oportunidades has reduced maternal-infant mortality rates, decreased morbidity and incapacity, increased the access to public health services and reduced the use of private services.

With regards to nutrition: Oportunidades reduced the prevalence of anemia and increased the height and weight of young children. The program improved the household diet by enabling households to buy animal products and improved children's nutrition through the nutrition supplement.

The program has also operated well administratively. The World Bank states that the operational expenses represent less than 6% of the total cost of the Program (Rodriguez and Jordan 2007). The program is efficiently utilizing its resources because of its slim structure (Oportunidades optimizes processes institutionally by relying on links with the Health and Education sectors, and focuses on the demand side, not the supply), efficient targeting, and good administration and management. (Holmes & Slater, 2007)

Indeed this is a considerable achievement with regards to assistance programs generally in developing countries where these kinds of programs are characterized by poor targeting, leakage of benefits to the non poor and high administrative costs. Moreover, the program also depends on community volunteers to help organize and strengthen the efficient functioning of Oportunidades at the local level.

Oportunidades targeting criteria focuses on reaching the poorest 25% of the population. The

program has demonstrated effective targeting mechanisms with minimum exclusion errors (Patrinos and Skoufias 2007) indicating that the increased use of health and education services of Oportunidades participants has led to greater equality in access to public services for marginalized populations.

Another unique characteristic of the Oportunidades is that it puts gender empowerment at the core of the program design and implementation. This is achieved by transferring income to the female head of the household, financially encouraging girls' education, providing health support for pregnant and breastfeeding women and promoting the leadership and citizenship of women beneficiaries, particularly the local volunteers. Thus the program aims to contribute to changing gender roles and furthering the integration of women into their communities. (Holmes & Slater, 2007)

In addition, there is evidence that women participating in Progresas' activities such as health talks and collecting benefits had developed new forms of social capital (Adato 2000).

Oportunidades evaluations show that the program has increased women's independence (Cruz et al. 2006). There is some reported increase in the degree of involvement of beneficiaries in community activities but the impacts are not yet very clear. Qualitative evaluations show that in urban areas where Oportunidades operates there has been an increase in the sharing of food, lending money etc. between families. This is said to have improved social relations in the community in comparison to before beneficiaries participated in the program. Similarly in rural areas, there is a reported increase in participation in community activities which wasn't there before (authors' interviews, 2007).

One advantage of the Oportunidades that it realizes that health, education and nutrition are not enough on their own to help people to move out of poverty. Indeed, they need supplementary programs in order to equip them with the necessary skills to help them enhance their socioeconomic status. One of the main roles for Oportunidades is to act as a facilitator between these other programs and the Oportunidades families. Among these programs that Oportunidades are trying to connect to: adult education, social assistance, e.g. welfare for disabled children provided by the state, improving housing e.g. firm floor on the house and Infrastructure (Holmes & Slater, 2007)

Egypt can positively benefit from the Mexican experience and replicate Oportunidades. One difference should be that targeting of the poor should depend on the results of the integrated approach of proxy means testing and community based targeting. After identification of the poor and who should benefit from such a program and after building a reliable database to be used for different social assistance programs nationwide. A replication of Oportunidades should take place in the long run as a way of tackling the poverty issue with more precision and with a practical approach that would eventually support the poor and help them to be integrated in the economic mainstream.

CONCLUSION

Despite achieving a considerable cost reduction over the past few decades, the absolute cost of food subsidies in Egypt is still high relative to the benefits gained by the poor. Indeed, there is a significant opportunity for reform through many ways, the most important of which is better targeting and better identification for the poor who should benefit from food subsidies. The reform for the rationing system is crucial and more feasible since there is a considerable leakage of the benefits of the subsidized commodities to higher income groups on one hand and also commodities like the sugar, cooking oil, rice and tea are regarded to be less politically sensitive than the bread and the wheat flour. Thus a reform in these food items if done tactfully could gain some relative public consent.

Since the mid-1980s, the Government of Egypt has used variable strategies to gradually reduce food subsidy costs. These strategies have included increasing the price of subsidized food commodities; reducing the number of ration card holders; and decreasing both the number and quantity of subsidized food commodities available to beneficiaries. Consequently, the explicit cost of the food subsidy system has declined in both real terms and as a share of total government expenditures (Ahmed & Bouis 2002).

While the present system of food subsidies has generally been effective as a social safety net to help protect the poor during economic downturns, it has major disadvantages among which:

1. The absolute cost of the present food subsidy system is still high relative to the benefits received by the poor. The total cost of Egypt's food subsidy system in 1996/1997 prices was 3.74 billion Egyptian pounds (LE), or about US\$1.1 billion, The fiscal cost of food

subsidies kept rising until it reached about 2 percent of gross domestic product (GDP) in 2008/09 (LE 21.1 billion, or US\$ 3.8 billion). The rising cost of food subsidies can be explained by increased international commodity prices, exchange rate depreciation, increased number and/or quantities of subsidized food items, and expanding coverage of ration cards (Worldbank 2010)

2. The current system is not well targeted to the poor; almost 60% of subsidy benefits go to higher income groups constituting the top 60% of the population in the income distribution. (Ahmed & Bouis 2002).
3. A significant number of the poor have limited access to subsidy benefits. For instance, most of the manual labor who don't belong to the formal sector of the economy or women headed households who work as servants or as any form of manual labor.
4. Considerable shares of the food subsidy benefits are misdirected in the distribution system before reaching the target beneficiaries. A large part of the food subsidies are diverted away from the consumers through selling subsidized foods at a higher price in black markets or open markets. Also, a large part of these subsidies go to the richest groups while many poor do not receive any of these benefits. These are examples of leakages in the subsidy system. In 1997, the total cost of leakages in the Egyptian food subsidy system accounted for about 16% of the total cost of food subsidies. In 2008/09, LE 5.5 billion (28 percent) of food subsidies did not reach intended consumers, with baladi bread accounting for 68 percent of the leakage and cooking oil for 20 percent (Worldbank 2010)

Because of a combination of poor targeting and systemic leakage, only about one third of the total food subsidy incurred by the government goes to the poorest 40% of the population. There is scope for better targeting the food subsidy system in ways that can reduce benefits to non-needy (and, thereby, cut costs), while protecting the poor (Ahmed & Bouis 2002).

For that reason I attempted to study the target beneficiaries' response to one of the latest policy changes in the rationing system which is the introduction of the smart cards. Views ranged between opposition to some aspects of the new system and between total satisfaction due to the imposition of tighter measures on the ration shops and reducing their ability to manipulate the system.

Our qualitative analysis confirmed the loopholes inherent in the rationing system as well as the lack of vision regarding previous reforms taken by GOE. The disorganized, sporadic and non-confrontational government subsidy policies was the result of the political sensitivity of the food subsidy issue where any disruption in the system can easily fuel social unrest and cause political upheaval.

The need for social provision in general and for food subsidies in particular is analyzed through a political economy lens. The political economy approach is used in order to analyze the nature of social and welfare policies and the role of the state in them. Political economy is the best discipline to study subsidies and the nature of state intervention in the welfare of the citizens since it takes into consideration both the economic and political variables that affect the subject. (Soliman 2011)

Political economy perspective provides a number of tools that enables the analysis of the role of the state in social provision and the nature of the welfare systems. Integrating the political

approaches with the economic factors is essential for the intellectual debate regarding the social provision and also for evaluating the feasibility of alternative modes of provision.

I contend to analyze the Egyptian food system through the conceptual framework of New Institutional Economics theory since the existing models of welfare policy and social provision has proven to be limited. Alternative approaches that address the institutional component of the welfare arena and the diverse social, political, economic and ideological forces that affect decision makers need to be examined. Our analysis concludes that a move towards a more targeted provision is essential. NIE puts forward a targeting mechanism with an emphasis on the role of civil organizations and an intense reliance on private family or kinship networks in providing fundamental guarantees of livelihood security during periods of economic or social stress. This shift in the ideological approach away from universal state provision is imminent due to the administrative failure of the government in providing social and economic assistance.

NIE places an emphasis on the micro level behavior of the beneficiaries and their reaction to a certain policy. This is the tool that I used in my analysis where I made content analysis to the reactions to the smart card by the consumers. This preliminary reaction if extended and supported through further studies could provide a solid framework that can shape future policies and local institutions.

Our qualitative analysis has indicated that the smart cards are a good technological advancement but there are other problems that are intrinsic in the system that has not been addressed and that still cause a lot of inefficiency. The prime problem is the lack of a well targeted database of beneficiaries. The various reforms undertaken by the government have led to a random system of identification of beneficiaries which in turn led to many inclusion and exclusion errors. The identification of beneficiaries is still not well specified depending on certain criteria. Thus, I

proposed some policy options that could be implemented in the long term for a useful alteration of the subsidy system based primarily on minimizing the errors of exclusion of the poor and an accurate identification of the beneficiaries.

First a proxy means testing mechanism should be done. Proxy means testing will promote greater equality of consumption for it will encourage the poor people to consume more relative to rich people thus reaching relatively more equity (Grand 1991). This should be combined with a community based framework in the collection of the survey data. Also the poor opinions will be integrated in the identification of the necessary variables to be used in the proxy means testing.

There is remarkable evidence that the mixed approach of juxtaposing the community targeting mechanisms together with government's rules and regulations is the best approach that achieves the most desirable results. The best community targeting outcomes are likely to be attained within hybrid systems which allow for major local community agent discretion but also specify comprehensible rules and targeting framework which keep local agents responsible through external auditing and evaluation, and institutions such as obligatory meetings, and competition among groups for contracts. (Conning & Kevane 2000)

Before the revolution, the Egyptian society was suffering from major fragmentations due the embezzlement that the previous autocratic regime has exercised over the country's resources. The trickle down approach that the government claimed to adopt was a trickle down approach in the pockets of the corrupt politicians and the other businessmen associated with the regime. Rising inflation, increasing tax levels and higher unemployment rates were all catalysts to more public aggravation and discontent. What made matters worse is that the toppled regime targeted the areas of escalating political instability for increased social provision rather than relying on

poverty indices or even geographical targeting (Abdel Baki, 2011). Thus, that was an obvious form of political patronage that the regime used to stay in power rather than tackling poverty issues and societal demands.

Moreover public demands were suppressed by a police-state that supported the regime to impose a top down autocratic rule. Thus this is a serious lesson to be learned now with the recent attainment of self-rule in Egypt. Indeed this obligates future policymakers to establish a model that encourages the collection of knowledge based on a bottom up approach for decision making in almost all aspects. Knowledge should then be converted into objectives and goals that constitute an action plan that should be sustained beyond changes in governments (Abdel Baki, 2011). We have seen lately that in the past 18 months Egypt has seen several consecutive governments and this might continue depending on the degree of political stability that we will be achieved in the coming period. Thus, it is imperative that we have a clear vision and plan to be implemented with the changing governments.

As soon as we involve the community in the decision making process, it gives the community a form of empowerment due to involving stakeholders in formulation of future policies which eventually enables social mobility. This mechanism helps in dissolving the traditional hierarchy of power structure and strengthens intermediate institutions of civil society that would affect the overall reconstruction of the community through s strong prominence of participation and the endorsement of an equitable vision of rights and entitlements. Indeed these new social movements could make considerable changes in the formal relationship between the political leaders and its constituents and thus reaching new forms of democracy. This is not a new invention, in fact, a worldwide trend of dismantling of controls, disintegration and a search for

more authentic forms of democracy have taken place in many countries that has just completed the transition to democracy in such as Latin America, Southern and Eastern Europe (Roniger, 1994)

Moreover I contend that Egypt can benefit from other countries' experiences like the ones from Latin America of shifting from universal subsidy provision to conditional cash transfers. It is worth mentioning that the shift to cash transfers can solve one of the prime two drawbacks inherent in the Egyptian food subsidy system which is the leakage of the subsidy benefits between the ration shops and the consumers.

I have chosen one experience that links cash transfers to education, health and nutrition which is the Mexican experience. The reason for choosing this successful experience is that it is argued that poverty is not an economic state rather than a state of mind and a state of affairs. In other words, in order to alleviate poverty first the dependency relationship between the government and the needy has to be broken. I am not arguing that the government abandons social safety measures but I am advocating an empowerment approach that helps to break the inter-generational cycles of poverty in the long run. This cannot be achieved with in-kind or cash transfers alone but government assistance has to be linked to other programs with greater emphasis on integrating the poor into the economy so that they may eventually rise out of poverty through their own efforts (Sanders 1990). Thus phasing out of subsidies in the long run is the goal. As we have seen through the research that even with technological advancement there is a window of system manipulation. Yet the phasing out cannot be done abruptly or without enough preparation of the public. More importantly, in order to get rid of subsidies in the long run the poor need to get out of poverty. I proposed that this could be achieved through a public community partnership approach first through targeting of subsidies which would build

social capital through involvement in the decision making process. Then through the concept of co responsibilities such as the Mexican experience where the poor actually abide by certain conditions –mainly increasing access to education and health services- in order to get economic assistance.

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Appendix (A): Interview Questions

What are the shortcomings of the paper system that were addressed by the smart cards?

- Question 1: What are the pros and cons of the new smart card system? **Purpose: To test the effectiveness of the smart card in enhancing the administration and the distribution of rations**
- Question 13: is there a difference between the old paper card system and the smart ration card one? **Purpose: to test the similarities/differences in the procedures between the paper and the smart cards**

Do the ration cards address the commodity preferences of the consumers?

- Question2: What is the most important commodity in the ration cards? **Purpose: To test the consumers' preferences regarding the commodity mix on the ration cards**
- Question 9: What are the most essential commodities that are the most needed for you and that you want to include in the ration cards? In other words, what are the commodities that you can't live without? **Purpose: to test the relative importance of certain goods that are distributed through the rationing system with respect to the households who use the cards**
- Question 12: some people have problems with the quality of the commodities and they don't like it and they think that the commodities that they take on the ration cards are of low quality?? **Purpose: to test the end users' level of satisfaction regarding the quality of the food rations**
- Question 14: Since the start of the usage of smart cards you take your rations month by month, right? what happens if you went to take your rations for one month and you didn't find your rations from one commodity, you went again in the same month and you didn't find it either do you manage to take your ration afterwards during the following month? **Purpose: to test whether the new procedure controls the ration quantities in favor or against the beneficiaries**

What did it add to the system of administration of the rations?

- Question 4: It is called the family card, how many family members do the cards cover? Do they include everybody in the family? Who is included and who is excluded? **Purpose: To examine the system's ways of inclusion/exclusion from the ration cards**
- Question 5: With reference to the 2009 law that limits the number of family members on the ration card to 4 individuals, is there anyone of you who got harmed by this law? In other words, anyone of you who has family members who are not covered by his family ration card? **Purpose: To examine the system's ways of inclusion/exclusion from the ration cards**
- Question 6: was it ever possible before to separate the married sons and daughters from the original family card in order to have their own ration cards? **Purpose: To examine the system's ways of inclusion/exclusion from the ration cards**
- Question 8: what are your suggestions in order to improve the ration card system in general? **Purpose: to explore different ways of enhancing the distribution and the administration of the rations from the point of view of the end users**
- Question 10: what is the procedure of issuing new smart cards? With reference to the law that prohibited the addition of new-borns in the years from 1988-2005 to the smart cards and then opening the window of adding these children afterwards, did you manage to add your children who were born in this period? **Purpose: To examine the system's ways of inclusion/exclusion from the ration cards**

Did the reforms address the necessary shortcomings or were they unnecessary?

- Question 7: did the smart cards enhance or deteriorate the service and the whole ration system? **Purpose: to test the consumer's satisfaction**
- Question 11: what do you think about changing the subsidy system to cash transfers to the families instead of the family ration cards? **Purpose: to examine opinions regarding alternative ways of managing the food subsidy**

Appendix (B): Programme Components of Oportunidades

Health: a focus on preventative health to strengthen and improve the health of families themselves and the wider community through:

- o Preventive medicine: certain age groups receive a basic health care packet (which includes vaccinations, prevention and treatment of illnesses, family planning etc.)
- o Community workshops: to teach people how to take care of their health

Nutrition: improve nutrition of family members through:

- o Bi-monthly income transfer to improve nutrition
- o Nutrition supplements to prevent and address malnutrition for pregnant and lactating women

Education: help enrolment and retention rate in schools through:

- o Incremental grants from 3rd year primary to 3rd year high school – in secondary and high school girls receive slightly more than boys
- o Bi-monthly income support for school supplies or a school supplies packet

Young people: incentives for young people to finish higher education before they turn 22 through:

- o Transfer of money which is accumulated from 3rd year secondary for every year they complete. They then have limited options for what they want to spend or invest this money on/in

Elderly: improve the conditions of life for elderly people living in households receiving Oportunidades benefits through:

- o Bi-monthly income transfer for elderly over 70 years

Energy: help in the expenses associated with energy through:

- o Bi-monthly income transfer to help cover electricity, gas, candles etc.

Appendix (C)

Table 1: Subsidy Rates for Individual Food Items

		Sugar	Oil	Rice	Tea
Main Quota Before 2006	Main Quantity per Person per Month	1 Kg	0.5 Kg	Maximum 2 Kg per Family	.050
	Price LE per Kg	0.60	0.50	1.00	11.20
	Subsidy Rate	20.00	5.00	30.77	50.91
Additional Quota from July 2006 to May 2008	Quantity per Person per Month	0.5 Kg (Maximum 2 Kg per Family)	0.5 Kg (Maximum 2 Kg per Family)	1 Kg (Maximum 4 Kg per Family), added in 2004	
	Price per KG	0.75	1.75	1.00	
	Subsidy Rate	25 %	17.5%	30.77%	
New Additional Quota After May 2008	Quantity per Person per Month	0.5 Kg (Maximum 2Kg per	0.5 Kg (Maximum 2Kg per	1 Kg (Maximum 4 Kg per	

		Family)	Family)	Family)	
	Price per Kg	1.00	2.50	2.00	
	Subsidy Rate	33.33%	25%	61.54%	