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**EGYPTIAN DEVELOPMENT AND U.S. AID:
A 25-YEAR PERSPECTIVE**

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March 1992**

RDI MONOGRAPHS ON FOREIGN AID AND DEVELOPMENT #9

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ISSN 0748-0644

The Rural Development Institute is a privately funded, non-profit operating foundation working on the issues of poverty, hunger and development in less-developed countries and in former centrally-planned economies which are making a transition to new forms. The focus is particularly on the problems of the rural sector, where, in most countries, the bulk of the population lives. A persisting concern of the authors, who are at the University of Washington School of Law in Seattle and who also act as President and Executive Director of the Institute, has been the quality and effectiveness of foreign aid in addressing the issues of poverty and development. Egyptian Development and U S Aid: A 25-Year Perspective reflects fourteen rounds of extended fieldwork to assess the effectiveness of the bilateral U S aid program in addressing the needs of Egypt's poor majority. This is the ninth in a series of published monographs on Foreign Aid and Development issued by the Rural Development Institute.

The foreign aid assessment process evolved out of author Prosterman's work with a number of Senators and Representatives on foreign-aid legislation, especially his work in drafting the Magnuson-Humphrey-Packwood amendment, adopted in 1975 and now section 102(b)(4) of the Foreign Assistance Act. This established a series of criteria for the allocation of U S aid, and led to requests by legislators on both sides of the aisle that he undertake a regular, wholly-independent evaluation of how well AID was meeting the entire congressional mandate. This periodic evaluation process has now overlapped four administrations, those of Presidents Ford, Carter, Reagan and Bush.

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I INTRODUCTION

Egypt's critical role in the Gulf War focused American public attention on the relationship between the United States and Egypt. A major feature of that relationship since the Camp David Accords has been the United States' massive non-military, economic aid program to Egypt, currently running at \$815 million per year.¹ Between 1979 and 1991, the authors have carried out fourteen rounds of fieldwork in Egypt to make an independent assessment of the U.S. economic aid program and of the Egyptian development process to which it relates.

American economic aid to Egypt is, by far, the largest program of U.S. aid going to any developing country. We believe this aid represents a unique resource which the two countries have the opportunity to focus on Egypt's most desperate needs. If this opportunity is not utilized, we believe that it will be difficult for any moderate Egyptian regime to survive, and in turn difficult to achieve lasting peace in the Middle East.

Since 1977 we have assessed the principal elements of the U.S. bilateral foreign-assistance program to all countries in terms of its aptness to meet the legislative policy standards in the Foreign Assistance Act. Those policy standards direct AID to focus on the poor. Our general assessment has been in terms of the aptness of project conception to meet the policy standards, as those projects proposed to be funded in the coming fiscal year are set before Congress in the annual AID Congressional Presentation.²

But for certain major country programs, such as Egypt, we have turned to a more qualitative assessment of the U.S. aid effort as it actually operates, and as viewed in the context of the overall development experience within the recipient country. Initial Egyptian fieldwork was undertaken in 1979. The present monograph, following our fourteenth round of Egyptian fieldwork in May-June 1991,³ reviews our observations on the development effort in Egypt and the relevance of the large U.S. economic assistance program to that effort.

¹ Apart from food aid.

² See Prosterman and Hanstad, *Foreign Aid: A Report Card for the Proposed FY 1992 Program*, Rural Development Institute Monographs on Foreign Aid and Development #7, May 1991.

³ It was author Hanstad's sixth round of Egyptian fieldwork. All of our fieldwork has been undertaken with independent private funding, provided to the Rural Development Institute and the University of Washington.

We begin with some background on the Egypt development process, recent changes, and some persisting development issues. We then turn to both a quantitative and qualitative review of the U.S. aid program as we have seen it unfold over the last thirteen years. Finally, we provide a perspective on what we believe must be done if U.S. economic aid resources in Egypt are to adequately help meet that country's critical development needs over the coming ten years.

II BACKGROUND

With 54.5 million people, Egypt is by far the most populous country in the Mid-East and the second most populous on the African continent. Egypt's large population, 40 percent of which is less than 15 years old, had until recently been increasing at a rate of 2.9 percent per year. Fifty-five percent of that population resides in rural areas. Egypt's GNP per capita of \$630 ranks it near the Philippines and Zimbabwe in that category. By sector, 19 percent of Egypt's GNP is attributed to agriculture, 23 percent to petroleum and mining, and 22 percent to commerce.

When the United States began providing large amounts of economic aid to Egypt in the late 1970s, Egypt was experiencing an economic boom period due to a series of extremely favorable events. High oil prices, the reopening of the Suez Canal, increasing workers' remittances from the Gulf States, and President Sadat's "open door policy" to stimulate private investment resulted in real annual growth rates between six and eight percent in the late 1970s and early 1980s. This period of remarkable growth was not due to increased productivity, however, as a wide range of government policies left over from the Nasser era kept the government responsible for the important economic decisions in virtually every sector. The government's desire to control prices, maintain widespread subsidies, and invest heavily in inefficient public sector industry led to regulations and price distortions which discouraged increased productivity.

In the early 1980s, Egypt's boom period began to recede. Oil prices began declining in 1981 and dropped sharply in 1985, and workers' remittances from the Gulf States began to level off. Egypt, which had been accustomed to abundant revenues, began developing a serious balance of payments gap, ran large budget deficits, and became increasingly unable to manage its external debt.

Gradually, the Government of Egypt (GOE), with pressure from international donors, began to realize the need for structural reform within the economy, and in 1986 announced commitment to an economic reform program. In May, 1987 the GOE reached an accord with the International Monetary Fund in order to ease its debt situation. In exchange for promises to implement structural reforms, the IMF agreed to reschedule part of the foreign debt and give its imprimatur on new credits. However, only six months later the IMF concluded that Egypt had violated the accord by failing to implement the agreed-upon reforms and it suspended further standby credits. Egypt's reluctance to implement the reforms -- which

included decreasing subsidies and increasing consumer prices, in a general effort towards deregulation and market-based pricing of production, investment, foreign trade, services, agricultural goods, and inputs -- was based on belief that the reforms would lead to urban unrest and political instability

After 3½ more years of hard bargaining between the GOE and the joined forces of the IMF and World Bank, an accord was reached in May 1991, helped by Egypt's introduction of several "up front" reform measures to demonstrate good faith and by the felt political need to "reward" Egypt for its participation in the Gulf War. The accord came on the heels of actions by the U S to write off \$6.7 billion of Egypt's Foreign Military Sales debt, and by the Gulf states to write off \$6 billion of Egypt's debt.

The agreement provides the highly-centralized and debt-burdened Egyptian economy with a standby IMF loan and a package of World Bank structural adjustment loans, but more important, it cleared the way for a Paris Club agreement to forgive half the GOE's remaining government-guaranteed debt of about \$20 billion over 3 years. All the loans and debt write-offs are tied to Egypt's compliance with the agreed-upon reforms. The agreement also includes a World Bank social fund intended to offset the negative impact of structural-adjustment measures on Egypt's poor, to which almost \$500 million has been committed.

It is yet to be seen whether the GOE will stay in compliance with the tough economic reform program with its associated risks of social upheaval. Its record of failed attempts to drag itself out of the macroeconomic mire did not inspire confidence in all observers. Yet others, pointing to the carrot-and-stick nature of the new accord and the reform steps already taken by the GOE, remained optimistic. Reports on achievements in the early months of the structural-adjustment program were encouraging. As of early 1992, foreign-exchange reserves were up substantially and the GOE budget deficit was down. Moreover, unemployment, which had risen during the Gulf War period with the return of Egyptians employed abroad, appeared to be down substantially, as many of those workers went to new jobs in other Arab states. However, privatization of government-owned enterprises, while it appeared to be widely accepted in principle, was still moving slowly.

One sector in which the GOE has made great reform strides in recent years is agriculture. More than 40% of Egypt's labor force, and over one-half of Egypt's poor work in the agricultural sector. Egypt has principally a small-farm agriculture, with an average farm

size of about two acres⁴, comparable to farm size in Japan, Taiwan, or South Korea, and a bit larger than farm size on Java. Egypt's land area is 96 percent desert and its population is dependent on a narrow strip of agricultural land in the Nile River Valley and the Nile Delta for its domestic food sources. There is some prospect for limited expansion of the 7 million cultivated acres, but the costs are great. The ratio of total population to cultivated land, with about eight people per acre, is more than 50 percent greater than in Bangladesh. It is less, however, than in South Korea and Taiwan, both of which have had highly successful development processes.

Although Egypt has a relatively high ratio of people to cultivated land, its cultivated land is exceedingly rich. With a year-round favorable climate allowing three cropping seasons, fertile soils, and a dependable -- although finite -- supply of irrigation water by virtue of the Aswan Dam, Egypt has one of the richest endowments of agricultural resources in the world.

As of 1989, Egypt's overall average productivity of grain was 2.17 metric tons per acre, representing 79% of the productivity of the world's most intensive grain producer, the Netherlands. Egypt's per-acre productivity was up 32% from 1979-81 to 1989, and it has further increased in the past two years. Yet Egypt's agricultural endowment is such that productivity per acre could well become the world's highest, and significant scope for additional increases remains.

The land tenure and credit/input systems have also contributed to the relatively good productivity of Egyptian agriculture. A Nasser-era land reform redistributed about 15 percent of the cropland outright from 1952 to 1964. The land reform also shifted 40-45% of the cropland from traditional tenancy to a unique protected ("registered") tenancy arrangement. As of the early 1980s, 36% of all cultivated holdings still consisted wholly or partly of land under registered tenancy.⁵ Egypt is the *only* less-developed society within our knowledge and experience which has successfully regulated the landlord-tenant relationship over a long term.⁶ Our fieldwork has consistently confirmed that the Egyptian landlord-tenant relationship is regulated to such a degree that the protected tenants can be considered

⁴ The local measurement is "feddan". One feddan = 1.038 acres.

⁵ This was after twin processes of reduction in the quantity of such lands: registered tenants buying out the residual rights of the owner (often using money remitted by family members working in other countries), and owners buying back full land rights for a substantial consideration.

⁶ Taiwan also successfully regulated landlord-tenant relationships, but the basic program lasted for about three years, after which most tenants received full ownership of the land they tilled.

virtually "owner-like" in their motivation and agricultural investment-making. The protected tenants have hereditary right to possession of the land, they pay low fixed rents (a multiple of the land tax), and they are entitled to one-half the sales price if the land is sold to a third-party. After more than a quarter-century of this system, the nominal "landlords" -- who are virtually all engaged in urban and non-agricultural pursuits -- have only the most formalistic and tenuous connection with the land or the protected "tenants" ⁷

The agricultural credit and input system has also become very effective in recent years in reaching the typical small farmer with necessary credit and inputs. The production credit system, utilizing some 4,300 local depots for input delivery -- one in virtually every Egyptian village -- is run through the Principal Bank for Development and Agricultural Credit (PBDAC) which is under the Minister of Agriculture. Significant improvement has been made in PBDAC's credit and input system in recent years with the support of AID's Agricultural Production Credit project (APC) (discussed at pages 17-18)

With an ideal physical environment, farmers with ownership or secure owner-like tenure, and an effective and improving credit/input system, the potential exists for much higher yields on most crops. This potential is made increasingly evident by other recent developments: first, the liberalization in the government sector which is dismantling an inefficient system of government controls over production and marketing of major crops, second, tested improvements in irrigation and drainage which have proven to give significant boosts in yield, and third, new, effective technology packages which are being distributed to Egyptian farmers through a revamped and improved extension service.

Although Nasserite socialism has had lasting negative impacts on the Egyptian economy in terms of a large and inefficient public sector, excessive government control over the market, and widespread price distortions, it also had some positive impacts on Egyptian society. Besides the land reform, grassroots agricultural credit, and a subsidized food distribution system which placed a nutritional "floor" under most of the population, other signals of the significant Egyptian commitment to the less-well-off groups in their society since the 1952 revolution were evident at the time of our first fieldwork in 1979. An extensive network of some 3,500 health clinics had been established, especially in rural areas,

⁷ This has not kept landlords from attempting to roll back the protective laws through the legislative process, though so far with very limited success. For an account, see Yahya M. Sadowski, *Political Vegetables? Businessmen and Bureaucrat in the Development of Egyptian Agriculture*, pp. 292-303 (Brookings Institute, 1991)

and a large-scale immunization program introduced for childhood diseases. There had also been an effort to operate safe water systems in a large number of towns and villages.

Despite these numerous interventions, it was disappointing to find that in 1979 the infant mortality rate (IMR)⁸, which is regarded by many experts as the single most sensitive indicator of grass-roots well-being, stood around 120 per 1,000, nearly the same as the IMR in India. There was broad consensus that nutritional levels were generally adequate, and that the variable to which this high infant mortality rate could chiefly be attributed was the health and sanitation area. Human waste contaminated wide areas of the environment, including canals used for bathing and washing. "Safe water" systems alone can eliminate only a limited range of contact sources with contaminated water, and even these systems were frequently inadequate or broken-down. Neither preventive nor curative medical systems were adequate to address the consequent problems of water-borne disease, and even within their intended scope both systems had problems in delivering their services effectively.

High infant and child mortality were, in turn, probably a significant factor in keeping birth rates high, as parents sought "insurance" and "replacement" births. After a dip in the early 1970s, the crude birth rate (CBR)⁹ at the end of the decade had resumed its earlier level of around 41 per 1,000. The total fertility rate¹⁰ was about 5.1.

Meanwhile, other "pluses" in Egypt's development background have included the existence of substantial revenues from oil exports, Suez Canal tolls, tourism, and remittances from Egyptians working abroad.

Other "minuses" in Egypt's development background have been low energy prices which encourage wasteful use of oil at the expense of exportable surplus, the government as employer-of-last-resort for university graduates, leading to a bureaucracy which has been grossly overstaffed, underpaid, and maddeningly slow to act, the highly-centralized nature of the development process with little or no allowance for local government initiative, an underemphasis on the maintenance of facilities once they are built, an unresponsive commercial banking sector which has failed to provide credit to the thousands of small- and

⁸ The rate of deaths in the first year of life per 1,000 live births.

⁹ The number of live births per 1,000 population in a year.

¹⁰ The total fertility rate represents the number of children that would be born to a woman if she were to live to the end of her childbearing years and bear children at each age in accordance with prevailing age-specific fertility rates.

micro-sized businesses which line back streets in nearly every Egyptian village, town, and city, and despite the highly successful land reform program, the continued existence of at least several hundred thousand agricultural laborer families without access to any land

III GRASSROOTS DEVELOPMENT PROGRESS SINCE 1979

Much international attention has been paid to Egypt's macroeconomic situation throughout the 1980s and early 1990s. Egypt's debt climbed to over \$50 billion by 1990. Throughout the 1980s, inflation grew, economic growth slowed and a government reluctant to loosen its control on resource allocation and production appeared unable to drag itself out of the macroeconomic mire.

Meanwhile, a number of positive trends had been occurring at the grassroots, despite the macroeconomic mess, which were largely unnoticed by most international observers. Many of these positive trends have been strongly supported by AID initiatives.

The infant mortality rate, probably the best single measurement of overall grassroots well-being, dropped dramatically from 120 per 1,000 in 1979 to 50 per 1,000 by 1991. More broadly, AID has reported an increase in life expectancy at birth from a 50 year average in 1970-75 to 61 years in 1991. These important improvements in infant mortality and life expectancy are probably due to a combination of factors including substantial increases in the real wages of agricultural laborers, the significant impact of workers' remittances at the grassroots, and the impact of programs for providing health and sanitation services and for improving agricultural performance -- programs which in various ways and degrees are AID-supported.

Substantial improvement has also been made in crop yields. Egypt now produces the highest rice yields per acre in the world. Wheat yields have doubled since 1980. AID has played a major role in this tremendous improvement within the agricultural sector by support of complementary policy reform and project activities.

Crude birth rates appear to have made recent dramatic declines. Data indicate a fall from 39 per 1,000 population as recently as 1986 to 32 per 1,000 in 1990. AID's family planning efforts have played a major role in this. A range of socioeconomic improvements, both GOE and AID supported, have also helped in establishing the preconditions for successful family planning -- ranging from the Nasser-era land reform to the recent decline in infant mortality.

Schools have become much more accessible to children, especially girls. The percentage of primary school-age girls enrolled in school grew from 57 percent in the mid-1970s to 79 percent in 1987 and the proportion continues to increase. AID's basic

education activities have played a major supporting role with the building of over 1,800 primary schools throughout Egypt

Egypt has also shown some initial success in decentralizing government and the development process. Under an AID-sponsored local development project, over 20,000 small local subprojects initiated at the local village level have been completed, ranging from drainage to access roads to sanitation, and some local decision-making capacity has been created. But significant issues remain as to the ability of local governments to collect and keep revenue.

All of these positive developments denote that Egypt's well-publicized macroeconomic troubles over the last decade have not resulted in a total stagnation of Egyptian development at the grassroots. And, as indicated above, the GOE's initial performance in implementation of its promises of economic reform in exchange for new loans, debt rescheduling, and debt reduction offers hope that even the macroeconomic picture will improve, furthering prospects that grassroots development can be sustained, and perhaps hastened. The GOE's promising start has included liberalizing the exchange rate, lifting some consumer subsidies, removing most government controls on agricultural production and marketing, raising energy prices (albeit from a very low base), and introducing a sales tax.

IV SOME PERSISTING DEVELOPMENT ISSUES FOR EGYPT

Despite what we see as important progress on a number of fronts during the past thirteen years, a series of major development issues remain. The most salient are outlined below. Several of these are further discussed in the framework of our qualitative review of the U.S. aid program in section VI.

- The government-controlled price of cotton needs to be raised substantially. While major improvement has taken place in the area of agricultural pricing and regulation, the cotton price issue still remains. Egypt has a comparative advantage in cotton, but is making little use of it. As a result, prized Egyptian cotton, which has tremendous export potential, is losing world market share. The Egyptian government requires farmers to grow cotton and pays them set prices which are far below world market rates. Although the low set prices are attractive to Egyptian cotton mills, they are destructive to the cotton industry as a whole, and especially to Egyptian farmers. Cotton, which should be a profitable cash crop for farmers, has become a crop that farmers dislike growing. As a result, not only do farmers lose income, but cotton yields are much lower than they could be because farmers take little interest in the crop and plant it late to maximize production on the preceding crop. Nor are any areas planted in cotton beyond those mandated by the government. A concomitant point is that the government price, especially if it is significantly increased, needs to be announced before planting of the winter crop so farmers can adjust their cropping pattern and planting times for cotton to follow in the spring.

- Government-controlled energy prices are too low. Even with recent increases, the average price for electricity is still about one-third the world market price, and prices for most public-sector industries are even lower. Such heavily subsidized power has led to extreme energy waste and inefficiencies, at the expense of exportable surpluses of petroleum. Egypt is forgoing significant and needed government revenue and foreign exchange by keeping prices so low relative to world market prices.

- Government is still too centralized in Egypt. Nearly all revenue collection, decision-making, and spending is done at the central government level. These highly-centralized processes lead to waste, lack of accountability, and disincentives for local initiative. The highly-centralized government has not even been successful in eliminating large social and economic disparities between governorates. Local governments should be given more decision-making authority, as well as the power to collect and keep revenue.

- One issue that has risen recently involves the amount of farmland that each agricultural extension agent is responsible for. AID's Agricultural Production Credit Project showed that one well-trained extension agent could effectively service 500 acres of agricultural land, and agents were successfully deployed on that basis to nearly half the agricultural land. A recent decision within the Ministry of Agriculture, however, changed the model from one agent per 500 acres to one agent per 200-250 acres. This promises to place a nearly impossible strain on what is now the National Agricultural Research Project's job of retraining extension agents and providing them with incentives. Instead of needing 14,000 well-trained extension agents to cover all of Egypt's agricultural land, 28,000-35,000 agents will need to be trained and otherwise supported under the new model to do the same job that 14,000 could do. We believe that the decision to move to one extension agent per 200-250 acres should be reversed.

- Maintaining the integrity of the protected tenancy laws remains important. From time to time this successful system comes under attack from some (landlord) quarters. The full maintenance of these protections is vital, we believe, to both the performance of the agricultural sector and the long-term political stability of the country.

- The question of the efficiency of ongoing GOE efforts to "reclaim" land from the desert for agricultural purposes is an important issue which probably needs further study. A 1980 study on the economics of land reclamation was very negative and steered AID away from support of land reclamation, although GOE efforts have continued. The real costs of pumping and using additional water on desert lands are high. More recent studies have been more positive, but a lot of "ifs" remain. While we would encourage AID to support further study in the area, we again emphasize that there is still tremendous potential for yield increases on the "old lands", and that any study examining the costs and benefits of land reclamation must compare those with the relative costs of raising yields on existing agricultural land.

- One ingredient that appears to be missing from effective development efforts in Egypt is coordination among the various government ministries, or even between separate departments within the same ministry. We have seen this illustrated most evidently in the agricultural sector with the lack of coordination between the Ministry of Agriculture and the Ministry of Public Works and Water Resources, but the problem appears to be systemic. Formal mechanisms for coordination such as inter-ministerial committees are almost unheard.

of It appears that it would be beneficial for the central government to develop mechanisms both for inter- and intra-ministry coordination

- One of the most-watched issues over the near- and mid-term will be Egypt's compliance with the agreed-on economic reforms As discussed above, the carrot-and-stick nature of the current accord between the GOE and the donor community, and the reform steps that the GOE has already taken offer hope that the GOE will remain on track The donor community, however, should remain sensitive to the economic difficulties that the reforms will impose, especially on the poor, and the political difficulties that unpopular reform measures will present to the government

V THE U S AID PROGRAM A QUANTITATIVE ASSESSMENT

TABLE I

<u>Fiscal Year</u>	<u>Percentage to Projects with Significant Positive Impact on the Poor⁺</u>	<u>Overall Grade⁺⁺</u>
1977	8%	1 1
1978	5%	0 7
1979	3%	0 9
1980	5%	1 1
1981	26%	1 55
1982	25%	1 56
1983	17%	1 41
1984	27%	1 88
1985	20%	1 72
1986	40%	2 09
1987	39%	2 07
1988*	36%	2 08
1989	13%	1 59
1990*	18%	1 68
1991	20%	1 69
1992†	20%	1 78
1993†	20%	1 77

* \$115 million in cash transfer which was originally scheduled for FY 1988, but not released until FY 1990 is graded in FY 1988 to avoid distortion

† As projected in the February 1992 AID Congressional Presentation

+ 2 7 or better on a 4-point grading scale

++ 4-point scale

Table I traces the performance of the U S economic assistance program to Egypt since Fiscal Year (FY) 1977. Our report-card assessment of proposed and actual obligations measures the effectiveness of the aid program in complying with the legislative standards of the Foreign Assistance Act (FAA) which direct AID to promote poverty alleviation, and self-sustaining economic growth with an equitable distribution of benefits. The first goal set for

development assistance, and that which permeates the legislation is "the alleviating of the worst physical manifestations of poverty among the world's poor majority"¹¹ Although the aid program to Egypt is not from the development assistance account, but the economic support fund account,¹² these policy directions are still applicable Section 531 of the Act provides that efforts should be made, "to the maximum extent feasible," to cause economic support fund programs to meet the poverty-focused policy directions set forth for development assistance

Our grades are on a traditional 4 point scale (A = 4 0, A- = 3 7, B+ = 3 3, B = 3 0, B- = 2 7, C+ = 2 3, C = 2 0, C- = 1 7, D+ = 1 3, D = 1 0, D- = 0 7, F+ = 0 3, F = 0 0) As with all standard grading, they are appropriately weighted, based on the dollar amount obligated in the particular fiscal year for each project or other outlay

The significance assigned to each grade, following our field reviews of the Egypt program, may be briefly expressed as follows "A" projects appear to be fully implementing the intent of Congress as expressed in the guiding legislation mentioned above, and to have a clear, significant impact on the poor majority, "B" projects represent a reasonable effort at implementation, but have drawbacks somewhat limiting their impact, "C" projects are only marginally relevant to implementing the legislative intent, although some benefit may be gained by the poor majority, "D" projects are unsatisfactory as an effort to implement the legislative intent, producing virtually no benefit for the poor majority, and "F" projects are not only unsatisfactory, but appear to be injurious, through encouraging a recipient country to pursue clearly ill-conceived development goals and to waste its resources on programs that are irrelevant to the lives of the poor majority, indeed that may even widen the gap between the poor and a small minority of the well-off within that society

Judgments are made not only in terms of the specific nature and Egyptian setting of each project, but also in terms of factors, such as cost-per-family-benefited, which determine the prospective replicability of the project benefits for other similarly-situated members of the poor in that country

¹¹ FAA, Sec 101(a) A more detailed discussion of the legislative standards used and our grading process can be found in Prosterman and Hanstad, RDI Monograph #7 *Foreign Aid A Report Card for the Proposed FY 1992 Program*, May 1991, pp 4-9

¹² ESF resources as distinct from Development Assistance resources are foreign economic aid resources which are allocated to countries with "special economic, political or security conditions" involving U S national interests in amounts which "could not be justified solely under the development assistance portion of the foreign aid program" (Foreign Assistance Act, sec 531(a))

We have now graded the Egypt program for seventeen years. The assessments since 1979 are based on field review.¹³ Table I indicates that for the four initial years of grading, FY 1977-80, we consistently found the aid program nearly irrelevant to Egypt's grassroots development needs. The percentage of resources going to programs that we judged to have a reasonable prospect of improving the lives of Egypt's "poor majority," in accordance with the legislative standards -- that is, dollars allocated to undertakings to which we assigned a grade of 2.7 ("B-") or better, on a 4-point grading scale -- had never exceeded 8%, or around \$60 million out of the total \$750 million annual program. The overall weighted grade for the entire program, based on the grade we gave each of the components, had never exceeded 1.1 ("D").

Beginning in FY 1981, the grading reflected significant improvement over previous years. High-water marks were reached from FY 1986-88 with 36-40% of resources going to projects which significantly benefited the poor, and an overall grade point ranging from 2.07-2.09.

There was a significant drop-off in marks in FY 1989, when only 13% of the resources went to high-quality projects and the overall grade point slipped to 1.59. The marks for FY 1990 and 1991 show some improvement, although they are still far from the level of FY 1986-88. Marks for FY 1992 and 1993 are for the program as projected by AID, and are still subject to significant change. As we shall see below, consistent maintenance of the FY 1986-88 level -- though clearly falling short of an ideal -- would at least approach what is required to meet the most pressing needs of Egypt's poor majority over the next ten years.

¹³ Prior to 1979, the grading was based on project conceptualization, as presented to Congress in the request for funding, in the context of our field experiences in other countries. In the field, we found these provisional grades generally valid.

VI THE U S AID PROGRAM, A QUALITATIVE ASSESSMENT

A Agnculture Some of AID greatest successes in Egypt have come in the agricultural sector. AID currently has three major agricultural projects, all of which we judge to be high-quality projects: the Agricultural Production Credit Project (APC), the National Agricultural Research Project (NARP), and the Irrigation Management Systems Project (IMS).

The Agricultural Production Credit Project (APC) is the single most successful AID-supported agricultural project we have seen anywhere. The project's two elements grew out of the lessons learned under a successful predecessor project, the Small Farmer Production Project (SFPP). The first element has combined short-and medium-term credit packages with extension advice from newly-trained extension agents resulting in significant yield increases for project beneficiaries. This projectized element is now reaching roughly 1.5 million families of Egyptian small farmers -- about half the total --- with substantially improved packages of inputs and practices together with greatly improved extension services. Sensibly, the project builds upon the existing grassroots operation of the government's Principal Bank for Development and Agricultural Credit (PBDAC) with its 750 loan-granting village banks and 4,300 agencies where inputs are picked up by small farmers.

APC's second element is a policy component in which cash transfers are made to provide capital for PBDAC (dollars are transferred by AID to the Central Bank, and an equivalent allocation of Egyptian pounds is then made to PBDAC). These cash transfers are phased and releases are tied to successful implementation of previously negotiated policy reforms in the agricultural sector. As a result of these reforms, Egyptian farmers now receive market level prices for most key crops (except cotton -- see p. 11), most crop delivery quotas and planting requirements have been eliminated, wasteful subsidies for imported animal feed have been phased out, and the government is privatizing the production and delivery of fertilizers.

APC and its predecessor SFPP have also introduced numerous institutional improvements, many of which have influenced the nationwide behavior of PBDAC. These improvements include nearer-to-market-rate interest, dropping the requirement of formal land title or a "surety" to collateralize medium-term loans (as for equipment or animals) thus giving full access to tenants and the landless, retraining and much more effective deployment of extension agents (many of whom had formerly been used merely as "enforcement" agents for government production requirements), salary incentives for performance by bank and

extension personnel, computerizing banking records and processes, and streamlining of a range of banking procedures at the level of participating villages

One current issue concerning APC is AID's strictness on the release of the cash tranches. AID has been insistent that all policy reform benchmarks are met sufficiently before cash is released. Our concern is that overly strict requirements could result in starving PBDAC and the agricultural sector of needed capital, even when this sector is far ahead of other sectors in lifting government controls and implementing other policy reforms. Indeed, in some agricultural reforms such as the removal of rice quotas, implementation has come even faster than was called for by the negotiated benchmarks.

In light of this, and because some of the reforms asked for can be blocked by government ministries other than Agriculture, we believe that AID should show some flexibility in releasing cash to PBDAC.

A related suggestion, discussed further at page 38, would be to use the separate cash transfer resources,¹⁴ or some portion of it, to achieve policy reform benchmarks -- such as cotton price increases -- that are not sufficiently within the power of the Agriculture Ministry to implement.

One recent positive development affecting APC is that the GOE has decided to deposit AID's contribution of \$55 million (in local currency equivalent) to the World Bank's social fund in PBDAC. This should help improve the financial situation of PBDAC in what promises to be difficult economic times. Beyond this, it is clear that PBDAC could readily absorb and utilize, principally as small-farmer support, substantially more than the \$283 million total initially planned (of which \$183 million had been obligated as of FY 1990¹⁵).

AID's second major agricultural project is the \$300 million National Agricultural Research Project (NARP). Under NARP, which builds on previous AID-supported projects, Egypt's Agricultural Research Center (ARC) and related research institutions will be enabled to research, develop, and disseminate for extensive field trials a series of agronomic packages for a wide range of crops tailored to specific local conditions.

NARP has received congressional attention and criticism related to some negative audit findings. These included findings that the GOE was not fulfilling its obligations to make

¹⁴ For FY 1993, AID is requesting \$210 million for sector policy grants.

¹⁵ An additional \$49 million went to the predecessor Small Farmer Production Project.

contributions to the project, and that improprieties involving illegal import of some vehicles were committed by some of the GOE officials heading the project

We had a separate concern with NARP after our May 1990 trip to Egypt. This problem related to NARP's technology transfer component. At that time NARP was about to assume the technology transfer or agricultural extension activities that had until then been very successfully borne by the Agricultural Production Credit Project. It appeared to us during that round of fieldwork that both the U.S. contractor for NARP and the senior Egyptian management team for NARP were wholly unprepared to assume the technology transfer responsibilities that APC and PBDAC had so successfully implemented.

We were pleased to find on our May-June 1991 trip to Egypt that not only had all the major concerns raised in the audit been addressed and successfully dealt with, but that NARP also appeared to be doing a decent job in carrying out the technology transfer activities. Extension agents were being retrained and technology packages were being delivered to the field. We will continue to monitor NARP's progress on the technology transfer component, but for now we are pleased to report that the progress is satisfactory. Our chief current concern is over the increase in ratio of extension agents to land (see discussion at page 12) which had been opposed by both ARC and PBDAC. Our most recent discussions, however, have suggested flexibility on this issue at the Ministry of Agriculture, which should be pursued.

Although overall project implementation has been slow, NARP has achieved some successes. NARP research has contributed to the significant yield increases in both rice and wheat in recent years. NARP-supported research, coupled with extension, solved problems of viral diseases in Fayoum Governorate's tomato crop in 1989. Tomato yields approached 20 tons per acre in 1990 after falling to 5 tons per acre due to the diseases in 1989. NARP-supported research has also led to new all-purpose mechanical threshers, has resulted in controlling the problem of blossom blight in pears, and has led to the introduction of potato tuber seed production in Egypt.

AID's third major agricultural project is the Irrigation Management Systems (IMS) Project. The IMS is a complex umbrella project with ten components which is authorized for \$340 million, and is scheduled for completion in September, 1995. The objectives are both to increase agricultural production and to use water more efficiently. The various components are designed to improve the institutional capabilities of the Ministry of Public Works and Water

Resources (PWWR), improve farm-level irrigation, address social issues associated with irrigated agriculture, and upgrade the irrigation infrastructure

In our interviews with Egyptian farmers, water is consistently identified as one of the most pressing problems. For this reason we recognize the importance of the objectives sought by the IMS. Some early results from the farm-level improvements made under the project in Minya Governorate indicate that crop yields may be increased by as much as 40% with improvements in the farm delivery system and on-farm water management practices. These improvements include lining the local mesqas¹⁶ that deliver water to the fields, and making water available continuously rather than intermittently (which, paradoxically, reduces overuse by those at the head of the mesqa), in conjunction with on-farm drainage provided through a World Bank program. Although more studies are needed to determine the feasibility of certain improvements, we believe this is an area to which AID could devote substantial resources in the future. If farm-level improvements such as mesqa lining prove feasible in a range of in-country settings, it would seem to be an activity that could be replicated throughout Egypt.

The farm-level irrigation improvements under IMS also have a grass-roots democratization impact. As part of these improvements, farmers are organized into Water User Associations to help govern and coordinate water use on the mesqa the farmers share. The farmers are assisted in forming their own Water User Association, they hold elections for officers, they make group decisions on irrigation schedules, and often jointly purchase equipment.

Other components of IMS have also greatly benefited Egyptian farmers. Under the Structural Replacement Component over 15,000 irrigation structures¹⁷ have been completed to replace old and nonfunctional structures. A country-wide preventive maintenance and channel maintenance program for Egypt's complex irrigation system is being planned and implemented under the Preventive Maintenance Component.

Altogether, AID's agricultural projects have contributed substantially, and promise to contribute further, to the successes of Egyptian agriculture. Egypt's small-farm agriculture

¹⁶ A mesqa is an irrigation ditch that carries water from canals or branch canals to farmers' fields. One mesqa typically serves 20 to 100 farmers.

¹⁷ Mostly small and medium-sized structures in the irrigation system e.g., intake regulators, head regulators, tail escapes, spillways, bridges, and crossing structures.

has come a long way in terms of liberalization, privatization (in areas such as mechanization¹⁸ and input supply), and yield increases due to the combination of policy reforms and the good use made by motivated small farmers of improved technical packages, credit, extension, and irrigation. However, there is still much potential for additional yield increases. In the field we have seen NARP activities alone that have increased an individual farmer's yields by 40%, we have seen APC interventions that have improved farmers' yields by 40%, and early studies indicate that farm-level irrigation improvements have raised yields by 40%.¹⁹ But there is as yet no experience of how the *combination* of all three would affect yields. Indeed, there appears to be a strong need for improved coordination and cooperation among the three AID projects, as well as improved cooperation between GOE ministries (discussed at pages 12-13). In late 1990, an agreement was reached by all three AID projects and their GOE counterparts to coordinate their efforts in specific geographical areas. To date, this agreement has not been implemented and we would urge both AID and the concerned GOE ministries to resolve their differences and cooperate together for the good of the Egyptian farmer.

B Education AID has made tremendous strides in increasing the outreach of Egypt's primary education system. AID's Basic Education project (and its follow-up) constitute a \$290 million undertaking which began in Fiscal Year 1981. Until now the project has focused primarily on increasing access to primary school for Egyptian children, especially girls. Studies have shown that most Egyptian parents do not send their daughters to primary school unless the school is within 1.5 kilometers of their residence. Also, many Egyptian primary schools, especially in urban areas, were so overcrowded that they ran double- or even triple-shifts in order to have enough classroom space. This lack of classroom space limited enrollment. Many of the schools that did exist lacked necessary furniture and instructional materials and equipment.

To date the project has constructed more than 1,800 schools which enroll some 900,000 students each year. Instructional materials and equipment, including maps, globes, overhead projectors, science equipment, and carpentry tools, have been procured and

¹⁸ Private entrepreneurs now carry out many of the activities in land preparation, harvesting, seed drilling or laser land levelling that were formerly carried out – if at all – through government machinery depots.

¹⁹ Indeed, in our field interviews, some farmers insisted that farm-level irrigation improvements had increased their yields by 100%.

distributed among 15,000 primary and preparatory schools throughout the country. In addition, some 14,000 teachers and inspectors have been trained in the use and maintenance of USAID-donated school equipment.

An evaluation of the Basic Education project showed that the construction of new schools significantly increased grade one enrollment. In the *first* year after new schools opened, grade one enrollment increased on average by 18% over *expected enrollment*, and the increase for girl students was even greater. Country-wide statistics indicate that from 1981 to 1990, total primary school enrollment increased by 41 percent, and female enrollment increased by 57 percent, nearly four-fifths of school-age girls now attend primary school. These dramatic increases were achieved, in significant part, due to AID's support of the primary education sector.

The long-term effectiveness of using substantial AID resources to support primary education in Egypt cannot be overemphasized. Numerous studies have shown the high social returns to investment in primary education.²⁰ Such returns are measured by comparing the higher lifetime productivity of educated workers with the costs of education. But primary education also generates "externalities" that are difficult to measure. The indirect effects of primary education on health, nutrition, and fertility are significant. The children of literate mothers are healthier, better nourished, and have longer life expectancies than those of uneducated women, and studies have also shown that female literacy is linked to a drop in fertility rates.

The Basic Education project has been criticized in at least one press story for not focusing on changing outdated curriculum or training teachers in new concepts on how children learn and new methods to motivate them. However, the project has added components which are focusing on the quality of primary education as well as access. A new National Curriculum Development Center has been established, curriculum upgrading will start with first grade and move up one year at a time, and teacher training, using the upgraded curriculum, has begun.

We see primary education as another area in which AID could commit even more resources. The Basic Education project has in recent years had expenditure levels of \$30-35 million, and those involved with the project say that more could be effectively used.

²⁰ See *Financing Education in Developing Countries: An Exploration of Policy Options*, World Bank, 1986.

C **Health** Although health problems are serious in Egypt, and result in reduced life expectancy, depressed quality of life, and reduced productivity, we have seen major strides in the health sector since we first started visiting Egypt in 1979, especially in the area of child survival. These improvements are reflected, most generally, in the rapid decline of the infant mortality rate from 120 in 1979 to about 50 currently.

AID has played a major role in supporting improvements in the Egyptian health sector. AID presently has three ongoing health projects, the Control of Diarrheal Diseases Project, Cost Recovery Program for Health, and the Child Survival Project.

The Control of Diarrheal Diseases Project has played a major role in what has been the most spectacular success worldwide in reducing infant deaths caused by diarrhea. Oral Rehydration Therapy (ORT), is a simple, but relatively new technology consisting basically of a salt, sugar, and water mixture which prevents infant deaths from dehydration caused by diarrhea. Dehydration from diarrhea is the number one killer of infants in Egypt, as it is in most developing countries. The project, which supports a national ORT campaign, has helped to prevent tens of thousands of child deaths due to diarrhea each year.²¹ ORT clinics have been established in 85 percent of the 3,000 Ministry of Health clinics nationwide. Because of widespread education on ORT therapy, mostly through daily television commercials, 98 percent of Egyptian mothers are aware of ORT and 96 percent can mix the oral rehydration solution correctly. Before the project was implemented, diarrhea caused over 100,000 child deaths in Egypt each year. Now, less than half that many die annually from dehydration caused by diarrhea.

AID's Cost Recovery Project aims to establish a sound financial structure for the health sector through the use of both fee-for-service and insurance systems. The project includes focus on the implementation of policy changes to convert selected curative care institutions to fee-for-service facilities, the promotion of improved management practices in two health insurance systems currently operating in Egypt, and the expansion of the private health sector by providing credit guarantees for the establishment of individual rural medical practices. Studies indicate that a significant portion of the Egyptian population is willing and able to pay for quality health care. This project promises to support activities and policies which encourage the expansion of such health care while ensuring that a larger proportion of public

²¹ The program and its success are described in N. Hirschhorn and W. Greenough III, "Progress in Oral Rehydration Therapy," *Scientific American*, Vol. 264, No. 5, May 1991.

health care costs goes toward preventive health care services for those who cannot otherwise afford them

AID's Child Survival Project, which focuses on immunization, acute respiratory infections, child nutrition, and child spacing, has been successful in developing and promoting the widespread use of practical, cost-effective interventions that address childhood health problems. The project's contribution to Egypt's recent success in childhood immunization is particularly notable. Egypt's immunization rates for major childhood diseases ranged from 41 percent to 67 percent in 1984. In 1990, immunization rates achieved by routine immunizations in Primary Health Care facilities were over 85 percent for all major childhood diseases.

Although there have been a number of very positive developments in the health area, there are still problem areas to which AID could be contributing more resources. Schistosomiasis²² is the number one public health problem in Egypt. It is a disease of the rural poor population. Village prevalence rates in areas of the Nile Delta have been measured between 40-72% with particularly high rates in children. The World Health Organization (WHO) estimated the disease to lower productivity in the agricultural labor force by 33%, costing a half billion dollars annually in lost productivity. The problem does not appear to be getting better. The waters of the Nile river system provide an ideal breeding ground for snails, the parasite's intermediate host. Rising water tables and expanding irrigated agriculture activities have increased the amount of contact between people and infected snails.

The present strategy for controlling schistosomiasis has a limited impact. A curative drug, praziquantel, exists, but formulation of this drug treatment is not available for children, and the treatment is expensive.

Although AID supports a research project which is searching for a "magic bullet" schistosomiasis vaccine, we believe AID should also be devoting resources to schistosomiasis control. The AID mission in Egypt had developed and approved what appeared to be an excellent schistosomiasis control project a few years ago, but AID/Washington would not approve the project, presumably because it involved a public, rather than private sector undertaking. Meanwhile, schistosomiasis remains Egypt's number one public health problem.

²² Schistosomiasis, also known as bilharziasis, is a disease which can be both chronic and acute. The agents of the disease are flat-worms which live the early part of their life cycle in snails and the adult part in the deep blood vessels of humans.

and AID, Egypt's largest foreign aid donor, is not supporting sufficient efforts to control the disease

One other area within the health sector to which we think AID could be effectively devoting resources is nursing education. Although Egypt has a plentiful supply of qualified doctors, there is a great shortage of qualified, well-trained nurses. The AID mission had, in 1989, also developed a nursing education project which would have addressed this problem by upgrading nursing curriculum and training in 120 nursing schools throughout Egypt. Unfortunately, AID/Washington also withheld approval from this project. Again, the reason given was that the nursing education envisioned in the project involved the public sector. We are concerned with such knee-jerk reactions from AID/Washington to all projects which involve the public sector. A Libertarian ideological agenda of radical restriction of all state activities may raise a host of new problems for the grassroots development process that substitute for those raised by the old Socialist ideological agenda of unfettered state growth.

AID should be devoting resources to nursing education, and in Egypt as in nearly all developing (and developed) countries such education will be done through the public sector.

D Family Planning Heavy population pressure on land and other resources, and a population growth rate that until recently was 2.9% a year, make family planning a crucial issue for Egypt. Progress in reducing fertility rates and crude birth rates had been slow through most of the 1980s, but there have been dramatic declines in 1989 and 1990, with the Crude Birth Rate down from 37 per 1,000 to 32 per 1,000. Even though many Islamic societies have been slow to adopt family planning practices, the Egyptian religious leadership regards family planning as acceptable, although it considers abortion and sterilization to be impermissible as methods of family-size limitation. AID's support for Egypt's population program, and the grassroots development experienced in Egypt which has laid the social and economic preconditions for family planning acceptance, has been instrumental in achieving the recent, welcome declines. Those declines, however, represent only about one-third of what is needed if Egypt is to successfully complete the demographic transition to a low-birth-rate, low-death-rate society.

AID accounts for about 75 percent of all donor assistance to Egypt's population program. Through its large Population Project, AID provides support to both public and private sector family planning activities including expanded and improved family planning services in all public sector hospitals and 80 percent of rural health centers, establishing new

and comprehensive satellite family planning clinics in some 20 governorates, establishing contraceptive social marketing services which cover 8,000 pharmacies in Egypt, support for improved data collection and management, support in educational and mass media campaigns, and providing an adequate supply of oral contraceptives, IUDs, and condoms

AID has contributed significantly both to greatly-needed quality improvement in family planning services in public sector clinics and to the expansion of private sector family planning services. More than half of all Egyptian women get family planning services from private sector clinics

One issue which we have followed is the testing and awaited approval of the new contraceptive, NORPLANT. NORPLANT is a contraceptive which is implanted under a woman's skin and is designed to be effective for five years. NORPLANT, although it was recently approved by the USFDA has not yet been approved for general use in Egypt. Although its cost (\$34 for just the drug) and effectiveness for larger women may present obstacles even if approved, it is hoped that NORPLANT's approval would be a significant help in the attempt to increase contraceptive prevalence and effectiveness.

The IUD was the most commonly used family planning method in Egypt according to Egypt's 1988 Demographic and Health Survey. Even though use of the IUD had doubled since 1984, only 16 percent of married women of childbearing age were using an IUD. The pill is the only other method with widespread use in Egypt. Fifteen percent of married women of childbearing age were using the pill, but there is a high failure rate for pill users in Egypt due to incorrect use. In the survey, nearly one-third of all pill users surveyed had not taken the pill in the last two days. Although one-quarter of these were between cycles, many of the remaining three-quarters gave reasons that implied misunderstanding of the method.²³

There appears to be a significant need for more and improved family planning services in Egypt -- a need which may be entering a period of accelerated growth. We would urge that AID at least gradually increase both the resources and staff devoted to family planning in Egypt, and that it be prepared for the eventuality of a large increase.

²³ Nineteen percent said they take the pills "only as needed," 16 percent were "resting" from the pill, and 8 percent said their husbands were ill or away.

E Small- and Micro-Enterprise Credit Small- and Micro-Enterprise credit activities on a pilot scale are currently sponsored by AID in both rural Egypt -- as a separate activity recently spun-off from Local Development II in Damietta and Sharkiya -- and in urban Egypt, as a project recently started in Alexandria and Cairo. Both activities are currently generating new workplaces for little cost, reaching a class of entrepreneurs which has never been serviced by the traditional banking sector in Egypt, and appear likely to be the most effective and efficient intervention for expanding private-sector employment in Egypt.

The Rural Small-Scale Enterprise Credit program initiated under LD II has been underway in Damietta since December 1989. In May 1990, when we reviewed the project in the field, the average borrower there had 1-2 employees, while the largest borrower employed five persons. The loan amounts ranged from LE 250 to LE 2,500 (\$75 to \$751)²⁴, most being closer to the lower end of that range, while the average loan size was LE 876 (\$263). Repayment terms ranged from 2-12 months at an effective interest rate (though otherwise designated) of about 26%, with weekly installments repaid to loan officers who visit the borrowers at their place of business. The repayment rate had been 100%. We interviewed nine borrowers in Damietta governorate, ranging from an older man who repaired kerosene stoves in a tiny, alley-front shop to a young woman who bought a bandsaw to start a business in her mother's home, making decorative furniture parts. All the borrowers had expanded their output greatly and some had added new workplaces even with their first, small loan.

The borrowing enterprises and loan sizes are slightly larger in the urban Small- and Micro-Enterprise Credit Project in Alexandria and Cairo. The businesses have up to 15 full-time employees, but most have fewer than six. Average loan size is LE 2,200 (\$661) in Alexandria and LE 3,500 (\$1,051) in Cairo, and loans range from LE 500 to LE 10,000 (\$150 to \$3,003). AID requires that 70 percent of the loans go to micro-enterprises (up to five employees) and 30 percent of loans go to small-enterprises (6-15 employees). Borrowers make monthly repayments at a bank. The effective interest rate in Cairo is 28-30%, and even at those rates, demand appears to be almost endless. Actual loan delivery started in January 1990 in Alexandria, and November 1990 in Cairo, and so far the repayment rate has been almost 100%. This urban project has a policy of lending only to existing businesses.

²⁴ At current exchange rates one U S dollar = 3.33 Egyptian pounds (LE)

We interviewed 12 borrowers or loan applicants in Alexandria in May 1990, ranging from a shoemaking shop with three full-time and eight part-time employees crowded into two small rooms adjacent to the owner's apartment, to a tilemaker who had added two additional employees as a result of a LE 3,000 (\$901) loan for raw materials to expand production. Overall in Alexandria, one job is being created for about LE 1,000 (\$300) of continuous credit.

In May 1991 we interviewed four borrowers in Cairo, ranging from a man making aluminum pots and pans who had added four employees with a LE 5,000 (\$1,502) loan to a woman making stainless steel products who had previously paid an effective annual interest rate of 180 percent for supplier-provided credit. Loan officers appear to be having little problem finding additional borrowers.

We urge that these small- and micro-enterprise credit activities be continued and gradually expanded, with a few caveats. First, we hope that AID will not be too insistent in requiring that the traditional banking sector contribute its own resources to these activities early on. The traditional banking sector in Egypt typically does not give loans of less than LE 50,000 (\$15,015), and even then has strict collateral requirements and demands overly burdensome paperwork. The banking system is not accustomed to giving non-agricultural loans nearly as small as those given in these projects, especially without collateral, and it may take *several years* of demonstration before these banks are persuaded that the activity is worthwhile. In Indonesia, it took many years of successful micro-lending under the AID-supported BKK project before the banking system followed suit.

Second, the expansion should proceed slowly. Fine-tuning the credit activities as the projects slowly expand will avoid the possible negative demonstration effect of a rapid expansion before the kinks are worked out. Although it appears that some portion of the World Bank's new social fund will go towards small- and micro-enterprise lending, we urge the Bank not to put too much money too rapidly into this activity. Building the institutional framework and training of credit officers must proceed gradually.

Third, the loans should continue to focus on very small borrowers. The demand for micro-loans appears to be large and that demand should be met first before focusing on borrowers the next rung up.

Subject to the foregoing cautions, this should be an area for steady expansion of AID funding over the coming years.

F Local Development II Since 1978, the Egypt aid program has supported activities both in rural villages and urban neighborhoods aimed at enabling local elected councils (together with parallel appointed bodies) to select and fund small, local subprojects of high priority to their communities. Both the invigoration of local government and the provision of essential local services have been project goals. To date, approximately \$1 billion has been committed to these local development/empowerment activities (since 1986 this has been under the umbrella of the Local Development II project), and over 20,000 local subprojects have been completed, in all 26 governorates, bringing direct benefits to more than 30 million Egyptians. Principal activities have included provision of potable water, drainage of excess or standing water, paving village roads, expansion or renovation of schools and clinics, establishment of markets, youth centers or playgrounds, street lighting, and village maintenance centers. (Other undertakings supported under this umbrella include pilot activities in village wastewater collection and treatment, and small-and micro-enterprise credit, both discussed elsewhere.) Unfortunately, any assured form of AID funding for this project is now being terminated, although much of the funding in the immediate future is expected to be taken over by the World Bank's social fund.

We continue to be highly impressed with the accomplishments of this now-terminated project and its predecessors. With average recent funding of around \$60 million a year (until FY 1992), the project has been creating -- at a rate of about 3,000 a year -- significant improvements and facilities needed by local communities, and utilizing a process to do so that develops grassroots participation and local decision-making abilities. Tens of millions of Egyptians can now see these highly visible and welcome additions as the improvements that American aid has brought to their village or neighborhood. *These are the "monuments" that bring widespread recognition of the worth of what the United States is doing, because they make a difference to people's daily lives* -- not (see the Capital Projects discussion, below) some half-billion-dollar highway that lets the people with Mercedes autos improve their Cairo-to-Assuit driving time by an hour, nor a power plant that lets air conditioners run on cheap electricity and a public-sector aluminum plant continue to operate at a prodigious loss.

The administrative challenges of a Local Development project are, of course, enormous. A group of local Egyptian contractors has developed under the project that can perform to a high standard, using largely Egyptian materials and almost entirely local labor, a system for getting the "block grants" to local communities as they are needed, and monitoring results (through sampling, since oversight of every subproject would be impossible) had been

established, and a "pipeline" of unexpended funds that was long in the early 1980s had been reduced, as experience and momentum were achieved, to less than a year in length

On randomized visits to perhaps 25 of the subprojects during half-a-dozen of our annual fieldwork trips to Egypt, we have been consistently impressed. Even the Inspector General's Office, which consistently looks for problems in the implementation of any project, concluded after an exhaustive 1990 audit "that the program had successfully assisted local governments to plan and implement many thousands of local subprojects designed to provide basic services to the rural poor of Egypt." (At the same time, the IG complained at length that \$328,000 of project funds -- the only such instance cited out of hundreds of millions, which is the sort of point the IG never makes -- had been used for Egyptian-assembled tractors that incorporated Romanian spare parts, contrary to non-Free World procurement constraints.)

How did the end of AID support for so successful an undertaking come about?

A major policy issue in relation to the project in recent years had been the need to create powers in local government units to collect and retain user fees and taxes at the local level which could then be used for operation and maintenance of the individual subprojects, and for support of other basic services. Also at issue had been the provision of a more predictable stream of resources from central to local government. The Egyptian government agreed in 1990 to implement reforms in these areas.

Supporting this policy thrust, AID indicated it would recharacterize the project as a cash transfer to be made in return for sectoral policy reforms in the local-government area. The "projectized" thrust was, however, to be retained, since local currency equivalent to the dollars transferred was to be used for the construction of sub-projects chosen at the community level just as before. In practice, there was to be little change from the present project, *if* the dollars were released.

The possibility that funds might be withheld if adequate movement on policy change did not occur -- a possibility which had indeed already existed for several years -- created, however, a dilemma of which AID/Cairo appeared to be keenly aware. The policy changes were needed if LD II was to be sustainable over the long term, but AID would have to walk a careful line of being reasonably tough on the policy discussion and yet not losing LD II's momentum because of a want of funding. (Since there was little in the "pipeline," actual loss

of a year's funding would essentially bring the entire enterprise to a halt)²⁵ The Government of Egypt had shown some signs that it was willing to move on the policy reforms, but that it might take some time for those policy changes to be implemented. Moreover, there was a possibility that the central government might be willing to sacrifice funding for LD II -- a project that many key figures in the central government had never liked, precisely because of its decentralization features -- since these officials knew the money would then simply get diverted to a different, *centrally controlled* project.

Regrettably, when the Egyptian government resisted carrying through its 1990 promises to allow local government units to raise revenues, AID/Cairo decided that funding for LD II would be terminated. The damage in the short term has been limited, however, because the World Bank has indicated that it will use a major portion of its new \$500 million social fund to finance such local infrastructure projects -- which have the additional merit of being both quick-disbursing and labor-intensive, qualities which the Bank is seeking for social-fund projects. Such activities can also seek local-currency funding generated out of AID's Commodity Import Program, but this seems likely to be at a fraction of the previous funding level.

AID seems unlikely to use the funding that had gone to LD II for any activity nearly as beneficial to Egypt's poor majority, and should, we believe, begin looking beyond interim funding by the Bank to a *resumption* of funding for a similar project as early as FY 1994, in the meantime continuing efforts to resolve local-government-financing issues. Such funding should indeed be considered at a higher level. LD II had never received funding of more than \$75 million a year, and averaged around \$60 million. It seems clear, however, that both absorptive capacity and need would support outlays of \$100 million a year (apart from village wastewater activities, which might well spin off as a separate project as they enlarged beyond the pilot or demonstration stage). Thus, a new Local Development project should be considered a prime candidate for funding, at higher levels than its predecessor, in future years. If this activity is to be permanently foresworn, its funding instead used to buy telephones or cheap electricity for Egypt's small middle class, it will indeed be a sad day for Egypt's poor majority.

²⁵ The problem is somewhat analogous to that cited above in relation to the Agricultural Production Credit project, one is loathe to sacrifice important project activities if additional sectoral reforms are *not* carried out.

G Village Wastewater AID has spent large sums in providing modern sewerage systems for Cairo, Alexandria, and several provincial cities. Meanwhile, in the villages, where a majority of Egyptians continue to live, such systems have been at the demonstration stage (under LD II). Unfortunately, AID support of this activity is expected to terminate with LD II. Present sewage facilities in the villages -- which are densely-populated and built up, rather than spread out -- generally consist of an underground vault or cesspit attached to each extended family dwelling or small apartment building. When the vaults are full, they are pumped out by entrepreneurs using small donkey-drawn wagons, which in turn are emptied into the canal-and-drainage system, generally flowing back into the Nile. To save on pumping-out costs, many households dispose of their "gray water" from washing and bathing onto the ground rather than into the vault, where it often contributes to high water tables and standing water in the streets (even saturating, in some villages, the ground floors of the houses themselves). Drainage systems, many introduced through LD II, have reduced a number of the worst standing-water problems, but the overall process of sewage disposal at the village level remains costly and unsanitary.

The alternative is a village sewerage system, in which house-and-apartment connections are hooked to a collection network of sewer pipes (rather than into vaults), through which the collected effluent is in turn pumped, or fed by gravity, to a small wastewater treatment facility. AID is presently testing five different village wastewater treatment facilities -- the principle variable part of such a system -- under LD II in Damietta Governorate in the northern Nile Delta: stabilization pond, aerated lagoon, oxidation ditch, aqualife/Stog unit, and extended aeration or SOAF units. Without going into the technical details, it is sufficient to say that the above list progresses from the simplest to the most complex technology, with the simpler facilities requiring more land, but less capital, less operating skill, and less maintenance. Based on our visits to all five models, and our discussions with AID personnel and technical specialists, it now appears that the simplest technology, the stabilization pond, will prove the best. The stabilization pond has no moving parts or electric power requirements, is inexpensive to construct, is easily maintained, has no sludge by-product, requires little in operating costs, and can be easily upgraded to handle additional sewage (without using additional land) as village population increases. The one downside of the stabilization pond is that it requires more land area than the other models. But, even if enough stabilization ponds were built to handle all wastewater needs in rural Egypt, it can presently be estimated that less than 0.2% of Egypt's agricultural land would be

needed one acre per 3,000 people, for a total village population of 35 million. This would require a maximum of 11,600 acres out of the total cultivated area of 7 million acres, for universal application of such a model.

The resources needed for general provision of a collection system with stabilization pond treatment to Egypt's villages would be roughly as large as those that have gone to AID's Cairo Sewerage project -- in the \$1 billion range or more -- but would bring benefits to perhaps three times as many people. Preliminary calculations based on the present pilot projects would suggest costs per family benefited about one-third or less those experienced under Cairo Sewerage. This important activity should be viewed as another prime candidate to receive major AID funding in the 1990s. It should be spun-off from the terminating LD II project and given a separate identity, just as has been done with rural micro-enterprise credit.

The provision of continued funding by AID is clearly the threshold necessity. Beyond this, there are two issues. One relates to a series of technical points aimed at speeding up and improving both the present demonstration process and an eventual broader program. These points deal with the need for the village contribution to be a percentage of total cost rather than made in the form of land (which presently creates a bias towards the lowest land-using, most capital-intensive approaches), the need for better administrative and timing coordination of the system elements -- wastewater-treatment facility, collection network, pumping stations, and household connections -- and the need for advance commitment from households to make and pay for connections. Of course, any expansion of the project activities must also include expanded training for Egyptian operation and maintenance of these plants.

The second issue concerns the interpretation of Egyptian law no. 48/1982, which establishes the quality of effluent that can be discharged into the canal or drainage system, stated in terms of the biochemical oxygen demand (BOD) and suspended solids (SS) that are permitted to remain in the discharged effluent after treatment. Depending on this law's administrative interpretation, it is feasible to meet the standards of the law through a normal stabilization pond (as well as with the other models). An unduly strict interpretation of the law, however, would require additional treatment facilities that are so expensive that AID's participation in the village-wastewater area would have to be abandoned. The question to be resolved administratively is whether the BOD and SS limits in the law represent monthly averages or maxima. If they are construed as the latter, so that in effect the discharged effluent cannot exceed these limits *at any time*, the task of treatment is impossible within any

reasonable financial constraints Unless there is simply a waiver of the requirement, such an interpretation would effectively end AID's village wastewater efforts The paradox, of course, is that the donkey-cart operators are presently putting wholly-untreated sewage into the canals and drains -- but AID, if it becomes involved beyond the present pilot stage, will be held to a higher standard *How high is the question*

H Capital Projects From 1975 to 1991, AID provided more than \$1.3 billion in project and commodity support to develop Egypt's electric power generating sector An additional \$100 million has been programmed for fiscal year 1992

Large new power plants like Shoubra on the outskirts of Cairo -- built with substantial U S support -- are impressive "monuments" Viewed in themselves, they may be well-built, constructed under-budget and on time by U S firms, and well-managed Viewed in context, as part of the Egyptian energy sector, their subsidized construction can only be viewed as a disaster We regard the investment of grant (or concessional) aid resources in power plants as absolutely indefensible with Egyptian energy rates anywhere near as heavily subsidized as they presently are, and as an extremely marginal investment even if the rates were not subsidized For years, AID has held out the "carrot" of funding power plants in return for Egyptian increases in energy prices, yet as AID candidly admitted at the end of 1990, "over the past ten years energy price increases have lagged behind the overall inflation rate " At that time, average electricity rates were "one-fourth of world market rates", and heavily-subsidized public enterprises in energy-intensive areas like fertilizer and aluminum were paying rates equivalent to 1.5¢ per kilowatt hour or less (in many countries, average rates over 10¢/kwh are common)

One result of Egypt's heavily subsidized power has been per capita use far higher than in most less-developed countries, and rapid growth in such use -- 8% per year from the mid-1980s, though recently slowing somewhat Most of this growth comes at the cost of exportable petroleum, although Egypt has recently been switching more plants to burning previously unutilized natural gas There was also an average increase in electricity prices of around 50% in May 1991, as part of the overall deal on macro-economic reform worked out by the Egyptians with the World Bank and IMF Even though this did represent an increase significantly greater than the inflation that had intervened since the previous increase, and the GOE has promised further such "real" increases (with a goal of reaching world market prices by the mid-1990s), electricity rates still remain about one-third of world market rates

Power sector outlays of \$100 million a year are simply not justified while rates remain thus heavily subsidized -- and if rates ever approach world market levels, there will almost certainly be a period of negative growth in use, rendering expenditures on increased capacity unnecessary for a significant time. Moreover, if rates approach world market levels, and whenever Egypt does then require additional generating capacity, they should be able to borrow commercially to build such capacity and pay back the loans. In all events, the days of "free" power plants, built with foreign aid and providing highly subsidized power mostly to inefficient public enterprises and to the middle class should be declared to be over. At most, AID should provide a minor fraction of the present \$100 million a year, solely to increase the efficiency of existing power generation and use.

Another highly dubious area for new capital projects is telecommunications. Nearly all of the easy and relatively inexpensive improvements in the Egyptian telephone system have already been made. Recent undertakings in this area have reflected estimated costs of \$800 to \$1,500 to install the exchange equipment and lines necessary to provide one new telephone, enough resources, for example, to instead provide basic production credit to half-a-dozen small farmers, or to create three new jobs through micro-enterprise credit. Under the new Egypt Telecommunications project AID now proposes to commit an additional \$250 million in the telecommunications area over the next five years. With Egyptian telephone service already operating at a high level by less-developed-country standards, benefit-to-cost ratios for most future outlays appear strikingly adverse.

Another proposed capital project that had been earlier discussed in Cairo, AID support for the Cairo Ring Road (or at least for the bridges for that road), appears fortunately dead. Like most of the heavy capital projects, it would have brought the bulk of its benefits to a small middle-class segment of the Egyptian population, diverting resources that are still desperately needed for programs that will help the majority of Egyptians to become more productive, healthy and self-sufficient. In this case it would have been a small minority of auto owners, while in the other cases mentioned it would be largely the same small minority benefiting from telephones or air conditioning.

But the pressures for such capital projects must be consciously resisted, against the importunities both of American firms seeking valuable construction contracts, and of those Egyptian officials (and those in AID) who would like to see grand and visible "monuments". The extremely high opportunity costs of such "monuments" -- measured by what could instead be done with the same resources for the vast numbers of hard-working poor -- must

constantly be borne in mind. The termination of LD II and the proposal to fund a large new telecommunications project do not portend well for AID's current priorities.

I **Helwan Housing** We include a discussion of the Helwan Housing and Community Upgrading Project, which received its final obligation in FY 1981 because it has received negative media and congressional attention resulting largely from some inflammatory statements in an uncomplimentary IG audit. The latter were picked up in turn in a CNN Special Report which aired in December 1991. The Helwan project was developed in the mid-1970s to demonstrate that socially acceptable basic housing, public utilities and community facilities can be provided for low-income families at an affordable price that also allows a substantial recovery of the investment. An October, 1988 audit by AID's Regional Inspector General's Office in Cairo stated that, after 10 years and the expenditure of \$134 million, the project was still far from reaching its objectives. The statement in the audit that the media initially picked up on was that "[a]s of June, 1988, not a single low-income family occupied a house in the new community."

We visited the site in May 1991 and found that although many problems exist -- most of which are constructively detailed in a "Lessons Learned" paper²⁶ called for in the IG audit -- many families *are* now living in the new community, and the living conditions and opportunities for low-income Egyptians in the upgraded communities have been greatly improved. It is clear that while the project will not provide a replicable demonstration of low-income, affordable housing, it has provided substantial benefits to significant numbers of low-income Egyptians. Gardner and Van Huyck emphasize this point in the "Lessons Learned" paper. They state:

"It needs to be recognized that, in spite of all of the problem issues, the Helwan housing program should not be viewed as a basic failure. Contrary to the Inspector General's report, which was based on field work prior to mid-1988, the physical aspects of the project are now moving rapidly toward completion. Ultimately, more than 20,000 moderate income Egyptian households (more than 100,000 persons) will be able to purchase new housing units which would not otherwise have been available had AID not continued to

²⁶ Donald Gardner and Alfred D. Van Huyck, "The Helwan Housing and Community Upgrading Project for Low-Income Egyptian: The Lessons Learned," February 1, 1990.

press ahead with this project in spite of its difficulties In the upgrading component, seven areas in Helwan with a population 100,000 plus have already received some benefits and ultimately will receive substantial improvements in their environmental condition A decade from now, these projects in Helwan may well be considered successful from the perspective of their contribution to the beneficiaries " ²⁷

The Helwan Housing and Community Upgrading Project was, we believe, an innovative project designed to address a serious need facing Egypt's urban poor. Although the project failed in showing how that need could be replicably solved, we would rather see AID attempt such innovative projects and fail, than implement "safe" projects *which provide no grassroots benefits to the poor*

J Cash Transfer In recent years, until FY 1992, \$115 million each year has been given as dollars transferred to the Egyptian government in return for supposed macro-economic reforms of the economy, of the general kind sought also by the World Bank and IMF. In theory the amount of cash could be still larger since a previously existing legal ceiling on the amount of cash transfer has been lifted. The practice of granting general cash transfers has long been justified by reference to the Foreign Military Sales debt, as allowing an offset to the dollars that Egypt had to pay the U S to service that debt.

But the \$6.7 billion Egyptian FMS debt was cancelled by Congress in late 1990, in recognition of Egypt's role in assembling the coalition that supported the Gulf War and the costs incurred by Egypt, so that longstanding rationale for Cash Transfer no longer applies. The macro-economic reform rationale has always been a notably weak one, since the IMF and World Bank can hold out the prospect of vastly greater resources -- including the catalyzing of massive cancellations or reschedulings of Egypt's foreign debt -- in return for the same over-all reforms. And there is no development rationale in Foreign Assistance Act terms, since cash transferred to the Egyptian government effectively disappears into a vast hole, with no identifiable benefit for Egypt's poor majority -- indeed, the opportunity cost of this \$115 million a year, measured in terms of what *could* be done with equivalent resources, has been about the same as that for the annual expenditures in the power sector.

²⁷ Gardner and Van Huyck, p. 6

Whether for these or other reasons, it appears that AID/Cairo is now in the process of redirecting Cash Transfer from macro-economic reform to "sectoral" reform. AID is also increasing the amount to be used as cash transfer, from \$115 million to \$185 million in FY 1992, and a requested \$210 million for FY 1993. However, the redirection from macro-economic to sectoral reform provides only an opportunity, not a guarantee, that the resources will be used in ways that benefit the poor majority. Much depends on what sectors, and what reforms within sectors, are chosen for support, and on whether the transferred dollars call forth equivalent local currency that is then used for specific "projectized" purposes that, complementary with the sectoral policy reforms, benefit the poor. At its best, sectoral cash transfer accompanied by uses of equivalent local currency that are targeted on the poor becomes virtually indistinguishable from excellent existing projects such as Agricultural Production Credit and Local Development II.

Illustrations of desirable uses of Cash Transfer to support sectoral reforms might be

- Cotton pricing reform. Release of most or all of one or two years' cash transfer in return for sharp increases in the prices paid to farmers for their cotton. At the same time, pounds equivalent to the dollars would be allocated to actually pay increased cotton prices to the growers, who are principally small farmers.
- Banking loan-policy reform. Release of most or all of one or two years' cash transfer in return for changes in loan-policy for Egyptian banks that would lower minimum loan size from the present amount (around LE 50,000, or \$15,000), simplify paperwork, and eliminate collateral for the smallest loans, permitting widespread lending to micro- and small enterprises. At the same time, pounds equivalent to the dollars would be on-lent by the Egyptian government to the banking system, earmarked specifically for the making of such loans.

K Commodity Import Programs Generally, \$200 million a year (although \$300 million in FY 1989) has been provided to the Egyptians in the form of dollars to be used to import commodities from the U.S. In earlier years these commodities were all or mostly provided for public-sector enterprises and GOE ministries, while recently most have gone to private-sector enterprises. No overall development plan or priorities are served by the commodities brought in; they are a hodge-podge, furnished now mostly to private enterprise on a first-come first-served basis. The Egyptian pounds paid for the commodities go into local currency accounts, from which they are allocated mostly to Egyptian government ministries for general operating expenses, although somewhat less than 10% of the local currency is used to help support

AID's own operating expenses in Egypt. Further amounts are used from time to time to support some of the local-currency costs of AID projects. Some may now be used to support certain LD-II-type activities.

The CIPs represent nearly 25% of AID's entire program in Egypt, and like Cash Transfer given for supposed macro-economic policy reforms, it is unfocused in development terms, with essentially no benefit going to the poor majority. Nor is the bulk of the generated local currency used to provide such benefits.

Aside from the desirability of simply cutting CIP -- preferably to no more than \$100 million a year -- the most likely route to improvement probably lies in using more of the generated local currency for more targeted and specific uses, rather than for general undifferentiated support of ministry budgets, as at present. We have already suggested a possible use of local currency to support increased cotton prices to small farmers, which could as readily be done with pounds arising out of CIP as with pounds arising out of a sectoral Cash Transfer. Or, for example, a substantial amount of local currency taken out of the private sector by the latter's payments made for goods brought in by the Egyptian government under Private Sector CIP might be put back into the private sector by using that local currency to finance a loan program for small (and perhaps even micro-) enterprises via the banking system. A related approach might be to consistently use a large fraction of the local currency generated out of CIP to provide *incremental* (not substitute) local-currency support that would permit enlarging existing good projects that require substantial amounts of local currency, such as Agricultural Production Credit and a resuscitated Local Development project.

It needs to be recognized that the CIPs, together with general Cash Transfer and Power Sector Support, have consistently represented over half the annual program in recent years, \$415 million or more. This means that, at the outset, over half the total resources of the Egypt program have been lost for grassroots development purposes²⁸. And, ominously, as discussed below, there are dangerous new pressures that may lead to an *increase* in the amounts allocated to these or similar undertakings.

²⁸ Although, as noted, improvements could be made both in a sectoral Cash Transfer and in CIP that would give them a substantial grassroots development impact.

L Overarching International Issues for A I D In addition to issues concerning specific AID projects in Egypt, we have identified several overarching issues which pertain to AID's ability to implement high-quality projects, not only in Egypt, but worldwide

One central concern in the wake of our 1991 fieldwork trip is that three current developments affecting the personnel side could steadily force AID/Egypt to erode its support for the good and effective projects -- which tend to be labor-intensive in terms of administrative requirements -- and increase its funding for those with little grassroots impact, which tend to be much less demanding administratively

First, the Egypt AID mission has cut its force of direct-hire U S -national personnel from 134 to 102 over the past decade. With \$815 million in annual resources to administer, this gives one of AID's lowest personnel-to-dollars ratios in any country. Further cuts are in prospect. Driving these cuts is worldwide pressure on AID from the Office of Management and Budget (OMB) to carry out U S -national personnel reductions entirely at the expense of mission personnel in the field, rather than reducing personnel in AID/Washington. Over the past decade, direct-hire U S -national personnel in the field worldwide have been cut from 1,475 to 1,181, while AID/Washington personnel have actually gone up, from 1,926 to 2,021. OMB's supposed rationale for this pattern of cuts is that it is more expensive to maintain personnel in the field. But the logical extension of such reasoning would be that virtually all AID personnel would be in Washington, and none in the field, despite the fact that personnel in the field play a crucial role with respect to virtually all of AID's most effective projects, in Egypt and elsewhere. The ultimate result of such reductions of personnel in the field is that AID, in Egypt and elsewhere, becomes increasingly pressed to spend resources on cash transfers or large capital projects, undertakings that have little bearing on grassroots well-being or on political stability, but that require fewer on-the-spot AID personnel to administer. At the same time, AID/Washington personnel convey the message to us that the Agency has more people than it needs in its Washington headquarters. Such a pattern of personnel reductions of U S nationals in the field seems to make little sense, and should be stopped, and if possible, reversed.

The second development threatens AID's ability to continue the extensive use of Egyptian direct-hire personnel. With the cuts in direct-hire U S -national personnel, Egyptian direct-hire personnel have assumed an ever larger and more vital role in administering the program. But OMB has now put pressure on AID to reduce, or end, the use of local currency to support operating expenses, in Egypt and elsewhere. Such local currency, which is

generated out of a portion of general Cash Transfer and Commodity Import Programs and amounts to a second "bang" for those appropriated "bucks", currently pays the salaries of Egyptian personnel. If it could not be used, Congress would either have to appropriate additional dollars for the purpose, or Egyptian personnel would have to be laid off, to the great detriment of the program. OMB's rationale for withdrawing local currency, we understand, is that such local currency may not be available in the future, and should therefore not be relied upon. But *no* funds, dollars or local currency, are ever assured for foreign assistance beyond a one-year appropriation, or at most two-year authorization. Local currency has been generated in the Egypt program for some fifteen years, and appears likely to be generated as long as there is an Egypt aid program. Moreover, less than 10 percent of the local currency being generated in the Egypt program is used for operating expenses. The remote possibility that there may not be enough local currency to put to a particular good use at some moment in the future hardly seems to be a sufficient reason to stop making that good use of the resource today. (Indeed, most other local currency generated in Egypt out of Cash Transfer and CIP has not been used in effective ways.) Egyptian pounds in local currency accounts should continue to make their vital contribution to the operating expenses of the program. This should hold true of local currency accounts in other countries as well.

Finally, compounding the problem, the Egypt mission is now under pressure from the Regional Inspector General's office to do detailed tracking of local currencies that have been generated in "cost recovery" programs. Here it is not a question of reduction in personnel available to supervise the best grassroots projects, but of diversion of their time to accounting-type functions having to do with resources that the United States has *not* provided. Such "cost recovery" programs increasingly form a vital part of some of the most essential projects, such as those in family planning and health -- prospectively, they may play a role in such additional areas as small-farm irrigation. For example, a family planning clinic using IUD's supplied by AID may, pursuant to the project agreement, charge 1 Egyptian pound to examine a prospective user, 2 pounds for the IUD, and 2 pounds for its insertion, with the 5 pounds (about \$1.50) then deposited into a separate account which is to help defray future operating expenses of the clinic. The clinic building, most present operating expenses, and the physicians' training have all been Egyptian-funded. Yet it is claimed that AID must assume responsibility and spend time specifically tracking the uses of these locally generated "cost recovery" resources, which -- depending on the program -- might be spread around scores, or even hundreds, of individual small accounts around the country. It seems

appropriate to verify that the accounts have been set up and initial accounting procedures established to use such locally generated currencies for future operating expenses. Beyond that, imposing on U S salaried personnel the responsibility for detailed tracking of these non-U S resources, paid in by Egyptian users of Egyptian facilities, seems unreasonable and well-nigh impossible. Nor would hiring Egyptian accounting firms solve the problem, as long as the AID mission was held responsible for the use of the pounds, for mission personnel would then have to follow up on and be responsible for any audit recommendations of such accounting firms. Given AID's limited and already heavily committed personnel and the great needs in areas such as family planning and health, the Regional IG's demand for tracking of such non-U S "cost recovery" Egyptian pounds should be dropped.

Aside from these personnel questions, another worrisome trend is AID's new agency-wide focus on "Buy America." The Foreign Assistance Act has long provided a strong preference for U S procurement of commodities purchased for foreign aid projects. However, in the past, waivers were routinely granted for commodities which were produced within the aid-receiving country and could be obtained at a lower cost. This seemed logical, not only because the commodities were less expensive, but because it helped to promote a sustainable development process within the aid-receiving country.

AID/Washington has recently changed that policy, however, and is exerting pressure on AID Mission Directors in the field to procure a larger share of the commodities from the U S, at the expense of locally produced goods. This change in AID policy may in part be due to pressures from some in Congress to use the foreign aid program to help make the U S competitive on world markets. Whatever the source of the increased emphasis on "Buy America", we believe the policy is extremely short-sighted and is unlikely to provide any significant help in lowering the U S trade deficit. The "Buy America" policy emphasizes the short-term U S need -- greater exports -- at the expense of the long-term goals of raising standards of living and thus promoting eventual markets and economic stability.

The "Buy America" emphasis also encourages greater expenditures on infrastructure, where the U S has some advantage in the supply of heavy equipment, rather than the alleviation of poverty. The Foreign Assistance Act directs AID to focus on the poor in developing countries. One of the sound approaches outlined in the Act is to expand employment through the local private sector as a means of alleviating poverty. Now, however, AID/Washington has indicated that the U S private sector should be supported as

an end in itself through the use of foreign aid resources This approach leaves the poor behind There are better means than the foreign-aid program to encourage exports

VII A PERSPECTIVE FOR THE NEXT 10 YEARS

The ESF program for Egypt can most usefully be viewed, we believe, not as an "\$815 million a year" aid program, but as a fund of \$8 15 billion (perhaps more) available over the next 10 years to help solve Egypt's remaining grass-roots development problems and put the country well on the road to self-sufficiency thereafter

If we then visualize an aid program for the years FY 1993-FY 2002, we might see the obligation of a total of \$8 15 billion in funds falling roughly into the following pattern

1 Agricultural Production Credit

Complete the capitalization of the Principal Bank for Development and Agricultural Credit for both production and medium-term loans nationwide (but specify that the bulk of the additional resources are for small farmers of 5 acres or less -- 90% of the holdings and 57% of the land) This represents the difference between the \$243 million obligated or expected to be obligated through FY 1992 and a total PBDAC need for the dollar equivalent of up to LE 2 billion (obligations here would be projected to fall chiefly in the period FY 1993-97)

\$358 million

2 National Agricultural Research Project

Anticipated remaining obligations, after FY 1992, for the planned \$300 million project (obligations chiefly in FY 1993-97)

\$123 million

- 3 Irrigation Management Systems
 Anticipated remaining obligations for the existing IMS project (\$16 million in obligations chiefly in FY 1993-94), and, upon confirmation of initial results, funding for expanded or follow-on project, chiefly for mesqa improvement and related programs, calculated on assumption that such programs reach one-half of the 6 million acres of "old" lands (i e , non-reclamation lands) and that average cost is LE 1,000/acre (resulting in \$900 million in obligations, chiefly in FY 1994-2002) \$916 million
- 4 Basic Education
 Expansion of annual expenditure level to around \$50 million (obligations FY 1993-2002) \$500 million
- 5 Health
 Anticipated remaining obligations, after FY 1992, for Child Survival and Cost Recovery Health (together about \$91 million), in addition, obligations for these or equivalent activities are assumed to continue throughout the 10-year period at average level of \$20 million/year, finally, Nursing Education and Schistosomiasis Control are considered to be funded at the originally proposed level of \$30 million each (following whatever battle between Congress and AID/Washington is necessary to reverse the latter's disapproval of these projects and to achieve funding) (obligations FY 1993-2002, but peaking in mid-1990s with introduction of Nursing Education and Schistosomiasis projects) \$351 million

6 Family Planning

Anticipating costs averaging \$30 million/year during FY 1993-97 and \$45 million/year during FY 1998-2002, assuming that, from a mid-1980s base of 37 per 1000, crude birth rate is down to an average of 29 per 1000 during the first five years and 25 per 1000 during the second five years, and further using a highly provisional cost figure of \$60 per birth averted under family planning (this is reduced, taking recent Egyptian experience into account, from a higher figure developed in the mid-1980s on the basis of discussions within the Mission and experience elsewhere), also adjusted for the somewhat higher population base in later years

\$375 million

7 Small- and Micro-Enterprise Credit

Anticipating gradual funding of a nationwide program with revolving credit resources of \$300 million (obligations chiefly in FY 1994-2002, gradually increasing over the period)

\$300 million

8 Local Development

Assumes *resumption* in FY 1994, with expansion of annual expenditure level to around \$100 million, apart from village wastewater activities (obligations FY 1994-2002)

\$900 million

9	<u>Village Wastewater</u> Assuming confirmation of initial results, replication of stabilization pond or other least-cost appropriate technology for substantially nationwide application to Egypt's villages (obligations FY 1994-2002, gradually increasing over the period)	<u>\$1 billion</u>
Total of foregoing		\$4 823 billion
10	Maximum residual amount for <i>All Other Project Undertakings</i> (including capital projects) plus <i>Cash Transfer and CIPs</i>	<u>\$3 327 billion</u>
Grand Total		\$8 15 billion

Thus, a program which genuinely maximized the opportunities to use this projected \$8 15 billion over the coming 10 years to meet the needs of Egypt's grassroots development would spend approximately 59% of the total resource on projects targeted on the poor majority (items 1 through 9 , totalling \$4 823 billion) This may be compared with the best performance so far, the 36-40% proportion achieved in FY 1986-88 (see Table 1 above) In terms of available undertakings and the opportunities that exist in Egypt, such a program is certainly feasible, but would have to be carefully planned for and maintained over the course of a decade

If such a plan could be carried out by AID/Cairo and the GOE, using these unique aid resources, there is little doubt that the grassroots transformation of Egyptian society could be completed by the beginning of the new century

List of Abbreviations and Definitions

AID	Agency for International Development Executive branch agency which principally administers foreign economic aid
APC	Agricultural Production Credit An agricultural project funded by AID
ARC	Agricultural Research Center
CBR	Crude Birth Rate Number of live births per 1,000 population in a year
CIP	Commodity Import Program Foreign economic assistance which is provided to countries in the form of a range of U S commodities
DA	Development Assistance
ESF	Economic Support Fund These resources, as distinct from Development Assistance resources, are allocated to countries with special economic, political or security conditions involving U S national interests in amounts which "could not be justified solely" under the development assistance portion of the foreign aid program (FAA, sec 531(a))
FAA	Foreign Assistance Act Legislation which governs the use of the foreign aid
FY	Fiscal Year
GOE	Government of Egypt
IMF	International Monetary Fund
IMR	Infant Mortality Rate Number of deaths in first year of life per 1,000 live births
IMS	Irrigation Management Systems An AID project aimed to upgrade Egypt's irrigation system
NARP	National Agricultural Research Project An agricultural research and technology transfer project funded by AID
ORT	Oral Rehydration Therapy

- PBDAC** Principal Bank for Development and Agricultural Credit
- PWWR** Ministry of Public Works and Water Resources
- SFPP** Small Farmer Production Project An AID project that was the predecessor of the Agricultural Production Credit project
- USFDA** United States Food and Drug Administration

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