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Country Development Strategy Statement

FY 1989

EGYPT

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USAID/Cairo FY 1989 CDSS

Executive Summary

The current U.S. economic assistance program for Egypt began in 1976. The basic rationale was to demonstrate to Egyptians the real benefits associated with the political course their leaders had taken. The program's first objectives were to rehabilitate and expand a war-damaged and deteriorating infrastructure.

Today, with a much improved infrastructure in place, attention has turned to the Government of Egypt's economic policy environment as the focus for the next stage of effort. The government's current economic policies are a meld of Nasserist socialism and "infitah" capitalism. Neither is working very well.

The Government and donors are becoming convinced that the critical development problem which Egypt must now address is low productivity of the economy, particularly in agriculture, industry and the services needed to support them. The primary factor which prevents the economy from producing at its full potential is an economic system which stifles market forces.

USAID's strategy will be to increase the productivity of the economy by helping the Government of Egypt (GOE) in its efforts to remove the restrictions to operation of market forces. Key elements of our growth strategy are

- economic reform to provide the incentives for production increases;
- science and technology to provide the means; and
- cost-recovery in provision of legitimate government services, to promote efficient use and reduce the budgetary burden.

Our key assumption is that the GOE will reach agreement with the IMF and IBRD, will obtain multilateral debt rescheduling, and will implement a significant reform program.

USAID will support

- the policy dialogue process, by participating in the newly-emerging GOE-donor consultative process, and by providing technical assistance to the GOE for policy analysis when needed.

- the adjustment process, by providing limited cash and commodities, in a package of assistance with the World Bank and the IMF, as warranted by the pace of reform and other resource availabilities.

- increased productivity in key sectors:
  - agriculture and private industry;
  - services and infrastructure needed to support productivity improvement;
  - local development; and
  - education and training.

- development of institutions required to channel resources productively as the Egyptian government opens its market place to free market principles. Capital market development would be a key feature of such an intervention.

- family planning, health, and private voluntary agency activities to limit the erosion of productivity gains which can result from rapid population growth and to support provision of a safety net of basic services to the poor.

Support for the Policy Dialogue Process

The GOE is negotiating agreements with the IMF and the World Bank aimed at multilateral debt rescheduling. From this process, we anticipate the emergence of a donor consultative group. USAID will be an active participant, but policy issues and the donors' responses to them will be determined jointly through the consultative process.

We expect the IMF to take the lead on policy discussions regarding exchange rate unification and interest rate increments, as well as its standard series of monetary restrictions to curb internal demand. USAID, the IBRD, and other donors will focus on policy issues in agriculture, energy, and industry. A major theme for USAID will be private sector development.

Temporary Support for the Adjustment Program

USAID will be responsive to significant reform efforts. We are willing to increase the cash and commodity portion of the program, in coordination with the IMF and the IBRD, as warranted by the pace of reforms and needs of the economy. A basic element of the GOE's reform program is maintenance of a safety net for the poor. Some of our project assistance is directed to this goal.

Support for Increased Productivity in Key Sectors

The major share of USAID's program will be in projects during the planning period. Under an improved policy environment, the need for project assistance to promote growth in key sectors will increase. Assistance levels in these sectors will be determined by GOE progress in freeing them from the distorting influence of controlled prices and markets.

Agriculture has greater potential for immediate growth than any other sector of the economy. Egypt's agricultural production has grown only a disappointing 2 to 3 percent annually for the past several years. Production in crops for which Egypt has a comparative advantage could increase 25 to 75 percent, with the right economic incentives and use of modern technologies.

USAID will address key agricultural policies which restrict operation of market forces, including:

- mandated cropping requirements for certain key crops;
- state procurement at controlled prices;
- public sector monopoly of most inputs;
- restrictions on marketing; and
- inappropriate public sector investments in new lands.

Three major projects in agricultural credit, research and extension, and irrigation management will serve, along with PL-480 Title I, as the vehicle for this sectoral policy dialogue. These projects will also address key scientific, technical and physical constraints to increased productivity:

- the need to reorient research and extension services to be responsive to farmers' technology needs;
- inadequate physical capacity and control structures in the irrigation system to meet the demands of increased agricultural production; and
- inadequate availability of credit, and the need to reorient the agricultural bank towards banking services.

Despite "infitah", private industry has averaged growth of only 3 to 8 percent annually in recent years, far short of what other economies, which have encouraged market forces, have attained. USAID's strategy will focus on improving the investment climate and promoting investment, improving business services and business support institutions, and expanding business finance.

Key industry policies which USAID will address include

- privatization of public industries and allowing freer competition between private and public firms;
- removal of protective customs barriers;
- reduction in government interventions;
- export promotion; and
- removal of barriers to small scale enterprise investment.

USAID will support these policy discussions with project activities including:

- management and skills training to improve practices in production, marketing, accounting and finance;
- a capitalization fund to help in restructuring and sale of public sector industries to the private sector;
- export development and tourism planning; and
- import finance (private-sector CIP) and term credit, until such time as the policy environment has eliminated the need for these activities.

As the economy opens to market operations, industrial and agricultural growth will require expanded and more flexible support services through which to channel resources. USAID will direct project activities in private industry and agriculture to:

- development of capital markets;
- expanded access to unsubsidized, untied agricultural credit;
- improved banking facilities, equity and venture capital, for both agriculture and for small-scale enterprise.

The Local Development program is an important vehicle for providing community infrastructure needed both to support increased economic activity, and to contribute to a safety net of basic services. It also promotes the growth of democracy through increased authority for local elective and executive councils. Local governments are often more receptive to testing new technologies and policies than is the central government. USAID will continue this highly popular program, and will use it to demonstrate the potential for

- privatization of governorate-owned industries;
- improved cost-recovery mechanisms for government services;
- provision of banking facilities for small scale industry; and
- strengthened democratic processes.

Despite massive investments in power, problems in the system will prevent it from providing the energy needed for expanded productive activity. State-controlled, unrealistically low energy prices have fostered tremendous growth in consumption. Lack of attention to operation and maintenance and cost recovery have led to poor efficiencies in generation, transmission, and end use. Power shortages in the next few years will prevent the system from meeting peak demands of manufacturing and services.

USAID will support the World Bank in its dialogue with the GOE to increase energy prices. We will provide no funding for physical improvements in the sector in absence of significant price increases. With price increases, we will take a "least cost" approach focusing on rehabilitation, conservation, training and planning.

Urban water/wastewater systems have by now been substantially improved. USAID will phase down assistance for this sector. We will fund no urban capital investments beyond those needed to complete ongoing and planned activities. We will provide institutional support, however, for operation and maintenance, financial and technical training for water/wastewater agencies. We will continue efforts to improve cost-recovery through increased water/wastewater tariffs.

A literate, well-trained labor force is essential for growth of modern industry and agriculture. Basic education as well as management and technical training will remain the key elements of USAID's education and training program.

Health, Nutrition, Population, and Private Voluntary Organizations

A high population growth rate erodes the impact of productivity gains in industry and agriculture. Acceptance of family planning has been constrained by lack of access to reliable, effective family planning services. USAID's population program will increase emphasis on provision of clinical family planning services and expand support for private sector family planning programs.

To support provision of a basic safety net of services for the poor, USAID's health and nutrition assistance will focus on technological interventions to combat major childhood diseases. Science and technology activities will focus on service delivery systems and schistosomiasis research and vaccine development. We will help introduce a health care cost-recovery system so that the GOE can use its limited resources on primary and preventive health care. USAID will also expand support for PVO activities.

PART I - BACKGROUND

I. THE EVOLUTION OF USAID'S PROGRAM IN EGYPT

Egypt shares with the United States a strategic interest in the stability of the region and a commitment to peace. An important aspect of this shared interest is the economic assistance program. It began in 1976, and was designed to support Egypt economically and politically through programs which would

- get a stalled economy growing;
- improve the human environment which had deteriorated during the war years;
- demonstrate to the Egyptian people that there was a real benefit associated with the political course of action their leaders had taken; and
- compensate Egypt for lost Arab assistance because of their rapprochement with Israel.

The intent was to maintain a stable political environment so that Egypt could continue to play a constructive role in the region.

USAID's program initially concentrated on rehabilitating a war-damaged, deteriorating infrastructure. But as the 1970s came to a close, both USAID and the GOE began to focus on the need for improved productivity as a means of addressing the foreign exchange problem.

In January 1979 USAID prepared its first full-fledged CDSS for the 1980s. The strategy was to expand private sector development, increase agricultural productivity and improve the quality of life through a basic human needs program. The strategy viewed industry and agriculture as the driving forces for increasing productive output.

However, Egypt's brief boom period began tapering off in 1982. USAID realized that Egypt could no longer sustain growth, continue to provide widely distributed real income gains, and create employment on the basis of its existing policies. The import requirements for sustaining growth surpassed the foreign exchange revenues available.

From that point, policy reform moved to center stage of USAID's thinking as the key to productivity increases. The GOE, however, did not share this concern. With Congressionally-mandated assistance levels and with little support from other donors for policy discussions, USAID had limited leverage to press for reforms.

In the absence of policy reforms USAID opted for a multi-sectoral, multi-project approach, because economic distortions resulting from bad policies made it unwise to focus larger amounts of money into a few key sectors. Under this approach, USAID maintained a large number of projects in different sectors. Funds were shifted from one to another in response to sectoral policy improvements.

There were drawbacks to this approach:

- Investments in agriculture supported the GOE's thinking that technical solutions alone could increase agricultural productivity, thus delaying movement on the policy front and prolonging a stagnant agriculture sector.

- Investments in electricity allowed the growth of inefficient industries and a rise in expectations by consumers which the GOE will be unable to meet when prices rise to their economic levels.

- Water/wastewater investments may have created an infrastructure whose upkeep the GOE cannot afford.

- There was disproportionate concentration of USAID resources in urban areas, particularly in Greater Cairo, and relative neglect of the needs of rural areas.

Since 1984 Egypt's economic environment has changed dramatically. The GOE now spends more than it earns and external debt is becoming an unsustainable burden.

Because of these financial pressures, the GOE has become serious about economic reform as the means to increased economic productivity. The time is right for a change in AID strategy to support the Government's reform efforts and invigorate the economy by opening it to operation of market forces.

II. THE MACROECONOMIC ENVIRONMENT

From 1965 to 1974, Egypt had suffered severe balance of payments pressures, stagnating exports, rising domestic demand and a heavy burden of defense expenditures. But in the mid-'70's, the nation entered a phase of recovery spurred by petroleum exports, increased worker remittances, Suez Canal earnings, tourism and ample access to loans and grants. Foreign exchange receipts surged from $1.7 billion in 1975 to $9.2 billion in 1980.

These increased revenues had several important impacts on Egyptian spending:

- A sharp rise in public investment. Gross fixed investment jumped from 13 percent of GDP in 1973 to 29 percent in 1982/83.

- Large increases in imports, debt obligations and military expenditures.

- Increased subsidies and imposition of more price controls on key commodities. Artificially low prices led to economically questionable investments, and spurred consumption to ever increasing levels.

Growth came from increased imports of capital and intermediate goods, made available by the influx in foreign exchange. Efforts to improve the utilization of existing inputs -- that is, to improve productivity -- were not successful. In fact, price controls on basic inputs led to channeling of resources to marginally productive activities. As a result of distorted prices and a heavily controlled economy, market forces were repressed. Though production grew, productivity remained stagnant.

Now, however, the boom is over. The influx in foreign exchange fell with the drop in petroleum prices. USAID estimates that GDP fell from an 8 percent annual growth rate of 1975-1979 to no more than 3 percent during the past two years. GDP growth may even have been negative in 1986.

With this overview as context, major facets of the economic environment are described below.

A. Exchange Rates

There are three major exchange rates: a free market rate of approximately LE 2.00 = $ 1.00 and two controlled rates, the Central Bank rate of LE 0.70 = $ 1.00 and the Commercial Bank rate of LE 1.35 = $ 1.00. Most public sector transactions are carried out at the controlled rates. Almost all private sector transactions are passed to the free market.

The multiple exchange rate system is one of the primary instruments the GOE uses to allocate resources. By favoring public sector enterprises with cheap foreign exchange, it has given them an enormous advantage over private producers. Exchange rate distortions have favored non-productive investments and encouraged imports over exports. Highly subsidized exchange rates applied to imported food and raw materials have increased consumption of foreign commodities.

B. Imports and Debt Obligations

Imports, led by food purchases abroad, jumped from $3.6 billion in 1974 to $12.6 billion in 1984/85. During 1986/87, petroleum export revenues have fallen to about $1.0 billion from a high of $3.3 billion in 1981/82. Imports were reduced from $12.6 billion in 1983/84 to $11.4 billion in 1985/86, and will be even lower in 1986/87.

Egypt's debt soared from $2.0 billion at the end of 1972 to $12.6 billion at the end of 1981/82 and passed $38 billion in 1986. Egypt owes about $10 billion to the USG of which $4.55 billion is military debt. Arrears on annual debt payments are growing by about $1.5 billion annually and, excluding military obligations to Russia, totalled about $5.5 billion at the end of 1986.

C. Interest Rate Structure

Interest rates are controlled. The Central Bank lending rate is 13 percent. Interest rates on commercial bank loans range from 2 percent for "food security" loans to 7 percent for agriculture to at least 16 percent for commerce. At the current inflation rate of about 20 percent, interest rates are generally negative.

Banks prefer to extend credit to commercial activities paying the highest legal interest rate, rather than finance agricultural or industrial activities. Thus the activities which low interest rates are intended to favor are jeopardized by the unwillingness of banks to sacrifice more profitable lending opportunities.

Real interest rates on pound deposits are also negative. As an alternative to pound-denominated savings, depositors may choose foreign currency accounts with variable interest rates. This structure severely penalizes a saver for holding funds in pounds rather than in foreign currency.

Interest rate policies also stifle the development of capital markets. Though the interest paid on bonds is tax exempt, potential corporate bond issuers find the interest rate ceiling of 7 percent too low to attract buyers. Consequently, there is virtually no market for corporate debt in Egypt.

In the absence of a functioning capital market, the GOE covers a large part of its budgetary deficits through Central Bank "advances"

at a nominal 6 percent interest rate. The GOE views this as a low-cost form of deficit financing, which it would lose if interest rates were decontrolled. It is highly discriminatory against the private sector.

D. Subsidies

Subsidies are a long-standing GOE practice for keeping the cost of living low. For example, the subsidy to cover bread production losses alone amounts to about LE 800 million per year. The GOE also provides subsidies of about LE 900 million annually on sales of maize, edible oils, sugar, frozen chickens and other food items.

Consumer subsidies are by no means limited to food. The prices of transport facilities, water, electricity and other utilities, fertilizer and many industrial commodities are also fixed below economic costs.

The effect of subsidized consumer prices is rapidly increasing consumption. This, combined with stagnant growth in production and population increases, has led to growing balance of trade and budget deficits.

Subsidies described above are explicit, accounted for by line items in the GOE budget. In 1984/85 these amounted to LE 2.8 billion (about 39 percent of the total budget deficit of LE 7.2 billion). But implicit subsidies are far greater. The largest implicit subsidy is for the energy sector, estimated at LE 4.7 billion annually.

The distortions introduced by these subsidies are seen most clearly in public sector industry. A World Bank study shows that 20 of 25 public enterprises in metals, chemicals, paper and transport equipment had primary and intermediate input costs in excess of the value of their output at economic prices. A glaring example is the

Nag Hamadi aluminum plant, which now consumes 12 percent of all the electricity generated in Egypt. The economic cost of the electricity alone per ton of aluminum produced is now about $1,250, while the world price of aluminum is only about $1,160 per ton. It would cost less for Egypt to close the plant and pay the workforce not to perform any services.

E. Public Sector Domination of Industry

During the '60's, the GOE established almost total public-sector dominance of the economy. Sadat's "Open Door" policy and Law 43 sought to attract foreign investment into joint ventures to augment the GOE's stretched resources, but not to substitute for public industrial investment. Since the GOE continued to operate and expand its industrial holdings, Law 43 was attractive mainly to potential exporters and firms interested in areas not already dominated by the public sector.

The net contribution of public sector industries to domestic value-added is low, even negative in many cases, due to uneconomic investments, price distortions, and gross inefficiencies in operation. Their efficiency is likely to decline further as budget stringencies force the GOE to tighten its belt, making fewer resources available for maintenance and replacement of equipment.

F. The Trade Regime

While traditional sources of foreign exchange offer limited potential, the nation can expand its exports of agricultural and manufactured goods. For this to occur, it must allow prices to reflect the scarcity values of goods and services - produced both domestically and abroad - and it must take specific measures to liberalize its trade regime. These include elimination of multiple exchange rates and lowering of protective barriers through tariff reduction and fewer import and export controls.

G. Taxes

Taxes account for about 60 percent of total government revenue but only 35 percent of expenditures. Business profit taxes constitute the largest source of government tax revenue because this category includes taxes on the Suez Canal Co. and the oil companies. Customs duties and the consumption tax are the next in importance. Personal income and property taxes are unimportant revenue earners. The rate schedule is not equitable across industries. Government could raise revenues and stimulate savings by reforming the tax system.

H. The Second Five Year Plan 1987/88 - 1991/92

The Second Five Year Plan, which has just been developed, reflects the GOE's concern for increased productivity. It emphasizes an expanded role for the private sector and the need for continued policy reform. But it projects an unrealistically high annual real growth rate (6.3 percent) in light of the current economic situation and upcoming reform measures. It reserves too great a role for public industry, and plans investments in new lands reclamation and desert community development which are not economically justified.

Investment is projected at LE 45.5 billion, up from LE 39 billion in the 1982-87 plan. Priorities are scientific research and technology development and projects that use existing, underutilized capacity (most of which are in the public sector).

The plan's long-term economic reform objectives relate to agriculture pricing and procurement, energy pricing, reducing population growth rates, and enhancing the role of the private sector. Shorter term targets include reductions in public sector expenditure and employment (from 3.2 million employees to 2 million), and de-regulation of prices of sugar cane, rice and cotton.

III. ECONOMIC REFORMS

Since June 1985, the GOE has been struggling to develop a comprehensive economic reform program. Increasingly it has become clear that the current system is unsupportable. What is not clear is just what will evolve.

A. Elements of the Economic Reform Program

While economic reform is still under negotiation, we expect the following elements will be included.

- Exchange rates will be unified. By late 1988, there should be an almost complete pass-through of the price impacts of the devaluation; any remaining items whose prices do not fully reflect the unification should do so during 1989.

- Interest rates will be at positive real levels by the end of FY 1989.

- Energy rates will be moving toward the economic prices of the respective energy products. A 29 percent nominal price increase in electricity in early 1987 will be followed by annual price increases sufficient to bring the real domestic price up to its long run marginal cost (LRMC). This will bring the price from 2.2 to 10.4 pt/KWH (the LRMC). Proportional price rises are expected on other energy products. By late 1988 substantial progress should be realized in the elimination of pricing practices favoring public sector enterprises.

- Within five years, the agricultural sector should be liberalized with market-determined prices prevailing for both inputs and outputs. By late 1988, there should be no price controls on agricultural products except cotton. Input prices

should approach free market levels and the private sector should be free to operate in any area peripheral to agriculture. Substantial progress should have been made toward the dismantling of cropping controls.

- The growth of private sector industrial investment will also require the dismantling of a cumbersome system of restrictions and legal barriers which impede private sector development.

B. Role of IMF, the World Bank and USAID in the Economic Reform Program

The IMF program places special emphasis on two specific reforms: exchange rate unification and interest rate increments to real positive levels. In addition, the Fund program relies on its standard series of fiscal and monetary restrictions designed to curb internal demand which in turn will decrease the demand for imported items.

The World Bank program has as its centerpiece three sector loans in energy, agricultural and industry. Satisfactory progress in achieving reforms in these sectors will likely renew Bank interest in supporting specific development projects, in addition to its sectoral programs.

USAID supports these reforms. We will press for additional reforms related to removal of restrictions on private industry and encouraging cost-recovery of public services.

C. Scenario of the Egyptian Economy in FY 1989.

The economic reform program started early in 1987 will be more than half way through its second year. By then, the reforms will have had profound impacts on the Egyptian economy.

As Egypt introduces reform, little GDP growth is expected in 1987 and 1988. The most heavily subsidized industries will face serious adjustments. Agricultural production should increase dramatically by the second year of the reform program. However, private industry's response to the reform measures will take longer.

In the initial years, consumption is likely to decline. Public sector consumption, as well as investment, will be curtailed by the monetary restrictions imposed by the IMF stand-by, while private consumption will decline as prices are raised. Since the reform program will raise many administered prices, the economic measures will be clearly inflationary in the short run. Once the economy adjusts to the reforms, however, inflation would be expected to subside.

The decline in private consumption will be accompanied by higher unemployment. The public sector will have to restrict its wage and salary expenditures in reaction to a contractionary monetary and fiscal policy. Inefficient enterprises will be forced to reduce employment as their production is curtailed.

Declining living standards will be partially offset by compensatory measures to provide for the continuation of subsidies on items which are most essential to low income earners. As the reforms take effect and private investment increases, employment is expected to increase.

As agriculture is freed up to market forces, we estimate that agricultural employment will expand rapidly by up to 10 percent, primarily due to changes in cropping and increased cotton and rice production, both of which are labor intensive. Wages will increase from LE 4 in 1985 to LE 6 to 8 in 1989. Correcting input and output prices should increase demand for labor even more. Private industry, particularly small scale industry, will offer greater employment opportunities than agriculture over the longer term.

The balance of payments deficit will decline appreciably in both 1987 and 1988, principally due to debt rescheduling. We assume that all principal and interest payments as well as arrears are rescheduled for repayment over ten years with the first four or five years constituting a grace period. Other factors contributing to a reduced deficit are

- unification of the exchange rate (encouraging private sector exports while discouraging some imports formerly enjoying subsidized exchange rates);

- increases in interest rates (encouraging capital inflows while retarding outflows), and

- lower internal demand resulting from the monetary restrictions imposed by the IMF stand-by agreement and higher energy prices.

External debt obligations will increase dramatically, but their impact will be hidden. The rescheduling of interest payments along with large sector loans from the World Bank will constitute the principal additions to Egypt's external debt, but the burden of these obligations will not be felt before the 1990's.

This assessment suggests that the Egyptian economy will be in a delicate position in late 1988. The nation will have received short-term relief to its overwhelming debt burden and will improved its balance of payments situation. However, it will have endured almost two years of slow growth, increasing unemployment and declines in per capita consumption. The GOE will be under considerable pressure to pursue a more expansionary fiscal policy, providing relief both to consumers and to public sector enterprises.

Egypt's debt burden will rise at least 15 percent in 1987 and 1988. In the 1990's, the end of rescheduling will increase debt servicing enormously. Failure to provide the conditions needed for rapid private sector growth would portend further readjustment efforts.

D. The Poor in Egypt and How Reforms Will Affect Them

We define the poor as those who spend the majority of their income on food and other necessities, lack access to basic services such as potable water, sewage facilities, health and school facilities, are illiterate and generally work as unskilled laborers. The data for both urban and rural areas indicate that 15 to 20 percent of the households (between seven and ten million persons) exist below minimal acceptable standards of living. Expenditure levels for these households are below LE 1150 annually or LE 230 per capita. An additional two fifths of the population exist very close to the minimal acceptable levels of living with annual expenditures of less than LE 2000 per household, less than LE 400 per capita (1986 prices).

In urban areas 65 to 70 percent of the poor's expenditures are on basic survival items -- food, housing, utilities, and clothing -- with food taking between 55 to 60 percent of their total expenditures. Generally the smaller the total expenditure of the household, the greater the proportion spent on food. Similarly, rural households below the poverty line spend 64 to 70 percent of their expenditures on food. Utilities absorb only five percent of household expenditures.

In the long run, the reform program will benefit the poor by stimulating a significant increase in employment opportunities. During the transition, however, declines in employment and increased prices will probably affect the poor adversely. For a substantial part of the urban labor force, particularly unskilled laborers, an economic downturn will mean greater underemployment. The female unemployment rate, already high, will increase disproportionately, as more women are forced to enter the labor force to supplement family income.

The GOE, IMF and donors are in agreement that any structural adjustment program must provide a "safety net" for low-income households. Because of price increases in basic commodities, inflation, and reduced employment opportunities, poor households whose expenditures consist primarily of subsidized items need support to maintain even minimum standards of living. This is the responsibility of the GOE, and the GOE takes it very seriously. It is unlikely that the GOE would implement reforms which would seriously harm this group.

PART TWO: THE STRATEGY

USAID's proposed strategy is to increase the productivity of the economy by helping the GOE in its efforts to make structural adjustments and remove the restrictions to operation of market forces.

We will support:

- o the policy dialogue process, by participating in the newly-emerging GOE-donor consultative process, and by providing technical assistance to the GOE for policy analysis, if needed.

- o the adjustment process, by providing limited cash and commodity assistance as a package, with the Bank and the Fund, as warranted by the pace of reform and other resource availabilities.

- o Increased productivity in key sectors:
  - agriculture and private industry;
  - services and infrastructure needed to support productivity improvement;
  - local development; and
  - education and training.

- o health, family planning and private voluntary agency activities to help provide a safety net of basic services to the poor and to limit the erosion of productivity gains which can result from population growth.

IV. MARKET FORCES

The key assumption running through USAID's strategy is that encouraging market forces is the best way to achieve productivity increases. The sections that follow, describing the strategy elements, make frequent references to market development, private sector, cost-recovery, and privatization.

A. Market Forces: A Definition

Market forces are the array of economic and financial stimuli provided to producers and consumers in a society in which (1) individuals are relatively free to adjust their level of production and consumption and (2) prices reflect the relative availability of goods and services in the economy. If market forces are absent or highly distorted, individual behavior may not lead to the most efficient use of resources. This is certainly true in Egypt. The proper role of government is oversight and regulation of private production and consumption activity in a way that reduces market distrotions and fasters competition. It is not direct management of production and consumption.

B. Status of Market Forces in Egypt Today

Producer behavior and market entry: Mobility into and out of profitable productive activity is seriously constrained, primarily due to government restrictions and controls. This applies to agriculture as well as public and private industry.

Consumer Behavior: The cost of current consumption compared to future consumption is heavily discounted by the low official interest rates on savings. A significant number of those who save for future consumption move their funds out of the pound economy and into foreign exchange, where interest rates are higher. The existence of producer monopolies and oligopolies restricts consumer

choices. Current consumption is also encouraged by artificially low prices on a wide range of commodities and services, including basic government services such as utilities and irrigation.

Market Information: The knowledge required to take maximum advantage of market forces is limited to an exceedingly small elite.

Raw Materials and Resources: Though Egypt is well endowed with natural resources, the allocation of critical inputs is largely determined administratively with little relationship between the input's price and its scarcity value.

C. Elements of a strategy to encourage market forces

USAID considers these elements to be critical in encouraging market forces, and they are reflected in the sectoral strategies which follow:

- Exchange rate unification to allow firms to compete on equal terms and to encourage exports.

- Interest rates at market determined levels both for lending and for savings.

- Improvements in institutions to support private investment, including capital and equity markets and financial institutions.

- Increased cost-recovery of government services.

- Freer competition between public and private sector firms and divestiture.

- Elimination of price controls which dampen incentives for increased agricultural and industrial production.

V. SUPPORT FOR THE POLICY DIALOGUE PROCESS

The USAID-GOE policy dialogue process consists of formal meetings between US Mission representatives, the Economic Cabinet and the Prime Minister, and informal working groups with many of the Ministries. We expect this format to change, however, with the emergence of a donor consultative group, led by the IBRD and the IMF. We will be an active participant in the group and, because we have a large resident staff, will continue to provide strong analytical support to the process. We will continue to meet individually with GOE representatives to discuss policy issues. But these issues and our response to them will be coordinated through the consultative process. We expect this to lead to a stronger, more effective dialogue.

The GOE may well need outside expertise for policy analysis and advice. We will respond to GOE requests of this nature, as we are now doing through a series of policy dialogue consultants. However, we anticipate that the World Bank and other donors will share responsibility for provision of required technical support.

VI TEMPORARY SUPPORT FOR THE ADJUSTMENT PROGRAM

Structural adjustment takes a long time, even with vigorous policy actions by the government. A reform program which would lead to self-sustaining growth would take at least three to five years, and the proposal offered by the GOE, based on "gradualism", will take longer. In the meantime, the GOE will be forced to curtail imports and expenditures substantially, unless it receives external help.

USAID will be responsive to GOE policy reform efforts and is willing to increase the cash and commodity portion of the program to meet the periodic financing needs of the GOE during implementation of the adjustment program. The level of non-project assistance which we might provide annually would be determined in conjunction with the other major donors, as part of the consultative process.

USAID will supplement its non-project assistance in support of implementing macroeconomic reforms with projectized cash to support key sectoral reforms. For example, we would offer dollar disbursements to support energy price increases, privatization or removal of agricultural crop controls, as we are currently doing through the Agricultural Production Credit Project. This could provide substantial additional dollar resources to the GOE, if it moves swiftly on implementing sectoral reforms.

VII. SUPPORT FOR INCREASED PRODUCTIVITY IN KEY SECTORS.

The major portion of the program will be in projects during the planning period. Under an improved policy environment, in the key sectors affecting productivity the need for projects to promote growth will increase and the effectiveness of AID inputs will be enhanced.

We will increasingly focus assistance on the two sectors with the greatest potential for productivity increases: agriculture and private industry. Assistance levels will hinge on policy progress in freeing up these sectors to operation of the market.

A. Agriculture

1. The Potential

Compared with other countries, Egypt's present yields per hectare are high. Egypt achieves rice yields greater than both Japan and the U.S. Wheat yields are 32 percent higher than those of the U.S. With increased application of technology and appropriate policies, productivity could increase an additional 25 to 100 percent, depending upon crop and location. If agricultural production were to reach its potential, Egypt's reduced imports of wheat, corn, flour and oil, combined with expanded exports of cotton and rice, would save $2 billion annually on its food bill.

Long staple cotton, Egypt's specialty, is much demanded in international markets. Output could increase by up to ten percent under less restrictive government policies. By eliminating disincentives, rice output could also increase by as much as 60 percent. Fruits and vegetables require a more fully developed marketing system, but exports of these crops have significant potential, especially in non-EC and Middle East countries.

2. Constraints

a. Policy: Crop quotas, artificially depressed farm prices, subsidized inputs, and other market controls all combine to distort the allocation of resources and remove farmers' incentives to produce more. Availability of agricultural products under PL-480 Title I has enabled the GOE to maintain policies that discourage production.

- The GOE requires farmers to allocate fixed acreage to certain key crops over each three year cycle.

- The GOE procures 100 percent of the cotton and sugar cane and about 50 percent of the rice crop at below market prices.

- The GOE has a monopoly on most inputs, including production or import and distribution.

- Restrictions on marketing limit farmers' ability to obtain market prices for their crops.

- Import restrictions like those restrictions on meat and dairy imports give rise to internal prices two times world market levels, leading to inappropriate investments.

b. Technical and physical constraints: Even if policies provide proper incentives to farmers, their ability to increase production will still be limited by lack of the technologies and inputs needed for high yielding crops. The centrally-directed agricultural research and extension system is inadequate to respond to the needs of farmers. Extension has traditionally served as a means of control rather than technology dissemination. USAID's agricultural research investments have helped to create a research infrastructure. However, further work is needed to make it farmer-responsive, to integrate research and extension, and to institutionalize an interdisciplinary approach.

There is also a need for increased agricultural credit to procure the higher-cost inputs needed for use of high-yielding technologies.

The Aswan High Dam has allowed for year-round irrigation of crops, but it has also reduced productivity reductions, because of inadequate water management and control. The irrigation system (including drainage) must be brought to modern structural and management standards if it is to support more intensive agriculture. Physical capacity and control structures are inadequate to deliver water in the quantities and at the time needed for higher-yielding technologies.

Lack of adequate water management is leading to higher water tables, salinization and water logging in many areas. Improved system management will require different planning and design procedures, different control structures and machinery, technical staff improvement, education of water users, increased water user involvement and application of new techniques.

3. Strategy

We will increase investments substantially in agriculture, irrigation, and other rural infrastructure in response to implementation of policy reforms. We will also increase dollar disbursements, through projects, to support significant reforms. The first policy-centered agriculture project, the Agricultural Production Credit Project, has instituted a performance-based disbursement system for the credit component, contingent on the implementation of reform measures to free up agriculture. Prior to the beginning of the planning period, amendments will be completed for both the National Agriculture Research Project (NARP) and the Irrigation Management Systems Project (IMS). These projects will also offer substantial additional funding in support of policy progress. USAID and the GOE will establish policy benchmarks and review progress annually, similarly to the process now used in the water-wastewater portfolio.

The main elements of our strategy to increase productivity of agriculture follow:

- Project activities and PL 480 Title I will provide the vehicle for sectoral policy dialogue, in conjunction with the World Bank and other donors. Annual obligation levels to the sector will be determined based on policy progress.

- We will increase investments in irrigation, which must be strengthened to meet the needs of high yielding technologies.

- We will support further improvements in the agricultural research system. We will also consider supporting improved extension, through private as well as public channels, to facilitate its shift from a control to an information function.

- We will consider further support for agricultural credit. This would include expansion of the small-farmer credit window to 350 agricultural branch bank outlets, to ensure access of credit to those who cannot afford collateral.

- We will encourage development of private sector, agro-industry, and post harvest activities. We will also consider assisting the Ministry of Agriculture and other public agencies in divesting themselves of public agro-industries.

- We will continue to focus our project activities on old lands and will discourage the GOE from further investments to reclaim new desert land for agriculture.

The recurrent cost burden of USAID's past investments in agricultural research and irrigation management is substantial. USAID will carefully analyze the recurrent cost implications of new activities in the sector to ensure that adequate GOE budgetary

resources are made available for high priority investments. We will place heavy emphasis on introducing cost recovery components into programs wherever possible, as in the Irrigation Management Systems project.

B. Private Industry Development

1. The Potential

To quote AID's Private Enterprise Development policy: "The most efficient allocation of scarce resources occurs when individuals seek to increase their incomes in an environment characterized by open competition in the supply and exchange of goods and services .... It is clear that LDCs which have overextended the role of the public sector and restricted operation of the private sector have experienced slow growth, heavy budget deficits and rising debt burdens".

The real growth of private industry in Egypt has been between 3 and 8 percent a year since 1981. This compares with growth of at least 10 percent in countries which have opened their economies to private investment. Foreign industrial investment has also been limited.

2. Constraints

Nearly all of the constraints noted here stem from policies that discourage operation of market forces.

a. Investment Climate: This is the most critical constraint for both domestic and foreign investment. The management of the macroeconomy, bureaucratic processes and geopolitical Middle East tensions are important negative influences. Furthermore, lingering distrust of the private sector perpetuates government policies

restricting private industry, both domestic and foreign. For its part, the private sector is wary of government pronouncements and promises because of frequent and unpredictable regulatory changes.

The absence of a stable, predictable investment environment is aggravated by growing uncertainty about the economy. All of these factors lead investors and bankers to look for short-run ventures rather than more productive medium to long-term investment. These short-run strategies in turn encourage government intervention and regulation.

b. Competition from Public Sector: State-owned enterprises dominate all commodity production activities except agriculture. Private firms cannot compete because public sector industry enjoys direct and indirect subsidies on such critical inputs as energy and foreign exchange. The pervasiveness of public sector industry severely limits opportunities for private industrial investment.

c. Deficiencies in Financial Markets

Credit and banking: The distortions which the interest rate structure introduces into the credit and banking system have already been discussed. Another issue is that banking facilities for small and medium scale enterprises are concentrated in large urban areas. Small scale entrepreneurs outside of the major cities have limited access to the formal banking system.

Money and Capital Markets: The interest rate structure makes investments in bonds non-competitive with 5-year savings deposits. Consequently, there has been no real development of a capital market in corporate bonds or other corporate debt instruments. Public offerings of equity shares are also constrained. Traditional, family held companies do not like to share ownership with the

general public and the public is suspicious of the published financial statements of most Egyptian companies. Dividends are also taxable while interest on savings held in banks is not. These social and institutional constraints prevent growing companies from issuing shares to raise capital by broadening ownership. Nor are there viable venture capital institutions able and willing to strengthen the equity of industries in return for a share of equity. The stock exchanges in Cairo and Alexandria have only about 20 and 6 members, respectively.

d. Deficiencies in Technical and Managerial Skills: The educational system produces thousands of graduates, but most lack a basic business and accounting foundation, even for junior level managerial positions. Technical graduates have theoretical knowledge but little or no practical or lab experience. Therefore, new private ventures have the choice of drawing technical and managerial personnel from the public sector or investing heavily in training.

3. Strategy

Interest rate and foreign exchange rate reforms are essential for an energetic private industrial sector. But other measures are also needed to remove the constraints noted above:

- privatization of many public sector industrial companies;
- development of a money and capital market;
- removal of protective customs barriers;
- reduction in government interventions;
- export promotion;
- assistance to small scale enterprises.

Once exchange rates are unified and interest rates adjusted to provide appropriate incentives to lenders and borrowers, there will be no further justification for USAID's private sector CIP and term

credit programs. Similarly, once the private sector is free from the competition, intervention and controls of the public sector, USAID's programs of promotion and matchmaking will become less critical. Egyptian and foreign firms can then be counted upon to identify and pursue promising opportunities.

However, all the reforms may not be achieved during the planning period. During the transition, assistance will be needed to stimulate private industrial growth, but the priority and the mix of the elements will change. The elements of our industrial strategy follow:

a. Improved Investment Climate

Policy dialogue: USAID will seek the transfer of some public sector activities to the private sector, reduced restrictions on market entry, and relaxed controls over private sector activities.

Business laws: USAID will help the GOE to streamline the myriad laws and bureaucratic processes related to business licensing and operation. We will support efforts which place the private sector and the public sector on an equal competitive footing.

Divestiture: USAID will support the divestiture of governorate owned industries. We may consider establishing a fund capitalized from LE counterpart to help in the financial restructuring and sale of these public sector industries. If it is successful, we will pursue enlarging the privatization program to the larger, central government owned industries.

Public Industry: USAID will have completed most of its project assistance to public sector industry by the beginning of the planning period and will initiate no further assistance to these industries.

Market Information: USAID will continue assistance to both Egyptian and foreign private entrepreneurs and investors in (1) obtaining the necessary information, economic data and analysis to make intelligent business decisions and (2) locating partners or joint venturers.

b. Improved Business Finance. In this crucial area, the Mission's primary efforts will be to improve the policy environment and operation of the banking sector, the capital market and non-banking financial institutions. The most important endeavor is to move interest rates to a market basis, both on lending and on corporate paper floated in the capital market. In addition, new instruments of finance need to be introduced into the capital market. USAID is willing to provide project and non-project assistance to support these changes.

Capital markets: USAID will carry out activities to encourage capital market development. We are already providing training in finance and the basics of capital markets to selected private entrepreneurs and Capital Market Authority (CMA) staff. We are financing technical assistance to draft necessary regulatory laws, develop uniform accounting standards and implement other changes to develop the capital market. And we are supporting modern data management for the CMA. We will expand assistance as opportunities arise for development of a whole range of standards and institutions that build trust and confidence so that investment will come forth.

Private Enterprise Credit: Until interest rate and exchange rate reforms have been fully implemented, private industry will need both import financing (private sector CIP) and term credit. Private Sector CIP criteria are being sharpened to assure that newcomers and smaller companies have primary access. The program will also focus on the finance of capital equipment. The application and approval procedures for the term credit program have been streamlined. Expansion of investment and bankers training and our credit

guarantee fund for small enterprises will be important in reorienting bankers away from present collateralized lending practices, so that they will respond to the demand and incentives created by these reforms.

Small and medium scale enterprise credit: We propose an equity and venture capital program as a companion to the privatization effort and to provide support for small-medium scale enterprise development. The program will work through banks, selected investment companies/financing institutions and non-formal financial organizations. We will support the establishment of a viable stock market to trade and allow for sale and rollover of investments. We will seek opportunities to provide project support to improve and expand systems of institutional finance and to provide greater incentives for small scale enterprises outside the major urban areas.

c. Improved Business Services and Support Institutions

Management practices: Improved management of production, marketing, accounting and finance is basic to increased productivity in industry. We will expand technical assistance and training programs with existing training institutions and coordinated through private sector organizations. We will consider management and technical skills training to improve practices for selected industries, on a cost-share basis through trade syndicates in cooperation with universities and technical schools.

Export promotion, tourism and marketing: In export industry modernization, we will explore opportunities to improve export market data and analysis and export promotion efforts. We will encourage private sector tourism investment, as this could have immediate impacts on employment and foreign exchange earnings. We will support systematic planning through technical assistance, promotion of joint venture arrangements and modernization of facilities through term credit programs.

VIII. INFRASTRUCTURAL INVESTMENTS

Infrastructure programs, especially telecommunications, water and wastewater, and power generation have constituted a large percentage of USAID's assistance to Egypt. With a shift in our strategy to productivity, we have reexamined Egypt's infrastructure needs as they relate to this theme.

A. Energy

1. Characteristics of Egypt's Energy Sector.

Energy is a key factor affecting Egypt's productivity. A reliable power source is clearly a critical need for the growth of modern industry and agriculture. Just as important, Egypt's energy pricing policies have burdened the economy with a growing fiscal deficit, led to uneconomic industrial investments, and caused overconsumption and waste of this essential input to development.

Egypt's energy resources are substantial. Proven recoverable oil reserves are 550 million tons of oil equivalent and Egypt is a net oil exporter (historically about one-half of production). Proven natural gas reserves are between 5.5 and 8.0 trillion cubic feet. Hydropower potential may reach 3700 MW, if certain investments are included which are not currently economically viable.

The GOE controls 100 percent of the gas and oil reserves and over 95 percent of electric power generation, transmission and distribution. Government-owned industrial plants account for 80 percent of industrial energy use. To subsidize residential consumers and state-owned industries, the GOE has kept energy prices unrealistically low. Though electricity is priced to cover the Electricity Authority's costs, between 7 and 70 millemes per kilowatt hour, these prices are below the marginal economic cost estimated at 100 to 150 millemes/KWH. Domestic oil and oil product prices between

LE 7.7 and LE 36.0 per ton are far below world market prices of LE 100 per ton. Natural gas prices are based on oil prices, and thus are similarly underpriced.

Aided by low prices, energy demand has grown rapidly. Electric power generation grew at a 12.4 percent per year clip between 1975 and 1985, while peak demand grew at 11.8 percent. Oil and natural gas use grew at over 10.0 percent per year during the same period. Electric power demand is expected to grow at 10.0 percent per year in absence of significant price changes; oil and natural gas, at 6.0 percent.

2. Constraints to meeting the energy demands of increased production

Our analyses indicate that were energy prices raised to their economic value, demand would fall substantially. A future demand analysis by the Organization for Energy Planning should give us a more accurate picture. Nonetheless, there are problems with the current system which will prevent it from providing the reliable source of power needed for expanded productive activity. To meet burgeoning demand for energy, the GOE has placed emphasis on new generation rather than conservation, rehabilitation, and operation and maintenance. Willingness of donors to provide financing for new generation hasn't helped.

As a result, generation, transmission, and end use efficiencies are poor. Electric power losses are over 20 percent, compared to 10 percent or less for efficient systems. Ten to 30 percent of industrial oil, gas, and electricity use can be saved with little

capital investment through improved operating and maintenance procedures. Potential shortages in the next few years, primarily in electric power, will result in

- o poor system reliability,
- o inability to meet peak demands,
- o scheduled and unscheduled brownouts and blackouts,
- o reduced productivity in both the manufacturing and service sectors, and
- o unproductive investment in standby onsite diesel generation.

3. Strategy

Rational energy pricing is the first step in stimulating energy conservation and resolving many of these problems. USAID will emphasize price increases in concert with other donors. USAID will focus on a "least cost" energy strategy emphasizing rehabilitation, conservation, training and planning. This approach will increase energy productivity by directly improving on two of its major inputs: physical plant and manpower. In addition, we will assist in developing an energy demand/supply forecasting capability that should contribute to a rationalized energy policy.

Given the critical importance of pricing to remove distortions, USAID will not provide any further funding for physical improvements in the sector (rehabilitation or new generation) in the absence of significant price increases. Since we anticipate that the price increases already agreed to by the GOE will occur, we are willing to finance planning and feasibility work needed for such investments now.

Activities will focus on these areas:

- o Rehabilitating existing power generation infrastructure. USAID will fund analyses to identify targets for improvement, detailed engineering designs, and, subject to price increases,

actual rehabilitation. Reducing the cost of power supply will reduce the degree of price increases required to improve the financial status of the power sector in Egypt.

- Encouraging energy conservation technologies. USAID will fund on-site technology demonstrations, training, workshops, and seminars to improve the energy efficiency of private sector firms, develop institutional capabilities for delivering energy efficient systems, and help identify policies hindering cost-effective energy conservation.

- Developing and improving energy manpower. USAID will fund training to improve technical and management skills in energy supply, production technologies and energy planning, as well as industrial internships and technical and management assistance.

- Developing energy planning. USAID will emphasize developing a rational energy strategy through improved demand/supply forecasting, policy and pricing analysis, and energy program recommendations.

- New generation, if analysis indicates this is the "least cost" alternative compared to rehabilitation, and if it is warranted by projected demand after electricity price increases.

- Support for El Dabaa nuclear power plant. Assuming a US firm is awarded the contract for construction of the plant, USAID will support nuclear power O&M training and related non-nuclear site works.

- Alternative energy. USAID does not exclude activities of this nature from the strategy, but we assume that future funding for such projects will be quite small and subject to the same cost/benefit criteria as other programs in the sector.

B. Water and Wastewater.

1. Status and importance of the sector

USAID has committed $ 1.145 billion to major water/wastewater construction programs and Cairo, Alexandria, three provincial cities and three canal cities to date. Further obligations are planned for Cairo and the canal cities, to complete our investments in these areas. USAID's previous goal of rehabilitating and expanding the urban water/wastewater sector have now been largely met. On productivity grounds, there is little justification for further investment in this sector beyond what is now planned.

Since 1984, USAID and the GOE have annually set benchmarks aimed at addressing key institutional issues, such as operations and maintenance, and at achieving recovery of all O&M costs by 1990. To reach these goals, USAID has provided for O&M training for all sectoral construction contracts, and has provided the Institutional Support project. Each year's funding level for water/wastewater is determined based upon progress on annual benchmarks. As of this date, however, the sector is still several years away from proposed institutional and cost-recovery goals.

2. Constraints

Though major urban systems are now in place, existing systems are poorly maintained. The government institutions charged with operating the systems do not have the capacity to plan, construct, operate and maintain them. Since water and sewerage services are at very low cost to the consumer, water tends to be wasted, and the GOE does not capture sufficient revenues to operate and maintain the systems.

3. Strategy

USAID will reduce assistance in this sector, particularly for major capital activities in urban areas. With one possible exception, we will not fund new urban capital investments during the planning period.

However, to protect past investments and ensure that the improvements in urban areas are maintained, we will continue to provide assistance for institutional support in operation, maintenance, financial and technical training for water/wastewater utilities and agencies. We will continue our dialogue with the GOE to increase water/wastewater tariffs sufficient for utilities to meet their recurrent costs.

To redress the imbalance in our wastewater assistance favoring urban areas, and to meet the needs of lower and lower-middle groups currently not served, we will continue investments in local water and wastewater systems through the Local Development program. This program builds in cost recovery by offering loans rather than grants to local governments for infrastructure programs, which promotes institution of user fees.

Finally, we will consider funding the Cairo Water II Project to enhance our previous $100 million investment in the Rod El Farag Water Treatment plant. This project would expand and improve the Cairo water distribution system, which is currently inadequate to utilize new plant's treatment capacity. This project is of relatively low priority, and will only be financed if adequate funding is available for higher priority activities.

C. Other Infrastructure

USAID's past investments in improving telephone service have removed an important obstacle to modern industrial development. But Egypt has now reached the stage where it should move into commercial financing. Concessional assistance is no longer appropriate.

Roads have been a high priority to the GOE. Major road construction is generally good and maintenance is adequate. USAID has supported GOE efforts to improve roads and transportation through CIP funding and through T.A. activities under the Mission's PD & S project. In addition, we have provided $80 million for feeder road construction through Local Development. Our existing programs (CIP, PD & S and Local Development) are adequate to meet the needs of the sector. We will fund no roads projects during the planning period.

USAID's projects in support of Egypt's grain, tallow, fat and oil distribution system have dramatically reduced demurrage costs, waste, and loss and have facilitated transportation to inland destinations. The GOE is well underway toward completing the implementation of its grain storage requirements. USAID will provide no further capital assistance for public sector investment in this sector. However, we are prepared to finance some O&M assistance, as requested. We will promote and assist with privatization opportunities as they develop.

IX. INVESTMENTS TO SUPPORT PRODUCTIVITY

A. Local Development

1. The Importance of Local Development

The need for community infrastructure will continue to grow, both to provide basic services for low income groups, and to support the expansion of agriculture and small enterprise. But the way government chooses to provide community infrastructure and services affects their efficiency, quality, cost and long-term sustainability.

GOE development programs have traditionally been carried out through a strategy which inserts the central government in all levels of economic activity. The result is a huge public sector, relative neglect of local needs, unproductive investments, and lack of concern for cost recovery.

Recognizing these problems, the GOE increasingly looks to local government for provision of basic services and local economic development. The GOE has based local government legislation on the twin principles of decentralized authority and democratic decision-making. USAID has supported the local development program since 1978.

Local governments can also be an effective proving ground for policy changes which the central government is initially hesitant to try. Local governments have expressed interest, for example, in privatization, new cost-recovery mechanisms for local services, and small-scale credit programs.

2. Constraints

Several important factors limit the effectiveness of the local government/decentralization program.

- There is not a clear delineation of responsibilities between central and local units of government. As a result, local elected and executive councils have not assumed full responsibility for planning and project implementation as provided for in the local government laws.

- Governorates lack control over fiscal management and taxation within their jurisdictions. Central government still provides two thirds of each governorate's budget. There has been little success in mobilizing private resources for local development activities.

- Services are provided at little or no cost to the users. Little emphasis has been placed on proper operation and maintenance or on cost recovery.

- Local government units lack adequate technical and managerial staff.

3. Strategy

USAID will continue to support this program. Emphasis will increase on developing local government capacity to operate and maintain basic services and facilities and to develop mechanisms for cost recovery.

The program will include these elements:

- A revenue sharing system, as practiced in the United States, which will expand central government transfers of discretionary resources to finance locally chosen development activities.

- Technical assistance on local development issues, such as delineation of local government responsibilities, local resource mobilization, and cost recovery.

- Implementation of management and finance systems for maintenance of water/wastgewater facilities and local roads.

- Capital and/or technical assistance to develop credit services for small enterprise.

- Technical assistance and training to strengthen the planning and analytical capabilities of local government staff, particularly in economic analysis.

- Pilot activities to explore new technologies to improve the quality and reduce the cost of basic services delivery systems.

- An upgrading and home improvement loan program for low income communities in major urban areas to stimulate private sector activity in housing and to help ensure adequate shelter, a basic element in a safety-net for the poor. It will support improvements in informal settlements; that is, fringe areas of major cities which do not yet have basic urban infrastructure and services. It will not fund sites and services.

B. Education and Training

1. The Role of Education and Training in Increasing Productivity

A literate population is essential for a modern productive economy. Though school enrollment is increasing in Egypt, in 1980 about 25 percent of school-aged children remained unenrolled in primary school, and adult literacy was 44 percent. This is a very low literacy base upon which to build a trained labor force.

An adequate supply of trained technicians is essential for growth of modern industry, but the skills needed are of a higher level than those prevalent today. More technical programs will be needed, such as computer sciences, electronics, and technical agriculture.

Management training is needed to compensate for deficiencies in the formal education system. Throughout the sectors in which USAID works, management has been identified as a need, and many of our projects include management training components to meet specialized requirements.

2. Constraints

Access to education and training is not equally available to all Egyptians. Major disparities are found between males and females, urban and rural, Upper and Lower Egyptians.

The quality of education offered at all levels is generally low because of inadequate funding. This leads to a shortage of good teachers and books or printed material of any kind. Many schools are in a state of disrepair. Instructional methods and curriculum content, particularly at vocational and technical schools, are inappropriate.

There are also important policy constraints limiting the productivity of the education and training system. Information that contributes to sound educational policies or financial management is not available.

3. Strategy

USAID will improve access to education by:

- Continuing to construct schools in underserved rural and urban areas.

- Developing local means of support for basic education. The system is too large, complicated and costly to rely upon centrally provided funds for total support, particularly in light of increasing central government budget stringencies.

USAID will improve the quality of education by:

- Improving instructional materials available for basic education.

- Supporting in-service teacher training programs.

- Improving the teaching of science, computer skills and other basic technical subjects at secondary and junior college level.

USAID will support specialized training courses to upgrade the quality of the work force. This includes:

- Continued support for the Peace Fellowship program and other non-project participant training.

- Specialized training courses, through projects, to meet the manpower needs in key sectors.

- Development of an in-country management training capability with particular emphasis on productivity for both public and private sectors.

USAID will support for development of a planning capability within the Ministry of Education that can collect and process reliable information on enrollments, dropouts, expenditures and the general efficiency of the system. Only with such information can one enter into a meaningful policy dialogue concerning allocation of resources in the Education Sector.

X. HEALTH, POPULATION AND PVO ACTIVITIES

Health, nutrition and other social services are a basic ingredient of any safety net concept. The GOE's health program and the social service activities of private voluntary organization (PVOs) are aimed at reaching the poor, in both rural and urban areas. These groups will need direct protection as structural reforms are implemented.

Family planning programs limit the erosion of productivity gains which can result from rapid population growth.

The activities of 14,000 Egyptian private voluntary agencies (PVOs) contribute enormously to the mobilization of local resources for development. A widespread sense of social responsibility, public interest, motivation, and enthusiasm at the local level are essential ingredients of a successful national development program. Both indigenous and US PVOs have proven very successful in Egypt in developing these traits in the communities where they work.

A. Health and Nutrition

1. The problem

Poor health standards are a serious problem in Egypt. Debilitating parasitic (schistosomiasis), bacterial (typhoid, trachoma, TB), and viral diseases (hepatitis) are endemic among the adult population. Waterborne gastro-intestinal diseases strike all age groups. In 1980, prior to the current national oral rehydration program, the infant mortality rate was 101 per thousand. Fifty percent of all deaths were in children under age 5, and half of those were due to diarrhea. Respiratory infections are the second greatest cause of death in children. Though the overall nutritional status of the population is good, poor weaning practices increase vulnerability of infants to other disease problems.

Some three thousand clinics, 490 community hospitals, and 49 modern urban hospitals give almost all Egyptians access to some sort of health care. The ratio of doctors to population is among the best in the developing world. However, the quality of care is poor, especially in the primary care clinics. Health personnel are poorly paid, trained and motivated. The medical education system produces physicians who lack adequate knowledge of public health and preventive medicine, so the system is geared for curative care rather than preventive care.

The GOE is addressing this problem by supporting preventive health activities, particularly child survival programs such as oral rehydration therapy (ORT), immunizations, acute respiratory diseases, nutrition education and child spacing. The GOE plans to introduce cost recovery into health programs and to shift certain health programs to the private sector.

2. Strategy

USAID will continue our current strategy for health and nutrition.

In collaboration with UNICEF and WHO, we will support the GOE's program to implement interventions to combat major childhood diseases including diarrheal disease control and immunizations.

We will help the Ministry of Health to design and implement a project to introduce a rational health care financing system based on cost recovery principles. It will include expanded health insurance programs and support greater private sector participation in delivery of curative care on a fee-for-service basis.

Each health activity has elements of operations research focused on delivery of health services for child survival. The S&T for Development project includes broadly based research on schistosomiasis, and work will begin on developing a vaccine in FY 89.

B. Population

1. The Problem

Despite the high level attention given the population problem very few concrete achievements have come to pass. Over the last two decades millions of dollars have been spent to establish a national population planning and coordinating body; to train thousands of family planning personnel throughout the country and to support interventions designed to increase awareness, knowledge and use of contraception. Yet with a few notable exceptions such as the private sector Family of the Future program these interventions have had little impact. Taken as a whole, they have not resulted in a decline in Egypt's population growth rate. Since 1980, the annual population growth rate has remained stable at between 2.7 and 2.8 percent.

The key issue facing Egyptian population planners, therefore, is: why hasn't the population program succeeded to date and what can be done to make it a success?

Family planning is not the only factor which determines fertility. Factors contributing to high fertility in Egypt include

- early marriage practices;
- high rates of illiteracy (especially among rural women);
- low status of women generally and lack of female employment opportunities and other alternatives to childbearing;
- strong preferences for male offspring; and
- cultural opposition to family planning.

Nonetheless, recent rural studies indicate that the demand for family planning is greater than current contraceptive prevalence figures imply. What is missing is access to reliable, discreet and high quality family planning services.

Egypt's national family planning program has suffered from poor structural support, a poorly developed and managed approach to service delivery, lack of effective coordination among major service providers and poor linkages with community leaders. As a result, with few exceptions, nothing works very well.

2. Strategy

USAID will

- o expand support for successful private sector family planning programs such as the commercial marketing project of the Family of the Future.

- O support the design and implementation of effective family planning service delivery programs through the extensive network of hospitals, clinics and health centers of the Ministry of Health and the Egyptian Family Planning Association.

- o place more emphasis on a broad based analysis of fertility determinants to guide the design of programs.

- o accelerate discussions with key Egyptian policy makers at the National Population Council (NPC), the Ministries of Health and Social Affairs and other agencies to remove structural and operational obstacles to success. These include weak family planning delivery systems and salary disincentives to program performance.

- support redirection of public information efforts to encourage not only knowledge and awareness of population issues, but motivation to increase contraceptive usage.

- assist the NPC to develop the capacity to carry out its responsibility for national population planning, policy making and program coordination.

C. Private Voluntary Organizations

PVOs in Egypt have a long and solid record in local development and are widely disbursed throughout the country. They are venturing into new sectors with the provision of services for fees, including garbage and wastewater collection in unserviced areas, loan programs using near-market interest rates, day-care centers, and basic health services.

USAID supports indigenous PVO programs for a range of activities: day care centers, village public health clinics, literacy classes, vocational training centers for youth and adults and technical assistance to local public officials to improve social services planning, management and implementation. USAID also supports US PVOs (principally CARE and CRS) for activities in agriculture, health and income generation. Evaluations have shown these programs to be quite effective.

USAID will increase its support for PVO activities during the planning period, both through increased allocation of Local Development Project funding to PVOs, and through monetization of PL 480 Title II/Section 416 dairy proceeds to capitalize a PVO development fund.

XI. THE PILLARS

Policy dialogue and private sector development are such recurring themes throughout this document that they need no special attention here. This section reviews institutional development and technology transfer briefly, and also notes the impact of our strategy on women.

A. Institutional Development

USAID's strategy encourages institutional change needed to free up the economy to competitive market forces and improve the environment for productive activity. Most of these efforts are directed at the Government of Egypt. Here, institutional development means changing government involvement in the economy from direct management to oversight and regulation of private production and consumption activity in a way that reduces market distortions and fosters competition. This implies a dramatic change in government attitudes, which will only happen a little at a time, in response to constant hammering away by the donors.

Reluctance of the GOE to accept high levels of U.S. technical assistance and training has delayed institutional development progress in the past, and we anticipate that this will continue to be an issue in the future. In some sectors, the GOE is pleased to obtain US technical support, such as in health and agriculture. In other areas, however, such as water/wastewater and small-scale industry development, the GOE disagrees with USAID as to the need for technical assistance.

Based upon lessons learned from USAID's past experience, these guidelines will apply to our institutional development activities:

a. Institutional change takes time. Institutional development objectives should be realistic within a project time-frame, should be measurable, and should address specific problems. Incremental

benchmarks should be determined upon which progress towards institutional goals can be measured.

b. USAID will avoid overloading projects with T.A. Where possible, Egyptian consultants will be used. U.S. contracts will include joint venture or subcontract arrangements with Egyptian firms to improve local capacity.

c. USAID assistance to infrastructure and basic services will give top priority to strengthening capacity to manage, finance and sustain these institutions.

d. Specific institutional activities which we will assist include:

- policy analysis and formulation,
- local development,
- agricultural research, credit and extension,
- services essential to private enterprise, such as improvements in the financial system and capital markets,
- divestiture, and
- health, nutrition and family planning services.

B. Technology Transfer

New, more productive technologies will be needed for producers to take advantage of the new economic environment. However, the GOE has tended to view technology transfer alone, without policy changes, as the solution to its productivity problems. Technology transfer activities have been centrally-planned, have not related to the needs of the end-user and consequently, have not been widely adopted.

USAID has attempted to transfer technologies to Egyptians in a broad range of program areas, including:

- o construction and operations of urban and rural infrastructure;
- o production processes for public and private sector industries;
- o high-technology investments like telecommunications and energy control;
- o agricultural research;
- o direct scientific technology transfer programs; and
- o more effective human services (e.g., ORT, NORPLANT).

To improve the effectiveness of the Mission's technology transfer activities:

- o USAID will encourage the GOE to make the policy changes needed to promote the use of productive technologies.

- o USAID and Egyptian institutions should focus on technologies that address specific priority problems identified by the end users rather than on centrally-determined priorities.

- 0 Before attempting to transfer a technology, USAID should consider the need to package technical assistance and training with equipment or facilities to ensure adequate operations and maintenance and attention to cost recovery.

Important areas for technology transfer in support of increased productivity will include:

- o development, adaptation, and dissemination of productive agricultural technologies;

- o improvement of the financial system and capital markets to mobilize resources for industrial expansion and make short- and long-term credit widely available to producers at market prices;

- technologies in power plant rehabilitation and industrial energy conservation to reduce fuel wastage and increase reliability of electricity.

- improved delivery of education, preventive health care, and family planning. This includes assistance for a broad program to upgrade science education, so that Egyptians will be equipped to accept technologies as they become available.

C. Women in Development

USAID's new strategy should have a more direct impact on women's participation than did our previous project portfolio. It will expand activities in agriculture and private industry, which will open up employment opportunities for women as well as men. Activities which evaluations have shown to promote women's participation will be expanded. These include agricultural credit, small scale industry credit, local development, and education programs. More importantly, the program will focus on those policy changes needed to lead the economy to productivity and growth. In a declining economy, the impacts of reduced income and employment opportunities hit women first. An expanding economy which creates a demand for labor holds greater promise than any combination of projects for increasing the role of women in development.

XII. RESOURCE REQUIREMENTS

A. Program levels

The same assumptions about economic reform and the importance of productivity which govern the strategy dictate resource allocations for 1989 through 1992. Because the pace of economic reform in Egypt is still in question, some of the allocation decisions may need to be adjusted, particularly in the earlier years of the CDSS.

	CDSS					
	1987	1988	1989	1990	1991	1992
Cash	115	115	115	115	-	-
CIP	200	200	200	150	100	100
Sector Programs - Agriculture - Private Ind. Dev - Infrastructure - Local Dev. - Health/Population - Education - Science and Technology - Misc. Support	500	500	500	550	715	715
Total ESF	815	815	815	815	815	815
PL-480 Title I	169.1	150	125	100	75	50
PL-480 Title II	4.9	2.7	2.7	-	-	-
Monetization of PL 480 Title II or 416	2.5	2.5	2.5	2.5	2.5	2.5
Total Economic Assistance	991.5	970.2	945.2	917.5	892.5	867.5

1. Cash Transfer

	1987	1988	1989	1990	1991	1992
Cash	115	115	115	115	-	-

We assume that there will be an earmark for direct cash transfer, at least through part of the CDSS period. Cash disbursements will increasingly be tied directly to real progress in implementing economic reform. They will be a strong indicator of U.S. support for the government's reform program. If the scenario described in the strategy unfolds, we speculate that there may be little or no need for direct cash transfer by 1991. The cash that is shown in 1987 and 1988 and the first two years of the CDSS period will relate to implementing a comprehensive economic reform support program, part of which may be worked out in conjunction with a Consultative Group arrangement for Egypt. We expect that by 1990 a Consultative Group arrangement would begin to focus on sectoral programs aimed at improving the productivity of the economy.

2. Commodity Import Programs

	1987	1988	1989	1990	1991	1992
CIP:						
Public	100	100	100	100	100	100
Private	100	100	100	50	-	-

We assume that throughout the CDSS period there will be a requirement to maintain some level of commodity imports, both to meet a real demand for import financing in Egypt and to support Congressional initiatives which obligate the Agency to financing certain commodities.

The three questions we have tried to answer in allocating CIP resources are:

- what level of CIP should be in the program;
- what is the appropriate split between public sector and private sector CIP; and
- what uses should the public sector CIP be put to.

We have straightlined the public sector CIP at $100 million a year. We show the private sector CIP declining to $50 million by 1990 and then no further financing. This assumes that the exchange rate, when fully unified, will obviate the need for a private sector CIP.

We are not sure how fast the rate will be unified or if indeed there will be full unification. It is possible that USAID may continue the private sector CIP throughout the entire period, particularly if the government moves to a dual exchange rate where the public sector accesses the official rate and the private sector is forced into the free market for its foreign exchange.

Finally, we will encourage the GOE to use the public sector CIP for procurements which support classic public sector investment, that is, categories like road maintenance equipment and spare parts for public utilities. If the GOE continues to import consumer goods or industrial raw material, we will encourage it to value those imports at their real cost, passing them on to the final consumer or the intermediate processor, and utilizing the local currency generated for appropriate and mutually agreed to public investments.

3. The Sector Programs

	1987	1988	1989	1990	1991	1992
Sector Programs	500	500	500	550	715	715

As the narrative indicates, our sector programs will concentrate in agriculture, private industrial development, infrastructure, local government, health, population, education, and science and technology. The total value of resources devoted to these programs will grow to over $700 million annually by 1992.

- Among these specific sectoral programs highest priority will be given to those programs which directly support productivity. These will be agriculture and private sector industrial development.

- Second priority will be support for infrastructure and institutional development programs which directly relate to our productivity initiatives. These will be policy dialogue support, local development, science and technology, and energy development.

- Third priority will be support for those programs which directly address the human resource needs of a productivity strategy, and support the safety net strategy. These include population, health, basic education and training.

- Fourth priority will be to complete programs which are underway. This will include water and wastewater programs.

- We will also continue a small program of studies, technical support and design efforts to meet important ad hoc requirements of the program and classic project development and support activities.

Throughout the sector program we will utilize a mixture of project, commodity and cash financing which will allow us to meet specific sectoral objectives most effectively. We will utilize cash transfer or performance payment disbursement mechanisms to provide additional

cash support if there is a a critical cash need in any particular year. These disbursement mechanisms, combined with our ability to shift or delay obligations of slow-moving programs and the general deobligation/reobligation authority granted under the Foreign Assistance Act, give us adequate flexibility to meet unplanned cash requirements of the program during the CDSS period.

4. PL-480 Title I

1987	1988	1989	1990	1991	1992
169.1	180	150	125	100	75

In line with the Agency's intention, we propose to phase down the Title I program over the CDSS period. By the end of the CDSS planning period we will reach a near equilibrium level of Title I.

5. PL-480 Title II

	1987	1988	1989	1990	1991	1992
Title II	4.9	2.7	2.7	-	-	-
Monetization	2.5	2.5	2.5	2.5	2.5	2.5

Likewise, the Title II program reflects the agreed to phaseout. We show a small monetization program which has already begun through the reprogramming of current stocks on hand. This important effort will support private voluntary organizations which are an important element in the Mission's efforts to shift resources towards private sector financing programs. The PVOs, both indigenous and U.S., offer a unique opportunity to mobilize local initiatives and financing to support a wide range of development programs targeted at making the poor part of the productivity equation.

B. Personnel Levels

The requirement through 1992 for USDH program and project management will not decline under current assumptions. We have, therefore, straightlined the staff at 111 USDH positions. If massive shifts to nonproject assistance were to occur for two to three consecutive years, there would undoubtedly be less need for USDH. A massive shift for one year, however, would not appreciably diminish the need to continue to maintain and design the regular program.

There are, in fact, trends which will mean an increase in USDH staff intensity as we enter the CDSS period. Chief among these are:

- The staff intensity of policy dialogue. As we have learned over the last 18 months, policy dialogue requires a huge investment of staff time. Discussions with the government, policy analysis, preparation for public, national and international presentations, assisting and encouraging efficient decision making and monitoring policy progress, all take a lot of time. As we move towards performance-based dollar disbursements in our projects, the staff requirements for performance monitoring will increase.

- Pressure to move toward A.I.D. direct contracting. A.I.D. has resisted pressure so far to move toward significantly more A.I.D. direct contracting. We remain committed to the idea that in the long run host country contracts are more efficient and effective. There remains, however, a pent-up pressure, mainly among the construction contractors, currently to move toward A.I.D. direct contracts.

- Contract closeout problems. As we close out a good portion of the ongoing infrastructure program there will be considerable pressure to involve USAID in time-consuming closeout procedures, including dispute resolution and arbitration. To the extent that USAID must play a more pronounced role in these efforts, it will mean a significant increase in staff time devoted to these processes.

Even with the above considerations and the design and monitoring responsibility of the regular program, we can maintain appropriate oversight within the current ceiling of 111 USDH. Reallocation among offices and functions will be used as a means of achieving effective management.

XIII. MEASURABLE INDICATORS OF PROGRESS

The strategic goals and measurable benchmarks below are consistent with those used in the Action Plan which accompanies this document, but are organized according to the strategy elements described here, and focus on longer-term indicators.

A. Support for the Policy Dialogue Process

Strategic Goal: Promote long run political stability and economic growth and development by encouraging the GOE to undertake structural economic reform.

Measurable Indicators:

Unify foreign exchange rate according to agreement reached with the IMF in FY 1987. Our current expectation is that full unification will occur by the end of FY 1989.

Equalize effective interest rates for public and private sectors at positive real levels by the end of FY 1989 or allow them to move to market-determined levels.

Reduce GOE budget deficit starting in 1986/87 and reaching 4 percent of GDP in 1991/92.

B. Support for Increased Productivity in Key Sectors

Agriculture

Strategic Goal: Increase agricultural production by 30% from 1989 to 1993 through the following sub-goals:

Remove controls on production and allow output prices to move to market levels.

Measurable Indicators:

Remove procurement quotas on all crops except cotton by 1993.

Remove mandated area controls on planting for all crops except cotton by 1993.

Raise real farm price of cotton to world market price equivalent by 1993.

Increase generation, extension and adoption of improved technologies and increase availability of credit to farmers.

Measurable Indicator:

Provide increased credit and improved banking services to small farmers in over 350 village branches of the Principal Bank for Development and Agricultural Credit by FY 1992.

Strengthen the private sector by increasing its capacity to market farm outputs and inputs through deregulation of trade, divestment of public operations, promotion of private businesses and reduction of GOE subsidies for commodities sold by public sector suppliers.

Measurable Indicators:

Increase loans to agriculturally related private businesses to 5 percent of PBDAC loans by the end of FY 1992.

Privatize government owned or operated farm input supply systems by FY 1992.

Eliminate government farm input subsidies by FY 1991.

Improve the overall water use efficiency of the irrigation distribution system by 8 percent between FY 1986 and FY 1991 and develop mechanisms for cost recovery.

Measurable Indicators

Develop and implement an integrated system for upgrading maintenance of the irrigation system. Make the maintenance system operational in 16 agricultural directorates by 1993.

Rehabilitate the irrigation delivery system down to the farm level on 300,000 feddans by 1991.

Begin charging fees to cover 100 percent of irrigation O&M costs in rehabilitated areas in FY 1992.

Private Industry

Strategic Goal: Increase private industrial output by 10 percent annually through 1993.

Measurable Indicators:

Increase the private sector share of industrial investment from 15 percent in 1986 to 50 percent in 1993.

Divest 32 enterprises owned by local governments to private sector by FY 1993.

Strategic Goal: Improve private industry productivity and management practices through support for business service and support institutions.

Measurable Indicators:

Improve access to market information. Locate 30 partners for joint ventures annually through 1993.

Expand uniform standards of accounting nationwide by 1993. Refine capital market law favorable to the issuance and trading of new capital market instruments.

Strategic Goal: Expand access to and availability of institutional finance for private industrial needs.

Measurable Indicators:

Credit guarantee fund to service 500 small scale industries by 1993.

Nationwide small-scale enterprise credit program operating through all regional banks of the National Bank for Development by 1993.

C. Infrastructural Investments

Energy

Strategic Goal: Ensure a reliable, economically - priced energy base to meet the needs of modern agriculture and industry through the following sub-goals.

Increase electricity tariffs and petroleum product prices on a path toward total elimination of implicit GOE subsidies by mid-1992.

Measurable Indicators:

Increase electricity tariffs by 30 percent above inflation annually from FY 1988 through FY 1992.

Increase real prices for domestic petroleum products 40 percent annually until economic prices are achieved.

Increase the supply of electrical power to meet demand by 1993 through expansion of new generating capacity, rehabilitation of existing generating capacity, and/or conservation - whichever means proves to be most cost effective. (USAID will pursue this goal through new projects only if electricity tariffs are increased)

Measurable Indicators:

Reduce distribution losses in the national grid by 20 percent by FY 1991 through the installation of distribution capacitors.

Improve energy conservation and production through planning, manpower development, and introduction of energy efficient technologies.

Water and Wastewater

Strategic Goal: Improve Egyptian capability to manage and finance water and wastewater systems.

Measurable Development Benchmarks:

Increase urban user tariffs to cover 100 percent of operation and maintenance costs by 1990.

By the end of 1989 all completed facilities to have on-the job training programs in operation and maintenance.

D. Other Investments to Support Productivity

Local Development

Strategic Goal: To improve the capacity of local governments and non-governmental organizations to plan, finance, implement, operate and maintain locally chosen basic services projects.

Measurable Indicators:

Ministries of Planning and Finance routinely providing to local governments, on a matching basis, discretionary capital and recurrent cost financing equivalent to 30 percent of A.I.D.'s annual capital contribution to the Local Development Program.

Establish a comprehensive operation and maintenance system for governorate infrastructure, equipment, and services by 1991.

By 1993 introduce four urban upgrading activities managed and financed at the Governorate level.

Education and Training

Strategic Goal: To build a literate and trained labor force capable of meeting the needs of modern industry and agriculture.

Measurable Indicators:

Rural enrollment in basic education (grades 1-9) increased to 90 percent by 1993.

1,000 new participants trained in the U.S. each year from 1987 through 1993.

E. Health and Population

Health

Strategic Goal: Reduce the infant mortality rate to 51/1000 and the child mortality rate to 7/1000 by 1993 through support for child survival interventions.

Strategic Objective: Establish a rational health financing system to expand cost-effective investments for health services, emphasizing cost recovery and allowing government health services to shift emphasis from curative to preventive care.

Increase the number of government health facilities charging fees for service by 80 percent in FY 1992.

Increase utilization of private health insurance, health maintenance organizations, preferred physician organizations, and other prepaid health services by 30 percent in FY 1992.

Expand private medical practices by 50 percent in secondary cities and rural areas in FY 1992.

Shift GOE health expenditures significantly from curative to preventive care by 1993.

Population

Strategic Goal: Increase modern contraceptive prevalence in Egypt from 31 percent in 1986 to 40 percent in 1993, thus supporting the GOE's target for reducing the population growth rate from the current 2.7 percent to 2.1 percent in 2001.