

## Egypt's Political and Economic Transition at a Crossroads

Subcommittee on the Middle East and South Asia  
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Testimony by

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Thank you, Mr. Chairman, for the honor of testifying before the subcommittee. I will focus on the economic issues in post-revolutionary Egypt.

Egypt one year after the fall of Hosni Mubarak is a confused place, in which the shape of the political transition is still disputed, insecurity is rampant, civil society is more harassed than ever, and an economic crisis is looming. Between the United States and Egypt, relations have deteriorated to a point where a suspension of US assistance is a real and imminent possibility. Transitions from authoritarian government are typically difficult and lengthy, so some of this is not surprising, but in Egypt's case the fact that much of the Mubarak-era state infrastructure remains intact complicates matters. Egyptian demonstrators in February 2011 forced the overthrow of Mubarak and relied on the military to see them through to democracy, which made their uprising shorter and less violent than some others in the region. But there are also costs associated with that choice, which have become increasingly apparent over the last year.

Egypt's economy has been one of the victims of this disorderly transition and an approaching economic crisis threatens to disrupt an already troubled political process. Getting the economy back on its feet—after a popular uprising that repudiated the Mubarak regime's liberal economic policies because of their association with corruption—would have been a difficult task under any circumstances, but the Supreme Council of the Armed Forces (SCAF) and the cabinet officials they appointed have made it much harder than it needed to be through a series of poor policy decisions. They have run through Egypt's foreign reserves at a breakneck

pace, expanding the country's already bloated bureaucracy in order to provide employment and promising increased public sector wages for which they cannot pay. They have recently been forced to undertake limited austerity measures, rolling back fuel subsidies to industry, as it has become clear that they cannot sustain the current spending trajectory.

### **Needed: Security, a Clear Political Transition, and Foreign Assistance**

Beyond decisions on economic issues themselves, the SCAF-led government has hurt prospects for post-revolutionary economic recovery by failing to reform police and internal security, manipulating the political transition process to serve military interests, and mishandling offers of international assistance. Reforming the interior ministry, the various internal security forces, and regular uniformed police should have been a top priority for the SCAF during the last year. All had lost legitimacy in the eyes of the public through systematic human rights abuses before and during the January 2011 revolution. When the SCAF assumed executive powers on February 11 last year, the military had the mandate to do a thorough housecleaning but failed to do so beyond putting former Interior Minister Habib al-Adly on trial. The lack of effective policing and resulting rise in crime and insecurity, seen most recently in the February 1 soccer riot in Port Said in which 74 Egyptians were killed, strongly discourage the domestic and foreign investment badly needed to get the economy moving again. The SCAF's failure to respond to the demands for justice and accountability from the families of the more than 1000 demonstrators killed during the past year, as well as the tens of thousands subjected to human rights abuses and military trials, has fueled ongoing protests. Tourists and investors will not return to Egypt until security does.

Egyptian businesspeople and investors cite lack of clarity about the political transition timetable as another factor inhibiting economic revival. For months the SCAF resisted calls for a roundtable process or a joint civilian-military leadership to make important decisions about the sequence and timing of the democratic transition, seeking to maintain control until a new constitution was written in order to enhance the role of the military in the new Egypt. Even setting aside the troubling political implications of such actions, Egyptian and foreign investors need to see a clear political timetable, one designed to serve the national interest rather than that of the SCAF, in order to have the confidence to begin putting in capital again.

The transitional government's decisions on foreign assistance also have been ill-advised. They turned down a \$3.2 billion loan from the International Monetary Fund and a \$4.5 billion loan from the World Bank in June 2011, deciding instead to hold out for cash assistance from Arab and other G20 donors. Only \$1 billion in grant aid (from Saudi Arabia and Qatar) has actually arrived, as all donors have insisted that they need to see a clear economic plan, blessed by the IMF, before giving further assistance. The Egyptian government has now re-engaged with the IMF and World Bank and new loans are likely, but they are taking some time to arrange because international institutions are understandably hesitant to reach agreements with the transitional government and are seeking broader buy-in, particularly from the Islamist forces that now dominate the elected parliament.

Moreover, the transitional government has put at risk the \$1.5 billion assistance package from the United States through an unprecedented campaign against American as well as Egyptian non-governmental civil society organizations. This crisis and other decisions by the transitional government on foreign aid show a common approach: an insistence that foreign aid must be delivered as direct budget support to the Egyptian government—rather than project aid, grants to Egyptian NGOs, or investment in the economy—with no strings attached. Rather than working cooperatively with international donors and creditors to martial support for a democratic transition, the military-led government has behaved as though Egypt could afford to dictate terms, a failed strategy that has only served to isolate the country from international partners in its hour of greatest need.

### **Serious Economic Risks**

The economic results of these missteps have been disastrous, and a crisis is likely within the next few months. Egypt's reserves of foreign currency have dropped by at least 55 percent and perhaps as much as 70 percent (analyst estimates are more dire official statistics from Egypt's Central Bank), from \$36 billion to \$10-16 billion, over the last year. The government now only has enough currency on hand to pay for needed food imports, particularly wheat, for a few months at most. The ranks of unemployed workers have swelled by 37 percent, and tourism revenues in 2011 were one-fifth of what they were in 2010. The Egyptian pound has lost only 4 percent of its value against the US dollar in the last year, but analysts believe the currency is facing a much steeper drop as the government loses the ability to continue propping up it up through spending reserves. A collapse of the Egyptian pound, hyperinflation, and a food shortage as a result of dwindling reserves have all become real possibilities. And this might well unfold while the country passes through a particularly sensitive political phase; the writing of a new constitution, election of a president, and transfer of authority back to civilians are all supposed to take place between now and the end of June.

### **Implications for the United States**

The challenge for the United States is to indicate clearly to Egyptians that it is ready to support them as long as they remain committed to a genuine democratic transition, but not if the new Egypt will be even more repressive than the old one. If Egypt holds a free and fair presidential election, the military returns to its barracks, the constitution writing process is fair and inclusive, and civil society organizations are allowed to work without harassment, the United States should support the transition through continued bilateral assistance, debt relief, and opening free trade talks. As soon as a freely elected civilian government is in place, the United States should propose a bilateral process to review all forms of military and economic assistance, as well as trade policy, in order to reinvent a partnership based not only on shared strategic interests but on mutually beneficial economic and trade ties that will propel Egypt into the international community of free and prosperous democracies. If, on the other hand, the military-led government continues to hound American and Egyptian civil society organizations, manipulates the constitution writing process to win for the armed forces a continuing political role and freedom from oversight and accountability, and allows unreformed security services to carry out abuses unchecked, the United States should suspend assistance until Egypt returns to

a democratic course.

A transition to rule by elected civilians, security reform, and freedom for civil society are essential not only to ensuring that Egypt's transition leads to democracy, but also that it leads to sound economic growth that generates jobs and gives Egyptians hope. After thirty years during which the United States supported authoritarian leadership in order to secure peace but turned a blind eye to the costs in terms of corruption and human rights abuses, it is the least that we owe to the Egyptian people, who came out by the hundreds of thousands a year ago calling for dignity, freedom, and economic opportunity.

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