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**Role of Food Subsidies
on Poverty Alleviation in Egypt**

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1- Introduction

Food subsidies play a pivotal role in combating poverty during periods of economic hardship, especially those brought on by reforms. Often, this policy chooses between either administrative targeting or self-targeting in order to reach out to the poor. Under the self-targeting method, which is adopted in Egypt, food subsidies are offered to all people. However, it is originally designed to benefit only the poor through directing resources to goods used only by them, or what Adams (2000) refers to as inferior goods.

The adoption of the economic reforms in Egypt since the early 1990s - known as Economic Reform and Structural Adjustment Program (ERSAP) - led to a dramatic reduction in public spending. In general, the main two arms of ERSAP¹ have not yielded the anticipated sustainable growth and poverty reduction. Thus, great efforts are needed to achieve a pro-poor development strategy (Yamada, 2008).

Food subsidies, the main component of Egyptian public subsidies, decreased in both number of goods and overall volume. They are originally directed to assist the Egyptian poor, who greatly suffered because of the reform measures. The application of food subsidies reveals some drawbacks, the most important is the leakage to the rich. There are increasing calls in the society, therefore, for reforming, not eliminating, the Egyptian food subsidy system.

Though the adoption of the ERSAP reform package in Egypt yielded significant economic results, the program has also resulted in some social hardships for the poor who cannot adapt with prices increasing and cutting in public spending. During the recent wave of price increases, food subsidies prove viability to act as a buffer to

¹ economic stabilization and structural adjustment.

stave off social unrests such as the riots of January 1977, despite some amount of leakage to the rich. Thus, because of its importance, this paper will analyze that reforming - but not eliminating - the current scheme of food subsidies will gain the aspired welfare for the poor.

This paper is organized as follows: in section II, I deal with a theoretical framework for the role of food subsidy policy (self-targeting vs. administrative targeting) in alleviating poverty. The discussion will include the broader theoretical framework of how a food subsidy program may lead to significant poverty alleviation as well as the empirical application in different countries. Section III deals with an overview of the poverty in Egypt since the inauguration of ERSAP. The developments of subsidy policies adopted in Egypt will be analyzed critically in section IV, which will also explore the effects of subsidy policies adopted in Egypt on poverty. I conclude the paper with closing remarks in section V.

I1- Role of Food Subsidy Policy in Poverty Alleviation

According to Adams (2000), food subsidy programs in developing countries differ in their objectives and targeting. As for objectives, they may be designed to improve the nutritional status of some vulnerable groups or to help the poor at large. From the targeting point of view, there is either administrative targeting or self-targeting. The administrative targeting uses some specific methods in selecting people deserving the subsidies, and is somewhat more efficient in resource allocation. However, it needs some state organization or bureaucracy in order to reach to the intended groups of beneficiaries. This needs much more resources to cover expenses of organization construction and administration as well as bureaucracy remunerations.

The criterion of selection is often made on income basis (Adams 2000). As most of developing countries lack accurate income data, and due to spread of corruption in most of those countries, the administrative targeting becomes not suitable tool in this regard.

Under the self-targeting method, which is applied in Egypt and now under great pressures to be replaced by other more suitable schemes, food subsidies are offered to all people. However, it is originally designed to benefit only the poor through directing resources to goods used only by them, or what Adams (2000) refers to as inferior goods.

Self-targeted food subsidies prove success in some countries. This scheme is highly effective when subsidies are centered on products whose expenditure elasticities are either low or negative in the countries of high income-inequality. South Africa and Tunisia have an ideal experience of applying the self-targeted system, with recent successful improvements (Alderman & Lindert, 1998).

On the other hand, this policy has some limitations. A great percentage of subsidies, about one third of total transfers, is expected to leak to the rich. This scheme also has a very limited impact on poverty alleviation efforts. However, this policy may play a vital role in this regard until designing a full-comprehensive policy aiming at targeting the poor (Alderman & Lindert, 1998).

The debate on food subsidies gains its importance recently as it was the core component of any reform program initiated by the IMF and World Bank. The most common argument of developing countries governments to reject the suggestion of eliminating food subsidies is the fear of the resulting social unrests. As the leakage of

most current food subsidy programs is the key criticism, the minimization of these leakages becomes the first priority for any policy reform (Besley & Kanbur, 1988).

III- Overview of Poverty in Egypt since ERSAP inception

Theoretically, it was known from early beginning of adopting the IMF-World Bank reform strategies that these policies, whether stabilization or structural adjustment, have dramatic contraction effects on the whole economy. It was supposed that the state will compensate these effects through some government expansion programs aiming primarily to hit the resulting unemployment, which is the major contributor responsible for increasing poverty in the society (Ghandour, 1992).

It is well-known that ERSAP consists of three integrated components: stabilization program, structural adjustment program, and social aspects, which were taken into consideration through building up the Social Fund for Development (SFD). The first program aims at decreasing the budget deficit mainly through reducing the public spending (in which food subsidies are the major element). The second program aims at privatizing the public sector, and hence laying off its employees (Ghandour, 1992). The figure of unemployment, therefore, increased and the need for sufficient subsidies became evident.

In contrast to the bright successes achieved in the economic stability and structural adjustment, Egypt remains a low-income country with significant poverty years after the economic reform began (Pfeifer, 1999). Soliman (1995) conceives that ERSAP measures, though economically successful, are deemed responsible for the decline of the growth rate in per capita income and its social consequences, i.e. the continuity of poverty. Per capita growth in the 1990s has been more disappointing.

While Pfeifer (1999) considers that per capita income was about the same in 1995 as in 1985, Sachs (1996) estimates that Egypt's per capita GDP has declined by around 3 percent between 1990 and 1995.

On the other hand, a new global income tax was applied in January 1994. In Korayem's view (1996), levying this new tax, which is a regressive indirect tax, as well as widening the base of the other existing taxes and raising their rates, as part of ERSAP, has relatively more reducing impact on the incomes of the low-income population. This was because low-income earners allocate a large part of their incomes to consumption expenditure, which forms the base for indirect taxes.

Another negative effect can be attributed to devaluation of the Egyptian pound. Devaluation increased the wealth of owners of foreign currency deposits. This means a redistribution of income to favor foreign currency deposit owners. ERSAP also calls for reducing the government wage bill by 15 percent in real terms. Hence, the impact on government employee incomes was negative (Korayem, 1997).

Regarding the impact on wages in private sector, the increase in some prices caused by ERSAP measures led to a reduction in real wages in the private sector as well. Korayem (1996) concludes that with relatively scarce job opportunities in the Gulf countries and high domestic unemployment, the private sector witnessed a decrease in real wages, though not dramatic.

Since the implementation of the ERSAP, which included the cancellation of most direct and indirect support, the problems facing poor families in general have constantly increased, particularly because of the extreme inadequacy of the Social Relief Program (SRP's). The SRP's are directed to the poor and destitute families, incapable of joining the labor force, as the family earns an income ranges between 12

and 18 pounds from them. The total number of beneficiaries from SRP's reaches about 1m people (Soliman, 1995).

On the expenditure side, Subramanian (1997) notes that the total cut was obtained through the reductions in both investment expenditure and current expenditure. The remaining cut came from a reduction in net lending. Within investment expenditure, the share of spending according to the social services sectors remained unchanged. The bulk of the investment cuts came from the government's cuts on projects in the electricity and tourism sectors. Within current expenditure, subsidies and transfers witnessed a decline, while wages and salaries saw a modest reduction.

Poverty is an intrinsically dynamic problem. It is a relatively new concept in Egypt, as academic studies started exploring it only in 1980s (World Bank, 2007). Although there is no unique definition of poverty (World Bank, 2007), Walton offered a generally accepted one. Walton (1990) defines poverty as the inability to attain a minimal standard of living. In order to combat poverty, the Egyptian government pursued the long-adopted policy of food subsidies, which had its origins in the 1940s after the World War II.

Poverty in Egypt, measured by the number of households living at or below the poverty level, has increased remarkably (Korayem, 1996). While less than eight percent of the population are abjectly poor (living on less than \$1 per day), consumption surveys in the early- to mid-1990s show the overall poverty rate has risen, with 44 percent of the population unable to spend enough to have minimally adequate diet. Falling average incomes have resulted in falling household expenditure on food (Pfeifer, 1999).

The impact of ERSAP on the poor can be well measured through the cost of living criterion. Cost of living increased because of the main ERSAP policies, such as the elimination of subsidies; devaluation; increase in prices of energy, transportation, public enterprise commodities, ... etc; as well as raising indirect taxes and widening their base. Subsidies were given for basic consumer commodities and services, like basic food items and transportation. Reducing the subsidy bill has a greater impact on the poor, since a large portion of a poor family's budget is spent on subsidized basic food items. Similarly, the devaluation of the pound raised energy prices, which led to an increase in the price of imported commodities, including basic food items like wheat and flour, as well as the prices of imported capital and intermediate goods. These in turn raised production costs of domestically produced goods and the general price level, and hence the cost of living (Korayem, 1997).

ERSAP's impact on the poor could secondly be measured through observing the reduction in real income resulted from price increase. After adoption of ERSAP, the Egyptian economy has witnessed the decline of real wages (Said, 2002). This is measured as either the rising in prices or decreasing of nominal wages. The working poor, who are mostly illiterate or have low education levels, earned low incomes and were thus more vulnerable to increased prices. Moreover, ERSAP's tight fiscal and monetary policies and calls for reduction in government spending depressed job creation. Since the poor are the least educated and do not have influential social connections, their chances of getting jobs is thus relatively slim when the labor market tightens up (Korayem, 1996).

The third criterion to measure the impact of ERSAP on the poor is through social services provided by the government at little or no cost. Despite the increase in real

investment in education and health, their services remained below the level achieved in the late 1980s. With the increase in the number of students and population, the result was a decline in real investment per student and per capita in education and health. Consequently, although students at all levels now pay a small fee, this does not necessarily translate into improvement in the quality of education provided, nor may adequate reasonable quality health services be expected at subsidized price (Korayem, 1997).

The implementation of ERSAP, therefore, had negative effects on the poor, a matter that was acknowledged by both the IMF and the World Bank. The SFD was created to alleviate hardship on the poor, but the limited resources of the SFD made this unfeasible. This gives room for food subsidies to play a wider role in alleviating the suffering of the poor from the reform measures.

IV- Effect of Food Subsidy Policies Adopted in Egypt on Poverty

The subsidy scheme was under great pressures from international organizations to be eliminated. The whole debate on food subsidies in Egypt centers on economic and social considerations. Those who call for elimination of subsidies for economic considerations ignore any resulting social unrests that may happen. The claims for economic considerations are either the necessity for applying market mechanism or production efficiency. The other problem in their point of view is the volume of leakage of these subsidies to the rich (Salevurakis & Abdel-Haleim, 2008). Table 1 below illustrates some of the effects of such leakage in Egypt.

Table (1): Food Subsidies Distribution between the Poor and the Better-off

Items	The Poor				Better Off (%)	Total (%)
	Extreme Poor (%)	Moderate Poor (%)	Near Poor (%)	Total (%)		
Baladi Bread	4	14	20	38	62	100
10-piaster Bread	0	1	3	4	96	100
Ration Cards Subsidies	4	16	23	43	57	100
All Food Subsidies	4	14	20	38	62	100

Source: World Bank. 2007. Arab Republic of Egypt: Poverty Assessment Update. Washington, DC: The World Bank.

However, despite this obvious leakage, the effect of food subsidies is impressive on both the standards of living and poverty. The subsidy on 5-piaster baladi bread for example helped about half of those lifted out of poverty (World Bank, 2007).

On the other hand, as a result of the application of ERSAP in Egypt, food subsidies as percent of total public spending decreased dramatically - from 16.9 per cent in 1975 and 18.4 per cent in 1984-85 to 7.4 per cent in 1990-91, then to 6.5 per cent in 1996-97 (Adams, 2000). Then, the social spending as a percentage of GDP in Egypt increased from an average of 7.5 per cent during the period 1996 – 2000 to 9.8 per cent during the period 2001 – 2005. The spending on food subsidies, as illustrated in table 2 below, shows an upward trend to reverse what happened during 1990s (World Bank, 2007).

Table (2): Development of Spending on Food Subsidies

Year	Spending on Food Subsidies as Percentage of	
	Total Public Spending (%)	GDP (%)
2002	3.3	1.2
2003	3.8	1.2
2004	4.1	1.7
2005	5.6	2.1
2006	4.6	1.5
2007	4.0	1.2

Source: World Bank. 2007. Arab Republic of Egypt: Poverty Assessment Update. Washington, DC: The World Bank.

The empirical experience also reveals the importance of food subsidies. Violence has occurred in a great number of countries, such as Algeria, Morocco, Sudan, Jordan and Tunisia between 1977 and 1989 as a result of reform policies aimed primarily at applying structural adjustment, stabilization, liberalization and privatization (Salevurakis & Abdel-Haleim, 2008). This gives an important indicator of the role that food subsidies play in society stability, as the opposite will result in severe costs on the country.

V- Conclusion

There are genuine fears that economic stabilization may prove reversible if the adjustment does not deliver significant growth in the near future. Lofgren (1993) substantiates that it was clear that GOE had opted for a very gradual implementation of the ERSAP, which led to a long-run cost in the form of lower incomes and continuing poverty. Bromley & Bush (1994) further confirm that the adjustment problems center on this cautious pace of implementation.

However, despite the very high economic growth rate of 7.1 in 2007² according to IMF, the people in Egypt do not feel the fruitful results of such growth. The main reason is the inequality in distributing the gains resulted. Egypt still faces the same problems of high inflation rate (19 per cent in the monthly average in May 2008 according to CAPMAS data) and high gross domestic public debt as percent of GDP (67.5 per cent in June 2007 on annual basis)³. Moreover, the increasing growth rate does not guarantee a just distribution for the resultant benefits among people. This indicates that a redistribution policy should be applied in favor of the poor.

In conclusion, the above analysis reveals that despite the normative goals of ERSAP, the reforms do not effectively alleviate poverty. One should not criticize the subsidies policy only for ideological concerns, as it demonstrates viability, especially in case of Egypt after adopting ERSAP. The social and human considerations cannot be sacrificed for the sake of pure theoretical hypnos. With continuous price increases, vast groups of population witnessed a great deterioration in their social positions and became unable to fulfill their basic needs. The need, therefore, arises for reforming, not eliminating, the current food subsidy system in Egypt which appears to function more likely as a safety valve.

However, poverty in Egypt can be handled from some different aspects. Upon constructing reform policies, the whole reform package should be applied. In this regard, Egypt should not have applied reduction in public spending, mainly the subsidies component, without having established its efficient system of social safety nets. Subsidies are very important in the Egyptian case and cannot be eliminated.

² This high rate actually succeeded a trend of very low growth rate, especially in the early 2000s.

³ Ministry of Finance, The Financial Monthly, May 2008. Vol. 3, No. 7. (P: 4).

Great efforts, however, should be exerted to reform the current system in order to make it more contributing to the poor.

Moreover, creating new jobs and minimizing wage inequalities to the lowest degree are critical factors that may greatly contribute to help eradicate poverty in Egypt. These are the factors on which any reform process should concentrate. Without them, nothing of the reform process could be felt by the poor, as the case now in Egypt.

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