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DEVELOPMENT FINANCING AND PRICE STABILITY
IN THE UNITED ARAB REPUBLIC

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ABSTRACT

In this part of the world as elsewhere, the question of economic development is becoming more and more significant. One of the problems in economic development is the problem of financing. It is certain that the achievement of higher rates of development requires, among other things, an increase in the rate of investment which tends to generate an upward pressure on the price level unless people give up some of their desires to consume.

People in underdeveloped countries expect their governments to run the development process. On the other hand people are opposed to the idea of giving up a greater part of their income to finance the development required. Governments, not possessing the means to mobilize domestic saving by the free will of citizens are tempted to resort to deficit financing. This method of development financing created inflationary tendencies in some countries which ultimately defeated the purpose of development which the financing aimed at.

The purpose of this thesis is to study the size of financing applied by the United Arab Republic, Egypt, to study the sources of financing, and to study the impact of these methods of financing on price levels. The period considered is that

which followed the coup d'etat of 1952 up till 1960. Thus, the study has three aspects:

1. The size and purpose of development financing which is the subject matter of Chapter I.

2. The sources of financing and the changes in the significance of each source. These are divided into three principal sources: a) Private savings including business saving, discussed in Chapter II; b) Government saving discussed in Chapter III; c) The "rest of the world" which is the equivalent in amount to the deficit of the balance of payments on current account, treated in Chapter IV.

3. The trends in price level, causes of changes in price level and the role of development financing in this trend are dealt with in Chapter V.

How much domestic saving was possible to realize and at what ratio it has risen are examined in Chapters II, III, and IV. Numerical findings are tentative and lacking in perfection. The findings with regard to trends are more reliable. There were no accurate available data on savings that could have been used with full confidence. Best sources available mixed, sometimes, between gross savings and net saving. Most probably there are some duplications and omissions.

With regard to the rest of the world an attempt is made in Chapter ^{IV} / to match the total deficits in the balance of pay-

ments on current account to total funds offered by the rest of the world. There is an arithmetic difference that is due to omissions and duplications that are not possible to assess with great precision.

In Chapter V the attempt aims at finding the cause of the rise in prices which was significant only in 1956-1957. For this purpose the methods of financing used and changes in the role of each are examined. The behavior of each of the following relevant variables was followed: national output, consumption, government deficit, expenditure, money supply and foreign economic relations. It is not possible to attribute the incidental rise in prices to any single factor. The factors themselves are inter-related. How much each factor is in turn influenced by the development financing methods is highlighted.

It is thus apparent that the area of the study, its scope and coverage, are rather wide which makes for lack of perfection and perhaps depth. The difficulty of finding relevant, reliable and consistent data is not to be underrated.

The whole attempt may have contributed more to the study of financing trends than to numerical facts. Among the trends studied, two are of great significance to development financing and price stability, that are worth noting here. Domestic financing is turning to become more and more a direct public duty, less dependent on personal decisions. Foreign financing on the other hand is shifting from equity financing and private contribution to a government long-term borrowing.

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C H A P T E R I

THE PROBLEM OF ECONOMIC FINANCING

Introduction

Chapter I is an introduction to the main subject and it serves as background material. It describes the pressing demand to raise the national income per capita to a higher level, and shows the attempts of the New Regime, ever since 1952, to turn a greater part of the national resources into capital goods. The trends in the national income and investment during the preceding period were followed up from 1939 to 1952 in the first part of this Chapter.

Actual investments by private and public sectors during the period 1952-1960 are stated in figures. In addition to this, the change in national income in monetary and real terms is stated too. Explanations of these trends and of the role of the government in development process are also treated.

Being the major objective of economic development, the problem of national income is of central importance to this study.

The available data on national income for the two periods, before and after the coup d'etat, do not lend them-

selves to reliable comparison for different reasons: for one thing, their sources are different. While the data for the period 1939-1951 was taken from Dr. Mahmoud Anis, that for the period 1953-1956, was taken from the Department of Statistics and Census. With regard to the period 1956-1960, the data used consist of estimates based on the findings of the Department of Statistics before 1956. The Committee for Development Planning prepared data on national income for the year 1959/1960. It is believed that this later data is consistent with the data by the Department of Statistics. However, it is the only data available for the year 1959/1960. The data used in this text are also used by reputable references quoted in the text.

A. NATIONAL INCOME BEFORE 1952

In 1939 the size of the national income in Egypt, in current prices, was estimated at LE. 168 million, which is equivalent to LE. 10.2 per capita.¹ During the 2nd World War the national income continued to drop up till 1943 to rise again until 1947. In that year however there was another decline. 1950/51 was another good year. These fluctuations which took place were apparently due to foreign

1. Mahmoud Anis, "National Income in Egypt", Egypte Contemporaine, v.44, p.48, (January 1953)

circumstances. During the war some of the industries, whose products were demanded by the British troops and the domestic market developed. The protection that was provided by the war circumstances to the domestic products, ^{did} ~~has~~ not shown positive effect on national income early during the war, because the latter caused shortage in the supplies and equipment necessary for agrarian and industrial development. Immediately afterwards war circumstances became more favorable. Foreign peace products were too short to compete with domestic products. Supplies and equipment became available. Savings of Egyptians cumulating in England during the war served as source of financing. Foreign products appeared again as competitive substitutes to domestic products. Another chance for development occurred at the break of the Korean War, a chance which was not properly utilized. Conspicuous consumption and luxury investment went away with a great part of former savings and current earnings of foreign currency. There was no overall economic planning to mobilize savings and to channel them into more feasible projects.

Below is a Table showing the trends of national income in the period 1939-1953. The source of the data in the first column is Doctor Mahmoud Anis.¹ The Wholesale Index is from the Economic Bulletin of the National Bank of Egypt.²

1. Ibid

2. op.cit. Economic Bulletin, v.X, p.221, (1957)

TABLE I*

NATIONAL INCOME IN SELECTIVE YEARS

	1	2	3	4
	Current	Wholesale	1939	in LE. million
	Prices	Index	Prices	Per
				Capita
1939	168	100	168	10.2
1943	390	253	154	8.6
1945	502	317	190	11.-
1950	860	376	229	11.9
1951	926	386	240	12.2

Data in column 3 are computed by dividing 1 ÷ 2.

The per capita income is computed by using the figure 10.2 as base and deflating by 2 per cent per year on the assumption that the average annual increase in the population is 2 per cent.¹ Accordingly, the real income per capita increased during the 13-year period by 20 per cent. The rate of increase per year per capita was 1.5 per cent. The use of the wholesale index as deflator remains the best available inspite of some drawbacks.

In an effort by the Council for National Development to trace the trend of national income, they came to a conclusion that it declined from LE. 10.2 per capita, per average

1. Permanent Council for Development, Yearbook, 1955, p.4, Cairo: 1955.

* Sources are quoted in the text.

year in 1937-1939, to LE. 9.5 per average year in 1950-53.¹ Their figure for total national income, in constant price, is LE. 202 million in the average years 1950-53. This figure is lower than that for the year 1951 as shown in Table I by LE. 38 million. The difference is about 15 per cent.

Even if we accept that there was an increase of 1.5 per cent per year per capita, ^{that} is no satisfactory progress at this low level of income besides it's not being steady. The whole increase was in fact due to the period 1943-1950. The national income in 1953 was only as much as in 1950.² The national income that year was LE. 856 million according to the Department of Statistics.³ However, comparison with Dr. Anis' computations is not quite reliable, because of the difference in source. Later in this Chapter when using them for this purpose, some reservations are considered.

B. CAPITAL INVESTMENTS DURING 1939-1952

The instability of the national income and the little long-run development was mainly due to ^{changes} fluctuations in

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1. Council for National Development, Yearbook, 1955, p.10
 2. Department of Economics, U.N., Economic Development in the Middle East, p.46, New York: 1955
 3. Department of Statistics, National Income, 1953 p.11, Cairo: 1954

the size of investment. Total savings during the war-years, 1939-1945, amounted to LE. 550 million according to Doctor Anis:¹ LE. 13 million, LE. 33.4 million, LE. 55.1 million, LE. 77.4 million, LE. 91.1 million, LE. 140 million, and LE. 139.6 million, respectively.

In addition to the war circumstances, the lack of imported luxuries forced savings which nevertheless were not invested in the country. Instead they augmented the Sterling balances in London. The purchasing power of these savings decreased with the international ^{rise} increase in prices. Actually ~~total~~ net domestic capital formation was negligible. Investment in some industries was counterbalanced by the decrease in the productivity of land and the depreciation in the fixed assets.

During the years 1945-1952, a considerable amount of investment was performed. The average capital formation per year amounted to LE. 100 million; 60 per cent was invested in new buildings; 15 per cent in public works, and electricity, and communication; and 25 per cent in business projects. The share of government in these capital expenditures was 12 per cent.² Assuming national income in the average year LE. 750 million,* the rate of investment to national income would amount to 13 per cent. This was an active period compared to the preceding period 1939-45. After 1945, investment ex-

1. Egypte Contemporaine, v.49, p.45, (January 1953)

2. Samir Amin, "Development Financing in South U.A.R." Egypte Contemporaine, v.50, p.5, (July 1959).

* by taking the average of figures presented by Dr. Anis

penditures covered fields of industry, agriculture, services, and public works. The government planned to spend LE. 35.6 million on specific projects according to a separate budget. A total of LE. 154.2 million was allocated in the five yearly budgets 1946-1950 to apply to public works vested with the different ministries. However, only LE. 12.5 million were spent on the projects and LE. 97 million were spent by the ministries on replacement and improvement. The scheme was not well planned and the administration was incapable of implementing the scheme.¹

The rate of investment was slower after 1950. Investment in industry, which developed at a rate greater than any other sector during and after war, declined after 1950. During war the average annual increase in industrial output was 12 per cent.² After the war industrial investments continued at a considerable pace and industrial companies increased their capital by LE. 25 million between 1945 and 1950.³ Sixty per cent of the increase in companies' capital was invested in industrial concerns. During the years 1951, 1952, and 1953 only LE. 2.1 million, 2.1 million, and 1.2 million ,

1. op.cit. Economic Development in the Middle East, p.28.

2. Samir Amin, Egypte Contemporaine, p.19 (October 1958).

3. op.cit. Economic Development in the Middle East, p.46.

respectively were invested in industry.¹ In commerce and other services LE. 9.1 million, LE. 11.6 million, and LE. 7.4 million were invested during the respective years.² Investment in buildings, which absorbed 60 per cent of total investments during 1950-52, also declined. According to the U.N. Department of Economic affairs,³ constructions reached a bottom in 1942 and a peak in 1950. They declined thereafter to recover in 1954. Since the investment in buildings in 1954 reached LE. 40 million it should have been less in the average year between 1951 and 1953, and much less than the average of LE. 60 million, estimated by Doctor Samir Amin, for the period 1945-52.* In other words, investment declined in total and in respective fields after 1950 but the greatest decline still remained in industrial investment. It is the sector which was stimulated by World War II and the Korean War circumstances and was doomed to collapse with the disappearance of these circumstances. The investment figures available for 1952 as mentioned above add up as follows:†

Industry	LE. 2.1 millions
Commerce and Services	LE. 11.6 "
Buildings	LE. 40.- "
Government	LE. 15.- "
	<u>LE. 68.7 millions</u>

1. Council for Development, Yearbook, 1955, p.13, Cairo: 1955

2. Ibid.

3. op.cit. Economic Development in the M. East, p.47.

* Table VI, later in this Chapter.

+ Sources are mentioned in the text below.

For buildings the figure used is that of 1953 and 1954 calculated by the Chamber of Industries.¹ The figure for "government" is the average annual investment computed by Doctor Amin representing investments in public works including electricity, transport, and irrigation. Using the 1951 national income, by Doctor Anis, as base, the rate of gross investment amounts to 8.5 per cent. Since the deficit on the balance of payments on current account in 1952 amounted to LE. 53.4 million² the real saving from current income of 1952 was about LE. 15 million only. However rough these calculations are, they show how great was the propensity to consume, and how little were the domestic savings during the year 1952.

C. INVESTMENT TRENDS SINCE 1952

1. New Role Assumed By The State

After the coup d'etat of July 1952, the New Regime promised to raise the standards of living by securing greater development and by redistributing wealth and allowing equal opportunities for all citizens. The New Constitution announced in January 1956 made it the "duty" of the state to realize these economic targets.* Article 7 reads: "National economy

1. Federation of the Chambers of Industry, Yearbook, 1956/57, p.8, Cairo: 1958.

2. National Bank of Egypt, Economic Bulletin, v.XIV, p.151 1961.

* Articles 6-17.

is to be organised according to plans which conform to principles of social justice, and which aim at promoting national productivity and at raising the standards of living."¹ Article 15 reads: "The State encourages private savings, supervises the regulation of credit, and promotes means for the profitable employment of the people's savings."²

As early as 1952 the government appointed the Permanent Council for National Development whose duties were to select, prepare, and implement economic projects. The Council was independent of the official routine and was presided over by the President of the State. In brief, the whole economy was to be directed according to plans studied and prepared ahead of time. No waste of resources was to be allowed. Planning, however, moved slowly. The first coherent plan was an Industrialization Plan for five years declared in 1957. The first overall plan for ten years was announced late in 1959 to be applied as from 1959/60. Prior to these two plans, the role of the government was mainly to create opportunities for private capital, to encourage private saving, and to invest directly, mainly in projects that have the public utility nature or in business projects that are too large^{for}/or too far from the experience of the private sector. The following paragraphs will treat the private investments in the large sectors

1. Egyptian Economic and Political Review, p.37, (February, 1956).

2. Ibid

of the economy. The next section will treat public investments in order to reveal the trend in size and distribution of these investments. The changes in national income are left for the next sections, reversing the order with which the previous period was treated.

2. Private Investments 1953-1960

The sectors of economy that received new private capital are themselves those mentioned in the previous section, namely, buildings, industry, trade and services. With regard to buildings all statistics use the data available in the municipalities for the latter issue licences before a person is allowed to build in towns and cities. With regard to the 1939-51, Doctor Amin estimated the value of new buildings by using the taxes collected on new buildings as base, and capitalizing by a 5 per cent ratio.

The data used by the Federation of Chambers of Industries is computed in a similar manner. By buildings, here it is meant residential buildings in towns and cities and wherever registration of new buildings is legally required. In fact only the least expensive buildings, in which iron and cement are not used, are not registered. Industrial and public buildings are included in industries and in public sector investments, respectively.

Capital investments in the fields of services and industry, by private sector, are the investments of those firms

that are registered in Chambers of Commerce and Industries. Small workshops and tradesmen are not included. However, since trends rather than size are more interesting to the purpose of this Chapter the data presented serve the purpose.

TABLE II

PRIVATE INVESTMENTS IN L.E. MILLION

	1953	1954	1955	1956	1957	1958	1959	Total
Buildings	40	40	42.5	51.4	53.3	59	43	392.2
Industry	1.2	6.8	9.7	25.6	12.4	12.8	18.9	87.4
Trade and Services	6.2	4.3	2.9	2.9	2.7	3.4	5.1	27.5
Total	47.4	51.1	55.1	79.9	68.4	75.2	67	444.1

Source: Federation of Chambers of Industries, Yearbook, 1956/57, p.8 and Yearbook, 1959/60, p.23.

The peak of private investment in buildings was reached in 1958 when the government prevented the demolishing of old buildings without a special licence authorized only when old buildings are no longer safe to use. The State wanted to discourage expensive luxurious construction. The consequences were the decline in investment in buildings the following year from LE. 59 million to LE. 43 million.

3. Measures Contributing To Increased Investments By The Private Sector

The government policy to encourage industry raised investment from LE. 1.2 million in 1953 to LE. 25.6 million in

1956. The following years investments in this sector declined in 1957 and 1958, to rise again in 1959 reaching LE. 18.9 million. After this year the government became a large investor in industry co-sharing with the private sector in joint stock companies as mentioned later in this Chapter. It became difficult after 1959 to separate public from private investment in this sector. Total investments in industry by private sector in the seven years amounted to LE. 87.4 million at an average of about LE. 15 million. Investment in trade was not as progressive as in industry. In 1953 investment in trade was five times greater than investment in industry, while in 1956 the latter was nine fold the former and in 1959 four fold. Foreign trade organizations especially declined. The public sector was gradually taking over foreign trade, trade in cotton and other commercial functions to maintain supply at stable prices.

Foreign trade policy aimed at increasing home demand for products that could be processed locally. Textile and yarn imports were reduced ever since the first year of this period. This industry developed greatly immediately after the coup d'etat. For Egyptian yarn, markets were found by the large number of bilateral trade agreements with markets completely new to the Egyptian exporter. Yarn was sold to China, East and West Germany, and Poland among other countries. Textile was sold in the U.S.A. Rubber tyres, a new industry, are

being sold to Yugoslavia. In addition to reserving the domestic market for domestic products the policy of diversification of foreign trade relations was the main cause of the industrial awakening. It is interesting to note at this stage, that what war accidentally offered to industry was now being offered to this sector on a more permanent and solid basis. Not to mention the higher taxes on imports or subsidies to exports. These measures were used prior to this period but the rich could still buy the goods as long as these remained available. A new method applied was the foreign trade budget, renewable every three months. The foreign earnings were allocated, in this budget, to the required imports in order of priority. On the top were food supplies for mass consumption; next came in order, machinery, equipment and supplies for approved industries, agrarian expansion projects and public works. These supplies and equipment were exempted from import taxes. Prices of equipment and freight charges were negotiated by government representatives to obtain reduction. In several cases such savings were considerable.

Related to the point of providing markets is the redistribution of national wealth and income. The best customers of domestic products are the low-income groups. Their capacity to buy and consume became far greater. Textile and food industries have doubled their products in the period 1952-1960. Their exports were far less than the actual increase in products. The difference was sold locally, compensating for

reduced imports and for additional exports.

Inside the country the government established Industrial Supporting Funds. These Funds were to help industries with technical assistance, to improve quality and productivity. Technical schools were established by the State to furnish new industries with skilled labor at moderate cost. Upon the request of the government help in this respect was extended by Germany, U.S.A, Russia, and other advanced countries.

The State provided political and social stability. The capitalist was sure that favorable circumstances are not accidental as in the case of industrial development during wars. The fear of foreign interference and foreign competition has been completely removed after the Suez Canal incident has proved the effectiveness of international opinion in maintaining peace and order.

Stability in business relations was achieved since 1952. There was one attempt on the part of the workers to realize better employment terms through coercive action. The resulting strike was, however, severely suppressed. No other incidents of violence were reported ever since. Law organized the relations between landowners and tenants, and between workers and employers. All disputes were subjected to compulsory arbitration. Workers on one hand were protected from exploitations, and businessmen on the other hand were protected from strikes and other coercive actions.

Stability in prices of materials was guaranteed by the

State, especially the price of cotton which formed a great portion of textile and yarn cost of production. The cotton exchange was reorganized as to allow no exploitation of speculators. A minimum price was guaranteed for producers and a maximum cost for the industries that purchased raw cotton for production.

The government encouraged joint stock companies and other limited companies, by a series of laws and positive steps to help. In September 1953, Law No. 430 was passed. It provides limited companies to be exempted from business income tax once they are established to invest in certain fields, approved by the Council for National Development.¹ Exemption lasts for seven years starting with the date of registration of the new company. The law applied to the portion of capital, of old companies, that have been subscribed after the date of this law. Other laws followed and made the registration routine simpler. The rights of subscribers were protected by making inspection by the State compulsory, by limiting the maximum return to the Boards of Directors and by reorganizing the Stock Market. General price index of stock of all companies moved from 57.1 in 1953 to 77.1 in 1958. A decline in this index started after 1946. In 1946 it was 100, it has risen again after 1953 up till 1958 and declined in the following two years.²

1. Federation of the Chambers of Commerce, Egyptian Economy During 1952-1957, pp.48-60, Cairo: 1958.

2. National Bank of Egypt, Economic Bulletin, v.X, p. 223 (1957) and v.XIV, p. 226 (1961).

After Egyptianization of foreign banks in 1957, and the increase in government ownership and control of banking and credit institutions, the joint stock companies were favored with greater share of the total credit facilities especially those of long-term nature. The registered capital of industrial companies, limited and unlimited, increased from LE. 36.2 million by the end of December 1954 to LE. 136.6 million by the end of April 1961. Capital of commercial and services companies increased from LE. 167.3 million to LE. 211.2 million over the same dates.¹ The industrial capital multiplied about four times.

Later, in this Chapter the government's endeavor to develop sectors supplementary to business will be illustrated with figures.* Expenditure on, and development of means of communication, health, vocational education, electricity, petroleum, and mining reduced business costs by providing external economies.

To encourage investment in new fields of industry the State guaranteed minimum profits to subscribers. In the case of Iron and Steel Factory at Hilwan, the government guaranteed 4 per cent return on profit. In the case of the Nile Hotels Company, the rate guarantee was 5 per cent. The government

1. op.cit. Economic Bulletin, No.3, v.XIV, Table 32, (1961).

* Table III, later in this Chapter.

started to subscribe to large industries like the Iron and Steel to cover the shortage in subscriptions. The policy was to sell government shares to the public, once these projects proved profitable, and to turn to new fields into which private capital was reluctant to enter. (However, there is no evidence of the application of this policy yet.) In other words, public capital was to encourage and complete, not to compete with private capital.

However, there were two measures taken by the government that could have hampered development of private investment. Nationalization of a number of foreign organizations in 1956 and 1957, including the Suez Canal, created fear of expansion of nationalization to include domestic enterprise. The other point was the determination of the government to reduce distribution of dividends that was manifested after 1958 by decrees and regulations that are to be discussed in greater detail in the following Chapter. Table II has shown in fact, that private investment in 1959 was below the 1956 investments.

4. Public Capital Investments

The picture of the total investment during the period 1953-1959 is completed when the investments by public sector are added. The latest data available on public capital expenditure were prepared by the National Bank of Egypt, and are presented in Table III. This Table includes development expenditures not appearing in other data from other sources.

Since 1953/54 the government has been following a practice of preparing a development budget, separate from the ordinary budget. The sources of these budgets are different from the sources of the ordinary budgets. But the ordinary budgets themselves furnished the respective ministries with funds to realize new works of ordinary nature. These funds are included in Chapter III of each ordinary budget under the caption "New Works." The National Bank has added these "Works" to the development expenditure. This is done, first, because there are actually expenditures of capital nature that governments undertake in ordinary times. Secondly, the budgets before 1953/54 were united and data on capital expenditure was taken from this Chapter III, "New Works." The Table therefore, in this form allows comparison with the years before development became a "duty" of the State.

Table III shows that the total expenditure by government on new works declined in 1952/53 and has then risen steadily up till 1956 after which it declined again over the following two years to shoot up again in 1958 and reach more than five times the expenditures of 1952/53. 1958 was the first year of the Five-Year Industrialization Plan. In that year the government started to participate directly, and considerably, in industrial projects. The government investments in industry and electricity during the year 1958/59 amounted to LE. 26 million and to LE. 58 million in the next year. Govern-

TABLE III

DISTRIBUTION OF PUBLIC DEVELOPMENT EXPENDITURES

	50/51	51/52	52/53	53/54	54/55	55/56	56/57	57/58	58/59	59/60	8 years Total
Agriculture	+1.8	4.8	3.1	14.5	7.3	8.8	7.7	9.3	8.3	9.0	74.6
Irrigation and Drainage	+5.4	+7.5	+4.7	+9.7	+5.5	+6.9	+5.7	+5.3	-7.9	+6.7	+65.3
High Dam	---	---	---	---	---	---	---	---	---	---	---
Industry	+7.5	-1.3	+1.4	+4.6	+6.0	7.9	8.5	5.1	17.4	+13.2	+19.5
Electricity	1.8	4.8	3.1	14.5	7.3	8.8	7.7	9.3	8.3	9.0	74.6
Transport-Cummi- cation & Storage	5.5	9.6	6.6	8.8	11.5	13.3	17.4	15.9	16.2	19.6	124.4
Housing and Utili- ties	1.9	3.1	3.2	5.1	11.2	20.9	9.5	9.5	8.6	7.0	80.0
Defence, Security, and Justice	0.3	0.5	0.1	0.1	0.3	1.1	0.2	0.5	0.6	0.2	3.9
Education Services	4.1	3.4	2.0	1.3	1.7	3.7	2.1	2.0	4.6	2.9	27.8
Health	1.1	0.9	0.7	0.6	1.8	3.2	1.0	0.8	1.0	0.9	12.0
Commerce, Research, and Other Servi- ces	2.7	2.4	2.2	1.5	2.2	8.9	3.3	4.1	4.0	4.6	35.9
	30.9	34.5	24.6	47.2	56.9	87.6	66.6	59.0	77.6	127.3	612.6

Source: National Bank of Egypt, Economic Bulletin, v.XIV, p.204,
(1961)

ment expenditure in electric industry started earlier. In 1953/54 such expenditure was LE. 14.5 million. The government considered electricity and petroleum essential for industrial development by the private sector. Before 1958 the industrial investment by government was mainly a share in the two large projects: The Steel and Iron Works at Hilwan, and the Fertilizer Plant, at Aswan. The shares of the two plants were not possible to be totally subscribed by the private sector. Government resources were too busy with other sectors: agriculture, transport, and other services that bring no direct return to capital. Expenditure on agriculture, including drainage, irrigation, dams, and land reclamation continued to rise as Table III shows, but at a lower rate than industry and electricity. Transport got a sizeable share of public investments. Investment in housing facilities and public utilities has risen sharply to register LE. 21 million in 1955/56 and have declined later, but in the last year such expenditures were still more than twice those of the years 1952 and 1953. On commerce, research, and other services fields there was a year when expenditures were specially high that was in 1955/56 when the government subscribed to a large share of the Nile Hotels Company. All over the period expenditure on research was increasing.

The general feature of these expenditures revealed by Table III is the feature of balanced growth planned ahead of time. Though industrialization was the principal goal it was not given priority in time. Already existing industries flourished

by indirect measures. Meanwhile, the agrarian sector was supported by direct investment. Sectors supplementary to business were given time-priority. The available resources at an earlier stage were spent mainly on agriculture and on these supplementary sectors like transport, housing, electricity, vocational training, and research. Later expenditure on these sectors will develop only at a lower rate than that of industry until the latter is mature enough and a balance in the economic structure is attained. This trend is ^{most} evidently reflected in the overall Five-Year Development Plan that started in 1959/60.

5. Investments By Two Sectors Added

Now, by adding up totals of Tables II and III we get the total gross investments in the U.A.R. (Egypt). To keep the years 1951 and 1952 for comparison purpose the data on private investments during the two years were borrowed from the Council For National Development¹, as far as industries and services are concerned. For buildings the same figure of 1954 as in Table II is taken. The result appears in Table IV.

Only during the years 1956 and 1957 investment trend declined. This recession is attributed to the great military effort before, and immediately after the Suez Canal. But the year 1957 witnessed the preparation of the First Industrial Plan

1. The Council For National Development, Yearbook, 1955, p.13, Cairo: 1955.

TABLE IV

DISTRIBUTION OF GROSS INVESTMENTS

in LE. million

	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959
Private	----	49.-	52.-	47.4	51.1	55.1	79.9	68.4	75.2	67
Public	30.9	34.5	24.6	47.2	56.9	87.6	66.6	59	77	127.3
		83.5	76.6	84.6	108	142.7	136.5	127.4	152.2	194.3

Source: Former Tables II and III.

that had set targets. The Plan accounted for the sources of funds and their application to specific projects for which blue-prints were already made. In 1958 investments were 30 per cent greater than in 1957, and those of 1959 were 30 per cent greater than those of 1958. The trend continued through 1960 in conformity with an Overall Development Plan. Still greater development of public share in investment is yet expected and greater share shall be invested in industry. In 1959 investments by the public sector have reached twice those of the private sector. Total gross investments were 230 per cent of the gross investments in 1951.

D. NATIONAL INCOME SINCE 1952

1. Growth Of National Income

It is to be remembered here that investment trends are

not immediately reflected on income trends. The first two years after the coup d'etat, development in national income was due rather to a stimulation of productive factors to utilize idle capacity. During the first two years of the period studied 1952-1954, national income increased from LE. 748 million in 1952 to 780 million in 1953 to 868 million in 1954.¹ Price indexes were 343, 354, and 342, in the three years without perceptible change.² The rise amounts to LE. 120 million during the two-years which is equivalent to 16 per cent. An increase of 8 per cent per annum is more than any state would aspire to achieve. But as has been mentioned it looks that the 1954 income was only as high as that of 1950. The explanation that could possibly account for this phenomenon is the great drop in cotton prices. The price index used as deflator, most probably, was not sufficient to account for this drop. Income from cotton was estimated at LE. 250 million in 1950³, while it was estimated at LE. 80 million in 1953.⁴ This factor, in addition to the recession in industrial output, has made the 1952 income much lower than that of 1950.

1. I.M.F., International Financial Statistics, p.108, (July, 1961).

2. op.cit, Economic Bulletin, v.X, p.221, (1957)

3. M. Anis, Egypte Contemporaine, p.60 (January, 1953)

4. op.cit, National Income, 1953, p.13

It was not possible to find data on national income for all years from one source. For the sake of comparison Table V below, combines national income from three sources in an attempt for comparison. For 1950 the data are those of Dr. Mahmoud Anis. For the year 1953 the data are the findings of the Department of Statistics and Census. For the year 1959 the data were prepared by the Higher Commission on Planning. No better sources were available for each of the respective years, therefore, used here as have been used by reputable references quoted in this text.

TABLE V

NATIONAL INCOME DISTRIBUTION IN SELECTIVE YEARS

	1		2		3 in LE. million	
	1950	%	1953	%	1959	%
Agriculture	374	43	273	32	400	31
Industry	105	12	94	11	273	21
Services	<u>381</u>	<u>45</u>	<u>489</u>	<u>57</u>	<u>609</u>	<u>48</u>
	860	100	856	100	1282	100

- Sources: 1. Mahmoud Anis, "National Income in Egypt", Egypte Contemporaine, v.44, p.48 (Jan.1953).
 2. Department of Statistics, National Income, 1953 p.10, Cairo.
 3. Abdurrazzak Abdumajeed, "Monetary Planning", Egypte Contemporaine, v.17, p.50 (Oct.1960).

The aggregate national income has shown a considerable growth over the six years 1953-1959. The increase amounted to

LE. 426 million in current prices. Accounting for the change in the wholesale price index*, the rise in national income would be reduced to LE. 1030 million in 1953 prices. The total increase in real terms is LE. 180 million which is equivalent to 21 per cent over six years. The average increase per year was 3.5 per cent. Assuming the rate of national increase in population to be 2 per cent, as in the preceding periods, the rate of increase per capita per year would become 1.5 per cent. This is only equal to the rate of growth per capita in the preceding period, 1939-1951 as per previous computations, from Dr. Anis' data.

Almost a similar result could be reached from the figures adopted by Mr. Abdurrazzak Abdulmajeed.¹ Below are those figures of national income at constant prices of the year 1954:

	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>
LE. million	868	919	935	873	945	996

According to those data the average rate of growth is 3 per cent, one per cent higher than the rate of national growth of population in the U.A.R.

Until the year 1959 the ambitions to arrive at a rate of economic growth that exceeds considerably the rate of population growth were not yet realized.

1. "Monetary Planning", Egypte Contemporaine, v.51, pp.11-17, (Octobér, 1960).

* 342 in 1953 and 418 in 1959.

2. Changes In Structure Of National Income

However, the fruits of industrialization that started in 1957 have not been fully reaped yet. Industrial production developed more than any other sector. The Industrial production index rose from 96.7 in 1953 to 100 in 1954, to 123.7 in 1957, and to 141.5 in 1959.¹ Concerning 1960 and 1961 the latest reports of the industrial census which are issued four times a year, are quite encouraging. While the sample used by the census cover 10 per cent of the industrial firms it includes 73 per cent of the industrial output. The 1960 output showed 17 per cent rise above that of 1959,² while the output of the year 1961 showed 25 per cent over that of 1960.³ During these two years the changes in prices were not perceptible. This proves the success of the Five-Year Industrialization Plan later reduced to 3 years in order to be terminated in 1961. It is believed that the 1961 national income would have shown considerable growth, except for the hard luck that cotton met.* The Overall Five-Year Plan aims at 8 per cent increase per annum in the period 1960-1965.

With regard to agriculture the quantum indexes, in order to avoid price complications, showed progress. Taking 1947 as

1. National Bank of Egypt, Economic Bulletin, v.XIV, p.110, (1960).

2. op.cit, Economic Bulletin, v.XIV, p.180, (1961).

3. Ibid, p.319.

* Latest reports tell that one-third of the crop was lost due to a cotton disease.

100, the National Bank presents the following indexes for the years 1953-1959 consecutively: 106, 98, 110, 109, 108, and 121.¹ The 21 per cent increase in volume of products over 6 years is also not too much compared to the growth of the rural population and to the effort spent and the financing achieved. The cropped area in the same period was increased by 890,000 feddans², which is equivalent to 1.5 per cent of the total cropped land, per annum. Reclaimed lands exceeded 100,000 feddans. During the previous 50 years, and since the Aswan Dam was built, the rate of increase in the crop area was only 0.5 per cent per annum. Increased cropped area, accordingly, was 9.5 per cent during the six years. The rest of the increased production was due to the effort and expenditure spent on raising productivity per feddan. There was, on the average, a 9 per cent increase in the total weighted productivity per feddan from the period 1948-1952, to the period 1953-57. In the period 1958-1959 the rate of increase in productivity per feddan was 13 per cent over the said base year.³ However, the growth is still

1. op.cit, Economic Bulletin, v.XIII, p.69, (1960).

2. Ibid.

3. Information Service, The Union after Three Years, p.42, Cairo: 1961, (Arabic).

mostly absorbed by the growth of population. The only hope is the success of the Overall Five-Year Plan and of the High Dam. The first is expected to increase the national income by 40 per cent at constant prices. The other is expected to raise agrarian production by 25 per cent, beside its value as a huge source of electric power.

With regard to the structure of the national income, Table V reveals the rapid advance of industry toward becoming a principal sector. Its share of national income increased from 11 per cent to 21 per cent. While the share of agriculture dropped from 32 per cent to 31 per cent. The share of commercial and other services dropped from 57 to 48 per cent. The Five-Year Plan aims at raising the share of industry to 33 per cent in 1965. The share of agriculture will eventually drop to 28.5 per cent.

3. Investment-Income Ratio

Before arriving at the Investment-Income ratio which is a significant point in the problem of financing, some amendments of previous data are due.

According to Table I private investments are not inclusive of all private sector investments. Dr. Samir Amin has got his data of total investments in profit-making enterprise by using the imported capital goods as base. Table VI, below, borrows his data on total investments and on public investment to reach total private net investments.

TABLE VI

DISTRIBUTION OF INVESTMENTS

in LE. million

	Average 1945-52	'53	'54	'55	'56	'57	'58	Average 1953-58
Buildings	60	47	47	47	46	48	48	47
Non-Profit Enter- prise.*	15	32	41	47	51	56	56	47
Profit Enterprise	25	38	43	65	66	39	67	53
Total	100	117	131	159	163	143	171	147
<u>Less: Public</u> Investments	12	32	44	50	56	60	63	51
Private Investment	88	85	87	109	107	83	108	96

Source: Dr. Samir Amin, "Development Financing in South U.A.R.", Egypte Contemporaine, v.50, pp.5-13, (July, 1959).

The data in Table VI are actual for the first four years and provisional for the other two years. The difference in data on buildings between Table I and Table VI is due to greater portion of buildings added to other sectors, by Dr. Amin.

By adding the private investments found in Table VI to public investments⁺ as in Table III the result would appear as follows:

* The so-called "equipment de base", including public works, irrigation schemes, transport, social service buildings, electricity, and others, usually government investments.

+ The average of two fiscal years is taken to apply to a calendar year.

	1953	1954	1955	1956	1957	1958	Average 1953-58
Private	85	87	109	107	83	108	96
Public	36	52	72	78	63	73	62
Total	121	139	181	185	146	181	158

Using the average national income in current prices, LE. 969 million given by Mr. Abdurrazzak Abdulmajeed,¹ as base, the ratio of investment to national income amounts to 16 per cent. The ratio of the total investments in the preceding period 1945-52 was 13 per cent. Besides, there was a serious recession in 1957 that reduced investments from LE. 185 million to LE. 146 million. The same year witnessed the beginning of comprehensive planning in the U.A.R. Investment in 1958 rose to the level attained in 1956. In 1959/60 government investments alone reached LE. 127.3 million, 65 per cent more than the year before, as Table III shows. The year 1960/61 was the first in the Overall Five-Year Plan. During this first year public allocation for development reached LE. 284 million. The private sector, most probably will not develop at this speed but the public sector alone will contribute to capital formation in the average year twice as much as the total investments in 1956. According to the plan the investment-income ratio shall rise to 21 per cent in 1964.

1. "Monetary Planning", Egypte Contemporaine, v. 51, pp. 11-17, (October, 1960).

Beside the rising trend in the ratio and the base, the change in the distribution of investments among sectors is very important. While residential buildings absorbed 60 per cent of investments before 1952, according to Table VI, the same ratio dropped to 35 per cent in the average year afterwards. Industrial investment which was negligible in 1951 and 1952 has risen to 26 per cent of the total investments, during 1953-1959. Agricultural projects absorbed 14 per cent; transport 12 per cent; educational and health centres 4 per cent; research, hotels, commerce, and other services received the remaining 9 per cent of investments during the period 1953-1959. The trend is towards still greater share of industrial development, as revealed by the Overall Five-Year Plan. The planning aims not only at raising aggregate national income but also at achieving a balance among the different sectors of production. The least developed was industry while facts prove that industry has the highest marginal profit. War time provided good experience which supported this fact in Egypt.¹

The reason as to why the rise in development financing has not raised with it at the same ratio the real national income is attributed mainly to two factors. First investment

1. Council for Development, Yearbook, 1955, p.11. Also Department of Economics, U.N., Middle East Economic Development 1945-1954, pp.26-30, New York: 1955.

started with public utilities and non-profit fields. Second the real increase in public investments in profitable enterprise started in 1957 and is expected to appear in 1961 and the following years. In view of these facts it seems that the Overall Five-Year Plan was conservative in estimating the increase in real national income during the fifth year at only 40 per cent of the base year, 1959/60. This is equivalent to 7.5 per cent per year, not accounting for the increase in population. This is only twice as high as the rate already achieved inspite of the fact that planned investment shall be more than doubled in absolute amounts.

While the present Chapter represents an attempt to throw some light on the magnitude of financing required and used in the U.A.R. during the period 1952-60, The next Chapters will try to identify the sources of this financing and the ways by which local savings were mobilized and the extent to which foreign sources were utilized.

C H A P T E R I I

PRIVATE SAVING

Introduction

The main purpose of this chapter is to treat the savings originating in the private sector. Savings of the other two sectors, the public sector and the "rest of the world" are treated in the next two chapters. Below are brief explanations and definitions of the terms which are repeatedly used throughout the study. The main two points that are to be defined right at the beginning are the meaning of saving and the meaning of sources of saving.

The Meaning of Saving

In order to realize investment, in the sense of increasing the gross capital of a nation, savings must be incurred. In other words a part of the national income must be withheld from the stream of current consumption. Borrowing from abroad implies drawing on future savings. National assets abroad imply former saving but foreign grants relieve a country from an equivalent saving from its own resources. Along those lines realized investment therefore always has a saving counterpart. Thus the term "realized saving" is used ^{here} to mean that there is an equivalent

realized investment. It is to be pointed out however that realized savings are not necessarily equal to planned saving. In fact it is a big responsibility of economic planning to make planned and realized savings (hence realized investment) equal.

The term "investment" is used to mean expenditures on new fixed capital goods and inventories. It is the additional physical goods on the national balance sheet between two dates.

In view of the above explanation, the investments which were actually realized should have had a saving counterpart. Fortunately for Egypt and for the rest of the poor developing countries, the counterpart is not confined to present saving, there is a chance to draw on previous saving and on future saving, by drawing their liquid foreign assets (previous saving) and by obtaining foreign loans (future saving.) The merits of the latter source is that if foreign loans were properly applied to really economic projects, these projects can settle the loans without then becoming a burden to the rest of the economy. This however depends on the terms of the loans and on the productivity of the projects.

Accordingly this chapter and the next two are to find out how much savings were realized from current income and how much funds were received from the "rest of the world". The quantity of savings could have been computed by deducting "rest of the world" from realized investments, but the manner in which such savings were realized remains the major point. The study of savings, which may or may not be realized, is of great

significance to planned economy. Knowing the share in total savings of each source compared to the capacity of this source helps planning to realize greater savings from sources with the greater capacity. The plan should start on assumptions based on experience.

Sources of Saving

A source of saving is also a source of financing. Sources of financing are divided into domestic and foreign sources. Financing from foreign sources is the contribution of the "rest of the world" to the financing of capital formation, that contribution which is equivalent to the deficit in the balance of payments, on current accounts. This source will be the subject of Chapter IV.

The contribution of the domestic source to development financing is equivalent to the savings realized from internal resources. Domestic savings are divided into government and private savings. Government savings will be discussed fully in the next chapter. Private savings come from three sources: Insurance Funds savings, Personal savings, and Business savings. The share of each source in aggregate savings is revealed in Table VII.

Savings of insurance funds are determined by the net increase in the reserves of the insurance companies and of the social insurance schemes. Those reserves are real savings be-

cause they are the excess of premiums received by the insurance funds over and above payments by the funds to their beneficiaries. Table VIII shows the savings of those funds over nine years.

TABLE VII

DISTRIBUTION OF SAVINGS AMONG SECTORS OVER SIX YEARS

in LE. million

	1953	1954	1955	1956	1957*	1958*	To- Tal	Aver- age
<u>A. Private Sector</u>								
Personal Savings	59	82	71	71	43	49	375	62.5
Business Savings	25	26	38	38	23	37	187	31.-
Saving Funds	8	9	8	10	13	15	63	10.5
Total	92	117	117	121	86	101	625	104
<u>B. Government Saving</u>	17	14	7	12	30	37	117	19.5
<u>C. Rest of the World</u>	8	---	35	32	34	33	142	23.5
Grand Total	117	131	159	163	143	171	884	147
A :- Grand Total Per cent	80	89	74	75	60	59		78

Source: based on data by Dr. Samir Amin, "Development Financing", Egypte Contemporaine, v.50, p.14, (July, 1959) (Arabic).

* the last two years are provisional.

Personal savings are the excess of personal disposable income over personal consumption, and are equivalent to the self-financing of the household sector plus the loans which it extends to other sectors. The development of personal savings over a period of six years is shown in Table VII.

"Net" business savings are those business profits that are retained, i.e. not distributed to shareholders, while gross savings include depreciation reserves as well. Business "profit" usually, excludes depreciation.

It is to be mentioned at this stage that Dr. Amin's data¹ on savings were selected to serve the purpose of long-run analysis. It is not the most accurate but the most comprehensive. His data covered a number of consecutive years large enough for the purpose of trend analysis. Besides, his data included all sectors that shared in the aggregate saving, a merit not credited to any other accessible source. Furthermore it was the only accessible source which could furnish data on personal savings. However, all other data that were available were used in the text to check on the data of Dr. Amin. Dr. Amin accumulated his data on savings by saving funds, using as his primary source the statements of those institutions. The question of accuracy in this respect, does not come up.

Business savings are also collected from statements of Joint Stock Companies, and other business firms registered in the Chambers of Commerce and Industry. Other business firms not registered are relatively of little significance as can be seen in the section on business savings, later in this chapter. In

1. Samir Amin, "Development Financing in South U.A.R.", Egypte Contemporaine, v.50, pp.6-26, (July,1959), (in Arabic).

the case of retained profits of these companies Dr. Amin's data and the other sources, presented some differences. These differences, apart from the question of depreciation are attributed to the difficulty of distinguishing the personal sector from the numerous small business firms. (Dr. Amin used "net" saving, excluding depreciation reserves.) It was for this same reason that Dr. Amin attributed to this source, as in Table VII, the residue after computing all other sources, private, and public. In his book "Statistics of General Equilibrium"¹ Dr. Amin uses another method. He contributes one-third of the increase in time and current deposits with all banks plus post office savings to this sector and adds individual's investments in bonds and buildings to find the total uses of this sector. To obtain the net savings of the sector he deducts the increase in liabilities of the sector to mortgage banks and to other long-term creditors. He has applied this method to one year only, 1957.

Before shifting to the details about each group of the private sector it is interesting to find out the significance of the private sector as one group.

From Table VII some initial conclusions may be drawn. The ratio of private saving declined from 89 per cent in 1954 to 59 per cent in 1958. It has declined in absolute amounts

1. p.200.

too but at a lower rate. Total savings continued to increase except in 1957 as has been shown also in the previous chapter in the case of investment. The role of the government and the rest of the world as sources of development financing are ever increasing as will be explained in greater detail in later chapters.

A. SAVINGS BY INSURANCE FUNDS

Table VIII reveals the trend in the savings of insurance companies and social insurance schemes. The figures in Table VIII represent the annual increase in the reserves of insurance companies and the two social insurance funds.

There was a continuous rise in the annual savings of these three organizations. The savings in 1960 were five times greater than those of 1952.

Savings accumulating with insurance companies remained constant up till 1960 when they rose by 250 per cent. Most probably, that was due to the Egyptianization of insurance business in accordance with the laws enacted in 1957 following the Suez Canal crisis. Before this year only eleven, out of 131, companies were Egyptian. Also, in October 1959 a law was enacted exempting life insurance premiums from income tax, by allowing the insured to deduct from his taxable income the amount of the premium.¹

1. "Business Legislation", Egypte Industrielle, v.35, p.81, (November, 1959), (in Arabic).

The practice of insuring one's life develops by educational and administrative efforts. The great educational efforts by all publishing and educational bodies, and the efforts of administration may have contributed to the establishment of this habit.

TABLE VIII

ANNUAL INCREASE IN INSURANCE RESERVES

	1952	1953	1954	1955	1956	1957	1958	1959	1960
Insurance	3.5	3.5	3.5	3.5	3.5	3.5	3.3	3.8	9.3
Employees in- surance fund	0.9	4.2	5.6	4.3	6.-	8.1	12.3	12.3	9.8
Workers insura- nce fund	---	---	---	---	0.5	1.5	2.5	3.1	3.2
	4.4	7.7	9.1	7.8	10.-	13.1	18.1	19.2	22.3

Sources: 1952-1957; Samir Amin, "Development Financing", Egypte Contemporaine, v.50, p.13, (July,1959), (in Arabic).

1958-1960; Egypte Industrielle, v.37, p.15, (February,1961), (in Arabic).

Greater saving accumulation was due to the two social insurance funds of workers and of employees. The employees insurance and pensions fund was established before 1952 while the insurance fund for workers was established by Law No.419, in 1955. Law stipulated that each of the worker and employer pay 5 per cent on the earned wage, to be retained with the Social Insurance Fund. Another two per cent was to be paid by the employer alone to insure

workers against disability and old age. The law covered 750,000 workers employed by 1420 firms. All were to be covered by this scheme before the end of 1961. The initial estimates were that the savings by this scheme should reach 12 million pounds in 1961.¹ This source of financing is expected to develop further when social insurance coverage applies to new employees, with the same or with new firm.* Social insurance will also cover gradually a greater number of urban workers. New laws to cover workers in other sectors of the economy are anticipated.

The third saving fund is that of government employees. Though this scheme was established before 1952, it developed greatly to add new benefits and accumulated greater funds. This fund is expected to develop further by enhancing the role of the government in direct participation in business. The greater the number of government employees the greater the funds saved by this scheme. According to the table above, the net savings of this fund were less than one million in 1952, and more than LE. 12 million in 1959.

The flow charts prepared by Dr. Amin² for the year 1957, show that the savings with the saving funds and with insurance companies were invested in bonds and other long-term loans.

1. Speeches of President and Ministers to National Assembly? pp.771-866, Cairo: 1958.

2. Statistics of Equilibrium, Appendix 2, Cairo:1959 (Arabic).

* Decision 92 of 1959 extended coverage to all urban business, except those employing less than 5 employees and having no machines and paying less than LE. 20 tax, per annum. Egypte Industrielle, p.91, (November,1959).

Employees insurance fund bought LE. 1.7 million long-term securities to be used by the School Building Organization. It invested LE. 3.6 million in government and business bonds and also one million in hire-purchase loans. Its total savings that year were LE. 8.1 million according to Table VIII.

In 1957 the workers insurance fund invested its savings which amounted to LE. 1.5 million, in long-term securities except for LE. 100,000 which were deposited in banks.

Out of their accumulating reserve the insurance companies invested LE. 2.6 million in long-term securities, LE. 500,000 in fixed assets and the rest in bank deposits. All three insurance entities are net sources of financing and as to themselves they invest very little. The significance of this source of financing is that it provides long-term financing applicable to fixed assets and therefore it may be regarded as the best source for new projects. In 1957, their total long-term investments amounted to LE. 10 million. These funds are subject to rules and laws governing all banks and credit institutions. They have to present regular statements including every particular transaction that exceeds LE. 5,000.

B. PERSONAL SAVINGS

1. Magnitude Of Saving By The Household Sector

Table VII shows that savings originating in the household

sector have been declining. Many are the factors which account for this decline. First, the savings with insurance funds were increasing and the contribution by members of this sector to insurance funds reduced their capacity to save. It is believed that they reduced the every day worries which usually make saving much an urgent precaution. The rate of consumption too continued to rise up till 1958, as will be shown later in this chapter. It is also believed that the rapid rise in prices in 1956 and 1957 has had a great effect on the savings of this sector.* While the public saving increased from LE. 12 million in 1956 to LE. 30 million in 1957, the personal savings of the household sector dropped from LE. 71 million to LE. 43 million. The high rate of business saving during certain years such as 1955, 1956, and 1958 affected the size of personal disposable income and consequently the saving capacity of the household sector.

The household sector is a net source of financing since its savings are greater than its self-financed investments. This is another source for businessmen and government to utilize. Dr. Samir Amin estimated that the whole increase in deposits with the Post Office Bank and one-third of all other time and current deposits are personal savings. Such savings amounted to LE. 17 million in 1957. Other LE. 5 million of personal savings were invested in stocks and bonds, the rest was directly invested

*. Prices have not dropped after the rise in 1956-57 as will be shown in Chapter 5.

especially in buildings.¹

Since savings with the post office banks reflect savings by the household sector, a follow-up of these saving throws additional light on this problem. The increase in post office savings in each of the six years, 1955-1960, consecutively was, in LE. million, as follows: 0.8, 1.4, 4.9, 3.3, 3.8, and 11.8.² The trend is towards greater accumulation of savings with the post office. The great rise in these savings in 1960 is an indication of fruitfulness of the efforts paid in order to increase household savings. Post office branches receiving savings were spread and made accessible even to rural population. Among the multiple services of the 250 collective units established all over rural areas, was the task of running post office saving branches. The cumulative saving over the six years was LE. 21 million. The "account of sources and uses" of this fund shows an investment in bond and long-term loans of LE. 4 million out of the LE. 4.9 million net receipts in 1957.³

Another indicator of personal savings is the saving accounts and time deposits with commercial banks. All private

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1. Samir Amin, Statistics of Equilibrium, pp.198-200, and appendix I, Cairo: 1959 (Arabic).
 2. Federation of Industries, Yearbook, 1955/60, p.20 (French) and Egypte Industrielle, v.37, p.15, (Feb. 1961) (Arabic).
 3. Statistics of Equilibrium, Appendix 2, Cairo: 1959 (Arabic).

savings and deposits with commercial banks were divided between the household sector and the business sector in the ratio of 1 to 2 in an attempt* by Dr. S. Amin to compute personal savings.¹ It is nevertheless believed that saving accounts are much more of a household contribution. Business entities are more likely to keep the greatest part of their liquid assets in the form of current deposits. Saving deposits in each of the six years, 1955-60, consecutively, increased as follows, in LE. million: 1.6, 0.4, 3.8, 11.6, 15, and 10. There was a great increase in time and saving deposits since 1957 up till 1959. There was a decline in deposits in 1960.

Personal savings are affected by the measures taken to reduce distribution of business dividends and by the increased contribution to social insurance schemes. Both ways reduced disposable income. The second way was discussed in the section on saving funds, the first will be discussed in the section on business saving. Other measures taken by the state to reduce disposable income and to reduce the consumed part of it are treated in the next section.

2. Measures To Reduce Personal Disposable Income

One of the measures taken was direct taxation. The rates

1. Samir Amin, Statistics of Equilibrium, p.198, Cairo: 1959, (Arabic).

* However, this was not the way that Dr. Amin used to find personal savings presented in Table VII, as was mentioned before.

of taxation on income were slightly increased. Before July 1961, the income tax rates themselves were not a significant factor in reducing disposable income. Instead the management of tax collection has had the greatest effect. Less taxable income could escape tax payment because of the control and management. Of greater effect on income received by persons was the government retention of profits of certain groups such as the Royal Family. The property of this family was confiscated, and Awkaf property was turned to yield profit to the State instead of profit to individuals. Nationalization of foreign property in 1957 affected the rest of the world but not the disposable income as will be explained in the next chapter. Not until July 1961 did nationalization turn domestic business profits of perceptible size to the State. The subject of taxation and government profits from property will be discussed in greater detail in the next chapter.

Another factor that affected real disposable income was the sudden rise in prices in 1956. The reduction in the real purchasing power beside the drop in the real national income itself accounted for the drop in savings of both personal and business sectors as can be seen in Table VII above.

The other two ways to reduce disposable income mentioned before, were the social insurance schemes and the retention of profits with business firms. The problem of business savings is treated in the next part of this chapter.

A counterpart to the insurance schemes in the urban area are the Cooperatives, Agrarian Reform, and the Popular Building Organization. Membership in cooperatives was compulsory and all agrarian population receiving new land as a result to the Land Reform of 1952, and its amendment of July 1961 were required to join. Membership in agrarian cooperatives amounted to 200,000 in 1959. Their cumulating profits amounting to LE. 867,000¹ were retained. Members thought more of the services rendered to them at reduced costs more than they did the cooperative profit. Some of the cooperatives deal in marketing, in residential buildings, in rural industries, etc..... The Petroleum Distribution cooperative earned net profits, LE. 845,000 in the period 1953-1956. Its members were about 17,000.²

The subscription of the members to the cooperatives, and the installments they pay on land or residential buildings bought from the Agrarian Reform Authority, or from the Popular Building Organization reduce consumption from the disposable income. The agrarian reform received installments in each of the five years 1953-1957, in LE. million: 2.8, 2.8, 6.4, 6.1, and 6.8, consecutively. Its net savings in each of the same years consecutively were: 2.2, 2.4, 2.1 0.8, and 1.9.³

1. Information Service, The Union During Three Years, p.6, Cairo: 1961 (Arabic).

2. Information Service, Yearbook, 1959, p.501, Cairo: 1959, (Arabic).

3. S. Amin, Statistics of Equilibrium, p.180, Cairo: 1959.

3. Measures to Increase Savings From Disposable Income

The greater effort after 1952, and before 1961, was directed toward increasing voluntary savings. Two approaches were followed to realize personal saving. One was the way to attract saving for the sake of return from its investment, and the other was to affect consumption habits. In other words, one attempt was to increase the marginal utility of investment, and the other to reduce the marginal propensity to consume.

a- To attract Savings

Protection and support measures used by government, and mentioned in previous chapter raised profits of business enterprise from about 10 per cent in 1952 to 17 per cent in 1958, as shall be explained in the next section on business. The re-organization of the stock market was another measure to facilitate and encourage investments in bonds and stock of companies. The general index of share prices has risen from 57 in 1953 to 70.8 in 1954 and to 77.1 in 1958.¹ Industrial shares index has risen from 58 to 76.7 to 114.5 over the same years. The capital of companies increased from LE. 192 million in 1953 to LE. 286 million in 1958 to 336 million in 1960. The great rise in investment in business is not entirely contributed to the indivi-

1. National Bank of Egypt, Economic Bulletin, v.XIII, p.223 (1960).

duals. In 1956 out of LE. 22.2 million LE. 13 million was contributed by the public sector, later this ratio increased too. But in the five years, 1953-57, the share of individuals was 64 per cent of the addition to capital of companies. This share was about LE. 50 million.

To encourage small subscriptions, legislation reduced the minimum value of stocks to LE. 2 and likewise the minimum capital for limited companies was reduced to LE. 10,000 in order to facilitate company organization. Limitations on the share of the boards of directors were enforced, in addition to some other measures to protect small investments. Other facilities to encourage investment were mentioned in the previous chapter.

The greater contribution of personal saving was to the construction of buildings which has increased from LE. 40 million in 1954 to LE. 59 million in 1958 as Table II shows. This was private saving to which the household sector contributed much more than the business sector itself. Thus, the Household Sector in Table VII includes the self-financed part of the buildings.¹ The greater economic activities created demand for residential buildings, a familiar and popular type of investment. The household sector responded to the said demand. It was only in

1. S. Amin, "Development Financing in South U.A.R.", Egypte Contemporaine, p.15, July 1959.

1958 that the government discouraged the luxurious type of buildings, and licences were issued to build the popular type which costs less. A decline in this type of investment appeared in 1959. A greater share of residential building construction was assumed by cooperatives and by public organizations. New constructions by the Ministry of "Awkaf" were let for public use at nominal rent. Cooperatives specialized in building construction, and the Public Organization for Popular Buildings sold their buildings to low-income groups on installment basis. Installments paid were the savings from the disposable income of those groups, similar to installments paid by new landowners. The economic advantage which this developing institutional investment over free individual construction is manifested in two ways. First, costs are less per unit due to quality and large scale economies. Second, savings are attracted from low-income groups that have a high propensity to consume. Besides, these institutions retain all their profits.

In order to channel savings of the household sector which exceed what the sector can invest by itself, saving advertisement are used and easy and least expensive access to saving has been provided. The spread of post office saving branches has already been mentioned.

In underdeveloped countries, especially in the rural areas, the acquaintance of the public with the saving institu-

tions, beside the interest given, affect the hoarding trend.* The creditor rate of interest for commercial banks is fixed at 1 1/4 per cent allowed to increase up to 3 per cent on time deposits and to 2 1/2 per cent on saving deposits.¹ The development of saving and time deposits was already illustrated in figures.

b- To reduce the Rate of Consumption

Early in the period namely in 1952 and 1953, the New Regime resorted to redistribution of income in order to reduce inequality. The Agrarian Reform Acts reduced rent, the main cost for agrarian population. In urban areas the wages of the lowest wage-level workers were fixed at a minimum of 25 piasters per day for an unskilled worker. Though the later procedure was not fully applied especially in the rural area where government control is less effective the gradual application of law increased gradually the income at the disposal of low-income groups. However small the increment is in abstract terms, it was considerable to the hundreds of thousands whose wages were below 10 piasters a day. In the absence of the above-mentioned measures to tap the additional income during the earlier part of the period, the propensity to consume was definitely rising.

1. Economic Bulletin, v.12, p.150, (1959).

* Hoarding in the strict sense, i.e. savings in the form of banknote and gold.

It was thought that, in the absence of data on personal disposable income, the national income itself could be used as a base to judge the change in the rate of consumption. The International Financial Statistics bulletin presented data on private consumption during the years 1953-1956.¹ During the four years consecutively, the private consumption was, LE. 697 million, LE. 763 million, LE. 832 million, and LE. 885 million. The rate of increase in consumption was about 9 per cent per year. This was the time national income was rising at 5 per cent per annum according to the same source. This explains the declining trend in private individual saving. Table VII, shows that from LE. 82 million in 1954 it declined to LE. 71 million in 1956 to LE. 41 million in 1957 to LE. 49 million in 1958. There was a little rise in 1958 but the level of personal saving was still far below the level in 1954. Government saving does not explain the trend since it was also declining. Business saving was constant during 1955 and 1956 and dividend distribution was not seriously checked. Disposable income was not reduced because direct taxes were practically unchanged. The only variable that could possibly explain the declining personal saving was the rate of consumption which has risen by 9 per cent per year.

1. v.XV, p.110, (March, 1962).

The greatest tangible procedure carried by the authorities to reduce consumption from personal disposable income was by restricting the supply of unnecessary goods and services while controlling prices. The foreign-exchange-budget method used, after the First Industrialization Plan of 1957, reserved foreign currency earnings to necessary food supplies and to the requirements of development projects. Travel abroad for pleasure was reduced and finally stopped. Precious metals (excluding monetary gold) that constituted 4.8 per cent of the total imports in 1951 were completely restricted. Imported drinks were heavily taxed and most types were completely restricted. Imports of consumption-goods category dropped in 1955 to LE. 44.5 million from LE. 94.6 million in 1952.¹ Among the remaining imported supplies are wheat, tea, and coffee. Even those essentials were not allowed to enter the market at high cost. A popular loaf of bread was devised to insure both low cost and nourishment value. Since essentials could not be eliminated, low-cost categories were selected. The foreign-exchange-budget gave priority to import of omnibus to sedan cars, diesel to benzine engines, low consumption to high consumption cars.

Restriction of supply was not confined to foreign products. Internal products were directed as to allow no excess of

1. Federation of the Chambers of Commerce, Egyptian Economy, 1952-57, p.172, Cairo: 1958.

one item in the market. Licences were offered to producers according to a priority schedule because resources were to be directed to the projects with the higher social or/and economic utility. Among these projects are capital equipment production, power and raw materials extraction that compete for resources with consumption production projects.

The last resort to insure low consumption was rationing. The main consumption commodities were and are still rationed. Rations allowed per capita are far lower than the general consumption. These commodities include rice, sugar, edible oil, and kerosene. When shortage is expected other commodities may be added to the rationed list. However, there is no evidence that private consumption has been seriously reduced or in other words, that private saving has considerably increased. Funds can always find a way to consumption whenever the holder is not interested in saving. The resort of the government to a highly progressive taxation system in July 1961 suggests that the response of the private sector to save was not commensurate with the financing requirements of the Five-Year Plan. The public sector finally selected to reduce the personal disposable income and to turn the part collected to a government saving instead of leaving it to the unpredictable choice of individuals. The next chapter treating public saving will illustrate further the relation between the government saving and the public saving.

C. BUSINESS SAVINGS

Gross business saving is equivalent to retained profits plus depreciation reserves. Business profit is the net income after subtracting expenses, therefore, excludes depreciation. Net business saving is determined by the profit and the rate of profit distributed. Distribution of profit depends on the decisions of the individual shareholders, and on the legislation related to this distribution. This section is an attempt to find out the size of business profit and what affects the decisions of business owners to retain or to distribute a part of the profit. The size of depreciation reserves, which is very often greater than the size of retained profits, will be also treated in this section.

1. The Magnitude And Structure Of Business Saving

In 1955 a study was carried by the National Bank covering a sample including 50 per cent of paid-up capital of joint stock companies.¹ One of the findings of the study was that profits of the companies represented were LE. 5.4 million and LE. 4.5 million in the years 1952 and 1953 respectively. The ratio of profits to capital was 10.7 per cent and 8.9 per cent in the two respective years. This result shows the business profits during the earlier

1. Economic Bulletin, v.8, p.101, (1955).

part of the period. Another study applied to a larger number of joint stock companies was made by the Bank in 1959.¹ The sample represented 53 per cent of paid-up capital of all joint stock companies. Net profits in 1957 and 1958 were LE. 17.4 million and 17.8 million respectively. Paid-up capital of companies represented was LE. 103 million and LE. 113 million at the end of the respective years. The corresponding return to capital, therefore, was 17 per cent and 15 per cent.

This high rate of profit does not portray the accurate, real profit of functioning enterprise, because four large companies with large capital that were not earning any profit were included in the sample. Among these was the Iron and Steel factory with a capital of LE. 19 million (Raised later to 23 million).

The capital of these joint stock companies has more than doubled between the two years, 1952 and 1958. The rate of profit has increased also from 10.7 per cent to 15 per cent. Reserves of companies in the sample increased during 1952/53 by LE. 865,000.² In 1957/58 provisions and reserves, other than depreciation reserve, increased by LE. 5.2 million. A statement of sources and uses of funds' of all joint stock companies could be drafted by dividing all figures by the 53 per cent which is the size of the 1958 sample. Total paid-up capital of the joint stock companies could accordingly, add up to LE. 213 million as of the end of 1958.

1. Ibid, v.XII, pp.85-100, (1959).

2. Ibid, v.8, p.102.

Another study was made by the Committee on National Planning for the earlier years 1951-1955. The retained profits of joint stock companies, according to this study, were in the five consecutive years in LE. million, as follows: +19.6, -2, +10.5, +38.7, and +30.7.¹ It appears that retained profits are not positively related to the rate of profit. In the year 1952 the rate of profit was greater than in 1953, but the retained profits were negative in 1952 and LE. 10.5 million in 1953. Also in 1957 profits were about 17 per cent of paid-up capital. During that year savings dropped to a very low level. The following year net savings increased but the rate of profit was 2 per cent less. Distribution of profits depends on the decisions of owners which are nonetheless unpredictable.

According to Table IX, the joint stock companies used LE. 27.5 million of their own resources to apply to an additional investment in gross fixed assets amounting to LE. 31 million. The excess of investment in fixed assets over internal financing amounted to only LE. 3.5 million. The increase in the companies' capital and fixed liabilities was far greater than this excess. In other words, the companies financed their current assets from fixed liabilities. This increased the liquidity position of the companies and reduced the necessity of retaining profits next year.

1. Mohammad Sami Mohammad, The Role of Banking System in Mobilizing Private Savings, Appendix I, Cairo: 1957.

TABLE IX

STATEMENT OF SOURCES AND USES OF FUNDS BY JOINT STOCK COMPANIES
DURING THE YEAR 1957/58.

in LE. million

Uses		Sources	
Gross Fixed Capital Formation	31.-	<u>Self-Financing</u>	
Inventories	<u>23</u>	Profits	32.-
Total Physical Assets	54.-	Less: Dividends	<u>24.2</u>
Monetary Assets and Securities	12.2	Retained Profit	7.8
		Less: Withdrawals from Reserves	<u>2.-</u>
			5.8
		Depreciation Reserve	17.5
		Provisions	<u>4.2</u>
		Total of Self-Financing	27.5
		Increase in Capital	18.2
		Long-term Liabilities	<u>5.8</u>
		Plus: Short-term Facilities	14.7
	<u>66.2</u>		<u>66.2</u>

Source: based on National Bank of Egypt, Economic Bulletin, v.XII, pp.85-100, (1959).

Some conclusions may be drawn based on Table IX. Net savings of joint stock companies were only 10 million. The other LE. 17.5 million were from depreciation reserves. The retained profits are 30 per cent of total net profits. Profits were perceptably high amounting to 15 per cent of paid-up capital. Dividends distributed plus reserves withdrawn were 12 per cent of capital.

With regard to the total gross savings of business com-

panies the same findings can be equally applicable to those companies that are not joint stock. Total capital of companies limited and unlimited amounted to LE. 286 million at the end of 1958.¹ Since the joint stock companies' capital, as mentioned above, was LE. 213 million the remaining capital amounting to LE. 73 million belonged to other companies. Assuming that these companies retain profits only in the same ratio to their capital, the total self-financing of gross saving of companies amounts to LE. 37 million. This is the share of the business firms that register their capital with official departments. This figure is exactly equal to the figure presented by Dr. Samir Amin as Table VII above shows. But Dr. Amin's data excludes depreciation and includes savings of small business that are not registered. The two data are not comparable.

Table X combines Mr. Mohammad's data which was issued by the Committee on National Planning for the years 1951-1955, and that data already presented for the year 1958 based on the National Bank study. With regard to the years 1956 and 1957, Table VII may be used only with some reservation.

Profits retained were lowest in 1952 and highest in 1954. Though their gross fixed investment was LE. 25 million in 1952 and the profits about 10 per cent of the paid-up capital, the retained profits were negative. A great part of the fixed assets was financed by current loans. In 1951 it was just the opposite.

1. National Bank, Economic Bulletin, Table 32, v.XIV, No.3, (1961).

TABLE X

— funds of
STATEMENT OF SOURCES AND USES OF JOINT STOCK COMPANIES* IN LE.
MILLION

Sources	1951	1952	1953	1954	1955	1958**
<u>Internal Financing:</u>						
1-Net Savings	19.6	-2	10.5	38.7	30.7	10
2-Gross Savings	28.6	13.1	17.2	45.6	49.5	27.5
<u>Outside Financing:</u>						
3-Capital Financing	14	7.7	2.5	6.3	13.2	24
Total 2 + 3	42.6	20.8	19.7	51.9	62.7	51.5
4-Net Current Liabilities	----	10.9	----	----	----	2.5
<u>Uses</u>						
5-Gross Fixed Capital	3.1	25.4	8.4	30.7	36.6	31.-
6-Inventories	9.8	6.3	6.6	-14.1	7.4	23
7-Net Current Assets	29.7	----	4.7	35.3	18.7	----
	<u>42.6</u>	<u>31.7</u>	<u>19.7</u>	<u>51.9</u>	<u>62.7</u>	<u>54.-</u>

Source: based on Mohammad Sami Mohammad, The Role of Banking in Mobilization of Domestic Saving, Appendix I, Cairo: 1957.

** based on: National Bank, Economic Bulletin, v.XII, pp.85-100, (1959).

Internal saving was much while investment in fixed assets was little, thus causing the companies to invest in current assets. Even capital contributions in 1951 were not used to create fixed

* Net Saving of other companies were estimated, by the same source, at LE. 2.7 million, in 1956. Depreciation reserves were estimated at LE. 3.3 million.

capital. In 1954 a great reduction in inventories made it possible to invest in other current assets. In 1953 net savings rose while fixed assets dropped. In 1954 and 1955 the greater rise in savings of companies was associated with the increase in investment in fixed assets. The only relation that could be deduced from this data is that the savings of one year are decided in the light of next year's investment especially in fixed assets. A positive relation between savings and the rise in profits does not seem to exist. Another source of internal financing was used and that was the reduction in current assets. The fluctuations in the size of inventories and other current assets and current liabilities were deep and frequent. Capital Financing mainly explains new establishments issuing stock, but does not bear any direct relation to the savings of older companies. Capital stock is the only item that continued to decline up till 1953 when it rose again. No decline has been observed ever since. Much of this regular rise is due to the government's encouragement of particular industries and to the direct subscription of public organizations. It can be concluded that internal savings were irregular. The rise in profits, only when it suggested further rise, had a positive effect on internal savings. In the years 1954, 1955, and 1956 private business was reaping the fruits of the government's protection and support. Textile industry expanded by means of internal financing. The year 1956 was the last to witness sizeable self-financing, while

1957 was a year of decline of investment from all sources. The year 1958 offered the final test for business conduct. It however, carried lucrative profits, as was mentioned earlier. New projects were undertaken under government protection and promise. LE. 24 million new capital, was covered mainly by government direct subscription and stimulation. In that same year only LE. 10 million were retained, for net investment. This was less than one-third of the self-financing of business companies in 1955. In the absence of high and progressive taxation the government failed to insure autonomous financing by the large firms. In the year 1958 the Five-Year Industrialization Plan was inaugurated. The plan depended on business and private savings but the response was not encouraging. A reasonably high rate of certainty is required in the case of development planning. Business savings which constitute a large source of financing, are neither certain nor predictable. The profit distribution in 1958 was large enough to raise the price index of stock as was mentioned before. The high rate of profit distributed diverted savings from possible investments in new enterprise to speculation on old stock. Development planning expects business to invest in new projects in the absence of internal business expansion. Early in 1959 the government began a series of decrees to insure greater savings by business and individuals. The nationalization and high progressive taxation Laws of July 1961 are part of this series.

2. Measures To Secure Business Savings

There was an old law that required business to retain a so-called legal reserve. Such a measure was meant to strengthen the position of capital and to check the desire of shareholders to cash profits. However, many of the old prosperous business firms have been able to accumulate legal reserves in accordance with this law. Capital reserves of companies in the National Bank sample amounted to LE. 61.7 million by the end of 1958. This was equivalent to 54 per cent of the paid-up capital. Most of these companies, therefore, were exempted from the legal reserve terms.

Another law enacted in 1952 made a compensation for dismissed workers compulsory. An amendment to this law was decided in 1959. Reserves for compensation were to be earmarked annually. The compensation was almost doubled. It was 10 days pay for each of the first five years of service, and 15 days per year thereafter. The amendment made the compensation 15 days and one month respectively.¹ This had nothing to do with the contribution of companies to social insurance funds. Compensation reserves alone were supposed to add up to profit retention 4-8 per cent of the total payroll of all business firms, companies or otherwise.

1. "Business Legislation", Egypte Industrielle, v.36, p.21, (February,1960).

Other laws aiming at profit retention were issued during 1959 and 1960, after the government's disapproval of the large rate of profits distributed in 1958. Upon examining Table IX, distribution from profits plus withdrawals from former reserves amounted to LE. 26.2 million out of a LE. 32 million, profits. The ratio was 83 per cent while net saving amounted to 17 per cent. The ratio of distributed profit to paid-up capital exceeded 12 per cent. The taxes were not high enough nor progressive enough to check distribution. It seems that the government was not yet convinced to the effectiveness of resorting to taxes to finance projects. Other laws and decisions were enacted in 1959 in order to change the trend of dividend distribution and withdrawal of former reserves.

On January 11, 1959 a decree law was issued providing that companies earmark 5 per cent of their net profits for the purpose of purchasing government bonds, after distribution of dividends not less than 5 per cent. Besides, dividends distributed in 1959 were not allowed to exceed the 1958 dividends by more the 10 per cent, unless there was a reason believed convincing to the Ministry of Economics. The bond, or treasury bills held were not to be disposed of except upon the approval of the Minister.¹

Before the progressive income tax and nationalization laws of July 1961, one decision which affected the dividend

1. Middle East Economist, v. II, pp. 11-12 (January, 1959).

distribution greatly was taken. It was the law which gave the workers 25 per cent of the profits of business companies. Out of the 25 per cent only 10 per cent were to be distributed to its beneficiaries. The remaining 15 per cent were to be retained with business. Like other insurance funds these retained funds could be invested in development bonds.

The public did not respond favorably to these laws.¹ The response was reflected on stock price index which dropped from 77.1, by end of 1958 to 70.1, end of 1959 to 55 by the end of 1960. All categories of companies' shares dropped without exception. The actual effect on profit retention was not reported but stock prices respond to expectations of dividend distribution. The large dividend distribution in 1958 was responsible for the high level which the price index reached that year.

The most effective weapon that secured autonomous financing by business companies was actually the direct holding of the public sector of business entities.

In December 1959, the total registered capital of companies was about LE. 300 million.² The Economic Development Organization, a public entity, owned a share amounting to LE. 63.5 million.³ The Misr Bank, nationalized early in 1960, held about

1. Ibid

2. Economic Bulletin, v.XIV, Table 35, No.3 (1961).

3. Middle East Economist, v.60, p.43, (January,1960).

LE. 20 million worth of capital in these companies. The two Public Organizations held more than 50 per cent of industrial and banking capital. Their control was far greater than their shares because their shares were mainly holding shares in various companies. Misr Bank alone handled 40 per cent of credit facilities in the country and 20 per cent of industries as of end of 1959.¹ The share of E.D.O. in industries was LE. 45 million when all industrial registered capital was LE. 101.3 million.

The profits of the economic organization in 1957 and 1958 were slight. The reason goes back to the many new projects that were not yielding actually profit such as the huge Iron and Steel Factory, the Fertilizers Factory at Aswan, and others. The E.D.O's share in companies' dividends are included under business saving in Table VIII. This sector has not included the Suez Canal, the Electric Plants, the Military Factories nor the Oil Business. Profits of the latter firms are included in Government Saving in Table VII.

3. The Future Of Savings Structure

Two sources of private saving are expected to continue to accumulate greater savings: The Insurance Funds and Business. Savings of both are manageable because of the government control.

1. Middle East Economist, v.60, p.43, (January,1960).

Saving by individuals depends on disposable income and on the propensity to consume. The first is affected by the managed increase in retention by business and insurance schemes. But the changes in disposable income may be partly offset by the size of expenditure and the rise of total national income. Even the affect of nationalization measures on disposable income is alleviated by the generous compensation which the government gave to the Nationalized entities. The National Bank and Misr Bank were given government bonds bearing 5 per cent interest on the market value of the stock nationalized and not only on paid-up capital. As has been mentioned earlier reserves cumulating were 54 per cent of the paid-up capital in all companies. That is to say, that while personal disposable income lost a portion amounting to about 10 per cent on paid-up capital, it received about 7 1/2 per cent. Companies other than the two large Banks, that were nationalized received 4 per cent bonds. The value of the bonds is also equal to the market value of the stock which usually accounts for the capital surplus beside the paid-up capital. By buying these entities the government insured certain and predictable savings, two qualities believed essential to successful planning. Of greater importance in the case of the disposable income than nationalization is the rise in taxation rates. The same measure is supposed to affect the distribution of dividends because retained profits escape the high tax on personal income.

TABLE XI

PLANNED SAVINGS, BY SECTOR, DURING THE FIVE-YEARS, 1960-1965

in LE. million

<u>Domestic Resources</u>	<u>Total</u>	<u>Average per Annum</u>	
1. Business Savings (Companies)	390	78	34 per cent
2. Budget Savings for Development	180	36	16 "
3. Suez Canal Net Reserve	145	29	12 "
4. Social and Private Insurance	130	26	11 "
5. Household Sector Savings	75	15	7 "
6. Municipalities' Self-financing	60	12	5 "
7. Utilization of Idle Resources	30	6	3 "
8. Others	140	28	12 "
Total	1150	230	100 per cent
Rest of the World	500	100	
	<u>1650</u>	<u>330</u>	

Source: Yearbook, 1961, pp.224-225, Cairo: Information Service, 1961.

The propensity to consume, may continue to be checked by all passive and active measures used including rationing. It is believed that the government has more experience and more effective tools to be able to manage the consumption tendencies.

The domestic sources of financing according to the Five-Year Plan outline the trends mentioned. Table XI shows the great rise in business savings expected, the rise in savings by social insurance funds and the decline in personal savings by the household sector.

Business companies' savings are estimated to account for

34 per cent of the total domestic savings. Together with those of the Suez Canal the rate rises to 46 per cent. A great part of the government budgets for development is also due to business activities by the public sector. By adding the first three items the estimate rises to 62 per cent. Social insurance and private insurance savings that were negligible in 1952 have risen to 11 per cent of total domestic savings, according to the Plan. Personal savings that were the highest single source¹ have dropped to a low rate namely 7 per cent.

The role of government vis-a-vis the ^{private} public sector, is gaining in importance. As was mentioned earlier the share of government in business companies was rising too. The nationalization of big enterprises and of the large shares of individuals in other enterprises made the public sector a larger shareholder, than the private sector. Therefore, the public sector is responsible for the greater share of the savings in item 1, Table X. The public sector holds sole responsibility in providing savings represented in Table XI by items 2, 3, 6, and 8. Social Insurance savings are also created by government legislation. Only item 5, the household's savings will have to be contributed by the Free will of individuals. Since this item is becoming insignificant the government will be practically responsible for all

1. See Table VII.

savings required to finance the development schemes. In other words, the State assumed the "duty" of development financing, in conformity with the Articles of the Constitution. The "rest of the world" which is another responsibility of the State shall provide about one-third of the financing required. The domestic sector will have to provide the other two-thirds, as shown in Table XI.

C H A P T E R I I I

P U B L I C S A V I N G

Introduction

The previous Chapter treated Private Savings including business self-financing. This chapter treats the Public Savings that were not included before. Due to the fact that the Public Sector owned shares in business firms, the savings treated in the present chapter exclude its share in the retained profits of business firms.

Government Savings are the surplus of public current receipts over current expenditures. Receipts are those collected without creating liability, they include all taxes and returns to the government from services and property but they do not include borrowed funds. Borrowed funds represent a source of funds for financing government investment but do not add to total savings. The excess of public investment over government saving is to be borrowed from private savings that were already treated in the previous chapter, or from foreign sources that shall be treated in the next chapter.

A. CURRENT EXPENDITURE AND THE BUDGETARY SURPLUS

1. Trends In Current Expenditure

There are two ways for the government to increase saving: a) to increase revenue; or/and b) to suppress current expenditures. Over the first two years the New Regime suppressed current-expenditure. The actual ordinary expenditure dropped from LE. 231.5 million in 1951/52, to LE. 208 million in 1952/53, and to LE. 200 million in 1953/54.¹ This was possible by reducing the cost of living subsidies and the allowance for the cost of living by LE. 13 million. But expenditures on national security and social and economic services increased rapidly thereafter, and were not checked before the year 1957/58.

Expenditures on national security have ~~been~~ rapidly risen from LE. 54.3 million in 1953/54 to LE. 93.3 million in 1956/57. Likewise expenditures by the Ministries of Education, Health, and other Social Services increased from LE. 87.3 million to LE. 104.4 million over the same ^{three} years. Total ordinary expenditures increased from LE. 200 million to LE. 280.5 million,² in the same three-year period. Revenue increased only at the same ratio.³ All this adds up to the fact that there was no actual

1. Chamber of Commerce, Egyptian Economy During 1952-57, p.193, Cairo: 1958, (in Arabic).

2. Ibid.

3. Ibid., p.195.

saving to apply to the development budgets. Budgeting for development started in 1953/54 and the size of the development budget has been growing ever since that time. The lack of any surplus in the ordinary budget forced the public sector to resort to borrowing by floating development bonds and treasury bills, as will be shown later in this chapter and also in the next chapter.

As from 1957/58 a change in the trend was noted. The rising trend in expenditures on defence and social services was checked. Fortunately, after the Suez Canal crisis there was no further urge to spend more on defence. For the first time defence and national security allocations dropped from LE. 93 million to LE. 90 million. Social services expenditures also dropped slightly. The revenue from customary sources continued to rise thus allowing for a perceptible surplus, for the first time in 1957/58. A year later the Suez Canal became a significant source of revenue.

It has just been mentioned that before 1957/58 there was no perceptible surplus from ordinary budget, to apply to the development budget. Yet, there were some allocations for "New Works" in the ordinary budget itself. All such allocations mentioned in Chapter III of the ordinary budget were turned to the development budget ever since the year 1960/61.¹

1. National Bank, Economic Bulletin, v.XIII, p.84, (1960).

Therefore, before 1960/61 the savings of the public sector were equivalent in amount to the expenditures of the various ministries from the allocations for "new works", plus the overall surplus, or minus the overall deficit in the ordinary budget. The trend of public savings is shown in the following Table, No.XII, as prepared by Dr. Samir Amin.

TABLE XII*

THE MAIN SOURCES OF GOVERNMENT INVESTMENTS OVER 7 YEARS 1953-59
in LE. million

	1953	'54	'55	'56	'57	'58	'59	To- tal	Aver- tal age
Self-Financing	15	12	5	10	28	35	35	140	20
<u>Borrowing: From</u>									
Public Buildings									
Organization	1	3	3	3	4	5	6	25	3.5
From Treasury	<u>16</u>	<u>29</u>	<u>42</u>	<u>43</u>	<u>28</u>	<u>23</u>	<u>53</u>	<u>234</u>	<u>33</u>
Total Investment	32	44	50	56	60	63	94	399	57

Source: Samir Amin, "Development Financing in South U.A.R." Egypte Contemporaine, v.50, p.13, (July,1959).

2. Budgetary Surplus

The total public investments in Table XII are not comparable to those in Table III. The data given here are in ca-

* Data on first four years are final; on the other years, provisional.

lendar years. By accounting for this factor the difference would remain considerable. The investments as per Table III, changed into 7 calendar years, would still be more by LE. 60 million. Also, it is believed that self-financing in Table XI includes "net" investment excluding depreciation as was the case with Dr. Amin's data on business self-financing. There was no written evidence to verify this belief. Table XII, does not include projects of municipalities, nor projects achieved by independent public authorities through credit facilities other than the treasury facilities. But all resort to the treasury by public organizations is included under "borrowing from Treasury." The data of Dr. Amin is the best available for trend study.

Public sectors' "self-financing", or saving, include self-financing of public organizations, but exclude the Economic Development Organization and shares in business companies that were included in "Business self-financing." "Total public investments" include the investments of these same organizations from their own resources and from treasury facilities. A mention of these organizations will be presented later in the chapter.

The trend of public sector's savings, as is revealed above declined after 1953. It was relatively high in 1953 because of the above-mentioned saving from ordinary expenditures in the years 1952/53 and 1953/54. It declined later when current expenditures, on defence, social services, and economic administration rose. It will be revealed later that revenue has not

increased sufficiently to exceed this rise in expenditures. Savings have risen again in 1957 when the Suez Canal began to add considerable revenue to the budget. In 1958, beside the Suez Canal revenue, the rising trend in government expenditure on national defence and education was checked. Savings have risen again reaching LE. 35 million. Savings continued to rise thereafter. The "surplus" in the general budget* of the year 1959/60 was estimated at LE. 28 million.¹ Expenditures on "new works" under Chapter III of the ordinary budget were estimated at LE. 24 million. Therefore, total savings amounted to 52 million in 1959/60. In 1960/61 the estimated surplus in the general budget was LE. 70 million.² This amount includes "new works" because this item was finally excluded from the ordinary budget and added to the development budget. In 1961/62, public saving, applicable to the development budget, was estimated at LE. 88 million.³ This increase in the rate of saving could not

1. National Bank, Economic Bulletin, v.XIII, p.84 (1960).

2. Ibid.

3. Ibid, v.XIV, p.129, (1961).

* General Budget includes railways budget, petroleum authority budget, and the Suez Canal budget, beside the ordinary budget.

have been verified had current expenditures continued at the former rate of increase. According to Table XI, in the previous chapter, savings from ordinary revenue will contribute to development financing LE. 180 million in the five years 1960-1965. This is other than LE. 154 million the contribution of the Suez Canal Authority, LE. 60 million, the contributions of municipalities, and LE. 100 million from other public sources. That makes public sectors' contribution in the average year amounts to LE. 97 million.

In peaceful times, it is believed that expenditure on defence could be reduced or at least maintained at the same level. Expenditure on education, health, and other social services and economic administration will not need to rise at the same high rate required during the earlier period. But, on the ^{other} side public revenue has to increase to care for these expenditures and to realize additional saving. Current expenditures continued to increase but at a lower rate. These expenditures have risen from LE. 200 in 1953/54 to LE. 280 million in 1956/57¹, equivalent to 40 per cent increase, over four years. Expenditures have risen to LE. 301 million in the year 1960/61², the increase was equi-

1. Chambers of Commerce, Egyptian Economy During 1952-1957, p.192 op.cit.

2. National Bank, Economic Bulletin, v.XIII, p.84 (1961).

valent to 7 per cent during these latter four years. The expenditure side has been tackled, and the great rise in expenditure on nonproductive activities was checked. The other side of the public sector which is the revenue side is to be investigated.

B. PUBLIC REVENUE

The other side that determines government savings is the revenue from taxation, public services, and public property. Table XIII shows the development of public revenue over a stretch of nine years. Each of the three sources: taxation, public services, and revenue from public property, is singled out to serve the purpose of trends study. The data represent budget estimates not actual receipts, as the latter figures are not available for a long period. However, upon studying the few early years actual figures¹ it is believed that the trend revealed is not different.

1. Taxation Trends

The data in Table XIII ~~is~~^{are} divided into tax revenue and non-tax revenue. Taxes are divided into direct taxes and customs- and excise. The non-tax revenue is divided into profits from

1. op.cit. Egyptian Economy During 1952-57, pp.193-195.

TABLE XIII

		PUBLIC REVENUE ESTIMATES						in LE. million	
		1952/ 53	Per cent	1954/ 55	1955/ 56	1960/ 61	1961/ 62	Per cent	
A. <u>Direct Taxes</u>									
Land and Building Tax		15.3		18.3	18.3	18.8	20.2		
Movable Property and Earned Income		16		14	15.5	29	28		
General Tax on Inc. Estates Tax		9.7		4.3	4.1	5.5	5.7		
Property Transfer Tax		3.5		3	3	3	3.5		
		3		3.6	3.6	4	4		
Total Direct Taxes		47.5	23.1	43.2	44.5	60.3	61.5	14.5	
B. <u>Customs and Excise</u>		94.8	46	98.5	102.9	120.7	130.2	30.8	
C. <u>Public Property</u>									
1. Industrial Establishments		5.5		17.6	21.6	13.3	13.9		
2. Profit from Public Organizations							40.2		
3. Contribution to Development Projects by Public Org's						16.9	39.7		
4. State Domain and Natural Resources		4.2		11.*	4.9	4.6	3.4		
Total Public Property		9.7	4.7	28.6	26.5	34.8	97.2	23.-	
D. <u>Other Revenue</u>⁺		54	26.2	57.6	64.4	155.1	134.2	31.7	
Total		206	100	227.9	238.3	370.9	423	100	

Source: based on Tables in National Bank, Economic Bulletin, v.VII, p.105, 1955; and Ibid, v.XIV, p.130, 1961.

- * Includes LE. 6 million from confiscated property which is included under a different caption in other years.
- + Mainly fees and duties against public services: railways stamps, telegrams, commercial and other services.

public property and other revenue which is mainly, stamps, fees, and dues in return for government services and government commercial activities.

a- Direct Taxes

Direct taxes that were 23.1 per cent of the total revenue in 1952/53 have dropped to 14.5 per cent in 1961/62. All taxes, (A+B) represented 69.1 per cent of total revenue in 1952/53 and have dropped to 45.3 per cent in 1961/62. The greater decrease was in the direct tax. It is worthy to note that this item continued to decrease in absolute amounts up till 1955/56. General Income Tax and Business Income Taxes were especially reduced, inspite of the fact that there were business profits stimulated by the protection and business-support policies. In the early years little increase was imposed on the highest brackets of high incomes. During the period 1952-1954 some increase in direct tax rates has been imposed. On General Income, on the highest two brackets, the tax was increased from 20 per cent and 30 per cent to 25 and 35 per cent respectively. On movable property, commercial and industrial income, the 16 per cent tax became 17 per cent. On taxable income from free professional practice the increase was 1 per cent: from 10 per cent to 11 per cent. An inheritance tax was imposed on property transfered to the heirs ranging from 5 per cent to 40 per cent on estates exceeding LE. 5000 in value. It was only in July 1956 that a

considerable increase of tax rates on incomes was imposed. A tax for Defence was added at a rate of 3.5 per cent of taxable income from movable property, business and professions; and a rate of 1 - 2 per cent of taxable income from employment; and 2 - 10 per cent on taxable general income.¹ This tax is mainly responsible for the increase of revenue from direct taxes, since 1956/57.

Against these increases in direct taxes there were reductions in others. Buildings were formerly exempted only if rent was less than LE. 5 per annum, the exemption level was raised to LE. 18. This was to encourage construction of low-cost buildings. Small land owners were exempted from taxes. Exemption applied to lands that were watered by rain. Large capital investments in basic industries were exempted from business income tax for the first seven years. Right to search for new sources of ore were given gratuitously.²

b. Indirect Taxes

Apparently, there were no intentions to rely upon business and personal income taxes to finance large development schemes.* Neither were the customs-and-excise taxes manipulated on sub-

1. Chambers of Commerce, Egyptian Economy During 1952-57, p.202, Cairo: 1958 (in Arabic).

2. Ibid, pp.201-206.

* In July 1961 a law was enacted that imposed a steeply progressive taxation rates on incomes. The effects of this law on direct tax revenue have not appeared yet.

stantial scale to yield income for development financing. The small increase in item B, Table XIII, was rather due to taxes on tobacco, alcoholics, and consumption goods. Excise alone accounted for 23.6 per cent of this source of revenue in 1957/58. The policy of protecting domestic industries by restricting imports and exempting materials and machinery deprived the government from a sizeable and manageable revenue. The revenue from customs and excise dropped from 46 per cent of the total revenue in 1952 to 30.8 per cent in 1961 although there was a considerable increase in absolute amounts.

The Egyptian government had to count on two sources of revenue, the price of some services rendered to the public and the property which the public sector possessed. The contribution of both increased tremendously in ratio, as well as in absolute amounts.

2. Revenue From Public Services And Public Property

Item D, "Other Revenue" has increased because of the expansion of government services horizontally and vertically. The Railways, Post Office, Telegrams more than doubled their services and their revenue. The government assumed new activities especially in the field of commerce and trade. Almost all export-import trade has been entrusted to public organizations.

Item C, of Table XIII, is the most significant of all. Annual revenue from public possession of industrial, commercial,

banking firms and from the Suez Canal increased from LE. 5.5 to LE. 93.8 million* in the nine-year period. The trend is towards more holdings of profit-yielding enterprise by the public sector. While the revenue from Item D includes the costs of running these services, the revenue from Item C, Nos. 2 and 3, represents the net profit, including dividends received by the government as a shareholder in companies and self-financing of public organizations that were not included in business saving in Chapter II.

For the purpose of further analysis of the items that have developed to become significant contributors to public saving Table XIV shows the details of items C and D in Table XIII, under Revenue 1 and 2. Though the year selected for Table XIV is not represented in Table XIII, yet it serves the purpose. While Table XIII helped to high light the general trends. Table XIV sheds more light on public revenue from property and services. Budgets of two important organizations: The Petroleum Authority and The Railways Authority that were included in Table XIII do not appear in Table XIV. The two budgets exceeded LE. 86 million in the year 1958/59. The main interest, in Table XIV is the net contribution of such public enterprise rather than the total

* Excluding revenue from Public Domain which practically has not changed.

budget of each. The net contribution to public saving of the two authorities and other independent organizations will be treated later and will be added to the findings.

The traditional revenue from taxes amounted in the 1958/59 budget, to LE. 193.5, without much difference from the preceding year or the succeeding year. This revenue was enough to cover all ordinary current expenditures except transfer payments and subsidies. In other words, Revenue A-1 was enough to pay expenditures B-1. Net return from public services and public property was estimated to reach L.E 69 million (revenue 1 plus 2). After transfer payments and subsidies, a saving of LE. 41 million was expected. LE. 3.8 million were to be used by the industries and public services, mentioned under A-3 in Table XIV, from their own income. LE. 22 million were to be expended by the respective ministries on "new works" according to Chapter III in the ordinary budget. The remaining LE. 15.3 million would be one source of financing that the treasury uses to realize new projects according to the separate development budget.

Eighty per cent of the increase in revenue between 1952/53 and 1957/58 was from items 3 and 2, while only 20 per cent was due to taxes, item 1.¹ The development of these two items continued later as shown in Table XII. What are these items?

1. Chambers of Commerce, Egyptian Economy During 1952-57, p.194 (in Arabic).

TABLE XIV

1958/59 ORDINARY BUDGET ANALYSIS

in LE. million

A. REVENUE (Net)			
1-Taxes: Direct Taxes, customs, and excise, and stamps			193.5
2-Net Receipts for Public Enterprise			
a-Sale of inventories	1.941		
b-Interest	2.108		
c-Dividends	2.284		
d-Unusual Revenue ¹	14.077		
e-Miscellaneous ²	28.331		
f-Profits of Trade in Supplies	7.950		
g-Confiscated Property Revenue	<u>6.000</u>		62.7
3-Revenue from the following:			
h-Industrial Enterprise ³	16.794		
i-Post Office	2.474		
j-Telephone and Telegrams	6.380		
k-Public Domain	1.859		
l-Mines and Quarries	<u>3.028</u>	30.5	
Less Expenses		<u>22.3</u>	8.2
			<u>264.4</u>
B- CURRENT EXPENDITURE			
1-Administrative Expenses	191.4		
2-Transfer Payments	23.2		
3-Subsidies	<u>8.7</u>		223.3
C- Saving			
1-Invested in "new works"			41.1
2-Invested by items h-l above			22
3-Carried forward to Treasury			3.8
			<u>15.3</u>

Source: Samir Amin, Statistics of General Equilibrium, pp.164-173, Cairo: 1959.

1. Mainly profits of the Cotton Committee, LE. 14 million.
2. Mainly the Suez Canal, LE. 28 million.
3. The Defence Factories, Cairo Electricity, Insecticides Factory, and Mines & Quarries.

a- New Sources of Revenue

1- Dividends

Sub-items a and b are not new sources. Sub-item c is the government share in distributed profits of business companies. This was not a source of revenue prior to the government's participation in industrial enterprise and before nationalization of foreign companies. This source will develop rapidly after 1960 because of the great expansion of business activities of the public sector. Together with the Suez Canal the total net profit has been estimated at LE. 40.2 million in 1961/62 as is shown in Table XIII. Not less than LE. 10 million is expected to be the dividend receipts against public shares in industrial and commercial companies that have the joint stock status. The par value of the investments of the Economic Development Organization and the Misr Bank Organization in business firms amounted to about LE. 85 million at the end of 1959. Most of the new public industrial investments after this date were held by these two organizations. Public industrial investment in 1959/60 reached about LE. 50 million. Such investments were far greater in the following year. Profits from large enterprises that have been implemented in accordance with the Five-Year Industrialization Plan shall add to net profits in 1961 and the later years, not to mention the wide nationalization of large companies in July 1961. All of this shows that the trend is towards continuous and rapid increase in public receipts from dividends. It would not be surprising to

find that this source realizes LE. 10 million dividends in the year 1961/62 and a greater return in the next years.

2- The Cotton Committee

Sub-item d, "unusual revenue" is mainly income from cotton marketing. The Committee on Cotton Affairs entered the cotton market to absorb the fluctuations in the prices of this staple good, which is the most important single product in the Egyptian Economy. The Committee buys at a price suitable to growers and guarantees for spinning factories raw cotton supply at a fair, stable rate. The object of this interference was not to collect profits but rather to insure stability in prices for growers and industries at the same time. While this practice eliminated harmful speculative practices it realized in many years profits for the public sector. During this particular year such profits were estimated at LE. 14 million. Though this is not a certain and permanent income, the government is realizing real profit from the legitimate trade in cotton. The laws issued in July, 1961 confined this trade to organizations in which the public sector has a holding share. Therefore, profits are expected to return to the public sector in the form of dividends beside the profit, or loss, of the Cotton Committee.

3- The Suez Canal

The most interesting and most profit-yielding single public enterprise is the Suez Canal. In Table XIII, sub-item e,

"miscellaneous" includes mainly the net revenue from Suez Canal tolls. This revenue was estimated at LE. 28 million while the total receipts in 1959 amounted to LE. 44.5 million.¹ In order to save LE. 28 million only LE. 16.5 million expenses should be incurred. So much saving has never been realized throughout the history of the Canal nor is it likely to be realized in the year 1959.

Before nationalization, in 1955, the receipts of the Canal company amounted to LE. 32.5 million. Out of these tolls, LE. 19 million were spent abroad: LE. 2.8 million pensions and salaries of foreign employees, LE. 9 million coupons payments to foreign shareholders, LE. 1.5 million for imported machines and equipment, LE. 4 million investments in foreign assets. Receipts of the Egyptian Government were LE. 2.3 million.*

The gross receipts of the Canal increased after its re-opening in 1957, to LE. 42 million in 19~~5~~⁸, and exceeded LE. 50 million in 1960. It is expected that tolls will increase after the projects of improvements of navigation have permitted vessels with a draught of 37 feet to pass safely. These projects were finished in June 1961.² New projects are scheduled in the Five-Year Overall Plan to allow vessels with a draught of 45 feet to pass. In order to realize these improvements a loan was nego-

1. National Bank of Egypt, Economic Bulletin, v.XIII, p.237, (1960).

2. National Bank, Economic Bulletin, v.XIV, p.202, (1961).

* The Egyptian Economic and Political Review, v.IV, p.37, Cairo: (March, 1958).

tiated with I.B.R.D. as shall be seen in the next chapter.

The net income of the Canal transferred to development budget amounted to LE. 22 million in 1960.¹ That is beside LE. 2.3 million² dues to the government appearing as ordinary receipts. According to Table XI, the expected net savings of this source will be as high as LE. 130 million in the five year 1960-1965, at an average of LE. 26 million per annum. This is apart from the depreciation reserves. The canal authority has to pay LE. 23 million in six annual installments to the former shareholders of the Suez Canal Company thus adding to its burdens.* The first installment was paid on January 1st, 1959.³

4- Profits of trade in Supplies

The public profits from supplies are due to the monopolistic dealing of the Ministry of Supply of a number of imported food-supplies. These are mainly tea, coffee, wheat, flour, kerosene, and edible oils. In 1958/59 subsidies to reduce cost of living were estimated at LE. 6.7 million.⁴ The profits, on the other hand, were estimated at LE. 7.9 million. The profit is from tea and coffee and from free kerosene, first-class bread and

1. Ibid, p.35.

2. South U.A.R. Budget, 1960/61, p.22, (in Arabic).

3. Ibid, p.8.

4. Samir Amin, Statistics of General Equilibrium, p.163, Cairo: 1959, (Arabic).

* The assets of the former company outside Egypt, amounting to 72 mil. pounds sterling, were allowed to the shareholders.

flour, and free sugar. While the Ministry undergoes loss on popular category of bread and rationed items it makes profits from selling the same items in the free market, at higher prices. This, however, is not a permanent profit source and as long as prices are rising the Ministry shall incur losses to stabilize prices. When price trend is stabilized by other means, supplies will become a considerable source of profit for the public sector, this is highly probable since prices showed relative stability after 1957, as will be shown in Chapter V.

5- Confiscated Property

An interesting source is the revenue from confiscated property. The main source of this revenue is the property of the Royal Family that has been confiscated in 1953. About 170,000 feddans of most fertile land were turned into public property.¹ The net revenue from this property appeared in the ordinary budgets at LE. 6 million per annum, since the year 1954/55. Since that date this revenue has been totally allocated to finance investments vested with the Council of Social Services. Among the achievements of the Council were the 250 Collective Units, established in the scattered rural areas to do multiple social and economic services. The size of public buildings constructions could be read in Table III. The future of this

1. National Bank, Economic Bulletin, v.XIII, p.105 (1955).

source proved constant as no further confiscation was reported. Nationalization was associated with compensation and therefore, would not yield to the government a net income as did confiscation.

b. Development of revenue from Customary sources

1- Industrial Enterprise

Industrial enterprise appearing in Table XIV includes only a few projects which remained under the direct supervision of the ministries. These are the Cairo Electric and Gas Service, the Military Factories, an insecticides factory, and mines and quarries. Table XIII shows that the revenue from this source decreased in the budgets of 1960/61 and 1961/62. This was due to the transfer of the Military Factories to the autonomous Nasr Organization, that embraces since 1960 firms engaged in heavy industries. In 1952/53 the income from this source was only LE. 5.5 million. The LE. 16.8 million as shown in Table XIV are the gross revenue of the four industrial projects in 1958/59. Their expenditures amounted to LE. 12.451 million,¹ and their savings, to about LE. 4.3 million. But, of the expenditures, LE. 2.7 million were capital expenditures. This makes their total savings during the year amount to LE. 7 million, apart from the depreciation reserve.

1. op.cit. Statistics of General Equilibrium, p.168.

2- Post office, Telephone, and Telegram

The remaining LE. 5 million out of the LE. 12 million savings of items 3, Table XIV, were due to the Post Office, the Telephone, Telegram, and Public Domain which are no new enterprises, but whose services were developed tremendously during the period 1952-57. Revenue from Telephone service alone has increased from LE. 3.5 million in 1950/51 to LE. 6.4 million in 1956/57. The assets of the Telephone and Telegram were estimated at LE. 8.7 million in 1950/51, and at LE. 20 million at the end of 1955/56.¹ The Post Office gross revenue also increased in a similar manner. It was LE. 1.55 million in 1951 and LE. 2.1 million in 1956. The net profit increased from LE. 107,000 to 475,000 over the same period.² The same rate of development is not expected to continue. But the profits from these services shall continue to rise in abstract amounts.

There remains some sources of revenue that have not appeared in Table XIV. The Petroleum Authority and the Railways Authority are independent public bodies, but their budgets are totally included in Table XIII. Their budgets are usually annexed to the ordinary budget.

3- Petroleum Authority

The budget of the Petroleum Authority amounted to LE.

1. U.A.R. Government, Speeches of President and Ministers in the National Assembly, p.611, Cairo: 1957 (Arabic).

2. Ibid, p. 627.

62.1 million in the year 1958/59. The receipts were the result of sale of oil refined in the two large public refineries, in Alexandria and Suez. The current expenses to run the research, production, and operation of the refineries, pipelines and marketing were estimated at LE. 59.7 million. The net savings of this source, therefore, amounted to LE. 2.4 million.¹ The net profits of this source were estimated at LE. 2.8 million in 1959 and 4.7 million in 1960. That is other than LE. 4 million, the public revenue from royalties received in 1960 from oil companies operating in the U.A.R.² The contribution of this source to development financing is expected to rise steadily due to the large investments in this industry. The investments in petroleum industry amounted to LE. 40 million as per the Five-Year Industrialization Plan that started in 1957. The source of this financing was mainly foreign, especially Russian loans.

4- Railways Authority

The other annexed budget is that of the Railways Authority. The railways budget for 1958/59 was estimated at LE. 24 million. Out of this LE. 21.5 million were running expenses and LE. 1.5 million savings to self-finance part of the railway's projects. The net profits of the Railways is expected to rise

1. op.cit Statistics of General Equilibrium, p.179.

2. U.A.R. Government, South U.A.R. Budget, 1960/61, p.13
Cairo: 1961, (Arabic).

to LE. 4 million after all locomotives are turned to run by diesel. Great part of improvements in the railways were contributed by the U.S.A. as shall be shown in the next chapter. This service was running at a loss before 1957 because of the kind of management, and the old-fashioned equipment used. The "authority" was offered independence to run the railways in the most economic manner, and to implement improvement and expansion projects related to railways, according to the plans.

5- Al-Awkaf

The "Awkaf" property was controlled and directed to yield net revenue. 75,000 feddans of the Awkaf lands of the best quality were reclaimed from the former king.¹ Hundreds of thousands of tied lands (Ahli) were released. Their legal owners were given free hand to dispose of them. The remaining, "Khairi" Wakf, was given to small tenants to cultivate at the reduced rent rates. The Ministry of Awkaf assisted them by extending credit in kind and by giving technical assistance. Some lands were distributed to small owners through the Agrarian Reform. Out of 133,000 feddans, only 56,910 were still held by the Ministry at the end of 1960.² The following table shows the surplus that the Ministry contributed to the public saving in the period 1957-1960 in LE. millions.³

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1. op.cit Speeches of President and Ministers, pp.1147-1181, Cairo: 1957.
 2. The U.A.R. Southern Region Budget, 1961/62, p.12 and Ibid, p.422, (Arabic).
 3. Ibid.

	1957	1958	1959	1960
Revenue	4.80	3.40	3.50	3.40
Expenditure	-.69	-.65	-.57	1.--
Surplus	4.11	2.75	2.93	2.40

This surplus, beside the surplus of the years 1953-56 was spent in investments in land, buildings, and industry.

In 1956 alone, al-Awkaf extended financial aid to tenants LE. 568,456. During 1952-56, the value of new buildings constructed amounted to LE. 1.9 million. Schools construction amounted to LE. 400,000. During this period, al-Awkaf invested LE. 876,000 in industries, LE. 170,000 in new commercial projects, LE. 30,000 in the Bank of the Republic, and LE. 750,000 in public production bonds. In addition to this about LE. 3 million were invested to religious buildings.¹

These savings by al-Awkaf were neither included in Table XII nor in Table XIII. They are an addition to public savings appearing in the ordinary or development budgets.

6- Municipalities

The other significant public institutions contributing to aggregate saving are the municipalities. Municipalities contributed to development financing mainly by saving from current expenditures and by more efficient management. During the period

1. Speeches of the President and Ministers in the National Assembly, pp.1147-1185, Cairo: 1957.

1952-1957, municipalities invested on constructions an amount of LE. 23.5 million, while only LE. 12.4 million¹ were spent during the preceding 5 years. Municipalities are estimated to save LE. 60 million in the five years, 1960-1965.² The estimated rate of increase in their contribution to development financing is realizeable as long as efficiency of their management continues to improve and as long as expansion in towns and cities likewise continues. Savings by municipalities is not included in Tables XII and XIII, since municipalities have independent administration and independent budgets.

C. PUBLIC SAVING VIS-A-VIS PRIVATE SAVING

1. The Impact Of The Growth Of The Public Sector On Other Sectors

The development of the role of the public sector as an owner of property and as an operator of services explains the ever increasing savings of this sector, as was shown earlier in the chapter. A question arises whether such public saving through economic activities is achieved at the expense of the private sector's savings.

1. Ibid, p.973.

2. U.A.R. Government, Yearbook, 1961 , p.424, Cairo: 1961.

Before July 1961, some expansion of the public sector was at the expense of three groups: Foreign holders, The Royal Family, and Dealers in foreign trade.

Foreign owners of business firms in Egypt were earning some LE. 20 million, net profits in some years. The greatest part of these earnings were not invested in Egypt. It was already mentioned in this chapter under the "Suez Canal" that dividends paid abroad to shareholders alone were LE. 9 million in 1955, before nationalization, beside investments of the company abroad of LE. 4 million. The Canal receipts increased later, the profits returning to the Canal Authorities exceeded 22 million in 1960, as mentioned before. This source of revenue was nationalized at a cost of LE. 23 million, which was agreed to be paid in 4 installments beginning 1959.¹

Other than the Suez Canal, earnings of foreign enterprises transferred to countries of origin amounted to LE. 2.1 million in 1955 and LE. 3.8 million in 1956 then dropped sharply to LE. 200,000 in 1957 and LE. 415,000 in 1958 and LE. 225,000 in 1959.² These exclude also profits of banks that were Egyptianized and whose capital amounted to LE. 12 million.³ Average transfer of interest and dividends per year during 1950-1959 amounted to LE.

1. National Bank of Egypt, Economic Bulletin, v.XIV, No.2 Table 17, (1961).

2. "Foreign Investments in South U.A.R", Middle East Economist v.11, p.18, (December, 1960).

3. Ibid.

12 million, reaching highest level in 1954 with LE. 18 million.¹ Total compensations due to nationalized and Egyptianized enterprise in 1957, including banks, was agreed upon to amount to Sterling pounds 27.5 million. The whole amount had to be paid in 1959 and 1960 from Sterling balances.²

In view of the above nationalization of foreign enterprise added perceptible savings to Egypt, mainly originating in the public sector. Nationalization of foreign enterprise did scare foreign equity financing. This type of investment, however, has already declined inspite of legislative measures taken by the Egyptian authorities to encourage it. A discussion of the subject of foreign equity financing will be due in Chapter IV.

The confiscation of the property of the Royal Family eliminated the fabulous expenditure of this family on conspicuous consumption and consequently may have reduced the "demonstration effect" on the middle class. Thus, beside the large size of "savings" that result from confiscating this property other classes were relieved of the desire to imitate the consumption patterns of the ^{moneyed} elite.

1. National Bank, Economic Bulletin, v.XIV, p.149, (1961).

2. International Monetary Fund, International Financial News Survey, v.11, p.288, (November, 1959).

The third practice by government sector, that is apt to compete with the private sector, is the state's commercial practice. Government participated in this field, mainly to stabilize prices, to regulate supply of essential commodities, to check smuggling of the Egyptian pound and, lastly, to make profits. In the essential supplies trade the government incurs losses to maintain a stable cost of living. In cotton trade there is the risk of incurring great losses due to unstable international prices. The public sector undertakes these losses and settles them from profits from sale of other commodities or from other year's profits. However, these objectives lead the public sector to go too far in this practice. Almost, all import-export trade, beside food supplies and medical supplies are becoming public monopoly.¹ Again this practice is carried at the expense of the highest income groups that used to benefit from large transactions including the benefit from monopolistic prices. The rest of the commercial firms dealing in retail met only with competition from cooperatives that are themselves private institutions.

The larger commercial firms, excluding cooperatives, have, no doubt, diminishing profits and therefore diminishing savings, too. The diminishing savings from trade practice return to the public sector that do the economic planning. As said before, a cri-

1. National Bank, Economic Bulletin, v.XIV (1961), also p.117.

tical job of economic planning is to see to it that realized savings are equal to the planned savings. The surest way to achieve this objective is to have the sector that is expected to invest do the actual saving. One might say a progressive income tax could have achieved the required results, but such a tax was thought to be difficult to apply. Besides, it could have affected the activities of all economic fields. Government interference aimed at certain fields only where foreign influence was great and where the response to the national economic planning was hampered by selfish interests.

Other revenue of public sector was mainly from new investments. Reproductive investments of this sector, as revealed by Table III and Table XI, increased steadily.

The actual trend showed a decline in the saving of the household sector. The decline due to the expansion of the public sector equals the portion of profits that would have been invested inside the country, by the foreign proprietors, the Royal Family, the big landlords, and the dealers in import-export trade. The planning administrators admitted this fact in their overall five-year plan, and expected from the household sector only LE. 75 million saving during the said five years.¹ On the other hand savings of the members of the household sector

1. See Table XI.

increased in the form of insurance and social security reserves. The business sector's savings continued to rise, but the public sector acquired a holding share in this sector, especially after the nationalization laws of July 1961. This coupled with the steeply progressive taxation laws has made the public sector the main provider of domestic funds for development financing. The means to provide savings are: 1) The sector's rise in ownership of an ever growing business sector; 2) The increase in revenue from services and trade; 3) The resorting finally to progressive taxation on income; 4) Last but not least, the checking of public current expenses.

The economic advantages to this growing role of the public sector are the certainty and predictability of a sizeable financing from domestic resources.

2. The Interflow Of Savings Among Sectors

As shown in Table XI, as a source of financing the credit facilities provided by the treasury were far greater than the government savings. The treasury resorted to the central bank and to the public to collect funds. The central bank was the main creditor, its main source in turn was the "rest of the world". Table XV is a summary of the flow of resources from the "rest of the world" to the central bank and the flow from this bank to the treasury and other public organizations in the year 1957.

TABLE XV

CENTRAL BANK

NET SOURCES AND USES OF FUNDS FOR THE YEAR 1957 IN LE. MILLION

Sources		Uses	
Rest of the World	34	Facilities to Treasury	33
Commercial Banks	13	to E.D.O and Specialized Banks	13
		to Individuals	1
	<u>47</u>		<u>47</u>

Source: Samir Amin, Statistics of General Equilibrium
p.207, Cairo: 1957, (in Arabic).

The central bank's holdings of treasury securities in the form of bonds and bills increased by LE. 40 million. On the other hand, treasury deposits with the bank increased by LE. 7 million. Net facilities to the treasury amounted to LE. 33 million which is stated in the Table XV. "Net" facilities to the Economic Organization and specialized banks were LE. 13 million. The central bank's sources, on the other hand, are the net indebtedness to the "rest of the world" LE. 34 million, and reduction of commercial bank's liabilities to the central bank, LE. 13 million. Total facilities offered by the rest of the world were LE. 58 million, but the facilities allowed by Egyptian firms to importers abroad were about LE. 24 million.

The LE. 34 million provided by the rest of the world are slightly more than the deficit in the balance of payments for the same year, which was LE. 31.3 million ^{1*} The facilities offered by the rest of the world contributed to equilibrium in Egyptian foreign economic relations. At the same time these facilities contributed to internal equilibrium since they slightly exceeded the credit facilities of the central bank to the government. The rest of the world will be treated in the next chapter. And the subject of equilibrium shall be finally discussed in the chapter on prices.

The treasury received LE. 33 million from the central bank to apply to development works undertaken by ministries and other independent public organizations. Table XVI is a summary of the flow of funds through the treasury.

TABLE XVI

THE TREASURY

NET SOURCES AND USES OF FUNDS FOR THE YEAR 1957 IN LE. MILLION

Sources		Uses	
From: Central Bank	33	To: Public Economic Orga-	
From: Public Buildings		nization	21
Organization	2	To: Ministries	16
From: Custodian Depo-		To: Agrarian Bank	3
sits	9	To: E.D.O	4
	<u>44</u>		<u>44</u>

Source: Samir Amin, Statistics of General Equilibrium p.206, Cairo: 1959, (in Arabic).

1. Ibid, p.195.

* The difference is most probably due to the time lag

The net liability of the treasury was not only to the Central Bank but also to other public organizations. The treasury extended these funds to the bodies vested with economic development tasks. Out of the LE. 44 million facilities by the treasury to these bodies, LE. 16 million were seasonal credit to facilitate the increase in cotton stocks. The remaining LE. 28 million were applicable to capital investments. This figure appears in Table XII against "Borrowing from Treasury."

Table XVII shows the resort of the treasury to float bonds and bills to finance development projects and inventories. Development bonds issued during the period 1953-60 amounted to LE. 144 million. Out of the total issue LE. 85 million were issued in 1960. This reflects the great rise in government role in direct financing of development projects. It was already mentioned that self-financing of this sector was estimated at about LE. 70 million during 1960/61. Other LE. 33 million development bonds were issued before June 30, 1961.¹

Part of these bonds was purchased by the Central Bank. But the larger burden fell upon the business sector, insurance funds, and the household sector, directly and through commercial banks.

1. National Bank, Economic Bulletin, v.XIV, No.3, Table 10, (1961).
which takes place between buying foreign goods abroad and receiving the goods in Egypt.

TABLE XVII*

DEVELOPMENT OF BORROWING OF THE TREASURY AND PUBLIC ORGANIZATIONS

in LE. million

	1953 & 1954	'55	'56	'57	'58	'59	'60	Period To tal	Out- standing Total
1-Development Bonds		10	25		4	20	85	144	287
2-Treasury Bills	12	33	75	14	10	15	10	145	185
		43	100	14	14	35	95	289	
3-Specialized Public Banks Bonds					20		3	23	23
4-Nationalization Bonds							20	20	20
5-Agrarian Reform Bonds	12	43	100	14	34	35	118	332	515
	12	3	2	6	10	4	5	42	42
	--	46	102	20	44	39	123	374	557

Source: National Bank, Economic Bulletin, No.3 v.XIV, Table 10, (1961) and p. 257, v.IX, (1956), and v.XII, p.188, (1959).

Treasury bills increased during the period by L.E 145 million. The two years 1955 and 1956 were responsible for the greater part of the issue. LE. 108 million were issued during the two years and the central bank was the main buyer of the bills. The trend as seen in Table XVII is toward greater resort to long-term bonds to finance part of the greatly increased develop-

* Computations by writer.

ment projects, as per the Five-Year Plan, starting in 1959/60. Treasury bills were resorted to at the time of the Suez Canal crisis to finance the accumulated inventories because of export difficulties. Short-term borrowing was also used to finance current public expenditures that exceeded the budget estimates. In ordinary times, 1957-60, bill issues were moderate in size and commensurate with the natural increase in the inventories of a developing economy. A return to this subject will be due when the question of price stability is discussed.

The other bonds, item 3 in Table XVII, were issued by the agrarian bank and Industrial bank, guaranteed by the treasury. Item 3, denotes the bonds issued to the former shareholders of Misr Bank, National Bank, and Port Said Bank that were nationalized in 1960. The Agrarian Reform bonds are those issued by the Reform in settlement of the price of sequestered lands in accordance with the Agrarian Reform Law of 1952. The two classes of bonds are neither a direct burden on the government since the respective nationalized firms and sequestered lands are capable of servicing and settling the loans; nor do they show saving or flow of saving.

CHAPTER IV

THE REST OF THE WORLD

Introduction

The remaining source of development financing is the "rest of the world." The size of this source is measured by the deficit of the balance of payments on current account which had accumulated during the period. Measuring the cumulative deficit and claiming that it is the size of total development financing offered by the rest of the world, does not fully serve the purpose of this thesis. It is important to find out how was it possible to maintain the deficit and to find its future course. There were two sources that covered the deficit: 1) Egyptian assets abroad and 2) the credit facilities offered by the "rest of the world." This chapter discusses the role of the two sources during the period 1952-1960 and the significance of each with regard to the future development.

Financial assistance by the rest of the world, a new source realized by the New Regime, was totally and directly applicable to development projects. There is indication too that it is going to be the only foreign source after the depletion of the sterling assets. In view of the above mentioned reasons it is given greater attention in this chapter. The terms of these credit facilities and the way they are used are

related to price stability, a phenomenon to be treated in the next chapter.

The trend of the equity type of foreign financing is discussed in this chapter in order to show the failure of the attempts to utilize this source, although it was the main type of foreign financing prior to World War II.

A. THE BALANCE OF PAYMENTS ON CURRENT ACCOUNT

1. Trends In Foreign Exchange

Early in the period the deficit of the balance of payments was alleviated by the control methods used to suppress imports. On the other hand the total exports in that period did not rise. The increase in population and the rise in the propensity to consume created a rising demand for domestic goods. Besides, new industries consumed more domestic raw materials. Receipts from exports continued to drop from the high level attained in 1951 to reach the lowest level in 1956. Later in the period, there was a considerable rise in receipts from exports. This was mainly attributed to a rise in the prices of cotton, caused by the opening of new markets for raw cotton, cotton textiles, and yarn. Table XVI shows that the export receipts in 1960 were estimated at LE. 193 million. This

figure is 18 per cent greater than that of 1959 and 42 per cent greater than that of 1953. New export items were registered. Rubber tyres were already an export item. Textile and yarn exports increased by more than 200 per cent. Export of cement, manganese and other ores were greatly rising. Rice consumption was rationed in order to save more of it for export.

Imports have showed a different trend. There was a continuous rise in imports with the exception of the year 1954. The reduction in imports during this year was due to a good wheat crop, which has been the largest imported consumption item in some other years. Wheat imports amounted to LE. 34 million in 1951, to LE. 32 million in 1952, and to LE. 17.8 million in 1958.¹ Fertilizers imports ranged from LE. 6 million in 1950, to LE. 14.2 million in 1958. Import of fertilizers declined later because of the increase in local production.

There was a continuous rise in the total imports inspite of the decrease in the import of consumption goods and the complete restriction of luxury goods, cotton and rayon fabrics. Total imports in 1958 were still slightly below the imports of 1950. The 1951 import figure was never exceeded until 1960. Imports have risen to old high levels only their structure was

1. National Bank of Egypt, Economic Bulletin, v.XIV, p.143, (1961).

different. In 1950 the value of imported metals, machinery and apparatus was 22.5 per cent of the total imports, while in 1958 the ratio was 37 per cent.¹ Petroleum imports increased by 224 per cent over the same period. Fertilizers imports doubled, as mentioned before. These items are also required for development.

The trade policy was able to hit important targets. Diversification of exports and diversification of markets created a chance to stabilize export prices and to improve terms of trade. Raw cotton remained the main export commodity. Price and quantity of cotton exports continued to determine the total export proceeds. There was however a clear trend toward an increase in exports of manufactured goods. The value of exports of articles that have undergone advanced transformation was LE. 4.4 million in 1950, LE. 3.9 million in 1953, LE. 13.7 million in 1956, and LE. 12.9 million in 1959.² The period 1953-1956 witnessed the greatest rise in export of yarn, textile and cement items.

On the other hand, imports were restricted in order to save foreign exchange for development purposes. All through

1. Ibid, p.141.

2. Ibid, p.139, v.XIV, (1961).

the period the balance of trade remained negative. In 1954, however, it was possible to reduce the deficit greatly, just because wheat imports were very slight that year. The import of development goods was continuously rising, the greatest rise being observed in the second half of the period 1956-1960. During the years 1955-60 the deficit of the balance of trade was great but only in 1960 it surpassed the previous peak reached in 1952.

The deficit in the balance of payment on current account of the year 1951 remained in the lead among the deficits with that of 1959 coming next in order of size. The surplus of the balance of invisible transactions was LE. 35 million in 1959, against LE. 53 million in 1951. The main items of invisible receipts were the "British Army" before 1956 and the "Suez Canal" tolls after 1957. The receipts from the Suez Canal tolls reduced the pressure on the balance of payments caused by increased imports for development purposes. The greatest change in invisible disbursements was the rise in government expenditure abroad. This item ranged from LE. 5.1 million in 1950 to LE. 27.9 million in 1959.¹ This rise was affected considerably by expenditure on educational missions and on the foreign office.²

1. Ibid, p.149.

2. Ibid, p.149.

Disbursements of interest, dividends and profits of foreign business scored an average of LE. 12 million during the period 1950-1959, reaching the highest level in 1954 with LE. 18.1 million. "A declining tendency is quite evident after 1956 due mainly to the nationalization of the Suez Canal and the promulgation of the Egyptianization laws which stipulated the conversion of foreign liabilities in banks and insurance companies into Egyptian holdings."¹

2. The Trend In the Deficit Of The Balance Of Payments On Current Account.

Each of the above mentioned trends has had either a negative or a positive effect upon the balance of payments on current account. The only time, however, when a positive balance was noted was in 1954. During the period under consideration (1953-60) the highest deficit registered was that of 1959. During this year sizeable development equipment was received and was mainly responsible for raising imports from LE. 214 million to LE. 235 million in one year. Exports increased too but only slightly. During the following year 1960, import of development equipment continued to increase, but exports were raised by about LE. 30 million. The deficit of the balance of payments on current account dropped from LE. 36 million in 1959 to LE. 25

1. Ibid,

million in 1960

With regard to the same eight years, the total deficit of current transactions amounted to LE. 178 million as Table XVII reveals. The total deficit of merchandise accounts was LE. 386 million and the total surplus of invisible transactions was LE. 208 million during the same period. Assuming that only 30 per cent¹ of the imports consisted of metals, machinery, and apparatus and other development items the total value of imports of this category amounts to LE. 483 million. This figure is LE. 100 million greater than the total deficit of the balance of trade during the eight years apart from the imports of petroleum, coal, and other raw materials imported for industrial and agricultural development. The deficit of current transactions is less than half the value of the capital equipment imported. In other words, the greater part of imported capital equipment was financed from domestic sources.

B. STERLING BALANCES AND OTHER FOREIGN ASSETS

1. The Rise And Decline Of The Sterling Balances

There were in the possession of Egypt assets abroad in the form of Sterling Balances that constituted a claim against Britain.

1. Based on the two minimum and maximum ratios mentioned above: 22.5 per cent and 37 per cent.

TABLE XVIII

THE DEFICIT OF THE BALANCE OF PAYMENTS ON CURRENT ACCOUNT OF U.A.R (EGYPT) **

	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960 +	8 years Total
<u>1-Merchandise Ac-</u>												
<u>counts</u>												
Receipts	184.8	201.9	145.6	135.3	139.8	133.1	129.9	166.-	161.-	164.-	192.9	
Payments	221.7	241.9	210.5	165.2	150.7	190.3	192.3	217.5	214	235.3	250.7	
Trade Balance	-36.9	-40	-64.9	-29.9	-10.9	-59.2	-62.4	-51.5	-53	-71	-57.8	386
<u>2-Other Current Ac-</u>												
<u>counts</u>												
Receipts	82.3	90.3	73.1	79.8	82.4	94.2	88.9	71.2	89.2	100.6	105	
Payments	55.8	65.5	61.6	67.8	67.9	71	59.5	50.9	56.3	65.6	72.3	
Balance	+26.5	+24.8	+11.5	+22	+14.5	+23.2	+29.4	+20.3	+32.9	+35	+32.7	208
<u>3-Balance of Curr-</u>												
rent Accounts	-10.4	-15.2	-53.4	-7.9	+3.6	-34	-33	-31.2	-20.1	-36	-25.1	178.1

Source: National Bank of Egypt, Economic Bulletin, v.XIV, p.151, (1961).
+ : Estimate, Ibid, No.3, Table 17.

** Including Trade with Syria.

These balances cumulated during the World War II from a surplus in the Egyptian balance of payments. The surplus was due to the expenditure of British troops in Egypt of Egyptian pounds that had been borrowed, mainly, from the central bank. The impact of this way of borrowing has caused a great inflation in Egypt on one hand, and deprived Egypt of a source of development financing on the other hand. However, it is quite doubtful whether these savings could have been realized at all were they not forced by the circumstances of war and by the inflationary measures used to force this saving. What was certain^{was} that the balances lost a great part of their value by the continuous rise in prices abroad, by the depreciation of the value of Sterling pound.

Immediately after the war the sterling balances declined rapidly because of the great deficit in the Egyptian Balance of Payments. Between 1945 and 1951 about half of the sterling assets were withdrawn. These assets were estimated at \$1408 million in 1945 and \$783 million in 1951.¹ Out of the difference, \$120 were converted into monetary gold.* The rest was used to offset the greater part of the deficit of the balance of payments on current account.

1. Economic Development in the Middle East, 1945-1954, p.16
New York: U.N., 1955 (Arabic).

* LE. = \$2.87 at official rate.

The New Regime was determined to reserve the sterling balances for essential imports, especially development equipment. The realization of this objective was made possible by the adoption of a foreign trade policy which discriminated against import of consumption goods and favoured imports of development commodities. It was already shown that the value of the development capital equipment imported alone was more than double the deficit of the balance of current accounts. The policy of restricting unnecessary imports was effective. The rise of the deficit in the balance of payments on current account later was due to the increasing importation of capital goods. After the sterling balances are depleted, credit facilities offered will become the main component of the rest of the world. In fact "the second half of the last decade saw the end of the sterling balances and dispensed with the comfortable privilege of recouring to the accumulated forced surpluses of previous years."¹ In the absence of these balances, the great rise in imports shall definitely result in recouring to credit facilities offered by the rest of the world.

Table XIX shows the change in foreign assets held by Egyptian official and private banks. The central bank's holdings have included a constant amount of monetary gold which has always amounted to about LE. 60 million ever since 1951. The de-

1. National Bank of Egypt, Economic Bulletin, v.XIV, p.30, (1961).

crease in foreign assets is due to the decrease in sterling assets because first the assets were dominantly sterling and second, because foreign assets other than sterling were little more in 1960 than in 1952, as will be seen later.

TABLE XIX

EGYPTIAN FOREIGN ASSETS HOLDINGS

in LE. million

	1952	'53	'54	'55	'56	'57	'58	'59	'60	Total Change
Central Bank	249	241	247	217	189	162	141	127	128	-121
Deposit Banks	13	13	13	11	8	17	27	36	27	+ 14
Total Change;		-8	+6	-32	-31	-18	-11	-3	-8	-107

Source: I.M.F. International Financial Statistics, v.15, p.110, (March 1961).

Excluding LE. 60 million, which is monetary gold, the actual remaining foreign assets at the disposal of the U.A.R. at the end of 1960 amounted to LE. 95 million. The market value of these assets is actually less because of capital loss on the nominal value.¹ When they are used for exchange the market value is the one that counts. The value of the total remaining assets in dollars adds up, according to the International Financial Statistics with all banks to \$184 million. At the official rate of \$2.87 = LE. 1, the total remaining assets amount to LE. 64 mil-

1. International Financial Statistics, v.15, p.110, (March, 1962).

lion. The National Bank reports the figure LE. 60 million as of the same date, end of 1960.¹ Since a great part of the remaining foreign assets is not sterling, the sterling balances are practically at an end.

2. The Uses Of Sterling Balances By The New Regime

The U.A.R economy has benefitted from the foreign holdings to the value of LE. 107 million during the period under study, 1953-1960. The average deficit on current account as Table XIX shows, was about LE. 22 million. The foreign assets reduced the liability for this deficit by about 60 per cent. At the same rate foreign assets can still be of use for another 4 or 5 years. But the planned development projects have increased by three-fold in one year, from LE. 98 million in 1959/60 to LE. 284 million in 1960/61. The development projects are supposed to exceed this rate in the following years. The pressure on the balance of payments on current account will increase by far more than the export trade can offset. The Five-Year Plan, starting 1959/60, estimated the contribution of the rest of the world at LE. 500 million out of a LE. 1650 million which is the total financing required.² This is over and above compensation

1. Economic Bulletin, v.XIV, p.31, (1961).

2. U.A.R Government, Yearbook, 1961, p.424, Cairo: 1961.

remittances expected to be paid.

The drop in sterling assets was not all due to imports alone. There were liabilities outstanding and liabilities created during that period and were paid from these assets. In 1957, sterling pounds 19.5 million were paid to the Sudan to redeem the National Bank's liability in connection with the Egyptian pounds circulating till that year in the Sudan.¹ The compensation to the Suez Canal shareholders was about LE. 23 million, payable in five installments. Two installments were paid in 1959 and 1960. LE. 15 million are to be paid to the Sudan in compensation for the damage accruing from the High Dam construction. The first installment, out of four, was due in January 1960.² The compensation for Egyptianization of most foreign, French and British assets in Egypt, amounted to sterling pounds 27.5 million out of which £3.5 million were paid in 1959 and the remainder was paid in 1960.³ Accordingly, compensations paid from sterling assets were LE. 5.3 million, LE. 6.5 million and LE. 33.4 million in the years, 1958, 1959, and 1960 respectively.⁴ These capital

1. International Monetary Fund, International Financial Statistics, v.14, p.112, (Feb.1961).

2. I.M.F. International Financial News Survey, v.12, p.168, (1960).

3. Ibid, v.11, p.28, (March, 1959).

4. Economic Bulletin, Table 17, No.2, v.XIV, (1961).

remittances are not included in the balance of payments on current account.

3. The Role Of Sterling Balances In The "Rest Of The World"

Table XX shows the share of the sterling balances as one of the two main sources of the "rest of the world". An attempt is made to sum up all findings with regard to the Rest of the World in one statement in an "account form". The method used to compute the figures in the said table is mentioned under the table itself. The figures are the result of the tables and findings already presented in this chapter.

The difference between "uses" and the sterling balance source is credited to foreign liabilities except for approximately ^{L.E} 3 million donations. These were offered by Kuwait and China in the years 1956 and 1957. Other donations were not mentioned among capital nor current receipts by the sources reporting foreign transactions. Donations in kind do not pass through the Exchange Bureau, which prepares the foreign accounts. Only the International Financial Statistics mentions donations received from official and private foreign sources and these are reproduced below.¹

	<u>1952-53</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>
Official	none	1.3	2.7	9.-	3.4	0.3	none
Private	none	1.-	7.4	2.6	0.2	0.8	none

1. I.F.S. v.14, p.119, (Feb.1961) and Ibid, (Feb.1957).

Where donations are sizeable as in 1956 the balance of current transactions, as reported by the International Financial Statistics is greater than that reported by the National Bank, the source of Table XVIII above. This suggests that the I.F.S. included donated items in the imports and in the proceeds. On the other hand the data in table XVIII excludes the said donations.*

TABLE XX

REST OF THE WORLD

USES AND SOURCES OF FUNDS

For the period 1952-1960

in LE. million

Sources		Uses	
Sterling Balances ¹	136	Deficit of Current Accounts ³	178
Donations	3	Increase in Foreign Assets ⁴	29
Increase in Foreign ²		Compensations (Paid during	
Net Liabilities	<u>123</u>	the last three years)	<u>55</u>
	<u>262</u>		<u>262</u>

Sources: 1. Economic Bulletin, v.XIV, Table 17, No.3 p.152, (1961).

2. Balance of the Account.

3. Table XVII.

4. The difference between the 136 above and total change in foreign assets: 107, Table XIX.

Donations were not entered by the Foreign Exchange Bureau on the receipts side nor on the payments side. Donations

* The details, in the Economic Bulletin on the balance of payments mentions only the donations we presented, in turn, in Table XX.

mentioned later are therefore treated as an addition to the Rest of the World "sources" under Donations. On the other hand they are an addition to the rest of the world "uses" under Deficit on Current Account.

Net capital remittances, other than donations and compensations, were not significant during the period. Some reports include the International Bank's loans and the International Monetary Fund's facilities, and the value of American wheat imported against Egyptian pounds among capital remittances.¹ These facilities created a liability to the U.A.R and, therefore, they are included in the LE. 123 million in Table XX. For the purpose of this thesis they are treated, like other liabilities as credit facilities offered by the "rest of the world." However, a distinction will be made to show the difference in the terms of different credit facilities. These facilities are the subject of the second part of this chapter, since they are the second component of the "rest of the world", after the first component, foreign assets have been treated.

C. DEVELOPMENT FINANCING FROM FOREIGN FACILITIES

1. Foreign Equity Financing.

The earlier policy of the New Regime with regard to fo-

1. National Bank, Economic Bulletin, Table 17, No.3, v.XIV (1961).

reign capital was to encourage foreign equity investment. Law No.156, promulgated in 1953 allowed foreign share in business to rise from 49 per cent to 51 per cent in order to encourage foreign private capital to flow in. Another privilege was offered to foreign private investors in 1954. Law No.475 permitted the outflow of foreign capital after five years of its investment at the rate of exchange prevailing at the time this capital flowed in. The law stipulated that the return of capital in one year may not exceed 20 per cent of the total. All profits of such foreign capital, beside 50 per cent of the salaries of foreign technicians employed in Egypt were allowed to be paid in foreign currency at the official rate.¹

Foreign capital has also benefited from the general regulations and supportive measures taken with the intention to raise the profitability of invested capital. All new capital, foreign or domestic, was exempted from business income tax, for a period of seven years provided it was invested in fields deemed essential to the economy. Imports of raw materials and equipment for development purposes were exempted from customs duties. Other measures taken to support investment, applied to foreign equity financing as much as they applied to domestic financing.

1. Amin Abdulla, History of Egyptian Economy, pp.497-501, Cairo: 1955.

Foreign equity financing, however, continued its declining trend which had started before the period under consideration. In the two years 1948-1950, foreign investment amounted to LE. 788,000; in 1955 it reached 900,000 and declined later to negligible levels in 1956 and 1957.¹ According to the International Financial Statistics, there was a net outflow of capital during the period 1953-1959.² The following figures show the movement of private capital in each of the said eight years, consecutively: -1.2, -1.7, -5.2, +2, +1, -1.2, and -0.6. The figures are in LE. million. There was more outflow of private capital than there was inflow.

The attitude of the State toward foreign equity has undergone change ever since 1956. In a press conference held with German press representatives, President Nasser made it clear that Egypt preferred obtaining foreign loans to receiving equity financing. He also added that before 1957, there were years when the profits of foreign capital reached about LE. 20 million.³ Total earnings of foreign enterprise, transferred to countries of origin, dropped sharply after the nationalization and Egyptianization laws of 1956 and 1957. These transfers amounted to LE. 200,000 in 1957, to LE. 415,000 in 1958, and to LE. 225,000 in 1959.⁴

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1. Federation of Chambers of Industry, Yearbook, 1954/55, p.23 Cairo; (Arabic). and Yearbook, 1959/60, p.23, (French). and Egypte Industrielle, p.6 (Feb.1961).
 2. I.F.S. v.19, p.114, (February, 1961).
 3. Middle East Economist, v.III, p.58, Cairo: (Jan.1960).
 4. Ibid, p.18, (December, 1960).

The British and the French, two of the leading foreign investors in Egypt were the least to respond to the encouraging facilities offered. It is believed that the lack of response is due to two factors: first, foreign capital preferred fields of investments that were not deemed essential by the New Regime; and second, foreign private capital required greater guarantees of safety and freedom of action that an independent state, embarking on economic development planning and ^{having} socialistic views, could not give. Thus direct foreign investment ceased to be a significant factor in development financing in Egypt and the nationalization measures put a final end to the slight hope of any receipts from this source.

The German Demag Company has agreed to participate in the capital of the Iron and Steel Factory with an amount equal to 20 per cent of the total f.o.b. price of all deliveries of equipment.¹ The company itself supplied and installed the equipment required by the plant. This type of equity financing that carries with it technical skills continued to be favored by Egypt. In 1959 other small industries which called for greater skill such as the cosmetics and medication industries, were realized by foreign private participation. They were allowed

1. International Monetary Fund, International Financial News Survey, v.6, p.281, (March, 1954).

to hold high shares amounting in some instances to 60 per cent in the firms established.¹ With their technical help and under their brands, cosmetics and pharmaceutical products appeared in the markets. The total capital of these companies, however, has not exceeded LE. 1 million.² Among these companies are the German Wella, the American Max Factor, and the Pfizer-Egypt joint stock company for the production of antibiotics under the American Pfizer brand.

2. Loans And Advances

Neither the exhausted foreign assets, nor the meagre foreign equity financing will be able to finance the rising foreign requirements for economic development in Egypt. While the role of these two foreign sources has been declining, a third source was rapidly rising to become of major importance to foreign financing, namely the foreign credit facilities. This type of financing gained popularity among the recipient countries because of merits not normally available in equity financing. First, it is limited with regard to time and yield for the recipient knows exactly the date of settlement and the cost. Second the loans fit into the economic development planning, in the sense that they are used to develop economic fields that are

1. Middle East Economist, v.II, p.12, (November,1959).

2. Ibid.

thought most beneficial for national economy. On the other hand the credit suppliers encounter less capital and yield risks and are given guarantees to this effect. In addition to this credit suppliers gain the ordinary trade profits, guarantee the sale of their own products and the investment of the surplus of their balance of payments at least risk. The greatest guarantee is the rising productivity of the economy that receives the loans in the form of reproductive equipment, in most cases supplied, installed and run for an initial period by the creditor. This was the case with the Egyptian credit agreements with the economically and technically advanced creditors.

a- The Magnitude of the credit facilities required for Development Financing

Credit facilities include all payments for the rest of the world which may be postponed, for more than one year, according to payment agreements negotiated between Egypt and the respective foreign creditors. Egypt has debtors too, ^{* however} the total credit facilities allowed are greater than the net indebtedness. According to Table XX, the net outstanding indebtedness of Egypt to the rest of the world has amounted to about LE. 123 million, at the end of the year 1960. This includes the Egyptian receipts of American agricultural surplus and excludes

* For instance, in 1957 commercial banks and the Agricultural Bank allowed a credit to foreign importers of Egyptian goods to the amount of LE. 14 million. Samir Amin, Statistics of General Equilibrium, pp.196-197, Cairo: 1959.

donations. The value of the American wheat and other agricultural supplies offered was deposited in Egypt in a non-resident account. In other words, the value was paid in Egyptian pounds. The cumulative value of the agricultural surplus sold in this way to Egypt amounted to LE. 51.8 million at the end of 1960.¹ A part of this American money in Egypt, was extended to the government and public firms, as shall be mentioned later. With regard to donations received in kind a brief description comes later.

The most serious attempt to negotiate loans abroad was started in 1957. The same year witnessed two changes in the economic strategy with regard to foreign economic relations. The government could no more count on foreign equity investment. On the contrary they took the first step to liquidate foreign equity already invested and used foreign currency for compensation. Secondly, the first Five-Year Industrialization Plan was promulgated in 1957; the foreign capital equipment required by this plan was estimated at half the total cost, about LE. 150 million. During this year the foreign assets that Egypt held abroad were blocked in England. The first part to be released were to be used to pay the compensations to Britain and France. In order to realize the Industrialization Plan, there remained

1. National Bank of Egypt, Economic Bulletin, v.XIV, Table 17, No.2, (1961).

only one course open before Egypt and that was to obtain equipment and skill from the only few developed countries that agreed to offer them on credit basis. The main two sources were Russia and West Germany. After three years of abstinence the United States resumed offering credit in 1959. The Minister of Economy announced in July 1960 that the U.A.R "government had concluded technical and economic cooperation agreements with a number of foreign countries in order to obtain credit facilities, loans and the services of experts. These agreements, among other means, are adopted to speed up implementation of the Five-Year Industrialization Plan. Credit arrangements amount to about LE. 355 million, of which only LE. 113 million has so far been used."¹ The line of credit allowed reached LE. 355 million, out of which LE. 113 million were used until July 1960. This does not include any credit facilities obtained for consumption goods like wheat obtained from the U.S.A and a loan for a similar purpose from Italy. It includes the part of these latter loans that was borrowed from the two parties, in Egyptian currency, to apply to development projects.

The utilization of these facilities created rose from LE. 113 million in July 1960, to LE. 156 million in July 1961 which was supposed to be the date of the fulfilment of the first

1. Middle East Economist, v.III, p.4, Cairo: (August, 1960).

Industrialization Plan. The amount of foreign currency used was close to estimates. The contracts to supply equipment and technical help were mainly signed with the countries that extended the credit. At least one loan escaped this rule and that was the loan from the International Bank to the Suez Canal Authority amounting to LE. 20 million out of which LE. 11 million were used at the end of 1960.¹ The Russian loans agreements allowed U.S.S.R. to utilize the experts and products of East European countries. Table XXI shows the size of the contracts signed with various countries to implement projects on credit basis. The number of countries reached seventeen, representing both East and West camps. The overall Five-Year Development Plan envisaged the need to draw on this source at an average of LE. 100 million per year. There were LE. 242 million outstanding facilities in July 1960.² The outstanding credit facilities have risen to LE. 269.2 million in July 1961 according to Table XXII inspite of the use of about LE. 62 million during nine months. In July 1960 the foreign credit facilities used amounted to 113 as has been just mentioned; in July 1961 the cumulative use of foreign facilities has risen to LE. 175 million as Table XXII shows. These figures suggest that the resort to foreign facilities during the second year of the Five-Year Plan has been close to the average envisaged by the Plan. On the other hand, negotiations were successful in creating a

1. National Bank of Egypt, Economic Bulletin, Table 17 No.2, v.XIV (1961).

2. Egypte Contemporaine, v.51, p.27, (October,1960).

line of foreign credit close to the size of the foreign facilities required for financing the foreign goods and services required for development by the Plan.

TABLE XXI

DEVELOPMENT PROJECTS AND CREDIT FACILITIES ALLOWED TO FINANCE THEM, BY COUNTRIES

in LE. million as of end of 1960.

Creditor Country	Projects	Value	Total Value
U.S.S.R.	53	46.9	
East Germany	23	6.5	
Checkoslovakia	13	3.6	
Hungary	1	0.1	
China	1	0.2	57.3
U.S.A	28	10.-	
West Germany	76	53.9	
Italy	28	19.5	
Britain	19	5.6	
Switzerland	23	4.2	
Japan	11	3.9	
Six other Western Countries	30	2.1	99.2
			156.5

Source: Chambers of Industries, Egypte Industrielle v.37, p.6, Cairo: (February, 1961).

b. Terms and Structure of the Loans and Advances

Table XXII shows the large number of countries which offered credit facilities to the U.A.R. These facilities were almost equally divided between the Western Countries and the East-European Countries. The benefits from this diversification of

credit are numerous and may be observed from studying the terms and uses of the credit allowed by the respective parties.

1- Rate of interest

The rate of interest on long-term loans received from Russia was $2\frac{1}{2}$ per cent on the balance of loans used.¹ No lower rate was ever offered to Egypt by any other source. Other East-European countries charged the same rate. It is believed that no such terms could have been obtained from the customary suppliers of capital namely Britain and France. Prior to this deal with Russia the I.B.R.D. failed to extend any loan to Egypt. When it agreed to give the LE. 20 million Loan to the Suez Canal Authority in 1960 the rate of interest was 6 per cent.² American long-term loans offered in 1959 and 1960 were bearing $4\frac{1}{2}$ per cent interest. Similarly, West-German long and medium term loans were bearing $4\frac{1}{2}$ per cent.³ Terms of Japanese loans were similar to the terms of German loans.

2- Duration of Credit and Terms of repayment

Short-term credit, with five years duration or less, were usually negotiated after a sizeable deficit appeared on the balance of payments of Egypt to the respective countries. The first significant agreement of this sort was signed with West-Germany in 1956. The cumulative deficit was about DM. 63 million. Germany accepted to allow the deficit to increase by another DM. 22

1. Middle East Economist, v.II, p.39, Cairo: (Jan.1959).

2. Middle East Economist, v.III, p.12, Cairo: (June,1960).

3. Ibid, p.2, (October, 1958).

million, and the total be paid in five annual installments at a rate of 2 per cent.¹ Since there was no perceptible deficit in the balance of payments with East-European countries there were no short-term facilities negotiated with this block.

The greatest part of the credit facilities offered by Italy was due to a deficit in the balance of payments to this country, mainly due to wheat imports. The deficit in 1959 reached LE. 18 million. It was agreed that it should be paid in installments over a period of 16 years.²

The deficit on the balance of payment with the U.S.A. arising mainly from wheat imports was treated in another way. Payment for the wheat imported was effected in Egyptian pounds. The non-resident account of the U.S.A. so arising was a source of borrowing from which the U.S.A. extended several loans to the government and other public organizations. American government loans were longer in duration of all the other loans. A loan of LE. 4.5 million from the value of the wheat surplus was extended to the Television Authority which had to be liquidated over 30 years at a rate of 4 per cent.³ A similar loan was extended to the Industrial Bank.

1. International Financial News Survey, v.8, p.280, (March, 1956).

2. Ibid, v.12, p.304, (April, 1960).

3. Middle East Economist, p.8, v.III, (March, 1960).

The Export-Import Bank of Washington offered two short-term loans to a chemical company. One for $3\frac{1}{2}$ years and the other was for five years negotiated in June 1959, after the first loan has been fully paid. The two loans amounted to \$12.2 million.¹ In August 1959 another \$12 million loan was offered by the same bank to the Railways Authority. A third loan of \$22.5 million was offered to the government in September, 1959 payable on installments over 8 years. All American loans were to finance purchases of locomotives, industrial equipment, and tools in the U.S.A.²

The loan of the International Bank to the Suez Canal, signed on December 22, 1959 was payable over 13 years, in 26 semi-annual installments beginning March 1962.

Long-term credit from West-Germany reached DM. 400 million in October 1958. The duration was 10 years. A similar agreement with Japan to the amount of \$30 million was signed in September 1958. Both creditors received a down payment of 10-20 per cent; the remainder to be repaid in 10 annual installments. German long-term credit increased after 1958 as shown in Table XXI.

Agreement on the first line of credit with Russia was reached late in 1957. The value of the loans used for industrial development was redeemable in 12 annual installments beginning in

1. I.M.F. International Financial News Survey, v.12, p.6 (July, 1959).

2. Ibid, p.546.

1964. The maximum credit allowed by this agreement was about LE. 61 million.¹ The second and third lines of credit negotiated in 1959 and 1960 were to finance the High Dam project. Repayment was to start after the completion of the project, in 12 annual installments. The line of credit opened for this project was estimated at LE. 130 million,² all repayments to be effected in Egyptian pounds.

3- Size and Use of credit facilities

Table XXII shows that credit facilities reached LE. 443.8 million. Out of these facilities, LE. 269 million were not used up till March 1961. The U.S.A. loans and advances shown in Table XXII include the balance of the non-resident account arising from sale of agricultural surplus against Egyptian currency. This was also the case with Italy which supplied consumption commodities. The rest of the loans, including the American and Italian loans from their Egyptian balances, were borrowed to finance development projects. The portion of these loans already used has been paid against equipment and technical service procured from the countries extending the loans. The largest single creditor was Russia, only the amount used out of the high line of credit offered was relatively small. This was because of the long time required before the High Dam is finished, and because the balance of payments with

1. Middle East Economist, v.II, p.39, Cairo: (Jan.,1959).

2. I.M.F. International Financial News Survey, v.12, p.241, (February, 1960).

TABLE XXII

FOREIGN LOANS AND ADVANCES

LE. million*

	Total Credit Allowed	Used till March '61	Balance Available
<u>From Eastern Block</u>			
U.S.S.R	186.-	32.6	153.4
Easter Germany	9.5	3.4	6.1
Checkoslovakia	9.2	7.1	2.1
Hungary	5.9	----	5.9
Yougaslavia	7	4.3	2.7
Total	217.6	47.4	170.2
<u>Western Block</u>			
U.S.A	68.1	41.3	26.8
Western Germany	53.1	30	23.1
Italy	34.3	15.9	18.4
Japan	17	11.4	5.6
France	10	----	10
U.K	5.4	5.4	----
Holland	5	0.5	4.5
Switzerland	4	1.9	2.1
Sweden	3.3	3.3	----
Others	6.3	6.3	----
Total	206.5	116.-	90.5
I.B.R.D.	19.5	11.2	8.5
Grand Total	443.8	174.6	269.2

* Source: Al-Ra'id Al-Arabi, v.II, No.13, Beirut, (November, 1961), in Arabic.

Russia has in some years shown a surplus in favor of Egypt. Next comes the U.S.A because of the large agricultural surplus which was sold to Egypt against Egyptian pounds. Third comes Germany

with credit facilities allowed amounting to LE. 53 million. Table XXI has shown that work contracts taken by West-Germans were greater than work contracts taken by Russia. Germany was given the greatest part of industrial construction in Egypt. The value of their contracts exceeded the line of credit they allowed to Egypt. They obtained contracts to supply equipment and build the main parts of the largest two industrial projects devised in the U.A.R., the Hydroelectric plant at Aswan and the Iron and Steel Works at Hilwan.¹ The total cost of the two firms amounted to LE. 55 million. The contracts with Germans as with Russian, Japanese, and American concerns were to supervise production for a period of time to train Egyptians.

Various specialized technical institutions were opened in Egypt. Instructors, especially in metallurgic fields were Germans. In the fields of oil and medicine production techniques, Russian instructors were called upon. The Japanese assisted in building dockyards and food processing factories. Americans were the earliest to offer free technical assistance. The American USOM assisted in making the first comprehensive survey on the development opportunities available in Egypt. The result, which appeared in the "Opportunities for Industrial Development in Egypt" (1955) was very helpful in preparing the first Industrialization Plan. Another American public institution (EARIS) offered

1. Middle East Economist, v.5, p.54, Cairo: (May, 1955).

technical assistance to rural economy and supplied heavy equipment to reclaim fallow land. The total value of equipment and technical help offered for the said projects and for building roads and railways was estimated at \$40 million. Assistance however ceased in 1956 before the total value was used. Later in March 1959 it was resumed and the balance of all said assistance funds was again allocated to the Egyptian Government.¹ The balance amounted to LE. 9 million. The Railways Authority received a large number of diesel locomotives, partly from grants and partly through long-term loans from U.S.A.

Other grants which were fully utilized were offered to Egyptian students by German, American, and Russian technical schools and universities. The grants however do not appear in the above tables nor on the balance of current transactions. The grants from the rest of the world are added to the deficit of the balance of payments on current account in order to get the real contribution of the rest of the world to development financing.

CONCLUSION

The total credit facilities used, as revealed by Table XXII amounted to LE. 175 million, while the net increase in the liability to the rest of the world in Table XX was LE. 123 million.

1. Egyptian Economic and Political Review, v.VI, p.33, Cairo: (January, 1960).

It is to be kept in mind that there is a difference of three months between the dates. In July 1960 cumulative credit facilities used amounted to LE. 113 million as mentioned before, a difference of LE. 62 million used in nine months. Therefore, time accounts for a part of the difference between the two figures. Second, a part of the used credit facilities should have been already settled as is stipulated in the terms of these loans and advances. All the loans were payable in installments. Third, the LE. 123 million is the "net" liability, Egyptians must have offered credit to the rest of the world, as has been noted.¹ As the sources of the data are also different, no claim can be made to the effect that the data are free of error and omission. The LE. 123 million which is the balance in Table XX included the net charges in non-resident accounts. Table XXII does not seem to have accounted for all changes in non-resident accounts. The data in the table account only for the countries that offered assistance according to signed agreements. Net outstanding facilities offered by the International Monetary Fund, alone at the end of the years 1956 through 1960, in U.S. dollars reached, 15, 30, 27.3, 52.5 and 49.8 respectively.²

In spite of the possible error in data, the trends revealed are reliable. The tendency is towards greater reliance on credit

1. See footnote, p.128.

2. I.M.F., International Financial Statistics, v.15, p.114, (February, 1962).

facilities from the rest of the world for financing development. That is due to the ambitious development plans that require foreign purchases of goods and technical services more than what the increase in exports can offset. Since the Egyptian foreign assets are being depleted and equity financing is negligible there shall be greater resort to the line of credit offered by the various countries. Foreign developed countries show increasing tendency to offer such help because of the international peaceful competition, because of surplus in their balance of payments and because this is the type of international financing acceptable and surely redeemable by Egypt. The greatest assurance of the country's capacity to pay is the fact that the loans are applied to development projects that are implemented according to prepared plans aiming at ultimate surplus in the balance of foreign payments.

C H A P T E R V

THE PRICE LEVEL TREND AND THE ROLE OF DEVELOPMENT EXPENDITURE

Introduction

Chapter V will be treating the problem of price level in the United Arab Republic during the period 1953-1960. Price level trend is to be determined by reference to the wholesale and cost of living indexes that are available.

The role of development financing in shaping the price level trend will be assessed, and other factors that contributed to the change in the price level will be discussed. All factors discussed might have been influenced, in turn, by the development financing methods and policy. While treating each of the relevant factors a reference to the role of development financing is made.

In the course of studying the role of development expenditure and other factors in price changes many of the main points covered in the preceding chapters are used for illustration. By pointing out the main issues already treated this chapter will also serve as a summary of the previous material.

A. TRENDS IN PRICE LEVELS DURING 1952-1960

1. The Official Price Indexes

The data in Table XXIII were compiled from two sources namely the National Bank of Egypt and the International Financial Statistics. Both data show almost similar trend with regard to price movement over the period 1952-1960. Beginning in 1951 and continuing up to 1955, the wholesale prices and the cost of living had declined only to mount again during 1956 and 1957 and then to achieve fair stability thereafter. Wholesale and cost of living indexes have moved in the same direction but the cost of living was moving at a lower rate. This phenomenon was due to greater control over the prices of the main items included in the cost of living index. There were too subsidies allocated to reduce the cost of living, as shall be mentioned later.

Over the whole period the magnitude of change was moderate. According to the two sources the index of the cost of living, as of the end of 1960 was only 4 per cent greater than seven years before while the wholesale index rose by 18 per cent over the same period. The greatest rise in price level, according to Table XXIII, reached 8 per cent in the cost of living and 22 per cent in the wholesale index.*

* Resulting from dividing the index as of the end of 1957 by the index at the end of 1954.

TABLE XXIII

WHOLESALE PRICE AND COST OF LIVING INDEXES, 1950-1960

End of:	Cost of Living Index		Wholesale Index	
	I.F.S.**	National* Bank	I.F.S.**	National* Bank
1950		306		376
1951		328		386
1952	107	296	105	343
1953	100	294	100	354
1954	96	283	92	342
1955	96	283	99	351
1956	98	297	110	415
1957	102	306	119	419
1958	102	301	118	418
1959	103	304	117	418
1960	103	306	118	418
1960--1953	103%	104%	118%	118%
1957--1955	106%	106%	120%	120%
Greatest Change	7%	8%	22%	22%

Sources:

* National Bank of Egypt, Economic Bulletin, v.X, p.221, (1957), and Table 21, No.3, v.XIV, (1961).

** I.M.F., International Financial Statistics, v.XV, p.110, (February, 1962).

Few countries in the whole world were able to maintain a lower rate of increase in the cost of living. Taking 1953 as a base, the cost of living index as of the end of 1959, in a number of countries was as follows: Lebanon 118, Tunisia 114, Sudan 115, Morocco 118, Algiers 131, Israel 142, Cyprus 135, U.S.A. 109, England 120, India 113, Spain 150, Iran 163, Turkey 172 (end of 1958), Uruguay 224, Argentina 464, Chile 1043, and Egypt 103.¹

1. Compiled from: International Labor Review, Statistical Supplement, v.81, pp.125-132, Geneva: International Labor Office, 1960.

Many countries which embarked upon development schemes faced inflationary tendencies as can be seen from the index numbers for Spain, Turkey, Iran, and Israel. Arab states listed above have had a rise in the cost of living over the six-year period at a rate of 2 per cent or more per year.

Careful examination of the data on Egypt is necessary before a reliable comparative analysis can be made. The source of all the data is the Department of Statistics and Census. The cost of living index is based on family budget expenditures. The families taken into account are those of the lower middle class whose monthly income ranges between LE. 12 and LE. 18 and with 6.3 members on average.¹ The main expenditure groups and the weight given to each group (percentagewise) are: food, fuel, and soap 45, rent 16, fares 13, petty expenses 5.8, sundry expenses 7, clothing 16.7, school fees 6.5.² In the clothing group alone, 33 representative items are selected and weighted according to the significance of each to the average family.

The Index Number of Wholesale Prices "cover 88 items subdivided into 278 varieties for which 583 quotations are collected weekly. Monthly prices are averages of the weekly prices."³ The number of quotations per item is relative to its importance.

1. L'Egypte Contemporaine, v.XLIV, p.102 (1953).

2. Ibid.

3. Ibid, p.87.

or weight, in the whole sample. The articles selected comprise practically the main staple commodities used in the country irrespective of whether they are imported or produced locally. The 88 items are divided into 15 groups, six pertaining to foodstuffs and nine others. The foodstuffs are: cereals; dairy products; edible oils; meat and fish; sugar, tea, coffee, and others. The other nine consist of: fuel; soap and chemicals; paper; building materials; and pharmaceuticals. Each group is also weighted according to its significance.¹ The implicit weight of raw cotton is about 15 per cent.²

2. The Effect Of Price Control On The General Level Of Prices

An objection to the reliability of the above data arises from the effect of price control on the said indexes. Most of the important commodities covered by the wholesale index are controlled and subjected to domestic taxes or subsidies, "and it is their domestic prices that are included in the index."³ The price-control policy aimed mainly at preventing individuals and groups from taking advantage of the circumstances created by the overall development policy. The development policy created shortage in the supply of certain commodities or services by diverting resources to production of other commodities. Accidental short-

1. Ibid.

2. I.M.F., International Financial Statistics, v.XIV, p.113, (November, 1961).

3. Ibid.

age could have raised the price of an important commodity; such a rise could have developed into general inflation. Among the commodities that could have caused a spiral rise in prices is labor. Both positive and negative measures were taken to control wages. The commodities that constitute the cost of living were controlled to maintain the level of the real income of the workers, on the one hand, while on the other labor was prevented to seek raises by resorting to strikes or collective action. A law was passed to this effect. In case of conflict in industrial relations arbitration was made compulsory and final.

Prices of almost all commodities were fixed at cost-plus basis. A margin of profit was set for each commodity imported or produced and the margin was divided between the respective dealers according to the risk and the turnover of each of them. Law No. 132 issued in 1952 made the labelling of prices of all commodities compulsory in order to allow the buyer to see the price and to allow authorities to check and to see to it that rules and regulations are being observed with respect to prices. Effective measures were used to enforce the law.

Prices were often revised in the light of changes in costs. When freight rates were reduced in May 1959, and customs tariffs on many goods for industries were cancelled, a list of 600 items was issued, prices of which were reduced.¹ A mark up on domestic

1. Middle East Economist, p.48, (July, 1959).

industries was fixed at a maximum of 30 per cent, of production cost. Experts were appointed to define costs.¹ For the purpose of determining costs and fixing the prices for fertilizers, timber, chemicals, and other imported products a committee^e was established consisting of the under-secretaries of Economy and Supply.² During the same year "a total of 2903 articles produced by 193 local companies had been subjected to price control in accordance with the cost-plus method."³ Resolution No.167, 1960 reduced all prices of imported medicines by 25 per cent. This resolution fixed the profit of retailers at 16 per cent. At this time the state became the only supplier of this line. Total profit on paper was fixed at 20 per cent, out of which the importer was entitled to 8 per cent and the wholesaler and retailer to 12 per cent.

The Government exercised control over the prices of both products and factors of production. On one hand the return to labor and capital was fixed at a "fair" level and, on the^{other} hand prices of products were fixed according to a formula: "cost plus normal profit." This formula, however, did not prevent a general rise in prices when inflationary forces were effective. It only

1. Ibid, p.48.

2. Ibid, p.36, (October, 1959).

3. Ibid,

eliminates the instability arising from institutional and individual practices in the short-run. It could not, however, prevent the shift in the general price level which was caused by forces beyond its power.

3. Subsidies To Reduce The Cost Of Living

The second objection to the reliability of the price indexes presented in Table XXIII arises from the inclusion of prices of subsidized items. The cost of living index for instance includes prices of major items which were subsidized by government allocations. The retail prices of such principal items like bread, kerosene, and edible fats are lower than the cost price; the difference is a loss to the government. Commodities have also been subsidized before 1952. In fact these allocations were reduced greatly after 1951/52 as the following table shows. It also shows the decrease in subsidies allocated for the purpose of reducing costs of living immediately after the coup d'etat. Figures are in million Egyptian pounds and years are fiscal years.¹

1951/52	18.3	1956/57*	8.9
1952/53	13.4	1958/59	6.7
1953/54	7.8	1959/60	8.9
1954/55	1.7	1960/61 ⁺	9.-
1955/56	1.9		

1. National Bank of Egypt, Economic Bulletin, v.9, (1956) p.186 and v.XIII (1959) p.103.

* Middle East Economist, v.III, p.23 (August 1960).

+ South U.A.R. Budget 1960/61, p.506, Cairo: Amiriyya Press 1961, (in Arabic).

What was spent to reduce prices of bread, oil, beans, corn, and kerosene during the first six years of the New Regime amounted to LE. 37.5 million but during the six years, 1947-1952, such subsidies amounted to LE. 63.4 million.¹

The allocations to reduce the cost of living made the deviation of the price trend narrower but they did not obscure the trend. Subsidies were greater when prices were rising and less when prices were declining. In 1956/57 subsidies rose to LE. 8.9 million from a figure of LE. 1.9 million in the preceding years. The year 1956/57 witnessed the sharpest rise in prices during the period. After 1957 the annual allocations to reduce the cost of living have not changed much because prices have been fairly stable. Therefore, if the subsidy factor is to be considered the corrected cost of living index moves along a line lower than the trend shown in Table XXIII when the trend declines, and above the trend when it rises. In other words the corrected cost of living trend becomes closer to the wholesale price index.

4. Determination Of the Cost Of Living And Wholesale Indexes

Dr. Samir Amin uses in his analysis a cost of living index that was 16 per cent higher in 1957 than the index in 1952,²

1. Minister of Finance, Speeches of President and Ministers to the National Assembly, p.197, Cairo: Amiriyya Press, 1957 (in Arabic).

2. Statistics of General Equilibrium, p.232, Cairo: Risala Press, 1959.

while according to Table XXIII the rise was only 3 per cent during the said period. It seems that Dr. Amin has taken his index from a source other than the Department of Statistics. There was one private firm that published an annual cost of living index, that has been reported by the National Bank of Egypt together with the official rate up till 1959. The index used by Dr. Amin seems to be taken from this firm. There was no explanation available about the way which this firm followed to obtain the indexes. The index of the said firm is presented below;¹

Before War	100	1955	302
1951	298	1956	309
1952	274	1957	319
1953	289	1958	324
1954	298	1959	324

The magnitude of change in the level of the cost of living shown by this firm is far greater than that shown in the official cost of living index. It has been already mentioned that the policy followed by the government to reduce the cost of living by subsidies resulted in making price fluctuations narrower. It might be concluded that this firm accounted for this factor by taking the price quotations of the subsidized items from the free market where these items are sold at profit as specified by the price control management. There have been two markets created for each commodity that was subsidized: one market sold limited

1. National Bank of Egypt, Economic Bulletin, v.VXII, p.231, and v.XIV, Table 27.

rations at the reduced price and another market sold free amounts at a specified rate of profit. Assuming the said private firm built its cost of living index on the free market quotations, this index would represent the real trend better than the official index.

The changes in the cost of living presented by the said firm were still less in magnitude than the changes in the wholesale prices, as presented in Table XXIII. The index reached its highest in 1958 and its lowest point in 1952/53. But the highest point the wholesale price index reached was in 1957 and the lowest was in 1954. The ratio of the highest point in the wholesale price index to the lowest was 122 per cent as in Table XXIII. This rise was reached in 3 years, from the end of 1954 to the end of 1957. The ratio of the highest cost of living index to the lowest cost of living index was 119 per cent according to the private firm. This rise was reached in a six-year period, 1952-1958. If the index of the private firm was to be accepted as the best representative of the cost of living trend the conclusion could be reached that the cost of living index was less subject to fluctuations, in the short-run as well as over the whole period, than the wholesale index. The factors responsible for this phenomenon were two: first, the wholesale index included more imported commodities and therefore was more susceptible to changes in prices of foreign commodities in terms of Egyptian currency.

Second, the wholesale index comprises less of the commodities that are subject to price control.

For the purpose of studying the forces that influenced prices and the effect of development financing on these forces, it is necessary to state the findings that are common among all price indexes that have been presented above. All price indexes show that prices dropped considerably in 1952. The rise in the following three years was slight. During the following two years 1956 and 1957 both wholesale and cost of living indexes rose sharply. In 1958 only the cost of living index showed one per cent increase. The wholesale index has been almost constant, over the three-year period 1958-1960. The index at the end of 1960 was 1/4 per cent below the index at the end of 1957.

It is believed that the wholesale index is more susceptible to be influenced by inflationary and deflationary forces than the cost of living index especially in the presence of the price controls and price subsidies. Therefore, in the remaining part of this chapter the discussion will concentrate on the forces that worked to shape the wholesale price index as described above.

B. CAUSES OF CHANGE IN THE PRICE LEVEL.

Changes in the general level of prices in the United Arab Republic indicate disequilibrium in the domestic market.

During the periods when prices were rising, there was an excess of aggregate demand over aggregate supply. The excessive demand may be due either to a rise in development expenditure or/and a rise in consumption expenditure without a parallel rise in the supply of goods and services in the domestic market. The supply includes beside the national output, the deficit on the balance of payments. Because the main interest lies in the role of development financing, the emphasis is placed on the demand for capital goods and services. The main purpose is to assess the contribution of development financing to the rise in price level. First the annual changes in investment from domestic sources will be tested against the changes in national income. Second, other factors that have been stimulated by the development expenditure and in turn influenced the price level will be detected. Among these factors the behavior of the national output and the foreign trade policy are of significance.

1. The Significance Of Investment From Domestic Sources To The Problem Of Change In Price Level

It has been shown that the wholesale index during the period 1953-1960 was lowest in 1954 and highest in 1957. In order to find the relationship between the development expenditure and the price index the analysis should cover a period that includes these two years. Table XXIV is prepared for this purpose.

TABLE XXIV

THE RATIO OF NET INVESTMENT FROM DOMESTIC SOURCES TO NATIONAL INCOME AND THE RATE OF CHANGE OF EACH
(in Current price)

	1953	1954	1955	1956	1957	1958	Average
1-National Income in LE.*	780	868	931	970	935	1027	918
2-Domestic Investments in LE.**	107	131	124	133	116	138	125
3-Ratio of Investment to National Income, per cent		15	13	14	12	13.4	13.6
4-Per cent Change in National Income		11	7	4	-4	10	6.4
5-Per cent Change in Investment from Domestic sources		20	-5	7	-13	10	5.4

Source:

* I.M.F., International Financial Statistics, Vol.XV, p.110, (February 1962) and Abdurrazzak Abdul-majeed, Egypte Contemporaine, Vol.51, p.17 (Oct.1960).

** "Total private and public savings", Table VII, p.37 above.

It relates net investment from domestic sources (realized domestic saving) to net national income, both in current prices. The data on national income for the years 1953 and 1954 were taken from the International Financial Statistics and those for the period 1954-1958 from the Egypte Contemporaine. Both sources used the same figure for 1954, the only year appearing in the two series. The figures on investment from domestic sources are the

net savings of the two private and public sectors as in Table VII, Chapter II.¹

According to Table XXIV the expenditure on investment over the period amounted to 13.6 per cent of the national income. In 1954 the ratio of net domestic investment to national income was 15 per cent, the highest figure attained. The lowest rate however was in 1957 when it reached 12 per cent. The increase in development expenditure per year was also greatest in 1954 when it was 20 per cent greater than the investment expenditure in the previous year. The greatest decrease in development expenditure was in the year 1957 when it dropped by 13 per cent. The wholesale index on the other hand was at lowest in 1954 and at its highest in 1957. Another drop in the rate of development expenditure was observed in 1955 when the price index was rising. These findings suggest that the rise in prices could not be attributed to the rise in development expenditure. 1956 was the only year during which both have risen together. In 1958 the rate of increase in development expenditure was 10 per cent while the price index remained constant. It may be concluded therefore that the role played by the size of development spending in generating inflationary pressures in the economy is far from

1. p.37.

being obvious. The average increase in development spending from domestic sources was moderate and was lower than the average rise in national income. The first amounted to 5.4 per cent and the second to 6.4 per cent in the average year.

The rate of increase in total development financing was greater than the rate of increase in development expenditures, from domestic sources. This is attributed to financing from foreign sources. It is believed that foreign financing is supposed to reduce the pressure of demand in the local market. In this instance foreign financing represented purchases abroad that were reflected on the balance of payments which was in deficit all through the period except in 1954. The ratio of domestic development financing to total financing is shown in Table XXV.

TABLE XXV

THE RATIO OF DEVELOPMENT FINANCING FROM DOMESTIC SOURCES TO TOTAL FINANCING

	1953	1954	1955	1956	1957	1958	Average
Domestic Financing	93.2	100	77	80	76	80	84
Foreign Financing	6.8	---	23	20	24	20	16
	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

Source: Computed from Table VII, p.37, above.

A trend toward greater resort to foreign sources for development financing is thus noted. It was shown in the pre-

vious chapter that foreign financing was supposed to account for one-third of the required financing for the Overall Five-Year Plan.¹ In a period of nine months, July 1960-April 1961, LE. 62 million were drawn from foreign loans to finance development projects.² The role of Sterling balances and credit extended by the rest of the world was discussed in detail in the previous chapter.

The national output shows correlation to the price index more than the development expenditure. Table XXIV, above reveals this correlation. But it would be still clearer if the change in national income at constant prices is used for the purpose of analysis. The rate of change in national income at constant prices is computed from the data on page 26 above.

	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>Average</u>
Per cent Change in National Income at Constant Prices	11	6	2	-7	8	9	4 per cent

The lowest rate of increase in the national product was in 1956 when it was only half the average rate. In 1957 the national product dropped by 7 per cent. In all the other years the national product has shown a perceptible rise. The greatest

1. Table XI, p.69.

2. Page 131.

rise in a single year was in the year 1954 when the price level was lowest. In 1956 the price index rose while the rate of increase in national output dropped. The price index continued to rise while the increase in national product continued its decline. Both trends reached the maximum in 1957 and both were fairly stable in 1958 and 1959. This close correlation cannot be purely accidental. The people's as well as the government's intentions to spend are based on income expectations and expectations are normally dependent on past experience. A change in the income in one year, unlike its normal course in previous years causes the gap between intended and realized expenditure. The behavior of the government expenditure on both development and current needs during the period which will be discussed under government deficit expenditure, is closely related to this phenomenon of the drop in the rate of increase of national output.

Before ending the discussion of the national output its relation to the development expenditure has to be studied. It was shown in Chapter I that while the total gross investment increased from 13 per cent of the national income during 1945-1952 to 16 per cent during 1953-1958, the national output has not risen by as much.¹ Table VI shows the great increase in expendi-

1. See page 31.

ture on roads and public buildings and public constructions which generate no immediate output. Besides, large capital expenditure on the Iron and Steel Factory, Aswan Electricity Plant, and Aswan Fertilizers Plant have not generated any marketable output during the period discussed (1952-1958). While the whole increase in investment during the period has risen by 47 per cent, the expenditure on public works more than tripled.¹ However, the structure of development in a short period is not responsible alone for the change in national output during the same period. The behavior of national income in one period is also due to the size and structure of investment in a previous period. The greater expenditure by the government in 1953-1958 on public onstruction was mainly due to the lack of expenditure on new construction and replacement during the previous period.

Another phenomenon related to the rate of investment from domestic resources, is the consumption funtion. The rate of investment expenditure from domestic sources has risen according to Table XXIV at a lower rate than the increase in national income. In this case consumption should have been rising in absolute terms, and slightly in ratio to national income.

1. Table VI, p. 30

The trade policy aiming at reserving greater foreign resources for development purposes, suppressed import of consumption goods and controlled consumption supply without checking demand for consumption good. This is another possible factor of imbalance which contributes to price change especially when national output is also not rising or rising at a lower rate than expected.

The responsibility of development financing in the case of imbalance in the consumption market does not seem to be greater than the responsibility of the consumption function. It was shown in Chapter II¹ that consumption has risen by 9 per cent per year during the period 1953-1956. The increase in current expenditure of the public sector increased as was shown in Chapter III,² and to which further reference will be made later in this chapter in the section on government deficit expenditure.

It was mentioned in Chapter II that the rising consumption tendency was checked after 1957 when government reduced the rate of its consumption expenditure and when measures to reduce private consumption began to show positive results.³ With regard to the supply of consumption/^{goods} it will be treated in greater detail in the section on the balance of payments.

1. p.53.

2. p.74.

3. p.55.

2. Government Deficit Financing

The role of government as a source of development financing and as a direct participant in investment has been rapidly rising as was discussed in Chapter I and III.¹ Consequently, the behavior of government expenditure is of great significance in the course of analysis of the causes of change in price level. A brief description of the change in government expenditures is given below before assessing the size of the government deficit expenditure.

Government saving dropped from LE. 17 million in 1953 to LE. 7 million in 1955 to rise again to LE. 30 million in 1957, and LE. 37 million in 1958.² Government saving is expected to continue to rise to reach LE. 90 million in 1960/61.³ New revenue that mainly contributed to the increase in government saving came from the Suez Canal profits, the confiscated property, and the profit from commercial practices.⁴ While total private savings increased by 10 per cent, from LE. 92 million in 1953 to LE. 101 million in 1958 the government saving has almost tripled over the same period.⁵

1. See Table III on investment, p.20 and Table XIII on the size of government budgets, p.80.

2. Table VII, p.37.

3. pp.77-78.

4. pp.88-91.

5. Table VII, p.37.

Government expenditure on development on the other hand has increased in amount more than the increase in government saving. Government expenditure on development has risen from LE. 25 million in 1952/53 to LE. 88 million in 1955/56 to LE. 127 million in 1959/60. There was a decline in the volume of government gross expenditure in the years 1956/57 and 1957/58.¹

Government current expenditure on defence and social activities especially in 1956/57, the year of the Suez Canal crisis, increased considerably. While development financing by government declined from LE. 88 million in 1955/56 to LE. 67 million in 1956/57,² expenditure on defence increased from LE. 54 million in 1953/54 to LE. 93.3 million 1956/57. While government revenue increased by 40 per cent over the same period expenditure on social activities increased by the same ratio and expenditure on defence increased by double this ratio.

During the year 1956/57 the deficit in the government ordinary budget reached LE. 43.5 million.³ The preliminary budget estimates have not shown a deficit,⁴ which suggest that the deficit was not expected. However, to assess the deficit expenditure

1. Table III, p.20

2. Ibid

3. National Bank of Egypt, Economic Bulletin, v.XIV, p.401, (1961).

4. Federation of Chambers of Commerce, Egyptian Economy During 1952-1957, pp.194-197, Cairo: 1958.

by the government it is thought most helpful to include the increase in net indebtedness of the government to the central bank (National Bank of Egypt). Net indebtedness is equal in amount to the rise in government borrowing from the central bank minus the increase in government deposits with the bank at the end of each year. The data in Table XXVI show the development of government indebtedness to the central bank. Data are collected from the National Bank's balance sheets. The central bank did not engage in selling securities to commercial banks or to the open market to shift the "indebtedness burden".¹ The central bank allowed credit facilities to commercial banks that have been steadily rising from LE. 4.4 million in 1952 to LE. 31 million in 1959.² Deposits of commercial banks with the central bank rose at a slower rate, from LE. 35 million to LE. 51.3 million over the period.³

Table XXVI shows, the great increase in government deficit expenditure as reflected on the balance sheets of the central bank. The greatest increase was in treasury bills. The practice of issuing treasury bills by the government started on a significant scale in 1955. "In June 1955 two laws were issued autho-

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1. Abdulmajjed Abdurrazzak, "Monetary Planning" Egypte Contemporaine, v.51, pp.20-21, (October 1960).
 2. National Bank of Egypt, Economic Bulletin, v.XIV, p.37, (1961).
 3. Ibid.

rizing the Minister of Finance to issue Treasury Bills up to LE. 200 million. The main purpose was to finance the cotton season and to serve as cover of banknote"¹ The other law authorized the Minister to float 15-year bonds to the extent of LE. 100 million, for the purchase of free sterling from the National Bank of Egypt*, to cover external expenditures relating to the development projects.² During 1955 the government issued LE. 33 million treasury bills. These were all held by the central bank as shown in Table XXVI.

According to Table XXVI, the government has been resorting to the central bank all over the six years covered by the table. Deficit expenditure started in 1955, the same year when the general level of prices showed a tendency to rise.

Treasury bills held by the central bank rose from LE. 99 million at the end of 1955 to LE. 154 million at the end of 1957. The greatest issue in one year was in 1956, the year that witnessed the highest rate of increase in the price level. During 1957, ^{when the} price level rose by 9 per cent, the total net credit extended by the central bank to the government was the highest in a single year. The rise during this year was more in the long-

1. National Bank of Egypt, Economic Bulletin, Vo.XII, p.110, (1955).

2. Ibid.

* The N.B.E. has been itself the central bank up till the end of 1960.

term securities than in treasury bills. The size of annual credit extended by the central bank decreased greatly in 1958 and, though rose again later, was far less in 1959 and 1960 than in 1953, 1956, and 1957. The period 1958-1960 was a period of stable level of prices. The correlation between the price trend and the size of credit expenditure cannot be ignored. But whether the deficit expenditure was due to investment or due to current expenditure could not be determined with precision. The govern-

TABLE XXVI

GOVERNMENT INDEBTEDNESS TO THE CENTRAL BANK in LE. million

End of	1955	1956	1957	1958	1959	1960*
Treasury Bills	99.-	141	154	170	187	194
Long-term Securities	17.6	17.7	45.7	46.3	40.7	59.6
	116.6	158.7	199.7	216.3	227.7	243.6
<u>Less: Increase in</u> Government Deposits	2	8.4	8.9	19.8	10.1	10.8
	114.6	150.3	190.8	196.5	217.6	232.8
Net increase over one Year	33*	35.7	40.5	5.7	21.1	15.2

Source: Central Bank of Egypt, Economic Bulletin, v.I, p.348, (1961).

* National Bank of Egypt, Economic Bulletin, v.X, p.197, (1957).

* Excluding LE. 45 million foreign exchange bonds which represent purchase of sterling assets from the bank.

ment issued treasury bills mainly to finance the stocks of cotton that were not possible to dispose of during the Canal crisis. Secondly the small increase in national income during 1956 and the drop in national income during 1957 reduced the actual government revenue below what was expected. The government could have reduced its actual expenditure on development projects but it could not have stopped spending on defence. Another way was possible to be done to avoid excessive spending to resort to the rest of the world. There was in fact a great deficit in the balance of payments, ^{which} ~~it~~ was not able to counter-balance the inflationary pressure in the same manner as it did in other years. The foreign deficit could not solve the problem of the urgent need to spend on goods and services inside the country. The government had to buy the cotton product and had to spend on a nonproductive service, defence. In the latter period 1958-1960 government continued to resort to the central bank without apparent inflationary results. This time the national income was rising steadily, the borrowing was less and the use of funds borrowed was different. The government borrowed like all businessmen to finance natural increase in the inventories that the government held in its capacity as a business sector.

The above discussion leads to the role of the whole credit system in raising the price level. The change in private money supply is matched ^{with} / the change in national income in constant

price in Table XXVII below.

TABLE XXVII

THE CHANGE IN NATIONAL OUTPUT COMPARED TO THE CHANGE IN PRIVATE MONEY SUPPLY

	1954	1955	1956	1957	1958	1959
Change in output [†] per cent	11	6	2	-7	8	5
Change in money [†] supply per cent	-3	4	15	4	-5	+5

Source: † I.M.F., International Financial News Survey, v.15, (January, 1961).

* Table XXIV, above.

The money supply in Table XXVII includes banknotes in circulation and private bank deposits. The output in the table is the net national income in constant prices. Table XXVII reveals a fact that the only time money supply was rising at a perceptibly greater rate than the rise in output was in the two years 1956 and 1957. The Suez Canal crisis caused great accumulation of cotton stocks. The government encouraged commercial banks to extend credit upon the security of stocks. Claims on the private sector has risen by LE. 10 million in 1955 and by LE. 25 million in 1956 and LE. 26 million in 1957. The annual increase dropped to LE. 8 million in 1959 and to LE. 7 million in 1960, reaching a total of LE. 310 million.¹ Currency in circulation

1. I.M.F., International Financial Statistics, v.XIV, p.106, (December 1961).

has risen from a constant level of LE. 168 million during 1953-1955, to LE. 209 million at the end of 1956.¹ It reached LE. 213 million at the end of 1957 and declined steadily to LE. 200 million in 1959. The trend of money supply over the whole period was rather deflationary. This phenomenon is mainly due to the persistent deficit of the balance of payments. The deficit resulted in depletion of the foreign assets held by the central bank as was shown in Chapter IV.² In 1958 private money supply index was LE. 114 million, 10 per cent greater than the private money supply in 1952. In one year 1956, on the other hand the index has risen from 101 to 116 when national output increased by 2 per cent only. In 1957 the rise in the money supply index was only 4 per cent but the national output dropped by 3 per cent during the same year.

There is no evidence that the increase in private money supply during 1956-1957 was due to development expenditure. It is true that the credit control policy discriminated in favor of business credit against individual credit and consumption credit. But this discrimination increased later in 1958-1961 period without causing increase in money supply beyond the in-

1. Ibid.

2. p.118.

crease in output. The share of agrarian and industrial short-term credit was rising rapidly during 1958-1961 reducing the share of other business sectors. The share of joint stock companies and cooperatives, consequently rose rapidly reducing the share of individual enterprise.¹ But the excessive credit in the year 1956 was not used to finance working capital but rather to finance idle inventories.

3. Foreign Trade Policy And The Deficit In The Balance Of Payments

The deficit in the balance of payment played a great part in counterbalancing the inflationary forces in the Egyptian economy after the World War II. There was a persistent deficit in the balance of payments all through the period except in 1954 when there was a small surplus as Table XXVIII shows. Though the overall deficit in the balance of payments was relatively large in 1956 and 1957 yet it did not prevent the rise in the price level. The deficit in the balance of payments was LE. 62 million during the two years while the deficit in the government expenditure as shown in Table XXVI amounted to LE. 75 million.

It is believed that the foreign trade policy reduced the

1. National Bank of Egypt, Economic Bulletin, v.XIV, p.300 (1961).

TABLE XXVIII

THE BALANCE OF PAYMENTS OVER EIGHT YEARS

in LE. million

	1952	'53	'54	'55	'56	'57	'58	'59
1. Balance of Trade	-65	-30	-11	-57	-62	-52	-53	-31
2. Balance of Invisi- ble Transactions	<u>+12</u>	<u>+22</u>	<u>+15</u>	<u>+23</u>	<u>+29</u>	<u>+20</u>	<u>+20</u>	<u>+33</u>
3. Balance of Current Transactions	-53	-8	+4	-34	-33	-31	-20	-36
4. Overall Deficit or Surplus	-55	-8	+3	-32	-31	-31	-23	-25

Source: National Bank of Egypt, Economic Bulletin,
v.XIV, p.151, (1961).

influence of the deficit in the balance of payment as a counterbalancing force. The foreign trade policy aimed at reserving the greater part of foreign facilities for the import of development equipment. At the time consumption was rising at a rate not less than the rise in the rate of national income,¹ shortage in consumption goods was possible to exert inflationary pressures. Development equipment imported was 37 per cent in 1958 against 22.5 per cent in 1950.² Actually total imports were not more in 1958, but consumption goods suffered a perceptible decline. Import of food, drink, and tobacco for consumption dropped from

1. p.53, and Table XXIV, p.155.

2. See pp.11 and 117.

LE. 49 million in 1952 to LE. 18.2 million in 1956 and ^{rose} risen again to LE. 33.5 million in 1957.¹ Other undurable consumption imports dropped steadily from LE. 13.3 million in 1952 to LE. 8.4 million in 1956 to LE. 8.2 million in 1957. Durable goods for retail sale or consumer use dropped from LE. 16 million to LE. 13 million to LE. 6.9 million in the same years respectively.²

Imbalance in the market of consumption commodities may have contributed to the price change. There is one point that makes the imbalance in the consumption market less effective in price level change: The price control policy that bases prices on cost irrespective of demand. It is believed that exceptional cases that escape the control are not heavily represented in the price indexes. It was learned that there were instances when shortage occurred in supply of rice which is a main consumption commodity produced locally. Shortage in this item once it occurs is mostly due to the foreign trade policy which favors exports. After 1957 the foreign trade policy continued to favor import of equipment and export of rice, textile, and other consumption goods. But prices have not risen any more as far as recent reports tell. It seems that other factors such as the rate of consumption, the size of output and government expenditure worked

1. National Bank of Egypt, Economic Bulletin, v.XIV, p.142, (1961).

2. Ibid.

toward equilibrium.

Another factor is believed to be of significance to the purpose of price trend analysis, namely the rate of exchange. Imported goods are subject to price control and their selling price is based on cost plus normal profit. Therefore, the cost to the local producer of foreign goods is a factor that determines the price. Cost of foreign imports depend on the rate of exchange of the Egyptian pound.

It was difficult to get written evidence regarding the changes in the value of the Egyptian pound abroad. The difficulty arose from the control practised on the foreign exchange by the government. The exact rate of exchange could be determined only in a free market. But since the main interest here is to find out the effect of the rate of exchange on the price level it would be helpful to find out the premium that importers are willing to pay to obtain foreign exchange.

In 1953 the government allowed exporters to repurchase their receipts of hard currency (dollar, sterling, and mark), or sell it to other importers at the official rate.¹ The premium paid by importers to obtain the right to use the foreign exchange was suitable to measure the depreciation of the Egyptian pound. There were no written data available on the dealings of individuals with each other. It was learned from Egyptian merchants that the premium has been rising steadily ever since.*

* The writer has had personal contacts with merchants in Cairo in 1958. It is believed that there is no need to mention names.

1. International Financial Statistics, v.8, p.90 (Dec.1955).

The exact figures for the early periods were not possible to obtain. However, in 1955 the said "entitlements" were limited to hard currency received from the export of vegetables, flowers, and a few manufactured products.¹ This restriction raised the premium paid to obtain the foreign currency to higher levels in the succeeding years. It was learned from a businessman in Egypt that he received 90 per cent premium on his foreign receipts obtained from exportation of dehydrated onions in 1958. Importers of cars, home appliances, and similar "unessential" goods were not allowed foreign exchange except what they obtained from this special account.* Other importers, after obtaining import licences were allowed foreign exchange at fixed premiums. The premium was 37 per cent in February 1958, reduced to 27 per cent in March and to 26.6 in September of the same year.²

Beginning September 1959 another change in the premium was decided. All importers paid a premium of 10 per cent on exchange purchased for approved imports. A premium of 27.5 per cent was collectible or payable on certain invisible items.³ Most imports were subject also to a surcharge of 9 per cent beginning 1959.

1. Ibid.

2. International Financial Statistics, v.XV, p.110, (Nov.1961).

3. Ibid.

* So-called Barter Account.

From the data available it could be concluded that the cost of imported goods was rising since 1953 and specially in 1957. The same rule did not apply to all imported goods because foreign exchange was one of the weapons used to discriminate against some visible and invisible imports.

A way is resorted to in order to test whether premiums paid represented the real discount in the value of the Egyptian pound. The prices of gold are quoted daily in Musky, Cairo. The trend of gold price index reflects the change in the actual gold content of the Egyptian pound. The price of a dirhem of pure gold dropped steadily from LE. 1.75 in December 1952 to LE. 1.53 in 1955. Then the price rose sharply to LE. 1.68, to LE. 1.85 and LE. 1.96 in the following years respectively.¹ In 1959 it reached LE. 1.98 and in 1960 it reached LE. 2.03.² The greatest depreciation of the pound, in terms of gold, was in the two years 1956 and 1957, the same years that witnessed the sharp rise in the price level as mentioned before.

The role of development financing in the depreciation of the Egyptian pound could not specifically be located. The main cause of the depreciation was the deficit in the balance of pay-

1. National Bank of Egypt, Economic Bulletin, v.XII, p.232, (1959).

2. Ibid, No.3, v.XIV, Table 21 (1961).

ments, therefore, the development share in this depreciation is limited to how much it added to the deficit in the balance of payments. The foreign trade policy gave development equipment a priority to other commodities. Therefore, development equipment replaced other commodities, and caused a rise in their prices through creating scarcity of supply, but not through deflating the value of the pound. It is believed that the resort to obtaining long-term foreign loans to finance projects reduced the pressure on the Egyptian pound inspite of the continued deficit in the balance of payments.¹

Conclusion

There was a moderate rise in the price level in the U.A.R over the period discussed in this thesis 1953-1960. The rise was perceptible in the two-year period 1956-1957. The trend is toward a stable price level at the high point reached in 1957.

There was no single force that could have been a cause of the rise. Several factors met together to shape this trend. Among these was the drop in the rate of increase in national output in 1956 caused by dislocations due to the Tri-partite aggression, which was followed by absolute decrease in national output in 1957. Such a decline was not expected by the government and people who plan their expenditures on investment as well as on investment in the light of their income expectations. Coupled with the stressing need to spend on defence and to finance idle inventories, the government resorted to the central bank for credit and encouraged commercial banks to extend credit for a

1. See "Foreign Loans", Chapter IV.

similar purpose. The size of money rose at the time national output dropped. The counterbalancing factor which is the deficit in the balance of payments was working but was not adequate to fill the gap and combat the inflation. The structure of the imports that created the deficit in the balance of payments were not all consumers' goods. The trade policy favored capital goods and in many cases imported by the government, itself. Besides, the deficit on the balance of payments created pressure on the Egyptian pound reducing its purchasing power abroad and raising the costs of imported goods that enter the wholesale price index.

The role of development expenditure in the problem of price stability was not as significant as other factors. The size of expenditure on development from domestic sources has risen at a lower rate than the national income over the period. The role of the rest of the world in contributing to total investment relieved the national economy from mobilization of greater resources for investment and relieved the government from resorting more often to compulsory saving. The long-term loans financing policy relieved also the Egyptian pound from continuous depreciation in terms of foreign currency resulting from current claims by the rest of the world. But the policy of foreign trade toward reserving all foreign facilities for development purposes reduced the chance of lifting the pressure of demand in the market for consumption goods especially in the years 1956 and 1957 when the

increase in national product was lower than expected. Finally it is believed that the greater the savings from domestic resources the better for price stability on condition that resources saved contribute to a continuous increase in the national income. The recent policy of raising income taxes and increasing the government share in business activity for the purpose of financing development might help to realize the two goals: the reduction in the ratio of consumption demand to output and the continued rise in the rate of increase in output. Such success depends after all on the efficiency of management.

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