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Egypt and the IMF: Overview and Issues for Congress

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Summary

Congress, which annually oversees and appropriates $1.55 billion in bilateral foreign aid to Egypt, is following the political and economic situation in Egypt closely. Economic conditions in Egypt have deteriorated rapidly since the 2011 "revolution." Political uncertainty abruptly reduced foreign capital flows into Egypt; growth, while still positive, has slowed substantially; the central bank is at risk of running out of foreign exchange reserves; and unemployment has increased from 9.2% before the revolution to 12.3% in 2012. Many policymakers and analysts fear that the fragile economic conditions in Egypt jeopardize the country's political transition and broader stability in the region.

Egyptian authorities and the International Monetary Fund (IMF) have been in negotiations for more than two years over an IMF loan to Egypt in exchange for policy reforms that, if successful, could stave off economic collapse and create more "inclusive" growth. The IMF reached tentative agreements with first the military-controlled Supreme Council of the Armed Forces (SCAF) in June 2011 and later with Egyptian President Mohammed Morsi in November 2012. The November 2012 program would have provided $4.8 billion in assistance, and other donors pledged about $9.7 billion in additional financing once the IMF program was in place. No agreement has been finalized or implemented to date.

Egyptian authorities have been reluctant to commit to economic reforms that may be politically unpopular and increase the country's debt. Pressure to cut fuel subsidies is a particular issue. More broadly, many Egyptians associate the IMF programs in the late 1980s and 1990s with adverse social outcomes. On its part, the IMF has resisted a program that does not have sufficient conditionality consistent with its lending policies. Continuing political concerns and uncertainty in Egypt have also contributed to the delay. In the absence of an IMF agreement, the Egyptian government has recently secured financial support from Libya and Qatar.

Issues for Congress

Some lawmakers who oppose ongoing U.S. bilateral assistance to Egypt may oppose any existing or future IMF support of Egypt, on several potential grounds. Some may be concerned that in the rush to stabilize Egypt, the Administration could be too lenient in terms of the reforms it seeks from the Egyptian government. Others may not want the Administration to overly politicize an IMF loan. They fear that the application of too much pressure on the Morsi government could make accepting a possibly unpopular IMF deal too politically controversial to pursue and that the lack of IMF involvement in Egypt could undermine U.S. interests in the region.

The United States makes the single largest financial commitment to the IMF, and, with the largest voting power at the IMF, the United States wields a high degree of influence over IMF decisions. If Congress wanted to shape U.S. policy toward Egypt at the IMF, it could pass a "legislative mandate" legislation directing the U.S. representative at the IMF to use its "voice and vote" to push for certain policies toward Egypt at the IMF.

Lawmakers may also want to use the terms of IMF conditions as "benchmarks" for the provision of existing or new bilateral economic aid to Egypt. Congressional concerns about bilateral debt relief are, in part, related to the absence of an IMF agreement. Additionally, legislative language (S.Amdt. 44) proposed in March 2013, but not adopted, would have tied U.S. bilateral economic assistance to Egypt to, among other things, an IMF program.

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Introduction

After more than two years of social unrest and economic stagnation following the 2011 popular uprising, the government of Egypt is facing serious economic pressures that, if not remedied, could lead to economic collapse and possibly new levels of violence. The International Monetary Fund (IMF) has been in negotiation with the government of Egypt for at least $4.8 billion in loans in exchange for structural economic reforms, such as subsidy reduction. Egyptian acceptance of an IMF loan could also pave the way for billions more in financial assistance from other bilateral and multilateral donors, potentially providing Egypt with time to stabilize its political system and economy. The Obama Administration is encouraging President Mohammed Morsi to reach out to the opposition and the public in order to gain the political support to quickly reach a deal with the IMF in order to stave off further economic uncertainty. Egyptian leaders are concerned about the political ramifications of required IMF reforms, which could be politically unpopular.

Congress, which annually oversees and appropriates $1.55 billion in bilateral foreign aid to Egypt, is following the situation in Egypt closely, including the Islamist-led government's stated commitment to, among other things, pursuing democratic principles and continued peace with Israel. Some Members of Congress are also closely monitoring Egypt-IMF negotiations. U.S. funds to provide bilateral debt relief to Egypt have been tied to Egypt committing to an economic program in conjunction with the IMF. Legislative language also has been proposed that would tie U.S. bilateral economic assistance to Egypt to, among other things, an IMF program and implementation of reforms under the program. Congress could also pass legislation to shape U.S. policy toward Egypt at the IMF. More generally, in the 113th Congress, lawmakers have proposed a number of bills that would prohibit, restrict, or rescind bilateral U.S. assistance and/or arms sales to Egypt.[1]

This report provides an overview of the economic situation in post-revolution Egypt and negotiations between Egypt and the IMF. It also analyzes why an IMF program is controversial in Egypt and the relationship between an IMF program for Egypt and U.S. foreign policy goals in the region. It discusses the IMF program from a congressional perspective, including how debt relief for Egypt has been tied to an IMF program and legislation that would condition U.S. bilateral economic assistance to Egypt on an IMF program.

For more information on the political situation in Egypt, see CRS Report RL33003, *Egypt: Background and U.S. Relations*, by Jeremy M. Sharp. For more information on the IMF, see CRS Report R42019, *International Monetary Fund: Background and Issues for Congress*, by Martin A. Weiss.

[1] For example, see H.Res. 87; H.R. 276; H.R. 416; H.R. 939; H.R. 1039; H.R. 1302; S. 201; and S. 207.

Background

Deteriorating Economic Conditions in Post-Revolution Egypt

Economic conditions in Egypt have gradually deteriorated since the 2011 revolution, potentially exacerbating an already polarized Egyptian political climate. Neither military nor civilian authorities have been able to restore confidence in the economy. Continued insecurity stemming from deterioration in law and order has hampered investment. The Islamist-led government and the opposition have blamed each other for worsening economic conditions, and while Egypt has not reached a crisis "tipping point," there is some concern that economic shocks, such as a dramatic currency devaluation or sudden steep rise in the cost of living, could lead to street violence.

Before the political changes began taking shape, Egypt's economy was strong in many respects. The economy was growing at a fairly rapid pace, averaging 5% a year between 2000 and 2010.[2] Starting in 2004, the government pursued wide-ranging structural reforms, including tariff reductions, privatization of state-owned enterprises, and reductions in regulation of the private sector, among other policy measures, that aimed to improve the business environment and make Egypt's economy more competitive.[3] The 2008 World Bank *Doing Business* report ranked Egypt as the top worldwide economic reformer.[4] In general, reforms helped attract foreign capital, and foreign direct investment (FDI) in Egypt surged from 1.2% of GDP in 2000 to 9.3% of GDP in 2006. The global financial crisis of 2008-2009 had limited impact on Egypt's economy, due to low exposure to the types of structured financial products at the heart of the financial crisis and the government's accommodating fiscal and monetary policies following the onset of the crisis.

Behind strong growth and capital inflows during the 2000s, however, Egypt's economy faced a number of vulnerabilities. Average Egyptians saw little immediate benefit from the economic reforms praised by outside observers and investors. Growth had done little to lower persistently high unemployment, which averaged 9.9% during the 2000s (and was reportedly much higher among youth), or substantially reduce poverty. Fifteen percent of the population, or about one in seven Egyptians, were living on less than $2 per day in 2008. The government was also running relatively large budget deficits, averaging 8.2% of GDP between 2002 and 2010. In its 2010 annual review of Egypt's economy, the IMF cautioned about the need for fiscal consolidation and recommended a value-added tax (VAT), energy subsidy reform, and measures to contain the fiscal cost of pension and health reforms.[5] Persistent budget deficits also left public debt at 73% of GDP in 2010, above the 60% threshold that some economists believe is stable and conducive to growth. The IMF also warned about the need to continue reform "momentum" to further improve the business environment and build the private sector. Finally, inflation had steadily increased through the decade, from 2.8% in 2000 to 11.7% in 2008.[6]

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[2] Unless otherwise noted, data in this report is from the IMF, *World Economic Outlook*, April 2013 or the World Bank, *World Development Indicators*, 2013.

[3] World Bank, "Egypt: Positive Results from Knowledge Sharing and Modest Lending," Independent Evaluation Group Assistance Evaluation, 2009.

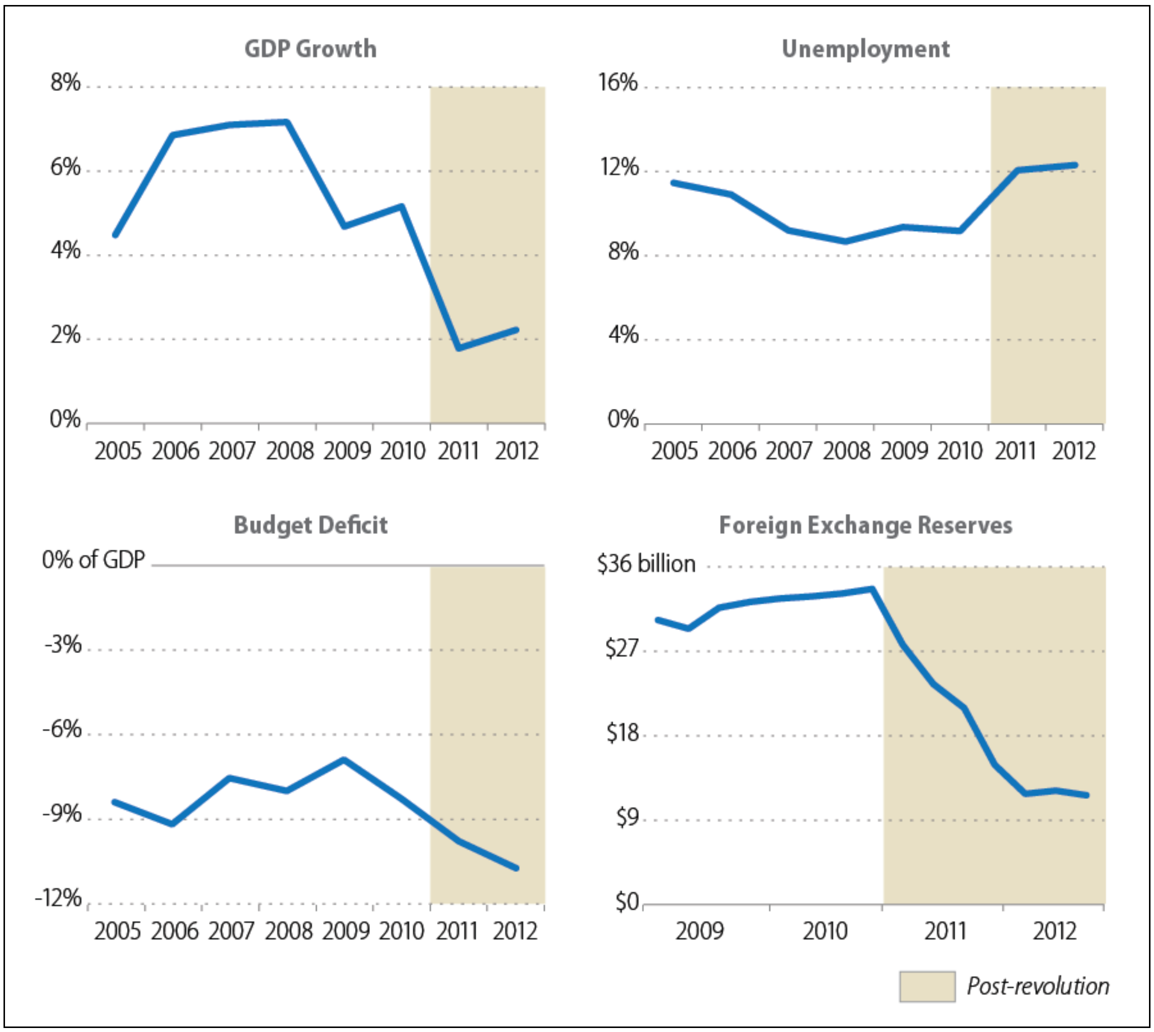
[4] World Bank, "Most Improved in Doing Business 2008," http://www.doingbusiness.org/reforms/top-reformers-2008.

[5] IMF, "Arab Republic of Egypt: 2010 Article IV Consultation," April 2010.

[6] Average consumer prices, end of year.

The revolution in Egypt unraveled the conditions underpinning growth in the 2000s and brought potential vulnerabilities to the forefront. The revolution and ensuing political uncertainty eroded investor confidence, triggering a sharp reduction in capital inflows and an abrupt decline in tourism revenue, on which many jobs depend.[7] Economic growth fell to 1.8% in 2011 and 2.2% in 2012. Unemployment rose from 9.2% in 2010 to 12.3% in 2012. The new Egyptian authorities, brought to power in elections in mid-2012 as the military regime that took power in early 2011 formally stepped aside, retreated from previous pledges for fiscal consolidation, and the budget deficit widened from 7.8% of GDP in 2010 to 11.2% in 2012. General economic trends in Egypt before and after the revolution are depicted above, in **Figure 1**.

Figure 1. Economic Challenges in Post-Revolution Egypt



Source: IMF, *World Economic Outlook*, April 2013; IMF, *International Financial Statistics*, 2013.

The Morsi government has been reluctant to reduce fuel subsidies, and has continued to earmark a large proportion of fiscal expenditures for social spending, seemingly as a means for securing

7 IMF, "Arab Countries in Transition: Economic Outlook and Key Challenges," Prepared for the Deauville Partnership Ministerial Meeting, October 12, 2012, http://www.imf.org/external/region/mcd/deauville/note101212.pdf.

continued political support.[8] The government has also increasingly relied on domestic markets to finance the deficit, which is more expensive than borrowing on international markets and has further strained government finances. Public debt rose from 73% of GDP in 2010 to 80% in 2012.

Political uncertainty and capital outflows have also reduced demand for Egypt's currency, the Egyptian pound, resulting in pressure on the Egyptian pound to depreciate. The Egyptian central bank generally does not allow its currency to be determined entirely by market forces (i.e., to float freely, like the U.S. dollar), and has been selling foreign exchange reserves in an attempt to manage a gradual depreciation. The central bank's holdings of foreign exchange reserves fell from $34 billion in the fourth quarter of 2010 to $12 billion in 2012, a level that many economists fear puts the central bank at risk of running out of reserves and triggering a currency crisis.[9] The central bank has also increased interest rates to stem pressure on the pound, which some economists fear undermines the government's growth objectives in the short-term. A depreciated local currency means that Egyptian households' wealth and wages are worth less in terms of purchasing power, as imported goods become more expensive.

Egypt-IMF Negotiations

With slowing growth, rising unemployment, dwindling foreign exchange reserves, and a growing budget deficit, many economists argue that Egypt faces two broad economic challenges: (1) sustaining macroeconomic stability in the short-term; and (2) implementing economic reforms in the medium-term to deliver growth to broad segments of society ("inclusive growth"), foster private sector development, and create jobs.

The IMF is in a position to help stabilize Egypt's economy and, potentially, advance reform efforts. The IMF provides loans to countries facing economic crises, and its short-term loans (typically disbursed over one- to three-years) can ensure continuous access to affordable financing, providing the government with breathing space to implement needed economic reforms. IMF loans are disbursed in phases ("tranches"), contingent upon the implementation of economic reforms, which have been negotiated between the government and the IMF at the onset of the program ("conditionality"). Targets may be revisited, however, over the course of the program in response to changing economic conditions.[10] Other Arab countries in "transition" are facing similar pressures, and the IMF has negotiated and started programs in Jordan, Morocco, Tunisia, and Yemen.

Egyptian authorities and the IMF have been in on-again, off-again negotiations essentially since political changes started taking shape in Egypt. Two tentative ("staff-level") agreements were reached, in June 2011 and November 2012, but no agreement has been finalized or implemented. Egyptian authorities have been reluctant to commit to economic reforms that may be politically unpopular and ultimately saddle the economy with more debt. A particular source of concern are fuel subsidies, which many economists view as inefficient and regressive but constitute a financial safety net for many Egyptian households. In turn, the IMF's lending policies prevent it from pursuing a program that does not have adequate conditionality commitments in place.

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[8] Economist Intelligence Unit, "Country Report: Egypt," March 2013.

[9] IMF, *International Financial Statistics*, 2013.

[10] For more background on the IMF, see CRS Report R42019, *International Monetary Fund: Background and Issues for Congress*, by Martin A. Weiss.

Continuing political concerns and uncertainty in Egypt have also contributed to the delay. In the absence of an IMF deal, Egyptian authorities are increasingly turning to other countries in the region for financial assistance, such as Libya and Qatar (described in greater detail below). However, funds from other governments may only provide a bridging mechanism and could fail to ensure that Egyptian authorities address underlying structural challenges.

Tentative Deal #1: June 2011

At the time of the first staff-level agreement, in June 2011,[11] the military-controlled Supreme Council of the Armed Forces (SCAF), led by Field Marshal Mohamed Hussein Tantawi, was exercising executive authority in Egypt and therefore negotiating with the IMF. Tantawi rejected the proposed $3.2 billion IMF loan, reportedly because he was hesitant to burden Egypt with what he considered was too much foreign debt and perhaps believing that Egypt could receive short-term loans or grants from Gulf Arab countries instead.[12] Many economists have since suggested that the terms of the June 2011 staff-level agreement would have been far less onerous in terms of conditionality than subsequent proposals; as economic conditions in Egypt continued to deteriorate in coming months, the size of the IMF program for Egypt, and the reforms attached to it, have become more ambitious.[13]

The June 2011 staff-level deal was reached before the Muslim Brotherhood began to wield real political power in post-Mubarak Egypt, but the party generally applauded the SCAF's rejection of IMF assistance as an assertion of Egyptian sovereignty, while being careful not to rule out any future multilateral lending. According to one Muslim Brotherhood communiqué published after the SCAF's rejection of the $3.2 billion IMF loan:

> The Egyptian government has adopted a new policy to strike a balance when dealing with international financing institutions. It has recently refused to finance the deficit through loans loaded with political and economic conditions. The importance of this policy is that it signals that the authorities are reconsidering ensuring the independence of the state, which is consistent with the aspirations of the revolution, to get rid of the inherited dependency of the old regime. Regardless of the methods of handling the issue and covering the budget deficit, this step would recast the Egyptian relationship with the IMF and the World Bank, which would require a great deal of effort directed at achieving stability, development, production, self-reliance and the development of our local resources. This approach also delivers a clear message to international financial institutions regarding the need to move from an era of political loans that have supported many authoritarian governments, and shifting towards taking into account more balanced relations in the new era, which would be based on the interests of the states and safeguarding their economic development.[14]

[11] For information about the tentative agreement, see IMF, "IMF Reaches Staff Level Agreement with Egypt on a US$3 Billion Stand-By Arrangement," June 5, 2011.

[12] "Bread Riots or Bankruptcy: Egypt faces stark Economic Choices," *Christian Science Monitor*, April 3, 2013.

[13] According to one IMF official, "The IMF arrangement included a number of benchmarks, which consisted of measures that were already in the government's economic plan, none of them related to privatization or requiring changes to the subsidy regime during the period of (the) IMF arrangement." See, "IMF says it is still ready to help Egypt," *Agence France Presse*, June 30, 2011.

[14] Open Source Center, "MB Statement On Current Domestic And Regional Affairs," Document ID# GMP20110709966104, London, *Ikwanweb* (in English), July 9, 2011.

Tentative Deal #2: November 2012

Following the 2011-2012 parliamentary elections that enabled the Muslim Brotherhood's Freedom and Justice Party to form a majority coalition, Islamists assumed partial control over governance amidst a worsening economic crisis. Though the SCAF still maintained executive authority in the first half of 2012, the Brotherhood insisted that it would not support any new IMF deal unless a new, more broadly-based government was formed of which it would presumably be a part. In March 2012, Saudi Arabia reportedly deposited $1 billion in Egypt's central bank, which eased some of the immediate pressure on the Egyptian government to secure financing from the IMF quickly.[15] Egypt also reportedly received financial assistance from Qatar.

Months later, former Brotherhood leader Mohammed Morsi became president and wrested most day-to-day executive authority from the SCAF. Islamists also controlled the upper house of parliament (the lower house having been dissolved by the courts pending new elections). A second staff-level agreement was reached between Egypt and the IMF in November 2012, to provide a 22-month, $4.8 billion loan program.[16] Reaching an agreement with the IMF was also expected to unlock funds from other bilateral and multilateral donors. It is not uncommon for other donors to wait until an IMF program is in place, which can serve as a seal of approval for the government's economic policies and provide greater assurance that assistance would be used by the government wisely. The total financing package, including funds from the IMF, was reportedly $14.5 billion in loans and deposits on relatively favorable terms (compared to borrowing on the private debt market).

At the time, the government was planning on reducing spending, primarily by cutting energy subsidies, and boosting revenue, including through reforms to move from a general sales tax to a value-added tax. Possibly to demonstrate good will, the government lifted subsidies on 95-octane petrol in line with the plan in November 2012.[17] The program likely included other policy measures as well; specifics would have been released publicly when the program was finalized. One analyst expected the IMF "to ask Egypt to do all the things that the IMF always asks a country to do, which is to get its fiscal house in order; increase taxes, reduce the budget deficit, get rid of subsidies so that it can bring down inflation, do other things that will boost growth, and then get Egypt back on some kind of path toward recovery."[18]

In December 2012, public outcry erupted over the proposed tax increases, causing the government to reverse course. The Egyptian finance minister requested a delay in the program, and, eventually the government postponed the program until after the parliamentary elections, which were to end in June 2013.

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[15] Abdel Latif Wahba and Mariam Fam, "Egypt Gets $1 Billion from Saudi Arabia, Minister Says," *Bloomberg*, May 10, 2012.

[16] IMF, "IMF Reaches Staff-Level Agreement with Egypt on a US$4.8 Billion Stand-By Arrangement," November 20, 2012.

[17] Economist Intelligence Unit (EIU), *Egypt: Country Report*, February 13, 2013.

[18] Arvind Subramanian, "Egypt's $4.8 Billion IMF Loan: Could it Affect Gaza?" Peterson Institute, Interviews on Current Topics, November 20, 2012.

Current Status

By the spring of 2013, with the economic situation still unstable, it appeared that the government would not be able to wait on IMF assistance until parliamentary elections were completed. The elections have been put on hold, possibly until the fall of 2013, due to judicial review of the electoral law. In the meantime, President Morsi has attempted to replace hundreds of judges who he believes are obstructing his agenda. Moreover, ensuring broad Egyptian public support for an IMF loan, a goal sought by many IMF members, seemed distant at best, as trust between President Morsi and his opponents had deteriorated significantly in prior months.

In March 2013, the IMF suggested that Egypt could qualify for emergency short-term financing from the IMF to stave off imminent economic collapse. Assistance would have taken the form of a bridge loan, smaller and shorter-term than the programs previously negotiated between the IMF and Egypt. It would have provided about $700 million, substantially smaller than the $4.8 billion previously on the table, but would have not come with the same conditions attached to more standard (non-emergency) loan facilities. This support could have provided Egypt with much-needed short-term cash to get through the elections, while providing the government with time to negotiate a more traditional, longer-term IMF program. However, the Morsi government eventually ruled out such emergency assistance. One Western diplomat reportedly said that the rejection of emergency financing by the government was an attempt to "bully the Fund to giving Egypt the loan."[19] Likewise, Steven Cook of the Council on Foreign Relations has cautioned that "Egypt will likely get the aid it needs to keep the country afloat, but the way they have gone about securing this assistance suggests a misplaced arrogance.... the Egyptians should dispense with their implicit 'give it to us or else' approach. Whether they like it or not, donors are not going to hand over cash without any terms."[20]

In contrast, President Morsi reportedly argued that it had "done what was required" for a longer-term IMF program and had prepared a program of reforms.[21] Reforms announced in early 2013 include, for example, elimination of energy subsidies for industrial firms over a three-year period, increases in the price of wheat, and implementation of a progressive property tax on large properties.[22] Reforms were also announced to protect the most vulnerable segments of society, including plans to implement universal health care and, for low-income families, raising the minimum tax exemption and increase social security pensions).[23] The reforms have not been without political costs. For example, the government's plans for bread subsidy reforms resulted in bakeries across Egypt threatening to shut down.[24]

Meanwhile, the Obama Administration has stressed the urgency facing Egypt with regard to an IMF program, and regarding economic and political conditions more broadly. On April 2, 2013, Secretary of State John Kerry remarked, "We share a very real concern in the Obama

[19] Ibid.

[20] Steven A. Cook, "Is Egypt Too Big to Fail?," "From the Potomac to the Euphrates" blog on Council on Foreign Relations website, February 7, 2013.

[21] Heba Saleh, "Egypt Rules out IMF Emergency Finance," *Financial Times*, March 12, 2013.

[22] Al-Masry Al-Youm, "Energy Subsidies will Disappear by 2016, Says Minister," *Egypt Independent*, February 26, 2013; "Egypt's President Morsi Unveils Raft of Tax, Subsidy Reforms," *Ahram Online*, February 25, 2013.

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[24] Al-Masry Al-Youm, "Bakers Threaten Strike if Govt Doesn't Shelve Bread Subsidy Plan," *Egypt Independent*, February 25, 2013.

Administration about the direction that Egypt is apparently moving in.... We have been working very, very hard in the last weeks to try to get the government of Egypt to reach out to the opposition, to deal with the IMF, to come to an agreement which will allow Egypt to begin to transform its economy and improve the lives of its citizens."[25]

While negotiations with the IMF continued, the Egyptian government reportedly received pledges for financial support in April 2013 from Libya ($2 billion deposit to the central bank) and Qatar ($3 billion purchase of government bonds).[26] A list of selected bilateral financial assistance to Egypt is provided in **Table 1**. Some analysts believe that financial support from neighboring countries could again delay an IMF program, while others argue that this assistance could be the start of a broader financial assistance program, which includes IMF funding.[27]

Table 1. Select Budget and Central Bank Support to Egypt

Country	Date	Type and Amount of Aid
Qatar	April 2013	$3 billion loan
Libya	April 2013	$2 billion in central bank deposits
United States	March 2013	$190 million cash transfer (for debt relief)
Qatar	January 2013	$2.5 billion total (of which $2 billion loan, $500 million grant)
Turkey	September 2012	$2 billion loan
Qatar	July 2012	$2 billion in central bank deposits
Saudi Arabia	May 2012	$1 billion in central bank deposits, $750 million credit line for oil imports
Saudi Arabia	November 2011	$500 million grant
Qatar	October 2011	$500 million grant

Sources: Analysis of new reports announcing financial support to Egypt.

Notes: List may not be exhaustive, and it is not always clear to what extent announcements of financial support were fully met or re-pledged at later dates. In addition, various media sources report that the Egyptian government is seeking, or has sought, aid from other countries such as Iraq ($4 billion requested), Algeria ($2 billion), Russia, and the Arab Monetary Fund. In 2011, the UAE pledged $3 billion in various aid to Egypt, but the funds were not transferred. In April 2013, Iran offered to loan Egypt $1 billion.

By mid-April, Egypt's latest round of talks with the IMF ended without an agreement. Reportedly, the IMF stated that Egypt has taken "valuable first steps" to address energy subsidies, and that the Egyptian authorities "intend to build on these steps with further actions to address, in a socially-balanced way, the country's fiscal and balance of payments deficits, and create conditions for sustained recovery of the economy." It is not clear when talks will resume.[28]

[25] "Egypt Under IMF Spotlight as Loan Talks Resume," *Reuters*, April 3, 2013.

[26] Rob Minto, "Egypt: Qatar Loan Puts IMF on Hold," *Financial Times*, April 10, 2013; "Egypt Gets US$2 Bn Loan from Libya," *Al-Masry Al-Youm Online*, April 13, 2013.

[27] Mohsin khan, "Qatar to the Rescue—Again!" *Reuters*, April 10, 2013.

[28] Alaa Shahine, "Egypt's IMF Loan Talks in Cairo End Without Agreement," *Bloomberg*, April 16, 2013.

Meanwhile, spending on fuel subsidies has increased by 40% from the previous fiscal year, largely due to a steady decline in the Egyptian pound.[29]

Stopgap funding from Qatar and Libya may allow Egypt to "muddle through" until later in the year, perhaps after parliamentary elections. By late April 2013, some economists began predicting that Egypt could avoid a fiscal crisis until late 2013. According to former finance minister Samir Radwan, "They [the Morsi government] go through the motions of pretending they are serious about an IMF deal, but actually they are not."[30] U.S. officials continue to emphasize the importance of an IMF deal, but may be frustrated by Egypt's inability to reach a deal. In recent testimony before the Senate Appropriations Subcommittee on State, Foreign Operations and Related Programs, Secretary Kerry remarked that:

> Egypt is more of a question mark right now. I mean, I'll just tell you, there are a lot of ifs about Egypt at this moment. And we've been working very, very hard with the Egyptian government to try to bring them to a point where they're prepared to embrace important reforms that are key to the IMF money, to be more inclusive with the opposition, to build out civil society, to live up to their promises regarding democracy, and it's a question mark whether they're going to make the right choices. And I can't frame it any other way for you now.[31]

Egyptian Politics and IMF Assistance

Many Egyptians view the history of modern Egypt as characterized by a long and painful legacy of the state being beholden to foreign powers, including the Ottoman Empire, European colonizers, and the United States. The narrative of colonialism and anti-imperialism permeates Egyptian political discourse and is particularly potent on issues of foreign lending and assistance. The IMF in particular is a controversial institution in Egypt, largely due to the popular association of IMF programs with autocratic rule under the Mubarak regime, and a common belief that IMF programs directly led to the rise of unemployment, poverty, inequality, and corruption (see **text box**).

[29] Asma Alsharif, "Egypt's Soaring Energy Bill to Exceed Previous Estimate," *Reuters*, 2013.

[30] Paul Taylor, "Egypt Seen Muddling Through Without IMF," *Reuters*, April 16, 2013.

[31] Senate Appropriations Subcommittee on State, Foreign Operations and Related Programs, Hearing on Fiscal Year 2014 State Department Budget, April 18, 2013.

Egypt and the IMF: Experience in the 1980s and 1990s

Egypt had four lending programs with the IMF in the late 1980s and 1990s, with commitments totaling about $1.7 billion. The programs focused on macroeconomic stability, including a large fiscal adjustment, an exchange rate anchor, conservative monetary policies, and moves toward liberalizing interest and exchange rate markets. The programs, particularly in the1990s, also included structural adjustment measures, such as privatization, trade liberalization, and deregulation, among other measures. From the IMF's perspective, policies aimed at macroeconomic stabilization were successful, producing "a remarkable turnaround in Egypt's macroeconomic fortunes in terms of reducing inflation, restoring confidence, and engendering external viability."[32] Egypt's efforts at structural adjustment are viewed more widely as less successful, although there is disagreement on why they failed to achieve the intended goals. Some analysts argue that the Mubarak regime did not commit strongly enough to the policy reforms, for example, by eventually largely abandoning privatization efforts due to fears of rising unemployment.[33] Other analysts argue that the government did implement reform efforts, but they came with high social costs, leading to mass layoffs of public workers, a more limited role for unions, and growing inequality.[34]

Older Egyptians from the middle and lower classes may have particularly high disregard for the IMF, as many associate reductions in their standard of living and political freedoms with IMF-mandated reductions in government spending and privatization. The IMF's lack of credibility with large segments of Egyptians has contributed to the reluctance of new leaders in Egypt to pursue a program.[35] One historian notes how former President Mubarak's government was acutely aware of the popular opposition to Egyptian acceptance of IMF reforms in the early 1990s:

> In the eyes of the regime, the economic reforms were a potential source of trouble not only because they led, or could lead, to material losses for a large part of the population; they were also potentially dangerous in that a considerable part of 'public opinion,' influenced by the dominant discourse of the past, considered them irreconcilable with the social and political achievements of the [1952] revolution and with their own interests.[36]

At present, it is difficult to gauge the extent of anti-IMF sentiment in Egypt. Although opposition to any Egyptian dealings with the IMF exists, most Egyptians are not necessarily blaming foreign lenders for their poor economy—yet. To date, small-scale protests have occurred outside the Egyptian stock exchange with protestors chanting that IMF support is akin to "economic colonialism."[37] Islamists, including hard-line Salafists, at times also have expressed reservations over accepting IMF support, arguing that Islamic law bans the payment of interest on loans. Egyptian leftists—who currently constitute the backbone of political opposition to Morsi—have been the most vocal opponents of IMF credit. They are led by third-place finisher in the 2012 presidential election, Hamdeen Sabahi, who has denounced the IMF loan on his Facebook page. Some analysts believe that there is widespread public apathy toward the IMF, with a poll

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[32] Arvind Subramanian, "The Egyptian Stabilization Experience: An Analytical Retrospective," IMF Working Paper Wp/97/105, September 1997.

[33] For example, see Alison Elizabeth Chase, "The Politics of Lending and Reform: The International Monetary Fund and the Nation of Egypt," *Stanford Journal of International Law*, vol. 42 (2006), pp. 193-236.

[34] Bretton Woods Project, "Rehash of Failed Policies for Arab States?" June 13, 2011.

[35] Chatham House, "The Role of International Loans and Capital in Egypt's Transition," MENA Programme: Egypt Dialogue Workshop Report, September 2011.

[36] Kienle, Eberhard, *Democracy and Economic Reform in Egypt,* I.B.Tauris, New York, NY, 2001, page 152.

[37] Stephen Kalin, "In Anti-IMF March, Austerity Fears and Economic Disillusion," *Egypt Independent*, November 11, 2012.

conducted in August 2012 showing that only two-thirds of Egyptians were aware of the IMF loan under discussion.[38]

During an IMF delegation visit to Egypt in mid-April 2013, fund representatives held meetings with various opposition figures and political parties, including Amr Moussa, Amr Hamzawy, Mohamed ElBaradei, the Wafd party, and Hamdeen Sabahi. Reportedly, these political figures voiced various demands, including calls for greater transparency in government-IMF negotiations, and concerns, such as the burden IMF-mandated reforms would pose for the average citizen.[39]

Egypt, the IMF, and U.S. Foreign Policy Goals

The Obama Administration has supported IMF involvement in Egypt, arguing that it promotes economic reforms in Egypt and would stabilize the economy and facilitate democratic transition. The Administration has encouraged President Morsi to reach out to the opposition and the public in order to garner political support to quickly reach a deal with the IMF. In April 2013, Treasury Secretary Jacob Lew expressed support for an IMF loan to Egypt, and explicitly stated that "It would be very much in the United States' best interests for Egypt to be on a more sustainable course."[40] Likewise, in a March 2013 visit to Cairo, Secretary of State John Kerry remarked that:

> In all my meetings, I conveyed a simple but serious message: The brave Egyptians who stood vigil in Tahrir Square did not risk their lives to see that opportunity for a brighter future squandered. The Egyptian people must come together to address their economic challenge. I encouraged President Morsi to implement the homegrown reforms that will help his country secure an IMF agreement, put Egypt on the path to establishing a firm economic foundation and allow it to chart its own course. He agreed and said that he plans to move quickly to do so.... The United States can and wants to do more. Reaching an agreement with the IMF will require further effort on the part of the Egyptian government and broad support for reform by all Egyptians. When Egypt takes the difficult steps to strengthen its economy and build political unity and justice, we will work with our Congress at home on additional support. These steps will also unlock much-needed private-sector investment and broader financial assistance.[41]

More broadly, however, there is debate within Washington over whether an IMF deal (among other things) is an opportunity, or not, for the United States to exert influence over the Islamist-led government of Egypt to pursue policies in line with U.S. interests and values. Some argue that Egypt's need for external assistance presents the United States, which has the largest financial stake and voting power in the IMF, with an opportunity to condition U.S. support for Egypt at the IMF on the government's commitment to, among other things, pursuing democratic principles and continued peace with Israel. Some analysts are especially concerned that President Morsi, a former Muslim Brotherhood leader, appears to be consolidating power at the expense of non-Islamist political forces—behavior that they believe the Obama Administration should signal is unacceptable. These advocates suggest that U.S. support for an IMF deal amidst perceived rising

[38] Ahmed Feteha, "Egypt and the IMF: Hardly Revolutionary," *Ahram Online* (in English), February 3, 2013; "Egyptians Split over IMF Loan: Opinion Poll," *Ahram Online* (in English), October 3, 2012.

[39] For example, see Aya Batrawy, "IMF Leaves Egypt after Hearing from Opposition," *Associated Press*, April 16, 2013.

[40] "U.S. Supports IMF Loan for Egypt to Stabilize Economy," *Reuters*, April 24, 2013.

[41] "U.S. Support for the Egyptian People," Department of State, March 3, 2013.

Islamist autocracy would be a setback for democracy in post-Mubarak Egypt. According to Egypt experts Robert Kagan (Brookings) and Michele Dunne (Atlantic Council):

> The United States made a strategic error for years by coddling Mubarak, and his refusal to carry out reforms produced the revolution of Tahrir Square. We repeat the error by coddling Morsi at this critical moment. The United States needs to use all its options—military aid, economic aid and U.S. influence with the IMF and other international lenders—to persuade Morsi to compromise with secular politicians and civil-society leaders on political and human rights issues to rebuild security and get the economy on track.[42]

On the other hand, some observers suggest that the United States should not push Egypt too hard in its negotiations with the IMF, arguing that Egypt is "too big to fail"—from a political and an economic standpoint (Egypt has the largest population of any country in the Middle East and North Africa [about 83 million]).[43] Proponents of an IMF deal assert that if economic collapse were to occur there, the consequences for global, regional, and U.S. national security would be severe. Examples of U.S. security interests in Egypt could include access to the Suez Canal for global commerce and U.S. naval vessels; Egypt's 35-year-old peace treaty with Israel; and U.S.-Egyptian and Egyptian-Israeli military and intelligence cooperation.

Moreover, opponents of stringent conditionality assert that any Egyptian government acceptance of IMF-mandated reforms would be politically painful enough; additional behind-the-scenes U.S. political pressure on President Morsi could unintentionally push him to seek financial aid from other, non-Western sources. Egyptian authorities have already received financial support from Saudi Arabia, Libya, and Qatar. It is unclear whether the Gulf countries support an IMF program for Egypt, and whether they are willing to commit to similar funding levels. It is also unclear what implicit or explicit political or economic conditions would be attached to financial assistance from neighboring countries in the absence of IMF involvement, and whether these conditions would be in line with U.S. interests.

Issues and Options for Congress

Considering U.S. Policy Toward Egypt at the IMF

Congress may reflect the bifurcated views identified above over the optimal U.S. policy toward Egypt at the IMF. Some lawmakers who oppose ongoing U.S. bilateral assistance to Egypt may oppose any existing or future IMF support of Egypt. For other lawmakers who may support existing aid to Egypt, the prospect of additional support to Egypt, either through the IMF, bilateral aid, or both, poses several potential concerns. First, some may be concerned that in the rush to stabilize Egypt, the Administration could be too lenient in terms of the reforms it seeks from the Egyptian government. Second, other lawmakers may not want the Administration to push for tough conditions on an IMF loan, fearing that onerous conditions could risk the Egyptian government avoiding an IMF loan and risking economic collapse, and/or risk pushing the Egyptian government to other sources of financing that may not be aligned with U.S. interests.

[42] Robert Kagan and Michele Dunne, "Standing by as Egypt Unravels," *Washington Post*, February 22, 2013.

[43] Heba Saleh, "Egypt Rules out IMF Emergency Finance," *Financial Times*, March 12, 2013.

If Congress wants to influence U.S. policy toward Egypt at the IMF, it has legislative tools at its disposal to do so. The executive branch, through the Treasury Department, manages day-to-day participation of the United States in the IMF, but Congress over the years has passed a number of "legislative mandates" that impact actions of the U.S. Executive Director at the IMF. Often, but not exclusively, included in appropriations bills, legislative mandates can direct U.S. representatives at the IMF to advocate certain policies, direct the U.S. Executive Director to vote for or against certain types of programs or policies, and/or require the Treasury Department to submit reports to Congress on IMF issues or activities. Existing legislative mandates focused on specific countries direct the U.S. representatives at international financial institutions (IFIs) to, for example, oppose non-humanitarian assistance to a specific country (as in the case of Belarus[44]); advocate assistance to help a government improve its economic system and accelerate development (as in the case of Mongolia[45]); or oppose any non-humanitarian financial assistance to a specific country until certain political conditions have been met (as in the case of Zimbabwe[46]). Congress could pass similar legislation directing the "voice and vote" of the U.S. Executive Director at the IMF with regard to IMF programs and policies toward Egypt. It could also pass resolutions laying out congressional views on IMF engagement with Egypt.

Using the IMF as a Benchmark for U.S. Assistance to Egypt

Some lawmakers may seek to use the terms of IMF conditions as "financial benchmarks" for the provision of existing or any new bilateral economic aid to Egypt.[47] One potential concern, however, is how stringent the conditionality attached to the IMF program would be. According to Egyptian economist Ashraf Swelam, "[a]t a time when the economic situation in Egypt is going from bad to worse, every new draft of the reform program submitted to the IMF—in the endless rounds of negotiations dating all the way back to February 2011—has been a watered down version of its predecessor."[48]

U.S. debt relief has already been tied to an IMF program (see **text box** below), and legislation has been introduced in the 113th Congress to require an IMF agreement as a condition for U.S. bilateral assistance. Specifically, during Senate debate in March 2013 over the full-year continuing resolution (H.R. 933, passed into law as P.L. 113-6), a proposed amendment (S.Amdt. 44) would have, if adopted, conditioned the obligation of U.S. economic assistance to Egypt on the President's certification, among other things, that the Government of Egypt has "signed and submitted to the International Monetary Fund a Letter of Intent and Memorandum of Economic and Financial Policies designed to promote critical economic reforms and has begun to implement such measures." This amendment was not included in the final legislation as enacted.

44 22 USC 5811 note; P.L. 109-480.

45 S.Res. 192.

46 22 USC 2151; P.L. 111-117.

47 Previous U.S. economic aid in the form of cash transfer had been tied to specific economic reforms undertaken by the government of Egypt and verified by the U.S. State Department and USAID.

48 "Egypt's Moral Hazard,"by Guest Blogger Ashraf Swelam for Steven A. Cook, Council on Foreign Relations, March 5, 2013.

U.S. Debt Relief for Egypt

On September 28, 2012, the Administration notified Congress of its intent to provide a $450 million cash transfer to Egypt (comprised of unobligated Economic Support Funds previously appropriated for other purposes) in order to repay its debts owed to or guaranteed by the United States. According to USAID, the $450 million was to be distributed in two tranches. The first tranche of $190 million would be released to the government of Egypt upon "the issuance of a public statement from the [Government of Egypt] GOE of its commitment to a national economic and fiscal stabilization,[49] recovery, and governance reform plan and to reach an agreement with the International Monetary Fund (IMF) on a loan package." The second tranche of $260 million would be distributed once the United States government determined that:

> The GOE has committed to and/or achieved actions on a homegrown economic and fiscal stabilization, recovery, and governance reform program that accords with international standards. The GOE would implement such a program in coordination with international financial institutions, including the IMF. The GOE could commit to and/or achieve such actions as reducing and streamlining energy subsidies; improving the government financial management; and increasing taxation revenues through a broadened tax base and reducing tax exemptions.

The Congressional Notification was issued weeks after an attack against U.S. diplomatic facilities in Libya in September 2012, which led to the death of Ambassador Christopher Stevens, and a protest outside the U.S. Embassy in Cairo in which a mob breached the Embassy walls and replaced the U.S. flag with a black one associated with Islamist extremist movements. Many lawmakers were angered by Morsi's failure to condemn the act immediately, apologize for the incident, and take more forceful police measures to protect the Embassy.

Upon receipt of the Congressional Notification, Representative Kay Granger, Chair of the House Appropriations Subcommittee on State and Foreign Operations, placed a "hold" on the $450 million cash transfer, stating that "This proposal comes to Congress at a point when the U.S. - Egypt relationship has never been under more scrutiny, and rightly so. I am not convinced of the urgent need for this assistance and I cannot support it at this time. As Chair of the Subcommittee, I have placed a hold on these funds."[50] Then-House Foreign Affairs Committee Chair Ileana Ros-Lehtinen also placed a hold on the aid.

The hold remained in place until lawmakers lifted it on the first tranche of $190 million only.[51] The notification of the release of these funds was made by Secretary of State John Kerry during his March 2013 visit to Egypt, where he said that, "In light of Egypt's extreme needs and President Morsi's assurance that he plans to complete the IMF process, today I advised him the United States will now provide the first $190 million of our pledged $450 million in budget support funds." As of April 2013, the second tranche of $260 million in cash transfer remains on hold.

Outlook

Financial assistance from neighboring countries may reduce the immediate fiscal pressures on Egypt, but it does not address deeper structural problems in Egypt's economy. If Egypt ultimately fails to reach an agreement with the IMF, it could signal a temporary setback for the Obama Administration, or it may be indicative of an oncoming period characterized by less U.S.-Egyptian cooperation on economic matters. In testimony before the House Appropriations Subcommittee on State, Foreign Operations, and Related Programs, Secretary of State Kerry questioned whether the United States should be doing more to influence Egypt, when he remarked that:

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[49] In November 2012, the IMF noted that "The Egyptian authorities have developed a national program that seeks to promote economic recovery, address the country's fiscal and balance of payments deficits, and lay the foundation for rapid job creation and socially balanced growth in the medium term." See, IMF, "IMF Reaches Staff-Level Agreement with Egypt on a US$4.8 Billion Stand-By Arrangement," Press Release No. 12/446, November 20, 2012.

[50] "Granger Holds Cash Transfer to Egypt," Rep. Kay Granger Press Release, September 28, 2012.

[51] "Obama Push to Aid Egypt Remains Stalled in Congress," *CQ Roll Call*, November 13, 2012.

> I can't give you assurances about what this current [Morsi] administration is going to do, because I think they're still sorting through that. And the die is not cast yet. That was the purpose of my visit [to Egypt] and the purpose of the money which I am grateful to you for releasing. Qatar has put another $2 billion at the availability of Egypt just in the last week or so. Before that, they put about $4 billion or $5 billion. Libya has loaned them $2 billion in the last week or so. And the IMF is in negotiating for $4.8 billion. We promised $1 billion and until I took the 190 [$190 million] that you kindly helped us to be able to provide, we didn't provide them with a dime, not a dime. We gave them a promise and a year later, we've given them zero. Now, you know, you don't buy your interests and you don't buy your—that's not what foreign aid is about. But I'll tell you, if you're not helpful to people in their time of need, if you're not there, part of the process, it's very, very difficult to have the kind of leverage to say, a diverse pluralistic politics is critical to us when they say, what's it matter to you? You don't really care. You're not helping us. The other guys are helping us. Thank you, we'll, you know, do what we want to do.[52]

On the other hand, though U.S. officials may not entirely embrace aid from non-IMF sources for Egypt such as Qatar, the Administration may feel that it must deal cautiously with Morsi's government so that the United States does not alienate friendly elements of the Egyptian opposition. Some policymakers may feel that non-IMF lending for Egypt may keep Egypt's financial situation in shaky, but workable order, and help to stave off a worst case scenario. However, it remains uncertain whether President Morsi's government can receive non-IMF stop-gap lending indefinitely, and on what terms.

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[52] House Appropriations Subcommittee on State, Foreign Operations, and Related Programs, Hearing on President Obama's Fiscal 2014 Budget Proposal for the State Department and Foreign Affairs, April 17, 2013.