



Editors: Paul Rivlin and Yitzhak Gal      Assistant Editors: Teresa Harings and Gal Buyanover

Vol. 2, No. 6    August 2012

## **Have Mercy on Morsi: Islamic Options for Egypt's Economy**

**Paul Rivlin**

The election of Mohamed Morsi to the presidency of Egypt in June 2012 means that the Muslim Brotherhood has come to power, or close to power, in the country's first democratic elections. While it is not clear how much power the new president will have, the potential for an Islamic agenda now exists. Given Egypt's huge economic problems, the question "What is Islamic economics and what can it do for Egypt?" has become crucial.

Islamic economic thought is concerned with social justice, good governance and respect for private property. Given the experiences of many countries in the Middle East that experimented with Arab socialism and then moved towards forms of capitalism inspired by the Washington Consensus, Islamic economics seems like a "middle way." It attempts to combine efficiency with equity, something that has obviously not been achieved in the Arab world in recent years and potentially brings to economic decision-making a moral or ethical consideration that has been missing.

In Morocco, Tunisia, Egypt and Jordan, Islamic parties have announced economic programs based on religious principles and they have had major electoral success. The public demands less corruption, more effective and more socially-oriented economic policies. There has been no open debate about how far the state should dominate the

economy: the unwritten assumption is that under Islamic rule, private assets will not be nationalized, unless they are large monopolies.

Three general principles dominate Islamic economic thinking. The first is that God created the world for mankind. While it is the right of every human being to secure his share of this world's wealth, his role is that of a caretaker. There is a kind of dual ownership shared between God and humanity. While personal property is accepted in Islam, the *Shari'ah* (Islamic law) limits human ownership with the notion that everything ultimately belongs to God.

Second, Islam aims to balance individual freedom and the communal benefit. Individuals thus have freedom of enterprise and competition in a context of morality, fairness and social harmony.

Finally, there is great emphasis in Islam on social and economic justice. This is possible only when all members of society can fulfill their economic needs. Therefore, those who are unable to take part in economic activity and those who need assistance should have their chances to exist assured. The goals of socio-economic justice and equitable distribution of income and wealth are integral parts of the moral philosophy of Islam. The poor and the needy are entitled to a share of the society's wealth.

*Zakat*, the giving of a fixed portion of one's wealth to the poor and needy, has central importance in Islamic society. While in Saudi Arabia *Zakat* has been enshrined as a tax, in other Arab and Muslim countries it is voluntary but state-regulated. Everyone is permitted to accumulate wealth that is left over after meeting one's legitimate commitments and after giving a percentage of one's income to charity. Another major tool for achieving socio-economic justice is the prohibition of *Riba* (usury) to avoid any unfair advantage in exchange dealings between parties.

Behind these principles there are religious beliefs and specific references that can be used as guides for policy. The first, as mentioned, is that real ownership belongs to Allah. Second, Islamic law (*Shari'ah*) forbids usury (*Riba*), which includes interest and monopolies. The head of an Islamic government (*Waliy al-Amr*) has the authority

to supervise and control the flow of the wealth in the country so as to maintain the public interest.

Can these principles be implemented or can they provide a framework for economic policy in Egypt? Before attempting an answer, we need to look at the state of the economy. From 2005 to 2010, Egypt's economic growth was relatively fast, largely the result of reforms that encouraged foreign investment. This growth did not transform the labor market and unemployment, especially among young people, remained a major problem. Inflation was high and when international food prices surged in 2008, the effect was felt in Egypt, posing a threat to the majority who live in poverty or close to the poverty line and spend 40 percent of their income on food. There was a widespread feeling that economic welfare was deteriorating and these factors all contributed to strikes and eventually to the massive demonstrations that forced Hosni Mubarak from power.

One and a half years after the revolution, Egypt's economy remains in recession. As a result, economic conditions have worsened. Given demographic growth of about 1.8 percent a year, an estimated three million people have been added to the population since January 2011.

Lower revenue collection and higher government spending since the revolution have widened the budget deficit, which is likely to have reached nearly 10 percent of GDP in the fiscal year 2011-12 (July 2011 to June 2012). This has caused an increase in the interest rates that the government pays on domestic treasury bills to almost 16 percent. The balance of payments has also worsened, with capital outflows and the sharp drop in tourism revenues and foreign direct investment. As a result, international reserves (including the central bank's foreign currency deposits in domestic institutions) declined to \$15 billion at the end of June (enough to cover three months' imports), from \$43 billion at the end of December 2010. The banking sector has remained relatively stable through this period, but liquidity conditions have tightened, credit to the private sector has fallen in real terms, and the growth of deposits has slowed.

In July, thousands of Egyptian state textile workers suspended strikes after receiving concessions following a pay dispute that brought a large part of the industry a halt. Some 23,000 employees at the Misr Spinning and Weaving Company—Egypt’s biggest textile company—had been on strike for more than a week, demanding better pay and conditions. They had been joined by about 12,000 staff from other state textile firms. The workers said their demands had been partially met but that they would resume industrial action in September if they did not receive more concessions.

President Morsi is seeking to use public spending to build a base of support in diverse sectors of society. He has promised a 15 percent increase in social allowances for public sector workers and pensioners, as well as a rise in payments provided to the poor. The rise in the base salary for public sector workers and pensioners will cost LE3.5 billion (\$580 million). It will be paid for by the state’s recently passed budget for 2012-13 and would be applied to salaries starting this month. Military pensioners will also get a 15 percent increase in their social allowances. Prior to Morsi’s announcement, the Cabinet had made plans to raise the social allowance by 10 percent across the board. Over six million public sector workers would benefit from the social allowance increase, irrespective of the level of their wages. An additional eight million pensioners would benefit, with a minimum increase of LE50 being applied. The social welfare assistance given to poor pensioners will also increase, from LE200 to LE300 per month.

Egypt has been trying for the last year and a half to negotiate a \$3.2 billion loan with the International Monetary Fund (IMF). But the IMF has insisted that a consensus among Egyptian political players be reached as a condition for the loan, and this has caused discussions to break down.

The economy faces a shortage of liquidity, with a large budget deficit, balance of payments pressures and the threat of devaluation. Initiatives such as the increased social allowance rely on finding a way to plug the growing hole in the budget, and help from the IMF is seen as a stepping stone to further external lending.

In 2012-13, state spending is expected to rise to LE533.7 billion (\$89 billion). About 80 percent of the budget is already allocated for public workers’ salaries, paying off Egypt’s debts, and food and fuel subsidies. This leaves only 20 percent for new

spending. Part of this will come from a reduction in fuel subsidies, which are due to be reduced to LE70 billion (\$12 billion) in 2012-13, compared with LE95 billion (\$16 billion) in 2011-2012.

Egypt needs to increase taxes paid by the better off and reduce subsidies paid to those who do not need them. It needs to find productive employment not only for the unemployed but for millions of public sector workers who contribute little to the economy but cost much. It also needs to create a level playing field in many markets that are the preserve of monopolies that came into being under Mubarak's regime and continue to play a role in the political system.

Morsi and the new government have to steer carefully because the military still dominate much of the economy as well as the political system. On 17 June 2012, the Supreme Council of the Armed Forces (SCAF) issued an annex to the constitutional declaration. This limited the President's powers, giving the SCAF the right of veto over the drafting of a new constitution, as well as legislative powers until a new Parliament is elected. The annex also stated that the SCAF remains responsible for the budget.

Budgetary freedom is also limited by its ability to create competitive markets. Finally, the international community needs to be catered to: the International Monetary Fund, the U.S., the Saudis, foreign bankers and potential foreign investors all want Egypt to maintain an open economy. Time is of the essence: Egypt's economy needs to run just to stand still; growth needs to be fast and durable for living standards to rise. Now it needs to run even faster to make up for the losses of the last year and a half. It does not look as if the government has enough room for maneuver. Implementing Islamic economics may be Morsi's *raison d'être*, but in the current environment, this will have to mean more than just raising wages. That was what Mubarak did and in the end it was one of the factors that generated inflation and helped to undermine him.

For the previous issue of *Iqtisadi*, click [here](#).

To republish an article in its entirety or as a derivative work, you must attribute it to the author and the Moshe Dayan Center at Tel Aviv University, and include a reference and hyperlink to the original article on the Moshe Dayan Center's website, <http://www.dayan.com/>