

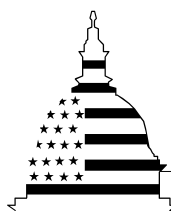
GAO

Report to the Chairman, Committee on
International Relations, U.S. House of
Representatives

July 2005

FOREIGN ASSISTANCE

USAID's Cash Transfer Program in Egypt Supports Economic Reform Activities, but Various Factors Have Limited Its Influence



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Highlights of [GAO-05-731](#), a report to the Chairman, Committee on International Relations, U.S. House of Representatives

Why GAO Did This Study

Since 1992, the U.S. Agency for International Development (USAID) has focused the Cash Transfer Program in Egypt on supporting economic reform activities to move Egypt toward a more liberal and market-oriented economy. USAID has provided funds to Egypt's government as it completed agreed-on economic reform activities. In fiscal year 2002, the Department of State and USAID conducted a review of U.S. economic assistance in Egypt that led USAID to renegotiate the program's terms. USAID and Egypt signed a new agreement in March 2005.

GAO's review of the Cash Transfer Program focused on the program's disbursement of funds and Egypt's completion of agreed-on activities, factors affecting the program's influence on Egypt's economic reform, USAID's efforts to evaluate the program's impact, and USAID's changes to the program in response to the 2002 review by the Department of State and USAID.

GAO received comments on a draft of this report from USAID. USAID stated that the draft was fair and clear but that Egypt's completion of about 70 percent of the activities resulted from the program's structure rather than shortcomings in Egypt's policy reforms. USAID also stated that extending the target dates for completing reforms increased U.S. influence in accomplishing reforms.

www.gao.gov/cgi-bin/getrpt?GAO-05-731.

To view the full product, including the scope and methodology, click on the link above. For more information, contact David Gootnick at (202) 512-3149 or gootnickd@gao.gov.

FOREIGN ASSISTANCE

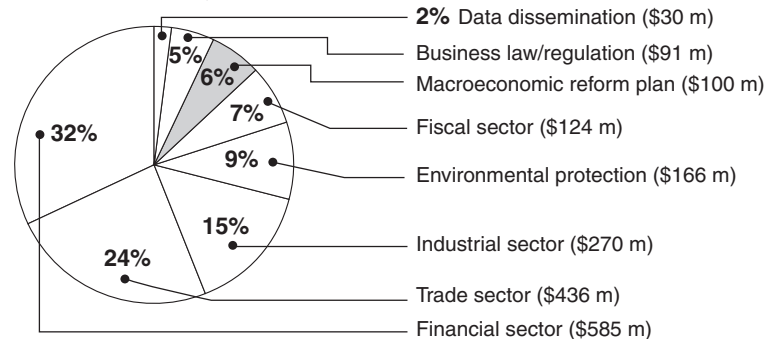
USAID's Cash Transfer Program in Egypt Supports Economic Reform Activities, but Various Factors Have Limited Its Influence

What GAO Found

Since fiscal year 1992, USAID's Cash Transfer Program has provided about \$1.8 billion in economic assistance to the Egyptian government for completing reform-related activities, such as privatizing state-owned companies. USAID and Egypt have identified 196 reform-related activities, and Egypt has completed 136 of them (about 70 percent), primarily in the areas of finance and trade.

Cash Transfer Program Disbursements by Reform Area

Total Disbursements: \$1.8 billion



Source: GAO analysis of USAID data.

Although the Cash Transfer Program supported Egypt's completion of reform activities, several factors have limited its ability to influence the Egyptian government to undertake certain reforms. First, the financial costs of certain reforms affected the Egyptian government's willingness to undertake them despite their potential benefits; although the Cash Transfer Program offsets some of those costs, its contribution to Egypt's overall budget is small. In addition, Egypt is cautious about undertaking reforms that may lead to domestic instability. Finally, USAID granted numerous extensions that allowed Egypt additional time to complete agreed-on activities, thus weakening the conditions tied to funding disbursement.

Despite the difficulty of determining the impact of policy reform, USAID conducted two evaluations of Cash Transfer activities as well as a series of opinion surveys on the impact of certain activities supported by the program. Although these studies reported some positive results, GAO found limitations with some of the measures used to evaluate the activities' impact on Egypt's economy.

In response to recommendations in the 2002 Department of State and USAID review, USAID (1) narrowed the Cash Transfer Program's focus to reforms in the financial sector, (2) will obligate funds when it is certain that the Egyptian government will complete activities rather than when the government agrees to undertake them, and (3) is improving its monitoring and evaluation system.

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Abbreviations

DSP	Development Support Program
IPR	intellectual property rights
IMF	International Monetary Fund
MOU	memorandum of understanding
PMP	Performance Management Plan
SPR	Sector Policy Reform
SDDS	special data dissemination standards
State	Department of State
USAID	United States Agency for International Development
WB	World Bank
WTO	World Trade Organization

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United States Government Accountability Office
Washington, D.C. 20548

July 11, 2005

The Honorable Henry Hyde
Chairman
Committee on International Relations
House of Representatives

Dear Mr. Chairman:

Since 1992, the U.S. Agency for International Development (USAID) has focused the Cash Transfer Program in Egypt on supporting economic reform activities intended to move Egypt toward a more liberal and market-oriented economy. Under the terms of the program, USAID provides funds to the Egyptian government as it completes specific activities related to reforms in a range of areas, including finance, trade, and industry. USAID and Egypt agree on these reform areas and activities in memorandums of understanding (MOU). In addition, USAID provides technical assistance to facilitate Egypt's completion of the reform-related activities. In 2002, the Department of State (State) and USAID conducted a joint review of USAID's activities in Egypt. Based on the review's recommendations, USAID began renegotiating the terms of the program, to which Egypt assented when it signed a new MOU in March 2005. The review by State and USAID recommended, among other things, that USAID narrow the Cash Transfer Program's focus, strengthen the agency's ability to enforce activity deadlines, and improve performance monitoring.

GAO's review of USAID's Cash Transfer Program in Egypt focused on (1) the program's disbursement of funds and Egypt's completion of agreed-on activities, (2) factors affecting the program's influence on Egypt's economic reform activities, (3) USAID's efforts to evaluate the program's impact on Egypt's economic reform, and (4) USAID's changes to the program in response to recommendations in the 2002 joint review by State and USAID.

To achieve these objectives, we analyzed USAID's criteria for making disbursements, as well as the total disbursements made under the Cash Transfer Program since fiscal year 1992. We also reviewed legislation, USAID regulations, and other relevant program documentation. We developed a database of all activities USAID targeted under the program and, to better understand the range of activities targeted and completed, we further analyzed three subsets of the reform areas covering a range of activities that had a mix of results—privatization, banking, and intellectual property rights. To determine the monetary significance of the Cash

Transfer Program, we calculated the program's annual share of Egypt's foreign exchange earnings and government revenue using relevant data provided by the Egyptian government to the International Monetary Fund (IMF). Although we were unable to assess fully the reliability of the Egyptian government data, we noted that Egypt recently subscribed to the IMF's special data dissemination standards (SDDS), which were created for nations that already meet high data quality standards. While these data probably have some limitations, we determined that it is unlikely that potential errors would materially impact our use of this information in our report. To understand USAID's efforts to evaluate the program, we reviewed USAID studies and opinion surveys that attempted to assess the impact of reform activities on the Egyptian economy and USAID's performance monitoring plan. We examined State's and USAID's joint 2002 review of U.S. economic assistance to Egypt and other relevant documents related to USAID's response to the review. We interviewed officials from USAID, the Department of State, the Department of the Treasury, the IMF, the World Bank, and the government of Egypt, as well as representatives of the European Union, economists, and academics. We performed our work between August 2004 and May 2005 in accordance with generally accepted government auditing standards. Appendix I provides a more detailed description of our objectives, scope, and methodology.

Results in Brief

Since fiscal year 1992, USAID's Cash Transfer Program has provided about \$1.8 billion in financial assistance to Egypt. Additionally, USAID had provided about \$70 million in technical assistance to the Egyptian government to support Cash Transfer Program related reform activities. USAID and Egypt jointly identified and agreed on 196 economic reform-related activities, of which Egypt has completed 136—for example, privatizing state-owned companies and drafting and passing intellectual property rights laws.¹ Egypt did not complete or receive program funds for 60 of the 196 activities because (1) a change in the program in 1999 allowed Egypt to select from a menu of reform activities, and (2) the United States withdrew from a 2001 MOU after the joint State and USAID review

¹We reviewed activities that were identified for reform in agreements between USAID and the Egyptian government, and we calculated the number of completed activities based on those for which USAID disbursed program funds. We included activities that USAID deemed partially complete and for which it consequently disbursed a percentage of program funds based on activity completion criteria.

recommended renegotiating the program's terms.² The program's disbursement values have ranged from \$0.1 million to \$150 million, with a median disbursement of \$10 million per reform activity. However, Egypt had received about \$730 million, or 40 percent of the total funds disbursed, for completing 20 activities, including \$100 million for developing a macroeconomic reform plan approved by the Egyptian government.

The Cash Transfer Program has supported Egyptian economic reforms, and USAID has provided technical assistance that aided Egypt's completion of reform-related activities; however, various factors have limited the program's ability to influence Egypt to undertake certain reforms. First, the financial costs of undertaking certain reforms have limited the Egyptian government's willingness to implement reforms despite their potential benefits. Second, although Cash Transfer Program payments help offset some costs related to reform activities, its contribution relative to Egypt's overall foreign exchange earnings and government revenue is small. Third, the Egyptian government is cautious about undertaking reforms that may negatively affect certain groups and lead to domestic instability. Fourth, USAID has granted numerous deadline extensions that allowed Egypt additional time to complete agreed-on activities, weakening the conditions tied to funding disbursements.

USAID has attempted to assess the impact of program-supported activities on the Egyptian economy, despite challenges involved in evaluating the impact of policy reform; however, its measures of the program's impact had limitations. USAID officials pointed out the difficulty of isolating the Cash Transfer Program's influence from other factors affecting Egypt's trade and investment environment. Nevertheless, to evaluate the impact of the program's activities, the agency has conducted agency-funded studies and opinion surveys of Egyptian business leaders and academics, and has linked some activities to its performance management plan. While each of these efforts highlighted the activities' positive impacts, they had limitations. For example, a study on the impact of privatization activities pointed out that the reforms helped reduce Egypt's fiscal deficit and improved some companies' financial performance. However, the study

²In 1999, USAID provided the government of Egypt with a "menu" of reform-related activities from which to choose, rather than a narrowly defined set of activities to undertake. Because the value of the total activities targeted under the menu approach was greater than funds available through the program, Egypt was not expected to complete all of the activities.

acknowledged the difficulty of drawing definitive conclusions regarding the activities' impact.

USAID has taken steps to respond to several recommendations regarding the Cash Transfer Program made in the joint State and USAID review. To narrow the program's focus, USAID's March 2005 MOU with the Egyptian government targets only financial sector reform activities.³ To strengthen its ability to ensure that the Egyptian government meets reform requirements, USAID will now obligate funds when it is clear that Egypt will complete the activities. To improve its measurement of program performance, USAID signed a contract in January 2005 with Management Systems International to revise the agency performance management plan, which assists USAID in monitoring and evaluating how well it is meeting its strategic objectives in Egypt. The details of the changes to the performance management plan were not available during the time of our review.

The Acting Assistant Administrator of USAID, Bureau of Management, provided written comments on a draft of this report which are reproduced in appendix II. He stated that the draft was fair and clear, but that the Egyptian government's completion of 70 percent of the 196 agreed-on activities related substantially to the Cash Transfer Program's structure rather than to shortcomings in Egypt's policy reforms. Additionally, USAID stated that granting deadline extensions to permit Egypt to complete activities increased the U.S. government's influence in accomplishing reforms. USAID also provided technical comments as did the Department of State, which we incorporated where appropriate.

Background

Since 1975, the United States government has provided more than \$25 billion in economic assistance to Egypt. The U.S. continues to support Egypt, in part because of its political leadership in making peace with Israel and fostering a broader peace between Israel, the Palestinians, and other Arab states, including its efforts in the war on terrorism. U.S. assistance to Egypt has three components. (1) The Cash Transfer Program provides assistance conditioned on the Egyptian government's achievement of specific reform-related activities. (2) Traditional project assistance focuses on, among other things, economic reform, health and education, and the environment. (3) The Commodity Import Program supplies financing to

³The new MOU negotiated by USAID and the Egyptian government was developed by the Department of State, the Department of the Treasury, and USAID.

Egyptian private sector importers of U.S. goods and provides funding that is not specifically conditioned on any reforms.⁴ In 1998, the United States and the Egyptian government agreed to reduce annual U.S. economic support by \$40 million per year, resulting in a reduction of total funds from \$815 million to \$407 million by fiscal year 2009. Annual Cash Transfer Program appropriations are projected to remain constant at about \$200 million annually until fiscal year 2007 and decline to \$150 million by fiscal year 2009.

In the early 1990s, USAID focused on fostering economic reforms aimed at achieving a stable macroeconomic environment in Egypt, then shifted its focus to encouraging economic growth and development in the mid-1990s. The goal of USAID's program activities in Egypt is to create "a globally competitive economy benefiting Egyptians equitably."⁵ Although Egypt has made progress at the macroeconomic level, including reducing inflation and unifying the exchange rate, USAID has stated Egypt's continued state ownership of companies and banks and its existing laws and regulations continue to hinder its transition to a market economy.

The Cash Transfer Program began as the Sector Policy Reform (SPR) program and complemented Egypt's economic reform and structural adjustment program, which began in 1991.⁶ In 1999, the program was renamed the Development Support Program (DSP) and focused on improving the trade and investment environment and increasing private sector employment.⁷ The Cash Transfer Program targeted eight general

⁴GAO, *Foreign Assistance: Observations on USAID's Commodity Import Program*, GAO-04-846T (Washington, D.C.: June 17, 2004).

⁵U.S. Agency for International Development, *USAID/Egypt Strategic Plan Update: FY 2000-2009, Advancing the Partnership* (Cairo: 2000).

⁶The IMF and World Bank (WB) supported an economic reform and structural adjustment program in Egypt that focused on (1) restoring macroeconomic balance and reducing inflation, (2) adjusting economic policies to stimulate medium- and long-term economic growth, and (3) revising social policy to minimize the negative effects of economic reforms on the poor. The IMF loaned Egypt approximately \$221 million and WB loaned Egypt \$300 million for these efforts. The IMF continues to provide Egypt technical assistance. In addition, under its Industrial Modernization Program, the European Union granted Egypt \$124 million dollars to support policy reforms between 1998 and 2004.

⁷For the purposes of this report, we refer to the program as the "Cash Transfer Program" since different names were used during our review period.

reform areas until the State and USAID review in 2002 recommended that it be narrowed to a single sector. These areas include the following:

- *Financial sector*—reforming the banking and insurance industries;
- *Trade sector*—reducing trade barriers;
- *Industrial sector*—privatizing state-owned companies;⁸
- *Business law and regulation*—modernizing laws that affect business and trade such as intellectual property rights laws;
- *Fiscal sector*—establishing tax policy and improving public access to fiscal data;
- *Monetary policy*—reforming foreign exchange rate and domestic credit policy;
- *Data dissemination*—improving standardization of data and statistical transparency; and
- *Environmental protection*—improving environmental regulations and conservation.

Funding for the Cash Transfer Program is provided in annual appropriations to the Economic Support Fund.⁹ The annual appropriation makes this funding available for the program with the understanding that Egypt will undertake economic reforms in addition to those it has undertaken in previous years.¹⁰ Grant agreements and MOUs between the U.S. and Egyptian governments outline the ways that Egypt may use program funds and the types of reform-related activities that it must

⁸USAID's definition of privatization evolved from "reducing a company's public ownership to less than 50 percent", to "reducing a company's public ownership to less than 20 percent."

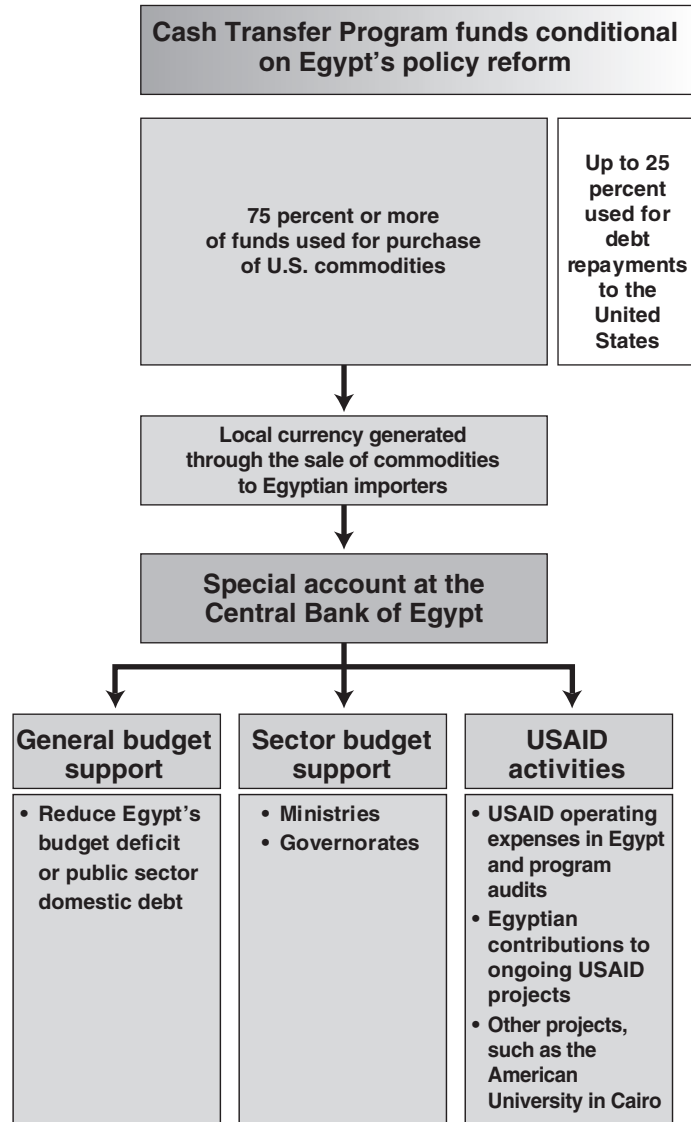
⁹22 U.S.C. § 2346 (2004).

¹⁰Consolidated Appropriations Act of 2005, Pub. L. No. 108-447, div. D, title II, 118 Stat. 2809, 2976 (2004).

undertake to receive them.¹¹ According to the grant agreements, the Egyptian government is authorized to use 75 percent or more of the funds to purchase U.S. commodities, such as wheat or equipment, and up to 25 percent to repay its debt to the United States. After purchasing commodities in U.S. dollars that the program provides, the Egyptian government must deposit the equivalent amount of Egyptian local currency into a special account. A separate MOU between USAID and the Egyptian government stipulates that the government of Egypt may use funds from this account for its general budget, sector support, or USAID activities. In addition to providing a source of budgetary funds for the Egyptian government, the Cash Transfer Program serves as an additional source of foreign exchange for Egypt. Figure 1 depicts the flow and use of Cash Transfer Program funds.

¹¹In this report, “reform-related activities” are activities that USAID identified for reform and the Egyptian government agreed to through MOUs. USAID uses various terms for these activities, such as “policy measures,” “indicators,” and “benchmarks.”

Figure 1: Cash Transfer Funding Flow



Source: GAO analysis of USAID data.

According to USAID officials, if the Egyptian government does not meet the agreed-on criteria for a specific activity, USAID may withhold funding and redirect it to support other Cash Transfer Program activities. To determine the funding that Egypt should receive for completing each

reform activity, USAID considers the activity's significance, the cost to the Egyptian government associated with completing it, the Egyptian government's willingness to implement it, the U.S. government's interest in seeing it implemented, and the contribution of the completed activity to Egypt's economic growth.

USAID Provided Financial and Technical Assistance to Support Egypt's Completion of Reform Activities

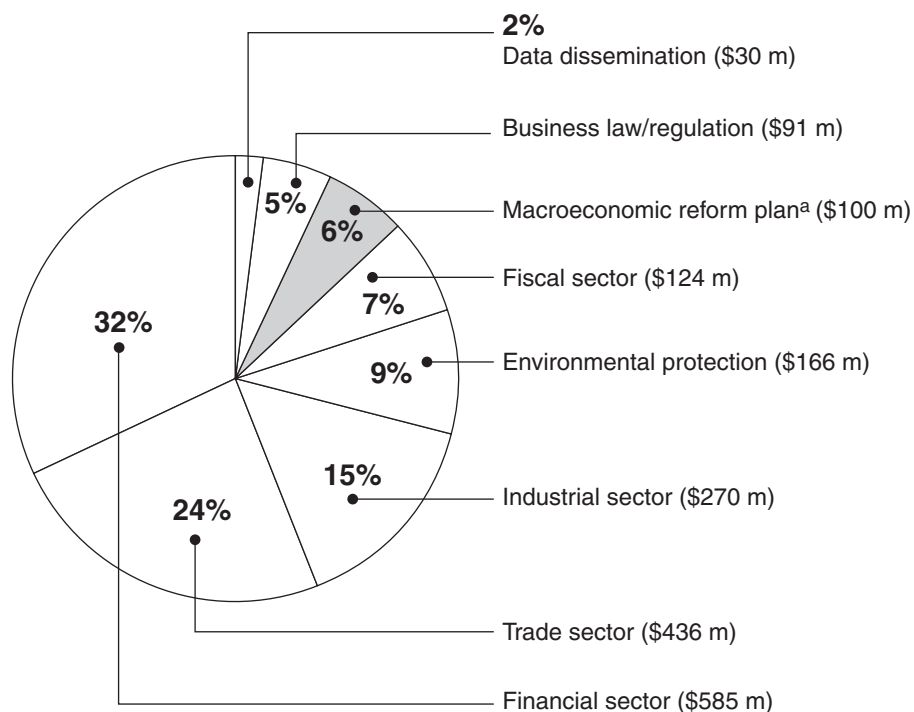
Since fiscal year 1992, USAID's Cash Transfer Program has provided about \$1.8 billion in financial assistance to the Egyptian government. USAID has also provided about \$70 million in technical assistance to the Egyptian government to support Cash Transfer-related reform activities. The Egyptian government has completed 136 of the 196 activities targeted for reform, including financial and industrial sector reforms. The Egyptian government did not complete 60 of the targeted activities and consequently received no money for them, in part because of a change in the program in 1999 that allowed Egypt to choose from a menu of reform activities. Although Egypt completed many activities, the results of some of the targeted reform areas were mixed. USAID's disbursements per activity ranged from \$0.1 million to \$150 million, with a median disbursement of \$10 million. However, Egypt received about \$730 million, or 40 percent of total funding, for 20 of the completed activities.

USAID Provided Almost \$2 Billion in Cash Transfer Program Funding and Technical Assistance

USAID disbursed about \$1.8 billion in Cash Transfer Program funds to the government of Egypt as it completed agreed-on economic reform activities, primarily in the areas of finance and trade. Figure 2 shows the distribution of program funding among the reform areas since 1992.

Figure 2: Cash Transfer Program Disbursements by Reform Area

Total Disbursements: \$1.8 billion



Source: GAO analysis of USAID data.

^aThe Macroeconomic Reform Plan was a crosscutting activity not included under any specific reform area.

In general, the targeted activities represented the steps associated with a major reform in agreed-on areas. For example, privatizing state-owned companies, an aspect of industrial sector reform, required

- initial steps such as conducting a study of the social and economic costs and the benefits of opening an industry to private investment,
- intermediate steps such as developing a national privatization plan, and
- final steps such as privatizing a number of companies.

In addition, USAID provided approximately \$70 million in technical assistance, in part to support the Egyptian government's completion of

agreed-on activities. For example, USAID's technical assistance funding supported the government of Egypt in formulating and implementing policies, training government personnel, and purchasing office equipment. USAID also used technical assistance funds to hire contractors to monitor and verify the government of Egypt's completion of agreed-on activities. According to Egyptian officials, USAID's technical assistance helped the Egyptian government complete intellectual property rights (IPR) reform activities targeted under the Cash Transfer Program, such as drafting an IPR code, and provided technical information on the World Trade Organization's (WTO) Trade-Related Aspects of Intellectual Property Rights requirements. Technical assistance funds were also used to promote public awareness of the importance of IPR and modernize the patent and copyright offices.

Egyptian Government Completed the Majority of Agreed-on Activities, but Results of Some Targeted Activities Were Mixed

Beginning in 1992, USAID and the Egyptian government identified 196 activities for reform. Egypt completed and received program funds for 136 of those activities (about 70 percent) and did not complete or receive money for 60 of them. Egypt had the option of not completing some of them, because under a new program approach initiated in 1999, USAID and the Egyptian government agreed to a broad range of activities that allowed Egypt to select those that best fit its reform agenda. The 60 uncompleted activities included 3 of 25 activities targeted for reform in a 2001 MOU. Egypt did not complete these 3 activities because the U.S. government unilaterally withdrew from the program following the 2002 review by State and USAID.¹²

Table 1 shows some of the 60 activities that the government of Egypt did not complete or receive program funds for under the terms of the program. We found that roughly 10 percent of the completed activities involved conducting studies and reviews, 10 percent involved drafting laws and issuing decrees, and about 20 percent involved adopting plans or implementing procedures. The remaining 60 percent involved various sector specific activities, such as reducing the number of tariffs and

¹²In responding to a draft of this report, USAID officials commented that the Egyptian government subsequently completed some of the activities—such as new regulations for customs procedures and reducing its shares in joint venture banks—but USAID did not disburse any funds for these activities because it was still negotiating the terms of the new MOU.

removing price controls from hotels, restaurants, and other businesses associated with tourism.

Table 1: Examples of Targeted Reform Activities That Egypt Did Not Complete, or Receive Funds for under the Terms of the Program

Reform area	Uncompleted activities
Fiscal policy	• Establishing a system to generate and publish revenue and expenditure data on a quarterly basis with a lag of no more than 2 months • Implementing key components of corporate tax reforms • Creating regulations to establish and regulate margin trading • Revising a draft competition law submitted to People's Assembly
Trade sector	• Reducing the cost of Egyptian air freight • Reducing import tariffs • Creating new regulations to improve customs valuation • Providing data for marketing approval of pharmaceutical products
Financial sector	• Reducing state ownership in at least five joint venture banks^a • Reducing Egyptian government share in at least one state insurance company to achieve private sector majority ownership • Passing legislation to facilitate a public debt law • Amending a capital market law

Source: USAID data.

Note: These examples include activities in all program years, although the Egyptian government may have subsequently completed some of them without receiving a payment from USAID.

^aJoint venture banks are private banks that have partial Egyptian government ownership.

To understand the range of activities USAID targeted and the extent to which Egypt completed them, we analyzed reform activities in three subsets of the program's general reform areas—privatization (industrial sector), banking (financial sector), and IPR (business law and regulation)—and found that the results of these targeted activities were mixed. For example, although Egypt privatized some of its state-owned companies and its joint venture banks, less than half of its state-owned companies and none of its public sector banks had been privatized as of May 2005. Likewise, according to USAID, although Egypt has improved its IPR legal framework, the country still does not fully comply with international standards for pharmaceutical protection.

Industrial Sector: Privatization

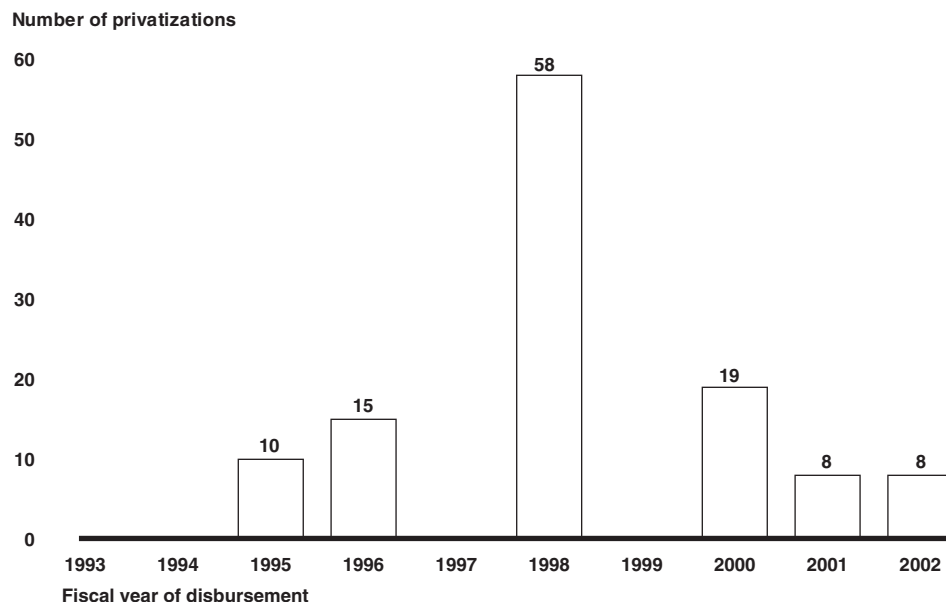
USAID disbursed \$169 million for the completion of 12 privatization activities in fiscal years 1992-2004. Six of the activities supported

privatization of companies—for example, developing a national privatization plan, reducing indebtedness of public companies, and improving the process for valuing of them. The other six activities consisted of actually privatizing public and joint venture companies.¹³ In 1991, the Egyptian government identified 314 companies to be privatized. During fiscal years 1993-2002, it privatized 118 of these companies, 3 of which were joint ventures, according to Cash Transfer Program disbursement justifications (see fig. 3).¹⁴ Privatizations slowly increased through fiscal year 1996, peaked in fiscal year 1998, and then declined through fiscal year 2002. Of the 196 remaining public companies, some are profitable but others are unprofitable, including indebted textile companies.

¹³Joint venture companies are private companies with partial Egyptian government ownership.

¹⁴Joint ventures were not included in the original list of 314 companies identified by the Egyptian government for privatization. Over time, some of the companies became joint ventures and remained on the list of companies to be privatized because the Egyptian government retained controlling ownership.

Figure 3: Number of Privatizations Supported by the Cash Transfer Program, Fiscal Years 1993-2002



Source: GAO analysis of USAID data.

According to Egyptian government and USAID officials, as well as documents we reviewed, three reasons contributed to the decline in privatizations after 1998. (1) The companies remaining on the list were difficult to sell because of unprofitability or were difficult to liquidate because of concerns about mass layoffs.¹⁵ (2) The Egyptian government did not fully support privatization, as demonstrated by its unwillingness to realistically value companies. (3) The global economic environment became less conducive to privatization, particularly in the Middle East after September 11, 2001. According to a USAID contractor responsible for tracking privatization progress, the best companies were sold initially and many of the remaining companies required large investments to stay operational.

¹⁵USAID counted liquidation as a form of privatization. Liquidation involves selling off the assets of a company to the extent that the company ceases to exist.

Financial Sector: Banking

In fiscal years 1992-2004, USAID disbursed \$260 million for the completion of 11 activities associated with banking reforms in Egypt. According to USAID documents, banking activities focused on improving regulations and strengthening banks' capital structure, including the following:

- allowing foreign banks to establish branches or gain full ownership of local banks and deal in local currency;
- removing controls on banking service fees;
- establishing new accounting and auditing procedures for all sectors, including insurance, based on the International Accounting Standards;
- revitalizing capital markets and improve the transparency of financial flows;
- ratifying an anti-money-laundering law, satisfying the Organization for Economic Cooperation and Development's Financial Action Task Force on Money Laundering, and
- reducing Egyptian government shares in 22 of 25 joint venture banks in Egypt.¹⁶

Additionally, the Egyptian government agreed to transfer majority ownership of at least one of its state-owned banks under the Cash Transfer Program in 1995 and sell its shares in the four public sector banks in 2000. Although the Egyptian government identified the first bank for privatization in 1997, none of the four state-owned banks had been privatized as of May 2005. In March 2005, the Egyptian government signed a new MOU with USAID that once again made the privatization of a state bank a priority. According to U.S. and Egyptian officials, a public sector bank is expected to be privatized by the end of 2005, owing in part to increased political will in Egypt's cabinet and more experienced management in the Central Bank of Egypt. However, a Central Bank senior

¹⁶Until 1998, the government of Egypt's state banks partially owned most of the joint venture commercial banks, which had a negative impact on the joint venture banks' profitability and competitive position in the banking sector. This activity reduced the Egyptian government's share of joint venture banks to less than 20 percent in each bank.

official stated that the sale of the public sector bank depends on its handling of nonperforming loans and finding an investor, which could prove difficult.

Business Law/Regulation: Intellectual Property Rights

USAID disbursed about \$75 million for the completion of six IPR-related reform activities undertaken to support Egypt's commitments under the WTO's agreement on Trade-Related Aspects of Intellectual Property Rights. According to a USAID contractor, although the reforms that Egypt completed moved it closer to international IPR standards, more reforms are needed for Egypt to achieve compliance with international standards related to data dissemination and data exclusivity for pharmaceuticals. The activities that USAID supported included the following:

- conducting a study of the benefits of consolidating the patent, trademark, and international design offices;
- joining the Patent Cooperation Treaty in June 2003;¹⁷ and
- enacting a new IPR law in May 2002 that incorporated both the patent and industrial design laws.

Small Number of Activities Accounted for Large Share of Program Funds

Since 1992, USAID has disbursed between \$0.1 million and \$150 million to Egypt for completed activities, with a median disbursement of \$10 million per activity;¹⁸ however, the Egyptian government received large disbursements, totaling about \$730 million (40 percent) of total program funds, for 20 of the 136 activities that it completed. Our analysis showed that the largest disbursements included \$150 million for passing an anti-money-laundering law and \$100 million for developing a macroeconomic reform plan approved by the government.

- *Antimoney-laundering law.* In 2002, Egypt received a disbursement of \$150 million for passing a law against money laundering. According to

¹⁷Although Egypt joined the Patent Cooperation Treaty, USAID did not disburse funds for this activity because the government of Egypt missed the activity's deadline.

¹⁸The average disbursement was about \$25 million; the average was higher than the median because of several large payments USAID made for activities completed between 2002 and 2004.

USAID, as Egypt's economy and financial systems have opened they have become more susceptible to use as conduits for laundering proceeds from criminal activities such as drug trafficking and terrorism. USAID first targeted anti-money-laundering reform in a 2001 MOU and formally specified the requirements for passage of a law in June 2002, the same month Egypt received a disbursement for completing the activity. According to USAID documentation, Egypt received a large disbursement because the law addressed the concern of the Organization for Economic Cooperation and Development's Financial Action Task Force that Egypt was noncooperative in addressing money-laundering problems.

- *Macroeconomic reform plan.* In 2001, Egypt received a disbursement of \$100 million for developing and approving a macroeconomic reform plan. According to USAID, this activity supported major Egyptian reforms in the face of the economic crisis after September 11, 2001, that included Egypt's slowed growth and loss of revenues. Among the areas the plan addressed were Egypt's exchange rate, monetary and fiscal policy, and legislation for issues such as IPR, labor and mortgage laws, and banking reform. According to USAID documents, the plan was added to the program in December 2001 and was approved by the U.S. Ambassador to Egypt, the Egyptian Prime Minister, and several of Egypt's economic ministers before the disbursement in January 2002.

Our review of program activities showed that USAID generally paid the Egyptian government once for each activity. However, we identified one instance in which USAID made disbursements twice to Egypt for the privatization of three companies. In 1998, USAID disbursed to the Egyptian government \$20 million dollars for meeting criteria to privatize 25 companies. Egypt's privatization of three of these companies—United Poultry Production, Ramsis Agriculture, and the Egyptian Company for Meat and Dairy Production—were listed in subsequent documents as justification for additional disbursements of \$2.4 million in 2000 and \$1.2 million in 2001.¹⁹ In commenting on a draft of this report, USAID officials agreed that these disbursements had occurred.

¹⁹The privatization of Ramsis Agriculture and the Egyptian Company for Meat and Dairy Products were used to justify a payment of \$2.4 million in 2000 and the privatization of United Poultry Production was used to justify a payment of \$1.2 million in 2001.

Various Factors Have Limited the Program's Ability to Influence Egypt's Reforms

Although the Cash Transfer Program provided financial and technical assistance to support Egypt's completion of reform-related activities, several factors have limited the program's ability to influence Egypt to undertake certain reforms. These factors include the following:

- *Financial costs versus benefits of reform-related activities.* Although the reforms are expected to generate financial benefits by correcting inefficiencies in the economy, financial costs are also associated with the reforms. For example, the authors of a USAID-sponsored study estimated the financial benefit to the Egyptian government of privatizing the remaining state-owned companies and banks would be over \$17 billion.²⁰ However, the financial benefits are not guaranteed; privatized companies may not operate more efficiently or produce additional tax revenues. For example, according to USAID's privatization study, some privatized Egyptian companies failed to undertake significant restructuring and therefore did not produce many of the expected benefits they were supposed to bring, including improved financial performance.
- *Size of program funding relative to Egypt's overall foreign exchange earnings and revenue.* Although the Cash Transfer payment provides U.S. dollars for the purchase of U.S. commodities and repayment of debt to the United States, the payment represents a small portion of Egypt's foreign exchange earnings. For example, in fiscal year 2003, the program's funds accounted for about 1 percent of Egypt's overall foreign exchange earnings and less than 2 percent of its foreign reserves. Additionally, the Egyptian pounds generated by the program and used by the Egyptian government for budget support are a small portion of its revenue; in fiscal year 2003, the program funds accounted for about 1 percent of the government of Egypt's annual revenues and grants. According to a State Department official, the \$200 million that the program provides annually is not sufficient by itself to persuade the Egyptian government to undertake an unpopular reform such as privatization.

²⁰David T. King, Bruce MacQueen, and Mack Ott, *The Cost of Not Privatizing: An Assessment for Egypt. Survey and Empirical Analysis. Submitted to USAID/Egypt* (Bethesda, Md: IBM Business Consulting Services, 2004).

-
- *Reforms' potential effects on domestic stability.* Since IMF sponsored economic reforms triggered protests and domestic unrest among Egypt's populace in the 1970s, the government of Egypt has been cautious about reforms such as liberalizing prices and lifting subsidies because of the potential negative impact on certain groups. For example, in January 2003, the Egyptian government introduced a more flexible and market-oriented exchange rate regime as outlined in its macroeconomic reform plan. However, as a result, the value of the Egyptian pound fell by about 30 percent in its initial months, raising the prices that Egyptians paid for imported goods, including food. According to the IMF, the Ministry of Finance partially negated this change when in September 2003, concerned about rising food prices, it introduced a special exchange rate for imported items such as grains.²¹
 - *Cash Transfer Program deadlines.* The Cash Transfer Program was designed to provide funding to Egypt based on its compliance with agreed on conditions, including meeting deadlines. Since fiscal year 1992, the government of Egypt requested, and USAID granted, 19 extensions to the deadlines originally agreed to in MOUs. The extensions were generally for an additional 3 to 6 months; however, certain performance periods had multiple extensions that allowed the government of Egypt 2 or more years from the original deadline to complete the activities.²² Although USAID documents justified the extensions, the number and length of extensions may have weakened the conditions tied to the funding disbursement by assuring that Egypt continued to receive funds, in some cases well beyond the established deadlines. For example, in March 1997, USAID extended the Egyptian government's deadline to complete agreed-on activities for an additional 6 months and then granted five other extensions, resulting in a final deadline of September 1999. According to USAID documents we reviewed, the 1997 extensions were granted to give the government of Egypt time to negotiate a new IMF agreement, prepare for the Cairo economic summit, and redefine reform priorities after a shift in Cabinet members—factors that contributed to a delay in Egypt's completion of Cash Transfer Program reform activities. USAID approved additional deadline extensions for a separate set of activities in September 1997,

²¹International Monetary Fund, *Arab Republic of Egypt—Staff Report for the 2004 Article IV Consultation* (Washington, D.C.: 2004).

²²A performance period is the period of time between the date that the government of Egypt agreed to undertake an activity and the deadline for completing it.

subsequently extending it four more times to June 2000. The need to tighten conditions tied to the program's funding disbursements was highlighted in the 2002 review by State and USAID.

USAID Made Efforts to Evaluate Cash Transfer Program's Impact on Egypt's Reforms, but The Assessments Had Limitations

Demonstrating the impact of policy reforms is challenging, according to USAID officials and academics studying such reforms; however, USAID conducted two evaluations related to the Cash Transfer Program activities, as well as a series of opinion surveys that attempted to assess the impact of economic reform activities supported by the program. These evaluations and opinion surveys reported that the program's activities had some positive results, but we found limitations with the two studies. We also reviewed USAID's performance management plan (PMP) and found that some of its measures had limitations.

Measuring Policy Reform's Impact Is Challenging

USAID officials and academics studying policy reform pointed out the difficulties of demonstrating the impact of policy reforms. USAID officials stated that it is nearly impossible to isolate the impact of the Cash Transfer program from other factors that have influenced Egypt's trade and investment environment. In addition, collecting reliable data is problematic in Egypt. For example, according to a USAID contractor responsible for tracking Egypt's privatization efforts, basic data, such as the number of privatizations completed, were not readily available from the Egyptian government. Furthermore, the nature of policy reform often results in delayed impacts, thus evaluations cannot take place until sufficient time passes. For example, according to USAID's privatization evaluation, it was difficult to draw definitive conclusions regarding financial performance for some of the companies because of inadequate time between the privatizations and evaluation. Although measuring the impact of reforms is difficult, USAID continues to fund various assessments.

USAID Efforts to Evaluate Program's Impact Showed Positive Results but Had Limitations

To evaluate the impact of Cash Transfer Program activities in Egypt, USAID conducted two agency-funded studies, twelve opinion surveys of private sector business leaders, and linked some activities to its PMP. However, we found that some measures that USAID used in their performance management system had limitations.

- **USAID-funded reform area studies**

A study of USAID-supported privatization activities published in 2002 pointed out some positive impacts, such as helping to reduce Egypt's fiscal deficit, facilitating the entrance of new companies into Egypt's market, expanding product varieties and availability, and improving some firms' financial performance.²³ However, the study also found that privatization did not increase Egypt's foreign direct investment relative to other developing countries although this reform was related to USAID's strategic objective of enhancing Egyptian business opportunities by attracting private sector investment. In addition, the study acknowledged some challenges in evaluating privatization's impact because access to some of the Egyptian government's data was limited and sufficient time had not passed to assess the financial performance of some privatized companies.

A study of USAID technical assistance for Egypt's IPR reforms published in 2004 found that this assistance, among other factors,²⁴ motivated the Egyptian government to implement reforms. The study found that these reforms led to: a legal framework that was more compliant with WTO IPR requirements; a modernized IPR-related facilities; a reduction in the time required to obtain a patent from 6 years in 1996 to less than 3 years in 2003; and, increased public awareness of the benefits of intellectual property rights.²⁵ However, the study focused on the outcomes of USAID's technical assistance to support the completion of IPR-related activities rather than on the impact of these activities on the Egyptian economy, such as increasing confidence among foreign investors, with regard to doing business in Egypt.

- **Opinion surveys**

²³Carana Corporation, *The Results and Impacts of Egypt's Privatization Program* (Cairo, Egypt: USAID Coordinating and Monitoring Services Project, 2002).

²⁴Other factors included (1) USAID's Cash Transfer Program, (2) Egypt's IPR-related obligations under the WTO's membership, and (3) Egypt's placement on the U.S. Trade Representative's Priority Watch list.

²⁵Development Associates, Inc., *Assessing the Effectiveness of Technical Assistance for Policy Reform: The Case of Intellectual Property Rights Reform in Egypt* (Cairo: USAID, 2004).

USAID conducted a series of periodic questionnaires and roundtables with Egyptian private sector leaders and academics to gauge the progress and impact of the Egyptian government's economic reforms and structural adjustment program.²⁶ Every 6 months for a 6-year period, respondents were asked to score and give opinions on 24 policy areas in three main categories: stabilization policies, structural adjustment policies, and social policies. The surveys found that, in general, business leaders agreed that the Egyptian government had taken modest steps forward in stabilization policies. However, the survey also found that business leaders were concerned about slow progress in many reform areas, such as banking and privatization, exchange rates, and the growth of small and midsize businesses. USAID recognized that the survey scores and opinions are subjective. However, USAID pointed out that respondents' perceptions of the behavior of the domestic and international marketplace served as a proxy for the larger business community's opinion of Egypt's progress with economic reform. As a result, USAID said the survey could be a useful tool for evaluating policy initiatives.

- **USAID's performance management plan**

USAID uses its PMP to measure progress toward strategic goals and objectives. Although the PMP does not directly evaluate the impact of the Cash Transfer Program, USAID pointed us to it as a measure of the program's progress and impact on the Egyptian economy during our fieldwork. However, we found limitations in some of the indicators used in the PMP in that they primarily assess outputs and do not link the outputs to the activities' impact on Egyptian economic reform. For example, two privatization indicators—*the value of sale proceeds from privatized state-owned and joint venture companies* and *the cumulative number of qualified joint venture companies and banks divested*—measured the quantitative results of privatization rather than the activities' effects on the companies' efficiency. Other PMP indicators were influenced by factors outside the program. For example, USAID used the indicator *trade weighted average tariffs* to show progress in reducing trade barriers; however, other factors, such as a shift to imports with lower tariffs, could have contributed to a

²⁶The results of the survey cannot be viewed as representative of all academics and or business leaders in Egypt because its population was small and not selected randomly and had a response rate of about 50 percent.

reduction in trade barriers, and thus the change could not be attributed only to the reform's impact.

USAID Is Taking Steps to Respond to Recommendations by State and USAID

USAID has taken several steps to address the 2002 State and USAID review's recommendations that the agency narrow the focus of the Cash Transfer Program, reprogram funds if deadlines for reform-related activities are not met, and improve the USAID mission in Egypt performance monitoring system.

1. To narrow the program's focus, USAID signed an MOU on March 20, 2005, focused on reforming the financial sector.²⁷ The new MOU aims to support financial sector modernization by:
 - strengthening the management of the Central Bank of Egypt;
 - creating a government securities market consistent with international standards;
 - increasing the private sector's share of the banking system;
 - strengthening the legal and regulatory framework of the overall financial system; and
 - implementing a code of corporate governance.

USAID and the Egyptian government agreed to 19 reform-related activities that support these goals, including privatizing one of four state-owned banks before the end of December 2005. According to USAID officials, if the Egyptian government completes all 19 reform-related activities by the agreed-on time frames, it will receive disbursements of \$800 million, or 67 percent of the \$1.2 billion that USAID expects to obligate for the Cash Transfer Program through fiscal

²⁷The review recommended that the Cash Transfer Program focus on "no more than two broad sets of economic reform goals at any one time," whereas previous MOUs targeted several reform areas.

year 2009.²⁸ USAID has not yet determined the conditions for disbursement of the remaining funds, but a State official stated that the agency will likely target trade reform.

2. To respond to the review's recommendation to reprogram funds if reform-related activity deadlines are not met, USAID changed its process for obligating Cash Transfer funds. Beginning in 2005, USAID will obligate Cash Transfer funds only after it is certain that the Egyptian government will complete agreed-on activities. This change is intended to ensure that obligated funds do not accumulate and to strengthen USAID's ability to encourage the Egyptian government to satisfy activity requirements.
3. To improve its measurement of the mission's programs' contribution to meeting USAID strategic objectives, the agency contracted to revise its performance monitoring system by updating its PMP.²⁹ The review by State and USAID indicated that the previous system did not allow USAID to reprogram resources from programs that were not producing desired results. According to a USAID official, the system's measures also did not provide timely information for management purposes. However, at the time of our review, details of PMP revisions were not available; therefore, we were unable to determine how USAID will address the issues raised by the review and whether the new system will improve evaluation of Cash Transfer Program activities.

Conclusions

Although the Cash Transfer Program has supported reform-related activities since 1992, several factors have constrained its influence and potential to be a more effective force for change in Egypt. However, the recently signed MOU, which makes deadlines explicit for the first time, and Egypt's renewed political support to undertake certain reforms, such as bank privatization, offers a new opportunity to better leverage this program. For example, by not making funds available until it is clear that

²⁸In addition to the \$800 million that the Egyptian government may receive for completing financial sector reform activities by the end of fiscal year 2009, it received \$100 million for signing the financial sector MOU and developing a related matrix of time-bound reform-related activities. For the first time, deadlines for completing the activities were specified in the new MOU, whereas previously deadlines were determined after an MOU was signed.

²⁹The Cash Transfer Program falls under USAID's strategic objective of strengthening the environment for trade and investment.

Egypt will complete program activities, USAID is strengthening conditionality. Given the recent program changes and Egypt's regional importance, it is critical that policymakers continue to monitor Egypt's progress in achieving economic reform and the Cash Transfer Program's contribution to those reforms, especially in light of the broader political environment in which the program operates.

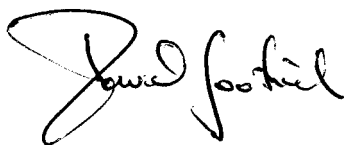
Agency Comments and Our Evaluation

The Acting Assistant Administrator for USAID, Bureau of Management, provided written comments on a draft of this report, which are reproduced in appendix II. He stated that the draft was fair and clear, but that the Egyptian government's completion of 70 percent of the 196 agreed-on activities related substantially to the Cash Transfer Program's structure rather than to shortcomings in Egypt's policy reforms. Additionally, USAID stated that granting deadline extensions to permit Egypt to complete activities increased the U.S. government's influence in accomplishing reforms. USAID also provided technical comments as did the Department of State, which we incorporated where appropriate.

As arranged with your office, we plan no further distribution of this report for 30 days from the date of the report unless you publicly announce its contents earlier. At that time, we will send copies to interested congressional committees and to the Administrator, USAID and the Secretary of State. We will make copies available to others upon request. In addition, this report will be available at no extra charge on the GAO Web site at <http://www.gao.gov>.

If you or your staff have any questions regarding this report, please contact me at 202-512-3149 or gootnickd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix III.

Sincerely yours,

A handwritten signature in black ink, appearing to read "David Gootnick". The signature is fluid and cursive, with the first name "David" and last name "Gootnick" clearly distinguishable.

David Gootnick
Director, International Affairs and Trade

Objectives, Scope, and Methodology

This review for the Chairman of the House Committee on International Relations, focused on (1) the Cash Transfer Program's disbursement of funds and Egypt's completion of agreed-on activities since in fiscal year 1992, (2) factors affecting the program's influence on Egypt's economic reform activities, (3) U.S. Agency for International Development's (USAID) efforts to evaluate the program's impact on Egypt's economic reform, and (4) USAID's changes to the program in response to the 2002 Department of State and USAID review.

To identify the requirements of the Cash Transfer Program and total funding disbursed since fiscal year 1992, we reviewed legislation and USAID's regulations, grant agreements, and memorandum of understanding. We reviewed USAID's program documents and interviewed USAID and State officials to learn how USAID identified reform areas and assigned values for reform-related activities and to determine the number and types of activities that the government of Egypt completed. We also developed a database of all the activities targeted by USAID to identify: the number of completed and uncompleted activities, the various types of activities, any duplication in the activities or payments, and any changes to the originally targeted and agreed-on activities. We developed the database using attachments to the program's memorandum of understanding (MOU), which included activities that USAID and the Egyptian government agreed to undertake in support of economic reforms. To determine the number of completed activities, we used USAID disbursement memorandums. We also included activities for which USAID disbursed program funds although the entire activity was not completed (in 20 instances, USAID disbursed partial payments based on the percentage of the activity that it determined Egypt had completed). We did not include activities that Egypt completed outside the terms of the program because there were no disbursement memorandums for these activities. We corroborated testimonial evidence from USAID, State, and Egyptian officials with our analysis of program activities by reviewing and comparing information in USAID's program documents. We reviewed internal controls, including reports by USAID's Office of Inspector General, as well as potential for fraud and abuse and compliance with laws and regulations and found no significant issues. We did not independently evaluate Egyptian laws and regulations, and our discussion of them is based on secondary sources.

To better understand the range of activities targeted and completed under the program, we selected three subsets of the reform areas. The three subsets for which we conducted a more in-depth analysis were privatization, banking, and intellectual property rights (IPR) and these

subsets covered 29 out of 196 targeted activities (15 percent). They did not constitute a representative sample of all the activities; however, we consulted USAID and identified areas with varying results. For example, USAID characterized IPR reforms as successful, whereas banking and privatization had varied levels of success.

To determine factors affecting the program's influence on economic reform in Egypt, we reviewed documents and interviewed U.S. and Egyptian officials with knowledge of the Cash Transfer Program. We also met with International Monetary Fund (IMF), World Bank, and European Union officials, as well as an expert at the Egyptian Center for Economic Studies. We reviewed studies on the benefits and the costs of reforms that were published in refereed journals or completed by USAID contractors; we also interviewed the authors of one of these studies¹ and discussed their methodology. To determine the monetary significance of the Cash Transfer Program, we calculated the program's annual share of Egypt's foreign exchange earnings and government revenue using relevant data provided by the Egyptian government to the IMF. Although we were unable to fully assess the reliability of the Egyptian government data, we noted that Egypt recently subscribed to the IMF's special data dissemination standards, which were created for nations that already meet high data-quality standards. Although these data probably have some limitations, we determined that it is unlikely that potential errors would materially impact our use of this information in our report. To identify other factors affecting the program's influence, we analyzed program documents to calculate the number of times that the Egyptian government requested, and USAID granted, deadline extensions to complete program activities.

To assess USAID's evaluation of the program's impact on economic reform, we reviewed studies that addressed the methodological challenges of conducting impact evaluations. We also met with, and reviewed studies by, contractors hired by USAID to assess the impact of two program areas, IPR and privatization. In addition, we reviewed USAID's opinion surveys reports and performance management plan.

To determine the steps that USAID has taken in response to the 2002 review by State and USAID, we interviewed USAID and State officials who participated in or had knowledge of the review, focusing only on those recommendations that referred to the Cash Transfer Program. We

¹King, MacQueen, and Ott, *The Cost of Not Privatizing*.

interviewed USAID, State, Treasury, and Egyptian officials who were involved in negotiating the new financial sector MOU, and we reviewed funding data to determine the amount and proportion of program funds allocated to financial sector reform. To corroborate testimonial evidence provided by USAID, State, and Treasury officials, we also reviewed the USAID mission in Egypt's updated strategic plan, revised in March 2004. Further, we consulted USAID officials regarding any legal issues to reprogramming Cash Transfer Program funds, and we reviewed documents showing USAID's funding process. To understand how the USAID mission in Egypt plans to improve its performance monitoring system, we interviewed USAID officials and contractors who are responsible for developing it.

We performed our work between August 2004 and May 2005 in accordance with generally accepted government auditing standards.

Comments from the U.S. Agency for International Development

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



June 15, 2005

Mr. David Gootnick
Director
International Affairs and Trade
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Gootnick:

I am pleased to provide the U.S. Agency for International Development's (USAID) formal response on the draft GAO report entitled "*USAID's Cash Transfer Program in Egypt Supports Economic Reform Activities, but Various Factors Have Limited Its Influence*" (GAO-05-731) (July 2005).

We have reviewed the draft report and appreciate the time and effort of your team. While we appreciate the fairness and clarity of the draft GAO report, there are several points raised in the report on which we have provided comments in the enclosed document.

Thank you for the opportunity to respond to the GAO draft report and for the courtesies extended by your staff in the conduct of this review.

Sincerely,

A handwritten signature in black ink, appearing to be "S. Wisecarver".

Steven G. Wisecarver
Acting Assistant Administrator
Bureau for Management

Enclosure: a/s

U.S. Agency for International Development
1300 Pennsylvania Avenue, NW
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DRAFT COMMENTS

USAID appreciates the GAO's very close and professional collaboration with USAID staff in studying the U.S. cash transfer program to Egypt. USAID also appreciates having had the opportunity to provide detailed comments on a draft of the report.

The GAO's draft included valuable descriptions of progress that Egypt has made in several areas where USAID provided support through cash transfers. Based on the Congressional request, the GAO's draft report also focused on four specific issues, stated in the draft's Appendix 1. With respect to these issues, USAID would like to draw attention to two principal points.

1. Completion of Agreed Reforms

Because of the extraordinary breadth of the USG's policy dialogue with the Government of Egypt (GOE), USAID and the GOE have agreed on reforms worth significantly more than the available cash transfer funds. To expedite implementation of the overall reform program, some cash transfer agreements were structured to trigger disbursements on a first-come, first-served basis. As this implies, the GOE subsequently implemented some reforms without receiving cash transfer disbursements. Examples of agreed, implemented, but unremunerated reforms include creation of regulations to establish and regulate margin trading, drafting and enactment of a competition law, new regulations to improve customs procedures, and reduction of state ownership in joint venture banks.

Thus, the GAO draft's finding that "the Egyptian government completed about 70 percent of the 196 activities it agreed to" related in substantial part to the structure of the cash transfer program, and not entirely to shortcomings in policy reforms. Furthermore, please note that the GAO's draft did not suggest that only 70 percent of cash transfer disbursements were justified. On the contrary, disbursements of more than 100 percent of the cash transfers would have been justified by the GOE's implementation of agreed reforms, had additional funding been available.

2. Deadlines

The draft mentioned that USAID and the GOE had revised the initial target dates for some of the agreed reforms, and that these reforms were subsequently implemented and cash transfer disbursements approved. Given that the initial target dates were estimates and were not material to the desired impact of the reforms, the GAO draft's factual findings tended to show that the revisions of

See comment 1.

See comment 2.

See comment 3.

target dates increased the USG's influence in accomplishing reforms. With the two points above taken into consideration, USAID believes that the GAO's draft provided a clear and fair response to the Chairman's inquiry.

Finally, USAID notes that the scope of the Congressional request did not appear to allow the GAO to address broader questions concerning the Government of Egypt's overall progress in modernizing its economic policies and USAID's overall approach to assisting this progress. USAID's approach includes a substantial program of technical assistance, NGO grants, and multilateral cooperation, in addition to the cash transfers. This program addresses some priorities, such as trade capacity building, that extend beyond the cash transfer program's present focus.

USAID is committed to a continuous effort to adapt its policy-reform program in Egypt to the evolving state of knowledge about policy-reform assistance and to the opportunities afforded by events on the ground. We welcome the GAO's valuable contribution to this effort.

The following are GAO's comments on the U.S. Agency for International Development letter dated June 15, 2005.

GAO Comments

1. In our report we acknowledge the collaborative process between USAID and the government of Egypt to identify and agree on reforms (see pages 1, 2, 11). However, in reviewing program agreements and discussing the program with USAID officials, we found only one agreement that used the “menu approach”—that is, targeting activities that were worth more than the available cash transfer funds during the 12-year period of our review (1992-2004). We explain that the scope of activities we reviewed was limited to those targeted under the USAID program (see pages 2 and 26) and that Egypt completed some reform activities for which they did not receive program funds (see pages 3, 11).
2. USAID states that our finding that the Cash Transfer Program completed 70 percent of the targeted activities “is related in substantial part to the structure of the Cash Transfer Program, and not entirely to shortcomings in policy reforms.” As we note in comment 1 and on pages 3, 9, and 11 of the report, the structure that USAID refers to was in effect only from 1999 to 2003. Regarding USAID’s concern that presenting the percentage of agreed-on activities completed by Egypt suggests a shortcoming in Egypt’s progress in policy reform, our findings reflect the fact that USAID and the Egyptian government agreed on 196 reform activities during the period covered by our review and the Egyptian government completed 136 of those activities.
3. USAID states that our findings show that the revisions of target dates increased the U.S. government’s influence in accomplishing reforms. Although USAID’s provision of extensions may have allowed the Egyptian government to complete the reforms, we disagree that our findings show that revising the target dates increased the U.S. government’s influence, as USAID asserts. Rather, we believe that the practice weakened one of USAID’s tools of conditionality—deadlines. Additionally, the 2002 review by State and USAID pointed out the need to focus more tightly the conditionality of the Cash Transfer Program and indicated that “in the event that outcomes, benchmarks and timelines agreed with the Egyptian government are not met within a reasonable time of the originally agreed target dates the team agreed that DSP II funds will be reprogrammed to fund other USAID projects in Egypt.”

GAO Contact and Staff Acknowledgments

GAO Contact

David Gootnick (202) 512-3149

Acknowledgments

In addition to the individuals named above, Phillip Herr, Julie Hirshen, Adrienne Spahr, Ming Chen, Joel Green, Eve Weisberg, Grace Lui, Reid Lowe, and Martin de Alteriis made key contributions to this report

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