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Liberal Economic Reforms and the Rise of Crony Capitalism in the MENA Region

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Abstract: This article examines how the economic liberalisation in the Middle East and North Africa (MENA) region created a ripe climate for crony capitalism. The incomplete character of the neoliberal program that was encouraged by Western governments and international financial institutions in the 1990s resulted in selective liberalisation and allowed for the tightening of state-business relations. The implementation of the liberal economic agenda facilitated the takeover of state resources and privileged access to the domestic market by dominant political-economic coalitions and produced a novel regime whereby hopes of a plural political system and a de-regulated free market were replaced with a version of Arab 'crony capitalism'. The evolvement of this phenomenon is analysed and explained by appealing to the example of economic reforms that took place in Egypt and Tunisia, two countries which, between the 1990s and 2010s, were hailed as success stories of the neoliberal reforms in the Arab World. Although the façade of the countries' respective economies became apparent as de-regulated, new reforms became a powerful instrument for the foundation of a novel network of preferential beneficiaries leading to the reshuffling of alliances among the country's major players. The overarching argument of this paper is that liberalisation efforts in Egypt in Tunisia, rather than eradicating distributional coalitions, have merely rearranged them by reshuffling the existing alliance among the countries' major players.

Keywords: Neoliberal Reform, Economic Liberalization, Crony Capitalism, International Monetary Fund

1. Introduction

To achieve economic growth through reforms, North outlines a number of necessary preconditions: 'impartial system of laws and courts for the enforcement of formal rules, the 'correct' societal sanctions to enforce norms of behaviour, and strong normative personal standards of honesty and integrity to support self-imposed standards of behaviour' [29]. These are problematic, as none are typical features of economic procedures in the Arab world. Their absence provides some explanatory power as to why economic liberalisation encouraged by Western governments and international financial institutions in North Africa and the Middle East (MENA) have brought suboptimal results, creating a ripe climate for crony capitalism. The incomplete character of economic liberalisation, which Kadir terms as 'crony liberalism' [17] facilitated the takeover of state resources and privileged access to the domestic market by dominant political-economic coalitions. Neoliberal programs for development resulted in selective liberalisation and what Van der Walle called 'partial reform syndrome' allowing for the tightening of state-business relations and inevitable results: corruption and rent-seeking [43]. The implementation of the liberal economic agenda produced a novel economic regime whereby hopes of a plural political system and a de-regulated free market, was replaced with a version of Arab 'crony capitalism'. Owen claims, that under such conditions 'competition was stifled and entrepreneurs with close connections to the regime were able to obtain most of the major contracts' [32]. This paper will argue that liberalisation efforts, rather than eradicating distributional coalitions, have simply rearranged them. Structural readjustment facilitated the restructuring of a society where a small fraction of the population owns the lion's share of resources at the expense of the wider sufferance of the masses. How this happened will be analysed in detail on the examples of Egypt and Tunisia.

2. The Liberal Economic Model: Historical Context

Lipset's hypothesis that 'the more well-to-do a nation, the greater the chances that it will sustain democracy' [22] focused attention on the nexus between reform and democratic transition, which became an underpinning element of modernization theory. Refuting Marxist analyses of political change, it holds that economic growth is positively correlated with socio-political change. Although some debunk the theory's universalist trajectory, a form of this thinking re-emerged after the Cold War and the ideological triumph of capitalism [30]. Modernization theory suitably coincided with the post-Cold War era's renewed aspiration to reshape the world in accordance with Western principles, a development which some, such as Said described as binary oppositions rooted in the Orientalist paradigm- the West versus the Orient, democracy versus non-democracy or traditionalism versus modernity [37]. The significantly influenced Western policymaking as the intellectual roots of the 'one-size-fits-all' perspective. This logic was reflected in the formulation of what Williamson termed the Washington Consensus - the general agreement reached by institutions such as the World Bank, the International Monetary Fund (IMF) and the U.S. Department of the Treasury on a set of ten reforms that should be endorsed in developing countries to stimulate economic growth [46; 47]. Among the prescriptions was the adherence to fiscal discipline, the reordering of public expenditure priorities, liberalisation of policies on trade, interest rates and finance, privatisation [12].

Thus, the general shift away from the ISI redistributive and interventionist model in favour of a liberal economic model, which began during the 1970s and 1980s was reflected in the MENA region. Although during the post-independence period, the Arab states saw populist and socialist-oriented programs an easy answer to enduring developmental difficulties, the same very schemes proved to be a doubled-edged sword- although they produced substantial results, they proved unsustainable in the longer run [21]. It was against the backdrop of the collapse of the Soviet Union, stagnant economic growth rates and the inability of state-led Import Substituting Industrialisation (ISI) schemes to accumulate sufficient capital for investment, that this Consensus started to gain ground [44]. However, as correctly argued by Rodrik: 'function does not translate into form', meaning there is no one set of policies that could be implemented universally to stimulate economic prosperity in all countries [35]. Unsurprisingly, having followed these 'single cut' structural adjustment policies, the MENA region experienced rising corruption. According to King this shift towards market liberalisation prompted the shift in MENA'S ruling coalitions [21]. To successfully govern, regimes historically sought to establish a network of corresponding interests represented by their coalition allies [40]. As held by Waterbury in the Arab Republics ancient regime, such coalitions typically represented the interests of the military, the public sector as well as the peasants and organised labour [45]. In a process which was particularly prominent during the 1990s, the ruling populist coalitions were superseded by alliances which, although still heavily reliant on the military, realigned their coalitions towards regime sympathisers in the export sectors, commercial agriculture and elite state agents who had used privatized state assets to move into the private sector usually with the benefit of [45]. The intersection between business elites and government personnel was a by-product of economic liberalisation, which encouraged rent-seeking and patronage, and thus, crony capitalism, a development, seen clearly in the examples of Egypt and Tunisia.

3. The Growth of Crony Capitalism in Egypt

In Egypt, crony capitalism grew 'in the shadow of economic liberalization' [10]. Although Nasser's presidency is mostly associated with his socialism, the General commenced a modest liberalisation of the Egyptian economy prior to his death in 1970. It was his presidential successor, Anwar Sadat, who stimulated market reform with what became popularised as assertive 'de-Nasserisation' [4]. Sadat's policy of economic opening named after the Arabic word Infitah was launched in hopes of reinstating diplomatic relations with former colonial powers as well as the United States, and strengthening the position of Egypt's local capitalists, the commercial elite and landowners. Sadat aimed to reverse Nasser's restrictions on the role of private capital in the local economy, and thus the Infitah policy became his tool to reinstate and reinvigorate Egyptian private business- 'the internal introduction of capitalist economic norms' [15]. The private sector's stimulation generated strong interests with a stake in the Egyptian regime. Already by the end of the 1970s, Sadat replaced the 'state bourgeoisie', which characterised the Nasser era and remodeled them into a 'private property owning bourgeoise' with particular access to state assets, which in the words of Hinnebusch created 'a growing web of marriage, political and business alliances' [15] and created a climate ripe for 'cronyism and corruption' [2]. Thus, the sudden swelling of prominent consumption at the top reinforced the impression that class gaps were expanding, as the rich got richer, and the poor poorer.

Whereas Sadat's initial Open-Door policy led to the consolidation of an alliance between the government and a handful of domestic businessmen, Skafianakis maintains that it is only under his successor, Hosni Mubarak, that cronyism achieved its final form [39]. This argument is in line with that of King who localises the surge in crony capitalism to Mubarak's political opening in 1984, which was followed by a wave of politicised privatisation policies (which benefited the economic elites), modifications in political institution policies, reshuffling of ruling coalitions and legitimacy strategies [21]. Chekir and Diwan reflect on this period in Egyptian history: 'during 1990s a larger new class of capitalists connected to the state grew very rich' [6]. Property was privatised at a frenetic pace, a development which Momani called a 'bold and aggressive privatisation plan' as it aimed to sell 'one public company per week', which according to the scholar was done to astound the IMF [26]. As soon as the early 2000s, Egypt's economic elite expanded further. Armbrust reflects that 'in Mubarak's Egypt business and government were so intertwined that it was difficult for an outside observer to tease them apart' [3]. However, Henry and Springborg highlight as particularly illustrative how the surge of connected firms in the economy during the late 1990s directly corresponds to the increase in the political power of President's son- Gamal MubaraK [41]. Gamal's expanding political capital quickened the pace of trade and financial reforms [31]. Regardless of this wide umbrella of economic liberalisation reforms, the regime instituted barriers to entry for others, as governments permission became the golden ticket to benefit from developments. Diwan, Keefer and Schiffbauer provide examples of this: new banks and new business in energy-intensive manufacturing sectors, such as cement or steel, necessitated special government licenses; housing projects and tourist resorts were built on lands previously owned by the government; capital investments in gas and oil demanded the regime's consent; other selected import products necessitate special licenses; and other non-tariff barriers were implemented to insulate domestic producers (all member of the economic elite) from competition [18]. In fact, Eibl and Malik conduct an exhaustive study on the impact of Egypt's trade liberalisation on trade tariffs in the aftermath of the 2004 EU-Egypt Association Agreement, which established a free-trade area between the two [11]. Whereas the scholars found that this agreement 'reduced Egypt's number of tariff bands to twelve', they have also noted a 'major upward shift of non-tariff measures', which became the prevailing practice of trade protectionism [11]. As a result of these maneuvers, Schlumberger records that from 1990 to 2000, the share of exports as a percentage of GDP 'decreased from 31% to 18.6% and from 40.6 to 24.8% respectively' [38]. Meanwhile, Diwan et al. conducted a study, which provides evidence that the vast majority of all energy subsidies in 2010, which accounted for 24.9 per cent of total energy subsidies or $7.4 billion were directed to politically connected firms in heavy industries [10]. Together, this evidence suggests that politically connected manufacturing firms majorly benefited from trade protection and subsidies at the expense of the broader disadvantaged Egyptian population.

The power of Egypt's cronyism was not limited to the economic sphere, as under Mubarak, they increasingly infiltrated significant governmental positions as well as instrumental committees and boards, which concluded with the founding of the Nazif Cabinet in 2004 within the National Democratic Party (NDP). Infiltrated by leading Egyptian businessman, it was here that cronyism thrived until the outbreak of the Arab Spring in 2011 [6; 23]. The NDP metamorphosed from a populist party to one that serves Egypt's entrepreneurial elites- a shift, which had begun under Sadat [21]. The outcome of the intersection between political and economic power is well illustrated by the second phase of privatisation in 2004, directed by a 'dream team' of main Egyptian businessmen. The regime and its party, the NDP launched their crusade to liquidate the state sector- as noted by Cook, between 1991 and 2003, private businesses acquired 210 public firms, and in the five years following the creation of the Nazif Cabinet, 191 companies were privatized [8]. The NDP assisted with commercial contracts, hindered legal inspections and built a complex arrangement with Egypt's security agencies, police and the army, which was often ordered to contain those who resisted Mubarak's crony capitalist order. The Egyptian military performed a critical role in the regime's corrupted practices, camouflaged under the name of liberalisation, as generals and officers concluded deals with the private business. In this accommodating political climate, it is unsurprising that the military has concluded, what Springbord called a 'horizontal expansion' into a broad spectrum of business activities [14]. Although the military is known to 'manufacture everything from olive oil to shoe polish to the voting booths used in Egypt's 2011 parliamentary elections the complete valuation of its share of the Egyptian economy is unknown [25]. However conservative estimates put it anywhere between 15 and 40 per cent [36]. This fact has led Hashim to label it a military-industrial-business-commercial complex (MIBCC), which 'steps into every corner of Egyptian society' [13]. It is important to note that prior to the Arab Revolts in 2011, the army entered a conflict with Mubarak as well as his son and their orbiting business associates. WikiLeaks from 2008 revealed the Egyptian Minister of Defense's staunch criticism of the proposed privatization schemes, as Gamal Mubarak's ambitions hungrily stretched towards military assets [1]. Hosni Mubarak's strategy of alliance-building backfired, as he failed to appease all the 'crony groups' he engaged with. Having miscalculated the real strength of the Egyptian army and disregarded their position in broader privatisation schemes, the military took advantage of the 2011 revolution to assert their influence without competition. Thus, Mubarak's own system turned on him, and without the army's protection, he was forced to step down after just 18 days of popular dissent.

4. The Growth of Crony Capitalism in Tunisia

Analogous practices of crony capitalism to those in Egypt were found in the Tunisian example as the rent-seeking alliance materialised shortly after President Ben Ali assumed office. President Habib Bourguiba was replaced in a bloodless coup that ended his 30-year rule in 1987 and in the years that followed the new political elite instituted a period of le Changement, French for 'Change', which became a tool for erecting a new distribution coalition. At this point, Tunisia had already undergone almost two decades of economic liberalisation, originally at a slower pace (1970-85), and increasingly sternly enforced post-1986. During the second wave of economic liberalisation policies, backed by an IMF-Structural Adjustment Program and World Bank as a response to economic stagnation, Tunisia was used as a North African model of economic efficiency and stability [28]. Although macro-economic estimates initially suggested growth, balancing at around 4-5% per annum [34] it was questioned whether referring to this improvement as an 'economic miracle' was appropriate in the long-term, considering the widespread youth unemployment, underfunded welfare system or unequal economic growth [27]. However, the 'miracle' rhetoric was so deeply ingrained, that several academics were 'puzzled by the mysterious timing' of the Arab Uprisings, which broke out in Tunisia [7]. With a widespread international consensus on Tunisia's successful liberalisation, how can one make a sound claim for the predominance of cronyism in the country? Khiari and Lamloum explain, that after years of structural adjustment, it was close to impossible to determine the social costs these reforms carried, as official data is either not credible or nonexistent [19].

In an effort to follow IMF's and World Bank's reform recommendations, in 1987 Ben Ali launched an aggressive privatization policy, which instantly spawned cronyism [24]. Having recruited like-minded technocrats into the Rassemblement Constitutionel Democratique (RCS) Party, which he led, Ben Ali almost instantly established a new elite distributional or rent-seeking coalition [33]. As in Egypt, marketization spawned new rents, a development, which also began with Ben Ali's family. The family of the President's wife (Leila) were the main beneficiary of privatisation deals together with 'other well-placed families' [20]. Within a very short period of time, the Ben-Ali-Trabelsi entourage accumulated a wide portfolio of companies, which cut through almost every sector of the economy. Their economic influence was built under crony capitalism and gained momentum after Ben Ali intensified his control over the political arena in 1992, dissolving all political opposition [16]. In a quantitative study, Rijers et al. examine 214 Tunisian firms owned by the Ben Ali clan that were expropriated after the Jasmin Revolution, which 'accounted for 5% of all private sector output and 16% of private sector profits' [34: 53]. The scholars find that firms in Ben Ali's business empire were 'associated with significant increases in exit and concentration rates in sectors subject to authorization and restriction on FDI'. The Ben Ali extended family extended to over 140 persons and those who lacked insider contracts or strong network connections with them suffered tremendously at the hands of the new regime's arrangement [34]. Other than marrying one of the members of the President's close circle, business 'outsiders' were left three alternatives: sell the business to the Ben Ali's economic empire, ally with them, or be subject to regime's pressure, intimidation and unjust competition until going bankrupt. These choices created a division within the capitalist class itself [16]. What's more, companies owned by the family lobbied for specific industrial policies that would further their gains. Cronyism grown from privatisation was not limited solely to public companies but also extended to public land. Upward distribution of land, which also took place under Sadat in Egypt, also occurred in Tunisia. The agrarian counter-reform had already begun by 1985, but flourished under Ben Ali, as the regime relocated over 600,000 hectares of Tunisia's most cultivable land to the rural elite [48]. On top of that, privatisation of land extended to over 2.7million of hectares of communal land, which had dramatic effects on the small peasantry that already suffered from unstable access to land and employment [20]. Thus, the resources collected from the privatisation of state-owned enterprises and land opened a window of opportunity for the regime to form 'a new ruling coalition of rent-seeking urban and rural economic elites' [20], which disregarded the broader Tunisian masses.

To protect the crony capitalist status quo the Tunisian political elite, comparable to that of Egypt, needed to form alliances with their country's security apparatuses. Unlike in Egypt, where Mubarak rewarded the army's support with lucrative business contracts, both Bourguiba and Ben Ali sidelined its Tunisian counterpart, instead of giving their backing to the security forces [16]. To safeguard the economic benefits in the form of foreign direct investment (which stimulated job creation), international aid and tourism (which financed over 80 per cent of Tunisia's deficit), Ben Ali had to preserve the country's profile as an 'economic miracle' and to signal stability [5]. Evidence of popular dissent would threaten that narrative, which could effectively reverse the rent-seeking coalitions Ben Ali formed over the years. Thus, in a country of 10 million people, the President had a wide network of informants, which worked with 80,000-133,000 police officers and 7,500 local branches of the RCD [42]. Together, this created a truly Foucauldian system of surveillance. However, as in Mubarak's case, this panopticon system of control extended over the entire country was not enough to prevent Ben Ali's fall from power during Arab Revolts.

5. Conclusion

Dillman's reflection that 'the more they 'deregulate'' the more they ''re-regulate'' [9] appears a well-suited description of the outcomes of liberal economic reforms in the discussed examples of Egypt and Tunisia. New reforms in the respective countries became a powerful instrument for the foundation of a novel network of preferential beneficiaries. Although the façade of their economies became apparent as de-regulated, as Egypt and Tunisia became the model success stories of neoliberal reform in the Arab World from the 1990s through 2010, political elites erected barriers to entry for other, who did not receive privileged access to state assets resulting from reshuffled alliances within the country's major players. Thus, whereas in Egypt the nadir of crony capitalism has been reached under the Nazif Cabinet in 2004 during the Presidential term of Hosni Mubarak, in Tunisia, it was Ben Ali's extended who launched a campaign to liquidate state assets. The scale of their crony capitalist activity, including 'land appropriation at below market prices, the manipulation of government regulation to stifle competition, subsidized borrowing from state banks or privileged access to subsidized energy' [9], was brought to the attention of the broader public during the trials of their leading businessman in the aftermath of the Arab Spring. Thus, the failures of structural readjustment to trigger economic growth can be explained by the economic order that has evolved out of these reforms. Egypt and Tunisia developed into capitalist, but not competition-rooted market systems, a possibly inevitable result of their rent-based economic histories as well as the fact that both Mubarak's and Ben Ali's regime prioritised their own agendas and successfully instrumentalised liberalisation reforms to carter benefits to themselves and those who surrounded them.

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