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## Executive Summary

- Food Marketing in Egypt is characterized by an important role of the public sector in food processing and distribution, which – if fully accessed – would cover about 65 - 70 % of the average calorie intake per person.
- A dichotomy between a free market food production and import system on one side and a government controlled processing and supply system of heavily subsidized foods on the hinders a free and efficient marketing for basic foods (wheat products, rice, vegetable oil, sugar). As a consequence, private households spend about 85% of their food budget for acquiring the remaining 30 - 35 % of food calories not covered by the public food distribution system (total per capita consumption 2990 kcal/person/day).
- Food subsidies are with 17% only a minor element in the overall government subsidy system. They are however relatively more important for the average household. The income transfer per household of the entire subsidy system is estimated to be about 85. - US\$/month, which is more than 50 % of average salaries. Competitive wages and consequently a low unemployment rate depend on the subsidy structure and any changes of the latter can only be done gradually and in line with economic development.
- The introduction of vulnerability targeting of the food subsidy and rationing system is not recommended. The lack of sufficient income data and a rather fragile public administration would make targeting technically and politically difficult. There exist several private and government cash subsidy systems to support the poor and vulnerable.
- The marketing of subsidized bread and bread-flour seems to be largely out of control. The fact that traditional bread cannot be legally produced and distributed outside the subsidy system has led to a wide discrepancy between legality and reality.
- The practice of the government food procurement agency (GASC) to compete with the private sector in the procurement for local wheat and rice is counterproductive and has lead to exaggerate price levels within the free food market. Since wheat production capacity in Egypt has already reached its economic limits, the intention of GASC to achieve greater “self sufficiency” through increased local procurement does not make sense.
- In order to create a competitive and unified food market, the entire procurement and distribution system should become privatized and the food subsidies should be paid to the final food outlets (shops and bakeries).
- Farm gate as well as market prices for local foods should not be linked to world market prices. Supply stability for wheat and rice depends on remunerative floor prices for these crops which must be in line with the profitability of competing crops. Therefore, government could guaranty floor prices and regulate imports when international prices are too low.
- WFP’s future role should focus on the following activities: nutrition support to children in poor families as well as support to government through its VAM-unit by providing data on household income and on the functioning of private markets.

## Foreword

The purpose of this study is to provide a basic understanding of the food supply and marketing system in Egypt for the UN-World Food Programme. The limited timeframe for this study of less than 4 weeks did not allow much genuine field research in order to solidify the often very controversial data found in various official documentations and studies, in particular with respect to overall food supplies and household incomes. Therefore, some conclusions and recommendations given in this report might not withstand further scrutiny, although all efforts were made to discuss the findings with as many persons knowledgeable on the subjects as possible. Of course, the limited number of household interviews, discussions with traders and visits to the food markets undertaken by the mission can not provide statistically solid results. They were however necessary to draw a more realistic picture of the extraordinary complexity of the Egyptian food marketing system.

The study was undertaken during a time of great economic uncertainty following the worldwide financial crisis. Recent food policy decisions and an increased coverage through the food subsidy system had been undertaken as a reaction to the soaring food prices during the last quarter of 2007 and the first quarter of 2008. Now, with the Egyptian economy possibly being negatively affected by the worldwide economic downturn, government revenues might no longer permit ever increasing subsidy payments benefiting every household. At the end of the mission, the Ministry of Social Security (MOSS) has, from November 1<sup>st</sup> 2008 onward, made additional changes to the food subsidy allocation system, which could alter some income-transfer data presented in this report.

# 1 Background

In order to understand the Food Marketing System in Egypt, first of all one should look closer at the historical, political and social background from which the present system has evolved. Any outsider taking a short glance at the extraordinarily complex and costly system of the state controlled food subsidy system is immediately tempted to apply the ruler of sound economic management and propose solutions. This however has been attempted for more than 30 years, with not too many good results.

The Egyptian system of controlling agricultural production as well as of the rationing and subsidy system for food has its roots in the food shortages caused by the Second World War. After the Revolution in 1952 it became an integral part of a state managed, socialist production and distribution system. A main justification for the food subsidy system then had been to provide public sector jobs at low wages to the large number of unemployed, many of whom were landless peasants.

The core elements of a state regulated food production and distribution system had been:

- Expropriation of rich landlords and redistribution of land without ownership titles
- State imposed cropping patterns, given preference to the production of export crops and for low cost urban food supplies within a state controlled pricing and distribution system.
- State control of production inputs, credits and purchases from the farmers.

This system since the mid-seventies has been gradually modified through the introduction of elements of a free marketing system, a process which is still ongoing. The most important milestones were:

- 1976 No longer compulsory delivery to government/cooperatives.
- 1977 Attempt to reduce bread subsidies met fierce public resistance with 800 persons killed during riots in Cairo.
  
- 1987 compulsory delivery of wheat to government reinstated.
  
- 1987 begin of market reforms, voluntary delivery to state, producer prices set before planting.
  
- 1991 Start of second phase of reforms: elimination of state subsidies for farm inputs, liberalization of production and marketing of ALL crops (principally cotton and rice), encouragement of private sector to trade.
  
- 1992/ private sector can produce, import and trade with “fine flour” (72%  
1993 wheat extraction rate), must however use for it imported wheat.
  
- 1992 Beginning of land reform and reform of payments for land rent. Return of land to previous owners and land titles reinstated. This process lasted until 2000.

Although the reforms brought near total freedom from state control for the producers, the marketing and distribution of a variety of basic food is still dominated by the government through its subsidy and ration card system. Consequently, a fully functional free marketing and food processing structure for basic food items could not yet develop. It is this dichotomy between a free market food production and a costly, inefficient and distorting state intervention in the processing and distribution of basic food items which causes free market foods to be expensive. High prices on private food markets thus make even middle income groups dependent on the food subsidy system.

It is very important to understand that the government food subsidies represent only a small portion of a much wider subsidy structure, covering cooking gas, liquid fuels, electricity, housing, water supply, free irrigation water etc. Much of the Egyptian economy revolves around a cheap workforce, a fact which only can be sustained by the large subsidies for all basic needs for the urban and rural working classes. Apart from the burden on the government budget (about a third of all budget expenditures used for subsidies), the subsidy structure hinders private investment in the production, trade and processing infrastructure. Sometimes, the private sector can only operate profitably by exploiting loopholes in the system. A widespread culture of “cheating the system” also provides additional incomes to a large number of public service workers. Many of them would lose their jobs after a privatization of their workplaces (e.g. public mills employ 4.5 times the required workforce).

It is therefore important to understand that the subsidy system represents a core feature of the entire economy and that removing one element of it can create a very dangerous domino effect, politically, socially and economically. There can only be a gradual reduction of subsidies in line with a continuous improvement of the income situation of an overwhelmingly poor population. Unfortunately, one logical solution for improving the subsidy system – better targeting - is not feasible out of two reasons: insufficient knowledge of incomes/living conditions and a fragile administrative structure. As will be explained further on, the introduction of targeting might also not be cost effective, considering that an estimated “inclusion error” of less than 20% is within tolerable limits.

## 2 Baseline Information

### 2.1 Economy, Budget and relevant Government Policies

For the last couple of years, the Egyptian economy has experienced solid growth between 6 - 8% annually, with increased revenues from oil exports, tourism, investments and transfers from Egyptians living abroad. Of particular importance had been the growth in the following sectors (January – March 2008 on one year basis):

- Tourism + 25 %
- Construction + 15 %
- Suez Canal revenues + 19 %
- Agriculture + 3.4 %

Remittances from Egyptians living abroad were 5.034 billion US\$ during the past fiscal year. The value of exports grew from 9 billion US\$ in 2003 to 24 billion US\$ in 2007. This solid economic growth has so far allowed the government to meet the costs of a growing import bill, although now the negative trade balances as well as the budget deficits are increasing in an alarming rate. A growing inflation rate, which in August 2008 has reached 23.6 %, is of particular concern. For food items, the inflation had even reached 29.9 % (on one-year basis).

**Table 1: Basic Economic Data<sup>1</sup>**

GDP (2008/09 estimates)	163 billion US\$ (= 2260.- US\$/capita)
Total Revenues 2007/2008	34,6 billion US\$
Total Expenditures 07/08	43.1 “ “
GDP growth 2007/08	7.2 %
GDP projected growth revised 2008/09	6 %
Inflation 07/08 (nominal)	22 %
Total Cost Subsidy Programme	10.6 billion US\$
Total Cost Food Subsidies	1,75 billion US\$

One of the main additional cost factors in 2007/08 were a reported 137 % increase of the cost of food imports for the food subsidy system as consequence of the soaring international foods prices from mid 2007 to mid 2008. Egypt traditionally imports about 40 - 50 % of its wheat requirements, nearly all of its vegetable oil needs and more than 50 % of its sugar requirements. There is very limited scope to increase local food production, in particular of wheat, due to the already fully stretched land and water resources. Also, the production of non-staple foods, like vegetables, fruits and pulses is becoming increasingly more lucrative for the farmers.

A considerable portion of the food imports are channeled into the vast food subsidy scheme of the government, which absorbs about 5 % - 6% of the revenues. Subsidies for bread and bread flour (= baladi, 82% extraction rate) amount to 75 % of all food subsidies. It is estimated that the subsidy system has the following shares in the total consumption of:

<sup>1</sup> Exchange rate for the Egyptian pound for 2008: 1 US\$ = 5.5 LE, for other years the appropriate average exchange rates have been used.

Wheat/wheat flour	50 %
Rice	46 %
Vegetable oil	77 %
Sugar	46%

With a share of only 17.4% within the budget allocated for the entire subsidy system, the food subsidies represent however a relatively small portion. By far the biggest share of the subsidy budget is absorbed by the subsidies for the energy sector (cooking gas, petrol, electricity). More details on the subsidy system are provided in a separate paragraph.

A particular feature of the Egyptian economy is the very low cost of labor, which has contributed to the solid growth of the service and manufacturing sectors and which is important for job creation as well as for labor migration. Unemployment – if one can believe official figures – is with 10.4% relatively modest compared with similar countries. The near universal subsidy system, which covers a very large portion of basic costs of living (food, energy, water, housing, medical expenses etc.) certainly has been an important factor for keeping labor costs as well as unemployment down.

## **2.2 Socio-Economic Information, Food Intake**

As with several other baseline information on Egypt, socio-economic data are very often contradictory. This report relies as much as possible on the data provided in the official statistical yearbook of December 2007 as well as on the World Bank Poverty Assessment update of 2007. Very valuable information is also contained in the recent report of the WFP-VAM unit (October 2008) and in the various reports of IFPRI, which however are to a large extent based on household information collected 11 years ago. Own household assessments carried out during the mission try to correct unrealistic assessments and provide core data on actual food intakes, both from the free markets as well as from the subsidy system. Since this paper's focus is on the functioning of food markets, vulnerability issues as well as problems of economic access are not discussed in detail. WFP's Vulnerability Assessments as well as the World Bank poverty reports provide more detail

As in most countries with a similar development structure, incomes in Egypt are unequally distributed, with the rich taking an over-proportionate share of the overall incomes. Although average wages are much higher (for the lucky ones enjoying regular employment), it is estimated that incomes in the lower 20% of income groups are US\$ 36. -/month and in addition 18. - US\$/month of transfers (through family members, the mosque or NGO).

Most likely as a remnant of socialist policies followed until 1977, government policy has continued to keep wages low and to compensate rising costs of living with an expanding system of state subsidies for nearly all basic needs. As an example, for a family (4-5 persons) with an income of 120. - to 150. - US\$/month in Cairo, housing expenses can be as low as 3.50 to 5. - US\$/month, with in addition electricity cost of 6.50 US\$, cost for water of 1. - US\$ and for cooking gas of 1.50 US\$, totaling US\$ 12.50 – 15 US\$/month.

As of November 1<sup>st</sup> 2008, 63 million persons will be registered in the food subsidy system. It is said that there is an exclusion error of 25 % for the least privileged, a fact which could not be confirmed by the mission. The subsidized food basket, in case all would have access and all of its ingredients would always be available (a big “if “!), would provide 2035 kcal/person/day for a cost of 11. - US\$/month for a family of 4. Total basic expenses for housing and food for a 4 person family therefore would be only 23.50 to 26. - US\$/month. Commodities of the food basket would have a free market value of 45. - to 48. - US\$ (at October 2008 prices).

The reality however is much different, since there are problems with registration as well as with the availability of the various items of the food basket. A particular problem now is the access to subsidized bread (baladi) which either is not available in sufficient quantities (in addition there are high opportunity costs for queuing!) or is of such bad quality that many people reject it. The largest share of a family’s food expenses is used for food items outside the subsidy system (including bread from the free market). Egyptians spend a considerable amount of their income on fresh vegetables and fruits as well on additional supplies of cooking oil and sugar. These additional food expenses can exceed 100. - US\$/month/family and are therefore much more important than the free market value of the subsidized food. It is estimated that the recent hike in food prices has increased household food expenditures by 24 %. Only the public sector salaries had been increased by 30% in May 2008, which for the average government worker however only has amounted to a net transfer of 10.- to 20.- US\$/month.

The very low wages, especially for unskilled workers, have been instrumental in the rapid growth of the service sectors, in particular in tourism. They are also attractive for investments in the manufacturing sector and contribute to the large number of Egyptians working outside the country. De facto, the state subsidizes wages through the subsidy system and in addition to that reduces unemployment by an inflated number of civil servants (3 million out of a total workforce of 23 million). Every reform effort therefore has to look at the impact on employment. A 10.4 % unemployment rate, as quoted in the most recent statistic, seems to be an underestimate, considering that a large number of the “employed” might only have very temporary or seasonal jobs.

The following baseline data are useful for understanding the socio-economic context with respect to access to food and food consumption:

**Table 2: Baseline Data**

Total Population (2008)	75.4 million
Population Growth Rate	2.05 %
Share of Urban Population	42.5 %
Household Size (Official Statistics 2008)	Urban: 3.9, Rural 4.4
Average Household size (WFP-VAM)	5.4
Workforce	23 million, including 6 million public sector workers
Unemployment	10.4 %
Average monthly wages :	Public Sector 194.- US\$ Private Sector 127.- US\$
Average per capita food intake <sup>2</sup>	2990 kcal/day

<sup>2</sup> Mission estimate!

## 2.3 Food Production

As it is well known, Egypt produces most of its food on irrigated land along the river Nile. Farms are tiny (most below one ha), with individual plots very fragmented and production is labor intensive. Consequently, mechanized agriculture is restricted. There is a rapid increase in newly reclaimed desert land, which now covers 15 % of the agricultural area. Plot sizes are larger in the new lands, with an upper limit set at 21 ha. Most of the production in the new lands however consists of vegetables for export. Access to these new lands has become near impossible for ordinary farmers, with land prices for non-developed land now averaging 2000. - US\$/ha.

Many farmers in the “old lands” are landless or have land holdings less 0.2 ha (some estimates quote 50%) and consequently depend on working on other farms or having incomes outside agriculture. During cultivation and harvesting, most farms employ temporary laborers.

There are two cropping seasons:

- Winter season, with wheat and berseem (Egyptian clover) being the main crops, together with vegetable and beans cultivation.
- Summer season, with rice, maize, vegetables and cotton predominant.

Due to the sharp rise in other sectors of the Egyptian economy, the share of agriculture in the overall GDP has proportionally been reduced to 16 % in 2007. It however still employs a quarter of the workforce, at least on seasonal basis, usually at low wages (e.g. below 3.-US\$/day). However, during peak planting or harvesting times in the Delta region, manpower can become scarce and wages can reach up to 4.50 US\$ per half-day shift.

Farmers are now entirely free to produce whatever they like. Irrigation water is provided free by the state. In order to save irrigation water, farmers are however (in theory!) required to observe quotas set for rice cultivation. Total rice cultivation should not exceed 500 000 ha, is in reality however much larger (725 000 ha according to statistical yearbook 2007 or 840 000 ha as per local sources in the Delta).

Cost of rice production is 865. - US\$/ha, if land has to be rented; renting land adds another 865.-US\$/ha to production costs.

Due to the tiny size of most farms, farmers are obliged to have diversified income sources, within and outside the agricultural sector. According to an IFPRI study (1997), farmers’ income sources are as follows:

• crop sales	30 %
• own consumption crops	25 %
• own cons. Animal products	9 %
• livestock	20 %
• agr. Wages	4 %
• other wages	12 %
• non-farm self employment	4 %
• transfer + remittances	4 %
• others	1 %

Therefore cash incomes represent 66 % of all incomes and the share of non-farm incomes is 25 %. According to the same study, 49 % of the labour demand of farms is hired, with labour cost representing 27% of farm expenses (9.5 % of revenue). Fertilizer costs are 23 % and machine hiring 20 % of the production costs.

Farmers are highly commercialised and consequently sell 50 – 70 % of the grain, in most cases immediately after the harvest in order to repay loans. The possibility to buy subsidized wheat flour, bread or rice at much lower cost compared with farm gate prices for wheat and rice, is certainly an incentive for reducing the self-consumption out of own production.

**Table 3: Agricultural Production in 2007<sup>3</sup>**

<b>Crop</b>	<b>Area planted (million ha)</b>	<b>Yields ton/ha</b>	<b>Total Production (million tons)</b>	<b>Share of total crop income (%)</b>
Wheat	1.39	5.80	8.1	18.7
Clover	0.97	--	--	11.6
Rice	0.75 <sup>4</sup>	7.5 (paddy) <sup>5</sup>	3.65 (milled)	15.3
Maize	0.71	6.50	4.60	7.88
Vegetables	0.50	-	-	12
Cotton	0.24	?	?	23.5
Sugar cane	0.15	8 <sup>6</sup>	1.2	?

## 2.4 Food Imports and Food Exports

More or less reliable data on food imports could only be found with respect to the import of wheat. (see table on page17). The main supplier of wheat during recent years has now become Russia with 40.5 %, followed by the USA (16.6 %), Australia (12.3 %), Argentina (12%) and France (9.8%).

With rapidly falling world market prices, private importers are at present (October 2008) reluctant to import wheat, in expectation of further falls. Some traders still have stocks of locally produced wheat, purchased at much higher prices when they had been hoping for further price increases. They are trying now to reduce market supplies in order to maintain a reasonably high price level until the old stocks are exhausted.

Egypt is self sufficient in rice and it is estimated that on average, 1 to 1.1 million tons of rice (net, corrected by rice imports) are exported each year. In April 2008, government has declared a one year export ban for rice in order to keep local prices low. For beans, the 2007 import figure shows 250 382 tons and for maize (for animal feed!) imports are close to 6 million tons annually.

Sugar production is declining in Egypt. Previously, the country had been about 50% self sufficient in sugar. Since sugar is imported in various stages of processing, it had been difficult to estimate an even approximate amount (based on refined sugar equivalents) from import sources. Import figures for sugar for 2007 show 455 426

<sup>3</sup> Calculations based on statistical yearbook 2007 and on IFPRI 1997

<sup>4</sup> Local sources quote 840 000 ha, which is double the allowed area

<sup>5</sup> Official statistic figure, FAO quotes a rice yield for 2008 of 10.2 tons/ha

<sup>6</sup> as sugar

tons (equal 5 kg/person/year!), which seems too little. Based on actual per capita sugar consumption, the sugar imports should be around 1.5 million tons/year.

All the vegetable oil destined for the subsidy system is imported by one public company, Multi Trade, which imports various not yet refined varieties of vegetable oil from the world market and reprocesses it into finished consumer products. There are numerous other importers, which import vegetable oil either in bulk or as packed products.

There is only a small production of vegetable oil from national oil seeds. The total volume of vegetable oil imported into Egypt, as per statistics, is 1.29 million tons (= 17.2 kg/person/year) which seems to be a reasonable figure.

### 3 Food Consumption and Expenditures

Per capita food consumption is considered to be very high in Egypt. FAO statistics for 2008 show an average per capita food intake of 3320 Kcal/person/day, and a FAO publication of 2006, quoting the food balance sheet of the Ministry of Agriculture, reaches the astronomical figure of 4423 kcal/day. A FAO-ESA working sheet of 2007 quotes daily food intakes of 1979 kcal/person/day to 2506 kcal/person/day depending on various urban and rural income levels. Food intake in the early seventies is said to have been 2363 kcal/day and the FAO minimum requirement for Egypt is 1840 kcal/day.

This is of course very confusing. Therefore, in this paper an attempt has been made to cross-check availabilities with information gained through household interviews. Seed use, losses and milling rates for local cereals have been included, although there is not much information about feed use of wheat (in particular the use of baladi bread as animal food).

Local production of wheat is about 8 million tons and 6 million tons of wheat is now imported. The mission estimates that a wheat equivalent of about 100 000 tons is re-exported as wheat flour. By deducting 15 % for seed use and impurities for local wheat and assuming an average milling rate of 79 %, the per capita food intake from wheat is about 132.5 kg wheat flour/year equivalent to 1270 kcal/day. Rice availability is about 2.65 million tons<sup>7</sup>, with about 1 million tons of exports deducted. This results in domestic rice consumption of 35 kg/person/year or 340 kcal/day. In addition, 1.5 million tons of maize is used for human consumption, which provides additional 170 kcal/day. Therefore, total intake from cereals is about **1780 kcal/person/day**.

Egyptians consume a very high amount of sugar (estimated 400 kcal/day/person) and vegetable oil (estimated 400 kcal/day). Meat consumption as well as consumption of vegetables and fruits adds 100 kcal and 150 kcal/day respectively. A further allowance of 150 kcal/day is made for other foods like pulses, nuts etc. Therefore, the average calorie intake per person in Egypt is estimated to be about **2990 kcal/person/day**, which might be considered a high figure compared with the low income levels and high prices for non-subsidized foods. Cereal consumption represents about 60 % of total calorie intake, which is in line with consumption patterns in many similar countries with similar conditions.

**Table 4: Household Food Consumption**

Commodity	g per day	Kcal per day	% of total
Bread (20% moisture)	360	1270	42.5
Rice	96	340	11.4
Sugar	100	385	12.9
Vegetable oil	50	425	14.2
Meat/fish	50	100	3.3
Vegetables	500	150	5.0
maize	50	170	5.7
others	---	150	5.0
<b>Total</b>	---	<b>2990</b>	100

<sup>7</sup> official statistics figure had been used. In case average paddy yields would be 10.2 tons/ha, per capita rice consumption is about 53 kg/person/year or 510 kcal/day.

As it is common, households exaggerate food intakes and expenditures during interviews by often a wide margin, leaving considerable discrepancies between declared incomes and expenditures. There is a need to conduct further measurements of actual household food intakes in order to have a reality check of the – possibly exaggerated - household consumption patterns. Likewise, some production/supply figures seem to be on the high side too (in particular for wheat, whereas official rice production figures are much lower than information gathered by the mission in the delta).

Provided that the official rations introduced since May 2008 could in fact have been accessed, a family of 4 persons<sup>8</sup> would have had to spend 36.6 L.E. = 6.65 US\$/month on subsidized rice, sugar and vegetable oil. For baladi bread (consumption 4 loafs/day/person) a further 24. - LE or 4.36 US\$/month would have been spent. The rationed food items (rice, sugar, oil) provide about 915 kcal/person/day plus 1120 kcal/day from baladi bread (4 loafs a 100g). Therefore, subsidized commodities can provide **2035 kcal/day/person** for a monthly food expenditure of **US \$ 11. -** of a 4-person household.

Since the subsidy level is on average 74%, the income transfer to this household through the subsidy system is about **US\$ 34.80 month**. Even poor households however spend in addition about 500. - LE/month (**US\$ 91.-**) on additional foods, with vegetables, additional sugar and higher quality bread the main expenditure items. Meat is eaten rarely, mostly only twice per week at a cost of about LE 150.-/month (US\$ 27.-).

Expenses for housing, cooking gas, electricity and water consume another 70. - - 80. - L.E. per month (= **US\$ 13.50/month**). Consequently, an average household in the poorer population group (lowest two quintiles) spends around **115.50 US\$/months** on basic needs, out of which 79% are for food expenses outside the subsidy system. The total value of government subsidies (food + non-food) to this household are estimated to be in the range of 85. - **US\$/month**. These expenditures for basic needs have to be compared with the following average monthly wages according to the statistical yearbook of 2007:

*Agricultural Sector:*

- Public sector 267.- US\$
- Private sector 79.- US\$

*Manufacturing Sector:*

- Public sector 179.- US\$
- Private sector 111.- US\$

*Construction sector:* 172. - US\$

The extraordinary high share of food expenses within the family budget has been confirmed during all household interviews. The subsidy system can guarantee

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<sup>8</sup> Ration cards often cover more persons than are actually living in a household, since children born after 1989 are listed on the card of the parents

minimum food calories even to the poorest income groups (quoted to be US\$ 54.-/month/family), in case all would have full access to it. The average wage earner spends about 6 times more on food from the free market than on subsidized food. In reality, since not all subsidized food is available and since there are high opportunity costs (e.g. 1 – 2 hours queuing for bread) for obtaining it, a large number of households cannot collect all officially allocated commodities from the subsidy system. The majority of households interviewed by the mission have bought baladi bread on the open market at 2 to 5 times the official price. It should be mentioned that this baladi bread officially should not exist, since no free market in bread flour (82% extraction) is permitted.

The high costs of food on the free market in urban areas are therefore of particular concern to the average consumers. Many prices for vegetables, meat, milk, beans are nearly at the level of prices in Western Europe. Some example of market prices (October 2008) are given below:

➤ Wheat flour	0.72 US\$ /kg
➤ Rice	0.70 “ “
➤ Vegetable oil	1.82 “/liter
➤ Sugar	0.50 “/kg
➤ Lentils	2.55 “/ “
➤ Meat	5.00 to 7.50 US\$/kg
➤ Milk	0.90 US\$/liter
➤ Vegetables/fruits	0.75 US\$/kg

Better functioning and integrated food markets certainly would help to reduce the extraordinary high food bills for the lower and middle class income earners and would make it easier for government to gradually phase out the food subsidies. The above calculations also show that government subsidies add about 60 % to the average salaries. If they would be completely phased out, Egypt would lose much of its competitiveness in the manufacturing and tourism sectors, in particular during the present time of a world wide recession.

## **4 Food Markets and Processing**

The following paragraphs describe mainly the trade in cereals, since these are the most important locally produced staples. For the trade in the other commodities, not much supply and trading data could be collected during the short time of the study (26 days).

### **4.1 The Wheat Sector**

Bread being by far the most important and also politically most sensitive food item in Egypt, it is not astonishing that the trade in wheat and wheat flour as well as bread making has made the least progress in the transition from a state controlled, socialist food market into a free market economy. There had been no lack of trying, but the political costs and the impact on the overall economy proved to be too high to undertake more than gradual changes. More than 70% of all funding for the food subsidies covers the subsidies for bread and bread flour.

Wheat production has increased steadily through an expansion of planted areas, at the expense of berseem (Egyptian clover) production, which is the second most important winter crop. With yields between 4.5 to 7 tons/ha, there is – considering the high costs of inputs and rudimentary use of technology - not much room left for expanding production beyond the present 8 million tons. There are other crops, which are better suited for the tiny plots of a predominant “garden agriculture” and which make better use of manpower as well as of the limited land and water resources.

Government policy, which tries to increase local production further by promising higher than world-market prices, is ill advised. It will shift wheat marketing only away from the private sector and pushes prices further up. Apart from that, it will be difficult to predict world market prices at planting time in October for a harvest in April the following year. Nevertheless, government still plans to pronounce itself each October on the minimum purchase price of local wheat. A committee representing 4 ministries will revise purchasing prices in regular intervals.

With growing demand and limited local supplies, there will be a continuing need for large wheat imports. At present, close to 6 million tons of wheat are imported annually, with the largest share of imports used for the subsidy system for bread and wheat flour. GASC (General Agency for the Supply of Commodities) is the government agency in charge of imports. GASC issues tenders to the local trade, which then makes its offers. The winners are a mix of large importers (e.g. Cargill Egypt) and smaller trading companies. Latter pool their import needs to profit from better prices and lower shipping costs. GASC offers a credit line to the traders. Deals of the smaller traders take place on confidence basis without bank involvement. Shipments of the smaller traders are done CIF Alexandria. Costs after CIF between Alexandria and Cairo are about 7.30 US\$/ton.

**Table 5: Import Statistic for Wheat by WORLD TRADE**

<b>Period</b>	<b>Average cost fob US\$)</b>	<b>Net Weight MT</b>
2004	----	4,366,841
2005	162.-	5,687,760
2006	166.-	5,816,910
2007	263.-	5,911,036

There are no longer restrictions on private import of wheat. However, privately imported wheat can only be used for the production of “fino flour” (72% extraction rate). Likewise, locally produced wheat purchased by private traders and sold as flour in the open market equally can only be milled into “fino flour”. Theoretically, there can be no traditional baladi bread (which uses flour with 82% extraction rate) on the open market. Anyone who wants to bake own baladi, has to buy wheat grain and have it milled in the small artisan mills to be found in many places. Since probably most of the baladi bread consumed in Egypt is supplied by private bakeries, the source of their bread flour therefore remains a mystery.

#### **The Wheat Mills**

Government purchased wheat is predominantly milled in one of the many public mills (about 131) which have a daily capacity of 22 000 tons. These mills are operated by two publicly owned holding companies: HCRWM (Holding Company for Rice and Wheat Mills) and FIHC (Food Industry Holding Company). These public mills supply most of the flour used for the baking of subsidized bread, although in some governorates, where they are no public mills, private mills are contracted to produce baladi flour.

Private mills are supposed to produce only “fino flour” (72% extraction rate) for the open market. Some public mills also produce “fino” flour and thus compete with the private sector.

Most of the public mills are of very old design, with some of them being stone mills. Private mills in contrast are modern roller mills. Public mills, it is said, employ about 4.5-times the required work force, and therefore have to be considered highly uneconomical. Milling losses too should be considerable. GASC pays about 14.50 US\$ US\$/ton for milling, whilst the private sector has milling costs of only about 9. - US\$/ton. Subsidized wheat is sold to the mills by GASC at a price of US\$ 131.-/ton. The average cost to GASC for imported wheat was about 265. - US\$ f.o.b. in 2007 (166. - US\$/ton during 2006). For local wheat, GASC has paid up to 497. - US\$/ton in 2008.

Baladi flour is then sold to bakeries (the majority of them being public ones) at a price of 85. - US\$/ton, whereas the price for subsidized wheat flour ex-warehouse (for distribution in rural areas with not enough bakeries) is 147. - US\$/ton.

There are several thousand small private mills – most of them in rural areas – which mill baladi flour or integral flour (98% milling rate) for home-baking. The milling costs are very low with US\$ 7.30 per ton milled flour. Clients have to bring their own wheat to these mills and take back the bran. Baladi wheat flour is not supposed to be on sale in the markets. It seems that there are considerable leakages at the public mills

and with the bakeries. The government now intends to separate baking of subsidized bread from distribution, and for that purpose will set up a separate publicly owned shareholder company (El – Masreen) to distribute baladi bread.

Wheat bran is sold by the public mills at a price of 218. - US\$/ton (ergo is much more valuable than subsidized flour!) and it can only be bought by registered animal breeders on a quota basis. Free market bran sells at US\$ 245.-/ton. Processed animal feed cost even much more: 575. - US\$/ton. With the cereal equivalent of baladi bread costing only 125. - US\$/ton (or 22% of animal feed prices), one can easily imagine that a considerable share of the bread production is not used for human consumption.

Government policy is to have 5 months of wheat consumption as strategic reserve stocks as a buffer against disruptions of imports or sudden price changes. However, due to lack of storage, imports in the pipeline are now included in these stocks.

## **4.2 The Rice Sector**

Egypt is self sufficient in rice and exports about 700 000 to one million tons of rice per year. Most of the rice is purchased by local traders and sold to private mills. Different wholesale-traders then collect the rice from the mills and sell it in their localities to retailers or directly to clients. GASC also purchases rice from these mills and channels it to the subsidy scheme, which until recently had absorbed 46 % of the locally consumed rice and which from November 2008 onward should supply the reduced amount of about 1 million ton/year of or 40 % of national needs.

Rice prices in Egypt are linked to world market prices due to the important rice exports. In October 2008 fob prices in Alexandria have decreased to 364. - US\$/ton. Retail price however is still high, with 472. - US\$/ton (7 % broken in 10 kg bags). Many traders are still holding stocks purchased at much higher prices in expectation of further price increases. They are therefore reluctant to make losses and artificially restrict supplies.

The milling of rice is performed by large rice mills producing for export and by many smaller, private mills for locally consumed rice. Public rice mills are estimated to have a share of 30 % in the milling of local rice for GASC, which also procures rice from the private mills through a tendering system.

## **4.3 Other Foods**

There was not sufficiently information available to the mission to produce reliable data on the supply and usage of the other important food items: Sugar, vegetable oil and pulses. 2007 import statistics show sugar imports of 455 426 tons (certainly too low!) and vegetable oil imports of 1 290 000 tons. A per capita calorie intake of 400 kcal/day of vegetable oil would require imports of 1.1 million tons of vegetable oil. GASC plans, from November 1<sup>st</sup> 2008 onward, to distribute 882 000 tons of vegetable oil or 68 % of national needs.

The national demand for sugar, based on 400 kcal/person/day would be 2 750 000 tons of sugar. The public distribution system distributes 1 260 000 tons of sugar or 46% of national needs.

Supply figures for Egypt are also distorted by the fact that there is a considerable export of processed food products to other Arab countries, in particular to the Gulf region.

#### 4.4 The Private Trade in Food

Food marketing in Egypt is characterized by a large number of wholesalers and retailers operating mostly at local levels. Government officials and economic research institutes interviewed by the mission mentioned the existence of monopolistic structures for food imports, however without providing much evidence.

For locally produced foods outside the subsidy system, the private trade can best be described as fragmented, disconnected and inefficient. One important reason for that is the still important role of the government in the food distribution system, in particular the subsidy system. Although farmers are now totally free to sell their products to anyone, the private trade finds it often difficult to compete with public enterprises and “Holding Companies” (in essence disguised former state enterprises). As already mentioned, the government procurement and food distribution systems in theory can cover up to 70% of the food intake of Egyptians.

Since basic food supplies of the population are to a large extent provided by the government subsidy system, the private trade has to content itself with the “surplus demand”. The inelasticity of the demand in basic food also allows traders to increase prices when they see an opportunity (e.g. an increase of government salaries).

At local level, a large number of small traders seem to be competing with each other. However, there is a great uniformity of prices at the same locality, with important seasonal and non-seasonal price fluctuations occurring in harmony between the various trade outlets. Seasonal price spreads are 18 – 25 % in urban markets and 15 – 19 % in rural markets. Between January 2007 and January 2008, food prices have increased by 16.2 % as against 11.5% of overall price increases. Paradoxically, food price increases were higher in rural areas (18.9%) than in towns.

Whereas up to May 2007 food prices followed closely – or were even below – the overall inflation rate, there had been a sharp increase for wheat products, rice, vegetable oil and pulses thereafter (see tables in the ANNEX). For April 2008 (the latest available data) the increases were as follows:

Wheat Flour	+ 112 %
Rice	+ 53 %
Sunflower Oil	+ 77 %
Beans (domestic)	+ 79 %
Lentils (imported)	+ 88 %

These price increases are in line with similar increases in world market prices, because – with the exception of rice – a large percentage of the consumption needs of above commodities are imported. Since up to 30 % of the local rice production is exported, the higher export prices influenced local market prices. The sharp increase in prices for local cereals – last not least caused by an increased competition by GASC for the procurement of local wheat and rice – also has prompted traders to build up stocks in expectation of further price rises. They now want to dispose first of these expensive stocks by holding back supplies and imports. This is the main reason why local market prices for the above commodities did not yet follow the present downward trend in international prices.

Prices for meat as well as fish remained stable, with the exception of chicken prices, which had increased by 17.5 due to an outbreak of avian flu. Prices for vegetables and

fruits followed the usual seasonal patterns, with increases on yearly basis remaining below the inflation rate. The supply of vegetables, but in particular that of pulses, also depends on their relative profitability of production. With the profitability of wheat and rice production most likely to decrease during the 2008/2009 season, farmers are now planting more beans and vegetables. This could reduce their market prices.

The increase of the commodity basket for subsidized food as well as the additional beneficiary registration has effectively shielded poor households from the impact of rising international food prices, since only relatively small additional quantities of wheat flour, rice and vegetable oil had to be procured from the private market. As already mentioned, the bulk of private market food purchases consists of vegetables, fruits and meat products, for which the price increases had been minimal.

Trades volumes per trader are usually small (e.g. for rice or wheat flour 200 - 300 tons/year) and there is little capital for keeping stocks for a longer period, although – as mentioned - the recent soar in food prices might have tempted many traders to keep larger stocks in expectation of further price rises.

Regional markets are seen to be disconnected, since traders usually trade only within their locality. Most of them possess no own transport and have limited storage space. For goods coming from outside their region, traders have established supply sources which they usually keep over many years (e.g. rice mills in the Delta).

Transport and storage costs are very low, with labor costs the most important element. Compared with these low operational expenses for marketing, profit margins (e.g. 30 % for rice) appear to be high. Although traders are considered to be “rich” by the local population, this wealth is not visible in the modest structure of their trade outlets and their life-styles. The small volume of their trade does not allow them to make larger investments, which at the end could lead to more efficient trading structures and competition within wider areas. The oddities and corruption in the government subsidy system, in particular in the trade of wheat flour and bread, also allow some traders to make profits in deviating commodities from the public supply system into the private trade.

## 5 Role and Impact of the Food Subsidy System on Beneficiaries and Markets

The rapidly rising international food prices between mid 2007 and mid 2008 have sparked off a heated discussion about the further sustainability of the food subsidy system in Egypt. In the meantime (October 2008) international food prices are falling rapidly towards the long term averages, whilst another shock for the Egyptian economy is about to happen: the impact of the world wide financial crisis combined with a global economic downturn.

First a look at some baseline figures, which will help to see the entire complex from a less emotional platform: During the 2007/2008 financial year (July to June), Egypt spent about 6.5 % of its budget on food subsidies. Until the reforms in 1987, the expenditures for food subsidies always had been above 10% of the budget. Total expenditures on subsidies are now about 10.6 billion US\$ (nearly a third of the budget), out of which 83 % are for non-food subsidies; the subsidies for petroleum products and electricity contributing the lion share. As an example, the government subsidies for cooking gas exceed the ones for food subsidies by 72 %! Since food subsidies make up about a third of the total subsidies benefiting individual consumers, they are relatively more important to the average citizen than to the state budget. It also must be considered that all subsidies together add about 60 % or US\$ 85.- to the average individual incomes, which has very large repercussions on the purchasing power for food and non-food consumer goods and – by keeping wages very low -for attracting foreign investments in the manufacturing and servicing sectors. Subsidies are therefore an important element of the entire economic structure of Egypt and therefore cannot be dealt with on a piece-meal basis.

The share of the individual subsidized commodities within the overall cost for food subsidies is as follows<sup>9</sup>:

- Wheat and wheat products: 75.0 %
- Vegetable oil 10.5 %
- Sugar 10.0 %
- Rice 4.5 %

Development agencies usually complain about the insufficient targeting of the subsidies to the poor and the over-proportionate share of the wealthier population group in it. However, the subsidy system never had been intended to be targeted to anyone and its structure is not designed for such a task. Apart from that, insufficient information on actual incomes and consumption is presently available to attempt a “poverty targeting” which would be politically acceptable. Apart from that, considering the very low salaries of the vast majority of Egyptians, the “inclusion error” of the present system is probably not much above 20%, which has to be considered as satisfactory for even more sophisticated targeting systems. This said, there is of course ample scope for reducing waste and misuse.

The origins of the present subsidy system can be found in the food rationing system after World War II as well as in the socialist period (1952 – 1976), during which the state provided public sector jobs to many of the unemployed and landless. Extremely low wages or salaries were compensated by subsidizing nearly all basic needs.

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<sup>9</sup> Cost of tea subsidy is with 91 000.- US\$/year negligible

Over several decades many attempts to reform the subsidy system have been made. In January 1977, the attempt to abolish bread subsidies, led to a revolt which left 800 people dead in Cairo. It is therefore not without reason that the government regularly declares that bread subsidies will not be touched in the foreseeable future.

### 5.1 Components of the Subsidy System

Food subsidies are provided in complex and often not sufficiently transparent ways at various points of the food supply and distribution chain:

- Subsidies of food imports
- Premiums for locally procured cereals
- Subsidies to milling of wheat
- Subsidies to bread making
- Maintenance of large and unproductive public enterprises in the distribution chain.

Consumers profit from two levels of the food subsidy system:

- Supply of baladi bread (or of baladi flour in some rural areas), which theoretically is not rationed
- The ration card system supplying rice, sugar, vegetable oil and tea

Registration for the ration card system had been halted in 1989. However, in May 2008, to quell public unrest caused by rising food prices in the free market, government re-opened registration for an additional 16.82 million newborns between 1988 and 2005, bringing the total number of ration card beneficiaries to 55.09 million. Planning figures of the Ministry of Social Security (MOSS) however have now been increased to 63 million beneficiaries from November 2008 onwards. The total number of ration cards remained with 11.54 million the same. Assuming an average “benefiting family size” of up to 6 individuals (including children no longer with their parents), 69.2 million Egyptians (= 92 % of all) should have access to the ration system, although not all family members might be registered.

In the wake of the soaring food prices during the last months of 2007 and the first months of 2008, government has considerably increased the amount of subsidized commodities per household. Whereas previously there had been two types of registration cards (the original green one for full benefits and a red one with reduced benefits), there is now only one uniform card.

**Table 6: Ration Scale as of May 2008**

Commodity	Type of Ration	kg/family (4 persons)	Price US\$ /kg	% of market value
Rice	Base	(eliminated)	--	
“	1 <sup>st</sup> additional	4	0.18	26
“	2 <sup>nd</sup> additional	4	0.36	55
Sugar	Base	4	0.11	18
	1 <sup>st</sup> additional	2	0.14	23
	2 <sup>nd</sup> additional	2	0.18	30
Vegetable Oil	Base	2	0.18	9
	1 <sup>st</sup> additional	2	0.63	33
	2 <sup>nd</sup> additional	2	0.91	48

As of November 2008, this rations scale will again be modified and simplified.

**Table 7: New Ration Scale of MOSS (November 2008)**

Commodity	Type Ration	Kg per person	Price /kg US\$	% of market value
Rice	Uniform	1.3	0.27	24
Sugar	Base ration	1.0	0.09	15
Sugar	Additional R.	0.66	0.31	52
Vegetable oil	Base ration	½	0.18	9
Vegetable oil	Additional R.	0.66	0.77	40

The calculations presented in this report are based on the ration system of May 2008. As the mission found out, this official plan for subsidized food distribution shows many variations depending on governorates and even depending on the locality. As an example, in Suhag governorate the ration card provides each family member with the following allocations:

**Table 8: Subsidized Food Ration in Suhag (October 2008)**

Commodity	Quantity kg/person	Price/kg US\$	% of market value
Wheat flour	8	0.11	15
Sugar	0.66 -1,50	0.32	53
Rice	1.00 -1.30	0.27	19
Vegetable oil	0.66 – 1.00	0.72	38

The access to baladi bread is not rationed. However, most bakeries allow only a maximum of 20 or 30 breads to be collected by any individual at one time. Since there are often long queues (reported waiting time over one hour), this discourages the collection of more bread by queuing at another bakery. However, subsidized bread finds many “unofficial” outlets, as had been found by the mission when served subsidized bread in a luxury hotel. The extremely low price of less than 0.01 US\$ per bread of 100 grams obviously invites waste and misuse.

Free market baladi bread is available everywhere in the towns at 2 to 5 times the price and probably is the most consumed bread anyhow due to the often bad quality or unavailability of the subsidized bread. The still low cost of the free market bread

would not be possible if the flour would have been obtained at free market prices. Consequently, there must be serious leakages in the system.

One particular oddity is that according to the still existing regulations, no private bakery can access non-subsidized bread flour (82% extraction rate) and bake baladi bread for the open market. The system only allows wheat grain to be traded on the open market, which the buyers then can have milled into bread flour in the many small artisan mills. Commercial mills, unless specially contracted by GASC to mill baladi flour, can only produce “fino flour” (72 % extraction rate).

## **5.2 Interactions between Food Markets and the Subsidy System**

The Food Marketing system in Egypt is characterized by two contradicting elements:

- A predominantly free market system of production and purchasing of locally produced foods as well as for food imports.
- A state dominated distribution system to consumers covering about 70% of the basic food calories consumed.

Being a relict from the previous socialist planned economy, the subsidy system understandably has difficulties to integrate itself into a free market economy. In a socialist system, production, supplies and distribution go hand-in-hand and all fits together. With farmers being now free to produce what is most profitable to them and traders free to trade, to import or export and to compete with the public procurement agencies, this inevitably had to lead to difficulties and distortions in the marketing system. The rather rigid quotas for purchases and distributions set by MOSS and channeled through GASC for the subsidy system collide with a free market volatility of prices and changing production patterns. Improvements in the efficiency of the distribution system as well as more private sector participation are also made difficult by the very large number of public sector jobs at stake.

Some of the most serious obstacles and distortions are:

- GASC is attempting to purchase an increasing share of the local production of wheat to reduce the need for imports.
- The market for traditional bread (baladi) is in disarray. Since there is no legal way to obtain bread flour, private bakeries must exploit the loopholes of the subsidy system in order to be able to sell baladi bread into the free market.
- During periods of falling world market prices, local prices are now kept artificially high, to the detriment of “free-market” consumers and food exporters.
- The public flour mills need new investments. Their low productivity of manpower and equipment results in a loss making production, with losses covered by government. They compete with the private sector, leading to overcapacity and high costs there.
- It defies logic when private traders compete with GASC in the procurements from farmers and thereafter sell much of the purchased food back to GASC.
- Concerning rice, sugar and vegetable oil, private trade services mostly “surplus demand” after basic food requirements have been met by the subsidy system.
- The subsidy system discourages investment in larger, interregional or national trading structures dealing with basic food supplies. The modernization and enlargement of private milling capacities for wheat are hampered.

- The very high costs for animal feed, to a large extent caused by the distorted wheat market, make meat and milk products inaccessible to a large population group.

Until 2007, GASC could only procure a small share of its wheat needs from local production. During the 2006/07 season, GASC bought only 1.7 million tons because it offered 236. - US\$/ton to the farmers whilst the private trade offered 368. - US\$/ton. The GASC target for the 2007/08 season is to procure locally 3 million tons. In order to achieve that, GASC has since May 2008 regularly raised the procurement price, always upping the prices paid by local traders by 20.- L.E. (3.60 \$) per ardup (= 150 kg), until it finally had reached **497.- US\$/ton** in the Delta region. Farmers however still preferred to sell to local traders, since they collect the wheat at the farms whilst GASC requires delivery to the mills. Local traders also provide cheap loans for production inputs. With wheat imports prices now rapidly falling to below US\$ 200.-/ton CIF Alexandria, traders now suffer from this competition since they are still holding expensive local stocks. The price difference between locally purchased wheat held in stock and import parity price is at the moment (October 30, 2008) 121. - US\$/ton, which is the loss to traders.

With traders now (October 2008) holding back with purchases, farm gate prices are falling too and consequently farmers are now reducing the planted areas for wheat and substitute it with the cultivation of berseem (= Egyptian clover) and beans. GASC policy probably has thus reduced “wheat self sufficiency”.

For the 2008/09 season, the government does not announce a “floor price” for wheat, but still seems to be promising a premium (e.g. 20%) above the international CIF prices. Since no-one can predict how international prices will be in April 2009, this is rather meaningless to farmers, who certainly want concrete assurances before they plant. Since wheat production - given the limited land available, the need for crop rotation to maintain soil fertility and the already high yields - can not be expanded significantly beyond the record production of 2008, the government’s strife to more “self-sufficiency” only will shift local wheat from the private to the public sector, thus increasing prices on the free market and consequently also the subsidies to be paid by the government. Import needs will largely remain unchanged, although the importers might make a windfall profit from cheaper imports after local prices have been pushed up by GASC.

In the rice sector, the government has attempted to shield the local rice market (and to reduce costs for rice purchases by GASC) from the soaring world market prices by declaring an export ban for one year, starting April 2008. This too had serious consequences for the private trade and the local rice production. Many large private rice mills, which specialize for the production of export quality rice, could not profitably switch to the milling of local rice. They consequently halted production and did not buy local rice, which has created a local surplus for rice and which in theory, should have reduced market prices. This however has not happened yet, since traders are still holding expensively purchased stocks from last year. With world market prices now lower than Egyptian rice prices, the export sector also would not be in a position to compete with the world market in case the export ban would be lifted. The most likely consequence of all this will be a significant reduction of the rice production in 2009. Farmers have many options to switch production to other - now more lucrative - crops in the 2009 summer season.

## 6. Conclusions and Recommendations

### 6.1 Conclusions

- The current systemic financial crises affecting banking and credit market on a global scale (originating from the sub-prime mortgage crises) has re-opened a debate on the right doses of Government regulations & responses. Soaring food prices – with their climax end 2007/ beginning 2008 - are followed by a stark fall of commodity prices in basic food markets - showing how the global banking/credit crash infects the real economy and thus millions of poor<sup>10</sup>.
- Volatility of prices is a very high risk for the vulnerable and extreme poor population which depends on food market supplies and food subsidy systems. This stretches response capacity of Government Ministries responsible for Food Subsidies to the maximum.
- There cannot be two parallel and competing systems for the distribution of basic food items. Food procurement and distribution must take place within a unified market with open competition.
- The wheat subsidies as well as the rationing system for rice, sugar and cooking oil hinder a free market in those food commodities and consequently contribute to the high food prices in the free market.
- The present economic, social and political situation in Egypt does not allow a significant reduction in food subsidies.
- Instead of reforming a food subsidy system which in the longer run needs to be abolished, immediate efforts should be made to make the subsidy system more compatible with the private trade.

It is unfortunate that an overreaction to soaring food prices between mid 2007 and May 2008 had led to a step into the opposite direction - an expansion of the food subsidy system - and has introduced, through the export ban on rice, an additional hurdle for the private trade. The proposal – as now often suggested – to reduce the ever increasing burden to the government finances through the introduction of targeting, misses the point. The longer term objective must be to eliminate the subsidies. The introduction of targeting into a system which anyhow is very cumbersome and expensive to administer, will create more problems than it solves. Since at least 70 % of the population cannot afford free market prices for food and amenities (housing, electricity, cooking gas etc.), any targeting would be an “exclusion targeting” and would have serious political consequences. As has been explained above, the food subsidy system basically represents a “baseline salary” to every Egyptian. Therefore, it should not be linked to poverty or malnutrition. There are already other – governmental and private - social support systems in place to take care of the poor and vulnerable.

Since elimination of food subsidies has to remain a long term goal, immediate efforts should concentrate on removing the most serious market distortions created by the subsidy system. To achieve that, subsidies should be provided at the end of the supply chain, which means at the outlets to consumers. The entire marketing chain from the

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<sup>10</sup> Reference to the current banking/financial crises is essential since this crises created a speculative bubble on the stock exchange which also infected future food markets leading to high speculation with commodities. Economists now agree that past prices hikes also stemmed from investors who 'discovered' food market (futures) as a profitable investment.

farmer or port of importation to the consumer should be managed by the private trade. A tendering system, as it is already in place for the procurement of rice or imported wheat from the private trade, should then select the most competitive outlets. GASC then would reimburse the trade outlets the difference between the tendered price and the subsidized price to consumers.

It will be near impossible for GASC to negotiate with thousands of small shops or bakeries. To reduce that burden, shops and bakeries could form associations who negotiate on behalf of the individual shops. Of course, GASC should never pay above free market prices. Bread will then need to be rationed too. Rationing could be achieved through the “Smart Card” now being introduced, which however might at least in the beginning face technical hurdles. An alternative to smart cards would be food stamps, which are successfully used in many countries.

The privatization of the supply chain will be made difficult by the need to abolish a large number of public sector enterprises and jobs. Public mills need to be privatized as well as the many public bakeries and food outlets. The process can only be gradual, but the direction and the will to do it should be there from now onwards.

Of particular urgency is to allow the free trade in baladi wheat flour. More than 70 % of the food subsidies are used for bread subsidies, with baladi bread at official prices hardly available in many places. A very large portion of the bread subsidies at present reaches the consumers only indirectly, through the private bakeries which manage to procure subsidized wheat flour through often obscure channels.

To replace food subsidies by cash subsidies is not an option either, because with markets being fragmented and inefficient as they are, most cash subsidies would soon be made worthless by price rises. This is also the opinion of all the beneficiaries interviewed by the mission. In any case, the public welfare system as well as many NGO working in the social sector provide already cash support to poor population groups.

A stable food marketing system in Egypt depends on predictable supplies from the rural producers. Farmers in Egypt react very well to signals from the market and adjust their production accordingly. They have a wide variety of options to choose between the cultivation of food crops, vegetable production and the planting of fodder crops.

If supply stability has to be achieved, producer price stability is necessary. It is therefore wrong to allow producer prices to change with volatile world market prices. Farmers have to take planting decisions 6 months in advance before they can sell their crops. They therefore want guaranteed floor prices, which should be set to be in line with the profitability of competing crops. In case the floor prices are higher than import costs, import tariffs should bridge the gap to avoid that traders sell imported grain at the higher local prices to GASC. If floor prices are lower than import costs, a free market will let farmers profit from this situation leading to higher farm gate prices.

The government policy of keeping strategic stocks has some justification. Considering the uncertain share of the local production within the government allocations for the subsidy system as well as the variations in world market prices, reserve stocks should cover approximately 3 – 4 months of the needs of GASC ( 1.5 to 2 million tons).

Egypt seems to lack a reliable market information system, which would allow government to adjust its policies (and eventually also the food rations in the subsidy

system) to the variations in supplies and prices. The establishment of such a system is highly recommended. It would also provide valuable information to the trade and to farmers as well. Food marketing could also be made more efficient and transparent if there would be more investment in setting quality standards and in quality control.

Of particular concern are the very high prices for meat and milk products as well as the ones for pulses. The main reason for that are the extraordinary high costs for animal feed and the scarcity of agricultural land. Egypt already imports vast amounts of maize for animal feed as well as meat and meat products. This by default leads to meat prices which are in line with world market prices. Only a higher purchasing power, last not least made possible by the subsidy system for basic food, can improve the access to essential secondary foods and thus create a more healthy diet.

## **6.2 Recommendations**

### **Possible Role for WFP**

With the government food subsidy system providing basic food security to everyone, including low income groups, there is no role of WFP to complement that with an additional food security based intervention. The commodity basket of the subsidy system however does not include pulses, meat and milk products and consequently the diet of average Egyptians is poor on protein. High costs for meat and milk on the free market do not allow compensating for this protein deficiency, which is particularly problematic for a healthy development of children. Households interviewed by the mission complained that the weaning food obtained through special government programmes (distributed through pharmacies) is not digestible by their children and that weaning food on the free market is by far too expensive. WFP therefore should look into the need for and the practicalities of nutritional support programmes for children targeting poor households.

WFP is presently supporting the Ministry of Social Affairs (MOSS) with a food safety net advisory team, whose role is to help restructuring the food subsidy system. As has been argued in this report, a revision of the food subsidy system should go hand in hand with a reform of the far larger subsidy structure for non-food needs. The aim must be to gradually phase out all subsidies in line with economic development. After that had been achieved, targeting of food assistance to vulnerable groups possibly will make sense. This process will need reliable information on household incomes and market prices.

Targeting of social benefits makes sense if a clearly definable minority of a population falls into a vulnerable group. At present, at least 70 % of the population would become highly vulnerable if the existing subsidies for living expenses would be eliminated. Therefore targeting at the present stage of development would have to be an “exclusion targeting”, which – apart from many other problems associated with it - would be politically very problematic.

The food safety net team as well as the VAM unit of WFP could valuably assist government during the transition from a government dominated food supply system to a free market economy for food. Main tasks would be to provide information on household incomes/expenditures as well as on the structure and efficiency of private food markets. In order to do that, the capacity for economic analysis in the VAM unit should be strengthened.

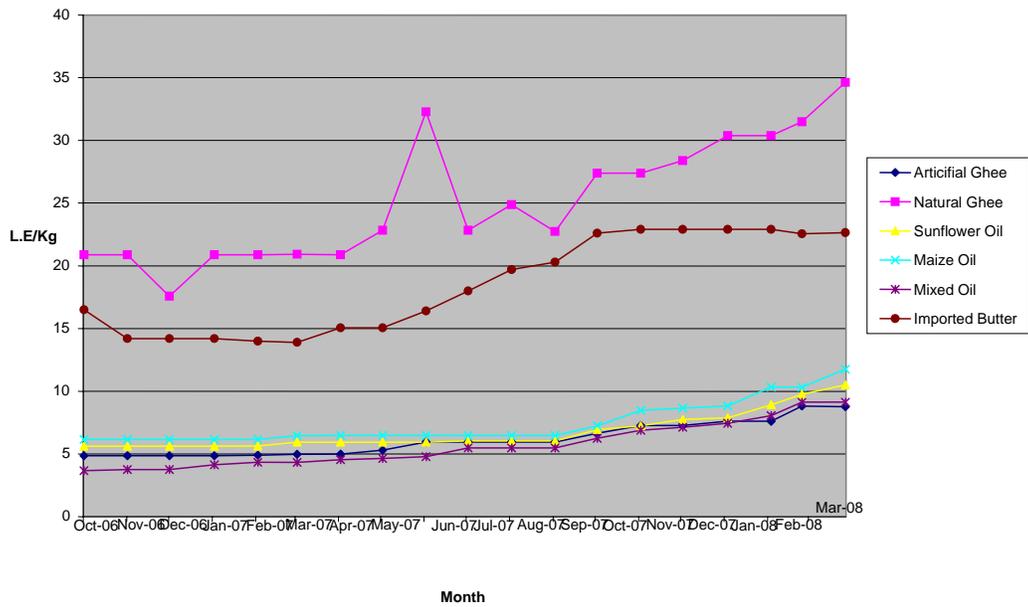
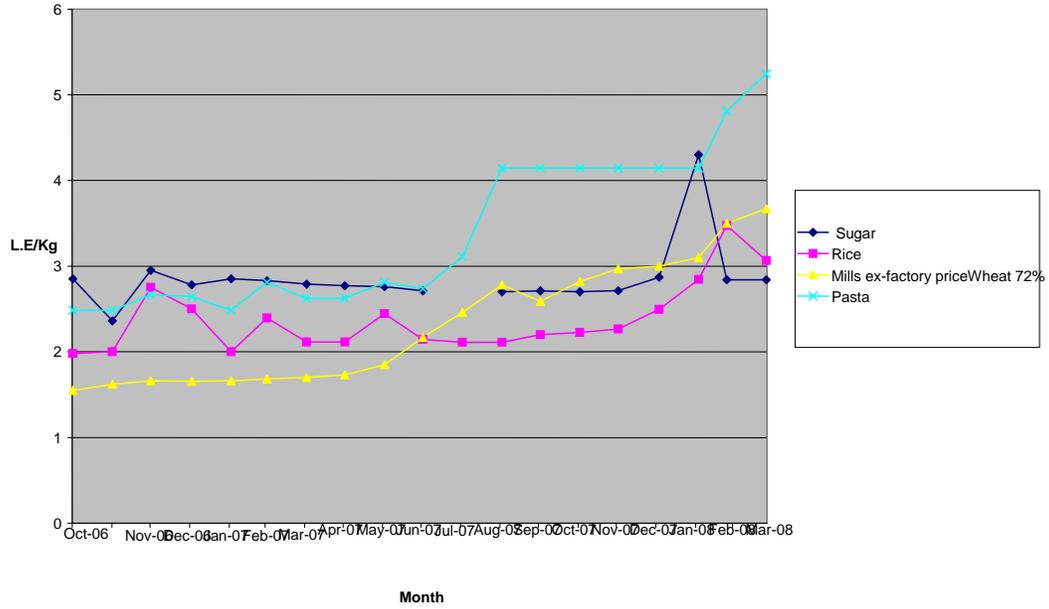
## **Recommendations for the WFP Country Office**

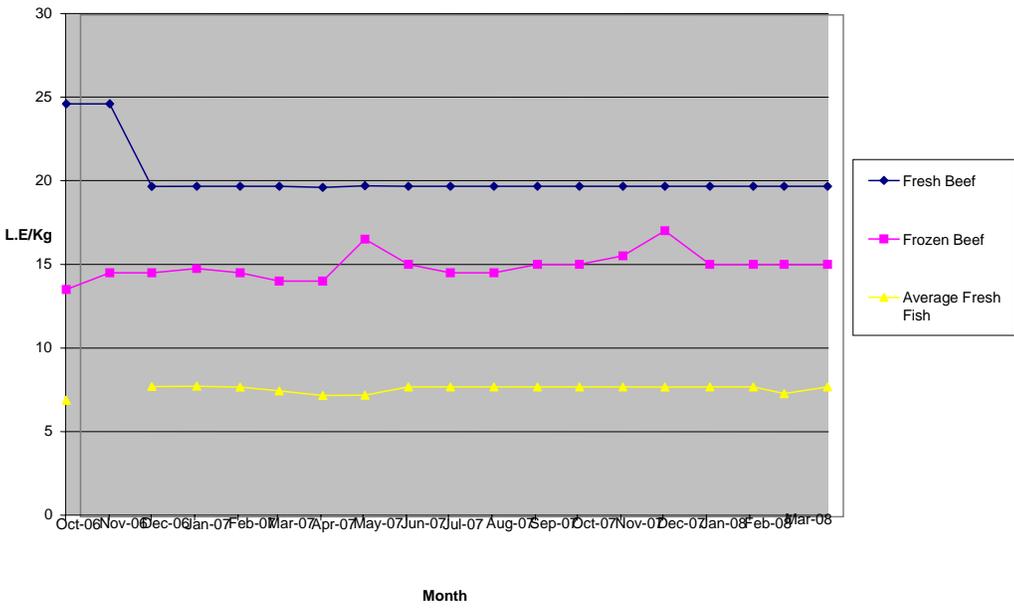
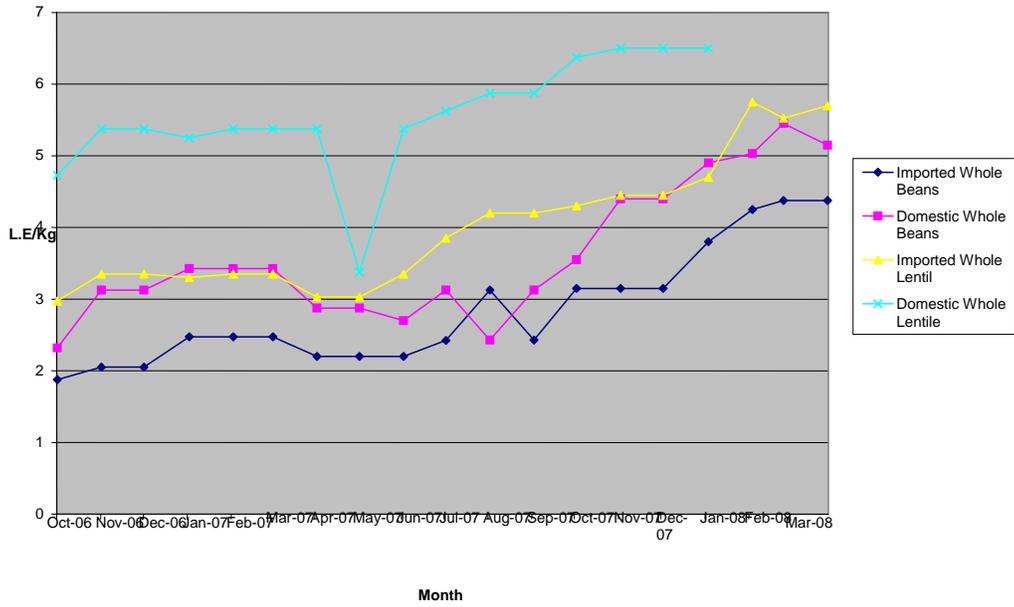
- WFP CO needs to develop its capacities for market analysis with a view to assess and analyze market trends of basic food commodities with the intention to assist food market players and the Government to control inflation and maintain price stability. Building "market knowledge and analytical capacity" would contribute to a better understanding of the modification of public spending into food safety nets which are increasingly under pressure for its large contribution on government spending and its inefficient use of funds.
- WFP CO needs to prepare frequent market & price reports (for which index and structure is to be determined) as a service to selected clients, such as Government Ministries and other NPO stakeholders dealing with the Egypt Food Subsidy System and its overhaul.
- Building of market capacity is by no means an end in itself for the CO Egypt, but needs to be translated into capacity building of WFP's most important clients (MoSS) to provide decision makers with regularly updated information on price trends and market movements.
- WFP CO needs to urgently build enhanced skills to provide a role model to monitor and analyze price trends and changing market structures to enhance capacities of MoSS and other counterparts (implementing food distributing projects).
- The building of WFP as an organization with a special competence in collecting and analyzing food prices and related market trends, shall feed into platforms/ food safety networks that deal with the overhaul and modification of the Food Subsidy System (in Egypt and elsewhere).
- WFP should offer and provide training to selected counterpart staff building analytical capacity to monitor/ analyze food price trends with the aim to trigger responses (use specific trade tools, price control/stabilization instruments) to effectively respond to price changes within an established social safety net system.
- The on-going Food Subsidy Reform Project should urgently recruit an economist (specialization in food markets) making good use of available funds from the recently approved grant: "Review of Reforms to national Food Subsidy and Safety Net Programs: Opportunities for WFP Capacity Reform". Should this funding not materialize, it is suggested to use funding of the Food Subsidy Reform Project (Dutch Funding).

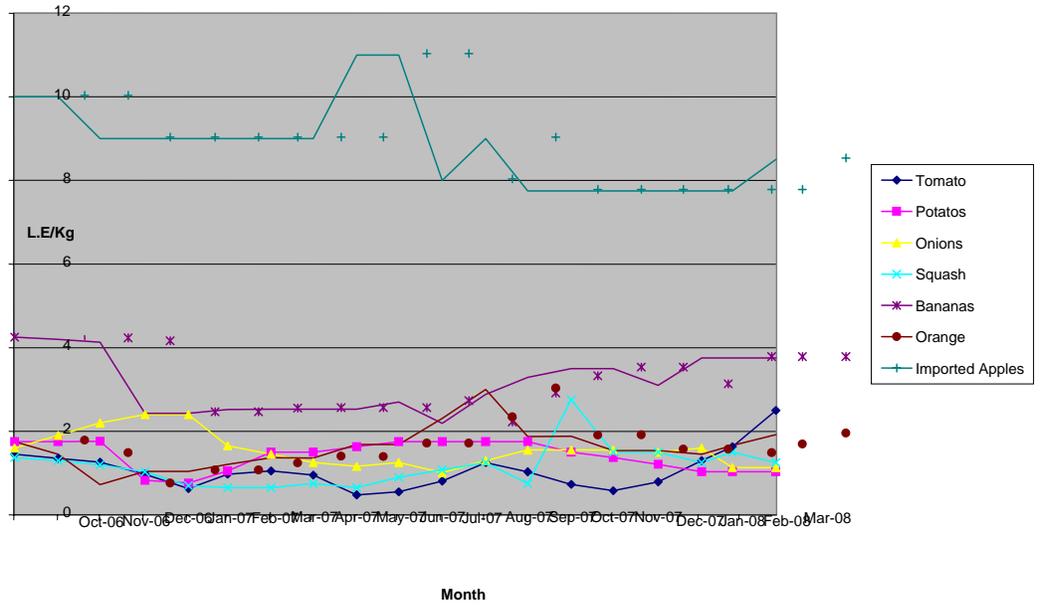
# ANNEXES

# ANNEX 1

## Whole Sale Prices of Basic Staple Commodities During the Period October 2006 to April 2008







## ANNEX 2

### List of References

- Arab Republic of Egypt: Toward Agricultural Competitiveness in the 21st Century; An Agricultural Export-Oriented Strategy
- Arab Republic of Egypt, Analysis of Housing Supply Mechanisms
- Building Infrastructure and Social Capital in Rural Egypt
- Challenges of Economic Reform in Egypt
- Changes in Structure, Conduct and Performance of the Wheat Sub Sector in Egypt during APRP
- Arab Republic of Egypt; Country Environmental Analysis (1992–2002)
- The Demographic Benefit of International Migration: Hypothesis and Application to Middle Eastern and North African Contexts
- Dietary Diversity as a Food Security Indicator: Mechanisms of Impoverishment of the Rural Poor in Contemporary Egypt
- Egyptian Workers in Paris: Pilot Ethnography
- Egypt and the Millennium Development Goals: Challenges and Opportunities
- Civil Society and the Uncivil State Land Tenure Reform in Egypt and the Crisis of Rural Livelihoods
- FAO – Nutrition Country Profile
- Arab Republic of Egypt; Poverty Reduction in Egypt, Diagnosis and Strategy
- Poverty Assessment Update 2007
- Poverty Reduction Strategy for Egypt 2004
- Poverty Reduction in Egypt: Diagnosis and Strategy
- Arab Republic of Egypt: Client Perspectives on Elements of World Bank Support
- Vulnerability Analysis and Review of Food Subsidy in Egypt 2005
- The Egyptian Food Subsidy System
- Wheat Policy Reform in Egypt
- Nutritional Assessment in Noubarea and Matrouah
- Nutritional Survey of Bedouins in Sinai
- Reform of Social Safety Nets: Targeting and Delivery Mechanisms
- The Monetary Transmission Mechanism in Egypt

- Arab Republic of Egypt Upper Egypt—Challenges and Priorities for Rural Development
- Household Income Structure and Determinants in Rural Egypt

**ANNEX 3**

**Schedule of Meetings  
Market Mission October 13- October 25**

<b>Date</b>	<b>Official in Charge</b>	<b>Agency</b>
October 13- 01:00 PM	Mr. Sameh Abdel Hakim	Resalaa Charity Association
October 13 -04:30 pm	Dr. Ashraf El Araby	Ministry of Economic Development
October 14 – 01:00 pm	Dr. Hisham Ragab	Ministry of Trade and Industry
October 14 – 03:00 pm	Mr. Amin Selim	Ministry of Social Solidarity
October 15- 11:00 am	Dr. Mahmoud Abdel Hai	Institute of National Planning
October 15- 02:00 pm	Mr. Adel Naiem	Importer and Trader- El Sawah- Khornish El Nil
October 16- 10:00 am	Mr. Nasreddin Alamin	FAO
October 19 – 9:00- 3:00 pm	Field Visits in Cairo	Field Visits in Cairo- Visiting 5 Poor Households in Manshiet Naser
October 20 - 10:00 am	Dr. Hanna Kheir El Dien	Egyptian Center for Economic Studies
October 22 & 23	Field Visits to Sohag Governorate	Visit poor household in Beni Helal village Visit Ministry of Social Solidarity Extension Visit Ministry of Agriculture Extension
October 29 -8 am- 5 pm	Field Visits in Damietta	Visit Rice Mill and Farmers planting rice