New Avenues to be Opened for Social Protection in the Arab World

The Case of Egypt

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Abstract

The article’s subject is social protection in the Arab world. Giving the example of Egypt, it asks why poverty is so widespread and why – despite the country’s numerous sophisticated social protection systems – social risks are a major contributing factor to it. It concludes that reforms are due. The existing systems are well funded but comparatively inefficient and more to the benefit of the better-off than the poor. A reform approach is proposed which builds on both, conventional and more innovative strategies of social protection. On the one hand, campaigns should be launched to raise public awareness of social risks, social assistance spending be increased and the operating public pension schemes be reformed. On the other hand, new avenues have to be opened to meet the specific protection needs of informal sector workers who are not covered by either social insurance or assistance. To this purpose, micro insurance schemes based on a partnership of NGOs, commercial insurance companies and the state are a new but promising approach for the Arab world region.
The situation of Egypt is symptomatic for many developing countries, especially in the Arab World. Poverty is wide-spread and it is further rising. Although the country spends more than a fifth of gross domestic income (GDP) on most different social protection schemes (some of them rather sophisticated), more than a quarter of the population is poor in absolute terms and the majority of the poor is made up of typical risk groups like women-headed households, orphans, the disabled and the underemployed.

Social protection is referred to as any mechanism which helps individuals to manage social risks (illness, widowhood, unemployment, old-age...). The question is, why social protection systems, despite sufficient funding, are unable to cushion the rise in poverty by preventing households from falling into poverty as a result of social shocks. But we will go beyond a pure analysis and discuss how the effectiveness of these systems could be improved with regards to reducing the vulnerability of the population to risks.

We note that the major problem of social protection in Egypt is not a lack of resources but the inefficient allocation of these resources within the systems and the unequal distribution of benefits with their tendency to benefit the better-off more than to serve the poor. A huge share of the population is not or only partly covered by the operating schemes.

Comprehensive reforms are due. We conclude, that a multi-approach strategy is called for to meet the social protection needs of all groups of the population: On the one hand, the existing social insurance and assistance schemes can be and must be reformed to make them more efficient and more egalitarian and to spread their out-reach. On the other hand, new avenues have to be opened up to extend the coverage of social protection to additional social groups as to reduce these groups’ vulnerability and to prevent them from falling into poverty. Micro-
insurance schemes should be taken into consideration; built up by partnerships between NGOs, commercial insurance companies and the state these schemes should focus on the largely unprotected informal sector workers.

Section 1 gives insight into the causes and the profile of poverty in Egypt, it shows that many Egyptians are poor as a result of social shocks. Section 2 looks into the goals and possible strategies of a state-led social protection policy. It serves as an analytical framework for sections 3 and 4. Section 3 is an analysis of the country’s operating social protection systems. Section 4 ends with an agenda for reform.

1 Poverty and the vulnerability to social risks

Poverty rates are comparatively high in Egypt and they are even rising. According to the most recent in-depth study, at least 25% of the population had an expenditure below the absolute poverty line in 1997 (Datt / Jollife / Sharma, 1998, p. 15; World Bank, 2001, p. 4). Moreover, Egypt’s Human Development Index in 2000 was ten ranks behind the country’s per capita income position (UNDP, 2002).

Wide-spread poverty is the result of different factors. The 2000 World Development Report notes that poverty at the individual level is caused by a combination of low levels of assets, low returns on these assets, and high volatility in returns to these assets.

This in fact holds true for Egypt, where a lack of physical, human and social assets is an important poverty factor. Generally, the country suffers from a lack of natural resources but poor families are particularly lacking in physical assets: The distribution of land, productive assets and stocks is very uneven. In agriculture, for example, 70% of the exploitable land was con-
centrered in the hands of 20% of all farmers in the mid-1990s (KfW, 1997). Similarly, Egypt suffers from a lack and uneven distribution of human assets. As an example, almost half the population is illiterate. Finally, the poor also have fewer social assets (social ties, social rights, political influence...) than the rich. They have fewer wasṭa (knowing the right people), which is so important for finding employment or getting applications approved in a country like Egypt.

Low returns on assets and labour are another reason for the spread of poverty. During the 1990s, the government carried out an ambitious stabilisation and structural adjustment program and succeeded in reducing the inflation rate, accelerating growth and reducing the budget deficit to near balance. However, the distribution of income worsened because real wages stagnated, productivity dropped and unemployment rose significantly (Korayem, 1996; Subramanian, 1997). Correspondingly, poverty increased. The high growth rates of the 1990s did not result from increases in labour productivity or economies of scale but from the proceeds of capital-intensive industries and windfall gains (oil exports; Suez Channel taxes). They induced no capacity or spill-over effects and only led to higher returns on capital. While for decades Egypt’s labour income rate had remained relatively stable at about 40%, it sharply declined during the 1990s (World Bank, 1999a).

Finally, volatility in returns to assets is a third poverty factor. It results from households’ vulnerability to social risks like unemployment, illness, work disability, longevity, the early death of the main provider, land loss, drought and livestock epidemics. When such risks occur, households suffer from a decline in income or rise in expenditure or even both.

In most cases, the Egyptian poor were not destitute before they were hit by social shocks. Before, they had low income but were still living above the poverty-line and managed to spend
for their most basic needs. Their drop below the line came only after and as a result of the occurrence of one or more risks (divorce or separation of women; death, work-disability or underemployment of the main provider). The great majority of the poor is made up of three typical risk groups:

*Women-headed households and orphans:* Poverty is more often found among unmarried, divorced, widowed and abandoned women than in any other social group. More than a third of Egypt’s women-headed households are living below the poverty-line (Assaad / Rouchdy, 1999, p. 19). Likewise, orphans are concerned with poverty. Although there are no reliable data, most observers agree that more and more orphans are living on the streets, bagging for support (World Bank, 1999b, Annex A4).

*The work-disabled:* 29% of the recipients of the social-assistance-like Sadat-pension were handicapped in 1995, which sheds light on this groups’ vulnerability (Diwan / Walton, 1995, p. 75).

*The underemployed:* At first glance, unemployment seems not to be a serious risk. Only 27% of the country’s registered unemployed live below the poverty line. This is, because the real poor cannot afford not to work at all. They have to accept any income-generating activity and are officially regarded as underemployed. But, while only 12% of the labour force are officially registered unemployed, four times more are underemployed or outside the labour force, because they have given up looking for work. A high 39% of these persons live below the poverty line, compared to 15% of those with permanent employment (Datt / Jollife / Sharma, 1998, pp. 45f.).
Old age is much less a serious social risk. Poverty is only slightly overrepresented among those at age 60 or above (Datt / Jollife / Sharma, 1998, pp. 28 - 30). The average number of senior members is only slightly higher among poor households (0.38 senior members) than among non-poor households (0.37).

2 The goals and strategies of social protection

Since poverty is the result of low levels of assets, low returns on these assets and a high volatility in returns (see above), an effective poverty eradication strategy would address all of these three factors:

- give the poor opportunities by improving their access to physical and human capital (e.g. better education, better and more efficient health care, security from loss of land ownership, redistribution of land and other productive assets),
- give the poor possibilities by raising their rates of return to employment and to assets and
- give the poor securities by providing them support in their risk management efforts.

Here, we shall focus on the third component only.

In response to their vulnerability to social risks, most different risk management strategies can be employed by households and communities. In general, one may distinguish

- prevention mechanisms, which reduce the probability of risk occurrence,
- mitigation mechanisms, which reduce ex ante the magnitude of their net impact and
- coping mechanisms, which relieve the impact ex post, once the shock has materialised.

Nevertheless, large shares of the population in developing countries, are not sufficiently protected. On the one hand, many households are unable to make provisions. Others are able to
do so, but they do not know the nature of their risks or they are hit by social shocks before they have accumulated sufficient savings. Moreover, it is difficult in advance to assess the nature, time of occurrence, probability and size of impact of one own’s risks. On the other hand, many households are also unwilling to provide for social shocks or to prevent them. They underestimate the probability of a risks’ occurrence or the size of its impact; or they just do not care about the future (myopic behaviour) and count on public social assistance or the support from relatives and friends.

Meanwhile, households may also lack access to adequate provision mechanisms. Insurance markets often fail because of information asymmetries. Insurers are unable to assess potential clients’ risks and to determine risk-specific premium levels. At any price, bad risks are adversely selected while low risks find the offer unattractive. Only the highest premium levels promise gains for the insurance company. Moreover, clients, once insured and knowing that their risks are covered, tend to become less cautious (moral hazard). Other insurance markets fail because risks are correlated. Droughts, for example, usually hit the entire rural population of a country at one time. Insurance markets also fail when the demand for insurance contracts is small, because in this case risks cannot be sufficiently pooled.

In these cases, governments should intervene and support households in their risk management efforts

- to overcome market-failure and improve the efficiency of the overall allocation patterns
- and to restore the social balance and justice between low- and high-income households.

Of course, these are not always the key motives of social policy makers, who may have different goals in mind (e.g. to improve their reputation, legitimacy or power basis within the population) when they decide to build up, respectively reform a social protection system or
not. This political economy aspect of social protection is very important to consider. However, it would require in-depth analysis to identify the leading forces behind social policy decisions in a country like Egypt. Such analysis would go beyond the given scope of this article, but it was done elsewhere (Loewe, 1998).

Government interventions can take three different approaches: First, governments can support the efforts of households in *preventing risks*: raise their awareness about the impact and frequency of social risks, provide information about their nature and advice on how to reduce the probability of their occurrence (healthy way of living, prudent behaviour...).

Second, governments can support households in providing for social shocks through *mitigation strategies* which shift life-time income from the good times in life to the bad times (*intertemporal redistribution*). Governments might, for example, overcome some of the mentioned market failure problems by making insurance against social risks mandatory within social insurance schemes. Such strategy is efficient because social insurance benefits are in the long-run equivalent to contributions for everyone: However, it cannot improve distribution patterns, because it does not shift considerable transfers from the rich to the poor.

Third, governments can support households in *coping with risks*. They might, for example, redistribute inter-temporally from the better-off to those who have been hit by social shocks. Governments usually act through tax-financed social assistance or subsidisation programmes. Such *intertemporal redistribution* improves social equality, but it often provokes inefficiencies. People evade contributions and taxes when they are higher than the expected benefits. Others misuse the assistance programmes. Subsidies are particularly inefficient, because the subsidised goods are often wasted and consumed by the better-off as well as by the poor.
As a rule, government intervention should pursue several approaches at the same time. Each of them has some advantages. There is a trade-off between the two mentioned goals of social security - efficiency and social justice. A compromise has to be found that reflects society’s idea of justice. This usually requires government interventions to strengthen both, people’s mitigation and coping strategies.

3 Social protection in Egypt

This section explains why poverty is highly correlated with the incidence of social risks. It shows, that Egypt’s social protection schemes are ineffective and leave many households, especially low-income groups, vulnerable to a wide array of risks.

The major problem of social protection in Egypt is not a lack of financial resources. Egypt is a middle-income country and central government income exceeded 35 % of total GDP throughout the 1990s. In fact, more than 20 % of GDP are spent on social protection and public schemes alone accumulate at least 9 % (Loewe, 2000a, Table 3).

The ineffectiveness of social protection in Egypt rather results from the inefficient allocation of available resources. Almost half of social protection spending (9 % of GDP) is for risk coping, i.e. it is redistributed interpersonally with the goal to support those in need: public social assistance and subsidies to social insurance, public health care and basic commodities. Another 9 % of GDP is private saving, an individual risk mitigation strategy (intertemporal redistribution), that does not allow for the pooling of risks and is, hence, inferior to insurance. Private and social insurance contributions amount to 0.2 and 2.7 % of GDP only (idem, pp. 16f.).
Moreover, Egypt’s social protection systems are not equitable. Most of them discriminate against the poor while benefiting the urban higher and middle classes. By law, every Egyptian is covered by social insurance. In practice, however, only half the population is insured and benefits for the bourgeois and state elite are much more generous than those for the poor. Similarly, social transfers benefit the middle class more than they support the poor: 2.3 % of GDP is spent on subsidies but less than 0.2 % on social assistance (Tzannatos, 2000, pp. 25f.).

Traditional mutual support networks are eroding. Relatives, friends and neighbours used to support one another in case of a social crisis, and the well-off were expected to give some of their income as Zakât to the needy. Today, the total volume of such voluntary interpersonal transfers is in constant decline and does not exceed 1.8 % of GDP (including remittances from migrant workers to their relatives). Even within the family, transfers are decreasing and have only limited effects.²

Market and community-based protection systems cannot compensate for the erosion of social solidarity. The private saving’s rate is low and deposits with banks are concentrated on the better-off. Only a small minority of households can afford commercial life or health insurance. The Gama‘iyyât, rotating savings and credit associations, are quite popular in Egypt. For lower and middle income groups, they constitute a substitute for formal saving and lending from banks and help to cushion fluctuations in income. But, just like saving with banks, they do not pool risks and, hence, do not protect from the long-term impact of risks.

Social insurance

Egypt’s social insurance is an elaborate system with its total receipts making up more than 5 % of GDP. By law, every employed person has to enrol and for a majority of workers, the
legal provisions are in fact comprehensive. But the system suffers from five deficits, which make it inefficient and inequitable: (1) its split-up into six schemes with different legal provisions, (2) the non-protection of serious risks, (3) its low coverage, (4) low benefit levels and (5) low returns to contributions.

**Six different social insurance schemes:** Considering legal benefit provision, Egypt is a highly stratified society. Six social insurance schemes operate for six different groups of the employed. Most of them are administered by the National Social Insurance Organisation (NSIO) but the coverage of risks insured and the generosity of benefit provisions varies:

The first of these groups consists of public and private sector employees (50% of the labour force). They are required to enrol with the *General Social Insurance Scheme*, that was originally designed on an intertemporal redistribution base to be financed by contributions from the employee (14% of basic and 11% of variable salaries) and the employer (26% of basic and 24% of variable salaries). In practice, however, the treasury has taken over the financing of parts of the benefits. The benefit provisions are almost comprehensive: they include pensions, sickness and maternity pay and unemployment benefits. Employees enjoy free treatment by the National Health Insurance Organisation’s health care facilities but their dependants are not insured.

Pensions are granted to those aged 60 or more, to work-disabled persons and to the survivors of a deceased employee. Their level depends on the insured person’s last *basic* salary before retirement and the number of contribution years - with a provision for maximum and minimum pensions (Brown / Formosa, 1999). A pensioner, after 30 years of contributions, receives a pension which equals 67% of his last basic wage. But pensions are not automatically
adjusted for inflation; increments are decided upon by the government on an annual basis and financed by the treasury.

Old-age pensions are supplemented by a variable pension component, which is calculated as a share of the average monthly variable wage over the entire contributory period - times the number of contribution years. Here, the current value of the variable wage is increased by 2.5% a year, but this adjustment does not compensate for actual inflation, which peaked to 20% during the 1980s. Not before 1996, it fell below the 10 %-line and was still around 4 % in 2001. No inflation adjustment is provided for after retirement (ILO, 1998).

The second group of the insured is made up of the members of some of the professional associations and employees of foreign and some big Egyptian companies. Professional unions and commercial companies may opt out of the general scheme with their employees. They may conclude preferential group insurance contracts with private insurers, that grant higher pensions and provide better medical treatment than the general scheme.

The third group consists of Egyptian migrant workers abroad, employers and the formal sector self-employed. For these groups, two separate contributory schemes have been built up, where contribution rates can be chosen within a certain interval. Enrolment is mandatory for employers and the self-employed, but optional for migrant workers. These schemes have a slightly better pension / contribution ratio than the general scheme, but both do not provide health, maternity or unemployment benefits (INP, 1998).

However, some employers and high-ranking employees draw an income high enough to make additional provisions. This fourth group of the population can afford to insure with private
companies or to pay for treatment in private hospitals out of pocket and enjoys higher pension entitlements and better health care.

The fifth group, all workers not covered by any other social insurance scheme, has to enrol with the Comprehensive Social Security System. Contributions are deducted by the purchase of an LE 1 stamp each month. The scheme only provides for a flat rate old-age, invalidity and survivors pension of 63 LE per month. This pension is low but still advantageous for the insured: Retirees are eligible for it if they have contributed just LE 1 a month for a minimum of 120 months. Even a one-time payment of LE 120 after retirement is accepted in lieu (ILO, 1998, p. 26). Contribution receipts are only a tenth of the scheme’s expenses, the difference being covered by cross-subsidisation from the other social insurance schemes (idem, p. 30).

The sixth and last group is the army and top bureaucracy, who enjoy the most generous insurance provisions. They are protected against all kinds of social risks by the “Collective Social Security Systems”, non-contributory schemes outside the NSIO’s responsibility. They are administered by some of the ministries and financed through taxes.

**Non-insurance of serious risks:** All of the schemes provide for pension benefits. But only 40% of the working population (the permanent employees) are insured against work-related injuries and diseases, and no more than 16% are entitled to unemployment benefits.

Even worse, only 30% of the population have health insurance (some 25% are insured with the NHIO, another 5% with private insurance companies). The public health care system is open to all for free, but its quality is bad and those without health insurance opt to consult private or NGO clinics, if they can afford.
Some serious risks are not covered at all. None of the schemes insures separation (with or without divorce). By law, a husband has to care for his wife, even when he divorces or abandons her. In practice, however, men usually fail to do so and most women do not claim their rights or are unable to find their husbands once they have left. The need for nursery care is not insured, either. Many of those who cannot care for themselves are looked after by their family, though a growing number are abandoned. The government runs some homes for the old and the handicapped, but places are scarce and most of them are expensive.

This, in fact, explains to some degree the overrepresentation of some groups of work-disabled persons, and abandoned and divorced women among the desperate poor.

**Low actual coverage:** In theory, the entire population is covered by one of the insurance schemes. In practice, however, only 53% actually enrol. The reasons for this are threefold:

First, many Egyptians do not want to enrol. They prefer to have their income for today’s consumption instead of paying contributions to provide for the future. Others feel mistrust towards the NSIO and believe that the effective insurance yield is too low.

Second, many employees are not informed about their right to enrol. Sometimes, casual workers often cannot pay their contributions because there are no tax stamps left with the NSIO offices (Rieger, 1996, p. 36). After retirement, potential beneficiaries, especially the poor, find it difficult to claim their rights, because they do not know where to apply, how to apply and how to fill in the application forms. Widows and orphans face another problem when they do not hold identity cards, which are required for application.

Third, the monitoring of the system is weak. Almost 100% of state and public sector employees are insured. But in the private sector, where the state does not deduct contributions itself,
only 62% of the employed pay contributions. The NSIO is unable to supervise private employers in registering their employees and properly deducting their contributions. Some workers are ignorant about the fact that their employer does not pay insurance premiums for them. Others reach agreement with their employers on non-registration as a means to save contributions on both sides.

**Low benefit levels**: Contribution rates and replacement ratios are high when compared to those of other middle-income countries. In 1995, average pensions were equivalent to 147% of private sector employee’s nominal life-time taxable salaries (102% for state employees).

However, many pensions are far below the poverty line for many Egyptian households. The average state employee receives LE 4272, but the medium private sector employee is entitled to LE 1716 only (ILO, 1998, p. 55). Average pensions are particularly low for survivors and the work-disabled. When an earner is injured or dies at young age, accumulated contributions are low, so that pension entitlements are insufficient for the family to survive. Low survivor and invalidity pensions are a reason for poverty-concentration among women-headed households.

Three factors explain this discrepancy: First, the rate of return to contributions is low in all of the schemes except for the comprehensive system (see above). Real pension levels are low because the pension formula does not provide for automatic adjustments for inflation. Increments are decided on by government decree and averaged only 10% a year between 1980 and 1995, while inflation was much higher equalling 20% in some years (ILO, 1998, p. 21).

Second, contribution payments are low in absolute terms. Average salaries are low and the income threshold is even lower (LE 1025), so that large parts of the income of higher-income
groups are not included in the computing basis: In 1997, average monthly contributions were LE 108 for government employees and LE 117 for private sector workers (idem, p. 25).

Third, actual contribution rates are far below those stipulated by law, because non-payment of due contributions is rarely sanctioned. According to legal provisions, the combined employer and employee contributions should be some 32% of covered earnings. However, the NSIO reports aggregate contributions to represent just 17% of taxable wages (World Bank, 1993, Vol. II, p. 107).

**Low returns to contributions:** The NSIO’s cash flow balance posts a surplus amounting to 2.5% of GDP. Total receipts are two times higher than aggregate expenses. This ratio is far higher than necessary for even a funded social insurance system (World Bank, 1993, Vol. I, p. 4; Vol. III, p. 51).

Nevertheless, the NSIO’s long-term financial sustainability is in question. It is expected to be short of cash income by 2008 (ILO, 1998, p. 40). While overall expenses have been stable since 1985, contributions have been decreasing over the whole time span to 37% of all receipts in 1997 (exceeding total spending by only 2%). Another 42% are returns on invested funds while 21% are government subsidies paid to cover the follow-up costs of pension increments.

Four major causes are responsible for the dangerous development in the NSIO’s financial status: The first cause is the frequent misuse of the schemes’ legal regulations by employers and employees who find it easy to manipulate income declarations to their own benefit. They mutually agree, for example, to underreport salaries during most of the employee’s working life to lower contributions, while overstating salaries during the last two contribution years,
upon which basic pensions are calculated. Moreover, many pensioners receive benefits under the provisions of the comprehensive insurance system, although they fall under the criteria of one of the other schemes, which is a problem in that the comprehensive system is not self-financing.

The second cause consists of some overgenerous qualifying conditions. Early retirement pensions are granted without any sound actuarial reduction in respect of normal pensions. Likewise, some special concessions for privileged groups should be named at this place: the cross-subsidisation of the generous comprehensive scheme by other schemes and the tax-financed non-contributory ‘comprehensive schemes’ for the army and the top bureaucracy.

A third cause of the NSIO’s financial problems is the high ratio of pensioners to contributors within the insurance (0.37). Over the whole population only 14 people aged 60 years or more stand against 100 people at working age (15 to 60 years). This is due to (i) the high and growing number of early retirees and (ii) rising unemployment rates.

The fourth and most important cause is the NSIO’s unsound investment policy. A third of the NSIO’s reserves are claims against the treasury resulting from pension adjustments. These transfers have never been disbursed because contribution collections have until now exceeded expenditures. The promised subsidies are entered in the books only - as government liabilities.

The remaining two thirds of the assets represent the NSIO’s funds. The NSIO is not allowed to invest more than 1 % of funds at a competitive interest in the capital market but obliged by law to transfer current surpluses to the National Investment Bank (NIB). Deposits that go back to 1992 or earlier yield only 5-6 % a year. New investments bear interest of 11 %, but the old assets still represent 43 % of total assets (ILO, 1998, p. 26).
Social insurance contributions in Egypt have to be seen as a tax used to finance government investments. The NSIO’s funds represent 68% of the deposits of the NIB, which was founded to provide credit to the central and regional governments, public sector institutions and public enterprises. Of course, these public entities do not have to pay free market interest rates: The NIB’s lending rates have been negative in real terms, as have its depositary rates.

Moreover, the NSIO’s funds exist on paper only (World Bank, 1993, Vol. II, p. 104). They are invested in infrastructure projects which bear no yield and cannot be sold when needed. When, in 2008, current expenditures will exceed contribution receipts, the NSIO will face a financing gap (ILO, 1998, p. 26). Pensions can only be paid out if the treasury settles its liabilities or if the NIB pays out the NSIO’s interest instead of reinvesting the capital yields. In both cases, the government will have to raise taxes to settle the claims. This is inefficient and has negative impacts on income distribution as well: While taxes are paid by the entire population, social insurance benefits only 53% of the Egyptians.

Public health care

The major problem of Egypt’s health sector is not its lack of resources but its fragmentation into five different health care systems, a source of inefficiencies and social imbalances.

This segmentation is inefficient, because the systems are badly co-ordinated. Some regions are undersupplied, while there is a duplication of specific services offered in others.

The segmentation is unjust and further aggravates prevailing social imbalances because each of the five systems is accessible to a certain group of the population only: (1) The bourgeois upper class can afford health treatment in private hospitals. (2) The top bureaucracy and the
army enjoy first-class treatment in exclusive hospitals run by some of the ministries and financed through tax revenues. (3) Parts of the upper urban middle class are insured with the Curative Care Organisations of Cairo and Alexandria, that run their own high-quality health clinics. (4) Members of the General Social Insurance Scheme are treated for free by the NHIO’s health care system. It is mainly financed by health insurance contributions but the state has to add a yearly rising subsidy, which amounted to 0.5% of GDP in 2000. (5) The poor, finally, have to search treatment in public health care facilities, which are in a desperate state.

The public health care system is a dense infrastructure network but it is living on its capital. 98% of Egyptians live within a radius of no more than two kilometres from the next health station. But funding declined from 5% of GDP to 1% during the 1990s. Necessary reinvestments are being neglected, most rural health centres lack some of the even most basic equipment and even hospitals are reported to be dirty. Most of the personnel is badly trained and paid. Physicians are unmotivated and said to claim extra-payments for every service offered. (INP, 1998).

Those who can afford, pay for referrals to private doctors or NGO clinics. So, 56% of total health care spending is paid for by households and not refunded by the state or the NSIO (INP, 1998). Such development is inefficient and unjust: Unanticipated health care spending is not insured, so that people have to accumulate huge savings to be solvent in case of an illness. But the poor are unable to save.
Commodity subsidies

In the past, Egypt took several different approaches to fighting poverty through interpersonal redistribution. One of these was to subsidise basic commodities. Such indirect transfers are supposed to raise the real income of the poor by reducing the price of essential consumer goods. But they are far less fair and efficient than direct transfers (like social assistance). Usually, the better-off benefit along with the poor, while some of the poor do not benefit, since they do not demand the subsidised goods. Precise targeting is difficult and costly.

Today, though less money is spent, efficiency losses continue to be high. Most subsidies were discontinued in 1992; only sugar, tea, cooking oil and the basic ‘baladi’ bread are still subsidised. But administration costs are still high and deceit in the administration and in the bakeries is reported. To channel LE 1 to the poor, the state spends LE 3 on bread subsidies, LE 10 on sugar subsidies or LE 33 on oil subsidies (Cornia / Stewart, 1995). Inefficiency losses are even higher for the subsidisation of piped water, electricity, petrol and gas. Moreover, the rich benefit more from these expenditures than the needy, since most of the poor are not connected to the water and electricity systems and they have no cars or oil ovens.

Social assistance

Egypt’s direct income transfer programmes are too small in scale and scope to have substantial effects on poverty levels. Aggregate spending represents only 0.15 % of GDP (van Eeghen 1995) and average per capita transfers equal only 5 % of the absolute poverty line. The error of inclusion (rich people receiving assistance) is small, but 80 % of the needy have no financial support. They are not informed about the programmes or unable to fill in the application forms or simply do not fall under the programmes’ eligibility criteria.
Another problem is transfer inefficiency. The public welfare sector is split up into three major and a number of smaller programmes. They are under the administration of different institutions, the largest being run by the Ministry of Insurance and Social Affairs (MISA). Widows, orphans, divorced women, invalids and old-aged people may apply for social assistance from the MISA, but the unemployed and underemployed are not eligible. Per capita transfers are low averaging 36% of the poverty line in 1997 and ranging between LE 132 and 444 per household and year (Assaad / Rouchdy, 1999; Azer, 1995: 114; ILO, 1998, p. 29).

The second programme consists in the Ministry of Awqâf’s activities. In 1991, it spent LE 5 million on social assistance and social credits. But the employees of the ministry formed 80% of the recipients (Wippel, 1996, p. 191).

The third programme is run by the Nasser Social Bank (NSB) and primarily financed by the Zakât of public enterprises. It spends LE 160 million on its social assistance and credit programme, in which it co-operates with local Zakât-committees. These committees collect Zakât from local donors and transfer the funds to the NSB. On request, funds are returned to the committees to grant stipends, finance weddings, support poor old-age or unemployed persons or assist divorced women in claiming their rights from their husbands. The programme seems to be very efficient – probably because the Zakât committees know well the needs in their neighbourhood.
4 Strategies for reform

Reforms are due to improve the efficiency of social protection in Egypt and to extend its overall coverage to additional groups of the population and further risks. The operating schemes leave large parts of the population vulnerable to social shocks.

We propose a four-component strategy to include all of the three conventional approaches of government intervention mentioned above and at a time open new avenues to meet the special needs of the currently unprotected. No considerable extension in out-reach is possible unless reforms go beyond a pure restructuring of the existing schemes.

First, campaigns are called for to raise public awareness about social risks. They are to stress the importance of risk prevention, inform about possible strategies to mitigate risks and provide support in coping with risks.

Second, the actual coverage of social insurance must be extended and the existing schemes be re-designed as to align their benefit provisions, raise their effectiveness in protecting against a high number of risks and improve their benefit-cost ratio and financial sustainability.

Third, the out-reach of social assistance schemes must be broadened and their spending be raised. Social protection policies cannot build on mitigation strategies only; these are more efficient than social transfers but unable to reduce social imbalances. Social insurance always leaves out some individuals, who have small incomes and are unable to pay contributions. Interpersonal re-distribution is required to pool social risks across the whole society.

Fourth, micro-insurance should be promoted to reduce the vulnerability of the currently unprotected. Micro-insurance is a new approach to bridge the gap in social protection between
social insurance and social assistance. Large parts of the Egyptian population – namely urban informal sector workers – fall into this gap.

On the one hand, urban informal sector workers are the least-well protected social group in Egypt. A first group of the population, most of them in rural areas, is still ruled by traditional values; their mutual support in crisis pertains to be strong. A second group, formal sector employees, contributes to the national social insurance systems or holds private insurance contracts. A third group, the desperate poor, is eligible for social assistance. Informal sector workers, finally, fall into gap between all of the mentioned protection strategies. Most of them live in towns, where the reciprocal support among neighbours has become weak and commercial insurance is too expensive for them. Meanwhile, they have no permanent employment and no regular income, so that the NSIO has difficulties in checking on their enrolment.

On the other hand, informal sector workers have some income and they are able to spend some of it for their social protection. Hence, they are not eligible for social assistance. micro-insurance is a way to overcome this dilemma.

**Public awareness and information campaigns**

Many Egyptians are not aware of social risks and have no interest in enrolling with the NSIO. These problems are major factors in the insufficient social protection of many Egyptians.

A first step to address these problems is to launch campaigns in order to (i) make the population aware of social risks and the necessity to insure against them, (ii) foster and support people’s efforts in preventing risks, (iii) inform people about their rights and the way the operat-
ing social systems function and (iv) make qualifying conditions and administrative application procedures better known:

A second step is to support the insured and the applicants for social assistance in applying for benefits and claiming their rights. Such support is best provided by NGOs because people trust them more than they trust public institutions. Foreign NGOs with relevant experience in these tasks could provide the necessary training of local NGO workers in (i) informing clients about their rights, (ii) supporting applicants (especially the illiterate) on their way through the administration, (iii) providing legal advice and (iv) representing claimants in court.

**Social insurance reform**

Egypt’s social insurance schemes are inefficient and socially unfair. But they are elaborate systems and minor modifications can do a lot to reduce some shortcomings in the short-run. In the longer run, however, more comprehensive reforms are needed to guarantee their long-term sustainability. As far as immediate reforms are concerned, the four major deficiencies of the system have to be addressed:

First, the NSIO’s unsound investment strategy should be revised. It is the major factor of the low rate of return to contributions for contributors. To promote the NSIO’s capital income, the NSIO must have permission from the government to decide itself on fund investments. Then, the NSIO should build up an independent board of investment, carefully work out a high-yield low-risk portfolio investment strategy and invest all future surpluses at competitive rates of interest in the free capital market.
The NIB, in turn, is called on to check the prospects of making funds solvent to repay its liabilities to the NSIO. If there are none, the NSIO should at least be granted higher interest on its deposits with the NIB. Additional costs have to be born by the treasury, as the NIB lends exclusively to public institutions. On the other hand, treasury subsidies will be reduced once the pension formula has been modified (see below).

Second, the pension formula has to be modified. Pensions have to calculated in such a way that contributions can finance all benefits. The income threshold must be abandoned with a view to making all labour income taxable. With a higher basis of calculation, contributions rise in absolute terms. Then contribution rates can be reduced by some percentage points to allow for today’s benefit levels. This is important to provide more incentives to enrol and to reduce tax evasion. Moreover, the differentiation between basic and variable salary components can be overcome and pensions be computed according to one single formula. Most important, however, the treatment of inflation should be integrated into the formula. Before retirement, pension entitlements should be based on average career earnings, and be indexed to wage inflation. The same applies for the increase of pensions after retirement and for minimum pension provisions.

Third, the treasury should rationalise its subsidisation of the system. On the one hand, some overgenerous benefit conditions should be tightened up: (i) The financing of the costs of pension increments has to be stopped with the help of the new rent formula. (ii) The ‘collective social security systems’ must become contributory. (iii) Early retirement pensions have to be reduced according to sound actuarial principles.

On the other hand, the treasury should take on responsibility for redistributive elements within the schemes. It should (i) subsidise minimum pension provisions and (ii) directly finance the
deficient Comprehensive Social Insurance System. Today it is financed by other insurance schemes, although such cross-subsidisation contradicts the equivalence of contributions and benefits and is a disincentive for workers to enrol with the General Social Insurance Scheme.

Fourth, the NSIO should reform its administration: (i) streamline application procedures to make them more transparent for the insured, (ii) improve its customer orientation, (iii) fight corruption, (iv) enhance the monitoring of compliance and contribution deduction and (v) build capacities (train employees and managers and improve its information systems).

The medium-to-long-term reforms should be more comprehensive: As a first step, the provisions of the six insurance schemes should be brought into line. The schemes need not be unified, but all groups (high-ranking officials, military persons, employers, seasonal workers and the self-employed) should be treated like permanent workers according to the legislation of the General Social Insurance Scheme.

As a second step, a more comprehensive rebuilding can be taken into consideration by bringing the private sector in. A multi-pillar insurance system should emerge in which the existing public social insurance system would be supplemented by a second mandatory tier. Here the government could make use of the widespread occupational and professional pension schemes, transforming them into competing private defined-benefit funds, focusing on the income replacement needs of middle and higher income earners. Such transformation would free the public insurance system from some of its responsibilities and enable it to concentrate on (i) providing basic protection for all of the population by shifting income intertemporally from working life to old-age and (ii) fighting poverty through minimum pension provisions.
Only multi-tier insurance systems can balance out the different risks of private and public insurance providers: The NSIO suffers from all the weaknesses associated with public sector institutions: First, it is not really autonomous in developing the social insurance schemes and investing accrued funds. Second, it does not compete with other providers. Hence, there is no need for the NSIO to achieve high rates of return on funds. Third, the NSIO’s administrative and monitoring efficiency and customer orientation are weak. Private insurance funds, on the other hand, bear their own risks: investment in risky assets, concentration of investments, danger of fraud, deceit of customers.

**Increase in public social assistance spending**

Public spending on social assistance has to be increased, although this is a difficult task for a middle-income country like Egypt: Closing the entire poverty gap would require a social assistance budget of LE 1600 million (INP, 1998, p. 127; World Bank, 1991, p. 145). Strategies have to be developed to use all available resources in the best possible way:

First, *the government* could further reduce subsidy costs and use the funds saved to extend social assistance spending. Subsidies on petrol, electricity and oil can be abolished without any negative social impacts. The subsidies on bread, on the other hand, have a positive impact on secondary income distribution and should be continued as long as social assistance programmes do not reach the greater majority of the poor.

Second, *the different assistance programmes* must better co-ordinate and improve their targeting. Measures have to be taken to prevent individuals from drawing social assistance from different sources or from claiming assistance when they are entitled an insurance pension. One way is to integrate electronic information systems. *The NSIO* is already building up a com-
puter-based customer database. From now on, it is to record all households and file them by their ID number. Then the NSIO could give access to its database to all social assistance providers.

Third, the duplication of administrative machineries has to be rationalised: (i) The Ministry of Awqâf can close its social aid programme, as it benefits only its own employees. (ii) The MISA should reconsider the duplication of its own and the NSIO’s local offices. But the MISA could also consider copying the NSB’s successful experiment in cooperating with local Zakât-committees. It might initiate co-operation with local NGOs, which need no means-tests to assess claimants needs. They are in constant contact with the poor from their neighbourhoods and know how much assistance and what kind of assistance the people concerned need.

**Micro-insurance projects**

Egypt should not only focus on developing its public schemes but open new avenues to broaden the overall out-reach of the social protection system. To our opinion, the micro-insurance approach is recommendable to integrate the least well protected social group – urban informal sector workers. It bridges the gap between mutual support mechanisms and public and market-based protection schemes. The idea is not new but has been successfully tried in many countries and different world regions (Brown / Churchill, 1999).

Research in different countries has revealed, that informal sector workers are willing and able to deduct some part of their income for their own social protection. However, commercial insurers do not offer low-premium low-benefit insurance contracts that informal sector workers would demand. The reasons are twofold:
First, insurance providers face higher information problems when dealing with low-income groups: It is much more difficult for them to have an information informal sector workers living in squatter areas than about private or public sector employees registered with all administrative offices. So, commercial insurers do not know whether the potential client is insuring only after the damage (illness or invalidity) has already occurred (adverse selection). Moreover, low-income groups are more likely to be hit by social shocks (because of more hazardous living conditions) and they are more likely to behave carelessly once they are insured (moral hazard).

Second, fixed per capita costs do not allow for small-premium insurance contracts. The insurer has to market and conclude the contracts, distribute information, collect the premiums, verify insurance claims and pay out benefits. The costs of these transactions and their administration do not depend on the amount insured. If the amounts insured are low, costs may even exceed contributions collected, and thus the insurance company incurs losses.

Some NGOs in Egypt have already tried to bridge this gap in the insurance market. They were able to organise mutual insurance groups and to offer low-premium contracts. Transaction costs were low, because NGOs operate next to the low-income target group of these micro-insurance projects. Keeping the regular contact to their clients also enabled the NGOs to know their individual risks and to reduce the information asymmetries. Moreover, NGO workers are usually paid on a low-wage basis, and therefore administration costs were very low as well.

Nevertheless, the projects failed. The NGOs were unable to calculate the contribution-benefit ratio according to sustainable actuarial principles, to invest accumulated funds in a sound way and to sufficiently pool the risks among a high number of contributors. The NGOs’ micro-insurance schemes went bankrupt because benefit-contribution ratios were too high, because
the invested funds bore insufficient yields or because bad risks coincided with a hazard. In the end, the target group felt mistrust in NGOs without experience in financial affairs.

International experience suggests that micro-insurance schemes should be designed according to the ‘partner-agent model’, were the different tasks of insurance are divided between a distribution agent (an NGO, a labour union or a co-operative union) and a commercial partner (a public or private insurance company). Each of the parties is responsible for the tasks, where it is strong: The agent does the marketing of the product, the collection of premiums and the management of claims. In turn, the product design and the investment of accumulated funds is provided by the agent’s partner, which has the necessary actuarial and financial know-how of these tasks.

The success of the partner-agent model, however, is linked to three conditions:

1. The NGOs must be capable of collecting contributions and providing benefits.
2. The NGO must be stable, well known and active in a large area.
3. The potential insured persons must trust the NGO and its re-insurance partner.

In Egypt, the first condition is not given a priori. Few of the country’s NGOs have experience in financial affairs and this experience is limited to small credit schemes (LaTowsky, 1997). However, foreign donors can help to bridge this gap, by: (i) imparting the required actuarial know-how needed to calculate the contributions and benefits, (ii) assisting in formulating the contracts and establishing a detailed reporting system, (iii) training the NGO social workers, (iv) bringing interested NGOs into contact with interested insurance companies and (v) financing the starting costs. Co-operatives should be taken into consideration as well.
The second and third conditions are interdependent. The target group’s confidence increases when the NGO is considered stable and when the project starts up successfully. But few NGOs in Egypt are - at a given time - stable enough and well-known in more than one town. None of the country’s independent NGOs are active in a large region. There is a way to solve the problem: A network of regional NGOs could be established to take the place of the one big NGO. In negotiations, one of the NGOs would have to speak on behalf of the others, but all would directly co-operate with the commercial re-insurer. The weakness of this solution consists in its additional co-ordination costs. Its strength is that small NGOs usually have more intensive contact to their clients.

One might object that Egypt already has a comprehensive social insurance scheme, which is responsible (among other things) for the social protection of informal sector workers. One might argue that this system is very lucrative for the insured, as a payment of LE 120 only qualifies for a life-long pension of LE 63 per month. One might even ask why the poor should opt for a contributory micro-insurance system with low benefits instead.

We do not see that as a contradiction: First, the micro-insurance could insure currently non-covered risks (health, work injuries, widowhood...). Second, the comprehensive scheme’s benefits are below the poverty line and households might want additional pension insurance. Third, the possibility of a future linking of the NGO-private micro-insurance project to the public pension insurance should be taken into consideration: Egypt’s Comprehensive Social Insurance System is a hybrid between a social insurance and a social assistance programme. Contributions are collected, but they are too low to finance the benefits.

In Egypt, informal sector workers could be given the choice of enrolling either in the NGOs’ scheme or in the public scheme, both of them being subsidised by the treasury. This would
bring the state into the partnership between NGOs and commercial insurers. If the government wishes to redistribute to the poor it could do so by supporting micro-insurance projects run by NGOs. Such an approach has more than one advantage:

‘Organizations such as NGOs and co-operatives have a good understanding of the particular needs and priorities of their client groups... In the social field NGO action integrates the traditional social security measures with complimentary measures in the field of (primary) health care, child care, housing and targeted social action. In the economic field, more security can be achieved through self-help and self-employment.” (van Ginnecken, 1990)

Notes

1 Some of the figures quoted in this article are a little out of date. The most recent data are often not available from a country like Egypt, when they exist at all. Here, figures are meant to illustrate and old figures are only used, where substantial changes are not likely to occur within a couple of years.

2 Due to limited space, this article concentrates on public protection systems. For an analysis focussed on informal and private social protection systems, see: Loewe 2000a.

3 The basic salary is all regular labour income up to LE 525 a month; the variable wage is made up of all regular labour income from LE 525 to LE 1025 and all one-time compensations.
4 E.g. Loewe et al. (2002) found the majority of Jordan’s urban sector workers ready to contribute pay a considerable share of their income for health, life or work-disability insurance.
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