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Privatization and Exclusion

"The truth is that we have simultaneously too much state and too little state," writes Brazilian political theorist Joao Guilherme Merquior in describing his homeland but capturing the dilemma facing reformers in many developing countries.[1] As the Egyptian and Mexican cases show, state withdrawal requires state intervention. While withdrawing the state from some activities, reformers must redeploy other state institutions to enlist the private sector's backing and cushion the popular classes, a daunting challenge that requires strong interventionist capabilities and windfalls of revenue, both of which are increasingly scarce in a world economy where development aid is declining and the reigning discourse of neoliberalism is patently anti-statist.

Mexican reformers accomplished this task, overseeing one of the most far-reaching economic restructuring programs ever. De la Madrid and Salinas carried out extensive reforms, liberalizing trade, selling off much of the public sector, fundamentally changing property rights in rural areas, altering church-state relations, and liberalizing the financial sector, but, to insure the support of business and the popular classes for these measures, they introduced political reforms and created institutions that provided business with rents and subsidies and labor with more benefits, candidacies, and channels for demand making. Egypt won praise in the late 1990s for its privatization program, but labor opposition eventually brought the process to a halt. The question I have addressed is, Why were Mexican leaders able to overcome the opposition of a labor movement that was larger and more organized and whose electoral support was crucial to regime stability, while their Egyptian homologues were unable to override the opposition of a smaller, less militant, historically docile labor movement?

I have argued that the Mexican state enjoys a higher administrative and political capacity. Since incorporation, the Mexican state was a mediated state, controlling the popular classes through PRI-affiliated rural and labor elites. In Egypt, the regime also used the rural middle class to rule the hinterland, but in urban areas the regime has historically lacked control, preferring the departicipation of urban masses and relying on the cooperation of labor bosses to deliver benefits and insure the docility. Since incorporation, the bargain struck between the Mexican state and the popular classes—electoral support in exchange for benefits, representation, and the right to strike—was fundamentally different from the Nasserist bargain, which did not grant the right to strike and extended benefits in exchange for social peace. These differing bargains produced different state structures.

Moreover, labor in Mexico was mobilized and incorporated into the ruling party, and the PRI was a crucial institution for distributing patronage, representing interests, and co-opting opposition. The Egyptian regime, on the other hand, from its founding moment, used the state bureaucracy (and later the public sector) for political control. The brief flirtation with "popular participation" in the Liberal Age (1930s–'40s), was seen as a cause of the ancien régime's corruption and the failure to liberate Palestine in 1948. Nasser banned political parties and cut off all ties between labor and the Wafd, Muslim Brotherhood, and Communist Party, which had considerable support in poor working class areas. The Free Officers proceeded to follow a strategy of departicipation for the popular classes; the aim was to demobilize and depoliticize the lower classes, particularly in urban areas, so as to prevent their capture by the Communist Party or the more threatening Muslim Brotherhood movement, which had posed the greatest threat to the Free Officers. The state would thus develop few institutional linkages with organized labor other than the Labor Ministry, which delivered benefits and oversaw trade union elections, and a crop of elite unionists, whose duty was to control (not represent) the rank and file. Nasser would set up a series of single parties but would eventually dismantle them. Sadat would build the National Democratic Party but, fearing labor's mobilization, would cut off all ties between the ruling party and the labor confederation.

When the adjustment process began, Mexican state elites would use their numerous levers of control over labor—through the PRI and state bureaucracy—to gain workers' support for privatization. State elites initially relied on their traditional intermediaries and power brokers in the labor movement and rural areas (*charros* and *caciques*) to override labor resistance. But this strategy proved ineffective after the 1986 and 1988 elections when the PRI did very poorly in urban working class areas and rural areas. Realizing that top-down reform measures needed popular-level support, Mexican reformers went directly to the base, targeting lower-level unionists, the rank and file, and other unincorporated popular groups and enlisting new political intermediaries. The Egyptian state lacks the institutional ties to societal actors and control mechanisms of the Mexican regime. The Egyptian regime exemplifies the World Bank's "remote and imperious" low-capacity state that is unable to mobilize public resources and use them efficiently or effectively.[2] The ETUF elite have not been able to deliver labor's support or quiescence for privatization. The NDP lacks the reach and popularity to gain the backing of the lower classes, and the regime is facing a coalitional vacuum. The political apathy that Nasser aimed for has calcified, as the popular classes still believe that they should abstain from politics in exchange for welfare benefits. And if Mexican leaders could in crisis go directly to the base or work through pro-reform allies, the Egyptian state is not so able. Despite recent reforms, the NDP still lacks the PRI's reach, legitimacy, and institutional carrying capacity. No Egyptian ruling party has ever been able to reach all the way down to the lowest levels of the trade union hierarchy.

The Egyptian regime has historically relied on the rural middle class to deliver the rural vote, but in urban areas the regime's isolation was and still is striking. In moments of crisis, the Egyptian state revitalizes its alliance with the rural middle class and may extend some benefits to disgruntled urban groups, but this strategy has not succeeded because austerity measures have cut back welfare guarantees and fundamentally violated the Nasserist bargain. Lacking other intermediaries and with much of the population unincorporated, Mubarak is trying different support-mobilization strategies. Attempts to co-opt Islamist notables, who provide public goods in popular areas, are failing. The current coalitional strategy appears to be using the ruling party to gain the support of the propertied classes—big business and landed elites—and slowly integrate pro-reform Islamist groups into the parliamentary system while excluding the more populist groups that could jeopardize the neoliberal project. As the NDP becomes more of a party for middle class and business interests, labor's importance will recede, and its veto power will be reduced. A strategy of exclusion however risks mass violence on the scale of the Chilean or Algerian experiences. The reformers who triggered the least violence in Latin America were those that rebuilt their party systems to include labor, at least partially through the granting of political voice and benefits.

Corroboration from Latin America

An examination of privatization in Latin America reveals that the states that have gone farthest in reforming their public sectors—Mexico, Venezuela, and Argentina—were all cases of party incorporation where reformers used long-standing party-labor links or restructured parties to solidify their urban base. For example, after 1989, Venezuela privatized extensively.[3] The Democratic Action Party (AD) had dominated the Confederation of Venezuelan Workers (CTV) since the 1940s, and, although in May 1989 during the privatization process the CTV joined other confederations in an anti-reform strike and came close to breaking their alliance with the governing party, the AD was ultimately able to retain the CTV's support passing a law enhancing worker rights and union privileges. The AD's institutional capacity—"organic ties to individual unionists"—and granting of candidacies to compliant labor leaders at all levels proved crucial in maintaining labor's support.[4] Argentina, like Mexico, was able to privatize broadly only after rebuilding the Peronist Justicialista Party, and developing a strong urban base of support. Like Nasser, Peron had banned political parties upon assuming power. The "poorly institutionalized nature of the party-union linkage," some have argued, allowed Argentine reformers to restructure the Peronist party, building territorial and urban-based networks that sidestepped unions and delivered patronage directly to urban working class and the unemployed underclass.[5]

Interestingly, the Latin American states that historically granted workers the right to strike were better able to "deliver" labor than those states that criminalized striking, such as Chile and Brazil. Chile, a case of state incorporation, privatized extensively but only by brutally repressing labor for two decades. Brazil, the other prominent case of state incorporation, is still struggling to reform the state and economy in face of labor opposition. Scholars have noted the similarities between Nasser's state and the Egyptian labor code and Vargas's Estado Novo and the Brazilian labor code, a code that was considered to be the "purest form of corporatism" and was imitated by Spain and Portugal, also countries that Nasser looked to during the state-building period. As in Brazil, where the state to this day is known as a *cabide de emprego* (source of jobs), successive Egyptian leaders would use the state bureaucracy to provide employment for every university graduate and as the main mechanism for support mobilization and control.

In Brazil, like Egypt, despite much rhetoric, privatization has gone forward haltingly, and various observers have attributed this to the country's weak parties and inchoate party system. Haggard and Kaufman have argued that countries with fragmented political systems—as opposed to an institutionalized two-party system or dominant-party system—have the most difficulty retaining labor's support during the adjustment process.[6] Since incorporation, Brazil has lacked a party to mediate state-society relations. Brazil's military regimes during the 1970s and 1980s failed to develop institutional mechanisms linking state to society, and in 1989 the country would emerge as a fledgling democracy with a fragmented

party system, prompting some to describe Brazil as a "unique case of party underdevelopment."[7] Since the democratic transition, the Brazilian president's base has rested on a tenuous coalition of parties, some of which draw support from trade unions staunchly opposed to privatization and could bring the government down if the president attempts divestiture. Recently, Javier Corrales argued that it is Brazil's "state-without-party" condition that has prevented successive presidents—from José Sarney to Henrique Cardoso—from pursuing reform; Cardoso was forced to shelve plans to privatize the state-owned oil company because of lack of support from his ruling party and a strike by the leading labor union.[8]

Algeria

It has been argued that that the weakness of the Arab state is critical to understanding the lack of democracy in North Africa and the Middle East.[9] I believe that state weakness can also help explain the region's troubled experiences with economic restructuring. In North Africa and the wider Arab world, Algeria has gone furthest in implementing market reform, extensively restructuring the public sector and earning plaudits from IFIs for adjusting faster and further than Egypt and other regional pupils of the IMF. Because the Algerian story is also one of colonial legacies, state corporatism, and rentierism, it can serve as a useful foil for understanding the Egyptian case (and can offer a cautionary tale for Egyptian reformers about the perils of rapid reform or an alliance with neoliberal Islamists). The Algerian experience is worthy of note because the Algerian state was even more isolated than in Egypt and yet managed to radically transform state-society relations. Faced with resistance from the FLN, public sector managers, and labor, rather than reform the ruling party or try to gradually build pacted support, Algerian reformers rammed through with reforms eviscerating the public sector, building alliances with new political intermediaries, and shoring up the regime's capabilities and social base. To understand the origins of this reform strategy, it is necessary to examine the founding moment of the modern Algerian state.

Algeria's postcolonial regime came to power in July 1962 following a revolution, the eight-year war of independence against French rule. As in Egypt, despite the presence of a revolutionary party, the popular classes were incorporated into the party-state apparatus and granted myriad welfare benefits—free health care, education, public transportation, housing, subsidized foodstuffs, and even employment—so that many Algerians christened their government the "providential state." Labor and the peasantry were economically included but politically excluded; worker and peasant organizations had little say in policy making and were expected to offer quiescence and ideological backing—not electoral support. The General Union of Algerian Workers (UGTA) founded by the wartime FLN in 1956 would at independence be placed under the control of an institutionally undeveloped single party and expected to maintain docility and support the party line. At independence, the Algerian working class was very small, numbering 110 thousand urban industrial workers. (Some historians note that the 400 thousand Algerian migrant workers in Europe were better organized than their counterparts back home.) When Ahmed Ben Bella, the prestigious figurehead of the revolutionary regime (who played a similar role to General Naguib in Egypt), tried to encourage independent power centers and to bring the army under control, Colonel Haouri Boumedienne removed him from power.

When Boumedienne assumed power in 1965, he abolished the National Assembly, the Political Bureau, and the Central Committee of the FLN, establishing a highly centralized state apparatus ("bureaucratic dictatorship") and transforming "the single party into a powerless, parallel and inert administrative apparatus."[10] The FLN would emerge as a club of elites—military rulers and their clients—who would divvy up property confiscated from the departed French colons and land expropriated from landowners. Unlike Egypt, which had elections on and off with the Arab Socialist Union and tried to organize the lower classes, there was little electoral competition in Algeria, and the ruling party never developed the institutional capacity to mobilize workers and peasants for elections, channel participation, or manage inter-elite conflict. In 1967, Boumedienne dissolved the national secretariat of the trade union federation. He announced plans to develop political institutions—the FLN regularly proclaimed the "year of the party" and its own reorganization, but the party was never restructured, neither before nor after oil revenues began flowing, and Boumedienne died suddenly in 1978 before his revised blueprint for the FLN and various ancillary structures could be implemented. Despite the FLN's revolutionary aura and populist appeal, the party would remain an undeveloped shell of an institution.[11]

Although rentier theorists have argued that it was Algeria's access to oil rents that afforded the state such autonomy and allowed it to purchase popular acquiesce through a generous "preindustrial welfare state," recent scholarship shows that the postrevolutionary state's institutional weakness and isolation—a lack of intermediaries, which became starkly evident when the regime tried to reform the economy in the late 1980s—can be better understood by examining the disruptive effects of French colonialism. By this account, it was not oil revenue that stunted Algeria's institutional capacity but French colonialism, which thwarted the emergence of any viable Algerian intermediaries and the subsequent struggle for independence, which further decimated Algeria's intellectual and propertied elites. At independence, Algerian elites were largely exiled or discredited by association with the colonial power, and there were few power centers in civil society or leaders with mass following that the new regime could work with. As Clement Henry writes, "Algeria's institutional weakness was born in 1962, before the oil from Hassi Messaoud started to flow in significant quantities . . . The original sin then was not the 1956 discovery of oil, but the 1830–31 French invasion of Algeria and the subsequent destruction of the Ottoman governing infrastructure." Noting that "rentier theory, fixated on extraction capabilities and volatile petroleum revenues, cannot explain the pathology of bunker states [like Algeria]," Henry argues that such an approach "tells us little about rent-seekers or about institutional development and decay." Moreover, underlining the importance of disaggregating different state capabilities, Henry notes that Algeria in fact imposed high taxes in the 1960s and 1970s, and, "even if the assumption is correct that oil riches diminish a state's ability or willingness to tax, it is not clear if or how overall institutional capacity decays without an impetus for extraction."[12]

The lack of mediating institutions or social groups meant that the collapse of oil prices in 1986 had a devastating impact on the lower and middle classes. This fiscal crisis would lead to economic belt-tightening and a retrenchment of social services and would unleash urban riots in 1988 and prompt attempts at simultaneous economic and political reform. Earlier proposals to "decentralize" the public sector had been torpedoed by state elites, including members of the Securité Militaire, whose networks dominated the state monopolies. In 1989, Prime Minister Mouloud Hamrouche's reform team put forth an economic reform package that would eliminate monopolies, liberalize prices, and establish a framework for each public enterprise, including the banks, to operate as an independent enterprise responsive to market forces. As with Egypt's Law 203, which set up holding companies, in Algeria a similar system of state-holding companies was introduced in 1988 to replace the supervision of public sector enterprises by parent ministries. Each enterprise was to be released from its parent ministry and given the freedom to operate in partially deregulated markets. The state, however, lacked the administrative capacity to supervise the holding companies, and these reformist technocrats did not have broad societal support. Despite pro-reform legislation from the newly elected parliament, privatization was actively opposed by party officials, public sector managers, and labor, but the reformers enjoyed the backing of the president, Chadli Benjedid.

The reformers within the regime also had the tacit support of the Islamic Front of Salvation (FIS), which, like the Egyptian Brotherhood, controlled nine thousand mosques and a vast network of welfare, recreational, and educational associations and had repeatedly called for economic liberalization. The FIS leadership saw Algeria's economic predicament as part of the country's overall moral crisis, and the movement's "economic doctrine" had strongly attacked Algeria's centralized state economy as "discouraging the spirit of initiative . . . in favor of mediocrity and incompetence . . . [and] penalizing small enterprises." The FIS's economic program called for limiting state intervention in the industrial sector and protecting private property but also "watching that the latter not be transformed into a monopoly infringing on the public interest, for this would be an open door for economic, political and social parasitism."[13] Regime reformers and the FIS began to discretely and strategically work with each other. By pursuing political liberalization, the reformers allowed the FIS to formally enter the political arena, and, by vanquishing the FLN in the municipal elections of June 1990, the FIS discredited the regime's anti-reform hardliners and strengthened the reformers' hold over the FLN-dominated parliament.

But this curious collaboration between "moralizers" and "globalizers" would not last long. The alliance between regime reformers and the FIS and the attempt at simultaneous political and economic liberalization threatened to tear the regime apart. FIS leader Abbas Madani's call for a general strike in 1991 prompted military leaders, threatened by economic reform, to force President Chadli Benjedid to declare a military emergency, even as the strike was fizzling out. The reform government subsequently resigned, and, when the Islamist opposition resorted to violence, the junta behind Chadli adopted repressive counter-insurgency tactics and used the pretext of maintaining security to gain a free hand politically and economically. The fiscal crisis had severely constrained the regime's capacity to quell urban unrest; the attempted political opening was after all a way to appease disgruntled social groups and broaden the regime's support base. As the political violence escalated, many observers thought the Algerian regime was on the verge of collapse, and some have since argued that it was access to external rents that saved the state. A sharp dip in oil prices and a looming balance of payments crisis led the regime to sign an agreement with the IMF in 1993, which brought debt relief and by 1995 delivered the funds necessary to redouble the military's counterinsurgency efforts and roll back the Islamist guerillas.[14]

With the outbreak of the civil war, structural adjustment proceeded rapidly. The IMF reported that Algeria "adjusted faster" than other Arab states—Egypt, Jordan, Morocco, and Tunisia—that had embarked on reform earlier, and its macroeconomic performance had "equaled or even surpassed" them by the end of 1996.[15] Privatization also proceeded swiftly. As in Egypt, more public-private ventures appeared. If the 1992 investment law had permitted majority foreign investment in the non-hydrocarbon sector, the privatization and investment code of 2001 did away with the old distinction between foreign and Algerian investment and allowed foreign majority holding in the hydrocarbon sector as well. After the IMF agreement of 1994, SOEs were subjected to more stringent budgetary constraints. The subsequent restructuring eliminated hundreds of SOEs—by April 1998, some eight hundred had been privatized or dissolved—and threw an estimated 450 thousand workers out of work. In the construction sector alone, 93 thousand workers were laid off between 1995 and 1997. Another scholar estimates that privatization reduced the public sector labor force in the nonoil sector by half.[16] Organized labor simply could not block the divestitures. The UGTA organized waves of strikes against privatization and loudly opposed new legislation meant to facilitate public sector reform but ultimately to no avail; at the height of the civil war, the regime forged ahead prevailing over all opposition. As one analyst wryly noted, "With hundreds of enterprises closed down, the unions cannot be said to have been particularly powerful."[17]

The restructuring undertaken by the military junta dissolved hundreds of SOEs but also created scores of joint ventures—introducing a new mixed economy and concentrating wealth in the hands of state elites and their new clients. Some analysts think that public-private arrangements may have become the norm, the preferred property regime and method of control for the Algerian state: in 2000, a World Bank report noted that "after a decade of restructuring public enterprises, at an estimated cumulative cost of some DA840 billion (US$21 billion equivalent) and some 450,000 jobs, Algeria's privatization program has not yet resulted in a single sale of corporatized public enterprises to outside private interests."[18] By the late 1990s, writes Dillman, Algeria boasted "a liberalized economy operating through a circulation of rent between the military, a deficient public sector and a largely commercial private sector."[19] The privatization process in Algeria was also singularly "opaque," benefiting businessmen tied to the military, and would eventually engender a new class of economic actors and societal power brokers that would serve as the regime's new intermediaries. Privatization strengthened not only a coterie of state officials—and capitalists tied to the military—but also local notables ("emirs") who were able to exploit newly privatized sectors (shipping, *trabendo*) and expand their local authority. The state began to outsource its own fighting of the war to these local notables and their proxy forces; preferring to keep the Algerian army small, possibly to prevent Islamist infiltration, regime officials outsourced counterinsurgency to village defense forces and after 1997 to Islamist militias.[20] These new allies and proxy forces benefited from the adjustment process; various analysts have noted that all the groups involved in the Algerian civil war had a keen interest in the fate of the public sector.[21] One analyst observes that the more political violence intensified, the faster privatization occurred, noting that the Armed Islamic Group (GIA) frequently targeted unprofitable state-owned enterprises, and the most "exposed" state companies (e.g., transport) were often privatized following GIA attacks—suggesting that Islamist power brokers had an interest in privatization and were working with elements in the Algerian state.[22]

The Algerian experience shows that even reformers within a "bunker state" need allies. The adjustment process in Algeria, carried out with brute violence, restructured the economy and allowed the state to in effect create new social groups—local rural elites and urban capitalists—who benefited from the new market opportunities and have emerged as the regime's middlemen. The Algerian state has emerged—post-adjustment and civil war—as less isolated than it was before, and even the FLN has gained popularity, with many voters thinking it can govern better than the Islamists. Under the leadership of Prime Minister Ali Benflis, the FLN has moved away from its old ideology of populism and third worldism, now emphasizing economic development and winning 199 seats in the May 2002 parliamentary elections and performing impressively in local elections the following October.[23] But the adjustment process inflicted massive suffering and violence on the Algerian people. In addition to the one hundred thousand victims of the civil war, wages and living standards fell sharply. One study reported that 35 percent of the Algerian population lives in poverty, and unemployment continues to hover at 30 percent.[24] Between 1990 and 1995, over four hundred thousand Algerians emigrated, including tens of thousands of professionals and managers.[25] Algerian expats now hold an estimated thirty-five billion dollars overseas.

The Algerian story offers several lessons for Egypt. First, the Algerian case demonstrates that rents do not necessarily prevent reform and do not automatically preserve the political and economic status quo; external revenue subvented a fundamental transformation of state-society relations in Algeria. More importantly, Algerian reformers were faced with an institutional setting shaped by the country's colonial and postcolonial struggle, and it was only through mass violence that they were able to overcome these historically constructed obstacles and entrenched interests. Egyptian commentators across the political spectrum point to Algeria's violence to emphasize the importance of gradualism, dialogue, and institution building, warning Egypt's more ardent reformers of the perils of "shock therapy," exclusion, and repression. Better to peacefully integrate the Islamist opposition as in Turkey than attempt a rapid liberalization only to have

to resort to drastic exclusion once the political opening fails. But analysts are also aware that the Egyptian state has more mechanisms and social actors to work with than its Algerian counterpart.[26] Unlike their Nasserist predecessors, Egyptan state elites today are aware of the importance of participation—that, as Amartya Sen says, "the need for popular participation is not just sanctimonious rubbish" but is crucial to successful development. The challenge is how to incorporate broad sectors of society, when the regime is lacking participatory institutions and when the lower classes are mobilized by a formidable Islamist counter-elite, which could block neoliberal reform.

The "rediscovery of the market" seems to have led to a "rediscovery of the state." Political economists now acknowledge that the Washington Consensus's desire to reduce state activity often led to the cutting back of state capacity across the board, and many now recognize the need to unpack the different dimensions of "stateness" and to show how they relate to economic development.[27] By the end of the 1990s, scholars were also aware that external IFI conditionalities and adjustment programs can erode a state's capabilities, allowing a leader to cut back on the provision of welfare (in the name of reform) while expanding the scope of the neo-patrimonial state by reconfiguring patronage and rent-seeking networks[28] and reconstituting the state according to a new political calculus. Markets cannot function well without a state that can formulate and implement the required policies, administer services, and respond to the demands of the citizenry.

Over five decades ago, in *The Great Transformation*, Karl Polanyi warned of the importance of "embeddedness" and social mediation in the transition to a market economy and cautioned how socially unmediated transitions where the individual is not protected from the vagaries of the market produced deep crises and led to the rise of extremist movements in Europe. Egyptian reformers seem aware of the importance of state intervention; they are pursuing a party-mediated economic restructuring and courting the support of influential social actors in economic transformation. But a key difference between the Mexican and Egyptian experiences was that market reform in Mexico was accompanied by the extension of rights and benefits to select groups in the lower classes, while in Egypt divestiture has entailed the withdrawal of rights and benefits to groups most impacted by market reform. To peacefully shift to a market economy as in Mexico, the Egyptian state needs to put in place a more inclusive pact, a new class compromise that will give voice and rights to the lower classes. Given the polarization between the Egyptian state and Islamist opposition, it is not clear if a coalitional strategy that excludes the lower classes will lead to peaceful reform and depolarization, or more repression, further polarization, and a resurgence of political violence.