Uncovering Egypt’s Slush Funds

The government’s efforts to attract foreign investments are at odds with such lack of transparency and accountability.
Business Today Egypt interviewed Jeremy Hodge and Nizar Manek, co-authors of ‘Opening the black box of Egypt’s slush funds,’ a much-discussed Angaza File investigation for Africa Confidential newsletter, a specialist publication on Africa published since 1960. Manek and Hodge spent around a year investigating Egypt’s extra-budgetary ‘special funds,’ finding that at least USD 9.4 billion of state revenues were plundered and used to make unaccountable payments to Egypt’s bureaucrats in the fiscal year that ended when Abdel Fattah Al-Sisi became president, and can be used to fuel regime patronage networks. Manek and Hodge’s inquiries shed light on the systematic abuse of special funds, the individual actors implicated in various misappropriations along the way, and how foreign companies, investors’ funds, and financial aid flowing into Egypt from international donors can become entangled in the web of special funds.

Manek and Hodge’s report considers the debit and credit activity – inflows and outflows – of Egypt’s special funds. The journalists noted in an interview with Business Today Egypt that alarming discrepancies exist between the figures put forth in the financial records they were able to review and public statements made by Egypt’s Ministry of Finance, Central Bank, Central Auditing Organization (CAO), previous parliaments and other senior government officials over the total size of Egypt’s ‘special funds.’ The pair, who were forced to flee Egypt shortly after they began their investigations, told us they corroborated the figures in the official records they reviewed and cross-checked facts by talking with people close to the relevant ministries, regulators and people in the bureaucracy with insider knowledge.

“In the 2010/2011 fiscal year, the amount of annual revenue these special funds took in was USD 14.1 billion, according to internal Central Bank records, but appeared to drop USD 4.7 billion to USD 9.4 billion by the 2012/2013 fiscal year, according to records from Egypt’s CAO that are based on financial information received from the Central Bank and Finance Ministry,” said Hodge. “By August 2014, the Finance Ministry under Sisi’s Finance Minister, Hany Kadry Dimian, publicly claimed the total size of special funds was USD 3.8 billion, however didn’t specify whether this was an estimate for a year-end balance or annual credit activity. This begs the question: what happened to the remaining USD 5.6 billion? There are lies, damned lies and statistics… then there’s highly idiosyncratic Egyptian budgetary accounting,” Hodge affirmed.

“But just as Sisi has issued a presidential decree enabling him to sack heads of ‘independent’ regulators at will, in defiance of his own military-backed constitution, the head of the CAO, Hisham Genena, has given an interview to Al-Ahram, claiming that a total of 70 billion Egyptian pounds had been squandered over the last fiscal year,” Manek continued.

“In other words, approximately EGP 66 billion (USD 9.4 billion) – an equally massive amount as during the 2012/2013 fiscal year – has been lost as a result of corruption in the first fiscal year of Sisi’s presidency, according to Genena. Although Genena never specified the way in which this EGP 70 billion was squandered, the fact that this figure is so close to the number put forth in our own investigation (EGP 66 billion) could mean that he is referring to special funds,” Manek explained.

Al-Sisi administration keeps shtum

Since the publication of their report, the pair said they have neither received nor seen any direct public response by Egypt’s government or any other public statements from any other officials within the Ministry of Finance or Central Bank regarding the size of special funds commenting on the accuracy of their findings. “Egypt’s government has so far failed to provide a credible and transparent official valuation of the size of special funds, while the country’s four-year anti-corruption strategy (published last December) – which makes brief mention of the need to reform special funds – doesn’t task any specific department with valuing their size. For a government serious about sorting out such a unique mess, coming up with an honest valuation of the funds’ size would be an important starting point to determining what discrepancies exist, where state money has been diverted to, and into whose pockets.”

In Morsi’s legislative shadow

In a recent interview with the Carnegie Endowment, Manek and Hodge made reference to a public budget law passed by the Muslim Broth-
erhood-controlled parliament in 2013, which required that the state appropriate 10% of all total revenue coming into special funds.

Business Today Egypt asked the pair for more details, and whether the Ministry of Defense (MOD) and Ministry of Interior (MOI) could be said to have hindered the purpose of that legislation. “The law was passed in 2013 but was the public budget law for the 2013/2014 fiscal year,” said Manek. “Insofar as they helped depose ex-President Mohamed Morsi on July 3, 2013, yes, the army and police had an effect on that particular piece of legislation’s implementation. The ousting of Morsi led to the disbanding of the Muslim Brotherhood parliament which passed that budget law, leaving no-one to enforce it during the 2013/2014 fiscal year,” Manek clarified.

According to their findings, no other government bodies in possession of special funds made any effort to transfer any of their revenues from special funds to the Ministry of Finance, Central Bank or Treasury during the 2013/2014 fiscal year, notwithstanding their obligation to do so under Morsi’s public budget law. “But most of what Morsi and the Brotherhood-controlled parliament did during their rule was rendered null and void as a result of the military putsch,” Hodge noted.

Monetary stability... What monetary stability?
The two reporters said that by the end of the 2010/2011 fiscal year, nearly USD 1 billion in foreign currency was held in a series of special funds existing within the Central Bank of Egypt (from US dollars, pounds sterling and Euros to Saudi riyals, Kuwaiti dinars, Japanese yen, Swedish krona, Danish kroner, Swiss francs and Emirati dirhams). The fact that this foreign currency was held in special funds suggests that Egypt’s official estimate of its total foreign currency reserves did not include this USD 1 billion amount, they said.

In any case, if the government estimate did account for this reserve of USD 1 billion, then this may raise three questions, Manek elaborated: Why didn’t the Central Bank use these funds to help stave off a balance of payments crisis? Why did the Supreme Council of the Armed Forces authorize a USD 1 billion foreign currency loan to the Central Bank in late 2011? And why did the Central Bank feel obliged to accept this payment?

“But other than the USD 1 billion figure, and the information we have regarding aid and loans, it is hard to value the exact amount of foreign currency slushing about in special funds,” Manek continued, “without this certainty, it is difficult to extrapolate the exact effect that the incorporation of special funds into Egypt’s Central Bank reserves would have on price stability (monetary stability being a particular responsibility of central banks).”

Hodge added further that it is conceivable that special funds may well have been used as a tool for officials and businesspeople closely associated with the state to facilitate illegal capital flight out of the country in the days following the January 25, 2011 uprising, which did much to hurt confidence in Egypt’s economy (with business operations scaled back significantly) and likely also affected its trade
balance, and, in turn, monetary stability.

“Many point to the potential for reining in of special funds to help put a cork on Egypt’s spiraling budget deficit (civil service salaries, official and unofficial, form a substantial part of government expenditure), and say that this could eliminate one driver of incentives for the government to continue increasing the rate at which it prints money, causing inflation and the devaluation of the Egyptian pound. It is more complicated than this, however,” Hodge said.

Military-industrial wheeling and dealing

Following Egypt’s recent high-profile investment conference in Sharm El-Sheikh, which attracted dozens of heads of states and investors from around the world, Manek and Hodge’s findings appear particularly significant. Manek told Business Today Egypt there is evidence that the Suez Canal Authority (SCA), which is associated with major investment projects, has special funds. “If the SCA-controlled special funds follow the usual trend, then it is likely that their spoils will be treated as economic rent to be carved up between SCA’s ranking staff and other influential stakeholders. We don’t, however, have evidence to suggest that the SCA is any more of a front for backroom deals than any other body within Egypt’s government.”

The Arab Organization for Industrialization (AOI) has a unique history in Egypt, which many Egyptians, Egypt watchers and investors interested in Egypt may not know about. So Business Today Egypt asked Manek and Hodge to give us a more detailed background on what the AOI is. Hodge said: “The AOI is a treated as an ‘economic authority’ according to the Central Bank records we have reviewed, along with the SCA, Egyptian General Petroleum Corporation and others. The AOI began as a joint military venture between Egypt, Saudi Arabia, Qatar and the United Arab Emirates in the aftermath of the 1973 war as a means of presenting a united front against Israel. It enabled joint economic cooperation between the four countries, allowing for its board members (whether Egyptian, Saudi, Qatari or Emirati) to establish bank accounts in any of the four countries, that would be used to fund military production within factories. In 1976, a series of laws were passed in Egypt protecting these accounts from oversight from auditing authorities and from taxation by the state. Members of the AOI were granted the status of diplomatic immunity and protected from prosecution, even if they were nationals living in their own country.”

“In 1976, a now declassified United States National Intelligence Board National Intelligence Bulletin report described the first AOI Chairman Ashraf Marwan as a ‘brash wheeler-dealer in his early thirties with a well-deserved reputation for corruption,’ with senior Egyptian military officers increasingly resentful of the then presidential advisor’s involvement in military purchasing activities, and the fact that they often had no control over his purchasing choices. Marwan, who in 2007 fell to his death from a balcony in London in mysterious circumstances, had become something of a political issue in his own right within Egypt because of his reputation for using his business transactions to line his own pockets, according to the bulletin. Then, after Egypt’s peace treaty with Israel, the Gulf countries declared the AOI and its funds liquidated, but after Egypt’s refusal, it continued to operate as an exclusively Egyptian entity. Still, the same protections were
afforded to its members,” Hodge continued. “In 1980, Sadat attempted to amend the laws protecting the AOI, in order to be able to tax its revenues, but, as we reported, a local military affairs expert told us these amendments were never put into practice. A year later Sadat was assassinated. The same person told us that the AOI is still able to establish overseas bank accounts holding foreign currency. It’s notable that during the course of a legal dispute between a British aerospace company and the AOI (Westland Helicopters v. Arab Organization for Industrialization [1995] QB 282) that the Egyptian government operating through the AOI claimed to be the ‘true owner’ of deposits at six banks with offices in London,” Manek added.

Manek told Business Today Egypt that the AOI quickly became central to Egypt’s military-industrial complex, operating its own factories and companies. “The military controls all AOI operations, however we do not know the full extent of its budget. We do know that the AOI controls a dozen factories, which produce military hardware including aircrafts, armored vehicles, engines and spare parts for aircrafts (including the Jumhurriya, Cairo 200, Cairo 300 and K-8E models), tanks and armored vehicles, missiles, 122mm artillery, RPGs, mine detection technology, anti-aircraft weaponry, helicopters, drones and Malyutka and Swing Fire anti-tank missiles. As tensions between Egypt and Israel simmered down, the AOI expanded into the civilian sector as well, producing polyethylene pipes for export abroad, gas pipes, fiberglass products, electricity generators, internal engines for metro cars and trains, GPS navigation systems, metro and tram cars, water purification and desalination stations, chlorine cylinders and water sterilizing filters for apartment buildings.”

Anti-corruption strategy chicanery
Hodge said the text of Egypt’s National Anti-Corruption strategy, in the form it took when published in December, cannot be read in a
vacuum, and outside of the prevailing political environment. “The body it tasks for being primarily responsible for its implementation, the National Coordinating Committee for Combating Corruption, is staffed almost entirely by the heads of Egypt’s most unaccountable institutions, such as the Ministry of Interior, or at the very least institutions that most people would recognize have no business monitoring domestic corruption, such as the General Intelligence Directorate or Mukhabarat intelligence service. Meanwhile, bodies whose mandate is to monitor corruption are now all at the mercy of Al-Sisi and his office, as a result of his latest presidential decree this month.”

Further, Hodge added that one of the bodies represented on the National Coordinating Committee for Combating Corruption, the Central Auditing Organization, is actively investigating other bodies that are also part of the committee, including the Interior Ministry, Public Prosecutor, Ministry of Justice and others. “The strategy almost comically discusses at length the need to ‘strengthen the role of media and civil society to act as a check against the government’.” The European Union may also have a stake in the effectiveness (or not) of Egypt’s new anti-corruption strategy, according to Manek, who points out that Egypt has been one of the main beneficiaries of the European Neighborhood and Partnership Instrument (ENPI). They pointed Business Today Egypt to a public 50-page report by the EU’s expenditures watchdog, the European Court of Auditors, which says that an ENPI anti-corruption project was launched in 2011 with an objective to produce an anti-corruption strategy, and therefore argue that “its viability, implementation, and ultimate effects may be of direct concern to the EU. The same EU audit watchdog report (‘EU Cooperation with Egypt in the Field of Governance,’ Special Report No. 4, 2013) appears to suggest the EU was involved in funding the Al-Sisi administration’s anti-corruption strategy.

On Al-Sisi’s new decree allowing him to fire regulatory chiefs

When asked by Business Today Egypt about the decree issued by Al-Sisi this month (giving him carte blanche to dismiss officials from institutions concerned with monitoring state bodies), Hodge said: “It means that Al-Sisi now has the right to fire the heads of regulatory agencies whom he deems to be a threat to the stability of the regime, or as he puts it, ‘national security,’ which could very well include those who are looking into corruption within special funds.” “Yet, it should be noted that in some autocracies or military regimes, anti-corruption campaigns are themselves used as a means to target political opponents, enemies and rivals, Hodge continued. “We believe one of the reasons CAO Chairman Hisham Genena – soon expected to be impeached by Al-Sisi, if the latest public statements of Al-Sisi’s new Justice Minister Ahmed Zind are anything to go by – was so vocal in the days after the military putsch was because of his own entanglements in the patronage of Al-Sisi and the Armed Forces, which gave him a green light to pursue corruption within certain state institutions that may have posed as rivals to the Armed Forces in the immediate weeks and months following the putsch. This has been a time when the country’s internal, domestic power balance between institutions was still being shaped and to play for. The fact that Genena repeatedly absolved the Office of the Presidency and the Armed Forces of any guilt vis-à-vis corruption and special funds, and at the same time created an uproar about the obvious venality of the Ministry of Interior, we believe is evidence of his selective, regime-backed focus.”

“Al-Sisi has the option of using this new decree as a yet another tool to solidify and strengthen his grip on power by forcing regulatory agencies to pursue his potential rivals or opponents, or selecting heads of these regulatory bodies that will in any case be highly sympathetic to his own agenda,” said Hodge. “In the sense that Egypt’s intelligence and security forces are now clearly playing an expanded role in corruption, this does chime with the Algerian example, where Algeria’s intelligence service, the Département du Renseignement et de la Sécurité, had its mandate expanded from a focus on security and counter-terrorism matters before the civil war in the 1990s, then were given power to investigate internal corruption in state institutions, including ministries and state-owned enterprises. In practice, this has resulted in an entanglement between prevailing elite interests and anti-corruption. It is conceivable that Egypt’s army and military intelligence could follow a similar direction.”

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