

## **Egyptian Pre-revolution Budget Deficit: Tax Lethargy or Public Policy?**

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Despite a chronic budget deficit over the last 30 years, the tax effort of the Egyptian economy has been declining.

The Fiscal regime in Egypt is similar to many other developing countries. Most of these countries rely on commodity taxes rather than income taxes and have neutral or regressive tax regimes. The Egyptian case is slightly frustrating as a move towards more equitable tax structure and income distribution was reversed in the last twenty five years. The IMF supported Economic reform and Structural Adjustment program of 1991 is partly responsible for these results. On the one hand it reduced taxes on foreign trade while sponsoring large increase in domestic sales taxes. On the other hand, modifications in income tax laws exempted most rentier incomes from taxes. This included interest payments on bank deposits, public bonds, and capital gains on the stock exchange transactions. In the meantime, inflation led to drastic deterioration in real wages, and the privatization program led to a wholesale loss of public sector employment.

The main hypothesis of this paper is that the chronic budget deficit in Egypt is not outside the domain of policy. A more active tax policy is likely to be able to cover a large portion of the budget's cash deficit. Failure to follow obvious policy options is in itself an indication of policy.

The paper is divided into four sections: 1- Review of the Literature, 2- Methodology and discussion of basic hypotheses. 3- Assessment the present level of tax effort in Egypt. An econometric model will help us identify major economic and policy variable affecting tax effort in Egypt. We shall compare that a theoretical level of tax capacity using methodology proposed by the World Bank. 4- Findings and Policy recommendations.

Key words: Egyptian Economy and fiscal policy, public finance, tax capacity models, income distribution, and developing countries.