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Governing Militaries in Liberalizing Economies: China, Iran, Egypt

A Dissertation

Presented to

the Faculty of the Josef Korbel School of International Studies

University of Denver

In Partial Fulfillment

of the Requirements for the Degree

Doctor of Philosophy

by

Loosineh Markarian Senagani

November 2017

Advisor: Dr. Rachel Epstein

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Title: Governing Militaries in Liberalizing Economies: China, Iran, Egypt
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Degree Date: November 2017

Abstract

Why have some economically-active militaries of autocratic regimes gained more autonomy vis-à-vis their civilian elite as a consequence of economic liberalization processes adopted in 80s and 90s, whereas others have remained subordinate to civilian control? This dissertation examines the impact of economic liberalization since 1980s on civil-military relations (CMR) in autocratic regimes. Prior to liberalization, the centrally-planned governments of Egypt, Iran, and China utilized their militaries to implement economic development projects. Post-liberalization, these militaries expanded into new economic sectors like finance, banking, and trade. The expansion impacted the balance of CMR differently in each case. Egypt's military took over the state, the China's People's Liberation Army retreated to the domain of defense, and Iran's Islamic Revolutionary Guard Corps became a coalition-maker. This research argues that the modes and pace of liberalization in general, and privatization specifically, are crucial to understanding CMR variations. Aspects of liberalization led to varied capitalist development projects, which conditioned the empowerment or disempowerment of militaries. If liberalization and privatization fostered economic competitiveness, militaries had fewer opportunities for enhancing their autonomy. Whereas if incomplete liberalization and rapid privatization did not lead to the establishment of a competitive economy, militaries had more opportunities to expand their autonomy.

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Introduction: Bridging the Gap: Economic Liberalization and Civil-Military Relation

The Puzzle

The implementation of economic liberalization policies in the final decades of the twentieth century provided an alternative path for development in closed economies that relied on central planning. The political science literature has examined the consequences of economic liberalization on domestic politics and economies. However, a more specific question on the impact of such policies on economically-active militaries, and their control, in autocratic regimes has not received much scholarly attention. In my dissertation, I identify a puzzling outcome in terms of economically-active militaries behavior in liberalizing economies. I explain why some economically-active militaries of autocratic regimes have gained more autonomy vis-à-vis their civilian elite as a consequence of economic liberalization processes adopted since 1980s, whereas others have remained subordinate to civilian control. More specifically, in these three states, similar economic policies led to different outcomes for civil-military relations: near-total military autonomy in Egypt but much less in Iran and not at all in China. Why?

By analyzing three aspects of control, i.e. political, functional, and social control, I argue that the specifics of liberalization and privatization impacted the control of forces differently in each case. If haphazard economic liberalization and rapid privatization fails to establish a competitive market economy, the economically-active militaries are more likely to amass political power. Additionally, the militaries turn into economic interest groups and likely outcomes are decreased functional and social controls. If a gradual economic liberalization and private sector development fosters economic competitiveness, economically-active militaries have fewer opportunities to amass political power. Additionally, there are less incentives for militaries to operate as economic actors as well. Hence, the functional and social controls either increase or remain the same.

Therefore, in three cases under study, fluctuations in the power of economically-active militaries vis-à-vis their civilian counterparts were a function of states' capacity to establish a competitive economy. In a relatively competitive economy, militaries had higher incentives to limit their activities to the domain of defense since carrying out both tasks of defense and economic production effectively were costly. Therefore, they were more dependent on civilians and could not increase their political autonomy. This was the case of the Chinese People's Liberation Army. Conversely, in economies characterized by cronyism, militaries were able to maintain their economic activities and to pressure the government for more economic and political gains. This was the case of the Egyptian Armed Forces. Iran's Islamic Revolutionary Guard Corps' trajectory took the middle-ground providing mixed outcomes: the IRGC established itself as an economic and political player but failed to take over the government completely. Additionally, in states

where economically-active militaries established themselves as economic interest groups, functional capabilities and social controls declined.

Motivation

Following the emergence of the modernization discourse after the Second World War, autocratic regimes in several Middle Eastern and Asian countries assigned their militaries the dual role of state defense and socio-economic development. The success of revolutionary armies in defeating conventional armies in China, Southeast Asian countries, Algeria, and Cuba drew attention to the role of militaries in combating domestic revolutionary armed groups. Simultaneously, US military assistance in Latin America underscored the role of local militaries in counterinsurgency, nation-building, and civic action; there was an increasing belief that “professional military expertise” could be utilized for domestic purposes, such as provision of internal security. A new perspective, known as new-professionalism, argued for interrelated nature of politics and military. This shift to the increasing politicization of militaries; it also resulted in militaries’ role-expansion as governors of national development projects, particularly in states with weak civilian governments (Stepan 1986, 136-137).

Latin American states were not the only countries that assigned development projects to their militaries. Other states across the developing world also adopted similar policies. Frequently, the outcome was the emergence of economically-active militaries that not only received official budgets for defense spending, but also generated extra-budgetary income via economic activities. In response to this development, the study of Civil-Military Relations (CMR) also focused on the role of militaries in modernization. Scholars such as

Levy (1971), Needler (1971), and Quinlivan (1999) examined the changing dynamics between civilians and militaries in modernizing economies. The focus, however, was on destabilizing effects of modernization and possibilities for militaries' intervention in form of coup d'états.

For example, Levy (1971) and Needler (1971) studied the likelihood of military coups d'états in modernizing states. Levy argued that the governments utilized careful military recruitment policies to reduce possibilities for military coups¹. Similarly, Needler (1971) considered coups as likely consequences of deteriorating economic conditions: dominant classes, discontent from the process of modernization, used their militaries to stage a coup and retain the status quo. Although above-discussed studies focused on the interrelation of economic development and coups, they failed to examine the specific question of militaries' economic role-expansion and their impact on local economies or politics. Furthermore, not only they took political control as the sole measure of civilian control, they also adopted a narrow definition of political control—coup d'états or overt military intervention.

Coup-proofing literature was also primarily concerned with the question of coup-d'états. The scholarly work that observed militaries' economic power, did so in the context of examining the possibilities for coups. For example, Quinlivan (1999) discussed various coup-proofing strategies in Iran, Saudi Arabia, and Syria by identifying strategies such as establishment of parallel militaries to counterbalance regular militaries or providing

¹ Specifically in form of palace coups

funding for militaries² (Quinlivan, 1999: 135). Similarly, Makara examined the effectiveness of coup-proofing strategies in Arab states of Egypt, Syria, Libya, Bahrain, and Yemen. In states where parallel institutions or unequal distribution of material incentives divided militaries, defections were more likely (Makara, 2013: 334-335). Albrecht (2014) also compared the cases of Egypt and Syria and argued that those strategies that kept officers outside of the politics, and meanwhile enhanced their corporate autonomy, were more ineffective for the times of crisis (Albrecht, 2014: 37). The above-discussed literature, among other things, underscored the economic aspect of military's susceptibility to coups. However, it overlooked a systematic study of military's economic role-expansion and its impact on domestic politics.

While preventing coup-d'états is a significant sign of civilian control, the empirical evidence suggests that militaries' intervention in politics takes various shapes, in addition to coups. Autocracies could be immune to coups and still be vulnerable to other forms of military influence such as military politicization by civilians or military's interference in governance, such as foreign policy or economic policy decision-makings. Therefore, on the one hand, studies on the interrelation of economic development and civil-military relations focused on a narrow definition of military interferences. On the other hand, they did not treat those militaries engaged in developmental tasks as economic actors since they overlooked the implications of militaries' economic-role expansion. My dissertation focuses on economically-active militaries specifically and treats them as economic actors.

² Quinlivan, *Coup Proofing*, 135. Other coup-proofing strategies included creation of multiple intelligence organizations for monitoring, exploitation of group loyalties (ethnic, religious, family), and fostering military professionalism.

In doing so, it also draws on recent literature that problematizes a sole focus on coups, and hence accounts for varied forms of military intervention in autocratic politics.

More recently, scholars (Feaver 1999, Taylor 2003, Avant 2005, Epstein 2008) have theorized varied forms and aspects of control, expanding the CMR literature beyond the study of coup d'états. Brian Taylor, in his *Politics and the Russian Army: Civil–Military Relations, 1689-2000* (2003), categorized some of those forms of interference that go beyond coup d'états. He classified *military interventions* as an actual or threat of use of force aiming at changing the executive; other forms of interference are *military arbitration* when militaries become mediators between legitimate civilian actors, and *no military intervention* for cases where an otherwise expected coup doesn't occur (Taylor 2003, 7).

Similarly, Feaver (1999) also highlights the multifaceted nature of civilian control by identifying coup d'état, military influence, civil military friction, and military compliance as four main dependent variables commonly considered by theoretical studies of CMR. Feaver explains that military institutions' inclination to coups, i.e. the frequency and likelihood of military seizures of state power, has been the focal interest of classic literature, as in works by Huntington, Finer, Nordlinger, Bienen, Jackman. However, according to Feaver, there are other conceptual categories, such as *military influence* that acknowledge the *degrees* of political power militaries could exercise: arguing for a continuum as opposed to a coup versus non-coup dichotomy (Feaver 1999, 217-219).

Epstein's *In Pursuit of Liberalism: International Institutions in Postcommunist Europe* (2008) is another work underscoring the importance of contextual differences in both understanding and conceptualizing military control and autonomy. The author

examined NATO's role in reforming CMR in the socio-political context of post-communist legacies and transformations. Instead of military seizure of the state's power—commonly seen in non-communist states—militaries in the post-communist states of Central and Eastern Europe struggled to remain autonomous and free from civilian interference. The Soviet legacy of military autonomy in return for subordination to civilian authority posed a challenge as democratic control required limiting militaries' autonomy both functionally and normatively (politically). This process particularly required civilianizing the security–military apparatus with democratic institutions, where civilians, instead of military personnel, would run ministries of defense, parliamentary defense committees, and would oversee the intelligence services, and the defense budget (2008: 109). The above-mentioned studies provide a more nuanced understanding of the question of political control. These works highlight the sophisticated nature of civil–military interactions in the domain of politics, possibilities include: politicization of militaries by civilians, militarization of politics, or other forms of military interference such as occupying government positions.

Furthermore, challenging the one-dimensional views that either focused solely on one aspect of political control or employed various aspects of control vaguely or interchangeably, Avant explains that the CMR literature often rests on different concepts of control (Avant 2005). Though many implicitly appreciate that what we mean by civilian control includes a military that is capable (functional control), responsive to leaders (political control), and serving societal values (social control), analyses tend to elevate one or another (2005: 5-6). In analyzing the question of civilian control, specifically

privatization of security, Avant (2005) argues that “the control of force has been most stable, effective, and legitimate when all three aspects have reinforced one another – when capable forces have been governed by accepted political processes and operated according to shared values” (2008: 6). Hence, as discussed thus far, recent scholarly works have adopted a more sophisticated framework in understanding the concept of military control by underscoring various aspects of civilian control.

In studying the role of economically-active militaries in China, Iran, and Egypt, I embrace this broader framework that moves beyond a study of coup d'états and takes into consideration various forms of military influence in politics. I focus on military influence as a continuum that manifests itself not only in the domain of politics, but also in the domains of society, and economy. Moreover, as mentioned before, the literature surveying militaries in autocratic regimes has failed to critically examine militaries' political economy; it has not offered theoretical frameworks or hypotheses that would explain the consequences of militaries' economic power not only on political control but also on military capabilities and social values. I take various types of intervention in politics, as well as functional and social controls into account. In doing so, I identify political economy variables that impact militaries economic behavior, and ultimately, explain the processes that sometimes increase the functional, political, and social power of economically active militaries and at other times have a reverse effect on those dimensions.

A systematic study of economically-active militaries is imperative in understanding an unexplored dimension of military power. There is an emerging body of research examining militaries' roles as economic actors, as well as case studies focusing on the

economic activities of militaries. These studies, primarily focus on the following issues: classification of different types of militaries' economic activities (Brömmelhörster and Paes 2003, Mani 2007), contingent generalization on interrelation of militaries' economic activities and civil-military relations (Alaggapa 2002, Mani 2007, Mani 2010), and case studies (Mulvenon 2001, Siddiqa 2007).

For example, Brömmelhörster and Paes's collection provides a descriptive typology of militaries' business activities classified as *budgetary assistance, pensions welfare, developmental role, import substitution, economic opportunism, and opportunities for corruption* for the cases of Argentina, Central American states, China, the DRC, Indonesia, Pakistan, Russia, and Vietnam (2007: 681). Mani (2007) also offers a typology of militaries' economic activities: institutional (benefiting the institution), spoils (benefiting the individuals), statist-institutional (state-led benefiting the institution), and statist-spoils (state-led benefiting individuals) (2007: 596). Two causal variables of state capacity (weak vs. strong) and military's organizational nature (professionalization vs. parochial) determine the above outcomes. In strong states, militaries' economic activities are directed by the state; in weak states, military's organizational nature (professional versus parochial) determines the outcome (2007: 595). In a later piece, Mani (2010) explains that cultural, structural, and rational approaches could help us understand the reasons behind trajectories of civil-military relations regarding economically-active militaries but doesn't offer testable hypotheses.

Other studies such as Siddiqa's *Military Inc.: Inside Pakistan's Military Economy* (2007), Cheung's *China's Entrepreneurial Army* (2001), Mulvenon's *Soldiers of Fortune:*

The Rise and Fall of the Chinese Military–Business Complex, 1978-1998 (2001) focus on individual case studies. These case studies provide insights and testable hypotheses on the role-expansion of militaries for individual cases but do not provide comparative case studies. Other studies, such as Alagappa (2002) in his *Coercion and Governance: The Declining Political Role of the Military in Asia* (2002), offered contingent generalization.

In discussing militaries' role-expansion in Asian states, Alagappa (2002), argued that what mattered was the scope of military's participation in economic governance. A simple increase in the scope of participation (breadth of participation in governance) in the socio–economic domain didn't necessarily mean expansion of the military's role. It was considered role-expansion only when it was linked to an increase in the military's jurisdiction and decision-making power (32, 2002). The role-expansion³ was a function of the weakness and illegitimacy of the governing elite and not a function of unprofessionalism. CMR patterns, hence, were determined by the interrelation of the following factors:

“beliefs, interests, and power of administrative, military, and political institutions (bureaucracy, presidency, legislature, communist party), and military institutions (armed forces, paramilitary forces, intelligence agencies, and the security agencies) mediated by the beliefs and power of civil society and international society” (Alagappa 2002, 58).

In the context of strong political institutions, the beliefs and values, norms and principles determined the CMR patterns. In institutionally weak states, the distribution of power among major actors and their interests, which were influenced by civil and international society, determined the outcome. Alagappa's work is among very few studies

³ Based on Stepan's notion of new professionalism, i.e. militaries involvement in non-defense related tasks.

focusing on the causes behind militaries' economic role-expansion. Similar to previous studies, however, Alagappa does not take into account varied aspects of control. Moreover, the causal explanation considers the impact of several variables, making it difficult to analyze the causal process and identify the most determinant variables.

Building on above-mentioned works, my project takes a step further in comparing and contrasting cases in terms of the militaries' power-expansion in politics, the militaries' effectiveness, and changes in their values. I propose testable hypotheses leading to contingent generalizations regarding economically-active militaries' political behavior, as well as their functional and social control. Furthermore, the above works mainly focus on organizational character, elite interactions, or domestic state capacity variables; they do not expand the underlying micro-mechanisms of militaries' economic expansion or contraction under conditions of changing economic systems. While the literature of political science has examined the consequences of liberalization on domestic economies and on politics alike, it has not systematically examined the relationship between liberalization and economic activities of militaries in autocratic regimes. The literature also overlooks discussion of the changing conditions under which these militaries became economically-active. The economic activities of militaries under central planning and import substitution policies had a different character and meaning compared to the liberalized economies of today. My research intends to breach this gap by examining militaries of China, Iran, and Egypt.

First, centrally-planned economies of China, Iran, and Egypt all had economically-active militaries and have experimented with state control over their militaries during the

phase of their nationalized centrally-planned economies. The liberalization programs in all three cases included trade liberalization, financial sector reforms to attract foreign capital and foreign direct investment, and a process of privatizing state-owned enterprises. As a consequence of these reforms, not only these militaries expanded their economic power, but also, in some cases, they succeeded to translate their economic power into political authority in the decades following the reforms. The economic liberalization also had varying impacts on the functional and social aspects of control. Together, these shifts translated into varying degrees of military influence.

On certain occasions, militaries have profited from their power to engage in preferential bidding, tax evasion, smuggling, and unfair competition. Their economic expansion resulted in exercising different degrees of political power such as interfering with foreign policy decisions, electoral processes, or coup d'états. The functional control varies as well, with some militaries acquiring more capabilities and expanding their functional power while others' capabilities have decreased. In terms of social control, some militaries have become self-interested institutions, pursuing or even prioritizing their corporate interests while others still maintain the values and ideologies of the societies they represent or adhere to the international humanitarian values. Despite the above-mentioned economic policy changes, the discipline has failed to analyze the impact of these changes on various patterns, as well as three aspects of CMR, i.e. political, functional, and social controls.

While all three implemented liberalization policies, overall China has been most successful in maintaining or expanding civilian political control, as well as functional and

social control. In Iran, there is a balance of power between civilians and the Islamic Republic's Guard Corps (IRGC); the IRGC has turned into a power bloc. The economic reforms have negatively impacted the functional capabilities of the military. With regards to the social values, the IRGC has remained loyal to the ideals of the Islamic Revolution but it has also become a self-interested corporate entity making decisions to serve its narrow economic interests. Its pursuit of narrow self-interest at times is in the expense of Iran's national interests, i.e. the revolutionary developmental goals such as alleviating poverty. In Egypt, the military continued to monopolize its power during Hosni Mubarak's regime and became a power broker during the Egyptian Revolution of 2011. The functional control has not registered significant changes while liberalization has negatively impacted the social control since the military has become a self-interested corporate entity representing social values in conflict with the majority in the society.

The dependent variable of civil-military relations varied as follows: the Chinese PLA divested its businesses and returned to barracks. Egypt's EAF fought to maintain and expand its economic empire, and ultimately took an almost complete control of the state. The IRGC's political leverage was not as extensive as the EAF's, but unlike China, it has established itself as an accepted political player. Why?

I argue that civilians' ability to foster economic competitiveness and private sector growth conditioned and constrained militaries' behavior, and subsequently the CMR. Particularly, incomplete liberalization or selective protectionism provided opportunities for economically-active militaries to capture state resources and provided them with enough leverage to translate their economic power into a political power. In the absence of

competition in the economy, economically-active militaries enjoyed an edge and could use their government linkages to their advantage, thus increasing military influence in the political domain; militaries became less dependent on their civilians because they could maintain their businesses in an uncompetitive economy, Where economic liberalization fostered decentralization of economic activity and competition, however, economically-active militaries had fewer opportunities to capture state resources and transform their economic power into political influence. In more competitive economies, military businesses needed to maximize profit and out-compete other actors to gain success. Without selective protectionism, maintaining profitability for militaries became increasingly difficult, weakening their leverage over civilians and hence their potential influence.

Moreover, economic liberalization that allowed for economic integration also generated more income, which allowed for increases in defense spending, which decreased the need for militaries to maintain businesses. This process improved the military's capabilities and its incentives to remain subordinate. Conversely, unintegrated economic liberalization did not generate income that could be used for increases in defense spending, leading militaries to continue their focus on economic activity instead of focusing on improving their capabilities. In these instances, militaries turned into self-interested corporate entities pursuing institutional interests rather than adhering to the values of the society.

This dissertation's findings offer insights on how International/regional Organizations', or United States', economic policy recommendations impact the balance

of power between militaries and civilians in autocratic regimes, and what subsequent security implications of those changes are. A military's economic role-expansion and their ability or inability to leverage their economic power into a political one is crucial in state's political liberalization process, and ultimately possibilities for democratization. Also a military's economic role-expansion, if not in service of developmental goals, could impede economic development, as it has been in the cases of Iran and Egypt. Ultimately, in terms of security sector reforms, the findings underscore the importance of combining economic reforms and security reforms; it highlights the importance of coordination among developmental agencies in terms of recommendations they could offer to those developing states where the militaries have a history of economic activity.

Structure of the Dissertation

This dissertation consists of five chapters. The first chapter outlines the theory, hypotheses, and methodology. It develops the theoretical framework based on capitalist development models that informed the selection of independent variables and generation of testable hypotheses. Then, it explains the process of case selection, the dependent variable of military control (political, functional, and social control) and its operationalization.

The second chapter analyzes the reasons behind the willingness of China's People's Liberation Army (PLA) to dissolve its economic empire following the civilian order in 1998; it explains why, to the surprise of many, the PLA divested its enterprises and returned to barracks.

The third chapter focuses on Iran's Islamic Revolutionary Guard Corps (IRGC). It aims at explaining why despite its success to considerably expand its both economic and political power, the IRGC nevertheless failed to completely dominate Iran's economy and politics.

The fourth chapter delineates the process of economic liberalization in Egypt and how it facilitated expansion of the Egyptian Armed Forces (EAF) into the economy and its later success in transforming its economic power into political power: a complete government take-over. The final chapter wraps up the findings, suggests the policy implications of the findings, and offers recommendations for future research.

Chapter 2: Hypotheses on Economic Competitiveness and Civil-Military Relations

Theory: Pathways to Capitalist Developments

This dissertation (i) suggests that specifics of liberalization and privatization processes are crucial for understanding the variations in the balance of power between the civilian elite and militaries, and (ii) identifies variations in the degrees of political, functional, and social autonomies that militaries exercised prior to and after liberalization processes. The types of economic liberalization, and their outcomes, i.e. gradual liberalization coupled with reform of regulations and bureaucracy leading to competitiveness versus a rapid process of deregulation and privatization that hinders competitiveness, impact militaries' political, functional, and social controls. This study formulates hypotheses by referring to capitalist development models developed by King and Szelenyi (2005) and by Harris' (2013). The theory King and Szelenyi offer informs the selection of independent variables, and the subsequent formulation of testable hypotheses.

King and Szelenyi, in their *Post-Communist Economic Systems* (2005), present three ideal types of capitalist development in Eastern Europe. Like the literature that argues for examining divergent capitalist projects (Hall and Soskice 2001), the authors articulate

the unique features of class, private-property formation, and market institutions in several post-communist states, and how they mitigated the privatization and liberalization. Capitalism from above, capitalism from below, and capitalism from without were three pathways of capitalist development that resulted in divergent capitalist systems. In capitalism from above, elites followed a neoliberal plan to transform a socialist economy into a capitalist one. The process enabled the *nomenklatura* to convert itself into a new capitalist class. Labeled as *patrimonial capitalism*, characteristics of capitalism from above have included patrimonial relationships and network-based economic activity. Capitalism from below emerged as a hybrid system of new actors, private property owners, and a market economy that kept operating alongside the old redistributive system. Hybrid capitalism was an outcome of capitalism from below where state-owned enterprises and a small private sector coexisted. Finally, capitalism from without, like capitalism from above, adopted neoliberal policies but with a significant difference. In this scenario, instead of privatization and empowerment of the older *nomenklatura*, states relied on foreign ownership and multinational corporations. Liberal capitalism was a system where market institutions had developed and there was a globally integrated economy (King and Szelenyi 2005, 205-208).

By utilizing capitalist developmental models, Kevan Harris, in his “The Rise of the Subcontractor State: Politics of Pseudo-Privatization in the Islamic Republic of Iran” (2013), also discusses the impact of state capacity and instructional competency on different forms of capitalist development. He adopts King & Szelenyi’s three models of

capitalist development⁴ to explain various periods of economic reform in Iran, comparing them to other cases in the developing world.

In Harris' account, the Iranian economy experienced all three forms of development, with Ahmadinejad's privatization policies amounting to capitalism from above, and the consequent empowering of the IRGC. Similarly, Egyptian economic development took the path of capitalism from above, while China, in contrast, experienced capitalism from below and origination of a private sector operating parallel to the state sector. Harris' work provides a basis for understanding the interaction of political and economic institutions in the cases under study. Given the fact that the economic activities of militaries in China, Iran, and Egypt have been embedded in capitalist development projects, my research builds on King and Szelenyi (2005) and Harris' (2013) framework to explain why, under conditions of varied capitalist development projects, militaries in each state have acquired different degrees of power in relation to civilians.

I focus on the variables of economic liberalization and modes of privatization to examine (i) states' ability to implement market mechanisms, and (ii) the process of private sector development, and (iii) the extent to which both of these conditions create a degree of competition in which militaries must operate. Subsequently, I test the interrelation of economic competitiveness and the question of military control.

⁴ Harris, *The Rise of Subcontractor State*, 65-66. Capitalism from above leads to the engineering of a Weberian rational-bureaucratic state and the implementation of liberal policies resulting in export-oriented and foreign capital-intensive economic strategy. In the case of capitalist development from below, a coalition between technocratic elite and domestic bourgeoisie operating in a politically powerful state bureaucracy leads to the emergence of a "hybrid system of capital accumulation and mixed forms of property", where the balance of power between the two groups has led to the emergence of a private sector co-existing with a big public sector. The outcome of privatization in the absence of a solid bureaucratic-institutional framework—capitalism from above—has been states' asset-stripping by the elite in power.

Explanatory Hypotheses: Competitive versus Uncompetitive Economies

Hypothesis#1: If rapid or haphazard economic liberalization fails to establish a competitive economy, or does not facilitate private sector development, economically active militaries turn into economic interest groups. A likely outcome is increased autonomy in the political domain, and decreased functional and social controls.

In other words, incomplete economic liberalization (or selective protectionism) conditions maintenance of economically active militaries as economic actors and increases their political leverage.

Causal explanation: Rapid liberalization in the absence of market institutions and regulatory regimes, as well as the transfer of previously state-owned enterprises to private actors, provides an opportunity for existing networks of influence in the state to engage in asset-stripping. In transition economies, liberalization via transfer of both ownership and management of state-owned enterprises to private actors takes place under the conditions of weak economic institutions. Subsequently, due to weak regulatory regimes, existing networks of influence, in this case economically-active militaries, are able to further enhance their economic power and translate it into political leverage by becoming a pressure group impacting civilian decisions.

Civilians' Functional control over the military also decreases because militaries expand economically to support themselves or to simply generate profits. Since the state doesn't increase defense spending, the military has an incentive to remain economically active. Moreover, rapid liberalization provides opportunities for transformation of military's economic base into a political one. The military turns into an interest group; it

might still adhere to social values but self-interest takes precedent over social values. (Cases of Egypt and Iran).

Hypothesis#2: If economic liberalization and private sector development establish a competitive economy, economically-active militaries have less incentive to operate as economic actors. The outcome is increased civilian control in the political domain. The functional and social controls either would increase or would not change.

In other words, relatively thorough-going economic liberalization that establishes a competitive economy reduces incentives for militaries to engage in economic activities, which in turn leads to a decrease in militaries' political leverage.

Causal explanation: If the state carries out gradual economic liberalization, where state-owned enterprises are not rapidly transferred to the private sector but instead a new private sector emerges parallel to the public sector, the chances for economically-active militaries to enter the new private domain are slimmer. In other words, if the state engages in partial privatization—where it still retains either partial management or ownership of state-owned enterprises, outsources activities previously done by the state but doesn't necessarily transfer them to the private sector, or engages in joint public–private ventures—then privatization is gradual. Under these circumstances, the existing networks of influence have smaller windows of opportunities to engage in asset-stripping. This is because if the economic liberalization fosters competition, the economic space opens for new entrepreneurs to flourish, meaning the emergence of new businesses in those private sectors that are not dominated by the state.

In terms of the sectors dominated by the state, privatization is controlled and gradual, with private actors holding less power in relation to the state. Subsequently, the state faces the emergence of parallel public and private sectors where state and private actors engage in different kinds of economic activities. The best examples of these types of privatization are the cases of China during Deng's leadership and continuing to the present (Gao 2014), and Iran during the presidency of Khatami (Harris 2013).

If the state is generating income via economic liberalization, the probability for an increase in defense spending is higher. Therefore, there are improvements in militaries' functional control as the military receives extra funds. A military's incentive to engage in economic activities is also reduced. Moreover, gradual privatization doesn't provide opportunities for asset-stripping. In this scenario, the military is more likely to remain loyal to the regime and uphold the values of the autocratic regime. (This was the case for China).

Most Similar Systems Design

Why did China's People's Liberation Army (PLA) divest its businesses and return to barracks following economic liberalization policies in the 90s, whereas Iran's Islamic Revolutionary Guard Corps (IRGC) established itself and became a coalition-maker but Egyptian Armed Forces (EAF) rose into political power? Despite the similarities these cases share in terms of military control prior to the economic liberalization, as a result of economic liberalization the EAF gained significant power—almost a complete government take-over. In China, on the other hand, liberalization consolidated civilian control over the PLA. In Iran, the IRGC entered into coalitions with the leading civilian elite. I aim to understand why seemingly similar policies led to such different outcomes. I argue that

when liberalization and privatization does not foster competitiveness, militaries have opportunities to expand their economic base, engage in stripping of state resources, and turn their economic power into a political power. In contrast, when liberalization and privatization assist establishment of a competitive economy, militaries have limited opportunities to transfer their economic base into a political one.

By adopting a Most Similar Systems Design (MSSD) (Della Porta, 2008), my research utilizes a historical institutionalist approach and a method of process-tracing to provide a causal explanation for the impact of economic liberalization policies on civil–military relations in the three cases of China, Iran, and Egypt. MSSD is used to rule out similarities and identify the points of divergence among the three case; the dependent variable is the civil-military control post-liberalization. Aiming to offer contingent generalization, I utilize the method of process-tracing to find critical processes by comparing historical cases (cited in George and Bennett 2005, 205). I look at those critical moments in history where policy choices changed the states’ economic trajectory in general, militaries’ economic power in particular, and ultimately their political leverage.

The countries under study share similarities in terms of civil–military relations prior to liberalization in the 1980s, as well as in their adoption of economic liberalization policies as a remedy for the economic constraints they faced. The balance of civil–military power subsequent to the liberalization, however, varies. Therefore, given similarities the cases shared with respect to their nationalization policies, their militaries’ role in economic development, and their adoption of economic reforms, what variables determined the divergent outcomes in civil–military relations (CMR) following liberalization?

Through process-tracing, this study will identify those market and state institutions that conditioned the interactions of civilian and military elites in autocratic regimes; it will also explain how the introduction of new market policies led to different types of capitalist development projects that provided opportunities for empowerment or disempowerment of militaries. In order to compare these three cases, this study adopts the comparative method of MSSD to rule out similarities and find the most determinant variable. Case selection focused on three theoretically relevant similarities in the domains of historical legacy, economic policy, and the militaries' position in the society. Those similarities are the following: regime collapses via revolutions followed by the establishment of autocratic regimes, the adoption of a leftist economic orientation accompanied by central planning, an anti-imperialist discourse, the militaries' ideological role as guardians of newly formed independent states or regimes, and finally the allocation of economic development tasks to militaries are similarities all cases share. In addition, all cases adopted similar economic liberalization policies: reforming exchange-rate systems, banking/financial sector, and privatization packages.

Similarities: Cases of China, Iran, Egypt

Table 1: MSSD, Similarities of China, Iran, and Egypt

Similarities		Iran	China	Egypt
Historical legacies/ State Institutions	Revolution	✓ (1979)	✓ (1945)	✓ (1952)
	Establishment of Autocratic regime	✓	✓	✓
	Civilian autocracies	✓	✓	Monarchy
		✓	✓	✓
	Established autocracies (no civil wars/ not in transition)	✓	✓	✓
Cultural	Anti-West rhetoric	✓	✓	✓

Economics	Centrally Planned Economy/ ISI	✓	✓	✓
	Shadow Economies	✓	✓	✓
	Existence of Private sector along with the public one, but dominance of State Owned Enterprises	✓	✓	✓
	Openness/Economic Reform Policy	✓	✓	✓
	Trade liberalization	✓	✓	✓
	Exchange rate reform	✓	✓	-
Militaries	Assigning the militaries dual roles of defense and development	✓	✓	✓
	Ideologically oriented militaries (defending the ideology of state)	✓	✓	✓
	Militaries under civilian control prior to the liberalization policies	✓	✓	✓

In these three cases, the revolutions and implementation of economic liberalization policies occurred at different times. However, they share both the same international context and the same domestic ideologies. China experienced revolution in 1949, at the beginning stages of the Cold War. Egypt and Iran experienced revolutions and established new regimes in 1952 and 1979 respectively. Although their revolutions occurred in different times, all three happened during the Cold War and were similar in terms of their adoption of anti-western and anti-capitalist ideologies. In all three cases the revolutions brought left-leaning elites into power and were responses to a polarized international environment. In all three cases, the elite in power adopted centralized economic policies.

In addition, all three states are established regimes with a strong state capacity to monitor their borders, and subsequently have not experienced civil war. Therefore, the literature related to states in transition, militaries in the process of state formation, as well as civil wars should be excluded from this study.

The Dependent Variable

The dependent variable (DV) is *degree of civilian control over the armed forces* measured along the three aspects of political, functional, and social control. The DV is a military's political, functional, and social values both prior to and after economic liberalization processes in the eighties and nineties. Therefore, operationalization requires assessment of DVs both prior to and after economic liberalization.

Political control. I base my measurement of a military's political control on Brian Taylor's (2003) definition: militaries' involvement in politics includes "military intervention" and "military arbitration." In the former case, intervention is "the use, actual or threatened, of force by members of the military, either alone or with civilian actors, in an attempt to change the executive leadership of the state" (Taylor 2003, 7). Hence, military intervention could be operationalized based on (i) coups, (ii) attempts/threats to coups, (iii) direct intervention in electoral processes or exercise of a veto-power over electoral results, (iv) the military assuming governmental positions, and (v) the military's responsiveness to the government or at least to a faction of the civilian elite.

According to Taylor (2003), military arbitration is "when multiple persons or groups claim to hold legitimate state power and the military is forced to decide from whom to obey orders" (Taylor 2003, 7). Military arbitration is evidence of military interference in politics. However, in autocratic regimes, due to the absence of both institutional mechanisms of control and democratic norms, the line between militaries and civilians is blurred. The militaries are usually politicized and serve interests of a faction of the elite in power. Hence, drawing a clear distinction illustrating a shift from non-interference to

interference is difficult. Therefore, I will take arbitration as evidence of interference only when arbitration serves the corporate interests of the military rather than expressing the military's responsiveness (or loyalty) to a particular political faction. In other words, the motivation behind military's decision-making is important: if the military switches sides constantly, makes coalitions with various elite factions, in order to advance its economic interests, I will count it as military interference in politics.

By assessing each military's political autonomy, prior to and after economic liberalization I can identify whether there was a shift in the military's political power after economic liberalization.

Functional control: Civilians have functional control of the military when it has “the capacity to create military power from a state's basic resources in wealth, technology, population size, and human capital.” As put by Brooks and Stanley, “A military's level of effectiveness varies with the degree to which it is organized to make good use of these material and human resources” (Brooks and Stanley 2007, 9-13). In keeping with this definition, I use the following attributes to measure military effectiveness: (i) integration: the ability to ensure consistency in military activity, create synergies, and avoid counterproductive activities, (ii) responsiveness: the degree to which the state accommodates internal and external threats to prepare itself for armed conflict, (iii) skill: preparation and motivation of military personnel to execute tasks in the battlefield, (iv) quality: capacity of the state to provide itself with weaponry.

Based on Brooks and Stanley's classification (2007, 15), some of the following indicators (given available data) are used to measure military effectiveness across time: (i)

Integration: consistency between tactics with broader political goals, consistency of training system of personnel with tactical concepts, logistics and operational plans support strategic objectives. (ii) Responsiveness: tactics designed to address weakness of adversary, modification of forces in response to new threats and challenges, rigorous internal monitoring system (intelligence gathering), officer selection. (iii) Skill: fluid assimilation of technology, highly motivated soldiers, proficiency in executing doctrines; assessing the education and training programs. (iv) Quality: Nature of weapons procured, ability to minimize trade-offs in mobility

Social control: Social control refers to the values that underlie military activity. Based on Avant's (2005) classification of various types of control, I assess social control in terms of changes in military values, i.e., adherence to social norms of the society (43). If militaries start operating based on narrow self-interest rather than an adherence to previously-established social norms and expectations, there is a change in the social control.

DV Prior to and Post-Economic Liberalization

Iran: I focus on sixteen years of liberalization policies since 1997; the policies were adopted during Khatami's and Ahmadinejad's presidencies (1997-2013). Rafsanjani's presidency from 1989–1997 was marked by the politicization of the IRGC and its role-expansion. That is the DV (prior) to the effective economic liberalization policies in 1997. Although Rafsanjani attempted to liberalize the economy, his policies did not succeed. The period of post-liberalization is identified with two changes under two presidencies: liberalization during Khatami's presidency (1997-2005) when Iran faced the rise of a

private sector parallel to the public sector, and acceleration of liberalization since 2005 following Ahmadinejad's election when the state privatized rapidly and sold state owned enterprises (SOEs) to private actors.

DV (prior to liberalization): 1989 to 1997 (during Rafsanjani's presidency), the IRGC was assigned an economic development role and was tasked to generate its own income. The IRGC was institutionally autonomous and politically subordinate to the civilians' demands. It upheld the values of the 1979 Revolution.

DV (post-liberalization): Since 1997, the IRGC began interfering in the politics but the quality and forms of intervention differed significantly under two presidencies of Khatami and Ahmadinejad. During Khatami's presidency (1997-2005), the IRGC started interfering in the politics but not as extensively as in Ahmadinejad's period (2005-2013). Its economic base did not expand and its interference in politics was a result of its politicized nature (linkages to the hardliner elite). Since 2005, however, following rapid liberalization and privatization policies of Ahmadinejad (2005-2013), the IRGC turned into a political power block. The functional capabilities of the IRGC have not registered dramatic changes. Despite claiming to uphold the values of the revolution, the IRGC behaved as a self-interested institution. It still upheld the values of the Islamic Revolution and Iran's theocratic ideology but it also, at times, acted as a corporate institution undermining national security, or hindering state's developmental goals.

One could argue that the IRGC gained power via political means and expanded its economic empire. There are also arguments regarding a symbiotic relationship between the IRGC's political and economic power. However, this research marshals evidence to

illustrate how the increasing power of the IRGC was resulted from the types of privatization policies adopted since 1997 by Khatami's and Ahmadinejad's governments.

Egypt: This section focuses on the aftermath of the economic liberalization that commenced post Sadat's Camp David Accords (1978), and accelerated under Hosni Mubarak's regime until the breakdown of his regime in 2011. The period prior to the liberalization coincided with Nasser's rule; it was characterized by policies of central planning (1956-70). The liberalization policies coincided with Sadat's (1970–81) and Mubarak's (1981–2011) presidencies. Liberalization during Sadat's period was marked by the adoption of Infitah (an open-door policy) but the process did facilitate the emergence of a real independent private sector and led to macroeconomic instability. The acceleration of the liberalization-privatization process in the aftermath of the Camp David Accords (early 80s), supported by international institutions such as the World Bank and the International Monetary Fund, however, produced new windows of opportunity for the capture of state resources by elite networks with linkages to the state. This process of rapid reform continued under Mubarak's rule and led to the further expansion of the Egyptian Armed Forces in Egypt's economic, and, later, political domains.

DV (prior to liberalization): Since 1952 until 1978, and primarily during Nasser's rule, the military was assigned an economic development role and was tasked to provide its own budget. It was politically subordinate and upheld the values of the revolution.

DV (post-liberalization): Since late 1978 (post-Camp David), the military expanded its economic power. The capabilities increased primarily due to foreign aid. The military remained ideologically subordinate to the values of the regime. Since 1981, During

Mubarak's rule (1981–2011), however, the military further expanded its economic power, as well as its political power and ultimately assumed the state's control during and after the 2011 Egyptian Revolution. The military's functional capabilities did not register radical changes. The military behaved as a self-interested institution; it took over the state primarily, maintained its economic interests, and expanded its businesses.

China: Mao's rule (1945–1976) was the period of economic centralization and military's involvement in development projects. This period resembles Rafsanjani's presidency in Iran and Nasser's rule in Egypt. Liberalization started in 1979, during Deng's rule, and led to the expansion of PLA businesses. This period was marked by the formation of the PLA's economic conglomerates. Meanwhile, it was also noticeable for the spread of corruption and the engagement of the PLA in illegal activities such as smuggling. Following the Tiananmen Square protests in 1989, however, a subsequent backlash among the Chinese Communist Party's elite against liberalization and resulting purges in the military, China adopted a policy of reforming the PLA's economic activities. The reform process, however, intensified in 1998 and led to the near eradication of the PLA's economic power and the restoration of civilian supremacy in the economic domain.

DV (prior to liberalization): From 1945, during Mao's rule, the PLA was assigned the development task of rebuilding the country but also was expected to generate its own income. The PLA was institutionally autonomous and politically subordinate. It upheld the values of the revolution.

DV (post-liberalization): Since 1979, during Deng's rule (from 1979–1989), the military gained economic autonomy but was politically subordinate to the civilians. The

PLA commercialized and gained economic autonomy through the process of gradual privatization; China experienced the rise of a private sector parallel to the public sector. Since 1998, during Zemin's rule, the PLA's began divesting its businesses; the PLA became subordinate to the civilians in the political and social domains; its functional capabilities increased.

Alternative Hypotheses

The literature assuming globalization as an inevitable process (race-to-bottom literature) (Hirst 2009, Cerny 1995) or works such as Bunce and Wolchik's (2010) on transnational norm diffusions argue that the pressure of liberalization produces a race to the bottom, pushing states to liberalize their economic and political systems. Subsequently, the spread of democratization and the liberalization of domestic political systems, or international norm diffusion, should impact civil–military relations. The expectation in this race-to-the-bottom literature is democratization of civil–military relations with civilians gaining more autonomy vis-à-vis civilians.

Alternative hypothesis#1: Changes in civilian control are dependent on the degree of political liberalization that states have undergone due to the spread of globalization. In states with a greater degree of political liberalization, militaries are politically less autonomous, culturally more democratic, and functionally more capable.

Note: In line with the literature of democratization and political liberalization, the alternative hypothesis 1 would suggest a causal pathway whereby political liberalization is the most determinant variable in explaining civil-military relations.

Falsified if: (i) There is political liberalization but civil–military relations have not changed. (ii) There is no evidence of democratization but the political control of the military has decreased. Or there is political liberalization but the military has gained more political power.

Regarding the professionalization thesis, Huntington’s (1957) concept of objective control underscores professionalization as an important factor determining civil-military relations. Based on Huntington’s professionalization thesis, once militaries professionalize, there should be an expectation for increased objective control, or increased civilian control, over militaries, regardless of economic liberalization.

Alternative hypothesis #2: Changes in the civilian control are dependent on the degree of militaries’ professionalization. In states where militaries are professionalized and modernized, there is a lower likelihood for the military to interfere in politics.

Falsified if: (i) military is professionalized but the degree of civilian control is the same or has declined. (ii) There is equifinality. There is increase in the degree of political control but the cause is another variable, meaning the professionalization is a development parallel to other variables that determined changes in the CMR.

Data Collection

In this study, I use processes-tracing to find the political critical junctions in each case. In order to identify the causal chains or causal mechanism between the independent and dependent variables (George and Bennett 2005, 2006), method of process-tracing assists researchers in “figuring out *which* aspects of the initial conditions observed, in conjunction with *which simple principles* of the many that may be at work, would have *combined* to

generate the observed sequence of events.” (emphasize added, cited in George and Bennett 2005, 206). Through process-tracing, the researcher assesses the alternative causal pathways to rule out equifinality; it allows the researcher to identify the causal process that determined the dependent variable (George and Bennett 2005, 207). This study utilizes the method of process-tracing to rule out explanations based on political variables such as regime type, institutional engineering, or inter-elite relations. Instead, it identifies the economic variables as the most determinant causes in explaining the behavior of economically-active militaries.

I use library research to gather data on IVs and DVs. I utilize Persian-language books published by Iranian economists on Iran’s economic trajectory, news sources such as Persian-language sources of BBC Persian Television, Deutsche Welle’s Persian service, Radio Farda, Radio Zamaneh, *Entekhab* newspaper, Roozonline, Rajanews, and others, as well as information available in the websites of the IRGC.

I also use English-language newspapers such as *The Wall Street Journal*, *Business Insider*, *The Washington Post*, Public Broadcasting Service’s (PBS) *Frontline* and Tehran Bureau, The Cable News Network (CNN), Bloomberg (world news), Al-Monitor, and Al Jazeera. Reports by the International Monetary Fund, the World Bank, and Stockholm International Peace Research Institute (SIPRI), RAND Corporation, and the International Institute for Security Studies (IISS).

These sources are used to find evidence of (i) economic policies, (ii) primary discussions among local economists or influential elites in the countries under study: criticisms, compliments, or recommendations, and (iii) statements made by state officials,

including the militaries, with regard to the militaries' businesses, politics, or other aspects of control under study.

Chapter 3: People's Liberation Army's Inability to Compete in China's Competitive Economy and Divestiture in 1998

Introduction

Why did the People's Liberation Army in 1998 relinquish its business holdings and submit to the civilians' will, despite its ability to leverage its economic power for political gains? This chapter examines mechanisms behind the expansion and retrenchment of PLA's businesses in the context of China's economic trajectory. It argues that the pace of liberalization and modes of privatization in China created conditions whereby the drive for competitiveness via productivity improvements and export-promotion motivated firms' behavior. In the context of a consensus over China's need to modernize and integrate in the global economy, competitiveness was incentivized, which in its turn rewarded instrumental profit-maximizing behavior for firms. The PLA was not exempt from competitive forces. Its decision to return to barracks during the 1998 divestiture campaign was a consequence of both the state's assertiveness in implementing market reforms and the PLA's inability to run its businesses effectively in a competitive economy.

The first section of this chapter outlines the Chinese economic trajectory that conditioned the PLA's business expansion and later its contraction. The subsequent

sections explain the causal mechanisms—the impact of economic liberalization—on the variation in the dependent variables of political, functional, and social control.

Economic Reform Processes and the PLA’s Economic Behavior

The Chinese economic trajectory gradually departed from central planning, and assumed liberalization policies since 1978. China adopted an Open-Door Policy that combined a gradual trade liberalization with careful experimentation with reforming domestic institutions and regulatory frameworks. A significant consequence of this cautious liberalization has been China’s relative ability in fostering productive capacities of firms, encouraging competition, and relatively strengthening market mechanisms. Parallel to this process of economic reform, the Chinese Communist Party ordered the expansion of PLA businesses into new sectors, such as international trade and manufacturing. This economic role-expansion occurred under conditions of a liberalizing economy; the specifics of the PLA’s role-expansion reflects the overall characteristics of China’s economic liberalization. This section will explain Chinese economic trajectory and the process of the PLA’s economic role-expansion.

China set the primacy of a state-led economic liberalization and adopted a reform strategy of “gradualism” (Chow 2004), “segmented deregulation” (Zweig and Zhimin, 2007), or what became known as “socialist commodity economy” and ultimately “socialist market economy⁵”. In China, there emerged what King and Szelenyi (2005) would name “hybrid capitalism” or “capitalism from below”, a system of co-existence between the

⁵ Vogel, *Deng and Transformation of China*, 682. A concept introduced by Jiang Zemin in 1992 to replace “planned socialist market economy”; it was introduced in the 14th Party Congress.

public and a growing private sector. New private property owners emerged gradually, and the market economy operated alongside the old redistributive system, which also became reliant on market mechanisms (King and Szelenyi 2005, 211). This hybrid system⁶ did not fully prevent clientalism but limited it significantly; it also facilitated a high capacity developmental state (Harris 2013, 66). This was a significant development since the PLA as an economic actor also operated in this increasingly competitive economy, and hence, had fewer opportunities to pressure the civilians for economic gains.

The first aspect of economic liberalization was decentralization of authority over foreign trade via empowering non-central government actors, i.e. “provinces, municipalities, industrial sectors, and enterprises” (Song 2012, 74). This policy of trade decentralization broke the monopoly that state trading companies enjoyed. It allowed new state agencies, various levels of government, and industrial ventures to engage in trading (Chin 2007, 157). To attract foreign capital, China permitted joint ventures’ formation or foreign-run businesses; it offered preferential treatment to foreign investors, such as allowing exports for hard currency, encouraging export by tax holidays, lowering tax rates, and reducing tariffs. It also encouraged modernization of infrastructure, and promoted flexible wage and labor policies, and less bureaucracy. In return, its SEZs were expected to receive foreign capital⁷, foreign management skills and new technologies (Marti 2002,

⁶ Harris uses King and Szelenyi’s (2005) Capitalist Development Pathways typology for his argument.

⁷ World Bank, *Foreign Direct Investment, Net Inflows*. For example, according to the World Bank data, the FDI inflows increased from \$430 million in 1982 to \$43.751 billion in 1998. <https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?locations=CN>

7-8). In accordance with this overall reform strategy, the Communist Party also sanctioned PLA's extensive entrance into new economic domains, which led to both decentralization of PLA's economic activities and joint-venture formation.

In 1985, government and the military issued the 'Provisional Instructions Concerning the Army's Engagement in Production, Business and Foreign Trade' that officially ordered the expansion of the military's economic activities (Cheung 2003, 53). The decentralization strategy led to the establishment of the PLA business at lower levels of its organization, such as regional unit-level businesses. The PLA also began forming joint-ventures. Bickford (1994) categorizes PLA ventures into levels of (i) businesses mainly administered⁸ by General Logistics Department (GLD), (ii) collective enterprises of individual units, and (iii) joint ventures. Furthermore, extending beyond generating funds and operating in domestic market, these ventures entered the international domain, and operated under conditions of the market economy (Bickford 1994, 461). Newly-established PLA firms also varied in their sizes. While regional and unit level firms were small or mid-sized, the PLA established 20 conglomerates until 1993 (Mulvenon 2001, 104).

Therefore, following decentralization and trade liberalization, the PLA businesses turned "from a relatively primitive system of farms and factories to a multi-billion-dollar international business empire of unit-, region-, and sector-based conglomerates, designed to centralize control of enterprises and exploit economies of scale" from 1978 to 1998

⁸ Bickford, *Chinese Military and Its Business Operations*, 461. Although some were also run by the General Staff Headquarters and the General Political Department.

(2001, 136). The PLA firms consisted of ventures operating in diverse sectors of economy, were owned by various levels of military establishment (national, regional, or local units), and had different sizes (small, medium, or conglomerates).

The striking outcome of the Chinese economic trajectory was the government's support for proliferation of new economic actors that operated alongside its old public sector. In fact, the process of economic reform in China did not encompass rapid privatization programs common in many post-communist states, or in both Iran and Egypt. Along with strengthening of its local governments, China also reformed its public sector. With regard to State Owned Enterprises (SOEs), however, the process of reform did not include an ambitious privatization plan; discussions on privatizing ensued in later stages of liberalization, mainly in the 90s. Support for the emergence of new economic actors along with a delayed process of SOEs' privatization reduced opportunities for asset-stripping or capture of state resources in China by economic actors, including the PLA.

The initial policy of SOE reform focused on adopting “the responsibility system” in 1978—that was granting a selected number of SOEs autonomy⁹ in determining their plans for production, marketing, employment, and technological innovation (Huang 2012, 99). The reforms in the 80s gradually increased SOEs' domain of responsibilities; they did not eliminate state ownership; instead, China adopted the “contract system” consisting five contract types with specified responsibilities and rights for the enterprises (Huang 2012, 102). But, the process of privatization did not accelerate until the 90s, more specifically

⁹ Chow, *Economic Reform and Growth in China*, 130. Under the responsibility system, SOEs paid fixed state taxes and had autonomy over their spending.

under Jiang Zemin's¹⁰ leadership (1989-2002). In the 90s, the discussion centered on property rights¹¹ reform; since 1994, a policy known as “emphasizing the big and liberalizing the small” (Huang 2012, 105) guided the state’s privatization plans; the government sanctioned the maintenance of 1000 SOEs via a shareholding system, whereas smaller and medium-sized SOEs were privatized (Huang 2012, 105-106). This strategy of gradual privatization limited the PLA’s opportunities to assume ownership of the SOEs. In China, unlike cases of Iran and Egypt, the process of privatization did not lead to transfer of SOEs to government-affiliated groups, such as crony-networks or the military. The overall outcome has been relative strengthening of the private sector and emergence of small economic actors. For example, half of China’s GDP in the early 1980s was produced by small or mid-sized firms in the service sector and the household farming agricultural sector. 40 percent of industrial production was by what could be accounted as small sized firms in industrially advanced states (Yusuf et al 2006, 52). This development impacted the PLA’s economic production as well.

Throughout the process of reform, the PLA transformed itself from what Cheung calls “a military production complex” to “a military business complex” (Cheung 2001, 20). According to Cheung’s classification, PLA’s businesses encompassed army-owned companies (mainly in service sector), foreign trade companies, along with hotels and

¹⁰ Mulvenon and Yang 2002, *The People’s Liberation Army as Organization*, 7. Run by Central Military Commission’s members, General Logistics Department is one of four general departments (Staff, Political, and Equipment) that engage in policy-making for the PLA.

¹¹ Huang, *State-Owned Enterprise Reform*, 105. The debate was divided into three strands—some linked SOE efficiency to full autonomy in decision-making, others argued for privatization or divestiture, while another group blamed inefficiencies on the uncompetitive environment, and not on ownership.

transportation businesses, military personnel centers, and hospitals (2001, 29-31). For example, by acknowledging the primacy of foreign trade, PLA's central headquarters departments founded trading companies, such as Polytechnologies Ltd., China Xiaofeng Ltd., and Xinxing Corp. as PLA's main trading bodies. Trade, however, was not limited to central headquarters; regional level companies were also eligible to trade. Military units in the regions began establishing small hotels, transportation companies, local stores, and hospitals (Cheung 2001, 29-30).

PLA's enterprises substantially grew in agriculture, industry and service sector. In agriculture, establishment of fisheries, animal husbandries, food crops, and cash crops extended PLA's enterprises beyond historically limited agricultural production such as farming, fishing, or livestock breeding. In industry, PLA owned small or mid-sized firms in mining or manufacturing. These firms produced vehicles, pharmaceuticals, textiles, building materials, machinery, and chemicals. For example, 3700 factories were under PLA's control by 1987 producing 62 percent of PLA's total economic output value. In service industry as well, PLA ventures grew impressively in areas of hotel and boarding services, health services (hospitals), real estate, transportation, and technologies and communications among others (Mulvenon 2001, 86-95).

Table 2: PLA's Expansion into New Economic Sectors

Industry	Service Sector	Agriculture	Int'l Trade
vehicles, pharmaceuticals, textiles, building materials, machinery, and chemicals	hotel and boarding services, health services (hospitals), real estate, transportation, and technologies and communications	fisheries, animal husbandries, food crops, and cash crops	Polytechnologies Ltd., China Xiaofeng Ltd., Xinxing Corp.

Alongside decentralization and cautious privatization, China also adopted an export-oriented strategy. This strategy, incentivized by a foreign exchange rate policy, empowered local governments and private enterprises to engage in international trade and exports (Song 2012, 74). Subsequently, non-central government bodies and non-state actors had to learn to adapt to new circumstances of the international markets. Not only the reform facilitated origination of economic actors that were not linked to the central government, it allowed them to assume responsibilities as traders; their success depended on their performance and their profitability rather than selective protectionism. The PLA's businesses also operated in this gradually liberalizing economy; their survival, similar to other economic actors, depended on their ability to compete with an emerging private sector.

Regardless of size or their ownership, all PLA enterprises also began pursuing profitability instead of merely generating fund for the military. Since 1985, with the decision of the Central Military Commission, PLA's mission was altered: instead of protecting the state from a possible nuclear attack, PLA was assigned the task of aiding the civilian economy. In the context of demobilization of PLA soldiers, and general emphasis on self-employment and productivity, PLA both reintegrated its discharged soldiers in businesses and focused on profitability as a goal (Karmel 1997, 105-107). PLA's focus on profitability was an offshoot of Chinese governments' continued support for marketization and increased competitiveness.

Examining the process of economic liberalization in China reveals a consistent effort to support to encourage competitiveness, within which the PLA businesses had to

operate. The data on China’s economic performance supports above conclusion. World Economic Forum’s growth competitiveness rank suggests China’s increasing economic competitiveness.

World Bank data also suggests incremental improvements in the GDP growth, capital inflows, and domestic credit to the private sector.

Table 3: China’s GDP Growth, Domestic Credit to Private Sector, FDI inflows (1980-2015)

<i>China</i>	1980	1990	2000	2015
GDP growth	\$ 191.15 Billion	\$360.859 Billion	\$1.211 Trillion	\$11.065 Trillion
Domestic Credit to Private Sector (% of GDP)	52.627	86.2	111.123	152.552
FDI (net inflows)	\$ 430 Million (in 1982)	\$ 3.487 Billion	\$ 42.095 Billion	\$242.489 Billion

From 2010 to 2012, 90% of the Chinese exports were produced by the private sector. In addition, it was private sector that produced two-thirds/ three-quarter of Chinese GDP in the same period. While agricultural sector employs 33% of the labor force, service sector and industry employ 36.1% and 30.01% respectively. 9.2% of the GDP production is provided by agricultural sector, whereas service sector produces 48.1% and industry produces 42.7% of the GDP by 2016¹². China has also registered advancements in the domain of new technologies and research and design.

¹² Eckart, Jonathan, “8 Things You Need to Know About China’s Economy”, *World Economic Forum*, June 23, 2016. <https://www.weforum.org/agenda/2016/06/8-facts-about-chinas-economy/>

Table 4: World Economic Forum, China's indicators of Competitiveness in the last decade

	2004/2005(out of 104 states)	2005/2006 (out of 117 states)	2017(out of 134 states)¹³
Company spending on R&D	72 (93)	31 (35)	25
Firm-level tech. absorption	37 (48)	37 (42)	60
FDI and Tech. transfer	44 (51)	57 (65)	59

Due to reforms, China registered both “extensive growth” and “intensive growth”—increased factor input, and growing productivity and efficacy. IMF analysis challenges the conventional wisdom attributing the growth mainly to capital increase and labor inputs. While these factors contributed to the growth, “improvements in productivity and efficiency” were essential to the success of Chinese reform. Restructuring of resources, a shift away from agriculture to the more productive sector of manufacturing was central to growth. Non-state sector development, as well as marketization, has also boosted productivity. The declining share of SOEs in industrial production, and the increasing role of non-state enterprises, demonstrate the impact of opening and gradual marketization. Therefore, growth has not been solely a result of capital accumulation but also caused by “productivity gains resulting from sectorial reallocation, market-oriented reforms, technical progress, and external opening” (1997, 123-124).

Scholars emphasize the significance of competitiveness and contribution of non-state actors to Chinese economic production. Cao (1996) argues that economic

¹³ World Economic Forum, *Global Competitiveness Index: China*, 2016-2017 edition, http://reports.weforum.org/pdf/gci-2016-2017/WEF_GCI_2016_2017_Profile_CHN.pdf

advancement, whether at regional, sectorial, or enterprise levels, was determined predominately by market dynamics. For instance, a cluster of profitable businesses with various ownerships, i.e. state-owned, collectives, funded by foreign partners, townships, or enterprises owned privately, all shared the strategy of utilizing competitive market forces. Adjusting to market alterations, and meanwhile extricating oneself from state's designated tasks, allocation of fixed-priced materials drove the success. Marketization encouraged innovation and helped enterprises to reify their capacities; evidence from China illuminates the vigor of market-oriented policies in pursuit of actualizing a socialist market economy (Cao, 1996, 3-4).

Yusuf et al. (2006) also concluded that small profit-maximizing units controlled three quarters of Chinese economy in the early 1980s. This process of reform also fashioned macroeconomic stability during the initial years. There were low levels of price increase and inflation. The state provided pensions and benefits for SOEs' workers, and suppressed urban industrial labor growth. The banking system did not suffer from the burden of unprofitable assets. If SOEs could not return their capital loans to the banks, the state covered. The Chinese state also did not have any international debts during initial years, and hence, was for the most part macro-economically stable (Yusuf et al. 2006, 52-53).

The ultimate outcome has been (i) the emergence of a private sector operating along with the public one with the private sector producing 90% of China's exports by 2015¹⁴,

¹⁴ Tsai, *The State of China's Economic Miracle*, 144.
http://nbr.org/publications/asia_policy/free/091715/AsiaPolicy20_BookReview_Roundtable_July2015.pdf

(ii) the dominance of mainly small or mid-sized level businesses in this domain, and (iii) gradual property rights' reform delaying/or limiting opportunities for state-level colossal cliental networks' formation. In this economic environment, firms' operation under new conditions depended on their ability to maximize profits. While PLA's businesses grew drastically post-liberalization, under conditions of emerging market economy, PLA as an economic actor as well had to abide by rules of the new system. Hence, based on the conclusions from Chinese economic policies, what were the implications of these reforms, the gradual movement towards a competitive economy, for the PLA's economic activities and the question of the political control?

The Political Control of the PLA

This section tests hypothesis number one (H1) on political control of the PLA. If the economic liberalization and privatization led to the establishment of a competitive market economy, the PLA had limited opportunities to translate its economic power into a political one. The outcome was increased civilian control. The independent variable is the specific nature of economic liberalization, and subsequent competitiveness, discussed in the last section. The increase in the civilian control of the PLA is the dependent variable. Since the PLA's businesses were unable to compete as profitable enterprises in an increasingly competitive economy, the PLA could not leverage its economic power for political gains. In a relatively competitive economy, the PLA became dependent on the civilians' demands, divested its businesses, and returned to barracks.

Regarding Chinese civil-military relations, scholars observed changes in the civilian control of the PLA in the late 90s and early 2000s. There is a consensus suggesting

an observable increased civilian control over the PLA and a reduction in the PLA's political clout in the following decade of liberalization. There has been an increase in the degree of the civilian control along two dimensions: responsiveness and military's assumption of governmental positions. My dissertation, specifically, focuses on the success of divestiture as a critical event signaling an increasing PLA responsiveness to their civilians' demands.

Historically, Chinese militaries engaged in agricultural or industrial production to fund themselves. This tradition of self-financing continued in the Maoist era¹⁵; PLA participated in the economy to fund itself and to assist with the implementation of developmental projects (Mulvenon 2001, 36). However, under Deng's leadership since 1978, the scope of PLA's economic engagement changed; the PLA businesses proliferation in diverse economic sectors. Hence, the PLA's decision to divest its businesses in the 1998 was a puzzling political outcome, especially given both the historical tradition of militaries' participation in the economy, as well as the PLA's transformation into an economic conglomerate. Contemporary reports on divestiture indicated a politically risky decision. Analysts of Chinese politics (1999) characterized it as "one of the biggest gambles" (Lawrence and Gilley 1999, par. 1) of Zemin's career, as well as "one of the most painful and acrimonious initiatives" of his rule.

In examining changes in China's civil-military relations (CMR), scholars have studied political variables, such as inter-elite relations, Chinese Communist Party's institutionalization, state capacity-building, and professionalization of the military as

¹⁵ Mulvenon, *Soldiers of Fortune*, 36. Securing resources for the Korean War, reducing budgetary pressures on the state, and Mao's usage of the military as a means for development justified PLA's participation in the economy.

determining variables. In explaining the divestiture, scholars draw on the above approaches and offer political explanations for the PLA's divestiture. In my research, I depart from those explanations that underscore the role of above-mentioned political variables in the success of divestiture. Instead, I put the locus of explanation on economic variables. I do not dismiss the roles of political institutions, state-level changes, and professionalization, but I argue that the success of divestiture—and succeeding increased political control over the PLA—was a consequence of economic policies discussed in the previous section. In this section, I explain why the PLA was not successful in transforming its economic role into a political one and increasing its leverage over the civilians. Or in other words, I explain how economic considerations played a crucial role in the PLA's decision-making process pushing it to forgo its businesses in 1998.

By testing the H1, I illustrate that the most determinant cause explaining the PLA's compliance with divestiture was the cost-effectiveness of maintaining its businesses in a newly emerging competitive economy. The political variables of PLA's professionalization and transformation of elite relations were parallel developments that contributed to the PLA's compliance with the divestiture. Hence, the evidence suggests that the PLA's economic behavior, i.e. its willingness to divest its businesses, was a consequence of economic policies, and the PLA's economic cost-benefit considerations. The outcome was increased civilian control and the PLA's return to the domain of defense.

As mentioned before, in order to explain PLA loyalty to the Chinese Communist Party, especially after termination of Mao's, and to an extent Deng's personalistic rules, approaches to the study of CMR place the locus of explanation on political variables.

Kiselycznyk and Saunders (2010) categorize Chinese CMR analysis into traditional, combination, and contemporary approaches. The traditional approaches (1989-1995) include the factional model, symbiosis, professional, and party control 1989-1995. The combination approach (1995-1997) merges the above models. Finally, contemporary approaches (1998-2003) focus on the PLA's social or economic linkages, but offer no analytical models (Kiselycznyk and Saunders 2010, 11). The factional model examines elite factions' rivalries, while coalition models underscore cooperation by considering the party and the military as functionally separate institutions. Party control models also focus on Chinese institutions, specifically on institutional peculiarities determining the CMR. The symbiosis model¹⁶ hypothesizes the functional inseparability of the two institutions, and their ambiguously delineated boundaries due to elites' movement across institutions in earlier decades of the CCP rule.

To explain the change from symbiosis to an increasing bifurcation of elite relations in the mid-90s, scholars studied professionalization as an independent variable. For example, Kiselycznyk and Saunders (2010) summarize works of Harlan Jencks, Ellis Joffe, and Paul Godwin. These scholars challenge Huntington's view on professionalism and argue that in the case of China, PLA has been a "political force" but its main motivation has been retaining its institutional interests. Labeling it "political quiescence¹⁷", the PLA has primarily been concerned with improving its defense capabilities. These scholars

¹⁶ Kiselycznyk and Saunders, *Civil Military Relations in China*, 13. Also known as "dual elite role" or "interlocking directorate".

¹⁷ Cited in Kiselycznyk and Saunders, *Civil Military Relations in China*, 15. A characterization offered by Jencks.

identify the party-army relations as a “red versus expert” relations (cited in Kiselycznyk and Saunders 2010, 15). When explaining the divestiture of 1998, the scholars also draw on above CMR models to explain the PLA’s behavior.

For example, Lee (2006) uses the bifurcation model to explain the success of divestiture. Lee (2006) uses Huntington’s notion of subjective control but with a caveat—“strategic subjective control”. Strategic subjective control suggests a shift from subjective personal control to an institutional subjective control coupled with professionalization of the PLA. Deng exercised subjective personal control. Professionalization in Chinese context meant development of institutional mechanisms, bifurcation of civilian and military institutions, rather than adoption of democratic normative values. Hence, “Pulling in” of the PLA into the economy in 1979 during Deng, and its “pulling out” during Zemin in 1998 illustrated civilian elites’ ability to utilize the military in times of transition (Lee 2006, 440-449). While my dissertation does not dispute the gradual bifurcation of China’s civil-military relations, it challenges the view that assumes a professionalizing PLA would prefer to focus on defense only. Why would not an economic conglomerate retain its businesses if it was generating enough profits to fund its defense-related activities?

Explanations based on professionalization thesis do not address four relevant matters: (i) initial negotiations between the civilians and the military included a promise by the government to offer a compensation package to the PLA in return for divesting its businesses, (ii) the civilians began the process of divesting businesses in the mid 1980s— a process known as rectification. The rectification campaign was not as successful as divestiture due to resistance from the military. Unless one can prove that the PLA’s degree

of professionalization changed dramatically within a decade, one cannot attribute a causal relation between professionalization and divestiture. (iii) PLA's involvement in economic activity was in accordance with Chinese militaries' tradition of self-sufficiency. What change forced the PLA to break from its tradition of self-financing? (iv) Ultimately, if professionalization was the cause for divestiture, then why were there reports of tensions between the civilians and military leaders over divestiture?

I argue that the PLA's willingness to divest its businesses was not mere subservience to civilian leaders' needs but a strategic choice made in accordance with the broader consensus on encouraging competitiveness. Given China's steady progress towards global economic integration, and an incremental but consistent process of liberalization despite political or economic obstacles, one can conclude there was a consensus within the society and among the elite to continue the path towards marketization. In the context of this consensus, the PLA's mid- and small-sized ventures' inability to compete effectively was deemed economically costly.

The state's assertiveness in fostering competitiveness, discussed in detail in the previous section, the requirement of competitiveness to succeed in this new economic system, and limited opportunities for asset-stripping made the PLA's businesses reliant on market forces for profitability. In the context of the emerging competitive private sector, running parallel to the public one, as well as carefully executed privatization that gradually transformed the property rights, the PLA fell short of efficiently performing the two tasks of defense and economic production. Divestiture was the logical outcome, despite the poor compensation package. There is ample evidence supporting this conclusion.

For example, PLA's firms' annual revenues increased from 1986 to 1995 by 20 percent on average. This growth however declined to 5.5 percent from 1994 to 1996. PLA's ability to fund itself also declined since 1990. Their after-tax profits (as percentage of defense expenditure) was 3.34% in 1985. Those profits reached to 12% in 1989; from 1990 to 1992, PLA's profits were about 11%. However, by 1996, the profits fell to 7.36% (Cheung 2001, 150). The PLA firms' performance began to decline. Two-third of PLA factories were registering losses. Although the service industry was the most profitable sector, it comprised only 40% of the PLA profits, while firms in this sector were prone to corruption and tax evasion (Cheung 2001, 151).

Reports indicated both low levels of productivity and presence of corrupt practices. For example, with regard to PLA firms' competitiveness, Mulvenon (2001) reviews PLA firms' sector-level productivity. The government was concerned for decentralized and uncoordinated nature of PLA businesses, as well as the their "poor integration", which led to low output. For example, Larger PLA enterprises in the late 80s produced one-third less than other SOEs (Cheung 2001, 42-44). In the agricultural sector, despite regulations and organizational reforms to improve PLA firms' agricultural production, the overall profit was low. Since this sector was not as lucrative, the crime in this economic domain was relatively lower too (Mulvenon 2001). However, both corruption and misconduct at various levels were detrimental for PLA businesses' profitability. Discussing the PLA businesses' losses, Karmel explains, "the high profits and taxes from some businesses... [were] almost certainly eaten away by high expenses and losses." While one-third of state businesses registered losses, the PLA's enterprises' profits were less than average relative to other

state-owned ones, with more than 40 percent of its businesses losing money in the 1990s (Karmel 1997, 110-111).

Cheung (2001) divides PLA businesses' growth into two periods coinciding with the Seventh Five-Year Plan (1986-1990), and part of the Eight Five-Year Plan (1991-1993). From 1986 to 1990, the government encouraged emergence of new PLA enterprises, which facilitated a fast growth of service sector firms in the coastal regions; the regional military units owned these firms and earned seven times more profits (also paid taxes) in 1990 than they did in 1985. Like township and village enterprises (TVEs), 90 percent of these firms were small-sized (low capital and small labor size) and primarily mushroomed in the regions. Producing cheap labor-intensive goods, these firms were primarily autonomous with low government support. Due to lack of adequate government monitoring, however, in a few years, these firms began engaging in illicit activities, specifically smuggling of illegal goods.

Furthermore, competition in the market economy created new demands. Local businessmen and regional governments expected the PLA to compete fairly and to give-up its monopolies. An evidence of such change in attitudes was local Shanxi Province's local government's demand to end PLA's monopoly over mines. PLA owned overall 150 major mines and sold its products either to the government or in the market. Officials of Shanxi Province, however, demanded the Central Government to stop PLA's price manipulations. To resolve the tensions, the Central Government ordered the PLA to transfer more than sixtly mines to the local officials (Mulvenon 2001, 94).

Ultimately, various PLA companies and enterprises competed with one another over market share. Mulvenon (1997) questioned the conventional wisdom that considered the PLA's enterprises as part of "a larger commercially-oriented strategy". He identified three kinds of businesses in China: defense-industrial companies¹⁸, military companies¹⁹, and civilian ones. Military businesses were run by non-civilians. The bureaucracy²⁰ in charge of the defense-industrial companies is distinct, unlike the popular belief. These businesses are bureaucratically separated; their profits allocations are disjointed as well. The author suggests that even military-related companies competed for market-share in both China and the US, and should be viewed as competitors rather than cooperators (1997, 5-9).

Mulvenon's conclusion implies that PLA's corporate activities were uncoordinated and competed over market share. "There is little centralized coordination among the literally thousands of businesses with military affiliations", reported the BBC, describing how individual or retired officers, or even civilians run these ventures, and the GLD was unaware of the actual numbers of these businesses. June Teufel Dreyer, an expert on Chinese politics, referred to the PLA as an entrepreneurial army resembling "feudal

¹⁸ Mulvenon, *Professionalization of Chinese Officer Corps*, 5-9. Defense industrial companies were civilian and accountable to ministers, or the Premier as the head of the government's State Council.

¹⁹ Mulvenon, 1997, 5-6three General Departments (Staff, Political, and Logistical), military regions and districts, reserve or active-duty personnel of three branches of military, as well as Strategic Rocket Forces, are authorized to engage in regulated economic activities. They pay taxes to General Logistics Department (GLD) and reinvest their profits on improving themselves.

²⁰ The Commission on Science, Technology, and Industry for National Defense (COSTIND) was founded in 1982 to centralize supervision over defense-industrial companies and respond to the Central Council and Central Military Commission, which made many believe that defense-industrial companies' proceeds are directed to the PLA.

Chinese warlords”. ‘It’s not a state within a state, but fiefdoms within a state’, states Dreyer in an interview to BBC²¹. Uncoordinated and market-reliant, PLA businesses were pressured to operate as profitable firms. The PLA started generating income but it also began grappling with corruption and losses, especially at lower levels. The presented data thus far suggests unprofitability and uncompetitive nature of the PLA businesses operating in an increasingly competitive economy. Unable to compete effectively, the PLA’s complied with the civilians.

Scholars also have cited the costliness of maintaining the PLA businesses as a justification for divestiture. For example, Bingman (2009) analyzes SOEs’ costliness. He states that the SOEs, including the PLA businesses, were extremely incompetent and operated with deficits; the money spent on maintaining these businesses diverted resources from in the military. Additionally, there was a system of subsidies keeping these PLA businesses afloat. The businesses that were profitable produced civilian goods. Hence, it was reasonable to divest them by returning them to the competitive civilian sector (Bingman 2009, 98). In agreement with Bingman’s assessment, my central argument also suggests that the PLA’s inability to profit from its businesses was the reason behind its willingness to divest its businesses. The implication of this economic behavior on civil-military relations was increasing PLA’s dependence on the civilians for both funding and legitimacy.

²¹ “Business, the Economy: China’s Army Goes Out of Business”, *bbc.com*, December 15, 1998. <http://news.bbc.co.uk/2/hi/business/235592.stm>

The divestiture campaign was a direct response to the dangers of corruption on functionality of market and competition. Since the central government collected revenues through tariffs, and relied on taxation money collected from SOEs, smuggling impacted the state budget (Yang 2004, 115). The conflict of interests between central and local governments led the central government to begin a crackdown on illicit activities in 1990s, particularly under Zemin after the CCP meeting in mid-July 1998. Like other institutions, the PLA was also ordered to put its house in order. (Yang 2004, 118). The extensive and heavy-handed crackdown was set in motion by employing the whole machinery of the state. The purpose of the crackdown was not solely saving the state revenue. The civilians led by Zemin were concerned about the role of businesses run by the military, the police, the judiciary, and various government and party institutions since they impeded market functionality. the process of marketization due to utilization of their privileges or because of existing corruption. For instance, even in 1989, Wang Mengkui, a State Council advisor warned about the dangers of corruption in the PLA both for morale and for its impact on the development of market institutions (Yang, 126). Yang argues that the character of divestiture, its “swift implementation,” illustrated the primacy of political decision-making and civilian elites’ assertiveness (Yang 2004, 134). In addition, the divestiture was in line with an effort to transform “the Chinese state into a regulator state and creating a fairer economic environment²²” (Yang 2004, 143).

²² Yang, *Remaking the Chinese Leviathan*, 143-144. This was due to the government’s push to further decrease the supervisory role of the ministries over SOEs; instead of sectoral agencies, the macro level agencies assumed the role of supervisors and regulators, which meant decreased role of the central government agencies over regulation and ownership. For example, 4 asset management companies and 18 enterprise groups were a result of combining 1546 PLA ventures in provinces, along with 50 governmental institutions.

In explaining the reasons behind the success, Yang offers three explanations: 1- low levels of opposition from PLA leaders, 2- a compensation package offered to the PLA decreased incentives for resistance, and 3- an increased competitive environment made it less attractive to maintain businesses for the PLA. The PLA's inability to compete under market conditions had diminished their profitability; hence, their contribution to the defense budget was in decline. Although firms that were linked to the General Logistics Department— such as Sanjiu Group and Poly Group— were successful, the rest, especially small ones, were not profitable (Yang 2004, 140-141). Yang concludes the following:

“the declining profitability of businesses in an exceedingly competitive business environment appears to have provided the single most important incentive for the military and other institutions to give up their commercial operations that have quite often become a financial burden” (Yang 2004, 141).

In agreement with Yang's argument, this chapter has illustrated how the process of economic reform conditioned the PLA's economic behavior, both its expansion into new economic domains and its decision to retrench from economic domain. The PLA's increasing responsiveness was a result of its growing independence on civilians following its inability to maintain its businesses effectively.

There are alternative accounts that explain the PLA's return to barracks. For example, Jencks (1989) points to the older generation's resistance to reforms, but emphasizes the determining role of young, professional, and less-politicized military personnel (266). In his analysis, however, Jencks also acknowledges the problem of low profitability; he explains that concerns over low profitability of the PLA's businesses existed prior to Zemin's leadership. From 1978 to 1985, the PLA removed itself from construction and police work in order to focus exclusively on defense. It was in the mid-

80s that lower level units entered into production, profitability became imperative, and problems emerged. Economic production became the PLA's major preoccupation, and it even became susceptible to the illegal activities of local authorities and SOEs (Jencks 1989, 265). While generational change could be a plausible reason for the PLA officers' compliance with the divestiture, it doesn't take into account new officers' decision-making logic. After all, the new generation had experienced a new PLA, the one involved both in the economy and defense. Additionally, Jencks, himself, focuses on the economic loss as an important dimension of in Chinese CMR. Even if the generational change impacted the PLA's decision-making process, it does not exclude the importance of PLA businesses' unprofitability as a deciding factor.

Mulvenon (2007) also challenges the following schools of thought in explaining the divestiture: one stresses Zemin attempts to reaffirmed civilian control over the PLA; the other underscores the military leaderships' discontent with corruption as a motivating force for divestiture. The first school offers its evidence based on Zemin's choices, and his attempt to create his own cult of personality, for instance being named "a supreme leader" by military officers (Mulvenon 2007, 225). The second school studies the bargaining process between the two distinct institutions of the military and civilians²³. In disagreement with above explanations, Mulvenon (2007) maintains that divestiture questioned the bargaining process. Despite common belief, the civilians did not hold their end of the

²³ Mulvenon, *The PLA in the New Economy: Plus Ca Change, Plus C'est la Meme Chose*, 225-226. This explanation sees the divestiture as a bargain between military and civilian leaders whereby (i) PLA enterprises had to be transferred to local and regional governments in a one-time process, and (ii) PLA yearly budget had to increase.

bargain²⁴. The PLA received less than expected in compensation both in absolute and relative terms; the compensation did not cover the PLA enterprises' losses (Mulvenon 2007, 227). This is a significant conclusion: first, it suggests increased dependence of the PLA on the civilians. Secondly, by highlighting PLA's demands for compensation, it undermines those arguments that underscore the role of PLA's professionalization as a determinant variable. If professionalization was the reason behind compliance, why were there reports of tensions between civilians and military elite?

Not only was the process of divestiture kept relatively secret, interviews with PLA leaders indicated "heavily strained" relations between civilians and the military. There were two main reasons behind the PLA's dissatisfaction: damage to the PLA's reputation due to publicized information on corruption and a poor compensation package²⁵ (Lawrence and Gilley 1999, par. 2-3). For example, US intelligence reported tensions between premier Zhu Rongji and the PLA after Zhu commented on smuggling by Tiancheng, an important company owned by the PLA's General Political Department. Zhu pointed to the company's failure to pay 50 million renminbi in sales and import taxes (Lawrence and Gilley 1999, par. 7). there were also fears of serious tensions between civilians and the PLA, which were expected to emerge over Taiwan policy or other security-related issues, such a Chinese

²⁴ Mulvenon, *The PLA in the New Economy: Plus Ca Change, Plus C'est la Meme Chose*, 226. Mulvenon explains that sources suggested a compensation of RMB 15-30 billion per year, but two months later, the same sources suggested RMB 50 billion. US sources suggested a negotiation between civilians offering RMB 1.2 billion and military demanding \$ 24 billion. Whereas, GLD claimed yearly RMB 4-5 billion in addition to double digit budgetary increase.

²⁵ Lawrence and Gilley, *Bitter Harvest*, par. 3. "compensation... this year were based on a wildly low estimate of 3.5 billion renminbi (\$422.7 million) in annual profits from the companies, or less than 4% of the military's annual allowance from the government."

weapons' proliferation policy or its foreign policy in South China Sea territorial disputes (Lawrence and Gilley 1999, par. 6). Experts also expressed concerns regarding Zemin's decision. Huang Jing, a Utah State University expert on Chinese economics, states that "I am a person who is generally positive on PLA reforms, but in this case, I think Jiang has lost more than he gained." (Lawrence and Gilley 1999, par. 6).

Furthermore, the divestiture campaign was not civilians' first attempt to limit the PLA's business activities. Concerned with problems associated with low productivity and corruption, the Chinese state adopted measures to address both inefficiencies and corruption in the 80s. For example, In the industrial sector, series of reforms aimed at making firms competitive and reliant on the market forces. The reforms, however, failed to improve the situation because the PLA firms still relied on subsidies; their labor force was also inefficient. Furthermore, PLA firms' competition over raw material and market share contributed to what Mulvenon characterized as "underindustrialization and serious waste" (2001, 91-92).

As in the broader efforts to direct the process of reform, PLA smuggling was addressed by new regulations. To address corruption in the PLA, the state embarked on a process known as rectification in 1988–1990 that prohibited the following activities by military units: import of restricted commodities, production and sale of low quality commodities, utilization of military equipment for economic production purposes, using infrastructure for smuggling, unapproved usage of personnel for economic activities, price distortions, and operation of business by active-duty or retired personnel (Cheung 2001, 43). Additionally, Civilian elites, as well as the General Logistics Department began

adopting measures to address illegalities and inefficiencies. For example, in the late 1980s, the Central Military Commission (CMC) prohibited military departments from participating in commercial activities, specifically those involved in trade. In 1989, among other economic activities²⁶, the military was banned from importing restricted commodities (equipment, cars, electrical appliances, accessories). (Cheung 2001). Several attempts aimed at limiting the military's economic activities, however, failed in effectively curbing illicit activities.

Therefore, evidence of rectification campaign in the 80s and existence of tensions between the civilians and the military over the divestiture in 1998 undermines the professionalization thesis. Additionally, while in some places PLA handed over its businesses, in other cases, it tried to maintain the management and profits of its businesses, especially in strategic sector companies such as China United Airlines and Great Wall Telecom. Another strategy the PLA units used in order to keep their businesses was reclassification of military enterprises to non-military ones (Mulvenon 1-3). It is also worth noting that the divestiture never completed, but about 10,500 enterprises were transferred in one year impacting 70,000 workers. Nevertheless, there were still 10,000 PLA ventures, as well as SOEs, that remained under the PLA's control in 2009. More importantly, Bingman explains that the divestiture took place in the context of valuing "competitive

²⁶ The production and sale of low-quality goods, utilizing military equipment for production, exploitation of military facilities for smuggling, unauthorized sell and lease of military farms, exploiting military vehicle licenses, bank accounts, and invoices, exploitation of profits, unauthorized labor and business services, misuse of privileges in taxation in order to buy off local businesses, haphazard expansion, purchasing high priced products, unlawful purchases, racketeering, or increasing prices, individuals.

contracting” under the conditions of a market economy, and that the PLA “dumped mostly the low-end debt ridden activities onto local governments” (2009, 98-100).

Although Mulvenon dismisses the local media’s perception of tensions between civilians and the military over divestiture, but he, also, stressed the importance of the existence of negotiations between military and civilians over both a compensation package and defense budget. It appears that disagreements came from tensions within the military, with senior military leadership and combat units favoring divestiture whereas regional and district commanders and members of the departments of logistics and management of enterprises opposing it. Since the idea of compensation hinged upon what might be called ‘the trickle-down theory of PLA economics,’ local military units were suspicious of receiving profits out of this deal. The PLA adopted measures to calm discontent by increasing rank and file wages by 10 to 25 percent. Regardless, military units resisted divestiture by folding their enterprises under other institutions or handing over the unprofitable ventures but meanwhile protecting the profitable ones (Mulvenon 1-3).

Above discussed discrepancies in the PLA’s behavior suggests that it divested its businesses because of their lack of profitability as oppose to other political considerations. The proliferation of the PLA ventures at lower levels, and a privatization policy limiting prospects for capture of state resources, coupled with increasing economic competitiveness created conditions where the PLA’s firms’ survival depended on their profitability. The PLA’s smaller firms’ inability to compete did not leave the PLA with any choice but relinquishing its lower level business assets. The ultimate outcome was increased civilian authority.

Explanations that rely on political variables are fruitful for understanding the changing nature of CMR in China; however, they fail to fully explain the PLA's economic behavior regarding submission to divestiture, which led to increased civilian control. The 1998 divestiture was, in reality, a culmination of previous rectification campaigns. Moreover, the PLA's continued compliance despite the poor compensation package was also puzzling. These approaches offer explanations for PLA decision to divest but fail to account for the causal mechanism behind the decision-making process, that is the role of economic considerations in decision making.

The specifics of economic reform, i.e. the focus on trade liberalization, decentralized center-regional relations, and the gradual reform of property rights, produced two significant outcomes: the emergence of small- and mid-sized ventures in the regions and a private sector parallel to the state, and the reliance of newly emerged enterprises on playing market rules for productivity. These developments impacted the PLA businesses as well, since not only did lower-level units begin expanding, they also focused on profitability as a goal. Divestiture targeted the lower-level economic ventures to curb the effects of illegal smuggling, as well as low profitability, in the regions. Since the reform process had created dispersed and uncoordinated PLA businesses—or in other words, there were considerable numbers of lower-level businesses and the PLA businesses did not operate as unified entities—the PLA's top brass did not have incentives to sanction the continuation of regional units' operation.

Therefore, the consensus between military and political leaders to focus on professionalization of the PLA was part of the decision-making equation regarding the

divestiture, but the fact that PLA's economic performance in the regions was poor ultimately decided the outcome. In the absence of opportunities for economic expansion, the PLA did not have enough economic reason, or leverage, to pursue economic activities. Subsequently, it did not have enough incentive to resist divestiture and transform its economic power into political power. The PLA's compliance might have been partially influenced by the political determinants of professionalization and party–military bifurcation, but the determinant cause was the absence of or gradual decrease in opportunities for economic expansion outside of market mechanisms.

The Functional Control of the PLA

This section tests hypothesis number two (H2) concerning the impact of economic policies on the functional control. According to H2, if gradual economic integration generates income for the state, the economically active military (the PLA) will have fewer opportunities to turn itself into an *economic* interest group, and the subsequent outcome would be a possible increase of the PLA's functional control. By examining available data on the Chinese military doctrine, defense expenditure, weapon procurement, organizational restrictions, and recruitment policies, this section examines PLA's functional capabilities.

With regard to integration, the PLA's record has been mixed. Military doctrine has undergone changes for decades to match the demands of a changing international environment, but the actual capacity to carry out new tasks has not met expectations. Military doctrine has transformed from “people's war” (1935-1979), to “people's war under modern conditions” (1979-1985), “limited war” (1986-1991), “limited war under high technology conditions” (1991-2005), and ultimately “limited war under high

technology and information conditions” (Mulvenon 2007, 84). Doctrinal changes demonstrate the Chinese leaders’ ability to assess and adapt to the international security environment. Since mid 1980s, along with economic liberalization process, the military doctrine also echoed China’s shift of attention to procurement of new technologies. A change from a people’s war doctrine to preparedness to conventional wars under new technological conditions suggest a shift in planning and priorities.

For example, since the Gulf War of 1991, China manifested a new direction in its doctrine by investing in new technology, especially electronic warfare and countermeasures, ballistic missile systems, early warning and command systems²⁷. Correspondingly, the Commission on Science, Technology, and Industry for National Defense (COSTIND) pressed for improving China’s industrial base. The PLA began reorganizing and learning new skills, and adopted what Shambaugh names “flexible response”—that is the PLA’s attempt to improve capabilities that would allow it to face conventional war, nuclear war (or WMBs), air-to-air or coastal and naval battles, and force deployments in the peripheries (Shambaugh 2002, 69-72). Similarly, Chase et al. (2015) point out the impressive transformation for a military that was referred to as “junkyard army,” characterized by low quality weaponry, personnel, and training, as well as by rampant corruption (13-14).

Hence, the data illustrates the overall success of economic reform and its contribution to GDP growth; the growth enabled civilians to invest in military

²⁷ Shambaugh, *Modernizing China’s Military*, 69. The new doctrine was known as “limited war under high-technology conditions”.

modernization without heavily burdening the state. The quality of the functional control, i.e. the nature of weapons and ability to trade-offs in mobility, has also increased. China has invested in the production of new weapons as well as in weapons procurement. It's ability to utilize those weapons, i.e. the skills aspects of functional control, however, has not kept pace. Therefore, while budgetary increases, as well as investing in China's industrial base, have led to its overall technological modernization, the training of soldiers to utilize new equipment has been slow.

China's Military-Industrial Complex (CMIC) is the main provider of the weaponry to PLA's ground-forces, air-force, navy, and missile forces. For example, since 1960s, China has masterfully produced short and mid-range, and intercontinental ballistic missiles. Production of competitive surface-to-air and surface-to-surface missiles in the 1980s was another accomplishment. However, overall, the CMIC hasn't been successful in production of modern weaponry (Shambaugh 2005, 85). Bitzinger (2000) also elaborates Chinese Industrial Complex's capabilities to produce and utilize advanced military technology. The industrial complex has incrementally advanced for the past two decades, but the overall progression has been limited since some areas of technology have been developing relatively better than others (Bitzinger 2000, 9-10).

Improvements in the civilian technologies, specially advancements in science and technology, has also benefited the military from overall advances in tech and science. In the domain of the defense solely, China has aimed at producing "long-range precision-strike, command, control, communications, computing, and intelligence (CI), information warfare, and area denial". With regard to other technologies, such as commercial dual-use

technologies in areas of aerospace, shipbuilding, and microelectronics, China purchases them from Russia, Israel, and some Western states (Bitzinger 2000, 11-16). These findings suggest that overall economic development has assisted China in enhancing its functional capabilities. Therefore, there is clear evidence of increasing functional control prior to and post economic liberalization. China's ability to produce competitive weaponry occurred in the aftermath of its modernization plan—following economic liberalization.

Examining functional capabilities reveals a consistent effort on the civilians' part to address the inefficiencies. For example, two factors of institutional reorganization and marketization contributed to the shift in military production in 2001. Establishment of PLA General Armaments Department in 1998 and demotion of Commission on National Science, Technology, and Industry for National Defense (COSTIND) allowed for new supervisory body to introduce successful reforms. More importantly, modifying the CMIC from a state-owned and heavily subsidized organization to that of sensitive to market mechanisms was another major step. The process has been incremental (mainly since 2004), but introduction of contract-bidding was imperative in reforming the CMIC's procurement process (Shambaugh 2005, 87). Economic liberalization policies, not only increased state's budget and its ability to invest in the military, they also sanctioned growth of an industrial base capable of producing weaponry.

Analysis underscores the importance of continued economic success on improving military capability. Projecting the PLA's modernization process through 2025, Chase et al. (2015) list slowing economic growth, social instability, and possible violence in Tibet as some of the factors that could possibly change the current trajectory. Since economic

growth and the subsequent growth of the defense budget, without burdening the GDP and government spending, were imperative in the success of the modernization project, RAND predicts that a decline in growth, as well as negative externalities of growth, could be detrimental to defense spending and modernization plans (2015, 21-22). Therefore, economic policies and economic growth are imperatives in creating suitable conditions for increasing functional capabilities.

With regard to skill and training, however, China is not as efficient as modern armies. It appears that increase in functional control has been linked to changes in the strategy, weapons procurement, and modernization due to the economic growth. But the actual capacity in utilizing those new resources is weak. Chase et al. (2015) examine “two incompatibles” and “two gaps” prevalent in Chinese discourse on PLA efficacy since 2006. The “incompatibles” are (i) the gaps between the level of modernization and the capability for winning a local war in the information age, and (ii) between the military’s current capability and its historical mission.

The two incompatibles and two gaps assess the same issue from different angles, i.e. the former states the problem while the latter identifies the root causes. The problems include an incongruence between training and required skills to win in combat in an “informatized” age; organizational and structural problems, as well as personnel’s inaptness to carry out the tasks of modern warfare; obstacles for force development due to structural inefficiencies; and ultimately ineffective logistics. In terms of the PLA’s ability to carry out historical tasks, with the exclusion of force development, the related areas of training, organization, and logistics lag behind (2015, 69-72).

Despite disadvantages²⁸, as mentioned before, Chinese authorities have been adopting measures to address systemic weaknesses, which indicates a willingness to invest in functional capacity. For example, in order to address its shortcomings in the quality of personnel, PLA accepts graduates from science and engineering schools, and programs to pay for student loans in return for joining the PLA has been put in place. Higher education requirements for admission, and better pay and benefits are other strategies (Blasko 2012, Kindle Locations 2012, 5499-5501).

In conclusion, the PLA's functional capability has improved post-liberalization. Economic growth has generated funds for the state to invest in military modernization. It has also strengthened the industrial base, which has contributed to weapons production programs. The state's capacity to invest in the military's capabilities has also meant that the civilian and military leaders were responsive to the changing international security environment, and adapted its military doctrine.

The Social Control of the PLA

According to hypothesis number 3 (H3), if gradual economic reform reduces opportunities for transformation of militaries into economic interest groups, social control would either remain the same or increase. As a dependent variable, social control refers to militaries' values and their compatibility with societal norms, both domestically and

²⁸ Bitzinger, *Going Places or Running in Places?*, 28-30. Listing the impediments to utilizing new technologies, Bitzinger also elaborates technical, structural, and cultural categories. The author names "weak system integration capabilities" and "limited workforce expertise" as two main technical issues, while "overcapacity" (redundancy in production), "lack of sufficient capital", "the highly compartmentalized, vertically integrated, and secretive nature of the Chinese arms industry" as cultural obstacles. "Heavily centralized, hierarchical, bureaucratic, and risk-averse corporate culture" constitutes the cultural problem; in addition to managerial problems, the 'SOE mindset' hinders capacity to achieve competitiveness.

internationally. Militaries' social control is measured by observable changes in military values and attitudes. Therefore, the social control changes if the military's values either do not reflect the collective values of the society or transform in accordance to changes in societal values. This section argues that during the period of illegal smuggling in the 1980s, the PLA's values did not reflect the overall values of the communist revolution, as well as traditional values of the PLA. However, since the PLA could not transform itself into an economic interest group, it has been able to maintain its commitment to both communist and traditional Chinese values pertaining to militaries' position in society.

In terms of the PLA's military culture, a Report by Kaufman and Mackenzie (2009) explains PLA's cultural transformation. Both Chinese traditional military thinking and teachings of Marxism-Leninism contributed to the PLA's culture. From Marxist-Leninist thinking, the PLA concludes the importance of "party-army principle", "mass mobilization", "broad consultation, limited participation", and "voluntarism". There is a belief in prominence of morality vis-à-vis material capability, and calling itself a "people's army". Hence, PLA defines a moral obligation to treat people humanely and its personnel with kindness. PLA perceives itself morally superior to average citizens and is expected to garner populations' support by modeling socialist morality and behavior²⁹. If the PLA prided itself on being the "people's army", its illegal smuggling and corruption in the 1980s illustrated how the liberalization and privatization complicated the above aspect of the social control. However, throughout decades of communist rule, the PLA has remained

²⁹ These moral obligations have been codified in "Three Main Rules of Discipline and Eight Points of Attention", and "Servicemen's Moral Standards".

loyal to the values of communism and, when necessary, has sided with the ruling elite and their social constellations that favored early revolutionary values.

There is also consistency with Chinese traditional values of humanitarianism and the PLA's practices. Drawing on Confucian tradition of "Soldiers must be righteous, violence must be directed at the right targets" (cited in Wenjuan 2013, 6), the PLA is trained to value humanitarianism in its conduct (Wenjuan 2013, 6). Hence, the PLA's social values have not changed post-liberalization. Wenjuan (2013) argues that both the Chinese government and the PLA have been implementing measures in compliance with international humanitarian law (IHL). Not only does China have a tradition of humanitarianism, it also has both ratified and undertaken legal measures to implement IHL.

China is signatory to Hague Convention (ratified in 1917), Geneva Convention (ratified in 1956), Additional Protocol I & II (ratified in 1983), The Hague Cultural Property Convention (2000), Treaties on the Use of Certain Weapons (ratified in 2000), and Geneva Gas Protocol (ratified in 1952). It promotes further expansion of these protocols; it also supports Biological Weapons Convention, Chemical Weapons Convention, and Comprehensive Nuclear Test Ban Treaty. (Wenjuan 2013, 8-15).

China has adopted legal measures domestically to implement the above-mentioned protocols. For example, article 67 of National Defense Law of PRC sanctions the military to comply with international treaties. "Export Control of Dual Use Biological Agents and Related Equipment and Technologies Regulation" and "Export Control of Chemical Products and Related Equipment and Technologies Regulation" are among other legislature enacting compliance with conventions. In addition, it has actively supported

international criminal justice cases , has a history of complying with the Geneva Convention during its wars, and has incorporated international humanitarian law's education into the PLA's curriculum (Wenjuan 2013, 8-15).Therefore, PLA's loyalty in upholding humanitarian values suggests that despite its economic activities post-liberalization, the PLA did not transform its social values.

Therefore, in terms of social control, China's economic reform policies have not changed the PLA's social values. The PLA remains a professional army loyal to the CCP. As a professional institution, it does assert itself in areas relevant to its expertise but it does not operate as an economic interest group.

Conclusion

This chapter argued that a relative success in establishing a competitive economy, gradual privatization coupled with reforming regulatory frameworks, limited opportunities for asset-stripping. Although there was corruption in the form of illegal smuggling, economic actors and primarily the PLA did not have opportunities to capture state resources. Moreover, state's commitment to establish market mechanisms manifested itself in its persistence in reforming regulations regarding PLA businesses. Under conditions of an emerging market mechanisms, the PLA businesses were also expected to operate as profitable firms. However, PLA was not successful in maintaining its economic production effectively. Its firms registered losses and could not compete with an emerging private sector. The outcome was PLA's subservience to the civilian demands by divesting its businesses in 1998. Unable to profit economically, the PLA became more dependent on its civilian counterparts for both funding and legitimacy. Furthermore, unable to transform

itself into an economic interest group, the EAF's functional and social controls have increased and remained the same respectively.

Chapter 4: Iran's Islamic Revolutionary Guard Corps: An established but non-Domineering Economic and Political Player

Introduction

As a consequence of Mahmood Ahmadinejad's privatization and economic liberalization policies from 2004 to 2013, businesses of Islamic Revolutionary Guard Corps (IRGC) expanded into new sectors of the Iranian economy, including finance, trade, and oil and gas. Not only did the IRGC become a more visible economic player a result of this expansion, it also amassed a considerable degree of political leverage that culminated in the so called "election coup" in 2009 that brought Mahmood Ahmadinejad into power³⁰. Subsequently, many analysts and politicians, including then U.S. secretary of state, Hillary Clinton, warned about Iran's transformation into a military dictatorship³¹. Furthermore, many cautioned that the Iranian economy was becoming militarized. Belying these speculations, the IRGC failed to dominate Iran's economy or politics. It did, however, succeed in establishing itself as a significant economic and political player. The IRGC is

³⁰ "The Leaders of Iran's 'Election Coup'," *pbs.org*, last modified June 18, 2009, <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2009/06/the-leaders-of-irans-election-coup.html>

³¹ "Clinton: U.S. sees Iran moving to military dictatorship," *cnn.com*, last modified February 15, 2010, <http://www.cnn.com/2010/POLITICS/02/15/clinton.iran/>

not the most dominant actor but it has amassed enough leverage to engage in the process of bargaining with the ruling elite.

This chapter will illustrate how Iran's uneven liberalization process since 1989 both conditioned the IRGC's economic role-expansion and constrained its ability to completely dominate the economy, and consequently, the political arena. On the one hand, privatization policies facilitated the proliferation of crony-networks, including the IRGC businesses, in a semi-public economic domain that operates parallel to the private and state sectors. On the other hand, haphazard economic planning failed to establish a competitive, diversified economy. In this uncompetitive economic system, the survival of the IRGC's businesses did not depend on their profitability; this uncompetitive economy created conditions that facilitated the maintenance of the IRGC businesses. However, competition among the crony-networks operating in the semi-public domain constrained the IRGC's ability to capture the state completely. The outcome has been the establishment of the IRGC as an economic actor that has enough leverage to engage in negotiations with the dominant elite but has been unable to gain sole control of Iran's economy and politics. The rest of this chapter will explain Iran's economic trajectory, the IRGC's position in Iran's economy, and its economic behavior, and finally the impact of economic policies on three dimensions of military control.

Economic Conditions and the IRGC's Economic Behavior

When Ahmadinejad came to power, Iran had already undergone two decades of inconsistent and unorganized liberalization and privatization. This uneven economic trajectory impacted the economic power of the IRGC in three ways: (i) the acceleration of

privatization since 2004 provided the IRGC with opportunities to capture the state resources, (ii) the economic system characterized by overall lack of competitiveness meant that the IRGC could keep its businesses despite their unprofitability, and ultimately (iii), the IRGC, unlike the case of Egyptian Armed Forces, failed to dominate Iran's economy and politics. Iran's caveat, compared to China and Egypt, lied in the existence of competition among the crony-networks operating in Iran's extensive semi-public economic sector; established and consolidated throughout decades of haphazard privatization, these crony-networks checked the IRGC's economic ambitions. The rest of this section will delineate two parallel developments: the trajectory of IRGC's economic role expansion and the overall economic processes that conditioned and constrained the IRGC's economic behavior.

The IRGC's Economic Expansion

It was during Rafsanjani's presidency (1989–1997) that the IRGC became an economically-active military. Rafsanjani—who assumed office in the aftermath of the Iran-Iraq war (1980-1988)—focused on combined goals of economic liberalization and reconstruction³². Known as the “Reconstruction Era³³”, the government focused on rebuilding Iran's war-torn economy by addressing inefficiencies of central-planning and undertaking massive developmental projects. To implement his modernization plans, Rafsanjani ordered the IRGC to engage in economic reconstruction projects; it was a

³² Karshenas and Hakimian, *Dilemmas and Prospects of Eco. Reform & Recon. In Iran*, 44-45. The economic liberalization aimed at reforming price controls, quantitative trade restrictions, and to unify the exchange rate.

³³ دوران سازندگی

strategy to both demobilize the IRGC in the aftermath of war and to utilize its capacities for economic development³⁴.

The scope of the IRGC's economic activities changed with its expansion into new economic sectors concomitant with the acceleration of liberalization and privatization since 2004–2005. This period corresponded to the final two years of Khatami's presidency (1997-2005) and primarily the period of Ahmadinejad's presidency (2005-2013). The IRGC expanded into new economic sectors, such as oil and gas, and finance. Although the data is inconclusive, the estimates suggest that the IRGC businesses produced at least one third of Iran's GDP by 2010³⁵—during Ahmadinejad's first tenure. According to the WikiLeaks cables, the IRGC's total assets by 2010 were about \$180-\$250 billion³⁶. While there is no available data on the total assets of the IRGC before privatization, local analysts estimated that Rafsanjani's sold \$7 billion worth of State Owned Enterprises (SOEs) during his privatization plan, whereas by the beginning of 2005, the government sold \$50 billion worth of assets, the majority of them to the IRGC³⁷.

It is worth noting that in the cases of China and Egypt militaries became economically-active during the periods of central planning. The IRGC's economic role-expansion, however, occurred during Rafsanjani's liberalization period when the

³⁴ Mobilized during the Iran–Iraq war (1980-1988), the IRGC has operated parallel to the Islamic Republic of Iran Army, the regular military.

³⁵ Borger Julian, and Tait, Robert. “The Financial Power of the Revolutionary Guard”, *theguardian.com*, February 15, 2010. <https://www.theguardian.com/world/2010/feb/15/financial-power-revolutionary-guard>

³⁶INSIGHT- IRAN- List of IRGC firms- IR2, The Global Intelligence Files, *Wikileaks.com*, February 13, 2010. <https://search.wikileaks.org/gifiles/?viewemailid=1116599>

³⁷ Ganji, Akbar. “Iran: The High Cost of the IRGC's Economic Might”, *nationalinterest.org*, December 4, 2013. <http://nationalinterest.org/commentary/iran-the-high-cost-the-irgcs-economic-might-9495>

government intended to curb inefficiencies caused by economic nationalization that was adopted post 1979 Revolution. Despite this seemingly different context, my research accounts for Rafsanjani's presidency as a period of central planning for three reasons: (i) the emphasis of the government was primarily on state-led reconstruction, (ii) the liberalization process was short-lived, caused a short-term debt crisis, and was reversed, and (iii) Article 44 of the constitution, adopted post-revolution, allocated the control of key industries to the state sector³⁸; That meant the government had limited options for privatization. In addition to the above-mentioned developments, it was with the leadership of Rafsanjani that Iran's semi-public sector grew with significant implications pertaining to the IRGC's economic power in the following decades.

Therefore, regarding to both overall economic planning and the IRGC's economic role-expansion, Rafsanjani's period resembled periods of central-planning in Egypt and China. Similar to the cases of the People's Liberation Army and the Egyptian Armed Forces, the IRGC was primarily involved in economic development projects. The IRGC, in 1989, with Khomeini's approval, established Khatam Al-Anbia³⁹, its engineering company. Its commanders assumed managerial positions in the firm. The reason for Khatam Al-Anbia's establishment, according to the supreme leader's representative, was

³⁸ "The Constitution of the Islamic Republic of Iran", *Iran Human Rights Documentation Center*. The Constitution's Article 44 classified the economy into three sectors of state, cooperatives, and private. While the state assumed management of large-scale industries, foreign trade, major minerals, banking, insurance, power generation, dams and large-scale irrigation networks, radio and television, post, telegraph and telephone services, aviation, shipping, roads, railroads, etc. The private sector entailed agriculture, animal husbandry, trade, and industry that supplemented the state sector.
<http://www.iranhrdc.org/english/english/human-rights-documents/iranian-codes/3017-the-constitution-of-the-islamic-republic-of-iran.html?p=19>

³⁹ قرارگاه سازندگی خاتم الانبیا

utilization of the IRGC's war-era machinery and equipment for reconstruction projects⁴⁰. In an interview with *Entekhab* newspaper in 2014, Rafsanjani justified his decision to assign the IRGC economic projects. Specifically in reference to Karkheh Dam's project, Rafsanjani stated that "...[the IRGC] had acquired machinery for the [Iran-Iraq] war. It had bought bulldozers, trucks, loaders, and cranes required for Karkheh Dam's embankment, and accomplished the task easily and quickly. It did a quick job but did not own anything."

The extensive nationalization of industries, sanctioned by the Article 44 of the constitution, marginalized the private sector. Since 2004, however, the Guardian Council⁴¹ issued a directive permitting privatization of "foreign trade, banking, insurance, power generation for domestic consumption and export, telecom and postal service, railway, airlines, and shipping"⁴². In 2005, the supreme leader, Khamenei, also sanctioned⁴³ acceleration of privatization by Ahmadinejad's government (since 2005). This privatization, however, did not lead to the growth of an independent private sector. On the contrary, Ahmadinejad's privatization became detrimental for the private sector's growth since it did not focus on selling the SOEs to the private actors. By 2013, the sale of

⁴⁰ "Shedding Light on IRGC's Extensive Economic Activities," *dw.com*, August 20, 2007. <http://www.dw.com/fa-ir/پاسداران-سپاه-عظیم-اقتصادی-فعالیت‌های-بر-پرتوی-ir/a-2745386>

⁴¹ "Guardian Council," *bbc.com*. An influential clerical body in charge of monitoring passage of bills in the parliament to assure their consistency with teachings of Islam. It has veto power over Parliament's decisions. http://news.bbc.co.uk/2/shared/spl/hi/middle_east/03/iran_power/html/guardian_council.stm

⁴² Mostashari, Ali. "Privatization of State-Owned Enterprises in Iran: Panacea or Prescription for Disaster," *Payvand.com*, May 11, 2004. <http://www.payvand.com/news/04/nov/1043.html>

⁴³ "General Policies of the Supreme Leader Regarding Article 44 of the Constitution," *Ministry of Interior*, n/d. <https://moi.ir/Portal/file/?226759/سیاست‌های-کلی-ابلاغیه-مقام-معظم-رهبر-ی-در-خصوص-اصل-44-قانون-اساسی.pdf>

government assets constituted \$ 80 billion, but only 17 percent had been sold to the private sector; the rest had been transferred to the IRGC and other crony-networks⁴⁴. Encompassing transfer of SOEs to regime affiliates, including the IRGC, Ahmadinejad's privatization plan became infamous as "pseudo-privatization"⁴⁵ or "customization"⁴⁶ (*ekhtesasi-sazi*).

There is a consensus among analysts and journalists in the Iranian media that Ahmadinejad's pseudo-privatization conditioned the IRGC's expansion into new economic domains such as finance, banking, oil and gas, and manufacturing. Embracing Khamenei's privatization proclamation, Ahmadinejad accelerated privatization in Iran. He claimed that the sum of privatization prior to 2005 had been \$3 billion while under his presidency about \$30 billion were transferred via the Tehran Stock Exchange. Iran's Privatization Organization⁴⁷ provided similar numbers. Reportedly, Ahmadinejad prided on "Iran's speed of privatization compared with other state-run economies, which, Ahmadinejad said, had taken twenty years to achieve what Iran had achieved in five" (Alfoneh 2010, 3).

In this context, newspapers reported on the IRGC's assumption of new economic projects on non-bidding basis. For example, in 2007, the IRGC won several big projects:

⁴⁴ Ganji, Akbar. "Iran: the Cost of the IRGC's Economic Might," *The National Interest*, December 4, 2013. <http://nationalinterest.org/commentary/iran-the-high-cost-the-irgcs-economic-might-9495?page=3>

⁴⁵ شبه خصوصی سازی

⁴⁶ اختصاصی سازی

⁴⁷ "Short History", Iranian Privatization Organization, *en.ipo.ir*. An organization established in 2004 to assist with privatization. However, its mission expanded significantly since 2008 by adoption of "Law on Implementation of General Policies of Article (44) of the Constitution".

the Asaluyeh natural gas pipeline, completion of Tehran's Metro, and the pipeline for fifteenth and sixteenth phases of the South Pars oilfield. Those three projects totaled \$7 billion and were awarded without a bidding process. The construction of Development of Shahid Beheshti Waterfront, worth \$341 million, was another project granted to the IRGC⁴⁸. Brigadier General Abdol-Reza Abed-Zadeh announced completion of 1220 projects in mining and other industries, and management of another 240 projects⁴⁹ by 2007.

The IRGC became active in the financial sector. The IRGC-affiliated lending funds were turning into financial institutions, expanding their monetary activities and later transforming to accredited banks⁵⁰. The first IRGC bank started its operations in 2009. Ansar Finance and Credit Institution was established after the Iran–Iraq war and began lending, while under Ahmadinejad it became a financial institution and then a bank. Some of these organizations engaged in banking for decades. Their activities were not transparent. Under Ahmadinejad, they became established financial institutions, changing their names to conceal their military ownerships.

The IRGC also expanded to strategic sectors. Kaveh Omidvar (2010)⁵¹ highlights the negative impact of sanctions on Iran's oil sector and argues that the retreat of foreign companies, such as Shell, Repsel, and Total—due to the difficulties of doing business in

⁴⁸ Shedding Light on IRGC's Extensive Economic Activities," *dw.com*, August 20, 2007.
<http://www.dw.com/fa-ir/پاسداران-سپاه-عظیم-اقتصادی-فعالیت‌های-بر-پرتوی-ir/a-2745386>

⁴⁹ Ibid

⁵⁰ "Iran's IRGC Establishes a Bank", *bcpersian.com*, September 23, 2009.
http://www.bbc.com/persian/business/2009/09/090923_ka_bankansar_sepah

⁵¹ Omidvar, Kaveh. "IRGC: Sanctioned in the World, Encouraged in Iran," *bcpersian.com*, June 21, 2010.
http://www.bbc.com/persian/business/2010/06/100621_101_sepah_khatam_sanctions

Iran, —opened space for local companies. Faced with rising criticism for his inability to attract investors for the South Pars Oil Project, Ahmadinejad decided to hand the South Pars project over to state and semi-public institutions, the IRGC obtaining the highest shares.

Lack of transparency makes it difficult to measure the growth of businesses but it is safe to assume that the majority of financial institutions and manufacturing companies emerged during the recent decade, once the IRGC began expanding its businesses. Some of those organizations such as Khatam Al-Anbia were established during Rafsanjani’s era. Majority of the affiliated companies, however, were founded or expanded recently. The following tables contain lists of IRGC-owned or IRGC-affiliated companies. They do not offer timelines for companies’ emergence, but they illustrate the extent of the IRGC’s economic engagement⁵².

Table 5: IRGC Companies

Financial Institutions	Engineering	Some Companies under Sanctions
Basij Coopertaive Foundation; Ansar Financial-Credit Foundation, Armed Forces Retirement Organization, Mehr Financial-Credit Foundation (formerly Basijis Benevolent Fund), and Mehr Economic Investment., Sepah Cooperative Foundation,	Khatam Al-Anbia Construction Base (KA) KA’s Ghorb Nooh KA’s Hara Institute KA’s Sahel Institute KA’s Makin Institute IRGC’s Ground Forces’ Construction Base and Ghaem Base South Region’s Base of Islamic Republic’s Military	Imensazan Consultant Engineers Institute, Gharargahe Sadandegi Ghaem, Omran Sahel, National Iranian Oil Company, Mehr Bank Mehr-e Eqtesad-e Iranian Investment Company Ghorb Karbala Tehran Gostaresh Company Rah Sahel Institute

⁵² INSIGHT- IRAN- List of IRGC firms- IR2, The Global Intelligence Files, *Wikileaks.com*, February 13, 2010. <https://search.wikileaks.org/gifiles/?viewemailid=1116599>

Ansar Financial-Credit Foundation, Mehr Economic Investment and SATA (Armed Forces Pension Fund)		Deep Offshore Technology Company Fater Engineering Institute Pouya Air Rahab Institute Sahel Consultant Engineers Naftiran Intertrade Co. (NICO) Tidewater Middle East Co. Sepasad Engineering Company Sepanir Oil and Gas Engineering Company Makin Institute Hara Company Oriental Oil Kish Iran Marine Industrial Company, SADRA Syrian Arab Airlines
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Table 6: IRGC-affiliated Companies⁵³

Bahman Group Company Investments	Pasargad Bank
Saipa Co. National Iranian Investment Co. Bahman Investment Co. Bahman Leasing Co. Bahman Diesel Co. Mellat Insurance Co. Bahman Brokerage Co. ⁵⁴	Pars Arian Investment Co., Pasargad Insurance Co., Pasargad Bank's Electronic Payment Co., Pasargad Bank's Financial and Investment Co., Pasargad Banks' Brokerage Co., Pasargad Leasing Co., Pasargad Bank' Leasing of Machinery and Equipment Co., Aryan Construction Management Co., Iran's Credit Consulting Company, Pasargad Mass Production Development Co., Aryan's Saman Construction Co., Pasargad Aryan's Support Services Co., Pasargad's Financial Service's Labor's Supply

⁵³ Ghaseminejad Saeid. "Sepah's Role in Iran's Economy," *roozonline.com*, July 28, 2010. <http://www.roozonline.com/persian/news/newsitem/article/-49b7caea7c.html>

⁵⁴ There are investors in each company that overlap with previously-listed companies as well.

	Services, Pasargad Energy Development Co., Middle East Mining and Mining Development Co., Pasargad's Andishenegar Trade Development Co., Pasargad's Tadbirgaran Co., Pasargad's Ayandenegar Commercial Management Co., Eight Urban Building Co., Pasargad Currency and Exchange Services Co., Pasargad's International Trade Development Co., Construction Company for expansion and Modernization of Industries (MANA), Iranian Zarand Steel Co., Khavar-Mianeh Aftab Derakhshan Trading Co., Iranian Sirjan Steel Co., Middle East Industry Standard Engineering Co., Pars Hafez Investment Co.
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It is worth noting that the IRGC's expansion into the Iranian economy has been an incremental process that has continued under Khatami's presidency as well. However, the IRGC's economic expansion under Ahmadinejad differed in two significant ways: the type of economic activities, and their scope. First, while under Khatami the IRGC was mainly involved in smuggling or covertly assuming economic projects, under Ahmadinejad this process became transparent and was 'legitimized' due to the newly adopted privatization policy. Second, the scope of the IRGC's expansion under Ahmadinejad was distinctly different to that of Khatami's.

For example, while Khatam Al-Anbia's economic role was a public knowledge in Iran, the extent of the IRGC's involvement in the economy was not known until mid-2000. The IRGC's illegal economic activities during Khatami's presidency, those in the ports and at Payam Airport were the most scandalous. The speaker of the Sixth Parliament (2000–2004), Mehdi Karroubi, announced that the IRGC had established sixty waterfronts in the south of Iran, unlicensed. Following Karroubi, another Sixth Parliament member, Ali Ghanbari expressed regrets since “one-third of state imports...[came in] unofficially via

illegal markets, the underground economy, and waterfronts⁵⁵”. Another illegal project occurred in Karaj’s Payam Airport for postal services. Khatami’s minister of intelligence, Ali Yunesi, provided data on smuggled goods amounting to 150 billion Iranian Rial confiscated at the airport in 2005. Under Khatami, however, the growth of the IRGC’s economic empire was not as extensive. As Ali Afshari, an activist and a contributor to foreign and domestic news outlets wrote of the IRGC’s growing economic power in Roozonline, “During Khatami’s presidency, this expansion came to a stop, but during Ahmadinejad’s term, large economic projects in the country were handed to the Guards.”⁵⁶

During Ahmadinejad’s rapid privatization, the private sector either could not compete with the IRGC or was marginalized in the absence of relevant laws and regulations. For example, Iran Marine Industrial Company’s main shareholder is IRGC. Khatam Al-Owsia, on no-bidding basis, took over the development of 14th and 15th phases of South Pars project, removing Shell and Opsel from the project, as well as local companies. By 2012, Khatam Al-Anbia and Khatam Al-Owsia were granted total of 51 contracts, equating \$17 milliard. Khatam Al-Anbia has been established since Revolution and has been involved in construction projects; its activities, however, expanded into oil and gas and pharminochemicals since 2006. By 2012, it oversaw 30, high level and low level, oil and gas projects in Iran.

⁵⁵ Ibid

⁵⁶Afshari, Ali. “Ahmadinejad and the Guard: Battle Between Former Allies”, *Roozonline.com*, January 15, 2013. <http://www.roozonline.com/english/opinion/opinion-article/archive/2013/january/15/article/ahmadinejad-and-the-guard-battle-between-former-allies.html>

Another significant shortcoming was lack of political will in passing laws that would direct privatization and encourage the growth of a productive private sector. For example, Kamal At’hari, in an interview broadcast on Radio Zamaneh in 2010⁵⁷, criticized Iran’s subsidy reform and underscored the need to create economic institutions prior to implementation of reforms. Targeted subsidies coupled with price liberalization were expected to optimize resource allocation. In the absence of institutions encouraging production, research and design, and the division of labor, price liberalization would not yield expected results. Criticizing the pace of privatization, At’hari argued that the Fourth Five Year Economic Development Plan’s shock therapy was a populist policy⁵⁸. If global market forces determine prices, the economic system should be capable of competing in global markets. He argued that liberalization should be gradual, i.e. there should be a period of building institutions and structures, preparation of the private sector, and innovation. In Iran, institution-building goals identified by the third and fourth development plans have not been actualized.

Prior to Ahmadinejad’s presidency, the IRGC either performed economic reconstruction projects or was involved in illicit activities. It was after Ahmadinejad’s rapid privatization that it became an established and accepted economic actor. Prior to privatization, many IRGC officials consistently rationalized IRGC’s economic activities,

⁵⁷ This is Vulgar Economism,” *Radiozamaneh.com*, December 25, 2010. <https://www.radiozamaneh.com/29793>

⁵⁸ Ramazani, Alireza. “Does Rouhani Want to Scrap Iran’s Five Year Development Plans?”, *al-monitor.Com*. Since 1979, Iran five Five Year Economic Developmental Plans in order to develop Iran and improve its economy, October 21, 2016. <https://www.al-monitor.com/pulse/originals/2016/10/iran-five-year-development-plans-rouhani-scrap.html>

but only in those areas that the private sector could not undertake developmental projects. IRGC's mission was to serve the state and its reconstruction needs. Majority of its work was expected to serve underdeveloped regions⁵⁹. While Khatam Al-Anbia officials claimed that its activities have been limited to major projects that cost more than \$100 million (implying that Khatam Al-Anbia was not competing with the smaller business and the private sector), the data published in Khatam Al-Anbia's website suggests that the IRGC has taken over many smaller projects costing less than \$100 million⁶⁰, and hence, has been impeding private sector's ability to take over smaller projects.

Therefore, both the civilian leaders and analysts, such as the former Speaker of the Majlis (parliament) criticized the privatization program's inability to boost private sector's growth. For instance, the Majlis' Strategic Research Center reported that only 19% of the SOEs were purchased by private economic actors in the years between 2005 to 2009. 12.5% went to the "public" sector, and 68.5% went to the cooperatives (bonyads) (Alfoneh, 2010, 3). "The state sector's privileges, monopolies, and unlimited access to investment capital frustrate[d] private-sector involvement".

Masoud Behnood, a renowned Iranian journalist, also referred to the growing dangers of the IRGC's economic role expansion. Citing a report by the newspaper *Sarmayeh*, Behnood discussed how private-sector managers were concerned with the IRGC's presence in development projects, the existence of conditions favoring Khatam Al-

⁵⁹ "Eleven Questions Regarding IRGC's Economic Activities," *Entekhab.ir*, December 1, 2012. پرسش-در- 11/85773-مورد-فعالیت-های-اقتصادی-سپا-<http://www.entekhab.ir/fa/news>

⁶⁰ Ibid

Anbia over private-sector companies, and the detrimental role the IRGC's was playing by creating obstacles for private-sector growth⁶¹.

If one monitors the process of privatization in recent history, as Razaghi (2013) argues, it becomes evident that privatization has never been an instrument directing economic development and the creation of a strong productive private sector. On the contrary, it has been a strategy to remedy the state's budgetary constraints (Razaghi 2013, 133). Additionally, the strategy to privatize has taken the shape of a mere transfer of SOEs' ownership without a comprehensive reform package to encourage productivity. The most significant outcome of privatization has been transfer of ownership from the state to the IRGC operating in the semi-public sector, or at times the private sector, but without changes in managerial composition of already-inefficient industries. Furthermore, privatization has not been coupled with effective labor law reform, which left companies with bloated payrolls to preserve their employees. Privatization also has led to tax evasion or reduction in taxation for privatized SOEs. The state not only sold state companies cheaply, but also imposed their inefficient management on new owners, which made it difficult for those companies to pay taxes (Razaghi 2013, 131).

This pseudo-privatization, and subsequent economic expansion of the IRGC, sparked criticism; the militarization thesis gained traction among analysts who warned about the growing economic dominance of the IRGC—militarization of Iran's economy⁶².

⁶¹ Behnood, Masoud "US Sanctions' Aim is IRGC's Khatam Al-Anbia," *bbcpersian.com*, http://www.bbc.com/persian/iran/story/2007/10/printable/071026_ka-mb-us-iran-sanction-khatam.shtml

⁶² Hen-Tov, Elliot, and Gonzales, Nathan. "Militarization of Post-Khomeini Iran: Praetorianism", 2011. <https://www.csis.org/analysis/twq-militarization-post-khomeini-iran-praetorianism-20-winter-2011>

Political developments after Ahmadinejad's presidency (post-2013), as well as analyses of scholars (Harris 2013, Mohseni 2016) challenged the conventional wisdom regarding the militarization of Iran's economy and politics. Unlike expectations of analysts, the IRGC did not become the most dominant actor in Iran's economy or politics. It did however establish itself as an economic player. Unlike China's PLA, the IRGC maintained its businesses. Unlike Egypt, it could not outcompete its contenders, or execute a government take-over to expand its economic assets. Why did the IRGC establish itself as an economic actor but fail to become a dominant player?

The answer lies in understanding two interrelated economic conditions: (i) Iran's overall reform strategy—haphazard liberalization and privatization—fostered an uncompetitive economic system where survival of the military businesses did not hinge upon their profitability but their relationship with the government instead. (ii) Existence of crony-networks operating in the semi-public domain limited the IRGC's possibilities to take over the Iranian state/government.

An Uncompetitive Economy

Outcomes of three presidents economic reform projects illustrate Iran's inability to foster competitiveness throughout decades. Rafsanjani's policy of economic reform focused on trade liberalization and initially boosted private consumption, but a macro-economic instability reversed the course of reform. During liberalization, due to easier access to foreign credit, both the public and private sectors received more investments. However, increased government's spending on reconstruction projects during the period of high oil revenues in the 1980s was coupled with an increase in both consumption and

import of intermediate and capital goods. When oil prices plummeted in 1992, Iran experienced a shortage of foreign exchange and suffered a heightened short-term debt crisis (six-fold debt increase from 1989-1993). Iran's inability to attract long-term credit pushed the government to renegotiate its debt payments, and to reinstate tighter import controls (Karshenas and Hakimian 2000, 48–50). Instead of liberalizing the economy, the state implemented control over trade, continued its multiple exchange rate system, and maintained price controls.

In addition to sanctioning IRGC's economic role-expansion and an attempt for liberalization, albeit unsuccessful, Rafsanjani's period was also notable for the expansion of crony-networks. The revolutionary forces of 1979 revolution, with Khomeini's order, confiscated assets of the deposed Shah and his affiliates and formed revolutionary foundations known as bonyads. These bonyads operated in a semi-public sector⁶³ and as Saeidi characterizes them were "giant private monopolies with no governmental discretion over their operations" (2004, 480). They were bulwark of the Supreme Leader and the religious clergy, were unaccountable, enjoyed privileges⁶⁴ such as tax cuts or easy access to credit, and were used to implement populist policies (Saeidi 2004, 484–485). Consisting of primarily conservative elite factions (Islamists and clergy), a few of these famous bonyads are Panzdah Khordad Foundation, Islamic Revolution's Martyrs Foundation, Islamic Revolution's Housing Foundation, Foundation of Oppressed and Disabled.

⁶³ Also known as paragonmental or parastatal sector.

⁶⁴ Saeidi, *The Accountability of Paragonment Organization*, 485. They had easy access to fiscal and monetary sources, preferential exchange rates, and obtained income from religious charities.

When Rafsanjani's economic reform project included privatization of the SOEs, those elite that were already benefiting from bloated public and semi-public sectors opposed his policies. Instead of privatizing, Rafsanjani's government engaged in sale of SOEs to their ex-owners or capitalists, which led to the transfer and sell of those SOEs to regime-affiliates, i.e. religious loyalists⁶⁵ (Amirahmadi 1996, 12-13). It was during this time that the semi-public sector's bonyads, such as the Imam Reza Foundation and the Foundation for the Oppressed expanded, with assets reaching \$12 billion (Clawson 2008, par. 22). Rafsanjani's policies had two implications pertaining to competitiveness: (i) those crony-networks that expanded during this period contained economic ambitions of the IRGC when rapid privatization in 2004/2005 facilitated IRGC businesses' growth. (ii) Rafsanjani failed to implement meaningful reforms that would assist private sector's growth.

This process of uneven liberalization and privatization continued under Khatami (1997-2005) and Ahmadinejad (2005-2013) and led to an economic system crippled with inefficiencies and lack of competitiveness. Perhaps the most intriguing economic innovation under Khatami was government's circumvention of the article 44 of Iranian Constitution by permitting private enterprises to operate in sectors not subject to constitutional limitations. Hence, the privatization during Khatami focused on facilitating

⁶⁵ Farazmand, *Privatization and Public Enterprise Reform*, 185-187. In 1991, the government approved privatization of 391 out of 770 SOEs via "transfer to government employees, transfer to stocks to general public, corporate bidding, and the like". Through implementation, however, the state transferred SOEs to special groups, an outcome incompatible with the goals of privatization. From 1989-1993, privatization transferred public shares via bidding (30%), and stock market (70%). During the initial two years, private sector purchased 100% of the stocks, but the trend changed in the following years with state-related organizations securing higher shares.

development of new businesses rather than an extensive sale of SOEs (Harris 2013, 53). This process was coupled with a financial reform supporting private sectors' financial activities with establishment of private banks as his main accomplishment (Valadkhani 2001, Alizadeh 2003, Amuzegar 2006, Harris 2013). Along with supporting private sector growth, Khatami also adopted policies of trade liberalization via tariff reductions, corporate and individual tax reforms, and offered incentives to foreign investors (Alizadeh 2003, 276-277).

In addition, with regard to privatizing the SOEs, Khatami promised to reform prevalent methods of privatization. For example, Khatami forbade the negotiated sale of the SOEs and established the "Privatization Organization" to regulate privatization process. Prior to Khatami, in an unregulated environment, the privatization encompassed transfer of SOEs to regime-affiliated groups. For example, lack of relevant labor laws led to either layoffs or falsified bankruptcy claims by new owners who abused the system to receive benefits. Khatami's regulations mandated up to 15% sale of shares with discounts to the workers of the privatizing companies. The rest were sold through the stock market or on a bidding basis⁶⁶. Continuing the reforms, the state was barred from investing in new companies. In addition, a new law demanded bonyads' sale of their shares to the private sector after three years in order to prevent monopolization by bonyads. As a result, Panzdah Khordad, Mostazafan, Shahid, and Sandogh bonyads sold parts of their shares to the public⁶⁷.

⁶⁶ Mehrzad, Ruzbeh. "What did Khatami Do to Iran's Economic Cure?" *bbcpersian.com*, January 31, 2015. http://www.bbc.com/persian/business/story/2005/07/050731_ra-iran-privatization.shtml

⁶⁷ Ibid

Despite his attempts, Khatami—who was notable for his political reforms rather than for his economic policies—failed foster competitiveness. First, the state remained heavily dependent on oil and its expenditure grew from 24.5% of GDP in 1999 to 27.2 % in 2004⁶⁸. Additionally, government’s strategy of supporting private businesses by offering them subsidies exacerbated the economy’s reliance on the oil revenues (Karshenas and Hakimian 2005, 76). Therefore, although Khatami boosted the private sector and made significant changes, Ahmadinejad inherited an economy that suffered from the same structural problems—undiversified, uncompetitive, and oil-dependent.

Proposing an ambitious economic plan, President Mahmood Ahmadinejad’s Fourth Five Year Economic Development Plan (2004/2005—2009/2010) was expected to improve annual GDP growth, per capita income, and employment, and meanwhile reduce inflation, economic disparities, the Gini coefficient, and poverty. It also proposed to diversify the economy by increasing non-oil exports to 10.7 percent, along with state retrenchment— a 10 percent reduction of the national budget to GDP ratio and a 5 percent reduction of government employment (Amuzegar 2010, 114–115). The results were disappointing though. Challenging Ahmadinejad’s false claims regarding the nation’s economic performance, Amuzegar explains that “a combination of structural weaknesses, resource misallocation, and worsening business climate produced *stagflation*” (emphasis added) (Amuzegar 2010, 117).

⁶⁸ Azad, Shirzad. “The Politics of Privatization in Iran,” *Rubin Center: Research in International Relations*. <http://www.rubincenter.org/2010/12/azad-2010-12-05/>

The state struggled with inflation and unemployment; it also failed to boost productivity, specifically its low labor productivity. Investment rates also decreased because of a drop in capital returns caused by lack of competitiveness internationally, short-term trades' lucrativeness and speculations in the stock-market, and banking systems' inadequacies impeding domestic financing, offshoring prospects, and changing regulations (Amuzegar 2010, 116). Additionally, state did not align currency's value with rising inflation resulting in over-valuation, and subsequent decline in competitiveness of domestically produced goods. Coupled with increased importation of intermediate and capital goods, foreign direct investment and non-oil exports dropped, and Iran experienced capital flight (Amuzegar 2010, 116-121). Therefore, similar to both Rafsanjani and Khatami, Ahmadinejad's economic liberalization and privatization also did not contribute to an overall competitiveness. On the contrary, productivity declined, while cronyism, including the IRGC businesses, thrived.

Available data from World Economic Forum and the World Bank also supports above conclusions regarding the lack of competitiveness. The World Bank's data suggests that Iran registered volatile annual GDP growth rates fluctuating between the highest rate of 13.6 in 1990 and the lowest rate of -6.6 in 2012⁶⁹. These radical fluctuations in growth rates are also evident during each presidency (Rafsanjani 1989-1997, Khatami 1997-2005, Ahmadinejad 2005-2013)⁷⁰. Based on the World Economic Forum data, after decades of

⁶⁹ GDP Growth (annual %), *The World Bank*, <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=IR>

⁷⁰ In 1988, a -6.1 rate increased dramatically to 13.6 during first years of Rafsanjani's presidency but it dropped again to -1.5 and -1.7 in 1993 and 1994 during the years of debt crisis. During Khatami, growth has been mainly positive but with fluctuations, and during Ahmadienjad, especially his second term the

attempted reforms, including structural adjustment policies, Iran is ranked 76 out of 138 states in 2017 for its global competitiveness⁷¹. The World Economic Forum does not provide data from the earlier decades of Iran’s performance in order to compare the degrees of change in competitiveness. However, given decades of economic liberalization, Iran’s ranking in terms of its competitiveness would be expected to have been higher than it is today.

Table 7: World Economic Forum, Iran’s Competitiveness Index (134 states, by 2017)

Goods Market Efficiency	Labor Market Efficiency	Financial Market Development	Technological Readiness	Business Sophistication	Innovation
111	134	131	97	109	89

Three consecutive presidents’ policies also did not originate a strong independent private sector. Despite attempts to privatize the SOEs, the public sector remained bloated and inefficient. Ironically, the government’s size compared to the GDP during three presidencies of Rafsanjani, Khatami, and Ahmadinejad has been 22%, 53%, and 66% respectively indicating an incremental growth of the public sector despite attempts to privatize (Vaezi 2014, 51). With regard to the strength of the private sector, indicators of technological readiness, business sophistication, and innovation show Iran’s underdevelopment in terms of its private sector’s capacity⁷².

growth has been negative. GDP Growth (annual %), *The World Bank*, <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=IR>

⁷¹ World Economic Forum, *Global Competitiveness Index: Iran*, 2016-2017 edition. http://reports.weforum.org/pdf/gci-2016-2017/WEF_GCI_2016_2017_Profile_IRN.pdf

⁷² World Economic Forum, *Global Competitiveness Index: Iran*, 2016-2017 edition. http://reports.weforum.org/pdf/gci-2016-2017/WEF_GCI_2016_2017_Profile_IRN.pdf

Table 8: Iran's Technological readiness, Business sophistication, Innovation

Technological Readiness		Business Sophistication		Innovation	
Firm Level Technology Absorbtion	Exports	Local Supplier Quality	Production Process Sophistication	Capacity for innovation	Company Spending on R&D
124	119	103	78	108	89

The World Economic Forum and the World Bank do not offer data from earlier decades of Iran's economic performance. However, the recent data illustrates the overall uncompetitive nature of Iran's economy, its private sector's weakness, and public sector's inefficacy despite two decades of economic reform processes. This overall lack of competitiveness and state's inability to establish market mechanisms has created conditions conducive to operation of the IRGC businesses.

How did this lack of competitiveness impact the IRGC's businesses? First, the IRGC's substantial economic expansion occurred in the absence of a strong private sector that could have challenged the IRGC's economic power. There are two rationales behind this conclusion: first, while the privatization aimed at supporting emergence of an independent private sector, the IRGC's economic expansion had negative consequences on private-sector development. Therefore, one possible conclusion is that the private sector in Iran never had the capacity to challenge the IRGC's economic aspirations. In other words, absence of domestically or internationally competitive private interest groups, and their social constellations, made it less costly for the IRGC to enlarge its economic empire. If decades of economic liberalization and privatization had made the Iranian economy a competitive one, the IRGC would have logically faced greater competitors from domestic

and international markets and the destabilizing costs of its economic role-expansion would have arguably been higher when it aimed at expanding its businesses since 2004.

Secondly, If Iran's overall economy is uncompetitive, and the IRGC is estimated to produce one-third to two-third of Iran's GDP, then the IRGC's businesses are uncompetitive as well. Anecdotal evidence supports this conclusion. For example, in 2016, there was a disagreement between IRGC and the executive branch of Rouhani over South Korean Hyundai Heavy Industries deal with the Islamic Republic of Iran Shipping Lines Co.. The Korean company assumed responsibility to build ten container ships. The press and analysis speculated that IRGC's behavior was a result of its nervousness regarding the opening of Iran's economy and introduction of competitors. As an analyst in RAND, Alireza Nader stated, "[t]hey are worried about competition internally", "[t]hey want to make sure for any given deal, they get a part of it."⁷³ First Vice President Eshagh Jahangiri responded claiming the contract had been signed in 2008 but the production stopped following the sanctions; after Iran's Nuclear Deal, Hyundai agreed to continue the project. While the head of Khatam Al-Anbia, Ebadollah Abdollahi, complained about South Korea's history of signing contracts and not completing them, government officials blamed IRGC for its history of not completing projects on time⁷⁴. IRGC's complaints about foreign or domestic competitors suggests that a competitive marketing economy poses a threat to

⁷³ Gambrell, John. "Revoluionary Guard Faces New Foe In Iran's Opening Economy", *www.apnews.com*, December 15, 2016. <https://www.apnews.com/d1cee287b4194fa0bd1a85eca8911d75>

⁷⁴"Jahangiri Reacts to IRGC's Criticism of a Shipbuilding Contract with South Korea," *Radio Farda*, December 12, 2016. <http://www.radiofarda.com/a/f8-jahangiri-sepah/28171416.html>

military businesses. In addition, civilian elites' criticism of its economic performance implies the IRGC's incompetence.

The evidence of IRGC's anxieties for losing its economic power illustrate how its economic activity is contingent upon an economic system operating based on cronyism and selective protectionism. A most stark example supporting this view was IRGC's advantageous economic position during international sanctions. Mehdi Karoubi, an oppositional presidential candidate in 2009, explained that "part of the state and IRGC pursue sanctions because sanctions help them obtain huge and astronomical profits⁷⁵". For example, post-sanctions, IRGC succeeded in replacing foreign investors in the gas and oil sector. In addition, analysis criticized IRGC's role in limiting private sector growth. According to reports in the Iranian media, IRGC found strategies to circumvent the sanctions, but its ability to do so was linked to the linkages it had with political or security elite in the government. Subsequently, continuation of sanctions was deemed beneficial for these elite groups and IRGC⁷⁶. Therefore, while IRGC strives in a closed, uncompetitive, and undiversified economy, the introduction of foreign and domestic competitors threatens its economic power.

Therefore, lack of competitiveness created conditions conducive to the IRGC's business operations. Although the IRGC established itself economically, it could not completely militarize Iran's economy. Why?

⁷⁵ "IRGC: Sanctioned in the World, Encouraged in Iran," *dw.com*, October 24, 2013.
<http://www.dw.com/fa-ir/ان-عليه-ايران-تحریمها-از-سپاه-از-تحریمها-عليه-ايران/a-17179679>

⁷⁶ Ibid

A Competitive Semi-Public Domain

Examining Iran's political economy post-Ahmadinejad, following the election of Rouhani (2013–present), suggested that the IRGC was not the most dominant economic player. For example, in 2016, Rouhani refused to grant Khatam Al-Anbia with 10 projects; he also annulled the contract that had granted 50% of Iran's telecommunications company to IRGC-affiliated companies⁷⁷. In the summer of 2016, IRGC agreed to Rouhani's plan of shifting its focus on development projects in rural and bordering regions. As *The Wall Street Journal*⁷⁸ concluded, this agreement indicated Rouhani's attempt to control IRGC and contain its unrestrained expansion into the economy. Some also argued that it implied a bargain between the president and IRGC whereby the IRGC would remove itself from lucrative sectors such as oil and gas and finance—sectors needing foreign capital investments— in return for IRGC's engagement in rural development projects⁷⁹. Examples of negotiations and tensions between the elite in power (primarily the executive branch) and IRGC implies that unlike speculation, IRGC's economic expansion has been limited in the aftermath of Rouhani's presidency. The IRGC is an established but not the sole economic player.

⁷⁷ Alfonhe, Ali. "Iran's 'Reformist' President Is Shielding The Revolutionary Guards," *businessinsider.com*, January 12, 2015. <http://www.businessinsider.com/rouhani-is-shielding-the-powerful-revolutionary-guard-from-his-anti-corruption-campaign-2015-1>

⁷⁸ Faucon, Benoit, Meichtry, Stacy, and Fithc, Asa. "Iran's Government and Revolutionary Guards Battle for Control of Economy," *wsj.com*, <https://www.wsj.com/articles/irans-government-and-revolutionary-guards-battle-for-control-of-economy-1463584510>

⁷⁹ Lob, Eric, Habibi Nader. "There is a Battle Over Islamic Revolutionary Guard Cops Business Empire," *washingtonpost.com*, January 5, 2017. https://www.washingtonpost.com/news/monkey-cage/wp/2017/01/05/theres-a-battle-in-iran-over-the-islamic-revolutionary-guards-corps-business-empire/?utm_term=.1a6287e02e63

Scholars also have challenged the militarization thesis. Harris offers the most intriguing analysis on outcomes of liberalization and privatization policies in Iran, and particularly during Ahmadinejad. By analyzing the reforms in pension funds and Iran's Social Security Organization, the Justice Share Program, and the IRGC's economic activities, Harris disputes the militarization thesis. Although the privatization did not lead to the growth of an independent private sector, it did transfer economic activity from a relatively transparent public sector into the semi-public domain; Harris (2013) names this semi-public domain a "parastatal subcontractor state" populated by interest groups such as bonyads and the IRGC.

BBC⁸⁰ reported in 2013 that Gen. Ramazan Sharif, Director of Public Relations and spokesman for the IRGC, considers companies affiliated with the 'Nationalist-Religious'⁸¹ political front as its economic competitors. According to Ramazan Sharif, IRGC assumed economic projects with the Supreme Leader's permission and that "70 to 80 percent of its competitors are large companies affiliated with Nationalist-Religious groups. While no one criticize the National-Religious groups, everyone condemns IRGC". While IRGC's claim might be false (there is no clear evidence supporting or falsifying this claim), the mere fact that IRGC either complains or justifies its economic projects is a testament to the existence

⁸⁰"IRGC: Our Main Competitors are National-Religious Groups," *bbcpersian.com*, September 17, 2013. http://www.bbc.com/persian/iran/2013/09/130917_145_sepah_revolutionary_guard_melli_mazhabi

⁸¹ "Iranian nationalists who also believe in an enlightened interpretation of Islamic teachings", Sahimi, Mohammad. "The Nationalist-Religious Movement: Part 1: Patriots and Mosaddeghists," *pbs.org*, <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2011/06/the-nationalist-religious-movement-part-1-patriots-and-mosaddeghists.html#ixzz4jpt4RKRL>

of disagreements among the elite, as well as IRGC's inability to pull enough leverage for its economic projects.

While the economic activities of bonyads is not transparent, based on public pronouncements of IRGC commanders and other elite in Iran, one can conclude there exists competition among various elite-networks over assumption of economic projects in Iran. For example, in 2015, Deputy Representative of Supreme Jurisprudence (Khamenei's representative), Abdollah Haji Sadeghi, stated that "if IRGC enters the domain of the economy, it is not for personal or economic benefits but to protect the revolution", and that "the governmental elite should know that IRGC is not competing against ministries even if it enters a specific domain because its goal is to consolidate the Islamic Republic's position⁸²". Such statements signal the IRGC's need to justify its economic activities, and attain the support of dominant civilians.

While Khamenei has defended IRGC's economic activities, Rouahni implicitly criticized its corruption. Corrupt economic activities, however, are not IRGC's monopoly. A massive portion⁸³ of Iran's economic activities have been monopolized by other religious and state-affiliated groups, such as Bonyad Astan Qods-e Razavi. Furthermore, these bonyads and the IRGC cooperate in carrying out economic tasks, such as joint-projects performed by Barekat Bonyad and the IRGC⁸⁴. These joint projects show the

⁸² "Defending IRGC's Economic Activities in the Name of Protecting the Revolution," *dw.com*, September 22, 2015. <http://www.dw.com/fa-ir/انقلاب-از-انقلاب-اقتصادی-سپاه-به-نام-صیانت-از-انقلاب/a-18730898>

⁸³ Ibid

⁸⁴ "Blessing Foundation and the Revolutionary Guard Cooperating to Erradicate Deprivation", *www.barakatfoundation.com*, July 16, 2014. <http://barakatfoundation.com/fa/news/1070>

IRGC's economic inability to carry out economic tasks alone due to economic or political considerations.

Further evidence of competing crony-networks was Ahmadinejad's constant threats to expose economically corrupt elite in Iran, as well as his harsh attacks against the previous president, Rafsanjani and his economic-network. In 2011, Ahmadinejad threatened to expose the corruption of his opponents as a tactic to silence them. He threatened to expose only 25% of them and promised to keep the rest to himself out of his consideration for the regime. According to Duetsche Welle's analysis, Ahmadinejad's strategy was to signal to Khamenei that he would not expose the Supreme Leader's economic corruption, but meanwhile referred to three different groups as possible targets: 1-United Principalists' Front⁸⁵- Resistance Front⁸⁶, and 3-groups within IRGC and other security forces conspiring to remove Ahmadinejad from power⁸⁷. Elite infighting, criticisms over the management of economic assets, and threats to expose one another implies the existence of competition among these crony network, as well as their shifting alliances. What were the implications of this competitive system on the IRGC's political control?

The IRGC's economic and political expansion under Ahmadinejad concerned analysts of Iranian politics who discussed Iran's transformation into a military dictatorship with the IRGC as the main political and economic player. Given the changing nature of

⁸⁵ Spearheaded by Larijani (former speaker of the Parliament), Ghalibaf (former Mayor of Tehran and presidential candidate), and Mohsen Rezaei (former IRGC Commander)

⁸⁶ Consisting of Radicals like Mesbah Yazdi

⁸⁷ These groups supported Ahmadinejad's election initially and used him to expand their power, later the relationship between changed; his supporters began criticizing Ahmadinejad.

civil-military relations, this outcome seemed plausible. However, the IRGC was unable to assume an all-encompassing role in Iran's domestic politics. The next section will explain why, despite its aspirations, the IRGC failed to dominate Iran's politics.

The Political Control of the IRGC

The growth of IRGC businesses was also coupled with its ambitious pursuit of political power. In fact, those that warned about militarization of the Iranian economy were also concerned about the militarization of Iranian politics. Unlike speculations, and despite IRGC's attempts to amass political power, IRGC failed to dominate Iran's politics. Why? Utilizing a political-economy framework, this section tests hypothesis set forth in this dissertation: (H1) if Iran's rapid economic liberalization failed to establish a competitive economy, there is a higher likelihood for the IRGC to establish itself as economic actors, and subsequently, transform its economic power into a political one. In testing the case of Iran, this section will illustrate that the (H1) applies to the case of the IRGC but with a caveat: the uncompetitive nature of Iran's economy has facilitated the IRGC's establishment as a political player. However, the IRGC relies on factions of the elite with linkages to the government who could provide the IRGC with new economic projects. Consequently, the IRGC is relatively dependent on the civilians and is constrained by the elites and elite-coalitions in different times.

This section will develop two interrelated arguments: First, the IRGC's political power increased following its expansion into the economic domain. Prior to privatization, the IRGC obeyed Iran's Supreme Leader's demands. Post-privatization (since 2005), however, it has become an established political player; its agenda is sometimes at odds

with the Supreme Leader's interests. Furthermore, due to the uncompetitive nature of Iran's economy, the IRGC garnered enough economic leverage to pressure the government for economic and political gain. Secondly, despite its attempts to dominate Iran's politics, the IRGC has been unable to become the most dominant political actor; the economic-political elite networks in Iran constrain the IRGC's political ambitions as well. In other words, the limitations of the IRGC's economic power has had significant implications for its ability to leverage its economic power into a political one—the IRGC's is dependent on at least a faction of the civilians to expand its economic power.

Did the IRGC's political autonomy change as a consequence of liberalization and privatization? Yes. The degree of IRGC's political autonomy increased. It became, and at times acted, more independent of the Supreme Leader. Due to the politicized nature of the IRGC in Iran, the line between civilian and military controls has always been blurry. However, there is an observable change in the nature of the IRGC's interference in politics. The IRGC has changed from a military that engaged in acts of arbitration to a military operating as an independent player at times. In other words, prior to privatization, the IRGC arbitrated among the civilian elite by siding with the Supreme Leader and advancing his political agenda. Post-privatization, it became a player that at times challenged the Supreme Leader; the political coalitions or infightings either helped or constrained the IRGC's political maneuverability.

Historically, the IRGC was instrumental in consolidation of the theocratic right⁸⁸ in Iran. During the initial years after the 1979 Revolution, the revolutionary elite used the

⁸⁸ The conservative clergy

IRGC to suppress their opponents⁸⁹. Article 150 of the Constitution cemented IRGC's role as the "protector of revolution"⁹⁰. Article 109 appointed the Supreme Leader as the supreme commander of the Armed Forces⁹¹. By codifying the role of Velayat-e Faqih (the Guardianship of Jurisprudence⁹²), the constitution demands IRGC's allegiance to Velayat-e Faqih (Ottolenghi 2011, Kindle Locations 192-195). Hence, the constitution provides an institutional mechanism for civilian control of the IRGC, although that control is limited to the office of the Supreme Leader.

Existence of an institutional mechanism to supervise the IRGC, however, did not mean that the IRGC remained apolitical. On the contrary, the unintended consequence of the IRGC's subjugation to the office of the Supreme Leader was its politicization by Khamenei; he utilized the IRGC to advance his own political agenda (Alfoneh 2008). For example, the IRGC became a stark critique of Rafsanjani's economic liberalization and Khatami's political liberalization policies. Opposing Rafsanjani's liberal agenda, then IRGC commander, Mohen Rezaei, publically warned about dangers of economic

⁸⁹ Alfoneh, Ali. *The Revolutionary Guard's Role in Iranian Politics*, par.10-11. Islamists marginalized the Tudeh Party (Iran's Communist party) in 1983, as well as secular or liberal political elite, such as Bazargan and Bani Sadr, who argued for relegation of IRGC's roles were marginalized consistently.

⁹⁰ "The Constitution of the Islamic Republic of Iran", *Iran Human Rights Documentation Center*, <http://www.iranhrdc.org/english/english/human-rights-documents/iranian-codes/3017-the-constitution-of-the-islamic-republic-of-iran.html?p=19>

⁹¹ "Article 110, Constitution of Islamic Republic of Iran", *www.iranhrdc.org*, nd. His responsibilities include assigning chief of the Joint Staffs (IRGC and Islamic Republic of Iran Army), chief commander of IRGC, supreme commanders of the Armed Forces, and conflict-resolution among the three wings of the Armed Forces. <http://www.iranhrdc.org/english/english/human-rights-documents/iranian-codes/3017-the-constitution-of-the-islamic-republic-of-iran.html?p=16>

⁹² "The Constitution of the Islamic Republic of Iran, General Principals, Articles 1-5", *www.iranhrdc.org*, nd. Iran's theocratic regime requires guardianship of Supreme Jurist and a body of clerics over political decision-making. <http://www.iranhrdc.org/english/english/human-rights-documents/iranian-codes/3017-the-constitution-of-the-islamic-republic-of-iran.html?p=5>

liberalization in 1996 (Alfoneh 2008, par. 22). During Khatami, the IRGC became more politically vocal and sided with the conservative elite, including the Supreme Leader, who loathed Khatami's political liberalization agenda. The IRGC became notorious for meddling with Khatami's reformist agenda, such as suppressing student protests in 1999⁹³, issuing a public ultimatum⁹⁴ to Khatami, and criticizing his reformist agenda⁹⁵. However, these interferences in politics were sanctioned by Khamenei, the Supreme Leader.

Takeyh analyzes the role of IRGC in Iranian politics and concludes that the IRGC "functioned very much as a political entity" (2009, 22-23). But he also draws attention on the IRGC's adherence to conservative elite's ideology. This attitude was evident in IRGC's commander Safavi's remarks regarding 1999 Student Riots. While emphasized the apolitical nature of IRGC, he also discussed IRGC's adherence to a 'political line', referring to the hardliner ideology of Khomeini's revolutionary values (Takeyh 2009, 24). Safavi's remarks exemplified IRGC's 'responsiveness' to the Supreme Leader as the main figure protecting the values of the 1979 Revolution. This loyalty was best exemplified by Commander Safavi's labeling of reformists as 'hypocrites' who, he thought, threatened the Islamic Republic. Following the arrest of Kharbaschi, a reformist and pro-Rafsanjani Mayor of Tehran, Safavi stated:

⁹³ "Iran: Five Years After Protests, Release Students", *hrw.com*, July 6, 2004. Students protesting the closure of the Salam newspaper in 1999 put the reformist camp against the conservatives. Sanctioned by Khamenei, the protests were suppressed violently by the Basij militia.
<https://www.hrw.org/news/2004/07/06/iran-five-years-after-protests-release-students>

⁹⁴ Siddiqi, Ahmad. "Khatami and the Search for Reform in Iran," *Stanford.edu*,
https://web.stanford.edu/group/sjir/6.1.04_siddiqi.html

⁹⁵ "From People's Army of Iranian Revolution to the Guard Corps", *bcpersian.com*
http://www.bbc.com/persian/iran/2009/04/090422_mg_sepah_anniversary

“[w]e do not interfere in politics but if we see that the foundations of our system of government and our revolution is threatened...we get involved. When I see that a [political] current has hatched a cultural plot, I consider it my right to defend the revolution against this current. My commander is exalted leader and he has not banned me [from doing this]” (Ehteshami and Zweiri 2007, 22).

The nature of IRGC’s political involvement however, took a different turn under Ahmadinejad’s presidency. Since Ahmadinejad’s presidency, the IRGC began to serve its own institutional interests, including its economic interests. First, the quality of the IRGC’s interference in politics changed from arbitration to intervention in the electoral process, as well as assumption of governmental institutions. The most striking change in the civil-military relations, however, was the IRGC’s contentious relationship with the Supreme Leader, and the emergence of neo-principalist faction in the Iranian politics that opposed the conservative clerical establishment, including Khamenei.

First, in collaboration with the conservative elite, and presumably Khamenei’s son⁹⁶, the IRGC intervened in Iran’s presidential election in 2009. Ahmadinejad was brought into power for the second term in what became known as an ‘election coup-d’état’. The IRGC and IRGC-affiliates also began controlling significant governmental institutions such as ministries of Commerce, Defense, Economics, Intelligence, Interior, Islamic Guidance, and Oil. Furthermore, an IRGC commander also ruled the Iran Armed Forces General Command (the regular military) (Ottolenghi 2011, 689).

⁹⁶ Sahimi, Muhammad. “The Man in the Shadow: Mojtaba Khamenei”, July 16, 2009. <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2009/07/the-man-in-the-shadow-mojtaba-khamenei.html>

Additionally, the most important sign of changing IRGC's political power was the rise of "neo-principalists" or "neo-fundamentalists". While principalists⁹⁷ were traditional conservative right wing elite, the neo-principalists⁹⁸ were a new group consisting of Ahmadinejad and middle-rank IRGC members (Ahdiyyih 2008, par. 17). Safshekan (2010) considers neo-principalists as "political manifestations of IRGC", and challenges the conventional wisdom assuming IRGC loyalty to the clergy. He argues how IRGC has been challenging the clergy not only by questioning the legitimacy of clerical governments prior to Ahmadinejad, but also by attacking prominent clerical establishments like Rafsanjani and Nateq-Nouri⁹⁹. In a process qualified as "de-legitimizing the clergy", Safshekan argues how Ahmadinejad talked about his relationship with Mahdi¹⁰⁰; it was a strategy to break the clerical monopolization of having a relationship with Mahdi (Safshekan 2010, 552-553).

IRGC's lack of responsiveness to the conservative camp, and the Supreme Leader, was also evident in the increasing polarization between the IRGC and conservative clergy. The press reported on examples of elite reshufflings as signs of disagreements between them. For example, Ahmadinejad's dismissal of Gholam Hossein Mohseni Ejehei, then Minister of Intelligence and Khamenei's trustee, signaled tensions between the two camps.

⁹⁷ Safshekan, *The Ayatollah's Praetorians: Guard and 2009 Elections*, 549. Safshekan distinguishes between the neo-principalists and ex-IRGC leaders such as Mohsen Rezai, Mohammad Baqer Qalibaf, and Ali Larijani, who have entered politics and identify as principalists, but are not formally connected to IRGC.

⁹⁸ Ahdiyyih, Mohebat. *Ahmadinejad and the Madi*, par. 13. This new clique drew on Hojjatieh teachings, was supported by a powerful cleric in the Assembly of Experts, Mesbah-Yazdi. His pro-Mahdi teachings influenced Ahmadinejad, and IRGC.

⁹⁹ Former Minister of Interior, Former Chair of the Parliament, and a presidential candidate in 1998

¹⁰⁰ In Shiavism, Mehdi is redeemer of Islam who will rule the world before the Day of Judgment

Ejehei was believed to possess information with regard to the 2009 elections that could undermine Khamenei's power (Smith 2011, 5). According to a report by the Tehran Bureau, both cases of Mashaei and Ejehei "were meant to be IRGC's high command's signals to Ayatollah Khamenei that they were in control and that he should toe the line—their line"¹⁰¹. It seemed that not only did Ejehei not keep Ahmadinejad in the loop by directly reporting to Khamenei instead, but his ministry's reviews contradicted IRGC claims regarding Green Movement's qualification as a 'velvet revolution'¹⁰². The Ministry of Intelligence's report also considered Mashaei, and commander of Basij, cleric Taeb as "security risks", and subsequently undercut IRGC commander's accusations¹⁰³. The above confrontation, and similar incidents, signaled a change in the relationship between both the Supreme Leader and his affiliated conservative clergy and the IRGC.

Why did the IRGC's responsiveness to civilians, precisely the Supreme Leader and conservative elite, decline? The rapid privatization led to the expansion of the IRGC's economic power, and subsequently, an increase in its political weight. The IRGC's capacity to both assume economic projects and preserve its businesses was a function of state's inability to foster economic competition. Not only did the privatization facilitate the IRGC's economic rise, the lack of economic competition made the IRGC more independent of the civilians. Therefore, although there is an evidence of creeping growth

¹⁰¹ Sahimi, Mohammad. "Showdown Between Khamenei and IRGC", *pbs.org*, July 28, 2009. <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2009/07/showdown-between-khamenei-and-irgc.html>

¹⁰² A reference to color revolutions in the post-communist states.

¹⁰³ Sahimi, Mohammad. "Showdown Between Khamenei and IRGC", *pbs.org*, July 28, 2009. <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2009/07/showdown-between-khamenei-and-irgc.html>

of IRGC's role in the Iranian politics, a radical transformation of the civil-military relations occurred during Ahmadinejad's presidency, following the acceleration of privatization. In other words, one should distinguish between the intentions and the capacity to act. Even if one argues that the IRGC manifested aspirations to enhance its political influence, it became capable to actualize those political goals during Ahmadinejad's presidency, and more specifically in the aftermath of privatization policies.

The IRGC's political expansion was not decoupled from its economic aspirations. Some argue that the IRGC grew into political and economic power due to the support it received from Ahmadinejad as well as the Supreme Leader. Although that's an accurate observation, what the analyses miss is the reason behind the IRGC's economic expansion. If a political power, in this case the presidency and the Supreme Leadership, had the goal to elevate the IRGC politically, why grant it with economic projects too? Moreover, why implement privatization policies and reinterpret the constitution in order to give the IRGC economic projects? It seemed that if co-opting the IRGC was the ultimate goal, it would have been logical to transfer SOEs from one sector of the government to another (to the IRGC) by maintaining the article 44 of the Constitution rather than declaring an economic reform project and facing ample criticism from both the elite and the public. The IRGC's economic role-expansion was a consequence of the type of privatization implemented in Iran; it was an unintended consequence of privatization. Consequently, a transformation in the IRGC's corporal interests also was an unintended outcome of this policy. That's why both the conservative elite and the Supreme Leader have been cautious with the IRGC.

There is evidence of tension, and hence negotiations, among the IRGC and various factions of the civilian elite who ultimately limited the IRGC's political ambitions.

The militarization of Iran's political thesis proved wrong once Hassan Rouhani was elected president in 2013. During the early stages of the presidential election in 2013, there were speculations regarding both the Supreme Leader's and IRGC's preferred candidates for presidency, which implied existence of disagreements both within the IRGC and between the IRGC and the Supreme Leader. IRGC commander Jafari, as well as several high rank commanders along with Khamenei's son and office of the Supreme Leader formed one faction who supported candidacy of Iran's chief nuclear negotiator and secretary general of the Supreme National Security Council, Saeed Jalili. Another group consisted of IRGC officers, who were reputable for being uncorrupt and professional. They supported a former IRGC commander of the air force, and then mayor of Tehran, Ghalibaf. The last group were those IRGC members who amassed wealth following the privatization projects sanctioned by Khamenei. They rallied behind the previous IRGC Commander, Mohsen Rezaei¹⁰⁴.

The election of Rouhani signified an important outcome in terms of IRGC's power in Iran, that it was not the dominant actor. Even since his election, Rouhani has been trying to limit the IRGC's economic and political power. For example, as Business Insider reports, Rouhani embarked on an anti-corruption campaign that focused on Ahmadinejad-era economic scandals. Under the slogan of "equality under the law", Rouhani succeeded

¹⁰⁴ Sahimi, Mohammad. "IRGC, Opposition Split Over Whom to Support in Iran's Presidential Election," *muftah.org*, Jun 8, 2013. http://muftah.org/irgc-opposition-split-over-whom-to-support-in-irans-presidential-elections/#.V4da0Ff3_ww

in passing a bill in the parliament that removed tax-exemptions for several bonyads¹⁰⁵ as well as for Khatam Al-Anbia. Rouhani's criticism of IRGC's power triggered its reaction when the IRGC condemned the president for "insulting the nation". In response, government officials praised IRGC and stated that it posed no threat to private sector growth. Business Insider considers Rouhani's setback in this case as an example of the Supreme Leader's ability to balance the power between IRGC and the executive branch. This incident offers two conclusions. First, IRGC does not have an independent leverage, despite its attempts to take-over the Iranian economy. It still needs support of the elite in power to have access to state resources. Secondly, ample examples of public pronouncements by IRGC and other government officials indicates the existence of tensions, along with a process of bargaining and negotiations among the political players in Iran.

In discounting Iran's militarization thesis, scholars of Iranian politics underline political variables as the most determinate factors driving IRGC's behavior (Thaler et al. 2010, Sohrabi 2011, Ottolenghi 2011, and Mohseni 2016). Mohseni (2016) underscores both inter-elite relations and republican features of institutional engineering¹⁰⁶ as determinant factors and concluded that Ahmadienjad's election was a function of "internal transformations within the confines of the same system of multiple contentious power

¹⁰⁵ Astan-e Qods-e Razavi, Setad-e Farman-e Emam, Bonyad-e Mostazafan

¹⁰⁶ Mohseni, *Power and Change in Iran*, Kindle Locations 1265-1266. Iran's unique institutional engineering highlighted the significance of "decision-making centers" and their role as veto-players. Within a system of checks and balances, veto-players blocked policies, and hence, obstructed the general transformation of Iran's institutions. In other words, the possibility for a change from a theocratic government to a military one, via institutional transformation, was minimal due to the existence of checks and balances and multiple power centers.

centers that had been established with the revolution”. Contrary to the thesis of power-mobilization, alterations in institutions and power dynamics should not be confused with a regime change (Mohseni 2016, Kinle Locations 918-919). Similarly, others have discussed the networked characteristics of Iranian politics and the existence of multiple power centers fostering competitiveness rather than monopolization of power (Thaler et al. 2010, Sohrabi 2011). Ottolenghi (2011) identifies a symbiotic relationship whereby “IRGC takes advantage of its influence and capabilities in one realm in order to increase its involvement in another. Its growing economic clout is both an end in and of itself and a tool to advance other agendas.” (Ottolenghi 2011, Kindle Locations 952-953). Above explanations stress the role of multiple centers of power in constraining the IRGC’s behavior.

The IRGC’s adheres to the values of revolution and has constitutional mandate to protect revolution, and thus, is an ideological military. In its history, IRGC has branded itself as an ideological guardian of Islamic Revolution and has created an institutional identity around this ideology. It has intervened in politics on ideological grounds, especially during Khatami’s reform movement. The IRGC has maintained this loyalty, even during Ahmadinejad’s presidency, but it has also grown increasingly calculating and requires compensation in return for its loyalty. This transformation is evident primarily after the privatization policies of Ahmadinejad and IRGC’s growth as an economic player. Since Ahmadinejad’s period, the IRGC has been leveraging its accumulated economic and political leverage to further its corporal interest, disregarding the long-term consequences of those activities on Iran’s economy. For example, both the former Speaker of Majlis, Larijani, and Ahmadinejad praised Khatam Al-Anbia and supported the IRGC’s takeover

of oil projects to signal that they would compensate IRGC for the losses caused by sanctions on the nuclear program (Alfoneh 2010, 1-2).

However, Recent public pronouncements between president Rouhani and commander in chief, Abdollah Abdollahy¹⁰⁷, illustrate existence of a contentious relationship between the two. While Rouhani¹⁰⁸ criticized the transfer of economic assets to what he called a “government with guns”¹⁰⁹, the commander underscored the IRGC’s superior capacity to carry out economic tasks compared to foreign investors or the private sector¹¹⁰. Constant debates about the economic role of the IRGC indicates civilians’ inability to completely contain the IRGC but also the IRGC’s inability to completely override the civilians’ demands.

While primary explanations of Iranian politics highlight the role of political variables, such as Iran’s republican features of institutional engineering or its network-based politics, I underscore the importance of economic policy-making in understanding the IRGC’s behavior. I do not disagree with political explanations. In fact, my argument draws on the literature about Iran’s network-based economic and political character and underscores the constraints the IRGC faces in pursuing its economic and political agendas. My argument deviates, however, by highlighting the political implications of a change in the IRGC’s capacities as a consequence of the privatization under Ahmadinejad. In the

¹⁰⁷ The head of the IRGC’s engineering company, Khatam Al-Anbia

¹⁰⁸ “Rouhai’s Criticism of Transferring the Economy to the “Government with Guns”, *www.dw.com*, 23 June, 2017. <http://www.dw.com/fa-ir/انتقاد-روحانی-از-سپردن-اقتصاد-به-دولت-با-تفنگ/a-39377726>

¹⁰⁹ A reference to the IRGC

¹¹⁰ “IRGC Commander: I Have a Serious Complaint Against Rouhani’s Government”, *www.dw.com*, July 7, 2017. <http://www.dw.com/fa-ir/سردار-سپاه-از-دولت-روحانی-گلایه-شدید-دارم/a-39603856>

absence of competition and due to pseudo-privatization, the IRGC amassed a degree of economic power that allowed it to carve out its own unique space in the Iranian politics. Subsequently, it established itself as an economic and also a political player that regularly negotiates with the civilians and sets forth new economic demands.

Despite establishing itself as an economic and political player, the IRGC needs to partner with the civilian elite to further access the state resources. After all, its capture of state resources has become a stark topic of criticism by Rouhani's government. In order for the IRGC to be able to continue its economic expansion, the IRGC needs the support of elite-linkages to obtain new projects. If the executive branch chooses to dismiss its demands, the IRGC enters into a process of bargaining, and succeeds if it is able to gain support of the Supreme Leader or a different elite-network.

The Functional Control of the IRGC

Hypothesis number two suggests that if the state is successful in opening to the global economy, and subsequently generating money, there should be a higher likelihood for state increase of military spending; the outcome would be a probable increase in the military's functional control. In contrast, incomplete liberalization and the state's lack of sufficient income incentivizes the military to retain its income-generating businesses. A military that focuses on both tasks of defense and economic activity would have a lower prospect of increasing its functional efficacy. In other words, H2 suggests that the state's incomplete liberalization and its economic incompetence negatively impact the military's functional capacities. The reasoning lies behind (i) the state's inability to fund the military

and (ii) the military's occupation with two simultaneous tasks of defense and income generation.

Testing the second hypothesis, this section's empirical evidence illustrates Iran's incompetence in functional capabilities. Extrapolating from Iran's doctrinal changes, as well as available data on indicators of functional control, it argues that incomplete economic liberalization resulted in the IRGC's inability to advance its military capabilities noticeably. Drawing on Brook and Stanley's (2007) operationalization of military effectiveness, this section assesses the indicators of integration, responsiveness, skill, and quality. Integration refers to consistency between tactics, logistics, and strategic plans with political goals, whereas responsiveness signifies to the modification of forces to address adversaries' weaknesses and new threats. Skill and quality refer to personnel's training and nature of weaponry.

First, the data suggest that Iran has not been generating sources of income and subsequently has not increased the defense expenditure. SIPRI¹¹¹ data on Iran's military expenditure as a percentage of GDP demonstrates a decline in military spending from 6.3% in 1988 to 2.6% in 1997, which coincides with Rafsanjani's presidency. During Khatami, there was a slight increase in military spending from 2.6% to 3.3% in 2005, whereas during the term of Ahmadinejad, military spending fluctuated unevenly between 3.0% to 3.6%, with the final years reaching as low as 2.3%. A lack of transparency makes it difficult to assess whether the money was spent on the regular military or the IRGC. SIPRI speculates

¹¹¹ "SIPRI Military Expenditure Database", Stockholm International Peace Research Institute, <https://www.sipri.org/databases/milex>

that, with the exception of year 2012, the figures based on the Central Bank indicate inclusion of the IRGC's budget in the data. Nevertheless, the data suggests that Iran has not been increasing its military budget dramatically, at least officially.

The rest of this section will illustrate how the IRGC's functional capabilities have not increased throughout decades despite its attempts to expand its military capabilities. As explained in the previous section, Iran's incomplete economic liberalization, the state's inability to generate funds, and low military spending have incentivized the IRGC's maintenance in the economy. The inevitable consequence of this dual role has been lagging functional capabilities. Therefore, despite liberalization attempts, IRGC's functional capabilities' development has not been remarkable.

The crux of Iran's doctrine has been an instrumental assessment of Iran's military capabilities vis-à-vis US and Israeli capacities and subsequent adoption of a "deterrence-based doctrine that stresses raising an adversary's risks and costs rather than reducing its own" (Ward 2005, 576). This doctrine looked for strategies to circumvent conventional war and instead focused on irregular warfare, development of WMDs, and sponsoring terrorism. Paired with threats to internationalize conflicts via disruption of oil trade routes, these strategies' goal was to pressure for diplomatic solutions to conflicts (Ward 2005, 567). For example, following the US deployments in Afghanistan in 2001, and Iraq in 2003, Iran was forced to reconsider its strategic doctrine; the goals did not change but the methods did. The evidence suggests Iran's ability to assess its economic resources and its threat environment and plan accordingly.

In 2004, Vice-Defense Minister Mohammad Shafayi Rudsari announced that Iran's defense strategy was "diverse," would allow Iran to combat great powers, and would compensate for Iran's weakness in 'classic' forms of military capability. In 2005, the IRGC announced its "mosaic doctrine" and reorganized its structure by creating 31 command centers in Iran's provinces. The decentralization was expected to increase unit cohesion and local level commanders' authority; it was expected to make infiltration of the US forces into Iran difficult¹. Although Iran has been able to integrate its doctrinal developments and its political goals, other aspects of its functional capabilities lag behind.

The IRGC's tasks, especially in non-conventional warfare, have met the strategies of the military doctrine. For example, the IRGC's Al Quds force involvement with Hamas, Hizbollah, and Iraqi groups in Afghanistan to engage in irregular warfare and defend Iran's interest against US and Israel has been well-documented. It is estimated that 5000 men in the IRGC are assigned to unconventional warfare tasks. The IRGC has one special force division, plus smaller units, that have been prioritized for training to conduct operations abroad. In another example, the doctrine states that Iran should take advantage of Persian Gulf's geography and the limitations that it offers for the enemies' maneuverability. Iran should use islands to launch attacks, disrupt oil trade routes, and target enemy oil installations; due to the Gulf's limited depth and width, Iran could use anti-ship cruise missiles and mines, conduct hit-and-run missions using fast boats, deploy submarines to the Gulf of Oman for initial defensive purposes, and employ electronic warfare. According to Ward, a report published in 2004 explained the maneuver of Ettehad-83 where the navy practices electronic warfare, camouflage, concealment, and deception activities aiming at

an enemy; these practices seem to be compatible with the overall doctrine (Ward, 2005: 568).

Regarding organizational training and skills, the IRGC transformed itself from a disorganized revolutionary militia to a professional military institution by adopting military-like ranks and uniforms and valuing knowledge and skills for promotion rather than sole ideological loyalty; education level, experience, and managerial and administrative skills became important factors (Cordesman 1999, 37). However, as Ward argues, despite the attempts to create a coherent military doctrine, there seems to be either an inability or unwillingness to train and support the armed forces effectively (2005, 573). The effectiveness of the IRGC since 1988 has declined, with bureaucratization, corruption, careerism, and financial abuses as likely causes. “It is the elite elements of IRGC that give it real meaning” (Cordesman 2007, 4-6).

In terms of training and skills, as well as weaponry capabilities, the data is contradictory. For example, some IRGC units operate as conventional army divisions, whereas other divisions are capable of conducting asymmetric warfare and covert operations, but the majority of the IRGC’s land force is trained to maintain internal security rather than external defense. Cordesman (2007) underscores the existence of inconsistencies in reports about the IRGC manpower capabilities and organizational structure. It appears that the IRGC’s claims about its capabilities do not match experts’ opinions. The evidence of Iran’s ballistic missile capabilities and nuclear program do not match the IRGC’s claims either. Although Iran’s air-force strategy includes the development of ballistic missile program and air defense due to its limited nature of

technology, it might threaten civilian targets rather than military ones. The limitations of Iranian armed forces, such as its immobility, an infantry that utilizes towed artillery, and the IRGC's poorly trained reserve force, make it difficult to plan for conventional warfare (Ward, 2005: 571-573).

Similarly, although Iran has acquired the capacity to build missiles with the IRGC in leadership position, the ballistic missile program has not produced impressive outcomes. By 2008, Iran's ballistic missile capabilities consisted of short- and mid-range missiles, capable of protecting Iran against its enemies in the Middle East (Alexander & Hoenig 2008, 176-177). In 1998, however, the Commission to Assess the Ballistic Missile Threat to the United States (Rumsfeld Report) determined Iran's domestic missile program to be underdeveloped and dependent on foreign assistance. Different reports estimated that Iran possessed 300 domestically-produced Shahab1 short-range ballistic missiles in the 80s. Since then, Iran has tested updated versions of Shahab, but the results have not been impressive. Although there is disagreement among analysts regarding Iran's missile capabilities (Alexander & Hoenig 2008, 182), there are reports of failed launches, such as the Iranian media's reporting on photo-shopped fake images of missile tests portraying failed attempts as successful in 2008¹. It is safe to assume that Iran also lags in developing its defensive technological capabilities.

This section marshalled evidence suggesting IRGC's incompetence in conventional warfare, its reliance on unconventional strategies, poor equipment and training. Overall lack of development and weak industrial base impedes IRGC's military production as well. Therefore, despite economic liberalization, Iran has failed to improve its economic

performance and generate funds for the state. The result has been state's inability to increase defense spending and to invest in procurement of better weaponry, or investment in conventional capabilities.

The Social Control of the IRGC

The third hypothesis suggests that if economic liberalization conditions the maintenance of military's economic activities, there is a higher likelihood for militaries to operate as interest groups. Subsequently, the social control would decrease. In other words, the commercialization of militaries (their expansion into new domains after liberalization and privatization) accentuates their corporal interests as economic actors, and hence, negatively impacts their social integration. Militaries, in their pursuit of self-interest, might dismiss previously accepted social values at times, or may adopt new social values corresponding to newly emerging values in the society.

In terms of the IRGC's social values, the liberalization and privatization complicated the social aspect of the military control. On the one hand, the IRGC has remained loyal to conservative values of revolution, despite a political liberalization during Khatami that challenged some of those fundamentalist or traditional political assumptions. On the other hand, in the process of protecting its economic interests, the IRGC has been undermining some of the economic and developmental values of the 1979 revolution, specifically alleviation of poverty and "defending the oppressed"¹¹².

Since Khatami's presidency, there has been a shift among the elite and their social constellation in support of democratization, liberalization, and human rights. Although the

¹¹² دفاع از مستضعفان

reformist elite in Iran remained loyal to Islamic values, they offered reinterpretations of Islamic teachings and sharia law, and championed the necessity to provide political and social rights in accordance with the universal human rights values. Prompting Iran's conservative elites' reaction, Khatami's presidency became a battleground between pro-democracy and traditional-Islamist forces and their respective social constellations. During these tensions, and up until today, the IRGC has consistently presented itself as the guardian of traditional revolutionary values. Therefore, in a sense, it has not changed its initial social values; its social values are still in accordance with values of a portion of population that favors islamist and traditional ideals of the 1979 Revolution. However, given the pervasiveness of Khatami's reform movement, as well as the Green movement that rallied behind the reformist candidates in the 2010 presidential election, one can conclude that the IRGC has not incorporated values of the pro-democracy portion of the population.

Additionally, the rapid privatization led to the transformation of the IRGC into an economic actor. The consequences of this change have been twofold: first, although the IRGC maintains the Islamic revolutionary values, in pursuit of its economic interest, it deviated from its initial responsibility of assisting the state in development. In other words, although the IRGC has been portraying itself as an institution that upheld revolutionary value of "defending the oppressed", its behavior has not been reflecting a devotion to the revolutionary values of eradicating poverty. For an institution that portrays itself as the servant of the state, it has been undermining state's attempts to facilitate economic development.

For example, the IRGC's self-interested behavior was evident in the activities of its Mehr Finance and Credit Institution. Mehr provided housing and loans to the Basij members, had more than seven hundred branches, and were known as "the largest 'Private' Bank in the Islamic Republic". However, this institution has been criticized for refusing to give out loans to disadvantaged groups and instead has been caught in large trades in the Tehran Stock Exchange through its subsidiary, Mehr-e Eghtesad-e Iranian Investment Company (Afloneh 2010, 3-4). Such evidence highlights a disconnect between the ideological convictions of IRGC and its actual behavior. The IRGC's economic projects in strategic sectors, and the subsequent impacts it has on foreign capital attraction, is another example of IRGC's negative influence on Iran's economic development.

There have also been rumors regarding the IRGC's involvement in illegal activities. Sadri explains how the IRGC is believed to have monopolized the "smuggling of alcohol, cigarettes and satellite dishes, among other things in great demand" (Sadri 2009, 102). In fact, during a political rift between Ahmadinejad and Khamenei, Ahmadinejad, in retaliation, revealed information about the IRGC's illegal smuggling of cigarettes. If the rumors were true, the IRGC engages in the import of alcohol and satellite dishes and simultaneously preaches Islamic values, condemns consumption of alcohol, arrests people for possession of alcohol, destroys satellite dishes, and criticizes the dissemination of Western values. The contradictory behavior illustrates how the IRGC operates based on the interests of its own corporation rather than a simple adherence to the values of the revolution.

Hence, the IRGC began behaving like a corporate entity seeking profit-maximization. The IRGC is still ideologically Islamic and in line with traditional social values, but is also a self-interested organization with a network of beneficiaries and social constellations that exert pressure on the organization. Moreover, the IRGC's self-interested behavior in the economic domain has undermined the state's economic growth and prosperity. Therefore, the IRGC might claim that it is protecting the regime and serving the values of the 1979 Revolution, but its economic role expansion and subsequent behavior has hurt the state and the future of its economic development.

Conclusion

This chapter sets forth three hypotheses: The haphazard or incomplete economic liberalization in Iran, has conditioned emergence of the IRGC as an established economic and political player. The outcome has been decrease in civilian control of the IRGC relative to the decade prior to the liberalization. Functional capabilities of the IRGC has not changed dramatically, whereas decades of engagement in economic activities has turned the IRGC into an economic interest group, and hence has reduced the social control.

Chapter 5: Economic Liberalization and Egyptian Armed Forces' Government

Take-Over

Introduction

Decades of economic liberalization and privatization policies in Egypt culminated in the establishment of crony capitalism. Different from the state-led reforms in East Asia or China, the economic liberalization and privatization in the Middle East and North Africa, including in Egypt, led to “nomenklatura privatization” (Cammett et. al 2015, 280) or “capitalism from above¹¹³” and the emergence of crony capitalism in Egypt. These reforms have incorporated trade liberalization and rapid privatization in a context of incongruent regulations; they also focused on the task of reform as an objective rather than a strategy to achieve developmental goals, and hence, failed to direct the liberalization and privatization to boost Egypt’s private sector and support productivity.

The Egyptian Armed Forces (EAF) operated under the conditions of a rapidly liberalizing and privatizing economy. Like the cases of Iran’s IRGC and China’s PLA, the EAF also had a history of engaging in economic developmental projects under Nasser’s

¹¹³ Drawing on King and Szelenyi’s (2005) and Harris’ (2013) classification of capitalist developmental models.

leadership. Since 1980s, and primarily under Mubarak's privatization plan in the 90s, the EAF captured opportunities offered by rapid privatization and acquired new economic projects. The EAF expanded into new economic sectors, such as international trade and energy. The economic power struggle between the EAF and Mubarak-affiliated elite, more precisely Hosni Mubarak's son, Gamal Mubarak, ended when the EAF defected from the civilian elite during the 2011 Egyptian revolution.

In this chapter, I illustrate how the economic liberalization and privatization during Sadat, and specifically Mubarak, led to the EAF's rise into economic power; later the EAF transformed its economic empire into a political power. I argue that the types of economic liberalization and privatization resulted in the EAF's economic role-expansion and made it less dependent on the civilians. This changing balance of power between governing civilians and the institution of military became problematic once the civilians attempted to limit the EAF's economic power. In the absence of both economic competition and an independent private sector, economic tensions rose between the civilians and the EAF over Egypt's future economic trajectory. The EAF resisted economic change. In the context of these rising tensions, the 2011 Revolution became a catalyst for the EAF to assert its independence from the civilians. The economic calculation played an integral part in EAF's decision to defect from Mubarak's regime.

The next section will outline the economic liberalization and privatization under Sadat and Mubarak to illustrate the process through which Egypt facilitated the emergence of crony-networks, including the establishment of the EAF as an economic player.

Egyptian Economic Trajectory and the Rise of the EAF's Businesses

Economic liberalization since 1974 aimed to address inefficiencies of Nasserist command economy. An uneven process of trade liberalization, capital attraction, and privatization of State Owned Enterprises (SOEs) failed to establish market mechanisms. Instead of fostering private sector growth and economic productivity, Egypt struggled with macro-economic instability, capital attraction in unproductive sectors, and capture of state resources by crony-networks consisting of several state-linked business networks, primarily Mubarak's affiliates, and the EAF. The economic liberalization and privatization did not stimulate economic competitiveness, private sector growth, and economic diversification. In fact, Egypt's low economic performance coupled with the dominance of crony-networks, including the EAF, exemplified its lack of competitiveness.

The EAF, similar to the IRGC and the PLA, entered the economic domain during the period of central planning. Nasser (1956-1970) assigned high rank officers the supervisory role over nationalization and import substitution industrialization policies and thus sanctioned the EAF's entrance into the non-defense sectors of the economy¹¹⁴. Pan-Arab nationalism and the prominence of statist developmental models colored Egyptian economic policymaking; the EAF became a major player, accepted both by domestic and international actors such as the USAID, to accomplish domestic industrialization and developmental projects. The EAF became involved in projects on land reclamation, infrastructure building, basic commodity provision, manufacturing of appliances and

¹¹⁴ Joudeh, Safa. "Egypt's Military: Protecting its Sprawling Economic Empire," *Atlantic Council*, January 29, 2014. <http://www.atlanticcouncil.org/blogs/menasource/egypt-s-military-protecting-its-sprawling-economic-empire>

electronics, and other industrial projects such as steel and fertilizers. Officers became managers and administrators in factories and SOEs (Marshall 2015). Seeing itself at the forefront of national development, the military obtained power over both use of public lands and public enterprises (Roll 2017, 2). Hence, similar to Iran and China, the EAF engaged in developmental projects during the period of central planning; it also became active in industrial production.

The EAF's economic expansion into new domains has been a gradual process. However, the acceleration of the privatization process during Mubarak was the turning point in terms of the EAF's capability to amass substantial economic leverage. This economic expansion occurred in an economy where selective protectionism had established state-linked businesses since the late 1970s and 1980s. In the absence of economic competitiveness, the crony-networks pressured the government to obtain economic resources. Once privatization accelerated, the EAF was offered ample opportunities to establish itself as an economic player too. Therefore, an interplay of weak private sector, an undiversified economy, and privatization that prioritized the sale of SOEs to strategic actors over to private ones, enabled the EAF's economic rise. In the late 2000s, the EAF refused to privatize its businesses and finally outcompeted other crony-networks once the revolution destabilized Mubarak's regime in 2011.

El-Ghonemy summarizes four economic development periods in Egypt: market-based economic policies that existed pre-1952 revolution, Nasser's central-planning from 1956 to 1970. Financial liberalization and structural adjustments from 1970 to 1990 that did not resolve Egypt's economic problems, such as its bloated public sector, and

ultimately a stark shift to a new strategy of economic liberalization from 1991-2000 that focused on the goal of achieving technological advancement and competitiveness in the global economy (El-Ghonemy 2010, 74). The types of EAF's economic role-expansion also corresponded to the above strategies. While during Nasser, the military was engaged in development and industrialization projects, since liberalization in 1973, the EAF's economic projects increased gradually. However, it was under Mubarak that the EAF's focus shifted away from economic developmental roles; in line with Mubarak's policy of opening to the global economy, the EAF also diversified and entered global markets. Specifically, a privatization policy focusing on joint-venture formation enabled the EAF's entrance into the global economy. The EAF began diversifying its businesses and commercializing by partnering with domestic and foreign private investors to access both finances and technology. The EAF's international joint ventures operated in industries such as car manufacturing, hardware, and solar panels. In addition, the EAF became a shareholder in critical domestic projects such as privately owned cargo container facilities (Marshall 2015, 4-6).

The modes of economic liberalization, and specifically privatization policies, explain the reasons behind the growth of crony-networks, as well as the EAF businesses and its ability to outcompete other economic players since 2001. Drawing on King and Szelenyi's (2005) and Harris' (2013) arguments on capitalist developmental models, I illustrate that the Egyptian rapid liberalization and privatization, in the absence of regulatory and bureaucratic reforms, established a state characterized by "capitalism from above". In this system, as Harris (2013) would explain, preserving patrimonial

relationships took precedent over entrepreneurship; political exchange, rather than market exchange, determined the nature of economic relationships. The economic system suffered from a lack of industrial dynamism; its market mechanisms were weak, and capture of SOEs by the patrimonial networks was common (Harris 2013, 65-66). Under these uncompetitive economic conditions, the state-linked business elite, including the EAF, maintained the economic system that benefited them.

Some of Sadat's and Mubarak's main economic liberalization policies encompassed trade liberalization, capital attraction, and industrialization. Embarking on trade liberalization, Sadat's rapid trade approach created a balance of payment deficit. Sadat inherited an economy overburdened by ambitious development projects (1960-65), aid-dependency and a low rate of private savings (Amin 1981, 430). His strategy of rapid trade liberalization and utilization of short-term credits to finance projects exacerbated inherited budgetary problems; the outcome was import of 'capital and intermediate' goods for consumption rather than production. While the trade boosted the housing market, other industries such as cement, paper, cigarettes, tires, and buses declined (Amin 1995). Ultimately, the Egyptian economy suffered a balance of payment deficit. Since the late 1980s and 1990s, Mubarak also adopted his own version of trade liberalization, which also negatively impacted production since it did not account for the impact of product dumping on domestic manufactures. Similarly, Mubarak's trade liberalization increased imports and weakened domestic production (El-Ghonemy 2010, 78-83).

The experience of trade liberalization illustrates the inadvertent character of economic policy-making. Egypt's liberalization and privatization attempts did not

encompass specific plans to meet state's developmental goals. As Gillespie and Sotever (1998), Egypt liberalized "for its own sake, without viewing...[liberalization] as a means to an end". This kind of undirected reform was evident in Egypt's policies of capital attraction and industrial development plans as well. For example, this lack of planning was evident in fluctuating net inflows of capital: in 1990, capital inflow to Egypt was \$ 734 million; in 2003, it was around \$237 million. It hiked to \$11.578 billion in 2007 and dropped to about \$-482 million in 2010.

Regarding capital attraction during Sadat's rule, investments went to unproductive sectors. As evident in sharp fluctuations¹¹⁵, capital attraction efforts were vulnerable to inept planning and execution, and were exacerbated by political instabilities. This incompetence was primarily a result of decoupling economic liberalization from the reform of regulatory and institutional frameworks, a process whereby foreign investment was not directed to achieve developmental goals. For example, the state created free zones but did not adopt export-oriented policies that would boost competitiveness. The state enforced joint-venture formations with foreign companies, but because the domestic private companies were not large enough, the foreign investors were forced to work with the SOEs, which subsequently discouraged the foreign companies from investing in the domestic economy (Gillespie and Stoever 1988).

¹¹⁵ "Foreign Direct Investment, net inflows", World Bank Data, n/d. The data suggests that Foreign investment fluctuated radically at different periods. According to the World Bank data, there were substantial fluctuations of FDI (net inflows, BoP), with \$ 1.216B in 1979 and \$1.25B in 1989 as the highest points and then dropping to \$295.571B in 1982.
<https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?locations=EG>

Therefore, Egypt's trade and capital attraction strategies did not promote exports, nor did they promote competitiveness in production. Its policies instead contributed to the establishment of an economically uncompetitive system. Due to the economy's uncompetitive nature, the EAF businesses were able to survive and thrive. For example, the process of investment in unproductive sectors continued leading to investment in domains dominated by the EAF. The military's position in profitable sectors were greater than other economic actors, and subsequently attracted more foreign investment. Additionally, military businesses have been able to establish partnerships with gulf conglomerates and western multinational corporations using the International financial institutions' loans (Casabon 2015).

Although both Sadat and Mubarak adopted industrialization strategies, neither succeeded in fostering private sector development. Sadat's industrial policy retained Egypt's rentier economy instead of boosting industrial production. Mubarak attempted to resolve inefficiencies of a rentier economy and Egypt's bloated public sector. State's heavy debt, however, hampered Mubarak's industrialization plans. Under Sadat, Egypt's GDP share of industrial production exceeded agricultural production by 1979 (30.5% for industry and 21% agriculture), but the main portion belonged to largely oil production. Along with an increase in the oil production (57.4% of GDP in 1983), the share of manufacturing in the industrial sector dropped from 79% in 1975 to 40% in 1983 (Algan 2003, 160-161). Instead of an export-oriented strategy, Mubarak (1981-2011) also attempted to reestablish import substitution industrialization to boost industrial production. His plan offered protective tariffs to domestic industries and lowered their interest rates

and taxes. Mubarak, however, could not resolve the problem of domestic debt, partially due to the high political costs of cutting spending. Again, as has been discussed thus far, Egypt's economic reform failed to foster productivity, competitiveness, and diversification of the Egyptian economy.

Although Egypt registered GDP growth, it failed to improve its global competitiveness relative to China's ranking. For example, the World Economic Forum's data suggests that in the category of ability to encourage technological advancement, the rank of spending on research and design was 70 out of 104 in 2004/2005, whereas China ranked 26. Hence, the privatization in the late 90s and early 2000s, and the liberalization that focused on technological advancement, did not yield expected results. This is despite the fact that Egypt had a higher rank for FDI and technology transfers compared to China: Egypt's rank was 44 while China ranked 52. Therefore, although Egypt opened its economy, it could not foster economic competitiveness. Egypt's global competitiveness index fluctuated dramatically and did not indicate a consistent growth over decades either.

Table 9: World Economic Forum¹¹⁶, Egypt's Growth Competitiveness Ranking (1985-2017)

	1995 (out of 48 states)	2000(out of 58 states)	2004/2005(out of 104 states)	2005/2006 (out of 117 states)	2015 (out of 134 states)
Egypt	27	42	62	53	115
Adjusted rank (out of 134 states)	75	97	80	61	115

¹¹⁶ World Competitiveness Reports (1995, 2000, 2004/05, 2005/06, and 2015).

The above rankings highlight the outcomes of Mubarak's implementation of Structural Adjustment Policies (SAP) following constant renegotiations with the IMF and the WB. After the Gulf War in 1991, along with a promise for debt cancelation, Egypt agreed to a new package of the SAP policies (Amin 1990, 21). While these policies¹¹⁷ boosted growth, they also received ample criticism (Ansari 1987, Belev 2001, Sika 2013) since they addressed short-term fiscal problems instead of establishing market mechanisms and competition. Instead of resolving structural inefficiencies, the regimes' implementation of the SAP exacerbated political and economic instabilities. In Egypt, particularly, crony-networks emerged and consolidated their power in the 90s, with the EAF rising into power in 2000s (Casabon 2015).

Therefore, the state, unable to implement the SAP effectively, constantly struggled with introduction of new workable policies. Privatization being one of those strategies, Egypt also experimented with various privatization policies, but these policies did not strengthen the private sector either. On the contrary, during privatization, as Wurzel (2004) discusses, Egypt experienced the growth of interest groups. Wurzel (2004) underscores the institutional context, i.e., the specifics of the rentier state, to explain the economic networks' behavior in the context of privatization. To alleviate the state's fiscal burden of indebtedness and inefficient state-subsidized SOEs, privatization was destined to alter the "power equilibrium" by favoring new actors vis-à-vis public actors. Instead, unlike expectations, privileged networks manipulated pre-reform conditions in their favor (Wurzel 2004: 104-105).

¹¹⁷ The Washington Consensus.

As Nagarajan explains, not only did the SAP produce a “triangle of poverty,”¹¹⁸ it also facilitated the emergence of “conglomerates owned by politically well-connected families” instead of establishing a competitive market. “Osman, Bahgat, Seoudi, Mohamed Mahmoud and Orascom groups” were families that formed conglomerates and formed joint ventures with foreign partners (cited in Nagarajan 2013, 32). Sika, similarly argues, that the Washington Consensus has not produced the expected results. In the case of Egypt, liberalization and privatization contributed to “strengthening ties among the government, the ruling party, and the businessmen.” For example, the Investment Law 8 in 2005 did not lead to the establishment of a free market; on the contrary, deregulation and tax-marketization conditioned the emergence of monopolies, whereby alliances between the government and the business elite led to the misuse of public resources (Sika 2013, 45-47).

Shahid (2002) also assesses the reasons behind the success of some networks in capturing resources. The author underscores the impact of privatization in creating networks—a process through which state officials and former bureaucrats formed networks, captured the spoils of privatization, and sidelined the established business actors (Shahid 2002, 78). A new network consisting of state-business connections emerged in the 90s whereby the businesses played a two-level game: preserving crony capitalism and competing over rents created by shifting policies (Shahid 2002, 78). These business elite consisted of mainly 32 businessmen involved in import substitution; they benefited from protectionism and could not compete in the international markets. They were further strengthened in the 90s because the privatization allowed them to both sustain and enlarge

¹¹⁸ Unemployment, low wages, and income inequality.

their interests against exporters who suffered from a collective action problem. These networks sustained the uncompetitive character of the system—access to information, connections with the bureaucrats, and economic opportunities—because it benefited them and weeded out competitors (Shahid 2002, 98). EAF also operated as an economic actor, and subsequently benefited from the same privatization policies.

In terms of the EAF's economic power, scholars (Abul-Magd 2011, Casabon 2015,) have highlighted the linkages between privatization policies under Mubarak and the EAF's economic growth. For example, Abul-Magd explains that Sadat's privatization and import of consumer goods led to a partial downgrading of military power due to the privatization of a portion of military-controlled SOEs and facilitated the rise of new Sadat-affiliated crony capitalists as competitors with the military economic power. However, this period was short-lived and was reversed after the 1979 Peace Accord; the following years' policies strongly contributed to the further expansion of the military's economic clout accompanied by subsidies and tax exceptions for the EAF. Later, Mubarak's privatization and liberalization project in 1992 did not include the privatization of military businesses. On the contrary, the military retained its businesses, and the corruption in the process of privatization benefited high-ranking officers who received positions in privatized SOEs¹¹⁹. Although since 1998 Egypt attempted to make the privatization reliant on market forces, the process did not result in the sale of SOEs to private actors. Instead, it mainly took place via the sale of SOEs to strategic investors (Shahid 2002).

¹¹⁹ Abul-Magd, Zeinab. "The Army and the Economy in Egypt," *Jadaliyya*, December 23, 2011. <http://www.jadaliyya.com/pages/index/3732/the-army-and-the-economy-in-egypt>

Casabon¹²⁰ (2015) also argues that although Sadat's Infitah introduced market mechanisms and boosted US-Egyptian private sector growth, it was the privatization in the 90s that entrenched the military's role as an economic actor. Offering an estimate of the military's share of the GDP as 40 percent, military businesses were part of a broader public sector whose enterprises benefited from "private oligopoly" system that originated post-privatization. While SOEs privatized and the welfare state shrank, the oligarchy emerged with the aid of "state subsidies and almost exclusive access to bank credit"; furthermore, the state offered tax cuts to boost investment. In the context of capital inflight, the EAF businesses attracted international investments due to their dominance in the profitable sectors. Meanwhile, the tax system did not support smaller businesses. Smaller businesses were unable to grow and incapable of guaranteeing basic rights and benefits to laborers due to the lack of opportunities to borrow (Casabon 2015). Therefore, selective protectionism, instead of competitiveness, prioritized state-linked economic actors, specifically the EAF, over the private sector.

There are radically different estimates on the EAF's share of the Egyptian economy. Marshall and Stacher (2012) report that estimates vary between 5 to 40 percent or more (2012, 12). Other reports suggest fluctuations between 40 percent (Naguib Sawiris) to 40-60 percent (Transparency International). Springborg, an expert on the EAF, offers an estimate of 10 to 40 percent¹²¹. If the EAF controlled about the 40% of the Egyptian

¹²⁰ Casabon, Christina. "Egypt's Military Economy", *opendemocracy.net*, July 29, 2015. <https://www.opendemocracy.net/north-africa-west-asia/cristina-casabon/egypt%27s-military-economy>

¹²¹ Kholiaf, Dahlia. "The Egyptian Army's Economic Juggernaut", *Aljazeera.com*, August 5, 2013. <http://www.aljazeera.com/indepth/features/2013/08/20138435433181894.html>

economy, and since 2012 has been acquiring more projects, it is safe to assume that the EAF has become a central economic player in the Egyptian economy. In an interview with Al Jazeera, Springborg, an expert on Egyptian military, stated that "The question isn't what sectors do they [the EAF] invest in, but rather: is there a sector that they don't invest in?" For example, Ministry of Military Production runs 14 companies that produce military equipment such as tank shells and ammunition, as well as civilian goods such as "fertilizers, sports equipment, cement, pasta and cars"¹²².

Therefore, since Sadat, and following liberalization policies in 1970s, the EAF's assumed new economic projects in building infrastructures (waterways, transportation, telecommunication, construction); it also became involved in real estate and housing, food self-sufficiency, and import of commodities (Roy 1992, 703). Furthermore, the 1979 Egyptian-Israeli peace treaty led to cuts in defense expenditure, and the EAF was ordered to generate its own defense revenue¹²³ (Harding 2016, par.3). Hence, transforming its military production into a civilian one, the Ministry of Defense-affiliated National Service Project Organization (NSPO) controlled the military's economic production in the civilian domain, including the production of washing machines, heaters, clothing, pharmaceuticals, tourism etc.¹²⁴

¹²² Ibid

¹²³ Harding, Henry. "Analysis: Egypt's Military-Economic Empire," *Middle East Eye*, March 26, 2016. <http://www.middleeasteye.net/news/analysis-egypts-military-economic-empire-35257665>

¹²⁴ Stephen, LTC., Gotowicki, H. "The Role of the Egyptian Military in Domestic Society", 1997. <http://fmso.leavenworth.army.mil/documents/egypt/egypt.htm#26>

The EAF is also affiliated with the Arab Organization for Industrialization the National Services Projects Organization (NSPO), and the Ministry of Military Production, as well as infrastructure-building semi-public or private companies. It also operates in strategically significant civilian sectors, such as airports. According to Transparency International, the businesses profit both the military institution and individuals. The EAF has been controlling most the public land (desert, agriculture, and urban: 94 percent of Egyptian land) and receives compensations from the government by auctioning the land and transforming military zones into civilian ones. Control over the coastline, categorized as a border, is another source of revenues following developments in tourism industry. The following table summarizes both the sectors of activity and known companies related to the EAF:

Table 10: The EAF's Economic Role Expansion (Sectors & Companies)

Sector	Company name	Notes
Food Production	The National Service Projects Organization (founded in 1979)	Army runs chain of supermarkets representing 28% of population living below poverty line
Energy	Since 2016, Ministry of Military Production and Ministries of Petroleum and Electricity established a joint company to maintain state's power-stations Tharwa Petroleum Company Arab Organization of Industrialization formed joint ventures with a firm from UAE to invest in renewable energy	Provision of electricity Veto power over oil and gas production since 2016
Mixture of civilian and military goods	Ministry of Military Production Arab Organization of Industrialization	

Construction and Infrastructure	Armed Forces Engineering Authority	Developmental projects +Building parks and ports in the Suez Canal
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Therefore, overall privatization strategies were irregular, the pace of privatization fluctuated, and the ultimate outcome was consolidation of crony-networks rather than the development of a private sector. Similarly, even in 2000s, when Mubarak authorized Gamal Mubarak to embark on a rigorous economic reform project to strengthen the private sector, the reform produced mixed outcomes. A privatization program, overseen by Ahmad Nazif’s cabinet (2004-2011), aimed at creating a corporate sector capable of competing internationally. The program included banking privatization, reforms of trade and the tax system (tax cuts and restructuring administration), and liberalization of the financial sector in 2005. These policies led to an increase in growth, as well as an increase in FDI (8.1% of the GDP) in the energy, real estate, and tourism sectors, as well as a construction boom. However, from the mid-2000s, a combination of insider firms and ventures linked to Gamal Mubarak directed this process of reform. These ventures had the support of the state, were financed by international and Arab interests, and profited from the privatization process. These emerging businesses had positions in the governing bodies and were connected to one another, which gave them leverage over economic policies (296). Privatization did not resolve inequalities and did not alleviate poverty or unemployment. The “[c]rony nature of private-sector development” hampered private sector development and has empowered “a new class of capitalists connected to the state” (295-296).

In 2008 Mubarak, adopted a new proposal to privatize 86 out of 153 public companies via “voucher privatization” and “mass privatization.”¹²⁵ Despite a history of privatization in Egypt, according to Saif, the problem was over a “highly publicized shift” in privatization after the adoption of new regulations in 2008. Citing Mubarak’s interview in Al-Ahram Weekly, where he defends “greater involvement of the people in managing public assets,” Saif expressed concerns regarding Mubarak’s attitude towards ownership, and public-private relations. Saif explained that the literature suggests that a mere transfer of ownership has not been the most important factor in successful privatization but rather coupling of the ownership-transfer with suitable regulation and increased competition. The author argued that allowing the public to partake in ownership would not facilitate wealth distribution. He anticipated, then, that what was required was the establishment of institutions that would thwart monopolies and their formation. Unlike Mubarak’s expectation, the author predicted the rise of “opportunistic businessmen” in the absence of a clear institutional mechanism to manage privatization, along with unclear goals such as the involvement of the Egyptian population to manage the SOEs.

Liberalization and privatization strategies of Sadat and Mubarak (in 90s and in 2000s) did not foster competitiveness. On the contrary, the state experienced emergence of business-elite that benefited from selective protectionism and hampered competition. What were the implications of this uncompetitive economy? In an uncompetitive unfair system, the military businesses benefited. First, the military utilized the cheap (forced) labor by

¹²⁵Saif, Ibrahim, Choucair, Farah. “Egypt's Privatization Initiative Raises Questions,” *Carnegie Endowment*, December 2, 2008. The IMF imposed SAP since 1991 contributed to the sale of 26% of the SOEs to Employee Shareholder’s Associations, 24% were privatized via stock market, 24% via liquidation, and 22% were sold to anchor investors. <http://carnegieendowment.org/sada/22479>

conscripts who were employed in military businesses. It also benefited from a system of licenses and permits that favored the EAF in biddings for public contracts and facilitated creation of partnerships with private investors. While these public-private partnerships held the state reliable for losses, the EAF reaped the profits. Moreover, the EAF had an advantage over competitors due to its access to off-book subsidies. For example, the Supreme Council of Armed Forces (SCAF) decided to increase the prices of fuel for industries that competed against EAF businesses while the EAF purchased subsidized fuel. Additionally, not only were military businesses not productive, they prevented the growth of small-sized private sector enterprises due to unfair competition.

An example is EAF's profiteering via imports without a necessity to create jobs or be productive. Roy (1992) identifies the EAF as a major contributor to the 'secret economy. It manages lands, produces food for domestic consumption, engages in real estate development, speculations, and investments, provides for-profit health services to the civilians by utilizing its military hospitals; it makes textbooks, smuggles goods via free economic zones, uses military resources for private constructions, and reclaims lands (Roy 1992, 704). This hidden economy utilized inadequacies of the public sector, and its operation had repercussions for wealth distribution. It created wealthy groups who did not necessarily invest in domestic projects but rather sent their capital overseas, benefited from corruption, and created a business environment un-conducive to production, innovation, and profitability. This economic system also created coalitions between the military and big businesses (Roy 1992, 709-710). These networks have created a self-perpetuating cycle of inefficiency whereby economic survival is a function of selective protectionism and

access to the state resources rather than of firms' profitability and competitiveness in a free market economy. In turn, these economic actors, including the EAF, impede the development of a functioning market and an independent private sector.

Abul-Magd (2011), in an article titled "The Army and the Economy in Egypt,"¹²⁶ raises the issue of transparency of the EAF's economic activities. Not only have the EAF's economic activities not been subject to public debate, the EAF also lacks sufficient expertise for economic tasks. Abul-Magd explains that the military has announced its engagement in profitable enterprises such as "selling and buying of real estate on behalf of the government, domestic cleaning services, running cafeterias, managing gas stations, farming livestock, producing food products, and manufacturing plastic table covers," but there has been a taboo on public discussion around these activities, especially their contribution to the military budget. Although the defense-related activities' budget was available to the public due to the demands of foreign donors (US aid) for transparency, it is the non-defense portion of the military budget that is kept secret. Abul-Magd argues that the military were an obstacle to liberalization policies (neoliberal model) not due to its convictions to a socialist model but due to its economic interests. Corrupt practices, such as forcing the purchase of army-produced food by the soldiers in remote areas, offering deals to civilian distributors to assist the military in selling its products, and a law permitting the military to take over public lands for defense or commercial purposes also became sources of profit.

¹²⁶ Abul-Magd, Zeinab, "The Army and the Egyptian Economy," *Jadaliyya.com*, December 23, 2011. <http://www.jadaliyya.com/pages/index/3732/the-army-and-the-economy-in-egypt>

As discussed thus far, new elite-business alliances emerged post-privatization, in the early 2000s. Although the EAF's expansion into new domains occurred from the 1980s, the Egyptian economy, in the late 1990s, also faced the emergence of Gamal Mubarak's network of businessmen whose ambition to monopolize and privatize threatened the EAF's economic empire. Known for their neoliberal ideology, this new group challenged the ruling elite by seeking to expand their control within the National Democratic Party (NDP). This group challenged the EAF's monopolies in some sectors; they emphasized privatization in sectors controlled by the state and the military, i.e., national banks and land reclamation projects (Salem 2013, par. 10-11)¹²⁷. The threat of the new business elite was later instrumental in the EAF's decision-making process but also illustrated how the establishment of the EAF as an economic actor provided it with enough economic leverage to weed out its competitors when the opportunity presented itself.

The EAF succeeded in securing economic assets over the course of rapid privatization and transformed itself into an economic actor. Once the state decided to target military-owned businesses, the military reacted by defecting and later executing a government take-over in order to expand its businesses. Hence, taking over the Egyptian political and economic system, under Gen. Sisi's leadership, the Egyptian military was in a unique position to further expand its economic empire. Egypt's economic liberalization and privatization led to the emergence of what Harris (2013) characterized as capitalism from above. The EAF's economic expansion was also an integral part of this economic

¹²⁷Salem, Sara. "The Egyptian Military and the 2011 Revolution," *Jadaliyya.com*, September 6, 2013. <http://www.jadaliyya.com/pages/index/14023/the-egyptian-military-and-the-2011-revolution>

developmental model. The next section will focus on the impact of these economic policies on the question of civilian control.

The Political Control of the EAF

This section tests the number one hypothesis regarding the impact of Egypt's uncompetitive economy on increased political leverage of the EAF. (H1) suggests that the incomplete economic liberalization and inability to establish competitive mechanisms provided opportunities for the EAF's consolidation of its businesses, and ultimately led to the EAF's assumption of political power. Although the EAF, similar to the militaries of Iran and China, has been involved in the political sphere, the degree of civilian control over the military declined following the EAF's further expansion into the economy. The economic interest played an integral part in the EAF's decision to defect from Mubarak's regime during the 2011 uprising, and later in its takeover of the government in 2013.

Similar to other autocratic regimes, Egypt's civilian control is also void of democratic institutional mechanisms of control. Since the 1952 Revolution, the Egyptian military has been an indispensable part of the autocratic rulers' power calculation and has played an integral role in suppressing dissent. However, given the account of civilian control as a continuum in the present study, the degree of civilian control of the EAF changed in the aftermath of Mubarak's liberalization policies. Although the line between civilian and military control has historically been ambiguous, the EAF's responsiveness to the government changed in the aftermath of the privatization policies, specifically in the late 2000s.

It is imperative to note that in Egypt, similar to Iran and China, the military initially obeyed the civilians' orders. Although the EAF exerted influence, the scholars of Egyptian civil-military relations discuss its limited role in Egyptian politics. Droz-Vincent explains that the armies of Arab autocracies, despite their vital role, did not constitute the core of the autocratic regimes. Even in states where militaries were integral in forming new states, "there has been a creeping 'civilianization' or a 'demilitarization' of political systems" (2011, 2-3). The imperative has been state control via "a few networks of family members, high bureaucrats, political elites, economic cronies, and high officers linked to the president or king." In these autocratic regimes, including Egypt, the army supported the rulers, especially during crisis. There was a degree of separation between military and political affairs in Egypt. Even though some officers exerted political power, the military as an institution maintained distance from everyday politics. The military portrayed itself as the protector of the state and engaged in tasks of external defense. Examples of the army's involvement in crushing protests, such as the 1986 riots over salaries or the 1997 attacks of armed Islamists, according to the author, were exceptional moments rather than the norm (Droz-Vincent 2011, 3-4).

For example, Frisch (2013) also describes Egyptian politics as a system consisting of an authoritarian leader, who in operation with a small group of family members, businessmen, and experts "severely limited the military influence" (2013, 182). This status continued under both Nasser and Sadat, and later Mubarak (during the 90s). Although the EAF had significant influence over the defense ministry, Mubarak, for example, attempted to weaken the EAF by enhancing the budget and power of the police and allocating the

task of internal security to intelligence agencies, the Egyptian Intelligence Services. Mubarak also kept top military officers away from the position of Prime Minister (Frisch 2013, 183). Other scholars (Noll 2017, Droz-Vincent 2011) also underscore the limited political role of the EAF. Noll (2017) also points to the EAF's low political profile until the 2011 uprising (2017, 2), which later led to the removal of Mohammad Morsi in 2013.

Therefore, in assessing civil-military relations in Egypt, scholars underscore the contained nature of the EAF's role in the political governance of the state. Simultaneously, the discussions highlight the EAF's economic privileges. While the EAF was a politically subservient military, its role as a political player changed in the final years of Mubarak's regime. Understanding the EAF's defection from Mubarak's regime without an examination of its economic motives would be incomplete.

For example, Noll (2017) states how Arab regimes have utilized various strategies to keep militaries loyal, such as permission for the Egyptian military to engage in tourism-related activities in Sinai and coastal lands (Noll 2017, 3). Frisch (2013) also relates that the Egyptian state enabled the EAF's substantial economic expansion, especially in the 1990s. Frisch states that "the new more economic-oriented concept of national security was manipulated to enhance the Army's privileged role in the state and its economy" (Frisch 2013, 184). The increasing economic power became a major culprit for the civilians. The privatization in the 90s offered opportunities for networks with linkages to the state to expand their power; the state did not take measures to stop this process. On the contrary, the state facilitated this process by offering provisions to those groups, including the EAF.

It was when Mubarak's regime decided to limit the EAF's economic power that the EAF reacted. Although it succeeded in reducing the role of military in governing positions (reducing from 12 to 7 by 1989), attempts to curb the EAF's economic power failed. For example, in 1991, Mubarak assigned Yusuf Sabri Abu Taleb to the position of Defense Minister. Taleb aimed to divest military businesses but was removed and replaced by Mohamed Hussein Tantawi, who protected and retained the military's economic empire¹²⁸.

Furthermore, the EAF's rise into power in Egypt is an economic story. Analysis of civil-military relations in Egypt highlight the EAF's economic interest as a crucial factor in its decision-making. Albretch and Bishara (2011) discuss a change in the EAF's behavior since Mubarak's new wave of economic liberalization policies in 2003. The authors argue that although the EAF historically influenced Egypt's politics and economics, it did not have a direct governing role; the EAF remained in the background and retained its privileges. After 2003, however, the EAF became distressed with the increasing power of Gamal Mubarak, Husni Mubarak's son and his possible heir, as well as Gamal's economic policies. Suspicious of Gamal Mubarak's liberalization and privatization, the military supported state interventionism (Albretch and Bishara 2011, 18). Not only did rapid privatization and liberalization upset the public, the EAF capitalized on the situation to impede the process of reform.

The EAF's persistence in maintaining its economic interests post-2013 also supports the economic story. Under Mubarak, the EAF had a low political profile.

¹²⁸ "Die Welt: Egypt's Army Is its Real Economic Power", *www.middleeastmonitor.com*, April 5, 2014. <https://www.middleeastmonitor.com/20140405-die-welt-egypts-army-is-its-real-economic-power/>

However, since the 2011 uprising and removal of Mohammad Morsi in 2013, EAF has shown a consistent commitment in protecting its economic interests via political means. Ever since, the Ministry of Military Production has been growing in importance, signaling Sisi's priorities, which have been evident in his emphasis on the military's role in Egypt's national development as well (Noll 2017, 2). In September of 2016, Sisi spoke against the critics who considered the military's economic activities as an impediment to fulfilling its defense role competently; he claimed that the military is assisting the government to "rebuild" the state¹²⁹.

For example, Aljazeera¹³⁰ reports that on April 6th of 2012, grassroots groups initiated a campaign to boycott military products. As an activist state, "[j]ust like we're trying to bring them down politically, now we're also trying to do it economically and redistribute the wealth to the people." There was anxiety among generals regarding a possible increase in oversight over the budget. The military tried but failed to ensure its autonomy from budgetary oversight by trying to pass constitutional declarations¹³¹. Other newspapers also offer similar insights. The Middle East Monitor¹³² published a report based on a local newspaper's analysis of the EAF's motives. The report argues that the military junta "worked with all of its strength to protect its lucrative economic interests that made

¹²⁹ Hendawi, Hamza. "Egypt's President Defends Military's Economic Role," *apnews.com*, September 26, 2016. <https://apnews.com/e061093a45ab42b29074e7e95d1252f4/egypts-president-defends-militarys-economic-role>

¹³⁰ "Egypt Military's Economic Empire," *Aljazeera.com*, February 15, 2012. <http://www.aljazeera.com/indepth/features/2012/02/2012215195912519142.html>

¹³¹ Ibid

¹³² "Die Welt: Egypt's Army is its Real Economic Power," *www.Middleeastmonitor.com*, April 5, 2014 <https://www.middleeastmonitor.com/20140405-die-welt-egypts-army-is-its-real-economic-power/>

the military establishment a business empire and one of the most important factors influencing the country's economy.”

Moreover, measures have been taken to further reduce civilian control over the military budget. The 2014 Constitution assigns the National Defense Council, consisting of mainly military individuals, to control of the defense budget, eroding a civilian mechanism of control via parliament. In addition, important parliament committees and positions, such as the head of Defense and National Security Committee, were assigned from military intelligence services, eroding another mechanism of civilian control. There has also been evidence of increasing militarization of governmental positions ever since (Noll 2017, 6). It was in the context of threatened economic interests that the military began establishing itself as a political player. If one cannot distinguish the story of Egyptian revolution of 2011 from its broader economic context, it is safe to assume that the military as an economic actor operated to protect its interests.

The discussion so far highlights one key theme in all analyses—the EAF's economic interest as a motivating factor. Hence, any explanation underscoring political variables such as elite rivalries or the role of uprising must consider the EAF's economic interests in decision-making. In fact, understanding the Egyptian revolution of 2011 without studying the economic dimension would be incomplete. Scholars discuss the relationship of neoliberal economic policies to the 2011 uprising. Salem¹³³ explains how Gamal Mubarak's neoliberal agenda aggravated the anxieties of the public, leading to a

¹³³ Salem, Sara. “The Egyptian Military and 2011 Egyptian Revolution,” *Jadaliyya*, September 6, 2013. <http://www.jadaliyya.com/pages/index/14023/the-egyptian-military-and-the-2011-revolution>

revolution that, if it succeeded in overthrowing the regime, would also negatively impact the military's privileges. These economic policies also altered the balance of power among the ruling elite, incentivizing the EAF to intervene in 2011, resulting in a military-led transitional government and ultimately a constitution that under Morsi protected the military's businesses (Salem 2013, par. 17).

Similarly, Hanieh (2011) also analyzes the political crisis of Arab Spring by underscoring the significance of economic policies—neoliberalism. Beginning with Sadat's Infitah, the neoliberal policies empowered state-sponsored capitalist classes of military officers and a commercial bourgeoisie involved in foreign trade. Mubarak accelerated this process. With a specific aim to boost private sector, the liberalization of agriculture and state sector retrenchment resulted in the transformation of social relations in rural areas and the deterioration of working conditions for privatizing SOE workers (11-13). Growing disparities, whereby the state-affiliated elite benefited from privatization and the rest suffered gravely, led to waves of protests in Egypt in 1977 and later during Mubarak's reign in 2006-2008.

For example, Nagarajan argues that the IMF's and WB's evaluation of Egypt's success relied on measuring "short-term fiscal parameters." The policies were not conducive to long term growth but instead focused on supply-side economics, did not promote export-led strategies, and boosted the growth of the construction sector. In addition, SAP contributed to income disparity, growing inequality due to rising food prices, and stagnating wages (Nagarajan 2013, 31-32). Ghonemy (2010) also discusses the

consequences of short-term stabilization and long-term adjustment programs¹³⁴ that aimed at alleviating the fiscal/monetary system and resource distribution, respectively. Although data suggests a dramatic growth in the private sector's market share (from 9% in 1980s to 67%), its growth resulted primarily from a shrinking public sector; meanwhile, the export-promotion lagged. Unaddressed institutional barriers and lack of efficient infrastructure were among the factors impeding exports.

Challenging the neoliberal thesis, Hanieh (2011) argues that the IMF and the WB misjudged the success and resilience of the Egyptian economy when they praised Mubarak's attempts to implement the liberalization and privatization policies (Hanieh 2011, 15). Furthermore, unable to mitigate the shocks of the 2008 global economic crisis, Egypt suffered due to a decreased demand in exports to Europe, massive layoffs in Middle Eastern countries, and a loss of revenue from remittances, as well as increasing costs of food and energy (17-18). In this context, the protests that overthrew Mubarak were not merely political demands but a result of decades of accumulated grievances in the economic domain (Hanieh 2011, 22). In this scenario as well, the EAF became an arbiter during an economic struggle between the disenfranchised population and a political elite; it did so not out of concern for the population but to protect its own economic interests in a crippled regime.

Arguments criticizing the impact of neoliberal reforms on the social makeup offer two significant insights regarding the hypothesis of this section: first, decades of failed policies created a major cleavage between the poor and the elite, which resulted in uprisings

¹³⁴ Spearheaded by the IMF, the WB, Paris Club, and the US.

in 2011. Second, once the population began protesting in 2011, the EAF became pivotal in supporting the regime vis-à-vis protestors. However, given the history of tensions between the business elite and EAF over Egypt's economic policy, and vulnerability of the regime to ongoing protests, the EAF defected from Mubarak's regime, protecting its own institutional interests, primarily its economic interests, over the ruling elite. It did not defect in order to side with the population but to maintain its narrow economic interests.

Despite a plurality of stakeholders—the political elite, public sector technocrats, public sector managers, private sector, interest-based organizations, and various identity- and interest-based actors—the political elite have historically benefited from the rentier economy. Comprised of a network of families, these elite exploited the national economy and internal finances and maintained their political power and also co-opted various actors by offering economic privileges. Hence, throughout privatization, maintaining this pre-reform system of economic distribution helped preserve these alliances and networks and was in the interest of the state. Similarly, having established itself as an accepted economic player, the EAF reacted to a new wave of privatization policies targeting its businesses from 2003. The explanations for its defection from Mubarak's regime in 2011 would not be complete without considering the role of its economic interests, along its struggle with Gamal Mubarak's camp over economic policies.

The Functional Control of the EAF

This study assesses the impact of economic liberalization on the functional power of the EAF. Hypothesis number 2 suggests that if economic liberalization is incomplete, there is a higher likelihood for the military to turn into an economic interest group, which

would decrease the functional efficacy. Note that this study assesses changes in the functional control prior to and after economic liberalization. However, assessing H2 with regard to economic policies impact on the EAF's functional power is challenging given the role of the US military aid and training. Separating the impact of economic liberalization on functional capabilities from the impact of military aid would be a problematic task.

Testing four dimensions of functional control—integration, responsiveness, skills, and quality—this section will illustrate that despite the US military support, the EAF has not registered a remarkable improvement in its functional capabilities. Given the lack of evidence and reports on Egyptian military's functional power, as well as on the role of military aid, this section will argue that an absence of strong evidence suggesting a notable change in functional capabilities of EAF throughout decades could help extrapolate two relevant conclusions: (i) as the hypothesis would predict, the incomplete economic liberalization and subsequent transformation of EAF into a commercialized military has turned it into an interest group and consequently negatively impacted its functional capabilities, and (ii) even if lagging functional capabilities are the results of non-economic variables, one could conclude that economic liberalization did not have a positive impact on functional capabilities or had no impact, to say the least.

First, Huntington's (1964) argument of objective control and professional military's obedience to the civilians does not apply to the case of Egypt given EAF's role as governors of the state today. Hence, because the EAF has assumed political roles, the presumed relationship between professionalization and subsequent objective control does not exist. Given the EAF's political role in governing the state, one could conclude that the

EAF has not undergone professionalization to an extent that would turn it into an exclusively professional military. Consequently, its functional capabilities have lagged throughout the decades.

Since 1987 to 2012, the US provided \$1.3 billion yearly in aid to Egypt's military. Egypt has been the number two receiver of US bilateral foreign assistance after Israel. Despite US aid and military training, analysts highlight discrepancies between readiness, training, and weaponry. After 1973, the EAF underwent professionalization in terms of weapons' acquisition and trainings. However, the outcome was deemed slow and incompetent. As Kechichian and Nazimek (1994-95) explain, the professionalization of the military institution followed the 1979 peace treaty (Kechichian and Nazimek, par. 1). This transformation has not been easy. First, despite \$1.3 billion in yearly US aid since 1979, the transformation from Soviet to Western equipment was challenging, with 50% of the equipment belonging to the Soviet era by the mid-1990s. A change in weaponry was coupled with new training, especially via programs such as International Education and Training (IMET) provided in the aid package. The officers trained in the US acquired new skills; since the 1990s, new tactical concepts were introduced to the military. However, as Kechichian and Nazemik assess, "a cadre of Egyptian military leaders remained primarily Soviet-trained," which resulted in their attempts to marginalize US-trained officers via mechanisms such as loyalty tests or limitations on promotions (par. 6-7).

Reports of such inconsistencies between the quality of procured weapons and personnel's ability to utilize them, or implement their skills, are not limited to the 90s. McGregor, in a report published in 2006, explains that although the EAF has been a

recipient of US aid and training since the 1979 Camp David Accord, the military's personnel are mainly underpaid conscripts who do not pursue a career in the military. Relying on inexpensive manpower, the military has become bloated; there have been riots and defections as well. Importing modern technology does not translate into effective utilization of such equipment due to low education levels of conscripts from the regions (McGregor 2006, 283). According to CNN's¹³⁵ analysis of the WikiLeaks cables, there have been reports of mid-level officers' discontent with their leadership; an account in 2008 suggested that promotions were based on loyalty, and those officers who were considered too skilled were perceived as threats to the government.

With regard to its strategy, Egypt since 1979 has adopted a defensive strategy. Stratfor¹³⁶ (2015) reports that even after the revolution of 2011, the military has been primarily focusing on conventional capabilities despite its leaders' awareness of threats of asymmetric warfare (insurgency and terrorism). The wars with Israel, albeit highly unlikely, are still part of the consideration (Khaled 2015, par. 9). A focus on conventional capabilities is in line with Egypt's military tradition of preparing for large-scale wars, partially due to the military's goal of exhibiting a positive image of itself (Khaled 2015, par. 11-12). There is a consistency, at least until 2011, in Egypt's defensive approach. For example, in an interview in 1987, the then Minister of Defense and War Production announced, "military balance in relation to surrounding countries and deterrence" (cited in

¹³⁵ "Egypt's Military: Key Facts," *cnn.com*, February 15, 2011.
<http://www.cnn.com/2011/WORLD/africa/02/14/egypt.military.facts/index.html>

¹³⁶ Khaled, Mahmoud, "Egypt's Conventional Military Thinking", *stratfor.com*, June 12, 2015.
<https://www.stratfor.com/analysis/egypts-conventional-military-thinking>

Khaled 2015) as primary goals of Egypt's military strategy, which was aimed at protecting its territorial integrity and economic interests.

Assessing military effectiveness, Springborg (2013) offers three indicators: military objectives, professionalization and civilian control, and finally 'security sector reform,' referring to compatibility with the rule of law and human rights (100). For the purpose of this study, the third indicator belongs to the section of social control and will be discussed in the next section. With regard to setting a doctrine and professionalization, Springborg (2013) explains in terms of the "roles Egypt assigns to its military, they remain ambiguous, as there is no official national security policy, nor any documents or official proceedings that specify them" (2013, 100). Based on statements from the military, however, defense of the territory and external threats have been the main objectives of the military—defense against the regional states of Israel, Libya, and Sudan, as well as Iran-connected Islamic extremism. Springborg (2013), similar to previous authors, also underlines Egyptian military's "less impressive" capabilities regarding the "sophistication of its procedures, readiness, and its capacity to meet sudden or diverse threats." The problems lie in the military's focus on quantity rather than quality, as well as training (Springborg 2013, 101). Therefore, in terms of evaluating its political goals, its threat environment, and adopting a relevant strategy, Egypt has been consistent. The evidence on its capacity to meet those goals suggests a lack of efficacy.

For example, Dahsham¹³⁷ (2012) contends that the Egyptian military has been “mysterious” about its businesses and military capabilities. Regardless, occasional reports in the Egyptian media alluded to the military’s deteriorating capabilities. Media accounts of sinking vehicles in the Suez Canal, failing tank engines during exercises, and hijacking of army vehicles by an unknown SUV are numerous. There is a low-level readiness among the army personnel in the Sinai. Another piece of evidence indicating low readiness was the killing of 16 personnel due to a militants’ attack of a bordering post; militants also stole a tank from the post. Dahsham (2012) also draws attention to the economic activities of the military as its main priority as opposed to focusing on the task of defense. He criticizes the army for its inability to protect its vehicles from years of “neglect and complacency,” which has created “a situation, in short, in which the army upper echelon is more concerned about what’s happening in the army-owned pasta factory than in basic training”¹³⁸.

There are other reports on the repercussions of economic activity on military professionalism. For example, CNBC reported on a cable by US ambassador, Margaret Scobey, that warns about the military’s opposition to Mubarak’s privatization plans¹³⁹. There are reports of military officers assuming executive positions and spending their time in military-owned properties to foster allegiances within the military¹⁴⁰.

¹³⁷ Dahsham, Mohamed, “The Sad Reality of Egypt's Vaunted Military,” *Foreign Policy Magazine*, November 1, 2012. <http://foreignpolicy.com/2012/11/01/the-sad-reality-of-egypts-vaunted-military/>

¹³⁸ Ibid

¹³⁹ Kirckpatrick, David. D, “Egyptians Say Military Discourages an Open Economy,” *cncb.com*, February 18, 2011. <http://www.cncb.com/id/41659671>

¹⁴⁰ Ibid

Therefore, the evidence suggests that despite weapons' procurement, due to the incompatibility of training with new technology, marginalization of trained officers from decisive positions, and bloated military personnel based on poor conscripts, the EAF's functional capabilities are not impressive. Specifically, the EAF lags in the dimensions of skills and responsiveness. Moreover, the military's focus on maintaining its businesses has turned it into an interest group concerned with maintaining its economic interests, albeit via political means, rather than focusing on the task of defense.

The inability of the EAF to improve its functional capabilities throughout the decades offers the following conclusion with regard to H2. The present study examines the change in functional capabilities prior to and after economic liberalization. However, because the military's functional capabilities, especially in terms of its skills, have not undergone striking improvement, it is safe to assume that neither military aid nor economic liberalization positively impacted the functional capabilities. In other words, if the direct military aid did not substantially improve the military's professionalization in terms of its readiness, one can extrapolate that economic liberalization did not positively impact the military's functional capabilities either. On the contrary, given reports in the Egyptian media, the EAF's involvement with simultaneous tasks of defense and economic production has had a negative impact on its functional capability.

The Social Control of the EAF

Hypothesis number 3 suggests that if economic liberalization is incomplete, economically active militaries become economic interest groups and the outcome is decreased social control. With regard to the case of Egypt, the social control of the EAF

also changed as a consequence of the liberalization and privatization policies. While the EAF's anti Muslim Brotherhood attitude illustrates its support of the former ruling elite, and hence social values of a portion of the population, its state takeover and grave human rights violations demonstrate its commitment to its narrow organizational interests, primarily economic interests.

First, the Egyptian government, concerned with the rise of Islamism among the EAF's conscripts, kept the EAF's involvement with domestic insurgency and Islamic extremism in 1990s to a minimum. In 1992, Chief of Staff Salah Halaby expressed concerns about the rise of extremism and terrorism and urged that the issue be resolved without the EAF's intervention. To ensure the EAF's separation from internal security concerns, Egypt relied primarily on domestic intelligence agencies with limited help from the EAF (Hashim 2011, 110-111). In line with civilian anti-Islamist attitude, the EAF has adopted the secular social values, rather than Islamist values in its decisions. The most striking example of the anti-Muslim Brotherhood, and anti Islamist values, was the EAF's role in ousting Muhammed Morsi in 2013. Claiming to protect the secular portion of the Egyptian society from Islamism, after four days of anti-Morsi protests in July of 2013¹⁴¹, the EAF led by Al-Sisi ousted Morsi from power. Dismissing the results of the election, and hence the social attitudes of those supporting Muslim Brotherhood, the EAF portrayed itself as protectors and champions of secularism and democracy. In doing so, it sided with

¹⁴¹ "Egyptian military removes President Mohamed Morsi-as it happened", *theguardian.com*, July 3, 2013. <https://www.theguardian.com/world/2013/jul/04/egypt-morsi-removed-army-live>

Morsi's opposition leader, Mohammed Al Bradei, the sheikh of Al-Azhar mosque, the Coptic pope, and leaders of Islamic Nour Party¹⁴².

After the EAF's takeover of the government, however, the evidence suggests the EAF's focus on its narrow institutional interests as opposed to its commitment to values of the society. Not only does it not represent Islamist values, the EAF has been undermining both human rights and democracy. The Pew research data¹⁴³ suggests that by 2010, 59% of Muslim Egyptians supported democracy, 22% preferred a non-democratic government only under certain circumstances, and 18% did not have a preferred form of government. Although the EAF toppled Morsi's government in support of protestors in Tahrir square, its actions ever since either have not reflected values of the society or at best reflected a portion of the population. Ever since its dominance, the EAF has dismissed the general attitude of the society pertaining to human rights and democracy. By 2014¹⁴⁴, 72% of Egyptians were unhappy with the country's political direction. Pew also reports that by 2014, 54% of Egyptians supported Sisi over Morsi although the data might be skewed due to misreporting. 54% value democracy and human rights indicating a decrease from 66% in 2013.

There is ample evidence that the EAF violated human rights to maintain both its economic and political power, reflecting the EAF's refusal to incorporate values of human

¹⁴² Ibid

¹⁴³ Auxier, Richard, "Egypt, Democracy, and Islam", *Pew Research Center*, January 31, 2011. <http://www.pewglobal.org/2011/01/31/egypt-democracy-and-islam/>

¹⁴⁴ Wike, Richard. "Key Takeaways from Our Egypt Survey", *Pew Research Center*, May 22, 2014. <http://www.pewresearch.org/fact-tank/2014/05/22/key-takeaways-from-our-survey-of-egypt/>

rights into its practices. According to Human Rights Watch¹⁴⁵, under General Sisi's leadership, there have been numerous cases of torture and disappearance. Furthermore, in North Sinai, the military has been involved in extrajudicial killings during its pursuit of Islamic State. "Prosecutions, travel bans and asset freezing against human rights defenders, in addition to repressive new legislation" are other cases that violate civil and political rights; further violations include anti-union and anti-strike measures.

Conclusion

This chapter illustrated that a haphazard liberalization, rapid privatization, and failure to adopt laws to mitigate shocks of economic reform offered the EAF opportunities for capture of state resources. When the civilian elite decided to limit the EAF's economic power by new privatization policies, the EAF had amassed enough economic leverage to challenge the civilians' decision. Since the state had failed to establish a competitive economy and an independent private sector, the EAF was able to maintain its businesses, and leverage its economic power to gain economic power. Moreover, the EAF turned into an interest group, the outcome of which has been declining functional and social controls.

¹⁴⁵ "Egypt," *Human Rights Watch*, <https://www.hrw.org/middle-east/n-africa/egypt>

Conclusion: Policy Implications and Future Research

Three Cases: Findings

This dissertation illustrated that a state's ability to direct the process of economic liberalization and privatization determines its capacity to manage the influence of its economic interest groups, including its economically-active militaries. Implementation of a state's reform agenda depends, to an extent, on its ability to remain independent of social and economic pressure groups. If the state directs its economic liberalization and privatization process, progressively liberalizes and reforms its regulations and bureaucracy, it has a greater capacity to direct the power of economic interest-groups that would either benefit or lose from the process of reform. Conversely, if state engages in uneven and haphazard economic liberalization, zigzags between various policies without a cohesive strategy, its prospects for mitigating both the shocks to the liberalization and the pressures of socio-economic interest-groups declines substantially. This dissertation adds to this research area by examining the impact of reform processes on those militaries that operate as economic actors.

By comparing the three cases of China, Iran, and Egypt, the central hypothesis tests the empirical evidence for the impact of rapid versus gradual liberalization on militaries'

political, functional, and social powers. Out of the three cases, China was the only case where there was a state-led liberalization strategy coupled with regulatory reform to meet arising changes. China was also the only state that was successful in managing an economically-active military's aspirations, both via regulations and later via a divestiture campaign. The World Bank data on economic performances of three cases shows China's unparalleled success compared to Iran and Egypt, both of which adopted unsystematic and chaotic economic liberalization policies. Compared to Iran and Egypt, Chinese GDP growth increased dramatically from the 1980s to 2010, indicating China's success in fostering economic growth.

Table 11: World Bank, GDP Growth (Current US\$) in China, Iran, and Egypt (1980-2010)

	1980	1990	2000	2010
Iran	165.117 billion	205.514 billion	281.928 billion	467.79 billion
China	349.351 billion	829.562 billion	2.237 trillion	6.101 trillion
Egypt	52.6 billion	89.583 billion	136.381 billion	218.888 billion

In terms of the other economic indicators, China also performs outstandingly better. For example, China's merchandise exports in 2010 amounted \$1.573 trillion, whereas Iran exported \$101.318 billion and Egypt \$26.438 billion worth of goods in the same year.

Table 12: World Bank, Trade (Merchandise Export) in China, Iran, and Egypt (1980-2010)

	1980	1990	2000	2010
Iran	80.910.000	-361.950.000	193.575.000	3.649 billion
China	No-Data (430.000.000 in 1982)	3.487 billion	42.095 billion	243.703 billion
Egypt	548.285.710.069	734.000.000	1.235 billion	6.386 billion

Table 13: World Bank, FDI Net Flows (BOP, Current US\$) in China, Iran, and Egypt (1980-2010)

	1980	1990	2000	2010
Iran	12.338 billion	19.305 billion	28.739 billion	101.318 billion
China	18.099 billion	62.019 billion	249.203 billion	1.578 trillion
Egypt	3.046 billion	3.477 billion	5.278 billion	26.438 billion

In terms of capital inflows and private sector investments also, China is ahead of Iran and Egypt. Net flows of foreign direct investment (FDI) in China increased from \$430,000,000 in 1982 to \$243.703 billion in 2010. In comparison, Iran's FDI was negative in the 1990s and grew to \$3.649 billion in 2010. Egypt, on the other hand, performed better. Its FDI grew from roughly \$548.290 million to \$6.386 billion. While, growth of Egyptian FDI could be attributed to both its political position and Mubarak's renewed commitment to implementation of WB and IMF policy recommendations, Iran performed better both on its share of manufacturing and its private-sector development. The data provided by Iran's

Central Bank¹⁴⁶ suggests that Iran was number two in the region, raking above Pakistan, Egypt, Turkey, and Israel¹⁴⁷ for its GDP share of manufacturing for 2004, and from 2005 to 2007.

Table 14: World Bank, Private Sector (Domestic Credit to Private Sector, % of GDP) in China, Iran, and Egypt (1980-2010)

	1980	1990	2000	2010
Iran	29.691	22.979	26.25	54.615
China	52.627	86.2	51.953*	126.3
Egypt	13.181	25.436	111.123	33.072

Data on domestic sector development also points to China’s superior performance in the area of finance, with that state recording the highest percentage of GDP share of domestic credit to the private sector. Economic indicators in the cases of China, Iran, and Egypt suggest that China was the only case that has been able to register relative progress in its economic performance. Iran and Egypt have both lagged. Therefore, in China, gradual economic liberalization, alongside systemic legal–bureaucratic reforms, culminated in the establishment of relatively competitive economy. Export of goods, capital inflows, and private sector growth are indicators of such success.

Out of all three cases, China differed markedly with an economically-active military that divested majority of its businesses by early 2000 and returned to barracks. The road to containing the military’s economic empire was uneven, with the state passing

¹⁴⁶ “Comparison of the Iranian Economy With the Countries in the Region,” *Islamic Republic Central Bank*, www.cbi.ir/page/6925.aspx

¹⁴⁷ Referred to as “Zionist Occupying Regime” in the document.

regulations and insisting that the PLA's businesses operate based on market laws. In addition, decades of steady economic reform had conditioned the gradual establishment of market mechanisms and a private sector in which profitability was the measure of success. Under conditions of competitiveness, PLA firms could not compete effectively. They engaged in illegal smuggling instead. PLA's agreement to divest was a result of its inability to both sustain its businesses and simultaneously engage in the task of defense effectively.

The same was not true for Iran and Egypt. In both cases, haphazard economic liberalization provided opportunities for militaries to capture state resources. The state's inability to implement effective regulations, along with the rapid sale of SOEs, facilitated the emergence of crony networks. In this context, economically active militaries leveraged their positions to further their economic interests. Once the states decided to limit the militaries' economic power, the military had already amassed substantial economic clout relative to other economic actors, including the private sector. In the absence of laws encouraging market-based competition or discouraging selective protectionism, alongside the absence of an independent private sector, militaries had no incentives to pull out of the economy.

While in both Egypt and Iran, economically active militaries remained both economically and politically active, the degree of civilian control varies. This divergence is explicable by underscoring the role of bonyads and crony networks in Iran's semi-public domain. Formation of bonyads in the aftermath of the 1979 revolution created a semi-public domain characterized by a plurality of competing economic actors. Competition among these bonyads in the semi-public domain to capture Iran's state resources in limited

the IRGC's attempts to take over the state. On the contrary, the EAF's main rival was Mubarak's son, Gamal Mubarak; Gamal's attempts to monopolize economic power antagonized the EAF, pushing it to capture of the state once an opportunity presented itself.

Assessing Alternative Explanations

Since the collapse of the Soviet Union and acceleration of globalization, scholars have been arguing about the pressure globalization asserts on states to liberalize their economies and politics. For example, race-to-the-bottom arguments, and transnational norm diffusion discussion by Bunce and Wolchik (2010) suggest that given market pressures and the diffusion of norms, liberalization of economics and politics is inevitable. Civil–military relations are not exempt from this process. More specifically, arguments on the spread of democracy would suggest that a push for democratization should also democratize civil–military relations.

Hence, an alternative hypothesis would link changes in civil–military relations to the degree of political liberalization states experience. It anticipates that in states with greater degree of liberalization and economic integration, militaries are politically less autonomous, culturally more democratic, and functionally more capable. The empirical evidence from China, Iran, and Egypt disconfirms this hypothesis. Unlike China, Iran and Egypt had episodes of political liberalization. In fact, Presidency of Mohammad Khatami was distinguished for political and social liberalization, rather than economic reforms. However, among the three cases under study, China was the one that succeeded in increasing civilian control over the military.

Therefore, the evidence of increasing political power of the military in Iran and Egypt, especially given both regimes' attempts at political liberalization suggests that the spread of democratic norms or pressure to liberalize might not lead to democratization of civil-military relations. In fact, in autocratic regimes, political liberalization takes the form of broadening the space for political participation of formerly excluded opponents, and the reform of civil and political liberties, rather than a comprehensive institutional reform of civil-military relations. The regime might implement security sector reforms that would introduce institutional mechanisms of monitoring (such as creating internal security bodies to monitor the military's loyalty). The democratization of civil-military relations, however, is contingent upon regime change, not liberalization.

Another alternative hypothesis relevant to the cases of China, Iran, and Egypt is a professionalization argument. Based on Huntington's (1964) view of objective civilian control, professionalization of the military would be the determining variable explaining a change in civil-military relations. In fact, as discussed in the chapter on China, scholars underscore the professionalization of the PLA as an explanatory variable for changes in civil-military relations in China—an increasing degree of civilian control, or a change from a personalistic to an institutional form of control. On the contrary, lack of professionalization in Iran would explain the IRGC's political behavior—its interference in politics. The same would apply to the EAF case in Egypt.

In China, military and civilian leaders were alarmed by illegal smuggling and corruption in PLA businesses. The accounts regarding divestiture suggested both military's top brass officers and civilians' willingness to resolve corruption in PLA. The PLA's

officers' emphasis on PLA's need to focus on defense was interpreted as its professional attitude towards PLA's responsibilities. However, timing of the divestiture, civilians' fear of backlash by PLA, and civilians' compensation package in return for PLA's acceptance of divestiture illustrated that the situation was more complex. PLA had been undergoing modernization and professionalization, but its divestiture was not simply motivated by its values of professionalism. First, divestiture came after years of rectification campaigns aiming to regulate and restructure PLA businesses, not divest them. Secondly, there are contradicting accounts suggesting both PLA officers' inclination to divest versus their resistance to divest. These inconsistent reports indicate existence of tensions within the PLA with regard to divestiture. Ultimately, the civilian leaders had to negotiate a deal with the PLA and offer a compensation package for its economic losses in addition to increasing the defense budget. Therefore, although professionalization is an important factor, it was not the most determinant cause explaining PLA's divestiture.

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Policy Implications

This dissertation offers significant conclusions for policy-makers of international or regional organization, as well as United States’ foreign policy circles. It situates the study of economically active militaries in broader debates on states’ responses to the pressures of globalization. It draws attention to the impact of liberalization and privatization on an often-overlooked economic actor—economically active militaries.

The literature of political economy has already assessed the consequences of economic liberalization policies on domestic economies. The convergence or divergence of economic systems as a consequence of globalization constitutes a central debate in economic liberalization literature. Liberal race-to-the-bottom arguments, as well as Marxist explanations, argue for the convergence of economies into deregulated liberal economic systems. Subsequently, failures of development are associated with either a state’s ineptitude in implementing neoliberal policies, or its inability to tackle the devastating effects of globalization. The opposing camp, as in *Varieties of Capitalism* (Hall and Soskice 2001), and the literature about divergent outcomes of economic liberalization

or globalization (Kohli 2009, Schneider 2010) emphasize the impact of domestic institutional peculiarities and political forces in mitigating the forces of globalization.

In line with neoclassical race-to-the-bottom arguments, in the 1990s international financial institutions offered structural adjustment policies known as the Washington Consensus (WC). These policies aimed at promoting macroeconomic stability, exchange-rate and price liberalization. They also promoted a market-based allocation of finances and labor, private-sector driven growth, trade liberalization and increased exports. They expected these to lead to state retrenchment and price reforms, which would encourage capital inflows, private sector development, and would improve productivity and competitiveness at the international level. The outcomes, however, occasionally did not match the expectations.

For example, in criticizing WC policies, Cammett et al. cited scholars such as Polanyi (2001), Rodrik (2004), Stiglitz (2003, 2004), and Easterly (2011) who underscored the vital role of states in directing reform, as well as the need to adapt the reform strategies (modes of reform) to local conditions. For example, according to both Stiglitz (2003, 2004) and Easterly (2011), the WC's failure to offer "local adjustments" impeded expected growth—"a governance failure to develop checks and balances needed to make markets work, and economic failures particularly associated with the growth-reducing effects of private monopolies and destabilizing effects of capital mobility" (Cammett et. al 2015, 279). Unlike successful state-led reforms in East Asia or China, the authors refer to the WC-led "uncompetitive form of privatization" in the Middle East and North Africa, labeled as "*nomenklatura* privatization" that led the reallocation of public wealth to insider elites

(Cammett et. al 2015, 280). As discussed in this dissertation, economically active militaries' capture of state resources and their gradual increase in economic and political leverage was also an outcome of such rapid liberalization policies.

Following crisis and failures, the “Post-Washington Consensus” emerged in the aftermath of the 2008 economic crisis. It addressed the necessity of institutional reforms and a focus on political reform and governance, over mere economic liberalization; instead of perceiving the “state as the problem”, the post-WC advocated the need for strong states with regulatory capacity and the ability to provide public goods (Commatt et al. 2015, 281). Extending this view to the reform of civil–military relations, this dissertation’s findings advise a more careful examination of the implications of liberalization not only on states’ development, but also on the balance of civil–military relations in countries with economically active militaries. Encouraging the states to reform their institutions should also incorporate recommendations for regulating military businesses.

By examining changing power (political, functional, or social) of economically active militaries, this dissertation’s findings offer two areas of considerations for policy-makers: (i) economic reform packages should incorporate the possible impact of policy recommendations on militaries with a history of engagement in the economic domain. (ii) The international organization or Western policy-makers should consider the security implications of militaries’ economic power. Policy-makers who offer recommendations for security sector reform and economic reform in developing states should collaborate.

For example, donor states and organization after the Cold War required states to reduce military spending to receive money. The IMF and the WB spearheaded this change

for two reasons: their mandate prevented them from interfering in domestic politics. By reframing military spending as a fiscal issue, they could influence beneficiaries' decisions. The IMF and the WB also adhered to the neoclassical economic model that prioritized capital investments in productive sectors to boost growth and considered military spending as "pure waste." Since the late 1990s, the specific issue of military spending has become a part of a broader framework of security sector governance (Brozka 2003, 6-9). This dissertation's findings suggest that the interrelation of military spending and civilian control is not straightforward. The case of China illustrated how the state's ability to increase its defense spending and compensate the PLA served as a catalyst for both the PLA's return to barracks and increased civilian control. Therefore, policy-makers should pay closer attention to the domestic dynamics of state–military relations to be able to offer nuanced, or at times even counterintuitive, policy recommendations that would assist the states in their both economic and security sector reforms.

Future Research

This research puts forth a framework to assess the nexus of economic policies and civil–military relations in those autocratic regimes where militaries have had a history of economic activity. The evidence tells a causal story that links the impact of the specifics of liberalization and privatization policies to militaries' economic expansion and contraction. The future research could take six directions likely to improve our understanding of the interrelation of economic policy and civil–military relations:

First, research should focus on collecting more detailed evidence on the specifics of micro-economic policies and their impact on militaries' economic behavior in a smaller

time-frame. This dissertation examines specific policies to illustrate the overall economic success and failure of states to establish market economy, and its subsequent impact on militaries' power. A more careful and comprehensive elaboration of micro-economic policies was outside of this dissertation's scope. In order to postulate a more complete causal picture, future research should divide the study into both shorter time periods and look at more specific policy choices.

For example, there is a consensus among scholars that the pace of privatization in Iran and Egypt was relatively fast compare to that of China. The rapid privatization also led to asset-stripping of state resources. This dissertation draws on the above-mentioned arguments on the pace of privatization to explain militaries' opportunistic behavior as economic actors, specifically in Iran and Egypt. However, it would be valuable to conduct a microstudy of types of privatization arrangements, such as asset divestiture, outsourcing, or infrastructure partnership¹⁴⁸, along the span of shorter time-frames, such as during a specific administration; it would help to identify micro-causal relationships between a detailed policy and a military's behavior in a short span of time.

A second area requiring further research is variation militaries' business activities in different sectors. For example, military business productivity in the oil and gas sector as opposed to manufacturing. Was there a variation across time in a certain sector? Or were there variations across various military-owned companies in the same sector? The goal

¹⁴⁸ Poole J., Robert. "Privatization", *Library Economics Liberty*. n/d.
<http://www.econlib.org/library/Enc/Privatization.html>

would be to gather new evidence that would assist with testing the hypotheses set forth by this dissertation.

In this same area, investigators need to improve the quality of data on the economic activities these militaries operating in a non-transparent autocratic regime is sparse or likely to be inaccurate. Available data is anecdotal or speculative. Accurate evidence on profitability or losses of military businesses is lacking. While there are general reports about their overall performance, the data is scant. Access to data, especially on militaries' budget and business profits are the biggest challenge of such study. Therefore, the second direction should include collecting more specific data on militaries' business activities. As countries liberalize and begin opening their markets for investments, such data should become more available. Conducting interviews with officials, dissenting politicians or former military elites, would be another avenue to pursue.

The third avenue for future research would be analysis of the fate of military businesses under current leaderships. For example, what happened to those PLA companies that had engaged in international trade? Or what has been happening to IRGC companies following the lifting of sanctions against Iran and Iran's gradual opening to global markets? Assessing the negotiation process between the IRGC and the civilian elite in both the economic and the political spheres would be a logical continuation of examining the ability of this dissertation's hypotheses to predict future behaviors.

The fourth potential for research lies in assessing the relationship between militaries' economic activities and both the provision of social services and regime durability. In other words, do militaries engage in contracting, job-creation, or provision of

services, especially in underdeveloped or rural regions? If yes, understanding the possibilities of those activities for establishing loyalty and subsequent regime stability, would be an important issue to study. Do militaries foster social constellations that they are able to leverage during a crisis?

While China was relatively successful in demanding that the PLA divest, Iran and Egypt have not been able to push their militaries back to barracks. A fifth direction for research should examine whether there is a variation in the future course of economic liberalization in Iran and Egypt. If yes, how do the militaries of each country influence the process? In other words, given the enormous economic leverage the IRGC and the EAF have amassed, understanding the possible conflict of interests for the militaries, or their possible role in encouraging or discouraging economic as well as political reforms is crucial.

Ultimately, this research offered a comparative case study to offer contingent generalizations about the political behavior of militaries, as well as their functional power and social attitudes following economic reforms. The hypotheses should be tested against evidence from other cases with economically active militaries to examine their validity. For example, Turkey has had a similar trajectory regarding its economically active military and economic liberalization. However, the attempted coup d'état in the summer of 2016 has ended up with consolidation of power amounting almost to monopolization by President Erdogan. How would findings from this dissertation help us further our understanding of the interrelation of economic policies and civil–military relation.

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