LEBANON

Highlights

- **Lebanon has remained in a protracted period of low growth since 2011.** Since the start of the Syrian conflict, growth averaged 1.7 per cent, compared with 5.6 per cent in the decade before. The fiscal and external positions are deteriorating further.
- **The Capital Investment Programme (CIP) was adopted by the Cabinet and presented at the Paris IV conference.** The total cost of the phases of the programme until 2025 is estimated at US$ 17.3 billion and over one-third of the first phase has the potential to be fulfilled by the private sector.
- **Reforms progressed in 2017 in some areas, but lag behind in others.** Completed reforms in 2017 and early 2018 included passing the public-private partnership (PPP) law, new decrees regulating oil and gas exploration, new licences for a consortium of three international oil companies to start exploratory drilling, and adoption of a new electoral law.

Key priorities for 2019

- **A sustained and balanced fiscal adjustment is essential.** Without further adjustment, Lebanon's public debt burden, already among the highest in the world (relative to size of the economy) will continue to rise, adding to existing vulnerabilities and ultimately crowding out essential public spending.
- **Lebanon's infrastructure deficit needs to be addressed.** The current situation is the result of protracted under-investment and is exacerbated by the refugee presence. Slow internet speeds are a major burden for firm operations and growth, and strengthening infrastructure would help the development of the knowledge economy.
- **There is a critical need for electricity reform.** The electricity sector has been identified as the most pressing bottleneck for doing business and for competitiveness. Reforming this sector has been long-delayed, resulting in large fiscal costs.

Main macroeconomic indicators %

	2014	2015	2016	2017	2018 proj.
GDP growth	2.0	0.2	1.7	1.5	1.1
Inflation (average)	1.1	-3.8	-0.8	4.5	6.5
Government balance/GDP	-6.3	-7.9	-9.6	-6.0	-9.7
Current account balance/GDP	-23.9	-16.7	-20.5	-22.8	-25.6
Net FDI/GDP [neg. sign = inflows]	-3.4	-1.8	0.0	-4.3	-4.0
External debt/GDP	167.5	168.4	182.6	182.4	183.3
Gross reserves/GDP	76.9	73.6	78.1	75.0	63.3
Credit to private sector/GDP	143.8	147.4	147.1	n.a.	n.a.

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Macroeconomic performance

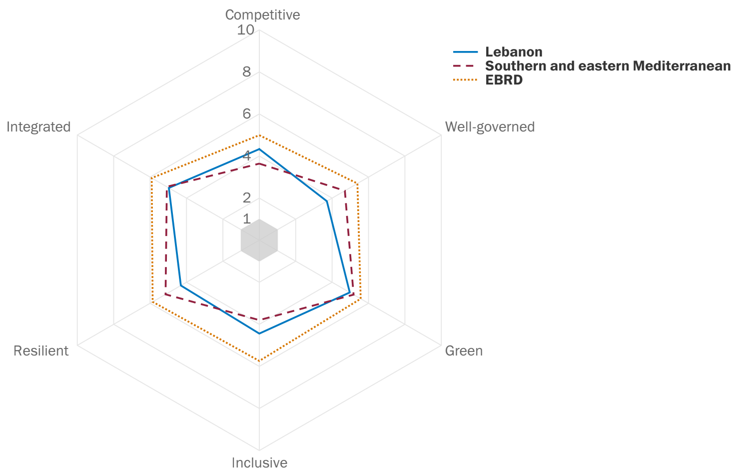
The economy remains in a protracted period of low growth. GDP growth averaged 1.7 per cent in 2011-17, compared with 5.6 per cent in the decade before, due to declining investment and exports and subdued private consumption and tourism. This is a result of political and security conditions, both domestic and regional, which affected traditional growth drivers – tourism, real estate and construction. The economy grew by 1.5 per cent in 2017, driven mainly by private consumption – sustained by remittances from the Lebanese diaspora – and exports. In per capita terms, GDP has been increasing at a mere 0.2 per cent per year on average since 2010, compared with 8.4 per cent in the six years before the Syrian crisis.

The fiscal situation is increasingly challenging. The fiscal deficit remained large in 2017, as subsidies to the electricity company – Electricité du Liban (EdL) – increased due to rising oil prices, and interest payments continued to increase, accounting for half of revenues and crowding out more productive forms of spending. At the same time, one-off revenues from taxing higher bank profits prevented the deficit from widening further. Meanwhile, public debt, the third highest in the world (relative to GDP), is now close to 150 per cent of GDP.

The external situation has worsened. The current account deficit widened to over 20 per cent of GDP in 2017 owing to the impact of regional conflict on key trading partners and routes, and the economy remains largely dependent on remittances (which account for 13.4 per cent of GDP) and deposits from non-residents (14.6 per cent of GDP). Reserves remain comfortable at over US$ 43 billion, covering around 14 months of imports and providing stability to the economy.

Growth is expected to rebound but remain subdued. GDP is forecast to grow at 1.1 per cent in 2018 and a range of 1.5 to 1.9 per cent in 2019 depending on the recovery in the construction and financial sectors, and the extent of reconstruction in Syria. Meanwhile, sizeable vulnerabilities and risks remain, including from internal political uncertainty, regional turmoil and increased spending pressures.

Assessment of transition qualities (1-10)



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Major structural reform developments

A new budget has been passed, the first for many years. The resolution of the political deadlock paved the way for the passage of the first budget since 2005, as well as the country's first parliamentary elections in nine years. In March 2017, Cabinet approved a draft 2017 budget, and in October 2017 it passed through parliament. In March 2018, parliament approved the 2018 budget, a few days before the CEDRE donor conference in Paris. The 2018 budget included a commitment to reduce current spending by 20 per cent, although this commitment did not materialise when executing the budget. Also, the Cabinet adopted a new electoral law based on proportional representation, which governed the recent parliamentary elections in May 2018.

The Capital Investment Programme (CIP) was approved by the Cabinet in March 2018. The total cost of the government's ambitious plan during the first two phases of the programme (2018-21 and 2022-25) is estimated at US$ 17.3 billion. The first phase is estimated at US$ 10.8 billion (including expropriation costs), of which around 38 per cent has the potential to be financed fully from private investment in cycle 1. The programme is expected to be an effective tool to help reinforce Lebanon's depleted infrastructure, thereby supporting a boost in economic growth.

The Public-Private Partnership (PPP) law has been ratified. The law, adopted in August 2017, introduced a new legal regime for PPP projects in Lebanon, to improve transparency, competitiveness and accountability standards. The PPP law grants the renamed High Council for Privatization and Partnerships (HCPP) the power to assess and evaluate potential PPP projects. Nevertheless, the PPP law includes certain gaps that remain to be bridged. For example, there are no clear criteria on what projects should be implemented as PPPs instead of traditional public procurement, the role of the Ministry of Finance is limited, the institutional set-up for PPPs appears complicated and geared toward the promotion of PPPs, without appropriate risk management, and the dispute resolution mechanism is insufficient.

The government has already begun to address some of the key factors that have caused delays in project start-up. All loans approved by lenders as of the end of 2017 have been signed or approved for signing by the Cabinet, and parliament ratified about US$ 400 million of loans over the past year. With regards to counterpart funds for projects for which foreign loans have already been provided, the government decided, in consultation with the central bank, to issue bonds worth US$ 700 million for the financing of land acquisition and other counterpart funds required, although this has not materialised to date.

Parliament approved a set of regulations to jump-start the oil and gas sector. The petroleum-income tax law—a necessity to complete the Lebanese petroleum fiscal regime—was enacted in October 2017, two years after it was first drafted. Four other important laws in this sector are currently at the initial stages of the parliamentary process. They cover the establishment of a petroleum asset-management department, a sovereign wealth fund and a national oil company, as well as prospects for onshore exploration. In addition, last year's Right of Access to Information Law, the Petroleum Transparency Law—which is reaching the final stages in parliament committees – and the plan to join the Extractive Industries Transparency Initiative should all contribute to greater transparency in the sector.

Concrete measures have been taken to solve the solid waste crisis. The Cabinet decided in January 2018 on measures to resolve the crisis including: the expansion of landfill facilities, the construction of a composting plant and upgrading of sorting plans, and the construction of waste to energy plants. At the same time, responsibility for solid waste management will be decentralised to municipalities. A Framework Law setting forth the mechanism for developing solid waste strategies and plans is currently under final consideration by parliament.

The public consultation process is being enhanced amid concerns about wage policy. A Socio-Economic Council has been reinstated in January 2018 after it was first formed in 2000. The Council serves as a consultative body on economic and social policy and is tasked with creating an efficient space for dialogue between the main actors of the public and private sector and contributes to the public governance in Lebanon. The Cabinet also passed the public sector's salary scale bill, which had been held up for years, although its uneven implementation has sparked ongoing protests, in addition to having a large fiscal cost, with insufficient revenue measures to finance it, and causing the ballooning of pension payments.