Lebanon

Highlights

- **The escalating war in Lebanon leaves the recovery outlook increasingly uncertain.** Living conditions have deteriorated further due to the political impasse and the dire national and geopolitical situation, although the currency has stabilised somewhat as the central bank's efforts to unify multiple exchange rates and rein in inflation have paid off.
- **Access to basic goods and services is precarious.** Lower global prices and a short-lived recovery in tourism and remittances have helped to ease pressure on the external accounts, but the current account deficit is still large and the country remains unable to attract international investment and donor support in the absence of progress on reforms.
- **Political paralysis is holding back reform.** Some limited progress on the fiscal and monetary fronts has been achieved, but far below what is required to support an economic recovery. Key reforms are at a standstill, including banking-sector restructuring and other regulatory reform prerequisites to an International Monetary Fund (IMF) programme.

Key priorities for 2025[1]

- **Completing the reforms required for an IMF-supported stabilisation and structural reform programme is the key priority.** An agreement with the IMF would help restore credibility with regard to reform commitment and provide access to necessary external financing. Progress on electing a president and forming a government with full executive powers is urgently needed, in addition to bank restructuring and critical institutional and governance reforms.
- **Significant improvements in government revenue mobilisation are critical to restoring access to essential services.** Establishing comprehensive social safety nets remains crucial in order to alleviate the economic pain the population is facing. Given its severe financing constraints, the government needs to attract donor assistance and gradually build robust support networks. It will also need significant investment to rebuild its capacity to provide public services.
- **Progress on energy-sector reforms is necessary to unlock the financing needed to develop capacity and restore a consistent power supply.** In parallel, capitalising on recent legislative reforms to promote renewable energy uptake is critical to providing a sustainable energy supply and helping to address severe shortages and high import dependence.

Main macroeconomic indicators (per cent)

	2020	2021	2022	2023	2024 proj.
GDP growth	-25.9	-10.0	0.0	-0.2	-1.0
Inflation (average)	84.9	154.8	171.2	221.3	na
Government balance/GDP	-3.5	0.6	-6.1	na	na
Current account balance/GDP	-16.1	-17.5	-36.1	-34.0	na
Net FDI/GDP [neg. sign = inflows]	-6.4	-9.6	-0.8	na	na
External debt/GDP	362.3	414.5	378.3	na	na
Gross reserves/GDP	72.1	66.5	48.8	na	na
Credit to private sector/GDP	54.3	na	na	na	na

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[1] The war continues to escalate as this report is being finalised, and different priorities will emerge if the war persists into 2025.

Macroeconomic developments and policy response

Political deadlock and ongoing conflict continue to hold back Lebanon's economic recovery and the population's living conditions are dire. The economy failed to grow in 2023, as armed confrontation in the southern part of the country weighed considerably on the economy. Meanwhile, the country's unyielding political deadlock and lack of progress on critical reforms have continued to hold back recovery. Real gross domestic product (GDP) is estimated to have contracted slightly, by 0.2 per cent, in 2023, adding to a cumulative loss of real GDP of more than 40 per cent since 2018. The country remains locked out of international markets as uncertainty continues to surround the long-awaited IMF programme. Lebanon's foreign-exchange reserves decreased slightly to US$ 14.5 billion (€13.1 billion, excluding gold) in 2023, despite benefiting from remittances and tourism flows in the first nine months of the year – until the war in Gaza broke out. Dire economic conditions and years of hyperinflation have caused large segments of the population to suffer severe hardship, with over a third of the labour force unemployed and more than 80 per cent of the population estimated to be living in poverty.

Efforts to unify the multiple exchange rates in the economy have helped to rein in inflation, but fiscal conditions and the public debt situation remain precarious. The Banque du Liban (BDL) introduced several measures to unify the economy's multiple exchange rates, including phasing out the Sayrafa platform. This step, in tandem with the adoption of the 2024 budget law, has helped to bring the official exchange rate closer to the prevailing market rate. This follows several years of exchange-rate fluctuations that eroded confidence in the local currency and increased dollarisation in the economy. Against this backdrop, the market rate has stabilised at around LBP 89,700 per US dollar since the end of August 2023 and inflation has dropped significantly as a result, falling to 32.9 per cent in September 2024 (from a peak of 269 per cent in April 2023). Meanwhile, the surge in the cash economy and informal sector as a result of the country's economic deterioration has further deprived the state of much-needed fiscal revenues. In contrast, significant reductions in spending have likely helped to reduce the budget deficit. The falling real salaries of public-sector employees have resulted in high numbers of resignations and increased absenteeism, further undermining Lebanon's already weakened public administration capacity. Public debt was estimated at around 195 per cent of GDP at the end of 2023.

The current account deficit has probably narrowed thanks to lower commodity prices and rising inflows, but food and energy security remains precarious. The deficit, estimated to have exceeded 23.5 per cent of GDP in 2023, is likely to have declined in 2024, helped by increasing tourism receipts and rising remittances from Lebanese nationals abroad, as well as lower global inflation. However, the country is still unable to meet the population's needs in terms of fuel, electricity and grain. A World Bank loan of US$ 150 million (€135.9 million) helped Lebanon secure most of its wheat needs and to maintain some bread price stability in 2023. Meanwhile, access to electricity in most areas remains limited to two hours a day, increasing households' dependence on private generators.

The outlook remains highly uncertain and increasingly weighed down by geopolitics. Any recovery will depend on a ceasefire agreement, as well as the speed of government formation, agreement on an IMF deal and swift reconstruction efforts. Before the recent escalation of conflict, the economy was forecast to see a further contraction of 1.0 per cent in 2024, with a return to growth of 2.0 per cent in 2025, conditional on cessation of the war and implementation of an IMF-supported programme by a reform-minded government that would also allow negotiations to resume with international partners. As of early November, the war in Lebanon continues to intensify and our earlier forecasts (above) are therefore subject to significant downside risks.

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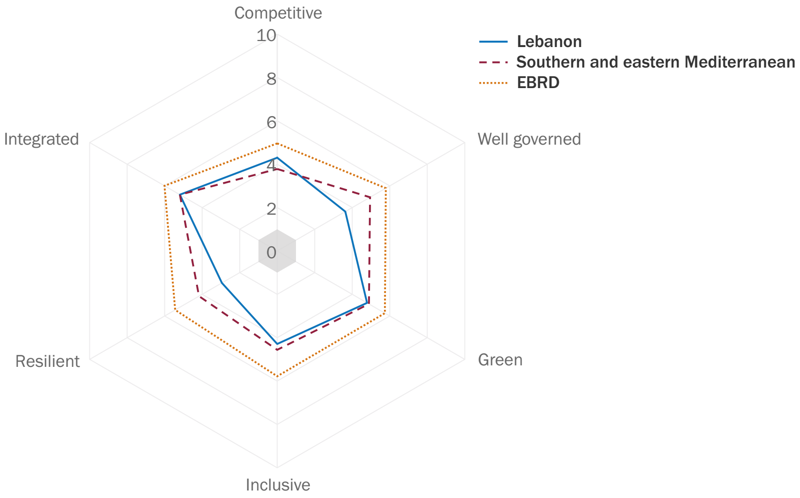
Assessment of transition qualities (1-10)



Structural reform developments

Lebanon has yet to make progress on an IMF programme. Discussions with the IMF are largely dormant, with no progress made to date on forming a new government or electing a new president. During its May 2024 staff visit, the IMF noted the country's progress on bringing down inflation and unifying its multiple exchange rates, but previously identified gaps remain unresolved. These include reaching an agreement on banking-system restructuring, as well as meeting several programme prerequisites, including draft laws on banking secrecy, banking resolution and capital controls.

There has been some progress on fiscal reform. Lebanon was able to pass its 2024 budget law in a timely manner and the Ministry of Finance has introduced a number of measures to improve revenue mobilisation, including an exchange-rate adjustment to the customs dollar, which has helped to close the fiscal gap. However, shoring up revenues to the levels needed to support recovery is still a remote prospect, as severe funding and human capacity gaps prevent effective tax collection. Consequently, public spending cannot ensure the adequate provision of key services, let alone the levels of social spending and capital investment needed to support an economic recovery. The ongoing war is likely to exacerbate the fiscal pain, as disrupted economic activity suppresses key sources of income, including customs and VAT, while raising pressure to increase spending to meet urgent humanitarian needs and demand for public services.

Some steps have been taken towards monetary policy independence, but essential transformative reforms remain to be done. In addition to phasing out the Sayrafa platform and efforts to unify the country's multiple exchange rates, the BDL has taken measures to end the monetary financing of the fiscal deficit. However, progress has yet to be made on strengthening BDL governance and internal controls, as well as improving transparency and accountability.

Consensus on the proposed economic recovery plan and subsequent bank restructuring is still out of reach. The plan, approved by the cabinet in May 2022, introduces sweeping banking-sector restructuring, including for the BDL. Banking-sector losses are estimated at around US$ 70 billion (€66 billion) and reforms are likely to result in large haircuts on deposits over US$ 100,000 (around €94,000). The plan is still facing pushback, as different parties continue to dispute the distribution of losses.

Reforming the electricity sector remains a top priority. Plans to address the electricity sector's numerous vulnerabilities continue to encounter political hurdles, even though the need to progress has become more urgent amid ever-more-frequent power supply interruptions. Large segments of the population are increasingly dependent on private generators to counter power cuts that last most of the day. Since its approval by the cabinet in early 2022, the electricity reform plan remains stuck in parliament, blocking international support and energy imports from neighbouring countries. The plan involves setting up an electricity regulator, carrying out a comprehensive audit of the state power company, Electricité du Liban (EDL), and adjusting tariffs. Still, some progress has been made independently of this plan, with the first tariff reform in 30 years becoming effective in early 2023. In addition, EDL disclosed its audited financial statements for the first time since 2011 (reflecting 2020 performance and published in August 2024), and developed a cost recovery plan approved by the prime minister. Furthermore, a new regulatory framework for decentralised renewable energy generation is a welcome development. In late 2023, parliament passed a distributed renewable energy law that introduces net metering and peer-to-peer renewable energy trading. ●

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