



May 19th, 2017

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The World Bank recently released their Lebanon Economic Monitor – Spring 2017 Issue. Below are the key views and suggestions the World Bank holds in regards to the Lebanese economy.

Economic Backdrop

The election of a President and the formation of a government marked the end of around two and a half years of political stalemate in Lebanon. This progress was the first bright spot in a bleak political scene that has impeded decision making and much-needed reforms. The election of a President in October 2016 is still generating positive effects on overall sentiment as we move across the year 2017.

According to the World Bank, Lebanon's Real GDP growth increased in 2016. The World Bank estimates that recoveries in real estate and tourism boosted real GDP growth from 1.3% in 2015 to 1.8% in 2016¹. Cement deliveries recovered from a low base rising by 4.4% in 2016 compared to an 8.6% decline in 2015. Tourist arrivals also increased by 11.2% in 2016 to reach 1.69 million. The World Bank notes that if Lebanon does not fall back into a political deadlock, improvements in tourism, real estate and construction could lead to a projected real GDP growth of 2.5% in 2017.

However, the geopolitical scene continues to pose a sizable impediment for Lebanon to reach its growth potential. The spillovers of the Syrian crisis are numerous and far-reaching; trade routes have been disrupted, the divide between Lebanese political factions has widened and security has been threatened. Moreover, the World Bank notes that for the fifth year, Lebanon remains the largest host of displaced Syrians (on a per capita basis) and that in itself weakens the already precarious infrastructure and social safety net.

The World Bank acknowledges the different aspects of the Syrian presence in Lebanon. On the one hand, the World Bank states that the increase in population reflects positively on the sector of Information and Communications Technology (ICT). In fact, the "percentage of individual using the internet rose from 52% in 2011 to 74% in 2015 while fixed broadband connections more than trebled to reach around 1.3 million persons with mobile cellular telephone subscriptions expanding by 35% over the same period." On the other hand, the World Bank also recognizes the strain this presence can have on public finances and on public services.

Overall, we believe that the net impact of the Syrian presence in Lebanon is largely negative. Any consumption boost that might have ensued from the Syrian presence in Lebanon is largely outweighed by the costs incurred in terms of education, infrastructure, utilities, health, and public finance. The Syrian presence also has some unquantified costs in terms of threats to social cohesion, widening inequalities, poverty and crime.

¹ The World Bank is slightly more optimistic than the IMF which estimates 2016's real GDP growth at 1.00%.

The World Bank also notes that international aid targeting Syrian refugees partially compensated for the overall loss of inflows since 2010. Also in this regard, we believe that inflows of international aid, estimated at over \$1 billion over the period 2012-2014 by the UNDP, are frail in comparison with the levels of Foreign Direct Investments and remittances which combined amount to around \$11 billion/year in periods of strong economic growth and around \$8 billion/year in slower periods.

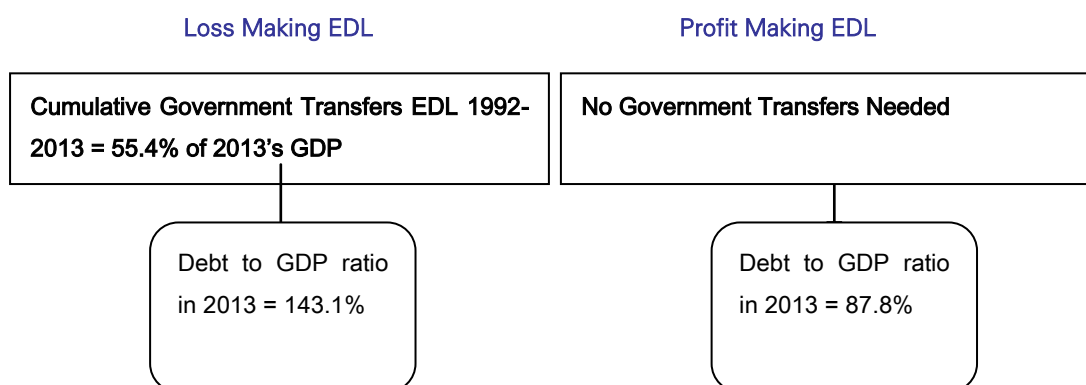
Lebanon's fiscal and debt positioning worsened in 2016. According to the World Bank, the fiscal deficit increased by 1.8 percentage points (pp) to 10% of GDP, reaching double digits for the first time since 2006. The larger fiscal deficit pushed the debt to GDP ratio to an estimated 157.5% in 2016 up by 8.1 pp from 2015².

Lebanon's current account deficit and falling capital inflows compelled the Central Bank to undertake a swap operation with Lebanese banks. The current account deficit widened from 17% of GDP in 2015 to an estimated 21% of GDP in 2016 on the back of higher imports and lower remittances. The Central Bank of Lebanon managed to boost its gross foreign reserves by 11.1% in 2016 to \$34 billion after falling by 5.4% in 2015. However, the World Bank notes that "notwithstanding the short-term needs, given the current fundamentals and lack of structural reforms, such interventions can exacerbate macro financial risks."

In 2017, two of the long-overdue items on the public agenda were partially addressed. In January 2017, the Council of Ministers approved two oil decrees which are necessary for Lebanon to proceed with the first licensing round of offshore gas exploration. In March 2017, the government adopted the 2017 budget and it is now waiting to be ratified by Parliament. The last budget Lebanon has seen was back in 2005. The World Bank notes that it remains unclear whether previous disagreements over past fiscal accounts will re-emerge between political factions. Also, the outcome of the \$800 million salary-scale adjustment for public sector employees which is set to be financed by a proposed package of tax hikes and fees remains uncertain.

The World Bank's Short-Term Priorities for Lebanon

According to the World Bank, the top short-term priority for Lebanon is the ratification of the 2017 budget by Parliament. The urgency of this priority lies in the fact that the fiscal deficit is growing and the country's indebtedness to finance this deficit is on an unsustainable path. The World Bank notes that the pass-through effect of higher global interest rates and oil prices will increase debt servicing costs and transfers to the state-owned Electricité du Liban (EDL).



The second priority according to the World Bank is the ratification of the Public Procurement Law of 2013. According to the World Bank, the procurement law of 1963, the "legal foundation of Lebanon's current institutional framework for procurement, is excessively centralized, resulting in procurement and execution delays." The recent revisions to this law introduced in 2013 have not yet been ratified. In Lebanon, the World Bank notes, "weak public procurement procedures have resulted in elite capture and prevented effective competition between bidders over a certain class of projects tendered out by the state."

² The IMF puts Lebanon's debt to GDP ratio at 144% in 2016

The third priority is enacting fiscal reforms, especially with regards to the burdensome transfers to EDL. The World Bank advises the Council of Ministers to pass a decree that states that any increase in the supply of power must be matched by an increase in average EDL tariffs and not by transfers to EDL. The World Bank confirms that the cost of EDL-supplied electricity would still remain far lower than the cost of electricity supplied by private generators.

The fourth priority is the updating of the existing draft Public Private Partnership (PPP) law.

The private sector can aid the public sector in delivering basic services more efficiently and in improving the state of infrastructure. With the government's lack of fiscal space and limited capacity, the Lebanese private sector can play a crucial role. Although PPP projects are undertaken in Lebanon they are undertaken to serve an immediate purpose and generate mixed outcomes. What Lebanon needs is a more coordinated PPP approach with regards to the *"selection, preparation, negotiation, implementation and fiscal management of private participation in delivering public and infrastructure services."*

The World Bank suggests Liquefied Natural Gas (LNG) as a more cost-efficient source of power generation and proposes steps towards higher power generation. LNG imports are less expensive and more environmentally-friendly than the liquid fuels Lebanon currently uses for power generation. Moreover, the 2,019 MW of energy produced by EDL fall short from the country's needs of 3,195 MW; this is why the World Bank advises the Council of Ministers to *"resolve and provide the necessary public financing to complete ongoing generation projects and to hire a transaction advisor to initiate implementation of a program to develop new generation capacity by independent power projects (IPPs)."*

-  Electricity from private generators costs three times more than EDL supplied electricity
-  The EDL tariffs have been unchanged since 1996, when the oil price stood at \$23/barrel
-  Only around half of electricity costs are recoverable
-  Lebanon has the second worst quality of electricity supply in the world according to the 2014-2015 World Economic Forum's Global Competitiveness Index
-  Electricity outages reach 12-13 hours/day in poor regions while richer areas like Beirut suffer only 3 hours of blackout/day

The World Bank's seventh short-term priority is the establishment of public transport. The World Bank argues that the Council of Ministers should allow and mandate the Council of Development and Reconstruction (CDR) to handle (execution, preparation and negotiation) the Greater Beirut Urban Transport Project. The project, which will involve the private sector, would consist of a "Bus Rapid Transit Network within Beirut and one between Beirut and Tabarja with extension of services to Byblos and Tripoli."

-  There are about 1.2 million vehicles for only 4.5 million people in Lebanon
-  Road transport accounts for 25% of all energy consumption in Lebanon
-  Lebanon's traffic congestion is estimated to cost the economy an estimated 8% of GDP per year according to the World Bank

Lebanon should strengthen its social safety nets according to the World Bank. According to the World Bank, the *"government spending on non-subsidy social safety nets does not exceed 1% of GDP"*. That is why the Council of Ministers should enhance the National Poverty Targeting Program (NPTP) launched in October 2011 by expanding the electronic card food voucher and increase the number of households targeted by the program from current 10,000 extreme poor households to 15,000 – 20,000 households. The NPTP's database of 110,000 households needs to be re-certified by the Ministry of Social Affairs and the Council of Ministers.

According to the Central Administration's Household Budget survey 2011-2012, 27% of the Lebanese were poor (prior to the influx of Syrian refugees) = this poverty rate implies that around one million people were living on less than \$8.5 per day.

With the garbage crisis that plagued the country, it comes as no surprise to see the solid waste treatment on the World Bank's list of priorities. Decree 8003 on Integrated Municipal Solid Waste Management was approved by the Council of Ministers in April 2012 and has been awaiting parliamentary approval since. According to the World Bank, this decree *"promotes an integrated and proper management of municipal waste by encouraging waste minimization, source separation, recycling, energy recovery, effective treatment facilities, etc."*

Finally, Lebanon should improve its business environment. Lebanon ranks low on the Doing Business Index standing as the 126th economy out of 190 economies. According to the World Bank, Lebanon's weak performance is especially in the areas of institutions, infrastructure, macroeconomic environment and labor market efficiency. The World Bank recommends changes to the commercial registry and licensing procedures, particularly in the tourism sector, and the passage of the e-signature law which will enable the dematerialization of the regulatory processes.

In sum, all the proposed measures boil down to one thing: restoring confidence in Lebanon's ability to address its vulnerabilities. However, the type of confidence that translates into economic prosperity is not the fleeting type but the type that is renewed at every stage of the reform process. The election of a President and the formation of a government signal positive **intentions** towards reform. However, it's only the **implementation** of reform that can create jobs, reduce inefficiencies, boost productivity and transparency and eventually generate higher economic growth.

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