

**THE WORLD BANK GROUP ARCHIVES**

**PUBLIC DISCLOSURE AUTHORIZED**

**Folder Title:** Subject Files: Country Files - Lebanon - Correspondence 01

**Folder ID:** 1328843

**Dates:** 12/04/1991 – 09/17/1993

**Fonds:** Records of the Office of the President

**ISAD Reference Code:** WB IBRD/IDA EXC

**Digitized:** 04/10/2017

To cite materials from this archival folder, please follow the following format:  
[Descriptive name of item], [Folder Title], Folder ID [Folder ID], ISAD(G) Reference Code [Reference Code], [Each Level Label as applicable], World Bank Group Archives, Washington, D.C., United States.

The records in this folder were created or received by The World Bank in the course of its business.

The records that were created by the staff of The World Bank are subject to the Bank's copyright.

Please refer to <http://www.worldbank.org/terms-of-use-earchives> for full copyright terms of use and disclaimers.



THE WORLD BANK

Washington, D.C.

© International Bank for Reconstruction and Development / International Development Association or

The World Bank

1818 H Street NW

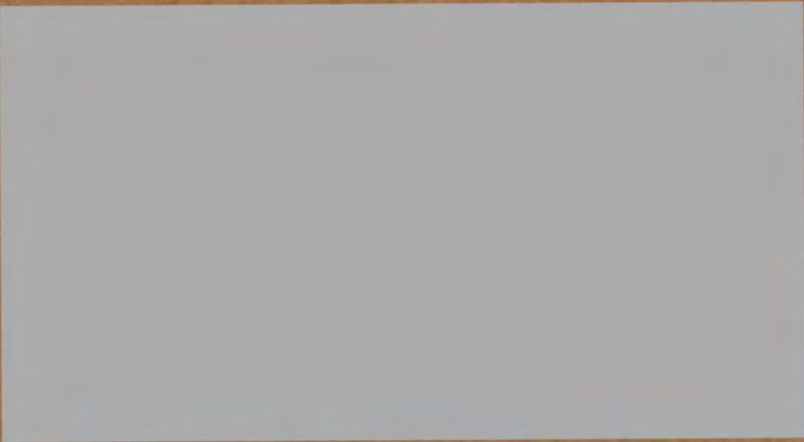
Washington DC 20433


Telephone: 202-473-1000

Internet: [www.worldbank.org](http://www.worldbank.org)

**PUBLIC DISCLOSURE AUTHORIZED**

Lebanon 1992-93  
Office of the President



 **Archives**  
1328843  
R1995-215 Other #: 5 209735B  
Subject Files: Country Files - Lebanon - Correspondence 01

**DECLASSIFIED  
WITH RESTRICTIONS  
WBG Archives**

1993 ANNUAL MEETINGS BRIEFName of Country: Republic of Lebanon      Date: September 17, 1993Meeting with: H. E. Fuad Siniora, Minister of State for Financial AffairsPopulation: 3.8 million (1992)      Estimated GDP Growth Rate: 10% (1993)  
GDP per capita: US\$ 1492 (1992)

	(\$million)		(\$million)
Total Commitments to date:	268.7	IBRD	FY93 Commitments: 175.0
Total Undisbursed:	175.0		Disbursements: 0.0
Lending Program: FY94-96	200.0		Amortization: 3.5

<u>Summary Data</u>	Est.	Proj.	
	1992	1993	
GDP Growth (%)	10	10	Aid Group Meeting: CG planned for December 1993
Export Growth (%)	23	24	
Import Growth (%)	12	10	IMF Status as of September 1993: Art. IV. (Discussions in May 1993)
Current Acc. Deficit/GDP (%)	40	36	
Gross Debt Service Ratio (%)	8	4	
Annual Inflation Rate (%)	116	25	

---

Background: The process of political normalization initiated in the context of the 1989 Ta'if Accord culminated in Parliamentary elections held in September 1992 and the appointment of a new Government with broad support in October 1992. Following a sharp post-war recovery and stabilization in 1991, a 200% public sector wage increase triggered economic instability in 1992, with a sharp depreciation of the Lebanese Pound, triple digit inflation and a loss of reserves. The confidence inspired by the appointment of Mr. Hariri as Prime-Minister in October 1992 triggered large capital inflows, with stabilization of the exchange rate and inflation, and a recovery of reserves. The new Government has taken initial measures to reduce fiscal imbalances, but the stability that has been achieved remains tenuous, and further adjustment measures will be required, particularly as the reconstruction program gets underway.

---

Part I: Issues Likely to be Raised by The Delegation

1. Consultative Group Meeting

Part II: Issues to be Raised by Senior Management

1. Bank Assistance Program
2. Economic Policy Actions and Role of IMF

Attachments - Biographical Information  
FY94-96 Lending Program (FY93 Actual)

LEBANONBACKGROUND

1. Political: Parliamentary elections were successfully held in September 1992 despite the opposition of Christian groups that felt that they should not take place while Syrian troops remain in Lebanon. A new Government, led by Prime Minister Hariri, took office in October 1992. The Government has further extended control over the national territory, and all militia groups, except for Iran-supported Hezbollah, have been disarmed; nevertheless, Hezbollah did participate in the Parliamentary elections and is represented. The new Government of, Sunni muslim, Prime Minister Hariri has broad domestic and external support. He and several of his colleagues bring a private sector background to the task of government, and they have had significant initial success in turning around a weak public administration, initiating an ambitious reconstruction program, and taking initial measures aimed at correcting fiscal imbalances, which, together with unforeseen domestic or regional political developments, could undermine the stability that has been established.

2. Economic: Following a sharp recovery in 1991, economic conditions turned unstable in 1992 after a 200% public sector wage increase widened the fiscal imbalance. Central Bank financing of a mounting fiscal deficit led to large monetary expansion and a run on the Lebanese Pound, which depreciated sharply, and, because of the openness of the economy, the rate of inflation accelerated to triple digit levels on an annualized basis. Instability continued throughout the first three quarters of the year. The appointment of Mr. Hariri led to a large inflow of capital, an appreciation of the Pound, and a reduction in inflation to single digit levels. The new Government has taken initial measures to reduce the fiscal deficit. However further fiscal actions will be required as the reconstruction program takes off.

3. Bank Operations: Following a hiatus of about one and a half decade, the Bank re-initiated activities in late 1991. A Donors Meeting was held in December 1991 to seek support for the reconstruction program. During 1992 the Bank initiated the preparation of an Emergency Reconstruction and Rehabilitation Project, which forms part of a broader \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96. A \$175 million loan was approved and signed in March 1993 and has recently become effective. Progress in project implementation is satisfactory. A Consultative Group (CG) meeting is planned for December 1993 to help mobilize external resources for the NERP and for technical assistance.

PART I: ISSUES LIKELY TO BE RAISED BY THE DELEGATION

1. (a) Consultative Group Meeting. The delegation may enquire about the Bank's plans for the convening of a Consultative Group Meeting.

(b) Recommended Position. The CG meeting is now planned for mid-December. You may wish to confirm that we would expect the Government to present to the meeting a credible fiscal program for 1994, as part of its overall economic program for that year. Targets for external resource mobilization should be realistic and it will be over-ambitious to expect that

the entire financing gap for the National Emergency Recovery Program can be filled on the occasion of the first CG. We should make joint efforts at canvassing donors in advance of the meeting.

PART II: ISSUES TO BE RAISED BY SENIOR MANAGEMENT

1. (a) Bank Assistance Program. Our ideas with respect to future assistance to Lebanon have been discussed in broad terms on the occasion of Management visits in the course of FY93 and work on a number of possible projects has been initiated. We will be discussing our strategy and lending plans with the delegation prior to your meeting.

(b) Recommended Position. You may wish to indicate that we look forward to developing an active relationship with Lebanon and that we would be willing to provide continued support to the National Emergency Recovery Program as well as for other projects, and that we would envisage a heavy focus on social sectors in our assistance program, as we consider this a priority area for Government intervention. The development of human resources and addressing issues of poverty and regional imbalances, will be key to sustained longer term growth, and maintaining social and political stability. In most other sectors, in particular the directly productive sector, and also the future expansion of physical infrastructure, beyond the immediate reconstruction, the private sector could be expected to undertake the required investments, provided Government ensures an appropriate legal and administrative framework, and maintains a viable macro-economic framework. You may wish to express your appreciation for the excellent cooperation that has been extended to our missions. We expect to invite Government shortly to negotiate a technical assistance project to support the strengthening of economic management and public administration, and preparations have begun for projects in health, education, rural irrigation, water supply, and environment. We would also be willing to consider an operation to support a social fund to finance small scale investments in physical and social infrastructure. You may wish to stress to the Minister that we would expect that adequate and timely local counterpart funding be provided for the ongoing Emergency Project and new projects that are being prepared.

2. (a) Economic Policy Actions and the Role of the IMF. Notwithstanding the progress made in 1993, the fiscal outlook remains of concern. The recently completed 1993 budget will set a higher domestic expenditures ceiling, the domestic interest bill continues rising, reconstruction expenditures are likely to rise rapidly as the program takes off, and key fiscal measures, in particular customs reform and electricity tariff adjustments, have been postponed.

(b) Recommended Position. You may wish to express your concern and ask the Minister to give his assessment and outline his plans to address the fiscal issue. At the same time, you may wish to enquire whether the Government would consider a more formal arrangement with the Fund. This would likely give confidence to donors and help the Minister maintain discipline now that pressures for higher expenditures are likely to increase.

LEBANON

H.E. Mr. Fuad Siniora

Mr. Siniora was born in Sidon, Lebanon in 1943. He obtained his undergraduate degree (B.S. Business Administration) and graduate degree (M.B.A.) in 1967 and 1970 respectively at the American University of Beirut. Until he was named to the post of Minister of State for Financial Affairs in this Cabinet of Ministers, he held the position of Chairman of the Board of the Saudi-Lebanese Bank, the Vice-President of the Board of Trustees of Hariri Foundation and the President of the Financial Holding Group Companies MIG (Mediterranean Investment Group). He was also Chairman and General Manager of Mediterranean Group Services. He served as the Chairman of the Banking Control Commission, a governmental body.

Lebanon

FY 93-96 Lending Program

(in US\$ millions)

	<u>Actual</u> <u>FY93</u>	<u>FY941/</u>	<u>FY951/</u>	<u>FY96</u>	<u>Total</u>
<u>Infrastructure</u>					
Emergency Recovery	175.0				
Water Supply/Sewerage				40.0	
Solid Waste/ Environment				40.0	
Subtotal	175.0			80.0	255.0
<u>Human Resources</u>					
Education		40.0			
Poverty Alleviation			40.0		
Subtotal		40.0	40.0		80.0
<u>Agriculture</u>					
Irrigation			20.0		
Subtotal			20.0		20.0
<u>Other</u>					
TA for Improving Economic Management		20.0			
Subtotal		20.0			20.0
TOTAL	175.0 (1)	60.0 (2)	60.0 (2)	80.0 (2)	375.0 (7)

1/ The FY94 and FY95 lending programs are currently being revised. A Health Project (FY94) would be added to replace the Education Project (now FY95). The Water Supply and Sewerage Project would be advanced to FY95.

# OFFICE MEMORANDUM



DATE: September 15, 1993

TO: Mr. Attila Karaosmanoglu, EXC

THROUGH: Mr. Caio Koch-Weser, MNAV *CKW*

FROM: Ram K. Chopra, MN2DR *Chopra*

EXTENSION: 32707

SUBJECT: LEBANON - CSN Review Meeting

Please find attached the Minutes of Discussion of the Lebanon CSN Managing Director's Review Meeting.

cc: Messrs./Mmes. Serageldin (ESD), Nishimizu (FRS), Ray (DPG), Wijnand (OPRPG), Morais (LEG), Hamid (IFC), Kalantzopoulos (EXC), Koch-Weser, Chopra, Hoppenbrouwer, Ozeki (MNA)

m:\leb\csnrevmtg.mem  
LHoppenbrouwer/mr



LEBANON CSN  
MANAGING DIRECTOR'S REVIEW MEETING

Minutes of Discussion

1. The above meeting, chaired by Mr. Karaosmanoglu, was held on September 3, and attended by: Messrs/Mesdames Serageldin (ESD), Nishimizu (FRS), A.Ray (DPG), Wijnand (OPRPG), Morais (LEG), J.Hamid (IFC), Kalantzopoulos (EXC), Koch-Weser, Chopra, Hoppenbrouwer, Ozeki (MNA). Copy of the meeting's agenda is attached.

2. Macro-economic performance. The Region informed the meeting of recent economic developments. Fiscal performance during 1993 to-date was in line with expectations, with the deficit for 1993 likely to come out at or below the level indicated in the CSN projections and Fund's macro-economic scenario. This performance reflected both a sharp increase in revenues (about 75%) and controls on expenditures, facilitated by the legal limits on expenditures in the absence of an approved budget under continuing resolution provisions. Nevertheless the fiscal situation remained of concern, particularly as the reconstruction program would take off and the 1993 budget, which had only recently been submitted to Parliament, would, once approved, establish higher expenditure ceilings for next year. The good macro-economic performance by a capable economic team, and the continued relative political stability, had contributed to a stabilization of the exchange rate and a sharp decline in inflation from over 100% in 1992 to a single digit level in 1993. The meeting encouraged the Region to closely monitor fiscal developments in collaboration with the Fund, and it was agreed that the presentation by the Government of a viable fiscal program for 1994 should precede the convening of a Consultative Group (CG). The Region should likewise ensure that the proposed projects would have adequate counterpart funding.

3. Political situation. The Region noted that despite the events in July and their aftermath, the political situation had remained stable and Prime Minister Hariri continued to have broad support, both domestically and from abroad. While many factors could upset this stability there are no immediate prospects for concern. The developments in the Middle East Peace Process held out hope that political stability would be consolidated and that economic prospects would improve.

4. Capital inflows. Concern was expressed about the macro-economic effects of the external borrowing for consumption that appeared to be implied in the macro-economic scenario and doubts were expressed about the sustainability of private capital inflows at the projected levels of \$1.8 billion p.a. The Region noted that the balance of payments for 1991 and 1992, constructed from an extremely weak data base, showed apparent net private capital inflows of close to \$2.5 billion p.a., notwithstanding the relatively unstable political and economic conditions during that period. A significant portion of these inflows were likely to have represented private transfers and remittances rather than capital flows and hence national savings, while still low, were higher than appeared from the data. This data problem was extended into the projections, but it was nevertheless clear that, notwithstanding the apparently very large amount of assets held abroad by the Lebanese diaspora, the private (and official) inflows required in the medium term would only be forthcoming if both economic and political stability would be maintained. The

meeting suggested that in the context of the proposed CG other donors should be expected to make a major contribution to Lebanon.

5. Social sectors. The meeting noted that Lebanese Governments had traditionally ignored social issues and regional development and enquired whether the Government would be interested to engage with the Bank in a relationship that envisaged from the Bank side a heavy focus on social sectors in the assistance program. The Region indicated that there was awareness among the political leadership that a lack of attention to these issues in the 60s and 70s had contributed to the subsequent period of disorder. Nevertheless, in early discussions the Government's position had been that the employment effects of reconstruction and restoration of price stability would be the answer to social problems, but since then the Government had been increasingly keen on Bank involvement in the social sectors, although some queried whether Lebanon should borrow at Bank terms for investments in these sectors, and regional balance is now an important consideration in the design of investment projects, particularly those that are funded with external assistance. The Government's reconstruction program rightly focussed on the rehabilitation of physical infrastructure, but also included important allocations for the social sectors. The current budget allocations for social sectors were still relatively small, reflecting the fiscal constraints, the weakness of sector institutions, and the traditional reliance on private sector and NGOs for the provision of services, but were likely to increase in future. Finally, the Region confirmed that it was not the Bank's intention, nor the Government's desire, that the poverty assessment focus on differences among religious or ethnic groups, but rather among regions. The meeting encouraged the Region to ensure that there would be full Government commitment to the proposed focus of the assistance program.

6. Risks and Strategy. The Region emphasized that the proposed strategy entailed relatively high risks, economic and political, but that the rewards were potentially significant. The meeting agreed that despite the risks it would be appropriate for the Bank to support Lebanon along the lines envisaged, but the Region should keep a close watch on political and economic developments, inform those concerned in the Bank of unusual events, and adjust the program downward if necessary in light of adverse developments. The meeting considered it appropriate that the strategy be reviewed again in about a year. The Chairman asked the Region to share with Government the overall objectives of the proposed assistance strategy and agree on the proposed approach. The Region was to stress that the Bank expected Government to continue the country's traditional reliance on the private sector and create the conditions necessary to attract private inflows and to maintain a viable macro-economic framework and pay due attention to social sectors and poverty issues. The CG should be an opportunity for the Government to present a coherent program, for the Bank to present its proposed program, and to invite others to fund the reconstruction effort. Finally, he reiterated the need for a close monitoring of the situation and for maintaining flexibility in our assistance program, which was endorsed along the lines proposed.

M:\leb\mdreview.2  
L.Hoppenbrouwer



hH

Managing Director's Review Meeting - September 3, 1993LEBANON - COUNTRY STRATEGY NOTEAGENDAThe Political Landscape

The Country Strategy Note is a well-written paper that makes the case for increased Bank involvement in Lebanon. The suggested update within twelve months seems appropriate. Still, Lebanon's economic performance is highly dependent on domestic and regional political developments. What are the latest views on the prospects for a more stable political environment?

Macroeconomic Management

The development scenario presented in the CSN is based upon an ambitious program of fiscal adjustment and macroeconomic stabilization. Has recent macroeconomic management and performance been in line with the fiscal adjustment scenario envisaged under the CSN? Is there sufficient evidence of commitment to fiscal reform for initiating the base case lending program? Did recent hostilities affect fiscal performance, inflation and growth?

Political uncertainties in the Region introduce important political and economic risks. What specific monitorable criteria would be used as indicators for switching to a low case lending scenario? What would be the size and composition of a low case program?

Investment and Capital Inflows

Renewed confidence in the country's political and economic management is expected to generate massive capital inflows from Lebanese living overseas. While capital inflows are indeed welcome, the projected magnitude of these inflows in relation to investment and GDP raises questions. With projected negative savings rates and consumption on average at about 111% of GDP, substantial part of capital inflows would be financing current consumption. Could the Region comment on the macroeconomic sustainability of this pattern of external finance -- which is projected to continue for sometime into the future -- and its implications for economic policy and performance.

Public Expenditures and Poverty

Lebanon has major physical and social infrastructure needs. Does the current composition of government expenditure reflect priorities between infrastructure improvement and provision of social services? Would the planned poverty assessment focus on the income distribution and social indicator disparities among different ethnic and religious population groups? Is military spending still an important component of government expenditures?

A. KARAOSMANOĞLU  
Managing Director

September 10, 1993

Mr. Caio Koch-Weser

Re: Lebanon Country Strategy

As we discussed, while the proposed strategy for Lebanon is sound and the lending program addresses the most crucial country needs, the macroeconomic and political uncertainties facing the country are still significant. The policy dialogue should aim at focussing the Government's full attention on the guiding principles of the Bank's strategy of fiscal discipline and increased attention to poverty alleviation across regions and ethnic groups.

As we agreed, the Bank will proceed with caution and flexibility, monitoring closely macroeconomic and political developments. Before convening a Consultative Group meeting, the Region should be confident that the Government shares the Bank's stabilization and poverty objectives. We will reassess our strategy in about one year, in light of macroeconomic and political developments, and in the context of a country strategy update.



cc: Messrs. Preston, Sandstrom, Stern, Bruno, Choksi, Husain, Jaycox,  
Kaji, Linn, Rischard, Ryrie, Serageldin, Thalwitz, Wood,  
McHugh, Chopra

A. KARAOSMANOĞLU  
Managing Director

September 10, 1993

Mr. Caio Koch-Weser

Re: Lebanon Country Strategy

As we discussed, while the proposed strategy for Lebanon is sound and the lending program addresses the most crucial country needs, the macroeconomic and political uncertainties facing the country are still significant. The policy dialogue should aim at focussing the Government's full attention on the guiding principles of the Bank's strategy of fiscal discipline and increased attention to poverty alleviation across regions and ethnic groups.

As we agreed, the Bank will proceed with caution and flexibility, monitoring closely macroeconomic and political developments. Before convening a Consultative Group meeting, the Region should be confident that the Government shares the Bank's stabilization and poverty objectives. We will reassess our strategy in about one year, in light of macroeconomic and political developments, and in the context of a country strategy update.



cc: Messrs. Preston, Sandstrom, Stern, Bruno, Choksi, Husain, Jaycox,  
Kaji, Linn, Rischard, Ryrie, Serageldin, Thalwitz, Wood,  
McHugh, Chopra

## OFFICE MEMORANDUM

DATE: July 12, 1993

CONFIDENTIAL

TO: Mr. Attila Karaosmanoglu, Managing Director

FROM: Caio Koch-Weser, MNAVVP *ckw*

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

EXTENSION: 35250

SUBJECT: LEBANON: Country Strategy Note

Please find attached the Country Strategy Note for Lebanon, which we reviewed at a Regional Loan Committee meeting on July 6, 1993.

Messrs./Mesdames

Sandstrom, Stern, Armitage, Kalantzopoulos (EXC); Thahane (SEC); Alisbah (PAAVP); Choksi (HROVP); Eccles (CTRVP); Einhorn (TREVVP); Husain (LACVP); Jaycox (AFRVP); Kaji (EAPVP); Kashiwaya (CFSVP); Linn (FPRVP); Picciotto (DGO); Rao (DECVP); Rischard (FPDVP); Serageldin (ESDVP); Shihata (LEGVP); Thalwitz (ECAVP); Wood (SASVP); Rylie (CEXVP); Iida (MIGEX); Ray (DPG).

Messrs./Mesdames

Husain, Squire, Murli, Bouhabib, Kafka (MNAVVP); Chopra, Tyler, Heron, O'Donnell (MN2DR); Kohli, (MN1DR); Sood (EMTDR); Voyadzis, Hoppenbrouwer, Ozeki (MN2CO); Okonjo-Iweala, Barres (MN2AG); Bhargava, Jordan (MN2IE); McKechnie, Graham (MN2IN); Keare, Sederlof (MN2PH); Hovaguimian (CMEDR); Alizai (COGDR); Pfeffermann (CEIED); Haddad (CMED2); Nishimizu (FRSDR); Bhattacharya (FRSCR); Sud (CFSDR); Birdsall (CECDR); Petit (AGRDR); El-Ashry (ENVDR); Iskander (PSD); Long (FSD); Adams (OPRDR); Hollywood (MIGGU); Morais, Abushahr (LEGMN); Chabrier, Handy (IMF); MNA Files.

L. Hoppenbrouwer  
M:\leb\csnmd

*L*

Document of  
The World Bank

CONFIDENTIAL

**DECLASSIFIED**

**MAR 31 2017**

**WBG ARCHIVES**

**REPUBLIC OF LEBANON**  
**COUNTRY STRATEGY NOTE**

July 12, 1993

Country Operations Division  
Country Department II  
Middle East and North Africa Region

LEBANON  
COUNTRY STRATEGY NOTE

TABLE OF CONTENTS

	<u>Page no.</u>
EXECUTIVE SUMMARY.....	i
Economic and Political Background.....	1
Development Issues and Policy Agenda.....	2
Physical and Social Infrastructure.....	4
Environment.....	6
Human Resources Development.....	7
Productive Sectors.....	8
Macroeconomic Prospects.....	9
Introduction.....	9
Base Case.....	9
Alternative Scenarios.....	10
Creditworthiness and External Capital Requirements....	10
Bank Assistance Strategy.....	11
Coordination with other Institutions.....	13
Bank Share of Financing.....	14
Downside Risks.....	15
Objectives and Instruments of Country Assistance Strategy.....	16
ANNEX I      Lending Program (Base Case)	
ANNEX II     Economic and Sector Work Program	
Social Indicators of Development Key Indicators and Projections	



# LEBANON

## COUNTRY STRATEGY NOTE

### EXECUTIVE SUMMARY

*Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of war. By 1990, per capita income (about \$820) was only about one-third of the 1975 level in real terms. The total damage to physical assets was estimated by the United Nations at \$25 billion. The impact on social conditions has been grave, with considerable loss in human resources, one quarter of the population of 3.6 million displaced, and public and social services either non-existent or of poor quality.*

*A sharp post-war recovery in 1991 was followed by an economic crisis in 1992, triggered by successive governments' failure to address fiscal imbalances. In October 1992, a new government took office following parliamentary elections. Prime Minister Hariri and his Cabinet enjoy broad political support. Government faces the daunting task of rehabilitating the war-damaged economy while maintaining economic and political stability, rebuilding a devastated public administration, and enticing the private sector to invest. Initial confidence triggered a significant inflow of capital and helped reestablish stability, which remains fragile, however, and will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.*

*Lebanon's vigorous and dynamic private sector continues to be the country's main asset. Beyond the initial stage of reconstruction to restore basic physical and social infrastructure, steady long-term growth will be predicated upon renewed private sector initiative. The government intends to support private sector initiative by creating an appropriate enabling environment, and efficient public administration, and investing in human resources. Before the protracted war, human resources were well developed and health facilities adequate, but there was a general neglect of social concerns. At present the*

*needs in health and education are massive. Continued political stability will not be maintained unless social issues and human resources development are addressed.*

*The serious damage sustained to basic infrastructure now presents the most immediate obstacle to economic revival. Mr. Hariri's government has a unique window of opportunity to undertake the ambitious task of reconstruction, establish economic stability, and lay the basis for private sector-led recovery. Lebanon needs substantial amounts of official external assistance to finance an ambitious \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96. In addition, reconstruction and recovery will require large amounts of private capital. Total capital requirements in the medium term would amount to around \$3.0 billion per annum. The bulk of this is expected to be available from private capital inflows, provided political and economic stability are maintained.*

*The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. The \$175 million Emergency Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which institutional and economic reform is feasible. The Bank now has a fairly unique opportunity, at above average risks, to play a major role in the recovery of Lebanon. Towards the overall objective of a resumption of rapid growth and reduction of poverty, the Bank would support a private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity,*

rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development.

Future lending would concentrate heavily on the social sectors, and would also support the strengthening of the public administration, and selected public investments in physical infrastructure during the reconstruction phase and future expansion by the private sector. The frontloaded ESW would underpin future lending and help government establish an enabling environment for private sector development. We would convene a CG meeting to help mobilize external resources for the NERP provided the Government continues to mount and implement an economic program satisfactory to the IMF and the Bank.

The proposed base case lending program of three operations for an average of \$85 million per year during FY94-98, with some frontloading, would be conditional upon the maintenance of an acceptable overall macroeconomic framework and the availability of financing from other sources. We would also need to continuously monitor the evolution of the political situation. A decline in government commitment to fiscal adjustment would trigger a low case lending program. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. The proposed ESW is for 180 SW on average during FY94-96 with frontloading.

In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank throughout the war. External public debt, an estimated \$360 million (8% of GDP) at the end of 1991, is low by any standard. Despite a projected five-fold increase by 1996 because of the external financing required for the NERP, debt indicators would remain low, with a public debt to GDP ratio of 18% and a public debt service to exports ratio of less than 5%. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP. The Bank would account for 12% of gross loan and grant disbursements during 1993-96, and 20% of external public

debt by 1999. Lebanon's stock of external public debt would remain small by any standard, while its external reserve position - \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. In view of the past track record with the Bank and the government's commitment to fiscal stabilization, the amounts of planned lending are considered prudent.

There are risks that current economic stability will not be sustainable in the absence of action to correct macroeconomic imbalances and that external events, particularly regional developments, could upset political stability. The population's high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war, and the need to carefully balance the interests of the various denominational factions, could hamper the government's ability to take required measures. With the continued presence of the Syrian army, and the occupation of part of the country's territory by Israel and the Southern Lebanese army, there could be far-reaching implications for Lebanon if the Middle East peace process were to fail.

In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The government is well aware that economic stabilization is a pre-condition for sustained, private sector-led, recovery and growth, and has begun to take fiscal actions. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

The main issue for Management is:  
are the proposed strategy and lending and ESW programs appropriate given Lebanon's circumstances, needs, prospects, and the various political and economic risks involved?

## LEBANON

### COUNTRY STRATEGY NOTE

#### Economic and Political Background

1. Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of turmoil as a result of violent civil strife and military occupation. In the period between 1950 and 1975, Lebanon's free market economy expanded by about 6% per annum. This growth was largely driven by the service sectors, namely trade, tourism, and finance, which attracted business from surrounding oil-based economies. After the eruption of civil war in 1975, the economy deteriorated markedly, with intermittent recovery during the two periods of relative calm, 1978 to 1981, and 1986 to 1988.
2. The civil war had a severe impact on the socio-economic conditions in the country. Lebanon's per capita GNP, about US\$820 in 1990, in real terms was only about one third of the 1975 level, and income inequalities have been accentuated. The total damage to physical assets during the war period was estimated by the United Nations at US\$25 billion. All principal sectors of the Lebanese economy - physical and social infrastructure, office and factory buildings, and housing - have been affected. Damage is both a direct result of the war, as well as the accumulated effects of a near total disruption in capital investment and maintenance.
3. The impact of the civil war on social conditions has been equally grave. The loss in human resources has been considerable; apart from the tragic loss of life and the disabling of hundreds of thousands of people, about 200,000 professional and skilled Lebanese have sought employment in other countries. While this has resulted in major shortages of skilled workers in various sectors of the economy, unemployment nevertheless is estimated at 35% of the resident labor force, and is believed to be particularly high among urban youth. Nearly one quarter of the population of 3.6 million has been displaced and now lives in unhealthy shanty towns, and in semi-destroyed and vacated buildings, with severe overcrowding and inadequate housing quality. Urban poverty problems are especially pressing in Beirut. Public and social services are either non-existent or of poor quality, with only about one third of power capacity operating, water treatment and sewage virtually nonexistent, and most schools and hospitals damaged.
4. The 1989 Ta'if Accord for National Reconciliation, sponsored by the Arab League, was a first step toward bringing an end to the violence in late 1990. The national army was reunified, and a Syrian backed national unity government reestablished its authority over the Greater Beirut area and most of the national territory. Attempts to achieve economic stabilization since the end of the fighting in 1990 have yielded mixed results. During 1991, activity took off in virtually every sector of the Lebanese economy, spurred by large inflows of private capital, with real GDP expanding by about 40%. At the same time inflation moderated to 30% by year's end from close to 100% the year before, and exchange rate stability was reestablished. However, the government's stabilization policy was not sustainable beyond the short term in the absence of adequate fiscal correction. Interest payments on Treasury Bills, issued to absorb the large speculative capital inflows, merely added further to the fiscal imbalance and the overall fiscal deficit was close to 20% of GDP in 1991. Economic recovery and a real appreciation of the Lebanese Pound led to a sharp surge in imports, which left the current account deficit at an unsustainable high level (more than 40% of GDP). The economic situation worsened in

early 1992, as Central Bank credit to finance the fiscal deficit expanded significantly after the government awarded a 200% retroactive increase in public sector salaries. This triggered a large outflow of capital, including a switch from Pound to Dollar denominated assets, put pressures on the Lebanese pound, and caused disruptively high rates of inflation. In an attempt to defend the value of the Pound, the Central Bank lost \$500 million in reserves in a matter of weeks. The resulting exchange rate crisis, which particularly affected the poorest segments of the population, precipitated a national strike and forced the government to resign in May 1992. A new government was appointed but failed to take stabilization measures and exchange rate depreciation and inflation accelerated throughout the first three quarters of 1992.

5. In September 1992, parliamentary elections were held, and on October 31 a new government was formed. Prime Minister Hariri and his Cabinet enjoy broad political support, and have sparked high expectations. The Christian groups that boycotted the elections are generally supportive of Mr. Hariri, who also reportedly maintains good relations with Shia religious leaders, as well as enjoying both Saudi and Syrian support. Prime Minister Hariri has assembled an impressive economic team, many of whom bring a private sector background to the task of rehabilitating the war-damaged economy while maintaining economic and political stability, and turning around a very weak public administration.

6. The confidence in Mr. Hariri's appointment triggered a significant inflow of capital, which reversed depreciation of the Pound and brought inflation to negligible levels. Since October 1992 the Pound has appreciated by about 25% and inflation has been reduced from over 100% to single digit levels. In addition, it enabled the Central Bank to replenish its reserves (by about \$1.0 billion), and the government to switch from Central Bank credit to Treasury Bills for the financing of its large

deficit (13% of GDP in 1992). The current monetary and exchange rate policy obviously has significant fiscal costs, but the authorities consider this to be an unavoidable consequence of stabilizing the exchange rate. Nevertheless, the speculative nature of these capital inflows suggests that stability will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.

7. Lebanon needs substantial amounts of external assistance in support of stabilization and reconstruction. The government has requested the Bank to assist in the mobilization of the large amount of external resources required to finance its \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96, and has sought IMF advice for the design and implementation of a macroeconomic stabilization program. The donor community has shown a willingness to support the reconstruction of the Lebanese economy. However, in addition to official capital, the reconstruction and recovery of the Lebanese economy will require large amounts of private capital, which will only be forthcoming if political stability is maintained and sustainable economic stabilization established by the government.

#### **Development Issues and Policy Agenda**

8. Endowed with an enterprising population and a geographical location on the trade route between Europe and the Middle East but with no mineral resource base and land that is difficult to cultivate, the Lebanese economy has been oriented to the development of services and light industry. Traditionally, Lebanon has been an open economy, characterized by a large external sector and unrestricted capital mobility, and it had achieved an export-oriented and private sector-led economic development at a good pace mainly through the development of international banking, transit trade, and tourism and, to a lesser extent, through the export of manufactured and agricultural products. With the destruction of much of the nation's infrastructure and productive assets and

dislocation of the human capital after an extended civil war, the reconstruction of the Lebanese economy is a daunting task, and is expected to take massive resource mobilization, capital investment, and development of human resources, and rebuilding of institutions over a protracted period of time. By training its unemployed manpower, restoring the pre-war quality of education, re-equipping labor with infrastructure and productive capital stock, and tapping the resources of its large expatriate community, Lebanon could relatively rapidly rebound and restore rapid growth.

9. Lebanon's reconstruction and development should be guided by the private sector initiative as Lebanon's vigorous and dynamic private sector continues to be the country's main asset. However, in the initial stage of reconstruction, government involvement is crucial as the first order of priority in reconstruction is given to restoration of basic physical and social infrastructure and is to be undertaken by the government under the NERP. Beyond a period of rapid growth that is likely to be associated with the reconstruction phase, sustained domestic investment and steady long-term growth will be predicated upon the renewed private sector initiative. The government's role would be to establish an enabling environment. Above all, it is imperative to sustain the confidence that has been placed in the new government and the Lebanese economy by vigorously pursuing macroeconomic stabilization measures. Moreover, government will need to strengthen public administration and macroeconomic management, and provide clear signals that Lebanon's traditional policies of non-interference with private sector activities will be maintained.

10. Although presumably Lebanon's comparative advantage still lies in international services, tourism, and high value added light manufacturing industry and agriculture, regional competition for financial services and transit trade has increased, the high regional growth associated with the petroleum boom is no longer

present, and other circumstances that had contributed to the rapid growth in the period prior to the mid-1970s are unlikely to be replicated. Hence, prospects for the longer term, including the direction of future growth, are somewhat uncertain at this time, although the resumption of past economic activity, including tourism in particular, is not to be excluded. However, whatever its composition, the potential for growth would be best exploited if government supports private sector initiative.

11. The new government faces the need to undertake stabilization measures simultaneously with its reconstruction program, in order to attract private and official financing for reconstruction. The restoration of fiscal balance - announced by the current government as one of its key objectives - will require drastic action through measures that both raise government revenues from the 1992 level of only 10% of GDP, and contain current expenditures at close to the 1992 level of 20% of GDP. This presents a challenging task, particularly given the virtual collapse of government revenues over the past several years, to the point where revenues covered less than 50% of current expenditures. Since reconstruction will lead to a sharp increase in the presently low level of capital expenditures (a projected average of 10% of GDP during 1993-96), a sharp reduction in the current deficit (10% of GDP in 1992) will be required in order to keep the fiscal deficit in check.

12. Revenue collection and expenditure control in the short run is complicated by administrative weaknesses and rigidity in key expenditure categories. It is therefore necessary to concentrate on policy measures that are straightforward in design, can be implemented quickly, and have good prospects for reducing the current fiscal deficit. Compared to other countries in the region, Lebanon's taxation yields are very low, particularly for direct taxes (2% of GDP in 1992). Key elements in expenditure control include adjustments in power tariffs to reduce budget transfers; the containment of interest payments on internal

debt (which stood at about 40% of GDP at the end of 1992) by gradually lowering interest rates; and containment of the wage bill by limiting wage increases and eliminating ghost workers from the payroll. Subsidies on electricity tariffs have been a major source of the fiscal deficit, as the weighted average tariff is only about one-fifth of economic cost.

13. Over the past half year, the government has already initiated a number of fiscal actions, including administrative measures to improve income and real estate tax and electricity tariff collection, the elimination of wheat subsidies, increases in fees and water and telephone charges and electricity connection fees. The government has maintained public sector wages at the level established in early 1992, in spite of triple digit inflation in 1992. The government's initial measures have resulted in a doubling of revenues during the first quarter of 1993, while expenditure growth has been contained, but further measures, along the lines enumerated in the recent CEM, in particular customs tariff reform and adjustments in power tariffs, will be required to achieve a sustainable reduction in the fiscal deficit.

14. The government envisages a phased strategy for rebuilding Lebanon's ravaged economy and addressing social problems, consisting of a short-term emergency reconstruction phase followed by a medium-term recovery phase. The NERP provides for initial urgent investments, which will be made concurrently with the identification and implementation of longer-term development strategies in the various sectors. The NERP is designed as a multi-sectoral operation, focussed on removing critical infrastructure bottlenecks, alleviating pressing social problems, and strengthening the existing institutions in charge of planning, financing, and implementing the NERP.

15. The phased recovery program envisions that much of the reconstruction will be undertaken by the private sector, with

government supporting the first phase of short-term emergency reconstruction. Lebanon's traditional liberal and investor friendly policies provide a solid base for an expansion of private sector activity and the Lebanese diaspora represents an important source of entrepreneurial skills and capital resources. Yet, the regulatory framework will need to be updated, in part to facilitate private investment for the provision of infrastructure services, and financial sector reform and capital market development will be required for the transformation of resources to long-term investments.

16. Notwithstanding the limited role envisaged for the public sector in the medium- to long-term, there is an urgent need to rebuild public institutions that are dilapidated after 15 years of war and lack qualified personnel, particularly at the middle-levels. The government has, with Bank assistance, begun to define a program for rebuilding public administration, including a technical assistance program to address short term needs for strengthening of economic management and public sector institutions.

#### **Physical and Social Infrastructure**

17. All principal sectors of Lebanon's economy are characterized by widespread damage to physical assets and the obsolescence of remaining facilities, given the reluctance during the years of conflict to invest in new capital or spend on maintenance. The serious damage sustained to basic infrastructure in virtually all sectors now presents the most immediate obstacle to economic revival. As a major regional trade and financial sector, Lebanon's transport infrastructure had been developed intensively prior to the civil war. The thriving service economy of Beirut, where many multinational companies located their regional operations, depended on efficient transport links. During the war, Lebanon's ports and Beirut International Airport, as well as the road and rail networks, sustained severe damage and suffered from a lack of maintenance. Substantial investment will be

needed to restore competitiveness, particularly since other countries within the region have greatly enhanced their own transport networks. The NERP focuses on rehabilitation of international and primary roads, restoring Beirut airport handling capacity to its pre-war level, restoring capacity of the port facilities, and rehabilitating the Beirut bus system. Increased cost recovery, for example through taxes on fuel, customs duties on vehicles, and higher bus tariffs and air passenger fees, is an essential element of the sustainable recovery of transport services.

18. Lebanon meets virtually all its energy needs with imported crude oil and petroleum products. Both of Lebanon's oil refineries sustained heavy damage during the war. The power sector is characterized by a damaged and dilapidated state of the electricity network, as well as an acute shortage of qualified staff at the state-owned Electricite du Liban (EdL). EdL suffers from serious financial difficulties, mainly due to low tariffs, illegal connections, and poor collections. Estimated rehabilitation and expansion needs of the sector amount to about \$830 million. Because of the breakdown in public power supply, most commercial and industrial customers have installed private diesel generating stations, and there is a need to revise the legislative framework in order to regulate private sector activities in the power sector. The high-cost, small-size private systems cannot be expected to fill an anticipated rapid growth of demand as commerce and business enterprises re-establish operations. Tariffs need to be adjusted to adequately reflect costs.

19. The immediate objectives for the power sector should be: (i) reconstructing the war-damaged facilities and removing deficiencies in existing facilities; (ii) setting and maintaining electricity tariffs at levels which cover the full cost of supply, while providing a life-line rate for the first 100 or 200 Kwh/month; (iii) restructuring and corporatizing EdL's activities, and contracting out certain activities (eg. billing, repair), with a view to eventual privatization;

and (iv) upgrading the quality of human resources employed in the sector through training and staff development programs. The NERP includes initial investments of about \$300 million, to provide an integrated and balanced package of improvements.

20. In the telecommunications sector, about one-third of subscribers do not receive service, and those who have access to the network suffer from low quality of service. With the breakdown of public services, private entrepreneurs installed and operated various unlicensed systems. As adequate telecommunications services will be required to restore Lebanon's role as a business, banking and services center in the Middle East, as well as for resuming normal economic and social life, their rehabilitation is among the highest priorities. The NERP focuses on urgent rehabilitation works that can be undertaken without the need for further studies, and which would be compatible with longer-term improvements that are to be identified. In addition to reconstruction of technical installations, the restoration of reliable services requires simultaneous actions to rebuild the sector's management, planning and operating capabilities. The government intends to encourage the role of the private sector in the reconstruction and future development of the telecommunications sector, which will require a review and up-date of the overall legal framework, as well as revamping the government's policy making, regulatory and licensing functions and authority. Tariffs need to be further increased progressively to bring them in line with costs.

21. In the water supply and sanitation sector, there are no functioning sewage treatment facilities in the country, and all water treatment plants have been damaged and are operated at reduced capacity. A 1990 water quality survey indicated unsatisfactory water quality on a widespread scale, which could have serious health implications. Operation and maintenance suffer from inadequate organizational structures and a lack of skilled staff. Damage assessment

surveys indicate that about \$325 million in investments are required for water supply and waste water and for improving solid waste disposal. The undertaking of these investments will require a reorganization of present institutions, with participation from the private sector. Tariffs will have to be raised to ensure adequate internal cash generation for a sustainable development of the sector. The NERP includes: (i) design and execution of physical rehabilitation works; (ii) preparation of a policy strategy paper for institutional and organizational development; (iii) preparation of development programs and feasibility studies for subsequent investments; and (iv) preparation of a water master plan for the country.

22. In housing, the inadequacies of the housing supply mechanism have been exacerbated by the war, but in themselves are more deeply rooted. Lebanon's relatively small size, coupled with its highly dense pattern of settlement and traditionally high construction costs, places housing at a great premium. Furthermore, there have been no urban growth strategy or land-use plans to anticipate and cope with population movements. Substantial capital inflows for real estate speculation led to further distortions in the market system. Because of the different effects generated by internal and external emigration during the war, there is at present a surplus of high quality housing, coexisting with severe pressures in the mid- and lower-quality market.

23. The relocation of displaced persons is considered Lebanon's most pressing social problem, and an appropriate policy framework is required to deal with the complexity of housing sector resettlement and development. The NERP contains a major component for housing finance. In order to initiate rehabilitation of the housing stock by the private sector, appropriate financial instruments need to be developed and mechanisms established for the management and implementation of housing credit, possibly through existing commercial banks. The substantial decline in household real

income levels that occurred during the war eroded the capacity of households to make payments on housing loans. The affordability of housing rehabilitation to certain beneficiary groups therefore will require direct subsidies. In conjunction with other infrastructure components, the housing component of the NERP also will alleviate the immediate environmental problems by resettling households into better conditions and by providing and/or rehabilitating the needed infrastructure services.

### Environment

24. The deteriorated conditions resulting from the extensive war damages cause severe risks to public health and to the environment. The main hazards are: polluted water distribution systems; scattered solid waste dumped all over the country; heavy air pollution on account of energy generation by large numbers of small generators, transport and industrial plants; haphazard expansion of dwellings over fertile lands and natural ecosystems; the abandonment of agricultural lands; the pollution of surface and underground aquifers; widespread deforestation; destruction of the cultural and natural heritage; and the degradation of marine and coastal areas. The planned reconstruction and rehabilitation programs would remedy some of the urgent problems, but the increasing demands for land, water and building materials resulting from them would put additional pressures on the environment.

25. While specific environmental issues are addressed in sector laws and regulations, there is no comprehensive national environmental framework, and the capacity of the Ministry of Environment that was re-established in late 1992 is still very limited. Beyond the actions envisaged under the sectoral programs of the NERP that would address some of the current public health and environmental problems, there will be a need to adopt an environmental strategy to ensure that the process of reconstruction and rehabilitation will contribute to sustainable development.



## Human Resources Development

26. Before the protracted civil strife, Lebanon had a well-trained population and labor force, with adequate health facilities. Nevertheless, there was a general neglect of social concerns during the period of rapid economic growth preceding the war, and at present the needs in health and education are massive. A considerable number of social services, especially in the health sector, are currently provided by non-governmental organizations (NGOs), and are linked to the war situation. In the future, to a large extent these will need to be provided by the public sector. Furthermore, as indicated above, all sectors of the economy, including public administration, suffer from a lack of skilled workers and managers. Social sector ministries are inadequately staffed and are particularly weak.

27. In the health sector, the Ministry of Health (MOH) plays a relatively minor role in the actual provision of services. With the reduced capacity of public hospitals due to war damage and insufficient funds for the rehabilitation and operation of facilities, the MOH ends up directing over 80% of its budget to an uncontrolled reimbursement of private sector (including voluntary agencies) hospital services. The subsidy program, currently running at about \$60 million annually, is poorly targeted and inadequately monitored and controlled. The provision of primary health care services is inadequate, and their delivery currently consists of small dispensaries operated by a myriad of public, private, voluntary and political groups. Overall, the government has little ability to control quality and to enforce standards in the health sector. While generally there is an oversupply of skilled medical doctors in Lebanon, major institutional reforms will be required in the public health sector not only to fill the existing shortage of professional staff, but also to provide greater flexibility in the administration of budgets and in personnel management.

28. The health sector component of the NERP (\$61 million) includes rehabilitation of public hospitals, dispensaries and laboratory services, as well as assistance to rehabilitate care facilities for the disabled provided by charities. Technical assistance components would identify and support the immediate requirements for reform and improved management of subsidy programs, the decentralization of health services management and planning, and the development of MOH into a regulatory body focusing on policy and wider issues of public health. Issues related to the funding of publicly-provided health services also will be examined.

29. Total enrollments in general education declined during the latter part of the civil war, with an increasing share in enrollments for the private sector, which historically has played a significant role within the education sector at all levels. Private sector schools comprise two categories: exclusively fee-paying, and those which are state-subsidized but privately run by welfare institutions. The public sector's share of enrollments is 31% in primary, 46% in intermediate, 33% in secondary, 27% in vocational and technical schools, and 47% in higher education. In the absence of reliable population data, it is difficult to assess enrollment as a percentage of relevant age cohorts.

30. Teacher training activities were essentially suspended in 1987 and in-service training has been conducted irregularly since that date; thus, while the overall pupil/teacher ratio in the public sector is apparently extremely favorable, teachers tend to be poorly trained and localized shortages exist, mostly in rural areas. Enrollments in vocational and technical institutions have been very sensitive to prevailing security and economic conditions. Technical curricula are not relevant to the needs for trained labor, and there is a lack of suitable instructors. The provision of higher education by the public sector (the Lebanese University) expanded rapidly during the war, with an

expansion of campuses in various parts of the country, but quality declined.

31. The development of education facilities in Lebanon must be accompanied by wide-ranging reforms in sectoral policies and in the planning, management and administration of the sector. Substantial expenditures will be required to rehabilitate physical infrastructure and key institutional and policy reforms will require considerable technical assistance. The NERP earmarks about \$150 million for the education sector, to be directed toward four major priorities: i) upgrading the capacity of the teacher training system; ii) improving vocational/technical training centers, curriculum development, instructor training, and instructional materials; iii) rehabilitating public schools, to enhance their capacity to cope with a recovery in enrollments, support the government's resettlement strategy, and enhance educational access for those who cannot afford access to Lebanon's traditionally strong private education sector; and iv) improving the equipment and buildings of the Lebanese University. The government currently does not recover costs for public education; thus cost recovery, particularly with regard to higher education, is an important issue.

32. The issue of women in development has not been high on the government's agenda, and while educational enrollment figures are high, female illiteracy rates are high as well and political participation is limited.

33. Poverty Reduction Efforts. As noted above, after 15 years of war, real incomes have sharply declined, social conditions have worsened significantly and the displacement of up to a quarter of the population from their homes represents a pressing social issue. While poverty appears to be more heavily concentrated in the Greater Beirut area, there are important pockets of rural poverty as well. Social assistance is currently being provided by a large number of NGO's operating in Lebanon, many of which concentrate their efforts on specific

denominational groups. The government lacks information about the incidence and concentration of poverty and neither does it have the resources or mechanisms to address poverty in the short run. The government is of the view that price stability combined with employment to be generated through the reconstruction program will particularly benefit the poor. Nevertheless, it has asked the Bank to help assess the need and possibilities for social safety net mechanisms to accompany the stabilization measures that would need to be undertaken to correct the macro-economic imbalances.

### Productive Sectors

34. Productive activities in Lebanon have traditionally been undertaken almost exclusively by a strong private sector, and it is on private initiative that future growth will depend. The government's main role will be to create an enabling environment for private sector activity in the productive sectors and in the provision of infrastructure. This will require a strengthening of public administration, the development of a legal and regulatory framework that is conducive to attracting private investment, as well as a strengthening of capital markets.

35. Agriculture. Much of Lebanon's arable land (an estimated one-third of the territory) is marginal land and Lebanon has always been a net importer of agricultural and food commodities. The sector contributes about 10% to GDP and accounts for about 20-25% of merchandise exports. The dislocation of production and marketing facilities during the war resulted in a decline in agricultural exports (mainly fruits and vegetables) from close to \$260 million in 1980 to \$170 million in 1990. To regain market shares, Lebanon will have to address both the extensive war damage and the pre-war weaknesses in the agricultural sector. Priority areas for public sector intervention include: (i) rehabilitation and improvement of irrigation schemes and recovery of at least O & M costs of irrigation schemes; (ii) physical reconstruction and institutional development of

the Ministries of Agriculture and Water and Electrical Resources; (iii) the upgrading of applied agricultural research and extension services. As in other sectors, the virtual absence of medium- and long-term credit, particularly for small and medium farmers and agro-industries hampers a recovery of the sector.

36. Industry. The industrial sector contributes about 20% to GDP and accounts for the bulk of merchandise exports. Except for oil refining, industry is entirely within the private sector. The industrial sector faced not only considerable war damage (close to 200 plants were destroyed in the heavy 1989/90 hostilities), but more importantly, a loss of its work force. Nevertheless, available data suggest that the sector has remained resilient in the face of the war, with real sector GDP in 1991 only some 20-30% below its pre-war level. A lack of skilled workers and managers, poor physical infrastructure and the virtual absence of medium- and long-term financing for working capital and investment stand in the way of a sustained recovery of the sector.

## Macroeconomic Prospects

### Introduction

37. The scenarios presented below are based on the macroeconomic framework in the recent Country Economic Memorandum ("Lebanon - Stabilization and Reconstruction") dated March 1993. The base case scenario is substantially similar to the medium-term scenario developed by the May 1993 IMF Article IV Consultation mission. Due to the paucity of data, and the absence of time-series, an unusual number of estimates and assumptions have been made to construct the framework. Thus, caution needs to be exercised in interpreting the results of the analysis. However, the projected scenarios are broadly indicative of general directions of developments and the likely outcomes of alternative policies and thus form a plausible basis for judgements on macroeconomic policy issues, resource needs and creditworthiness.

### Base Case

38. Sustained economic stability, together with political and social stability, is a prerequisite for economic recovery and sustained growth. Mr. Hariri's new government has a unique window of opportunity to both undertake the ambitious task of reconstruction and lay the basis for private sector-led recovery of the Lebanese economy. The base case scenario envisages major investments for reconstruction and significant external official and private capital inflows. Private per capita consumption levels would be maintained in the medium term, and rise steadily thereafter. Debt and debt service levels would initially rise rapidly but remain at manageable levels. This scenario centers around three main elements: (i) major fiscal adjustment in 1993 and 1994 (with the elimination of the fiscal current account deficit), and the successful stabilization of the economy; (ii) implementation of the reconstruction program with large increases in public and private investments; and (iii) availability of external financing. Clearly, successful reconstruction will require very sizeable amounts of both official and private capital from abroad. Only with stabilization and fiscal adjustment is there a chance that both will materialize.

39. With important fiscal adjustment taking place in 1993/94, in the base case scenario government revenues would increase from 10% of GDP in 1992 to 18% in 1994, while current expenditures would be contained at 19% of GDP. As the NERP takes off, public capital expenditures would rise from 3% of GDP in 1992 to 8% in 1993 and an average of close to 11% during 1994-96. With the virtual elimination of the current fiscal deficit, which stood at 10% of GDP in 1992, by 1994, the overall deficit could be contained to an average of about 11% of GDP during the period of reconstruction. Real GDP growth during that period is projected at 10% in 1993, and an average of 8% during 1994-96; beyond the reconstruction period real GDP growth is projected at an average of 6% p.a. based on

relatively low aggregate levels of efficient private sector investment. Total imports would increase substantially as reconstruction takes off and exports would rise steadily as overall economic activity picks up. The current account deficit would remain large, at an average of \$2.6 billion p.a. during the reconstruction period. Projected private inflows are sizeable throughout the period of reconstruction and thereafter; this

underscores the importance of sustaining stable economic policies. Despite the projected improvement in fiscal performance, relatively sizeable amounts of external loans and grants will continue to be required to finance the reconstruction of infrastructure. Key macroeconomic indicators in the base case scenario are presented in the table below.

<b>Base Case Scenario: Key Macroeconomic Indicators (%)</b>			
	1993	1994-1996	1997-1999
GDP real growth	10.0	8.0	6.4
Private Consumption real growth	2.3	0.9	4.8
Investment/GDP of which: public investments	23.8 7.7	30.4 10.8	18.9 4.9
Current Fiscal Balance/GDP	-4.3	0.2	3.2
Overall Fiscal Balance/GDP	-12.0	-10.7	-1.7
External Public Debt Service/Exports	4.2	4.2	4.2
Current Account Balance/GDP	-35.8	-32.0	-20.5

### **Alternative Scenarios**

40. The viability of the base case scenario centers around fiscal adjustment. An alternative scenario envisions a lack of fiscal adjustment, with a likely consequence being that the level of private capital inflows would be well below the levels projected in the base case as uncertainty in the economy would prevail. A lack of fiscal adjustment would prevent the government from contributing to public investments associated with the reconstruction program; official creditors would then withdraw from the program. As a result, overall investment levels would be significantly below those under the base case scenario. GDP growth would fall, and sharp declines in consumption per capita would occur. This is the most likely outcome of a failure to implement stabilization policies.

41. If, in spite of the lack of fiscal adjustment, the government would still attempt to maintain total overall investment at levels

similar to those under the base case scenario, this would be achieved by substantially higher levels of external borrowing by the public sector. In that event, the public sector's (domestic and external) debt service would rapidly become unsustainable, as debt service payments would soon absorb most of fiscal revenues, even under favorable lending terms. Also, GDP growth would be lower than under the base case scenario, as the efficiency of incremental public investments is likely to be well below the efficiency of private capital.

### **Creditworthiness and External Capital Requirements**

42. Lebanon's total capital requirements in the medium term would amount to around \$3.0 billion per annum (see table below). The bulk of this is expected to be available from private capital inflows, including return of the flight capital and direct foreign investment. During the period of implementation of the NERP,

relatively sizeable amounts of official assistance will be needed. During the Donors meeting held in December 1991, the international donor community showed increasing interest in supporting Lebanon. The amount of loan and grant financing required during 1993-96, about \$600 million per annum, can only be raised if Arab and other donors are willing to support Lebanon. Current indications are that this may indeed be the case, but financing for the NERP will need to be confirmed in the context of a Consultative Group to be convened in late 1993.

43. In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank, and its current outstanding

obligations amount to only about \$20 million. Lebanon's external public debt was estimated at about \$360 million (8% of GDP) at the end of 1991, which is low by any standard. While the level of public debt is projected to increase five-fold to about \$1.8 billion over the next four years because of the external financing required for the NERP, debt indicators would remain low, with an external public debt to GDP ratio of less than 20% and a public debt service to exports ratio of less than 5% by the mid-1990s. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP.

<b>Base Case Scenario: External Financing Requirements (Millions of US\$ p.a.)</b>			
	1993	1994-1996	1997-1999
Current Account Deficit	2,445	2,744	2,418
Public Loan Amortization	50	50	69
Reserve Build-up	289	391	208
Total Financing	2,784	3,185	2,695
Public Grants	200	200	100
Public Loans (Gross Disbursement)	340	410	305
Private Capital Flows/Investment	2,244	2,575	2,290

### **Bank Assistance Strategy**

44. The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. In response to the government's request, the Bank assisted in the preparation of the NERP. The \$175 million Emergency Reconstruction and Rehabilitation (ERRP) Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which essential institutional and financial reform is feasible. While proceeding with the implementation of the ERRP, we would

assist the government in inducing private sector investment in the same sectors and in strengthening institutions.

45. Beyond the immediate reconstruction supported with the ERRP, the Bank has a fairly unique opportunity to play a major role in the recovery of Lebanon. While the risks involved are above average, the potential benefits of a relatively modest Bank assistance program to help a serious and strong government, that has broad domestic and regional support, lay the basis for steady recovery and mobilize external support are significant. The overall objective of Bank strategy would be the resumption of rapid economic growth and reduction of poverty. Towards these goals the Bank would support a

private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity, rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development (see attachment). The mobilization of external resources and aid coordination to achieve the overall strategy objectives would be an important element of the assistance program.

46. Future Bank lending would concentrate heavily on the social sectors. These have traditionally been neglected by Lebanese governments, in good and bad times, and this neglect in part underlies the tensions and violence that Lebanon has experienced. Ultimately, continued political stability will not be maintained unless social issues are addressed. Moreover, the services sector is undoubtedly one of the main sources for potential growth and human resources development, virtually non-existent for 15 years, would thus be a high priority. The proposed lending program includes an education project, a poverty alleviation (social fund) project, a health project, and an additional social sector project, as well as investments in social infrastructure. Specific sector work would focus on the development of a strategy for human resources development and the design of a social safety net, which becomes all the more important as economic stabilization measures are being implemented, and would also include a poverty assessment, a living standards measurement survey, and a rural development study to lay the basis for poverty alleviation programs. Bank support for the environment would include an environmental assessment, which, together with planned METAP activities, would help the government develop a comprehensive environmental strategy and lay the basis for an environmental lending operation.

47. The Bank would support the initial strengthening of the public administration through a free-standing technical assistance project to strengthen economic management and

public administration, to be followed by a more narrowly focused operation to help Lebanon establish an efficient civil service. An early strengthening of public administration is particularly important since the temporary improvements in administration that have been achieved by utilizing resources of Prime-Minister Hariri and his team do not represent a lasting and politically sustainable solution. As part of Bank support for private sector development, our initial economic and sector work would help government to establish an enabling environment for private sector development, including a legal and regulatory framework for private investment in the provision of public services, reform of the financial sector, and the development of capital markets to facilitate the mobilization and efficient allocation of resources. We would jointly with government organize a seminar ("Lebanon 2005") to develop a vision of the Lebanese economy and its future role in the region, and sector work would include a private sector assessment to be undertaken jointly between government, the private sector, and the Bank. This assessment would also focus on issues and prospects for private sector provision of infrastructure services. In physical infrastructure, the Bank would initially support selected public investments, particularly during the reconstruction and rehabilitation phase, but future expansion of physical infrastructure should be left to the private sector. The ERRP includes a technical assistance component in support of institutional and regulatory reforms in the infrastructure sectors and the design of sectoral strategies, including plans for private sector participation. The proposed ESW in support of private sector development would extend, and expand on, the initial work being undertaken. It would more specifically support corporatization and commercialisation of public institutions to allow their eventual privatization, and the reform of the legislative, contractual and regulatory frameworks to facilitate private investment in, and operation of, utilities. The proposed lending program includes a number of projects that would support private sector

development of infrastructure beyond the immediate reconstruction phase.

48. The proposed base case lending program for FY94-98 consists of three operations for an average of \$85 million per year, with some frontloading. The composition and phasing of the lending program as discussed above and shown in Annex I is tentative and subject to change based on the sector work to be initiated, the definition by the government of its priorities for Bank support, and an assessment of the availability of financing from other sources. The base case program would be conditional upon: (i) the maintenance of an acceptable overall macroeconomic framework, in particular by reducing the current imbalances through fiscal adjustment, along the lines of the base case macroeconomic scenario discussed above and the medium term scenario developed in the context of the recent IMF Article IV Consultation mission; and (ii) the availability of financing from other sources to ensure the feasibility of the overall financing scenario and adequate burden sharing. The next few months will show whether the government has the resolve to continue to take the required fiscal measures, and the Consultative Group meeting planned for late 1993 (para. 50) would confirm whether there is adequate official donor support for Lebanon. We would also need to continuously monitor the evolution of the political situation. The proposed economic and sector work program as discussed above and shown in Annex II, an average of 180 staff-weeks per year during FY94-96, is heavily frontloaded in order to rapidly develop our knowledge base, underpin proposed lending, and advise government on the design of macro- and sector policies. Because of the frontloaded nature of the economic and sector work program and the need to develop a project pipeline of the magnitude envisaged in the base case program, and undertake country work on a regular basis, total resource requirements in FY94 are estimated at 14.7 staff-years. (This includes 8.3 SY for lending, 0.9 SY for portfolio management, 4.4 SY for

ESW, and 1.1 SY for country work, aid coordination and other).

49. Lebanon's creditworthiness largely depends on the expected fiscal capacity to service its debt. The present government has made an important initial effort to reduce fiscal imbalances. If the government's commitment to fiscal adjustment were to decline, we would move to low case lending program. We would therefore closely monitor a number of indicators, including (i) the evolution of overall fiscal deficit, relative to the targets in the base case macroeconomic scenario, (ii) progress in increasing public sector revenues, which will be critical to achieving fiscal adjustment, and (iii) the mechanisms used to finance the deficit, as excessive reliance on Central Bank credit would undermine economic stability, while excessive reliance on domestic debt could crowd out the private sector. The size of the low case program would be determined in the light of events and its composition would focus more heavily on social sectors. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. At this stage, we do not propose a high case program. We plan to review the country assistance strategy in about twelve months.

#### Coordination with other Institutions

50. The government has requested the support of the Bank in mobilizing external resources for the NERP. We would convene a Consultative Group meeting provided the government continues to make satisfactory progress in mounting and implementing an appropriate macroeconomic program satisfactory to the IMF and the Bank. The recent IMF Article IV Consultation mission has made a favorable assessment of the government's economic program and has agreed with government on an informal arrangement for monitoring progress in its implementation. However, in view of the economic stabilization issues at hand, a more formal IMF program

would be desirable, and we would therefore continue to seek to convince government, which thus far has cited political constraints to a formal arrangement, to pursue this option. The presence of both the Bank and IMF is seen as an important signal to other donors, including Arab countries, and will help to increase the confidence not only of the international community but also of the Lebanese private sector. The NERP has already attracted external support from the regional funds, the EEC and EIB and a number of bilateral donors, and the Bank's role in the implementation of the NERP, through the ERRP, would ensure donor coordination. A Bank lending program of the size and composition proposed would be an important catalyst for attracting the external funding from official sources that Lebanon will require during the 1990s, particularly during the reconstruction phase; the Arab regional funds have already expressed their interest in co-financing Bank projects in Lebanon. In addition to large-scale financial support for reconstruction, Lebanon requires massive technical assistance to compensate for the absence of qualified and experienced staff who left the country during the war. The Bank would work closely with UNDP in establishing a technical assistance trust fund aimed at channeling and coordinating the technical assistance likely to be available from several multilateral and bilateral sources.

51. In promoting private sector development, the Bank would work closely with IFC, which has also reinitiated operations in FY93 and could play an important role in Lebanon given the country's traditional private sector orientation. IFC has agreed to help undertake the capital markets development component of the proposed financial sector review. IFC's strategy for Lebanon focuses on three main areas. First, invest in domestic capital markets to: (i) help the banking sector play an effective role in reconstruction by providing long-term loans to intermediaries to fund projects of small and medium-sized enterprises; (ii) provide technical assistance to government on financial markets

issues; (iii) help establish model financial intermediaries to deepen the financial system and energize capital markets; and (iv) mobilize and channel resources for the re-emerging private sector. Second, attract private capital to rehabilitate infrastructure facilities that are essential to the service economy, in particular in telecommunications, and possibly finance projects in maritime and air transport and power generation and/or distribution. Third, support viable manufacturing ventures, particularly in the construction and building materials industry that face significant demand associated with the reconstruction effort.

### **Bank Share of Financing**

52. Based on the medium-term projections underlying the base case macroeconomic scenario, with the \$175 million ERRP loan and the base case lending program as proposed, the Bank would account for about 12% of total gross public M & LT loan and grant disbursements during 1993-96. The Bank's exposure to Lebanon would be about 3% of GDP at end-1996, out of the total external public debt equal to 18% of GDP. Lebanon's external public debt, which stood at only about \$360 million at end-1991, is projected to increase five-fold during the 1993-96 period of the NERP, but public debt indicators are projected to remain at very low levels, on the assumption that a major share of the total financing needs will be met by private flows, including the repatriation of capital. By 1999, the Bank's share in total public external debt of \$2.4 billion (18% of GDP) would amount to 20%. As a significant portion of projected official assistance is expected to come from regional banks, the share of preferred creditors in total public debt would be around two-thirds.

53. Lebanon's stock of external public debt would remain small by any standard, while its reserve position - currently about \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. With fiscal adjustment along the lines projected, virtual elimination of the current



deficit (10% of GDP in 1992) within two years and of the overall deficit by 1999 (with most of the reduction after 1996 representing the completion of the NERP), there would be adequate fiscal capacity to service the external and domestic debt to be contracted by the public sector during 1993-99, in particular during 1993-96. In view of Lebanon's past track record with the Bank and the government's commitment to fiscal stabilization and reconstruction, the amounts of planned lending are considered prudent.

### **Downside Risks**

54. The main risks are the failure by the government to establish and maintain a viable macroeconomic framework and political stability, and the security situation. Lebanon's track record of macroeconomic management in past years has not been favorable, due in large part to the protracted hostilities and their aftermath. Lebanon's current economic stability is not sustainable in the absence of action to correct macroeconomic imbalances, in particular the fiscal deficit. In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The present government is aware that the short term stability that has been achieved is tenuous and delicate.

55. The question of political stability is very much related to the need to ensure economic stability. If the stabilization and reconstruction programs were to fail, the current government would find itself under significant pressure to resign. Successful implementation of the programs represents a significant challenge. Unfulfilled expectations and the need to carefully balance the interests of the various denominational factions could hamper the government from taking the ambitious and

difficult measures that are required. The population has very high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war. However, the new government is judged to have the best chance in many years to provide a measure of macroeconomic stability and to foster confidence in the private sector. It is well aware that economic stabilization is a pre-condition for sustained, private sector-led recovery. It has begun taking measures to reduce the fiscal deficit and has stated that restoration of fiscal balance is a priority objective. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

56. External events, particularly regional developments, could upset hard-won stability. The Syrian army continues to play an important security role in most of the country, while in the South, Israel and the Southern Lebanese Army occupy part of the country's territory. If the peace process were to fail, there could be far reaching implications for Lebanon. Conversely, if the process were to be successful, prospects for a prosperous Lebanon as a regional trade and services center would be enhanced.

**LEBANON**  
**OBJECTIVES AND INSTRUMENTS OF COUNTRY ASSISTANCE STRATEGY, FY94-98**

<i>OBJECTIVES</i>	<i>INSTRUMENTS</i>	<i>COMMENTS</i>
<p><b>A. Macroeconomic stabilization/ Fiscal reform and adjustment.</b></p>	<ul style="list-style-type: none"> <li>• <i>Formulation of macroeconomic framework for stabilization jointly with IMF.</i></li> <li>• <i>Technical assistance project for economic management.</i></li> <li>• <i>Financial sector review and macroeconomic assessment, PSER, CEM, and other economic work.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>CEM issued March 1993, recommended stabilization measures.</i></li> <li>• <i>IMF conducted Article IV Consultation in May 1993 and made favorable assessment of government economic program.</i></li> </ul>
<p><b>B. Reconstruction of infrastructure.</b></p>	<ul style="list-style-type: none"> <li>• <i>Implementation of ERRP.</i></li> <li>• <i>CG meeting to mobilize external resources.</i></li> <li>• <i>Lending for social and physical infrastructure (solid waste, irrigation, water, housing, and transport).</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ERRP is part of NERP, to be implemented during 1993-1996.</i></li> <li>• <i>CG planned for November 1993.</i></li> </ul>
<p><b>C. Private-Sector led economic recovery.</b></p>	<ul style="list-style-type: none"> <li>• <i>Financial sector review.</i></li> <li>• <i>Private sector assessment.</i></li> <li>• <i>Lending for private sector investment in utilities.</i></li> <li>• <i>Technical assistance for capital market development (with IFC involvement), and legal, regulatory, and administrative reforms as part of T.A. projects.</i></li> <li>• <i>Conference on long-term vision for Lebanon planned for September 1993.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ESW heavily frontloaded in FY94.</i></li> </ul>
<p><b>D. Rebuilding of public administration.</b></p>	<ul style="list-style-type: none"> <li>• <i>Technical assistance projects for economic management and for strengthening of public administration/civil service reform.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>Coordinating with UNDP and IMF.</i></li> </ul>
<p><b>E. Development of social sectors/Human resources development/Alleviation of poverty/Environment.</b></p>	<ul style="list-style-type: none"> <li>• <i>Lending - Education / Poverty Alleviation / Health / Solid Waste / Environment / Water / Housing / Integrated Rural Development.</i></li> <li>• <i>Human resources sector work, including design of a social safety net, poverty assessment, and LSMS. Rural development study.</i></li> <li>• <i>Environmental assessment.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>First human resources sector mission in May, 1993.</i></li> <li>• <i>Elimination of inflation tax and generation of incomes through stabilization and economic recovery.</i></li> </ul>

## LEBANON

## FY93-98 Base Case Lending Program

<b>Fiscal Year</b>	<b>Project</b>	<b>US\$ Million</b>
<b>FY93</b>	Emergency Reconstruction & Rehabilitation	175
	<b>TOTAL</b>	175
<b>FY94</b>	Technical Assistance for Economic Management & Public Administration	10
	Emergency Education	50
	Irrigation Rehabilitation	30
	<b>TOTAL</b>	90
<b>FY95</b>	Poverty Alleviation	35
	Solid Waste/Environment	35
	Health	30
	<b>TOTAL</b>	100
<b>FY96</b>	Water Supply S	30
	Public Administration/Civil Service Reform S	15
	Private Sector Infrastructure Development	40
	<b>TOTAL</b>	85
<b>FY97</b>	Housing S	25
	Transport S	30
	Integrated Rural Development	25
	<b>TOTAL</b>	80
<b>FY98</b>	Social Sectors	40
	Private Sector Development II	30
	<b>TOTAL</b>	70

## LEBANON

Economic & Sector Work Program, FY93-96

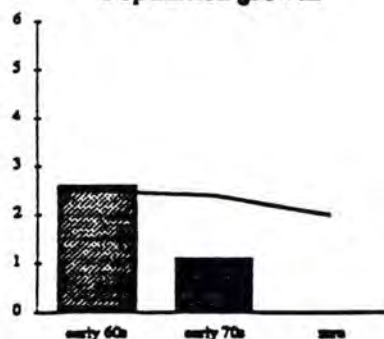
<b>Fiscal Year</b>		<b>Staff Weeks</b>
<b>FY93</b>	CEM	70
	EWO	15
	Human Resources/Poverty Assessment*	20
	<b>TOTAL</b>	<b>105</b>
<b>FY94</b>	Financial Sector Review/Macro-Assessment	70
	Private Sector Assessment*	60
	Human Resources/Poverty Assessment	50
	Environmental Assessment*	10
	EWO/SWO	40
	<b>TOTAL</b>	<b>230</b>
<b>FY95</b>	Public Sector Expenditure Review	60
	Private Sector Assessment	20
	Environmental Assessment	20
	Poverty/LSMS*	10
	EWO/SWO	40
	<b>TOTAL</b>	<b>160</b>
<b>FY96</b>	CEM	60
	Poverty/LSMS	30
	Rural Development Study	30
	EWO/SWO	40
	<b>TOTAL</b>	<b>160</b>

\* To be completed in subsequent FY

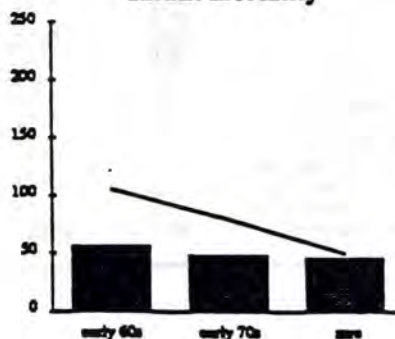
## Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>HUMAN RESOURCES</b>							
Size, growth, structure of population							
Total population (mre = ...)	thousands	2,151	2,767		256,356	629,102	458,731
14 and under	% of pop.	43.6	41.2	36.5	42.8	37.3	33.8
15-64		51.2	53.9	57.8	53.2	57.8	60.9
Age dependency ratio	unit	0.95	0.86	0.73	0.86	0.72	0.63
Percentage in urban areas	% of pop.	49.5	68.6	83.7	55.3	58.6	71.8
Females per 100 males	number						
Urban		..	..	..	..	..	..
Rural		..	..	..	..	..	..
Population growth rate	annual %	2.6	1.1	-0.1	2.9	2.0	1.7
Urban		6.7	3.8	0.6	4.1	3.2	2.8
Urban/rural growth differential	difference	7.9	8.3	4.7	2.6	2.4	3.6
Projected population: 2000	thousands	..	..	3,013	340,932	768,976	541,229
Stationary population		..	..	6,044	..	..	..
Determinants of population growth							
Fertility							
Crude birth rate	per thou. pop.	40.4	30.9	30.2	39.3	29.5	24.9
Total fertility rate	births per woman	6.17	4.55	3.62	5.39	3.74	3.10
Contraceptive prevalence	% of women 15-49	..	55.0	..	..	..	..
Child (0-4) / woman (15-49) ratios							
Urban	per 100 women	..	..	..	..	..	..
Rural		..	..	..	..	..	..
Mortality							
Crude death rate	per thou. pop.	12.4	8.9	8.8	10.1	8.5	7.5
Infant mortality rate	per thou. live births	56.0	48.0	45.8	79.5	49.5	41.3
Under 5 mortality rate		..	..	59.0	87.8	79.5	49.8
Life expectancy at birth: overall	years	62.0	65.0	65.5	60.5	65.3	68.3
female		63.9	67.0	67.5	62.2	67.9	71.5
Labor force (15-64)							
Total labor force	thousands	578	771	914	70,804	237,840	172,535
Agriculture	% of labor force	29.2	17.0	..	..	..	..
Industry		24.0	26.3	..	..	..	..
Female		16.1	20.5	27.8	14.6	32.3	30.4
Females per 100 males	number	..	..	..	..	..	..
Urban		..	..	..	..	..	..
Rural		..	..	..	..	..	..
Participation rate: overall	% of labor force	26.9	27.9	30.8	28.5	40.6	38.5
female		8.7	11.5	16.6	8.5	25.6	23.3
Educational attainment of labor force							
School years completed: overall	years	..	..	..	..	..	..
male		..	..	..	..	..	..
<b>NATURAL RESOURCES</b>							
Area	thou. sq. km	10.40	10.40	10.40	11,667	22,765	18,709
Density	pop. per sq. km	207	266	258	21	27	24
Agricultural land	% of land area	29.4	33.2	29.9	27.5	40.9	34.3
Agricultural density	pop. per sq. km	703	802	863	78	66	70
Forests and woodland	thou. sq. km	0.95	0.90	0.80	413	6,174	7,116
Deforestation rate (net)	annual %	0.0	0.0	0.0	0.5	-0.5	-0.5
Access to safe water	% of pop.	..	..	..	..	..	80.0
Urban		..	..	..	..	78.2	88.7
Rural		..	..	77.0	..	46.9	63.8

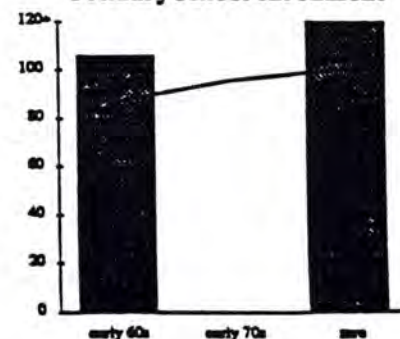
Population growth



Infant mortality



Primary school enrollment



■ Lebanon — Lower-middle-income

Note: Extreme values for population growth are unshaded.

## Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>INCOME AND POVERTY</b>							
<b>Income</b>							
GNP per capita (mre = ...)	US\$	--	--	--	1,830	1,530	3,450
Total household income							
Share to top 10% of households	% of income	--	--	--	--	--	--
Share to top 20% of households	"	--	--	--	--	--	--
Share to bottom 40% of households	"	--	--	--	--	--	--
Share to bottom 20% of households	"	--	--	--	--	--	--
<b>Poverty</b>							
Absolute poverty income: urban	US\$ per person	--	--	--	--	--	--
rural		--	219	--	--	--	--
Pop. in absolute poverty: urban	% of pop.	--	--	--	--	--	--
rural		--	--	--	--	--	--
Prevalence of malnutrition (under 5)	% of age group	--	--	--	--	--	--
<b>EXPENDITURE</b>							
Food	% of GDP	--	--	--	--	--	--
Staples		--	--	--	--	--	--
Meat, fish, milk, cheese, eggs	"	--	--	--	--	--	--
Cereal imports	thou. metric tonnes	401	585	356	39,093	38,868	39,280
Food aid in cereals		--	26	16	--	--	--
Food production per capita	1979-81=100	93.7	84.3	136.6	108.6	98.9	106.0
Share of agriculture in GDP	% of GDP	11.6	9.2	--	14.3	16.8	9.0
Daily calorie supply	calories per person	2,485	2,453	3,274	3,012	2,780	3,013
Daily protein supply	grams per person	67	61	86	79	72	77
Housing	% of GDP	--	--	--	--	--	--
Average household size	persons per household	--	--	--	--	--	--
Urban		--	--	--	--	--	--
Fixed investment: housing	% of GDP	--	--	--	--	--	--
Fuel and power	% of GDP	--	--	--	--	--	--
Energy consumption per capita	kg of oil equivalent	712.9	825.0	968.5	1,048.2	1,102.2	1,794.4
Households with electricity	% of households	--	--	--	--	--	--
Urban		--	--	--	--	--	--
Rural		--	--	--	--	--	--
Transport and communication	% of GDP	--	--	--	--	--	--
Population per passenger car	persons	22	12	--	67	24	11
Fixed investment: transport equipment	% of GDP	--	--	--	--	--	--
Total road length	km	--	--	--	--	--	--
Population per telephone	persons	--	--	--	--	--	--
<b>INVESTMENT IN HUMAN CAPITAL</b>							
Medical care	% of GDP	--	--	--	--	--	--
Population per: physician	persons	1,006	--	--	1,333	--	--
nurse		2,029	965	--	--	--	--
hospital bed		--	--	--	--	--	--
Access to health care	% of pop.	--	--	--	--	--	--
Immunized (under 12 months): measles	% of age group	--	--	15.0	78.9	65.3	78.5
DPT		--	--	33.0	84.8	67.1	81.5
Oral Rehydration Therapy use (under 5)	% of cases	--	--	10.0	45.4	39.8	--
Education	% of GDP	--	--	--	--	--	--
Gross enrollment ratios							
Primary: total	% of school-age group	106.0	--	128.0	89.7	100.5	105.9
female		93.0	--	94.0	81.2	97.4	--
Secondary: total		26.0	50.0	67.0	54.3	58.3	56.3
female		20.0	--	56.0	51.2	56.5	58.9
Tertiary: science/engineering	% of tertiary students	8.1	--	17.7	--	--	--
Pupil-teacher ratio: primary	pupils per teacher	24	10	6	22	26	25
secondary		17	--	--	20	18	--
Pupils reaching grade 4	% of cohort	--	--	--	--	86.7	77.8
Repeater rate: primary	% of total enrollment	--	--	--	10.2	6.6	17.6
Illiteracy rate: overall	% of pop. (age 15+)	--	--	19.9	47.0	22.9	15.1
female		--	--	26.9	59.5	28.8	17.7
Newspaper circulation	per thou. pop.	83.7	102.3	88.1	35.4	72.0	100.9

Source: World Bank International Economics Department, April 1992.

4:09 PM  
11 May 1993

Lebanon: Key Indicators

	+-----Estimate-----+		+-----Projected-----+							
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
<b>Real Growth Rates:</b>										
Gross Domestic Product (GDP)	-13.4	50.2	10.0	10.0	8.0	8.0	8.0	8.0	5.7	5.5
Gross Domestic Income (GDI)	-13.9	49.7	9.8	10.0	8.0	8.1	8.1	8.1	5.8	5.7
<b>Real Per Capita Growth Rates:</b>										
Gross Domestic Product (GDP)	-15.1	47.3	7.8	7.8	5.9	5.9	5.9	5.9	3.8	3.6
Total Consumption	-8.5	53.6	4.9	1.1	-4.0	1.0	1.3	7.1	0.7	0.3
Private Consumption	-11.1	56.4	6.0	0.2	-5.1	0.5	1.4	7.6	0.6	0.3
<b>External Debt &amp; D. Services (LT+ST+IMF):</b>										
Total External Public Debt (US\$M)	0.0	360.7	296.6	586.6	926.6	1301.6	1666.6	1921.3	2145.7	2374.0
Public Sector External Debt Service (US\$)	14.2	3.7	100.2	70.8	90.1	117.3	150.3	189.5	225.6	240.2
Public Sector Debt Service / Exports	1.7	0.3	7.6	4.2	4.1	4.0	4.1	4.1	4.3	4.1
Public Sector Debt Service / GDP	0.6	0.1	1.8	1.0	1.2	1.4	1.6	1.8	1.9	1.9
<b>Interest Burden (LT+ST+IMF):</b>										
Public Sector Interest Paid (US\$M)	14.2	3.7	36.0	20.8	40.1	67.3	100.3	129.2	149.9	168.6
Public Sector Interest / Exports	1.7	0.3	2.7	1.2	1.8	2.3	2.7	2.8	2.9	2.9
Public Sector Interest / GDP	0.6	0.1	0.6	0.3	0.5	0.8	1.0	1.2	1.3	1.3
<b>Gross Investment / GDP</b>										
ICOR (annual)	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
ICOR (5-yr ending year shown)	-1.5	0.4	2.0	2.3	3.5	4.5	4.7	4.2	4.2	4.0
<b>Domestic Savings / GDP</b>										
BOP Resource Balance / GDP	-46.4	-45.0	-35.2	-25.3	-14.9	-10.3	-7.0	-9.1	-6.7	-4.1
<b>National Savings / GDP</b>										
BOP Current Account Balance / GDP	-66.4	-65.0	-54.9	-49.1	-45.5	-42.4	-35.6	-29.3	-25.4	-21.8
<b>Government Investment / GDP</b>										
Government Savings / GDP	-4.0	-22.7	-20.1	-12.0	-3.8	-1.2	0.1	-3.4	-1.9	0.2
Private Investment / GDP	-24.0	-42.7	-39.8	-35.8	-34.4	-33.2	-28.5	-23.6	-20.6	-17.5
Private Savings / GDP	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Government Expenditures / GDP	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Budget Deficit (+) or Surplus / GDP	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8
Primary Deficit (+) or Surplus / GDP	31.3	-8.2	-10.1	-7.7	-2.8	-1.3	-1.1	-5.9	-5.0	-3.7
<b>Government Revenues / GDP</b>										
Government Expenditures / GDP	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Budget Deficit (+) or Surplus / GDP	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
Primary Deficit (+) or Surplus / GDP	38.1	19.3	13.1	12.0	11.5	10.7	9.8	2.4	1.8	1.1
<b>GDP Deflator (% growth rate)</b>										
	25.9	14.2	7.7	6.6	6.9	6.0	5.0	-1.4	-1.5	-1.7
	68.8	51.7	116.1	25.0	10.0	10.0	10.0	6.0	5.2	3.8

4:09 PM  
11 May 1993

Lebanon: Key Indicators

	+-----Estimate-----+		+-----Projected-----+							
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Continued										Continued
Real Exchange Rate (LL / US\$) (1990=100)	100.0	88.9	76.7	72.5	72.5	72.5	72.5	72.5	72.5	72.5
Terms of Trade Index (1990=100)	100.0	98.8	98.3	98.4	98.7	99.2	99.4	99.7	99.9	100.1
Export (GNFS)/Volume Growth Rate	-3.7	24.4	23.3	21.8	25.5	27.3	22.0	19.0	9.6	7.4
Exports (GNFS) / GDP	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports (GNFS) Volume Growth Rate	0.7	51.1	11.8	9.5	8.7	11.1	4.8	4.7	2.4	1.4
Imports (GNFS) / GDP	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Current Account Balance (US\$M)										
(before grants)	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
(after grants)	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
BdL Foreign Exchange Reserves (US\$M)	620.0	1233.3	1448.0	1737.1	2081.0	2539.3	2911.2	3161.4	3359.6	3535.5
Official Reserves (months imports) 7/	3.1	3.9	4.0	4.3	4.5	4.8	5.0	5.0	5.0	5.0

1. "LT" denotes "long-term debt;" "ST" denotes "short-term debt"
2. "DOD" denotes "debt outstanding and debt disbursed."
3. "ICOR" denotes "incremental capital output ratio" with a 5-years period.
4. "BOP" denotes "balance of payments"
5. Current account balance as defined in line F.1 on annex B3
6. "GNFS" denotes "goods and nonfactor service".
7. Excludes gold.



4:08 PM  
11 May 1993

Projection Table 1. Balance of Payments  
(in millions of US\$)

	1989	1990	1991	-----Projected-----							
				1992	1993	1994	1995	1996	1997	1998	1999
	(US\$ millions)										
Resource Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Merchandise Trade Balance	-1707.0	-1859.0	-2997.0	-3322.1	-3719.0	-4069.7	-4540.9	-4744.2	-4926.9	-5132.7	-5264.1
Merchandise Exports	539.0	537.0	750.0	987.0	1185.7	1479.5	1874.2	2242.6	2660.4	2930.4	3221.2
Merchandise Imports	2246.0	2396.0	3747.0	4309.1	4904.7	5549.2	6415.2	6986.9	7587.3	8063.1	8485.3
Net Nonfactor Services	200.0	200.0	200.0	222.0	365.6	583.8	903.0	1314.5	1761.5	2120.1	2433.7
Exports of Nonfactor Services	300.0	300.0	300.0	338.2	491.9	715.5	1039.8	1457.1	1920.8	2292.9	2618.0
Imports of Nonfactor Services	100.0	100.0	100.0	116.2	126.3	131.7	136.8	142.6	159.3	172.8	184.3
Net Factor Income	507.0	479.0	480.0	453.9	458.8	371.6	287.2	164.0	69.2	-2.8	-36.0
Net Current Transfers	680.0	580.0	480.0	400.0	450.0	475.0	500.0	525.0	550.0	575.0	600.0
Current Account Balance (before grants)	-320.0	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
Capital Official Grants	0.0	0.0	70.7	0.0	200.0	200.0	200.0	200.0	100.0	100.0	100.0
Current Account Balance (after grants)	-320.0	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
Direct Foreign Investment	0.0	0.0	0.0	0.0	300.0	800.0	800.0	800.0	500.0	500.0	500.0
Public M&LT (net disbursement)											
Gross Disbursement	..	..	..	0.0	340.0	390.0	425.0	415.0	315.0	300.0	300.0
Amortization	..	..	..	-64.2	-50.0	-50.0	-50.0	-50.0	-60.3	-75.6	-71.7
Net Disbursement	14.1	23.1	33.9	-64.2	290.0	340.0	375.0	365.0	254.7	224.4	228.3
Net Other Capital Flows 1/	262.9	279.9	2301.4	2525.1	1943.7	1643.3	1934.1	1747.6	1941.6	1814.3	1613.9
Overall Balance 2/	-43.0	-297.2	569.0	214.7	289.1	343.9	458.4	371.9	250.2	198.2	175.9
Increase in Bdl Reserves	43.0	297.2	-569.0	-214.7	-289.1	-343.9	-458.4	-371.9	-250.2	-198.2	-175.9

Sources: Data provided by the Bank of Lebanon; IMF, Direction of Trade;  
and staff estimates and projections.

1/: Comprised of net private medium and long term debt, net short term capital, trade credits, unidentified capital flows, and errors and omissions.  
2/: Includes only non-gold reserves of the Bdl.

Elasticity of total imp. to GDP growth rate/growth rate adjusted for Real Exchange Rate	-0.05	1.02	1.18	0.95	1.09	1.39	0.60	0.58	0.43	0.26	
Elasticity of NonInv.imports to GDP adjusted for Real Exchange Rate	-0.05	1.01	0.25	0.25	0.05	0.00	0.05	0.95	0.80	0.50	
Average Exchange Rate	496.5	701.8	928.2	1683.0	1912.8	2025.1	2146.1	2274.3	2322.5	2353.8	2353.8

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	Actual					Projection					
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
	(In billions of Lebanese Pounds)										
<b>Total Revenue</b>	62.6	126.4	456.7	984.0	2100.0	2794.1	3405.2	4164.9	4768.0	5299.3	5803.2
<b>Total Expenditure 1/</b>	534.7	794.5	1229.1	2229.3	3662.1	4571.4	5378.2	6314.2	5368.2	5803.9	6124.6
<b>Current Expenditures</b>	495.0	745.2	1036.6	1929.3	2657.2	2945.6	3374.9	3885.8	4130.4	4428.3	4618.1
<b>Wages &amp; Salaries</b>	96.9	210.0	370.0	738.9	887.0	1064.4	1224.1	1370.9	1480.6	1584.3	1663.5
<b>Other Current (incl. Transfers)</b>	58.3	96.7	240.6	425.8	875.1	1039.6	1235.0	1467.2	1704.7	1922.6	2105.4
<b>Extrabudgetary Transfers</b>	88.3	179.0	184.0	90.0	117.0	100.0	50.0	0.0	0.0	0.0	0.0
<b>Petroleum Subsidy</b>	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
<b>Interest Payments</b>	152.2	213.5	206.9	514.6	698.2	711.6	865.8	1047.7	945.1	921.5	849.3
<b>Private Sector Credit</b>	151.5	203.5	203.5	454.0	658.5	630.4	721.4	819.7	645.1	568.5	452.5
<b>Foreign Sector Interest</b>	0.7	10.0	3.4	60.6	39.7	81.1	144.5	228.0	300.0	352.9	396.8
<b>Capital Expenditures 2/</b>	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
<b>of which Reconstruction Program:</b>											
<b>in Lebanese Pounds</b>					573.8	1113.8	1394.9	1705.7			
<b>in US Dollars</b>					300.0	550.0	650.0	750.0			
<b>Current Budget Balance</b>	-432.4	-618.8	-579.9	-945.3	-557.2	-151.5	30.2	279.0	637.5	871.0	1185.1
<b>Overall Deficit</b>	-472.1	-668.1	-772.4	-1245.3	-1562.1	-1777.3	-1973.0	-2149.3	-600.2	-504.6	-321.4
<b>Financing</b>	472.1	668.1	772.4	1245.3	1562.1	1777.3	1973.0	2149.3	600.2	504.6	321.4
<b>External</b>	7.0	16.2	97.1	-108.0	937.3	1093.6	1234.0	1285.0	823.8	763.5	772.8
<b>Net Borrowing</b>	7.0	16.2	31.5	-108.0	554.7	688.5	804.8	830.1	591.5	528.2	537.5
<b>Grants</b>	0.0	0.0	65.6	0.0	382.6	405.0	429.2	454.9	232.2	235.4	235.4
<b>Domestic</b>	465.1	651.9	675.3	1353.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
<b>Net Bank of Lebanon</b>	134.2	351.9	-424.2	-577.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Net Other 3/</b>	330.9	300.0	1099.5	1930.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
<b>Memorandum Items:</b>											
<b>Domestic Public Debt</b>	..	..	..	4115.4	4740.2	5424.0	6163.0	7027.3	6803.7	6544.8	6093.4
<b>External Public Debt</b>	0.0	0.0	317.1	548.8	1158.5	1932.4	2876.7	3830.4	4492.2	5050.4	5647.1
<b>Total Public Debt</b>	..	..	..	4664.2	5898.7	7356.4	9039.7	10857.7	11295.9	11595.3	11740.5

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	1989	Actual 1990	1991	1992	1993	1994	Projection				
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
(In percent of GDP)											
Total Revenue	5.2	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Total Expenditure	44.6	45.3	30.8	23.5	28.0	29.5	29.2	28.8	21.4	20.8	20.1
Current Expenditure	41.3	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
Capital Expenditure	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
of which: Reconstruction Program					4.4	7.2	7.6	7.8			
Current Budget (- deficit)	-36.1	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Overall Deficit	-39.4	-38.1	-19.3	-13.1	-12.0	-11.5	-10.7	-9.8	-2.4	-1.8	-1.1
(In percent of Total Expenditure)											
Total Revenue	11.7	15.9	37.2	44.1	57.3	61.1	63.3	66.0	88.8	91.3	94.8
Overall Deficit	-88.3	-84.1	-62.8	-55.9	-42.7	-38.9	-36.7	-34.0	-11.2	-8.7	-5.2
Memorandum Items: (In billions of Lebanese Pounds)											
Nominal GDP	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
(In percent of GDP)											
Domestic Public Debt	..	..	..	43.3	36.3	35.0	33.4	32.1	27.1	23.5	20.0
External Public Debt	0.0	0.0	7.9	5.8	8.9	12.5	15.6	17.5	17.9	18.1	18.5
Total Public Debt	..	..	..	49.1	45.2	47.4	49.0	49.6	45.1	41.6	38.5

Sources: Data provided by the Lebanese authorities; and staff estimates and projections.

a/: Central Budget, Extra budgetary Accounts, Annexed Budgets and CDR.

1/: Includes net lending.

2/: Includes domestic financing of CDR capital expenditures assumed to have come through transfers from the central government.

The 1992 value is based on the proposed budget of 1992.

3/: Comprised of net commercial banks and non-bank public.

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

National Account, Estimates and Projections: 1990-1999 (in billions of current Lebanese Pound)											
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
GDP at market prices	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
Net Indirect Taxes	-95.7	-42.3	96.5	282.5	888.0	1288.9	1659.0	1970.9	2256.3	2507.7	2746.1
Indirect Taxes	3.6	3.7	131.6	442.5	968.0	1318.9	1659.0	1970.9	2256.3	2507.7	2746.1
Subsidies	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
GDP at factor cost	1294.4	1795.1	3898.6	9216.2	12172.7	14227.3	16774.2	19927.7	22813.2	25355.5	27766.6
Resource Balance	-748.2	-1164.2	-2596.3	-5217.4	-6414.4	-7059.4	-7807.3	-7800.1	-7351.5	-7091.1	-6662.0
Total Imports	1164.8	1751.6	3570.9	7447.7	9623.3	11504.6	14061.0	16214.2	17991.1	19385.5	20406.3
Total Exports	416.6	587.4	974.6	2230.3	3208.9	4445.2	6253.7	8414.1	10639.7	12294.4	13744.3
Total Expenditures	1946.9	2917.0	6591.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Total Consumption	1707.2	2566.5	5792.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Government Consumption	124.4	255.5	483.3	944.9	1324.5	1636.2	1965.1	2251.3	2503.5	2737.8	2926.7
Private Consumption	1582.8	2310.9	5309.0	11899.4	15037.6	16184.5	18375.5	21184.0	24853.4	26998.4	28845.5
Gross Domestic Investment	239.7	350.6	799.0	1871.8	3113.0	4754.9	5899.9	6263.4	5064.1	5218.1	5402.6
Government	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
Private	200.0	301.3	606.5	1571.8	2108.2	3129.0	3896.6	3835.1	3826.3	3842.4	3896.1
(In Millions of Current US Dollars)											
Memorandum Items:											
GDP at Market Prices	2414.3	2497.7	4304.0	5643.9	6828.0	7661.9	8589.3	9628.9	10794.4	11837.6	12963.3
Per Capita GDP	677.6	687.1	1160.7	1492.2	1769.9	1947.1	2140.0	2352.0	2585.0	2784.7	2995.6
Merchandise Trade Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Exports	839.0	837.0	1050.0	1325.2	1677.6	2195.0	2914.0	3699.7	4581.2	5223.3	5839.2
Imports	2346.0	2496.0	3847.0	4425.2	5031.0	5681.0	6552.0	7129.4	7746.6	8235.9	8669.6

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
National Account, Estimates and Projections: 1990-1999 (in billions of constant 1990 Lebanese Pound)											
GDP at market prices	2023.8	1752.8	2633.1	2896.4	3186.1	3441.0	3716.2	4013.5	4334.6	4579.5	4831.4
Resource Balance	-1129.4	-1164.2	-1915.3	-2057.6	-2140.7	-2141.7	-2156.8	-1959.7	-1744.6	-1604.6	-1458.8
Exports	610.1	587.4	730.6	900.9	1097.5	1377.8	1753.7	2139.8	2546.6	2790.6	2998.5
Imports	1739.5	1751.6	2645.9	2958.5	3238.2	3519.4	3910.5	4099.5	4291.2	4395.2	4457.2
Total Consumption	2748.4	2566.5	4021.8	4302.4	4434.7	4343.9	4475.8	4624.7	5050.6	5176.6	5285.2
Government Consumption	200.2	255.5	335.6	316.5	359.0	398.8	432.4	444.3	462.2	476.6	486.9
Private Consumption	2548.2	2310.9	3686.2	3985.8	4075.7	3945.0	4043.4	4180.4	4588.4	4700.0	4798.4
Gross Domestic Investment	404.8	350.6	526.6	651.7	892.1	1238.7	1397.3	1348.5	1028.6	1007.5	1004.9
Government	67.0	49.3	126.9	104.5	288.0	423.6	474.4	522.8	251.4	265.6	280.2
Private	337.7	301.3	399.7	547.2	604.1	815.2	922.9	825.7	777.2	741.9	724.7
Memorandum Item: Per Capita Real GDP	568.0	482.2	710.1	765.8	825.9	874.5	925.9	980.4	1038.0	1077.3	1116.4
(in percent of GDP)											
Resource Balance	-62.4	-66.4	-65.0	-54.9	-49.1	-45.5	-42.4	-35.6	-29.3	-25.4	-21.8
Exports	34.8	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports	97.2	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Total Consumption	142.4	146.4	145.0	135.2	125.3	114.9	110.3	107.0	109.1	106.7	104.1
Government Consumption	10.4	14.6	12.1	9.9	10.1	10.5	10.7	10.3	10.0	9.8	9.6
Private Consumption	132.0	131.8	132.9	125.3	115.1	104.3	99.7	96.7	99.1	96.9	94.5
Gross Domestic Investment	20.0	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
Government	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Private	16.7	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8

**The World Bank**  
Washington, D.C. 20433  
U.S.A.

Office of the President

September 1, 1993

To: Distribution

Attached for your information are the Issues for Discussion for the Lebanon Country Strategy Note. The review meeting will be held September 3, at 3:30 p.m. in Conference Room E-1208.

*Orsalia Kalantzopoulos*  
Orsalia Kalantzopoulos

**Attachment**

Messrs. **Karaosmanoglu**, Stern, Sandstrom, Choksi, Koch-Weser, Linn, Bruno, Serageldin, Shihata, Rischard, Ryrie, McHugh, Chopra

LEBANON - COUNTRY STRATEGY NOTE

Issues for Discussion

The Political Landscape

The Country Strategy Note is a well-written paper that makes the case for increased Bank involvement in Lebanon. The suggested update within twelve months seems appropriate. Still, Lebanon's economic performance is highly dependent on domestic and regional political developments. What are the latest views on the prospects for a more stable political environment?

Macroeconomic Management

The development scenario presented in the CSN is based upon an ambitious program of fiscal adjustment and macroeconomic stabilization. Has recent macroeconomic management and performance been in line with the fiscal adjustment scenario envisaged under the CSN? Is there sufficient evidence of commitment to fiscal reform for initiating the base case lending program? Did recent hostilities affect fiscal performance, inflation and growth?

Political uncertainties in the Region introduce important political and economic risks. What specific monitorable criteria would be used as indicators for switching to a low case lending scenario? What would be the size and composition of a low case program?

Investment and Capital Inflows

Renewed confidence in the country's political and economic management is expected to generate massive capital inflows from Lebanese living overseas. While capital inflows are indeed welcome, the projected magnitude of these inflows in relation to investment and GDP raises questions. With projected negative savings rates and consumption on average at about 111% of GDP, substantial part of capital inflows would be financing current consumption. Could the Region comment on the macroeconomic sustainability of this pattern of external finance -- which is projected to continue for sometime into the future -- and its implications for economic policy and performance.

Public Expenditures and Poverty

Lebanon has major physical and social infrastructure needs. Does the current composition of government expenditure reflect priorities between infrastructure improvement and provision of social services? Would the planned poverty assessment focus on the income distribution and social indicator disparities among different ethnic and religious population groups? Is military spending still an important component of government expenditures?

The World Bank/IFC/MIGA  
OFFICE MEMORANDUM

DATE: July 29, 1993 07:29pm

TO: See Distribution Below

FROM: Orsalia Kalantzopoulos, EXC ( ORSALIA KALANTZOPOULOS )

EXT.: 82636

SUBJECT: Lebanon: Review of Country Strategy Note

You are invited to a meeting chaired by Mr. Karaosmanoglu to review the Lebanon Country Strategy Note. The meeting will be held on Friday, September 3, 1993 at 3:30 p.m., in Room E-1208.

DISTRIBUTION:

TO: Caio Koch-Weser	( CAIO KOCH-WESER )
TO: Johannes Linn	( JOHANNES LINN )
TO: Ibrahim Shihata	( IBRAHIM SHIHATA )
TO: Ismail Serageldin	( ISMAIL SERAGELDIN )
TO: Armeane Choksi	( ARMEANE CHOKSI )
TO: William Ryrie	( WILLIAM RYRIE )
TO: Jean-Francois Rischard	( JEAN-FRANCOIS RISCHARD )
TO: D. C. Rao	( D. C. RAO )
TO: Attila Karaosmanoglu	( ATTILA KARAOSMANOGLU )
TO: Sven Sandstrom	( SVEN SANDSTROM )
TO: Ernest Stern	( ERNEST STERN )
TO: Matthew McHugh	( MATTHEW MCHUGH )
TO: Ram K. Chopra	( RAM K. CHOPRA )
CC: Jane Armitage	( JANE ARMITAGE )
CC: Institutional ISC Files	( INSTITUTIONAL ISC FILES )



File  
Lebanon

A. KARAOSMANOĞLU  
Managing Director

September 10, 1993

Mr. Caio Koch-Weser

Re: Lebanon Country Strategy

As we discussed, while the proposed strategy for Lebanon is sound and the lending program addresses the most crucial country needs, the macroeconomic and political uncertainties facing the country are still significant. The policy dialogue should aim at focussing the Government's full attention on the guiding principles of the Bank's strategy of fiscal discipline and increased attention to poverty alleviation across regions and ethnic groups.

As we agreed, the Bank will proceed with caution and flexibility, monitoring closely macroeconomic and political developments. Before convening a Consultative Group meeting, the Region should be confident that the Government shares the Bank's stabilization and poverty objectives. We will reassess our strategy in about one year, in light of macroeconomic and political developments, and in the context of a country strategy update.

*A. Karaosmanoglu*

cc: Messrs. Preston, Sandstrom, Stern, Bruno, Choksi, Husain, Jaycox, Kaji, Linn, Rischard, Ryrie, Serageldin, Thalwitz, Wood, McHugh, Chopra

1993 ANNUAL MEETINGS BRIEF

Name of Country: Republic of Lebanon      Date: September 7, 1993

Meeting with: H. E. Fuad Siniora, Minister of State for Financial Affairs

Population: 3.8 million (1992)      Estimated GDP Growth Rate: 10% (1993)  
 GDP per capita: US\$ 1492 (1992)

	(\$million)		(\$million)
Total Commitments to date:	268.7	IBRD	FY93 Commitments: 175.0
of which:			Disbursements: 0.0
			Amortization: 3.5
Total Undisbursed:	175.0		
Lending Program: FY94-96	200.0		

<u>Summary Data</u>	Est.	Proj.	
	1992	1993	
GDP Growth (%)	10	10	Aid Group Meeting: CG planned for December 1993
Export Growth (%)	23	24	
Import Growth (%)	12	10	IMF Status as of September 1993:
Current Acc. Deficit/GDP (%)	40	36	Art. IV discussions took place
Gross Debt Service Ratio (%)	8	4	in May 1993, Board discussion in July 1993
Annual Inflation Rate (%)	116	25 <sup>1</sup>	

---

**Background:** The process of political normalization initiated in the context of the 1989 Ta'if Accord culminated in Parliamentary elections held in September 1992 and the appointment of a new Government with broad support in October 1992. Following a sharp post-war recovery and stabilization in 1991, a 200% public sector wage increase triggered economic instability in 1992, with a sharp depreciation of the Lebanese Pound, triple digit inflation and a loss of reserves. The confidence inspired by the appointment of Mr. Hariri as Prime-Minister in October 1992 triggered large capital inflows, with stabilization of the exchange rate and inflation, and a recovery of reserves. The new Government has taken initial measures to reduce fiscal imbalances, but the stability that has been achieved remains tenuous, and further adjustment measures will be required, particularly as the reconstruction program gets underway.

---

**Part I:**      Issues Likely to be Raised by The Delegation

1. Consultative Group Meeting

**Part II:**      Issues to be Raised by Regional Management

1. Economic Policy Actions and Role of IMF
2. Bank Assistance Program
3. IBRD Capital Subscription

---

<sup>1</sup>/Average rate; year end rate < 10%.

- Attachment - Biographical Information
- ANNEX I - Country Sheet
- ANNEX II - Disbursements/Repayments/Net Transfers,  
Actual FY93, Projected 94-98
- ANNEX III - FY94-96 Lending Program (FY93 Actual)
- ANNEX IV - List of FY94-96S Projects
- ANNEX V - FY94-95 Economic and Sector Work

LEBANON

BACKGROUND

1. Political: Significant progress has been made in the process of political normalization in the context of the Arab-League-backed 1989 Ta'if Accord. Parliamentary elections were successfully held in September 1992 despite the opposition of Christian groups that felt that they should not take place while Syrian troops remain in Lebanon. A new Government, led by Prime Minister Hariri, took office in October 1992. The Government has further extended control over the national territory, and all militia groups, except for Iran-supported Hezbollah, have been disarmed; nevertheless, Hezbollah did participate in the Parliamentary elections and is represented. Syrian troops have withdrawn from Beirut, but they continue to be present in large parts of the country, while the Israeli-backed Southern Lebanese Army continues to occupy part of the South. The new Government of, Sunni muslim, Prime Minister Hariri has broad support, but there are concerns among Christian groups that his strong role may undermine that of, Maronite christian, President Hrawi, and thus upset the delicate balance of power between the country's denominational groups in accordance with the Constitution and the Ta'if Accord. The Prime Minister and several of his colleagues bring a private sector background to the task of government, and they have had significant initial success in turning around a weak public administration, initiating an ambitious reconstruction program, and taking initial measures aimed at correcting fiscal imbalances, which, together with unforeseen domestic or regional political developments, could undermine the stability that has been established.

2. Economic: The economy recovered sharply in 1991, with real GDP expanding by about 40%, and stabilization policies were successful, contributing to exchange rate stability, a moderation in inflation and a rebuilding of reserves. However, a 200% public sector wage increase in late 1991 triggered an outflow of private capital. Central Bank financing of a mounting fiscal deficit led to large monetary expansion and a run on the Lebanese Pound. After losing about \$0.5 billion in a futile attempt to defend the exchange rate during the first quarter of 1992, the Central Bank was forced to give up its intervention policy. Without a correction to the fiscal deficit, the Pound depreciated sharply (by over 50%) and because of the openness of the economy, the rate of inflation accelerated to triple digit levels on an annualized basis. Instability continued throughout the first three quarters of the year, with a further loss of reserves. The acceleration of inflation sparked riots May 1992 that forced the Karami Government to resign. The caretaker Solh Government, appointed in May 1992, failed to take corrective measures. The appointment of Mr. Hariri in October 1992 led to a large inflow of capital, an appreciation of the Pound, and a reduction in inflation to single digit levels. The Central Bank recovered about \$1.0 billion in reserves, and the Government was able to finance the fiscal deficit (an estimated 13.1% of GDP in 1992, compared to 19.3% in 1991) through the placement of T-bills.

3. The new Government has taken initial measures to reduce the fiscal deficit. These measures, primarily of an administrative nature, have contributed to a 75% increase in fiscal revenues during the first seven months of 1993. At the same time, in the absence of a budget for 1993, most Government expenditures were limited by legal provisions to the 1992 level, and as a result the overall deficit, including foreign financed reconstruction expenditures, is expected to remain below the 12% of GDP envisaged in the IMF macro-economic scenario. However further fiscal actions will be required as the reconstruction program takes off and because of the pressures on expenditures resulting from the high level of interest paid on T-bills, which is a consequence of the Government's current monetary policy stance that aims at maintaining exchange rate stability. Failure to address the fiscal imbalances would undermine the tenuous stability that has been established and the resulting continued economic instability would make it unlikely that the private sector will undertake the investments required as part of the monumental task of reconstruction that faces the country. This situation would also raise doubts about the Government's ability to provide counterpart funds for the external assistance it is seeking for the reconstruction program. In spite of the low level of external public debt (about \$315 million at the end of 1992), failure to correct the fiscal deficit could raise doubt about the country's creditworthiness, because of the inability of the public sector to raise the domestic resources required for future debt service.

4. Bank Operations: Following a hiatus of about one and a half decade, the Bank re-initiated activities in Lebanon until the latter part of 1991. Following an initial assessment of the economic situation and the reconstruction needs, a Donors meeting was held in December 1991 to seek donor support for the reconstruction program. During 1992 the Bank initiated the preparation of an Emergency Reconstruction and Rehabilitation Project, which forms part of a broader \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96. A \$175 million loan was approved and signed in March 1993 and is expected to become effective shortly following ratification of the loan agreement by Parliament in July 1993. Progress in project implementation is satisfactory. A Country Economic Memorandum was circulated to the Board in March 1993 and a Country Strategy Note to Senior Management in July 1993. A Consultative Group (CG) meeting is planned for December 1993 to help mobilize external resources for the NERP and for technical assistance.

#### PART I: ISSUES LIKELY TO BE RAISED BY THE DELEGATION

1. (a) Consultative Group. The delegation may enquire about the Bank's plans for the convening of a Consultative Group.

(b) Recommended Position. The CG is now planned for mid-December. You may wish to stress that it will be important to ensure that the meeting is a successful one. You may wish to confirm that we would expect the Government to present to the meeting a credible fiscal program for 1994, as part of its overall economic program for that year. We would expect such program to be broadly consistent with the macro-economic scenario that has been discussed with the Fund. Targets for resource mobilization should be realistic and it will be over-ambitious to expect that the entire financing gap for the National Emergency

Recovery Program can be filled. We should make joint efforts at canvassing donors in advance of the meeting. You may also wish to add that all documentation should be completed by early November, including agreed documents on the reconstruction and technical assistance programs, and an economic updating note reflecting fiscal plans for 1994.

PART II: ISSUES TO BE RAISED BY REGIONAL MANAGEMENT

1. (a) Economic Policy Actions and the Role of the IMF. Notwithstanding the progress made in 1993, the fiscal outlook remains of concern. The recently completed 1993 budget will set a higher domestic expenditures ceiling, the domestic interest bill continues rising, reconstruction expenditures are likely to rise rapidly as the program takes off, and key fiscal measures, in particular customs reform and electricity tariff adjustments, have been postponed.

(b) Recommended Position. You may wish to express your concern and ask the Minister to give his assessment and outline his plans to address the fiscal issue. At the same time, you may wish to enquire whether the Government would consider a more formal arrangement with the Fund. This would likely give confidence to donors and help the Minister maintain discipline now that pressures for higher expenditures are likely to increase.

2. (a) Bank Assistance Program. Our ideas with respect to future assistance to Lebanon have been discussed in broad terms on the occasion of Management visits in the course of FY93 and work on a number of possible projects has been initiated. Nevertheless, the delegation may not be fully aware of the objectives of our proposed assistance program. At a separate meeting, we intend to review with the delegation our proposed lending program.

(b) Recommended Position. You may wish to indicate that we look forward to developing an active relationship with Lebanon and that we would be willing to provide continued support to the National Emergency Recovery Program as well as for other projects, and that we would envisage a heavy focus on social sectors in our assistance program, as we consider this a priority area for Government intervention. The development of human resources and addressing issues of poverty and regional imbalances, will be key to sustained longer term growth, and maintaining social and political stability. In most other sectors, in particular the directly productive sector, and also the future expansion of physical infrastructure, beyond the immediate reconstruction, the private sector could be expected to undertake the required investments, provided Government ensures an appropriate legal and administrative framework, and maintains a viable macro-economic framework. You may wish to express your appreciation for the excellent cooperation that has been extended to our missions. We expect to invite Government shortly to negotiate a technical assistance project to support the strengthening of economic management and public administration, and preparations have begun for projects in education, health, rural irrigation, water supply, and environment. We would also be willing to consider an operation to support a social fund to finance small scale investments in physical and social infrastructure. You may wish to stress to the Minister that we would expect that

adequate and timely local counterpart funding be provided for the ongoing Emergency Project and new projects that are being prepared.

3. (a) IBRD Capital Subscription Status: Lebanon has subscribed 340 shares of the 606 shares it was allocated under the 1988 General Capital Increase (Res. No. 425); it has taken no action so far to subscribe the remainder. On subscription, it would have to pay \$96,000, as well as \$866,000 equivalent in national currency, which may be substituted by notes. This position has not changed since last year.

(b) Recommended Position: You may wish to ask the delegation the probable timing of the Government's subscription of its remaining shares. The Bank would prefer early subscription since its lending authority increases only when the shares allocated to the members are subscribed.

LEBANON  
COUNTRY SHEET

Operations	Status	Comments
<u>Disbursements</u>	N.A.	First loan approved March 1993
<u>Pipeline Developments</u>		
Project Identification	Good	Initial identification of a number of projects has taken place
Project number and amounts requested	Good	Project preparation has only recently started. Good prospects for reasonable end-FY94 pipeline
<u>Country/Bank Dialogue</u>		
Capital Increase	Poor	Subscription to 1988 GCI not completed
Macro	Good	Good initial implementation of a macroeconomic program but delays in key fiscal measures
Micro	Good	Very good cooperation from Government in project preparation and receptivity to advice.
<u>Donor Coordination</u>	Good	First CG is scheduled for December 1993.
<u>Cofinancing Prospects</u>	Good	A number of regional funds, EIB and EEC have extended loan/grants for NERP.

Economy	Status		Comments
	1992 (Estimate) (% change unless otherwise noted)	1993 (Projected)	
Growth Rate of Real GDP	10.0	10.0	Postwar recovery continues
Agricultural Growth Rate (value added)	n.a.	n.a.	Data not available
Industry and Mining Growth Rate (value added)	n.a.	n.a.	Data not available
Balance of Payments Current Account Balance (\$US bil.)	-2.2	-2.4	Deficit increases because of reconstruction related import growth. Deficit may be overstated because of underestimate of transfers and remittances.
Debt Service to Exports Ratio	7.6	4.2	Outstanding public external debt very low at just over \$300 million



Economy	Status		Comments
	1992 (Estimate) (% change unless otherwise noted)	1993 (Projected)	
Public Finance (Budget deficit as % of GDP)	13.1	12.0	Sharp rise in revenues due to administrative measures and better collections; start of reconstruction program
Inflation	120.0	10.0	Stabilization of exchange rate
Energy Policy			Petroleum products at market prices with low gasoline tax; power tariffs well below costs.
Population Growth	n.a.	n.a.	Population data not available
Employment	n.a.	n.a.	High unemployment combined with unskilled labor shortages point to structural labor market problems.
Income Distribution	n.a.	n.a.	No income data available
IMF Relations	Good	Good	Article IV report discussed with Board August 1993. Informal monitoring of macro-framework.
Environment			Severe environmental deterioration. Keen government interest to address issues

LEBANON  
DISBURSEMENTS/REPAYMENTS/NET TRANSFERS  
ACTUAL FY93 PROJECTED FY94-98  
(US\$ MILLIONS)

	ACTUAL	PROJECTED <u>a/</u>				
	FY93	FY94	FY95	FY96	FY97	FY98
Commitments	175	90	100	85	80	70
Disbursements	-	55	88	105	96	85
Repayments	4	4	4	4	16	19
Net Disbursements	-4	51	84	101	80	66
Interest and Charges	2	4	9	16	23	28
Net Transfers	-6	47	75	85	57	42

a/ Based on CSN Lending Program

Lebanon

FY 93-96 Lending Program  
(in US\$ millions)

	<u>Actual</u> <u>FY93</u>	<u>FY94</u>	<u>FY95</u>	<u>FY96</u>	<u>Total</u>
<u>Infrastructure</u>					
Emergency Recovery	175.0				
Water Supply/Sewerage				40.0	
Solid Waste/ Environment				40.0	
Subtotal	175.0			80.0	255.0
<u>Human Resources</u>					
Education		40.0			
Poverty Alleviation			40.0		
Subtotal		40.0	40.0		80.0
<u>Agriculture</u>					
Irrigation			20.0		
Subtotal			20.0		20.0
<u>Other</u>					
TA for Improving Economic Management		20.0			
Subtotal		20.0			20.0
TOTAL	175.0	60.0	60.0	80.0	375.0
	(1)	(2)	(2)	(2)	(7)

LEBANON

List of FY94-96 Lending Projects

<u>FY</u>	<u>Project Name</u>	<u>Description and Status</u>
94	Technical Assistance for Improving Economic Management	The objectives of the project are to improve (i) macroeconomic management and (ii) the legal and regulatory framework for private sector development. Appraisal completed. Board presentation scheduled for November 1994.
94	Emergency Education <sup>1</sup>	The project would help improve the quality of education in disadvantaged regions, develop new curricula, strengthen sector institutions, and rehabilitate the Lebanese University College of Science. Following identification mission decision was made to slip to FY95 and substitute a Health project (Preparation mission scheduled for September).
95(S)	Irrigation	The project would support the rehabilitation of rural irrigation schemes and strengthen sector institutions. FAO/CP preparation mission scheduled for September 1993.
95	Poverty Alleviation	The project would support a social fund to finance small physical and social infrastructure projects.
96(S)	Water Supply	The objectives of the project are: (i) rehabilitation of damaged infrastructure and new investment in the water supply and wastewater sector; (ii) institutional development; (iii) improved cost recovery; and (iv) private sector development. Preappraisal scheduled for May 1994.
96(S)	Solid Waste/ Environment	The project would improve the environment in the greater Beirut area by improving collection and disposal of solid waste and by reducing air pollution from industry and traffic through better incentives and management. Preappraisal scheduled for June 1994.

m:\leb\amb93.an4

---

1/ As per MIS July 1993.

LEBANONFY94-95 Economic and Sector Work

<u>Task</u>	<u>Aims and Coverage</u>	<u>Audience</u>	<u>Responsible Division</u>	<u>Total Staffweeks</u>	
				<u>FY94</u>	<u>FY95</u>
<b>A. <u>Economic Work</u></b>					
1. Financial Sector Review/Macro Assessment	Assessment of macroeconomic situation and the status of financial sector, identify sector reforms to help re-establish confidence and ensure mobilization of domestic and foreign savings and their efficient allocation.	Government Board	MN2CO	70	
2. PSER	Analyze public finance issues, assess current expenditure patterns and recommend an appropriate balance among various expenditure categories considering fiscal constraint and need to address social issues.	Government Board	MN2CO	60	
<b>B. <u>Sector Work</u></b>					
1. Private Sector Assessment	Assess administrative, regulatory, and legal environment as well as the macroeconomic and investment climate, and identify impediments to the private sector initiative.	Government/Private Sector Board	MN2IE	60	20
2. Human Resources Sector Note/Poverty Assessment (Started in FY93)	Provide sector overview, and identify issues related to the future development of human resources in Lebanon, and social sector and poverty issues.	Government Management	MN2PH	50	
3. Environmental Assessment	Identify environmental issues and identify policy options and ways to upgrade the quality of the environment. The assessment will include a water resource base study for Lebanon as part of the ongoing regional water resource base study and assess the impact of reconstruction on the environment.	Government	MN2IN	10	20

<u>Task</u>	<u>Aims and Coverage</u>	<u>Audience</u>	<u>Responsible Division</u>	<u>Total Staffweeks</u>	
				<u>FY94</u>	<u>FY95</u>
4. Poverty Assessment/ LSMS	The assessment would follow up on initial human resource sector work carried out during FY93-94 with a focus on the income distribution and social indicator disparities, particularly among different regions. It will identify the roles of social services and income support for poverty alleviation.	Government Board	MN2PH		30

LEBANON

H.E. Mr. Fuad Siniora

Mr. Siniora was born in Sidon, Lebanon in 1943. He obtained his undergraduate degree (B.S. Business Administration) and graduate degree (M.B.A.) in 1967 and 1970 respectively at the American University of Beirut. Until he was named to the post of Minister of State for Financial Affairs in this Cabinet of Ministers, he held the position of Chairman of the Board of the Saudi-Lebanese Bank, the Vice-President of the Board of Trustees of Hariri Foundation and the President of the Financial Holding Group Companies MIG (Mediterranean Investment Group). He was also Chairman and General Manager of Mediterranean Group Services. He served as the Chairman of the Banking Control Commission, a governmental body.

## OFFICE MEMORANDUM

File  
Lebanon

DATE: July 12, 1993

CONFIDENTIAL

TO: Mr. Attila Karaosmanoglu, Managing Director

FROM: Caio Koch-Weser, MNAV *Ckw*

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

EXTENSION: 35250

SUBJECT: LEBANON: Country Strategy Note

Please find attached the Country Strategy Note for Lebanon, which we reviewed at a Regional Loan Committee meeting on July 6, 1993.

Messrs./Mesdames

Sandstrom, Stern, Armitage, Kalantzopoulos (EXC); Thahane (SEC); Alisbah (PAAVP); Choksi (HROVP); Eccles (CTRVP); Einhorn (TREV); Husain (LACVP); Jaycox (AFRVP); Kaji (EAPVP); Kashiwaya (CFSVP); Linn (FPRVP); Picciotto (DGO); Rao (DECVP); Rischard (FPDVP); Serageldin (ESDVP); Shihata (LEGVP); Thalwitz (ECAVP); Wood (SASVP); Ryrie (CEXVP); Iida (MIGEX); Ray (DPG).

Messrs./Mesdames

Husain, Squire, Murli, Bouhabib, Kafka (MNAV); Chopra, Tyler, Heron, O'Donnell (MN2DR); Kohli, (MN1DR); Sood (EMTDR); Voyadzis, Hoppenbrouwer, Ozeki (MN2CO); Okonjo-Iweala, Barres (MN2AG); Bhargava, Jordan (MN2IE); McKechnie, Graham (MN2IN); Keare, Sederlof (MN2PH); Hovaguimian (CMEDR); Alizai (COGDR); Pfeffermann (CEIED); Haddad (CMED2); Nishimizu (FRSDR); Bhattacharya (FRSCR); Sud (CFSDR); Birdsall (CECDR); Petit (AGRDR); El-Ashry (ENVDR); Iskander (PSD); Long (FSD); Adams (OPRDR); Hollywood (MIGGU); Morais, Abushahr (LEGMN); Chabrier, Handy (IMF); MNA Files.

L. Hoppenbrouwer  
M:\leb\csnmd

*2*



Document of  
The World Bank

**CONFIDENTIAL**

**DECLASSIFIED**

**MAR 31 2017**

**WBG ARCHIVES**

**REPUBLIC OF LEBANON**  
**COUNTRY STRATEGY NOTE**

July 12, 1993

Country Operations Division  
Country Department II  
Middle East and North Africa Region

LEBANON  
COUNTRY STRATEGY NOTE

TABLE OF CONTENTS

	<u>Page no.</u>
EXECUTIVE SUMMARY.....	i
Economic and Political Background.....	1
Development Issues and Policy Agenda.....	2
Physical and Social Infrastructure.....	4
Environment.....	6
Human Resources Development.....	7
Productive Sectors.....	8
Macroeconomic Prospects.....	9
Introduction.....	9
Base Case.....	9
Alternative Scenarios.....	10
Creditworthiness and External Capital Requirements....	10
Bank Assistance Strategy.....	11
Coordination with other Institutions.....	13
Bank Share of Financing.....	14
Downside Risks.....	15
Objectives and Instruments of Country Assistance Strategy.....	16
ANNEX I      Lending Program (Base Case)	
ANNEX II     Economic and Sector Work Program	
Social Indicators of Development	
Key Indicators and Projections	

# LEBANON

## COUNTRY STRATEGY NOTE

### EXECUTIVE SUMMARY

*Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of war. By 1990, per capita income (about \$820) was only about one-third of the 1975 level in real terms. The total damage to physical assets was estimated by the United Nations at \$25 billion. The impact on social conditions has been grave, with considerable loss in human resources, one quarter of the population of 3.6 million displaced, and public and social services either non-existent or of poor quality.*

*A sharp post-war recovery in 1991 was followed by an economic crisis in 1992, triggered by successive governments' failure to address fiscal imbalances. In October 1992, a new government took office following parliamentary elections. Prime Minister Hariri and his Cabinet enjoy broad political support. Government faces the daunting task of rehabilitating the war-damaged economy while maintaining economic and political stability, rebuilding a devastated public administration, and enticing the private sector to invest. Initial confidence triggered a significant inflow of capital and helped reestablish stability, which remains fragile, however, and will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.*

*Lebanon's vigorous and dynamic private sector continues to be the country's main asset. Beyond the initial stage of reconstruction to restore basic physical and social infrastructure, steady long-term growth will be predicated upon renewed private sector initiative. The government intends to support private sector initiative by creating an appropriate enabling environment, and efficient public administration, and investing in human resources. Before the protracted war, human resources were well developed and health facilities adequate, but there was a general neglect of social concerns. At present the*

*needs in health and education are massive. Continued political stability will not be maintained unless social issues and human resources development are addressed.*

*The serious damage sustained to basic infrastructure now presents the most immediate obstacle to economic revival. Mr. Hariri's government has a unique window of opportunity to undertake the ambitious task of reconstruction, establish economic stability, and lay the basis for private sector-led recovery. Lebanon needs substantial amounts of official external assistance to finance an ambitious \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96. In addition, reconstruction and recovery will require large amounts of private capital. Total capital requirements in the medium term would amount to around \$3.0 billion per annum. The bulk of this is expected to be available from private capital inflows, provided political and economic stability are maintained.*

*The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. The \$175 million Emergency Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which institutional and economic reform is feasible. The Bank now has a fairly unique opportunity, at above average risks, to play a major role in the recovery of Lebanon. Towards the overall objective of a resumption of rapid growth and reduction of poverty, the Bank would support a private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity,*

rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development.

Future lending would concentrate heavily on the social sectors, and would also support the strengthening of the public administration, and selected public investments in physical infrastructure during the reconstruction phase and future expansion by the private sector. The frontloaded ESW would underpin future lending and help government establish an enabling environment for private sector development. We would convene a CG meeting to help mobilize external resources for the NERP provided the Government continues to mount and implement an economic program satisfactory to the IMF and the Bank.

The proposed base case lending program of three operations for an average of \$85 million per year during FY94-98, with some frontloading, would be conditional upon the maintenance of an acceptable overall macroeconomic framework and the availability of financing from other sources. We would also need to continuously monitor the evolution of the political situation. A decline in government commitment to fiscal adjustment would trigger a low case lending program. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. The proposed ESW is for 180 SW on average during FY94-96 with frontloading.

In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank throughout the war. External public debt, an estimated \$360 million (8% of GDP) at the end of 1991, is low by any standard. Despite a projected five-fold increase by 1996 because of the external financing required for the NERP, debt indicators would remain low, with a public debt to GDP ratio of 18% and a public debt service to exports ratio of less than 5%. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP. The Bank would account for 12% of gross loan and grant disbursements during 1993-96, and 20% of external public

debt by 1999. Lebanon's stock of external public debt would remain small by any standard, while its external reserve position - \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. In view of the past track record with the Bank and the government's commitment to fiscal stabilization, the amounts of planned lending are considered prudent.

There are risks that current economic stability will not be sustainable in the absence of action to correct macroeconomic imbalances and that external events, particularly regional developments, could upset political stability. The population's high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war, and the need to carefully balance the interests of the various denominational factions, could hamper the government's ability to take required measures. With the continued presence of the Syrian army, and the occupation of part of the country's territory by Israel and the Southern Lebanese army, there could be far-reaching implications for Lebanon if the Middle East peace process were to fail.

In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The government is well aware that economic stabilization is a pre-condition for sustained, private sector-led, recovery and growth, and has begun to take fiscal actions. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

The main issue for Management is:  
are the proposed strategy and lending and ESW programs appropriate given Lebanon's circumstances, needs, prospects, and the various political and economic risks involved?

## LEBANON

### COUNTRY STRATEGY NOTE

#### Economic and Political Background

1. Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of turmoil as a result of violent civil strife and military occupation. In the period between 1950 and 1975, Lebanon's free market economy expanded by about 6% per annum. This growth was largely driven by the service sectors, namely trade, tourism, and finance, which attracted business from surrounding oil-based economies. After the eruption of civil war in 1975, the economy deteriorated markedly, with intermittent recovery during the two periods of relative calm, 1978 to 1981, and 1986 to 1988.
2. The civil war had a severe impact on the socio-economic conditions in the country. Lebanon's per capita GNP, about US\$820 in 1990, in real terms was only about one third of the 1975 level, and income inequalities have been accentuated. The total damage to physical assets during the war period was estimated by the United Nations at US\$25 billion. All principal sectors of the Lebanese economy - physical and social infrastructure, office and factory buildings, and housing - have been affected. Damage is both a direct result of the war, as well as the accumulated effects of a near total disruption in capital investment and maintenance.
3. The impact of the civil war on social conditions has been equally grave. The loss in human resources has been considerable; apart from the tragic loss of life and the disabling of hundreds of thousands of people, about 200,000 professional and skilled Lebanese have sought employment in other countries. While this has resulted in major shortages of skilled workers in various sectors of the economy, unemployment nevertheless is estimated at 35% of the resident labor force, and is believed to be particularly high among urban youth. Nearly one quarter of the population of 3.6 million has been displaced and now lives in unhealthy shanty towns, and in semi-destroyed and vacated buildings, with severe overcrowding and inadequate housing quality. Urban poverty problems are especially pressing in Beirut. Public and social services are either non-existent or of poor quality, with only about one third of power capacity operating, water treatment and sewage virtually nonexistent, and most schools and hospitals damaged.
4. The 1989 Ta'if Accord for National Reconciliation, sponsored by the Arab League, was a first step toward bringing an end to the violence in late 1990. The national army was reunified, and a Syrian backed national unity government reestablished its authority over the Greater Beirut area and most of the national territory. Attempts to achieve economic stabilization since the end of the fighting in 1990 have yielded mixed results. During 1991, activity took off in virtually every sector of the Lebanese economy, spurred by large inflows of private capital, with real GDP expanding by about 40%. At the same time inflation moderated to 30% by year's end from close to 100% the year before, and exchange rate stability was reestablished. However, the government's stabilization policy was not sustainable beyond the short term in the absence of adequate fiscal correction. Interest payments on Treasury Bills, issued to absorb the large speculative capital inflows, merely added further to the fiscal imbalance and the overall fiscal deficit was close to 20% of GDP in 1991. Economic recovery and a real appreciation of the Lebanese Pound led to a sharp surge in imports, which left the current account deficit at an unsustainable high level (more than 40% of GDP). The economic situation worsened in

early 1992, as Central Bank credit to finance the fiscal deficit expanded significantly after the government awarded a 200% retroactive increase in public sector salaries. This triggered a large outflow of capital, including a switch from Pound to Dollar denominated assets, put pressures on the Lebanese pound, and caused disruptively high rates of inflation. In an attempt to defend the value of the Pound, the Central Bank lost \$500 million in reserves in a matter of weeks. The resulting exchange rate crisis, which particularly affected the poorest segments of the population, precipitated a national strike and forced the government to resign in May 1992. A new government was appointed but failed to take stabilization measures and exchange rate depreciation and inflation accelerated throughout the first three quarters of 1992.

5. In September 1992, parliamentary elections were held, and on October 31 a new government was formed. Prime Minister Hariri and his Cabinet enjoy broad political support, and have sparked high expectations. The Christian groups that boycotted the elections are generally supportive of Mr. Hariri, who also reportedly maintains good relations with Shia religious leaders, as well as enjoying both Saudi and Syrian support. Prime Minister Hariri has assembled an impressive economic team, many of whom bring a private sector background to the task of rehabilitating the war-damaged economy while maintaining economic and political stability, and turning around a very weak public administration.

6. The confidence in Mr. Hariri's appointment triggered a significant inflow of capital, which reversed depreciation of the Pound and brought inflation to negligible levels. Since October 1992 the Pound has appreciated by about 25% and inflation has been reduced from over 100% to single digit levels. In addition, it enabled the Central Bank to replenish its reserves (by about \$1.0 billion), and the government to switch from Central Bank credit to Treasury Bills for the financing of its large

deficit (13% of GDP in 1992). The current monetary and exchange rate policy obviously has significant fiscal costs, but the authorities consider this to be an unavoidable consequence of stabilizing the exchange rate. Nevertheless, the speculative nature of these capital inflows suggests that stability will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.

7. Lebanon needs substantial amounts of external assistance in support of stabilization and reconstruction. The government has requested the Bank to assist in the mobilization of the large amount of external resources required to finance its \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96, and has sought IMF advice for the design and implementation of a macroeconomic stabilization program. The donor community has shown a willingness to support the reconstruction of the Lebanese economy. However, in addition to official capital, the reconstruction and recovery of the Lebanese economy will require large amounts of private capital, which will only be forthcoming if political stability is maintained and sustainable economic stabilization established by the government.

#### **Development Issues and Policy Agenda**

8. Endowed with an enterprising population and a geographical location on the trade route between Europe and the Middle East but with no mineral resource base and land that is difficult to cultivate, the Lebanese economy has been oriented to the development of services and light industry. Traditionally, Lebanon has been an open economy, characterized by a large external sector and unrestricted capital mobility, and it had achieved an export-oriented and private sector-led economic development at a good pace mainly through the development of international banking, transit trade, and tourism and, to a lesser extent, through the export of manufactured and agricultural products. With the destruction of much of the nation's infrastructure and productive assets and

dislocation of the human capital after an extended civil war, the reconstruction of the Lebanese economy is a daunting task, and is expected to take massive resource mobilization, capital investment, and development of human resources, and rebuilding of institutions over a protracted period of time. By training its unemployed manpower, restoring the pre-war quality of education, re-equipping labor with infrastructure and productive capital stock, and tapping the resources of its large expatriate community, Lebanon could relatively rapidly rebound and restore rapid growth.

9. Lebanon's reconstruction and development should be guided by the private sector initiative as Lebanon's vigorous and dynamic private sector continues to be the country's main asset. However, in the initial stage of reconstruction, government involvement is crucial as the first order of priority in reconstruction is given to restoration of basic physical and social infrastructure and is to be undertaken by the government under the NERP. Beyond a period of rapid growth that is likely to be associated with the reconstruction phase, sustained domestic investment and steady long-term growth will be predicated upon the renewed private sector initiative. The government's role would be to establish an enabling environment. Above all, it is imperative to sustain the confidence that has been placed in the new government and the Lebanese economy by vigorously pursuing macroeconomic stabilization measures. Moreover, government will need to strengthen public administration and macroeconomic management, and provide clear signals that Lebanon's traditional policies of non-interference with private sector activities will be maintained.

10. Although presumably Lebanon's comparative advantage still lies in international services, tourism, and high value added light manufacturing industry and agriculture, regional competition for financial services and transit trade has increased, the high regional growth associated with the petroleum boom is no longer

present, and other circumstances that had contributed to the rapid growth in the period prior to the mid-1970s are unlikely to be replicated. Hence, prospects for the longer term, including the direction of future growth, are somewhat uncertain at this time, although the resumption of past economic activity, including tourism in particular, is not to be excluded. However, whatever its composition, the potential for growth would be best exploited if government supports private sector initiative.

11. The new government faces the need to undertake stabilization measures simultaneously with its reconstruction program, in order to attract private and official financing for reconstruction. The restoration of fiscal balance - announced by the current government as one of its key objectives - will require drastic action through measures that both raise government revenues from the 1992 level of only 10% of GDP, and contain current expenditures at close to the 1992 level of 20% of GDP. This presents a challenging task, particularly given the virtual collapse of government revenues over the past several years, to the point where revenues covered less than 50% of current expenditures. Since reconstruction will lead to a sharp increase in the presently low level of capital expenditures (a projected average of 10% of GDP during 1993-96), a sharp reduction in the current deficit (10% of GDP in 1992) will be required in order to keep the fiscal deficit in check.

12. Revenue collection and expenditure control in the short run is complicated by administrative weaknesses and rigidity in key expenditure categories. It is therefore necessary to concentrate on policy measures that are straightforward in design, can be implemented quickly, and have good prospects for reducing the current fiscal deficit. Compared to other countries in the region, Lebanon's taxation yields are very low, particularly for direct taxes (2% of GDP in 1992). Key elements in expenditure control include adjustments in power tariffs to reduce budget transfers; the containment of interest payments on internal

debt (which stood at about 40% of GDP at the end of 1992) by gradually lowering interest rates; and containment of the wage bill by limiting wage increases and eliminating ghost workers from the payroll. Subsidies on electricity tariffs have been a major source of the fiscal deficit, as the weighted average tariff is only about one-fifth of economic cost.

13. Over the past half year, the government has already initiated a number of fiscal actions, including administrative measures to improve income and real estate tax and electricity tariff collection, the elimination of wheat subsidies, increases in fees and water and telephone charges and electricity connection fees. The government has maintained public sector wages at the level established in early 1992, in spite of triple digit inflation in 1992. The government's initial measures have resulted in a doubling of revenues during the first quarter of 1993, while expenditure growth has been contained, but further measures, along the lines enumerated in the recent CEM, in particular customs tariff reform and adjustments in power tariffs, will be required to achieve a sustainable reduction in the fiscal deficit.

14. The government envisages a phased strategy for rebuilding Lebanon's ravaged economy and addressing social problems, consisting of a short-term emergency reconstruction phase followed by a medium-term recovery phase. The NERP provides for initial urgent investments, which will be made concurrently with the identification and implementation of longer-term development strategies in the various sectors. The NERP is designed as a multi-sectoral operation, focussed on removing critical infrastructure bottlenecks, alleviating pressing social problems, and strengthening the existing institutions in charge of planning, financing, and implementing the NERP.

15. The phased recovery program envisions that much of the reconstruction will be undertaken by the private sector, with

government supporting the first phase of short-term emergency reconstruction. Lebanon's traditional liberal and investor friendly policies provide a solid base for an expansion of private sector activity and the Lebanese diaspora represents an important source of entrepreneurial skills and capital resources. Yet, the regulatory framework will need to be updated, in part to facilitate private investment for the provision of infrastructure services, and financial sector reform and capital market development will be required for the transformation of resources to long-term investments.

16. Notwithstanding the limited role envisaged for the public sector in the medium- to long-term, there is an urgent need to rebuild public institutions that are dilapidated after 15 years of war and lack qualified personnel, particularly at the middle-levels. The government has, with Bank assistance, begun to define a program for rebuilding public administration, including a technical assistance program to address short term needs for strengthening of economic management and public sector institutions.

#### **Physical and Social Infrastructure**

17. All principal sectors of Lebanon's economy are characterized by widespread damage to physical assets and the obsolescence of remaining facilities, given the reluctance during the years of conflict to invest in new capital or spend on maintenance. The serious damage sustained to basic infrastructure in virtually all sectors now presents the most immediate obstacle to economic revival. As a major regional trade and financial sector, Lebanon's transport infrastructure had been developed intensively prior to the civil war. The thriving service economy of Beirut, where many multinational companies located their regional operations, depended on efficient transport links. During the war, Lebanon's ports and Beirut International Airport, as well as the road and rail networks, sustained severe damage and suffered from a lack of maintenance. Substantial investment will be



needed to restore competitiveness, particularly since other countries within the region have greatly enhanced their own transport networks. The NERP focuses on rehabilitation of international and primary roads, restoring Beirut airport handling capacity to its pre-war level, restoring capacity of the port facilities, and rehabilitating the Beirut bus system. Increased cost recovery, for example through taxes on fuel, customs duties on vehicles, and higher bus tariffs and air passenger fees, is an essential element of the sustainable recovery of transport services.

18. Lebanon meets virtually all its energy needs with imported crude oil and petroleum products. Both of Lebanon's oil refineries sustained heavy damage during the war. The power sector is characterized by a damaged and dilapidated state of the electricity network, as well as an acute shortage of qualified staff at the state-owned Electricite du Liban (EdL). EdL suffers from serious financial difficulties, mainly due to low tariffs, illegal connections, and poor collections. Estimated rehabilitation and expansion needs of the sector amount to about \$830 million. Because of the breakdown in public power supply, most commercial and industrial customers have installed private diesel generating stations, and there is a need to revise the legislative framework in order to regulate private sector activities in the power sector. The high-cost, small-size private systems cannot be expected to fill an anticipated rapid growth of demand as commerce and business enterprises re-establish operations. Tariffs need to be adjusted to adequately reflect costs.

19. The immediate objectives for the power sector should be: (i) reconstructing the war-damaged facilities and removing deficiencies in existing facilities; (ii) setting and maintaining electricity tariffs at levels which cover the full cost of supply, while providing a life-line rate for the first 100 or 200 kWh/month; (iii) restructuring and corporatizing EdL's activities, and contracting out certain activities (eg. billing, repair), with a view to eventual privatization;

and (iv) upgrading the quality of human resources employed in the sector through training and staff development programs. The NERP includes initial investments of about \$300 million, to provide an integrated and balanced package of improvements.

20. In the telecommunications sector, about one-third of subscribers do not receive service, and those who have access to the network suffer from low quality of service. With the breakdown of public services, private entrepreneurs installed and operated various unlicensed systems. As adequate telecommunications services will be required to restore Lebanon's role as a business, banking and services center in the Middle East, as well as for resuming normal economic and social life, their rehabilitation is among the highest priorities. The NERP focuses on urgent rehabilitation works that can be undertaken without the need for further studies, and which would be compatible with longer-term improvements that are to be identified. In addition to reconstruction of technical installations, the restoration of reliable services requires simultaneous actions to rebuild the sector's management, planning and operating capabilities. The government intends to encourage the role of the private sector in the reconstruction and future development of the telecommunications sector, which will require a review and up-date of the overall legal framework, as well as revamping the government's policy making, regulatory and licensing functions and authority. Tariffs need to be further increased progressively to bring them in line with costs.

21. In the water supply and sanitation sector, there are no functioning sewage treatment facilities in the country, and all water treatment plants have been damaged and are operated at reduced capacity. A 1990 water quality survey indicated unsatisfactory water quality on a widespread scale, which could have serious health implications. Operation and maintenance suffer from inadequate organizational structures and a lack of skilled staff. Damage assessment

surveys indicate that about \$325 million in investments are required for water supply and waste water and for improving solid waste disposal. The undertaking of these investments will require a reorganization of present institutions, with participation from the private sector. Tariffs will have to be raised to ensure adequate internal cash generation for a sustainable development of the sector. The NERP includes: (i) design and execution of physical rehabilitation works; (ii) preparation of a policy strategy paper for institutional and organizational development; (iii) preparation of development programs and feasibility studies for subsequent investments; and (iv) preparation of a water master plan for the country.

22. In housing, the inadequacies of the housing supply mechanism have been exacerbated by the war, but in themselves are more deeply rooted. Lebanon's relatively small size, coupled with its highly dense pattern of settlement and traditionally high construction costs, places housing at a great premium. Furthermore, there have been no urban growth strategy or land-use plans to anticipate and cope with population movements. Substantial capital inflows for real estate speculation led to further distortions in the market system. Because of the different effects generated by internal and external emigration during the war, there is at present a surplus of high quality housing, coexisting with severe pressures in the mid- and lower-quality market.

23. The relocation of displaced persons is considered Lebanon's most pressing social problem, and an appropriate policy framework is required to deal with the complexity of housing sector resettlement and development. The NERP contains a major component for housing finance. In order to initiate rehabilitation of the housing stock by the private sector, appropriate financial instruments need to be developed and mechanisms established for the management and implementation of housing credit, possibly through existing commercial banks. The substantial decline in household real

income levels that occurred during the war eroded the capacity of households to make payments on housing loans. The affordability of housing rehabilitation to certain beneficiary groups therefore will require direct subsidies. In conjunction with other infrastructure components, the housing component of the NERP also will alleviate the immediate environmental problems by resettling households into better conditions and by providing and/or rehabilitating the needed infrastructure services.

### Environment

24. The deteriorated conditions resulting from the extensive war damages cause severe risks to public health and to the environment. The main hazards are: polluted water distribution systems; scattered solid waste dumped all over the country; heavy air pollution on account of energy generation by large numbers of small generators, transport and industrial plants; haphazard expansion of dwellings over fertile lands and natural ecosystems; the abandonment of agricultural lands; the pollution of surface and underground aquifers; widespread deforestation; destruction of the cultural and natural heritage; and the degradation of marine and coastal areas. The planned reconstruction and rehabilitation programs would remedy some of the urgent problems, but the increasing demands for land, water and building materials resulting from them would put additional pressures on the environment.

25. While specific environmental issues are addressed in sector laws and regulations, there is no comprehensive national environmental framework, and the capacity of the Ministry of Environment that was re-established in late 1992 is still very limited. Beyond the actions envisaged under the sectoral programs of the NERP that would address some of the current public health and environmental problems, there will be a need to adopt an environmental strategy to ensure that the process of reconstruction and rehabilitation will contribute to sustainable development.

## Human Resources Development

26. Before the protracted civil strife, Lebanon had a well-trained population and labor force, with adequate health facilities. Nevertheless, there was a general neglect of social concerns during the period of rapid economic growth preceding the war, and at present the needs in health and education are massive. A considerable number of social services, especially in the health sector, are currently provided by non-governmental organizations (NGOs), and are linked to the war situation. In the future, to a large extent these will need to be provided by the public sector. Furthermore, as indicated above, all sectors of the economy, including public administration, suffer from a lack of skilled workers and managers. Social sector ministries are inadequately staffed and are particularly weak.

27. In the health sector, the Ministry of Health (MOH) plays a relatively minor role in the actual provision of services. With the reduced capacity of public hospitals due to war damage and insufficient funds for the rehabilitation and operation of facilities, the MOH ends up directing over 80% of its budget to an uncontrolled reimbursement of private sector (including voluntary agencies) hospital services. The subsidy program, currently running at about \$60 million annually, is poorly targeted and inadequately monitored and controlled. The provision of primary health care services is inadequate, and their delivery currently consists of small dispensaries operated by a myriad of public, private, voluntary and political groups. Overall, the government has little ability to control quality and to enforce standards in the health sector. While generally there is an oversupply of skilled medical doctors in Lebanon, major institutional reforms will be required in the public health sector not only to fill the existing shortage of professional staff, but also to provide greater flexibility in the administration of budgets and in personnel management.

28. The health sector component of the NERP (\$61 million) includes rehabilitation of public hospitals, dispensaries and laboratory services, as well as assistance to rehabilitate care facilities for the disabled provided by charities. Technical assistance components would identify and support the immediate requirements for reform and improved management of subsidy programs, the decentralization of health services management and planning, and the development of MOH into a regulatory body focusing on policy and wider issues of public health. Issues related to the funding of publicly-provided health services also will be examined.

29. Total enrollments in general education declined during the latter part of the civil war, with an increasing share in enrollments for the private sector, which historically has played a significant role within the education sector at all levels. Private sector schools comprise two categories: exclusively fee-paying, and those which are state-subsidized but privately run by welfare institutions. The public sector's share of enrollments is 31% in primary, 46% in intermediate, 33% in secondary, 27% in vocational and technical schools, and 47% in higher education. In the absence of reliable population data, it is difficult to assess enrollment as a percentage of relevant age cohorts.

30. Teacher training activities were essentially suspended in 1987 and in-service training has been conducted irregularly since that date; thus, while the overall pupil/teacher ratio in the public sector is apparently extremely favorable, teachers tend to be poorly trained and localized shortages exist, mostly in rural areas. Enrollments in vocational and technical institutions have been very sensitive to prevailing security and economic conditions. Technical curricula are not relevant to the needs for trained labor, and there is a lack of suitable instructors. The provision of higher education by the public sector (the Lebanese University) expanded rapidly during the war, with an

expansion of campuses in various parts of the country, but quality declined.

31. The development of education facilities in Lebanon must be accompanied by wide-ranging reforms in sectoral policies and in the planning, management and administration of the sector. Substantial expenditures will be required to rehabilitate physical infrastructure and key institutional and policy reforms will require considerable technical assistance. The NERP earmarks about \$150 million for the education sector, to be directed toward four major priorities: i) upgrading the capacity of the teacher training system; ii) improving vocational/technical training centers, curriculum development, instructor training, and instructional materials; iii) rehabilitating public schools, to enhance their capacity to cope with a recovery in enrollments, support the government's resettlement strategy, and enhance educational access for those who cannot afford access to Lebanon's traditionally strong private education sector; and iv) improving the equipment and buildings of the Lebanese University. The government currently does not recover costs for public education; thus cost recovery, particularly with regard to higher education, is an important issue.

32. The issue of women in development has not been high on the government's agenda, and while educational enrollment figures are high, female illiteracy rates are high as well and political participation is limited.

33. Poverty Reduction Efforts. As noted above, after 15 years of war, real incomes have sharply declined, social conditions have worsened significantly and the displacement of up to a quarter of the population from their homes represents a pressing social issue. While poverty appears to be more heavily concentrated in the Greater Beirut area, there are important pockets of rural poverty as well. Social assistance is currently being provided by a large number of NGO's operating in Lebanon, many of which concentrate their efforts on specific

denominational groups. The government lacks information about the incidence and concentration of poverty and neither does it have the resources or mechanisms to address poverty in the short run. The government is of the view that price stability combined with employment to be generated through the reconstruction program will particularly benefit the poor. Nevertheless, it has asked the Bank to help assess the need and possibilities for social safety net mechanisms to accompany the stabilization measures that would need to be undertaken to correct the macro-economic imbalances.

### Productive Sectors

34. Productive activities in Lebanon have traditionally been undertaken almost exclusively by a strong private sector, and it is on private initiative that future growth will depend. The government's main role will be to create an enabling environment for private sector activity in the productive sectors and in the provision of infrastructure. This will require a strengthening of public administration, the development of a legal and regulatory framework that is conducive to attracting private investment, as well as a strengthening of capital markets.

35. Agriculture. Much of Lebanon's arable land (an estimated one-third of the territory) is marginal land and Lebanon has always been a net importer of agricultural and food commodities. The sector contributes about 10% to GDP and accounts for about 20-25% of merchandise exports. The dislocation of production and marketing facilities during the war resulted in a decline in agricultural exports (mainly fruits and vegetables) from close to \$260 million in 1980 to \$170 million in 1990. To regain market shares, Lebanon will have to address both the extensive war damage and the pre-war weaknesses in the agricultural sector. Priority areas for public sector intervention include: (i) rehabilitation and improvement of irrigation schemes and recovery of at least O & M costs of irrigation schemes; (ii) physical reconstruction and institutional development of

the Ministries of Agriculture and Water and Electrical Resources; (iii) the upgrading of applied agricultural research and extension services. As in other sectors, the virtual absence of medium- and long-term credit, particularly for small and medium farmers and agro-industries hampers a recovery of the sector.

36. Industry. The industrial sector contributes about 20% to GDP and accounts for the bulk of merchandise exports. Except for oil refining, industry is entirely within the private sector. The industrial sector faced not only considerable war damage (close to 200 plants were destroyed in the heavy 1989/90 hostilities), but more importantly, a loss of its work force. Nevertheless, available data suggest that the sector has remained resilient in the face of the war, with real sector GDP in 1991 only some 20-30% below its pre-war level. A lack of skilled workers and managers, poor physical infrastructure and the virtual absence of medium- and long-term financing for working capital and investment stand in the way of a sustained recovery of the sector.

## Macroeconomic Prospects

### Introduction

37. The scenarios presented below are based on the macroeconomic framework in the recent Country Economic Memorandum ("Lebanon - Stabilization and Reconstruction") dated March 1993. The base case scenario is substantially similar to the medium-term scenario developed by the May 1993 IMF Article IV Consultation mission. Due to the paucity of data, and the absence of time-series, an unusual number of estimates and assumptions have been made to construct the framework. Thus, caution needs to be exercised in interpreting the results of the analysis. However, the projected scenarios are broadly indicative of general directions of developments and the likely outcomes of alternative policies and thus form a plausible basis for judgements on macroeconomic policy issues, resource needs and creditworthiness.

### Base Case

38. Sustained economic stability, together with political and social stability, is a prerequisite for economic recovery and sustained growth. Mr. Hariri's new government has a unique window of opportunity to both undertake the ambitious task of reconstruction and lay the basis for private sector-led recovery of the Lebanese economy. The base case scenario envisages major investments for reconstruction and significant external official and private capital inflows. Private per capita consumption levels would be maintained in the medium term, and rise steadily thereafter. Debt and debt service levels would initially rise rapidly but remain at manageable levels. This scenario centers around three main elements: (i) major fiscal adjustment in 1993 and 1994 (with the elimination of the fiscal current account deficit), and the successful stabilization of the economy; (ii) implementation of the reconstruction program with large increases in public and private investments; and (iii) availability of external financing. Clearly, successful reconstruction will require very sizeable amounts of both official and private capital from abroad. Only with stabilization and fiscal adjustment is there a chance that both will materialize.

39. With important fiscal adjustment taking place in 1993/94, in the base case scenario government revenues would increase from 10% of GDP in 1992 to 18% in 1994, while current expenditures would be contained at 19% of GDP. As the NERP takes off, public capital expenditures would rise from 3% of GDP in 1992 to 8% in 1993 and an average of close to 11% during 1994-96. With the virtual elimination of the current fiscal deficit, which stood at 10% of GDP in 1992, by 1994, the overall deficit could be contained to an average of about 11% of GDP during the period of reconstruction. Real GDP growth during that period is projected at 10% in 1993, and an average of 8% during 1994-96; beyond the reconstruction period real GDP growth is projected at an average of 6% p.a. based on

relatively low aggregate levels of efficient private sector investment. Total imports would increase substantially as reconstruction takes off and exports would rise steadily as overall economic activity picks up. The current account deficit would remain large, at an average of \$2.6 billion p.a. during the reconstruction period. Projected private inflows are sizeable throughout the period of reconstruction and thereafter; this

underscores the importance of sustaining stable economic policies. Despite the projected improvement in fiscal performance, relatively sizeable amounts of external loans and grants will continue to be required to finance the reconstruction of infrastructure. Key macroeconomic indicators in the base case scenario are presented in the table below.

<b>Base Case Scenario: Key Macroeconomic Indicators (%)</b>			
	1993	1994-1996	1997-1999
GDP real growth	10.0	8.0	6.4
Private Consumption real growth	2.3	0.9	4.8
Investment/GDP	23.8	30.4	18.9
of which: public investments	7.7	10.8	4.9
Current Fiscal Balance/GDP	-4.3	0.2	3.2
Overall Fiscal Balance/GDP	-12.0	-10.7	-1.7
External Public Debt Service/Exports	4.2	4.2	4.2
Current Account Balance/GDP	-35.8	-32.0	-20.5

### Alternative Scenarios

40. The viability of the base case scenario centers around fiscal adjustment. An alternative scenario envisions a lack of fiscal adjustment, with a likely consequence being that the level of private capital inflows would be well below the levels projected in the base case as uncertainty in the economy would prevail. A lack of fiscal adjustment would prevent the government from contributing to public investments associated with the reconstruction program; official creditors would then withdraw from the program. As a result, overall investment levels would be significantly below those under the base case scenario. GDP growth would fall, and sharp declines in consumption per capita would occur. This is the most likely outcome of a failure to implement stabilization policies.

41. If, in spite of the lack of fiscal adjustment, the government would still attempt to maintain total overall investment at levels

similar to those under the base case scenario, this would be achieved by substantially higher levels of external borrowing by the public sector. In that event, the public sector's (domestic and external) debt service would rapidly become unsustainable, as debt service payments would soon absorb most of fiscal revenues, even under favorable lending terms. Also, GDP growth would be lower than under the base case scenario, as the efficiency of incremental public investments is likely to be well below the efficiency of private capital.

### Creditworthiness and External Capital Requirements

42. Lebanon's total capital requirements in the medium term would amount to around \$3.0 billion per annum (see table below). The bulk of this is expected to be available from private capital inflows, including return of the flight capital and direct foreign investment. During the period of implementation of the NERP,

relatively sizeable amounts of official assistance will be needed. During the Donors meeting held in December 1991, the international donor community showed increasing interest in supporting Lebanon. The amount of loan and grant financing required during 1993-96, about \$600 million per annum, can only be raised if Arab and other donors are willing to support Lebanon. Current indications are that this may indeed be the case, but financing for the NERP will need to be confirmed in the context of a Consultative Group to be convened in late 1993.

43. In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank, and its current outstanding

obligations amount to only about \$20 million. Lebanon's external public debt was estimated at about \$360 million (8% of GDP) at the end of 1991, which is low by any standard. While the level of public debt is projected to increase five-fold to about \$1.8 billion over the next four years because of the external financing required for the NERP, debt indicators would remain low, with an external public debt to GDP ratio of less than 20% and a public debt service to exports ratio of less than 5% by the mid-1990s. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP.

<b>Base Case Scenario: External Financing Requirements (Millions of US\$ p.a.)</b>			
	1993	1994-1996	1997-1999
Current Account Deficit	2,445	2,744	2,418
Public Loan Amortization	50	50	69
Reserve Build-up	289	391	208
Total Financing	2,784	3,185	2,695
Public Grants	200	200	100
Public Loans (Gross Disbursement)	340	410	305
Private Capital Flows/Investment	2,244	2,575	2,290

### **Bank Assistance Strategy**

44. The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. In response to the government's request, the Bank assisted in the preparation of the NERP. The \$175 million Emergency Reconstruction and Rehabilitation (ERRP) Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which essential institutional and financial reform is feasible. While proceeding with the implementation of the ERRP, we would

assist the government in inducing private sector investment in the same sectors and in strengthening institutions.

45. Beyond the immediate reconstruction supported with the ERRP, the Bank has a fairly unique opportunity to play a major role in the recovery of Lebanon. While the risks involved are above average, the potential benefits of a relatively modest Bank assistance program to help a serious and strong government, that has broad domestic and regional support, lay the basis for steady recovery and mobilize external support are significant. The overall objective of Bank strategy would be the resumption of rapid economic growth and reduction of poverty. Towards these goals the Bank would support a

private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity, rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development (see attachment). The mobilization of external resources and aid coordination to achieve the overall strategy objectives would be an important element of the assistance program.

46. Future Bank lending would concentrate heavily on the social sectors. These have traditionally been neglected by Lebanese governments, in good and bad times, and this neglect in part underlies the tensions and violence that Lebanon has experienced. Ultimately, continued political stability will not be maintained unless social issues are addressed. Moreover, the services sector is undoubtedly one of the main sources for potential growth and human resources development, virtually non-existent for 15 years, would thus be a high priority. The proposed lending program includes an education project, a poverty alleviation (social fund) project, a health project, and an additional social sector project, as well as investments in social infrastructure. Specific sector work would focus on the development of a strategy for human resources development and the design of a social safety net, which becomes all the more important as economic stabilization measures are being implemented, and would also include a poverty assessment, a living standards measurement survey, and a rural development study to lay the basis for poverty alleviation programs. Bank support for the environment would include an environmental assessment, which, together with planned METAP activities, would help the government develop a comprehensive environmental strategy and lay the basis for an environmental lending operation.

47. The Bank would support the initial strengthening of the public administration through a free-standing technical assistance project to strengthen economic management and

public administration, to be followed by a more narrowly focused operation to help Lebanon establish an efficient civil service. An early strengthening of public administration is particularly important since the temporary improvements in administration that have been achieved by utilizing resources of Prime-Minister Hariri and his team do not represent a lasting and politically sustainable solution. As part of Bank support for private sector development, our initial economic and sector work would help government to establish an enabling environment for private sector development, including a legal and regulatory framework for private investment in the provision of public services, reform of the financial sector, and the development of capital markets to facilitate the mobilization and efficient allocation of resources. We would jointly with government organize a seminar ("Lebanon 2005") to develop a vision of the Lebanese economy and its future role in the region, and sector work would include a private sector assessment to be undertaken jointly between government, the private sector, and the Bank. This assessment would also focus on issues and prospects for private sector provision of infrastructure services. In physical infrastructure, the Bank would initially support selected public investments, particularly during the reconstruction and rehabilitation phase, but future expansion of physical infrastructure should be left to the private sector. The ERRP includes a technical assistance component in support of institutional and regulatory reforms in the infrastructure sectors and the design of sectoral strategies, including plans for private sector participation. The proposed ESW in support of private sector development would extend, and expand on, the initial work being undertaken. It would more specifically support corporatization and commercialisation of public institutions to allow their eventual privatization, and the reform of the legislative, contractual and regulatory frameworks to facilitate private investment in, and operation of, utilities. The proposed lending program includes a number of projects that would support private sector



development of infrastructure beyond the immediate reconstruction phase.

48. The proposed base case lending program for FY94-98 consists of three operations for an average of \$85 million per year, with some frontloading. The composition and phasing of the lending program as discussed above and shown in Annex I is tentative and subject to change based on the sector work to be initiated, the definition by the government of its priorities for Bank support, and an assessment of the availability of financing from other sources. The base case program would be conditional upon: (i) the maintenance of an acceptable overall macroeconomic framework, in particular by reducing the current imbalances through fiscal adjustment, along the lines of the base case macroeconomic scenario discussed above and the medium term scenario developed in the context of the recent IMF Article IV Consultation mission; and (ii) the availability of financing from other sources to ensure the feasibility of the overall financing scenario and adequate burden sharing. The next few months will show whether the government has the resolve to continue to take the required fiscal measures, and the Consultative Group meeting planned for late 1993 (para. 50) would confirm whether there is adequate official donor support for Lebanon. We would also need to continuously monitor the evolution of the political situation. The proposed economic and sector work program as discussed above and shown in Annex II, an average of 180 staff-weeks per year during FY94-96, is heavily frontloaded in order to rapidly develop our knowledge base, underpin proposed lending, and advise government on the design of macro- and sector policies. Because of the frontloaded nature of the economic and sector work program and the need to develop a project pipeline of the magnitude envisaged in the base case program, and undertake country work on a regular basis, total resource requirements in FY94 are estimated at 14.7 staff-years. (This includes 8.3 SY for lending, 0.9 SY for portfolio management, 4.4 SY for

ESW, and 1.1 SY for country work, aid coordination and other).

49. Lebanon's creditworthiness largely depends on the expected fiscal capacity to service its debt. The present government has made an important initial effort to reduce fiscal imbalances. If the government's commitment to fiscal adjustment were to decline, we would move to low case lending program. We would therefore closely monitor a number of indicators, including (i) the evolution of overall fiscal deficit, relative to the targets in the base case macroeconomic scenario, (ii) progress in increasing public sector revenues, which will be critical to achieving fiscal adjustment, and (iii) the mechanisms used to finance the deficit, as excessive reliance on Central Bank credit would undermine economic stability, while excessive reliance on domestic debt could crowd out the private sector. The size of the low case program would be determined in the light of events and its composition would focus more heavily on social sectors. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. At this stage, we do not propose a high case program. We plan to review the country assistance strategy in about twelve months.

#### Coordination with other Institutions

50. The government has requested the support of the Bank in mobilizing external resources for the NERP. We would convene a Consultative Group meeting provided the government continues to make satisfactory progress in mounting and implementing an appropriate macroeconomic program satisfactory to the IMF and the Bank. The recent IMF Article IV Consultation mission has made a favorable assessment of the government's economic program and has agreed with government on an informal arrangement for monitoring progress in its implementation. However, in view of the economic stabilization issues at hand, a more formal IMF program

would be desirable, and we would therefore continue to seek to convince government, which thus far has cited political constraints to a formal arrangement, to pursue this option. The presence of both the Bank and IMF is seen as an important signal to other donors, including Arab countries, and will help to increase the confidence not only of the international community but also of the Lebanese private sector. The NERP has already attracted external support from the regional funds, the EEC and EIB and a number of bilateral donors, and the Bank's role in the implementation of the NERP, through the ERRP, would ensure donor coordination. A Bank lending program of the size and composition proposed would be an important catalyst for attracting the external funding from official sources that Lebanon will require during the 1990s, particularly during the reconstruction phase; the Arab regional funds have already expressed their interest in co-financing Bank projects in Lebanon. In addition to large-scale financial support for reconstruction, Lebanon requires massive technical assistance to compensate for the absence of qualified and experienced staff who left the country during the war. The Bank would work closely with UNDP in establishing a technical assistance trust fund aimed at channeling and coordinating the technical assistance likely to be available from several multilateral and bilateral sources.

51. In promoting private sector development, the Bank would work closely with IFC, which has also reinitiated operations in FY93 and could play an important role in Lebanon given the country's traditional private sector orientation. IFC has agreed to help undertake the capital markets development component of the proposed financial sector review. IFC's strategy for Lebanon focuses on three main areas. First, invest in domestic capital markets to: (i) help the banking sector play an effective role in reconstruction by providing long-term loans to intermediaries to fund projects of small and medium-sized enterprises; (ii) provide technical assistance to government on financial markets

issues; (iii) help establish model financial intermediaries to deepen the financial system and energize capital markets; and (iv) mobilize and channel resources for the re-emerging private sector. Second, attract private capital to rehabilitate infrastructure facilities that are essential to the service economy, in particular in telecommunications, and possibly finance projects in maritime and air transport and power generation and/or distribution. Third, support viable manufacturing ventures, particularly in the construction and building materials industry that face significant demand associated with the reconstruction effort.

### **Bank Share of Financing**

52. Based on the medium-term projections underlying the base case macroeconomic scenario, with the \$175 million ERRP loan and the base case lending program as proposed, the Bank would account for about 12% of total gross public M & LT loan and grant disbursements during 1993-96. The Bank's exposure to Lebanon would be about 3% of GDP at end-1996, out of the total external public debt equal to 18% of GDP. Lebanon's external public debt, which stood at only about \$360 million at end-1991, is projected to increase five-fold during the 1993-96 period of the NERP, but public debt indicators are projected to remain at very low levels, on the assumption that a major share of the total financing needs will be met by private flows, including the repatriation of capital. By 1999, the Bank's share in total public external debt of \$2.4 billion (18% of GDP) would amount to 20%. As a significant portion of projected official assistance is expected to come from regional banks, the share of preferred creditors in total public debt would be around two-thirds.

53. Lebanon's stock of external public debt would remain small by any standard, while its reserve position - currently about \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. With fiscal adjustment along the lines projected, virtual elimination of the current

deficit (10% of GDP in 1992) within two years and of the overall deficit by 1999 (with most of the reduction after 1996 representing the completion of the NERP), there would be adequate fiscal capacity to service the external and domestic debt to be contracted by the public sector during 1993-99, in particular during 1993-96. In view of Lebanon's past track record with the Bank and the government's commitment to fiscal stabilization and reconstruction, the amounts of planned lending are considered prudent.

### **Downside Risks**

54. The main risks are the failure by the government to establish and maintain a viable macroeconomic framework and political stability, and the security situation. Lebanon's track record of macroeconomic management in past years has not been favorable, due in large part to the protracted hostilities and their aftermath. Lebanon's current economic stability is not sustainable in the absence of action to correct macroeconomic imbalances, in particular the fiscal deficit. In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The present government is aware that the short term stability that has been achieved is tenuous and delicate.

55. The question of political stability is very much related to the need to ensure economic stability. If the stabilization and reconstruction programs were to fail, the current government would find itself under significant pressure to resign. Successful implementation of the programs represents a significant challenge. Unfulfilled expectations and the need to carefully balance the interests of the various denominational factions could hamper the government from taking the ambitious and

difficult measures that are required. The population has very high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war. However, the new government is judged to have the best chance in many years to provide a measure of macroeconomic stability and to foster confidence in the private sector. It is well aware that economic stabilization is a pre-condition for sustained, private sector-led recovery. It has begun taking measures to reduce the fiscal deficit and has stated that restoration of fiscal balance is a priority objective. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

56. External events, particularly regional developments, could upset hard-won stability. The Syrian army continues to play an important security role in most of the country, while in the South, Israel and the Southern Lebanese Army occupy part of the country's territory. If the peace process were to fail, there could be far reaching implications for Lebanon. Conversely, if the process were to be successful, prospects for a prosperous Lebanon as a regional trade and services center would be enhanced.

**LEBANON**  
**OBJECTIVES AND INSTRUMENTS OF COUNTRY ASSISTANCE STRATEGY, FY94-98**

OBJECTIVES	INSTRUMENTS	COMMENTS
<p>A. <i>Macroeconomic stabilization/ Fiscal reform and adjustment.</i></p>	<ul style="list-style-type: none"> <li>• <i>Formulation of macroeconomic framework for stabilization jointly with IMF.</i></li> <li>• <i>Technical assistance project for economic management.</i></li> <li>• <i>Financial sector review and macroeconomic assessment, PSER, CEM, and other economic work.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>CEM issued March 1993, recommended stabilization measures.</i></li> <li>• <i>IMF conducted Article IV Consultation in May 1993 and made favorable assessment of government economic program.</i></li> </ul>
<p>B. <i>Reconstruction of infrastructure.</i></p>	<ul style="list-style-type: none"> <li>• <i>Implementation of ERRP.</i></li> <li>• <i>CG meeting to mobilize external resources.</i></li> <li>• <i>Lending for social and physical infrastructure (solid waste, irrigation, water, housing, and transport).</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ERRP is part of NERP, to be implemented during 1993-1996.</i></li> <li>• <i>CG planned for November 1993.</i></li> </ul>
<p>C. <i>Private-Sector led economic recovery.</i></p>	<ul style="list-style-type: none"> <li>• <i>Financial sector review.</i></li> <li>• <i>Private sector assessment.</i></li> <li>• <i>Lending for private sector investment in utilities.</i></li> <li>• <i>Technical assistance for capital market development (with IFC involvement), and legal, regulatory, and administrative reforms as part of T.A. projects.</i></li> <li>• <i>Conference on long-term vision for Lebanon planned for September 1993.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ESW heavily frontloaded in FY94.</i></li> </ul>
<p>D. <i>Rebuilding of public administration.</i></p>	<ul style="list-style-type: none"> <li>• <i>Technical assistance projects for economic management and for strengthening of public administration/civil service reform.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>Coordinating with UNDP and IMF.</i></li> </ul>
<p>E. <i>Development of social sectors/Human resources development/Alleviation of poverty/Environment.</i></p>	<ul style="list-style-type: none"> <li>• <i>Lending - Education / Poverty Alleviation / Health / Solid Waste / Environment / Water / Housing / Integrated Rural Development.</i></li> <li>• <i>Human resources sector work, including design of a social safety net, poverty assessment, and LSMS. Rural development study.</i></li> <li>• <i>Environmental assessment.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>First human resources sector mission in May, 1993.</i></li> <li>• <i>Elimination of inflation tax and generation of incomes through stabilization and economic recovery.</i></li> </ul>

## LEBANON

## FY93-98 Base Case Lending Program

Fiscal Year	Project	US\$ Million
FY93	Emergency Reconstruction & Rehabilitation	175
	TOTAL	175
FY94	Technical Assistance for Economic Management & Public Administration	10
	Emergency Education	50
	Irrigation Rehabilitation	30
	TOTAL	90
FY95	Poverty Alleviation	35
	Solid Waste/Environment	35
	Health	30
	TOTAL	100
FY96	Water Supply S	30
	Public Administration/Civil Service Reform S	15
	Private Sector Infrastructure Development	40
	TOTAL	85
FY97	Housing S	25
	Transport S	30
	Integrated Rural Development	25
	TOTAL	80
FY98	Social Sectors	40
	Private Sector Development II	30
	TOTAL	70

## LEBANON

Economic & Sector Work Program, FY93-96

<b>Fiscal Year</b>		<b>Staff Weeks</b>
<b>FY93</b>	CEM	70
	EWO	15
	Human Resources/Poverty Assessment*	20
	TOTAL	105
<b>FY94</b>	Financial Sector Review/Macro-Assessment	70
	Private Sector Assessment*	60
	Human Resources/Poverty Assessment	50
	Environmental Assessment*	10
	EWO/SWO	40
	TOTAL	230
<b>FY95</b>	Public Sector Expenditure Review	60
	Private Sector Assessment	20
	Environmental Assessment	20
	Poverty/LSMS*	10
	EWO/SWO	40
	TOTAL	160
<b>FY96</b>	CEM	60
	Poverty/LSMS	30
	Rural Development Study	30
	EWO/SWO	40
	TOTAL	160

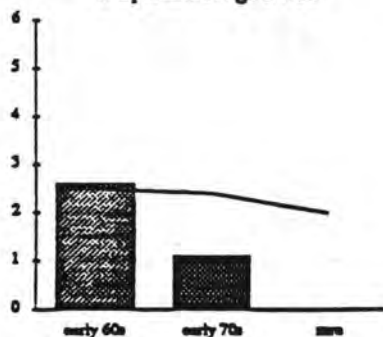
\* To be completed in subsequent FY

# Social Indicators of Development, 1991-92

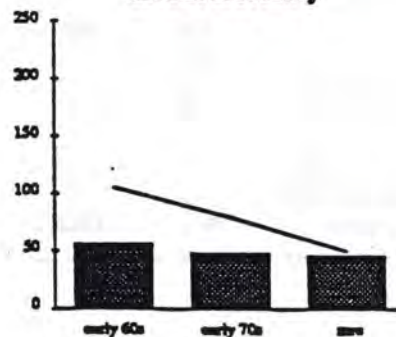
## Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>HUMAN RESOURCES</b>							
<b>Size, growth, structure of population</b>							
Total population (mre = ...)	thousands	2,151	2,767		256,356	629,102	458,731
14 and under	% of pop.	43.6	41.2	36.5	42.8	37.3	33.8
15-64		51.2	53.9	57.8	53.2	57.8	60.9
Age dependency ratio	unit	0.95	0.86	0.73	0.86	0.72	0.63
Percentage in urban areas	% of pop.	49.5	68.6	83.7	55.3	58.6	71.8
Females per 100 males							
Urban	number	--	--	--	--	--	--
Rural		--	--	--	--	--	--
Population growth rate	annual %	2.6	1.1	0.1	2.9	2.0	1.7
Urban		6.7	3.8	0.6	4.1	3.2	2.8
Urban/rural growth differential	difference	7.9	8.3	4.7	2.6	2.4	3.6
Projected population: 2000	thousands	--	--	3,013	340,932	768,976	541,229
Stationary population		--	--	6,044	--	--	--
<b>Determinants of population growth</b>							
<b>Fertility</b>							
Crude birth rate	per thou. pop.	40.4	30.9	30.2	39.3	29.5	24.9
Total fertility rate	births per woman	6.17	4.55	3.62	5.39	3.74	3.10
Contraceptive prevalence	% of women 15-49	--	55.0	--	--	--	--
<b>Child (0-4) / woman (15-49) ratios</b>							
Urban	per 100 women	--	--	--	--	--	--
Rural		--	--	--	--	--	--
<b>Mortality</b>							
Crude death rate	per thou. pop.	12.4	8.9	8.8	10.1	8.5	7.5
Infant mortality rate	per thou. live births	56.0	48.0	45.8	79.5	49.5	41.8
Under 5 mortality rate		--	--	59.0	87.8	79.5	49.8
Life expectancy at birth: overall	years	62.0	65.0	65.5	60.5	65.3	68.3
female		63.9	67.0	67.5	62.2	67.9	71.5
<b>Labor force (15-64)</b>							
Total labor force	thousands	578	771	914	70,804	237,840	172,535
Agriculture	% of labor force	29.2	17.0	--	--	--	--
Industry		24.0	26.3	--	--	--	--
Female		16.1	20.5	27.8	14.6	32.3	30.4
Females per 100 males							
Urban	number	--	--	--	--	--	--
Rural		--	--	--	--	--	--
Participation rate: overall	% of labor force	26.9	27.9	30.8	28.5	40.6	38.5
female		8.7	11.5	16.6	8.5	25.6	23.3
<b>Educational attainment of labor force</b>							
School years completed: overall	years	--	--	--	--	--	--
male		--	--	--	--	--	--
<b>NATURAL RESOURCES</b>							
Area	thou. sq. km	10.40	10.40	10.40	11,667	22,765	18,709
Density	pop. per sq. km	207	266	258	21	27	24
Agricultural land	% of land area	29.4	33.2	29.9	27.5	40.9	34.3
Agricultural density	pop. per sq. km	703	802	863	78	66	70
Forest and woodland	thou. sq. km	0.95	0.90	0.80	413	6,174	7,116
Deforestation rate (net)	annual %	0.0	0.0	0.0	0.5	-0.5	-0.5
<b>Access to safe water</b>							
Urban	% of pop.	--	--	--	--	78.2	88.7
Rural		--	--	77.0	--	46.9	63.8

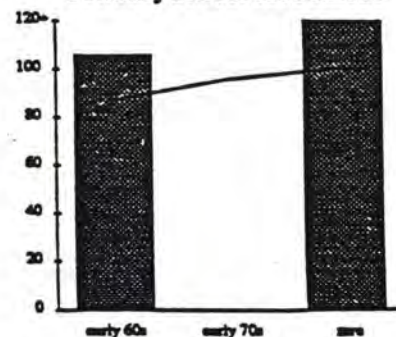
Population growth



Infant mortality



Primary school enrollment



■ Lebanon — Lower-middle-income

Note: Extreme values for population growth are unshaded.

## Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>INCOME AND POVERTY</b>							
<b>Income</b>							
GNP per capita (mre = ...)	US\$	--	--	--	1,830	1,530	3,450
<b>Total household income</b>							
Share to top 10% of households	% of income	--	--	--	--	--	--
Share to top 20% of households	"	--	--	--	--	--	--
Share to bottom 40% of households	"	--	--	--	--	--	--
Share to bottom 20% of households	"	--	--	--	--	--	--
<b>Poverty</b>							
Absolute poverty income: urban	US\$ per person	--	--	--	--	--	--
rural	"	--	219	--	--	--	--
Pop. in absolute poverty: urban	% of pop.	--	--	--	--	--	--
rural	"	--	--	--	--	--	--
Prevalence of malnutrition (under 5)	% of age group	--	--	--	--	--	--
<b>EXPENDITURE</b>							
<b>Food</b>							
Staples	% of GDP	--	--	--	--	--	--
Meat, fish, milk, cheese, eggs	"	--	--	--	--	--	--
Cereal imports	thou. metric tonnes	401	585	356	39,093	38,868	39,280
Food aid in cereals	"	--	26	16	--	--	--
Food production per capita	1979-81=100	93.7	84.3	136.6	108.6	98.9	106.0
Share of agriculture in GDP	% of GDP	11.6	9.2	--	14.3	16.8	9.0
Daily calorie supply	calories per person	2,485	2,453	3,274	3,012	2,780	3,013
Daily protein supply	grams per person	67	61	86	79	72	77
<b>Housing</b>							
Average household size	persons per household	--	--	--	--	--	--
Urban	"	--	--	--	--	--	--
Fixed investment: housing	% of GDP	--	--	--	--	--	--
<b>Fuel and power</b>							
Energy consumption per capita	kg of oil equivalent	712.9	825.0	968.5	1,048.2	1,102.2	1,794.4
Households with electricity	% of households	--	--	--	--	--	--
Urban	"	--	--	--	--	--	--
Rural	"	--	--	--	--	--	--
<b>Transport and communication</b>							
Population per passenger car	persons	22	12	--	67	24	11
Fixed investment: transport equipment	% of GDP	--	--	--	--	--	--
Total road length	km	--	--	--	--	--	--
Population per telephone	persons	--	--	--	--	--	--
<b>INVESTMENT IN HUMAN CAPITAL</b>							
<b>Medical care</b>							
Population per: physician	persons	1,006	--	--	1,333	--	--
nurse	"	2,029	965	--	--	--	--
hospital bed	"	--	--	--	--	--	--
<b>Access to health care</b>							
Immunized (under 12 months): measles	% of pop.	--	--	--	--	--	--
DPT	% of age group	--	--	15.0	78.9	65.3	78.5
Oral Rehydration Therapy use (under 5)	% of cases	--	--	33.0	84.8	67.1	81.5
	"	--	--	10.0	45.4	39.8	--
<b>Education</b>							
<b>Gross enrollment ratios</b>							
Primary: total	% of school-age group	106.0	--	128.0	89.7	100.5	105.9
female	"	93.0	--	94.0	81.2	97.4	--
Secondary: total	"	26.0	50.0	67.0	54.3	58.3	56.3
female	"	20.0	--	56.0	51.2	56.5	58.9
Tertiary: science/engineering	% of tertiary students	8.1	--	17.7	--	--	--
Pupil-teacher ratio: primary	pupils per teacher	24	10	6	22	26	25
secondary	"	17	--	--	20	18	--
<b>Pupils reaching grade 4</b>							
Repeater rate: primary	% of cohort	--	--	--	--	86.7	77.8
Mliteracy rate: overall	% of total enrollment	--	--	--	10.2	6.6	17.6
female	% of pop. (age 15+)	--	--	19.9	47.0	22.9	15.1
	% of females (age 15+)	--	--	26.9	59.5	28.8	17.7
Newspaper circulation	per thou. pop.	83.7	102.3	88.1	35.4	72.0	100.9



4:09 PM  
11 May 1993

Lebanon: Key Indicators

	Estimate		Projected							
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
<b>Real Growth Rates:</b>										
Gross Domestic Product (GDP)	-13.4	50.2	10.0	10.0	8.0	8.0	8.0	8.0	5.7	5.5
Gross Domestic Income (GDY)	-13.9	49.7	9.8	10.0	8.0	8.1	8.1	8.1	5.8	5.7
<b>Real Per Capita Growth Rates:</b>										
Gross Domestic Product (GDP)	-15.1	47.3	7.8	7.8	5.9	5.9	5.9	5.9	3.8	3.6
Total Consumption	-8.5	53.6	4.9	1.1	-4.0	1.0	1.3	7.1	0.7	0.3
Private Consumption	-11.1	56.4	6.0	0.2	-5.1	0.5	1.4	7.6	0.6	0.3
<b>External Debt &amp; D. Services (LT+ST+IMF):</b>										
Total External Public Debt (US\$M)	0.0	360.7	296.6	586.6	926.6	1301.6	1666.6	1921.3	2145.7	2374.0
Public Sector External Debt Service (US\$)	14.2	3.7	100.2	70.8	90.1	117.3	150.3	189.5	225.6	240.2
Public Sector Debt Service / Exports	1.7	0.3	7.6	4.2	4.1	4.0	4.1	4.1	4.3	4.1
Public Sector Debt Service / GDP	0.6	0.1	1.8	1.0	1.2	1.4	1.6	1.8	1.9	1.9
<b>Interest Burden (LT+ST+IMF):</b>										
Public Sector Interest Paid (US\$M)	14.2	3.7	36.0	20.8	40.1	67.3	100.3	129.2	149.9	168.6
Public Sector Interest / Exports	1.7	0.3	2.7	1.2	1.8	2.3	2.7	2.8	2.9	2.9
Public Sector Interest / GDP	0.6	0.1	0.6	0.3	0.5	0.8	1.0	1.2	1.3	1.3
<b>Gross Investment / GDP</b>										
ICOR (annual)	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
ICOR (5-yr ending year shown)	-1.5	0.4	2.0	2.3	3.5	4.5	4.7	4.2	4.2	4.0
<b>Domestic Savings / GDP</b>										
BOP Resource Balance / GDP	-46.4	-45.0	-35.2	-25.3	-14.9	-10.3	-7.0	-9.1	-6.7	-4.1
<b>National Savings / GDP</b>										
BOP Current Account Balance / GDP	-66.4	-65.0	-54.9	-49.1	-45.5	-42.4	-35.6	-29.3	-25.4	-21.8
<b>Government Investment / GDP</b>										
Government Savings / GDP	-4.0	-22.7	-20.1	-12.0	-3.8	-1.2	0.1	-3.4	-1.9	0.2
Private Investment / GDP	-24.0	-42.7	-39.8	-35.8	-34.4	-33.2	-28.5	-23.6	-20.6	-17.5
Private Savings / GDP	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Government Expenditures / GDP	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Budget Deficit (+) or Surplus / GDP	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8
Primary Deficit (+) or Surplus / GDP	31.3	-8.2	-10.1	-7.7	-2.8	-1.3	-1.1	-5.9	-5.0	-3.7
<b>Government Revenues / GDP</b>										
Government Expenditures / GDP	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Budget Deficit (+) or Surplus / GDP	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
Primary Deficit (+) or Surplus / GDP	38.1	19.3	13.1	12.0	11.5	10.7	9.8	2.4	1.8	1.1
<b>GDP Deflator (% growth rate)</b>										
	25.9	14.2	7.7	6.6	6.9	6.0	5.0	-1.4	-1.5	-1.7
	68.8	51.7	116.1	25.0	10.0	10.0	10.0	6.0	5.2	3.8

4:09 PM  
11 May 1993

Lebanon: Key Indicators

	Estimate			Projected						
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Continued										Continued
Real Exchange Rate (LL / US\$) (1990=100)	100.0	88.9	76.7	72.5	72.5	72.5	72.5	72.5	72.5	72.5
Terms of Trade Index (1990=100)	100.0	98.8	98.3	98.4	98.7	99.2	99.4	99.7	99.9	100.1
Export (GNFS)/Volume Growth Rate	-3.7	24.4	23.3	21.8	25.5	27.3	22.0	19.0	9.6	7.4
Exports (GNFS) / GDP	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports (GNFS) Volume Growth Rate	0.7	51.1	11.8	9.5	8.7	11.1	4.8	4.7	2.4	1.4
Imports (GNFS) / GDP	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Current Account Balance (US\$M)										
(before grants)	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
(after grants)	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
BdL Foreign Exchange Reserves (US\$M)	620.0	1233.3	1448.0	1737.1	2081.0	2539.3	2911.2	3161.4	3359.6	3535.5
Official Reserves (months imports) 7/	3.1	3.9	4.0	4.3	4.5	4.8	5.0	5.0	5.0	5.0

1. "LT" denotes "long-term debt;" "ST" denotes "short-term debt"
2. "DOD" denotes "debt outstanding and debt disbursed."
3. "ICOR" denotes "incremental capital output ratio" with a 5-years period.
4. "BOP" denotes "balance of payments"
5. Current account balance as defined in line F.1 on annex B3
6. "GNFS" denotes "goods and nonfactor service".
7. Excludes gold.

4:08 PM  
11 May 1993

Projection Table 1. Balance of Payments  
(in millions of US\$)

	1989	1990	1991	1992	1993	1994	Projected		1997	1998	1999
							1995	1996			
	(US\$ millions)										
Resource Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Merchandise Trade Balance	-1707.0	-1859.0	-2997.0	-3322.1	-3719.0	-4069.7	-4540.9	-4744.2	-4926.9	-5132.7	-5264.1
Merchandise Exports	539.0	537.0	750.0	987.0	1185.7	1479.5	1874.2	2242.6	2660.4	2930.4	3221.2
Merchandise Imports	2246.0	2396.0	3747.0	4309.1	4904.7	5549.2	6415.2	6986.9	7587.3	8063.1	8485.3
Net NonFactor Services	200.0	200.0	200.0	222.0	365.6	583.8	903.0	1314.5	1761.5	2120.1	2433.7
Exports of NonFactor Services	300.0	300.0	300.0	338.2	491.9	715.5	1039.8	1457.1	1920.8	2292.9	2618.0
Imports of NonFactor Services	100.0	100.0	100.0	116.2	126.3	131.7	136.8	142.6	159.3	172.8	184.3
Net Factor Income	507.0	479.0	480.0	453.9	458.8	371.6	287.2	164.0	69.2	-2.8	-36.0
Net Current Transfers	680.0	580.0	480.0	400.0	450.0	475.0	500.0	525.0	550.0	575.0	600.0
Current Account Balance (before grants)	-320.0	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
Capital Official Grants	0.0	0.0	70.7	0.0	200.0	200.0	200.0	200.0	100.0	100.0	100.0
Current Account Balance (after grants)	-320.0	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
Direct Foreign Investment	0.0	0.0	0.0	0.0	300.0	800.0	800.0	800.0	500.0	500.0	500.0
Public M&LT (net disbursement)											
Gross Disbursement	..	..	..	0.0	340.0	390.0	425.0	415.0	315.0	300.0	300.0
Amortization	..	..	..	-64.2	-50.0	-50.0	-50.0	-50.0	-60.3	-75.6	-71.7
Net Disbursement	14.1	23.1	33.9	-64.2	290.0	340.0	375.0	365.0	254.7	224.4	228.3
Net Other Capital Flows 1/	262.9	279.9	2301.4	2525.1	1943.7	1643.3	1934.1	1747.6	1941.6	1814.3	1613.9
Overall Balance 2/	-43.0	-297.2	569.0	214.7	289.1	343.9	458.4	371.9	250.2	198.2	175.9
Increase in Bdl. Reserves	43.0	297.2	-569.0	-214.7	-289.1	-343.9	-458.4	-371.9	-250.2	-198.2	-175.9

Sources: Data provided by the Bank of Lebanon; IMF, Direction of Trade;  
and staff estimates and projections.

1/: Comprised of net private medium and long term debt, net short term capital, trade credits, unidentified capital flows, and errors and omissions.  
2/: Includes only non-gold reserves of the Bdl.

Elasticity of total imp. to GDP growth rate/growth rate	-0.05	1.02	1.18	0.95	1.09	1.39	0.60	0.58	0.43	0.26	
adjusted for Real Exchange Rate	-0.05	1.02	0.49	0.67	1.09	1.39	0.60	0.58	0.43	0.26	
Elasticity of NonInv. imports to GDP adjusted for Real Exchange Rate	-0.05	1.01	0.25	0.25	0.05	0.00	0.05	0.95	0.80	0.50	
Average Exchange Rate	496.5	701.8	928.2	1683.0	1912.8	2025.1	2146.1	2274.3	2322.5	2353.8	2353.8

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	Actual					Projection					
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
(In billions of Lebanese Pounds)											
Total Revenue	62.6	126.4	456.7	984.0	2100.0	2794.1	3405.2	4164.9	4768.0	5299.3	5803.2
Total Expenditure 1/	534.7	794.5	1229.1	2229.3	3662.1	4571.4	5378.2	6314.2	5368.2	5803.9	6124.6
Current Expenditures	495.0	745.2	1036.6	1929.3	2657.2	2945.6	3374.9	3885.8	4130.4	4428.3	4618.1
Wages & Salaries	96.9	210.0	370.0	738.9	887.0	1064.4	1224.1	1370.9	1480.6	1584.3	1663.5
Other Current (incl. Transfers)	58.3	96.7	240.6	425.8	875.1	1039.6	1235.0	1467.2	1704.7	1922.6	2105.4
Extrabudgetary Transfers	88.3	179.0	184.0	90.0	117.0	100.0	50.0	0.0	0.0	0.0	0.0
Petroleum Subsidy	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
Interest Payments	152.2	213.5	206.9	514.6	698.2	711.6	865.8	1047.7	945.1	921.5	849.3
Private Sector Credit	151.5	203.5	203.5	454.0	658.5	630.4	721.4	819.7	645.1	568.5	452.5
Foreign Sector Interest	0.7	10.0	3.4	60.6	39.7	81.1	144.5	228.0	300.0	352.9	396.8
Capital Expenditures 2/	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
of which Reconstruction Program:											
in Lebanese Pounds					573.8	1113.8	1394.9	1705.7			
in US Dollars					300.0	550.0	650.0	750.0			
Current Budget Balance	-432.4	-618.8	-579.9	-945.3	-557.2	-151.5	30.2	279.0	637.5	871.0	1185.1
Overall Deficit	-472.1	-668.1	-772.4	-1245.3	-1562.1	-1777.3	-1973.0	-2149.3	-600.2	-504.6	-321.4
Financing	472.1	668.1	772.4	1245.3	1562.1	1777.3	1973.0	2149.3	600.2	504.6	321.4
External	7.0	16.2	97.1	-108.0	937.3	1093.6	1234.0	1285.0	823.8	763.5	772.8
Net Borrowing	7.0	16.2	31.5	-108.0	554.7	688.5	804.8	830.1	591.5	528.2	537.5
Grants	0.0	0.0	65.6	0.0	382.6	405.0	429.2	454.9	232.2	235.4	235.4
Domestic	465.1	651.9	675.3	1353.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
Net Bank of Lebanon	134.2	351.9	-424.2	-577.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Other 3/	330.9	300.0	1099.5	1930.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
Memorandum Items:											
Domestic Public Debt	..	..	..	4115.4	4740.2	5424.0	6163.0	7027.3	6803.7	6544.8	6093.4
External Public Debt	0.0	0.0	317.1	548.8	1158.5	1932.4	2876.7	3830.4	4492.2	5050.4	5647.1
Total Public Debt	..	..	..	4664.2	5898.7	7356.4	9039.7	10857.7	11295.9	11595.3	11740.5

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	1989	Actual 1990	1991	1992	1993	1994	Projection 1995	1996	1997	1998	1999
(In percent of GDP)											
Total Revenue	5.2	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Total Expenditure	44.6	45.3	30.8	23.5	28.0	29.5	29.2	28.8	21.4	20.8	20.1
Current Expenditure	41.3	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
Capital Expenditure	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
of which: Reconstruction Program					4.4	7.2	7.6	7.8			
Current Budget (- deficit)	-36.1	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Overall Deficit	-39.4	-38.1	-19.3	-13.1	-12.0	-11.5	-10.7	-9.8	-2.4	-1.8	-1.1
(In percent of Total Expenditure)											
Total Revenue	11.7	15.9	37.2	44.1	57.3	61.1	63.3	66.0	88.8	91.3	94.8
Overall Deficit	-88.3	-84.1	-62.8	-55.9	-42.7	-38.9	-36.7	-34.0	-11.2	-8.7	-5.2
Memorandum Items: (In billions of Lebanese Pounds)											
Nominal GDP	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
(In percent of GDP)											
Domestic Public Debt	..	..	..	43.3	36.3	35.0	33.4	32.1	27.1	23.5	20.0
External Public Debt	0.0	0.0	7.9	5.8	8.9	12.5	15.6	17.5	17.9	18.1	18.5
Total Public Debt	..	..	..	49.1	45.2	47.4	49.0	49.6	45.1	41.6	38.5

Sources: Data provided by the Lebanese authorities; and staff estimates and projections.

a/: Central Budget, Extra budgetary Accounts, Annexed Budgets and CDR.

1/: Includes net lending.

2/: Includes domestic financing of CDR capital expenditures assumed to have come through transfers from the central government.

The 1992 value is based on the proposed budget of 1992.

3/: Comprised of net commercial banks and non-bank public.

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

National Account, Estimates and Projections: 1990-1999 (in billions of current Lebanese Pound)											
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
GDP at market prices	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
Net Indirect Taxes	-95.7	-42.3	96.5	282.5	888.0	1288.9	1659.0	1970.9	2256.3	2507.7	2746.1
Indirect Taxes	3.6	3.7	131.6	442.5	968.0	1318.9	1659.0	1970.9	2256.3	2507.7	2746.1
Subsidies	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
GDP at factor cost	1294.4	1795.1	3898.6	9216.2	12172.7	14227.3	16774.2	19927.7	22813.2	25355.5	27766.6
Resource Balance	-748.2	-1164.2	-2596.3	-5217.4	-6414.4	-7059.4	-7807.3	-7800.1	-7351.5	-7091.1	-6662.0
Total Imports	1164.8	1751.6	3570.9	7447.7	9623.3	11504.6	14061.0	16214.2	17991.1	19385.5	20406.3
Total Exports	416.6	587.4	974.6	2230.3	3208.9	4445.2	6253.7	8414.1	10639.7	12294.4	13744.3
Total Expenditures	1946.9	2917.0	6591.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Total Consumption	1707.2	2566.5	5792.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Government Consumption	124.4	255.5	483.3	944.9	1324.5	1636.2	1965.1	2251.3	2503.5	2737.8	2926.7
Private Consumption	1582.8	2310.9	5309.0	11899.4	15037.6	16184.5	18375.5	21184.0	24853.4	26998.4	28845.5
Gross Domestic Investment	239.7	350.6	799.0	1871.8	3113.0	4754.9	5899.9	6263.4	5064.1	5218.1	5402.6
Government	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
Private	200.0	301.3	606.5	1571.8	2108.2	3129.0	3896.6	3835.1	3826.3	3842.4	3896.1
(In Millions of Current US Dollars)											
Memorandum Items:											
GDP at Market Prices	2414.3	2497.7	4304.0	5643.9	6828.0	7661.9	8589.3	9628.9	10794.4	11837.6	12963.3
Per Capita GDP	677.6	687.1	1160.7	1492.2	1769.9	1947.1	2140.0	2352.0	2585.0	2784.7	2995.6
Merchandise Trade Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Exports	839.0	837.0	1050.0	1325.2	1677.6	2195.0	2914.0	3699.7	4581.2	5223.3	5839.2
Imports	2346.0	2496.0	3847.0	4425.2	5031.0	5681.0	6552.0	7129.4	7746.6	8235.9	8669.6

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
National Account, Estimates and Projections: 1990-1999 (in billions of constant 1990 Lebanese Pound)											
GDP at market prices	2023.8	1752.8	2633.1	2896.4	3186.1	3441.0	3716.2	4013.5	4334.6	4579.5	4831.4
Resource Balance	-1129.4	-1164.2	-1915.3	-2057.6	-2140.7	-2141.7	-2156.8	-1959.7	-1744.6	-1604.6	-1458.8
Exports	610.1	587.4	730.6	900.9	1097.5	1377.8	1753.7	2139.8	2546.6	2790.6	2998.5
Imports	1739.5	1751.6	2645.9	2958.5	3238.2	3519.4	3910.5	4099.5	4291.2	4395.2	4457.2
Total Consumption	2748.4	2566.5	4021.8	4302.4	4434.7	4343.9	4475.8	4624.7	5050.6	5176.6	5285.2
Government Consumption	200.2	255.5	335.6	316.5	359.0	398.8	432.4	444.3	462.2	476.6	486.9
Private Consumption	2548.2	2310.9	3686.2	3985.8	4075.7	3945.0	4043.4	4180.4	4588.4	4700.0	4798.4
Gross Domestic Investment	404.8	350.6	526.6	651.7	892.1	1238.7	1397.3	1348.5	1028.6	1007.5	1004.9
Government	67.0	49.3	126.9	104.5	288.0	423.6	474.4	522.8	251.4	265.6	280.2
Private	337.7	301.3	399.7	547.2	604.1	815.2	922.9	825.7	777.2	741.9	724.7
Memorandum Item: Per Capita Real GDP	568.0	482.2	710.1	765.8	825.9	874.5	925.9	980.4	1038.0	1077.3	1116.4
(in percent of GDP)											
Resource Balance	-62.4	-66.4	-65.0	-54.9	-49.1	-45.5	-42.4	-35.6	-29.3	-25.4	-21.8
Exports	34.8	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports	97.2	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Total Consumption	142.4	146.4	145.0	135.2	125.3	114.9	110.3	107.0	109.1	106.7	104.1
Government Consumption	10.4	14.6	12.1	9.9	10.1	10.5	10.7	10.3	10.0	9.8	9.6
Private Consumption	132.0	131.8	132.9	125.3	115.1	104.3	99.7	96.7	99.1	96.9	94.5
Gross Domestic Investment	20.0	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
Government	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Private	16.7	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8

## OFFICE MEMORANDUM

Rec'd 7/14

DATE: July 12, 1993

CONFIDENTIAL

TO: Mr. Attila Karaosmanoglu, Managing Director

FROM: Caio Koch-Weser, MNAVP *ckw*

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

EXTENSION: 35250

SUBJECT: LEBANON: Country Strategy Note

Please find attached the Country Strategy Note for Lebanon, which we reviewed at a Regional Loan Committee meeting on July 6, 1993.

Messrs./Mesdames

Sandstrom, Stern, Armitage, Kalantzopoulos (EXC); Thahane (SEC); Alisbah (PAAVP); Choksi (HROVP); Eccles (CTRPV); Einhorn (TREV); Husain (LACVP); Jaycox (AFRVP); Kaji (EAPVP); Kashiwaya (CFSVP); Linn (FPRVP); Picciotto (DGO); Rao (DECVP); Rischard (FPDVP); Serageldin (ESDVP); Shihata (LEGVP); Thalwitz (ECAVP); Wood (SASVP); Ryrie (CEXVP); Iida (MIGEX); Ray (DPG).

Messrs./Mesdames

Husain, Squire, Murli, Bouhabib, Kafka (MNAVP); Chopra, Tyler, Heron, O'Donnell (MN2DR); Kohli, (MN1DR); Sood (EMTDR); Voyadzis, Hoppenbrouwer, Ozeki (MN2CO); Okonjo-Iweala, Barres (MN2AG); Bhargava, Jordan (MN2IE); McKechnie, Graham (MN2IN); Keare, Sederlof (MN2PH); Hovaguimian (CMEDR); Alizai (COGDR); Pfeffermann (CEIED); Haddad (CMED2); Nishimizu (FRSDR); Bhattacharya (FRSCR); Sud (CFSDR); Birdsall (CECDR); Petit (AGRDR); El-Ashry (ENVDR); Iskander (PSD); Long (FSD); Adams (OPRDR); Hollywood (MIGGU); Morais, Abushahr (LEGMN); Chabrier, Handy (IMF); MNA Files.

L. Hoppenbrouwer  
M:\leb\csnmd

*2*



Document of  
The World Bank

CONFIDENTIAL

**DECLASSIFIED**  
**MAR 31 2017**  
**WBG ARCHIVES**

**REPUBLIC OF LEBANON**  
**COUNTRY STRATEGY NOTE**

July 12, 1993

Country Operations Division  
Country Department II  
Middle East and North Africa Region

LEBANON  
COUNTRY STRATEGY NOTE

TABLE OF CONTENTS

	<u>Page no.</u>
EXECUTIVE SUMMARY.....	i
Economic and Political Background.....	1
Development Issues and Policy Agenda.....	2
Physical and Social Infrastructure.....	4
Environment.....	6
Human Resources Development.....	7
Productive Sectors.....	8
Macroeconomic Prospects.....	9
Introduction.....	9
Base Case.....	9
Alternative Scenarios.....	10
Creditworthiness and External Capital Requirements....	10
Bank Assistance Strategy.....	11
Coordination with other Institutions.....	13
Bank Share of Financing.....	14
Downside Risks.....	15
Objectives and Instruments of Country Assistance Strategy.....	16
ANNEX I      Lending Program (Base Case)	
ANNEX II     Economic and Sector Work Program	
Social Indicators of Development Key Indicators and Projections	

# LEBANON

## COUNTRY STRATEGY NOTE

### EXECUTIVE SUMMARY

*Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of war. By 1990, per capita income (about \$820) was only about one-third of the 1975 level in real terms. The total damage to physical assets was estimated by the United Nations at \$25 billion. The impact on social conditions has been grave, with considerable loss in human resources, one quarter of the population of 3.6 million displaced, and public and social services either non-existent or of poor quality.*

*A sharp post-war recovery in 1991 was followed by an economic crisis in 1992, triggered by successive governments' failure to address fiscal imbalances. In October 1992, a new government took office following parliamentary elections. Prime Minister Hariri and his Cabinet enjoy broad political support. Government faces the daunting task of rehabilitating the war-damaged economy while maintaining economic and political stability, rebuilding a devastated public administration, and enticing the private sector to invest. Initial confidence triggered a significant inflow of capital and helped reestablish stability, which remains fragile, however, and will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.*

*Lebanon's vigorous and dynamic private sector continues to be the country's main asset. Beyond the initial stage of reconstruction to restore basic physical and social infrastructure, steady long-term growth will be predicated upon renewed private sector initiative. The government intends to support private sector initiative by creating an appropriate enabling environment, and efficient public administration, and investing in human resources. Before the protracted war, human resources were well developed and health facilities adequate, but there was a general neglect of social concerns. At present the*

*needs in health and education are massive. Continued political stability will not be maintained unless social issues and human resources development are addressed.*

*The serious damage sustained to basic infrastructure now presents the most immediate obstacle to economic revival. Mr. Hariri's government has a unique window of opportunity to undertake the ambitious task of reconstruction, establish economic stability, and lay the basis for private sector-led recovery. Lebanon needs substantial amounts of official external assistance to finance an ambitious \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96. In addition, reconstruction and recovery will require large amounts of private capital. Total capital requirements in the medium term would amount to around \$3.0 billion per annum. The bulk of this is expected to be available from private capital inflows, provided political and economic stability are maintained.*

*The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. The \$175 million Emergency Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which institutional and economic reform is feasible. The Bank now has a fairly unique opportunity, at above average risks, to play a major role in the recovery of Lebanon. Towards the overall objective of a resumption of rapid growth and reduction of poverty, the Bank would support a private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity,*

rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development.

Future lending would concentrate heavily on the social sectors, and would also support the strengthening of the public administration, and selected public investments in physical infrastructure during the reconstruction phase and future expansion by the private sector. The frontloaded ESW would underpin future lending and help government establish an enabling environment for private sector development. We would convene a CG meeting to help mobilize external resources for the NERP provided the Government continues to mount and implement an economic program satisfactory to the IMF and the Bank.

The proposed base case lending program of three operations for an average of \$85 million per year during FY94-98, with some frontloading, would be conditional upon the maintenance of an acceptable overall macroeconomic framework and the availability of financing from other sources. We would also need to continuously monitor the evolution of the political situation. A decline in government commitment to fiscal adjustment would trigger a low case lending program. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. The proposed ESW is for 180 SW on average during FY94-96 with frontloading.

In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank throughout the war. External public debt, an estimated \$360 million (8% of GDP) at the end of 1991, is low by any standard. Despite a projected five-fold increase by 1996 because of the external financing required for the NERP, debt indicators would remain low, with a public debt to GDP ratio of 18% and a public debt service to exports ratio of less than 5%. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP. The Bank would account for 12% of gross loan and grant disbursements during 1993-96, and 20% of external public

debt by 1999. Lebanon's stock of external public debt would remain small by any standard, while its external reserve position - \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. In view of the past track record with the Bank and the government's commitment to fiscal stabilization, the amounts of planned lending are considered prudent.

There are risks that current economic stability will not be sustainable in the absence of action to correct macroeconomic imbalances and that external events, particularly regional developments, could upset political stability. The population's high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war, and the need to carefully balance the interests of the various denominational factions, could hamper the government's ability to take required measures. With the continued presence of the Syrian army, and the occupation of part of the country's territory by Israel and the Southern Lebanese army, there could be far-reaching implications for Lebanon if the Middle East peace process were to fail.

In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The government is well aware that economic stabilization is a pre-condition for sustained, private sector-led, recovery and growth, and has begun to take fiscal actions. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

The main issue for Management is:  
are the proposed strategy and lending and ESW programs appropriate given Lebanon's circumstances, needs, prospects, and the various political and economic risks involved ?

## LEBANON

### COUNTRY STRATEGY NOTE

#### Economic and Political Background

1. Lebanon, a prosperous upper middle-income country in the mid-70s, has been devastated by 15 years of turmoil as a result of violent civil strife and military occupation. In the period between 1950 and 1975, Lebanon's free market economy expanded by about 6% per annum. This growth was largely driven by the service sectors, namely trade, tourism, and finance, which attracted business from surrounding oil-based economies. After the eruption of civil war in 1975, the economy deteriorated markedly, with intermittent recovery during the two periods of relative calm, 1978 to 1981, and 1986 to 1988.
2. The civil war had a severe impact on the socio-economic conditions in the country. Lebanon's per capita GNP, about US\$820 in 1990, in real terms was only about one third of the 1975 level, and income inequalities have been accentuated. The total damage to physical assets during the war period was estimated by the United Nations at US\$25 billion. All principal sectors of the Lebanese economy - physical and social infrastructure, office and factory buildings, and housing - have been affected. Damage is both a direct result of the war, as well as the accumulated effects of a near total disruption in capital investment and maintenance.
3. The impact of the civil war on social conditions has been equally grave. The loss in human resources has been considerable; apart from the tragic loss of life and the disabling of hundreds of thousands of people, about 200,000 professional and skilled Lebanese have sought employment in other countries. While this has resulted in major shortages of skilled workers in various sectors of the economy, unemployment nevertheless is estimated at 35% of the resident labor force, and is believed to be particularly high among urban youth. Nearly one quarter of the population of 3.6 million has been displaced and now lives in unhealthy shanty towns, and in semi-destroyed and vacated buildings, with severe overcrowding and inadequate housing quality. Urban poverty problems are especially pressing in Beirut. Public and social services are either non-existent or of poor quality, with only about one third of power capacity operating, water treatment and sewage virtually nonexistent, and most schools and hospitals damaged.
4. The 1989 Ta'if Accord for National Reconciliation, sponsored by the Arab League, was a first step toward bringing an end to the violence in late 1990. The national army was reunified, and a Syrian backed national unity government reestablished its authority over the Greater Beirut area and most of the national territory. Attempts to achieve economic stabilization since the end of the fighting in 1990 have yielded mixed results. During 1991, activity took off in virtually every sector of the Lebanese economy, spurred by large inflows of private capital, with real GDP expanding by about 40%. At the same time inflation moderated to 30% by year's end from close to 100% the year before, and exchange rate stability was reestablished. However, the government's stabilization policy was not sustainable beyond the short term in the absence of adequate fiscal correction. Interest payments on Treasury Bills, issued to absorb the large speculative capital inflows, merely added further to the fiscal imbalance and the overall fiscal deficit was close to 20% of GDP in 1991. Economic recovery and a real appreciation of the Lebanese Pound led to a sharp surge in imports, which left the current account deficit at an unsustainable high level (more than 40% of GDP). The economic situation worsened in

early 1992, as Central Bank credit to finance the fiscal deficit expanded significantly after the government awarded a 200% retroactive increase in public sector salaries. This triggered a large outflow of capital, including a switch from Pound to Dollar denominated assets, put pressures on the Lebanese pound, and caused disruptively high rates of inflation. In an attempt to defend the value of the Pound, the Central Bank lost \$500 million in reserves in a matter of weeks. The resulting exchange rate crisis, which particularly affected the poorest segments of the population, precipitated a national strike and forced the government to resign in May 1992. A new government was appointed but failed to take stabilization measures and exchange rate depreciation and inflation accelerated throughout the first three quarters of 1992.

5. In September 1992, parliamentary elections were held, and on October 31 a new government was formed. Prime Minister Hariri and his Cabinet enjoy broad political support, and have sparked high expectations. The Christian groups that boycotted the elections are generally supportive of Mr. Hariri, who also reportedly maintains good relations with Shia religious leaders, as well as enjoying both Saudi and Syrian support. Prime Minister Hariri has assembled an impressive economic team, many of whom bring a private sector background to the task of rehabilitating the war-damaged economy while maintaining economic and political stability, and turning around a very weak public administration.

6. The confidence in Mr. Hariri's appointment triggered a significant inflow of capital, which reversed depreciation of the Pound and brought inflation to negligible levels. Since October 1992 the Pound has appreciated by about 25% and inflation has been reduced from over 100% to single digit levels. In addition, it enabled the Central Bank to replenish its reserves (by about \$1.0 billion), and the government to switch from Central Bank credit to Treasury Bills for the financing of its large

deficit (13% of GDP in 1992). The current monetary and exchange rate policy obviously has significant fiscal costs, but the authorities consider this to be an unavoidable consequence of stabilizing the exchange rate. Nevertheless, the speculative nature of these capital inflows suggests that stability will not be lasting until fundamental macroeconomic imbalances, in particular the fiscal deficit, are corrected.

7. Lebanon needs substantial amounts of external assistance in support of stabilization and reconstruction. The government has requested the Bank to assist in the mobilization of the large amount of external resources required to finance its \$2.3 billion National Emergency Recovery Program (NERP) for 1993-96, and has sought IMF advice for the design and implementation of a macroeconomic stabilization program. The donor community has shown a willingness to support the reconstruction of the Lebanese economy. However, in addition to official capital, the reconstruction and recovery of the Lebanese economy will require large amounts of private capital, which will only be forthcoming if political stability is maintained and sustainable economic stabilization established by the government.

#### **Development Issues and Policy Agenda**

8. Endowed with an enterprising population and a geographical location on the trade route between Europe and the Middle East but with no mineral resource base and land that is difficult to cultivate, the Lebanese economy has been oriented to the development of services and light industry. Traditionally, Lebanon has been an open economy, characterized by a large external sector and unrestricted capital mobility, and it had achieved an export-oriented and private sector-led economic development at a good pace mainly through the development of international banking, transit trade, and tourism and, to a lesser extent, through the export of manufactured and agricultural products. With the destruction of much of the nation's infrastructure and productive assets and

dislocation of the human capital after an extended civil war, the reconstruction of the Lebanese economy is a daunting task, and is expected to take massive resource mobilization, capital investment, and development of human resources, and rebuilding of institutions over a protracted period of time. By training its unemployed manpower, restoring the pre-war quality of education, re-equipping labor with infrastructure and productive capital stock, and tapping the resources of its large expatriate community, Lebanon could relatively rapidly rebound and restore rapid growth.

9. Lebanon's reconstruction and development should be guided by the private sector initiative as Lebanon's vigorous and dynamic private sector continues to be the country's main asset. However, in the initial stage of reconstruction, government involvement is crucial as the first order of priority in reconstruction is given to restoration of basic physical and social infrastructure and is to be undertaken by the government under the NERP. Beyond a period of rapid growth that is likely to be associated with the reconstruction phase, sustained domestic investment and steady long-term growth will be predicated upon the renewed private sector initiative. The government's role would be to establish an enabling environment. Above all, it is imperative to sustain the confidence that has been placed in the new government and the Lebanese economy by vigorously pursuing macroeconomic stabilization measures. Moreover, government will need to strengthen public administration and macroeconomic management, and provide clear signals that Lebanon's traditional policies of non-interference with private sector activities will be maintained.

10. Although presumably Lebanon's comparative advantage still lies in international services, tourism, and high value added light manufacturing industry and agriculture, regional competition for financial services and transit trade has increased, the high regional growth associated with the petroleum boom is no longer

present, and other circumstances that had contributed to the rapid growth in the period prior to the mid-1970s are unlikely to be replicated. Hence, prospects for the longer term, including the direction of future growth, are somewhat uncertain at this time, although the resumption of past economic activity, including tourism in particular, is not to be excluded. However, whatever its composition, the potential for growth would be best exploited if government supports private sector initiative.

11. The new government faces the need to undertake stabilization measures simultaneously with its reconstruction program, in order to attract private and official financing for reconstruction. The restoration of fiscal balance - announced by the current government as one of its key objectives - will require drastic action through measures that both raise government revenues from the 1992 level of only 10% of GDP, and contain current expenditures at close to the 1992 level of 20% of GDP. This presents a challenging task, particularly given the virtual collapse of government revenues over the past several years, to the point where revenues covered less than 50% of current expenditures. Since reconstruction will lead to a sharp increase in the presently low level of capital expenditures (a projected average of 10% of GDP during 1993-96), a sharp reduction in the current deficit (10% of GDP in 1992) will be required in order to keep the fiscal deficit in check.

12. Revenue collection and expenditure control in the short run is complicated by administrative weaknesses and rigidity in key expenditure categories. It is therefore necessary to concentrate on policy measures that are straightforward in design, can be implemented quickly, and have good prospects for reducing the current fiscal deficit. Compared to other countries in the region, Lebanon's taxation yields are very low, particularly for direct taxes (2% of GDP in 1992). Key elements in expenditure control include adjustments in power tariffs to reduce budget transfers; the containment of interest payments on internal

debt (which stood at about 40% of GDP at the end of 1992) by gradually lowering interest rates; and containment of the wage bill by limiting wage increases and eliminating ghost workers from the payroll. Subsidies on electricity tariffs have been a major source of the fiscal deficit, as the weighted average tariff is only about one-fifth of economic cost.

13. Over the past half year, the government has already initiated a number of fiscal actions, including administrative measures to improve income and real estate tax and electricity tariff collection, the elimination of wheat subsidies, increases in fees and water and telephone charges and electricity connection fees. The government has maintained public sector wages at the level established in early 1992, in spite of triple digit inflation in 1992. The government's initial measures have resulted in a doubling of revenues during the first quarter of 1993, while expenditure growth has been contained, but further measures, along the lines enumerated in the recent CEM, in particular customs tariff reform and adjustments in power tariffs, will be required to achieve a sustainable reduction in the fiscal deficit.

14. The government envisages a phased strategy for rebuilding Lebanon's ravaged economy and addressing social problems, consisting of a short-term emergency reconstruction phase followed by a medium-term recovery phase. The NERP provides for initial urgent investments, which will be made concurrently with the identification and implementation of longer-term development strategies in the various sectors. The NERP is designed as a multi-sectoral operation, focussed on removing critical infrastructure bottlenecks, alleviating pressing social problems, and strengthening the existing institutions in charge of planning, financing, and implementing the NERP.

15. The phased recovery program envisions that much of the reconstruction will be undertaken by the private sector, with

government supporting the first phase of short-term emergency reconstruction. Lebanon's traditional liberal and investor friendly policies provide a solid base for an expansion of private sector activity and the Lebanese diaspora represents an important source of entrepreneurial skills and capital resources. Yet, the regulatory framework will need to be updated, in part to facilitate private investment for the provision of infrastructure services, and financial sector reform and capital market development will be required for the transformation of resources to long-term investments.

16. Notwithstanding the limited role envisaged for the public sector in the medium- to long-term, there is an urgent need to rebuild public institutions that are dilapidated after 15 years of war and lack qualified personnel, particularly at the middle-levels. The government has, with Bank assistance, begun to define a program for rebuilding public administration, including a technical assistance program to address short term needs for strengthening of economic management and public sector institutions.

#### **Physical and Social Infrastructure**

17. All principal sectors of Lebanon's economy are characterized by widespread damage to physical assets and the obsolescence of remaining facilities, given the reluctance during the years of conflict to invest in new capital or spend on maintenance. The serious damage sustained to basic infrastructure in virtually all sectors now presents the most immediate obstacle to economic revival. As a major regional trade and financial sector, Lebanon's transport infrastructure had been developed intensively prior to the civil war. The thriving service economy of Beirut, where many multinational companies located their regional operations, depended on efficient transport links. During the war, Lebanon's ports and Beirut International Airport, as well as the road and rail networks, sustained severe damage and suffered from a lack of maintenance. Substantial investment will be



needed to restore competitiveness, particularly since other countries within the region have greatly enhanced their own transport networks. The NERP focuses on rehabilitation of international and primary roads, restoring Beirut airport handling capacity to its pre-war level, restoring capacity of the port facilities, and rehabilitating the Beirut bus system. Increased cost recovery, for example through taxes on fuel, customs duties on vehicles, and higher bus tariffs and air passenger fees, is an essential element of the sustainable recovery of transport services.

18. Lebanon meets virtually all its energy needs with imported crude oil and petroleum products. Both of Lebanon's oil refineries sustained heavy damage during the war. The power sector is characterized by a damaged and dilapidated state of the electricity network, as well as an acute shortage of qualified staff at the state-owned Electricite du Liban (EdL). EdL suffers from serious financial difficulties, mainly due to low tariffs, illegal connections, and poor collections. Estimated rehabilitation and expansion needs of the sector amount to about \$830 million. Because of the breakdown in public power supply, most commercial and industrial customers have installed private diesel generating stations, and there is a need to revise the legislative framework in order to regulate private sector activities in the power sector. The high-cost, small-size private systems cannot be expected to fill an anticipated rapid growth of demand as commerce and business enterprises re-establish operations. Tariffs need to be adjusted to adequately reflect costs.

19. The immediate objectives for the power sector should be: (i) reconstructing the war-damaged facilities and removing deficiencies in existing facilities; (ii) setting and maintaining electricity tariffs at levels which cover the full cost of supply, while providing a life-line rate for the first 100 or 200 Kwh/month; (iii) restructuring and corporatizing EdL's activities, and contracting out certain activities (eg. billing, repair), with a view to eventual privatization;

and (iv) upgrading the quality of human resources employed in the sector through training and staff development programs. The NERP includes initial investments of about \$300 million, to provide an integrated and balanced package of improvements.

20. In the telecommunications sector, about one-third of subscribers do not receive service, and those who have access to the network suffer from low quality of service. With the breakdown of public services, private entrepreneurs installed and operated various unlicensed systems. As adequate telecommunications services will be required to restore Lebanon's role as a business, banking and services center in the Middle East, as well as for resuming normal economic and social life, their rehabilitation is among the highest priorities. The NERP focuses on urgent rehabilitation works that can be undertaken without the need for further studies, and which would be compatible with longer-term improvements that are to be identified. In addition to reconstruction of technical installations, the restoration of reliable services requires simultaneous actions to rebuild the sector's management, planning and operating capabilities. The government intends to encourage the role of the private sector in the reconstruction and future development of the telecommunications sector, which will require a review and up-date of the overall legal framework, as well as revamping the government's policy making, regulatory and licensing functions and authority. Tariffs need to be further increased progressively to bring them in line with costs.

21. In the water supply and sanitation sector, there are no functioning sewage treatment facilities in the country, and all water treatment plants have been damaged and are operated at reduced capacity. A 1990 water quality survey indicated unsatisfactory water quality on a widespread scale, which could have serious health implications. Operation and maintenance suffer from inadequate organizational structures and a lack of skilled staff. Damage assessment

surveys indicate that about \$325 million in investments are required for water supply and waste water and for improving solid waste disposal. The undertaking of these investments will require a reorganization of present institutions, with participation from the private sector. Tariffs will have to be raised to ensure adequate internal cash generation for a sustainable development of the sector. The NERP includes: (i) design and execution of physical rehabilitation works; (ii) preparation of a policy strategy paper for institutional and organizational development; (iii) preparation of development programs and feasibility studies for subsequent investments; and (iv) preparation of a water master plan for the country.

22. In housing, the inadequacies of the housing supply mechanism have been exacerbated by the war, but in themselves are more deeply rooted. Lebanon's relatively small size, coupled with its highly dense pattern of settlement and traditionally high construction costs, places housing at a great premium. Furthermore, there have been no urban growth strategy or land-use plans to anticipate and cope with population movements. Substantial capital inflows for real estate speculation led to further distortions in the market system. Because of the different effects generated by internal and external emigration during the war, there is at present a surplus of high quality housing, coexisting with severe pressures in the mid- and lower-quality market.

23. The relocation of displaced persons is considered Lebanon's most pressing social problem, and an appropriate policy framework is required to deal with the complexity of housing sector resettlement and development. The NERP contains a major component for housing finance. In order to initiate rehabilitation of the housing stock by the private sector, appropriate financial instruments need to be developed and mechanisms established for the management and implementation of housing credit, possibly through existing commercial banks. The substantial decline in household real

income levels that occurred during the war eroded the capacity of households to make payments on housing loans. The affordability of housing rehabilitation to certain beneficiary groups therefore will require direct subsidies. In conjunction with other infrastructure components, the housing component of the NERP also will alleviate the immediate environmental problems by resettling households into better conditions and by providing and/or rehabilitating the needed infrastructure services.

### Environment

24. The deteriorated conditions resulting from the extensive war damages cause severe risks to public health and to the environment. The main hazards are: polluted water distribution systems; scattered solid waste dumped all over the country; heavy air pollution on account of energy generation by large numbers of small generators, transport and industrial plants; haphazard expansion of dwellings over fertile lands and natural ecosystems; the abandonment of agricultural lands; the pollution of surface and underground aquifers; widespread deforestation; destruction of the cultural and natural heritage; and the degradation of marine and coastal areas. The planned reconstruction and rehabilitation programs would remedy some of the urgent problems, but the increasing demands for land, water and building materials resulting from them would put additional pressures on the environment.

25. While specific environmental issues are addressed in sector laws and regulations, there is no comprehensive national environmental framework, and the capacity of the Ministry of Environment that was re-established in late 1992 is still very limited. Beyond the actions envisaged under the sectoral programs of the NERP that would address some of the current public health and environmental problems, there will be a need to adopt an environmental strategy to ensure that the process of reconstruction and rehabilitation will contribute to sustainable development.

## Human Resources Development

26. Before the protracted civil strife, Lebanon had a well-trained population and labor force, with adequate health facilities. Nevertheless, there was a general neglect of social concerns during the period of rapid economic growth preceding the war, and at present the needs in health and education are massive. A considerable number of social services, especially in the health sector, are currently provided by non-governmental organizations (NGOs), and are linked to the war situation. In the future, to a large extent these will need to be provided by the public sector. Furthermore, as indicated above, all sectors of the economy, including public administration, suffer from a lack of skilled workers and managers. Social sector ministries are inadequately staffed and are particularly weak.

27. In the health sector, the Ministry of Health (MOH) plays a relatively minor role in the actual provision of services. With the reduced capacity of public hospitals due to war damage and insufficient funds for the rehabilitation and operation of facilities, the MOH ends up directing over 80% of its budget to an uncontrolled reimbursement of private sector (including voluntary agencies) hospital services. The subsidy program, currently running at about \$60 million annually, is poorly targeted and inadequately monitored and controlled. The provision of primary health care services is inadequate, and their delivery currently consists of small dispensaries operated by a myriad of public, private, voluntary and political groups. Overall, the government has little ability to control quality and to enforce standards in the health sector. While generally there is an oversupply of skilled medical doctors in Lebanon, major institutional reforms will be required in the public health sector not only to fill the existing shortage of professional staff, but also to provide greater flexibility in the administration of budgets and in personnel management.

28. The health sector component of the NERP (\$61 million) includes rehabilitation of public hospitals, dispensaries and laboratory services, as well as assistance to rehabilitate care facilities for the disabled provided by charities. Technical assistance components would identify and support the immediate requirements for reform and improved management of subsidy programs, the decentralization of health services management and planning, and the development of MOH into a regulatory body focusing on policy and wider issues of public health. Issues related to the funding of publicly-provided health services also will be examined.

29. Total enrollments in general education declined during the latter part of the civil war, with an increasing share in enrollments for the private sector, which historically has played a significant role within the education sector at all levels. Private sector schools comprise two categories: exclusively fee-paying, and those which are state-subsidized but privately run by welfare institutions. The public sector's share of enrollments is 31% in primary, 46% in intermediate, 33% in secondary, 27% in vocational and technical schools, and 47% in higher education. In the absence of reliable population data, it is difficult to assess enrollment as a percentage of relevant age cohorts.

30. Teacher training activities were essentially suspended in 1987 and in-service training has been conducted irregularly since that date; thus, while the overall pupil/teacher ratio in the public sector is apparently extremely favorable, teachers tend to be poorly trained and localized shortages exist, mostly in rural areas. Enrollments in vocational and technical institutions have been very sensitive to prevailing security and economic conditions. Technical curricula are not relevant to the needs for trained labor, and there is a lack of suitable instructors. The provision of higher education by the public sector (the Lebanese University) expanded rapidly during the war, with an

expansion of campuses in various parts of the country, but quality declined.

31. The development of education facilities in Lebanon must be accompanied by wide-ranging reforms in sectoral policies and in the planning, management and administration of the sector. Substantial expenditures will be required to rehabilitate physical infrastructure and key institutional and policy reforms will require considerable technical assistance. The NERP earmarks about \$150 million for the education sector, to be directed toward four major priorities: i) upgrading the capacity of the teacher training system; ii) improving vocational/technical training centers, curriculum development, instructor training, and instructional materials; iii) rehabilitating public schools, to enhance their capacity to cope with a recovery in enrollments, support the government's resettlement strategy, and enhance educational access for those who cannot afford access to Lebanon's traditionally strong private education sector; and iv) improving the equipment and buildings of the Lebanese University. The government currently does not recover costs for public education; thus cost recovery, particularly with regard to higher education, is an important issue.

32. The issue of women in development has not been high on the government's agenda, and while educational enrollment figures are high, female illiteracy rates are high as well and political participation is limited.

33. Poverty Reduction Efforts. As noted above, after 15 years of war, real incomes have sharply declined, social conditions have worsened significantly and the displacement of up to a quarter of the population from their homes represents a pressing social issue. While poverty appears to be more heavily concentrated in the Greater Beirut area, there are important pockets of rural poverty as well. Social assistance is currently being provided by a large number of NGO's operating in Lebanon, many of which concentrate their efforts on specific

denominational groups. The government lacks information about the incidence and concentration of poverty and neither does it have the resources or mechanisms to address poverty in the short run. The government is of the view that price stability combined with employment to be generated through the reconstruction program will particularly benefit the poor. Nevertheless, it has asked the Bank to help assess the need and possibilities for social safety net mechanisms to accompany the stabilization measures that would need to be undertaken to correct the macro-economic imbalances.

### Productive Sectors

34. Productive activities in Lebanon have traditionally been undertaken almost exclusively by a strong private sector, and it is on private initiative that future growth will depend. The government's main role will be to create an enabling environment for private sector activity in the productive sectors and in the provision of infrastructure. This will require a strengthening of public administration, the development of a legal and regulatory framework that is conducive to attracting private investment, as well as a strengthening of capital markets.

35. Agriculture. Much of Lebanon's arable land (an estimated one-third of the territory) is marginal land and Lebanon has always been a net importer of agricultural and food commodities. The sector contributes about 10% to GDP and accounts for about 20-25% of merchandise exports. The dislocation of production and marketing facilities during the war resulted in a decline in agricultural exports (mainly fruits and vegetables) from close to \$260 million in 1980 to \$170 million in 1990. To regain market shares, Lebanon will have to address both the extensive war damage and the pre-war weaknesses in the agricultural sector. Priority areas for public sector intervention include: (i) rehabilitation and improvement of irrigation schemes and recovery of at least O & M costs of irrigation schemes; (ii) physical reconstruction and institutional development of

the Ministries of Agriculture and Water and Electrical Resources; (iii) the upgrading of applied agricultural research and extension services. As in other sectors, the virtual absence of medium- and long-term credit, particularly for small and medium farmers and agro-industries hampers a recovery of the sector.

36. Industry. The industrial sector contributes about 20% to GDP and accounts for the bulk of merchandise exports. Except for oil refining, industry is entirely within the private sector. The industrial sector faced not only considerable war damage (close to 200 plants were destroyed in the heavy 1989/90 hostilities), but more importantly, a loss of its work force. Nevertheless, available data suggest that the sector has remained resilient in the face of the war, with real sector GDP in 1991 only some 20-30% below its pre-war level. A lack of skilled workers and managers, poor physical infrastructure and the virtual absence of medium- and long-term financing for working capital and investment stand in the way of a sustained recovery of the sector.

## Macroeconomic Prospects

### Introduction

37. The scenarios presented below are based on the macroeconomic framework in the recent Country Economic Memorandum ("Lebanon - Stabilization and Reconstruction") dated March 1993. The base case scenario is substantially similar to the medium-term scenario developed by the May 1993 IMF Article IV Consultation mission. Due to the paucity of data, and the absence of time-series, an unusual number of estimates and assumptions have been made to construct the framework. Thus, caution needs to be exercised in interpreting the results of the analysis. However, the projected scenarios are broadly indicative of general directions of developments and the likely outcomes of alternative policies and thus form a plausible basis for judgements on macroeconomic policy issues, resource needs and creditworthiness.

### Base Case

38. Sustained economic stability, together with political and social stability, is a prerequisite for economic recovery and sustained growth. Mr. Hariri's new government has a unique window of opportunity to both undertake the ambitious task of reconstruction and lay the basis for private sector-led recovery of the Lebanese economy. The base case scenario envisages major investments for reconstruction and significant external official and private capital inflows. Private per capita consumption levels would be maintained in the medium term, and rise steadily thereafter. Debt and debt service levels would initially rise rapidly but remain at manageable levels. This scenario centers around three main elements: (i) major fiscal adjustment in 1993 and 1994 (with the elimination of the fiscal current account deficit), and the successful stabilization of the economy; (ii) implementation of the reconstruction program with large increases in public and private investments; and (iii) availability of external financing. Clearly, successful reconstruction will require very sizeable amounts of both official and private capital from abroad. Only with stabilization and fiscal adjustment is there a chance that both will materialize.

39. With important fiscal adjustment taking place in 1993/94, in the base case scenario government revenues would increase from 10% of GDP in 1992 to 18% in 1994, while current expenditures would be contained at 19% of GDP. As the NERP takes off, public capital expenditures would rise from 3% of GDP in 1992 to 8% in 1993 and an average of close to 11% during 1994-96. With the virtual elimination of the current fiscal deficit, which stood at 10% of GDP in 1992, by 1994, the overall deficit could be contained to an average of about 11% of GDP during the period of reconstruction. Real GDP growth during that period is projected at 10% in 1993, and an average of 8% during 1994-96; beyond the reconstruction period real GDP growth is projected at an average of 6% p.a. based on

relatively low aggregate levels of efficient private sector investment. Total imports would increase substantially as reconstruction takes off and exports would rise steadily as overall economic activity picks up. The current account deficit would remain large, at an average of \$2.6 billion p.a. during the reconstruction period. Projected private inflows are sizeable throughout the period of reconstruction and thereafter; this

underscores the importance of sustaining stable economic policies. Despite the projected improvement in fiscal performance, relatively sizeable amounts of external loans and grants will continue to be required to finance the reconstruction of infrastructure. Key macroeconomic indicators in the base case scenario are presented in the table below.

<b>Base Case Scenario: Key Macroeconomic Indicators (%)</b>			
	1993	1994-1996	1997-1999
GDP real growth	10.0	8.0	6.4
Private Consumption real growth	2.3	0.9	4.8
Investment/GDP of which: public investments	23.8 7.7	30.4 10.8	18.9 4.9
Current Fiscal Balance/GDP	-4.3	0.2	3.2
Overall Fiscal Balance/GDP	-12.0	-10.7	-1.7
External Public Debt Service/Exports	4.2	4.2	4.2
Current Account Balance/GDP	-35.8	-32.0	-20.5

### **Alternative Scenarios**

40. The viability of the base case scenario centers around fiscal adjustment. An alternative scenario envisions a lack of fiscal adjustment, with a likely consequence being that the level of private capital inflows would be well below the levels projected in the base case as uncertainty in the economy would prevail. A lack of fiscal adjustment would prevent the government from contributing to public investments associated with the reconstruction program; official creditors would then withdraw from the program. As a result, overall investment levels would be significantly below those under the base case scenario. GDP growth would fall, and sharp declines in consumption per capita would occur. This is the most likely outcome of a failure to implement stabilization policies.

41. If, in spite of the lack of fiscal adjustment, the government would still attempt to maintain total overall investment at levels

similar to those under the base case scenario, this would be achieved by substantially higher levels of external borrowing by the public sector. In that event, the public sector's (domestic and external) debt service would rapidly become unsustainable, as debt service payments would soon absorb most of fiscal revenues, even under favorable lending terms. Also, GDP growth would be lower than under the base case scenario, as the efficiency of incremental public investments is likely to be well below the efficiency of private capital.

### **Creditworthiness and External Capital Requirements**

42. Lebanon's total capital requirements in the medium term would amount to around \$3.0 billion per annum (see table below). The bulk of this is expected to be available from private capital inflows, including return of the flight capital and direct foreign investment. During the period of implementation of the NERP,

relatively sizeable amounts of official assistance will be needed. During the Donors meeting held in December 1991, the international donor community showed increasing interest in supporting Lebanon. The amount of loan and grant financing required during 1993-96, about \$600 million per annum, can only be raised if Arab and other donors are willing to support Lebanon. Current indications are that this may indeed be the case, but financing for the NERP will need to be confirmed in the context of a Consultative Group to be convened in late 1993.

43. In spite of difficult circumstances, Lebanon has met its debt service obligations with the Bank, and its current outstanding

obligations amount to only about \$20 million. Lebanon's external public debt was estimated at about \$360 million (8% of GDP) at the end of 1991, which is low by any standard. While the level of public debt is projected to increase five-fold to about \$1.8 billion over the next four years because of the external financing required for the NERP, debt indicators would remain low, with an external public debt to GDP ratio of less than 20% and a public debt service to exports ratio of less than 5% by the mid-1990s. This will be manageable considering the projected improved fiscal capacity to service the debt to be contracted for the NERP.

<b>Base Case Scenario: External Financing Requirements (Millions of US\$ p.a.)</b>			
	1993	1994-1996	1997-1999
Current Account Deficit	2,445	2,744	2,418
Public Loan Amortization	50	50	69
Reserve Build-up	289	391	208
Total Financing	2,784	3,185	2,695
Public Grants	200	200	100
Public Loans (Gross Disbursement)	340	410	305
Private Capital Flows/Investment	2,244	2,575	2,290

### **Bank Assistance Strategy**

44. The Bank has been inactive in Lebanon for over a decade and a half, and our knowledge of the country is very limited. In response to the government's request, the Bank assisted in the preparation of the NERP. The \$175 million Emergency Reconstruction and Rehabilitation (ERRP) Loan approved in March 1993, will finance high priority components of the NERP aimed at restoring a basic level of functioning to infrastructure services, strengthening institutional capabilities for undertaking the reconstruction program, rebuilding confidence and creating an environment in which essential institutional and financial reform is feasible. While proceeding with the implementation of the ERRP, we would

assist the government in inducing private sector investment in the same sectors and in strengthening institutions.

45. Beyond the immediate reconstruction supported with the ERRP, the Bank has a fairly unique opportunity to play a major role in the recovery of Lebanon. While the risks involved are above average, the potential benefits of a relatively modest Bank assistance program to help a serious and strong government, that has broad domestic and regional support, lay the basis for steady recovery and mobilize external support are significant. The overall objective of Bank strategy would be the resumption of rapid economic growth and reduction of poverty. Towards these goals the Bank would support a

private sector-led economic recovery, while helping to rebuild and strengthen a public administration that would focus on establishing an enabling environment for private sector activity, rehabilitating physical infrastructure, addressing social needs and environmental concerns, and investing in human resources development (see attachment). The mobilization of external resources and aid coordination to achieve the overall strategy objectives would be an important element of the assistance program.

46. Future Bank lending would concentrate heavily on the social sectors. These have traditionally been neglected by Lebanese governments, in good and bad times, and this neglect in part underlies the tensions and violence that Lebanon has experienced. Ultimately, continued political stability will not be maintained unless social issues are addressed. Moreover, the services sector is undoubtedly one of the main sources for potential growth and human resources development, virtually non-existent for 15 years, would thus be a high priority. The proposed lending program includes an education project, a poverty alleviation (social fund) project, a health project, and an additional social sector project, as well as investments in social infrastructure. Specific sector work would focus on the development of a strategy for human resources development and the design of a social safety net, which becomes all the more important as economic stabilization measures are being implemented, and would also include a poverty assessment, a living standards measurement survey, and a rural development study to lay the basis for poverty alleviation programs. Bank support for the environment would include an environmental assessment, which, together with planned METAP activities, would help the government develop a comprehensive environmental strategy and lay the basis for an environmental lending operation.

47. The Bank would support the initial strengthening of the public administration through a free-standing technical assistance project to strengthen economic management and

public administration, to be followed by a more narrowly focused operation to help Lebanon establish an efficient civil service. An early strengthening of public administration is particularly important since the temporary improvements in administration that have been achieved by utilizing resources of Prime-Minister Hariri and his team do not represent a lasting and politically sustainable solution. As part of Bank support for private sector development, our initial economic and sector work would help government to establish an enabling environment for private sector development, including a legal and regulatory framework for private investment in the provision of public services, reform of the financial sector, and the development of capital markets to facilitate the mobilization and efficient allocation of resources. We would jointly with government organize a seminar ("Lebanon 2005") to develop a vision of the Lebanese economy and its future role in the region, and sector work would include a private sector assessment to be undertaken jointly between government, the private sector, and the Bank. This assessment would also focus on issues and prospects for private sector provision of infrastructure services. In physical infrastructure, the Bank would initially support selected public investments, particularly during the reconstruction and rehabilitation phase, but future expansion of physical infrastructure should be left to the private sector. The ERRP includes a technical assistance component in support of institutional and regulatory reforms in the infrastructure sectors and the design of sectoral strategies, including plans for private sector participation. The proposed ESW in support of private sector development would extend, and expand on, the initial work being undertaken. It would more specifically support corporatization and commercialisation of public institutions to allow their eventual privatization, and the reform of the legislative, contractual and regulatory frameworks to facilitate private investment in, and operation of, utilities. The proposed lending program includes a number of projects that would support private sector



development of infrastructure beyond the immediate reconstruction phase.

48. The proposed base case lending program for FY94-98 consists of three operations for an average of \$85 million per year, with some frontloading. The composition and phasing of the lending program as discussed above and shown in Annex I is tentative and subject to change based on the sector work to be initiated, the definition by the government of its priorities for Bank support, and an assessment of the availability of financing from other sources. The base case program would be conditional upon: (i) the maintenance of an acceptable overall macroeconomic framework, in particular by reducing the current imbalances through fiscal adjustment, along the lines of the base case macroeconomic scenario discussed above and the medium term scenario developed in the context of the recent IMF Article IV Consultation mission; and (ii) the availability of financing from other sources to ensure the feasibility of the overall financing scenario and adequate burden sharing. The next few months will show whether the government has the resolve to continue to take the required fiscal measures, and the Consultative Group meeting planned for late 1993 (para. 50) would confirm whether there is adequate official donor support for Lebanon. We would also need to continuously monitor the evolution of the political situation. The proposed economic and sector work program as discussed above and shown in Annex II, an average of 180 staff-weeks per year during FY94-96, is heavily frontloaded in order to rapidly develop our knowledge base, underpin proposed lending, and advise government on the design of macro- and sector policies. Because of the frontloaded nature of the economic and sector work program and the need to develop a project pipeline of the magnitude envisaged in the base case program, and undertake country work on a regular basis, total resource requirements in FY94 are estimated at 14.7 staff-years. (This includes 8.3 SY for lending, 0.9 SY for portfolio management, 4.4 SY for

ESW, and 1.1 SY for country work, aid coordination and other).

49. Lebanon's creditworthiness largely depends on the expected fiscal capacity to service its debt. The present government has made an important initial effort to reduce fiscal imbalances. If the government's commitment to fiscal adjustment were to decline, we would move to low case lending program. We would therefore closely monitor a number of indicators, including (i) the evolution of overall fiscal deficit, relative to the targets in the base case macroeconomic scenario, (ii) progress in increasing public sector revenues, which will be critical to achieving fiscal adjustment, and (iii) the mechanisms used to finance the deficit, as excessive reliance on Central Bank credit would undermine economic stability, while excessive reliance on domestic debt could crowd out the private sector. The size of the low case program would be determined in the light of events and its composition would focus more heavily on social sectors. In the total absence of an appropriate macroeconomic framework, or if the political situation were to become unstable, we would stop all lending. At this stage, we do not propose a high case program. We plan to review the country assistance strategy in about twelve months.

#### Coordination with other Institutions

50. The government has requested the support of the Bank in mobilizing external resources for the NERP. We would convene a Consultative Group meeting provided the government continues to make satisfactory progress in mounting and implementing an appropriate macroeconomic program satisfactory to the IMF and the Bank. The recent IMF Article IV Consultation mission has made a favorable assessment of the government's economic program and has agreed with government on an informal arrangement for monitoring progress in its implementation. However, in view of the economic stabilization issues at hand, a more formal IMF program

would be desirable, and we would therefore continue to seek to convince government, which thus far has cited political constraints to a formal arrangement, to pursue this option. The presence of both the Bank and IMF is seen as an important signal to other donors, including Arab countries, and will help to increase the confidence not only of the international community but also of the Lebanese private sector. The NERP has already attracted external support from the regional funds, the EEC and EIB and a number of bilateral donors, and the Bank's role in the implementation of the NERP, through the ERRP, would ensure donor coordination. A Bank lending program of the size and composition proposed would be an important catalyst for attracting the external funding from official sources that Lebanon will require during the 1990s, particularly during the reconstruction phase; the Arab regional funds have already expressed their interest in co-financing Bank projects in Lebanon. In addition to large-scale financial support for reconstruction, Lebanon requires massive technical assistance to compensate for the absence of qualified and experienced staff who left the country during the war. The Bank would work closely with UNDP in establishing a technical assistance trust fund aimed at channeling and coordinating the technical assistance likely to be available from several multilateral and bilateral sources.

51. In promoting private sector development, the Bank would work closely with IFC, which has also reinitiated operations in FY93 and could play an important role in Lebanon given the country's traditional private sector orientation. IFC has agreed to help undertake the capital markets development component of the proposed financial sector review. IFC's strategy for Lebanon focuses on three main areas. First, invest in domestic capital markets to: (i) help the banking sector play an effective role in reconstruction by providing long-term loans to intermediaries to fund projects of small and medium-sized enterprises; (ii) provide technical assistance to government on financial markets

issues; (iii) help establish model financial intermediaries to deepen the financial system and energize capital markets; and (iv) mobilize and channel resources for the re-emerging private sector. Second, attract private capital to rehabilitate infrastructure facilities that are essential to the service economy, in particular in telecommunications, and possibly finance projects in maritime and air transport and power generation and/or distribution. Third, support viable manufacturing ventures, particularly in the construction and building materials industry that face significant demand associated with the reconstruction effort.

### **Bank Share of Financing**

52. Based on the medium-term projections underlying the base case macroeconomic scenario, with the \$175 million ERRP loan and the base case lending program as proposed, the Bank would account for about 12% of total gross public M & LT loan and grant disbursements during 1993-96. The Bank's exposure to Lebanon would be about 3% of GDP at end-1996, out of the total external public debt equal to 18% of GDP. Lebanon's external public debt, which stood at only about \$360 million at end-1991, is projected to increase five-fold during the 1993-96 period of the NERP, but public debt indicators are projected to remain at very low levels, on the assumption that a major share of the total financing needs will be met by private flows, including the repatriation of capital. By 1999, the Bank's share in total public external debt of \$2.4 billion (18% of GDP) would amount to 20%. As a significant portion of projected official assistance is expected to come from regional banks, the share of preferred creditors in total public debt would be around two-thirds.

53. Lebanon's stock of external public debt would remain small by any standard, while its reserve position - currently about \$3.0 billion in gold and \$1.5 billion in non-gold - is comfortable. With fiscal adjustment along the lines projected, virtual elimination of the current

deficit (10% of GDP in 1992) within two years and of the overall deficit by 1999 (with most of the reduction after 1996 representing the completion of the NERP), there would be adequate fiscal capacity to service the external and domestic debt to be contracted by the public sector during 1993-99, in particular during 1993-96. In view of Lebanon's past track record with the Bank and the government's commitment to fiscal stabilization and reconstruction, the amounts of planned lending are considered prudent.

### **Downside Risks**

54. The main risks are the failure by the government to establish and maintain a viable macroeconomic framework and political stability, and the security situation. Lebanon's track record of macroeconomic management in past years has not been favorable, due in large part to the protracted hostilities and their aftermath. Lebanon's current economic stability is not sustainable in the absence of action to correct macroeconomic imbalances, in particular the fiscal deficit. In the absence of macroeconomic and political stability, the overall reconstruction program could not be fully financed and implemented, and the private resources required for associated investments in the economy would not be forthcoming. Also, the fiscal capacity to service the debt to be contracted for the program could become in doubt. The present government is aware that the short term stability that has been achieved is tenuous and delicate.

55. The question of political stability is very much related to the need to ensure economic stability. If the stabilization and reconstruction programs were to fail, the current government would find itself under significant pressure to resign. Successful implementation of the programs represents a significant challenge. Unfulfilled expectations and the need to carefully balance the interests of the various denominational factions could hamper the government from taking the ambitious and

difficult measures that are required. The population has very high expectations about immediate reconstruction and renewal of services to quickly erase the effects of 15 years of war. However, the new government is judged to have the best chance in many years to provide a measure of macroeconomic stability and to foster confidence in the private sector. It is well aware that economic stabilization is a pre-condition for sustained, private sector-led recovery. It has begun taking measures to reduce the fiscal deficit and has stated that restoration of fiscal balance is a priority objective. At the same time, the aspirations of the Lebanese people after nearly two decades of conflict, and the evolving Middle East peace process, would appear to now make it more likely than before that political stability will also be maintained.

56. External events, particularly regional developments, could upset hard-won stability. The Syrian army continues to play an important security role in most of the country, while in the South, Israel and the Southern Lebanese Army occupy part of the country's territory. If the peace process were to fail, there could be far reaching implications for Lebanon. Conversely, if the process were to be successful, prospects for a prosperous Lebanon as a regional trade and services center would be enhanced.

**LEBANON**  
**OBJECTIVES AND INSTRUMENTS OF COUNTRY ASSISTANCE STRATEGY, FY94-98**

<b>OBJECTIVES</b>	<b>INSTRUMENTS</b>	<b>COMMENTS</b>
<b>A. Macroeconomic stabilization/ Fiscal reform and adjustment.</b>	<ul style="list-style-type: none"> <li>• <i>Formulation of macroeconomic framework for stabilization jointly with IMF.</i></li> <li>• <i>Technical assistance project for economic management.</i></li> <li>• <i>Financial sector review and macroeconomic assessment, PSER, CEM, and other economic work.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>CEM issued March 1993, recommended stabilization measures.</i></li> <li>• <i>IMF conducted Article IV Consultation in May 1993 and made favorable assessment of government economic program.</i></li> </ul>
<b>B. Reconstruction of infrastructure.</b>	<ul style="list-style-type: none"> <li>• <i>Implementation of ERRP.</i></li> <li>• <i>CG meeting to mobilize external resources.</i></li> <li>• <i>Lending for social and physical infrastructure (solid waste, irrigation, water, housing, and transport).</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ERRP is part of NERP, to be implemented during 1993-1996.</i></li> <li>• <i>CG planned for November 1993.</i></li> </ul>
<b>C. Private-Sector led economic recovery.</b>	<ul style="list-style-type: none"> <li>• <i>Financial sector review.</i></li> <li>• <i>Private sector assessment.</i></li> <li>• <i>Lending for private sector investment in utilities.</i></li> <li>• <i>Technical assistance for capital market development (with IFC involvement), and legal, regulatory, and administrative reforms as part of T.A. projects.</i></li> <li>• <i>Conference on long-term vision for Lebanon planned for September 1993.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>ESW heavily frontloaded in FY94.</i></li> </ul>
<b>D. Rebuilding of public administration.</b>	<ul style="list-style-type: none"> <li>• <i>Technical assistance projects for economic management and for strengthening of public administration/civil service reform.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>Coordinating with UNDP and IMF.</i></li> </ul>
<b>E. Development of social sectors/Human resources development/Alleviation of poverty/Environment.</b>	<ul style="list-style-type: none"> <li>• <i>Lending - Education / Poverty Alleviation / Health / Solid Waste / Environment / Water / Housing / Integrated Rural Development.</i></li> <li>• <i>Human resources sector work, including design of a social safety net, poverty assessment, and LSMS. Rural development study.</i></li> <li>• <i>Environmental assessment.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>First human resources sector mission in May, 1993.</i></li> <li>• <i>Elimination of inflation tax and generation of incomes through stabilization and economic recovery.</i></li> </ul>

## LEBANON

## FY93-98 Base Case Lending Program

Fiscal Year	Project	US\$ Million
FY93	Emergency Reconstruction & Rehabilitation	175
	TOTAL	175
FY94	Technical Assistance for Economic Management & Public Administration	10
	Emergency Education	50
	Irrigation Rehabilitation	30
	TOTAL	90
FY95	Poverty Alleviation	35
	Solid Waste/Environment	35
	Health	30
	TOTAL	100
FY96	Water Supply S	30
	Public Administration/Civil Service Reform S	15
	Private Sector Infrastructure Development	40
	TOTAL	85
FY97	Housing S	25
	Transport S	30
	Integrated Rural Development	25
	TOTAL	80
FY98	Social Sectors	40
	Private Sector Development II	30
	TOTAL	70

## LEBANON

Economic & Sector Work Program, FY93-96

<b>Fiscal Year</b>		<b>Staff Weeks</b>
<b>FY93</b>	CEM	70
	EWO	15
	Human Resources/Poverty Assessment*	20
	<b>TOTAL</b>	<b>105</b>
<b>FY94</b>	Financial Sector Review/Macro-Assessment	70
	Private Sector Assessment*	60
	Human Resources/Poverty Assessment	50
	Environmental Assessment*	10
	EWO/SWO	40
	<b>TOTAL</b>	<b>230</b>
<b>FY95</b>	Public Sector Expenditure Review	60
	Private Sector Assessment	20
	Environmental Assessment	20
	Poverty/LSMS*	10
	EWO/SWO	40
	<b>TOTAL</b>	<b>160</b>
<b>FY96</b>	CEM	60
	Poverty/LSMS	30
	Rural Development Study	30
	EWO/SWO	40
	<b>TOTAL</b>	<b>160</b>

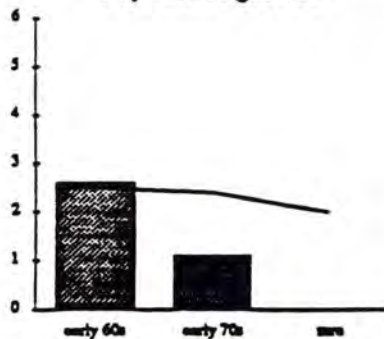
\* To be completed in subsequent FY

Social Indicators of Development, 1991-92

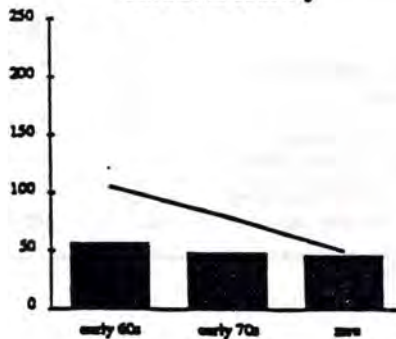
Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>HUMAN RESOURCES</b>							
Size, growth, structure of population							
Total population (mre = ...)	thousands	2,151	2,767	-	256,356	629,102	458,731
14 and under	% of pop.	43.6	41.2	36.5	42.8	37.3	33.8
15-64	% of pop.	51.2	53.9	57.8	53.2	57.8	60.9
Age dependency ratio	unit	0.95	0.86	0.73	0.86	0.72	0.63
Percentage in urban areas	% of pop.	49.5	68.6	83.7	55.3	58.6	71.8
Females per 100 males							
Urban	number	..	..	..	..	..	..
Rural	number	..	..	..	..	..	..
Population growth rate							
Urban	annual %	2.6	1.1	0.1	2.9	2.0	1.7
Rural	annual %	6.7	3.8	0.6	4.1	3.2	2.8
Urban/rural growth differential	difference	7.9	8.3	4.7	2.6	2.4	3.6
Projected population: 2000	thousands	..	..	3,013	340,932	768,976	541,229
Stationary population	thousands	..	..	6,044	..	..	..
Determinants of population growth							
Fertility							
Crude birth rate	per thou. pop.	40.4	30.9	30.2	39.3	29.5	24.9
Total fertility rate	births per woman	6.17	4.55	3.62	5.39	3.74	3.10
Contraceptive prevalence	% of women 15-49	..	55.0	..	..	..	..
Child (0-4) / woman (15-49) ratios							
Urban	per 100 women	..	..	..	..	..	..
Rural	per 100 women	..	..	..	..	..	..
Mortality							
Crude death rate	per thou. pop.	12.4	8.9	8.8	10.1	8.5	7.5
Infant mortality rate	per thou. live births	56.0	48.0	45.8	79.5	49.5	41.3
Under 5 mortality rate	per thou. live births	..	..	59.0	87.8	79.5	49.8
Life expectancy at birth: overall	years	62.0	65.0	65.5	60.5	65.3	68.3
female	years	63.9	67.0	67.5	62.2	67.9	71.5
Labor force (15-64)							
Total labor force	thousands	578	771	914	70,804	237,840	172,535
Agriculture	% of labor force	29.2	17.0	..	..	..	..
Industry	% of labor force	24.0	26.3	..	..	..	..
Female	% of labor force	16.1	20.5	27.8	14.6	32.3	30.4
Females per 100 males							
Urban	number	..	..	..	..	..	..
Rural	number	..	..	..	..	..	..
Participation rate: overall							
female	% of labor force	26.9	27.9	30.8	28.5	40.6	38.5
male	% of labor force	8.7	11.5	16.6	8.5	25.6	23.3
Educational attainment of labor force							
School years completed: overall	years	..	..	..	..	..	..
male	years	..	..	..	..	..	..
<b>NATURAL RESOURCES</b>							
Area	thou. sq. km	10.40	10.40	10.40	11,667	22,765	18,709
Density	pop. per sq. km	207	266	258	21	27	24
Agricultural land	% of land area	29.4	33.2	29.9	27.5	40.9	34.3
Agricultural density	pop. per sq. km	703	802	863	78	66	70
Forests and woodland	thou. sq. km	0.95	0.90	0.80	413	6,174	7,116
Deforestation rate (net)	annual %	0.0	0.0	0.0	0.5	-0.5	-0.5
Access to safe water							
Urban	% of pop.	..	..	..	..	78.2	88.7
Rural	% of pop.	..	..	77.0	..	46.9	63.8

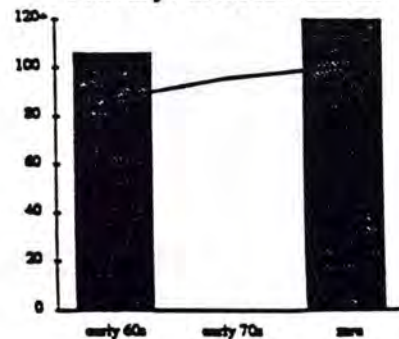
Population growth



Infant mortality



Primary school enrollment



■ Lebanon — Lower-middle-income

Note: Extreme values for population growth are unshaded.

## Lebanon

	Unit of measure	25-30 years ago	15-20 years ago	Most recent estimate (mre)	Same region / income group		Next higher income group
					Middle East & North Africa	Lower-middle-income	
<b>INCOME AND POVERTY</b>							
<b>Income</b>							
GNP per capita (mre = ...)	US\$	--	--	--	1,830	1,530	3,450
<b>Total household income</b>							
Share to top 10% of households	% of income	--	--	--	--	--	--
Share to top 20% of households	"	--	--	--	--	--	--
Share to bottom 40% of households	"	--	--	--	--	--	--
Share to bottom 20% of households	"	--	--	--	--	--	--
<b>Poverty</b>							
Absolute poverty income: urban	US\$ per person	--	--	--	--	--	--
rural	"	--	219	--	--	--	--
Pop. in absolute poverty: urban	% of pop.	--	--	--	--	--	--
rural	"	--	--	--	--	--	--
Prevalence of malnutrition (under 5)	% of age group	--	--	--	--	--	--
<b>EXPENDITURE</b>							
<b>Food</b>							
Staples	% of GDP	--	--	--	--	--	--
Meat, fish, milk, cheese, eggs	"	--	--	--	--	--	--
Cereal imports	thou. metric tonnes	401	585	356	39,093	38,868	39,280
Food aid in cereals	"	--	26	16	--	--	--
Food production per capita	1979-81=100	93.7	84.3	136.6	108.6	98.9	106.0
Share of agriculture in GDP	% of GDP	11.6	9.2	--	14.3	16.8	9.0
Daily calorie supply	calories per person	2,485	2,453	3,274	3,012	2,780	3,013
Daily protein supply	grams per person	67	61	86	79	72	77
<b>Housing</b>							
Average household size	persons per household	--	--	--	--	--	--
Urban	"	--	--	--	--	--	--
Fixed investment: housing	% of GDP	--	--	--	--	--	--
<b>Fuel and power</b>							
Energy consumption per capita	kg of oil equivalent	712.9	825.0	968.5	1,048.2	1,102.2	1,794.4
<b>Households with electricity</b>							
Urban	% of households	--	--	--	--	--	--
Rural	"	--	--	--	--	--	--
<b>Transport and communication</b>							
Population per passenger car	persons	22	12	--	67	24	11
Fixed investment: transport equipment	% of GDP	--	--	--	--	--	--
Total road length	km	--	--	--	--	--	--
Population per telephone	persons	--	--	--	--	--	--
<b>INVESTMENT IN HUMAN CAPITAL</b>							
<b>Medical care</b>							
Population per: physician	persons	1,006	--	--	1,333	--	--
nurse	"	2,029	965	--	--	--	--
hospital bed	"	--	--	--	--	--	--
<b>Access to health care</b>							
Immunized (under 12 months): measles	% of pop.	--	--	15.0	78.9	65.3	78.5
DPT	% of age group	--	--	33.0	84.8	67.1	81.5
Oral Rehydration Therapy use (under 5)	% of cases	--	--	10.0	45.4	39.8	--
<b>Education</b>							
<b>Gross enrollment ratios</b>							
Primary: total	% of school-age group	106.0	--	128.0	89.7	100.5	105.9
female	"	93.0	--	94.0	81.2	97.4	--
Secondary: total	"	26.0	50.0	67.0	54.3	58.3	56.3
female	"	20.0	--	56.0	51.2	56.5	58.9
Tertiary: science/engineering	% of tertiary students	8.1	--	17.7	--	--	--
Pupil-teacher ratio: primary	pupils per teacher	24	10	6	22	26	25
secondary	"	17	--	--	20	18	--
<b>Pupils reaching grade 4</b>							
Repeater rate: primary	% of cohort	--	--	--	--	86.7	77.8
female	% of total enrollment	--	--	--	10.2	6.6	17.6
Illiteracy rate: overall	% of pop. (age 15+)	--	--	19.9	47.0	22.9	15.1
female	% of females (age 15+)	--	--	26.9	59.5	28.8	17.7
Newspaper circulation	per thou. pop.	83.7	102.3	88.1	35.4	72.0	100.9

Source: World Bank International Economic Department, April 1992.



4:09 PM  
11 May 1993

Lebanon: Key Indicators

	+---Estimate---+		+---Projected---+							
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
<b>Real Growth Rates:</b>										
Gross Domestic Product (GDP)	-13.4	50.2	10.0	10.0	8.0	8.0	8.0	8.0	5.7	5.5
Gross Domestic Income (GDI)	-13.9	49.7	9.8	10.0	8.0	8.1	8.1	8.1	5.8	5.7
<b>Real Per Capita Growth Rates:</b>										
Gross Domestic Product (GDP)	-15.1	47.3	7.8	7.8	5.9	5.9	5.9	5.9	3.8	3.6
Total Consumption	-8.5	53.6	4.9	1.1	-4.0	1.0	1.3	7.1	0.7	0.3
Private Consumption	-11.1	56.4	6.0	0.2	-5.1	0.5	1.4	7.6	0.6	0.3
<b>External Debt &amp; D. Services (LT+ST+IMF):</b>										
Total External Public Debt (US\$M)	0.0	360.7	296.6	586.6	926.6	1301.6	1666.6	1921.3	2145.7	2374.0
Public Sector External Debt Service (US\$)	14.2	3.7	100.2	70.8	90.1	117.3	150.3	189.5	225.6	240.2
Public Sector Debt Service / Exports	1.7	0.3	7.6	4.2	4.1	4.0	4.1	4.1	4.3	4.1
Public Sector Debt Service / GDP	0.6	0.1	1.8	1.0	1.2	1.4	1.6	1.8	1.9	1.9
<b>Interest Burden (LT+ST+IMF):</b>										
Public Sector Interest Paid (US\$M)	14.2	3.7	36.0	20.8	40.1	67.3	100.3	129.2	149.9	168.6
Public Sector Interest / Exports	1.7	0.3	2.7	1.2	1.8	2.3	2.7	2.8	2.9	2.9
Public Sector Interest / GDP	0.6	0.1	0.6	0.3	0.5	0.8	1.0	1.2	1.3	1.3
<b>Gross Investment / GDP</b>										
ICOR (annual)	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
ICOR (5-yr ending year shown)	-1.5	0.4	2.0	2.3	3.5	4.5	4.7	4.2	4.2	4.0
<b>Domestic Savings / GDP</b>										
BOP Resource Balance / GDP	-46.4	-45.0	-35.2	-25.3	-14.9	-10.3	-7.0	-9.1	-6.7	-4.1
National Savings / GDP	-4.0	-22.7	-20.1	-12.0	-3.8	-1.2	0.1	-3.4	-1.9	0.2
BOP Current Account Balance / GDP	-24.0	-42.7	-39.8	-35.8	-34.4	-33.2	-28.5	-23.6	-20.6	-17.5
<b>Government Investment / GDP</b>										
Government Savings / GDP	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Private Investment / GDP	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Private Savings / GDP	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8
Government Revenues / GDP	31.3	-8.2	-10.1	-7.7	-2.8	-1.3	-1.1	-5.9	-5.0	-3.7
<b>Government Expenditures / GDP</b>										
Budget Deficit (+) or Surplus / GDP	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Primary Deficit (+) or Surplus / GDP	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
GDP Deflator (% growth rate)	38.1	19.3	13.1	12.0	11.5	10.7	9.8	2.4	1.8	1.1
	25.9	14.2	7.7	6.6	6.9	6.0	5.0	-1.4	-1.5	-1.7

Lebanon: Key Indicators

4:09 PM  
11 May 1993

	+---Estimate---+		+---Projected---+							
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Continued										Continued
Real Exchange Rate (LL / US\$) (1990=100)	100.0	88.9	76.7	72.5	72.5	72.5	72.5	72.5	72.5	72.5
Terms of Trade Index (1990=100)	100.0	98.8	98.3	98.4	98.7	99.2	99.4	99.7	99.9	100.1
Export (GNFS)/Volume Growth Rate	-3.7	24.4	23.3	21.8	25.5	27.3	22.0	19.0	9.6	7.4
Exports (GNFS) / GDP	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports (GNFS) Volume Growth Rate	0.7	51.1	11.8	9.5	8.7	11.1	4.8	4.7	2.4	1.4
Imports (GNFS) / GDP	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Current Account Balance (US\$M)										
(before grants)	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
(after grants)	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
BdL Foreign Exchange Reserves (US\$M)	620.0	1233.3	1448.0	1737.1	2081.0	2539.3	2911.2	3161.4	3359.6	3535.5
Official Reserves (months imports) 7/	3.1	3.9	4.0	4.3	4.5	4.8	5.0	5.0	5.0	5.0

1. "LT" denotes "long-term debt;" "ST" denotes "short-term debt"
2. "DOD" denotes "debt outstanding and debt disbursed."
3. "ICOR" denotes "incremental capital output ratio" with a 5-years period.
4. "BOP" denotes "balance of payments"
5. Current account balance as defined in line F.1 on annex B3
6. "GNFS" denotes "goods and nonfactor service".
7. Excludes gold.

4:08 PM  
11 May 1993

Projection Table 1. Balance of Payments  
(in millions of US\$)

	1989	1990	1991	-----Projected-----							
				1992	1993	1994	1995	1996	1997	1998	1999
	(US\$ millions)										
Resource Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Merchandise Trade Balance	-1707.0	-1859.0	-2997.0	-3322.1	-3719.0	-4069.7	-4540.9	-4744.2	-4926.9	-5132.7	-5264.1
Merchandise Exports	539.0	537.0	750.0	987.0	1185.7	1479.5	1874.2	2242.6	2660.4	2930.4	3221.2
Merchandise Imports	2246.0	2396.0	3747.0	4309.1	4904.7	5549.2	6415.2	6986.9	7587.3	8063.1	8485.3
Net NonFactor Services	200.0	200.0	200.0	222.0	365.6	583.8	903.0	1314.5	1761.5	2120.1	2433.7
Exports of NonFactor Services	300.0	300.0	300.0	338.2	491.9	715.5	1039.8	1457.1	1920.8	2292.9	2618.0
Imports of NonFactor Services	100.0	100.0	100.0	116.2	126.3	131.7	136.8	142.6	159.3	172.8	184.3
Net Factor Income	507.0	479.0	480.0	453.9	458.8	371.6	287.2	164.0	69.2	-2.8	-36.0
Net Current Transfers	680.0	580.0	480.0	400.0	450.0	475.0	500.0	525.0	550.0	575.0	600.0
Current Account Balance (before grants)	-320.0	-600.0	-1837.0	-2246.2	-2444.6	-2639.4	-2850.8	-2740.8	-2546.1	-2440.4	-2266.3
Capital Official Grants	0.0	0.0	70.7	0.0	200.0	200.0	200.0	200.0	100.0	100.0	100.0
Current Account Balance (after grants)	-320.0	-600.0	-1766.3	-2246.2	-2244.6	-2439.4	-2650.8	-2540.8	-2446.1	-2340.4	-2166.3
Direct Foreign Investment	0.0	0.0	0.0	0.0	300.0	800.0	800.0	800.0	500.0	500.0	500.0
Public M&LT (net disbursement)											
Gross Disbursement	..	..	..	0.0	340.0	390.0	425.0	415.0	315.0	300.0	300.0
Amortization	..	..	..	-64.2	-50.0	-50.0	-50.0	-50.0	-60.3	-75.6	-71.7
Net Disbursement	14.1	23.1	33.9	-64.2	290.0	340.0	375.0	365.0	254.7	224.4	228.3
Net Other Capital Flows 1/	262.9	279.9	2301.4	2525.1	1943.7	1643.3	1934.1	1747.6	1941.6	1814.3	1613.9
Overall Balance 2/	-43.0	-297.2	569.0	214.7	289.1	343.9	458.4	371.9	250.2	198.2	175.9
Increase in Bdl Reserves	43.0	297.2	-569.0	-214.7	-289.1	-343.9	-458.4	-371.9	-250.2	-198.2	-175.9

Sources: Data provided by the Bank of Lebanon; IMF, Direction of Trade; and staff estimates and projections.

1/: Comprised of net private medium and long term debt, net short term capital, trade credits, unidentified capital flows, and errors and omissions.  
2/: Includes only non-gold reserves of the Bdl.

Elasticity of total imp. to GDP growth rate/growth rate adjusted for Real Exchange Rate	-0.05	1.02	1.18	0.95	1.09	1.39	0.60	0.58	0.43	0.26	
Elasticity of NonInv.imports to GDP adjusted for Real Exchange Rate	-0.05	1.01	0.25	0.25	0.05	0.00	0.05	0.95	0.80	0.50	
Average Exchange Rate	496.5	701.8	928.2	1683.0	1912.8	2025.1	2146.1	2274.3	2322.5	2353.8	2353.8

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	Actual				Projection						
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
	(In billions of Lebanese Pounds)										
Total Revenue	62.6	126.4	456.7	984.0	2100.0	2794.1	3405.2	4164.9	4768.0	5299.3	5803.2
Total Expenditure 1/	534.7	794.5	1229.1	2229.3	3662.1	4571.4	5378.2	6314.2	5368.2	5803.9	6124.6
Current Expenditures	495.0	745.2	1036.6	1929.3	2657.2	2945.6	3374.9	3885.8	4130.4	4428.3	4618.1
Wages & Salaries	96.9	210.0	370.0	738.9	887.0	1064.4	1224.1	1370.9	1480.6	1584.3	1663.5
Other Current (incl. Transfers)	58.3	96.7	240.6	425.8	875.1	1039.6	1235.0	1467.2	1704.7	1922.6	2105.4
Extrabudgetary Transfers	88.3	179.0	184.0	90.0	117.0	100.0	50.0	0.0	0.0	0.0	0.0
Petroleum Subsidy	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
Interest Payments	152.2	213.5	206.9	514.6	698.2	711.6	865.8	1047.7	945.1	921.5	849.3
Private Sector Credit	151.5	203.5	203.5	454.0	658.5	630.4	721.4	819.7	645.1	568.5	452.5
Foreign Sector Interest	0.7	10.0	3.4	60.6	39.7	81.1	144.5	228.0	300.0	352.9	396.8
Capital Expenditures 2/	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
of which Reconstruction Program:											
in Lebanese Pounds					573.8	1113.8	1394.9	1705.7			
in US Dollars					300.0	550.0	650.0	750.0			
Current Budget Balance	-432.4	-618.8	-579.9	-945.3	-557.2	-151.5	30.2	279.0	637.5	871.0	1185.1
Overall Deficit	-472.1	-668.1	-772.4	-1245.3	-1562.1	-1777.3	-1973.0	-2149.3	-600.2	-504.6	-321.4
Financing	472.1	668.1	772.4	1245.3	1562.1	1777.3	1973.0	2149.3	600.2	504.6	321.4
External	7.0	16.2	97.1	-108.0	937.3	1093.6	1234.0	1285.0	823.8	763.5	772.8
Net Borrowing	7.0	16.2	31.5	-108.0	554.7	688.5	804.8	830.1	591.5	528.2	537.5
Grants	0.0	0.0	65.6	0.0	382.6	405.0	429.2	454.9	232.2	235.4	235.4
Domestic	465.1	651.9	675.3	1353.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
Net Bank of Lebanon	134.2	351.9	-424.2	-577.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Other 3/	330.9	300.0	1099.5	1930.3	624.8	683.7	739.0	864.3	-223.6	-258.9	-451.4
Memorandum Items:											
Domestic Public Debt	..	..	..	4115.4	4740.2	5424.0	6163.0	7027.3	6803.7	6544.8	6093.4
External Public Debt	0.0	0.0	317.1	548.8	1158.5	1932.4	2876.7	3830.4	4492.2	5050.4	5647.1
Total Public Debt	..	..	..	4664.2	5898.7	7356.4	9039.7	10857.7	11295.9	11595.3	11740.5

Projection Table 2. Lebanon: Consolidated a/ Central Government Operations: 1989-1999  
(In billions of Lebanese Pounds)

4:08 PM  
11 May 1993

	Actual				Projection						
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
	(In percent of GDP)										
Total Revenue	5.2	7.2	11.4	10.4	16.1	18.0	18.5	19.0	19.0	19.0	19.0
Total Expenditure	44.6	45.3	30.8	23.5	28.0	29.5	29.2	28.8	21.4	20.8	20.1
Current Expenditure	41.3	42.5	25.9	20.3	20.3	19.0	18.3	17.7	16.5	15.9	15.1
Capital Expenditure	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
of which: Reconstruction Program					4.4	7.2	7.6	7.8			
Current Budget (- deficit)	-36.1	-35.3	-14.5	-10.0	-4.3	-1.0	0.2	1.3	2.5	3.1	3.9
Overall Deficit	-39.4	-38.1	-19.3	-13.1	-12.0	-11.5	-10.7	-9.8	-2.4	-1.8	-1.1
	(In percent of Total Expenditure)										
Total Revenue	11.7	15.9	37.2	44.1	57.3	61.1	63.3	66.0	88.8	91.3	94.8
Overall Deficit	-88.3	-84.1	-62.8	-55.9	-42.7	-38.9	-36.7	-34.0	-11.2	-8.7	-5.2
Memorandum Items:	(In billions of Lebanese Pounds)										
Nominal GDP	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
	(In percent of GDP)										
Domestic Public Debt	..	..	..	43.3	36.3	35.0	33.4	32.1	27.1	23.5	20.0
External Public Debt	0.0	0.0	7.9	5.8	8.9	12.5	15.6	17.5	17.9	18.1	18.5
Total Public Debt	..	..	..	49.1	45.2	47.4	49.0	49.6	45.1	41.6	38.5

Sources: Data provided by the Lebanese authorities; and staff estimates and projections.

a/: Central Budget, Extra budetary Accounts, Annexed Budgets and CDR.

1/: Includes net lending.

2/: Includes domestic financing of CDR capital expenditures assumed to have come through transfers from the central government.

The 1992 value is based on the proposed budget of 1992.

3/: Comprised of net commercial banks and non-bank public.

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

National Account, Estimates and Projections: 1990-1999 (in billions of current Lebanese Pound)											
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
GDP at market prices	1198.7	1752.8	3995.1	9498.7	13060.7	15516.1	18433.2	21898.6	25069.5	27863.2	30512.7
Net Indirect Taxes	-95.7	-42.3	96.5	282.5	888.0	1288.9	1659.0	1970.9	2256.3	2507.7	2746.1
Indirect Taxes	3.6	3.7	131.6	442.5	968.0	1318.9	1659.0	1970.9	2256.3	2507.7	2746.1
Subsidies	99.3	46.0	35.1	160.0	80.0	30.0	0.0	0.0	0.0	0.0	0.0
GDP at factor cost	1294.4	1795.1	3898.6	9216.2	12172.7	14227.3	16774.2	19927.7	22813.2	25355.5	27766.6
Resource Balance	-748.2	-1164.2	-2596.3	-5217.4	-6414.4	-7059.4	-7807.3	-7800.1	-7351.5	-7091.1	-6662.0
Total Imports	1164.8	1751.6	3570.9	7447.7	9623.3	11504.6	14061.0	16214.2	17991.1	19385.5	20406.3
Total Exports	416.6	587.4	974.6	2230.3	3208.9	4445.2	6253.7	8414.1	10639.7	12294.4	13744.3
Total Expenditures	1946.9	2917.0	6591.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Total Consumption	1707.2	2566.5	5792.3	12844.3	16362.1	17820.7	20340.6	23435.3	27356.9	29736.2	31772.2
Government Consumption	124.4	255.5	483.3	944.9	1324.5	1636.2	1965.1	2251.3	2503.5	2737.8	2926.7
Private Consumption	1582.8	2310.9	5309.0	11899.4	15037.6	16184.5	18375.5	21184.0	24853.4	26998.4	28845.5
Gross Domestic Investment	239.7	350.6	799.0	1871.8	3113.0	4754.9	5899.9	6263.4	5064.1	5218.1	5402.6
Government	39.7	49.3	192.5	300.0	1004.8	1625.8	2003.2	2428.3	1237.7	1375.7	1506.5
Private	200.0	301.3	606.5	1571.8	2108.2	3129.0	3896.6	3835.1	3826.3	3842.4	3896.1
(In Millions of Current US Dollars)											
Memorandum Items:											
GDP at Market Prices	2414.3	2497.7	4304.0	5643.9	6828.0	7661.9	8589.3	9628.9	10794.4	11837.6	12963.3
Per Capita GDP	677.6	687.1	1160.7	1492.2	1769.9	1947.1	2140.0	2352.0	2585.0	2784.7	2995.6
Merchandise Trade Balance	-1507.0	-1659.0	-2797.0	-3100.0	-3353.4	-3486.0	-3638.0	-3429.7	-3165.4	-3012.6	-2830.3
Exports	839.0	837.0	1050.0	1325.2	1677.6	2195.0	2914.0	3699.7	4581.2	5223.3	5839.2
Imports	2346.0	2496.0	3847.0	4425.2	5031.0	5681.0	6552.0	7129.4	7746.6	8235.9	8669.6

Projection Table 3. National Accounts

4:09 PM  
11 May 1993

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
National Account, Estimates and Projections: 1990-1999 (in billions of constant 1990 Lebanese Pound)											
GDP at market prices	2023.8	1752.8	2633.1	2896.4	3186.1	3441.0	3716.2	4013.5	4334.6	4579.5	4831.4
Resource Balance	-1129.4	-1164.2	-1915.3	-2057.6	-2140.7	-2141.7	-2156.8	-1959.7	-1744.6	-1604.6	-1458.8
Exports	610.1	587.4	730.6	900.9	1097.5	1377.8	1753.7	2139.8	2546.6	2790.6	2998.5
Imports	1739.5	1751.6	2645.9	2958.5	3238.2	3519.4	3910.5	4099.5	4291.2	4395.2	4457.2
Total Consumption	2748.4	2566.5	4021.8	4302.4	4434.7	4343.9	4475.8	4624.7	5050.6	5176.6	5285.2
Government Consumption	200.2	255.5	335.6	316.5	359.0	398.8	432.4	444.3	462.2	476.6	486.9
Private Consumption	2548.2	2310.9	3686.2	3985.8	4075.7	3945.0	4043.4	4180.4	4588.4	4700.0	4798.4
Gross Domestic Investment	404.8	350.6	526.6	651.7	892.1	1238.7	1397.3	1348.5	1028.6	1007.5	1004.9
Government	67.0	49.3	126.9	104.5	288.0	423.6	474.4	522.8	251.4	265.6	280.2
Private	337.7	301.3	399.7	547.2	604.1	815.2	922.9	825.7	777.2	741.9	724.7
Memorandum Item: Per Capita Real GDP	568.0	482.2	710.1	765.8	825.9	874.5	925.9	980.4	1038.0	1077.3	1116.4
(in percent of GDP)											
Resource Balance	-62.4	-66.4	-65.0	-54.9	-49.1	-45.5	-42.4	-35.6	-29.3	-25.4	-21.8
Exports	34.8	33.5	24.4	23.5	24.6	28.6	33.9	38.4	42.4	44.1	45.0
Imports	97.2	99.9	89.4	78.4	73.7	74.1	76.3	74.0	71.8	69.6	66.9
Total Consumption	142.4	146.4	145.0	135.2	125.3	114.9	110.3	107.0	109.1	106.7	104.1
Government Consumption	10.4	14.6	12.1	9.9	10.1	10.5	10.7	10.3	10.0	9.8	9.6
Private Consumption	132.0	131.8	132.9	125.3	115.1	104.3	99.7	96.7	99.1	96.9	94.5
Gross Domestic Investment	20.0	20.0	20.0	19.7	23.8	30.6	32.0	28.6	20.2	18.7	17.7
Government	3.3	2.8	4.8	3.2	7.7	10.5	10.9	11.1	4.9	4.9	4.9
Private	16.7	17.2	15.2	16.5	16.1	20.2	21.1	17.5	15.3	13.8	12.8



# Record Removal Notice



<b>File Title</b> Subject Files: Country Files - Lebanon - Correspondence 01		<b>Barcode No.</b>  1328843		
<b>Document Date</b> 01 June, 1993	<b>Document Type</b> Memorandum			
<b>Correspondents / Participants</b> To: The Acting Managing Director, IMF From: Paul Chabrier, IMF				
<b>Subject / Title</b> Lebanon: Back-to-Office Report 1/				
<b>Exception(s)</b> Information Provided by Member Countries or Third Parties in Confidence				
<b>Additional Comments</b>		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.		
		<table border="1"><tr><td><b>Withdrawn by</b> Sherrine M. Thompson</td><td><b>Date</b> March 31, 2017</td></tr></table>	<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017
<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017			



## OFFICE MEMORANDUM

DATE: April 28, 1993

TO: Mr. Ram K. Chopra, Director (MN2DR)

FROM: Spiros Voyadzis ~~Chief~~ Chief (MN2CO)

EXTENSION: 32713

SUBJECT: Mr. Caio Koch-Weser's Visit to Lebanon - BTO Report

in Karasmanoglou  
Attika --  
Fyi.  
C/W  
4/29

1. Mr. Caio Koch-Weser, accompanied by Messrs. Voyadzis, Ijichi, Choucair and Ozeki, visited Lebanon from April 4 to 6. Messrs. Choucair and Ozeki were in Lebanon on parallel missions. A program of the visit is attached as Annex 1. The mission had several meetings with the Prime Minister and the Minister of State for Financial Affairs, and a meeting each with the President, Speaker of the Parliament, sector Ministers, and representatives from the private and academic sectors. A separate report on the economy will be filed by Mr. Ozeki.

2. Introduction. Based on two days of intensive discussions and productive policy dialogue, the mission came away with a strong feeling that all with whom it had met shared a strong sense of general purpose and direction, and that Lebanon is poised to launch an ambitious national program of reconstruction, and hopefully appropriate stabilization. The Lebanese authorities were optimistic about the prospects for the Middle East peace process, and its implications for economic development in Lebanon and in the region at large. They also are increasingly aware of the need for a vision for the longer term beyond the rehabilitation and reconstruction phase. However, the immediate task of stabilization and reconstruction requires the Government's full attention.

3. The task of reconstruction and stabilization is an enormous and complex one, and will require significant external technical and financial assistance. The cumulative effects of neglect of social services and macroeconomic mismanagement during the war period weigh heavily on the public administration whose capacity had been severely weakened. These effects include, in addition to enormous damages to the physical and social infrastructure, loss of human resources and a weakened public administration, skewed income distribution, large and persistent macroeconomic imbalances, massive capital flight, and highly advanced "dollarization" of the economy, all in a context of a complex and pluralistic composition of the social and political fabrics. Nonetheless, the authorities are optimistic and firmly believe that given its ingenious population and dynamic private sector, the nation has significant economic potential. In the near term, while the economic stability that has been reestablished since the appointment of Mr. Hariri's government last year has generally been maintained, there is concern that the investor confidence underpinning the current stable exchange rate may now be more fragile

than before, and the government will need to act on further stabilization measures without delay.

4. Stabilization. The main indicator of investors' confidence in the economy which is underpinning the current stability, is the increase in the value of the Lebanese Pound, which currently stands at LL 1,730 per US Dollar, some 40% higher than it was prior to the appointment of the new government. As a consequence of the exchange rate appreciation, the inflation rate has come down to negligible levels. In this sense, the government was successful in stabilizing the economy thus far, but at the cost of large interest payments on a rising stock of domestic debt. The continued stability critically depends on the adoption of further substantive adjustment measures and the credibility of macroeconomic policy. Investors are closely following the authorities' policy stance, and given the openness of the Lebanese economy, any deterioration in their expectations could greatly undermine the current state of stability.

5. The monetary authorities' strategy has been to stabilize the exchange rate as a nominal anchor with foreign exchange market intervention and at the same time to avoid monetization of the fiscal deficit by financing it with Treasury Bills; they have generally succeeded in achieving these twin objectives. This policy fundamentally rests on the investor confidence underpinning the demand for Treasury Bills, and may not be sustainable in the long run. There are two possible indications of some fragility in investor confidence was exhibited in the first quarter of 1993. First, net subscriptions of Treasury Bills were negative in that period despite higher interest rates, and the government deficit was financed mainly with a drawdown on its deposits with the central bank. Second, in an attempt to bolster the Lebanese pound through foreign exchange market intervention, the central bank lost a fairly significant amount of reserves (about US \$190 million) in the first two months of 1993. These developments again suggest that further stabilization measures are urgently needed. //

6. Fiscal Developments. While the fiscal outlook for 1993 remains uncertain, the results of the first quarter was relatively favorable, with an overall deficit of LL 183 billion, or about 6 percent of estimated quarterly GDP, a considerable improvement over the same period last year. Revenues have nearly doubled relative to the same quarter last year as a result of a number of fiscal measures already in place and improved collection, while expenditures have been limited as, under legal provisions, they are not to exceed the 1992 level in the absence of a budget for 1993. The 1993 budget is still under preparation, and given the time required for Parliamentary debate, it is not expected to be in effect until August. The 1993 budget process is proceeding in parallel with the preparation of a ten-year development plan (see Paragraph 11 below); the two will be jointly submitted to, and debated by, the Parliament in about two months. This joint debate is expected to take longer than a normal budget debate. //

7. The remainder of 1993 is subject to uncertainties. On the revenue side, adoption of further measures, i.e., the abolition of the customs dollar and adjustment of electricity tariff rates are still to be implemented. The new tariff structure of the Electricite du Liban (EdL) is expected to take effect within about a month, and that, accompanied by more efficient management, is expected to balance EdL's operating budget by 1994. This would significantly improve the budgetary outlook. The abolition of the customs dollar, and associated tariff reform, is now under intensive discussion with the private sector representatives; it remains to be seen, however, whether or when these measures will be implemented after the three month review period lapsed on April 10, 1993. On the expenditure side, the 1993 budget will come into effect mid-year and capital expenditures will take off under the NERP in the second half of the year. Furthermore, the government is saddled with some overdue obligations which it inherited from the previous government, e.g., rents and employee benefits as well as bilateral external debt payments.

8. IMF and the Consultative Group. The Bank's team emphasized that the IMF involvement in Lebanon's stabilization efforts is essential to mobilization of external assistance and private investment. Given Lebanon's openness, credibility of government macroeconomic policy and investor confidence is the key to stabilization; the Bank team stressed that credibility would be enhanced if the IMF staff were to approve the program and periodically review it. The team indicated to the authorities that if Lebanon has: (i) taken significant prior actions for macroeconomic stabilization, (ii) an IMF staff-approved stabilization program, and (iii) a reconstruction program consistent with the Government's implementation capacity, then there is a good chance that a CG meeting will be successful. A date for such a meeting could not at this stage be fixed.

9. The Prime Minister and the economic team agreed on the need of stabilization and the involvement of the IMF staff as a matter of principle. The Prime Minister, however, indicated that the IMF involvement is politically sensitive and that he would have to proceed cautiously. He indicated that he wants to have the adjustment measures actually in place before going to the CG meeting. On this basis, the Prime Minister envisaged that convening of a CG would not be possible until September this year. The Bank's team suggested that one way to cope with the political sensitivity is to formulate and launch a stabilization program as the government's own at an early opportunity, as did Mexico, and then to bring in the IMF staff to support it, thereby avoiding any semblance of external pressure. The IMF Article IV Consultation Mission is now scheduled for May 10-28, 1993. This mission could assist the Government in designing an appropriate stabilization program.

10. External Support. As regards the assistance from the Gulf nations, Mr. Koch-Weser indicated that the Gulf nations are increasingly demanding adjustment in the context of their external

assistance. The Prime Minister indicated that US \$300 to \$400 million in external assistance could be expected from the Gulf nations, and further amounts may be forthcoming from the Kuwait Fund, the Arab Fund, and other Arab donors.

11. Development Plan. The mission was informed that the Government is preparing a ten-year "development plan", costing US \$8 to \$10 billion, which is intended to build on the reconstruction under the NERP, and represent a longer term public investment program. This plan, expected to be submitted to Parliament, could represent a framework of the government's development strategy. The project for reconstruction of downtown Beirut, with an estimated cost of about US \$3 billion, is to be undertaken entirely by the private sector, starting in early 1994.

12. Gold Reserves. Regarding Lebanon's gold holdings, the Prime Minister indicated that although it may not make financial sense, they should remain untouched at this time as the last resort to inspire confidence.

13. NERP and ERRP. Preparations are well under way for establishing the implementation mechanism for the NERP and the Bank's ERRP. The EC, which is financing the services of foreign consultants for the PMU and SIU's, has issued invitations to a short list of consultants. Consultants for PMU are to be appointed by June 1, 1993 and those for the SIU's soon thereafter. As regards the ERRP, additional external funding was secured recently from the Arab Fund in the amount of US \$25 million in support of the housing component of the ERRP, and the Saudi Fund also expressed interest in providing funding for the same project. The government expects to receive further funding for the NERP when the CG meeting convenes. Concerning the ratification of the ERRP agreements, the Speaker of Parliament expressed his wish to have the Parliament ratify it within a period of about 20 days after receiving the loan agreement. The Council of Ministers has referred the loan agreement to the Parliament on April 7, 1993.

14. Social Sector Issues. Human Resources have traditionally been Lebanon's most important asset. At the same time, social sector issues are extremely complex due to the pluralistic composition of its social and political fabrics. Bank assistance can make a significant contribution in this area. The upcoming human resource development mission in May could possibly identify an emergency operation and what are the needs for appropriate sector work.

15. The Bank team stressed that, given political sensitivity and potential economic repercussions, it is important that a stabilization program be accompanied by some form of social safety net. The government's view is that the poor in Lebanon are not destitute, as there is traditionally family assistance from overseas. In addition, a relatively favorable standard of living in Lebanon in the lower income strata is suggested by numerous indicators, e.g., a large influx of Syrian labor. There are divergent views of this

issue, however, and the government's view is not necessarily shared by the private sector nor by academia. The basic approach of the government is to assure that the expected income and employment generation from the government's investment program and reactivated private sector investment activity benefit the poor. At the same time, in the revised tariff structure for the electricity company, the government is maintaining a life-line tariff for low electricity consumption with cross-subsidization from higher electricity consumption as well as industrial and commercial use. Nevertheless, the authorities agreed for the Bank to help design a social safety net and submit it to the Government for consideration. Such a social safety net could be included in the possible Education Emergency Operation or in the T.A. operation under preparation.

16. The war destroyed much of the institutions for public health as well as the majority of government hospitals. During the war, the militia and the NGOs provided medical services and international relief efforts provided medical supplies to Lebanon. Thus, the present need to restore medical services is enormous. Government hospitals will have to be rebuilt and more public health services provided at private hospitals. A social security system is in place, but there are problems with financing the high cost of hospitalization. There is a shortage of auxiliary medical personnel although there are enough medical doctors.

17. In the education sector, there are immediate needs for the rehabilitation and reconstruction of lost and damaged primary and secondary schools, vocational training centers and universities, as well as for the retraining of teachers and professors. Also, auxiliary teaching materials such as libraries, text books, computers are in short supply. These issues are applicable to all levels of education: primary, secondary, vocational training, and college education.

18. It was agreed that the Bank would consider providing financing for the rehabilitation of the Lebanese public university, either in the context of an emergency education loan and/or by reallocating funds under the ERRP. The latter option should be looked at as a contingency, and could be considered only if the progress of implementation indicates the feasibility of such a reallocation in about six months.

19. Technical Assistance. There are considerable technical assistance needs in Lebanon. As noted, the public administration has been severely weakened and is in dire need of strengthening in order to restore its normal functions. At the moment, there does not appear to be any clear cut coordination in providing technical assistance, which is commencing on an ad hoc basis. Some strong initiative in directing forthcoming technical assistance is required, and the Bank team has suggested the following three-track approach; first, TA under the NERP provided and coordinated by the CDR (Project related TA and TA to enhance the Ministries' implementation capacity); second, strengthening of the central government agencies

for economic management and studies to improve the judicial and administrative systems; and third, a comprehensive civil service reform. The Minister of State for Administrative Reform and the Resident Representative of the UNDP will be invited to Washington in late May or early June for discussions on the second and third points mentioned above.

20. Private Sector Development. The Lebanese authorities are in favor of privatizing a large segment of the parastatal sector. The coverage and timing are under consideration. The timing is influenced by considerations pertaining to initial government investments and appreciation of the assets. The candidates for privatization include the telephone company, the electricity company, the airport, ports, bus transportation, railroad, and the tobacco company. The mission expressed its view that with its private sector resources Lebanon could benefit from privatization of the parastatal sector and pledged Bank support.

21. In view of the predominance of private sector activity in Lebanon's economy, the mission suggested the creation of a tripartite committee to undertake a private sector assessment consisting of the government, the private sector, and the Bank. The objective of the committee would be to identify impediments to private sector activity and to recommend reforms to remove them to create an enabling environment. As part of the private sector assessment, studies will be needed on the financial sector, in particular, the development of capital markets.

22. Round Table on "Lebanon 2005". The mission discussed the convening of "Lebanon 2005" as a forum to discuss a vision for longer-term development of Lebanon beyond the reconstruction phase. The objective of the forum is to explore the possible future economic development path of Lebanon leapfrogging into the next century. Representatives will be invited from some Asian NIC's whose experience may serve as a model for Lebanon. The Prime Minister was very receptive to the idea, and tentative agreement was reached as to the timing and location. It is to be held in late August 1993 in Beirut.

23. Water Resource Study. The mission suggested, and the Government agreed to undertake, a water resource base study for Lebanon as part of the ongoing regional water resource base study involving Jordan, Syria, and Israel.

24. Summary and Conclusion. Provided that peace and calm continue, the Hariri Government can give perhaps the most appropriate combination of ministers needed by the country at this point in time. Their private sector background and personal wealth are the best ingredients for public confidence building. The calm and peace in Lebanon could also attract tourism back from the Gulf countries; this summer will provide an opportunity to test this prediction, particularly in view of the social unrest in Egypt.

25. What the country requires right now is to stabilize the economy, and, concurrently, to get the reconstruction process underway. Along with stabilization, there is the need to develop a social safety net and, if politically acceptable and technically feasible, to implement it. Strengthening of the institutions managing the economy and the reconstruction is another priority. In that context, the country has a unique opportunity to review and improve the administrative and judicial structures, as well as undertake a much needed civil service reform. The social sector, including education, is high on the Government's agenda. Sound economic management, security and peace, and implementation of the reconstruction program will undoubtedly induce private sector investment. There is also a need to review the financial sector, "jump-start" the capital market and remove any remaining impediments to private sector development.

26. In terms of the Bank's strategy I would propose that we concentrate our efforts on the following:

- (i) Together with the IMF assist the Government in implementing the needed economic reforms and NERP;
- (ii) Assist the Government in the reconstruction and development of its social sectors, including providing assistance in human resources development;
- (iii) Help the authorities to review and implement a comprehensive administrative and civil service reform;
- (iv) Aid the Government in developing the private sector. In this context undertake a PSA, a review of the regulatory environment, and the development of the capital market;
- (v) Finally, provided there is an appropriate stabilization program in place, to be periodically reviewed by the IMF, assist the Government in mobilizing the needed external financial support for the NERP through the CG mechanism.

c/w & cc: Mr. C. Koch-Weser

cc: Messrs. Squire, Hussein, Bouhabib, Ijichi (MNAV); Tyler, Heron (MN2DR); Okonjo-Iweala (MN2AG); Bhargava (MN2IE); McKechnie (MN2IN); Keare (MN2PH); Sood (EMPDR); Musalem, Hoppenbrouwer, Ozeki (MN2CO)

<M:\LEB\CK-WESER.BTO>  
Y. Ozeki/L. Hoppenbrouwer

## OFFICE MEMORANDUM

DATE: April 21, 1993

TO: Mr. Caio Koch-Weser, RVP

FROM: Abdallah Bouhabib, MNAV<sup>AB</sup>

EXTENSION: 3 4784

SUBJECT: LEBANON - Back-To-Office Report (April 14 - 18, 1993)

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

*Strictly Confidential*  
Please do not copy

1. Lebanon's economy is in the pre-take-off stage. There is considerable economic movement, but most Lebanese are still waiting for something "big" to happen: a breakthrough in the peace process, substantial grants from GCC countries, and/or a Syrian withdrawal in accordance with the Taif Accords. Nonetheless, there is a lot of anticipation for an improved economy and the coming months, especially the summer season, are crucial for a turn-around in the economic conditions. A large inflow of GCC Arabs for the summer could help the economy take off.
2. The World Bank loan has had an impressive positive influence on the economic situation, which was adversely affected by the lack of support from GCC countries in accordance with the Taif Accords. The loan is further hailed by the business community especially when compared to the volume of Arab funds loans. The RVP's visit and statement to the Lebanese press that the World Bank will continue its involvement in Lebanon was received with enthusiasm.
3. The support for Hariri is still overwhelming from the business community and the general public. Though economic recovery is not yet there, these groups are anxious to give Hariri sufficient time to realize economic prosperity. Two groups are showing their discontent in a variety of ways. First, the politicians, especially Sunni Moslem politicians (Hariri's sect), are nervous. Hariri's success could dwarf these politicians. The other group are government employees who are unhappy with the "freeze" on their salaries while inflation continues to be high. Public school/universities, teachers/professors and judges have been threatening to strike. The minister of Interior privately told me that judges unfortunately are the main problem as regards to improving security conditions. Judges' salaries are extremely low and the government is neither able to provide them with higher salaries nor physical protection, which is necessary for them to perform their duties. As a result, court cases are piling up and the cause of justice is suffering.
4. Despite the only slight improvement in the provision of services (electricity, water, phone, solid waste and roads), almost everybody agrees that the Cabinet's economic team is performing well. Many complain about the ministry of



Finance collecting past and present taxes. In seventeen years of war, many individuals and institutions avoided paying taxes and would not mind continuing this habit. Even electricity, water and telephone services were provided for free for a large part of the population. Government efforts, though unpopular to some, are hailed by most as constructive and necessary for building a modern state.

5. The stability of the currency remains Hariri's most important achievement. It has been stable at around LL. 1750 to the dollar. Both the Central Bank and the prime minister personally would interfere to support a stable currency. Accordingly, currency speculation has almost disappeared. People are, however, worrying about the consequences on the currency of a government without Hariri.

6. When Hariri took office last October, he tried and failed to get "emergency powers" which would enable his government to legislate without passing through the Parliament. It is claimed that Syrian President Assad indicated to Hariri that it was then important to strengthen the Parliament, especially because its legitimacy was in question due to the Christian boycott of the elections. Hariri was promised that the issue would be reconsidered in the Spring. On that basis, Hariri visited Syria and met with Assad for 4 hours during the second week of April. It is widely believed that they discussed the Lebanese government's requests for "emergency powers". Moreover, the Speaker of the Chamber of Deputies, Nabih Berri, a Shiite Moslem and an ally of Syria who conducts parliamentary business with an iron fist, continues to oppose such a proposal. He insists that the Parliament has never delayed government projects and has always acted in a timely manner on all proposals, and thus there is no need for such measures. The President, a Maronite Christian, who was significantly dwarfed by Hariri, stated his neutrality between the prime minister and the speaker. Opposition members of Parliament are accusing the prime minister of attempting to cover up "government failure" by requesting these measures.

7. Syria's influence in Lebanon remains significant. In addition to the "complete coordination" in foreign policy and security, the appointments of medium- and high-level officials have to be cleared indirectly by the respective Syrian officials. Accordingly, the delay in filling, firing, and/or naming new appointees does not suffer only from disagreements between the president, speaker, and prime minister, it also takes time to get Syrian clearance.


8. To sum up, though Hariri is not considered a "superman" anymore, the support for his government remains strong. The expectations are less than earlier anticipated. To most Lebanese, Hariri is a decent, serious, hardworking and clean politician. In a country like Lebanon, these qualities in one person are rare, and hence the support for Hariri despite some disappointments because of the earlier inflated expectations.

cc: Messrs. C. Koch-Weser, R. Chopra (MN2DR), S. Voyadzis.

# OFFICE MEMORANDUM

DATE: March 3, 1993

TO: Mr. Attila Karaosmanoglu, Managing Director

FROM: Caio Koch-Weser, MNAV 

EXTENSION: 35250

SUBJECT: LEBANON - Proposed Emergency Reconstruction and Rehabilitation Project

1. For the Board meeting tomorrow, March 4, 1993, please note that the Japanese ED's office asked if the present Government is a new Government, and whether it took office after parliamentary elections. We replied that the present Government took office on November 1, 1992, following national parliamentary elections.
2. The Saudi Arabian ED requested that a clarification be made as to the Saudi contribution to the Taif Accord mentioned in para. 3 of the MOP. This is being addressed in the speech.
3. We have indications that strong support will be forthcoming from the French, US, Japanese and Saudi chairs, and that the French ED will lead the discussion.
4. A copy of the speech which will be delivered by Mr. Choucair is attached.

Attachment

YChoucair:bw  
M:\LEB\PA013\LENN\RVPTOMD.MEM



# Record Removal Notice



<b>File Title</b> Subject Files: Country Files - Lebanon - Correspondence 01		<b>Barcode No.</b>  1328843		
<b>Document Date</b> 04 March, 1993	<b>Document Type</b> Board Record			
<b>Correspondents / Participants</b>				
<b>Subject / Title</b> Lebanese Republic Emergency Reconstruction and Rehabilitation Project Board Presentation, March 4, 1993				
<b>Exception(s)</b>				
<b>Additional Comments</b> Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.		
		<table border="1"> <tr> <td><b>Withdrawn by</b> Sherrine M. Thompson</td> <td><b>Date</b> March 31, 2017</td> </tr> </table>	<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017
<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017			

X

THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

LEWIS T. PRESTON  
President

January 15, 1993

Dear Mr. Minister:

I have learned of your appointment as Governor for Lebanon on the Boards of Governors of The World Bank Group. I realize this is incident to your responsibilities in your own Government, but I hope you will be in a position to actively participate in the affairs of the Bank Group, as well.

The Executive Directors, Officers and Staff of The World Bank Group believe very strongly in its development mission and in the battle against poverty. We look forward to working with you to make the Bank Group even more effective during the coming years. Congratulations on your appointment and thank you for your willingness to take on this additional responsibility.

I look forward to meeting you in the near future, and send my best regards.

Sincerely,

(Signed) Lewis T. Preston

His Excellency  
Fuad Siniora  
Minister of State  
for Financial Affairs  
Ministère des Finances  
Rue de l'Etoile  
(parallele a Riad Solh)  
Beirut  
Lebanon

cc: Mr. Al-Sultan  
Mr. Chopra  
Mr. Hovaguimian

ETSanidad:ret

THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

LEWIS T. PRESTON  
President

Le 15 janvier 1993

Monsieur le Ministre,

J'ai appris votre nomination aux fonctions de Gouverneur pour le Liban aux Conseils des Gouverneurs du Groupe de la Banque mondiale. Cette nomination n'est qu'un aspect des responsabilités qui vous incombent dans votre propre Gouvernement, mais j'espère qu'il vous sera possible de participer activement aux affaires du Groupe de la Banque.

Les Administrateurs, la direction et le personnel du Groupe de la Banque mondiale ont foi dans la mission de développement dévolue au Groupe et dans la lutte contre la pauvreté. Nous attendons avec le plus vif intérêt l'occasion d'oeuvrer avec vous pour que le Groupe de la Banque soit encore plus efficace pendant les années à venir. Nous vous adressons nos félicitations à l'occasion de votre nomination et nous vous remercions de bien vouloir assumer cette responsabilité supplémentaire.

Dans l'attente de vous rencontrer dans un proche avenir, je vous prie d'agréer, Monsieur le Ministre, les assurances de ma très haute considération.

Son Excellence  
Fuad Siniora  
Minister of State  
for Financial Affairs  
Ministère des Finances  
Rue de l'Etoile  
(parallele a Riad Solh)  
Beirut  
Lebanon

REPUBLIQUE LIBANAISE  
MINISTÈRE DES FINANCES

LE MINISTRE

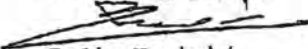
Facsimile Cover Sheet and Message

-----  
DATE: Monday, December 21, 1992  
NO. OF PAGES: 2 (including this page)  
FAX REPLY NUMBER: (212) 478-1669  
TO: Mr. T.T. Thahane  
Secretary  
International Finance Corporation  
Washington D.C.  
FROM: The Office of H.E. Mr. Rafic Hariri  
Head of the Council of Ministers and  
Minister of Finance  
Beirut, Lebanon  
-----

Dear Mr. Thahane,

Please be advised that H.E. Mr. Fuad Siniora - Minister of State for Financial Affairs is designated as Governor for Lebanon in the World Bank group.

Sincerely yours,

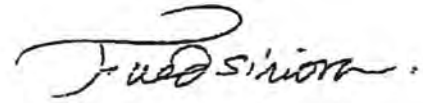
  
Rafic Hariri  
Head of the Council of Ministers and  
Minister of Finance

12-29-92 07:07AM P002 #24

29 DEC '92 09:53 MED GROUP SERV./BEY.

P.1

Please be advised that the facsimile signature specimen of H.E.  
Mr. Fuad Siniora is as follows:

A handwritten signature in cursive script that reads "Fuad Siniora". The signature is written in dark ink on a light background.

X

THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

LEWIS T. PRESTON  
President

January 15, 1993

Dear Mr. President:

I have learned of your appointment as Alternate Governor for Lebanon on the Boards of Governors of The World Bank Group. I realize this is incident to your responsibilities in your own Government, but I hope you will be in a position to actively participate in the affairs of the Bank Group, as well.

The Executive Directors, Officers and Staff of The World Bank Group believe very strongly in its development mission and in the battle against poverty. We look forward to working with you to make the Bank Group even more effective during the coming years. Congratulations on your appointment and thank you for your willingness to take on this additional responsibility.

I look forward to meeting you in the near future, and send my best regards.

Sincerely,

(Signed) Lewis T. Preston

Mr. El Fadl Chalak  
President  
Council for Development  
and Reconstruction  
c/o Presidential Palace  
Ba'abda  
Beirut  
Lebanon

cc: Mr. Al-Sultan  
Mr. Chopra  
Mr. Hovaguimian

ETSanidad:ret



THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

LEWIS T. PRESTON  
President

Le 15 janvier 1993

Monsieur le Président,

J'ai appris votre nomination aux fonctions de Gouverneur suppléant pour le Liban aux Conseils des Gouverneurs du Groupe de la Banque mondiale. Cette nomination n'est qu'un aspect des responsabilités qui vous incombent dans votre propre Gouvernement, mais j'espère qu'il vous sera possible de participer activement aux affaires du Groupe de la Banque.

Les Administrateurs, la direction et le personnel du Groupe de la Banque mondiale ont foi dans la mission de développement dévolue au Groupe et dans la lutte contre la pauvreté. Nous attendons avec le plus vif intérêt l'occasion d'oeuvrer avec vous pour que le Groupe de la Banque soit encore plus efficace pendant les années à venir. Nous vous adressons nos félicitations à l'occasion de votre nomination et nous vous remercions de bien vouloir assumer cette responsabilité supplémentaire.

Dans l'attente de vous rencontrer dans un proche avenir, je vous prie d'agréer, Monsieur le Président, l'assurance de ma haute considération.

Monsieur El Fadl Chalak  
President  
Council for Development  
and Reconstruction  
c/o Presidential Palace  
Ba'abda  
Beirut  
Lebanon

RÉPUBLIQUE LIBANAISE  
MINISTÈRE DES FINANCES  
LE MINISTRE

Facsimile Cover Sheet and Message

-----  
DATE: Tuesday, January 12, 1993  
NO. OF PAGES: 2 (including this page)  
FAX REPLY NUMBER: (212) 478-1669  
TO: Mr. T.T. Thahane  
Secretary  
International Finance Corporation  
Washington D.C.  
FROM: The Office of H.E. Mr. Rafic Hariri  
Head of the Council of Ministers  
and Minister of Finance  
Beirut, Lebanon  
-----

Please be advised that Mr. El Fadl Chalak - President of the Council of Reconstruction and Development is designated as alternate Governor for Lebanon in the World Bank group.

Sincerely yours,



Rafic Hariri  
Head of the Council of Ministers and  
Minister of Finance

01-12-93 10:10AM P002 #48

12 JAN '93 15:48 MED GROUP SERV./BEY.

P.1

Please be advised that the facsimile signature specimen of Mr. El Fadl Chalak will be forwarded at a later date since he is at present out of Lebanon.

01-12-93 10:10AM P003 #48

THE WORLD BANK/IFC/MIGA

***FROM THE DESK OF***

**Ram K. Chopra**  
(MN2, Ext. 32707, Room No. H10-067)

January 8, 1993

NOTE TO MR KOCH-WESER

Caio,

Attached please find communications received from the Lebanese Government on a number of measures related to customs, telephone, electricity fees, and wheat subsidies having been taken. These are very encouraging developments not only because of the substance of the actions being taken, but also because of the fact that they are acting in December and January as they had indicated to me during my visit in mid-December.



Ram Chopra

cc: Messrs. Karaosmanoglu, Voyadzis, Tyler

cc: DMT

RÉPUBLIQUE LIBANAISE  
MINISTÈRE DES FINANCES  
LE MINISTRE

08 JAN '93 11:06 MED GROUP SERV. /REY.

Facsimile Cover Sheet and Message

-----

DATE: Thursday, January 7, 1993

NO. OF PAGES: 1 (including this page)

FAX REPLY NUMBER: (212) 478-1669

TO: Mr. Ram Chopra  
Director  
Middle East and North Africa Region  
The World Bank  
Washington D.C.

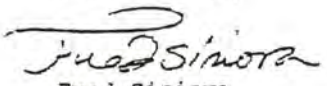
FROM: The Office of H.E. Mr. Fuad Siniora  
Minister of State for Financial Affairs  
Beirut, Lebanon

-----

Please be informed that the Parliament has passed a new law eliminating all customs exemptions and all non-tariff fees. Steps to reform the tariff structure and the exchange rate of tariff valuation are also expected to be completed before the end of January. We will notify you of these changes in due course.

Moreover, across the board telephone fees and some electricity fees have been raised and preliminary steps have been taken to raise other revenue generating fees.

Best regards,



Fuad Siniora  
Minister of State for Financial Affairs

cc: Mr. Fawzi Sultan, The World Bank  
Mr. Paul Chabrier, International Monetary Fund  
Mr. Shakour A. Shaalan, International Monetary Fund

P.1



# Record Removal Notice



<b>File Title</b> Subject Files: Country Files - Lebanon - Correspondence 01		<b>Barcode No.</b>  1328843		
<b>Document Date</b> 07 January, 1993	<b>Document Type</b> Facsimile			
<b>Correspondents / Participants</b> To: Fawzi Sultan, Executive Director From: The Office of H. E. Mr. Fuad Siniora, Minister of State for Financial Affairs				
<b>Subject / Title</b> Decision to liberalize the import of wheat and flour				
<b>Exception(s)</b> Communications of Executive Directors' Offices				
<b>Additional Comments</b>		<p>The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.</p> <table border="1"><tr><td><b>Withdrawn by</b> Sherrine M. Thompson</td><td><b>Date</b> March 31, 2017</td></tr></table>	<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017
<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017			

**OFFICE MEMORANDUM**

DATE: December 30, 1992

TO: Mr. Caio Koch-Weser, MNAV

FROM: Ram K. Chopra, MN2DR *RK Chopra*

EXTENSION: 32707

SUBJECT: LEBANON: BTO REPORT

*Mr. Karim Manoglu*  
*+71*  
*CKW*  
*1/4*

1. I visited Lebanon for three days of intensive discussions (December 15-17) with the new Government of Prime Minister Hariri. Messrs. Hoppenbrouwer and Choucair, whose Emergency Reconstruction and Rehabilitation Project (ERRP) appraisal mission was in the field, joined me in most of the meetings. Mr. Shamsedin joined in a number of the key meetings. In addition to meetings with all key authorities, including the President, the Speaker of the House, the Prime Minister, the Minister of State for Finance Siniora, the Foreign Minister and the President of the Council for Development and Reconstruction (CDR), we also met with several sector ministers, the private sector, donors, and AUB. A schedule of the visit is attached as Annex IV.
2. Mr. Hariri's appointment has inspired confidence and led to great expectations. Some of the consequences of this confidence on short term economic developments are reported in Mr. Hoppenbrouwer's note that is attached as Annex II. In summary, a significant inflow of capital has arrested the depreciation of the Pound and the inflationary spiral, allowed the Central Bank to replenish its foreign exchange reserves, and the Government to switch from Central Bank credit to T-bills for the financing of its large deficit. But the current monetary and exchange rate policy stance has its fiscal costs, perhaps unavoidable, and the short term stability that has been achieved is tenuous and delicate. It could be upset by unforeseen political developments and is not sustainable in the absence of action to correct the macro-economic imbalances, in particular the fiscal deficit. The present Government, very much unlike its predecessor, is well aware that this is the case. It has started taking a number of measures and is prepared to take the necessary additional measures soon. At the same time, while the population at large expects too much from Mr. Hariri with his can-do reputation, it does not expect sacrifice, but rather immediate reconstruction and services to be delivered. Thus the Government faces the challenges of undertaking acceptable fiscal actions and managing, lowering if possible, expectations about what can be done and how quickly to erase the effects of 17 years of war.
3. The Prime Minister and his Cabinet have broad political support. The Christian groups that boycotted the elections are supportive of Mr. Hariri. Among the organized groups, Hezbollah is the only exception, but Mr. Hariri has reached out to Shia religious leaders and his relations with the Speaker of the House, Nabih Birri (Amal faction), are reportedly good. With both Saudi and Syrian support, Mr. Hariri's position is relatively strong. It is unlikely that the question of redeployment of Syrian troops will soon be made a major issue. In any event the eventual Syrian withdrawal, first from Beirut and subsequently from Lebanon is likely to be related to developments in the overall peace process. The Prime Minister, who also holds the Finance portfolio, has assembled an impressive

economic team closely managed and controlled by himself with a close associate, Minister of State for Finance Siniora, who is the de-facto Minister of Finance. The sector ministers are generally very good, but with some exceptions. Many have, like the P.M. himself, a private sector background and use staff from their enterprises, and personal resources, to run matters. In fact, a superstructure, with typical Lebanese private-sector drive and dynamism, is being imposed upon a very weak public administration. This is plausibly the only feasible approach in the short run, but a strengthening of institutions will have to take place if the Government is to carry out the ambitious reconstruction program in a sustainable manner, and not remain overly dependent on Mr. Hariri. Yet, no one advocates that the public sector be expanded; in fact, intentions are for the scope of private sector activity to be further widened into physical infrastructure expansion through BOT arrangements, particularly in telecommunications and power, and private management of public assets. Once immediate reconstruction and rehabilitation of physical infrastructure has taken place, they envisage a very limited role for Government in the future, as it had in the pre-war past. In the meantime, the proposed approach for a massive TA program to address the public administration's weaknesses as the reconstruction program is undertaken, while probably unavoidable, raises questions of coordination and effectiveness that are further discussed in para. 9 below.

4. Stabilization Program, ERRP Loan, IMF and Consultative Group (CG). While the Government's main focus of attention is the reconstruction program, it is cognizant of the need to take stabilization measures and the link between the two. The joint Fund/Bank letter of December 8 was, overall, well received with some doubts and questions about a number of the points and suggestions made by the Fund (e.g. on monetary policy and Central Bank T.A.). The Government also had reviewed the informal draft economic report presented to the previous Government as well as the aide-memoires of the Bank and Fund missions. There was general agreement that early action must be taken to reduce the fiscal deficit, in particular the current account, primarily through revenue measures while at the same time limiting the increase in current expenditures, particularly through wage restraint and a reduction in the budget transfers to the power company.<sup>1</sup> The Government's short term plan of action is attached as Annex I. The administrative measures are already beginning to have an effect on revenue collection. The plans with regard to import duties are in line with the IMF Fiscal Affairs recommendation, but would yield less than the Bank mission's suggestion for a low flat duty rate. Prospects for early passage by the Parliament of the components subject to its approval are enhanced by the earmarking of 10% of customs revenues to municipalities. In all, on the revenue side current projections are for an increase in the range of 80-90% (70-80% in real terms). As regards expenditures, the intention to maintain public sector wages at their current level is a courageous one considering the approximately 100% average inflation in 1992. This decision is facilitated by the appreciation of the Pound that has taken place in recent months, as a result of which inflation has come down to negligible levels (after rising 155% during the

---

<sup>1</sup>/Mr. Hoppenbrouwer informally discussed the fiscal targets for 1993 and 1994 contained in the draft CEM with Minister Siniora's staff. These targets are for an improvement in the current account by about 10 percentage points of GDP between 1992 and 1994. The staff believed that this was a reasonable and achievable target. The overall deficit would not decline because of the initiation of the reconstruction program.



first nine months of the year, prices actually declined in October). The final decision regarding the planned early elimination of the wheat subsidy, currently about US\$25 million on an annual basis, will undoubtedly have to take into account the possible political repercussions of this sensitive issue. With respect to power tariffs, which, together with wage policy, are the key to expenditure control, current plans are to double them on average in early 1993, with further increases in the course of the year, and steps are being taken to improve billing and collection. On the basis of the actions being taken, the quality of the Cabinet, and their stated intentions of taking further action broadly in line with our recommendations, I recommend that we proceed with negotiations and Board presentation of the ERRP loan. Negotiations for the loan could possibly be completed by end-January and all indications are that initial key measures could be in place by that time.

5. The Government's team, together with the Central Bank, could likely design a consistent stabilization program. But IMF assistance would be extremely helpful. The Government may be reluctant to consider a formal IMF Stand-by program because it does not consider it politically acceptable at this stage. I indicated that endorsement of the program by the Fund vis-a-vis the donors in the context of a CG and presentation of the Government's program to its Board (if only for information purposes) would be desirable. In the concluding meeting, Prime Minister Hariri agreed that he would invite the IMF to assist the Government. He felt that the stamp of approval by the IMF would help the credibility of and confidence in his government. It was also agreed that the CG could not be held in February, as Mr. Hariri had initially expected. I indicated that I would recommend that we proceed with the ERRP regardless of the timing of the CG, and that we would attempt to convene a CG as soon as possible thereafter, once we are confident that it can be a successful one. The President and Prime Minister emphasized that a Bank decision to proceed with the loan would give confidence and an important signal to other donors.

6. During the final discussions, Mr. Siniora indicated that the Government would approach the Fund soonest with a request that the scope of work of the planned Article 4 Consultation Mission be expanded to include the design of the stabilization program. As regards the timing of this mission, the Government may be inclined to first complete the preparatory work it considers necessary, including formulation of the budget for 1993, even if that implies some delay in the CG.

7. The Emergency Reconstruction and Rehabilitation Project and the National Emergency Recovery Program (NERP). The appraisal of the ERRP is proceeding smoothly, without major issues, and Board presentation in February appears feasible. We discussed the issue of the size of the NERP, proposed by the Government at US\$2.6 billion over three years. There was full agreement with our suggestion to eliminate the proposal for public financing of productive sector credit to the private sector. This, together with other adjustments, including a reduction of about US\$100 million in the T.A. component, reduces the program to about US\$2.1 billion. There was an initial reluctance with our suggestion that the program be extended over four years (1993-96) in order to more realistically reflect implementation capacity, external financing possibilities and possibilities for contributions from the budget. The Government's initial position was that external financing can be arranged, in part because of Arab support, and that the Hariri "methods" will make quick implementation feasible. We suggested that it

would be advisable to lower expectations and in the end do better than planned rather than fall short. Our arguments as well as our analysis, based on the draft CEM, of the implications for fiscal policy of the counterpart fund requirements, convinced the Government to change its stance.

8. With an estimated direct and indirect foreign exchange component of about 80%, about US\$400 million would be required in counterpart funds to finance local costs over the four years. Despite the significant fiscal adjustment projected for the short term, little or no funds would be available in the first year, and less than required in the second. We confirmed that the Bank under its project could not finance 100% of project cost and indicated that other lenders would normally also limit their share to the foreign exchange component. We offered that we could possibly consider proposing a sliding disbursement scale and suggested that other donors be asked to consider the same. We suggested that a possible way to limit budget contributions in the initial years would be to seek program grant financing, including also food aid. Despite the above, there should be no problem with counterpart funds for the Bank financed project alone (about US\$30 million over three years).

9. Technical Assistance Coordination. Despite the reduction in the T.A. component of the NERP, the overall amount of T.A. needed for the program (about US\$200 million), much of it frontloaded, and for institutional strengthening outside the framework of the program, is very large. In addition to the current proposal to set up a T.A. coordination unit in the CDR, and the UNDP's proposal to establish a grant facility to channel donor contributions to the T.A. program, there is an urgent need for coordination at a higher level to ensure that the T.A. program adequately reflects both the short term reconstruction needs and the vision of the future role of the public sector, that T.A. activities for the public sector at large are selected in accordance with Government priorities and needs, that duplication is avoided, and that maximum use be made of the talents of Lebanon's private sector, both in Lebanon and from abroad. After consulting the UNDP Resident Representative on the idea, I therefore suggested to the Prime Minister that an inter-ministerial committee, including CDR and the Central Bank, be established, to be headed by the Prime Minister and supported by a small technical secretariat to undertake the required coordination. I indicated that we could consider a small free-standing T.A. loan to support this effort and to act as a catalyst for attracting the significant concessional or grant resources needed for the overall T.A. program. The Prime Minister agreed that it would be important to establish such a committee and welcomed the Bank's role and proposed T.A. loan.

10. Bank Assistance Beyond the ERRP. The Government is looking forward to working closely with the Bank. The Government would particularly welcome the Bank's advice and technical assistance, in addition to limited amounts of lending, because our terms are considered hard. The appreciation for the Bank, reflecting in part the work done so far by our ERRP and economic missions, was also evidenced by the Prime Minister's and President's request that we establish a resident mission and by the request for secondment of Bank staff working on the ERRP mission. While I expressed appreciation for the Government's confidence in the Bank and our willingness to work with the Government beyond the ERRP, I indicated that a resident mission and the requested secondments would not be possible at this stage.

11. The proposed focus of the future Bank program as outlined in my memo of November 30 to you is fully in line with Government priorities and, I am now even more convinced, responsive to the country's needs. The emphasis on human resource development is consistent with the views expressed repeatedly during my meetings that Lebanon has no assets but its people, that the high standard of education and health was the key factor behind the country's success in the 60s and 70s, including its role as a service center for the Arab world, and that Lebanon has to urgently make up for the lack of investment in human resources during more than a decade and a half. The early initiation of sector work in the human resources sector was welcomed by the Prime Minister, who stressed that he would want to see projects in this and other sectors developed in the context of a sectoral strategy that includes institutional and policy issues. In infrastructure, with the proposed Government approach to power and telecommunications development (para. 3 above), possible areas for early support, based in part on work done in connection with the ERRP, could include water supply, sewerage/solid waste and housing, with environment and transport as subsequent possibilities. The Government welcomed the idea to undertake sector work in the water supply and sewerage sector as soon as possible.

12. Social Safety Net. The discussions on this subject indicated that the Government does not consider it necessary or feasible to create a social safety net or to take special measures, other than designing policy changes to avoid the negative impacts on the poor, such as maintaining life-line consumption tariffs for public services and low import tariffs for basic necessities. There is genuine doubt that the public administration could deliver targeted subsidies efficiently, if at all, or that the budget could afford it. It is also clear that socio-political factors, particularly the denominational aspects, could make this a divisive issue. It is also argued that NGO's (broadly defined to include Hezbollah in the Shia areas) have traditionally provided this function, with external support, and continue to do so, although some of them may be less active now that the war is over. Finally, and more importantly in the Government's view, the stability of the exchange rate, through appropriate fiscal and monetary policies, and price stability, combined with the employment effects of the reconstruction and recovery program and overall growth generated by private sector confidence and activity will benefit the poor. On balance the initial fiscal measures being taken and proposed are probably not regressive and should not significantly affect the poorest and most vulnerable.

13. Concluding Remarks. Overall it was a productive mission and I came away favorably impressed by the quality and dedication of the new Government, the initial policy measures taken and the overall approach and future policies being considered. This Government has the best chance in many years to provide a measure of stability to foster the confidence of the private sector. Clearly there are risks. External events, particularly regional developments and the outcome of the ongoing peace talks, could upset the hard-found stability. Domestically, unfulfilled high expectations and factional differences could hamper the Government from taking the ambitious and difficult measures that are clearly required. On balance I recommend that the Bank should engage with the new Government, which would by itself help in increasing the confidence of the Lebanese private sector and the international community.

Attachments

Distribution: Messrs./Mmes. Squire, Husain, Murli, Bouhabib, Diwan, van Eeghen (MNAVP); Heron, Tyler (MN2DR); Kohli, Sood (EMTDR); Shamsedin (EDS11); Garg (EMTAG); Bhargava (MN2IE); Okonjo-Iweala (EMTAG); McKechnie (MN2IN); Keare (MN2PH); Walton (DECVP); Martinez (EMTTF); Hayward (EMTWU); Golladay (EMTPG); Voyadzis, Hoppenbrouwer, Erim, Ozeki, Courtney (MN2CO); Sven Burmester (MN2EG); Choucair (IMF); ECA/MENA Files, Chron

LHoppenbrouwer:lem  
M:\LEB\RCTOCKW

LEBANON: FISCAL MEASURES

I. Revenue Measures

The Ministry of Finance is confident that a substantial increase in government revenues in 1993 is achievable. This confidence is due to (i) some proposed fiscal reforms, (ii) tighter control procedures, (iii) real growth in the economy, and (iv) proposed increase in fees.

Some of these measures already taken include:

1. A proposed law (already sent to the parliament) to consolidate non-customs surcharges into the customs tariff and to totally eliminate most exemptions from custom duties.
2. Preparations regarding the simplification of customs tariff and the introduction of the dollar market rate for the valuation of imports have been completed. When the proposed law, mentioned above, is passed by the parliament (expected early January 1993) all the customs measures will be implemented simultaneously.
3. An additional inspection and audit unit has been introduced for the Beirut port and airport. No merchandise can be cleared without the approval of this unit.
4. A review of all fees such as car registration fees, traffic citations, stamp fees, etc. is being finalized and will be submitted to the parliament shortly.
5. The enforcement of actual values of property in the calculation of registration fees has started. To assist in this enforcement, zoning of all the main cities in Lebanon is almost complete. In addition, a task force comprised of inspectors from the public sector, auditors from the private sector and real estate experts has been formed with a clear mandate to ensure that all real estate divisions adhere to the new valuation system.
6. A tight computer control system has been introduced to track all real estate transaction values on a weekly basis.
7. A proposal regarding the settlement of building code violations and incursion of government property and seashores is being finalized and will be submitted to the parliament very soon.
8. An income tax reform is currently being discussed. The borrower believes that an across-the-board decrease in income tax rates will reduce the incentive for taxpayers to cheat on their declarations and may lead to higher income tax revenues. In addition, such a reform would help attract new investors.

9. A task force similar to the one described in point 5 above has been formed to (i) audit tax declarations and (ii) find ways to widen the base of taxpayers.

10. Telephone charges have been substantially increased. The increase has been approved by the cabinet and sent to parliament.

In short, the Government believes that the best way to increase revenues is by enhancing tax collection and diversification of the sources of tax.

II. Expenditure Measures

1. A decision has been taken in principle not to increase nominal wages and salaries.

2. An elimination of "ghost workers" by strictly controlling attendance.

3. Containment of internal debt service by gradually lowering the interest rates.

4. A study regarding the elimination of wheat subsidy is completed and expected to be implemented early January 1993.

5. An additional control unit has been established to check all tender offers for all ministries.

6. A plan regarding pricing and collection of electricity revenues is currently being prepared.

LEBANON-SELECTED SHORT-TERM ECONOMIC DEVELOPMENTS

1. Recent economic developments were last reported with Mr. Hoppenbrouwer's BTO Report dated October 26, 1992. The following is based on information obtained during his mission with Mr. Chopra.
2. The confidence inspired by the appointment of Mr. Hariri as Prime Minister led to large inflow of capital (including the conversion of US\$ to Lebanese Pound deposits). Because of Central Bank intervention in the foreign exchange market, the appreciation of the Pound was limited; the rate moved from about US\$1 = LL 2250 in mid-October to about 1850 at present. In the process the Central Bank replenished its (non-gold) foreign reserves holdings. Following a loss in reserves of US\$675 million during the first nine months of the year, close to US\$1.0 billion were added to the reserves, which by end-November stood at around US\$1.5 billion.
3. As a consequence of the increased Pound liquidity resulting from the Central Bank's purchases, the stock of outstanding T-bills sharply expanded (both on account of the reserve requirements on Pound deposits and voluntary purchases of T-bills). Whereas the stock of outstanding T-bills by end-September stood at about the end-1991 level, it subsequently more than doubled. In all, the stock of internal public debt, exclusive of interest on discounted T-bills, rose from LL 2.1 trillion to LL 3.2 trillion at the end of November. (In US\$ terms it declined from US\$2.4 billion to US\$1.7 billion.) Thus the financing of the Government's deficit switched from net credit from the Central Bank (about LL 750 billion during the first nine months of 1992) to T-bill financing; by end-November net Central Bank credit to the Government had become -LL 100 billion (a shift of LL 850 billion since end-September).
4. The parallels with the 1991 situation are clear. However, on this occasion, the Central Bank moved quickly to lower interest rates on short-term (3 months) T-bills (from 22.5% in mid-year to 13% at present). In order to induce a shift to longer maturities it set a sharply increasing yield curve, with rates on 2-year bills currently at 24%. The weighted average rate is about 17%. Despite this reduction, the current monetary and exchange rate policy obviously has significant fiscal costs. (With a stable exchange rate, there is an approximate 14 percentage point differential between the average rate paid on T-bills and the return on the added US\$ foreign reserves of the Central Bank.) The Central Bank is not currently considering the option of leaving T-bill rates to be market-determined, in part because it fears that the resulting decline will result in an excessive shift out of the Pound. The alternative of non-intervention in the foreign exchange market is also not being considered because of the expected resulting excessive appreciation of the LL. Thus, the authorities currently consider the fiscal impact of their sterilization policy to be the unavoidable cost of stabilizing, or moderating the appreciation, of the exchange rate.
5. Also in contrast to 1991, the current Government is fully aware that the fiscal deficit needs to be reduced despite the apparent stability that has been achieved. (Although CPI estimates are not yet available for November, it is likely that given the high import to GDP ratio and the appreciation of the exchange rate, inflation currently is negligible; after increasing by 155% during the first nine months of the year, the CPI index actually declined by 2% in October.) Based on information through November it is estimated that the overall deficit for 1992 will

be about LL 1.1 trillion, or about LL 150 billion less than had been estimated in October, with higher revenues and lower expenditures each accounting for about half of the difference. All of the deficit would be financed through domestic debt; both Central Bank financing and net foreign financing will be negative this year. (So far this year, the Government paid about US\$50 million in debt service arrears.) Government's plans for fiscal action are discussed in Mr. Chopra's BTO Report.



**CONFIDENTIAL**

FORM NO. 709  
(8-84)

**THE WORLD BANK/IFC**

**ROUTING SLIP**

DATE:

12/23/92

**FROM THE REGIONAL VICE PRESIDENT**

NAME

ROOM NO.

Mr. Karaosmanoglu

APPROPRIATE DISPOSITION

NOTE AND RETURN

APPROVAL

NOTE AND SEND ON

COMMENT

PER OUR CONVERSATION

FOR ACTION

PER YOUR REQUEST

INFORMATION

PREPARE REPLY

INITIAL

RECOMMENDATION

NOTE AND FILE

SIGNATURE

REMARKS:

For your information.

Caio Koch-Weser

**DECLASSIFIED**

**MAR 31 2017**

**WBG ARCHIVES**

FROM:

**OFFICE MEMORANDUM**

DATE: December 21, 1992

TO: Caio Koch-Weser, RVP

FROM: Abdallah Bouhabib, MNAVP

EXTENSION: 34784

SUBJECT: LEBANON Back-to-Office ReportNa Karagomanoğlu  
F71.CKW  
12/22

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

Confidential(Please do not copy)**A. INTRODUCTION**

1. To the average Lebanese, HOPE is currently spelled H,A,R,I,R,I. The appointment of Rafic Hariri as Lebanese prime minister has changed Lebanese priorities like no other development in peace-time Lebanon. Newspapers' headlines are presently focused on business and economics, while political issues are deferred to inside pages. Hariri dwarfed all other politicians, including the president and the speaker, and his activities dominate the Lebanese political and economic scenes. And although his "monopoly of power" is irritating many politicians within and outside the government, Hariri has a strong mandate from the general public to rehabilitate, reconstruct and renew the state. The expectations, from the once poor man who became a billionaire, are substantial after 17 years of conflict.

2. Hariri's government is expected to provide 24-hour supply of electricity and clean water; build a sewer system for all of Lebanon, especially the urban areas; clean the streets and collect solid waste; provide funds for housing to the poor and the displaced; rebuild public schools and the national university and modernize the educational system; resurface the road network and construct new urgently needed highways; support the rebuilding of the tourist and industrial sectors; revive agriculture; and curb inflation. The expectations are high and the prime minister is doing nothing to moderate them or to identify the road blocks. Hariri, to the Lebanese, is their wishful thinking, the angel who will bring back their "old glory" which was destroyed by the "wars of others on their land".

**B. WHY HARIRI?**

3. The summer's parliamentary elections left the Syrians and their Lebanese allies, including the presidency of the republic, very weak. Less than 30% of eligible voters participated in the election process (Christians 15%, Sunnis 30%, and Shiites 70%). The economy was rapidly deteriorating and an increasing number of Lebanese were leaving the country. To many observers, last May's 'cost of living' riots are a minor indication of what could happen if the political and economic situations continue their downward decline. Of

the traditional politicians, only Salim El-Hoss could have obtained a modest mandate to govern, but neither the president nor the Syrians would pick him for the job. El-Hoss was too educated and sophisticated for the modestly educated president and too independent and nationalistic for the Syrians.

4. The Syrians, on the other hand, wanted stability and peace in Lebanon. In a changing and unpredictable global situation, it is always important to keep things under control. Progress on the peace front is slow and all sides are waiting for Clinton to name his foreign policy team. Meanwhile, Clinton is on record during the election campaign for calling Assad a terrorist and demanding that the Syrians pull out of Lebanon. Also, the Syrians are afraid that the Clinton administration and Israel would attempt to pressure them to compromise at the bilateral peace talks more than they desire or are able to. After all, the issues that the US may raise are many and include Lebanon, terrorism, drug-trafficking, democracy, human rights and the peace process. Syrian cooperation on the last issue would send other issues to the back-burner. After the fall of the Soviet Union and the Gulf war, the Syrians feel vulnerable and in need for a mentor they can trust and live with. Accordingly, they want a period of calm in Lebanon as the leadership watch the developments in the US, Israel and the peace process.

5. By all counts, Hariri is a would-be savior who could alter the gloomy outlook in the country. His assumption to power is expected to bring about economic recovery to Lebanon, create business opportunity and employment, provide basic needs to the population and even replenish the vaults of the relatively well-to-do Lebanese and Syrians. Being also a Saudi citizen and close associate of King Fahd, Hariri, it is believed, would be able to obtain official Saudi and Gulf assistance and attract private investment as well. Moreover, Lebanese and Syrian decision makers thought that Hariri alone could implement the Taif accords' recommendation for establishing the "International Fund for the Reconstruction of Lebanon"; the Fund's capital is expected to be about \$5 billion. In addition, the Lebanese continue to expect that the balance of the commitments the Arab Summit of 1980 had allocated to Lebanon (\$1.6 b) would be added to the Fund. Should all the above be realized, and it is unlikely, Hariri then would be able to restore Lebanon's place in the region and the world. Lebanese do indeed believe that Happy Days would be back again.

6. In fact, when Hariri was asked to form a cabinet in mid-October, 1992, the Lebanese, from all economic classes, rushed to sell their dollars for the lira (LL) and the Central Bank was able to increase its foreign exchange holdings by \$1.5 billion, while the lira's value increased from about \$1 = LL2,850 to about LL1,850. The \$1.5 b is considered to be a reflection of the extent of the Lebanese confidence in Hariri.

7. One also should add to Hariri's political assets his careful planning and investment, in the past decade, for the potential of just such an opportunity. In Lebanon, almost all religious, philanthropist, academic, health and media institutions and individuals have benefitted from the generosity of Rafic Hariri. Tens of thousands of families also benefitted from the Hariri Foundation through scholarships given to their children in Europe, North

America and Lebanon. Politicians of all affiliations also received large contributions from Hariri. Even the presidency of the republic, with relatively small budget allocation for functioning, is kept financially viable by Hariri's support; in fact, the President lives in a Hariri owned house. More recently, it is said that a political leader received about \$8 million to include and insure that a Hariri relative win a parliamentary seat.

8. In Syria, Hariri's contributions were also generous. He built, as a gift to the government, the presidential palace and a convention center in Damascus, among other things. The Syrian Vice President, Abdul-Halim Khaddam, and other high ranking Syrian officials, are great allies and friends. Hariri keeps an impressive presence, business and public relations, in Damascus. Washington also rushed to support Hariri's appointment. Hariri has been coordinating with US officials on Lebanon since 1983. Hariri is also a generous contributor to many US think-tanks and universities where many retired career diplomats seek scholarly residence after retirement. Even in France, where foreign political contributions are not a major problem, Hariri has a large number of friends, including the mayor of Paris and the former Prime minister of France, Jacques Chirac. He also has a substantial business presence in banking and industry.

9. Accordingly, when Hariri saw the opportunity early this fall, he called all his IOUs. The Lebanese press paved the way, President Harawi asked for Hariri with determination, Washington, Paris and Riyadh blessed the Hariri's candidacy, Hariri's Syrian friends lobbied hard, the Parliamentary consultation supported Hariri overwhelmingly and President Assad obliged.

### **B. ISSUES AND PROSPECTS**

10. The Hariri cabinet is not totally under his full control. Security and foreign policy posts (Foreign Affairs, Interior, Defence and Information) remain with Syria's Lebanese allies. Other Syrian allies received less important portfolios, and some were kept out of the cabinet. Hariri has a limited overall mandate; but, his mandate to deal with economic and social issues is relatively wide. His selection of the economic and most social ministers is an indication of this mandate: The finance Minister was the CEO of Hariri's Banque Mediterranee; the head of the Council of Reconstruction and Development (CDR) was the president of the Hariri Foundation; the governor of the Central Bank was Hariri's candidate for the presidency in 1988; the minister of Economy (a successful businessman) is a board member of Banque Mediterranee; the minister of Culture and Higher Education (a successful lawyer & businessman) is the vice chairman of Banque Mediterranee; the minister of Justice is Hariri's lawyer who wrote the law of the "Real Estate Corporation" which will build downtown Beirut (Hariri is the general partner); the minister of Telephone (a competent civil servant) is a Hariri associate; the minister of Water & Electricity is a Lebanese industrialist with extensive interests in Saudi Arabia and the U.S.; and the minister of Public Works is also a Hariri associate.

11. Hariri's 'real' cabinet is composed of competent and successful Moslem and Christian ministers. Their weakness is their closeness to the prime minister in a country that values diversity. Their immediate impact on the economy is already felt. In addition to the stabilization of the foreign exchange, the ministry of Finance commenced its efforts to collect taxes and customs duties. The CDR has completed the reconstruction plans and implementation of previously studied and approved programs has started. The ministers are determined to succeed and they know their agenda very well. In short, Hariri's cabinet is expected to improve utilities and government services within a reasonable period of time. Full restoration of these services would, however, take years to be completed. Moreover, although the Central Bank is trying to absorb the immense liquidity that was generated from exchanging 1.5 billion dollars for Lebanese liras, the probability of controlling the hyper-inflation is modest. A spiral of inflation and wage increases could be used by Hariri's political foes to weaken his grip over the country.

12. Hariri could face a further problem in his attempt to implement a civil service reform plan. His government already asked, and will receive from the Parliament, a mandate for civil service reform. This could prove to be more difficult to achieve. After all, civil servants do belong to religious sects and are protected by political leaders. Furthermore, any new slate of high level appointees will have to be based on political and religious quotas, and accordingly, will be subject to scrutiny and bargaining with the political and religious establishment in the country. Some politicians, including ministers, believe that there is no need for making reform an issue. Out of 17,000 civil servants, excluding teachers and military, at least 7,000 are either dead, left the country or have better jobs. They still, however, receive salaries. One minister told me that he gave his 700 employees a warning to report to work or risk being expelled; only 400 reported to work.

13. Another potentially explosive issue is the presence, around Hariri, of very competent Sunni advisors. They are becoming the group of technical and decision-making advisors. Again, in a country like Lebanon where "man does not live by bread alone", such monopoly of power in the hands of one religious group would not sail smoothly for a long time. Sooner or later, if this competent group is not enlarged to include other sects, the advisors could become an issue and a liability.

14. But the most potentially explosive issue is the issue of conflict of interest. Though it is not in the law for the prime minister or any government official to put their business interests in a trust fund to be managed by a trustee, the large volume of the P.M.'s interests, its business ties with the state's affairs, the relatively large number of his former employees who are now in the government, and Hariri's control of the Real Estate Corporation in-charge of developing downtown Beirut, could create a substantial conflict of interest in the near future. Already two leading dailies have started to exploit this issue. One daily asked Hariri to choose between being the P.M. of Lebanon or the P.M. for the Real Estate Corporation.

15. The means of financing the reconstruction program is another potentially explosive issue. Hariri's ties to the Saudis have created an expectation among the Lebanese that he should obtain grants to finance the program. Traditional and pro-Syria politicians are already on record that they will oppose financing the reconstruction program by loans. It is widely stated that the parliamentary delay in approving the Kuwait Fund loan is due to the opposition to receiving 'loans' from Arab countries. Many politicians are stating that 'those who financed the war should finance peace', the reference is to oil money. Hariri's 'unofficial' trip to Riyadh and his meeting with the Saudi leadership did not produce any declared promise for assistance. The Saudis, it is said, do not have a Lebanese policy, but rather a Syrian policy. If their relation with Syria is good, they help Syria and do not need to assist Lebanon; if it is bad, they would not help either because any help to Lebanon could further irritate the Syrians. Some observers believe that Saudi funds could come when Hariri's government takes off; otherwise they may be associated with failure. Yet, many believe that the Saudis and the Gulf, after the two Gulf wars, have no extra funds to pass to Lebanon.

16. Two more issues, both political, could undermine Hariri in the first half of 1993. The first issue relates to regional and international politics. The consequences of the lack of progress in the bilateral talks (BLT) could have its adverse effects in Lebanon. Syria expects the Clinton Administration and Israel to exert pressure on them in favor of a separate peace agreement; an outcome that Syria would prefer to avoid. In the absence of a foreign policy team, however, the Clinton Administration is not yet clear with regard to its relations with Syria. But this will become clear in the Spring. It is greatly feared that any negative relation between Syria and the US would play itself out in Lebanon. Already Syria stopped issuing passports to its Jewish community (there is still about 2,000 Jews in Syria). Although no one expects Syria to withdraw from the BLT, the recent developments indicate nervousness on the part of Syria. President Assad does not like operating in vacuum, especially when he suspects that his understanding with Bush and Baker may not be honored by the Clinton Administration.

17. The other issue has to do with Syria's half-hearted support for Hariri. Syrian allies in Lebanon are not supporting the government fully. One pro-Syrian minister told me that the honeymoon with Hariri would last six months. Another ally of Syria asserted that their support would depend on the regional political situation and the present circumstances necessitates that Hariri be in place. Although Hariri's political investment in Syria is considerable, the fact that such decisions are taken by one person who is not affected by material gains, make alliances and political investments unimportant. It is President Assad only who decides who should be the P.M. in Lebanon, and his decision is based on what he perceives is the interest of his Syrian regime.

### C. CONCLUSIONS

18. Hariri's appointment to the premiership brought hope and expectations. He has a strong mandate from the people. He is surrounded by capable and experienced ministers and advisors and operates in a very difficult domestic, regional and international circumstances. His success, however, depends more on his recognition of the delicate political situation in Lebanon and his ability to accommodate the political and economic systems, than on the external situation. Although the latter could affect the life of Hariri's government, he has no influence on its developments. The fact that security ministries are in the hands of Syria's allies, would, to a certain extent, shelter Hariri from regional and international changes.

cc: Messrs. Chopra, Voyadzis.

THE WORLD BANK  
Washington, D.C. 20433  
U.S.A.

LEWIS T. PRESTON  
President

December 11, 1992

Dear Mr. Prime Minister:

I have learned of your appointment as Governor for Lebanon on the Boards of Governors of The World Bank Group. I realize this is incident to your responsibilities in your own Government, but I hope you will be in a position to actively participate in the affairs of the Bank Group, as well.

The Executive Directors, Officers and Staff of The World Bank Group believe very strongly in its development mission and in the battle against poverty. We look forward to working with you to make the Bank Group even more effective during the coming years. Congratulations on your appointment and thank you for your willingness to take on this additional responsibility.

I look forward to meeting you in the near future, and send my best regards.

Sincerely,

(Signed) Lewis T. Preston

His Excellency  
Rafik Hariri  
Prime Minister  
and Minister of Finance  
Bristol Hotel  
Ras Beirut  
Lebanon

cc: Mr. Al-Sultan  
Mr. Chopra  
Mr. Hovaguimian

*ET*  
ETSanidad:ret



# OFFICE MEMORANDUM

DATE: December 9, 1992

TO: Mr. T. Thahane, Vice President and Secretary

FROM: Mohamed W. Hosny



EXTENSION: 81027

SUBJECT: Appointment of H.E. Rafik Hariri as Governor -- Lebanon

We have been informed by our Lebanese authorities that H.E. Rafik Hariri, Prime Minister and Minister of Finance, has been appointed as Governor of World Bank Group for Lebanon.

RECEIVED

92 DEC 10 PM 7:19

December 10, 1992

Dear Mr. Prime Minister:

The Lebanese Government, financial institutions, and people now face very difficult challenges in rebuilding the country after years of war and instability. Not only is large-scale physical reconstruction needed but a rebuilding and reform of the basic institutions of government and economic management must be undertaken. These tasks, enormous in themselves, must be addressed while taking decisive steps to avoid hyperinflation, stabilize the economy, and lay the foundation for growth and economic recovery. Only if successful in all these endeavors can the private and official capital required for reconstruction be attracted, and a thriving economy with expanding incomes and social services be restored.

Fortunately, the confidence already demonstrated in your Government by the financial markets provides a strong mandate for decisive action on the economic front, even if this requires some short-term sacrifice. As the present window of opportunity should not be lost, we would like to share with you, with a sense of urgency, the views of our two institutions on policy measures and system reforms of most immediate importance.

Immediate Economic Policy Measures

Key to a lasting reduction in inflation and the achievement of stable growth is forcefully reducing the overall fiscal deficit, which has resulted from the existence of an inadequate revenue system, including weak tax administration and collection, rising debt service outlays, and weak controls on expenditures. The fiscal deficit in 1992 is expected to reach nearly 60 percent of expenditure, and will be largely financed through credit from the Bank of Lebanon (BDL). This has led to a more than doubling of private sector liquidity and price levels during the year, along with a rapid depreciation of the exchange rate (despite substantial BDL intervention and reserve losses in the early months of the year). Fortunately, with the announcement of your Government confidence was restored and flight from the Lebanese pound reversed, enabling the BDL to restore its foreign exchange reserves to comfortable levels. However, until the underlying fiscal and monetary imbalances are corrected the position will remain volatile and subject to a renewed bout of instability-- conditions that will discourage private investment and growth.

Financial policies for 1993 should be devised with the objectives of achieving a major reduction in inflation, a stabilization of the exchange rate (without direct intervention), and an expansion of private sector investment and production. This will mean targeting a much slower pace of credit and liquidity expansion while providing for the genuine credit needs of the private sector. Consequently, a first major step on the road to recovery is a sharp reduction in the overall fiscal deficit consistent with

much reduced bank financing--or other domestic financing--of government. Moreover, the degree to which government operations and the deficit can be financed from abroad (through reconstruction grants and loans, for example) will need to be limited to the non-inflationary absorptive capacity of the economy.

Advice on reducing the fiscal imbalance has been provided over the past year by both the Fund and the Bank. Particular measures to reduce the fiscal imbalance and specific targets for the overall deficit have most recently been outlined in the aide-memoire of the October Fund policy mission (a summary of whose fiscal recommendations are attached), while a recent Fund technical assistance mission has also provided recommendations on revenue reform and mobilization. There is, therefore, a strong basis already at hand for prompt action to improve the Government's finances. Additionally, discussion of fiscal targets and policies can usefully take place at the time of the forthcoming Fund consultation mission (scheduled for January or February 1993). As part of these immediate steps, we would emphasize the importance of putting in place a limited number of measures with sizable immediate yields--such as external tariff reform and customs valuation, petroleum taxation, excise taxation, and the elimination of subsidies--all of which can be implemented without the delays associated with securing parliamentary approval. Other measures with a more medium-term effect are fundamental tax reform and civil service reforms aimed at reducing government employment while providing, in time, competitive wages. In line with the fiscal objectives, you may also wish to consider the introduction of social safety net measures with a view to mitigating the impact of adjustment on the poorest and most vulnerable segments of society, as you may know, the Bank stands ready to provide assistance in the design of such measures.

Immediate pressures for expenditure increases will undoubtedly be strong, especially for reconstruction related outlays--including those of the Council for Development and Reconstruction (CDR). However, consistency with a stabilizing fiscal program will need to be assured so as not to endanger the macroeconomic growth, inflation, and balance of payments objectives. Clear priorities, therefore, need to be established in the reconstruction program within the limited resources available. In this context we would note that the recent Bank pre-appraisal mission for the proposed Emergency Reconstruction and Rehabilitation Project has reported on the CDR proposals for a US\$2.6 billion, three-year, national reconstruction program, of which the proposed Bank project would form a part. Our view based on a preliminary review of these proposals is that the size of the program should be reduced, in part by eliminating the proposed provision of credit to the productive sectors financed by external loans (to be contracted or guaranteed by the Government) or from other government resources. This aspect, we think, is best left to Lebanon's financial sector. At the same time it would be more realistic to aim at implementing the reduced program over a four-year period. As the Bank has already informed you, it is currently proceeding with the final appraisal of the proposed project. Consequently, early fiscal action is also important to

provide the donor community with assurances that the Government will generate, within a stabilizing overall economic program, the local counterpart funding for the Bank-financed project and the national reconstruction program, and that Lebanon will have the fiscal capacity to service debts contracted for reconstruction, including the Bank's loan. Finally, Bank staff consider it a high priority to establish a legal and regulatory framework which encourages privatization of public enterprises along with private sector development of utilities and physical infrastructure. The Bank would be pleased to provide assistance in this area.

Now that its foreign exchange reserves have been replenished, we think the BDL should refrain from further intervention in the foreign exchange market apart from some temporary smoothing of abnormal fluctuations. This policy should be reinforced by decontrolling interest rates to equalize risk-adjusted returns in domestic and foreign currency, thereby allowing market forces to work. Continued maintenance of Lebanon's open trade and payments system is, of course, an essential ingredient of this policy which has served the country well in the past. With a substantially reduced fiscal deficit, a stabilizing monetary policy to bring about low rates of inflation and exchange rate stability will be possible. Also, within this framework the BDL should move to "indirect monetary control" instruments in the implementation of monetary policy, essentially selling or buying treasury bills competitively to control domestic liquidity and inflation.

#### Financial System Reforms

The above financial policies need to be implemented in the context of improved systems of economic management and public administration. This need is particularly evident in the management of the Government's finances where a reform, led from the top, is needed to restore fiscal discipline. On the expenditure side of the budget this requires, at the policy level, a transparent process for arriving at comprehensive (or government-wide) expenditure allocations, which are then respected. For example, all fiscal operations, including the expenditures of the CDR, should be included in the budget and reflected in the financial program. They also need to be subjected to government expenditure control and monitoring procedures which meet international standards. Expenditure allocations should reflect the Government's priorities, which should encompass policy decisions on issues such as subsidies and the pace of infrastructure spending and, in time, reforms in civil service employment. With clear and firm policy guidance from the Cabinet, expenditure allocations should be enforced by controllers held accountable for implementing the Government's program. Equivalent reforms in the administration and enforcement of the tax laws are also essential while the tax system should be simplified and made more efficient so as to assist in resource allocation and in revenue mobilization.

As regards the banking system, the BDL has served Lebanon well over the difficult wartime and immediate post-war period. However, due to the circumstances, a number of banking and control practices were introduced

which are not consistent with an efficient modern banking system. Some of the systemic reforms now needed are quite technical (e.g., introducing internationally accepted capitalization standards and banking supervision requirements), others less so (e.g., the scaling back of banks' treasury bill purchase requirements). As noted above, one reform which is of particular importance is providing the BDL with authority (and responsibility) for the active management of domestic liquidity, with the objective of controlling liquidity and inflation. Setting monetary policy on such a basis, allied with comprehensive bank supervision reforms, will contribute substantially to restoring the banking system to international competitiveness and Beirut to its former status as a financial center. Some of these changes can be effected promptly, while others will be feasible only after the BDL staff is adequately trained and organized.

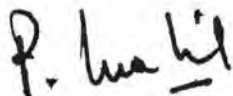
The financial and systemic reform policies described provide Lebanon with the best prospects for a rapid recovery in which the abilities and energies of the private sector are utilized to the fullest. These policies will require difficult and sometimes painful choices by your Government, as well as a determination to see this program of reform and adjustment to its conclusion. In this respect our two institutions can be of assistance.

Insofar as the Fund is concerned, a program to provide further technical assistance in the areas of tax reform, tax administration, and government financial management has been proposed for your consideration. Assistance on designing monetary policy instruments and banking sector reforms, as well as on training and organization of the BDL, is also available within certain staff constraints. Additionally, the Fund will be providing general macroeconomic policy advice and assistance in developing a suitably comprehensive policy package, together with assistance (if requested) in establishing targets and a monitoring framework in the context of the annual consultation discussions early in 1993.

On the Bank side, the establishment of a monitored macroeconomic framework, including prompt action to stabilize the economy through the correction of the current imbalances would permit mobilization of the external support needed for the reconstruction program, in the framework of a Consultative Group. To ensure a successful outcome of a Consultative Group meeting, a viable overall macroeconomic framework has to be in place and a realistic, balanced overall public investment program for reconstruction be presented. The Bank is also prepared to provide technical assistance and analytical support in a number of areas complementary to those of the Fund. These could be discussed with Mr. Ram Chopra, Director, IBRD, who will be arriving in Lebanon on December 14, 1992.

In sending this letter, Mr. Prime Minister, our intent has been to alert you to what we see as the most pressing issues in the economic policy area requiring your attention, and to assure you of the full support of our two institutions in addressing these issues. We look forward to working closely with your Government in the months ahead in the important task of restoring Lebanon to prosperity with financial stability.

Sincerely yours,



Paul Chabrier  
Director  
Middle Eastern Department



Caio Koch-Weser  
Vice President  
Middle East and North Africa Region

Attachment

His Excellency Rafik El-Hariri  
Prime Minister and Minister of Finance  
Prime Minister's Office  
Beirut, Lebanon

bcc: Messrs. Al-Sultan, Shamsedin, Hosny (EDS)

cc: Messrs. Husain (o/r), Squire (o/r) (MNAVP); Heron (o/r), Tyler (MN2DR);  
Hoppenbrouwer, Ozeki, Minhas, Courtney (MN2CO); File

December 10, 1992

LEBANON

Proposed Fiscal Measures

Revenue Measures

- (1) A thorough-going reform of the customs tariff in line with the recommendations of the IMF fiscal technical assistance missions (Aide Memoires dated March 31, 1992 and October 31, 1992), including the adoption of the market rate for the valuation of imports.
- (2) The consolidation of municipality, reconstruction, and specific import taxes, into the customs tariff; raising the minimum tariff rate to 5 percent, with municipality finances to be henceforth covered in the central government budget.
- (3) A substantial increase in petroleum taxes.
- (4) The raising of excise taxes on cement, alcoholic, and non-alcoholic beverages.
- (5) The enforcement of actual values of property in the calculation of registration fees.
- (6) The collection of property taxes on the basis of recently adjusted rental rates; and collection of income tax arrears on individuals and enterprises.
- (7) The application of a revaluation tax on fixed assets of private and corporate enterprises.
- (8) Increases in fees and stamp duties, particularly automobile registration fees.
- (9) Improved administration in the collection of personal and corporate income taxes, and the imposition of a business license tax.

Expenditure Measures

- (1) The elimination of subsidies on wheat and petroleum.
- (2) The full passthrough of petroleum price increases and other costs to electricity pricing (to eliminate subsidies), together with a determined effort to increase revenue collections and eliminate non-payment of bills.
- (3) A review of the employment rules to eliminate "ghost workers" and absentee workers.



THE WORLD BANK/IFC

ROUTING SLIP		DATE: 12/4/92
FROM THE REGIONAL VICE PRESIDENT		
NAME		ROOM NO.
Mr. Karaoşmanoglu		
APPROPRIATE DISPOSITION		NOTE AND RETURN
APPROVAL		NOTE AND SEND ON
COMMENT		PER OUR CONVERSATION
FOR ACTION		PER YOUR REQUEST
INFORMATION		PREPARE REPLY
INITIAL		RECOMMENDATION
NOTE AND FILE		SIGNATURE
REMARKS:  for your information  Caio Koch-Weser		
FROM:		

## OFFICE MEMORANDUM

Mr. Karamanoglu  
775.  
C/W  
K/S

DATE: November 25, 1992

TO: Distribution

Tariq Husain

FROM: Tariq Husain, MNAV

EXTENSION: 33907

SUBJECT: **LEBANON: Emergency Reconstruction and Rehabilitation Project**  
Minutes of Regional Loan Committee Meeting (RLC)

1. A Regional Loan Committee (RLC) meeting was held on November 23, 1992, to discuss the above project. The meeting was chaired by Mr. Koch-Weser and attended by Messrs./Mesdames: Wyss (CODDR); Morais and Abushakra (LEGMN); Kohli (EMTDR); Heron (MN2DR); McKechnie and Choucair (MN2IN); Bhargava (MN2IE); Voyadzis and Hoppenbrouwer (MN2CO); Bhattacharya (FRSCR); Mirza (CMECM); and Squire, Husain, Howarth, Bouhabib, van Eeghen, Yamine, Ijichi, Kafka (MNAV).
2. Introductory remarks by Mr. Koch-Weser and McKechnie established the meeting agenda and some project history. Mr. McKechnie explained that the project had taken longer to prepare than originally anticipated, as two missions had to be recalled. Mr. McKechnie also emphasized the extent of destruction of physical infrastructure and institutions.
3. Macroeconomic Framework. The meeting agreed that there should be no explicit link between this project and macroeconomic stabilization. Nevertheless, there was an issue as to whether Lebanon was creditworthy for any lending, including this project, and whether the project and overall reconstruction program were sustainable and implementable. An affirmative answer to these questions could only be made if, prior to Board presentation, there were a basic understanding on the major pillars of a stabilization program and some initial measures had been taken. A strong message to this effect should be given to the Government in the next weeks. Thus, a four step scenario could be envisaged: initial stabilization measures, approval of this project, approval of an IMF endorsed stabilization program (which would build confidence in Lebanon both domestically and internationally) and finally a Consultative Group meeting.
4. Project Scope. The meeting discussed the sectoral composition of the proposed project, the state of readiness of each component and whether there were any special sectoral issues requiring attention. The meeting agreed that the project should maintain all of the proposed components, because a broader based program provided for more flexibility to reallocate funds should there be nonperformance of any one component. There were two caveats to this decision. One related to the housing

component, discussed in (a) below. The other was the need, in accordance with existing guidelines for emergency operations, to include in the project components which could be committed within a maximum 12 to 18 months and disbursed within 36 months. The following conclusions were reached on each sectoral component:

(a) Housing: There was an extended discussion of this component. The meeting accepted that the component would not directly benefit the urban population and that subsidies to the final beneficiaries would be involved. With regard to intermediaries for channeling the funds, the project team explained its proposal to start with a few commercial banks, who were interested, financially viable, and had the appraisal capability. While the team welcomed the cautionary remarks of the IFC representative on IFC's past poor experience, in other countries, with commercial banks lending for housing, it felt that in the current Lebanese context, such lending could be viable. The project team further explained that while the housing bank was currently bankrupt, largely due to macroeconomic reasons, the Government and private sector had taken a decision to recapitalize it imminently, and the team wished to preserve the flexibility to bring in the housing bank, once it had been recapitalized and restructured. The meeting agreed in principle on the inclusion of a housing component with the project team's parameters, but decided that a final decision should be taken only upon review of the mission's findings.

(b) Water, waste water and solid waste components: The meeting agreed that these components appeared well prepared.

(c) Education: The project team briefed the meeting on the rationale for selecting only vocational and technical schools for the proposed project -- this permitted the Bank to avoid being drawn into endless discussion and negotiation (and possible political backlash) on which lower level schools in which ethnically dominated area it would support. This explanation was accepted by the meeting.

(d) Power: The meeting noted the importance for this sector of increasing tariffs, as well as billings and collection, inter alia, to minimize the drain of the sector on the central budget (25 percent of which currently went to the sector). It was agreed that while there should be no explicit conditionality, an understanding should be reached with the

Government on proposed action in this regard prior to submission of the project to the Board. Similar understandings should be sought if the same problem applied to any other sector we were financing.

5. Technical Assistance Component. The meeting queried whether the technical assistance activities for strengthening economic management and developing a framework for privatization belonged in an emergency project. It was agreed that this TA was important for a sustainable solution to the immense reconstruction needs and, hence, qualified as emergency needs meriting support under the project. The proposed technical assistance program, however, should be realistically sized and carefully reviewed for incorporation of Bank lessons on technical assistance.

6. Cost sharing. The Department explained that 100% financing of project costs was being proposed in the interests of rapid project implementation. However, the meeting agreed that there should be some local cost sharing, for project sustainability and government commitment. The mission could have flexibility in determining local cost sharing percentages, which could be on an increasing basis.

7. Implementation. The project team explained that project implementation arrangements provided for: (i) strong coordination through a central role for the Council for Development and Reconstruction (CDR) and the creation of the advisory Technical Coordination Committee (TCC); and (ii) strong sectoral inputs through the establishment in sector ministries of sector implementation units (SIU), which would not be islands but become integral parts of the ministries. Coordination between CDR and ministries had increased in recent months, and was expected to increase further under the new Government. The understanding among all parties, including CDR, was that in the longer term the CDR should be phased out. The meeting agreed with the arrangements, but noted that the MOP needed to demonstrate clearly how these would work.

8. Overall Size of the Three-Year National Emergency Reconstruction Program (NERP). The Department team explained that for political reasons, the Government wished to keep its \$2.4 billion estimation of the NERP, although the program was ambitious over three years. A realistic estimate was a \$2 billion program over four years. The meeting agreed that the Bank could not go to the donors at the Consultative Group (CG) meeting supporting an unrealistic program. It was pointed out that the Bank project was self-contained, and hence the mission should not be asked to establish the viability of the overall program. However, the Bank would need to get the necessary information on a parallel track as a basis for any forthcoming CG meeting.

9. Project Processing. The meeting agreed that the while the mission could pre-negotiate in the field, negotiations should take place in Washington according to

the current timetable in January, and that Board presentation should remain in February.

10. Concluding Statement: Mr. Koch-Weser summarized the key decisions as follows:

(a) While there should be no explicit link between the project and macroeconomic stabilization, a strong message should be given to the Government that we would expect before Board a basic understanding on the main pillars of stabilization and initial measures (para. 3).

(b) In principle, the project could maintain its broad sectoral scope, with two provisos: that all components should be committed within 12 to 18 months and disbursed within 36 months; and that a final decision on the housing component would be taken on the mission's return. While there should be no explicit conditionality, we should seek an understanding and action, before Board, on electricity tariffs, including billings and collection; the same should be pursued for any other sector facing similar issues (para. 4).

(c) The TA component should be retained but should take into account lessons of experience with TA (para 5).

(d) While explicit percentages should be decided by the mission, their should be some cost sharing on the part of the Government (para. 6).

(e) Proposed project implementation arrangements were acceptable (para. 7).

(f) While the proposed project was self standing, for purposes of the CG, the Bank needed to establish the overall NERP at a realistic size and timetable (para. 8).

(g) Negotiations should take place in Washington in January, with Board presentation as scheduled in February (para. 9).

Distribution:

Messrs./Mmes. Koch-Weser (MNAVP); Wyss (CODDR); Morais and Abushakra (LEGMN); Kohli (EMTDR); Chopra, Heron (MN2DR); McKechnie, Choucair (MN2IN); Bhargava (MN2IE); Voyadzis and Hoppenbrouwer (MN2CO); Bhattacharya (FRSCR); Mirza (CMECM); and Squire, Husain, Howarth, Murli, Bouhabib, van Eeghen, Yamine, Ijichi, Kafka (MNAVP); Chopra (MN1DR); Birdsall (CECDR); Nishimizu (FRSDR); Hovaguimian (CMEDR); Pouliquen (INUDR); El-Ashry (ENVDR); Pellegrini (EMTIN); Salop (OSPVP)



WDIAL  
.MN2CO  
OINFO

-----

-SUBJECT: LEBANON - NEW PRIME MINISTER  
 -DRAFTED BY: LHOPPENBROUWER/MR *Ch* EXT: 32716  
 -AUTHORIZED BY: CAIO KOCH-WESER, *Ch*  
 -CC: MESSRS. KARAOSMANOGLU (EXC); KOHLI (EMTDR); SQUIRE, HUSAIN,  
 -BOUHABIB, VAN EEGHEN (MNAV); CHOPRA, HERON, TYLER (MN2DR);  
 -VOYADZIS (MN2CO); OKONJO-IWEALA (MN2AG); BHARGAVA (MN2IE);  
 -MCKECHNIE, CHOUCAIR (MN2IN); KEARE (MN2PH); HOPPENBROUWER  
 (MN2CO); MENA  
 -FILE, CHRON  
 -BCC: MESSRS. AL SULTAN, SHAMSEDIN (EDS)  
 -DOCNAME: M:\LEB\HARIRI

-----

923 20900 -  
 -H. E. RAFIK HARIRI  
 -PRIME MINISTER  
 -OFFICE OF THE PRIME MINISTER  
 -BEIRUT, LEBANON

BT  
 WASHINGTON DC - October 27, 1992

I WOULD LIKE TO CONGRATULATE YOU ON YOUR RECENT APPOINTMENT AS PRIME MINISTER AND EXPRESS MY BEST WISHES TO YOU AND YOUR COLLEAGUES IN THE NEW CABINET. YOU WILL RECALL THAT WE HAD AN OPPORTUNITY TO EXCHANGE VIEWS ON THE BANK'S ACTIVITIES IN LEBANON ON THE OCCASION OF YOUR VISIT TO WASHINGTON D.C. SOME MONTHS AGO. I CAN ASSURE YOU THAT THE BANK CONTINUES TO STAND READY TO ASSIST LEBANON IN THE TASK OF RECONSTRUCTION THAT IT FACES AND MY COLLEAGUES AND I WILL BE LOOKING FORWARD TO WORKING CLOSELY WITH YOUR GOVERNMENT. OUR CURRENT PLANS ARE FOR A FINAL EVALUATION MISSION OF THE PROPOSED EMERGENCY RECOVERY PROJECT TO VISIT LEBANON IN THE COURSE OF DECEMBER OR JANUARY. WE ARE ALSO COMPLETING A DRAFT ECONOMIC REPORT WHICH WE HOPE TO PRESENT TO YOUR GOVERNMENT IN THE COURSE OF NEXT MONTH. THIS REPORT WOULD AMONG OTHERS DISCUSS THE NEED FOR STABILIZATION POLICIES TO ADDRESS THE FISCAL PROBLEM. AS I INDICATED IN MY LETTER OF JUNE 4, 1992 TO HIS EXCELLENCY RASHID SOLH, IN OUR ASSESSMENT, THE RE-ESTABLISHMENT OF AN APPROPRIATE MACRO-ECONOMIC FRAMEWORK WOULD BE REQUIRED IN ORDER TO ATTRACT THE FINANCIAL INFLOWS, BOTH PRIVATE AND OFFICIAL, INCLUDING WORLD BANK FINANCIAL SUPPORT, THAT WILL BE NEEDED TO MOUNT A PROGRAM OF RECONSTRUCTION, RECOVERY AND RAPID GROWTH. WE ARE CONFIDENT THAT WITH YOUR LEADERSHIP SUCH PROGRAM CAN BE SUCCESSFULLY UNDERTAKEN AND LOOK FORWARD TO SUPPORTING IT TO THE BEST OF OUR ABILITIES. WITH BEST PERSONAL REGARDS, CAIO KOCH-WESER, VICE PRESIDENT, MIDDLE EAST AND NORTH AFRICA REGION, WORLD BANK.

THE WORLD BANK/IFC

ROUTING SLIP

DATE:  
9/1/92

FROM THE REGIONAL VICE PRESIDENT

NAME

ROOM NO.

Mr. Karaosmanoglu

APPROPRIATE DISPOSITION

NOTE AND RETURN

APPROVAL

NOTE AND SEND ON

COMMENT

PER OUR CONVERSATION

FOR ACTION

PER YOUR REQUEST

INFORMATION

PREPARE REPLY

INITIAL

RECOMMENDATION

NOTE AND FILE

SIGNATURE

REMARKS:

for information

Caio Koch-Weser

FROM:



*Th Karasmanoglou*  
*FR*

*(CW)*  
*8/27*

A L L - I N - 1 N O T E

DATE: 24-Aug-1992 08:00pm

TO: Caio Koch-Weser ( CAIO KOCH-WESER )

FROM: Abdallah Bouhabib, MNAVP ( ABDALLAH BOUHABIB )

EXT.: 34784

SUBJECT: Lebanon: Algeria Revisited ??

Hussain Hussaini, the Speaker of the Parliament, the Godfather of the Taif Accords, the most influential of the Lebanese Troika has lost the election in the North Bikaa district of Baalbeck. The winners are Hizbollah, the pro-Iranian Moslem fundamentalists.

With only about 30% of the votes counted, Hizbollah was having a landslide. Only one out of three votes was going to Hussaini. The officials in charge of counting stopped the process and Hussaini asked that the elections be cancelled. The government is meeting tomorrow to discuss the situation.

The Baalbeck district is represented by 6 shiites, 1 sunni and 2 christians. It is a mostly shiite area. It is the base of Hizbollah since the Iranians were allowed to come to Lebanon following the Israeli invasion of Lebanon in 1982. The whole Hizbollah slate would win (it also includes a sunni and 2 christians), if the counting continues.

Now, Hizbollah threatened to revolt if the elections are cancelled. And if elections continue in the rest of Lebanon, it is kind of sure that Hizbollah will win in the south and in Beirut, where a large concentration of Shiites is living. It is Algeria revisited.

Of course, a major reason for the loss of the moderates Moslems is the absence of the Christian voters. By boycotting the elections, the Christians weakened the moderate Moslems like Hussaini. In Beirut, Sunni leaders such as Salim El-Hoss and Tamam Salam decided not to run for elections when the Christians decided to boycott the elections. But, the results indicate that the overwhelming shiite voters are supporting extremism.

The Christian boycott of the elections is not a major issue anymore. How to deal with Hizbollah and the rest of the election rounds is the one major issue. Another issue relates to Syrian withdrawal from Lebanon. With such a situation, the pressure on Syria to implement the Taif Accords may vanish. Who would want the Syrians to leave Lebanon now?

There is a lot of talk about a military coup. This can only succeed if the Syrians support it. Even then, the military would have to deal with Hizbollah. A military coup may be supported by the Sunnis, Christians, Druze and the moderate and weak traditional Shiite leadership, but not the Shiite community and the militant Hizbollah.

CC: Ram K. Chopra	( RAM K. CHOPRA )
CC: Spiros Voyadzis	( SPIROS VOYADZIS )
CC: Laurens Hoppenbrouwer	( LAURENS HOPPENBROUWER )
CC: Tariq Husain	( TARIQ HUSAIN )
CC: Lyn Squire	( LYN SQUIRE )
CC: Harinder Kohli	( HARINDER KOHLI )

<b>ROUTING SLIP</b>		Date July 9, 1992	
NAME		ROOM NO.	
Mr. Attila Karasmanoglu			
<b>URGENT</b>	For Action/Comment	Per Your Request	
Appropriate Disposition <input checked="" type="checkbox"/>	Information/Discard	Returned	
Approval/Clearance	Note And Return	See My E-Mail	
File	Per Our Conversation	Signature/Initial	
RE: IMF Mission to Lebanon			
REMARKS			
<p>Attila:</p> <p>As we discussed, I was somewhat unhappy that the Fund is sending a mission now, before the Government has demonstrated its commitment and ability to implement an emergency stabilization program.</p> <p style="text-align: center;"><i>ckw</i></p>			
From Caio Koch-Weser	Room No. H7-065	Ext. 35350/51	



# Office Memorandum

To: The Temporary Acting Managing Director

July 7, 1992

From: A. S. Shaalan *AS*

Subject: Staff Visit to Lebanon

At the request of Lebanon's Minister of Economy, I visited Lebanon for three days (June 24-27, 1992), where I had extensive discussions with a number of officials, including the President, the Prime Minister, the President of Parliament, the Ministers of Finance, Economy, Public Works and Transportation, Health, Electricity, and Industry, the Governor of the Central Bank, and parliamentary members of the Budget Committee. The security situation appeared to be satisfactory.

The discussions centered around the needed policy reforms, particularly in the area of budgetary policy, as an important input to a donors meeting tentatively scheduled toward the end of 1992. Following are the highlights of the meetings.

*may be* The most striking observation was the virtual unanimity at all levels of the Government that the sizable budgetary deficits and the manner they had been financed (by the Central Bank) were the main driving force behind the precipitous depreciation of the exchange rate and associated inflationary pressures. The Lebanese pound in the past four months had lost about half its value against the U.S. dollar. The authorities appeared to be determined to introduce legislation, possibly before the parliamentary elections (the first in 20 years) tentatively scheduled for the fall of 1992. No specific date has yet been set. It is to be noted that the Syrian forces stationed in Lebanon are to commence deployment in accordance with the terms of the Taif Agreement of 1990 on September 30, 1992.

The budgetary measures envisioned appear to be far reaching, viz; an immediate move to levy customs duties at a rate of LL 800-1,000 to the U.S. dollar from the present LL 200 per U.S. dollar, a sharp increase in the car license tax, a turnover tax, and collection of fines on real estate law infringements. On the expenditure side, cuts (still unspecified) in unproductive expenditures are planned. The authorities expect that whereas for the first half of the current year the budget deficit amounted to about 65 percent of total government expenditures, for the full year the ratio is targeted to fall between 25-30 percent. This would imply a small surplus in the second half of the year. If successful, this would represent a significant improvement.

- 2 -

With regard to financing the deficit, a tight ceiling is to be imposed on the Government's resort to the Central Bank. Additional financing will be made from nonbank sources at freely determined interest rates. Privatization, particularly of telecommunications and electricity, is being considered with the proceeds earmarked for reducing the stock of government debt.

The authorities pressed very hard for Fund support with certain donors (particularly Saudi Arabia) for establishing a stabilization fund. They feel very strongly that the success of the program will depend on their ability to stabilize the exchange rate. They are clearly cognizant of the fact that the sudden sharp depreciation of the pound in May 1992 which evoked a mass uprising, brought about the fall of the Karani Government in early May. It is reported that this was the first serious public reaction to the deteriorating economic situation. While sympathizing with the Lebanese authorities, I made it clear to them that at best, the creation of a stabilization fund was premature at this time. First, policy measures--credible both domestically and internationally--had to be implemented. I pointed out that the Central Bank, which had supported the Lebanese pound for two months earlier this year, not only lost about 45 percent of its foreign exchange reserves but also this action was not successful in stabilizing the Lebanese pound. Since mid-February the Central Bank had terminated its intervention and has no intention of any resumption.

The authorities were reportedly being pressed by some donors to sell some of the Central Bank gold holdings (valued at about \$3.5 billion) for reconstruction expenditures. I advised the authorities that any action to sell the gold at this time could have serious psychological and economic consequences. Consideration could be given to that once the reforms are firmly in place.

The banking sector in Lebanon is weak. A number of small banks were either insolvent or illiquid. Banking supervision has been weak. The authorities have taken action to liquidate a number of banks and have taken measures to strengthen bank auditing and supervision. On the capital adequacy of Lebanese banks, the authorities have prepared draft legislation which we shall be reviewing for them.

The authorities have asked for a Fund mission to resume the aborted discussions of last May on account of security considerations. A mission will shortly be leaving for Lebanon. The authorities have also asked for technical assistance in the budget area as well as the banking area. We shall be discussing this with the relevant departments. While in Lebanon I met with the UNDP representative, Mr. van der Kloet, who advised me that ample financial resources were available for this purpose. We shall be coordinating with the UNDP.

- 3 -

My personal assessment is that the political and economic problems in Lebanon are daunting. While the Government's intentions are laudable, implementation for political and technical reasons is not going to be easy. Nevertheless, I feel we have to work closely with the Lebanese authorities and provide them with the needed technical assistance.

cc: The Managing Director (o/r)  
The Deputy Managing Director (o/r)  
Heads of Departments:  
AFR, CTA, EURI, EURII, FAD,  
MAE, PDR, SEA, STA, WHD  
Mr. Andrews

- 4 -

bcc: Mr. Chabrier (o/r)  
Mr. Hitti  
Mr. Mookerjee  
DVC

**The World Bank**

Washington, D.C. 20433  
U.S.A.

CAIO K. KOCH-WESER  
Vice President  
Middle East & North Africa Region

June 4, 1992

H.E. Mr. Rashid Sohl  
Office of the Prime Minister  
El-Sanaii  
Beirut, Lebanon

Your Excellency,

I should like to congratulate you on your appointment as President of the Council of Ministers and extend our best wishes to your new Government. We are looking forward to working closely with your Government, particularly with respect to the reconstruction program. I would like to take this opportunity to inform you about some of our recent activities and our current plans. We recently had an opportunity to discuss these informally with your Minister of Economy and Trade, Dr. Samir Makdissi.

As you know, a number of Bank missions visited Lebanon during April and early May, but unfortunately their stay had to be interrupted because of the events that took place in Beirut during the second week of May. Nevertheless, the economic mission was able to substantially complete its work and present its findings to the previous Government. I enclose a copy of the mission's aide-memoire which was presented to His Excellency Dr. Harawi and to the then Minister of Finance.

I should like to endorse the mission's suggestion that early action be taken to resolve the fiscal problem that underlies the exchange rate depreciation and rapid inflation that have taken place this year. The re-establishment of an appropriate macro-economic framework is undoubtedly a precondition for attracting the financial inflows, both private and other, that are needed to mount a program of reconstruction, recovery and rapid growth. Lebanon's private sector clearly possesses the human talents and resources to lead such recovery process, but it will be Government's responsibility to create an appropriate enabling environment.

We realize that the bold actions that will be required to raise fiscal revenues and control public expenditures are difficult, and will affect the poor even if they are designed with equity in mind. The aide-memoire therefore suggests that it would be important for Government to design and establish a social safety net to mitigate the impact of the necessary measures.

As regards the Bank's support for the reconstruction program, I should like to assure you that, despite the interruption of the mission's work, my staff stands ready to review the damage assessment studies and the



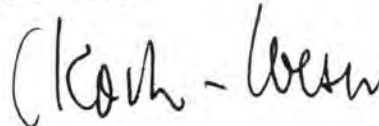
updated first phase reconstruction program to be prepared by CRD consultants. In a recent communication to CDR, my staff has proposed a plan of actions that would seek to recover the time lost in the preparation of the project because of the delays in the completion of the damage assessment studies and the need to withdraw our project identification mission from Beirut. The communication also requests CDR to prepare project implementation plans and management contracts for the operation and maintenance of the assets that are to be rehabilitated.

With respect to the convening by the Bank of a Consultative Group meeting, I should like to confirm that we would stand ready to assist the Government in mobilizing donor support for Lebanon's reconstruction and development at the most appropriate time. As I indicated in my communication to His Excellency Dr. Harawi, we believe that it is advisable to delay a Consultative Group meeting to sometime in the Fall. The exact timing of such meeting would depend in part on: (i) the status of implementation of a credible economic reform program to address the economic situation; (ii) advances in the preparation of the reconstruction program; and (iii) donor indications of support for such program. We would also need to take into account the documentation requirements for a Consultative Group meeting which need to be in place about one month in advance of the meeting. These would include an economic note with a favorable assessment of the economic program and outlook, as well as a document on the reconstruction program, both to be agreed between the Government and the Bank. Finally, in our view the meeting should also provide an opportunity for the Government to explain to donors how it is addressing the problems affecting Lebanon's economic development and to present a realistic first phase overall reconstruction program, including program priorities, institutional arrangements, domestic contributions, and the role of the private sector.

I should like to assure your Excellency of our desire to assist your country to the best of our abilities in the difficult task of reconstruction that it faces.

In view of their interest in these matters, I am sending copy of this letter and the attached aide-memoire to Their Excellencies Dr. Assad Diab, Minister of Finance, and Dr. Michel El-Khoury, Governor of the Banque du Liban.

Sincerely yours,



cc: Mr. Fawzi Al-Sultan  
Executive Director

Mr. Ezzedin Shamsedin  
Advisor, Executive Director's Office

cc: H.E. Dr. Assad Diab  
Minister of Finance  
El-Sanai  
Beirut, Lebanon

H.E. Dr. Michel El-Khoury  
Governor  
Banque du Liban  
Beirut, Lebanon

cc: Messrs. Karaosmanoglu (EXC); Kohli (EMTDR); Squire, Husain, Bouhabib, Van Eeghen (MNAVP); Chopra (MN2DR); Wijnand (CODOP); Voyadzis (o/r) (MN2CO); Okonjo-Iweala (MN2AG); Bhargava (MN2IE); McKechnie, Choucair (MN2IN); Keare (MN2PH); Hoppenbrouwer, Giugale (MN2CO); MENA File, Chron

m:\leb\pm  
LH/mr

DECLASSIFIED

MAR 31 2017

WBG ARCHIVES

Annex

CONFIDENTIAL

WORLD BANK ECONOMIC MISSION-- AIDE-MEMOIRE

INTRODUCTION.

1. A World Bank economic mission has visited Lebanon for two weeks to collect information for the preparation of an Economic Note to be presented to a possible Consultative Group (CG) Meeting for Lebanon and for a Country Economic Memorandum (CEM) to be presented to the Bank's Board of Executive Directors in advance of their consideration of a possible Bank loan to support the Government's Emergency Reconstruction Program. The mission comprised Laurens Hoppenbrouwer (Principal Country Officer, Mission Leader), Marcelo Giugale (Country Economist and Task Manager for the Economic Note and CEM), Willem van Eeghen (Economist in the Office of the Vice-President for the Middle East and North Africa Region), Raed Safadi (Economist in the International Trade Division), Cristian de Clercq (UNDP/UNARDOL), and Issam Montasser (Consultant). The mission was joined by Mr Spiros Voyadzis (Chief Middle East Division) for discussions of the mission's findings and the aide-memoire as well as other aspects of Bank operations with the authorities. Also, a Bank Emergency Reconstruction Project Identification Mission has begun work in Lebanon and will present its findings to Government upon its completion. The findings of that mission would also be incorporated in the documentation for the CG meeting and the CEM. Similarly, the Bank's reports would reflect the findings of the IMF mission currently in Lebanon to discuss financial policies.

2. The economic mission should like to express its appreciation for the cooperation provided by the authorities. This enabled the mission to advance significantly in its work in spite of the paucity of data. The mission's findings and suggestions presented in this aide-memoire do not reflect the full scope of the mission's work. Rather, the mission felt it important to focus on key issues confronting the authorities at this moment. This explains why the focus of this aide-memoire has been on issues of short-term stabilization rather than medium to longer term reconstruction and development; the CG Economic Note and the CEM would review medium term aspects of Lebanon's economic development and present, to the extent possible, alternative scenarios. The findings and suggestions presented below reflect the mission's views and are subject to review and confirmation by Bank management at Headquarters. The mission's report to be presented to management would of course reflect the authorities' reaction to this aide-memoire and the drafts of the Economic Note and CEM to be prepared by the mission would be discussed with the authorities prior to circulation.

PROSPECTS AND IMPACT OF ADJUSTMENT ON THE POOR.

3. The Lebanese economy currently faces a stability crisis. This aide-memoire reviews the origins of this crisis and suggests a possible response to overcome it as soon as possible. The mission believes that a resolution of the fiscal problem that underlies the current environment of high inflation and exchange rate depreciation would provide the basis for a rapid recovery of the Lebanese economy. Lebanon undoubtedly could thrive again as a major

growth center in the Middle East. Its dynamic private sector clearly possesses the human talents and resources to lead the post-war recovery and development effort. However, it is unlikely that the financial inflows needed to mount a program of reconstruction, recovery and rapid growth can be attracted without an appropriate macro-economic framework. Thus, in the short run, the Government's priority should be to address the problem of the fiscal deficit, through bold actions to raise revenues and control expenditures, in order to arrest the current slide. This would create an environment in which Lebanon's large development potential could be realized.

4. The actions that are required to overcome the current crisis are not without cost; experience elsewhere suggests that postponing them only makes the correction more difficult and increases such cost. The poorest segments of the population bear the brunt of the current inflationary process in a relatively heavier proportion. At the same time, some of the actions required, particularly as regards fiscal revenues, even if designed with equity considerations in mind, as the mission has attempted to do, will affect the poor as well. The mission, therefore, believes that the Government should take specific measures to mitigate the impact of the measures on the poor. However, rather than applying subsidies generally for all consumers, through, e.g. duty exemptions or pricing below cost, the mission believes that the Government should, within the limits of required fiscal restraint and administrative capacity, consider targetted subsidies and income supplements for the neediest, including, for example, food stamps and kerosene coupons. If the Government would so wish, the mission would recommend that the Bank assist Government in the design of such programs.

#### DEVELOPMENTS IN 1991.

5. Output. Although the beginnings of the current economic crisis can be dated to late 1991 (para. 8 below), developments in 1991 were relatively favourable. Following a significant decline during 1989-90, the Gross Domestic Product (GDP) recovered sharply during 1991. Based on very partial and preliminary output indicators, the mission estimates that real GDP may have increased by around 40% during 1991, with rapid growth in construction and manufacturing. Domestic price developments, as measured by the Consumer Price Index (CPI) 1/ , which increased by 52% on average, and the evolution of the exchange rate (from an average of LL 701 per US\$ in 1990 to 928 in 1991), suggest that the domestic price level rose by 15% in US\$ terms during 1991. On this basis, GDP in current US\$ terms is estimated at above US\$ 4.0 billion in 1991. 2/

Balance of Payments. The recovery of the economy and the further real appreciation of the Lebanese Pound during 1991 resulted in a sharp surge in imports from about US\$ 2.4 billion in 1990 to US\$ 3.7 billion in 1991 3/.

1/ In the absence of official price statistics the mission has used the CPI series as elaborated by the Consultant Research Institute (Beirut)

2/ In the absence of national accounts statistics the mission has used national account estimates for 1990 by UNDP (DTCD) as the basis for its estimate for 1991.

3/ In the absence of Customs or BdL trade and payments data, estimates of imports and exports have been derived from the IMF's Direction of Trade, BdL data on letters of credit and export data from the BCCI.

While exports also expanded rapidly (possibly nearly doubling from the estimated level of US\$ 510 million in 1990), the merchandise trade deficit further widened significantly by close to about US\$ 1.0 billion to an estimated US\$ 2.7-2.8 billion. The current account deficit, while smaller than the trade deficit because of net interest earnings and the inflow of private transfers (incl. remittances), remained at a significantly high level. Nevertheless, the Central Bank's (BdL) international reserves position improved sharply, with an increase in non-gold reserves of about US\$ 600 million during the year, because of a large inflow of private capital attracted by high domestic interest rates, combined with exchange rate stability, and reflecting increased confidence.

6. Fiscal. Compared to previous years, substantial improvements were made in Lebanon's fiscal performance during 1991. Government revenues increased sharply, from a low base in 1990, as the Government regained part of the authority it had lost during the years of war in enforcing tax collection. Total tax revenues increased more than five-fold from LL 55 billion in 1990 (3.1% of GDP) to LL 301 billion in 1991 (7.7% of GDP). Over half of this increase was on account of better collection of indirect taxes with import duties being the biggest contributor. At the same time total Government expenditures declined marginally as a percent of the estimated GDP (see Table 1) and, consequently, the overall consolidated Government deficit, including CDR transactions, as measured by data on financing, declined from 34% of GDP in 1990 to 29% in 1991. Only about 8% of the overall deficit of LL 1,132 (US\$ 1.2) billion 4/ was externally financed. At the same time, during 1991 the Government switched from primarily Central Bank (BdL) financing of the deficit to Treasury bill sales (para. 7 below).

7. The 1991 Stabilization Policy. In order to rapidly achieve price stabilization, and recognizing the high degree of openness of the Lebanese economy, including an absence of restrictions on capital transactions, the authorities decided to adopt the LL/US\$ exchange rate as the system's nominal anchor. Consequently, as from the beginning of the second quarter of 1991, BdL intervened in the foreign exchange market, in effect pegging the exchange rate to a slightly-appreciating path. To back this policy, a tighter monetary stance was adopted. In the absence of sufficient fiscal adjustment, that stance took the form of a switch from money (i.e. BdL) to debt (i.e., Treasury bills) as the dominant instrument for fiscal deficit financing. The stability (and subsequent appreciation) of the nominal exchange rate, as well as the authorities' perceived commitment to defend that stability, encouraged foreign investors and domestic savers to buy increasing amounts of the local currency-denominated Treasury bills, with a large proportion being accounted for by foreign inflows. The amount of outstanding Treasury bills soared from LL 1,023 billion at the end of 1990 to LL 2,333 billion, --equivalent to US\$ 1.4 billion at the present exchange rate--, at its peak in December 1991 and, as noted above, foreign exchange reserves increased rapidly, thus further fostering confidence in BdL's ability to maintain the policy.

4/ This estimate is based on information provided by: (i) the Ministry of Finance on budgetary and extra-budgetary transactions (incl. Treasury advances), (ii) CDR as regards its capital expenditures and external financing, and (iii) BdL as regards domestic financing.

## THE ECONOMIC CRISIS.

8. As noted in last year's Bank note on the economy, and in the mission's view, while the results achieved were encouraging, the price and exchange rate stabilization policy was not sustainable beyond the short term without a major fiscal adjustment as the costs of servicing the rapidly rising domestic debt were bound to aggravate the fiscal disequilibrium. The Government's decision in December of 1991 to grant a large and retroactive salary increase to the public sector, changed investors' perception of the authorities' ability to maintain the policy adopted in early 1991. The situation may have been exacerbated by alleged problems in the banking system which surfaced around the same time. Investors moved out of Treasury bills into foreign currency denominated instruments, in Lebanon and abroad, with the stock of outstanding Treasury bills declining by LL 288 billion during the first two months of 1992. The injection of liquidity as a result of the payment of the appr. 150% salary increase led to the expectation of a depreciation of the value of the Lebanese Pound, triggering a sharp loss of reserves (about US\$ 600 million), which led to the inability of the BdL to defend the exchange rate. Following the abandonment of the stabilization policy in late February of 1992, which was unavoidable in view of the sharp drop in reserves and absence of fiscal discipline, the Lebanese Pound rapidly depreciated from LL 878 per US\$ to about LL 1,200 within a matter of two weeks. The continued monetary financing of the fiscal deficit 5/ since then, combined with the absence of actions to quickly restore fiscal discipline, has led to a continuous further depreciation (to about LL 1,700 last week) and an acceleration of inflation to an annualized rate of about 500% during the first quarter (and 3,700% during the month of March). Because of these developments the real value of the stock of domestic debt has been sharply reduced. At the same time, the acceleration of inflation has particularly affected the poorest segments of the population. The graphs presented in the Annex illustrate the above events by tracking the evolution of selected monetary and price indicators during the period comprising the beginning and the end of the 1991 program.

## THE RESPONSE TO THE CRISIS.

9. The Committee of Experts. The mission has been informed that against the background of the developments discussed above, the Government has decided to adopt, and has announced, a plan along the lines of the recommendations of a Committee of Experts that seeks to address the problem underlying current developments, namely the fiscal deficit, by: (i) increasing revenue from a budget target of LL 867.5 billion to LL 1,100 billion; (ii) limiting total public sector spending to no more than LL 1,700 billion; (iii) limiting the total public sector deficit to no more than 35% of total public expenditures; and (iv) limiting financing from the Central Bank to no more than 10% of public expenditures. The mission has not been able to obtain details of the proposals, such as sources of revenue and expenditure categories within the above totals. It is also not clear to the mission to

5/ Preliminary data indicate that during the first quarter of 1992, the Central Bank financed all of the Government deficit (about LL 245 billion) as well as the repayment of Treasury bills. In all Central Bank credit to the Government increased by LL 437 billion, or 55 % of the end-1991 money base.

what extent the proposed expenditure limit includes non-budgetary expenditures (e.g Treasury advances and CDR expenditures).

10. The mission's assessment. The mission considers the announcement of the above plan an important first step towards control of the fiscal deficit. Obviously, fiscal discipline is the only available option to bring inflation under control, change expectations and arrest the slide in the value of the Lebanese Pound and thus restore economic stability. Such stability would be one of the preconditions for regaining private sector confidence and, hence, for economic reconstruction and sustained development. The option that was available in previous years, i.e. the financing of an increasing fiscal deficit through private subscriptions of Treasury bills has all but disappeared and in the mission's view the authorities degrees of freedom in designing economic policy have become very limited. The high degree of dollarization of the economy and the open capital account exacerbate the effects of a fiscal deficit that is not financed by domestic or external savings. Continued money creation would lead to accelerating levels of inflation, and a further depreciation of the value of the Lebanese Pound and/or a loss of reserves, while domestic debt financing would require increasingly high interest rates, with a vicious circle of ever higher interest payments feeding the deficit and a further depression of private investment. In both cases, confidence in the Lebanese economy will be undermined, private capital inflows are unlikely to materialize and increasingly scarce domestic savings will be used to finance Government's current operations. In the mission's view, the current situation calls for immediate and drastic measures to bring the fiscal deficit under control, going well beyond the current plan.

#### FISCAL STABILIZATION.

11. Overall targets. The mission is of the opinion that domestic financing of the public sector deficit (incl. Government, CDR and enterprises), i.e. that part of the deficit not covered by net external financing, including extra-ordinary grants from countries in the region, should not be set as a share of total expenditures. It should rather be set at a nominal amount that, given other developments in the economy, is designed to bring inflation sharply down to a moderate level. This can be achieved through a sharp reduction of the overall fiscal deficit through revenue and expenditure measures. The IMF mission currently visiting Lebanon has indicated that it will help the authorities in developing a monetary program for 1992, including a ceiling on domestic financing of the public sector deficit. Preliminary estimates of the Bank's mission suggest that total domestic financing would need to be kept at levels that are well below those implied in the Committee of Experts' proposals. The mission also notes that the Bank and most other sources of external financing for the reconstruction program would normally require a domestic contribution to the financing of their projects. This matter will be further discussed by the Emergency Project Mission. In any event, this would imply that, as a minimum, Government current expenditures should be covered by current revenues. (During 1991, less than 40% of current revenues were covered by current revenues, excl. grants, and the 1992 budget envisaged a coverage of 56%).

12. Government revenues. The achievement of the above targets will require the undertaking of bold actions, both as regards revenues and



expenditures. The restoration of confidence would require that such targets and actions be announced and taken quickly. As regards revenues, the mission endorses the recommendations made by the recent IMF Fiscal Affairs mission. The Bank mission is aware that a number of revenue measures cannot be considered in Lebanon in the short run because of the need to strengthen public administration in general, and tax administration in particular, and to undertake a comprehensive tax reform. The mission agrees with the suggestion of the IMF mission that selected high yielding and equitable revenue measures can be taken relatively quickly. A number of these are presented below :

(i) Customs duties. The current tariff schedule contains 31 ad-valorem rates ranging from 0% (for as much as 25% of all tariff positions) to 75%. About three quarters of all tariff positions have rates of 18% or less; the (unweighted) average rate is 25%. However, because of the valuation of the customs dollar at levels well below that of the market exchange rate (at LL200, or just over 10% of the current market rate, for all goods, except cars and alcohol, and less than 50% for the latter), the effective duty rates, excluding surcharges and specific duties, are very low, i.e. only about 2% of the value of imports for three quarters of all tariff positions. Effective rates for cars range from about 3 to 42% 6/. Import duty surcharges, which include a 3.5% tax earmarked for municipalities and a 1% tax for reconstruction, similarly have low effective values, while the value of specific duties has not been adjusted and has been eroded by inflation. The mission agrees with the suggestion of the IMF mission that all (private and public) imports should be valued at the market exchange rate (in one single adjustment) and that simultaneously the average nominal duty rate (including all surcharges) be reduced to a narrow range of 5 to 30%, or, as an alternative option, to a flat across-the-board rate of 10% plus a (temporary) 5% points "reconstruction" surcharge, without exemptions, except those required because of international conventions that are in force. The clear advantage of a low flat rate would be that it would help discourage evasion and illegal imports. The reduction in the level of nominal tariffs and in tariff dispersion would : (i) mitigate to some extent the impact of the valuation at the market exchange rate; (ii) facilitate collection, simplify administration and reduce the scope for "rent-seeking" behavior; and (iii) help establish a trade regime that is conducive to the development of exports and efficient import substitution. The mission recognizes that special arrangements may need to be made for formal transit trade and suggests that the Government consider the establishment of temporary admission or duty drawback schemes for imported inputs for exporters. The mission also suggests that items such as cars, luxury goods, alcohol and tobacco products should be subject to additional taxes outside the import duty regime. Finally, as a rough indication of the possible yield of the suggestion regarding import duties, the mission notes that at the 1991 import level of \$ 3.7 billion, current exchange rate, and exemptions or leakage of one-third, total collections would amount to about LL'630 billion. The Government might consider the use of pre-shipment inspection (PSI) companies to adequately assess the value of imports. Eventually, the same PSI could be used to enforce customs duties collection through the banking system.

6/ Estimate based on current market rate of LL 1,700, customs dollar for cars of LL 800, and nominal duties ranging from 7 to 90%.

(ii) Property and real estate taxes. With relatively simple methods the basis for property taxes and for taxes on real estate transactions could be revalued and assessed, and rental values of properties increased. The establishment of standard values, differentiated by zones would appear appropriate. IMF estimates suggest possible yields in a range of LL 100 to LL 300 billion for transaction taxes alone. Additionally, measures such as penalties for illegal construction, as considered by the Government, building permit fees and adjusting the value of the cement excise tax could contribute to Government revenues particularly since construction activity is likely to sharply expand.

(iii) Petroleum taxation. Domestic prices of petroleum products are among the lowest in the world for countries depending on oil imports for all or most of consumption. Current taxes on petroleum range from 4 to 18%, with a weighted average of about 11%. The mission suggests that they could be significantly increased, without exemptions for the Electricite de Liban (EdL) or the refinery. At 1991 levels of consumption for all products (about 22 million barrels) a 30% average tax on petroleum products (in addition to the proposed import duty) would yield about LL 300 billion.<sup>7/</sup> Within the average, a differentiation in rates, as in the current system, would be justified on equity grounds with the highest rates on gasoline and the lowest on kerosene. Such tax level is still low by international standards. With taxes on gasoline significantly above the suggested average, gasoline prices would still be lower than in neighbouring countries.

(iv) Luxury and "sin" taxes. As indicated above, it is suggested that taxes other than import duties should be applied on cars, luxury goods, alcohol and tobacco products both for fiscal, and for equity and health purposes. The mission notes that the Government has recently increased annual fees for cars but a whole range of other taxes can be considered, including taxes on services (e.g. taxes on hotel rooms and meals in higher category establishments). Excise taxes, if established at specific values, should be regularly adjusted to compensate for inflation and devaluation.

(v) Administrative measures. In 1991 income and profit tax collections amounted to only just over 1% of GDP; out of 65,000 commercial establishments registered in Beirut, only about 20,000 submit income tax statements. Out of these 20,000, 70 percent declare losses. In sum, less than 10% of all (registered) commercial establishments effectively paid income tax. Clearly, with relatively simple administrative measures quick improvements could be achieved in these areas, including e.g. the creation of a special unit to administer 200 largest taxpayers and provide incentives to best performing tax collectors.

(vi) Central Bank profits. During 1991 the contribution of BdL profits to Government revenues increased significantly to about LL 134 billion, accounting for 29% of total revenues, which was about 50% more than direct tax collection. With the decline in non-gold reserves the US\$ value of income earned on foreign reserves is likely to be reduced significantly in 1992. The mission notes that the reported 9.2 million troy ounces of gold

<sup>7/</sup> This estimate assumes an average international price of \$20 per barrel for crude and \$25 per barrel for imported products and a 15% import duty.

reserves (about \$ 3.0 billion) do not yield any returns; at current international dollar interest rates of 4 to 8 % for short and long term instruments respectively, income forgone amounts to about LL 200 to 400 billion at the current exchange rates. The mission is aware that these gold reserves do may have a special symbolic and psychological value in the Lebanese context. They may also be important for creditors' confidence and comfort, although less than generally believed since current legal provisions do not allow these assets to be sold or pledged. Finally, the mission notes that donors may well query the role of these reserves in the Government's external financing strategy, particularly in the context of the reconstruction program.

14. Government expenditures. Available information does not enable the mission to analyze in significant detail Government expenditures. The mission should like to highlight a selected number of issues.

(i) The public sector wage bill. The large increases in public sector salaries and the sharp rise in outstanding domestic debt during 1991 have contributed to a significant increase in Government outlays. In the mission's view drastic revenue measures will need to be accompanied by strict expenditure controls if the suggested deficit targets are to be achieved. It would thus be important to attempt to maintain the wage bill at current nominal levels in spite of pressures to increase civil service salaries that are likely to mount in the wake of high inflation levels so far this year. As regards the level of public sector employment, the mission notes that while there is a severe shortage of qualified staff, there also appears to be significant overstaffing in certain fields and institutions (e.g. teachers, railways). The total number of employees on the Government's payroll, including regular staff, contract and temporary staff, public enterprises staff financed by the Government, military and security personnel, teachers and nurses amounts to about 130,000. The mission understands that many work short hours, or not at all, and that some may not live in Lebanon or have deceased. It is suggested that the Government should critically assess the current situation as soon as possible. As regards the staff employed in non-productive areas, the mission, while recognizing that it does not have a basis to assess Lebanon's defense and security needs in the context of the country's recent history and regional issues, nor the authority to discuss the issues of military expenditures, notes that available estimates indicate that such expenditures exceed the level of public expenditures devoted to education and health.

(ii) The Electricite du Liban (EdL). Available information indicates that the operations of the EdL contribute significantly to the Government's deficit. Tentative estimates suggest that at the current exchange rate, without improvement in collections and increases in power tariffs, EdL would require Government transfers in an amount roughly equivalent to about a quarter of the Government's target expenditure level of LL 1,700 billion for 1992. According to EdL, current tariffs cover only about one-third of the cost of electricity. Tariffs were set at an average of LL 45 per kWh in early 1991 and their real value has since been sharply eroded. The cost of private generation is a multiple of EdL's tariffs. Hence, the mission suggests that the Government consider a significant adjustment in power tariffs with a specific program to reach levels of long term marginal cost within a specified, relatively short, time frame. Other charges (e.g. connection fees)

may have to be considered also to help financing the large needs for rehabilitation and expansion. The impact on lower income consumers could be mitigated through the introduction of cross subsidies (with low tariffs for an initial low level of consumption) and through a differentiation of tariffs between zones. As regards collection, consideration could possibly be given to contracting private services for bill collection with strict policies regarding the cut-off of supplies. Apart from the electricity sector, the issues of cost recovery should also be addressed in other sectors, including e.g. telecommunications and water supply. Similarly the privatization of public services could also be considered in other areas, e.g. garbage collection. The issues of cost recovery and privatization will also be explored by the Bank's Emergency Project Mission.

15. Divestment and Privatization. In view of the current fiscal situation and the large amount of resources that will be required to undertake the reconstruction and development program, the mission believes that the Government should carefully consider all possibilities for divestment and privatization, including the sale of public lands and public enterprises (e.g. electricity, telecommunications, oil refining, ports and railways), the privatization of services, and the undertaking by the private sector of reconstruction and expansion investments in the abovementioned sectors as well other areas (e.g. toll roads). This would however require a careful assessment of the issues involved and the establishment of an appropriate legal and regulatory framework.

#### EXTERNAL DEBT.

16. Information provided to the mission by the Ministry of Finance, CDR, and EdL indicates that the total level of medium and long term external public debt amounted to US\$ 360 million at the end of 1991, including US\$ 139 million in principal arrears (of which US\$ 61 million in non-military debt arrears) and US\$ 44 million in interest interest arrears. At less than 10% of GDP, Lebanon's external public debt remains low. The mission notes, however, that arrears amount to over a quarter of the end-March BdL non-gold foreign reserves level. The mission should like to seek confirmation from the authorities that these amounts represent all of Lebanon's public and publicly guaranteed external debt and would hope that information on any other public debt, owed by public enterprises or entities and BdL, can be provided as soon as convenient so that the Bank's Board of Executive Directors may be informed prior to the consideration of possible loans to Lebanon in accordance with standard practice. The mission would also appreciate receiving an indication regarding current plans for the settlement of the outstanding arrears, including its financing within the limits of the Government's financial program, particularly since this issue is likely to affect Lebanon's ability to attract the external financing required for the reconstruction program.

#### THE CONSULTATIVE GROUP AND WORLD BANK ASSISTANCE.

17. The mission reiterates the World Bank's readiness to contact donors with a view to organizing a Consultative Group Meeting at the most appropriate time to help the Government mobilize the needed financial resources in support of its economic adjustment and reconstruction efforts. Such a meeting would provide the Government with an opportunity to explain to donors how it is addressing the problems affecting the country's economic development and to

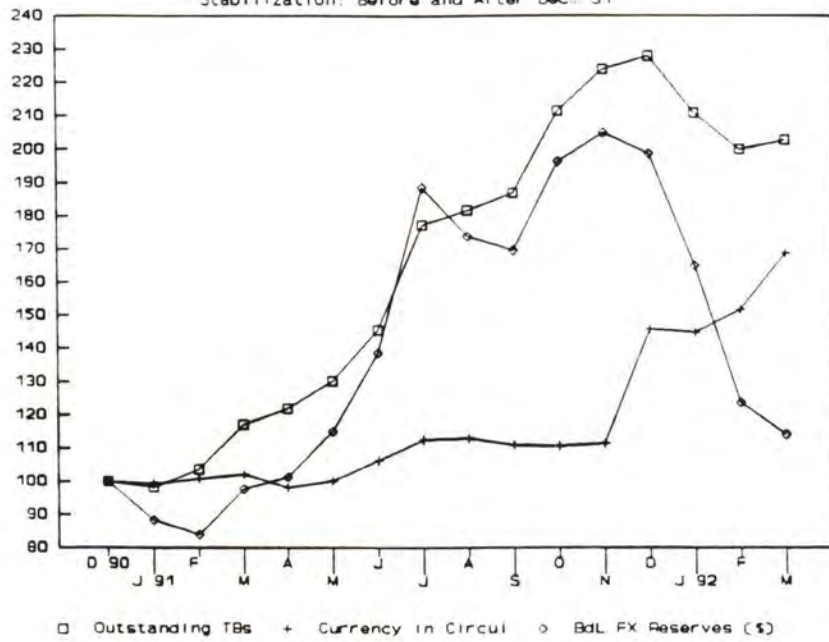
present a realistic first phase overall reconstruction program, including program priorities, institutional arrangements, domestic contributions, and the role of the private sector.

18. As indicated above, a parallel Bank mission is currently visiting Lebanon to define a possible project for Bank financing as part of the overall reconstruction program. The Government's implementation of the needed economic reforms would not only help in obtaining the co-financing that will be required for the emergency reconstruction operation, but also in the possible processing of additional operations in the years to come in a variety of sectors. The mission believes that in addition to reconstruction of physical infrastructure, the Government of Lebanon faces a need to rehabilitate public administration, develop and strengthen institutions, and strengthen economic management. The mission understands that other institutions, particularly the UNDP, are providing support in these areas and that proposals for the establishment of a technical assistance fund and secretariat are currently being developed by CDR and UNDP for consideration at a CG meeting. However, the needs for support are large and, in a number of areas, urgent. The mission will therefore recommend that in addition to helping finance reconstruction investment, the Bank should consider support for strengthening public administration and economic management in selected priority areas.

Beirut, May 6, 1992

## LEBANON

Stabilization: Before and After Dec. 91



## LEBANON

Stabilization: Before and After Dec. 91

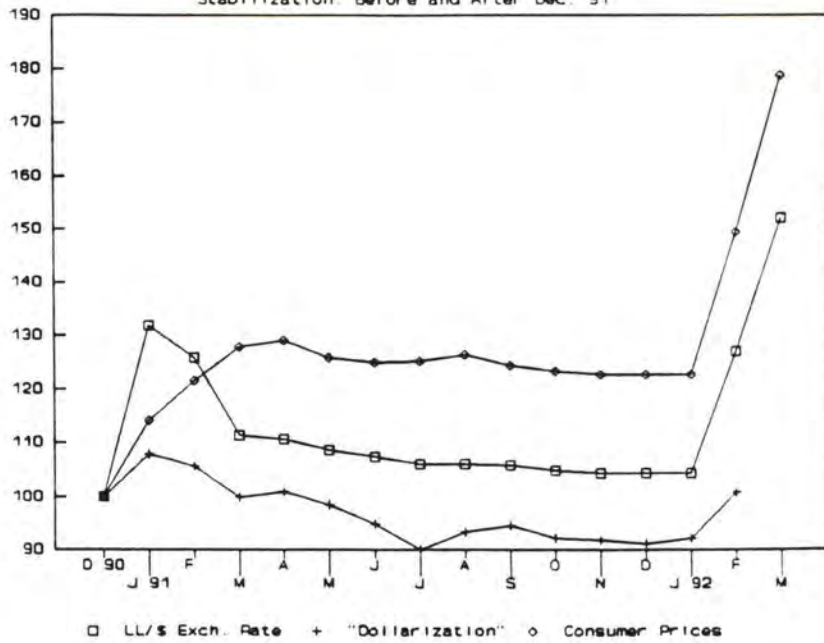


TABLE 1

Lebanon: Summary of Consolidated a/ Central Government Operations: 1989-1992

(in billions of Lebanese Pounds)

	1989	1990	1991	Proposed Budget 1992
Total Central Government Revenue (excluding grants)	62.6	126.4	456.7	867.5
of which:	25.1	55.3	300.7	730.5
Direct Tax Revenue	14.8	37.1	89.7	236.0
Indirect Tax Revenue	2.4	3.7	131.6	313.8
Other tax revenue	7.9	14.5	79.4	180.7
of which: Bank of Lebanon profits	37.5	71.1	156.0	137.0
	28.5	64.7	133.7	50.0
Total Central Government Expenditures 1	534.7	794.5	1398.8	2097.5
Current expenditures	495.0	745.2	1206.3	1460.8
Capital Expenditures 2/	39.7	49.3	192.5	636.7
of which: CDR	17.0	16.9	48.8	500.0
Adjustments incl. interagency transfers	5.9	58.2	-189.6	
Overall deficit (excl. grants)	-466.2	-609.9	-1131.7	-1230.0
Financing	466.2	609.9	1131.7	
Grants			65.6	
Net Foreign Financing	5.0	5.9	19.2	
of which: CDR	7.0	16.2	31.5	
Domestic Financing	461.2	604.0	1046.9	
Memorandum items	In percent of GDP			
Total Central Government Revenue	4.84%	7.05%	11.70%	
Total Central Government Expenditures 3	41.35%	44.31%	35.85%	
Total Central Government Expenditures 4	40.89%	41.06%	40.71%	
Overall deficit (excl. grants)	-36.05%	-34.01%	-29.00%	
GDP (million US\$)	2607	2558	4200	
Average exchange rate: 1 US\$=	496	701	929	
GDP (bn Lebanese Pounds)	1293.1	1793.2	3901.8	

a/: Central Budget, Extra budgetary Accounts, Annexed Budgets and CDR

1/: Includes net lending

2/: Total capital expenditures - domestic financing of CDR capital expenditures which are assumed to have come through transfers from Central Government

3/: Total expenditures and net lending, excluding adjustment items

4/: Total expenditures and net lending, including adjustment items

TABLE 1a

## Lebanon: Summary of Central Government Operations: 1989-1992

(in billions of Lebanese Pounds)

	1989	1990	1991	Prop Jan- Budg March 92 1992
<b>TOTAL RECEIPTS</b>				<b>867.5</b>
Identified receipts	62.6	126.4	522.3	817.5
Indirect Taxes 1/	2.4	3.7	131.6	313.8
Customs duties	1.8	2.2	98.0	250.0
Direct Taxes 2/	14.8	37.1	89.7	236.0
Registrations, fees and dues	7.9	14.5	79.4	180.7
Other 3/	37.5	71.1	221.6	87.0
Bank of Lebanon profits	28.5	64.7	133.7	50.0
Saudi Grant			65.6	
Unidentified receipts/8				50.05
<b>Total expenditures</b>	<b>527.7</b>	<b>778.3</b>	<b>1367.3</b>	<b>1597.5</b>
Budgetary expenditures	187.9	339.8	771.6	1254.7
Salary & wages/4	96.9	210.0	370.0	792.9
Capital expenditures/5	32.7	33.1	161.0	136.7
Other current/6	58.3	96.7	240.6	325.1
of which: advances and transfers				171.8
Extrabudgetary expenditures	339.8	438.5	595.7	342.8
Domestic interest	151.5	203.5	371.0	278.7
of which: interest on Treasury Bills				275.0
Foreign interest	0.7	10.0	2.0	
Petroleum subsidy	99.3	46.0	35.1	0.0
Other/7	88.3	179.0	187.6	64.0
of which: transfers to nfpe/7		160.8		64.0
	0.2	0.0	0.0	
<b>Overall deficit</b>	<b>-465.3</b>	<b>-651.9</b>	<b>-845.0</b>	<b>-730.0</b>
<b>Adjustment</b>	<b>-6.1</b>	<b>-58.2</b>	<b>189.6</b>	
<b>Financing</b>	<b>459.2</b>	<b>593.7</b>	<b>1034.6</b>	<b>244.3</b>
Net Foreign financing	-2.0	-10.3	-12.3	
Net Domestic financing	461.2	604.0	1046.9	244.3
TB Sales to public/9	66.2	31.6	473.0	-56.9
Bank of Lebanon/10	110.0	411.1	-268.4	437.2
Commercial banks/11	284.6	156.0	776.4	-143.7
Other/12	0.4	5.3	65.9	7.7
less treasury cash balance				90.9



Table 1a (cont)

*Lebanon: Summary of Central Government Operations: 1989-1992 (cont)*

(in billions of Lebanese Pounds)

<i>Memorandum items</i>	1989	1990	1991	<i>Prop Budg 1992</i>	<i>Rev. Jan- Plan March 92 1992</i>
Public Domestic debt (end of period)	982.8	1583.0	2630.0		2672.4
Tax revenue	25.1	55.3	300.7	730.5	
Current expenditure	495.0	745.2	1206.3	1460.8	
Current deficit	-432.4	-618.8	-684.0	-643.3	
	<b>In percent of GDP</b>				
Overall deficit	-35.98%	-36.35%	-21.66%		
Current deficit	-33.44%	-34.51%	-17.53%		
Tax revenue	1.94%	3.08%	7.71%		
Total receipts	4.84%	7.05%	13.39%		
Total budgetary expenditures	14.53%	18.95%	19.78%		
Total expenditures	40.81%	43.40%	35.04%		
	<b>In percent</b>				
Tax revenue/total expenditure	4.76%	7.11%	21.99%	45.72%	
Tax revenue/curr. exp.	5.07%	7.42%	24.93%	50.00%	
Tax revenue/salary&wages	25.90%	26.33%	81.27%	92.12%	
Total receipts/curr. exp.	12.65%	16.96%	43.30%	55.96%	
Total receipts/tot. exp.	11.86%	16.24%	38.20%	51.17%	
GDP (million US\$)	2607	2558	4200		
Average exchange rate: 1 US\$=	496	701	929		
GDP (bn Lebanese Pounds)	1293.1	1793.2	3901.8		

*LEBANON: Breakdown of Central Government Revenues*

	1989	1990	1991	Prop. Budget 1992
/1				
<b>Indirect taxes</b>	2.4	3.7	131.6	313.8
Customs duties	1.8	2.2	98.1	250.0
Other indirect taxes	0.5	1.5	33.5	63.8
of which:				
Excise on fuels			22.0	40.0
Excise on cement	0.4		1.8	6.0
Excise on alcohol			3.5	5.6
Excise on soft drinks	0.1		1.5	
Stamp tax				
Departure Tax				
Miscellaneous			4.7	
/2				
<b>Direct taxes</b>	14.8	37.1	89.7	236.0
Property taxes	2.1		6.1	9.0
Taxes on income and profits	9.7		52.2	200.0
Inheritance tax	2.6		12.3	15.0
Other	0.4		19.1	12.0
/3				
<b>Other</b>	37.5	71.1	221.6	87.0
Bank of Lebanon profits	28.5	64.7	133.7	50.0
Social security tax	8.8	9.6	22.3	
Other misc.			65.6	
of which: Saudi Grant			56.0	

*Lebanon: Breakdown of Central Government Expenditures*

	1989	1990	1991	1992
/4				
Salary & wages	96.9	210.0	370.0	792.9
Military				303.7
Surete Generale				20.0
Securite Interne				94.0
Education				138.0
Other				237.2
/5				
Capital expenditures	32.7	33.1	161.0	136.7
Transport and Public Works				45.3
Defense				49.5
Hydraulics and electricity			75.0	21.9
CDR				4.0
Other				16.0
NB: Capital expenditures exclude CDR executed investments				
These are/a:	17.0	16.9	48.7	500.0
/a: Projected disbursements for CDR over 3 years have been approved at US\$ 1.9 billion, of which an estimated \$333 million will take place in 1992.				
/6				
Other current	58.3	96.7	240.6	325.1
Advances and transfers				171.8
of which:				
Universite du Liban				40.0
Cooperation de la Fonction Publique (soc sec)				20.0
Health, hospitals, Red Cross				30.1
Conseil du Sud				40.0
Defense				8.0
Private primary and secondary schools				7.1
Gendarmes et prisons				4.5
Other				22.0
Other (non-transfer) current expenditures mainly O&M, office equipment, electricity etc.				153.3
/7				
Calculated as residual with total expenditures given				
Transfers to nfpe				64.0
Agriculture, Ag. Research, Office de Fruits du Liban				17.4
Railroads, Public Transport				8.0
Ministry of Housing				4.0
Civil Defense, fire fighting etc.				6.6
Ministry of Hydraulics and Electric Resources				1.7
Scientific Research				0.7
Internal security				0.4
Other				25.2
/8				
Calculated as residual with total expenditures (1,597.5) and overall deficit (730.0) given.				

*Breakdown and sources for financing data (examples given for 1991)*

- /9 Change in internal debt owed to public: 649.8-176.8; Source: BDL
- /10 Change in internal debt owed to BDL: 367.8-636.2; Source: BDL
- /11 Change in internal debt owed to commercial banks: 1536.2-759.8; Source: BDL
- /12 Change in internal debt owed to Gov. Inst. and Fin. Inst.: 71.6+4.5-9.9-0.3; Source: BDL

TABLE 2

**LEBANON: External Public Debt (M & LT)**  
**(US\$ million)**

<b>December 31, 1991</b>				
<b>Creditor</b>	<b>Outstanding and Disbursed</b>	<b>Principal in Arrears</b>	<b>Interest in Arrears</b>	<b>Total Debt Outstanding</b>
MULTILATERAL	55.49	3.92	7.33	62.82
ARAB FUND	20.61	1.31	.62	21.23
IBRD	21.94	-	-	21.94
EIB	12.94	2.61	6.71	19.65
BILATERAL	182.76	57.35	37.10	219.86
ABU DHABI	5.66	4.93	1.17	6.83
BELGIUM	0.79	.04	.01	.80
FRANCE	1/ 197.23	1/ 118.5	29.94	227.17
GERMANY	11.28	.94	.46	11.74
ITALY	12.57	6.02	2.09	14.66
USA	33.27	4.89	3.43	36.70
<b>TOTAL</b>	<b>316.29</b>	<b>139.3</b>	<b>44.43</b>	<b>360.72</b>

1/ Includes US\$ 78.04 million in estimated military debt principal in arrears.

✓ 5/26

**The World Bank**  
Washington, D.C. 20433  
U.S.A.

CAIO K. KOCH-WESER  
Vice President  
Middle East & North Africa Region

May 22, 1992

H.E. Elias Harawi  
President of the Republic of Lebanon  
BEIRUT  
Lebanon

Your Excellency:

I would like first of all to thank you for the personal attention you provided in helping the Bank missions in Lebanon at the time when the public order was so much disturbed during the second week of May. I regret that we had to decide to ask Mr. Voyadzis and his colleagues to leave the country because of security considerations.

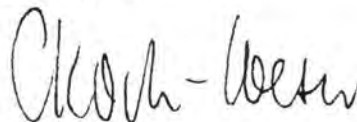
The economic mission, which had substantially completed its work at the time of departure, also very much appreciated to have had the opportunity to discuss with you the short-term economic difficulties that are facing the country and present to you the mission's aide-memoire which includes a number of suggestions on how to proceed. We are hopeful that the new Government that has recently taken office will decide to address the critical problems facing the economy.

As you know, we had an opportunity to informally discuss the economic situation and possible Bank support with the new Minister of Economy and Trade, Dr. Makdissi, during his recent visit to Washington, and we will shortly transmit the aide-memoire to the new Prime Minister, His Excellency Rashid Solh.

As was indicated by Mr. Voyadzis during his meeting with you, the Bank would stand ready to assist the Government in mobilizing donor support for Lebanon's reconstruction and development at the most appropriate time in the context of a Consultative Group meeting. In this regard, I would like to reiterate that it will be advisable, under the circumstances and in the absence of an economic reform program under implementation, to delay the Consultative Group meeting from early July to sometime in the Fall.

Thank you again for all your support and personal attention.

Sincerely yours,



cc: Mr. Fawzi Al-Sultan  
Executive Director

cc: Mdmes./Messrs. Karaosmanoglu, Shamsedin, Kohli, Chopra, Squire,  
Husain, Bouhabib, Bhargava, Keare, McKechnie,  
Okonjo-Iweala, Voyadzis, Tyler, Heron

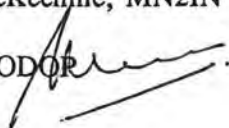
## OFFICE MEMORANDUM

5/13

✓

DATE: May 12, 1992

TO: Mr. Alastair McKechnie, MN2IN

FROM: Jan Wijnand, CODOR 

EXTENSION: 81491

SUBJECT: Lebanon - Emergency Recovery Project

Further to the memorandum dated April 28, 1992 informing Mr. Karaosmanoglu of the region's intention to process, in accordance with OD 8.50, an emergency recovery project in Lebanon, I have the following comments.

After a hiatus of nearly 15 years in Bank lending to Lebanon, the breadth of issues described in the EPS (para 11) is such that a more thorough preparation than the usual quick response of an ERL seems warranted. In contrast with the conclusion of the IEPS meeting which advocated a rapid and flexible response from the Bank for preparing and appraising an emergency rehabilitation/reconstruction project, the proposed processing schedule (para 15) is more in line with that of a normal investment operation (i.e., 13 months from the data gathering mission of November 1991 to the Board presentation currently scheduled for December 1992).

One of the main criteria of an ERL is that an urgent response to an extraordinary event of limited duration must be vital (OD 8.50 paras 2 and 13(e)). There is no need otherwise for processing a loan as an ERL. I would, therefore, advise to reconsider the proposed instrument in light of the Lebanese situation.

cc: Messrs. Karaosmanoglu (EXC); Rajagopalan (OSPVP); Koch-Weser, Husain (MNAV); Wyss (CODDR); Chopra, Heron (MN2DR); Kohli (EMTDR)



# OFFICE MEMORANDUM

5/1  
✓

DATE: April 28, 1992

TO: Mr. Attila Karaosmanoglu, Managing Director

FROM: Caio Koch-Weser, MNAVP *CKW*

EXTENSION: 35250

SUBJECT: Republic of Lebanon: Proposed Emergency Recovery Project

1. In accordance with Operational Directive 8.50 concerning Bank initiatives in Emergency Recovery Assistance, I wish to inform you that the Region is proceeding with preparation of an Emergency Recovery Project for Lebanon. The identification/preparation mission is scheduled to depart around May 3, 1992.

2. Attached, for your information, is a copy of the Executive Project Summary (EPS) and the minutes of the Initial Executive Project Summary meeting. As you may recall, the February 1992 identification/preparation mission was postponed at the last moment due to a deterioration in the security situation. Hence, the EPS reflects the revised project processing schedule, as well as the changes in task management. Paragraph 16 of the EPS provides a list of staff members who have agreed to serve on the Ad Hoc Advisory Group for the proposed project.

Attachments

cc: Messrs. Chopra, Heron, Tyler (MN2DR), McKechnie (MN2IN), Voyadzis (MN2CO), Bhargava (MN2IE), Keare (MN2PH); Mesdames: Okonjo-Iweala (o/r) (MN2AG)  
The Ad Hoc Advisory Group and Identification Mission Members

*K* KRasmussen:is

April 24, 1992

EXECUTIVE PROJECT SUMMARY

Country and Borrower: Republic of Lebanon

Implementing Agencies: To be determined

Project Name: Emergency Recovery Project

Project Cost: To be determined

Financing Plan: Bank loan of US \$150 million equivalent; co-financing and Government contributions to be determined

Tentative Appraisal Date: October 1992

Tentative Board Date: December 1992

1. Background. Lebanon is emerging from 17 years of violent civil strife and military occupation that has had debilitating consequences on economic and social development. Real per capita income (about \$1,000) has fallen to about one-third of the 1975 level and absolute poverty and income inequalities have increased. The physical destruction has resulted in massive damage to the country's infrastructure and housing, the loss of economic activity and production, the disintegration of institutions, the emigration of a large portion of the professional and business class, and a significant deterioration in social conditions.

2. The physical destruction is widespread. For example, the electricity sector has sustained significant damage to power stations and transmission lines. Of the 1,205 megawatts of installed capacity, about 360 to 560 megawatts are currently available, and Electricite du Liban (the national public utility), is only capable of supplying power to customers for about 6 hours per day. The dilapidation of water supply and sewerage facilities has led to inadequate supplies of potable water, a level of unaccounted-for-water roughly estimated at 50 percent, and environmental pollution from inadequate sewage treatment. A wide range of telecommunications facilities has been either destroyed beyond repair, or so severely damaged that their operation has been suspended, thus significantly hampering domestic and international communications. In the housing sector, about 28 percent of the housing stock has been either damaged or destroyed, and almost one quarter of the population has been displaced and is living in unhealthy and overcrowded conditions. Although a reliable estimate of total physical losses sustained during the past decade and a half is presently not available, it may well exceed annual GDP.

3. Response and Strategy. The October 1989 Taif Accord provided a basis for national reconciliation and a blueprint for reform of the political system in Lebanon. The new transitional government, which came to power in October 1990, has since extended its authority although it is still contested in some areas. During 1991, the improved security situation and some initial reconstruction activity contributed to a significant recovery in output from the depressed levels of 1989/90 when hostilities were particularly intense. Macroeconomic

policy succeeded in reducing inflation and stabilizing the exchange rate of the Lebanese Pound, which has remained convertible. Most recently, political issues (such as this Summer's elections and relations with Syria) as well as social unrest due to rising prices, forced the Government to backtrack on a few important stabilization measures and introduce price controls. As a result, the Lebanese Pound further depreciated from about \$1 = 875 to \$1 = 1400. Of most serious concern is the fiscal deficit (estimated at 21% of GDP in 1991), which is expected to increase unless the Government's revenue performance is drastically improved. Also of notable concern is the magnitude of the external deficit (about 35-40% of GDP). The above underscores the urgent need to improve the fiscal situation and to adopt the appropriate monetary policies which would provide the private sector - a traditional engine of growth for Lebanon - with the correct signals and incentives to resume investing in the Lebanese economy.

4. In December 1991, at the Aid Coordination meeting chaired by the Bank, the international donor community showed increasing willingness to support the reconstruction of the Lebanese economy. The European Community is financing consultants for sectoral damage assessments, while the Arab and Kuwait Funds have contributed \$110 million for emergency repairs in the power sector. A UNDP/Bank data gathering mission to Lebanon took place in November 1991. A country economic memorandum is under preparation, and is expected to provide the overall framework for the Bank's strategy in Lebanon. Close collaboration will be maintained between the economic and project preparation missions. An Aid Coordination or a Consultative Group Meeting has been tentatively scheduled for July 1992. This meeting would be organized only after we are satisfied that the Government has decided upon, and is in the process of, implementing the urgently needed macroeconomic actions, particularly those pertaining to the reduction of the fiscal deficit. It should be noted, however, that in accordance with O.D. 8.50, further processing of the proposed Emergency Recovery Project would not be contingent upon the implementation of macroeconomic reforms.

5. The rebuilding of the ravaged economy and the return to sustainable growth will involve three phases: (i) short-term emergency rehabilitation (1 to 3 years); (ii) medium-term reconstruction; and (iii) long-term expansion in a market-based and outward-oriented policy framework. During the first phase, emergency repairs and rehabilitation of physical assets are required to remove bottlenecks and restore productivity, combined with technical assistance, training and financial support to gradually rebuild institutional capacity, and key studies to determine future sector strategies. During the past year, the Government has revived the Council of Development and Reconstruction (CDR), a key agency responsible for planning and managing the national recovery program and coordinating with implementing agencies.

6. Project Objectives. The proposed project would assist the Government to: (i) assess the overall economic impact of the destruction and sectoral damage and recovery needs; (ii) define the scope of a three-year emergency recovery program; and (iii) solicit the support of donors for Lebanon's massive reconstruction efforts. The proposed project supports the Government's objectives to restore essential infrastructure and social services, thereby removing the obstacles to recovery in the short term (the emergency phase), while laying the groundwork for sustainable growth over the medium to long term. The project also aims to strengthen the existing institutional arrangements at the national level for planning and monitoring a nationwide reconstruction program, as well as the implementation and operational capabilities of line ministries and agencies.

7. Project Description. The Government is preparing a broad national recovery program, of which the 3-year emergency phase has been estimated at about US \$1.5 billion. The Bank proposes to undertake an assessment of the Government's 3-year Emergency Reconstruction Program. Based on the results of this assessment, the Government's priorities and the commitments or interest expressed thus far by other donors, the composition and design of the proposed Bank project (a Bank loan of US \$150 million equivalent) would be defined. Although the Bank has been requested by the Government to consider financing possible components in the power, telecommunications, water, waste water, solid waste and housing sectors, the choice of sectors and components will be determined during project preparation. The forthcoming identification mission would assess the suitability of a program approach (i.e., financing a time slice of the Government's Emergency Recovery Program) versus a project approach, recognizing that this would require institutions that were capable of preparing, implementing and operating rehabilitated facilities. In addition, the mission would explore the possibility and appropriateness of including a well-defined, quick disbursing component in light of the balance of payments prospects. The proposed project would focus on emergency rehabilitation and reconstruction of existing infrastructure (and possibly superstructure), to be implemented over a 3-year period.

8. Lessons from Previous Bank Involvement. The proposed project represents the first Bank loan to Lebanon since the 1977 Emergency Project (Loan 1476-LE). Implementation of this project was interrupted due to a resurgence of internal turmoil. The deteriorating security situation also undermined the Bank's efforts in the emergency reconstruction project planned for 1983. The main lesson learned from the Bank's involvement in Lebanon is that a reconstruction program would have a much greater chance of success and international support if it were initiated when government authority is restored, and the security and political situation is stabilized. A second lesson learned from the Bank's involvement in emergency assistance is the importance of ensuring that appropriate institutional arrangements, on both the national and sectoral levels, for managing and implementing a national recovery program are in place.

9. Rationale for Bank Involvement. At the request of the Government, the Bank has taken a lead role in aid coordination (para. 4), and is expected to play a catalytic role in mobilizing donor support for the country's emergency recovery program. Bank involvement in emergency reconstruction is regarded as crucial to rebuild essential infrastructure, restore productivity and alleviate human deprivation. The proposed project aims at removing critical infrastructure bottlenecks in key sectors, without which the supply response, to be led by the private sector, is unlikely to materialize. Nor will flight capital return or foreign direct investment increase. In the absence of significant growth, government revenue constraints will prevent a speedy reduction in the fiscal deficit, while pressing social issues will go unmet.

10. The proposed project meets the criteria spelled out under Operational Directive 8.50 for emergency recovery assistance. This project would prepare the groundwork for long-term institutional development which would be addressed through subsequent traditional investment lending. Hence, the immediate focus would be on strengthening the implementing capacity of executing agencies so as to ensure the financial and operational sustainability of restored facilities.

11. Issues and Actions. The major issues are: (i) the sectoral content of the proposed project and the state of preparedness of each potential component; (ii) the project design (a program versus project approach) including the suitability

of a well-defined, quick disbursing component in light of the balance of payments prospects; (iii) the role of CDR in planning, managing and aid coordination of the overall national reconstruction program and CDR's interface with executing agencies; (iv) the absorptive capacity of implementing agencies; (v) the sectoral implementation arrangements, particularly with respect to the fragmented water and waste water sector; (vi) cost recovery policies for water, telecommunications and electricity; (vii) co-financing; and (viii) the role of the private sector (national and international) during the rehabilitation and reconstruction phases. With respect to the housing sector, specific issues to be tackled include, but are not limited to: (i) the identification and appraisal of financial intermediaries; (ii) beneficiary selection; and (iii) the terms and conditions for the financial sustainability of the scheme. The viability of a housing sector component would be predicated on receiving substantial grants from donors to reduce the cost of funds to the beneficiaries. Concerning the telecommunications sector, attention would be given to the Government's financial, commercialization and privatization strategy for the sector, and the scope of bilateral interest expressed thus far. The identification mission will address all of these issues and propose a time-based action program.

12. Environmental Aspects. Since the major focus of the proposed project is to rehabilitate existing infrastructure (and possibly housing superstructure), it has been classified under environmental Category B. Environmental reviews are being undertaken in the context of the sectoral damage assessments, and attention will be paid to supporting a recovery process consistent with the adoption of prudent environmental policies and practices.

13. Project Benefits. The proposed project would assist the Government in the restoration of critical basic infrastructure and facilities that are needed to support economic revival and reduce social hardship. It would help strengthen the Government's capacity to plan, monitor and implement the country's recovery program. The project is also expected to have a positive impact on the social and physical environment.

14. Risks. The key risks relate to: (i) the hiatus of the Bank's involvement in Lebanon over the past decade; (ii) the institutional and financial absorptive capacity of implementing agencies which could delay project execution; (iii) the organizational and financial sustainability of executing agencies to operate and maintain rehabilitated facilities; (iv) the uncertain policy environment arising from the transitional nature of the current Government and implementation of the Taif Accord; and (v) the potential for a deterioration in the security situation. Although these risks are far from negligible, the first three endogenous types of risk can be reduced through careful project preparation. Moreover, the potential benefits from the project, in terms of removing impediments to economic revival and restoring basic services, would seem to outweigh the risks. In addition, Bank involvement would, a priori, strengthen the Government's capacity to manage and implement a national recovery program, and may serve as a catalyst to attract donor financing.

15. Project Processing Schedule

Identification Mission	May 3, 1992
Preparation Mission	July 1992
Appraisal Mission	October 1992
Board Presentation	December 1992

16. Project Management and Review (Managing Division: MN2IN)

Ad Hoc Advisory Group: Messrs.: Harth (AF1IN), Christie (AF1IE), Lomax (AFTIE), Howarth (INUWS), Gulstone (AFTIE), Mayo (INURD), Pommier (CODOP), Ms. Kreimer (ENVPR)

Task Manager: Youssef Choucair (MN2IN)

KRasmussen:is  
MN2IN

# OFFICE MEMORANDUM

DATE: February 19, 1992

TO: Files

FROM: *KR* Karen Rasmussen, Senior Financial Analyst, MN2IN

EXTENSION: 33056

SUBJECT: Republic of Lebanon - Emergency Recovery Project:  
Comments on the Draft Initial Executive Project Summary

1. A meeting was held on February 11, 1992 to discuss the Draft Initial Executive Project Summary for the above mentioned project. The meeting was chaired by Mr. Ram Chopra, Director (MN2DR), and attended by the following persons: Messrs./Mesdames Heron (MN2DR), Pommier (CODOP), Kreimer (ENVPR), Hoppenbrouwer (MN2CO), Kolan (MN2IE), Choucair (EMTIN), Ouahes (EMTIE), El Erian (LEG), Buttex, Mustafa (AFTIE), McKechnie, Rasmussen and Rasmussen (MN2IN). The main points discussed and agreements reached are summarized below.

## Bank Strategy and Lending Approach

2. A question was raised concerning the Bank's country strategy for Lebanon and its relationship to the proposed Emergency Recovery Project, the first Bank operation since 1977. It was explained that the resumption of an operational relationship with the Government has included the preparation of a country economic memorandum and launching an Aid Coordination Meeting for Lebanon.<sup>1</sup> The economic report is expected to provide the overall framework for the Bank's strategy in Lebanon.

3. The meeting concluded that a quick response to address the current situation in Lebanon was required, and that the most appropriate lending vehicle would be a free-standing emergency recovery operation. Hence, in line with Operational Directive 8.50, the Bank should proceed with the preparation of an emergency recovery project before embarking on traditional investment operations. A rapid and flexible response was needed from the Bank to assist the Government in: (i) assessing the overall economic impact of the destruction and sectoral damage and recovery needs; (ii) defining the scope of an emergency reconstruction program; (iii) soliciting the support of donors for Lebanon's massive reconstruction needs; and (iv) providing financial support to remove critical infrastructure bottlenecks in key sectors. A Bank emergency recovery project, versus the more thorough but time-consuming preparation associated with traditional lending operations, would help to restore essential infrastructure and social services, thereby removing obstacles to recovery in the short term, while laying the groundwork for sustainable growth over the medium to long term. The proposed project would nonetheless be designed within the framework of a consistent medium-term emergency reconstruction program, taking into account, inter alia, the likely contributions of other donors. Moreover, the project would prepare the groundwork for

---

<sup>1</sup> A UNDP/Bank data gathering mission took place in November 1991. Based on the findings of the mission, a paper was prepared and distributed at the December 12, 1991 Aid Coordination Meeting held in Paris. The main economic mission is presently in the field and scheduled to return in early March 1992.

institutional development issues to be addressed over the medium to long term through normal investment lending operations.

4. It was agreed that there would be close collaboration between the economic mission and the project identification mission concerning the analysis of macro and sectoral issues and recommendations which would form the basis of the Bank's policy dialogue with the Government.

#### Approach to Project Design

5. There was a consensus that, as a first step, the Bank should undertake an assessment of the Government's three-year Emergency Recovery Program, estimated at about US \$1.5 billion. It was mentioned that although a list of project profiles for emergency rehabilitation and reconstruction needs in key sectors had been prepared, reliable assessments of the physical damage to assets (including deferred maintenance) during the past decade and a half were not available in many sectors. Hence, flexibility would be required by the Bank in assessing the comprehensiveness and content of the Government's Emergency Recovery Program, including the analysis and prioritization of specific projects and the order of magnitude of the physical damages. In view of the need to undertake a broad assessment of the Government's Emergency Recovery Program (including for the transportation, health and education sectors), it was recommended that staffing requirements for the identification mission be reviewed.

6. Based on the results of a review of the Emergency Recovery Program, the Government's priorities and the commitments or interest expressed by other donors, the meeting concurred that Bank should proceed to define the scope and content of the proposed project (US \$150 million equivalent), including the sectoral composition, technical assistance requirements and implementation arrangements. The identification mission should explore the possibility and appropriateness of including a well-defined quick disbursing component in light of the balance of payments prospects. In addition, the mission should assess the extent to which a program approach to project design was feasible (i.e., financing a time slice of the Government's Emergency Recovery Program), while recognizing that this would require institutions that were capable of preparing, implementing and operating rehabilitated facilities. It was agreed that the IEPS would be revised to reflect the above flexible approach to project composition and design.

#### Institutional Framework for Managing and Implementing a National Recovery Program

7. Institutional Arrangements. A recurrent theme expressed by many participants was the institutional constraints in Lebanon and the importance of ensuring the sustainability of executing agencies to operate and maintain rehabilitated facilities, both from the financial and manpower perspectives. It was noted that the Council for Development and Reconstruction (CDR), created in 1977 to replace the Ministry of Planning, had been revived as the principal agency responsible with broad powers (planning and managing the national recovery program, and handling project financing and execution). Key institutional issues to be addressed by the identification mission included: (i) the role of CDR in planning and monitoring the overall national recovery program and CDR's interface with implementing agencies, including the extent to which CDR requires technical assistance to strengthen its planning, management and monitoring capabilities; (ii) the most appropriate mechanisms for implementation of specific sectoral rehabilitation components; (iii) measures to strengthen executing agencies' capacity to implement, operate and maintain



rehabilitated facilities; and (iv) the complementary role of the private sector for each project component. The identification mission would also assess the Government's proposed arrangements for handling procurement (plus accounting and auditing) for the national recovery program in general, and the Bank Emergency Recovery Project in particular.

8. Cost Recovery. Several questions were raised concerning the extent to which it was plausible to insist on cost recovery for the provision of potable water supply, electricity and telecommunications, given the poor quality of service presently rendered. It was also concluded that before proposing a Bank position on this matter, the project identification and economic missions should exchange views on the most appropriate means of tackling cost recovery in the context of the public deficit and the sustainability of restored assets.

9. Procurement. It was noted that a review of Lebanon's procurement laws and regulations would be required, but that it would not be feasible to undertake a full country procurement assessment report (CPAR) in line with Operational Directive 11.01, given the accelerated processing of the proposed project. It was agreed that an assessment of compatibility of the country's procurement procedures with the Bank's regulations for competitive bidding under both ICB and LCB procedures should be undertaken in respect of this lending operation, and reflected in the Loan documentation. A full CPAR would be carried out in advance of a resumption of normal lending operations.

10. Policy Conditionalities. The meeting concurred that the proposed project would be processed in line with Operational Directive 8.50. Hence, the project would not aim to address long-term macro-economic issues; rather, conditionality would be linked directly to ensuring the sustainability of rehabilitated project components. In accordance with paragraphs 6 and 7 of Annex B of O.D. 8.50, any proposal to deviate from sound long-term policies would be evaluated, and if considered necessary, limited in scope and time to respond to the emergency nature of the project.

Attachment: Revised IEPS

cleared with and cc: Messrs. Heron (MN2DR), McKechnie (MN2IN); Ms. Kreimer (ENVPR)

cc: Messrs./Mesdames: Kashiwaya (CFSVP), Chopra, Tyler (MN2DR), Kohli (EMDTR), Pouliquen (INUDR), Ray (EAS), Voyadzis, Giugale (o/r), Hoppenbrouwer (o/r) (MN2CO), Bhargava (o/r), Kolan (MN2IE), Pellegrini, Choucair (EMTIN), Wackman, Ouahes (EMTIE), Keare (MN2PH), Okonjo-Iweala (MN2AG), Rasmusson, Le (MN2IN), Kjellstrom (MN1IE), Buttex, Mustafa (AFTIE), Pommier (CODOP), Seth (EMTEN), Fong (EMPTH), Ranganathan (EMTPR), El Erian (LEG), Prefontaine (LOA), MENA Files, Division Blackbook

cc: The Ad Hoc Advisory Group: Messrs: Harth (AF1IN), Christie (AF1IE), Lomax (AFTIE), Howarth (INUWS), Gulstone (AFTIE), Mayo (INURD)

KRasmussen:is

# OFFICE MEMORANDUM

3/6 ✓

DATE: March 5, 1992

TO: Mr. J. William Stanton, EXTDR

FROM: Ram K. Chopra, MN2DR *(Chopra)*

EXTENSION: 32713

SUBJECT: Lebanon-Note for Mr Preston's breakfast meeting with Ms. Oakar

1. Last September, Ms. Maguire (External Relations), Mr. Voyadzis (MN2CO), and IMF Staff met with Congresswoman Mary Rose Oakar, Chairperson of a House Subcommittee with jurisdiction over the Bank and Fund, at her request, to discuss Bank/Fund activities in Lebanon. Ms. Oakar, who is of Lebanese descent, encouraged the institutions to become active in Lebanon; in fact she asked the IMF to follow the Bank's example.


2. A World Bank/UNDP mission visited Lebanon in late October to briefly assess the economic situation and identify priority rehabilitation requirements and technical assistance needs. The mission's report was discussed on occasion of a Lebanon Aid Coordination Meeting, chaired by the Bank, which took place last December. During the meeting a number of donors made preliminary commitments for support to the reconstruction effort in Lebanon, with major potential contributions from the EEC, Italy and a number of Arab Funds.

3. Following 15 years of destruction the reconstruction needs in Lebanon are enormous. Estimates by consultants contracted by the Lebanese Council for Development and Reconstruction put financing needs for the 1991-2000 decade at around \$10 billion, with emergency needs for the 1992-94 period of about \$1.5 billion. Following the Aid Coordination meeting the Bank began to plan for: (i) an economic mission to prepare a CEM on Lebanon; (ii) an Emergency Reconstruction Project preparation mission for a possible loan of about \$150 million; and (iii) a full Consultative Group (CG) on Lebanon to be held in July of this year. Please note that as of now we still do not know whether the Government wishes the Bank to chair a CG or another, more informal, Aid Coordination Meeting. The IMF on its part scheduled an Article 4 Consultation and Fiscal Affairs mission to Lebanon. However, following the worsening of the security situation in the aftermath of the events in Southern Lebanon in mid-February, the UN issued a ban on all travel to Lebanon on February 25; as a result, we decided to recall our economic mission from the field for security reasons and to postpone the Project mission.

4. Today we were informed that the UN had lifted the ban on travel, but prior clearance procedures remain in effect. We are now proceeding to reassemble the economic and project mission teams and are aiming for the missions to be in the field following the end of

Ramadan holidays in April. We understand that the IMF plans to proceed with its missions as well. Despite the delay, and subject to the security situation continuing to improve, we are currently maintaining plans for a Consultative Group/Aid Coordination meeting in July and Board presentation of a Bank loan towards the end of 1992/early 1993. Based on preliminary assessments our main concerns regarding Lebanon relate to the fiscal situation, the weakness of Government and public administration, and the institutional arrangements for the reconstruction effort.

cc: Messrs. **Karaosmanoglu** (EXC); Koch-Weser (MNAV); Chopra, Heron (MN2DR); McKechnie (MN2IN); Giugale (MN2CO)

  
LH/SV/mr  
m:\leb\congress.mem

ALL - I N - 1 N O T E

DATE: 20-Feb-1992 11:54am

TO: Attila Karaosmanoglu ( ATTILA KARAOSMANOGLU )

FROM: Caio Koch-Weser, MNAVP ( CAIO KOCH-WESER )

EXT.: 35250

SUBJECT: Lebanon

Attila,

In light of the deterioration of the situation in Southern Lebanon, and the increased security risks this poses for the Beirut area, I have decided to pull our economic mission out of the country as soon as possible (i.e., tonight or early tomorrow Beirut time) and to fly them to Cyprus. We can then decide by Monday (or later) whether we bring them back in or have them come back to Washington.

Both the U.N. and the State Department have alerted us to the increased security risks. The U.N. has pulled out one of their negotiators who happened to be in the country, but is not at this point evacuating visiting missions or other staff. A number of our staffmembers were beginning to feel uneasy. We considered other options: bringing the mission back to Washington right away; moving them out of West Beirut to East Beirut and the mountain resorts over the weekend (which are supposedly much safer); and the Government providing them with additional security protection. Bill Creeden was fully involved in the decision process, and, together with Ram, came to the same conclusion as I did.

A. Bouhabib has been helpful in quickly identifying local charter possibilities for the 20 min flight to Cyprus. An alternative is the next scheduled flight.

I will keep you posted.

Caio

ROUTING SLIP

DATE:  
1/16/92

FROM THE REGIONAL VICE PRESIDENT

NAME

ROOM NO.

Mr. Karaosmanoglu

cc: Mr. Bottelier

APPROPRIATE DISPOSITION

NOTE AND RETURN

APPROVAL

NOTE AND SEND ON

COMMENT

PER OUR CONVERSATION

ACTION

PER YOUR REQUEST

INFORMATION

PREPARE REPLY

INITIAL

RECOMMENDATION

NOTE AND FILE

SIGNATURE

REMARKS:

Per our discussion. In my absence, Pieter will give you further information.

Caio Koch-Weser

FROM:

# OFFICE MEMORANDUM

DATE: January 14, 1992

TO: Mr. Caio Koch-Weser

FROM: Tariq Husain *Tariq Husain*

EXTENSION: 33907

SUBJECT: LEBANON--Visit of Missions

*Mr. Khatamoglu  
in our discussion.  
in my absence, I think  
will give you  
further information.  
cc: P. Sotiria*

*ACK  
1/15*

As you wished I note below what Spiros plans to do.

1. The Emergency ~~Economic~~ Mission is scheduled to go in late January but provided UN gives the clearance to visit.
2. The Economic Mission is scheduled to leave on February 17 so there is no overlap between the two missions.
3. For both missions, the members will spend 1-1/2 weeks in Lebanon, then about half a week in Cyprus, and will then return to Lebanon.
4. No U.S. citizens will be sent on the missions, and we will minimize British and German participation.
5. Participants will go to different hotels as an added security measure.



# Record Removal Notice



<b>File Title</b> Subject Files: Country Files - Lebanon - Correspondence 01		<b>Barcode No.</b>  1328843		
<b>Document Date</b> 18 December, 1991	<b>Document Type</b> Board Record			
<b>Correspondents / Participants</b>				
<b>Subject / Title</b> Executive Director's Meeting - December 17, 1991 Lebanon Aid Coordination Meeting Presentation by Mr. Koch-Weser (SECM91-1606)				
<b>Exception(s)</b>				
<b>Additional Comments</b> Declassification review of this record may be initiated upon request.		The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.		
		<table border="1"> <tr> <td><b>Withdrawn by</b> Sherrine M. Thompson</td> <td><b>Date</b> March 31, 2017</td> </tr> </table>	<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017
<b>Withdrawn by</b> Sherrine M. Thompson	<b>Date</b> March 31, 2017			

Jordan  
Lebanon

December 6, 1991

Mr. Karaosmanoglu:

Attila:

You will receive a "cleaned up" copy for Mr. Preston later this morning. This is for your meeting with the Jordanians this morning. I suggest you -

- congratulate the Minister for the program agreed with the Fund, and the good progress in filling the 1992 financing gap;

- assure him of our strong support for the forthcoming financing tour which should now focus primarily on the medium-term (1993/94), and also financing of projects, in preparation for the CG (timing: about mid-January);

- state that CG should take place as early as feasible, ensuring a success (not agreeing on date yet);

- enquire about progress in relations with Saudis and Gulf countries (timing); and political support at home for what is a very demanding adjustment program.

They might raise the need for intervention with Paris Club. I told them that this should be divorced from broader financing tour because of different counterparts in G-7 capitals, and timing.

Cairo



## JORDAN

### BACKGROUND

Jordan was successfully implementing an adjustment program supported by the IMF and the Bank when the Gulf crisis erupted in August 1990. The crisis disrupted Jordan's trade, reduced remittances, and burdened the economy with returnees from the Gulf. In October 1991, the Government reached an agreement on a macroeconomic framework with a joint Bank/IMF mission. A Letter of Intent (LOI) has been agreed upon and will form the basis of an IMF Stand-By Arrangement to be presented to the IMF Board in early 1992. This would trigger new debt rescheduling agreements with the Paris and London Clubs. Implementation of the Government's adjustment program requires large amounts of highly concessional assistance. With the support of the IMF we are trying to mobilize such financing through a Consultative Group meeting tentatively planned for the end of February 1992. We plan to support this program through the release of the second tranche of the Industry and Trade Policy Adjustment Loan (ITPAL - US\$75 million) and additional operations in line with our overall exposure policies. In your meeting with the IMF MD you could bring up the issues presented below.

### ISSUES

- Risk of Policy Slippage Perhaps we, more than the IMF, think that the program has a high risk of policy slippage. First, the adjustment process involves a cumulative reduction in per capita consumption of about 20% over the next five years. Second, the program has severe compression of imports to achieve balance of payments viability. This may make the program socially and politically difficult to implement.
- Financing Requirements The adjustment program adopted by the Government needs total gross external financing of US\$ 5 billion over the next three years (1992-94). Taking into account US\$ 2.6 billion of rescheduling and regular financing the residual financing gap that needs to be mobilized is about US\$1.3 billion. Of that amount about US\$450 million is needed for 1992 alone. Towards this, so far, preliminary assurances for about US\$400 million have been received.

The financing effort now has the full support of the US. To that effect, State has asked the US Ambassadors to the G-7 capitals to urge the authorities to support Jordan. There is, however, a need for more contributions from the G-7 - particularly from Japan. So far no contributions have been received from Jordan's traditional supporters-- the Gulf States, especially Saudi Arabia. We believe that their participation is crucial for 1993-94 and beyond. You may ask Mr. Camdessus if he thinks that we should fix the timing of the Consultative Group meeting (aimed at securing the financing needed over the medium-term) only when we are assured of Gulf countries participation. We

believe that this issue should remain open at the present time to see how events will unfold.

• Debt Restructuring Jordan's financing plan involves the maximum possible debt rescheduling at the Paris and the London Clubs at highly concessional terms. Jordan's creditworthiness, nevertheless, remains marginal. Some form of debt relief would, therefore, be necessary to make Jordan's creditworthiness more acceptable for increasing Bank exposure. This would help the Government's implementation of the adjustment program by providing the necessary cushion. You may ask Mr. Camdessus if debt relief for Jordan is an achievable objective.

• ITPAL and other Bank Operations You may inform the Mr. Camdessus that we expect to release the second tranche of the ITPAL as soon as the IMF Stand-By is approved by the Board. The Board approval is taken as a signal that all the elements of an acceptable macroeconomic framework (including the financing) are in place. Currently, Bank operations are restricted to a small core program because of creditworthiness considerations. We expect to fully resume processing of our lending operations following approval by the IMF Board of the Stand-By arrangement. The level of lending will, however, be carefully calibrated to the concessionality of the financing available and the risks of policy slippage.

## LEBANON

For your information, Mr. Camdessus has informed IMF's Board of Executive Directors that a Bank-sponsored Aid Coordination Meeting will take place in Paris on December 12-13, 1991, and appealed for assistance to Lebanon.

Background. You will recall that, just before the Annual Meetings, Mr. Al-Assaf's wrote to you requesting that the Bank speed up its assistance to Lebanon and help coordinate a world donor effort. Since then we have convened two steering meetings in Washington and Bangkok. The key participants, including government representatives, proposed that an Aid Coordination meeting, open to all prospective donors, be convened as soon as possible. As a result we have organized the Paris meeting. A Bank/UNDP mission visited Lebanon to review economic developments, reconstruction plans and the related emergency projects. We have distributed their report to the prospective donors together with other documentation prepared by UNDP and the Government.

Next Steps We have scheduled a full economic mission and a project preparation mission for January 1992. Subject to continued improvement of security, we are aiming at a lending program of one or two projects per year including a reconstruction project which we may be able to bring to our Board by June 1992. Meanwhile, we intend to call a full Consultative Group meeting (subject to the decision of the December meeting) to secure financing for the overall reconstruction plan.

A. KARAOSMANOĞLU  
Managing Director

December 6, 1991

Messrs. Preston  
Sandstrom  
Stern

Lunch with Mr. Camdessus

Attached are some notes on Jordan, Lebanon and Algeria.

I don't expect the Algeria issue to be raised. Just in case the Fund raises it, we should note that there is a potential of losing seriously the momentum in our relations with Algeria. This morning I talked to Mr. Benhocine. My impression is that they want to keep close working relationships but they don't want to be pressured on the issue of privatization at this point. It seems that we will have to take up the whole issue of future content of adjustment process and our involvement in it after the elections to gauge the areas of potential action and cooperation.

I saw the Jordanian Delegation which is in town this morning. They seemed to have done quite well in their discussion with the Fund but they have tied themselves to a rather tough program which may not be all that easy to implement. It seems however that if they can keep up the reform efforts most of the financial gap for 1992 is likely to be covered but this calls for getting the best possible terms from the Paris Club at their forthcoming meeting in January. What we really have to find out, if the issue is discussed, is what message the Fund is likely to send to the Paris Club and whether they have any specific views with regards to the Aid Group meeting which we are planning to hold some time after the Paris Club meeting.

The note on Lebanon is short and self-explanatory.

*Attila*

# OFFICE MEMORANDUM

DATE: December 5, 1991

TO: Mr. Lewis T. Preston

THROUGH: Mr. Attila Karaosmanoglu *AK*

FROM: Caio Koch-Weser *CKW*

EXTENSION: 32678

SUBJECT: JORDAN and LEBANON: Lunch with Mr. Camdessus on December 9, 1991

I would like to propose that you discuss Jordan at your forthcoming luncheon with Mr. Camdessus planned for Monday, December 9, 1991. Please find attached a background briefing note. Also attached for your information is a briefing on Lebanon in case the Managing Director raises the issue.

cc: Messrs. Husain, Squire, Chopra, Erim, Chitale, Minhas, Espiritu

## OFFICE MEMORANDUM

DATE: December 4, 1991

TO: Mr. Lewis T. Preston, President  
THROUGH: Mr. Attila Karaosmanoglu *A.K*  
FROM: Caio Koch-Weser, Vice President, MNA *CKW*

EXTENSION: 35250

SUBJECT: Your Luncheon with Mr. Camdessus on December 9, 1991

You should be aware of potential difficulties in our relations with Algeria. The IMF is facing a similar situation and it is possible that Mr. Camdessus will check with you on the Bank's position vis-à-vis this country, for which he is deeply concerned. No decisions need to be taken at this stage. This memo is for background information only.

A few weeks ago, Algeria requested that the Bank suspend all preparatory work on possible future adjustment loans. The immediate reason for this appears to be a recent Bank letter to Algeria suggesting the urgent need for additional measures to promote private sector development, including legal changes that would permit private sector participation in state enterprises. We indicated that without additional measures and assurances in this area it would be difficult for the Bank to proceed with new adjustment loans.

The IMF was similarly disinclined to send an EFF preparation mission that had been scheduled for December. Instead, Algeria's Prime Minister, Mr. Ghazali, has invited the IMF's area director, Mr. Touré, to visit him in Algeria for private discussions later this month.

Underlying the Bank's insistence on additional measures to stimulate private sector development, including a role for privatization, is a growing concern about continuing economic stagnation in Algeria (zero growth since 1985 in spite of much reform activity) and questions about the practical feasibility of some key aspects of Algeria's model for gradual transition to a market economy. Although both Bank and Fund have actively supported Algeria's reform effort - two adjustment loans from the Bank (\$300 million in August 1989 and \$350 million in June 1991), and two Fund Standby programs (1989 and 1991, totalling \$1.3 billion) - there is now the possibility of an impasse in the relationship with both institutions. The IMF Board recently approved a waiver request needed for tranche release after a long debate in which many key shareholders expressed their dissatisfaction with Algeria's performance under the Fund's program.

The Algerians appear to have taken our letter and the Fund's Board discussion as a manifestation of excessive interference and pressure. It is possible that the threat of an impasse in our

relations with Algeria will fade away after the installation of a new Government following the forthcoming parliamentary elections (the first ever genuinely open multiparty parliamentary elections in that country) scheduled for December 26. It is also possible that our dialogue will not improve as a result of the domestic political situation which is very complex and highly charged. There are important segments in the two largest political parties (FLN and FIS) that are opposed to Bank and Fund conditionality for ideological reasons. Our leverage in Algeria may become substantially weaker if the Congress approves a Government proposal to open up selective oil and gas deposits for private sector participation. That would give the country access to large amounts of private financing (e.g. export pre-sales) such that there may be no further perceived need for financial support from the Bretton Woods institutions.

We are watching the situation closely and are in constant touch with our IMF colleagues. Meanwhile, we are making every effort to convince the Government of our good faith and continued availability for serious dialogue and support. An impasse in the relationship could also have major indirect implications for Algeria's external debt strategy which, as you know, has, up to now, been based on refinancing rather than on rescheduling or debt reduction.

PPB/njr