LEBANON

SUBSIDY REFORM NOTE

_____

December 2020

As policymakers in Lebanon consider a shift away from foreign exchange subsidy for imports of critical and essential goods towards direct transfers to households, the World Bank has prepared this note at the request of the Government of Lebanon. The note aims to inform the public debate on this important topic and present Lebanese stakeholders with options taking into consideration lessons learned from international experience.

LEBANON
SUBSIDY REFORM NOTE[1]

The real question regarding BdL's FX subsidy for imports of critical and essential goods, is <u>when</u> and <u>how</u> to remove it, <u>not whether</u>. This note shows that the sooner the subsidy is replaced with a cheaper and more effective compensation scheme, the better for the economy and for people's welfare. This is because the current FX subsidy is both distortionary, expensive (costing an estimated US$287m/month), and regressive (i.e., benefits predominantly wealthier consumers). Its elimination and possible replacement with a more effective and efficient pro-poor (targeted) program would improve Lebanon's balance of payments, meaningfully extend the time-till-exhaustion of remaining BdL reserves, and help cushion the impact on Lebanon's poor and middle class. This note suggests a broad-based cash transfer program as one such option, which should be in place <u>prior</u> to subsidy removal. However, while the removal of the FX subsidy would be welcome, it is a mere short-term patch as only a comprehensive reform package that is consistent with a credible macroeconomic framework can prevent the country from running out of reserves and being forced into a disorderly and highly disruptive exchange rate adjustment.

I. BACKGROUND

1.   Policymakers in Lebanon are considering a shift away from the FX subsidy for imports of critical and essential goods, towards direct transfers to households. The decision to remove the FX subsidy for imports of critical goods and essential food and other items (henceforth referred to as essential items) should be based on the most efficient and cost-effective use of pro-poor public spending. The subsidy concerns imports of critical goods—energy, medicine, wheat—and essential items (as identified by the Ministry of Economy and Trade, MoET). The estimated cost of the subsidy amounts to a monthly average of US$287 million (Table 1).[2] Maintaining the current subsidy scheme accelerates the steady depletion of FX reserves at the central bank (BdL) and reduces the time available to undertake reforms to avoid a forced and disorderly adjustment of the exchange rate. On the other hand, the subsidy prevents, in the very short-term, the prices of these products from increasing, which would exacerbate inflationary-depreciation pressures. The question policymakers ought to consider is: can a cheaper and more effective compensation scheme be immediately implemented to both protect poor and vulnerable households, and gain some time to protect the official exchange rate until a comprehensive set of policy reforms that are consistent with a stable macroeconomic framework can be introduced?

II. MACROECONOMIC CONSIDERATIONS

2.   As it stands, half of the cost of the FX subsidy is directed toward energy items, which are regressive in nature. Higher-income earners are more likely to consume more fuel, and thus profit more from the subsidy. The gains associated by implicitly subsidizing road transport are not distributed fairly; by income, the poorest 20 percent of the population receives only 6 percent of the subsidy, while the richest 20 percent receives 55 percent.[3] Finally, low fuel prices encourage over-consumption, adding to

---

[1] This note was prepared by a World Bank team at the request of the Government of Lebanon. It is based on a series of discussions with H.E. Minister Raoul Nehme (Minister of Economy and Trade) and his team and largely incorporates the outcomes of these discussions. The World Bank team was led by Haneen Sayed and Wissam Harake and includes: Yashodhan Ghorpade, Christos Kostopoulos, Mohammad Al-Akkaoui, Nadine Chehade, Ugo Gentilini, Ahmet Fatih Ortakaya, and Khalil Dagher.

[2] This is distinguishable from the total value of the subsidy, which amounts to an estimated US$ 437 million per month.

[3] UNDP, 2015, "Fossil Fuel Subsidies in Lebanon: Fiscal, Equity, Economic and Environmental Impacts."

negative environmental and health externalities—namely, local air pollution, congestion, accidents and roadway wear and tear. Hence, there is a socio-economic benefit in replacing the regressive portion of the subsidy with a targeted, and therefore cheaper, transfer program.

3.   Inflation is a highly regressive tax, disproportionally affecting the poor and vulnerable, and more generally, people living on fixed income like pensioners. This is especially so in Lebanon's case where key basic items of the consumption basket are primary drivers of overall inflation, which has reached 136.8 percent in October (latest available). In fact, the average year-on-year (yoy) inflation rate over the first 10 months of 2020 (10M-2020) for food and non-alcoholic beverages was 222.6 percent, while that for clothing and footwear was 245.6 percent, and 331.5 percent for furnishings and household equipment.

Table 1. Cost of FX import subsidy and impact of its removal

Product	Estimated 2020 Consumption[1] ($, mlns)	Subsidized Exchange Rate[1] (LL/S)	% Subsidized[1] (%)	Subsidy in Value[2] ($, mlns)	Cost of Subsidy[3] ($, mlns)	BoP Impact due to Estimated Reduction in Demand[4]		
						High Elasticity ($, mlns)	Low Elasticity ($, mlns)	Low Elasticity- High Passthrough ($, mlns)
Fuel EDL	1,000	1,515	90%	900	661	NA	NA	NA
Gaz (LPG)	110	1,515	90%	99	73	80	39	66
Mazout	1,195	1,515	90%	1,076	790	867	418	717
Other fuel	1,070	1,515	90%	963	707	776	375	642
Medication/ supplies	1,300	1,515	85%	1,105	811	1,067	455	780
Wheat	150	1,515	90%	135	99	57	57	96
Essential items	960	3,900	100%	960	303	367	367	612
Total	**5,785**	**1,911**	**91%**	**5,238**	**3,444**	**3,213**	**1,710**	**2,913**

1 Source: Ministry of Economy and Trade (MoET)

2 Calculated as: (estimated 2020 consumption) * (the subsidized exchange rate)

3 Calculated as: [(the average black market exchange rate - the subsidized exchange rate)/ (the average black market exchange rate)] * (subsidy in value)

4 Calculated as: (estimated 2020 consumption) * (percentage change in demand per selected scenario per product)

Average black market exchange rate in 2020 is assumed at 5,700 LL/US$

4.   Lebanon's sudden stop in capital inflows has implied a steady depletion of FX reserves at BdL, notwithstanding the introduction of informal capital controls (Figure 1). As of end-October 2020, BdL's gross foreign asset position reached US$25.4 billion, declining by US$11.8 billion since end-2019. The gross position, however, differs widely from its net reserves (i.e. FX reserves at the central bank net of FX liabilities to others).[4] BdL's gross position includes US$5 billion in Lebanese Eurobonds, an unpublished amount lent out to banks since October 2019, and required reserves on banks' customer FX deposits (estimated at US$17 billion).

5.   BdL officials have warned that falling FX reserves will force the central bank to halt its support for imports of critical goods and essential items at lower exchange rates. The officials indicated that in the next few months BdL's FX reserves will drop to the level of the Required Reserves on banks' customer FX deposits. Should BdL abandon its support for imports of critical goods and essential items (i.e., including energy products, medicine and food essentials), importers will be forced to fully revert to the dollar-note market rate[5] for the needed hard currency. New imports would thus be priced at the going dollar-note rate, exacerbating inflationary pressures and potentially stoking an inflationary-depreciation spiral. In fact, in anticipation of higher prices, importers, retailers and customers are already hoarding critical and essential goods, bringing forward price and volume implications.

6.   Demand effects resulting from the removal of subsidies are a key factor for an impact on the balance of payments (BoP). In principal, the absence of demand effects, dragged by the fall in income and increase in prices, would leave the BoP unchanged by the removal of subsidy. To estimate the impact

---

[4] BdL, contrary to other central banks, does not publish net reserves.

[5] This refers to the street market access to dollar notes, which has depreciated the Lira by up to 80 percent.

on demand, we use country specific, product-based, income and prices elasticities of demand as presented in Seale *et al* (2003).[6] Notably, the study finds that energy products and medical care are generally elastic for most countries, including in Lebanon; that is, if consumers' incomes decline by half, or if product prices increase by 50 percent, then demand for these products declines by half or more. Meanwhile, demand for food items are relatively inelastic; that is, if consumers' incomes decline by half, or if product prices increase by 50 percent, then demand for these products declines by less than half.[7] We shall preclude from our simulations Électricité du Liban (EDL) due to the company's obvious deficiencies, specifically, the severe and chronic shortages in power supply and tariff regulations, which distort the impact on demand. Further, there is uncertainty regarding the elasticities for these consumption goods in the Lebanese economy. Specifically, other literature suggest that energy products and medical care are inelastic goods.[8] For robustness, we also re-run simulations based on relative in-elasticities of energy products and medical care.[9] We shall henceforth refer to simulations based on Seale *et al* (2003) as *High Elasticity Scenario*, and those that assume the inelasticity of energy products and medical care as the *Low Elasticity Scenario*. We proceed by (i) assuming that income contracts by 20 percent across all scenarios; and (ii) simulating two scenarios for product price increases: a 50 percent increase in prices of energy products, medicine and food items, and a 100 percent increase (dubbed the *High Passthrough*). Hence, we present three scenarios:

1. *High Elasticity Scenario*: a high elasticity scenario that assumes a 20 percent contraction in income and a 50 percent increase in prices of energy products, medicine and food items;

2. *Low Elasticity Scenario*: a low elasticity scenario that assumes a 20 percent contraction in income and a 50 percent increase in prices of energy products, medicine and food items;

3. *Low Elasticity-High Passthrough Scenario*: a low elasticity scenario that assumes a 20 percent contraction in income and a 100 percent increase in prices of energy products, medicine and food items.[10]

7. **Removal of subsidies on imports of critical goods and essential items can lead to some BoP relief.** The sharp declines in consumption of the subsidized products translate into BoP relief; all three scenarios suggest improvements to the BoP, ranging from US$1.7 to US$3.2 billion depending on the scenario (Table 1).

8. **Based on the above, the removal of subsidy can meaningfully extend the time-till-exhaustion of remaining BdL reserves, thus delaying a forced and disorderly exchange rate adjustment.** Capital flow restrictions in and out of the country has induced a more direct trade-off between the stock of FX reserves at BdL and the import bill. As a result, the BoP relief expressed above will reflect on the foreign exchange reserves at BdL. We stress that the improvement in the BoP position and the extension of reserves are temporary and come at the expense of worsening economic activity and declining standard of living.

9. **As a result of subsidy removal, inflationary pressures would materialize via direct and iterative effects**. Through the direct effect, the inflation rate would increase as prices for critical goods

---

[6] James Seale, Anita Regmi and Jason Bernstein (2003), *International Evidence on Food Consumption Patterns*, United States Department of Agriculture, Electronic Report from the Economic Research Service.

[7] Specifically, according to Seale et al. (2003), income elasticities of demand for Lebanon are 0.632 for food, beverage and tobacco, 1.2 for gross rent, fuel and power, and 1.357 for medical care. The authors also present price elasticities of demand for Lebanon, which are -0.511 for food, beverage and tobacco, -0.971 for gross rent, fuel and power, and -1.098 for medical care.

[8] Accurate elasticities can be derived from more recent and comprehensive Lebanese household surveys which are not available.

[9] Toward that end, we assume income (price) elasticities of demand for Lebanon to be 0.5 (-0.5) for gross rent, fuel and power and 0.5 (-0.5) for medical care.

[10] Here we omit a *High Elasticity-High Passthrough* scenario that assumes a 20 percent contraction in income and a 100 percent increase in prices of energy products, medicine and food items. The reason is that when price elasticity of demand is at or lower than -1, a 100 percent increase in prices would wipe out demand, which is not a realistic outcome.

and essential items reflect the higher dollar-note exchange rate.[11],[12] Additionally, an iterative effect arises from an increased demand for dollars in the dollar-note market, which further depreciates the currency, fueling inflation. With surging inflation, demand for narrow money increases, which, if BdL meets by a corresponding increase in money supply (as is currently the case), would lead to exacerbated pressures on the exchange rate. Moreover, under panic conditions, inflation and exchange rates are key observables that drive sentiment, and their deterioration re-enforces the inflationary-depreciation cycle.[13]

10.   Removing the subsidy is estimated to increase inflation through the direct effect by 24 percentage points. (Figure 2).[14] This inflationary impact is frontloaded, hitting hardest the first months and diminishing over the course of the year. We caveat that this does not account for the impact on inflationary expectations and other related iterative effects, which are likely to be forceful dynamics. The inflation results are generated from an estimated Average Exchange Rate (AER)[15] and an exchange rate pass through effect on prices of about 50 percent[16] applied to the following two scenarios: (1) a hypothetical continuation of the FX subsidy through 2021, which we will refer to as the *Status Quo Scenario*;[17] and (2) a full termination of the FX subsidy on January 2021, dubbed the *Sudden Stop Scenario*.[18]

Figure 1. A steady depletion in the gross foreign exchange position at BdL.
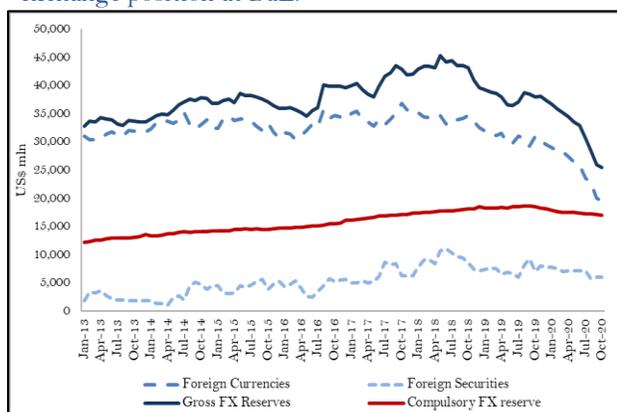
Sources: WB staff calculations based on WDI data.

Figure 2. Upon removal of FX subsidy, direct effects on inflation are substantial.
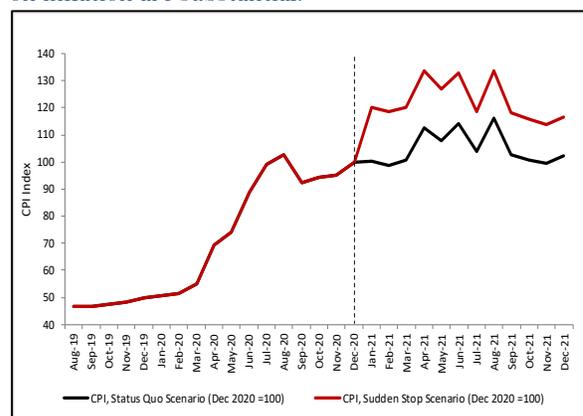
Sources: WB staff calculations based on WDI data.

---

[11] We note that energy products are final and intermediate goods, and changes to their prices impose economy-wide effects.

[12] While this will naturally reflect on volumes imported—since consumers will cut down on purchases, and there will be some substitutional effects for food products that can be manufactured locally (a process likely ongoing)—being critical goods, they will still be demanded in substantial volumes.

[13] There are also stock implications, whereby high inflation imposes a wealth effect via transfers from creditors to debtors; *ceteris paribus* borrowers would owe less—and hence, creditors would receive less—in real terms than what was determined at the time the contract was signed. Consequently, public debt denominated in local currency would be worth less in real terms, providing a fiscal benefit.

[14] We note that this estimation does not take into consideration the iterative effects, which can potentially drive an inflation-depreciation spiral.

[15] The average exchange rate is calculated using consumption-based weights applied on multiple exchange rates, specifically, the official exchange rate, the platform rate at BdL and the bank-note market rate. For further details on the AER, please refer to: The Lebanon Economic Monitor, Fall 2020, *The Deliberate Depression.*

[16] The exchange rate pass-through rate on inflation is calculated by first dividing the inflation rate by the AER depreciation rate for the same month and multiply by 100. This generates a series of pass-through rates for the time period August 2019 to September 2020, which we averaged out. The estimated exchange rate pass-through rate will likely change as more actual data are populated.

[17] This scenario is used for illustrative purposes and is not a likely option. Sharply falling FX reserves at the central bank precludes the option of continued support for the full list of critical goods and essential items.

[18] The Sudden Stop Scenario assumes (i) the subsidy is eliminated on January 2021; and (ii) the dollar-note exchange rate deteriorates to LL 10,000 per US$ by January 2021, stabilizing thereafter.

11.   **The Government of Lebanon (GOL) needs to prioritize a comprehensive, consistent and credible macroeconomic stabilization plan, the fiscal part of which should include a social safety net (SSN) component.** Given Lebanon's rapidly and continuously deteriorating macroeconomic conditions, a social safety net by itself will be insufficient, and indeed, as shown above, can trigger additional macroeconomic risks. Lebanon needs to incorporate SSN into a macroeconomic stabilization strategy that prioritizes the arrest of hyperinflation, currency depreciation and proliferation of multiple exchange rates. This strategy would be based on: (i) a debt restructuring program toward achieving debt sustainability over the medium term and fiscal space over the short term; (ii) a comprehensive financial sector restructuring toward regaining solvency of the banking sector; (iii) a new monetary policy framework aimed at regaining confidence and stability in the exchange rate; (iv) a phased fiscal adjustment aimed at regaining confidence in fiscal policy; (v) growth enhancing reforms; and (vi) enhanced social protection.

III. DESIGN OF BROAD-COVERAGE SUBSIDY REFORM COMPENSATION SCHEME

12.   **Governments often use generalized subsidies as a tool to lower the cost of living for poor households and to shield households from price fluctuations – hence Lebanon is not alone in this approach.** However, subsidies are a blunt and inefficient instrument, and some are regressive benefiting the rich more than the poor. International experience shows that a shift from generalized subsidies to direct support to the poor could result in an improvement in public welfare.[19]

13.   **The subsidy reform being considered by the GOL aims to replace implicit FX subsidies for fuel, medicines, wheat and essential items with direct cash transfers to Lebanese resident households**. The direct cash transfers should offer some compensation to households to purchase items at market prices (which will increase following the withdrawal of subsidies as shown above) and should not be restricted in their use (allowing greater autonomy and a dignified freedom of choice on the best use of assistance while offering compensation for the anticipated increase in prices).

14.   **As the withdrawal of FX subsidies will result in a considerable price shock[20] that will be felt by large sections of the population, the compensation program proposed is of a 'broad coverage' nature[21].** In year 1, the broad-coverage subsidy reform compensation scheme (Broad Coverage -Cash Transfer) could aim to cover approximately 80% of the Lebanese population. To ensure progressive coverage, the BC-CT will seek to exclude the top 20% of the population as they are better able to absorb the price increases and can afford to pay for the currently subsidized items at market price. The broad coverage approach would involve identifying and excluding the top 20% of the population (in terms of income/economic wellbeing) and covering the remaining 80% of the population. Unlike traditional poverty-targeted programs that seek to identify the poor (bottom 10-40%, depending on the country), in this case, the identification of the richest 20% would be based on affluence tests (i.e. markers of affluence to identify the ineligible) such as asset filters, dwelling ownership and characteristics, and formal incomes. Preliminary analysis undertaken by the World Bank points to the potential use of indicators such as number of rooms/bathrooms per household member, dwelling area per household member, and thresholds for wage and other formal income for such an affluence test. Implementing such an approach would require careful integration of data across multiple databases to ensure reliability and automation of eligibility decisions. In subsequent years, as the population adjusts to the new (market) prices for the currently subsidized items and as economic recovery begins, the coverage of this compensation program may be progressively reduced, along with the level of benefits (per adult and per child) to ensure a smooth

---

[19] Ruslan Yemtsov and Amr Moubarak "Assessing the readiness of Social Safety Nets to Mitigate the Impact of Reform"; World Bank Good Practice Note 5.

[20] Especially as higher fuel prices will lead to increases in prices of several other goods and services.

[21] Covering the majority of Lebanese households though not attempting universal coverage.

phasing out of the compensation program that dovetails with more sustainable and assured financing for a targeted safety net program that covers around 30% of the population over time.

15.   **We specifically analyze one proposal of a benefits scheme** under which Lebanese adults (age 23 and above) receive US$50 per month in year 1 of the compensation program, US$40 in years 2 and 3, and US$30 in years 4 and 5. Children get half this amount, and the coverage progressively declines from 85% in the first six months, to 75% in the next six, and 70%, 60%, 45% and 30% for the next 4 years, respectively (Figure 3).

Figure 3. Proposed Monthly Benefit Amount (US$), and Coverage (%), by Year
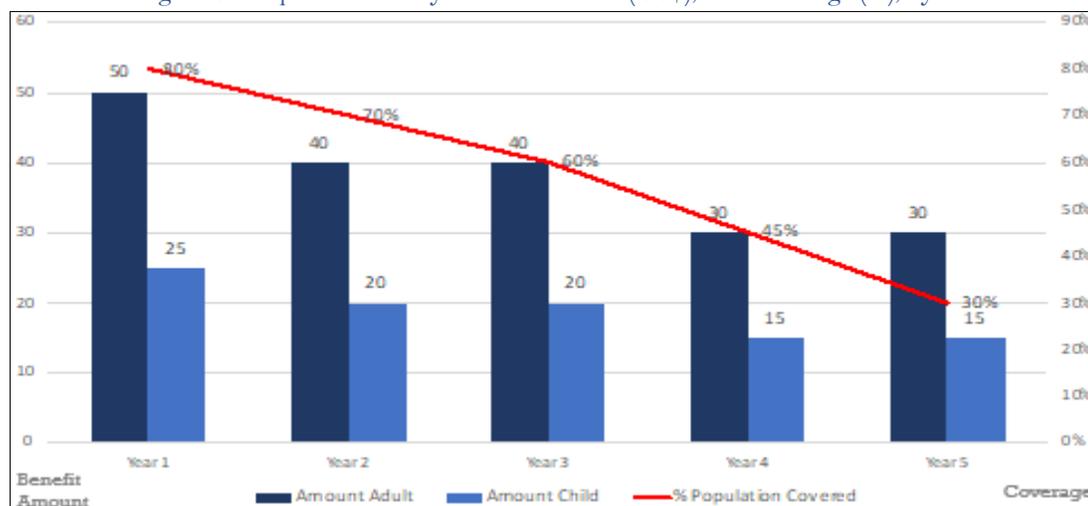
16.   **The scheme described represents compensation equivalent to 41% of the average Lebanese household's monthly consumption expenditure** in Year 1, 28% in years 2 and 3, and 21% in years 4 and 5, reflecting a substantial level of support to recipient households (compared to most unconditional cash transfer programs in upper-middle income countries that provide 22% of beneficiary welfare).[22]

17.   **One option we model is a phased approach to subsidy removal:** Phase 1 is removal of FX subsidy for the MOET essential items and fuel (except for EDL) to take place on January 2021. Phase 2 is removal of fuel subsidy for EDL along with a reform of EDL's pricing reform to take place on Jan 2022. Phase 3 is removal of medication subject to broad medical coverage for Lebanese citizens to take place on January 2023. Figure 4 shows the required outlay of the program and the resulting savings viz. Phase 1 of the removal of subsidies. The budgetary outlays start at US$1.5 billion in year 1 (80% coverage) and decline to US$311 million in year 5 (30% coverage); equivalent to an average annual expenditure of around US$779 million. The removal of phase I subsidies and the introduction of the cash transfer compensation as described will result in a net savings of an average annual value of around US$2.6 billion over the 5 years period.[23]

---

[22] World Bank (2018) The State of Social safety Nets 2018. Washington DC: The World Bank.

[23] These savings do not account for administrative costs of implementing the compensation program

Figure 4. Compensation Program Outlay and Net savings from Phase I Subsidy Withdrawal, US$ Mn

18. **BC-CT financing options and associated risks necessitate a credible medium-term macroeconomic framework.** In principal, financing options for the BC-CT include: (i) money printing by the central bank (i.e. monetization); (ii) budgetary allocations; and (iii) international assistance.[24] In light of BC-CT's large financing needs, monetization risks exacerbating in significant ways current macroeconomic conditions, further entrenching macroeconomic instability. This option will lead to further deterioration in monetary conditions, potentially stoking the afore described inflationary-depreciation effects. Alternatively, fiscal financing via additional (unfunded) budgetary allocations would not be qualitatively different from the monetization option; currently, the fiscal deficit is *de facto* monetized. The previous two options are also likely to preclude effective international assistance (option iii), which can only be a part of a credible medium-term macroeconomic framework. As mentioned above, this framework should include: (a) a debt restructuring program toward achieving debt sustainability over the medium term and fiscal space over the short term; (b) a comprehensive financial sector restructuring toward regaining solvency of the banking sector; (c) a new monetary policy framework aimed at regaining confidence and stability in the exchange rate; (d) a phased fiscal adjustment aimed at regaining confidence in fiscal policy; (e) growth enhancing reforms; and (f) enhanced social protection (i.e. the BC-CT program).

IV. IMPLEMENTING BROAD-COVERAGE SUBSIDY REFORM COMPENSATION SCHEME

19. **Delivering a broad-coverage cash transfer (BC-CT) scheme requires careful design, transparent implementation, and adequate financing.** It involves the following broad steps: (i) consultations and communications; (ii) identification and beneficiary selection; (iii) payment of benefits; and (iv) monitoring and grievance redress mechanism (GRM). These are explained below.

(i) Consultations & communication

20. **A well-prepared communication and out-reach campaign must precede and accompany the subsidy reform program**. International experience demonstrates that well-planned and consistent communication is critical for successful subsidy reforms. In Jordan, for example, a widely cast and well-designed communication strategy played a crucial role in addressing uncertainties and managing expectations during the 2008 and 2011/12 subsidy reforms. Making an effective use of available channels to project transparency, clarity on the role of the program, public information on objectives, operational rules, and results are necessary to tackle information asymmetries and concerns of different stakeholder. Bringing in different stakeholders in the design of the program would enrich the scheme and its

---

[24] For illustrative purposes here, we assume each of these options are utilized exclusively, when in practice there are financing modalities that use combinations thereof.

acceptability. Reforms can succeed only if an informed public accepts and supports the reform's rationale. Clearly communicating who will be impacted, and how, is vital to generate public buy-in.

(ii)   Identification and Beneficiary Selection

21.   The BC-CT scheme would aim to cover the Lebanese population residing in Lebanon only (which refers to individuals who spend at least 183 days in the country). The program is proposed to involve a simple mobile-based registration (self-declared information) to be filled by the applicant. No household visits will be undertaken. The program will require ownership of a National ID[25] (NID). Individuals who do not have a NID will be required to obtain a NID before registering. The program should provide two different registration options: (i) online through citizen interface (for individuals who can access the internet[26]) or (ii) physical visit to one of the registration sites which could include the LibanPost, and the Social Development Centers (SDCs), or the use of registration trucks. Each entry point will use the same "basic delivery system" accessible through a mobile compatible citizen interface. A selfie-based registration will be utilized for onboarding to the program[27]. During the registration, additional information will be requested to exclude well-off segments of the population.

22.   The exclusion criteria will be based on a phased approach whereby in Phase I basic demographics and information on income and assets will be collected for immediate exclusion. Households who pass the eligibility for Phase I will be onboarded and start receiving the benefits based on their preferred payment modality (see payment section). Phase II exclusion will be a recurrent process and will commence 3 months after the onboarding. Detailed demographics, information on employment, the value of assets and ownership, etc. will be collected at Phase II for exclusion purposes. The program should construct interlinkages with other governmental databases at Phase II depending on technical availability and IT infrastructure. A call center and a back-office team need to be built to undertake random spot checks (up to 3-5% of beneficiaries) to decrease potential fraud and/or under/misreporting (which would be communicated via a set of outreach & communication activities). The back-office team will also manage program GRM to ensure fairness, transparency, objectiveness, and accessibility.

(iii)   Payments Mechanism

23.   Upon registering to the program, applicants will be able to choose their preferred payment modality among the options currently available in the Lebanese market, namely receiving funds: (i) on an individually or jointly held bank account, 58% of Lebanese residents being banked;[28] (ii) on a physical or virtual banking card, with funds redeemed at automated teller machines (ATMs), or digitally spent for purchases on point-of-sale (POS) devices; or (iii) in LBP physical notes, with funds redeemed through money transfer operators (MTO) agents and/or LibanPost offices. Other payment modalities, including mobile wallets, can be added once available in the market. The GOL will send the payment orders to the financial institution(s) based on the applicants' preferred payment choice. Giving recipients the choice of the financial service provider often improves customer experience by incentivizing providers to offer the best services, while allowing governments to cut on costs and avoid lengthy procurement processes.[29] For recipients opting to receive physical notes, identification information, including biometrics where possible, will be used for authentication at disbursement time, hereby ensuring that the applicant and whomever is redeeming the funds are the same person.

---

[25] Initial assessment indicates that 78% of the Lebanese population have NIDs, World Bank Technical Mission for a Digital Transformation Project, ID4D, Sept 2019.

[26] Share of population who uses internet is 75.9% (penetration rate), Internet usage, Broadband and Telecommunications report by Internet World Stats, 2016

[27] For each HH member, a photo of the NID and a selfie will be taken to create a user profile in the system. Please note that this option is only valid for polycarbonate type of IDs

[28] Financial Inclusion Demand Side Survey Report, BDL, 2018.

[29] The Future of G2P Payments: Expanding Customer Choice, CGAP, 2019.

24. **It is important to note that the payment mechanism depends on whether GOL opts for a restricted or an unrestricted use of funds.** The above applies to an unrestricted use of funds, whereby recipients can spend the funds without any condition, be it digitally or in physical notes. It is not possible to use transfer to bank accounts as a payment modality in case of funds are restricted in their use.

(iv)   Monitoring & GRM

25. **An effective Grievance Redress Mechanism (GRM) and an effective monitoring system is critical for the success of any social safety net program and for establishing channels of trust with the communities.** A back-office team needs to be put in place to manage appeals, complaints, data updates, etc. through a GRM module.

V. COMPLEMENTARITIES BETWEEN BC-CT PROGRAM AND OTHER SSN PROGRAM

26. **The main targeted SSN program in Lebanon is the National Poverty Targeting Program (NPTP) which is being scaled up.** The scale up will be financed through a US$246 million World Bank supported Emergency Crisis and COVID-19 Response Social Safety Net Project (ESSN) and support from donors. The ESSN aims to provide cash transfers and access to social services to 147,000 extreme poor and vulnerable Lebanese households (approximately 20% of the population), as well as top-up cash to 87,000 children ages 13-18 who are at risk of dropping out from schooling. In addition, funding from donor partners will support an additional 50,000 households reaching in total of 200,000 of the poorest households – i.e. 27% of the Lebanese population.

27. **While the BC-CT and the ESSN have similarities and can both be considered types of SSN programs, they have different (albeit related) objectives and could be run in parallel.** The BC-CT is a compensation for subsidy reform aimed to the general public and likely will be temporary and time-bound. The NPTP/ESSN is a long-term sustained SSN program aimed at protecting extreme poor households facing multiple crisis. The two programs, which can carefully be run in parallel, are complementary to each other with gradual dovetailing over the next 4-5 years, especially as the necessary delivery systems are developed. The BC-CT program is likely to be financed by GOL and will entail a gradual reduction in coverage over 5 years. By year 5, the level of coverage would be in line with a sustainable GOL-financed social safety net program as the current crisis subsides. The 4-5-year horizon will also enable a smooth (rather than abrupt) reduction of coverage, as well as the establishment of a fully functional SSN delivery system (including social registry, GRM, payments system). The proposed timeframe is also suitable for the transition to a new macroeconomic framework to settle in and support an adequate and robust social safety net.