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In this edition

- Editorial: Putting International Goodwill to Good Use ........................................ 3
- President Wolfowitz’s Statement at Paris III – the Lebanon Donors Conference ................................................................. 4
- World Bank Grants, Technical Assistance and Human Resources Flow into Lebanon .......................................................... 6
- Economic Developments in 2006: War and Politics Undermine Positive Prospects ................................................................. 9
- Economic and Social Impact Assessment: From Recovery to Sustainable Growth ................................................................. 14
- Conflict-Hit Municipalities Awarded US$30 Million Grant ............................................................................................... 17
- Bank Group Operations ......................................................................................................................................................... 19
- News, Recent and Upcoming Activities ...................................................................................................................................... 22
- Recent World Bank Publications ............................................................................................................................................ 24
EDITORIAL

Putting International Goodwill to Good Use

Last summer’s hostilities cost Lebanon dearly - tragic human loss and enormous physical destruction dealt a severe blow to a promising tourist season and economic revitalization. Indeed, the hostilities created an enormous need for reconstruction, but Lebanon proved once again its great ability to surmount difficulties.

The speed and quality of Lebanon’s post-war emergency relief earned considerable respect and admiration from the international community. At the Stockholm conference, donors generously contributed to Lebanon’s Emergency Reconstruction bill, and later, at the Paris III conference, the Government attracted an impressive US$7.6 billion to support its Reform Program.

Fortunately, the Government is now in the process of revising its public procurement laws to remove opportunities for corruption, to introduce fair competition and reduce costs. The problems in the existing system reflect a need for modernization.

These are but a few examples of the international resolve to help put Lebanon back on a path of social and economic recovery.

The Government of Lebanon displayed high-level credibility on the emergency reconstruction front, completing a mammoth reconstruction task in a record 10 weeks. Power and water supplies were restored, the displaced were given shelter, road networks were repaired and schools were readied for the academic year.

The challenge now is more complicated: Lebanon has to meet its own reform commitments. This process could start with a few modest steps – a core reform program which the entire donor community stands prepared to support. Inaction would deal a serious blow to Lebanon’s ability to return to a path of recovery and would damage its credibility. It is critical now to make good use of international goodwill.

Under current conditions, it is unrealistic to aim for a complete and quick overhaul of Government finances and administration. Still, there are areas where reform measures with significant impact on the daily lives of its citizens can begin.

Social protection is one such area open to improvements on all levels. The Government, its citizens and political rivals could coalesce around a program for better services for Lebanon’s citizens and lower costs to Lebanon’s Treasury.

Win/win situations are attainable. One such example is the National Social Security Fund (NSSF), which boasts more than 450,000 subscribers, reaching 1.5 million beneficiaries. There are signs that the Government and the NSSF are moving towards revamping the institution and improving services. The Government has paid some of its debt to the NSSF in exchange for promises of internal reforms in the institution. This is a promising, quick-fix first step, which could be rapidly developed into wider solutions and replicated in other institutions to avoid losing momentum.

Another area the Government has begun to tackle is the power sector. Launching this process need not await political breakthroughs. The last three Governments saw Ministers of Energy coming from divergent political backgrounds backing almost identical solutions, irrespective of some differences in implementation details. Electricité du Liban (EDL) is responsible for many of Lebanon’s economic, fiscal, environmental and social problems. EDL is costing the country over US$2 million per day in subsidies, while charging the consumer the highest tariffs in the region. There is no quick fix, but specific steps have been agreed and have begun to fix the problem.

The citizens of Lebanon are grappling with day-to-day challenges that range from health and education bills, poor water, power and sanitation networks, a degrading environment and a scarce job market. Practical steps (not more studies to talk about) by individual ministries can now begin and can make a real impact. They would at once offer relief at home and leverage the goodwill of Lebanon’s many friends in the international community.

In this issue of the Update, the editorial team brings to its readers details of the World Bank’s involvement in post-crisis Lebanon. We also regret the delay in publication, which was caused by the hostilities and the subsequent engagement of the World Bank Country Team in its post-conflict assistance to Lebanon.
President Chirac, Prime Minister Siniora, Secretary General Ban Ki-Moon, President Barroso,

Lebanon today stands at a critical crossroad. After a long and costly civil war, Lebanon had managed — against great odds — to begin the transition from violence to reconstruction and development.

That effort encountered many challenges and a number of severe shocks. Nevertheless by July 2006, much had been achieved. Macroeconomic and fiscal indicators were improving. There was solid growth and demonstrable fiscal discipline.

But then came the war of last summer which inflicted enormous damage on Lebanon’s society and economy, along with terrible human suffering. That brought the positive trends to a halt and compounded existing challenges.

On top of the human tragedy — hundreds killed, thousands wounded — the war imposed a great burden on an already fragile economy. About US$2.4 billion in direct damages plus another US$700 to US$800 million in indirect damages.

Instead of the 6 percent growth that had been projected for 2006, the economy declined by 5 percent.

Even worse, the war caused incalculable damage to the fabric of a civil society known for its vibrant energy and enterprising spirit.

Up to 120,000 people lost their jobs, and now face the risk of sliding into poverty.

One million people were displaced at the height of the hostilities – one-quarter of the population of Lebanon.

About 200,000 people emigrated during the hostilities, many of them young and highly skilled.

The good news is that Prime Minister Siniora and his government have shown strong leadership in rebuilding from the devastation of war. In the first six months, substantial progress has been achieved in providing financial assistance to those most affected – repairing infrastructure, opening schools, and cleaning up environmental damages.

But as the Prime Minister also noted, Lebanon’s needs go beyond reconstruction. Lebanon now seeks our help to realize the hopes and dreams of its people, and its potential as a positive force in a troubled region.

To steer Lebanon back to the path of recovery, the Government of Lebanon has presented to us today an ambitious, comprehensive and coherent reform package. It addresses three critical agendas:

i. structural reforms to stimulate growth;
ii. fiscal adjustments to raise revenue and promote the efficient use of public resources; and
iii. third – critical for the success of the first two elements – social safety nets, special programs targeted to the poorest and most vulnerable, to ensure that they do not suffer unfairly and that they share in the benefits of reforms.

Restoring Lebanon’s economy cannot happen overnight. And it cannot be achieved by one individual or group. To reach its ambitious, but achievable goals, Lebanese society as a whole must equitably share the benefits and the burdens of these reforms.

We commend the Government on its preparation of detailed action plans for specific sector reforms, critical to successful program implementation.

We particularly welcome the announcement that the Government of Lebanon has invited the IMF to provide an Emergency Post-Conflict Assistance program. This will help give confidence to both Lebanese and international stakeholders that the program is on track and that the Government is moving forward. This vote of confidence is essential.

There is no question that the challenges that lie ahead are formidable. But the opportunities too are enormous. The greatest burden falls on the government of Lebanon to implement its ambitious reform program. But this is our chance as donors to help Lebanon succeed. Success in this effort will benefit all people of Lebanon and the region as a whole. None of us can afford the price of failure.
The World Bank Group has made an extraordinary effort to increase our support to the people and government of Lebanon during this critical period.

For our staff working on Lebanon, their work is much more than just a job—it is a mission that they approach with passion and commitment and it makes me proud, as head of the World Bank Group, to be associated with them. Immediately after the truce, staff who had been evacuated returned to Lebanon to work with the Government to assess the situation and lay the foundation for long term development.

An Economic and Social Impact Assessment of the hostilities was conducted in close collaboration with the Government, the private sector, international donors and other stakeholders. This assessment, completed in November, is a critical input to the latest reform package.

On the financing front, the World Bank Group is providing support in three areas:

First, we have taken the unprecedented step of providing grants from World Bank Group income. US$70 million in grants have been contributed for recovery and reconstruction efforts, and to support reforms in the power sector. An additional US$1 million grant has been made available to improve the Government’s ability to manage funds for reconstruction projects transparently and efficiently.

Second, the IFC—the private lending arm of the World Bank Group—will provide US$250 to US$275 million in financing for Lebanon’s financial and business community, including a guarantee program for small and medium-sized enterprises and a trade finance facility.

We are now also ready to extend up to US$700 million in IBRD financing to support the implementation of the Government’s program, particularly its efforts to stimulate growth and to meet the needs of the poorest and most vulnerable elements of the population. We expect that a significant part—up to US$400 million—of that amount can be made available in 2007, initially to support sector reforms, especially the power sector.

This package of World Bank Group financial assistance—totaling more than US$1 billion—exceeds our earlier plans, and is part of a comprehensive and extraordinary international effort. That reflects our assessment that the program in front of us merits exceptional support because it addresses boldly the fundamental requirements for a strong recovery that benefits all people of Lebanon.

Based on the implementation of the IMF program and sustained donor support over the life of the program, we expect that the capacity of Lebanon to absorb increased levels of finance will be improved, and accordingly we are prepared to consider increasing our assistance over time.

Finally, we are prepared to continue and intensify our efforts in assisting the Government to implement its programs, to build institutional capacity, to improve procurement and financial management to undertake sector reforms, with a particular focus on those sectors such as power, which are key to the overall success of the program.

Lebanon’s need is greater today than ever before—and the international response needs to be greater. We believe our resources—combined with a strong role for the IMF and a robust donor and Lebanese stakeholder response—can serve as an important catalyst to put the country back on the path to strong recovery and sustainability.

Ladies and gentlemen,

The people of Lebanon have called on the world to help revive their economy. We have an opportunity now, after the tragic events of last year, to restore hope and stability that the Lebanese people and their children so deeply deserve.

They have presented us with the first ever comprehensive plan that could bring jobs, education, safety nets and a better future within the reach of every citizen.

Now it is up to us to do everything we can to help Lebanon realize its great potential not only as an economic model but also as a model of diversity for the whole region.

When I was in Indonesia recently, a Muslim cleric pointed me to a wonderful saying from Surat Al Hujurat in the Holy Quran: ‘I have created you nations and tribes so you may know one another.’ The region needs more of that understanding and this conference today gives us all the opportunity to contribute to that goal.

Let me close by thanking the Government of France for convening and hosting this conference and thanking the Government of Lebanon for giving us all the opportunity to participate in an undertaking of great importance and potential benefit for all.

Paul Wolfowitz
President
World Bank Group
The World Bank has pledged US$700 million in financing for Lebanon over the next three years. This is the World Bank Group’s contribution to International Support to Lebanon which was pledged at the Donor Community’s conference in Paris on January 25, 2007.

This issue of the Update highlights Bank activities several months after the end of the hostilities.

**Background**

Even before the cease-fire took effect, the Country Office launched a quick assessment of the impact of the hostilities on the six projects that were under implementation when the hostilities erupted on July 12, 2006: Ba’albeck Water and Wastewater Project (US$44 million); Community Development Project (US$20 million); Cultural Heritage and Urban Development Project (US$32 million); Education Development Project (US$45 million); First Municipal Infrastructure Project (US$80 million); and Urban Transport Development Project (US$65 million).

All suffered delays in implementation after contractors were forced to abandon the work sites during the hostilities. Fortunately, none of the projects sustained any serious direct damage. Project implementation capacities remained intact, and work resumed under all projects. In short, the assessment found no reason for undue concern, although an extension of the closing date may be required for several projects:

**Examining Government Needs and Constraints**

It was clear from the outset that public finances would be severely constrained by the 34 days of hostilities. In its search for immediate assistance, the Bank swiftly agreed to finance 100 percent of expenditures under all projects, eliminating the Government’s counterpart contribution for a one-year period. The Bank reviewed in detail each project with Lebanese counterparts in order to re-orient activities and geographical coverage, as needed, to respond to the immediate needs of the population.

- **First Municipal Infrastructure Project.** This has been the Bank’s best performing project. The uncommitted funds (US$14 million) have been redirected to finance emergency repairs of municipal infrastructure in areas affected by the hostilities.
- **Community Development Project.** The previously uncommitted funds (US$3 million) are being used to fund about 70 emergency sub-projects through Non-Governmental Organizations (NGOs). Special procedures have been put in place in order to speed up implementation.
- **Cultural Heritage and Urban Development Project.** The uncommitted amount of US$10 million has been re-directed towards small-scale emergency repairs of municipal assets.
- **Urban Transport Development Project.** The funds uncommitted before the hostilities have been allocated to cover unexpected costs associated with ongoing contracts and claims for delays that occurred as a result of the hostilities.

**Assessing the Economic and Social Impact of the Hostilities**

In the wake of the hostilities, shrinking budget revenues and a sharply increasing demand for emergency and rehabilitation assistance exacerbated an already dire public finance situation. Consequently, rather than undertake a typical post-conflict needs assessment, the Government asked the Bank to review the broader economic and social impact of the hostilities on Lebanon’s reform agenda and recommend adjustments.

Against this background, the Bank embarked on an Economic and Social Impact Assessment (ESIA) of the recent hostilities. The ESIA folds a priority reconstruction program into a broader reform program by reviewing, for each sector, the key issues, the broad impact of the hostilities, the Government’s strategy and priority interventions. The ESIA covers 16 sectors in three broad areas: (i) infrastructure (transport, electricity, water, housing, municipal infrastructure and environment); (ii) economic (macro/fiscal, banking, private sector development, trade facilitation, agriculture and irrigation); (iii) social (education, health, pensions, social safety nets,
labor markets); as well as several cross-cutting issues (aid coordination and fiduciary management). The findings are brought together in a synthesis report that places sector reforms and reconstruction activities in the context of a sustainable medium-term fiscal framework. (Please refer to page 14).

Building on Strong Bonds and Experience

Compared with other engagements in post-crisis situations, the World Bank was fortunate in that many of its staff had been working on Lebanon for a long time, had extensive technical knowledge and was familiar with the economic and socio-political context of the country. The ESIA was a major logistical effort involving around 50 staff for a two-month period. The team was mobilized in a short period of time to launch the ESIA in the first week of September.

Support of Other Donors

The ESIA was undertaken in an iterative process with Government counterparts. Throughout, the exercise was closely coordinated with partners to obtain the best sector-specific expertise, including, in particular, the European Commission and UN agencies. A central element of the process was the consultations led by the Ministry of Finance and involving other ministries, the Bank team, donors and UN agencies. These consultations not only improved the quality of the ESIA, but also contributed to Government thinking as it was preparing its own reconstruction and reform program. The ESIA was delivered to the Government at the end of November 2006.

Mobilizing Financial Resources

Given the magnitude of the physical damages, the precarious fiscal situation and public debt dynamics which are expected to prevail over the next few years, the Government indicated to donors its need for grant support. In a gesture that reflects the importance the Bank attaches to Lebanon, the Executive Board of Governors approved, on September 20, 2006, the transfer of US$70 million from the Bank’s surplus to a Trust Fund for Lebanon to support a program of emergency assistance for economic and social recovery. Though modest in comparison to the country’s needs, the amount, provided in grant form, represented a significant Bank contribution compared to other post-crisis countries.

The Government and the World Bank held extensive consultations on the allocation of the grant funds and identified projects that not only help the population cope with urgent needs, but also build on the strengths of the pre-conflict reform program. The two sides agreed to allocate US$30 million to scale up the First Municipal Infrastructure Project, which is being implemented by the Ministry of Interior and Municipalities. This contribution helps restore basic services, finances rebuilding of priority public infrastructure in affected municipalities, supports local economic recovery and development in those municipalities that have suffered the heaviest damage and provides technical assistance and capacity building in municipalities to mitigate the impact of the hostilities on municipal finances. (Please refer to page 17).

Building on historical engagement and expertise in the water sector, the Bank also prepared a US$15 million Emergency Water Supply Project for the western Bekaa’a area, where available water resources cover only 55 percent of present demand. The project will increase the quantity and quality of water supplied to the population. It is expected to be operational in spring, coinciding with a US$5 million technical assistance project designed to support reform in the power sector.

The power sector has been a substantial drain on the Government’s budget for a long time. With the economic devastation caused by the recent hostilities, reform of the power sector has become more critical than ever in order to provide reliable and affordable electricity to the population.

The size of the Trust Fund for Lebanon permits only a modest impact if the Bank’s assistance is unilateral. As such, the Bank is working with other donors to ensure that projects are appropriately resourced and have a discernible, positive effect on the Lebanese population. In this respect, several donors have already joined Bank efforts in the power and water sectors.

International Finance Corporation (IFC)

The extent of damages, tight fiscal constraints and considerable demands on Government implementation capacities have combined to increase demand for inclusion of the private sector in the recovery process. To this end, IFC, the World Bank Group’s private sector arm, developed an emergency recovery program aimed at jump-starting economic activities and assisting the private sector to overcome its difficulties in the aftermath of the hostilities. IFC designed a risk-sharing facility
with local commercial banks using its own resources and funds from the Trust Fund for Lebanon. Activities focus, among others, on housing mortgages and funding small and medium enterprises.

**Setting Up Transparent Financial Monitoring Systems**

The Government had prepared itself well for a swift response once the hostilities ceased. Still, the Government faced a tremendous challenge dealing with the unexpected crisis and ensuing needs. Many players that were new to the country suddenly became active, especially agencies tending to the humanitarian needs of the displaced population and to those caught in the fighting. While the Government of Sweden hosted a donor conference on early recovery in collaboration with UN agencies within just two weeks of the cessation of hostilities, many of the Government’s longer-term needs remained unattended - an occurrence not untypical for a post-crisis country.

The World Bank was able to quickly respond to the Government’s technical support needs in a number of areas where it sought immediate assistance. The Bank approved a US$1 million grant from its Post-Conflict Trust Fund which to help establish an aid reporting system and a delivery mechanism for the Government’s reconstruction program. The grant finances the development of a comprehensive database on aid flows that is tailored to the requirements of the Ministry of Finance and also supports the simplification of procurement and financial management procedures to make Government actions more transparent and effective and, consequently, more attractive to donors.

**Strengthening Human Resources**

In terms of personnel, the Bank seconded two highly experienced staff to the Ministry of Finance for a three-month period. Their task was to help the Ministry, the Prime Minister’s Office and the Council for Development and Reconstruction in two areas: (i) prepare a local reconstruction and development strategy and expedite projects which reinvigorate the local economy in the municipalities affected by the hostilities; and (ii) strengthen donor coordination and programming to mobilize, manage and monitor donor funds that are allocated to various reconstruction and development programs.

Last, but not least, Bank staff specialists have been providing real-time assistance in a wide array of activities, with a particular focus on procurement and policy dialogue.

**Conclusion**

The challenges facing the Government are truly daunting. Indeed, consultations held as part of the Economic and Social Impact Assessment helped identify an almost intimidating list of critical support activities. Yet, the Government has taken specific measures to accelerate the implementation of reconstruction efforts and priority reforms. Mindful of the complex nature of economic and social recovery, donor assistance is needed to support the development of human resources, systems and procedures not just of Government entities, but also of other stakeholders involved in the reconstruction and reform process: local governments, academic institutions, civil society groups, local NGOs, service providers and private sector institutions.
Overview

In the first half of 2006, the Lebanese economy continued to benefit from an exceptionally constructive economic environment. Persistently high oil prices and ample liquidity in the region encouraged capital inflows and transfers to Lebanon, along with tourism, real estate activity, and import demand from Gulf countries. These factors helped sustain the demand for Lebanon’s products and services, offsetting a higher oil-import bill. Following a poor performance in 2005, GDP growth rebounded significantly during the first semester of 2006. Large capital inflows from the Gulf further strengthened the financial situation, and the fiscal deficit shrank by 12 percent thanks to a large increase in revenue collection and slow growth in expenditures.

But the summer 2006-conflict followed by rising political tensions had a significant negative impact on the economy with the result that, despite a strong first half, Lebanon’s economic and fiscal indicators deteriorated for the year as a whole. This is best illustrated by three statistics: (i) GDP growth is estimated to decline by 2.0-5.0 percent in 2006 as compared to a projected increase of 5.6 percent prior to the conflict. This signifies a large 7.6-10.6 percent reversal in output; (ii) the fiscal primary balance registered a deficit of 0.1 percent of GDP in 2006, as compared to a pre-conflict projection of a surplus of 3.0-3.5 percent of GDP. This implies a deterioration of 3.1-3.6 percent of GDP; (iii) the gross public debt increased to over 180 percent of GDP by the end of 2006, adding 5 percentage points to a debt/GDP ratio that was already among the highest in the world. In addition the conflict resulted in serious human and physical losses.

The substantial economic and social damage incurred as a result of the conflict undermined the rising confidence in and early signs of economic rebound and increased the urgency of adoption of a comprehensive reform package to facilitate economic recovery and reform. The Government adopted a reform program, which was presented to the donor community in Paris III Conference in January 2007. The program makes an effort to balance fiscal measures needed for stabilization with structural measures needed for higher growth performance. Participants in Paris III perceived the program to be ambitious and comprehensive, providing US$7.6 billion of pledges (mostly in the form of soft loans for project financing) to support its implementation. Timely implementation of reforms, however, requires a durable political settlement, which has yet to be achieved.

Real Sector Developments

During the first half of 2006, Lebanon continued to benefit from high liquidity in the region, which helped the economy recover from its poor performance in 2005. In the absence of official statistics, national accounts estimates for the first half of 2006 remain tentative. However, all indirect indicators pointed to a significant economic recovery in the first half of 2006 compared with 2005 (when real GDP estimated to grew by 1 percent, against an estimated 6-7 percent in 2004). The growth performance in the first half, if it had continued, would have brought about 5.6 percent real GDP growth for the full calendar year.

The summer-2006 conflict followed by rising political tensions, however, put an end to this recovery. Extensive destruction of physical capital and disruption of trade, tourism, markets and supply channels during July-August affected all sectors of the economy. Real GDP for 2006 is projected to contract by 2.0-5.0 percent. Expressed in real terms, total foregone output due to the conflict could be as high as US$2.2 billion. Moreover, the loss of investor confidence, the damage to the image of Lebanon as a tourist destination and the emigration of skilled workers will have a long-term impact on the health of the private sector and on the economy as a whole. It is estimated that the working force, both resident and non-resident, have declined by 150,000–200,000 workers. The decline in labor supply (as a factor of production) is by itself an indication of depletion in output.

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1 GDP estimates are based on World Bank staff calculations; other figures and estimates reflect combination of World Bank and Government estimates.

2 Based on the simplified Cobb-Douglas equation for output estimation \( Q = A \cdot K^\alpha \cdot L^{1-\alpha} \) where Q is the output, A is the technology, K is the productive capital, L the employed workforce and \( \alpha \) an operator indicating the combination of capital and labor in the productive process) and assuming no change
Several indirect indicators of activity point to a significant slowdown in economic activity. The Coincident Indicator of the Central Bank, which is a proxy for the overall activity, declined by 1.4 percent in 2006 against a 2.2 percent increase in 2005 (Figure 1).

This indicator sharply fluctuated during the year, increasing by 9.9 percent in the first half of 2006 and declining by 11.6 percent in the second half, compared to the same period a year earlier. Similarly cement delivery, which is an indicator of the activity in the construction sector (with about 8 percent share in real GDP), increased by 39 percent in the first six months of 2006 and declined by 6.4 percent in the second half the year—overall registering 12.6 percent increase in 2006, against an 11.4 percent rise in 2005. The evolution of construction permits in 2006, which is a proxy for future activity in the sector, followed a similar pattern, showing 68 percent rise in the first six months and 32 percent decline in the second half. On the demand side, compensated checks declined by 0.7 percent in nominal terms in 2006 and by 9.7 percent when deflated by the CPI. Finally, tourism activity, with a significant contribution in Lebanon’s key services sector, has been badly affected by the conflict and the rising political tensions as explained in what follows.

The consumer price index (CPI) was already on the increase in the first half of 2006, but its pace accelerated since the conflict. The CPI increased by 3.9 percent on average in 2006, against a decrease by 2 percent in 2005. This outcome is the combination of a 1.5 percent increase in the first half of the year followed by a 6.4 percent surge in the second half. The conflict has clearly exacerbated the upward trend, with the average CPI for the third quarter of 2006 increasing by 7.1 percent compared to the same period in 2005. This dynamic slowed down by the year-end, with the CPI growing by 5.9 percent in the last quarter compared to the same period in 2005. The recent data shows the persistence of relatively high inflation, with the CPI in January 2007 is 6.5 percent higher than its January 2006 level.

Fiscal Developments

The good fiscal outcome of the first six months in 2006 was eliminated in the second half of the year. The cumulative deficit excluding grants increased to 13.6 percent of GDP in 2006 from 8.5 percent in 2005 (Figure 2). The primary balance registered a 0.1 percent deficit against a 2.2 percent surplus a year earlier, undoing the progress made in reducing the fiscal deficit over the last several years. If maintained, significant improvement observed in fiscal indicators during the first semester of 2006 could have increased primary surplus to 3.0-3.5 percent of GDP. The fiscal deterioration in 2006 reflects combination of a 29 percent increase in interest payments, a 9.7 percent increase in primary expenditures (because of higher military spending, early relief expenditures and repair and reconstruction of key public infrastructure), and a moderate 1.5 percent decline in revenues (primarily as a result of a drop in trade, taxes and VAT).

in technology and capital, a drop in the employed labor force (L) in 2006 could have generated between 1.0-5.0 percent decline in GDP, depending on the length of decline in L and on the value of α. Taking into account the conflict’s toll on the physical capital, contraction in output could very well be in the upper end of this range.

3 Construction permits are an indication of the tendency of investments, mainly foreign, in the real estate and construction sector. The drop in permits during the second half of 2006 signals that the impact of summer’s conflict on construction and real estate would last over the year 2007, if not longer. The negative impact of this on the sector’s growth prospects could, however, be compensated by the surge in the post-conflict reconstruction.

4 Compensated checks increased by 18 percent in nominal terms in the first half of the year followed by a 17 percent decline in the second half compared to the same period in 2005.

5 The primary balance in 2006 shows the net effect of sharply fluctuating expenditures and revenues between the first and the second half of the year: while revenues increased by 15 percent in the first half, they declined by 16.6 percent in the second half compared to the same period in 2005; similarly, primary expenditures declined by 7.2 percent in the first half, but increased by 26.5 percent in the second half of the year.
The impact of the conflict on the expenditures is estimated to be substantial, but not fully accounted for. Although the conflict played an important role in the increase of primary expenditures, part of this increase is related to persistent deficits run by some public agencies. The electricity company, EdL, accounts for the largest share in this group, with its deficit in 2006 increasing by 50 percent excluding the direct impact of the conflict and by 78 percent taking account of conflict related expenditures. The significance of this fiscal burden is well illustrated by the fact that without the non-conflict related additional budgetary transfers to EdL, primary balance would have registered a surplus of about 1.3 percent of GDP and total deficit would have been 1.4 percentage points lower in 2006—i.e. even after accounting for the direct budgetary impact of the conflict. Similarly, higher debt service payments in 2006 partly reflect diminishing impact of Paris-II debt relief arrangements (starting mid-2005) and rising debt stock (by 7.3 percent) in 2005—all zero percent TBs and bonds subscription (US$3 billion) by commercial banks matured starting mid-2005 and were not re-conducted. This combined with higher risks during/in the aftermath of the conflict in the second half of 2006 explains the increase in the average cost of the debt from 5.2 percent in 2005 to 7.9 percent in 2006.

The composition of debt in currency slightly changed with the share of debt denominated in foreign currencies increasing to 50.5 percent of the total in end-2006 compared to 49.8 percent at end-2005. The average maturity of the debt denominated in foreign currencies increased to 6.4 years from 5.6 years at end-2005 and the average maturity of debt in domestic currency remained stable at around 1.6 years. The Government covered only part of its financing needs through the increase in debt. Therefore, the increase in gross debt (LBP 2,971 billion) is lower than the public deficit (LBP 4,582 billion) with the difference being covered through a decrease in public sector deposits by 21 percent in 2006.

External Accounts

The rising regional oil wealth had a positive impact on Lebanon’s external accounts in the first half of 2006. It triggered a rise in foreign demand for Lebanon’s goods and services. Tourist activity increased substantially, with 23 percent rise in passengers at Beirut airport. Similarly, exports increased by 49 percent; and foreign demand for real estate investments in Lebanon surged rapidly. Gulf investors initiated/announced investments valued at US$2.4 billion (11 percent of 2005 GDP) in Lebanon’s real estate sector. Finally, nonresident deposits in commercial banks increased by 9 percent, or US$820 million, which amounts to 25 percent of the total increase in deposits during the period. In parallel, imports increased by 17.2 percent, with the trade deficit slightly rising to US$3.7 billion. The widening trade deficit was, however, more than offset by growing net exports of services, remittances, transfers, and capital inflows, reaching US$6.3 billion during the period. The net foreign assets in the banking sector (commercial banks and Central Bank) estimated to increase by US$2.6 billion (12 percent of 2005 GDP).

This positive trend sharply reversed in the second half of 2006. First, the month-long war between July 12 and August 14 stemmed foreign demand and triggered a net outflow of capital. The sea and air blockades completely halted exports and imports of goods. Tourists fled the country in the first few days of the conflict, followed by at least 200,000 Lebanese nationals. Private financial inflows reversed, which was partly

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6 For more detailed analysis see World Bank’s Economic and Social Impact Analysis, November 2006.

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7 Indicators show percentage change in the first half of 2006 compared to the first half of 2005.

8 The net amount of these components is calculated by the sum of the merchandise trade deficit and changes in the net foreign assets of banks.
reflected in a US$1.8 billion decrease in money supply between mid-July and mid-August. Second, the rising political tensions in the post-conflict period slowed down the recovery. Passengers’ activity at Beirut airport declined by 40 percent—with the total decline in 2006 reaching 14.5 percent. Foreign demand for real estate investments in Lebanon stopped since July 2006, and nonresident deposits in commercial banks decreased by 9 percent during the second half of the year—with overall decline in 2006 is at 1 percent. Exports declined by 2.5 percent in the second half of the year—with the total increase in exports reaming at 21 percent in 2006. The decline in imports in the second half of the year reached 13.6 percent—with the total increase in imports for the year remaining at only 0.6 percent. Consequently, the trade-in-goods deficit in 2006 contained at 32 percent of GDP—down from 34 percent in 2005. With the net foreign assets turning to a negative US$78 million in the second half of the year, net exports of services, remittances, transfers, and capital inflows remained at US$2.5 billion in 2006. Judged by past trends, the total inflows in 2006 could have been higher (by up to US$2.5 billion) in the absence of the conflict (Figure 3)9.

The conflict and the persistent political tensions had a strong impact on BdL’s reserves. Gross foreign currency reserves had reached US$11 billion at the end of June 2006, just before the war, representing 13 months of imports, compared to US$8.4 billion (equivalent to 11.7 months of imports) in June 2005. Between July 15 and August 15, the Central Bank is estimated to have spent around US$2 billion to maintain the stability of the Lebanese pound, an amount that have been largely compensated for by the Saudi and Kuwaiti deposits. By end October, reserves were again on the increase (at US$11.2 billion), with the decrease in dollarization and the resumption of capital inflow to the country. After the assassination of Minister Gemayel in November, and with the rise in political tensions, conversions resumed and reserves declined to US$10.2 billion by end-2006 (Figure 4). The most recent data suggest a further decline in gross reserves to US$9.8 billion (as of March 15, 2007).

Regional oil wealth and international support have helped contain the negative effects of the conflict and political tensions on the external account. During the

9 The inflows in the second half of 2006 amounted to US$3.6 billion, down to just over 36 percent of total capital flows compared to past trend of 50-55 percent of the total capital inflows.
Financial Sector Developments

Despite deposit withdrawals during the conflict, money supply witnessed a strong upward dynamic in 2006. The broad money supply (M3), increased by 7.8 percent in 2006, compared to 4.4 percent in 2005. Resident deposits in foreign currencies increased by 13.6 percent while resident deposits in LBP declined by 4.7 percent. The dollarization rate of total deposits increased to 76.2 percent at end-2006 from 73 percent at end-2005. The changes in net foreign assets commanded the movements in M3 throughout 2006: excluding gold, they contributed to 77 percent of the overall increase in M3; the rest of the increase is explained by the change in Gold value, while the change in domestic assets had a negative 5 percent contribution. It should be noted that in July and August 2006, the decline in net foreign assets excluding Gold represented about 60 percent of the decline in M3 (Figure 5).

Figure 5. Counterparts of Money Supply (US$ million)

Source: Central Bank of Lebanon, World Bank staff calculation.

Domestic and foreign currency interest rates showed divergent pattern in 2006. The average interest rates on LBP denominated deposits declined by 21 basis points (bpt) since December 2005. This is due to the stabilization policy followed by the Central Bank. Facing substantial conversions, the Central Bank supplied the market with foreign currencies in coordination with commercial banks while keeping the interest rates on LBP monetary instruments unchanged (Certificates of Deposits and Treasury Bills). This policy helped keep interest rates on domestic currency deposits as well as public debt service at low levels (the latter would otherwise have increased due to higher cost of lending). The average interest rates on US$ deposits increased by 67 bpt between end-2005 and end-2006, reflecting international trends, but at a slightly lower pace, e.g. compared to the Libor rates (Figure 6).

Figure 6. Average Interest Rates Served on Deposits

Source: Central Bank of Lebanon, World Bank staff calculation.

The conflict and the political instability also affected performance of the Beirut Stock Exchange (BSE). The Blom index of the BSE declined by 9.6 percent in 2006. The index increased by 15.9 percent during the first half of the year (over December 2005), followed by about an equivalent rate of drop during the conflict in July (over June 2006 level). The authorities suspended trading operations for two weeks during the early days of the conflict before reopening the BSE in the first week of August. They then imposed restrictions on trading and suspended operations on shares experiencing declines that were greater than 5 percent of their opening price. BSE’s relative resilience to the conflict stems also from the quasi-monopolistic structure of the market with the real estate company, Solidor, representing more than 50 percent of BSE’s market capitalization. The BSE quickly recovered in the aftermath of the conflict, but declined again with the increasing political tension in November-December, 2006. All in all, the Blom index declined by 22 percent in the second half of 2006.

10 M3 = money in circulation in LBP + deposits in LBP + deposits in foreign currencies.
11 Money supply rose by 5.5 percent by end-June 2006 over end-2005, followed by a 3 percent decline in July-August compared to June, before rising by 5.3 percent between August and December 2006.

12 Banque du Liban et d’Outre Mer (Blom) calculates a daily index summarizing the performance of the BSE.
At the Government’s request, the World Bank prepared an Economic and Social Impact Assessment (ESIA) of the recent hostilities. A large multi-sector team undertook the assessment and an analysis of the macro and structural situation to provide an analytical basis to underpin a medium-term reform program. The ESIA sets out an overall framework including: (i) an assessment of the prevailing macroeconomic challenges and the complexities added to it by the physical, social and economic impact of the hostilities; (ii) the elements of a coherent reform program; (iii) the role of the donors and (iv) the importance of building consensus around and support of the reform. The process involved intensive consultations with Government officials, the private sector and other stakeholders in Lebanon. It also involved close collaboration with several donors, and, in particular, with the European Community (EC), the United Nations Development Programme (UNDP) and other UN agencies.

The analysis in the ESIA provides a starting point for Government and stakeholder consultations on developing and adopting a comprehensive short-term recovery plan and a credible strategy for medium- and longer-term sustainable growth. From an economy-wide perspective, this will require very substantial trade-offs among worthy objectives and a disciplined medium-term financing framework if the strategy is to avoid worsening the fiscal situation and undermining growth and social spending. The dilemma presented to the Government by this set of circumstances is a difficult one. While the reforms discussed in the ESIA provide guidance on focus and priorities, it is the prerogative and responsibility of the Government to develop a coherent, actionable strategy, which can be supported by donors. The report covers 16 sectors in three broad areas: (i) infrastructure (transport, electricity, water supply and sanitation, housing, municipal infrastructure and environment); (ii) economic (macro/fiscal, banking, private sector development, trade facilitation, agriculture and irrigation); (iii) social (education, health, pensions, social safety nets, labor markets); as well as several cross-cutting issues (aid coordination and fiduciary management). Below is the executive summary of the synthesis volume of the report:

The hostilities in the summer of 2006 resulted in serious human and physical losses and caused both short and long-term damage to the Lebanese economy. In addition to the human tragedy of those killed and injured, nearly one million people (one quarter of the national population) were displaced during the height of the hostilities. The lives and livelihoods of the families who lived in and around the nearly 107,000 housing units which were damaged or destroyed have been severely disrupted. In the key sectors analyzed by the World Bank, the direct damage from the hostilities is estimated at some US$2.4 billion. Indirect damage accounted for another US$700-US$800 million in losses.

The substantial social, economic and fiscal implications dealt a severe blow to Lebanon’s long-term prospects for recovery. Economy-wide losses from foregone output are estimated at US$2.3 billion in 2006 alone. A projected growth in real GDP of 6 percent in 2006 has been turned into a contraction of nearly the same magnitude. It is estimated that some 30,000 jobs have been lost. Government revenue is expected to decline by US$500 million, while hostility-related spending has increased Government expenditures by approximately US$690 million. As a result, Lebanon’s ratio of debt-to-GDP, which had begun declining in the first half of 2006 on the back of Government reforms and a growing economy, is now likely to reach 190 percent by the end of 2006. Analysis by the World Bank suggests that Lebanon now faces a public finance crisis unless substantial structural, social and fiscal reforms are undertaken. Barring these, the debt-to-GDP ratio is set to continue to climb, reaching new highs of perhaps 230 percent of GDP over the medium-term. This will impede growth and impair the Government’s ability to provide essential social and human development services.

The human and physical losses and the social and economic damage have undermined the two key ingredients for recovery: confidence in an economic rebound and credibility that the country’s institutions can implement realistic economic and social measures necessary to move the country forward and realize its potential. Restoring confidence and credibility requires urgent attention to sector policies and investment programs, modernization of the business environment and efficient expenditure practices. The challenge is daunting and there is no time to waste.
The hostilities have also brought into focus the historical neglect of the social sectors, especially the development of effective social safety nets. Lebanon has been hampered by the absence of a coherent social strategy and actionable program. Rather, weak coordination and politically-determined public spending has been the hallmark of social policy in Lebanon with the result that the pattern of spending is inconsistent with the actual needs of the most vulnerable populations. In the absence of appropriate social safety nets, families and businesses are left with the burden of supporting the vulnerable and unemployed. Overall, the impact of social sector programs, including both health and education, is not commensurate with the level of public spending. With additional strain on the system resulting from the hostilities, there is an urgency to initiate social strategies and programs which are inclusive, promote opportunities and provide protection across the population while addressing long-running inefficiencies.

The ability of Lebanon’s economy to recover and embark on a high and sustainable growth path is constrained by a business environment in need of immediate modernization. The cost of doing business locally is driven up by rigid labor markets, a lack of responsive debt and equity markets and risk mitigation instruments, remaining inefficiencies in the tax system and a legal and regulatory framework that is inadequate for a modern service-driven economy. This environment makes it more difficult for Lebanon’s private sector to adjust to shocks and to compete in the global economy.

The Government’s current reform agenda includes a number of proposals to expand reform efforts, as well as to introduce effective and efficient sector policies and expenditure programs. The draft program also includes key proposals to improve Lebanon’s business environment. This program needs to be agreed, articulated and supported by adequate resources. The speed and strength of this process are critical for avoiding a severe deterioration in public finances and returning the Lebanese economy to a path of growth.

A difficult dilemma is presented to the Government by this set of circumstances. The needs of reconstruction represent new challenges and exacerbate the fiscal, macroeconomic and sectoral problems which existed prior to the hostilities. While the reform program introduced in early 2006 remains broadly relevant, the hostilities have undercut the platform of strengthening confidence and credibility upon which the Government’s program was based. Moreover, the impact of the hostilities has raised the demand for additional public services, while at the same time reducing the revenue available to support public spending. Significant levels of new growth and fiscal efforts are now required just to get Lebanon back to the macroeconomic level prevailing in June 2006.

A three-pronged strategy is recommended to enable Lebanon to move beyond reconstruction to recovery and sustainable growth. This strategy focuses on the Government’s reform program, donor support and the building of public confidence among key measures to be undertaken by the Government:

First, a coherent reform program must contain the following elements: (i) structural measures aimed at improving business conditions for the private sector; (ii) fiscal adjustment measures that will yield additional public resources while distributing the burden fairly across society (this could include: improved collections in the electricity sector; additional taxation of the financial sector and other revenue-generating actions; and privatization of some State assets with revenues used to retire debt); (iii) increased attention to the social sectors, including health and education, and the provision of social safety nets to protect the poor and vulnerable; (iv) re-prioritizing infrastructure policies to sustain a modern service-led economy; and (v) efforts to address shortcomings in public financial management and procurement.

Second, coordinated donor support, including significant levels of assistance for the Government’s reform program in addition to the aid already committed for reconstruction, is essential. Donor assistance should be provided in lockstep with an agreed strategic plan by the Government and supported by appropriate technical assistance to enhance its effectiveness. Higher levels of donor financing in support of structural adjustments should be used to reduce borrowing and help the economy grow out of very high indebtedness. This goes significantly beyond financing for projects and reconstruction associated with post-hostilities reconstruction.

Third, measures to build credibility and confidence. This requires broad-based support for the reform agenda based on the public’s understanding that its burdens and benefits are shared equally. The main ingredients of a credible Government program are: clear objectives; an actionable implementation plan; a realistic timetable and sequencing; public monitoring of progress and full accountability for delivering results. Building confi-
dence and credibility requires burden-sharing arrangements that are seen as equitable and balanced, including broad-based sharing in the costs of fiscal adjustment.

Given the depth and breadth of the required reforms, the Government needs to identify a manageable program of critical reforms that will generate significant impacts on growth and fiscal and social outcomes. This reform program should also be prioritized and sequenced, and be credibly implementable given the limited institutional capacity and the country’s political challenges. The detailed background sector analysis presents within-sector prioritized recommendations. However, prioritization across sectors requires evaluations and judgment that is political, and hence, should be carried out by the Government, in consultation with stakeholders. This report’s technical analysis provides the material which forms the basis for making the cross-sector prioritization.

This report sets out an overall framework starting, in Section I, with a discussion of the prevailing macro/fiscal challenges and the complexities added to it by the hostilities. Section II presents the elements of a reform program to promote recovery and sustainable growth. Section III discusses the role of donors in providing financial and technical assistance in support of the Government’s program. Section IV reiterates the importance of building consensus around the reform agenda. The report is based on detailed technical analysis of economic, social and infrastructure sectors in terms of the impact of the hostilities and priorities for reform over the next several years.

For more information on the Economic and Social Impact Assessment report, please visit:
http://www.worldbank.org/lb
On November 2, 2006, the World Bank and the Ministry of Finance signed a Grant Agreement, providing US$30 million for the rehabilitation of municipalities that were hardest-hit in the July-August hostilities. The Grant is part of a US$70 million Trust Fund for Lebanon allocated by the World Bank to assist the Government’s post-hostilities reconstruction efforts.

Objectives

The objectives of the additional financing grant to the First Municipal Infrastructure Project (FMIP) are to: (i) restore basic services and rebuild priority public infrastructure in the municipalities and villages affected by last summer’s hostilities; (ii) support economic recovery and development in the municipalities that have suffered the heaviest damage; and (iii) build the capacity of municipalities to mitigate the impact of the hostilities on municipal finances within the context of developing the municipal sector. This is a supplemental project that builds on the success of an existing US$80 million loan targeting 720 municipalities across the country.

Following the 34 days of hostilities, the Government of Lebanon (GOL) carried out an assessment, which indicated that key infrastructure had sustained extensive damage, significantly disrupting the country’s ability to provide essential services to the population. In addition to vital infrastructure facilities (i.e., airports, ports, transport, power plants, etc.), the municipalities located in areas affected by the hostilities suffered wide-scale destruction with housing representing almost 50 percent of the total damage particularly in the Beirut’s southern suburbs, as well as Southern Lebanon.

Damage to the municipal sector (which included urban roads, retention walls, street lighting, water and sanitation, municipal buildings, equipment, etc.) was estimated at US$80 million. The combination of growing municipal expenditures and scarce resources further compromised the capacity of the municipalities to deliver basic services to the vulnerable population.

The grant from the Trust Fund for Lebanon (TFL) is designed to reverse these misfortunes. It will complement other donors’ reconstruction programs by covering most of the estimated damages to infrastructure in the municipalities. Moreover, it will foster economic recovery in select cities affected by the hostilities. The duration of the grant will be about three years.

Why the Municipalities?

The new project builds on the success of a US$80 million FMIP, which has been effective since November 28, 2000. By all accounts, the FMIP is the best performing Bank project in Lebanon and was well on track to achieve its development objectives and related outcomes before the outbreak of the hostilities. Almost 800 sub-projects had been implemented in more than 700 municipalities. By June 2006, over 1,500 kilometers of roads and 260 kilometers of retaining walls had been repaired and upgraded, over 12,000 street lighting poles had been installed and almost 350 kilometers of drainage, water and sewerage networks had been repaired. By September 30, 2006, disbursements had reached US$63 million (i.e., almost 80 percent of the loan amount) with the uses of all the remaining funds already identified.

However, work was interrupted in July 2006, and contractors abandoned the working sites located south of Sidon and in the Bekaa Valley. About 150 Civil Works contracts that were under implementation were suspended. The slow resumption of work in the aftermath of the hostilities was compounded by the onset of the winter season. As such, the work will not be completed before the closing date of June 2007, requiring a loan extension until June 30, 2008.

Considering the FMIP’s demonstrated implementation effectiveness and quality of assistance to the municipalities, the Ministry of Interior and Municipalities (MOIM) requested additional support from the Bank in early 2006 to expand the geographic scope of the project to newly created municipal councils. The summer hostilities necessitated a reorientation, focusing on replacing lost municipal assets, restoring basic services and relaunching economic activity in municipalities affected by the hostilities and villages that did not benefit from the financial support of other donors.
Components of the Grant

Reconstruction of Public Infrastructure (US$18 million). This component will finance the reconstruction of priority public infrastructure destroyed or damaged during the hostilities in about 120 municipalities not supported by other donors. Sub-projects would consist of, but not limited to, urban roads, sidewalks, retaining walls, street lighting, water and sewerage networks, municipal buildings and equipment. The selected sub-projects will comply with emergency reconstruction criteria, as well as the environmental and social safeguards adopted under the FMIP, with an added emphasis on simplicity and speed.

Municipal Recovery and Development (US$9 million). This component will provide assistance to build a new municipal infrastructure to help revive the local economy. Among others, it will finance market places, access to public facilities, site and services schemes and the upgrading of service delivery systems and related equipment. The grant will support development-oriented sub-projects in about 10 to 15 municipalities that: (i) receive reconstruction assistance from other donors; and (ii) show the highest potential to become growth centers for the regional economy. The selected sub-projects will also comply with the economic and financial eligibility criteria, as well as the environmental and social safeguards adopted under the FMIP.

Project Management and Capacity Building (US$3 million). This component will support the following activities: (i) project management and technical assistance for implementing the grant; and (ii) capacity building for increasing local revenues, primarily by reforming the property tax, and improving transparency in the management of intergovernmental transfers and financial flows between the Central Government and the municipalities. Both activities are critical to the sustainable recovery of the affected municipalities in particular, and the municipal sector in general.

<table>
<thead>
<tr>
<th>Component</th>
<th>Procurement Category</th>
<th>Trust Fund for Lebanon</th>
<th>Government of Lebanon</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>COMP. 1: RECONSTRUCTION OF PUBLIC INFRASTRUCTURE</td>
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<tr>
<td>a. Rebuild and repair damaged Public infrastructure including municipal buildings</td>
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<tr>
<td>b. Replace damaged ICT equipment</td>
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<td>COMP. 2: MUNICIPAL RECOVERY AND DEVELOPMENT SUPPORT</td>
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<td></td>
<td></td>
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<tr>
<td>a. Provision of public infrastructure to facilitate social and economic recovery</td>
<td>Works</td>
<td>7.0</td>
<td>23</td>
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<tr>
<td>b. Provision of equipment to facilitate social and economic recovery</td>
<td>Goods</td>
<td>0.3</td>
<td>1</td>
<td></td>
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<tr>
<td>COMP. 3: PROJECT MANAGEMENT AND CAPACITY BUILDING</td>
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<td></td>
<td></td>
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<tr>
<td>a. Capacity building to mitigate impact of the hostilities on municipal finances and technical assistance</td>
<td>Services</td>
<td>1.8</td>
<td>6</td>
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<tr>
<td>b. Preparation of the environment management plans for sup-projects screened as Category B and Periodic Social Assessments</td>
<td>Services</td>
<td>0.2</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>c. Project Management</td>
<td>Services</td>
<td>1.0</td>
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<td></td>
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<td>CONTINGENCIES (PHYSICAL AND FINANCIAL) *</td>
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<td>4.4</td>
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<tr>
<td>Total</td>
<td></td>
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</table>

* Note: Contingencies are allocated on a pro rata basis for works and goods under Components 1 and 2.
IBRD Ongoing Projects

The current World Bank portfolio in Lebanon consists of six projects for a total commitment amount of US$284.61 million, of which US$128.25 million had been disbursed by February 28, 2007.

Education Development Project (EDP) (US$44.6 million). This Project is designed to support the Government’s efforts to enhance the capacity of the Ministry of Education to function as an effective manager of the education sector and to restore the credibility of the Public Education System. The project was approved in March 2000.

First Municipal Infrastructure Project (FMIP-I) (US$80.0 million). This Project aims to address urgent municipal works while setting the stage for the gradual assumption of responsibility for municipal services at the local level. The project was approved in June 2002.

Community Development Project (CDP) (US$20.0 million). This Project is designed to raise living standards in targeted poorer communities, and to raise economic activity levels in such communities by investing in grass-roots social and small infrastructure activities, and in employment creation. The project was approved in June 2001.

Ba’albeck Water and Wastewater Project (US$43.5 million). The major development objectives of the Project include: (a) improving the access of satisfactory water supply and wastewater services to the region’s residents; (b) introducing appropriate sector reforms – particularly, the development and strengthening of the capacity of the existing Ba’albeck Hermel Water and Irrigation Authority and, once it is established, the Bekaa’ Regional Water Authority; and (c) involving the private sector in the operation and maintenance of water and wastewater facilities by preparing for a Management Contractor (MC) through a lease or concession contract that would secure the long term financial needs for sector investments. The project was approved in June 2002.

Urban Transport Development Project (UTDP) (US$65.0 million). The Project’s objectives are to provide the city of Beirut and the Greater Beirut Area with the basic institutional framework that is currently lacking, and to support critical investments needed to maximize the efficiency of existing urban transport infrastructure. The project was approved in June 2002.

Cultural Heritage and Urban Development Project (CHUD) (US$31.5 million). The Project will finance site conservation, enhancement investments, associated urban infrastructure improvements in selected sites and provide technical assistance to strengthen the capacity of the Directorate General of Antiquities, Ministry of Tourism and targeted municipalities in cultural heritage preservation and tourism development. The project was approved in April 2003.

Commitments and Disbursements as of February 28, 2007

<table>
<thead>
<tr>
<th>Project Name</th>
<th>Approval Year</th>
<th>Loan Amount</th>
<th>Amount Disbursed</th>
<th>Closing Date</th>
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<td>Dec. 2007</td>
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<td>First Municipal Infrastructure</td>
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<td>Community Development</td>
<td>2001</td>
<td>20.00</td>
<td>6.47</td>
<td>Feb. 2008</td>
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<td>Ba’albeck Water and Wastewater</td>
<td>2002</td>
<td>43.53</td>
<td>12.22</td>
<td>Sept. 2008</td>
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<td>Urban Transport Development</td>
<td>2002</td>
<td>65.00</td>
<td>16.08</td>
<td>June 2009</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2003</strong></td>
<td><strong>284.61</strong></td>
<td><strong>128.25</strong></td>
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</tbody>
</table>

For more information on projects, please visit: http://www.worldbank.org/lb.
IBRD Ongoing Grants

First Municipal Infrastructure Supplemental Project (US$30.0 million). This Grant aims to restore basic services and rebuild municipal infrastructure in the areas hardest hit during the summer 2006 hostilities, and provide technical assistance to and build the capacity of municipalities to mitigate the impact of hostilities on municipal finances.

Mechanism for National Reconstruction (US$1.25 million). The Grant supports the establishment by the Government of Lebanon of a system to manage and monitor the reconstruction funding in an effective and transparent manner, promoting international standards and good practice.

Rapid Social and Livelihoods Assessment (US$99,000). The objective of the Grant is to feed into the strategic planning processes related to post-hostilities reconstruction. As such, it is expected to identify social policies and interventions to help those affected by the hostilities and vulnerable segments of the Lebanese society. The Grant aims to fill a serious information gap on livelihoods and social conditions.

There are also two Institutional Development Fund (IDF) grants currently under implementation that pre-date the hostilities. They support: (1) a program to strengthen the capacity of national HIV/AIDS surveillance and monitoring and evaluation systems ($350,000) and (2) a program to strengthen the capacity of the Ministry of Justice and the Ministry of Environment in judicial enforcement in environmental affairs ($327,000), implemented by UNDP.

IFC Projects in Lebanon

Since the recent hostilities in the summer of 2006, IFC has focused its activities on supporting the recovery of the private sector, and in continuing technical assistance efforts with the Government of Lebanon to ease the administrative burden on the private sector.

IFC is in the process of implementing a series of projects in the financial sector, all aimed at providing access to finance for Small- and Medium-Enterprises (SMEs) which were directly or indirectly affected by the hostilities. To further support the private sector, IFC has expanded the trade finance lines held with three banks, both by increasing the overall amounts of these lines and lengthening their tenor. The trade finance activity is complemented by a number of lines opened to banks for on-lending to the private sector, and the establishment of a guarantee facility for SMEs. This guarantee facility is also supported by IBRD through granting of IBRD trust funds for the facility.

In addition to its traditional lending activities, IFC’s Private Enterprise Partnership for the Middle East and North Africa (PEP-MENA), a US$100 million, donor-financed technical assistance facility has focused on a number of areas relating to recovery from the hostilities and to implementing administrative reform.

Microfinance Portfolio Recovery – IFC sponsored a roundtable program to match international experts in microfinance in conflict areas with Lebanese microfinance institutions to help them develop techniques to recover from the hostilities.

Administrative Barriers Survey – The joint World Bank/IFC Foreign Investment Advisory Services group has finalized a survey of administrative barriers in Lebanon to identify reforms necessary to improve Lebanon’s business environment. Discussions are now underway on a program to implement the survey recommendations.

Business Enabling Environment – IFC continues its work on a technical assistance agreement with the Ministry of Economy and Trade to assist in the reform and streamlining of the business registration process. This program will take approximately one year and will tackle one of the issues in which Lebanon performed most poorly in the Doing Business Survey.

Corporate Governance – In partnership with the Association of Lebanese Bankers, IFC undertook a comprehensive review of Corporate Governance practices in the Banking Sector in Lebanon. Now, IFC is rolling out an extended Corporate Governance program that will focus on raising standards in businesses across all sectors.

Gender – As part of a wider regional program, IFC recently completed a survey of barriers to women entrepreneurs in Lebanon. This survey examines current practices in Lebanon compared to other countries in the region and will soon be published.
MIGA in Lebanon

Lebanon has been a member of the Multilateral Investment Guarantee Agency (MIGA) since 1994. Over the past decade, MIGA has received more than 20 preliminary applications from investors in Austria, Canada, France, Luxembourg, Saudi Arabia and Spain for investments in Lebanon in the finance, infrastructure, telecommunications and tourism sectors.

In addition, the Lebanese investor community has become increasingly interested in MIGA’s ability to provide non-commercial risk coverage for their investments in other developing countries. In fiscal year 2002, MIGA issued US$8.1 million in guarantees to Investcom, a Lebanese-owned company, for a telecommunications project in Benin involving the installation of a new GSM mobile telephone network. Lebanon is one of the lowest teledensity countries in the world. In fiscal year 2003, MIGA issued US$56 million in Guarantees to Investcom’s investment in Spacetel, Syria’s second mobile telephone network. Also, Lebanese investors have submitted preliminary applications in the finance, infrastructure and manufacturing sectors for investments in Côte d’Ivoire, Ghana, Sierra Leone, Gambia, Guinea and Syria. Eligible investors include those from MIGA-member countries investing in Lebanon, Lebanese nationals repatriating funds for investments in Lebanon, as well as Lebanese investors investing in developing countries, including the Middle East region.

The Investment Development Authority of Lebanon (IDAL), Lebanon’s Investment Promotion Agency, has submitted to MIGA a Needs Assessment request. MIGA performed the Needs Assessment in March 2006. The Needs Assessment will benchmark IDAL’s investment promotion capacity relative to international best practices and recommend steps to improve IDAL’s ability to attract FDI into Lebanon.

MIGA’s online investment promotion services (www.fidexchange.com and www.ipanet.net) feature 130 documents on investment opportunities and the related legal and regulatory environments in Lebanon.
The World Bank Group (WBG) has announced the appointment of Demba Ba as the new Lebanon Country Manager.

Mr. Ba is a renowned development economist with responsibility for private sector development in Sub-Sahara Africa at the World Bank Group. He served on the WBG Finance & Private Sector Development Board. In that role he oversaw a portfolio of US$1.2 billion of World Bank commitments across Africa.

Mr. Ba has initiated and led several ground-breaking programs, including firm level surveys used to produce Investment Climate Assessments, which are employed by policy makers to chart private sector-led growth strategies and action plans. These included a joint International Development Agency-International Finance Corporation program that aimed to provide services that enable access to finance for Small, Medium and Micro Enterprises (SMMEs).

Mr. Ba has spearheaded the use of Presidential Investor Advisory Councils for Heads of State and Government to engage the private sector in vetting policies and mobilizing domestic and foreign investments. These investor councils have been instrumental in designing and implementing the reforms that improve the countries’ ranking in the Global Doing Business Report.

Throughout his career, he has designed and implemented reforms of State Owned Enterprises, Corporate governance and export growth strategies. In this context he led the restructuring of key sectors such as power, commodities, transport, telecommunications and water and sanitation. Early in his career, Mr. BA worked for US Agency for International Development and as an observer for the International Committee of the Red Cross in the Western Sahara conflict.

During his WBG career, he has held several diverse posts in country offices such as Benin, Cote d’Ivoire, Germany, France, Guinea, Mali, Mauritania, Senegal, Somalia and Togo.

A native of Mauritanian, Mr. Ba is also a member of the Steering Committee of the Tokyo International Conference on African Development (TICAD). He holds a BS in Agriculture Economics from Ohio State University and a Masters in Development Economics and Finance from the University of Delaware. Mr. Ba is a graduate of the Harvard Business School Executive program. He speaks English, French and Arabic.

The new Lebanon Country Manager will formally assume his post in July. He succeeds Omar Razzaz, whose three-year tenure ended in July 2006.

Juan Jose Daboub, the newly appointed Managing Director of the World Bank, led a high-ranking delegation to Lebanon in February 2007 as part of a fact-finding mission to the Middle East on development needs.

Mr. Daboub was accompanied by Daniela Gressani, World Bank Vice President for the MENA region and Merza Hasan, the World Bank Executive Director for the Middle East region.

From February 7-9, 2007, the delegation met with Prime Minister Fuad Siniora and members of the Council of Ministers and congratulated them on the success of the Paris III Donor Conference in support of Lebanon. The World Bank reaffirmed its commitment to support the implementation of the reform program presented at the Paris III Donor Conference on January 25, 2007.

The delegation also exchanged views on Lebanon’s reform program in separate workshops with parliamentarians, civil society representatives and private sector members. The workshops highlighted the importance of deepening structural reforms, fiscal sustainability and improving governance and transparency for the successful implementation of the reform program.
“I have seen in the eyes of the people the determination to move forward. The reform program is ambitious but doable, and necessary to put Lebanon on the path to prosperity. This is why it has received the extraordinary support from the international community”, Mr. Daboub remarked. “Now is the time to implement the program, with full ownership and commitment from all segments of the society. The World Bank Group will continue to support the efforts of the Lebanese people in this direction”, he added.

“Addressing the needs of the poorest and the most vulnerable is critical for this program to work, so that it can bring better opportunities to all population. The World Bank will offer technical and financial support”, Ms. Gressani commented.

On a visit to southern Lebanon, the delegation visited sites of the Bank-supported Municipal Infrastructure Project in Saksakiye which is reconstructing priority public infrastructure to restore basic services to the municipalities. The delegation also visited two community development initiatives in Saida, funded by the Bank in partnership with civil society organizations and the private sector. “It is these types of projects and partnerships, that empower people through training and jobs, that should be emulated widely”, Mr. Daboub noted.

Other stops on the mission included the West Bank, Kuwait, Bahrain, Jordan and Iraq.

Lebanese Project among 105 Finalists in Global Development Marketplace 2007

A project team from Lebanon has been invited to World Bank headquarters in Washington, DC, from May 22-23, 2007 to display its project and vie for grant funding in the final round of the 2007 Global Development Marketplace (DM) competition.

This year’s DM, which paired up with the World Bank Health, Nutrition and Population (HNP) units to focus on improving health, nutrition and population services for the poor, attracted a record number of nearly 2,900 applicants.

Among the 105 finalists is the project presented from Lebanon by Ricerca and Cooperazione, an Italian non-profit Non-Governmental Organization which promotes and implements development, research and information programs in developing countries, Italy and Europe. The project will be implemented in cooperation with the Lebanon Family Planning Association (LFPA), a Lebanese NGO active in education, awareness and service delivery in the field of sexual and reproductive health.

The 105 finalists were narrowed by two rounds of assessments which brought together roughly 250 health and development experts from inside and outside the Bank.

The finalist from Lebanon has proposed an innovative idea to address health problems. The project aims to improve the access to reproductive health information and services of young Palestinians living in refugee camps through a creative game-based approach. Reproductive health of youth is a very sensitive subject for Palestinian communities. A board game is being developed which will incorporate fun and opportunities for recreational time, while also providing an opportunity for disseminating information and assessing the value bases, knowledge and attitudes related to reproductive health and the personal wellbeing of young people aged 13-22 years.

The total cost of this project is US$177,250, and funding requested from the DM amounts to US$98,600. The project will be incorporated into a larger program, which is already ongoing, and which focuses, through an integrated approach, on both capacity building to local health care and information providers, and community sensitization and advocacy.

The majority of the 105 finalists (34 percent) address sub-Saharan Africa. Latin America, the Caribbean and Southeast Asia will each be represented with about 20 percent of projects. Some 15 percent of the projects are from East Asia and the Pacific, 6 percent from Europe and Central Asia and 4 percent from the Middle East and North Africa region.


The majority of proposals were submitted by NGOs, but many have partnerships with foundations, academia, private enterprises, government and development agencies.

Recent World Bank Publications

World Development Report 2007: Development and the Next Generation (ISBN 0-8213-6541-X). The theme of The World Development Report 2007 is youth. With 1.3 billion young people now living in the developing world - the largest-ever youth group in history - the Report says there has never been a better time to invest in youth. As this population group seeks identity and independence, they make decisions that affect not only their own well-being, but that of others, and they do this in a rapidly changing demographic and socio-economic environment.

Supporting young people’s transition to adulthood poses important opportunities and risky challenges for development policy. Are education systems preparing young people to cope with the demands of changing economies? What kind of support do they get as they enter the labor market? Can they move freely to where the jobs are? What can be done to help them avoid serious consequences of risky behavior, such as death from HIV-AIDS and drug abuse? Can their creative energy be directed productively to support development thinking?

The Report will focus on crucial capabilities and transitions in a young person’s life: learning for life and work, staying healthy, working, forming families, and exercising citizenship. For each, there are opportunities and risks; for all, policies and institutions matter.

2006 Economic Developments and Prospects: Financial Markets in a New Age of Oil. This is the second annual issue of the World Bank’s Middle East and North Africa (MENA) Economic Developments and Prospects Report (MEDP), highlighting the recent key economic developments, as well as the forces underlying the region’s economic outcomes. It analyzes MENA’s medium term growth prospects given global forecasts, and charts the region’s progress with implementing comprehensive structural reforms needed for longer-term growth. As with last year, the 2006 MEDP also examines a theme of particular importance to the region, with this year’s theme devoted to regional financial markets. With oil prices continuing their soaring advances, the efficiency with which the region channels the oil-related resources into the real economy will depend critically upon financial sectors. It is, thus, particularly opportune to examine the state of the region’s financial systems to understand how they are poised to meet some of the region’s development challenges.


The ten indicators are: starting a business, dealing with licenses, hiring and firing, registering property, getting credit, protecting investors, trading across borders, paying taxes, enforcing contracts, and closing a business. The indicators are used to analyze economic and social outcomes, such as informality, corruption, unemployment, and poverty. This annually published Report gives policymakers the ability to measure regulatory performance in comparison to other countries, learn from best practices globally, and prioritize reforms. This year’s Report covers 20 additional countries.

Governance and Private Investment in the Middle East and North Africa (Working Paper Series 3934). This Paper addresses the issue of the low level of private investment in the Middle East and North Africa region, with special emphasis on the role of governance. Based on the existing literature, the Paper categorizes what types of governance institutions are more detrimental to entrepreneurial investments. It then estimates a simultaneous model of private investment and governance quality where economic policies concurrently explain both variables. The empirical results show that governance plays a significant role in private investment decisions. This result is particularly true in the case of “administrative quality” in the form of control of corruption, bureaucratic quality, investment-friendly profile of administration, and law and order, as well as for “political stability.”

Local Governance in Developing Countries (ISBN: 0-8213-6565-7 SKU: 16565). This book provides a new institutional economics perspective on alternative
models of local governance, offering a comprehensive view of local government organization and finance in the developing world. The experiences of ten developing/transition economies are reviewed to draw lessons of general interest in strengthening responsive, responsible, and accountable local governance. The book is written in simple user friendly language to facilitate a wider readership by policy makers and practitioners in addition to students and scholars of public finance, economics and politics.

Lebanon—Trade and Competition Policies for Growth: a General Equilibrium Analysis (Working Paper Series No. 43). Using recent data on concentration indexes, the Paper estimates that rents accruing from monopolistic positions represent more than 16 percent of GDP in Lebanon. The Paper compares the long-term impact of raising domestic competition with that of reducing import tariffs. Simulation results suggest that Lebanon would largely benefit from the reduction of anti-competitive practices.

Do Workers’ Remittances Promote Financial Development? (Working Paper Series 3957). Workers’ remittances to developing countries have become the second largest type of flows after foreign direct investment. The authors use data on workers’ remittance flows to 99 developing countries from 1975-2003 to study the impact of remittances on financial sector development. In particular, they examine whether remittances contribute to increasing the aggregate level of deposits and credit intermediated by the local banking sector. This is an important question considering the extensive literature that has documented the growth-enhancing and poverty-reducing effects of financial development. The findings provide strong support for the notion that remittances promote financial development in developing countries.

Emerging Capital Markets and Globalization (ISBN: 0-8213-6543-6 SKU: 16543). This book sheds light on the analytical, empirical, and policy dimensions of a basic stylized fact that the development of local capital markets in most of Latin America has been quite poor relative to other emerging economies and to global trends. Importantly, it discusses the implications for the capital market reform agenda going forward, emphasizing the need for revisions to the prevalent policy paradigm.

The Other Half of Gender: Men’s Issues in Development (ISBN: 0-8213-6505-3 SKU: 16505). The Other Half of Gender brings the gender and development debate full circle - from a much-needed focus on empowering women to a more comprehensive gender framework that considers gender as a system that affects both women and men. It draws on a slowly emerging realization that attaining the vision of gender equality will be difficult, if not impossible, without changing the ways in which masculinities are defined and acted upon.


The atlas provides a wealth of information on today’s key global issues including eradicating poverty, combating HIV/AIDS and corruption, and promoting environmental sustainability.

Inside the Atlas of Global Development you will find:
- easy-to-read and colorful world maps
- informative tables, graphs, text, and photographs
- selected indicators from the authoritative World Development Indicators database
- detailed information about goals and targets for the Millennium Development Goals
- definitions, sources, notes and abbreviation of terms commonly used in development

This title builds on the World Bank Atlas which has been published by the World Bank for the last 36 editions.

Financial Sector Development and the Millennium Development Goals (World Bank Working Paper # 89). Financial Sector Development and the Millennium Development Goals investigates the relationship between financial sector development and progress in reaching the Millennium Development Goals (MDGs). It assesses the contribution of countries’ financial sector development to achieving the MDGs. The focus is on the relationships between financial development and economic welfare and growth, and the following four MDG-themes: Poverty, Education, Health, and Gender Equality. In doing so, the book reviews the theoretical channels, surveys existing empirical evidence - both cross-country and case study evidence, and provides new evidence.

This book finds that financial development is an important driver for economic welfare in that it reduces the
prevalence of income poverty and undernourishment. In addition, new evidence is provided of a positive association between financial development and health, education, and gender equality.


Governance Reform: Bridging, Monitoring, and Action lays out a broad framework for analyzing and monitoring governance in developing countries. It identifies fourteen core indicators for governance monitoring—both broad measures of overall patterns and specific “actionable” measures that can be used to guide reforms and track progress.

Making the Most of Scarcity: Accountability for Better Water Management in the Middle East and North Africa (ISBN-10: 0-8213-6925-3, ISBN-13: 978-0-8213-6925-8). Water in the Middle East and North Africa region already causes major social and economic problems, resulting from insufficient supply, unreliable services and environmental damage. Per capita availability will fall by half by 2050, water quality is deteriorating, many aquifers are on the verge of exhaustion, and climate change may alter rainfall patterns. Unless current practices change, then, the situation will worsen considerably. For years, water professionals have been advocating comprehensive water reforms. Yet, although most countries have made considerable progress improving water policies and institutions, some of the most important elements of reform have remained politically intractable. This book explores a series of factors that are emerging that represent a potential opportunity to break this impasse.

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