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July 25, 1994

To: Members of the Executive Board

From: The Acting Secretary

Subject: Lebanon - Staff Report for the 1994 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1994 Article IV consultation with Lebanon, which is tentatively scheduled for discussion on Monday, August 22, 1994.

Ms. Eken (ext. 36511) or Mr. Martelino (ext. 38748) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Unless the Documents Preparation Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the European Communities (EC) and the Islamic Development Bank (IsDB), following its consideration by the Executive Board.

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LEBANON

Staff Report for the 1994 Article IV Consultation

Prepared by the Staff Representatives for the
1994 Consultation with Lebanon

Approved by S.H. Hitti and C. Puckahtikom

July 21, 1994

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I. Introduction

Discussions for the 1994 Article IV consultations were held in Beirut during April 27-May 15, 1994, and June 27-30, 1994. The Lebanese representatives were led by the Minister of State for Financial Affairs, H.E. Fuad Siniora, and the Governor of the Bank of Lebanon (BDL), H.E. Riad Salameh, and included senior officials of the Ministry of Finance, the Ministry of Economy and Trade, the BDL, the Council for Development and Reconstruction (CDR), the Banking Control Commission, as well as representatives of the private sector. Also, members of the staff team met with the Prime Minister, H.E. Rafiq El Hariri, during the later visit to Lebanon. 1/

In concluding the last Article IV consultations with Lebanon (EBM/93/105; 7/16/93), Executive Directors endorsed the priority given by the authorities to exchange rate and price stability, and emphasized the importance of tailoring economic and financial policies so as to sustain confidence and consolidate positive expectations. In this regard, the adoption of tight fiscal policies aimed at achieving a significant and rapid reduction of the budget deficit was viewed as the centerpiece of an appropriate policy mix. While recognizing the desire of the authorities to provide adequate resources to support reconstruction and pressing social needs, Directors emphasized the need for stabilization of the economy. Furthermore, they urged the authorities to exercise caution in implementing their ambitious reconstruction program, to link external financing to sound remunerative projects, and to monitor carefully the country's prospective debt service obligations.

Since late 1991 the Fund has been actively involved in Lebanon, providing policy advice and extensive technical assistance from virtually all functional departments of the Fund (Appendix IV). The World Bank has provided advice on reconstruction needs and implementation capacity, as well as technical assistance, particularly in the areas of reform of the financial sector (Appendix V).

Lebanon has an open economy and maintains an exchange system that is free of restrictions on payments and transfers for current international transactions. Effective July 1, 1993, Lebanon formally accepted the obligations under Article VIII, Sections 2, 3, and 4, of the Fund's Articles of Agreement.

1/ The staff team comprised Ms. Eken (Head), Messrs. Cashin, Erbas, Martelino, Mazarei, and Mrs. Rathnam (Administrative Assistant)--all MED. Mr. Hitti joined the mission for the final round of discussions. Mr. Shaalan (Executive Director for Lebanon) and Mr. Gaspard (Advisor to Lebanon's Executive Director) participated in some of the meetings. Mr. Chabrier, Mr. Hitti, Ms. Eken, and Mrs. Redman (Senior Administrative Assistant) traveled to Beirut in June 1994 to conclude the discussions with the authorities.

II. Background and Recent Developments

The signing of the Taif Accord in late 1989 brought to an end the 15-year civil war that exacted a heavy toll in terms of human life and material assets. 1/ Since the end of the civil war, confidence in the authorities' policies has had a major impact on short-term macroeconomic and financial developments. In early 1992, public confidence was shaken by very large retroactive wage increases and the announcement of an expansionary fiscal budget. A subsequent run on a number of banks and renewed disturbances in the south of the country triggered massive speculation on the exchange rate, large increases in prices, and increased dollarization of the economy (Chart 1). By September, the annualized rate of inflation had reached over 200 percent and the exchange rate fell to an all-time low of LL 2,528 per US$1 (from LL 879 at the beginning of the year). In the last quarter of 1992, confidence was restored after the completion of Parliamentary elections (the first in 20 years), and the installation of a new government under Prime Minister Hariri.

In 1993, Lebanon's economic and financial performance strengthened and was favorable when measured against the benchmarks established during the last Article IV consultation. 2/ Real GDP rose by an estimated 7 percent, compared with a target of 5 percent and 4.5 percent in the previous year, mainly reflecting an intensification of construction activity and real estate development (Appendix I, Table 1). Activity in the manufacturing and agricultural sectors remained subdued. Furthermore, the lack of adequate infrastructure, weaknesses in the institutional and legal framework, and shortages of human and physical capital continued to constrain overall economic activity. Meanwhile, the annual average rate of inflation decelerated sharply from 120 percent in 1992 to 29 percent in 1993, in line with the target. On an end-year basis, inflation dropped from about 170 percent in 1992 to slightly below 9 percent in 1993. On the external side, the current account deficit is estimated to have widened, due mainly to a rapid increase in imports (Chart 2). However, large capital inflows more than offset the widening external current account deficit, with the result that the overall balance of payments registered a surplus of US$1.2 billion, compared with a target of only US$100 million. Accordingly, official foreign exchange reserves of the BDL rose to a level equivalent to 6.3 months of

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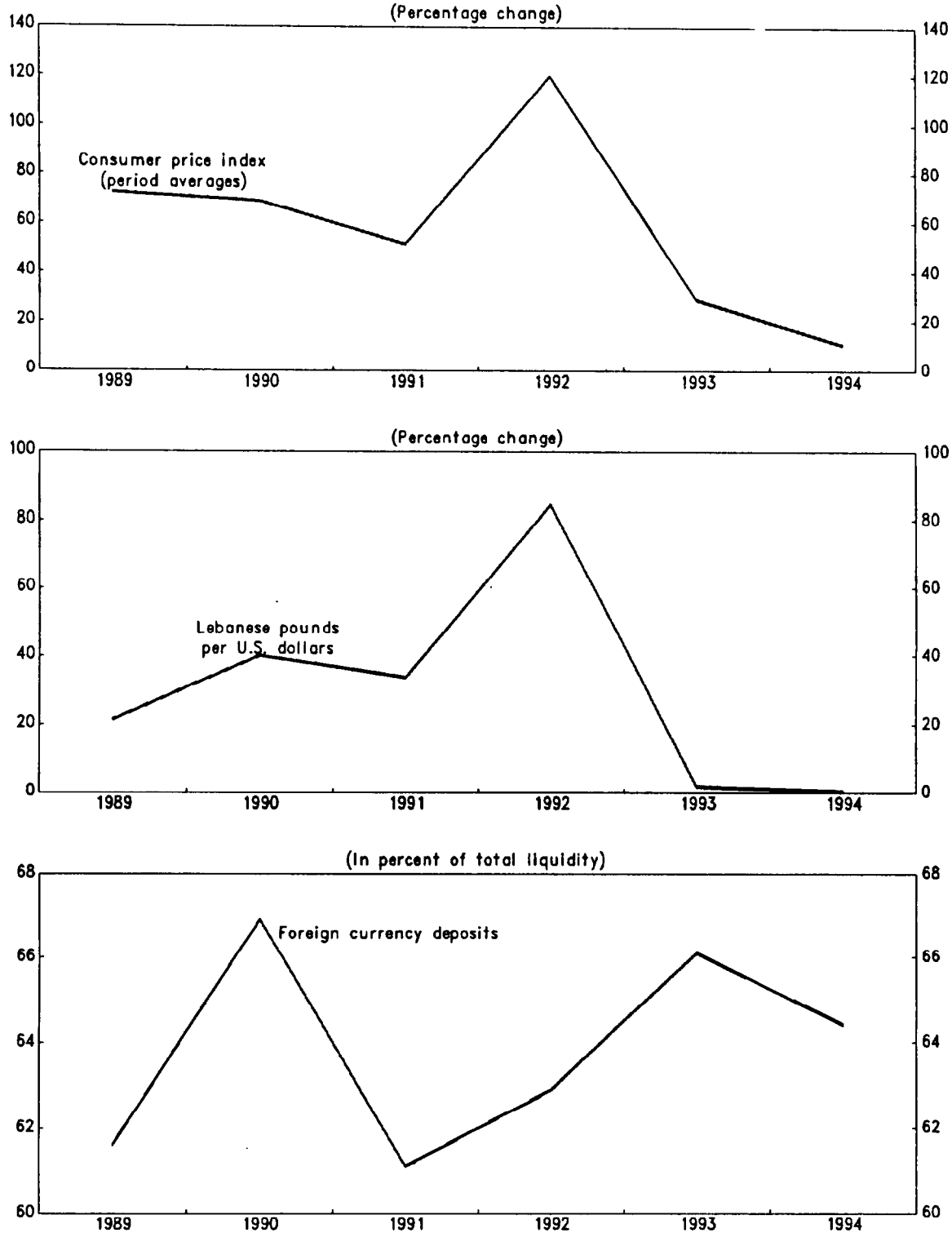
1/ For costs of the war, see Section I of the accompanying report on "Lebanon--Economic Recovery, Stabilization, and Macroeconomic Policies."

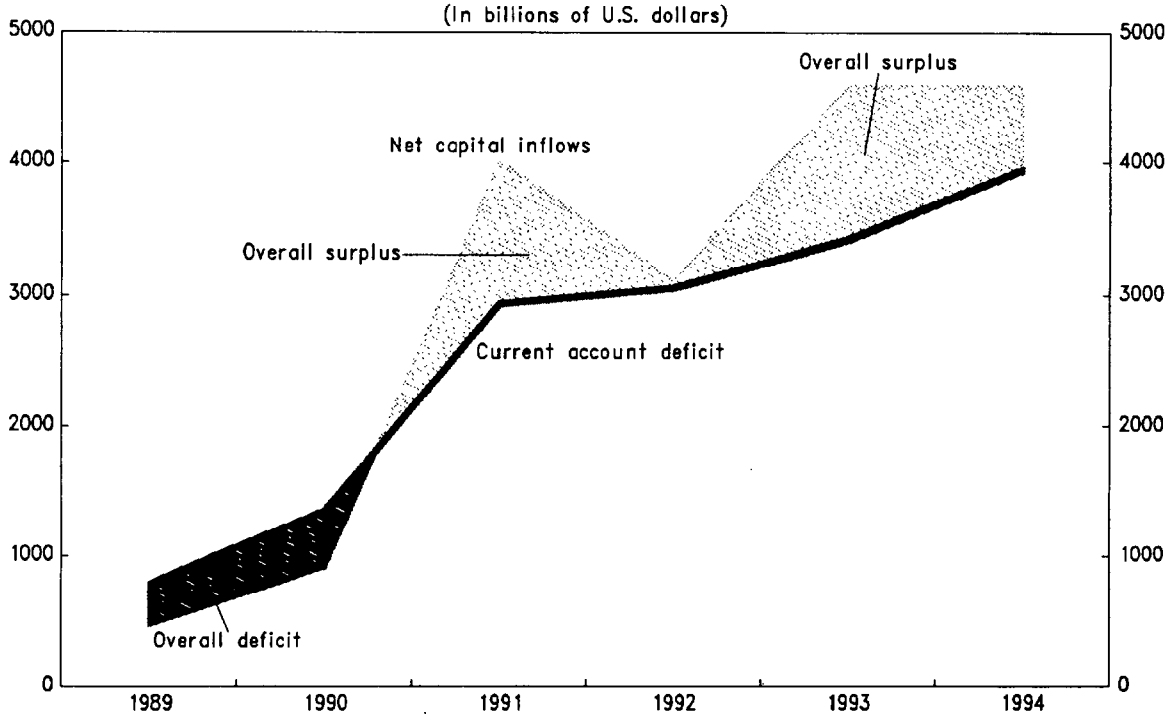
2/ Staff analysis of developments and prospects continues to be hampered by the lack of reliable and consistent data on key sectors of the economy, notably the real and external sectors (Appendix III).

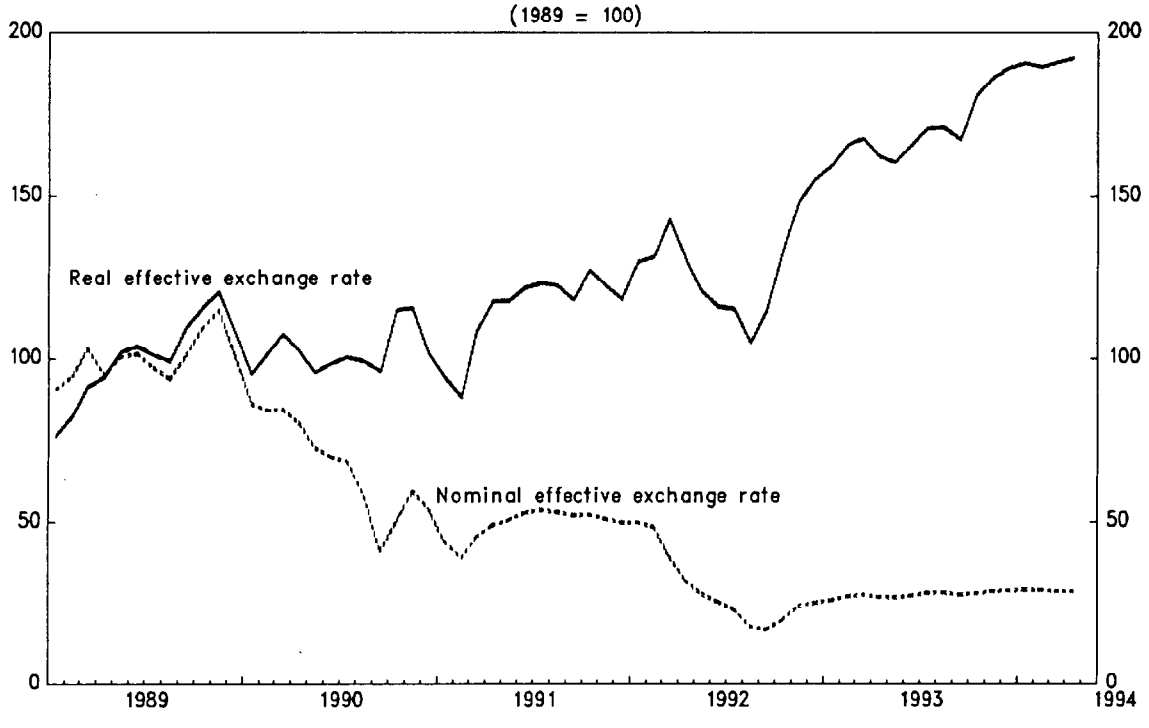
CHART 1
LEBANON
INFLATION, DEPRECIATION OF THE LEBANESE POUND, AND DEMAND FOR FOREIGN CURRENCIES, 1989-94



Sources: IMF, International Financial Statistics; and Consultation and Research Institute, Beirut.

CHART 2
LEBANON
BALANCE OF PAYMENTS AND EXCHANGE RATE MOVEMENTS, 1989-94





Sources: Bank of Lebanon; and Fund staff estimates.

imports, up from about 4.6 months at end-1992. 1/ These macroeconomic developments were facilitated by improved political stability, increased confidence, an exchange and trade system free of restrictions, and an effective adjustment effort.

On the policy side, the overall fiscal deficit as a percentage of total expenditure was reduced by 15 percentage points to 37 percent in 1993, or in terms of GDP from about 12 percent in 1992 to 8 percent in 1993 (Appendix I, Table 2, and Chart 3). 2/ This reduction was brought about by a sharp increase in total revenues, with tax revenues going up by 91 percent. Import duties more than doubled as a result of administrative improvements and tighter control over ports of entry. Nontax revenues rose by almost two thirds, reflecting better collection procedures, upward adjustments in telecommunications and electricity tariffs, and a more realistic assessment of property values for purposes of collection of real estate fees. Meanwhile, the increase in total expenditure was contained to 33 percent, with a tighter expenditure stance and delays in the implementation of the reconstruction program. However, interest payments on domestic debt increased by two thirds and accounted for more than one quarter of total spending and two thirds of the overall deficit. The budget deficit was financed almost entirely from domestic sources, with net bank financing accounting for 80 percent of it. Sales of treasury bills to commercial banks and the nonbank private sector exceeded the financing needs of the budget, and the BDL used the sale of treasury bills in the primary market to stem the effect on the money supply of the large foreign capital inflows. Consequently, the nominal value of outstanding treasury bills rose by LL 1.3 trillion to LL 6 trillion by end-1993.

Monetary policy in 1993 was aimed at enhancing financial and exchange rate stability while providing adequate support for the reconstruction effort. Reflecting the prudent stance of monetary policy, narrow money (LL currency in circulation and LL-denominated demand deposits) actually declined by 5 percent, while the increase in broad money (narrow money plus LL and foreign currency denominated time and savings deposits) decelerated to 32 percent in 1993 from 114 percent in 1992 (Appendix I, Table 3). Measured in terms of the money stock at the beginning of the period, net claims on the public sector rose by only 6 percent, while credit to the private sector grew by 9 percent. Effective August 1993, commercial banks and financial institutions were given the option of placing dollar deposits with the BDL, so as to provide the monetary authorities with a potential means to influence the dollar money multiplier by altering the interest rate paid on these deposits.

1/ At end-1993, about US$302 million of subscriptions to the Lebanese Company for the Development and Reconstruction of Beirut Central District (SOLIDERE) had been deposited at the BDL and counted toward the increase in reserves.

2/ All GDP estimates are tentative and therefore, for purposes of measuring fiscal performance, the authorities prefer to use ratios to budgetary expenditures.

Meanwhile, interest rates remained high. The yield on three-month treasury bills rose from 13 percent at end-1992 to 21 percent at end-March 1993, but declined steadily to 17 percent by end-December. This decline partly reflected the introduction of auctioning of treasury bills starting in May for bills of 3-12 month maturities. The 24-month treasury bills, which are used by commercial banks as a benchmark for determining lending rates, continue to be sold "on-tap". By end-1993, commercial bank lending rates for Lebanese pounds were at about 29 percent, compared with only 12 percent for U.S. dollar-denominated instruments. While these rates discouraged borrowing in Lebanese pounds, commercial banks found it relatively attractive to invest their funds in high-yielding treasury bills. Bank holdings of treasury bills at end-December 1993 amounted to 87 percent of LL deposits, significantly above the investment requirements. 1/ Furthermore, the BDL increased its own portfolio holdings of treasury bills with a view to building a reserve to facilitate open-market operations in the future.

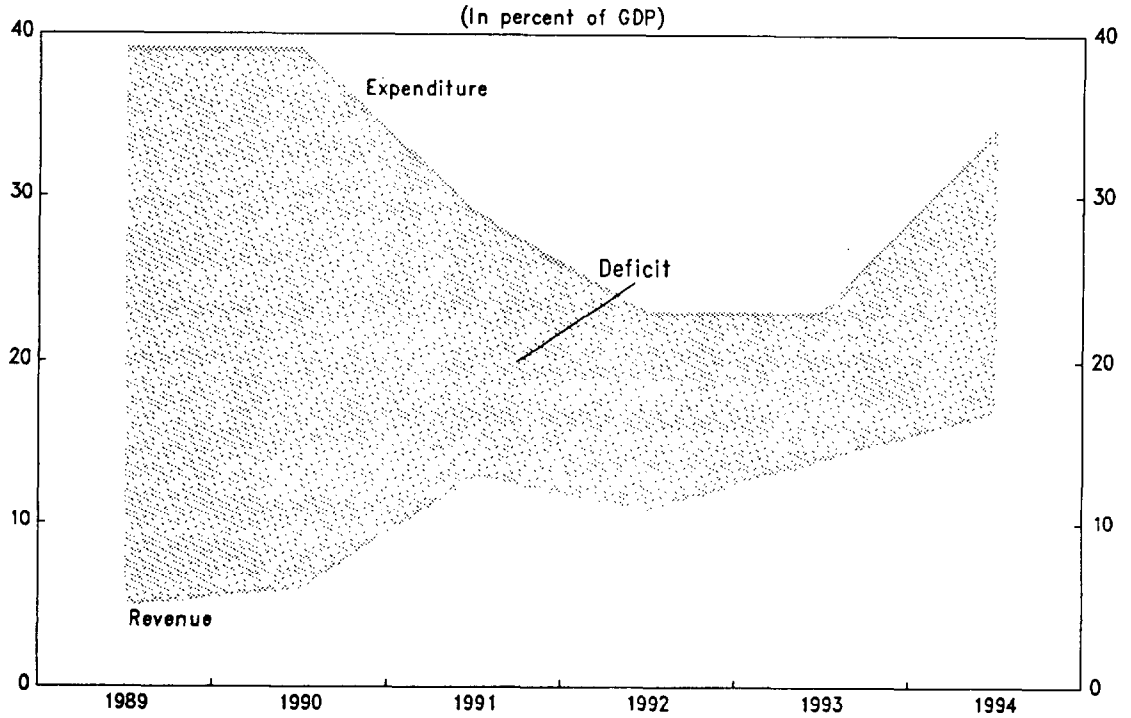
In response to the large capital inflows in the second half of the year induced by high LL interest rates, the BDL intervened in the foreign exchange market to moderate the appreciation of the pound against the U.S. dollar, and to build up further its cushion of foreign exchange reserves (Appendix I, Table 4). Despite this, the Lebanese pound appreciated vis-à-vis the U.S. dollar by 8 percent over the course of 1993, but the annual average exchange rate depreciated slightly in relation to 1992. Meanwhile, the real effective exchange rate continued to appreciate with inflation in Lebanon higher than that in its trading partners. 2/

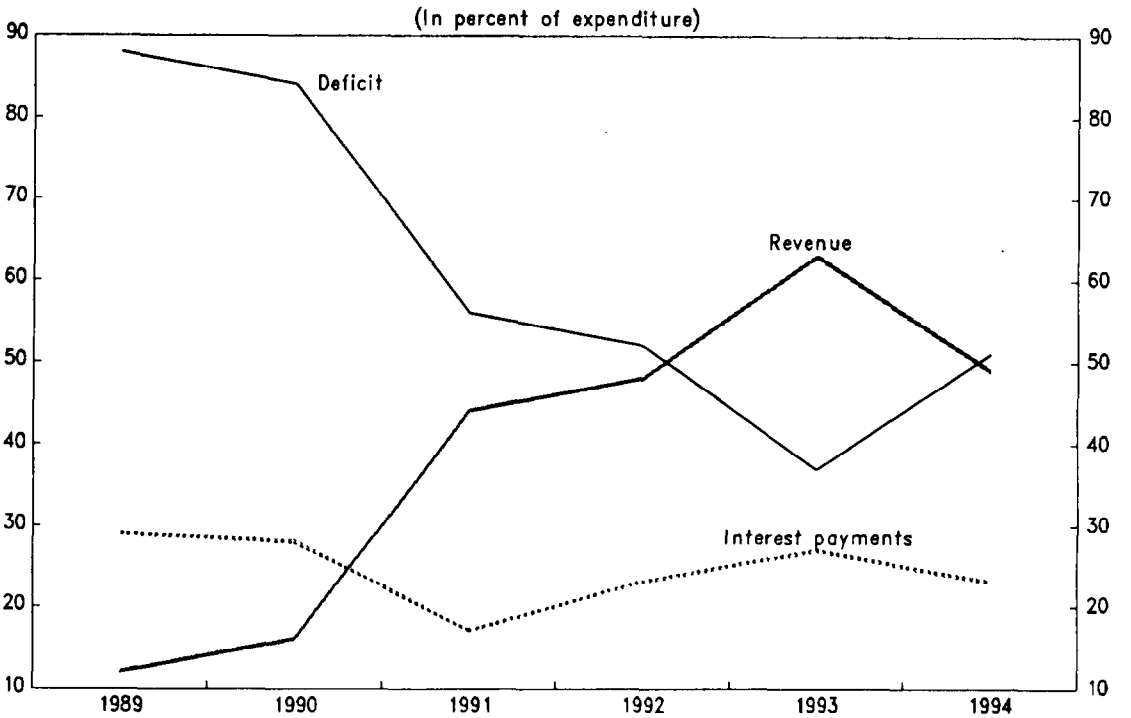
Preliminary information regarding developments in 1994 suggests that economic activity in the first quarter was more buoyant than in the corresponding period of last year, but had slowed in comparison with the last quarter of 1993, mainly reflecting some stagnation in investment activity and exports. The annual rate of change in consumer prices picked up in the month of March, resulting from the upward adjustments in electricity and telephone tariffs. However, indications are that inflationary pressures eased in April-May reflecting the slowdown in economic activity. Some dedollarization took place, as evidenced by the increased share of LL-denominated monetary aggregates in total liquidity. Reflecting this increased demand for intermediation in Lebanese pounds, the margin between LL-denominated deposit and lending rates continued to narrow. Meanwhile, the strong demand for treasury bills maintained the declining trend in treasury yields (below 16 percent in June). On the external side, foreign exchange reserves of the BDL rose sharply with continued large capital inflows.

1/ In addition to a 10 percent cash reserve requirement deposited with the BDL, commercial banks are required to invest 63 percent of their Lebanese pound deposits in treasury bills.

2/ On the basis of unofficial price indices, the real effective exchange rate is estimated to have appreciated by about 20 percent during 1993.

CHART 3
LEBANON
FISCAL TRENDS, 1989-94





Sources: Ministry of Finance, and Fund staff estimates.

III. Report on Discussions

Lebanon has an ambitious program of postwar reconstruction and development, the initial stage of which is embodied in the National Emergency Reconstruction Program. The private sector is also expected to contribute significantly to the rehabilitation of the economy. At the same time, the authorities' macroeconomic policies are directed at achieving price and exchange rate stability, which are considered to be priorities of paramount importance in view of the impact of confidence and expectations on economic performance in Lebanon. Given these objectives, the discussions focused on an assessment of the outlook and policies for 1994 and for the medium term. Broadly, policies in 1994 and beyond will need to be geared toward underpinning financial stability, while providing adequate resources to support reconstruction and pressing social needs so as to foster sustained economic growth and ensure external sector viability. In this regard, it is essential to increase domestic saving, formulate a public investment program compatible with the implementation capacity and the availability of external resources, reduce pressure on interest rates, free up savings for private sector investment, ensure the efficient allocation of resources, and maintain a competitive exchange rate.

1. Short-term outlook and policies

The authorities started 1994 with the aim of consolidating the improvements in macroeconomic and financial stability achieved in 1993, and accelerating the reconstruction program through investments in the real sector. They targeted a real growth in GDP of 7 percent with a pickup in reconstruction investment in the second half of the year, a deceleration in the annual rate of inflation to about 10 percent, a stable nominal exchange rate for the rest of the year, and a further buildup in foreign exchange reserves.

The 1994 budget was formulated with a view to making a determined effort to accelerate the process of rehabilitating the economy and rebuilding the country's infrastructure. This stance, with no new major tax measures, implied a significant widening of the overall deficit. In light of more recent information, budgetary projections were subsequently revised by the authorities, taking into account the better than expected revenue outturn in 1993, some anticipated improvement in nontax revenue, as well as higher expenditure estimates. The latter takes into account wage increases, 1/ "big projects" to be financed by a Eurobond issue, 2/ a revision of capital expenditures, and a recent government decision to finance the relocation and

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1/ In view of the deterioration of real wages, the authorities granted, effective January 1994, a 68.9 percent increase in the minimum wage from LL 118,000 per month to LL 200,000, with higher wage levels adjusted upward on the basis of a graduated scale.

2/ "Big projects" include investments related to sewer systems, telephone lines, and roads.

rehabilitation of Lebanese nationals displaced by various disturbances, particularly in the south. As a result, in the revised projections the overall budget deficit widens by 10 percentage points to 18 percent of GDP in 1994.

The revised projections assume that revenues would increase by 40 percent, mainly due to discretionary measures and the reassertion of government authority. Such an increase takes into account substantial upward adjustments (by as much as 10 times for some cases) in fees and charges effective January 1, 1994, the full year effects of the new valuation system instituted last year for assessing real estate fees, additional efforts at improving revenue collection through better tax administration and strengthened enforcement, and the tax amnesty which will both expand the tax base and enable collections of some back taxes from 1991-93. Meanwhile, total expenditures are projected to rise by 81 percent. This sharp rise is due mainly to the planned increase in capital spending for reconstruction from LL 200 billion in 1993 to LL 1.6 trillion in 1994, the near doubling of the wage bill, assuming no further salary adjustments than those granted in January and no increase in the civil service workforce with the recently initiated civil service reform, 1/ and a projected increase of about 60 percent in interest payments, on the assumption that domestic interest rates on treasury bills remain at their current levels. 2/ Of the projected overall deficit of about LL 2.8 trillion, over LL 1.5 trillion (10 percent of GDP) is envisaged to be financed from domestic sources.

The mission noted that the envisaged budgetary stance was overly expansionary and had adverse implications for the macroeconomic situation in 1994. More specifically, it could result in a weakening of confidence, adversely affect exchange rate and price stability, and possibly crowd out the private sector in the credit market. Furthermore, it would strain the scope for maneuver in the medium term. While the staff appreciated the urgent political and social needs behind certain expenditures in 1994, it urged the authorities to give serious consideration to additional measures with a view to improving the budgetary performance in this year. The authorities felt that private sector activity was unlikely to pick up significantly during 1994, and that the public sector would need to account for most of the targeted growth for this year. Furthermore, they viewed the planned infrastructure investments by the public sector as essential for the promotion of future private sector investment. However, they indicated that capital outlays during the first half of the year had been limited due to administrative bottlenecks, and hence the revised estimate for capital expenditure in 1994 was unlikely to be realized. The authorities did not

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1/ For details on the civil service reform and other fiscal measures, see Section II of the accompanying report on "Lebanon--Economic Recovery, Stabilization, and Macroeconomic Policies."

2/ As regards defense expenditure, the 1993 budget appropriation was LL 476 billion (3.6 percent of GDP and 16 percent of total expenditure) and such expenditure was budgeted to rise to LL 540 billion (3.5 percent of GDP and 10 percent of total expenditure) in 1994.

foresee any significant additional revenue measures in the current year, other than some possible sales of government assets (mostly vacant property). Finally, the authorities noted that the deficit in 1994 would be significantly smaller were it not for certain unforeseen exceptional expenditures (essentially related to unsettled conditions in the south) for which aid grants had been expected.

On the monetary side, the authorities indicated that their primary objective was containing inflationary pressures. Low and falling inflation would also, in principle, assist in dedollarizing the economy, and allow for lower interest rates. However, the authorities noted that Lebanon was embarking on the unusual and difficult task of simultaneous economic stabilization and reconstruction, and, therefore, monetary policy would also need to take account of pressing social needs and the capital requirements of public investment. In the first quarter of 1994, total liquidity increased by 6.8 percent. Of this increase, a major part was accounted for by a sharp rise in claims on the private sector. 1/ Furthermore, the dollar value of foreign currency deposits fell for the first time since October 1992, 2/ while claims on the private sector in foreign currency, as a share of foreign currency deposits in commercial banks, exceeded the 55 percent ceiling for on-lending of dollar deposits.

For the year as a whole the authorities have no prespecified target for foreign exchange reserves, but the accumulation of reserves is viewed as an important instrument toward the achievement of the objectives of exchange rate and monetary stability. Staff calculations, which were discussed with the authorities, indicate that to assist in attaining monetary stability in 1994, the authorities would need to aim at limiting the growth of liquidity to about 16 percent. 3/ Given the financing needs of the budget requiring an expansion of credit to the public sector of about 40 percent, in conjunction with the envisaged increase in credit to the private sector of about 11 percent, the implied increase in net foreign assets amounts to about US$640 million. Such a scenario, however, implied that outstanding claims of the banking system on the private sector at end-1994 would decline from its level at end-March 1994. Unless private sector activity in the remainder of 1994 remains subdued, the envisaged financing needs of the public sector might well result in compromising the inflation objective of the authorities and/or a lower buildup of net foreign reserves. In response, the authorities argued that techniques used in estimating the demand for money might have yielded too conservative a growth in liquidity. Moreover, they felt that an assumption of further declines in velocity stemming from increases in

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1/ This pickup was associated with large-scale borrowings in U.S. dollars, which were then deposited into the banking system as LL deposits.

2/ See Section III of the accompanying report on "Lebanon--Economic Recovery, Stabilization, and Macroeconomic Policies" for details on currency substitution and dollarization.

3/ See Section IV of the accompanying report on "Lebanon--Economic Recovery, Stabilization and Macroeconomic Policies" for details of the estimation of money demand in Lebanon.

confidence could allow for a larger expansion in credit without compromising their macroeconomic objectives. They also indicated that, given the outstanding level of foreign reserves, the buildup of BDL reserves could be eased, if during the year the economic costs of this policy is seen to outweigh the benefits.

The mission endorsed the efforts of the authorities to strengthen their monetary policy instruments. In this regard, the BDL envisages issuing in the near future dollar-denominated certificates of deposits as an additional means to control the dollar money multiplier. Furthermore, for prudential purposes and to enhance control over credit expansion, the BDL intends to enforce more vigorously the 55 percent ceiling for on-lending of dollar deposits at commercial banks. Also, the reserve and liquidity requirements as a whole are being reviewed to determine the extent of the relative disadvantage to intermediation in LL from the current system. As a means to control the LL component of money supply, the mission recommended less reliance on treasury bills since the BDL does not have complete autonomy over their issuance, and proposed the development of other instruments, such as repurchase agreements and certificates of deposit. The authorities argued that LL-denominated certificates of deposits would compete directly with treasury bills, but saw merit in enhancing the use of repurchase agreements. The mission agreed with the authorities that the BDL should be operating through the secondary market to undertake operations, rather than directly via the primary market for treasury bills, and that the development of secondary securities markets would facilitate the achievement of that goal.

The authorities are giving high priority to the development of financial markets and are fully aware that as the reconstruction and redevelopment of the economy gets underway, reform of the financial sector will assume considerable importance. To this end, they are currently reviewing the treasury bill auction system, following the recommendations of the recent Fund technical assistance mission, and intend to extend the auction system to 24-month treasury bills and increase the transparency of auctioning methods. To increase the volume of transactions in the Beirut secondary market, which started operations in June 1994 with the trading of SOLIDERE shares, new directives are being prepared to allow commercial banks to issue certificates of deposit (both in LL and U.S. dollars), and treasury bills will be changed to bearer form. On banking regulations, the authorities confirmed that supervision and control practices were being realigned with international standards, and that actual average capital adequacy ratios had already reached about 7 percent, ahead of the scheduled date of August 15, 1994. The authorities are also considering actively a number of reforms along the lines of the recent World Bank technical assistance recommendations in this regard, including the development of equity and bond markets, the creation of nonbank investment instruments such as mutual funds, and the development of contractual savings, such as insurance, pension funds, and social security.

The authorities were appreciative of the Fund's technical assistance. They noted that most of the recommendations of technical assistance missions related to monetary and fiscal matters were being taken into account in the formulation of policies and reforms. They hoped that the Fund would continue

to support any follow-up missions that may be required to complete tasks that were originally set out by previous missions, and react favorably to future requests for much-needed technical assistance. While in broad terms Lebanon was making effective use of technical assistance provided by the Fund, there was slow progress in implementing recommendations in the statistical area (Appendix III). This shortcoming was associated largely with inadequate staffing or the lack of other technical resources to devote to these tasks, and was expected to be addressed as soon as possible. The mission underscored that addressing these statistical issues and accelerating the process of building a consistent and comprehensive data base for Lebanon were essential for close monitoring of economic and financial developments and for facilitating more informed policy decisions.

2. Prospects and policies for the medium term

The staff, in consultation with the authorities, prepared a medium-term macroeconomic scenario on the basis of the authorities' objectives and policies (Appendix I, Table 5, and Appendix II). The scenario aims at achieving a rate of real economic growth of about 8 percent per annum during 1995-98, a gradual decline in inflation to that of trading partners by 1998, and maintaining international reserves high enough to enhance confidence in the domestic economy. The relationships underlying the scenario are not unequivocal and, essentially, the confidence factor will be the linchpin.

The authorities recognize that the firm anchoring of financial stability requires a reduction in the budget deficit, limited total debt accumulation over the medium term, and a path for monetary expansion consistent with the growth in real money demand over the period of reconstruction. Therefore, despite strong pressures in the Parliament to move ahead rapidly with the reconstruction and rehabilitation expenditures and not to increase taxes, the authorities are proceeding pragmatically to improve government finances. The medium-term budgetary projections, which incorporate the authorities' intentions with regard to revenue-enhancing measures and their envisaged timing, as well as the public expenditure program indicated by the Lebanese representatives, show an increase in the budget deficit as a percent of GDP to about 20 percent in 1995, before declining thereafter to about 6 percent by 1998. Assuming that all of the deficit is debt-financed and taking into account the envisaged external financing, total public debt would approach 75 percent of GDP by 1996, and subsequently decline to 71 percent of GDP by 1998. Meanwhile, interest payments on domestic and external debt would fall from about half of total revenue in 1994 to one fifth by 1998. External public debt, which is currently at low levels, would increase to about 34 percent of GDP by 1998, and to an even higher ratio if account is taken of foreign purchases of treasury bills.

The mission welcomed the authorities' intended revenue-enhancing and expenditure-containment measures to improve the savings performance of the public sector over the medium term (Appendix II, Section I). However, it noted that during 1995-96, deficits would still remain at very high levels. In addition, critical measures, such as the introduction of a general sales tax (GST) and phasing out the fuel subsidy, are deferred until 1997.

Furthermore, the size and the envisaged speed of the public investment program raised questions regarding its compatibility with the absorptive capacity of the economy, its realism given constraints on the speed of its implementation, and the availability of external financing on appropriate terms (including soft loans and grants) as envisaged earlier. In the circumstances, the mission expressed concern that deficits of these magnitudes in the near future could threaten the achievement of the authorities' medium-term macroeconomic objectives as a whole, weaken confidence in economic management, and put at risk the authorities' stabilization policies.

The medium-term balance of payments projections indicate substantial current account deficits over the projected period which, together with some foreign exchange reserve accumulation, would necessitate unusually large capital inflows relative to the size of the economy and external current account receipts. The mission noted that, in the case of Lebanon, a significant portion of capital inflows could reflect the underestimation of current receipts, in particular private transfers (principally by expatriate Lebanese) and expenditure on tourism-based services. The mission also noted that the authorities were improving the capital and equity markets to guide these flows into productive investments and promote direct investment. Even allowing for a favorable outcome for these developments, other capital inflows in the medium-term balance of payments scenario would still need to be very large. The realization of these inflows will hinge on the maintenance of sound and stable domestic financial conditions, and on the continuance of significant real interest rate differentials.

The attainment of the capital inflows assumed in the medium-term scenario would be expected to expand Lebanese pound liquidity and be channeled through the banking system as domestic credit. To the extent that domestic financing of the projected budget deficits reflects the channeling of capital inflows into purchases of treasury bills, and that private investments also depend on these capital inflows, the envisaged financing could be vulnerable to exogenous shocks. In addition, these capital inflows raise the potential for pressure on the Government to support financial institutions in the event of any reversal in such inflows. In this context, the mission welcomed the continuing efforts of the authorities to strengthen banks' capital bases and improve banking supervision and prudential standards.

The mission argued that the above-described medium-term scenario underscored the need to strengthen rapidly the savings performance of the economy so as to ensure a stable flow of funds for the reconstruction effort. On the external side, given the large import needs associated with reconstruction, this would imply improvements in the export performance of the goods and services sectors. In this regard, the mission underscored the need to ensure the competitiveness of the Lebanese economy. The authorities indicated that exchange rate policy was currently geared to maintaining a stable nominal rate, with limited fluctuations. Given the turbulence and substantial volatility experienced by the pound during 1989-92, the large degree of openness of the economy, and the direct links between exchange rate

movements and domestic inflation, the authorities considered that exchange rate stability would lead to a reduction in expectations of inflation and promote price stability. 1/ They also expected that the nominal exchange rate anchor policy and exchange rate stability could help to reduce wage demands, leading to a reduction in both the rate of inflation for nontraded goods and services and in the Government's budget deficit.

The mission noted the authorities' preference at this stage of promoting confidence and stability for the exchange rate to serve as the nominal anchor. However, it questioned the compatibility and the sustainability of such an exchange rate policy with the current fiscal policy stance, and indicated that, under unchanged policies, Lebanon's external current account would come under increasing pressure on account of the continued appreciation of the real effective exchange rate. In this context, the mission emphasized that with a stable nominal exchange rate, the only means of preventing excess demand and avoiding real appreciation in the face of large capital inflows was a significant and rapid reduction in the fiscal deficit. Otherwise, in order to contain monetary expansion, capital inflows would need to be sterilized, thereby maintaining interest rates higher than they would otherwise be, raising the cost of servicing domestic debt, and further stimulating capital inflows. The mission also argued that at the appropriate time, the authorities could gradually reassert the role of the exchange rate as a policy tool by shifting the burden of stabilization to the monetary aggregates. This would send a signal to economic agents that the authorities were not willing to support any given nominal rate at the cost of possible disequilibria in the real exchange rate. Such a stance would be consistent with Lebanon's long-established tradition of operating a market-determined exchange rate mechanism, with intervention limited to smoothing out abnormal short-term fluctuations. However, such a policy would again need to be accompanied by appropriate fiscal adjustments to ensure both financial stability and balance of payments viability.

Against this background the mission recommended that the authorities give consideration to a significantly more rapid fiscal adjustment in 1994 and the next two years, particularly by accelerating the timing of adjustment measures relative to the present schedule, which is substantially backloaded. In this regard, and in line with the recommendations of fiscal technical assistance missions of the Fund, the mission encouraged the authorities to: (a) hasten preparations to implement fully the GST earlier; (b) introduce a minimum profit tax of 1 percent of the previous year's turnover; (c) adopt as soon as possible the market value of the exchange rate for calculating import duty, and immediately implement the customs tariff reform; and (d) implement the excise tax reform without delay. The mission also suggested that duties and taxes on petroleum products be collected by the Customs Department before

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1/ For the relation between exchange rate movements and inflation, see Chapter V of the accompanying report on "Lebanon--Economic Recovery, Stabilization, and Macroeconomic Policies."

the release of goods, so as to minimize collection lapses and lags, and recommended that revenue resulting from the increase in taxation of tobacco and cigarettes be transferred to the budget and not remain in the hands of the tobacco monopoly.

On the expenditure side, the mission underscored the need to accelerate the reform of the civil service, to exercise caution with regard to wage increases, to eliminate all fuel subsidies as soon as possible with a full pass-through of electricity costs, to intensify efforts in collecting payments of electricity bills (eliminating illegal tapping of electricity lines, and adjusting electricity tariffs as necessary), and to reorder spending priorities away from unproductive spending toward reconstruction. On capital expenditure, the mission stressed the importance of limiting outlays to remunerative projects with clearly identified sources of external financing, establishing relative priorities for the various components of the investment program, and allocating sufficient resources to ensure adequate provisions of social services. The mission welcomed the stated intention of the authorities to substitute build-operate-transfer (BOT) schemes for some major development projects that would otherwise be undertaken by the CDR, as well as their plans for privatization and asset sales, and recommended their acceleration. Receipts from such operations could be used to retire public debt with a view to reducing interest expenditures. In addition, the planned shift of budgetary capital expenditure to the private sector could also help in slowing down the projected increase in public external and domestic debt.

The mission emphasized the need to consider carefully the impact on the economy of a considerable debt accumulation over the medium term. In this connection, it was noted that Lebanon has had substantial promises of regional and international aid, and had a case to present in the context of the ongoing Middle East peace process. The mission encouraged the authorities to pursue vigorously these avenues and present Lebanon's needs and claims in the context of a comprehensive program of rehabilitation.

The authorities underscored that Lebanon has recently come out of a 15-year civil war and was faced with enormous challenges. In the circumstances, they were aiming to strike a balance between stabilization on the one hand and the regeneration of economic activity on the other. The authorities, noting its concerns, assured the mission that despite the unusual reconstruction and rehabilitation requirements in the post-conflict era, which must be met as soon as possible, the Government was determined that the reconstruction program be consistent with macroeconomic stability and the availability of external financing at appropriate terms.

IV. Staff Appraisal

Lebanon's economic and financial performance in 1993 was very favorable, when measured against the outturn in 1992 and the benchmarks established during the last Article IV consultation. Real GDP growth picked up, inflation decelerated sharply, foreign exchange reserves were built up to a comfortable level, and the exchange rate stabilized. These developments were facilitated by improved political stability, elevated confidence, a completely open trade and payments system, and an effective adjustment effort, for which the authorities should be commended. With regard to reconstruction, the effort in this area lagged behind expectations, due mainly to implementation constraints.

The authorities started 1994 with the objectives of consolidating the improvements in macroeconomic and financial stability achieved in the recent past, as well as accelerating the program for reconstruction of the economy. However, these tasks have become more difficult as a result of political and security circumstances that imposed additional demands on government resources. The revised fiscal projections now envisage a widening of the fiscal deficit by about 10 percentage points of GDP. The staff considers such a budgetary stance overly expansionary, and is concerned that it is likely to have adverse implications for the attainment of the authorities' key macroeconomic objectives and would strain the scope for maneuver in the medium term. In particular, there is the risk that the envisaged public sector financing needs in 1994 could compromise the inflation objective of the authorities, thereby endangering the revival of confidence in the economy. Therefore, the staff urges serious consideration of additional measures to improve budgetary performance this year. The authorities emphasized that the fiscal situation in 1994 came under pressure largely because of circumstances beyond their control. The overall strategy was not changed and the Government intends to pursue with vigor the objective of continued financial stability.

The staff agrees with the Lebanese authorities' basic economic strategy, which aims at meeting the reconstruction and rehabilitation requirements of physical and social infrastructure while maintaining economic and financial stability. Over the medium term, the achievement of these objectives will require increases in domestic savings, improvements in the efficiency of investments, and a public expenditure program consistent with financial stability. In this context, the staff welcomes the authorities' intended revenue and expenditure measures, which will improve substantially the savings performance of the public sector over the medium term. However, during the next two years deficits would still remain at high levels, and total public debt would increase rapidly. Furthermore, the envisaged pace of the investment program may not be compatible with the availability of external financing. In the circumstances, the staff is concerned that these developments could weaken confidence in economic management, and put at risk the authorities' medium-term stabilization goals. Therefore, it is recommended that the authorities give consideration to a significantly more rapid fiscal adjustment in 1994 and the next two years, particularly by

accelerating the timing of adjustment measures relative to the present schedule, and the careful review and setting of priorities for the public investment program. The staff welcomes the authorities' plans for substituting BOT schemes for some major planned development projects, privatization and asset sales, and recommends their acceleration. Such operations could be used to retire public debt, and would be helpful in slowing down the projected buildup in public external and domestic debt.

The strengthening of the fiscal position should allow the authorities to redirect credit increasingly to the private sector, and promote investment while maintaining a restrained monetary stance. Such a stance would be aided by the ongoing efforts of the authorities to enhance both their monetary policy instruments and the role of market forces in determining interest rates. The staff also endorses the envisaged financial sector reforms, which should help in the mobilization of resources for the private sector and ensure their efficient allocation, as well as the efforts of the authorities to strengthen banking supervision and prudential regulations.

The continued large external current account deficits projected over the medium term, together with some foreign exchange reserve accumulation, would require sustained and very large capital inflows relative to the size of the economy. The realization of these inflows could necessitate the continuance of sufficiently attractive interest rate differentials. Furthermore, these capital inflows would render both government finances and private sector investments vulnerable to exogenous shocks, and hence could threaten financial stability. The staff believes that the above-described medium-term projections, given the large import needs associated with reconstruction, underscore the need to strengthen the export performance of the goods and services sectors. In this regard, it is essential to ensure the competitiveness of the Lebanese economy. The staff notes the authorities' preference, at this stage of the reconstruction program, for the exchange rate to serve as a nominal anchor to assist in the development of confidence and stability. However, such a policy together with the current fiscal stance is likely to affect adversely financial stability and maintenance of competitiveness. The staff believes that at the appropriate time, the authorities could gradually reassert the role of the exchange rate as a policy tool, and avoid supporting any given nominal rate at the cost of possible real exchange rate disequilibria. However, a Lebanese economy operating with either exchange rate stance would need to initiate a meaningful and rapid reduction in the fiscal deficit to ensure both financial stability and balance of payments viability.

While continuing to link external financing to remunerative projects, the authorities need to consider carefully the impact on the economy of a considerable accumulation of debt over the medium term. In this connection, possible sources of regional and international aid would need to be pursued vigorously, and Lebanon's needs and claims presented in the context of a comprehensive medium-term program of rehabilitation. Lebanon is fortunate at the present time in having relatively easy access to international financial markets, but this should not mean that the country is not in need of external aid, or that such access is unlimited.

Finally, Lebanon's database remains weak and hampers economic analysis. The staff urges accelerated efforts to improve the data base, in particular related to the real and external sectors, and vigilance in monitoring both public and private sector external debt obligations.

The next Article IV consultation is expected to be on the standard 12-month cycle.

Table 1. Lebanon: Selected Social, Economic, and Financial Indicators, 1989-94

I. Social and Demographic Indicators

Area	Population	Density (1988)
10.4 thousand sq km	2.9 million (est.) Rate of growth (percent): 2.0	258 per sq km 863 per sq km of arable land

Population characteristics	
Labor force (thousands)	941.0
Life expectancy at birth	66.0 years
Infant mortality (aged under 1 year, percent)	4.6
Child death rate (aged 1-4 years, percent)	5.9
Income distribution	
Percent of private income received by:	
Highest quintile	55
Lowest quintile	4
Access to safe water	
Percent of population - rural	77

Health	
Population per physician	537
Population per hospital bed	200
Nutrition	
Per capita calorie intake (per day)	3,247
Per capita protein intake (grams per day)	86
Energy consumption per capita	
Kg of oil equivalents	968

II. Economic and Financial Indicators

	1989	1990	1991	1992	Target 1993	Est. 1993	Proj. 1994
	(Annual percent change)						
National income and prices							
Real GDP 1/	-42.2	-13.4	38.2	4.5	5.0	7.0	7.0
Consumer prices (period average)	72.2	68.8	51.5	120.0	28.9	29.1	10.6
Consumer prices (end of period)	89.0	84.1	31.3	170.2	5.3	8.8	4.2
External sector							
Exports (f.o.b.) U.S. dollar basis	-23.0	2.5	-1.2	22.7	53.9	14.1	20.3
Imports (f.o.b.) U.S. dollar basis	-6.0	13.9	45.4	0.6	13.7	12.0	19.4
Nominal effective exchange rate (-depreciation)	-14.2	-33.4	-26.4	-41.5	...	-4.5	...
Real effective exchange rate (-depreciation)	41.7	7.3	6.5	24.3	...	19.7	...
Central Government							
Revenue	198.1	98.1	313.1	102.8	66.0	75.1	40.2
Expenditure	91.3	47.5	53.7	85.5	46.0 2/	33.3 2/	81.4 2/
	(Change in percent of broad money at the beginning of period, unless otherwise stated)						
Money and credit							
Net domestic credit, of which:	24.3	45.8	15.8	70.5	14.1	15.6	12.0
Net claims on Government	17.6	18.1	4.7	19.0	8.6	6.3	7.8
Claims on private sector	6.7	27.7	11.1	51.5	5.5	9.3	4.2
Money and quasi-money	13.4	56.3	43.7	114.3	18.4	32.1 3/	16.4 3/
Velocity (GDP/broad money)	0.547	0.512	0.746	0.800	0.933	0.834	0.851
Interest rates (end of period 3-month treasury-bills)	18.8	18.8	15.0	13.0	17.0	17.2	...

Table 1 (concluded). Lebanon: Selected Social, Economic, and Financial Indicators, 1989-94

	1989	1990	1991	1992	Target 1993	Est. 1993	Proj. 1994
				(In percent of GDP) 4/			
Consumption 5/	142	146	145	135	125	...	115
Investment 5/	20	20	20	20	24	...	31
Central Government							
Revenue	4.7	6.4	12.6	11.1	14.0	14.1	16.7
Expenditure	39.1	39.4	28.9	23.4	23.3 2/	22.5 2/	34.5 2/
Overall deficit	34.4	33.0	16.3	12.2	9.3	8.4	17.8
Exports (f.o.b.)	17.8	17.5	11.0	10.8	12.3	9.1	9.0
Imports (f.o.b.)	-83.2	-90.8	-84.2	-68.0	-56.9	-56.0	-55.0
External current balance (excluding official transfers)	-28.9	-47.6	-65.9	-55.1	-40.9	-45.3	-43.1
				(In percent of total expenditure)			
Central Government							
Revenue	12.1	16.2	43.7	47.7	60.0	62.7	48.5
Overall deficit	87.9	83.8	56.3	52.3	40.0	37.3	51.5
				(In millions of U.S. dollars)			
External sector							
Exports, f.o.b.	484	496	490	601	925	686	825
Workers' remittances	480	280	180	200	300	300	320
Imports, f.o.b.	-2,263	-2,578	-3,748	-3,770	-4,288	-4,222	-5,039
Current account (excluding official transfers)	-785	-1,351	-2,935	-3,053	-3,080	-3,417	-3,944
Overall balance (+ surplus)	-309	-431	1,074	54	100	1,170	640
Central bank liquid reserves (e.o.p.)	907	623	1,237	1,448	1,568	2,220	3,210
(As months of current year's imports)	4.8	2.9	4.0	4.6	4.4	6.3	7.6
External debt outstanding (e.o.p.) 6/	332	332	332	273	...	352	832
External debt service payments							
Principal	...	....	...	...	...	47	77
Interest	...	...	...	...	...	24	34
Debt service (as percent of current receipts)	...	...	...	...	...	5	7
				(Lebanese pounds per U.S. dollar)			
Exchange rate (year average)	497	695	928	1,713	1,744	1,741	1,695
(end of period)	505	842	879	1,838	1,730	1,711	1,690
				(In billions of Lebanese pounds)			
GDP 4/	1,350	1,973	4,132	9,499	13,122	13,122	15,528

Sources: Ministry of Finance (MOF), Bank of Lebanon (BDL); IBRD; Council for Development and Reconstruction (CDR); and Fund staff estimates.

1/ Based on IBRD, MOF, CDR, and Fund staff estimates.
2/ Includes capital (reconstruction) expenditures for CDR.
3/ Includes SOLIDERE escrow deposits with BDL.
4/ GDP data are estimated on the basis of fragmentary information and are unreliable.
5/ IBRD data: "Country Strategy Note" dated July 12, 1993.
6/ Data currently being revised by the authorities.

Table 2. Lebanon: Government Finances, 1989–94 1/

	1989	1990	1991	1992	Budget 1993	Outturn 1993	Budget 1994	Revised Outlook 1994
				(In billions of Lebanese pounds)				
Revenue	64	126	522	1,059	1,701	1,855	2,246	2,600
Indirect taxes	4	4	132	467	864	806	1,044	1,044
Customs duties	2	2	98	323	700	662	825	825
Other	2	2	34	144	164	144	219	219
Direct taxes	15	37	90	46	285	172	360	250
Fees, dues, charges	8	15	79	93	150	179	210	210
Other	38	71	222	453	403	697	631	1,096
Of which: BDL profits	29	65	134	79	63	63	112	112
Expenditure 1/	528	778	1,196	2,219	3,400	2,957	5,106	5,356
Current expenditures	495	745	1,035	2,073	2,909	2,757	3,319	3,779
Wages and salaries	97	210	370	660	750	640	1,020	1,192
Other current 2/	147	276	425	750	1,428	1,152	1,344	1,197
Interest payments	152	214	206	519	731	784	810	1,245
Domestic	152	204	204	454	731	754	750	1,187
Foreign	1	10	2	65	...	30	60	58
EDL fuel subsidy 3/	99	46	35	145	...	181	145	145
Capital expenditures	33	33	161	146	491	200	1,787	1,577
Of which: foreign financed	--	--	--	--	--	52	1,300	1,225
Deficit	-464	-652	-674	-1,160	-1,699	-1,102	-2,860	-2,756
Financing	464	652	650	979	1,699	1,131	2,860	2,756
Foreign	-2	--	--	-108	...	190	1,300	1,225
Grants	...	--	--	--	...	52	...	...
Net borrowing	...	--	--	-108	...	138	...	...
Disbursements	...	--	--	--	...	219	...	...
Amortization	...	--	--	-108	...	-82	...	-131
Domestic	466	652	650	1,087	1,699	941	1,561	1,531
Banking system	400	576	183	1,055	...	751	...	...
BDL	120	446	-424	-668	...	-119	...	...
Commercial banks	279	130	607	1,722	...	870	...	...
Nonbank private	67	76	467	32	...	190	...	...
Discrepancy 4/	--	--	-24	-181	--	29	--	--
				(In percent of GDP)				
Deficit	-34	-33	-16	-12	-13	-8	-18	-18
Deficit excluding foreign-financed capital expenditures	-34	-33	-16	-12	...	-8	-10	-10
Revenue	5	6	13	11	13	14	15	17
Expenditures	39	39	29	23	26	23	33	34
Current balance	-32	-31	-12	-11	-9	-7	-7	-8
Domestic financing	35	33	16	11	13	7	10	10
				(In percent of expenditures)				
Deficit	-88	-84	-56	-52	-50	-37	-56	-51
Deficit excluding foreign-financed capital expenditures 5/	-88	-84	-56	-52	...	-36	-41	-37
Revenue	12	16	44	48	50	63	44	49
Domestic financing	88	84	54	49	50	32	30	29

Sources: Ministry of Finance, Bank of Lebanon, and Fund staff estimates.

1/ Includes foreign and domestically financed CDR expenditure.

2/ Includes advances and transfers.

3/ Petroleum subsidy paid to Electricity Company of Lebanon.

4/ Disrepancy between deficit and financing.

5/ In percent of expenditures excluding foreign-financed capital expenditures.

Table 3: Lebanon: Monetary Survey, 1989–94

(End of period stocks, in billions of Lebanese pounds)

	1989	1990	1991	1992	March 1993	1993	March 1994	Proj. 1994
Total liquidity	2,465.2	3,853.4	5,538.5	11,869.5	11,855.0	15,678.5	16,741.2	18,251.0
Money	287.2	449.9	689.5	1,199.4	1,071.8	1,143.4	1,203.8	1,398.0
Currency	192.4	333.0	484.7	798.0	700.7	714.7	762.5	...
Demand deposits in domestic currency	94.8	117.0	204.8	401.4	371.1	428.7	441.3	...
Quasi–money	2,178.0	3,403.5	4,849.0	10,670.1	10,783.2	14,535.1	15,537.4	16,853.0
Domestic currency time and savings deposits	658.2	818.9	1,461.6	3,195.2	3,132.8	4,165.4	5,475.6	5,108.0
Foreign currency deposits 1/	1,519.8	2,584.6	3,387.4	7,474.9	7,650.4	10,369.7	10,061.8	11,745.0
Net foreign assets	3,349.8	5,206.0	6,203.1	12,488.8	11,900.1	15,030.2	15,219.2	16,110.5
Domestic claims	1,480.1	2,608.8	3,213.5	7,117.8	7,507.4	8,970.2	9,807.6	10,845.5
Net claims on public sector	595.2	1,042.6	1,222.3	2,276.9	2,558.2	3,027.9	3,020.4	4,249.6
Lebanese pounds	678.5	1,200.1	1,348.3	2,485.2	2,752.3	3,437.1	3,444.1	...
Foreign currency	−83.4	−157.5	−126.0	−208.3	−194.1	−409.2	−423.7	...
Claims on private sector	884.9	1,566.2	1,991.2	4,840.9	4,949.2	5,942.3	6,787.2	6,595.9
Lebanese pounds	181.9	276.2	363.5	473.0	590.6	675.9	728.7	...
Foreign currency	703.0	1,290.0	1,627.7	4,367.9	4,358.6	5,266.4	6,058.5	...
Other items (net)	−2,364.7	−3,961.4	−3,878.1	−7,737.1	−7,552.4	−8,321.9	−8,285.6	−8,705.0
Of which: Exchange revaluation account of Bank of Lebanon	−2,109.5	−3,429.0	−3,227.8	−6,252.5	−5,928.5	−6,630.3	−6,469.0	−6,514.0
Memorandum items:								
Total liquidity (percentage change) 2/	13.4	56.3	43.7	114.3	66.1	32.1	41.2	16.4
Lebanese pound component of liquidity (as percent of total liquidity)	38.3	32.9	38.8	37.0	35.5	33.9	39.9	35.6
Change in net credit to the public sector (as percent of total liquidity at beginning of period)	17.6	18.1	4.7	19.0	2.4	6.3	−0.1	7.8
Change in credit to the private sector (as percent of total liquidity at beginning of period)	6.7	27.6	11.1	51.5	0.9	9.3	5.4	4.2
Foreign currency component of liquidity (in US$ millions)	3,009	3,070	3,854	4,067	4,392	6,061	5,938	6,950

Sources: Bank of Lebanon, and Fund staff estimates.

1/ SOLIDERE deposits are included as foreign currency deposits.
2/ For March 1993 and March 1994, the data represent percentage changes from the stock at end of March the previous year.

Table 4. Lebanon: Balance of Payments, 1989–94

	Estimates					Proj.
	1989	1990	1991	1992	1993	1994
	(In millions of U.S. dollars)					
Current account	−785	−1,351	−2,935	−3,053	−3,417	−3,944
Trade balance	−1,779	−2,082	−3,258	−3,169	−3,537	−4,214
Exports f.o.b. 1/	484	496	490	601	686	825
Imports f.o.b. 1/	−2,263	−2,578	−3,748	−3,770	−4,222	−5,039
Services	514	451	143	−84	−181	−50
Factor	725	694	478	263	197	298
Interest earnings of the Bank of Lebanon	71	39	32	14	26	93
Commercial banks' investment income 2/	199	168	136	111	106	142
Nonbank investment income 3/	456	487	310	138	88	97
Interest on external public debt	...	...	...	...	−24	−34
Nonfactor	−211	−243	−335	−347	−377	−348
Insurance and freight	−226	−258	−375	−377	−422	−403
Travel and transportation	15	15	40	30	45	55
Private transfers	480	280	180	200	300	320
Capital account	476	920	4,009	3,107	4,587	4,584
Direct investment	...	...	...	...	902	1,198
Of which: SOLIDERE	−−	−−	−−	−−	252	298
External public debt disbursements	...	...	...	...	126	557
Public sector grants	...	...	...	...	30	243
Amortization on external public debt 4/	−4	−−	−−	−59	−47	−77
Nonbank short–term capital 3/	−735	−1,017	1,404	465	652	605
Claims on international banks	−833	−1,087	1,692	490	601	555
Liabilities to international banks	98	70	−288	−25	51	50
Other capital (including errors and omissions) 5/	1,215	1,937	2,605	2,700	2,924	2,059
Overall balance	−309	−431	1,074	54	1,170	640
Net foreign reserves (−increase)	309	431	−1,074	−54	−1,170	−640
Bank of Lebanon	43	297	−569	−231	−456	−990
Commercial banks	266	134	−505	177	−713	350
	(In millions of U.S. dollars unless indicated otherwise)					
Memorandum items:						
Current account balance/GDP (in percent)	−28.9	−47.6	−65.9	−55.1	−45.3	−43.1
External public debt 6/	332.1	332.1	332.1	273.4	352.2	832.2
External public debt/GDP (in percent)	12.2	11.7	7.5	4.9	4.7	9.1
Debt service	...	...	...	...	71.2	111.5
Debt service/current receipts (in percent)	...	...	...	...	5.3	6.7
Central bank foreign exchange reserves	906.3	623.3	1,236.7	1,448.0	2,220.0	3,210.0
Central bank foreign exchange reserves (in months of imports)	4.8	2.9	4.0	4.6	6.3	7.6

Sources: Bank of Lebanon; Council for Development and Reconstruction; Ministry of Finance; IMF, Direction of Trade Statistics; IMF, International Financial Statistics; and Fund staff estimates.

1/ IMF, Direction of Trade Statistics. Figures for 1993 were estimated using data for January–November of that year.
2/ Estimated by applying the average three–month Eurodollar rate, with appropriate margins, to the average stock over each year.
3/ Data on the flow of international bank lending to nonbank residents of Lebanon and on the flow of deposits by residents with international banks are obtained from the IMF, International Financial Statistics, adjusted for variations in U.S. dollar/nondollar exchange rates. Estimates of interest payments and receipts relating to such international bank lending and deposit–taking are derived by applying the average three–month Eurodollar rate, with appropriate margins, to the average stocks in each year.
4/ Figures for 1989–92 are net of disbursements.
5/ Includes valuation adjustments.
6/ The authorities are in the process of revising external debt data for 1989–91.

Table 5. Lebanon: Medium-Term Scenario--Selected Macroeconomic Indicators, 1993-98

(In percent)

	Est. 1993	Projections 1994	1995	1996	1997	1998
Real GDP growth	7.0	7.0	8.0	8.0	8.0	8.0
Change in consumer price index (year average)	29.1	10.6	8.0	6.0	5.0	4.0
Central government budget						
Revenues/GDP	14.0	17.0	18.0	18.0	21.0	21.0
Expenditure/GDP	23.0	34.0	38.0	34.0	30.0	27.0
Overall deficit/GDP	-8.0	-18.0	-20.0	-15.0	-8.0	-6.0
Government debt/GDP 1/	51.0	59.0	69.0	75.0	74.0	71.0
Monetary sector						
Growth in net credit to public sector	33.0	40.3	25.7	13.9	-1.0	-6.1
Growth in credit to private sector	22.8	11.0	16.4	19.5	19.6	18.2
External sector						
Current account deficit/GDP	45.3	43.1	47.5	46.6	45.6	44.9
External public debt/ GDP	4.7	9.1	17.7	25.0	30.0	34.1
Debt service/current receipts	5.3	6.7	7.7	5.6	18.6	7.6
Official foreign exchange reserves (in months of imports)	6.3	7.6	7.0	6.7	7.1	7.5

Sources: Data provided by authorities, and Fund staff estimates.

1/ Outstanding treasury bills and external public debt.

Medium-Term Scenario

This appendix complements the discussion of the medium-term scenario presented in the staff report. First, it provides details of the intended policy measures, and projected outcomes for the fiscal accounts. Second, it states the assumptions and provides details of the balance of payments projections. Finally, it describes the assumptions and methodology underlying the monetary projections and presents the outcomes for monetary aggregates that incorporate the results flowing from the fiscal and balance of payments projections.

The medium-term scenario is based on April 1994 World Economic Outlook (WEO) projections. In line with the authorities' objectives, it assumes that real GDP will grow by 8 percent per annum during 1995-98, inflation will decline to that of trading partners by 1998, and the exchange rate will remain stable at LL 1,690 per U.S. dollar through 1998.

I. Government Finances

Medium-term budgetary projections are predicated on the implementation of important revenue-enhancing and expenditure-containment measures that were detailed by the authorities. On the revenue side, these include: (a) the implementation of the general sales tax (GST) starting in 1997; (b) the unification of various excises, increases in excise rates, and the conversion of specific rates to ad valorem rates in 1996; (c) the enforcement of the fine for violation of construction regulations; (d) better enforcement of the income tax starting in 1995 by establishing a tax collection unit, mainly targeting large tax payers; (e) the generation of additional revenue through a salutary effect of tax amnesty, and collection of back taxes; (f) adjustments of the inheritance tax and the tax on rental income in line with the new income tax rates; and (g) implementation in 1994 of the new customs law (which is expected to be revenue-neutral) and improvements in customs duty collections.

On the expenditure side, the main expenditure measures and assumptions are: (a) adjustments in the number of government employees as well as in nominal wages so as to keep the budgetary wage bill constant in real terms at the 1994 level; (b) decline in the EDL fuel subsidy through 1995-96, and its complete elimination by 1997, owing to improvements in management, cost saving measures, improvements in tariff collection, and adjustments in electricity tariffs, as necessary; (c) maintenance of the budgetary component of development expenditure in real terms at the same level projected for 1995; and (d) an evolution of extra-budgetary development expenditure through 1994-98, as envisaged by the authorities.

Projections assume that the differential between domestic and foreign real interest rates would gradually decline to 2 percentage points by 1998. Interest payments on domestic debt are projected to be equal to half of the previous year's stock of treasury bills at face value times the previous year's nominal interest rate, plus half of the current year's stock of

treasury bills times the current year's interest rate; this assumption broadly reflects the current term structure of treasury bills. The flow of foreign loans and grants corresponds to the authorities' forecasts. The flow of domestic financing, which is estimated as a residual, is assumed to be met entirely by treasury bill issuance. Given the level of domestic and foreign debt at end-1993, the estimated yearly domestic and foreign financing flows are used to determine the outstanding levels of domestic and foreign debt for future years. Domestic debt is assumed to be the face value of the outstanding stock of treasury bills.

On the basis of the above framework and assumptions, the dynamic progression of key indicators (i.e., domestic and foreign debt, debt servicing, revenue, and expenditure) was calculated for the medium term (Table 6). The projections indicate a deterioration in the fiscal stance during 1994-95 and improvement thereafter. The overall deficit is projected to rise from 8 percent of GDP in 1993 to about 18-20 percent of GDP in 1994-95, and decline sharply to 6 percent of GDP in 1998. A similar path of adjustment is also projected for primary and current deficits, where, as stated by the authorities, current deficits are to be eliminated by 1996 and a current surplus achieved by 1997. The main reasons for the sharp improvement in 1996-97 are: (1) adoption of permanent tax measures (excise tax reform, GST), which substantially improve tax revenues; and (2) the containment of current expenditure, mainly through limiting the wage bill, eliminating the EDL subsidy, and limiting budgetary outlays on the rehabilitation of Lebanese nationals displaced by political disturbances.

Reflecting the decline in the domestic financing requirement of the budget after 1996, domestic debt as a percentage of GDP is projected to rise from 46 percent in 1993 to about 50 percent during 1994-96 and decline to 37 percent by 1998. On the other hand foreign debt, both as a percentage of GDP and foreign exchange revenues, is projected to continue rising substantially through 1994-98, as foreign financing of the budget is projected to remain high in line with the large reconstruction outlays planned for 1994-98. Interest payments on total outstanding debt are projected to rise to 34 percent of current expenditure in 1995, and to decline thereafter to 26 percent by 1998.

II. Balance of Payments

Balance of payments projections were prepared in line with the authorities' macroeconomic objectives (Table 7). Specific assumptions underlying these projections are described below. On the current account, it is assumed that exports will rise in line with the growth in nominal GDP, averaging about 9 percent of GDP throughout the projection period. Imports, after rising broadly in line with the nominal GDP in 1994, are expected to pick up sharply in 1995 due to an anticipated increase in demand for imported capital goods for the reconstruction effort and reach about 60 percent of GDP. During 1996-98, imports are projected to increase at a slower pace (averaging about 12 percent per annum), and decline to 57 percent of GDP by 1998.

With regard to the services account, interest earnings of the BDL are assumed to move in line with the projected accumulation of official foreign reserves, and the projections for LIBOR in the latest WEO exercise. Interest receipts and payments of commercial banks should rise over time due to projected increases in their assets and liabilities, and the LIBOR. Nonbank investment income is projected to decline, assuming that the nonbank private sector will gradually repatriate some of its external holdings, while at the same time borrowing from abroad for investment in Lebanon. Interest payments on the external debt of the public sector are computed based on debt service information on contracted debt for 1994-98 provided by BDL's foreign debt unit, as well as the debt service obligations arising from the new borrowing requirements in the above fiscal program. In view of prospective improvements in internal security, insurance and freight charges are reduced from an estimated level of 10 percent of the value of merchandise imports in 1993 to 8 percent in 1994, before gradually falling to 5 percent by 1998. Private transfers are projected to rise by about US$30 million per annum throughout the projection period.

With regard to the capital account, it is assumed that investment in SOLIDERE ends in 1994. However, other direct investment is projected to increase by one-third in 1995, and by about 20 percent per annum thereafter. External public sector borrowing and official grants are projected to increase in line with the budgetary projections. Amortization of external public debt is computed using information from BDL's debt unit and information from the Ministry of Finance. All external borrowing in excess of those projected by the BDL and the Eurobond issue is assumed to be contracted at concessional interest rates with grace periods of at least five years; hence, amortization payments on these loans are assumed to begin after 1998. Other capital inflows, which represent the bulk of unrecorded private capital movements as well as certain current account transactions, are projected to be at levels that would ensure the maintenance of official foreign exchange reserves equivalent to about seven months of imports throughout the projection period. On the basis of the above assumptions, the surplus in the capital account of the balance of payments would increase from US$4.6 billion in 1993 to US$7.8 billion in 1998. The overall surplus in the balance of payments would decline from US$1.2 billion in 1993 to US$322 million in 1996, but rise thereafter to about US$800 million by 1998.

The stock of external debt is projected to rise very sharply from US$352 million in 1993 (4.7 percent of GDP) to US$5.3 billion by end-1998 (34.1 percent of GDP). Debt service obligations are projected to average about 7 percent of current receipts in 1994-96, but rise sharply to about 19 percent in 1997 due to a bullet repayment of the Eurodollar loan, and then decline to about 8 percent of current receipts in 1998.

III. Monetary Aggregates

The monetary projections take into account the growth and inflation targets, the domestic and foreign financing requirements specified in the fiscal and balance of payments projections, and a continuance of the recent

process of dedollarization (Table 8). Specific assumptions underlying these projections are described below.

Total liquidity is assumed to grow in line with nominal GDP, given: (a) the findings of earlier work on money demand in Lebanon; 1/ and (b) the assumed constancy of the exchange rate over the medium term, which means that demand for both the Lebanese pound and U.S. dollar components of total liquidity each grow at the same rate, in line with the growth of nominal GDP. However, due to the assumed ongoing dedollarization of the Lebanese economy, the foreign currency component of total Lebanese liquidity is projected to gradually fall over the 1994-98 projection period, declining from 66.1 percent of total liquidity at end-1993 to 55.5 percent at end-1998.

The change in net foreign assets in the monetary survey is taken from the forecast change in the value of the overall balance of payments in the medium-term external projections, converted from U.S. dollars to Lebanese pounds at the constant exchange rate mentioned above. 2/ Other items net are projected to rise by LL 200 billion per year over the period, based on an historical analysis of previous movements in the nonexchange-revaluation component of this item. Given that the exchange rate is assumed to remain constant over the forecast period, there is no exchange rate-based revaluation of net foreign assets held by the central bank.

In all years of the medium-term monetary projections, the financing needs of the public sector are fully accommodated, with the public sector's domestic financing requirement taken from the medium-term fiscal projections. The domestic financing needs of the Government are assumed to be fully met from sales of treasury bills, which are then allocated between bank and nonbank finance in the end-1993 ratio of 79.8 percent for bank purchases of bills, and 20.2 percent for bills purchased by the nonbank sector. Claims on the private sector are then the residual item in the monetary survey during 1995-98.

Results from the monetary projections indicate that net credit to the public sector expands by 40.3 percent in 1994, then gradually declines to contract by 6.1 percent in 1998. An inverse relationship is exhibited by credit to the private sector, which increases by 11.0 percent in 1994, then accelerates to grow by 18.2 percent in 1998. Both outcomes are consistent with the authorities' view that in the early years of the projection period the public sector would be the engine of growth, with the private sector gradually taking over that role in later years.

1/ For further details see Section IV of "Lebanon--Economic Recovery, Stabilization, and Macroeconomic Policies".

2/ The exception to this methodology occurs in 1994, when after granting an 11 percent increase in credit to the private sector, the change in net foreign assets was the residual item in the monetary survey. This procedure results in a US$640 million increase in net foreign currency reserves of the BDL.

Table 6. Lebanon: Government Finances, 1993–98

	1993	Revised Outlook 1994	Projections 1995	1996	1997	1998
			(In billions of Lebanese pounds)			
Total revenue	1,855	2,600	3,205	3,835	5,002	5,582
Tax	979	1,294	1,626	2,036	2,973	3,312
Direct taxes	172	250	392	420	476	535
Income taxes	126	175	279	291	330	371
Other	46	75	112	129	146	164
Indirect	806	1,044	1,234	1,616	2,497	2,778
Customs duties	662	825	979	1,223	1,364	1,505
Other	144	219	255	392	1,133	1,272
Nontax	876	1,306	1,579	1,799	2,029	2,269
Total expenditure	2,957	5,356	6,801	6,994	6,947	7,143
Current	2,757	3,779	4,076	4,239	4,365	4,540
Wages and salaries	640	1,192	1,287	1,364	1,432	1,490
Interest	784	1,245	1,380	1,340	1,263	1,186
Domestic	754	1,187	1,263	1,170	1,025	874
Foreign	30	58	116	170	238	312
EDL fuel subsidy	181	145	100	50	--	--
Other	1,152	1,197	1,310	1,485	1,670	1,864
Development	200	1,577	2,725	2,755	2,582	2,604
Budgetary	...	627	500	530	557	579
CDR	...	300	--	--	--	--
Other	...	327	500	530	557	579
Extrabudget	...	950	2,225	2,225	2,025	2,025
CDR	...	500	1,700	1,700	1,500	1,500
"Big projects"	65	400	425	425	425	425
"Displaced projects"	...	50	100	100	100	100
Overall deficit	−1,102	−2,756	−3,596	−3,159	−1,945	−1,562
Financing (net)	1,131	2,756	3,596	3,159	1,945	1,562
Domestic (net)	941	1,531	1,371	934	−80	−463
BDL advances (net)	−119	--	--	--	--	--
Treasury bills (net)	1,060	1,531	1,371	934	−80	−463
Foreign (net)	190	1,225	2,225	2,225	2,025	2,025
Receipts	272	1,356	2,375	2,269	2,576	2,072
CDR	...	500	1,700	1,700	1,500	1,500
"Big projects"	...	510	425	425	425	425
Other	...	346	250	144	651	147
Repayments	−82	−131	−150	−44	−551	−47
Discrepancy 1/	29	--	--	--	--	--
			(In percent of GDP)			
Total revenue	14	17	18	18	21	21
Total expenditure	23	34	38	34	30	27
Current deficit	−7	−8	−5	−2	3	4
Overall deficit	−8	−18	−20	−15	−8	−6
Foreign financing	1	8	12	11	9	8
Domestic financing	7	10	8	5	−0	−2
Total debt 2/	51	59	69	75	74	71
Total interest payments	6	8	8	6	5	4

Sources: Bank of Lebanon, Ministry of Finance, and Fund staff estimates.

1/ Discrepancy between budget deficit and total net financing flows accounted for in the monetary survey; applies only to 1993.
2/ Outstanding treasury bills and external public debt.

Table 7. Lebanon: Balance of Payments, 1993–98

	Est. 1993	Projections 1994	1995	1996	1997	1998
		(In millions of U.S. dollars)				
Current account	−3,417	−3,944	−5,086	−5,721	−6,338	−7,020
Trade balance	−3,537	−4,214	−5,466	−6,135	−6,818	−7,501
Exports f.o.b. 1/	686	825	965	1,104	1,252	1,406
Imports f.o.b. 1/	−4,222	−5,039	−6,430	−7,239	−8,070	−8,908
Services	−181	−50	30	34	70	41
Factor	197	298	380	343	317	291
Interest earnings of the Bank of Lebanon	26	93	162	178	212	251
Commercial banks' investment income 2/	106	142	171	173	175	177
Nonbank investment income 3/	88	97	116	94	71	49
Interest on external public debt	−24	−34	−69	−101	−141	−185
Nonfactor	−377	−348	−350	−309	−247	−250
Insurance and freight	−422	−403	−450	−434	−403	−445
Travel and transportation	45	55	100	125	156	195
Private transfers	300	320	350	380	410	440
Capital account	4,587	4,584	5,617	6,042	7,051	7,812
Direct investment	902	1,198	1,200	1,440	1,728	2,074
Of which: SOLIDERE	252	298	--	--	--	--
External public debt disbursements	126	557	1,154	1,200	1,428	1,176
Public sector grants	30	243	252	143	96	50
Amortization on external public debt	−47	−77	−89	−26	−326	−28
Nonbank short-term capital 3/	652	605	450	450	450	450
Other capital 4/	2,924	2,059	2,650	2,835	3,675	4,090
Overall balance	1,170	640	531	322	714	792
Net foreign reserves (−increase)	−1,170	−640	−531	−322	−714	−792
Bank of Lebanon	−456	−990	−531	−322	−714	−792
Commercial banks	−713	350	--	--	--	--
		(In millions of U.S. dollars unless indicated otherwise)				
Memorandum items:						
Current account balance/GDP (in percent)	−45.3	−43.1	−47.5	−46.6	−45.6	−44.9
External public debt	352.2	832.2	1,897.2	3,071.2	4,173.2	5,321.2
External public debt/GDP (in percent)	4.7	9.1	17.7	25.0	30.0	34.1
Debt service	71.2	111.5	157.5	126.5	467.1	212.3
Debt service/current receipts (in percent)	5.3	6.7	7.7	5.6	18.6	7.6
Foreign exchange reserves	2,220.0	3,210.0	3,741.4	4,063.1	4,777.0	5,569.2
Foreign exchange reserves (in months of imports)	6.3	7.6	7.0	6.7	7.1	7.5

Sources: Bank of Lebanon; Council for Development and Reconstruction; Ministry of Finance; IMF, Direction of Trade Statistics; IMF, International Financial Statistics; and Fund staff estimates.

1/ IMF, Direction of Trade Statistics. Figures for 1993 were estimated using data for January–November of that year.
2/ Estimated by applying the average three-month Eurodollar rate, with appropriate margins, to the average stock over each year.
3/ Data on the flow of international bank lending to nonbank residents of Lebanon and on the flow of deposits by residents with international banks are obtained from the IMF, International Financial Statistics. Estimates of interest payments and receipts relating to such international bank lending and deposit-taking are derived by applying the average three-month Eurodollar rate, with appropriate margins, to the average stocks in each year.
4/ Includes valuation adjustments and errors and omissions.

Table 8. Lebanon: Monetary Aggregates, 1993–98

(End of period stocks, in billions of Lebanese pounds)

	1993	Projections 1994	1995	1996	1997	1998
Total liquidity 1/	15,678.5	18,251.0	21,126.0	23,715.0	26,455.0	29,220.0
Money	1,143.4	1,398.0	1,724.0	2,011.0	2,384.0	2,791.0
Currency	714.7	..	..	..	..	..
Demand deposits in domestic currency	428.7	..	..	..	..	..
Quasi–money	14,535.1	16,853.0	19,402.0	21,704.0	24,071.0	26,429.0
Domestic currency time and savings deposits	4,165.4	5,108.0	6,302.0	7,349.0	8,708.0	10,202.0
Foreign currency deposits 2/	10,369.7	11,745.0	13,100.0	14,355.0	15,363.0	16,227.0
Net foreign assets 3/	15,030.2	16,110.5	17,007.5	17,551.5	18,758.5	20,096.5
Domestic claims	8,970.2	10,845.5	13,023.5	15,268.5	17,001.5	18,628.5
Net claims on public sector, adjusted 4/	3,027.9	4,249.6	5,343.7	6,089.0	6,025.2	5,655.7
Lebanese pounds	3,437.1	..	..	..	..	..
Foreign currency	–409.2	..	..	..	..	..
Claims on private sector 4/	5,942.3	6,595.9	7,679.8	9,179.5	10,976.4	12,972.8
Lebanese pounds	675.9	..	..	..	..	..
Foreign currency	5,266.4	..	..	..	..	..
Other items (net) 5/	–8,321.9	–8,705.0	–8,905.0	–9,105.0	–9,305.0	–9,505.0
Of which: Exchange revaluation account of Bank of Lebanon 3/	–6,630.3	–6,514.0	–6,514.0	–6,514.0	–6,514.0	–6,514.0
Memorandum items:						
Foreign currency component of liquidity (In US$ millions) 3/	6,060.6	6.949.7	7,751.5	8,494.1	9,090.5	9,601.8
Foreign currency component of liquidity (In percent of total liquidity)	66.1	64.4	62.0	60.5	58.1	55.5
Income velocity of Lebanese pound component of liquidity (GDP/M2LL)	2.5	2.4	2.3	2.2	2.1	2.0
Total liquidity (percent change)	32.1	16.4	15.8	12.3	11.6	10.5
Net credit to public sector (In billions of Lebanese pounds)	751.0	1,221.7	1,094.1	745.3	–63.8	–369.5
Financing by the nonbank public (In billions of Lebanese pounds)	190.0	309.3	276.9	188.7	–16.2	–93.5
Public sector domestic finance (In billions of Lebanese pounds)	941.0	1,531.0	1,371.0	934.0	–80.0	–463.0
Net credit to public sector (percent change)	33.0	40.3	25.7	13.9	–1.0	–6.1
Credit to private sector (percent change)	22.8	11.0	16.4	19.5	19.6	18.2
Nominal GDP (percent change)	38.1	18.3	16.6	14.5	13.4	12.3

Sources: Bank of Lebanon, and Fund staff estimates.

1/ The monetary aggregates are assumed to grow at the same rate as nominal GDP, and have been adjusted to reflect the assumed continuation of the process of dedollarization, with the share of foreign currencies in total liquidity falling from 66.1 percent at end–1993 to 55.5 percent at end–1998.

2/ SOLIDERE deposits are included as foreign currency deposits.

3/ The values for end–1994 of the US$ component of total liquidity, net foreign assets and the exchange revaluation are calculated using an exchange rate of LL 1,690 = US$ 1. This rate is then assumed constant for the remainder of the period of analysis.

4/ For the medium–term projection it is assumed that claims on the public sector increase in line with the share of bank financing in total financing for 1993 of 79.8 percent. Credit to the private sector is the residual.

5/ It is assumed that other items net increase by LL 200 billion per year.

Lebanon - Statistical Issues

1. Outstanding statistical issues 1/

The analysis of developments and prospects in Lebanon continues to be hampered by the lack of reliable data on most sectors of the economy. Despite the three STA technical assistance missions over the past year, there has been little progress in the construction of consistent and reliable statistical data base. 2/ At present, only the monetary accounts and, to a more limited extent, central government accounts are available on a regular basis. Most other data (output, production, employment, non-government public sector, balance of payments) have had to be estimated on the basis of fragmentary information or partial indicators. The authorities attribute the apparent lack of progress in the statistical area largely to lack of manpower and other technical resources to devote to these tasks. Although the authorities were very appreciative of the Fund's technical assistance, they felt that such assistance could be more effective if the experts could stay for a longer period of time in the field to guide them in the initial stages of implementing the recommendations. Nonetheless, a program of follow-up technical assistance has yet to be firmed up with the authorities.

A brief summary of the status of the data is as follows:

a. Real sector

Lebanon currently reports no real sector data to the Fund for publication in IFS. The recent multitopic statistical mission (November 2-12, 1993) determined that "the most glaring gap in the economic database remains in the real sector data," essentially because the Central Administration for Statistics (CAS) is still not functioning due to internal problems. Official national accounts estimates have not been produced since the closure of the statistical office in the 1970s. No official price statistics exist; however, some consumer price indices are prepared by private organizations on the basis of a limited basket of goods for the greater Beirut metropolitan area. In an effort to expedite the collection of real sector data, a law authorizing the immediate creation of an "Institute for Statistical Services" has recently been passed. Meanwhile, the BDL has started to conduct independent surveys on various components of the national accounts.

1/ For details of the discussions with the authorities on Fund technical assistance, including STA, see section on policy discussions in this report.

2/ The recommendations of the STA technical assistance missions are contained in the reports "Aide-Mémoire on the Government Finance Statistics Mission," dated January 14, 1994; "Aide-Mémoire on the Multitopic Statistic Mission," dated January 4, 1994; and "Aide-Mémoire on the Balance of Payment Statistics Mission," dated May 4, 1994.

b. Government finance

No government finance data have ever been reported for inclusion in the Economic Information System. Following the recent technical assistance mission on government finance, the authorities are in the process of establishing a GFS data compilation system. It is envisaged that the compilation system would be established in three phases. Under Phase I, a fiscal database would be established that covered all central government operations that are included in the budget. Under Phase II, the operations of social security funds and the six extrabudgetary accounts, including the CDR, would be consolidated with those of the budgetary accounts to form consolidated central government. In Phase III, the operations of local government units (municipalities) would be consolidated with the rest of the government sector to form consolidated general government. A gradual approach to setting up a new database for government operations was proposed because of the prevailing circumstances in the country. Thus far, Phase I is almost completed, pending some minor refinements to the classification of accounts and the computerization program.

c. Monetary accounts

In general, the monetary accounts are received on a current and timely basis.

d. Balance of payments

At present the Lebanese authorities do not compile balance of payments statistics. Trade data for Lebanon that appear in IFS are drawn from DOTS and are built up entirely from the trade statistics of partner countries. Numerous data sources are available, however, for compiling such statistics, and procedures are being prepared for a quarterly reporting to the IMF of some items of the balance of payments and Lebanon's international investment position. External trade and external debt data are now being collected by the BDL in cooperation with the Ministry of Finance and the CDR.

The Statistics Department is arranging a balance of payments technical assistance program, which is scheduled to extend over a two-year period. A short-term work program to begin developing balance of payments data has been adopted by the BDL, based on recommendations made by the balance of payments statistics mission that visited Beirut in January/February 1994.

2. Technical assistance missions in statistics (1991-present)

Subject	Staff Member	Date
Government Finance Statistics	Mr. M. Wasfy	September 6-17, 1993
Multitopic Statistics	Mr. J. Bové Mr. R. Fiévet Mr. P. Cotterell Mr. J. Martelino	November 2-12, 1993
Balance of Payments Statistics	Mr. R. Fiévet	Jan. 23-Feb. 5, 1994

Lebanon: Fund Relations
(As of May 31, 1994)

I. Membership Status: Joined 4/14/47; Article VIII effective July 1, 1993

II. General Resources Account:

	SDR Million	% Quota
Quota	78.70	100.0
Fund holdings of currency	59.87	76.1
Reserve position in Fund	18.83	23.9

III. SDR Department:

	SDR Million	% Quota
Net cumulative allocation	4.39	100.0
Holdings	10.92	248.7

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements: None

VI. Projected Obligations to Fund: None

VII. Exchange Rate Arrangement:

The Lebanese pound is freely floating against the U.S. dollar. The Bank of Lebanon's (BDL) stated policy is to intervene in exchange markets to smooth out short-term fluctuations. The Lebanese pound depreciated to an historical low of LL 2,528 per US$1 in September 1992 but has gradually appreciated to its current level of about LL 1,690 per US$1.

VIII. Article IV Consultations:

Lebanon is on the 12-month Article IV consultation cycle. The last Article IV consultation discussions were held in April/May 1993 (SM/93/140; 7/2/93) and were concluded by the Executive Board on July 30, 1993 (EBM/93/105).

IX. Fund Technical Assistance

Date	Department	Purpose
Dec. 1-12, 1991	MAE	Monetary management issues
Mar. 16-31, 1992	FAD	Review of tax system
Oct. 20-Nov. 2, 1992	FAD	Reform of customs tariff
Jan. 25-Feb. 13, 1993	FAD	Taxes on income and profits
Feb. 7-11, 1993	RES	Monetary policy
Feb. 8-30, 1993	FAD	Public expenditure management
Apr. 13-24, 1993	INS	Financial programming
May 2-14, 1993	MAE	Reorganization of BDL
Sept. 6-17, 1993	STA	Government finance statistics

Date	Department	Purpose
Sept. 9-17, 1993	FAD	Expenditure control
Oct. 5-18, 1993	MAE	Central bank accounting
Nov. 2-12, 1993	STA	Multitopic statistical issues
Jan. 24-Feb. 4, 1994	MAE	Monetary instruments and controls
Jan. 24-Feb. 4, 1994	STA	Balance of payments statistics
Feb. 12-25, 1994	FAD	Taxes on goods and services
Apr. 22-29, 1994	FAD	Revenue enhancement and fiscal management

X. Resident Representative:

None

Lebanon: Relations with the World Bank

1. Lebanon's disbursed and outstanding debt to IBRD amounted to US$37.96 million as of end-May 1994.

2. On March 4, 1993, the Bank's Board approved a US$175 million loan for the Emergency Reconstruction and Rehabilitation Project. Subsequently, loans of US$57.23 million for the rehabilitation of agriculture and US$19.44 million for public sector management were approved on June 29, 1994.

3. In 1991 the Bank undertook an economic assessment and organized a donors' meeting. Bank economic missions visited Lebanon in February, April, and October 1992, and a Bank Country Economic Memorandum was issued in March 1993. The Bank's missions that prepared the above-mentioned project assisted the Government in the formulation of the US$2.3 billion National Emergency Reconstruction Program for 1993-96. In February 1994, the Bank also conducted a financial sector review which focused on the development of a securities market. A technical assistance mission visited Beirut in April 1994 to assist in the formulation of an IBRD/UNDP-financed project for revenue enhancement and fiscal management.

4. As a follow-up to the December 1991 donors' meeting, a Consultative Group meeting has been tentatively scheduled for the fall of 1994. The main purpose of the meeting would be to assist Lebanon mobilize external resources for the National Emergency Reconstruction Program.