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Report | Lebanon's Macro Economy in the First Nine Months of 2019

I. General Introduction

Lebanon's macro economy contracted during the first nine months of 2019, due mainly to continued internal political conflict and unfavorable regional conditions.

The activity of most economic sectors has contracted, leading to lower aggregate demand and supply in the national economy.

The monetary authorities have maintained its monetary stabilization and high interest-rate policies to support monetary stability and stimulate capital inflows. Inflation has continued but at a slower pace.

The balance of payments recorded a substantial deficit in the first nine months of 2019, compared to a lower deficit for the same period last year.

The fiscal conditions remain highly unfavorable due to continued fiscal deficits and growing public indebtedness.

Economic reforms must be the major priority of domestic authorities in order to support economic growth rates in the years to come, in line with the CEDRE Conference, which allocated a foreign aid of USD 11.6 billion for Lebanon. This should be accompanied by special efforts to address the continued negative repercussions of the Syrian crisis on the domestic economy and society.

II. Real Sector

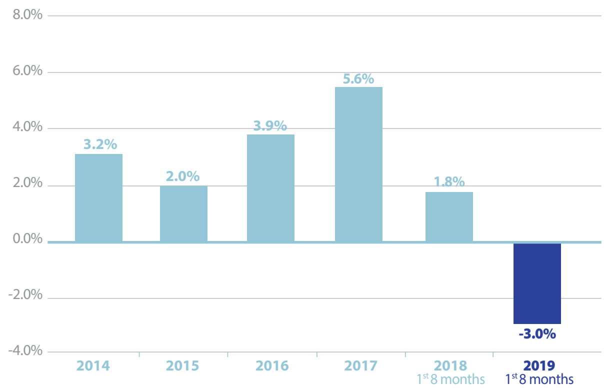
The real sector of Lebanon's economy experienced a contraction in the first nine months of 2019 relative to the corresponding period last year, mainly due to negative growth in the majority of economic sectors.

The Central Bank's Coincident Indicator, reflecting the overall performance of the real sector (since it comprises 11 real-sector indicators) reported an annual decrease of 3% for the first eight months of 2019. This level is lower than the one recorded in 2018 (1.5%), 2017 (5.6%), 2016 (3.9%), 2013 and 2014 (3.2% for each year), and 2015 (2%).

The major sectors that registered growth are: air transportation, exports, hotels and tourism. The major sectors that registered a contraction are: construction and real estate, and maritime transportation.

During this period, private consumption has remained strong, fueled mainly by the rise in wages of the public-sector employees following the ratification of the wage scale. However, private investment remains weak, due to the wait-and-see case prevailing in Lebanon.

Development of Central Bank's Coincident Indicator (CI) (growth rates)



1- Agriculture and Industry

The value of agricultural and industrial exports reached USD 2.5 billion for the first eight months of 2019, relative to USD 2 billion for the corresponding period of 2018, with an annual growth of 24.1%. The value of agricultural and industrial imports decreased by 0.9% from USD 13.9 billion to USD 13.8 billion during the same period.

These figures clearly reflect a better performing export activity and shrinking import activity, especially following the reopening of some routes namely the Jordan-Syrian border. These figures also reflect a positive contribution of the export activity to overall demand in the economy.

Electricity Production, an indicator of industrial activity, decreased by 1.9%, from 10,144 mkw in the first eight months of 2018 to 9,947 mkw in the first eight months of 2019.

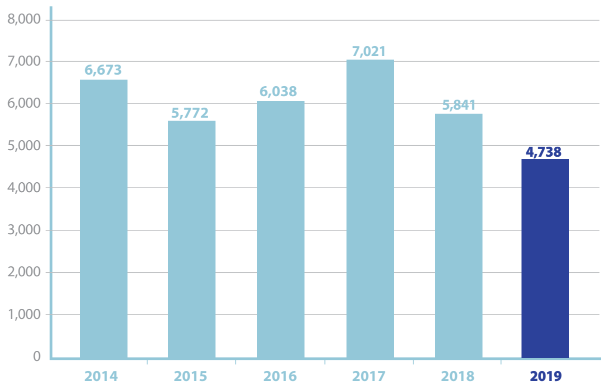
2- Real Estate and Construction

According to the figures of the Real Estate Registry and Ministry of Finance, the number of property sales operations decreased by 14.6% on annual basis to reach 36,952 operations in the first nine months of 2019. Also, the value of property sales dropped by 18.9% annually to reach USD 4.74 billion during the same period. This is partially affected by the recent seizure of housing loans by the Public Institution for Housing. These figures reflect a declining real-estate activity in the first nine months of 2019 as far as the demand side is considered.

Construction permits declined by 27.4%, from nearly 6.99 million sqm in the first nine months of 2018 to 5.1 million sqm in the same period of 2019. This suggests a curbed demand in the real-estate sector.

Cement deliveries dropped by 29.8% on annual basis to reach 2.24 million tons in the first eight months of 2019. This suggests a curbed supply in the real-estate sector during this period of 2019 relative to the same period last year.

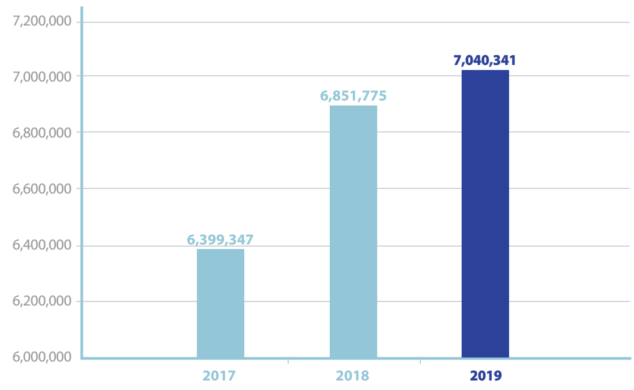
Value of Real-Estate Transactions, First Nine Months (USD, million)



3- Trade and Services

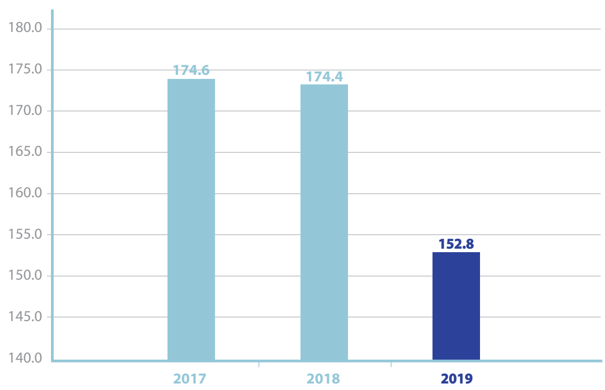
The statistics released by Beirut - Hariri International Airport indicate that the total number of passengers increased by 2.8% on annual basis to reach 7,040,341 passengers in the first nine months of 2019. The total freight handled by the airport recorded 67,820 thousand metric tons in the first nine months of 2019. The number of aircrafts recorded an increase of 0.5% on annual basis to reach 56,785 planes during the said period. These figures suggest an improvement in the airport activity.

Passengers at the Airport - First Nine Months



According to the statistics of the Port of Beirut, its revenues recorded a decrease by 12.3% on annual basis to reach USD 152.8 million in the first nine months of 2019. The number of ships recorded an annual decrease of 5.3% to reach 1.338 ships during the same period. In parallel, the number of containers recorded an annual decrease of 9.8% to reach 589,577 containers during the same period. The quantity of goods declined by 12.8% year-on-year to reach 5,184 thousand tons in the first nine months of 2019. These figures indicate that the Port of Beirut activity, an indicator of maritime transport and trade, was curbed during the period under consideration.

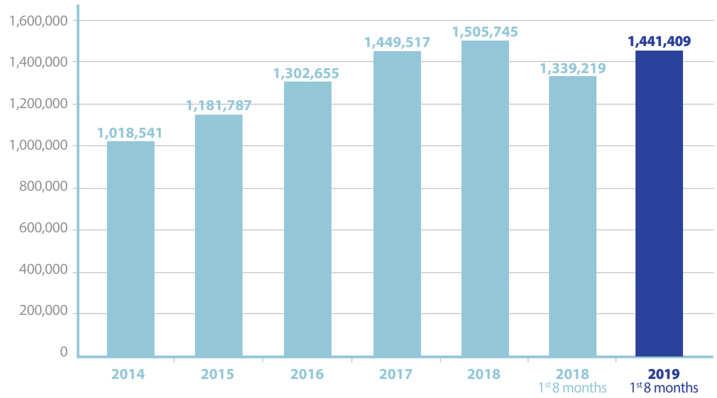
Port of Beirut Revenues, First Nine Months (USD, million)



The number of tourists visiting Lebanon totaled 1,441,409 tourists in the first eight months of 2019, growing by 7.6% from 1,339,219 tourists in the corresponding period last year.

According to the Survey of Ernst & Young, the Beirut's hotel occupancy rate, an indicator of tourism activity, increased from 62.6% in the first nine months of 2018 to 71.5% in the same period of 2019. The average room rate rose by an annual rate of 10.5% from USD 188 to USD 208, and the rooms yield rose by 26.3% from USD 118 to USD 149 during the same period. These figures reflect a growing hotel activity during the period under consideration.

Evolution of Tourists in Lebanon - First Nine Months



The statistics of the Association of Automobile Importers in Lebanon show that the number of new sold cars totaled 19,865 cars in the first nine months of 2019, with an annual decrease of 23.8% from 26,081 new cars sold in the same period last year.

According to the statistics of the Association of Banks in Lebanon, the total value of cleared checks, mirroring private consumption and investment spending, decreased by 14.6% on annual basis, from USD 49.6 billion in the first nine months of 2018 to USD 42.4 billion in the same period of 2019. The number of cleared checks decreased by 12.1% on annual basis to reach 7,791,506 at the end September 2019. This reflects a curbed private spending during the period under consideration.

The Kafalat loan guarantees decreased in amount from USD 36.2 million in the first nine months of 2018 to USD 5.6 million during the same period of 2019. SMEs constitute a major pillar of the corporate sector, and supporting it is a driving force of economic activity and job creation in Lebanon.

• Real-Sector Indicators

Indicators	First Nine Months of 2018	First Nine Months of 2019	% Change
Agricultural & Industrial Exports (USD, billion)*	2.0	2.5	24.1
Real-Estate Transactions (number)	43,263	36,952	(14.6)
Real-Estate Transactions (USD, million)	5,841	4,738	(18.9)
Number of Tourists*	1,339,219	1,441,408	7.6
Number of Passengers at HIA	6,851,775	7,040,341	2.8
Aircraft Activity at HIA	56,502	56,785	0.5
Value of Returned Checks (USD, billion)	1.16	1.05	(9.4)
Cleared Checks (USD, million)	49,648	42,398	(14.6)
Cleared Checks (number)	8,864,495	7,791,506	(12.1)
New Car Sales (number)	26,081	19,865	(23.8)
Hotel Occupancy Rate (%)	62.6	71.5	
Goods Quantity at Beirut Port (000, tons)	5,945	5,184	(12.8)
Numbers of Containers at Beirut Port	653,633	589,577	(9.8)
Number of Ships at Beirut Port	1,413	1,338	(5.3)
Revenues of Beirut Port (USD, million)	174.4	152.8	(12.3)
Kafalat Loans (number)	282	51	(82)
Kafalat Loans (USD, million)	36.2	5.6	(84.6)
Cement Deliveries (tons)*	3,195,652	2,243,348	(29.8)
Construction Permits (sqm)	6,987,681	5,072,442	(27.4)
Electricity Production (mkw)*	10,144	9,947	(1.9)

(*) First Eight Months.
Sources: Official and Related Directorates.

III. Fiscal Policy and Indebtedness

The fiscal conditions in Lebanon remain highly unfavorable in light of continued fiscal deficits and growing public indebtedness, and the crowding-out effect of private investment fueled by public borrowing.

1- Fiscal Deficit

The figures for public finances released by the Ministry of Finance show that budget revenues were 0.2% higher in the first seven months of 2019 relative to the corresponding period last year, and budget spending was 7.7% lower. This led to a budget deficit of USD 1.97 billion compared to USD 2.7 billion for the same period with an annual decline of 27.1%. The budget primary surplus stood at USD 1,018 million against USD 446 million for the same period.

The total revenues for the first seven months of 2019 were 3.7% lower than its amount for the same period last year, and total spending was 9.1% lower. This led to a total deficit of USD 2.4 billion against USD 3.1 billion for the same period, with a 21.7% drop. The total primary surplus stood at USD 577.2 million at end July 2019, relative to a lower level of USD 67.8 million a year earlier, with an annual increase of 751.1%.

As such, the total deficit represented nearly 25.7% of total spending at end-July 2019, relative to 29.8% at end-July 2018.

- **Fiscal Results for the First Seven Months of 2018 and 2019** (USD, million)

Indicators	2018	2019	% Change
Budget Revenues	6,663	6,678	0.2
Tax Revenues	5,498	5,554	1.0
Non-Tax Revenues	1,165	1,125	(3.5)
of which Telecom Revenues	485	458	(5.5)
Budget Expenditures	9,363	8,646	(7.7)
Budget Surplus / Deficit	**(2,700)**	**(1,968)**	**(27.1)**
% of Budget Expenditures	(28.8)	(22.8)	
Budget Primary Surplus	**446**	**1,018**	**128.5**
% of Budget Expenditures	4.8	11.8	
Treasury Receipts	584	298	(49.0)
Treasury Expenditures	962	739	(23.2)
Total Revenues	7,247	6,976	(3.7)
Total Expenditures	10,325	9,385	(9.1)
Total Deficit	**(3,078)**	**(2,409)**	**(21.7)**
% of Total Expenditures	(29.8)	(25.7)	
Total Primary Surplus / Deficit	**67.8**	**577.2**	**751.1**
% of Total Expenditures	0.7	6.2	

Source: Ministry of Finance.

2- Public Debt

The gross public debt of Lebanon reached USD 86.3 billion at end-August 2019, with an annual growth of 3.1% from USD 83.7 billion at end-August 2018.

The domestic debt totaled USD 53.8 billion at end-August 2019, with an annual increase of 11.3% from end-August 2018. The foreign debt reached USD 32.5 billion, with an annual growth of 8.1% during the same period.

The domestic debt represented nearly 63.2% of the gross debt at end-August 2019, against 37.7% for the foreign debt.

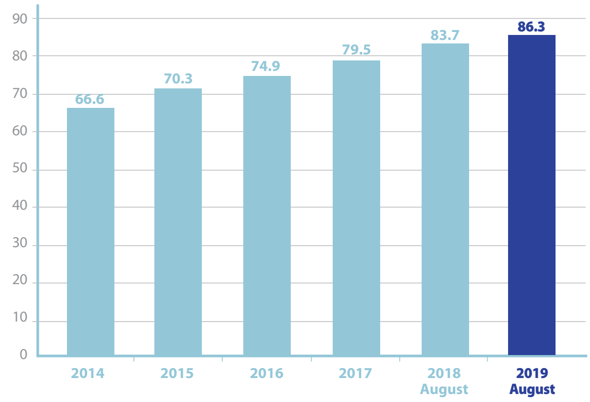
The net public debt grew by an annual 6.5% to reach USD 77.6 billion at end-August 2019.

• **Public Debt Indicators** (USD, billion)

Indicators	August 2018	August 2019	% Change
Gross Public Debt	83.7	86.3	3.1
Domestic Debt	48.3	53.8	11.3
Foreign Debt	35.4	32.5	(8.1)
Net Public Debt	72.9	77.6	6.5

Source: Ministry of Finance.

• | **Evolution of the Public Debt** (USD, billion)



3- 2020 Draft Budget

The 2020 draft budget endorsed by the Cabinet on October 21, 2019 shows the following estimates: (1) Budget revenues up by 5.5% from the 2019 budget, (2) Budget expenditures down by 20.4%, (3) Budget deficit at USD 358 million down by 91.7%, (4) Budget and Treasury revenues up by 5.3%, (5) Tax revenues up by 7.6%, (6) Non-Tax revenues down by 1.7%, (7) Current spending down by 19.7%, (8) Capital spending down up by 31.1%, (9) Interest payments down by 43.5%, and (10) Transfer to EDL down by 40%.

• **Projected Revenues and Expenditures in the 2020 Draft Budget** (USD, million)

	2020 Budget	2019 Budget	% Change
Budget Revenues	**13,145**	**12,460**	**5.5**
Tax Revenues	10,397	9,665	7.6
Non-Tax Revenues	2,747	2,794	(1.7)
of which Telecom Revenues	1,128	1,253	(10)
Budget Expenditures	**13,521**	**16,985**	**(20.4)**
Current Spending of which	12,855	16,020	(19.7)
- Interest Payments	3,114	5,514	(43.5)
- Wages, Salaries & Transfers to cover Salaries	3,398	3,781	(1.9)
- Retirement Salaries	1,879	1,679	11.9
- Transfers to EDL	995	1,658	(40)
- End of Service	100	299	(66.7)
Capital Spending	666	966	(31.1)
Budget Deficit	**(358)**	**(4,526)**	**(91.7)**
Treasury Receipts	747	737	1.3
Treasury Expenditures	-	-	-
Budget & Treasury Revenues	**13,892**	**13,197**	**5.3**
Budget & Treasury Expenditures	**-**	**-**	**-**

Source: Ministry of Finance.

IV. Inflation and Monetary Policy

The monetary authorities have maintained its monetary stabilization policy as well as its high interest-rate policy to support currency stability and stimulate capital inflows. This period has continued to experience inflation.

1- Central Bank

The Central Bank's statistics reveal that its balance sheet decreased by 0.94% on annual basis to reach USD 136.7 billion at the end of September 2019, compared to USD 138 billion during the same period of 2018. Assets in foreign currencies reached USD 37.9 billion at the end of September 2019, with an annual decrease of 12.1% from USD 43.1 billion at the end of September 2018.

As for the gold reserves, its value increased by 23.6% year-on-year to reach USD 13.9 billion as of end-September 2019.

• Monetary Indicators

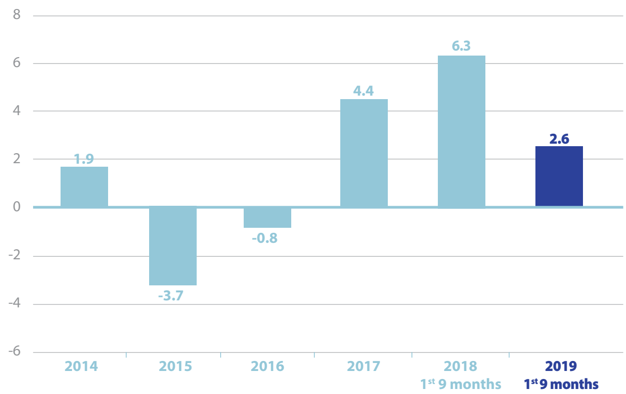
Indicators	2018 First Nine Months	2019 First Nine Months	% Change
USD/LBP Exchange Rate	1507.5	1507.5	0.0
Central Bank's Balance Sheet (USD, billion)	138.0	136.7	(0.94)
Central Bank's Assets in FX (USD, billion)	43.1	37.9	(12.1)
Central Bank's Gold Reserves (USD, billion)	11.2	13.9	23.6
Inflation Rate (%)	6.3	2.6	

Sources: Central Bank of Lebanon, Association of Banks in Lebanon, and Central Administration of Statistics.

2- Inflation

The Price Index of the Central Administration of Statistics increased by 2.6% on annual basis for the first nine months of 2019, compared to a higher level of 6.3% in the same period of 2018.

• | Evolution of Average Annual Inflation Rate (%)



3- Beirut Traders Association – Fransabank Retail Index

BEIRUT TRADERS ASSOCIATION
FRANSABANK
RETAIL INDEX
3rd Quarter 2019
45.04

Summer was full of promises and opportunities this year, and traders were looking forward for all the best, in terms of regain in activity and sales, that would allow wiping off some of the losses they have been incurring for so many quarters now because of the recessionary trend. Unfortunately, the Qabrshmoun incident took place and brought back immediately concerns and worries.

Concurrently, the government's decisions relative to new protectionist measures and tariffs imposed on a very wide range of imported products, and deliberations about these laws in the parliament, had a very negative impact on the outlook for a further deterioration of households purchasing power and the direct effects of such deterioration.

As a result, and instead of having a summer season characterized with high numbers of tourists and visitors and robust activity in all trade sectors, tourists and visitors did not come, and residents were all concerned with the measures taken by the government to curb the deficit instead of focusing on shrinking the volume of public expenditure and reducing the number of public servants, a number that has exceeded today levels the Lebanese economy cannot bear.

For all these reasons, results of the third quarter of 2019 posted further deterioration as compared to their levels for the same quarter a year before, and the number of shops and companies that have decided to cease activities and terminate the services of their employees has witnessed a noticeable increase: the consequence of this was clear and expected, and translated into a more difficult working environment for traders, lower levels of consumption, thus refraining all prospects for growth in the economy, while we all know that growth represents the sole way to salvage our faltering economy.

This deteriorating situation in the retail trading sectors is directly linked to the recessionary trend witnessed in the overall economy, an economy is affected to a large extent by the economic and political instability factors, including the deterioration of public finances, and public expenditures that appear to be unleashed and that have inflated to the detriment of the private sector which constitutes the prime and most essential engine of activity and growth in the economy.

Thus, markets activity and consumption momentum were weak during the summer of 2019: over and above the afore-mentioned factors, and on top of the falling purchasing power of Lebanese households because of the recession and because of the increasing unemployment levels accompanied with decreasing income, such activity and consumption momentum were also affected by the poor number of Arab and other tourists to Lebanon, and of Lebanese emigrants returning for summer holidays as usual, a fact that had an additional very negative impact on the turnover figures of shops and companies.

As a result, some traders continued to face the situation and resist the pressure, despite the sharp declines in their turnover figures, while others have decided to finally give up and close their shops or companies.

It should also be noted that the CPI between the third quarter of 2018 and the third quarter of 2019 as per the official CAS figures, posted a low + 1.09 % figure, and meaning that the impact of new taxes and customs rates had not yet fully reached the markets and had not started to impact significantly the prices of goods in the markets.

However, if sectoral inflation levels are scrutinized, it should be noted that inflation did reach some high levels in few sectors, and did reach – for the period under review the following:
+ 13.05 % in the clothing and footwear sector,
+ 6.83 % in the recreation, amusement, and culture sector,
+ 6.54 % in the furniture & decoration sector,
+ 5.08 % in the education sector.

Moreover, the food and non-alcoholic beverages accounted for only + 0.48%, while prices in restaurants increased by +1.19%.

CPI (as per CAS official results)	
Q4 '14 / Q4 '13	- 0.71 %
Q1 '15 / Q1 '14	- 3.38 %
Q2 '15 / Q2 '14	- 3.37 %
Q3 '15 /Q3 '14	- 4.67 %
Q4 '15 / Q4 '14	- 3.40 %
Q1 '16 / Q1 '15	- 3.57 %
Q2 '16 / Q2 '15	- 0.98 %
Q3 '16 / Q3 '15	+ 1.03 %
Q4 '16 / Q4 '15	+ 3.14 %
Q1 '17 / Q1 '16	+ 5.12 %
Q2 '17 / Q2 '16	+ 3.48 %
Q3 '17 / Q3 '16	+ 4.15 %
Q4 '17 / Q4 '16	+ 5.01 %
Q1 '18 / Q1 '17	+ 5.35 %
Q2 '18 / Q2 '17	+ 7.61 %
Q3 '18 / Q3 '17	+ 6.53 %
Q4 '18 / Q4 '17	+ 3.98 %
Q1 '19 / Q1 '18	+ 4.08 %
Q2 '19 / Q2 '18	+ 1.69 %
Q3 '19 / Q3 '18	**+ 1.09 %**
Q4 '14 / Q3 '14	- 1.49 %
Q1 '15 / Q4 '14	- 0.98 %
Q2 '15 / Q1 '15	- 1.12 %
Q3 '15 / Q2 '15	- 1.18 %
Q4 '15 / Q3 '15	- 0.16 %
Q1 '16 / Q4 '15	- 1.15 %
Q2 '16 / Q1 '16	+ 1.54 %
Q3 '16 / Q2 '16	+ 0.82 %
Q4 '16 / Q3 '16	+ 1.93 %
Q1 '17 / Q4 '16	+ 0.74 %
Q2 '17 / Q1 '17	- 0.04 %
Q3 '17 / Q2 '17	+ 1.47 %
Q4 '17 / Q3 '17	+ 2.78 %
Q1 '18 / Q4 '17	- 1.06 %
Q2 '18 / Q1 '18	+ 2.10 %
Q3 '18 / Q2 '18	+ 0.45 %
Q4 '18 / Q3 '18	+ 0.32 %
Q1 '19 / Q4 '18	+ 1.16 %
Q2 '19 / Q1 '19	-0.25 %
Q3 '19 / Q2 '19	**-0.14 %**

As a result, the consolidated real retail turnover figures (i.e. after applying the inflation rate weight on the nominal results) have posted a decline of – 6.18 % between the third quarter of 2018 and the third quarter of 2019, in comparison to the – 6 % posted for the previous quarter.

By excluding the fuel sector results (where a drop of – 2.18 % in volume was reported between the levels of Q3 '18 and Q3 '19), the real consolidated turnover drop reaches – 7.19 % in comparison to the Q3 '18 figures (also excluding fuel), against – 9.01 % for the previous quarter.

• Yearly Variation between 3rd Quarter '18 and 3rd Quarter '19

	Q3 2018	Q3 2019	
Nominal Year to Year Variation (incl. Liquid Fuels)	100.00	94.86	
Nominal Year to Year Variation (excl. Liquid Fuels)	100.00	93.83	
CPI between Sep '18 and Sep '19 (as per the official CAS figures)		**+ 1.09**	
Real Year to Year Variation (incl. Liquid Fuels)	100.00	93.82	**- 6.05%**
Real Year to Year Variation (excl. Liquid Fuels)	100.00	92.81	**- 7.19%**

* CAS – CPI – Sep '19

The above figures clearly display a sustained deterioration in consumption levels, with the continued prevalence of negative factors undermining the commercial activity, of which essentially the falling purchasing power of Lebanese households and its direct impact on the volume of their general expenditure, that is mainly geared towards essential sustainability products. This fall in the purchasing power is a direct result of the increasing number of entities that are deciding to close and cease their activities, and the resulting termination of employees from their jobs and the accompanying stop in those employees income, in addition to the inevitable rise in the prices of products in the markets as a result of the new measures. Consumption levels were also affected by the drop of transfers from abroad that the Lebanese working abroad are used to effect to their parents or relatives in Lebanon. All this is happening because of the uncertainty surrounding the prospects for the near future in the country, especially that no clear positive signs were emerging concerning the support that the international community pledged for Lebanon in the CEDRE conference, and in the absence of any public or private, local or international, investments in Lebanon.

One should not also forget the absence of the contribution of foreign visitors and tourists to the overall consumption in our local markets, a contribution that all traders usually rely on to make up for their weak turnovers.

The analysis of the performance during the third quarter of this year, and of the various retail trade market sectors, clearly translates the downtrend in the overall turnover figures, and shows that austerity has become normality in the spending pattern of Lebanese households, with selective consumption channeling main spending to basic necessities.

As a result, real figures (i.e. weighed with the respective CPI figures for every sector of the retail trade activities) posted by the main sectors where declines were registered during the third quarter of 2019 in comparison to the third quarter of 2018 included (in addition to the fuel sector where a drop in volume by – 2.18 % was recorded):

> Furniture (- 42.57 % against - 14.41 %)
> Cellular Phones (- 41.24 % against - 51.25 %)
> Shoes and Leather Products (- 23.92 % against - 54.78 %)
> Toys (- 19.77 % against - 28.78 %)
> Construction Equipment (- 16.41 % against - 38.51 %)
> Clothing (- 13.36 % against - 14.10 %)
> Household Electrical Equipment (- 12.16 % against - 22.15 %)
> Commercial Shopping Centers (- 11.21 % against - 13.27 %)
> Watches and Jewelry (- 8.69 % against - 2.63 %)
> Pharmaceuticals (- 8.51 % against - 15.57 %)
> Musical Instruments (- 6.83 % against - 53.55 %)
> Silverware and Decoration (- 6.54 % against - 27.18 %)
> Home Accessories (-5.88 % against - 7.78 %)
> Optical and Hearing Aid Instruments (- 4.57 % against - 19.37 %)
> Supermarkets and Food Shops (- 4.19 % against - 5.69 %)
> Liquor & Spirits (- 3.97 % against + 8.47 %)
> Sports Items & Equipment (- 3.72 % against - 2.89 %)
> Silverware and Decoration (3.27% against -10.15%)
> Used Cars Dealers (- 1.01 % against + 4.03 %)
> Medical Equipment (- 0.03 % against + 2.64 %)

The sectors that witnessed better results were:

> Tobacco (+ 12.86 % against + 7.01 %)
> Books & Stationery & Office Supplies (+ 11.14 % against - 12.88 %)
> Bakeries & Pastries (+ 4.43 % against + 1.50 %)
> Restaurants and Snacks (+ 0.28 % against + 7.37 %)
> Perfumes and Cosmetics (+ 0.18 % against - 2.41 %)

On the other hand, and despite the fact that the CPI between Q2 '19 and Q3 '19 indicated a drop in prices (- 0.14 %), the third quarter figures of retail trade sectors do reflect disparity between some sectors where a real quarterly improvement was experienced (Malls, Shoes, Clothing, Fuel, Home Electrical Appliances, Optical Instruments, ...) because of natural seasonal factors, and other sectors where sharp drops were posted (especially Construction Equipment and Furniture).

Lower turnovers were thus experienced in sectors that are not considered as vital, while other sectors, in addition to fuel, saw some increases, because of seasonal reasons (Air Conditioners, Clothing ..) and probably also because of continued extremely generous offers on prices conceded by traders to sustain their trading cycle.

As a result, the overall consolidated real result for the third quarter was only slightly negative, and displayed a real decrease of - 0.84 % as compared to the previous quarter (excluding Liquid Fuels, where a + 10.83 % increase was reported in terms of volume).

Sectors where declining activity was reported included:

> Furniture (- 31.52 %)
> Construction Equipment (- 29.61 %),
> Books & Stationery & Office Supplies (- 6.46 %)
> Pharmaceuticals (- 2.83 %)
> Supermarkets and Food Shops (- 1.75 %)
> Silverware and Decoration (- 1.31 %)

Positive results were posted, in addition to the fuels sector (+ 10.83 %) and to the Malls (+ 4.26 %), in the following sectors:

> Optical Instruments (+ 13.56 %)
> Toys (+ 7.44 %)
> Shoes and Leather Products (+ 6.65 %)
> Clothing (+ 4.71 %)
> Perfumes and Cosmetics (+ 4.09 %)
> Tobacco (+ 3.56 %)
> Bakeries & Pastries (+ 2.49 %)
> Cellular Phones (+ 2.97 %)
> Sports Items & Equipment (+ 1.86 %)
> Liquors (+ 1.56 %)
> Restaurants and Snacks (+ 1.29 %)
> Used Cars Dealers (+ 1.12 %)
> Watches and Jewelry (+ 0.74 %)
> Household Electrical Equipment (+ 0.53 %)

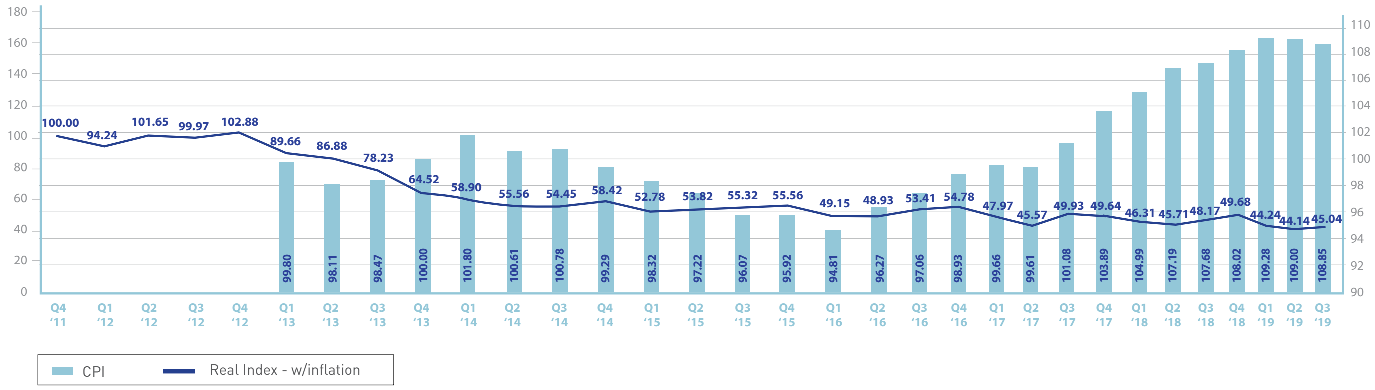
As a result, with the base index 100 fixed at the fourth quarter of 2011, and with a quarterly inflation rate of – 0.14% for the third quarter of 2019, as per the official CAS report, the "BTA-Fransabank Retail Index" is (with all sectors included): 45.04 for the third quarter of the year 2019. This figure compares to the level of 44.14 for the second quarter of 2019.

• BTA - Fransabank Retail Index for Q3 - 2019 (Base 100 : Q4 - 2011)

	2011	2012				2013				2014				2015			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real Index - w/out inflation	100	95.77	100.55	108.54	112.66	90.83	87.85	78.60	65.87	59.68	55.30	55.22	57.57	51.51	51.94	52.77	52.91
Real Index - w/ inflation	100	94.24	101.65	99.97	102.88	89.66	86.88	78.23	64.52	58.90	55.56	54.45	58.42	52.78	53.82	55.32	55.36
CPI						99.80	98.11	98.47	100.00	101.80	100.61	100.78	99.29	98.32	97.22	96.07	95.92

	2016				2017				2018				2019		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Real Index - w/out inflation	46.27	46.79	51.49	53.86	47.51	46.76	52.00	53.17	49.09	49.49	52.38	54.25	48.88	48.65	49.57
Real Index - w/ inflation	49.15	48.93	53.41	54.78	47.97	45.57	49.93	49.64	46.31	45.71	48.17	49.68	44.24	44.14	45.04
CPI	94.81	96.27	97.06	98.93	99.66	99.61	101.08	103.89	104.99	107.19	107.68	108.02	109.28	109.00	108.85

• **Evolution of the BTA - Fransabank Retail Index** (Base 100 : Q4 - 2011)



The "BTA-Fransabank Retail Index" for the third quarter of 2019 displays a very slight improvement, mainly attributed to an improvement in the inflation figure, on one side, and to natural seasonal factors on the other.

4- Stabilization Policy

The Central Bank of Lebanon has continued its monetary stabilization policy during the first nine months of 2019, just like in the previous years. The stability in the exchange rate (USD 1 = LBP 1,507.5) persists, thus contributing to overall monetary and economic stability.

To support this monetary stability, the monetary authorities have maintained its policy of moderating growth in money supply which increased by 1% only between September 2018 and September 2019. This is crucial also for controlling inflation.

V. Financial Markets

The banking sector has continued its growth in the first nine months of 2019, and so did the capital-market activity, but the activity of financial institutions contracted during the same period.

1- Banking Sector

The statistics of the Association of Banks in Lebanon and the Central Bank indicate that the total assets of commercial banks stood at USD 262.9 billion as of end-September 2019, with an annual growth of 5.1% from end-September 2018.

The loans extended by commercial banks to the private-sector decreased by 8.3% annually to reach 54.5 billion at end-September 2019. The dollarization rate of private-sector lending increased from 67.7% at end-September 2018 to 70.3% at end-September 2019.

The loans extended to the public sector reached USD 31.7 billion at end- September 2019.

The deposits of commercial banks at the Central Bank reached USD 152.7 billion at end-September 2019, with an annual growth of 23.2%.

The total private-sector deposits decreased by 2.1% on annual basis to reach USD 170.3 billion at end-September 2019. The dollarization rate of these deposits increased from 69.1% at end-September 2018 to 72.9% at end-September 2019.

The private-sector loans-to-deposit ratio was 32% at end-September 2019, compared to 34.2% at end-September 2018.

The commercial banks' capital base expanded by 2.7% year-on-year to reach USD 20.6 billion at end-September 2019.

Recently, the Central Bank has directed commercial banks to increase their Tier-I Capital by 20% to support their capital bases by nearly USD 3.7 billion by the end of June 2020.

• **Indicators of Commercial Banks** (USD, billion)

Indicators	2018 First Nine Months	2019 First Nine Months	% Change
Total Assets	249.5	262.2	5.1
Private-Sector Deposits	173.8	170.3	(2.1)
Private-Sector Loans	59.2	54.5	(8.3)
Loans to Public Sector	33.2	31.7	(4.5)
Deposits at Central Bank	123.9	152.7	23.2
Dollarization of Private Lending (%)	67.7	70.3	
Dollarization of Private Deposits (%)	69.1	72.9	
Loans to Deposits (%)	34.2	32.0	
Capital Base	20.1	20.6	2.7

Sources: Central Bank of Lebanon and Association of Banks in Lebanon.

2- Financial Institutions

The total balance sheet of financial institutions in Lebanon totaled USD 1.5 billion as of end-September 2019, down by 3.7% from end-2018. The claims on resident customers increased by 1.6% to USD 686 million. The claims on public sector expanded by 4.8%, while its deposits regressed by 37.8%.

The resident customer deposits decreased by 8.2% to USD 170.6 million as of end-September 2019.

The capital accounts of financial institutions went up by 1.04%, from USD 468.3 million as of end-2018 to USD 488.3 million as of end-September 2019.

These figures suggest a shrinking activity of the financial institutions operating in Lebanon in the first nine months of 2019.

• **Indicators of Financial Institutions** (USD, million)

Indicators	End 2018	2019 First Nine Months	% Change
Total Balance Sheet	1,539	1,482	(3.7)
Claims on Resident Customers	675	686	1.6
Claims on Public Sector	4.9	5.1	4.8
Resident Customer Deposits	185.8	170.6	(8.2)
Public Sector Deposits	4.5	2.8	(37.8)
Capital Accounts	468.3	488.3	1.04

Source: Central Bank of Lebanon.

3- Beirut Stock Exchange

The figures announced by the Beirut Stock Exchange (BSE) indicate that total trading volume reached 192.5 million shares in the first nine months of 2019, with an increase of 194.5% from 64.5 million shares in the same period last year.

The aggregate turnover increased by 72.4% during this period to reach USD 838.4 million as of end - September 2019.

Market capitalization of BSE decreased by 19% on annual basis to reach USD 7.9 billion at end-September 2019.

• Beirut Stock Exchange Indicators

Indicators	2018 First Nine Months	2019 First Nine Months	% Change
Market Capitalization (USD, billion)	9.75	7.9	(19)
Aggregate Turnover (USD, million)	486.6	838.4	72.4
Total Trading Volume (Shares)	70,283,902	192,542,592	194.5

Source: BSE.

VI- Foreign Sector

The balance of payments, mirroring the aggregate foreign sector activity, experienced a substantial deficit in the first nine months of 2019 relative to a lower deficit for the same period of 2018, due to shrinking capital inflows and big trade deficit.

1- Trade Balance

For the first eight months of 2019, the value of total exports reached USD 2.5 billion, with an increase of 24.1% from a year later. In parallel, total imports dropped by 0.9% to reach USD 13.8 billion during the same period. As such, the trade deficit narrowed by 3.1% on annual basis to reach USD 11.3 billion at end-August 2019.

The export-to-import coverage ratio improved from 14.4% in the first eight months of 2018 to 18.1% in the same period of 2019.

These figures indicate a better trade activity for Lebanon, fueled mainly by an improving export activity. The total amount of foreign trade expanded from USD 15.9 billion at end-August 2018 to USD 16.3 billion at end-August 2019, by USD 400 million during this period.

• Foreign Sector Indicators (USD, billion)

Indicators	2018 First Eight Months	2019 First Eight Months	% Change
Trade Deficit	11.9	11.3	(3.1)
Exports	2.0	2.5	24.1
Imports	13.9	13.8	(0.9)
Capital Inflows	10.7	6.9	(35.5)
Balance of Payments	(1.2)	(4.4)	

Sources: Higher Customs Council and Central Bank of Lebanon.

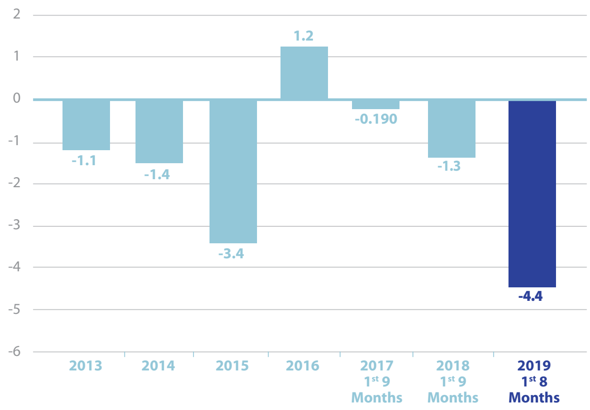
2- Capital Balance

The financial inflows to Lebanon declined by 35.5% on annual basis to reach USD 6.9 billion as of end-August 2019. This mirrors continued but lower capital inflows from foreign markets, which is partially stimulated by higher interest rates in Lebanon.

3- Balance-of-Payments

The statistics announced by the Central Bank show that Lebanon's balance of payments recorded a substantial deficit of USD 4.4 billion in the first eight months of 2019, relative to a lower deficit of USD 1.2 billion in the same period last year. The recorded deficit was due to a decrease of USD 3.4 billion in the net foreign assets of banks and financial institutions, and a decrease of USD 1 billion in the net foreign assets of the Central Bank.

Balance of Payments (USD, billion)



VII- Cabinet Resignation and Reform Plan

With the eruption of a wide civic protests in the country starting 17 October 2019 and afterwards, the Cabinet approved an Economic and Fiscal Reform Plan and a draft proposal for the 2020 General Budget before it resigned on 29 October 2019.

The 2020 General Budget proposal included the following directions: (1) 0.4% deficit, (2) BDL contributes to decreasing the debt service by half (nearly USD 3 billion), (3) Decreasing the salaries and benefits of current and previous presidents, ministers and Parliament members by half, (4) Income tax on banks for one year yielding nearly USD 400 million for the Treasury, and (5) No other taxes, besides no deductions on salaries of the public-sector employees.

The adjustment plan focuses on the following directions: (1) Freezing investment spending in 2020, (2) Transfer of surpluses of public institutions to the Treasury, (3) Cancelling and merging some public institutions, (4) Reducing the budgets of some councils (CDR, Council of the South, and Central Fund for the Displaced) by 70%, (5) Privatization of some public institutions, (6) Provision of electricity 24/24 by the second half of 2020, (7) Fighting corruption by some laws based on the establishment of a National Body for this purpose, (8) Implementing the CEDRE reforms, (9) Formation of some Regulatory Bodies, and (10) Reducing tax evasion and customs smuggling.

The civic protests have been calling for the formation of a technocrat government to restore confidence and support political-economic stability in the country. They are also calling for an early and new parliamentary elections to change the current Parliament. They are currently stressing the need to have an independent judicial system, and to restore the stolen public money.

Under such circumstances since 17 October 2019 and due to a major contraction in the macro economy during the first nine months of 2019, real economic growth is negative and estimated at nearly 0.5-1% this year. The country is currently experiencing a fiscal crisis coupled by a growing social crisis, and a major drain in the country's funds in US dollar. The country needs a fast formation of a new government, which is capable of restoring the degrading confidence in the country and its future, and resolving the current crises, mainly by implementing radical economic, fiscal and sectoral reforms that would support Lebanon's macro economy in the foreseeable and long terms.

Study | Foreign Direct Investment in Lebanon: Financial and Economic Dimensions

This study sheds light on the development of Foreign Direct Investment (FDI) in Lebanon over the past years, with its ups and downs, and the causes of such fluctuations mainly in recent years. The study compares the situation of Lebanon with other Arab countries as far as FDI and inward as well as outward FDI are concerned. The study explains the distribution of FDI in Lebanon according to the nationalities of foreign investors, and according to economic sectors. The study presents the major challenges and impediments prohibiting Lebanon from attracting increased substantial FDI to its national economy in recent years. The study proposes several policy recommendations in order to strengthen Lebanon's ability to attract further FDI to its economy, and to enhance its growth, stability and position on the regional and international investment maps.

I. Development of FDI in Lebanon

Lebanon has succeeded in attracting greater FDI to its national economy in 2018, despite the unfavorable political, fiscal and economic conditions prevailing for several years so far. The value of FDI in the Lebanese economy reached nearly USD 2.9 billion in 2018, relative to USD 2.6 billion in 2017, growing by an annual rate of 9.5%.

Since 1997, Lebanon attracted increased FDI to its economy, whereby its amount grew from USD 150 million in 1997 to USD 1.9 billion in 2004, and reached unprecedented levels of USD 4 billion in years 2008 (USD 4.3 billion), 2009 (USD 4.8 billion, and 2010 (USD 5 billion). However, FDI inflows afterwards regressed to USD 3.5 billion in 2011, increased to USD 3.8 billion in 2012, decreased to USD 2.83 billion in 2013, then increased to USD 3.1 billion in 2014. The average level of FDI stabilized at nearly USD 2.6 billion for the period 2015-2018.

• Evolution of FDI in Lebanon

Years	FDI (USD, million)
1995	35
1996	80
1997	150
1998	200
1999	250
2000	298
2001	249
2002	257
2003	358
2004	1,877
2005	2,000*
2006	2,500*
2007	3,000*
2008	4,330
2009	4,840
2010	4,960
2011	3,500
2012	3,780
2013	2,830
2014	3,100
2015	2,340
2016	2,610
2017	2,630
2018	2,880

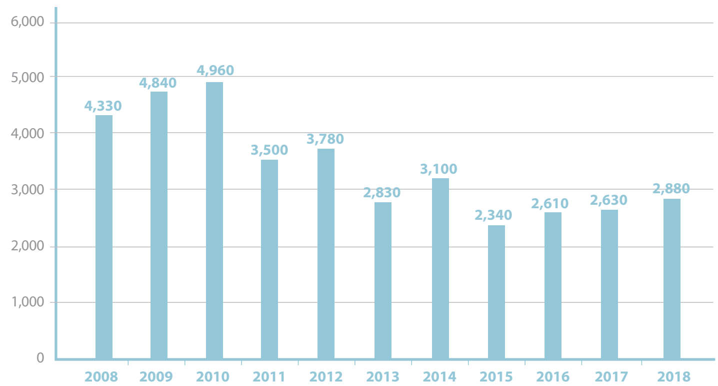
* Own estimates.
Sources: UNCTAD, IDAL, WB.

Later since 1997, FDI inflows started to boost, supported mainly by reconstruction efforts in real-estate and investment sectors, privatization of the mail system, lifting of travel embargo on U.S. citizens and companies to Lebanon, and monetary stabilization policy which controlled inflation and fostered monetary stability in Lebanon. In 2001, Lebanon passed a new investment law (Law n. 360 dated 16 August), which introduced new incentives, and authorized IDAL to issue investment permits. During the 2003-2009 period, FDI flourished, mainly in the tourism and telecoms sectors, and impediments were lifted on FDI by foreign companies.

The decline in FDI in Lebanon increased since 2010, due to the negative effects of the international financial-economic crisis, political instability in several countries of the region, drop in oil prices which affected countries investing in Lebanon, and the inflow of many Syrian refugees to Lebanon as a result of the erupted war in the country.

In recent years, FDI inflows into Lebanon have remain moderate relative to its previous levels during the 2008-2012 period. This is because of the eroding confidence in Lebanon's growth and prosperity prospects, as a result of the growing fiscal crisis (substantial fiscal deficit and debt), the aggravating economic crisis (very low levels of growth at nearly 1%), the serious social crisis (increased unemployment and immigration), and deteriorating foreign-trade sector (larger trade and balance-of-payments deficits).

Evolution of FDI in Lebanon (USD, million)



II. FDI in the Region

The Arab region has experienced substantial foreign investment inflows in 2007 and 2008, recording USD 80.3 billion and USD 88.5 billion respectively. However, these inflows then followed a downward trend since 2008, reaching low levels of USD 28.7 billion in 2017 and USD 26 billion in 2018 or 30.5% of its 2008 level. Several factors have caused this downward trend in FDI in the region, mainly:

• The economic slowdown fueled by a major drop in oil prices which negatively affected the economies of both the oil-producing countries and the non-oil producing countries. The observed economic slowdown was affected also by the international financial crisis which erupted in 2008 and lasted for several years, thereby reducing the growth of world economy and the highly-open regional economy.

• The emerging political, security, economic and social instability in some countries of the Arab region, following the so-called "Arab Spring" and internal conflicts in countries like Syria, Egypt, Libya, Tunisia, Yemen, Sudan and Iraq. The investment climate was negatively affected by such turmoil in those countries.

All these unfavorable events and developments have also led to FDI outflows from the Arab region toward key international markets. Such outflows increased from USD 18.9 billion in 2009 to more than USD 30 billion in 2015, 2016, 2017 and 2018. These outflows reached historic levels in some years like 2008 (USD 44.2 billion), and 2013 (USD 42.5 billion).

It should be noted that the FDI balance of the Arab world was in surplus (meaning that inward FDI was greater than outward FDI) during the 2007-2014 period, and in deficit (meaning that outward FDI was greater than inward FDI) after 2014. Net FDI in the Arab region which was positive and reached high levels above USD 40 billion in years like 2007, 2008 and 2010, and above USD 59 billion in 2009, but dropped in an acute manner and became negative in some years like 2013 (USD 1 billion), 2015 (USD 11.6 billion), 2016 and 2017 (more than USD 3 billion) and 2018 (nearly USD 4 billion).

• Evolution of Inward and Outward FDI in Arab Countries (USD, billion)

Years	Inward FDI	Outward FDI	Surplus or Deficit
2007	80.3	37.4	42.9
2008	88.5	44.2	44.3
2009	78.3	18.9	59.4
2010	70.1	21.1	49.0
2011	44.8	29.6	15.2
2012	52.7	21.6	31.1
2013	40.5	42.5	(2.0)
2014	31.6	17.0	14.6
2015	25.7	37.3	(11.6)
2016	32.4	36.2	(3.8)
2017	28.7	32.0	(3.3)
2018	26.0	30.0	(4.0)

Sources: Arab Investment and Export Credit Guarantee Corporation.

The net FDI in the Arab region as a percentage of its GDP has witnessed a downward trend over the past years, reaching an average rate for the 2017-2018 period 0.72% in Algeria, 0.59% in Qatar, 0.21% in KSA, and 0.91% in Sudan. The FDI balance was negative in countries like Iraq (2.62%), and Yemen (0.86%). However, it was positive and relatively high in the case of Lebanon (4.8%), Egypt (3.14%), Jordan (5.07%), and Sultanate of Oman (4.02%).

• Net FDI as a Percentage of GDP in some Arab Countries (%)

Year	Ratio
Lebanon	4.8
Algeria	0.72
Bahrain	1.46
Egypt	3.14
Iraq	(2.62)
Jordan	5.07
Morocco	2.44
Oman	4.02
Qatar	0.59
Saudi Arabia	0.21
Sudan	0.91
Tunisia	2.03
United Arab Emirates	2.71
Yemen	(0.86)

Source: World Bank.

The inter-Arab FDI has experienced a declining trend since 2008, from USD 64.7 billion in 2008 to nearly USD 12 billion in 2017 and 2018, thereby representing only 18.5% of its 2008 level. This shrinking inter-Arab investments occurred at times the executive program of the Greater Arab Free Trade Area (GAFTA) was launched in 2008, which paved the way for greater commodity trade exchanges between the Arab countries. The effects of such program were clearly noticed as the level of trade exchanges surged from USD 17.8 billion in 2007 to USD 64.7 billion in 2008, i.e. by more than 3.6 times. The major causes for the drop of such investments after 2008 was the commodity exemption lists presented by some Arab countries, besides the state of internal conflicts and instability in some Arab countries as mentioned above.

• **Evolution of Inter-Arab Investments** (USD, billion)

Years	Amount
2007	17.8
2008	64.7
2009	33.9
2010	17.2
2011	14.2
2012	20.7
2013	13.7
2014	11.4
2015	13.9
2016	22.2
2017	12.6
2018	12.0

Source: Arab Investment and Export Credit Guarantee Corporation.

Egypt attracted the largest share of FDI in the Arab region with more than 50%, followed by UAE with more than 13%, then KSA with over 10%.

As for inter-Arab investments, Egypt also got the largest share with over 40%, followed by UAE with more than 24%, then KSA with over 14%.

III. Lebanon's Position in the Region

The position of Lebanon in attracting FDI remained better than that of many other Arab countries, despite its declining trend in recent years. The share of Lebanon in total FDI flowing to the Arab region was 13.7% in 1995, in excess of 10% in 1999 and 2000, higher than 9% in 2015 and 2017, and nearly 11% in 2018.

• Evolution of Lebanon's Share in Total FDI in the Arab Region

Years	FDI in the Arab Region (USD, million)	Share (%)
1995	255	13.7
1996	3,582	2.2
1997	7,288	2.1
1998	8,740	2.3
1999	2,495	10.0
2000	2,629	11.3
2001	7,711	3.2
2002	5,378	4.8
2003	8,617	4.2
2004	46,695	4.0
2005	n a	n a
2006	n a	n a
2007	80,300	4.0
2008	88,500	5.0
2009	78,300	6.0
2010	70,100	7.0
2011	44,800	8.0
2012	52,700	7.0
2013	40,500	7.0
2014	31,600	10.0
2015	25,700	9.0
2016	32,400	8.1
2017	28,700	9.3
2018	26,000	11.0

Sources: UNCTAD, IDAL, WB.

Lebanon was the sixth largest country among Arab countries in attracting FDI into its economy in 2018 (nearly USD 2.9 billion) after UAE (USD 10.4 billion), Egypt (USD 6.8 billion), Sultanate of Oman (USD 4.2 billion), Morocco (USD 3.6 billion), and KSA (USD 3.2 billion).

Also, Lebanon was the seventh largest country among Arab countries in terms of FDI growth, with 14.2% between 2017 and 2018, following KSA (126.1%), Djibouti (60.6%), Sultanate of Oman (43.6%), Morocco (35.5%), Algeria (22.2%), Tunisia (17.6%), and Palestine (11.2%).

• **Evolution of FDI in the Arab Region** (USD, million)

Country	2017	2018	% Change	% Share
UAE	10,354	10,385	0.3	33.3
Egypt	7,409	6,798	-5.2	21.8
Oman	2,918	4,191	43.6	13.4
Morocco	2,686	3,640	35.5	11.7
KSA	1,419	3,209	126.1	10.3
Lebanon	2,522	2,880	14.2	9.2
Bahrain	1,426	1,516	6.2	4.9
Algeria	1,232	1,506	22.2	4.8
Sudan	1,065	1,136	6.6	3.6
Tunisia	881	1,038	17.6	3.3
Jordan	2,030	950	-53.2	3.0
Somalia	384	409	6.5	1.3
Kuwait	348	346	-0.7	1.1
Djibouti	165	265	60.6	0.8
Palestine	203	226	11.2	0.7
Mauritania	587	71	-88.0	0.2
Libya	0	0	0.0	0.0
Syria	0	0	0.0	0.0
Yemen	-270	-262	4.5	-0.9
Qatar	956	-2,186	-321.7	-7.0
Iraq	-5,032	-4,885	-2.9	-15.7
Total	**31,314**	**31,208**	**-0.3**	**100.0**

Source: UNCTAD – Investment Report 2019.

The inward FDI in Lebanon accounted for over 10% of total FDIs in West Asia, nearly 0.5% of FDIs in emerging economies, and nearly 0.2% of total world FDIs in 2018.

In parallel, the outward FDI in Lebanon was nearly USD 567.3 million in 2017, down by 11.6% from USD 641.9 million in 2016, and compared to an average of USD 998.4 billion for the 2010-2016 period. Its level reached its peak in 2013 with nearly USD 2 billion. Lebanon was the sixth largest country among 16 Arab countries in terms of outward FDI, and also among West Asia countries in 2017.

The net FDI in Lebanon was nearly USD 2.1 billion in 2017, up by 4.7% from USD 2 billion in 2016, and compared to a peak of USD 3.5 billion in 2009. This ranks Lebanon as the second largest attractor of such net FDIs among the Arab countries in 2017.

The FDI in Lebanon accounts for nearly 5% of its GDP as in 2018, relative to a peak rate of 15.5% in 2005. This ratio is the third largest ratio in the Arab world, following Djibouti (nearly 8%), and Mauritania (nearly 6%).

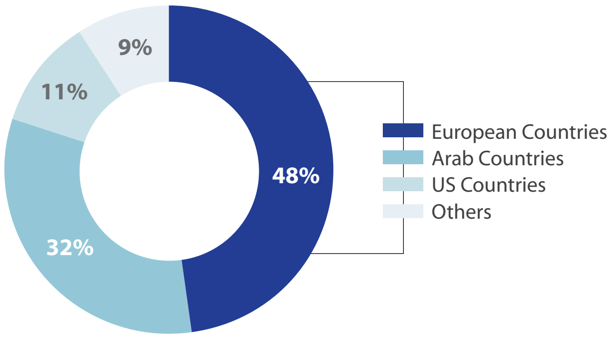
IV. FDI Structure in Lebanon

The average annual number of foreign investment projects in Lebanon was nearly 50 projects for the 2015-2018 period. European companies investing in Lebanon rank the first with a market share of 48% of the total number of foreign companies in Lebanon. The three major European countries investing in Lebanon are France and Germany with a market share of 9% for each, and Italy with a market share of 4.5%.

The Arab countries constitute the second major investor in Lebanon with a market share of 32% of the total number of foreign companies in Lebanon. UAE rank first among the Arab countries with a share of 22.7%, followed by Jordan 4.5%.

US countries have a market share of 11% of the total number of foreign countries in Lebanon, while the remaining 9% distributed among other foreign countries.

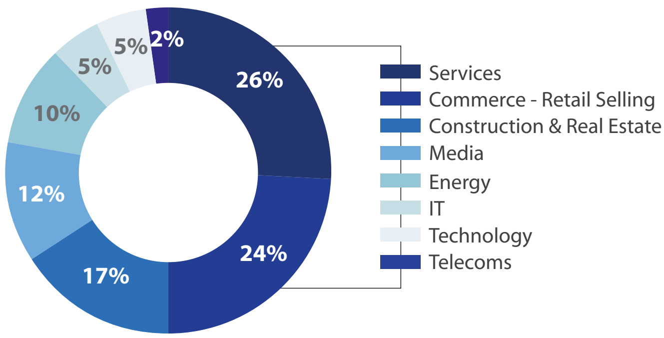
Distribution of Foreign Countries Investing in Lebanon according to Nationalities Average 2015-2018



Source: Ministry of Economy and Trade of Lebanon.

As for the distribution of FDI in Lebanon according to economic sectors, the services has a share of 26% of the total, followed by commerce and retail selling 24%, construction and real estate 17%, media 12%, energy 10%, IT and technology 10%, and telecoms (2%).

Sectoral Distribution of Foreign Companines Investing in Lebanon Average 2015-2018

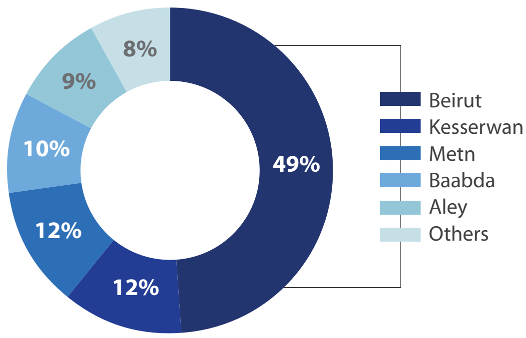


Source: Ministry of Economy and Trade of Lebanon.

In Lebanon, the real-estate sector has always remained a major sector attracting foreign investments, despite the observed slowdown in its activity in recent years, and despite the unfavorable domestic and regional conditions. Arab investors, in general, have maintained their investments in this sector for personal use and lease purposes.

Beirut has the greatest market share of foreign investments in the real-estate sector, with nearly 49%, followed by Kesserwan 12%, Metn 12%, Baabda 10%, Aley 9%, and other regions 8%.

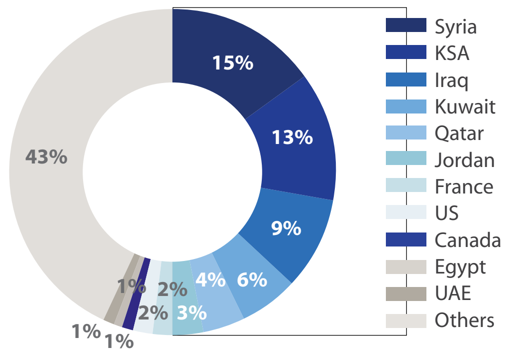
Distribution of Foreign Investments in Real Estate in Lebanon according to Regions Average 2015-2018



Source: General Directorate for Real Estate in Lebanon.

The distribution of real-estate purchases according to nationalities shows that the Syrians have the greatest market share of 15%, followed by the Saudi investors (13%), Iraqi (9%), Kuwaiti investors (6%), Qatari investors (4%), Jordanian investors (3%), French and US investors (2% for each), and Canadian and Egyptian and UAE investors (1% for each).

Distribution of Real-Estate Purchases by Foreign Investors in Lebanon Average 2015-2018



Source: General Directorate for Real Estate in Lebanon.

V. Challenges of FDI Attraction to Lebanon

It is clear that uninterrupted FDI inflows to Lebanon are not sufficient to stimulate an enhanced national economy and aggregate economic activity. This is evident if we know that this FDI represents nearly 5% of GDP, despite the fact that foreign investors have significant incentives in Lebanon.

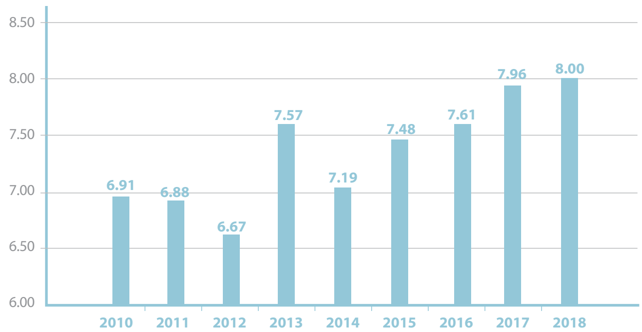
In this sense, several obstacles and challenges face an enhanced FDI activity in Lebanon in recent years.

The most noticeable challenge facing greater FDI inflows to Lebanon is the eroding confidence of the Lebanese and the international community in the ability of the government to implement radical fiscal, sectoral and economic reforms. Such reforms are necessary to deal with the aggravating fiscal-economic crisis Lebanon is currently facing and which have continued since the assassination of the late Prime Minister Rafic Hariri in 2005.

Lebanon is currently facing a critical fiscal crisis, where the public fiscal deficit stands at USD 6 billion annually, which represents nearly 10% of GDP, accompanied by a growing public debt of USD 85 billion, which accounts nearly for 150% of GDP.

Also, Lebanon is currently suffering from a substantial annual trade deficit of USD 17 billion, due to weak national exports (less than USD 3 billion) and huge national imports (more than USD 20 billion), declining remittances from the Lebanese Diaspora (nearly USD 8 billion currently), lower foreign capital inflows (nearly USD 11.6 billion in 2018 relative to USD 14.3 billion in 2017), and a substantial balance-of-payments deficit of nearly USD 5.4 billion in the first half of 2019.

Evolution of Remittances from the Lebanese Diaspora



Source: World Bank

This twin deficit (trade deficit and fiscal deficit) constitute the real cause of the aggravating economic problem in Lebanon in recent years. Another major cause is the weaker activity of leading productive sectors such as agriculture and industry and leading services sectors such as tourism, construction, real estate and banking. These negative factors curb aggregate economic growth rates to nearly 1% annually, which is not sufficient to create sufficient job opportunities for the flowing youth to the domestic labor market, where general unemployment is currently 20% and 40% among the youth.

It should be noted here that the donor countries and organizations have allocated international financial support by more than USD 11 billion to Lebanon in the context of CEDRE Conference. They conditioned that the Lebanese government should implement certain fiscal, sectoral and economic reforms. They also conditioned that the government should implement a plan to reform the energy sector, which is incurring annually a loss of USD 1.5-2 billion that accounts for 40% of the gross public debt. So far, the Lebanese government did not implement any of these reforms.

Therefore, the weaker FDIs to Lebanon in recent years is attributed to lower stability of the macro economy due to the twin deficit (trade and fiscal), slow economic growth rates, greater exposure of Lebanon to regional disturbances (political, security and economic) in some countries like Syria and Iraq, and the declining Gulf investments in the country.

The current distortions in the domestic labor market is another impediment to greater FDI inflows to Lebanon. The country has been experiencing for several years so far an inflow of Syrian refugees, a development that exerts further pressures on the local labor market and public services (especially energy, education and public health), and increased brain drain and aggravating unemployment. In this context, the World Bank estimated that Lebanon needs more than 23,000 job opportunities every year to integrate the inflowing youth into the local labor market. Between 2004 and 2007, for instance, Lebanon created only 3400 job opportunities per annum.

A major obstacle facing foreign investors in Lebanon is the energy crisis, where the provision of electrical power is interrupted in most Lebanese regions, a development that raises the cost of production. This discourages potential investors from investing in the country. There is also the growing state of corruption which again discourages foreign investors for increasing their investments in Lebanon.

The bad conditions of the energy sector is a major factor impeding economic diversification in Lebanon, especially the transformational industries which are attractive to foreign investors. These industries today account for nearly 5% of GDP, declining from 14% in 1998. This is caused by the closure of some factories over the past years.

VI. Policy Recommendations

FDI is defined as the inflow of foreign capital into a country and the formation of new partnerships and businesses, where foreign investors own shares of at least 10%. FDI secures several significant benefits and advantages for the host and investing countries: creating more productive and services enterprises in the local economy, expanding the scope of new activities, knowledge and technology transfer, increasing the local productive and export capacity, stimulating economic growth, widening job opportunities, supporting economic and social development, providing new financing in foreign currency, enhancing the position of public finances and trade balance, and creating better prosperity prospects for the national economy.

Hence, these advantages and benefits can be achieved by Lebanon if it promotes its capacity to attract further FDI to its national economy. To be able to achieve this, the government should strive to increase annual growth rates, which is a prime condition to attract foreign investors. This is why the inflow of greater foreign investments is a major indicator of the strength and resilience of an economy and its growth prospects.

To achieve better economic growth, the government of Lebanon has to implement the newly approved electricity plan. Focus should be set on enhancing the capacity of existing power plants, establishment of new power plants, development of transportation and transmission networks, seizure of technical and non-technical losses, corporatization of EDL and the formation of both a new board and regulatory authority. This reform in the power sector is necessary to lower the country's fiscal deficit and public debt, and decreasing the cost of production in the productive sectors mainly the industrial sector. Such a reform of the energy sector will encourage both the domestic and foreign private sector to invest in Lebanon to this sector, a development that will increase its economic contribution.

The attraction of FDI to Lebanon requires the creation of real partnerships between the public and private sectors, in the context of the existing Lebanese Law which was approved by the government. The potential sectors for FDI are telecoms, airports, roads, transportation, water, ports and others. These infrastructure sectors are attractive for local or foreign private investors. If some of these sectors are privatized, this could contribute to better FDI inflows to Lebanon.

The government of Lebanon must seek to rebuild and enhance its relations with the Gulf countries and Arab countries in general, because they are considered the major investors in Lebanon's economy, and the prime motivators of aggregate economic activity mainly construction, real estate, telecoms, technology, tourism, and banking.

The government should give special attention to the industrial sector, by increasing incentives, so as to enhance its productive and export capacity. This is crucial for controlling imports which consumes foreign-currency reserves. Such an attention to the industrial sector would also promote the attraction of FDI to this sector.

The government must address, seriously, the current state of corruption in the public sector, a factor that constitutes a prime condition to attract further FDI to Lebanon. This is a major reform required by the international community and also the local community to adjust the position of the public finances and national economy. The government should halt tax evasion and customs smuggling, control its maritime and river properties, and enhance revenue collection from public services sectors such as electricity. It should also implement radical administrative reforms to decrease the size of the public sector and ration its unproductive expenditures which constitute today more than 40% of GDP. This inflated public sector is causing a significant crowding-out effect in the national economy.

The government of Lebanon has to undertake serious and quick measures to consolidate the foreign-trade position, so as to stimulate exports and lessen imports which drains more than USD 20 billion in foreign currencies. It must revise, update and adjust Lebanon's existing trade and economic agreements with many Arab and foreign countries. It must implement the reciprocity principle, so as to decrease the substantial levels of trade deficit which exceed currently USD 17 billion. The government should, as well, seek to rationalize consumption of goods in general and foreign goods in specific. An economy that focuses on consumption, instead of investment, is not attractive for FDI and is unable to stimulate economic growth.

These much needed reform measures constitute a major prerequisite to rebuild and develop the international and local confidence in Lebanon, its currency, economy and future. It is also important to free Cedre funds which are significant for recovering the Lebanese economy, promoting economic and social development, seizing brain drain and capital drain, and encouraging foreign investors to invest in Lebanon.

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