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## **THE PARIS CONFERENCE IV: OPPORTUNITIES AND IMPLEMENTATION POTENTIALS**

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# **The Paris Conference IV: Opportunities and Implementation Potentials**

## **Introduction: Paris Conference IV and the Phenomenon of Assorted Conferences**

Between March 2018 and April 2018, three international conferences were respectively held in Rome, Paris and Brussels, with the declared strategic goal –especially for the Paris and Rome conferences- of shielding the political and economic stability of Lebanon. Theoretically, holding numerous conferences can be positive as long as they are convened under the banner of supporting Lebanon. However, this phenomenon is double-edged owing to its association with a long-standing dilemma that reflects the Lebanese State’s proven inability over time to invest for the future on its own and its permanent need for the help of “alternatives from abroad” to manage its affairs, especially when it comes to ways of facing major economic or political challenges, such as handling the country’s delicate confessional balance, or addressing the crisis of deficit and public debt or deciding Lebanon’s stance with respect of the region’s turmoil and its implication. The Rome Ministerial Meeting (March 2018) highlighted security and political issues related to supporting Lebanon’s sovereignty and armed forces and urged the country to finalize its defense strategy and apply the “dissociation” policy regarding regional

conflicts, pursuant to the relevant Security Council resolutions. The Brussels Conference (April 2018) was held with the aim of raising about \$9 billion for the United Nations to distribute to internally displaced persons in Syria and Syrian refugees in neighboring countries, especially Lebanon, of which \$4.4 billion was secured (about half of which was provided by France and Germany).

The Paris Conference IV (or Cedar 1) held on April 6, 2018, which is the subject of this paper, has been confined to one main issue: Providing concessionary loans to Lebanon to finance a Capital Investment Program (CIP) aimed at rehabilitating and developing its utility networks and obsolete infrastructure.

The Paris Conference IV documents<sup>2</sup> - “Final Report”, “Government Vision for Economic Stabilization, Growth and Employment”, “List of Projects” and “Proposed Privatization Projects” - included a capital investment program which covers the next 12 years, divided into three phases of 4 years each. Phases 1 and 2 (2018-2025) target a total of \$17.25 billion, while phase 3 targets an amount of \$5.7 billion, bringing the total amount to around \$23 billion. The transportation sector represents 33%, the electricity sector 21%, while water projects and wastewater treatment... account for 18%. In response

<sup>1</sup> Resolutions 1559 in 2004, 1680 in 2006 and 1701 in 2006

<sup>2</sup> Government of Lebanon: Capital Investment Program, Final Report, March 2018 – Vision for Stabilization, Growth and Employment – List of Projects – Potential PPP infrastructure projects.

to the Lebanese request, the conference committed to provide Lebanon with concessionary loans and others subject to guarantees and commitments, amounting to some \$11 billion<sup>3</sup>, of which 7.5% in grants<sup>4</sup>. The convening of the conference was rushed due to two major factors: The first is of domestic nature and is related to the lack of economic options available to Lebanon after most of the economic and financial indicators reached red lines; and the second is of foreign dimension, linked to the growing European (and especially French) fears that any economic collapse in Lebanon would leave the old continent contending with a new influx of Syrian (and non-Syrian) migrants.

This paper encompasses eight main axes:

The first axis reviews and analyzes the most important macro-economic indicators in Lebanon on the eve of the conference;

The second axis discusses the portrayal of the documents the Lebanese Government has submitted to the Paris Conference IV: Do they akin to a development vision, an economic plan, an investment program...?

The third axis examines whether the CIP has set in advance specific sectoral targets;

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<sup>3</sup> Some of these amounts were re-aggregated from previous unexpended loans, particularly those relating to non-performing loans from the World Bank (about \$1 billion)

<sup>4</sup> The donation rate was estimated at 30% at the Paris Conference (3)

The fourth axis weights the impact of implementing the CIP on public finances;

The fifth axis deals with the ramifications of linking between the CIP and the application of the Public Private Partnership (PPP) law;

The sixth axis anticipates the impact of the CIP implementation on the local labor market performance;

The seventh axis examines the public authorities and institutions' eligibility and aptness to implement the CIP;

The eighth axis examines the impact of the outcome of the country's long-awaited parliamentary elections on the CIP's chances to become reality;

The paper concludes with a summary of alternative future options.

## **1 - A New Phase of Serious Indicators of Worsening Economic Crisis:**

Lebanon is currently facing overlapping macro-economic crises. Annual economic growth rates that had ranged between 8.5% and 9% from 2007 to 2010, have since 2011 fallen to between 1% and 1.5% in average, leaving the country with an impossibility of realizing a positive breach in future growth projections, should current trends continue. Concurrent with this decline, deficits in external account increased, starting with a

chronic structural trade deficit where exports do not cover more than 15% of imports, to a cumulative deficit in the balance of payments for the seventh consecutive year<sup>5</sup>, to the current account deficit estimated at 24% of gross domestic product (GDP) in 2017. These macro indicators presage a rise of the public debt ratio from its current level of more than 150% of GDP, to record levels difficult to control, which has prompted the International Monetary Fund<sup>6</sup> (IMF) and sovereign credit rating agencies to repeatedly warn of risks threatening the financial and monetary stability of the country. The Lebanese State has become the main customer of the banking sector, with its debts to banks and to the *Banque du Liban* (BdL) accounting for 65% of banks' budget, which limits the ability of the banking sector to finance the private economy. In addition, the BdL will be required to provide \$4 billion in 2018 to only cover the interest costs on its dollar debt. This annual cost is likely to rise further as the BdL continues to increase its dollar debt and with the upward trend in the global dollar interest rate<sup>7</sup>.

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5 The *Banque du Liban* has adjusted the method used to calculate the balance of payments in a way that hides the continuing deficit since 2011. Since last November, it has added the Lebanese Republic's foreign currency treasury bills and bonds to its net foreign assets, contrary to the global trend. The balance sheet recorded a temporary technical surplus in early 2017 as a result of the financial engineering carried out by the Banque du Liban in 2016 and 2017; however, this surplus turned into a deficit of \$208.3 million at the end of June 2018. For more details on the actual situation of the balance of payments, see Mohammed Zbib's study, Capital Supplement, al-Akhbar newspaper, August 13, 2018.

6 See the preliminary reports (Article IV) of the International Monetary Fund of 12 February 2018 and 21 June 2018.F

7 Regarding the financial crisis on the eve of the Paris Conference IV, see the policy paper prepared by Dr. Toufic Gaspard: "The Financial Crisis in Lebanon", Maison du Futur and the Konrad Adenauer Stiftung, August 2017.

Despite the measures adopted by the Lebanese Government at the dawn of the new presidential term starting 2016<sup>8</sup>, growth rates have not regained their upward trajectory due to long-standing severe structural deficiencies. The rentier economic model<sup>9</sup> prevailing since the early 1990s has exclusively focused on two traditional determinants of growth: The first is promoting public and private consumption, which is mainly financed by public revenues, labor incomes, remittances from abroad (especially to households), and loans on which both the State and households relied to meet their consumption needs. The second is facilitating and maximizing private investment in the construction and real estate sector, with banks financing real estate developers and subsidizing housing sale (through BdL), and also financed with direct foreign investments and remittances. Other determinants of growth - such as public investment in infrastructure, and private investment in the export of goods and services and in the technology and knowledge economy - remained very modest.

It was clear that the mechanisms of this prevailing model, which remained relatively functional until the end of the first decade of the 2000s, gradually deteriorated towards

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<sup>8</sup> Including the approval of the country's first budget (2017) in 12 years and the passing of 2018 budget, the ratification of the public sector's long-standing salary scale bill in 2017, the adoption of a new electoral law in the same year, and holding general elections in 2018.

<sup>9</sup> The use of the expression "the rentier economic model" is no longer limited to a number of economists, but has also been adopted by the President of the Republic on several official occasions.



exhaustion and disruption starting 2011. This was due to turbulent internal and regional developments, mainly: Presidential, legislative and governmental vacuum, the ruling class ill-management of public economic affairs, the repercussions of the Arab Spring on the Lebanese economy especially in what pertains to the economic boycott of Lebanon launched by several Arabic Gulf states, and the effects of the massive displacement of Syrians from their war-torn country, sougning refuge in Lebanon (and neighboring countries). As a result of these events, the growth rates of total deposit in the Lebanese banking sector significantly slowed down, i.e. the basic safety valve that allowed banks to continue financing the growing public deficit and contribute to reducing deficits in external accounts. Amidst the inability of the Lebanese ruling lineups (and perhaps their unwillingness) to embark on real and sustainable reform, the only exit way was in resorting again to the international community, and therefore, the above-mentioned conferences were held and came to complement previous alike-ones.

## **2. The Paris Conference IV Documents: A Comprehensive Development Plan, an Investment Program, or Just a “Declaration of Intent”?**

On the sidelines of the periodic conferences held in Brussels on the issue of Syrian refugees (2016 and 2017), the Lebanese side found that dealing with the long-standing Syrian refugees’ fallout required more

than just asking for funding their urgent relief needs, at a time when “donors” were increasingly pressuring governments of destination countries to facilitate the gradual integration of refugees into the local community, and especially into local labor markets. This pressure was driven by two main factors: An economic factor that is the large difference between migrants’ relief and employment cost in European countries, compared to the cost of sustaining their survival in countries across the region. Preliminary estimates<sup>10</sup> indicate that such cost in Germany, for example, is eight times higher than in Lebanon; and a political factor related to increased fears on the civil and social peace and cultural fabric of European countries in the event of continued influx of refugees, amid a rise of populism, mostly conservative-leaning, throughout the continent. The international community pressure on Lebanon occurred not only amongst a worsening economic crisis, but also the collapse of an already weak and under-resourced public infrastructure benefiting both the Lebanese and the Syrian refugees. In fact, between 1993 and 2017, the Lebanese Government investment in infrastructure<sup>11</sup> has not exceeded 7% of the public expenditure. This investment continued to sharply drop from 3% of GDP annually between 2005

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10 INFO MIGRANTS - Mara Bierbach - [www.infomigrants.net/en/post/5049/how-much-money-do-refugees-in-germany-get](http://www.infomigrants.net/en/post/5049/how-much-money-do-refugees-in-germany-get) - 2017/09/12.

11 Figures retrieved from a statistical database available at the Ministry of Finance and the BdL.

and 2010 to 1.4% between 2011 and 2017<sup>12</sup>; accordingly it is safe to say that despite the drastic impact of the Syrian exodus on Lebanon's infrastructure it would be unfair to solely blame the Syrian refugees' presence in the country for its dilapidated infrastructure networks.

For the most part, investment projects the Lebanese Government has included in its CIP have been in the concept books for a long time, dearly preserved in the Council for Development and Reconstruction (CDR) and other relevant public institutions' registries. Some of the projects appear to be the leftovers from previous development efforts that, for one reason or another, were not funded. The CDR collected and itemized the projects' concept books according to a number of indicators: Readiness for implementation, priority rating, and estimated value of their costs and required labor days. Most of these concept books relate to public (national) networks that will cover the entire Lebanese territory, notwithstanding that only one-third refers to projects that will be geographically distributed<sup>13</sup>.

As some of these projects are of olden days, it is difficult to ascertain if they were streamlined in terms of cost re-

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12 It is noteworthy that more than 80% of the State's capital expenditures have been channeled by the CDR; this figure fell between 40% and 50% after 2008, due to some ministries' –especially the Ministry of Energy- newly acquired trend to self-managing its capital expenditures.

13 Some of these projects were included in the CIP for the only reason of achieving a balance of interests between the governing parties, regardless of their priority, the readiness of their concept books, and the ability of local authorities to contribute to their management once implemented.

budgeting, investment re-appraisal and re-prioritization, and if they involve sustainability elements whether from an environmental or social perspective. For many of these projects, the government has reached the stage of issuing decrees pertaining to funding its share, in particular the cost of expropriation. However, it did not actually provide these allocations for lack of funds or due to the bureaucratic red tape and the lengthy cycle of signatures between the relevant ministries and the CDR. This situation has extended to projects covered by commitments made by donors in previous international conferences, leading to recycling allocated funds year after year or to their fall due to statute limitations.

Notably, the documents of the Paris Conference IV did not include an assessment - even a brief one - for previous public capital investment spending experiences, in order to truly verify their contribution to increasing the productivity of the economy and creating new jobs. In the past, many questions have been raised about the effectiveness of the reconstruction programs implemented during the second half of the 1990s, which have not yet been subjected to a serious and in-depth evaluation of their successes and failures, in order to draw useful lessons for subsequent public capital investment projects. Had this gap been avoided, the Lebanese Government would have been able to define more precisely the current features and priorities (sectoral and regional) of its CIP, in order to maximize

the economic benefits of the proposed development projects, especially in light of the scarcity of local human, institutional and financial capacities. Combined, these factors leave one speculating about the seriousness and value of the CIP's strategic analysis and planning, and an impression that at this stage it is more conceptual than set in stone; an impression that it does not amount to a development vision or economic plan in the strict sense, without ruling out the possibility that it will turn into a mere "declaration of intent" if it is not supplemented by duly deep reforms in the State's performance and public policies. Notwithstanding, implementing these reforms has become a voiced pre-requisite for lenders in order to fulfill the financial pledges they have made at the conference.

### **3. Does the Capital Investment Program Introduce Clear Predefined Sectoral Priorities?**

The CIP did not identify specific sectoral economic targets, and did not present a convincing and adequate approach showing the direct positive correlation between the implementation of capital investments and their actual impact on increasing growth rates<sup>14</sup>. In addition, the CIP failed to assess the overlapping and interlacement patterns between sectoral activities and available pathways to enhance them, consequently

<sup>14</sup> In a workshop organized by the *Kulluna Irada* (All-Will) association in March 2018, before the Paris Conference IV, and in a speech delivered during its convening on April 6, 2018, the association came to the fore and raised its doubts in the CIP's potential ability to increase growth rates.

preventing clear awareness of how its projects relate to the urgent need for restructuring sectors and developing a division of labor among them as well as among their branches. It is universally accepted that sectoral targets considered as growth drivers, should be predetermined by a long-term economic plan that simulates their development and reflects the State, private sector and community's views of their current comparative advantages and prospects for future expansion. However, and unsurprisingly, the Lebanese Government has put the cart before the horse; during or after the announcement of its CIP, the government tasked the U.S.-based consultancy firm McKinsey & Co. to develop an economic plan – allegedly a 1000-pages report - to highlight the strengths and weaknesses of the Lebanese economy, explore its specialized and productive sectors, as well as its current and future comparative advantages<sup>15</sup>.

Regardless of what the McKinsey plan will entail - which the yet-unpublished detailed findings, should have been the underlying foundation of the CIP -, so far, the latter appears to replicate the same pattern of investment in the infrastructure networks historically imposed by the prevailing economic model, in particular in what pertains to its regional dimension (allegedly claiming to target a “ capital expenditure balance among regions”), yet realistically is nothing but a scheme to maintain the

<sup>15</sup> It is difficult to label the plan until after its publication, and one should wait for the release of its final findings to assess their compatibility with the CIP visions.

dominant nepotism system enshrined by the political establishment and which instead, instates a balance of interests among incumbent officials and powerbrokers. Hopes were high for example, that the documents of the Paris Conference IV would deeply analyze the structure of foreign trade for Lebanon's marketable agricultural and industrial production (as well as export of services, to identify specific packages, matrices or clusters of products that have comparative advantages in the context of foreign trade movement; this step would have helped to configure the best infrastructure networks able to stimulate and develop these packages, clusters and matrices, and to expand and diversify the agricultural and industrial production with particular emphasis on increasing the export share of products with high added value. Such a development objective should have been given priority, after the contribution of the agricultural and industrial sectors to the existing GDP and the total labor force fell to about half of what it was in the mid-1970s, and the export-import ratio fell to less than 15%, mainly due to the rapid and hasty liberalization of foreign exchange and the distortion of prices resulting from overly delving in monetary stabilization policy since the early 1990s.

In the same context, any economic plan was - and still is- required to approach issues that have a vital impact on the sectoral dimensions of the development process, including: The phenomenon of the boom of the micro-

enterprises in all sectors which represent about 91% of the total number of enterprises operating in Lebanon<sup>16</sup>, and are characterized by weak productivity and irregularity; the implications of the continued discretionary application of the Commercial Representation Act, which protects the largest foreign trade monopolies in a country that still to date lacks an anti-monopoly law; the long-standing legislative uncertainty and the weakness of the business climate, which have consolidate the widespread and deep-rooted government's "favoritism" and the unhealthy relationship between political officeholders and businessmen<sup>17</sup>, and the shielding of oligopolies whereas few firms and sellers control about two-thirds of the country's markets<sup>18</sup>; adding to that, the obstacles facing the transition from the predominance of simple and worn service activities to a new generation of "noble services" extrovert to entrepreneurship, technological development, scientific research and the knowledge economy. Cynically, the Lebanese people are endowed with aptitudes and skills enabling them to deal with most of these issues, yet they have failed to make a dent in a system reined by powerful political and economic forces.

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16 Results of the comprehensive census of buildings and enterprises - Central Statistics Department - 2004 (published in 2006).

17 See the summary of Ishaq Diwan and Jamal Ibrahim Haidar: Market-Friendly Policies, not Companies-Friendly Policies- al-Akhbar newspaper, March 12, 2018.

18 "Consultation and Research Institute" (in collaboration with Dr. Toufic Gaspard): Competition in the Lebanese Economy: A Background for a Competition Law in Lebanon, MoET – UNDP, 2002 (English).



## 4. Potential Impact of the CIP on Fiscal Deficits and Public Debt?

The document of Paris Conference IV asserted the government's commitment to reduce the fiscal deficit as a percentage of GDP to about 1% per annum over five consecutive years. This means that the government will be required to reduce its spending and/or increase its revenues by about \$550 million a year – cumulatively, about \$3 billion in the fifth year - without affecting the current cost of servicing the public debt, which accounts for about half of total revenues. But there is considerable doubt about the extent to which the State can achieve this goal in a country where relative autonomy or natural distance between power and the state is no longer in place, and where the former has absolute control over the latter. Let us recall - in light of the government's commitment to such a financial adjustment - that the country has remained for 12 years without regular public budgets and accountability over previous fiscal accounts. Into the bargain, let us also recall how the public authorities unprofessionally dealt with the salary scale adjustment for public sector employees issue, starting with more than four years of stonewalled discussions clouded by cross-estimation differences in appraising its cost, to the confusion of these authorities over a tax hikes package deemed essential to fund the additional cost of the new salary scale. It is worth noting the ill-assessment of the new public sector salary

scale's effective cost, as once endorsed it has proved to be much higher than previously estimated<sup>19</sup>. In the midst of this widespread chaos, it is legitimate to ask what economic drivers and sectors will a new tax increase hit allowing the government to meet its obligations? And how does the government claim its intention to increase the tax burden in line with the directions of the Paris Conference IV, while in its recent budgets (2018 and 2019) it has granted tax exemptions on the settlement of illegal constructions and other irregularities, enhancing tax evasion and impeding the implementation of the Directorate General of Urban Planning's vision as well as efforts for environmental protection? What public spending will be targeted to reduce public expenditure, when public sector salaries, the servicing of the public debt and the subsidizing of electricity account for more than three-quarters of total public expenditure? How will public capital expenditure increase by 2% of GDP per annum over the first four years of the CIP, mainly financed through loans, without anticipating drastic impact of these loans- though concessionary-, on fiscal deficits and public debt servicing? The CIP avoided to present any actual -rather than formal- simulation of the development of these rates, to the extent that it is

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<sup>19</sup> For example, some public institutions and independent authorities took advantage of the 2017 new salary scale to obtain legal "jurisprudence" that would allow them to benefit from this scale, although they have extensive powers to adjust their employees' wages and they did so when the State abstained from adjusting public employees' wages after 1996. This involved unprecedented wage increases, especially for public servants in the first and second categories (e.g. Ogero and Beirut Port .....), in a country where the public sector suffers from a quasi-concealed bankruptcy.

safe to say that even if the State makes adjustments in its financial policies, the ratio of public debt to GDP will remain very high in international comparisons, noting that these adjustments will not pass without stalemates among the different parties in power, and large-scale social and popular protests<sup>20</sup>. Not only does the citizen suffer from the burden of a high public debt and its service, but he is also suffering from a marked increase in corporate indebtedness (estimated at 110% of existing GDP) as well as household indebtedness, where the majority of Lebanese, individuals and companies, are living on debt as a result of high interest rates and erosion of incomes<sup>21</sup>.

These concerns overshadowing the financial situation are also echoed in the IMF's two preparatory statements<sup>22</sup>, which stress that the public debt in Lebanon cannot continue to be governed by the adopted baseline scenario due to the continued weak economic growth rates, and the negative impact of the global interest rates rise on the country (noting that local interest rates are among the world's highest). This subjects the dynamics of public debt to rapidly deteriorate to reach about 180 percent of GDP by 2023 (under the same baseline scenario), with the likelihood of continuing its upward trend after this period. Despite the seriousness of this

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20 It should be recalled that the 1% increase in the value-added tax rate has required years of wrangled negotiations and high level compromises among ruling parties.

21 Dr. Charbel Nahas, Interview with al-Akhbar newspaper on July 18, 2018.

22 See reference number (6).

warning, some officials and businessmen are betting on considering the Paris Conference IV as a grace period, relying that the expected flow of oil revenues will allow the government to stabilize the budget deficit. But this optimistic outlook, which implicitly underplays the urgency of implementing critical reforms, ignores the fact that pledged foreign loans to finance the CIP will increase the already high public debt of about \$82 billion (March 2018), leaving its ratio to GDP at record levels, even if the government fulfills its commitment to keep the absolute value of the annual deficit. It is worthy to mention that figures on the value of the public debt excluded the BdL's indebtedness, as well as the effects associated with the recent decision by the BdL and the Ministry of Finance to exchange treasury bills in Lebanese pounds against foreign currency bonds; such step would further expose Lebanon to the vagaries of global markets, and weaken its ability to maintain monetary stability.

Owing to the expected repercussions of the worsening financial crisis, fears are also being raised of the pressures that were exerted by foreign countries and international organizations participating in the conference<sup>23</sup> - undisclosed by the Lebanese Government in a transparent and forthright manner – to push the Lebanese Government to comply with the required financial conditions by adopting austerity measures that

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<sup>23</sup> According to media reports over interventions made by the Executive Director of the World Bank, the Deputy Director General of the IMF and officials of the French Foreign Ministry.

might include: Stop hiring in the public sector; increasing VAT rate and fees on fuel consumption; abolition of electricity subsidies; re-engineering of the social welfare benefits granted for public servants and reduce their retirement pensions; adopting a policy that is heavily weighted towards greater control of social spending, and the amendment of what's remains of the Customs Protection system in order to smooth foreign trade. Such measures do not account of subsequent drastic impact on both the societal and political level and do not draw lessons from previous popular demonstrations that have occurred between 2011 and 2015 protesting living conditions. This raises the question of how a country characterized by a high level of concentration of wealth and income, the decline in the share of wages in existing GDP and the predominance of taxes and indirect fees, can adopt the currently promoted austerity policies and tax adjustments, without anticipating their wide scale dire repercussions on the societal and political levels!

### **5- CIP and the Public Private Partnership Law:**

The 2017 Public-Private Partnership Act is central to the overall engineering of the CIP, and correlates with the policy of expanding external borrowing. According to the published literature, this law does not necessarily instate a change in ownership of public utilities, but provides the private sector with opportunities to implement, finance and operate these facilities, and then sell their

services to the state on agreed terms. Afterwards, the state shall distribute these services to consumers in accordance to preset tariffs. As per the documents of the Paris Conference IV, private sector partnership contracts will account for 40% of the total cost of investment in phases I and II, while external loans will account for about 50%; the remaining 10% will be secured by local bonds to finance land expropriation. Some of the proposed contracts go on to award investors extended royalties, including the exploitation of public resources and the collection of direct and indirect fees from users of public services, with the government committed to providing guarantees to foreign lenders, ensuring high investments' gains for domestic and foreign investors. Adding to this, the State will pledge to give foreign lenders priority over other Lebanese State creditors in terms of debt repayment.

This law is presented as a matchless alternative to the “State failure” and poor performance, turning it from a lever to privatize some of the public services into a headlong rush to privatize more through the implementation decrees it may entail. However, promoting privatization of state held assets as the sole solution to the country’s financial crisis and tailspinning economy, discounts the pre-civil war record of success of these assets<sup>24</sup>, that is, before the “Catholic marriage”

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<sup>24</sup> These relative successes have emerged especially during the Shahhabi period, the most prominent of which are the public education and higher education sector, the *Electricité du Liban* Company and the public transport, along with other public facilities and services.

between dominant sectarian leaders and the narrow nucleus “businessmen society”. This marriage has emphasized the power-sharing system that shapes Lebanon’s political landscape, and has contributed to the everlasting postponement of implementing a package of most-needed reforms. It has also influenced the private sector’s practices, as a result of the growing clientelism-based relationships between top political leaders and the nucleus businessmen society, and the benefit-distribution between the two parties. In such circumstances, it is feared that the oligopolistic minority will account for the bulk of the economic benefits that the PPP project may generate, especially in light of the primacy of the private sector (especially large private enterprises concerned with PPP) over the public sector often tagged with inefficiency, in addition to the existent gap between the two sectors in terms of human, managerial, technological and institutional capacities.

The growing perception of the State being overwhelmed by the ruling junta - not to say the complete absence of the State -, threatens to use the PPP project as a tool for easy seizure of public property and assets, while the State continues to be responsible for providing minimum basic goods and public services to citizens such as healthcare, education, social welfare, retirement, poverty alleviation and support for people with special needs (not to mention security and defense services, which alone account for more than half of the total wage bill in

the public sector). While one should beware of the mania for privatization and its unconditional implementation, one should not also fall into the trap of vociferously pro-state discourse pandered by those in power and aiming at exalting the size and role of government, while they daily contribute to dismantling the already spineless “existent state” through prevailing over its institutions, illegal grab and squandering of public funds, random appointments, clientelism and nepotism-based public services provision. It is noteworthy to point out that the World Bank itself recognizes in its literature that PPP contracts may force the State to provide guarantees to protect contractors from previously granted royalties to other investors, by ensuring relatively high returns on their investments; this will enhance existing monopolies and stimulate the emergence of new monopolies, while raising the cost of privatization contracts compared to conventional standard contracts according to which the State is responsible to build the nation’s infrastructure, or compared to public procurement done according to pre-established set of terms and conditions.

Beyond the scope of probabilistic analysis, the “cold” realities within the Lebanese context - governed by a political system that employs sectarianism in the service of power and money sharing among powerful leaders - often reflect the failure of limited privatization experiences achieved over the past two decades in accordance to pre-established governmental plans or by



de facto force due to the deterioration or “disappearance” of the public facility. The indicators of this failure are many: From the collection and management of household waste and bills imposed on the private sector for the distribution of electricity by privately owned power generators, the supply of drinking water and domestic use water and other services; through ambiguous contracts with operators of distribution, collection and maintenance services at *Electricité du Liban* (EdL); to the open and hidden forms of privatizing infrastructure management in Beirut Central District (Solidere), which despite building the finest facilities, have cost the state and the society large amount of funds and emptied the heart of the city of its social fabric. Adding to this, the distorted forms of privatization that have affected large parts of the education and health sectors, fueling growth of private institutions in these sectors at the expense of public establishments<sup>25</sup>. Therefore, any project of partnership between the two sectors - should internal power balances allow its implementation - must be preceded by the development of a broad and transparent implementation system that oversees the public sector reform and the re-building of its administrative and institutional frameworks, so as to restore to the State its basic functions, effectiveness and the relative independence it should enjoy from public authorities and leaders.

<sup>25</sup> Rates of enrollment in public schools and the Lebanese university have declined by more than a third since the mid-1970s, according to statistical data available at the Ministry of Education.

## 6- The Compliance of the CIP with Labor Supply and Demands Mechanisms

Although the CIP includes preliminary estimates of the number of labor days required for the implementation of each of the projects mentioned therein, it cannot be ascertained that they comply with the mechanisms governing the labor market, especially in what pertains to the Lebanese and non-Lebanese workforces, mainly the Syrian one. Needless to say that international and foreign lenders have been paying particular attention to the integration of Syrian refugees into the local labor market, in spite of the Lebanese Government's voiced concerns over the wide and compound consequences of this issue not only in terms of the Syrian refugees competing with nationals over scarce job opportunities, but also in terms of changes that might alter the Lebanese demographic and social fabric. In order to comprehend the expected impact of the CIP on employment, a review of the most important characteristics of the Lebanese labor market is due:

Firstly, this market is witnessing a sharp gap between total supply and demand for labor. The number of newcomers to the labor market (job supply) is annually estimated to be at least 50,000<sup>26</sup>, including about 35,000 tertiary education graduates, while the total annual demand on labor did not exceed 50% or 55%

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<sup>26</sup> School to Work Transition of Youth in Lebanon, CRI - International Labor Organization, 2015.

of the total supply as per the World Bank estimation<sup>27</sup>. Moreover the labor market witnesses imbalances between the structures of both supply and demand. The labor supply is governed by the annual entry of tertiary education graduates into work and the trend governing their specializations -that mostly leans towards law, literature, humanities and social sciences, etc.-, as well as a dual education system that exhibit significant quality disparities, whereas private education is mostly sought by the middle and upper middle income groups, while public education attracts lower middle income and poor social groups. As for the structure of demand for labor by private enterprises, it remains governed by the sectoral structure of the Lebanese economy – whereas trade and services account for about 78% of the actual GDP<sup>28</sup> - and the micro and low-productivity nature of the vast majority of these enterprises. Adding to this, the public sector demand for human resources, characterized by backdoor hiring, improvisation, clientelism and nepotism.

Secondly, the labor market is characterized by high informality accounting for about 40% of the total number of wage earners in the private sector and 80% of self-employed<sup>29</sup>. If we add to these figures the number of Syrian workers in the informal sector, the

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27 The World Bank estimated the total net number of jobs created during the six years 2004-2009 at about 162,000 jobs, equivalent to an average of 27,000 jobs per year.

28 Directorate of Central Statistics, Economic Accounts, 2013.

29 World Bank 2010: Survey of wage earners and employers in Lebanon.

share of informal labor would appear wider than related published studies have revealed. The broadening of informal labor coincides with the on-going profound changes in the sectoral distribution of the workforce where, as noted above, the prevailing contribution of the agriculture and industry to the total labor force as well as to the GDP since 1970, has witnessed a downward trend falling by almost half, amid enduring jobs' obliteration in these two sectors between 2004 and 2009<sup>30</sup>.

Thirdly, although it is difficult to estimate the actual unemployment rate in a volatile country subjected to crises and internal and external migrations<sup>31</sup> - and amid the absence of a residency law-, most of the available partial data indicates that unemployment has reached record levels. The World Bank figures for 2011 indicated a national unemployment rate of 11% with unemployment among youth standing at double this figure. In 2013, the World Bank re-estimated the unemployment rate at about 20%, whilst Lebanese syndicates and international organizations pointed out higher rates due to increasing poverty and a high substitutability between national workforce and cheap Syrian workers, especially in remote areas such as Bekaa and the North.

The documents of the Paris Conference IV released merely preliminary estimates on the potential impact of

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30 Ibid.

31 The latest official statistical studies on unemployment date back to the pre-regional crisis period.

the CIP on job creation<sup>32</sup>, with some senior officials stating that investments of \$1 billion in infrastructure would create 100,000 jobs! It is well known that specialized international literature has come a long way in modeling and “econometrically linking” between the size and type of capital investment and creating jobs (direct and indirect), and showed that the cost of producing one job widely varies depending on countries and sectors of economic activity<sup>33</sup>. Some of this literature suggests that in the case of Tunisia for instance, investing \$10 million in sectors such as trade, construction or the wood industry, would produce 300 direct jobs (about \$33,000 per one job opportunity), while only 100 job opportunities in the electrical and transport industries (i.e. about \$100,000 per one job opportunity). The number of job opportunities can increase and even double if indirect opportunities arising from the multiplier effect of the original investment are added to direct opportunities, noting however that indirect opportunities also require capital investments, which does not change much in the average value of investment to create a single job opportunity in the relevant sector<sup>34</sup>. The literature adds that job creation should not only be linked to its median cost index but also, and most importantly, to the social return this investment will generate.

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32 Projects’ approval, designs, financing procedures and implementation launch, could take two to three years before they are truly “shovel ready” and able to generate job opportunities.

33 DAVID ROBALINO :How much does it cost to create a job? World Bank (Post) February 15, 2018.

34 Ibid.

The Paris Conference IV documents also failed to address the social impacts related to the paid employment terms. In ignoring these impacts, the CIP seemed to implicitly embracing the “inferior view” of salary paid employment in the private sector, emphasizing that this view has, since the 1990s, played a key role in entrenching the migration of skills and competencies and university graduates. This bitter reality has been recently showcased in the results of a statistical study published in 2017, revealing that 2% of the private sector workers<sup>35</sup> have a lump of wages equal to the lump of wages of 59% of the workers in this sector. This reality was also confirmed by the recently released findings of a comprehensive approach<sup>36</sup>, that showed prevalent income inequality and the extent to which income is distributed in an uneven manner among the population. Incomes disparities have become so pronounced that 1% of income earners have 25% of the nation’s income and 40% of its wealth. This explains a whole host of issues including reasons behind the gradual decline in the wage share of existing GDP, and the upward trend in poverty rates, especially after 2011 (even if national poverty figures have not yet been updated<sup>37</sup>).

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35 MoF / UNDP: Assessing Labor Income Inequality in Lebanon’s Private Sector - February 2017.

36 Lydia Assoud: The extreme concentration of income and wealth in Lebanon 2005-2014 – WID. World WORKING PAPER SERIES - 2017/13.

37 Recent statistical studies on poverty at the national level lack, but some recent reports and studies include estimates of poverty rates in Lebanese areas with a high concentration of Syrian refugees.

## 7. On the State's Competency to Uphold the CIP:

The assessment of the State's competency to uphold the CIP is a twofold task which involves, on the one hand, evaluating the eligibility of the government apparatus: Legislative, executive and judicial; and appraising the proficiency of the administrative bodies stakeholders, particularly the Council for Development and Reconstruction (CDR), on the other hand.

The ambition of the CIP collides with the weakness of the political decision-making center within the current ruling class lineup, its lack of professionalism and its historic tendency towards dispersion. The modern history of the Lebanese Legislature - polarized by sectarianism through a narrow circle of leaders who have full control over the political scene – shows the absence of qualified professional pundits and prominent and independent figures among its members. The legislature has failed in fulfilling its legislative duties: It has failed to enact laws, it has failed to enact correlative implementation decrees, and when doing so, it has failed to oversee their enforcement in a transparent way. Notwithstanding that the Lebanese Member of Parliament's earning - including salary, allocations, "retirement" and additional privileges - is among the highest in international standards, especially when weighted against legislative poor performance and inefficiency. Equally, the executive authority has failed to develop and implement

successful and transparent public policies, to provide basic services and manage public utilities, including the organization of relevant public procurements. As for the judiciary considered to be the legitimate son of the ruling elite lineup, its role has remained ineffective - with certain exceptions in a number of cases – on account of its political subordination coupled with concerns to preserve its own gains, while turning a blind eye on major embattled issues vital to its own existence as well as to the Lebanese people, mainly addressing the pervasive corrupt sharing policies reigning the highest offices of state. It is widely established that laws relating to capital public spending in Lebanon have a complex history (that could pour rivers of ink) reflecting all forms of power rivalries and bickering within and between the parliament and the cabinet, which prevented the endorsement of laws for years. These legislative shortcomings underscore the importance to know how the State is going to approve the CIP's listed projects, and to determine the two councils' share of responsibility in this endeavor.

As for the proficiency of the relevant administrative bodies to uphold the CIP, it is noteworthy to point out that the CDR will be the main body entrusted with organizing its relevant procedural and institutional frameworks. Its tasks include proposing projects, supervising their feasibility studies, providing detailed technical advice on contracts and their applications, preparing the tenders



for public procurements, managing and supervising the execution of these procurements, evaluating their results and effects, and following up on compliance with deadlines and respecting loan repayment schedules. It is challenging to solely restrict the implementation of these tasks to the CDR, with most ministries and other public bodies deliberately weaken and left suffering from lack of equipment, manpower and transparent good governance practices. Based on past experience, the involvement of the CDR in managing public investments did not exceed the threshold of \$500 million annually<sup>38</sup>, whereas the CIP will put on its shoulders the management of public investment expenditures amounting to between \$1.5 billion and \$2 billion a year for the first four years, a threefold increase in the annual investment managed by the CDR since the mid-1990s<sup>39</sup>. Subsequently and even if the CDR closely cooperates with relevant ministries, it will encounter potential obstacles and challenges which, unfortunately, the ruling class failed to anticipate in order to take steps to ultimately address them.

## **8 - Political Factors Affecting the Implementation of the Capital Investment Plan after the Parliamentary Elections:**

The long-awaited last parliamentary elections

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38 The CDR has signed contracts valued at approximately \$14 billion between the end of December 1992 and the end of December 2017. During this period, it has actually completed about \$8.3 billion worth of contracts.

39 Official figures published by the CDR on planned investments and actual investments implemented during the period 1993-2016.

concluded one month after the convening of the Paris Conference IV - this coincidence may not be accidental-; it is crucial to assess the impact of the voting outcome on the balance of power among ruling parties, and to what extent it could eventually obstruct or advance the implementation of the CIP, especially in what pertains to the partnership between the public and the private sectors. Actually, the results of the elections reflected a shift in the domestic balance of power, with a relative decline in the positions of pro-international alliance forces, sponsor of Paris Conferences IV and their alike, while their opponents, i.e. the pro-axis of resistance and anti-international alliance forces, made big gains. It is likely that this new political reality - consonant to the outcome of the regional unrest -, will cast its shadow on the official dealing with the Paris Conference IV fallout. Once the CIP completes its processing cycle and leaves the CDR's doors to the cabinet and afterwards to the parliament announcing the onset of its listed projects' implementation phase, the process of endorsing these projects by both the legislative and executive branches within their new lineups is yet not clear, regardless of what is stated in the reports and background documents submitted to the Paris Conference IV. Will these projects be endorsed in chorus? Or tackled by sets according to the funding source or sectors? Or will they be tackled one case at a time? In addition to the problems raised by this issue, other "time bombs" remain, especially in what pertains to the opponent ruling parties reaching a

consensus over the implementation of the partnership agreement; two main obstacles arise: The first is political and can be summed up by the likelihood of a kingmaker party objecting the full privatization policy, owing to its constituency's harsh hostility vis-à-vis transferring public utilities to the private sector, even if this transfer exclude the ownership of these utilities and is only done on the management level. The second is economic involving conflicting interests, and is generated by the long-standing deep disparities between the ruling elite makeup and that of the private sector's influential hawks qualified to win the CIP's bids. To illustrate, a significant dent defect characterizes the relationship among each of the political main parties establishment and the businessmen community involved with the partnership between public and private sectors; in light of their growing political clout, some of the dominant political players might aspire to compensate decades of economic deprivation by securing a greater share of the awarded public procurement contracts relative to privatization for affiliated businessmen.

Should Lebanon edging towards economic "collapse scenario" turn into reality, it is likely to hinder chances for implementing the CIP, without necessarily call it off; however, the dire social consequences of such a scenario might push the ruling class to compulsorily reach consensus and take dreaded measures such as seeking help from international organizations for lack of

alternatives. Nevertheless, although such a consensus is probable, prospects are looming of clashes erupting among the ruling class over abiding to international bodies' political and economic conditions set for Lebanon to benefit from financial aids, including the continuation of the Lebanese Government's partial financing of the investment program. No one can predict the limits of these prerequisite commitments and conditions. They may include painful concessions in the files of Syrian refugees and Palestinian refugees, tackle the State having the sole monopoly over the use of arms, and confront the issue of Lebanon position vis-à-vis rivalry for regional hegemony, not to mention the imposition of strict austerity policies on the Lebanese for years to come. It should not be ruled out that the disparity among the ruling class over these prerequisite conditions might trigger social and political instability, as was seen in countries with similar challenges.

### **The Seeking Solutions Approach: Addressing all Problems at once or on Case-by-Case Basis? The Electricity File as Striking Example**

It is time to acknowledge that in the absence of structural reforms, the assorted conferences phenomena has failed to reduce the country's vulnerability, its increased dependence on foreign countries, its public debt growth and political squabbles and social inequality. It is also time to acknowledge that the policy of foreign and

domestic borrowings adopted since the 1990s was not only triggered by the weakness or inability of successive governments to address problems or their quest to delay catastrophic crises, but also - and essentially – by the greediness of a powerful nucleus political, business and financial community and its eagerness for making easy money<sup>40</sup> and amassing fortunes, due to a pattern of deficit and public debt management and the prevalence of the financial bulge phenomenon over the economy as a whole. The magnitude of this community's declared and hidden private interests hindered any serious structural reform of the existing political and economic systems. This nucleus community has been playing and continues to play a prominent role in determining public policies and bears a great deal of responsibility for the deteriorating economic situation in the country. Owing to its tightened grip on the country's decision making, one should not underestimate its ability to deviate the CIP's sought course of action to become a stream for self-wealth, regardless of the country's political and economic prospects.

While seeking suitable social and economic solutions, it is vain to sink into long way-out recipes, as is often the case in the successive cabinets' policy statements and the official wooden discourse, as well as in many studies by international organizations and local research

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<sup>40</sup> Dr. Ghassan Diibeh goes as far as describing the accumulation of public debt as "the result of the theft of public money and corruption", the Capital Supplement, al-Akhbar March 12, 2018.

centers. Rather, the search for solutions should start with a deep review of the economic and financial conditions that would allow the development of creative options – though it could be seen by some as an impossible task-paving the way for the State to rise again and restore its basic functions, as did most of the countries that preceded us in embarking on the road to development. The utmost criterion for achieving this revival is to develop a new taxation system based on accurate census data<sup>41</sup>, targeting wealth components, earnings and profits of big fat taxpayers<sup>42</sup> (contingent to the census' outcomes), so as to provide the State with income that allows it, even gradually, to fund the reconstruction of infrastructure. Needless to say that this taxation system will be inefficient if not correlated with structural reforms targeting the public administration and the public spending and its institutional and administrative frameworks, in order to activate and improve civil services and stop dubbing the state as a “failed dealer” and capitalizing on its failure to provide basic services as stalking horse to swoop public properties and assets. Such a policy is precisely what promotes growth and creates opportunities to motivate and reorient the private sector towards modernizing and developing high value added entrepreneurial activities in fields such as the knowledge economy, the digital

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41 The last and latest census dates back to 1932!

42 Among the proposals is the adoption of a progressive tax system which apply increased tax rate up to 20% or 30% on financial institutions' profits, including banks, real estate companies, major importers and big taxpayers, along with increasing VAT rate on luxury consumer goods.

economy, the economy of biodiversity, food technology, clean energy, high competitive healthcare, education and tourism services, instead of continuing to drown in the production of non-tradable goods and services; of similar importance is pushing to adopt a policy of import substitution industrialization, which advocates replacing foreign imports with domestic production through fostering “smart industries” that meet the need of local markets as well as export markets.

The identification of such options has ushered in a wide ranging debate about the usefulness of continued dependence on foreign loans if the Lebanese private sector is to fund more than one third of the projects. In that case, the requested guarantees for local funding - which the State is currently unable to secure - can be provided by involving donors mainly in resolving this particular issue rather than financing the majority of the CIP. The debate raises also questions about the government’s blatant handling of the electricity crisis, which has been for decade tainted by over-the-counter high-level bickering and sharing’s quarrels, and wasted years despite the readiness of the file to be implemented, at a time when the cost of this crisis accounted for annually about one third of the budget deficit, 40% of the total value of public debt. Lebanon could have avoided foreign borrowing if, in due course, it had provided the required solutions for that particular crisis. What has prevented successive governments from conceiving solutions to

the power crisis through responsible and enforceable decisions, covering transitional management, reforming and developing this sector, constructing power plants, adjusting the electricity consumption tariffs, and reducing subsidies to this sector down to its abolition, saving the state annually between one billion and one billion and a half dollars? Should such decision have been made at the time, the accumulated value of the savings would have exceeded the total of concessional lending commitments Lebanon has received at the Paris Conference IV - depending on the trends of electricity consumption tariffs, oil prices and global interest rates. What applies to this example is also true, and in other proportions and forms, to many files concerning vital and urgent public projects that have been repeatedly postponed several times.

This type of initiative is what the Lebanese people aspire to embody in order to embark on the path of State rebuilding as a development and non-sectarian State, a State that is free from the high level sharing of power and wealth, and from networks of interests, privileges and clientelism.