LEBANON ECONOMIC MONITOR

The Normalization of Crisis Is No Road for Stabilization

Spring 2023

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Lebanon Economic Monitor

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Spring 2023

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ACRONYMS

AA	EU-Lebanon Association Agreement
ABL	Association of Banks in Lebanon
AER	Average Exchange Rate
BdL	Banque du Liban
BNR	Banknote Rate
BTA	Beirut Traders Association
BoP	Balance of Payments
CA	Current Account
CAS	Central Administration of Statistics
CPI	Consumer Price Index
EU	European Union
ERPT	Exchange Rate Pass Through
EdL	Electricité du Liban
FEVD	Forecast Error Variance Decomposition
FX	Foreign Exchange
GDP	Gross Domestic Product
GNI	Gross National Income (per capita)
IMF	International Monetary Fund
LBP	Lebanese Pound
LEM	Lebanon Economic Monitor
MIDAS	Mixed-Data Sampling
MoF	Ministry of Finance
NPL(s)	Non-performing Loan(s)
PMI	Purchasing Manager's Index
Pp	Percentage Points
SLA	Staff-Level Agreement
TB(s)	Treasury Bond(s)
UN	United Nations
US$	United States Dollar
VAT	Value Added Tax
XM-2022	First X months of the year
yoy	Year over Year

PREFACE

The *Lebanon Economic Monitor* provides an update on key economic developments and policies over the past six months. It also presents findings from recent World Bank work on Lebanon. The *Monitor* places these developments, policies, and findings in a longer-term and global context and assesses their implications on the outlook for Lebanon. Its coverage ranges from the macro-economy to financial markets to indicators of human welfare and development. It is intended for a wide audience, including policy makers, business leaders, financial market participants, and the community of analysts and professionals engaged in Lebanon.

The *Lebanon Economic Monitor* is a product of the World Bank's Lebanon Macroeconomics, Trade and Investment (MTI) team. It was written by Dima Krayem (Senior Economist), Naji Abou Hamde (Economic Analyst) and Ibrahim Jamali (Consultant), with contributions from Lars Jessen (Lead Debt Specialist), Nadine Chehade (Senior Financial Sector Specialist) and Peter Salisbury (Consultant). The Special Focus entitled *Gauging the Size of the Cash Economy* was prepared by Dima Krayem (Senior Economist), Ibrahim Jamali (Consultant), and Naji Abou Hamde (Economic Analyst). The *Lebanon Economic Monitor* has been completed under the guidance of Eric Le Borgne (Practice Manager), Norbert Fiess (Lead Economist), and Jean Christophe Carret (Country Director). Zeina Khalil (Communications Officer) is the lead on communications, outreach, and publishing.

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EXECUTIVE SUMMARY

Recent Economic Developments

Lebanon's long economic contraction continued in 2022, albeit at a slower pace than in previous years. The deceleration in economic contraction in 2022 is largely owed to a base effect (referred to as a technical deceleration in economic contraction). Following a cumulative four-year contraction of 37.2 percent of GDP (2018–2021), real GDP is estimated to have declined by 2.6 percent in 2022. The BLOM-PMI index, which captures private sector activity, slightly improved to 48.4 in 2022, up from an average of 46 percent in 2021 but nonetheless still representing a contraction of activity (<50). A positive development is the growth in tourist arrivals (by 57 percent, 8M-2022). Nonetheless, the widening current account deficit (see below), a long structural imbalance, continue to weigh down on growth prospects.

The overall fiscal balance is estimated to have recorded a narrow surplus of 0.3 percent of GDP in 2022, down from 1 percent of GDP 2021. Revenues are estimated to have declined from an already low 13.1 percent of GDP in 2020 to 6.0 percent of GDP in 2022, one of the lowest rates globally. This was more than offset by a larger decrease in total expenditures, which declined from 16.4 percent of GDP in 2020 to a record low of 5.7 percent of GDP in 2022, pointing to a massive hollowing out of the state amid an unprecedented crisis.[1]

Testament to the lack of economic stabilization, the Lebanese Pound (LBP) continues to depreciate sharply. By February 2023, the currency lost more than 98 percent of its pre-crisis value. Despite the central bank (BdL)'s foreign exchange (FX) interventions to attempt to stabilize the BNR (i.e., the banknote rate/parallel market) using its gross reserves starting in December 2021, the BNR averaged 31,102 LBP/US$ in 2022. The depreciation of the BNR has accelerated since the beginning of 2023, breaching 140,000 LBP/US$ amid rising tensions, bank strikes, and relatively fewer FX interventions by BdL. A multiple exchange rate system persists, reflecting a variety of exchange rates to buy and sell currency, set import and other tariffs, and record internal accounts, creating economic

[1] World Bank fiscal estimates are based on the latest official Ministry of Finance statistics, and therefore do not include extra budgetary spending, including quasi-fiscal operations conducted by the Central Bank, arrears, usage of IMF SDR allocation for certain fiscal spending, among other expenditures not recorded in official statistics-the fiscal balance is likely to be significantly negative when taking the above-mentioned expenditures into account.

distortions, inaccurate accounts, and providing rent-seeking opportunities.

Inflation averaged 171.2 percent in 2022, one of the highest rates globally, primarily due to the depreciation of the LBP. Higher prices for food and non-alcoholic beverages contributed the most to inflation in 2022. Food inflation increased on average by 240 percent throughout 2022, reaching a maximum of 483 percent (yoy) in January 2022.

The current account deficit grew to 20.6 percent of GDP on the back of higher imports and falling exports. Imports reached pre-crisis levels in 2022, at a record US$19 billion. Exports declined by 10.2 percent. Customs data for merchandise goods indicates that imports grew by 39.7 percent year-on-year in 2022. Anticipated increases in the customs duties exchange rate ("the customs dollar"), which increased to 15,000 LBP/US$ at the end of 2022, likely contributed to the substantive increase in imports of industrial goods (a year-on-year increase of 45.8 percent) as businesses and consumers hoard goods in anticipation of a price adjustment.

The banking sector remains insolvent, as financial losses in the banking system exceed US$72 billion, equivalent to more than three times GDP in 2022.[2] Divergent views among key stakeholders on how to distribute the financial losses remains the main bottleneck for reaching an agreement on an equitable banking resolution. Delays in the day of reckoning with the magnitude and viable distribution of financial losses is only compounding human and social capital losses.

The current account deficit continues to be financed, for the most part, by BdL usable gross foreign reserves. BdL gross FX reserves declined by US$2.6 billion in 2022 reaching US$15.2 billion (including close to US$5 billion in foreign securities) by end 2022.

The Sayrafa exchange platform, BdL's primary monetary tool for stabilizing the LBP, is not only an unfavorable monetary tool, but has also morphed into a mechanism to generate arbitrage profits. The Sayrafa platform is in many ways a case study in the kind of weak, and often counterproductive, policies implemented by the Lebanese authorities since the outbreak of the crisis. Trading volumes on the platform are only weakly correlated with improvements in the BNR/parallel market exchange rate. BdL, facing hard currency supply constraints, has mostly relied on dwindling gross foreign exchange reserves to supply dollars through the platform to temporarily prop up the currency. More recently, BdL has taken to using printed local currency to buy US dollars on the parallel market before interventions on the Sayrafa platform, sharpening exchange rate volatility. Whether at the expense of burning through remaining reserves, or further depreciating the currency, such monetary tools have proven ineffective and highly costly. Finally, initial analysis suggests that buy-side Sayrafa platform participants may have profited by as much as $2.5 billion through arbitrage trades between the discounted rate offered on the platform and the BNR since the platform's initiation.

Outlook

Subject to high uncertainty, real GDP is projected to contract by 0.5 percent in 2023. The less severe contraction in real GDP in 2023 relative to 2022 is predicated on a continued, albeit modest, pick up in private consumption and a narrowing of the current account. Lack of political will to implement adequate and equitable reforms is expected to persist throughout 2023, markedly dampening the economic forecast for that year. A complete depletion of FX reserves at BdL in 2023 is not expected, but the continued erosion of reserves remains a matter of deep concern.

Inflation is expected to remain among the highest globally, at a projected 165 percent. Narrow money, inflation, and currency depreciation will continue to shape unstable macroeconomic dynamics in the absence of a new exchange rate and monetary framework.

The current account deficit-to-GDP ratio is projected to slightly narrow in 2023 but remains on an unsustainable path. The current account

[2] Please refer to: World Bank (2022), Lebanon Economic Monitor, Fall 2022: Time for an Equitable Banking Resolution. (Link).

deficit is expected to narrow to 14 percent of GDP in 2023, driven by a decrease in imports and consequent decrease in the trade-in-goods balance relative to 2022.

Against this backdrop, the normalization of the state of crisis obscures the fact that the Lebanese economy remains in precipitous decline, markedly distant from a stabilization path-let alone a recovery path. The longer the delay without a comprehensive, adequate, and equitable recovery plan, the bleaker the available policy options become as resources vital to that recovery are eroded. A deceleration in the contraction of economic activity does not imply a stabilization. In fact, a largely insolvent banking sector and a national currency that has all but lost its main functions have induced a pervasive dollarized cash economy equivalent to almost half of GDP in 2022, and further hindering prospects of economic recovery. For as long as the economy is contracting and crisis conditions persist, living standards are set for further erosion, poverty will continue to spiral, and an overall precarious environment will prevail. In short: the status quo ensures that capital of all kinds is depleted, giving way to profound social inequality with only a few (relative) winners and a large majority of losers.

Special Focus: Gauging the Size of the Cash Economy

The systemic failure of Lebanon's banking system and the collapse of the currency have resulted in a large, dollarized cash-based economy, worth an estimated US$9.86 billion or 45.7 percent of GDP in 2022 (Special Focus: Gauging the Size of the Cash Economy in Lebanon). A pervasive and growing dollarized cash economy is a major impediment to Lebanon's economic recovery. It not only threatens to compromise the effectiveness of fiscal and monetary policy, but also heightens the risk of money laundering, increases informality, and prompts further tax evasion. Moreover, the increasing reliance on cash transactions also threatens to completely reverse the progress that Lebanon made pre-crisis towards enhancing its financial integrity by instituting robust anti-money laundering mechanisms in its commercial banking sector.

ملخص تنفيذي

أحدث التطورات الاقتصادية

واصل الاقتصاد اللبناني انكماشه في عام 2022، وإن كان بوتيرة أبطأ مما كانت عليه في السنوات السابقة. ويعود التباطؤ في الانكماش الاقتصادي في عام 2022 إلى حد كبير إلى الأثر الأساسي (يشار إليه بتباطؤ تقني في الانكماش الاقتصادي). ففي أعقاب انكماش تراكمي بلغ 37.2% من إجمالي الناتج المحلي على مدى أربع سنوات (2018–2021)، تشير التقديرات إلى تراجع إجمالي الناتج المحلي الحقيقي بنسبة 2.6% في عام 2022. وسجّل مؤشر مديري المشتريات في بلوم، الذي يرصد نشاط القطاع الخاص، تحسناً طفيفاً إلى 48.4% عام 2022، مرتفعاً من متوسط قدره 46% في عام 2021، لكنه لا يزال يمثل انكماشاً في النشاط (<50). ومن التطورات الإيجابية نمو أعداد السائحين الوافدين (بنسبة 57%، خلال أول 8 أشهر في 2022). مع ذلك، لا يزال العجز المتزايد في الحساب الجاري (انظر أدناه)، والذي يشكل خللاً بنيوياً طويلاً، يؤثر على آفاق النمو.

وتشير التقديرات إلى أن ميزان المالية العامة سجل فائضاً طفيفاً قدره 0.3% من إجمالي الناتج المحلي عام 2022، مقابل 1% من إجمالي الناتج المحلي في عام 2021. كما تشير التقديرات إلى انخفاض الإيرادات من 13.1% من إجمالي الناتج المحلي وهو مستوى منخفض أصلاً، إلى 6 % في عام 2022، وهي من أدنى المعدلات على المستوى العالمي. وقد عوّض عن ذلك انخفاض أكبر في إجمالي النفقات، الذي تراجع من 16.4% في المئة من إجمالي الناتج المحلي في 2020 إلى مستوى قياسي منخفض قدره 5.7% من إجمالي الناتج المحلي في 2022، مما يشير إلى تفريغ هائل للدولة في خضم أزمة غير مسبوقة[3].

ويشكل التدهور الشديد في الليرة اللبنانية دليلاً على غياب الاستقرار الاقتصادي. فبحلول شهر فبراير/شباط 2023، فقدت العملة أكثر من 98% من قيمتها قبل الأزمة. وعلى الرغم من الإجراءات التدخلية في النقد الأجنبي التي يقوم بها البنك المركزي منذ ديسمبر/كانون الأول 2021 في محاولة لتحقيق استقرار سعر صرف العملة الورقية (السوق الموازية) باستخدام إجمالي احتياطياته، فقد بلغ متوسط سعر صرف العملة في السوق الموازية 31102 ليرة/دولار في عام 2022. وتسارعت وتيرة انخفاض قيمة العملة منذ بداية عام 2023، حيث تجاوزت 140 ألف ليرة/دولار وسط تصاعد التوترات، وإضرابات البنوك، وتراجع التدخلات في النقد الأجنبي نسبياً من جانب مصرف لبنان. ولا يزال نظام تعدد أسعار الصرف سائداً، وهو يشمل مجموعة من أسعار الصرف لشراء وبيع العملة، وتحديد رسوم الاستيراد والرسوم الأخرى، وتسجيل الحسابات الداخلية، مما خلق تشوهات اقتصادية، وعدم دقة في الحسابات، وأتاح فرص ريعية.

وبلغ متوسط التضخم 171.2% في عام 2022، وهو أحد أعلى المعدلات على المستوى العالمي، ويرجع ذلك في المقام الأول إلى انخفاض قيمة الليرة. وكان ارتفاع أسعار المواد الغذائية والمشروبات غير الكحولية هو الأكثر مساهمة في التضخم في عام 2022. وزاد معدل التضخم في أسعار الغذاء في المتوسط بنسبة 240% طوال عام 2022، مسجلا 483% كحد أقصى (على أساس سنوي) في يناير/كانون الثاني 2022.

وزاد عجز الحساب الجاري إلى 20.6% من إجمالي الناتج المحلي نتيجة لارتفاع الواردات وتراجع الصادرات. وبلغت الواردات في عام 2022 مستويات ما قبل الأزمة، مسجلة رقماً قياسياً قدره 19 مليار دولار. وانخفضت الصادرات بنسبة 10.2%. وتشير بيانات الجمارك عن البضائع إلى أن الواردات نمت بنسبة 39.7% على أساس سنوي في عام 2022. ومن المرجح أن الزيادات المتوقعة في سعر الصرف الخاص بالرسوم الجمركية (الدولار الجمركي)، الذي زاد إلى 15 ألف ليرة/دولار في نهاية عام 2022،

[3] تستند تقديرات البنك الدولي المالية إلى أحدث الإحصاءات الرسمية الصادرة عن وزارة المالية، وبالتالي فهي لا تشمل الإنفاق خارج الميزانية، بما في ذلك العمليات شبه المالية التي يقوم بها البنك المركزي، والمتأخرات، واستخدام مخصصات صندوق النقد الدولي لحقوق السحب الخاصة لبعض الإنفاق، من بين نفقات أخرى غير مسجلة في الإحصاءات الرسمية - من المرجح أن يكون الرصيد المالي سلبي بشكل ملحوظ عند أخذ النفقات المذكورة أعلاه في الاعتبار.

ساهمت على الأرجح في الزيادة الجوهرية في واردات السلع الصناعية (بزيادة سنوية قدرها 45.8%)، حيث قامت المؤسسات والمستهلكون باكتناز السلع تحسباً لتعديل الأسعار.

ولا يزال القطاع المصرفي متعثراً، حيث تتجاوز الخسائر المالية في النظام المصرفي 72 مليار دولار، أي ما يزيد عن ثلاثة أضعاف إجمالي الناتج المحلي في عام 2022.[4] ولا تزال الآراء المتباينة بين الجهات المعنية الرئيسية بشأن كيفية توزيع الخسائر المالية تشكل العقبة الأساسية أمام التوصل إلى اتفاق بشأن تسوية منصفة لإعادة هيكلة القطاع المصرفي. ويؤدي التأخير في الإعتراف بحجم الخسائر والاتفاق على آلية توزيعها بشكل عادل إلى تفاقم الخسائر على مستوى رأس المال البشري والاجتماعي.

ولا يزال عجز الحساب الجاري يُموّل، في معظمه، مما تبقى من إجمالي احتياطي النقد الأجنبي القابل للاستخدام لدى مصرف لبنان. وانخفض إجمالي احتياطي النقد الأجنبي لدى مصرف لبنان بمقدار 2.6 مليار دولار في عام 2022 ليصل إلى 15.2 مليار دولار في نهاية العام 2022 (بما في ذلك حوالي 5 مليار دولار من الأوراق المالية الأجنبية).

إن منصة صيرفة للصرف الأجنبي- وهي الأداة النقدية الرئيسية التي يستخدمها مصرف لبنان لتحقيق استقرار سعر صرف الليرة- ليست أداة نقدية غير مؤاتية فحسب، بل تحولت أيضاً إلى آلية لتحقيق أرباح من عمليات المراجحة. وتشكّل منصة صيرفة، من نواحٍ عديدة، نموذجاً للسياسات الضعيفة وغير المجدية غالباً، التي تعتمدها السلطات اللبنانية منذ اندلاع الأزمة. ترتبط أحجام التداول على المنصة ارتباطاً ضعيفاً بالتحسنات في سعر الصرف في السوق الموازية. ويعتمد المصرف المركزي، الذي يواجه قيوداً على المعروض من العملات الصعبة، في الغالب، على إجمالي احتياطي النقد الأجنبي المتضائل لتأمين الدولارات من خلال المنصة لدعم العملة مؤقتاً. وفي الآونة الأخيرة، لجأ مصرف لبنان إلى استخدام العملة المحلية المطبوعة لشراء الدولار الأمريكي في السوق الموازية قبل التدخل على منصة صيرفة، مما أدى إلى زيادة تقلب أسعار الصرف. وقد ثبت أن هذه الأدوات النقدية غير فعالة ومكلفة للغاية، سواء على حساب الاحتياطي المتبقي، أو لما تؤدي إليه من زيادة في تدهور قيمة العملة. وأخيراً، يشير التحليل الأولي إلى أن المشاركين في منصة صيرفة من جانب الشراء ربما حققوا أرباحاً تصل إلى 2.5 مليار دولار من خلال عمليات المراجحة بين السعر المخصوم المعروض على المنصة وسعر العملة في السوق الموازية.

الآفاق المستقبلية

مع الأخذ بعين الإعتبار انعدام اليقين بدرجة عالية، يتوقع أن ينكمش إجمالي الناتج المحلي الحقيقي بنسبة 0.5% عام 2023. ويستند الانكماش الأقل حدة في إجمالي الناتج المحلي الحقيقي في عام 2023 مقارنة بعام 2022 إلى استمرار الانتعاش في الاستهلاك الخاص، وإن كان متواضعاً، وتقييد الحساب الجاري. ومن المتوقع أن يستمر غياب الإرادة السياسية لتنفيذ إصلاحات مؤاتية وعادلة طوال عام 2023، مما يضعف بشكل ملحوظ التوقعات الاقتصادية لتلك السنة. ومن غير المتوقع استنفاد كامل احتياطي النقد الأجنبي في مصرف لبنان في عام 2023، غير أن استمرار تآكل الاحتياطي لا يزال يشكل مصدر قلق بالغ.

ومن المتوقع أن يظل معدل التضخم من بين أعلى المعدلات على مستوى العالم، إذ يتوقع أن يبلغ 165%. كما سيستمر تقييد حجم الأموال ومعدلات التضخم وانخفاض قيمة العملة في تشكيل ديناميكيات الاقتصاد الكلي غير المستقرة مع غياب سعر صرف وإطار نقدي جديدين.

ومن المتوقع أن تتقلص نسبة عجز الحساب الجاري إلى إجمالي الناتج المحلي قليلاً في عام 2023، لكنها لا تزال على مسار غير مستدام. فمن المتوقع أن يتقلص عجز الحساب الجاري إلى 14% من إجمالي الناتج المحلي في عام 2023، مدفوعاً بانخفاض الواردات وما يترتب عليه من انخفاض في رصيد التجارة في السلع مقارنة بسنة 2022.

وفي ظل هذه الخلفية، يحجب التطبيع مع الأزمة حقيقة أن الاقتصاد اللبناني لا يزال يشهد تراجعاً حاداً، بعيداً بشكل ملحوظ عن مسار تحقيق الاستقرار – ناهيك عن مسار التعافي. وكلما طال التأخير في اعتماد خطة شاملة ومناسبة ومنصفة للتعافي، ازدادت قتامة الخيارات المتاحة على صعيد السياسات مع تآكل الموارد الحيوية لتحقيق ذلك التعافي. ولا يعني تباطؤ وتيرة الانكماش في النشاط الاقتصادي أن الاستقرار بدأ يتحقق. في الواقع، أدى القطاع المصرفي المتعثر إلى حد كبير والعملة الوطنية التي فقدت الكثير من وظائفها الرئيسية، إلى نشوء اقتصاد نقدي مدولر يعادل نحو نصف إجمالي الناتج المحلي في عام 2022، مما زاد من إعاقة آفاق التعافي الاقتصادي. وما دام الاقتصاد آخذاً في الانكماش وأوضاع الأزمة قائمة، فإن مستويات المعيشة ستشهد مزيداً من التآكل، وسيستمر الفقر في الانتشار، وستسود بيئة عامة محفوفة بالمخاطر. باختصار: يؤدي الوضع الراهن إلى استنفاد رأس المال بجميع أوجهه، مما يفسح المجال أمام تعميق عدم المساواة الاجتماعية، حيث هنالك عدد قليل فقط من الفائزين (نسبياً) وغالبية كبيرة من الخاسرين.

قسم خاص: قياس حجم الاقتصاد النقدي

أدى فشل النظام المصرفي في لبنان وانهيار العملة إلى اقتصاد نقدي كبير مدولر يقدّر حجمه بنحو 9.86 مليار دولار أو 45.7% من إجمالي الناتج المحلي في عام 2022 (قسم خاص: قياس حجم الاقتصاد النقدي)**.** ويمثل الاقتصاد النقدي المنتشر والمتزايد بالدولار عائقاً رئيسياً أمام التعافي الاقتصادي في لبنان، فهو لا يهدّد بالمساس بفعالية السياسة المالية والنقدية فحسب، بل يزيد أيضاً من مخاطر غسل الأموال، ويزيد من النشاط الاقتصادي غير الرسمي، ويحفّز على المزيد من التهرب الضريبي. علاوة على ذلك، يهدد الاعتماد المتزايد على المعاملات النقدية أيضاً بعكس مسار التقدم الذي حققه لبنان قبل الأزمة نحو تعزيز سلامته المالية من خلال إنشاء آليات متينة لمكافحة غسل الأموال في القطاع المصرفي.

[4] يرجى الرجوع إلى: البنك الدولي (2022) المرصد الاقتصادي للبنان، عدد خريف 2022: حان الوقت للتسوية المصرفية المنصفة. (رابط)

RÉSUMÉ ANALYTIQUE

Évolution récente de l'économie

L'économie libanaise a continué de se contracter en 2022, bien que moins rapidement que les années précédentes. Ce ralentissement du rythme de contraction économique observé en 2022 est essentiellement dû à un effet de base (qualifié de ralentissement technique de la contraction économique). Après une contraction du PIB de 37,2 % cumulée sur une période de quatre ans (20182021), le PIB réel aurait, selon les estimations, diminué de 2,6 % en 2022. Établi par la banque BLOMINVEST pour le Liban, l'indice des directeurs des achats, qui évalue l'activité du secteur privé, s'est légèrement amélioré pour atteindre 48,4 en 2022 contre 46 en moyenne en 2021, mais indique néanmoins une contraction de l'activité (<50). L'augmentation du nombre de touristes entrant dans le pays (qui a augmenté de 57 % durant les 8 premiers mois de l'année 2022) est une évolution positive. L'accroissement du déficit du compte courant (voir ci-après) et l'existence d'un déséquilibre structurel persistant continuent néanmoins d'assombrir les perspectives de croissance.

Le solde budgétaire global devrait, selon les estimations, être faiblement excédentaire (0,3 % du PIB en 2022, contre 1 % du PIB en 2021). Toujours selon les estimations, les recettes seraient tombées par rapport au niveau déjà peu élevé de 13,1 % du PIB en 2020 à 6,0 % du PIB en 2022, soit l'un des taux les plus faibles observés à l'échelle mondiale. Cette évolution a été plus que contrebalancée par une baisse plus importante du volume total des dépenses, qui a été ramené de 16,4 % du PIB en 2020 à leur niveau le plus faible jamais enregistré de 5,7 % du PIB en 2022. Fait plus révélateur, les dépenses totales ont chuté de 17,6 milliards de dollars en 2018 (avant la crise) à 1,2 milliard de dollars en 2022, ce qui témoigne d'un rétrécissement considérable de l'action publique dans le contexte d'une crise sans précédent.[5]

La livre libanaise continue de se déprécier fortement par suite de l'absence de stabilisation économique. En février 2023, la monnaie avait perdu plus de 98 % de sa valeur d'avant la crise.

[5] Les estimations budgétaires de la Banque mondiale sont basées sur les dernières statistiques officielles du ministère des Finances et n'incluent donc pas les dépenses extrabudgétaires, y compris les opérations quasi budgétaires menées par la Banque centrale, les arriérés, l'utilisation de l'allocation de DTS du FMI pour certaines dépenses budgétaires, ces dépenses n'étant pas enregistrées dans les statistiques officielles. Le solde budgétaire est susceptible d'être considérablement négatif si l'on prend en compte ces dépenses susmentionnées.

Malgré les interventions menées par la banque centrale (Banque du Liban) sur le marché des changes depuis décembre 2021 dans le but de stabiliser le cours du billet de banque en dollars (c'est-à-dire le cours du billet par rapport au cours du marché parallèle) au moyen de ses réserves brutes, ce cours s'est établi en moyenne à 31 102 livres libanaises pour un dollar en 2022. Il se dégrade depuis le début de 2023 puisqu'il a dépassé 140 000 livres libanaises pour un dollar dans un contexte caractérisé par la montée des tensions, des grèves bancaires et une diminution relative du nombre d'interventions de la Banque du Liban sur le marché des changes. Le pays continue d'avoir un régime de taux de change multiples qui donne lieu à l'application de toute une série de taux de change différents pour l'achat et la vente de devises, la fixation des droits d'importation et d'autres tarifs et la tenue des comptes internes ; ce système se solde par l'apparition de distorsions économiques, la présentation de comptes inexacts et la création de possibilités de recherche de rente.

Le taux d'inflation a atteint, en moyenne, 171,2 % en 2022, et a été l'un des plus élevés enregistrés dans le monde, essentiellement par suite de la dépréciation de la livre libanaise. L'inflation a principalement été alimentée par la hausse des prix des aliments et des boissons non alcoolisées en 2022. L'inflation des denrées alimentaires a augmenté de 240 % en moyenne en 2022 pour culminer à 483 % par rapport à l'année précédente en janvier 2022.

Le déficit du compte courant a augmenté pour atteindre 20,6 % du PIB par suite de l'accroissement des importations et de la chute des exportations. Les importations ont retrouvé le niveau qu'elles avaient avant la crise pour atteindre la valeur record de 19 milliards de dollars en 2022. Les exportations ont diminué de 10,2 %. Selon les statistiques douanières, les importations de marchandises ont augmenté de 39,7 % en 2022 par rapport à l'année précédente. Le relèvement prévu des droits de douane et la hausse du taux de change appliqué à ces derniers, qui était de 15 000 livres libanaises pour un dollar à la fin de 2022 ont, selon toute vraisemblance, contribué à la forte augmentation des importations de produits industriels (45,8 % par rapport à l'année précédente), les entreprises et les consommateurs constituant des réserves en prévision d'un ajustement des prix.

Le secteur bancaire demeure insolvable, les pertes financières du système bancaire dépassant 72 milliards de dollars, soit l'équivalent de plus du triple du PIB en 2022.[6] Les divergences de vues des principales parties prenantes sur la manière de répartir les pertes financières restent le principal obstacle à la conclusion d'un accord sur une résolution équitable de la crise bancaire. Repousser le moment de faire face à l'ampleur des pertes financières et de procéder à une répartition viable de ces dernières ne fait qu'aggraver les pertes de capital humain et de capital social.

Le déficit du compte courant continue d'être financé, pour l'essentiel, par les réserves brutes de change de la Banque du Liban. Les réserves brutes de change de la Banque du Liban ont chuté de 2,6 milliards de dollars en 2022 pour s'établir à 15,2 milliards de dollars a la fin de l'année 2022 (dont près de 5 milliards de dollars sous forme de titres étrangers).

La plateforme de change Sayrafa, principal instrument monétaire utilisé par la Banque du Liban pour stabiliser la livre libanaise, sert non seulement, à mauvais escient, d'instrument monétaire, mais aussi, à présent, de mécanisme permettant de tirer profit d'opérations d'arbitrage. La plateforme Sayrafa témoigne, à de multiples égards, des politiques faibles et souvent contreproductives, mise en œuvre par les autorités libanaises depuis que la crise a éclaté. Il n'existe qu'une corrélation ténue entre les volumes négociés sur la plateforme et l'amélioration du cours du billet de banque en dollars par rapport au taux du marché parallèle. La Banque du Liban, dont les réserves en devises sont limitées, a eu principalement recours à ses réserves brutes de change, de plus en plus réduites, pour procurer des dollars sur la plateforme de manière à temporairement soutenir la livre libanaise. Elle a récemment entrepris d'utiliser des billets en livres libanaises pour acheter

6 Voir Banque mondiale (2022), Liban, Bulletin de conjoncture, automne 2022 : L'urgence d'une résolution bancaire équitable. (Lien).

des dollars sur le marché parallèle avant de procéder à des interventions sur la plateforme Sayrafa, ce qui n'a fait qu'accroître la volatilité du taux de change. Ces instruments monétaires, dont l'emploi a pour effet d'absorber les réserves restantes ou de déprécier encore plus la monnaie, se sont révélés inefficaces et extrêmement coûteux. Il semble, en première analyse, que les acheteurs sur la plateforme Sayrafa pourraient avoir dégagé des bénéfices à hauteur de 2,5 milliards de dollars en procédant à des opérations d'arbitrage entre le taux réduit proposé sur la plateforme et le cours des billets de banque en dollars, et ce depuis le lancement de la plateforme.

Perspectives

Selon les projections, aussi incertaines soientelles, le PIB réel devrait afficher une contraction de 0,5 % en 2003. Cette contraction du PIB réel moins prononcée qu'en 2022 repose sur l'hypothèse d'une reprise systématique, bien que modeste, de la consommation privée et d'une diminution du déficit du compte courant. Le manque de volonté politique nécessaire pour poursuivre des réformes adéquates et équitables devrait persister tout au long de l'année 2023, de sorte que les perspectives économiques devraient être moins favorables que prévu pour cette année. Les réserves de change de la Banque du Liban ne devraient pas être totalement épuisées en 2023, mais leur érosion persistante reste extrêmement préoccupante.

Le taux d'inflation qui, selon les projections, pourrait atteindre 165 %, devrait demeurer l'un des plus élevés observés dans le monde. L'agrégat monétaire au sens étroit, l'inflation et la dépréciation de la monnaie continueront de favoriser une dynamique d'instabilité économique en l'absence d'un nouveau cadre monétaire et de change.

Le ratio actuel du déficit du compte courant au PIB devrait, selon les projections, légèrement diminuer en 2023 tout en continuant de suivre une trajectoire insoutenable. Le déficit du compte courant devrait être ramené à 14 % du PIB en 2023, grâce à une contraction des importations qui permettra de réduire le déficit du commerce de marchandises par rapport à son niveau de 2022.

Dans ce contexte, la normalisation de l'état de crise masque le fait que l'économie libanaise continue de se dégrader extrêmement rapidement, et se trouve sur une pente très éloignée d'une trajectoire propice à la stabilisation et, a fortiori, à la reprise. Plus la mise en œuvre d'un plan de reprise global, adéquat et équitable se fera attendre, plus les options stratégiques pouvant être adoptées seront réduites en raison de l'érosion des ressources essentielles à la relance. Le ralentissement du rythme auquel l'activité économique se contracte ne signifie pas que la situation se stabilise. En fait, le manque de solvabilité généralisée du secteur bancaire et l'impossibilité pour la monnaie nationale de remplir la plupart de ses principales fonctions se sont soldés par l'apparition d'une économie dollarisée, représentant l'équivalent de près de la moitié du PIB en 2022, ce qui assombrit encore plus les perspectives de reprise économique. Tant que l'économie continuera de se contracter et que la situation de crise durera, le niveau de vie baissera, la pauvreté se généralisera, et les conditions demeureront, pour l'essentiel, précaires. En d'autres termes, le maintien du statu quo garantira que les capitaux de toutes sortes sont en voie d'épuisement, ce qui crée de profondes inégalités sociales caractérisées par un petit nombre de gagnants (relatifs) et une vaste majorité de perdants.

Dossier spécial : Évaluation de l'ampleur de l'économie fondée sur l'argent liquide

La défaillance systématique du système bancaire libanais et l'effondrement de la monnaie ont provoqué l'apparition d'une vaste économie dollarisée fondée sur l'argent liquide, d'une valeur estimée à 9,86 milliards de dollars, soit 45,7 % du PIB en 2022 (Dossier spécial : Évaluation de l'ampleur de l'économie fondée sur l'argent liquide). Une économie fondée sur un recours généralisé et grandissant à des billets de banque en dollars pour effectuer les paiements constitue un obstacle majeur à la reprise économique du Liban. Elle menace non seulement de compromettre l'efficacité de la politique budgétaire et de la politique monétaire, mais accroît aussi le risque de blanchiment d'argent, renforce le caractère informel de l'économie et encourage la fraude fiscale. L'augmentation du nombre de transactions réalisées en liquide risque également de réduire à néant les progrès réalisés par le Liban avant la crise dans le cadre des efforts qu'il avait déployés pour renforcer son intégrité financière en mettant en place de solides mécanismes de lutte contre le blanchiment des capitaux dans le secteur des banques commerciales.

1

THE POLICY CONTEXT

Since the end of the president's term on October 31, 2022, and following the failure to elect a new president, Lebanon has entered an institutional vacuum. According to article 75 of the constitution, upon a presidential vacuum, parliament becomes an electoral body, not a legislative one, until a new president is elected. Parliament has failed to elect a president in 11 consecutive sessions since the end of the former president's tenure in October 2022. Attempts to convene legislative sessions to pass critical laws under the premise of "extraordinary circumstances" have also failed, due to lack of quorum. Despite opposition and limited executive authority, the caretaker government has, however, convened several times to approve decisions on social assistance, subsidies, and treasury advances-attempting to ensure a minimal yet insufficient functioning of the state. Political tensions remain high, casting doubt on a comprehensive political settlement that would put an end to political deadlock and institutional paralysis.

One year after reaching a preliminary staff-level agreement (SLA), an IMF program remains in doubt as the authorities have yet to complete the required upfront reforms. More recently, one of the prior actions has been satisfactorily implemented: the special purpose audit of the Central Bank's foreign asset position. The final audit, however, is yet to be published. While parliament has ratified amendments to the bank secrecy law, amendments fall short of ensuring that the relevant agencies have access to data on individuals' transactions and deposits at the client level.

Parliament has also ratified a government budget for 2022; however, it only became effective six weeks before the end of 2022; the budget was also inconsistent with IMF program parameters (including the exchange rate to be adopted). A capital controls law is at the level of parliament and awaiting ratification; however, the law does not satisfy the parameters of effective regulation of capital flows. The draft law also includes articles that suspend the implementation of all existing and future judicial rulings against commercial banks in Lebanon and abroad as a way to protect banks from multiple ongoing lawsuits against them.

An IMF mission visited Beirut between March 15–23, 2023, to conduct the 2023 Article

IV consultation, assess the economic situation, and discuss policy priorities. In its concluding statement, the IMF warned against a 'never-ending' crisis in the absence of rapid reforms.[7]

Political tensions in the country are mounting, most recently fueled by a judicial row over the Beirut Blast investigation, bank strikes, and domestic and European probes into the central bank Governor. At the end of January 2023, the Beirut Blast probe ground to a halt following a judiciary row between the lead investigator and the top public prosecutor**.** The row ended with the public prosecutor releasing all detainees held in relation to the probe and pressing charges against the lead investigator, following more than a year of high-level political resistance to the inquiry.

More recently, commercial banks went on open strike (February 7–27, 2023) in protest of the multiple lawsuits against them. As part of several domestic investigations, charges have been filed against several banks for money laundering after they failed to lift banking secrecy on the accounts of their board members and shareholders. To end the judicial-banking sector row, the Caretaker Prime Minister has since intervened, while the public prosecutor has requested the suspension of proceedings against banks. As a result, the banking sector temporarily lifted the banking strike until mid-March 2023. In addition to five ongoing money laundering European probes into the BdL governor, a domestic probe against the governor has also resumed in February 2023, following a freeze since June 2021. Political tensions, more recently fueled by undermining the role of the judiciary and the principle of separation of powers, have contributed to yet another episode of rapid currency depreciation.

The Association of Banks in Lebanon (ABL) announced the resumption of the bank strike during March 14–22 in protest to what it considers arbitrary judicial rulings against it. In a statement issued on March 9,[8] ABL considered multiple judicial rulings to exhibit double standards-as more recent rulings have obliged banks to accept US$-denominated pre-crisis debt to be paid by cheque or in local currency at the former pegged exchange rate of 1,507.5 LBP/US$; while other rulings have obliged banks to pay back pre-crisis US$ deposits in cash and in dollars. This is of course compounded by previous rulings that have seized banks' assets. Commercial banks continue to demand the unification of the criteria used for the repayment of loans and the payment of deposits and putting an end to multiple lawsuits against them.

7 IMF staff concluding statement.

8 Link.

2

RECENT ECONOMIC DEVELOPMENTS

Output and Demand

Based on updated econometric techniques,[9] **real GDP is expected to contract by 2.6 percent in 2022 (down from a previous 5.4 percent contraction in the last run).** Estimates for real GDP for 2021 and 2020 remain unchanged (Figure 1). High frequency indicators (namely real estate, private sector, and retail indicators) continue to support a steady economic contraction, that has however, decelerated in 2022. The real estate sector continues to improve from a COVID-19 induced low base of 2020. Cement deliveries (a proxy for construction activity) increased by 10 percent in 9M-2022, on top of a 5 percent increase in 9M-2021. Nonetheless, cement deliveries remained 58 percent lower in 9M-2022 compared to the 9M average over seven years pre-crisis (2013–2019). The BLOM-PMI index (capturing private sector activity) has inched up to 48.4 in 2022, up from an average of 46 percent in 2021 (<50 represents a contraction of activity). The retail sector continues to suffer sizeable losses since 2020—the BTA Fransabank retail trade index declined by 63 percent (in real terms) during H1-2022 compared to H1-2021.

Looking at GDP from the demand side, private consumption was the sole contributor to growth in 2022 (Figure 2). The increase in private consumption is likely due to a stabilization in private sector activity and an increasing dollarization of wages. The growth in the size of the cash economy in 2021 and 2022 (see Special Focus: Gauging the Size of the Cash Economy in Lebanon) is likely also a driver of the increase in private consumption. In the early years of the crisis (2019–2021), net exports were a positive contributor to growth, as domestic demand, which is historically concentrated on imported goods, collapsed. Furthermore, the tourism sector had led an

9 Access to reliable and up to date GDP data in Lebanon is challenging; official GDP numbers are typically reported by the Central Administration of Statistics at low frequencies and with a long lag. The last official national accounts data published was for 2020. High frequency indicators, which can be used to gauge the state of the economy, are also only available with a lag. Notwithstanding these caveats, the best information set available and sophisticated econometric modelling techniques are used (both MIDAS Regressions and Dynamic Factor Models) to nowcast the real GDP growth rate for 2022 (see online annex published with this issue for further details).

FIGURE 1 • Lebanon's Economic Contraction Has Extended for a Fifth Consecutive Year in 2022

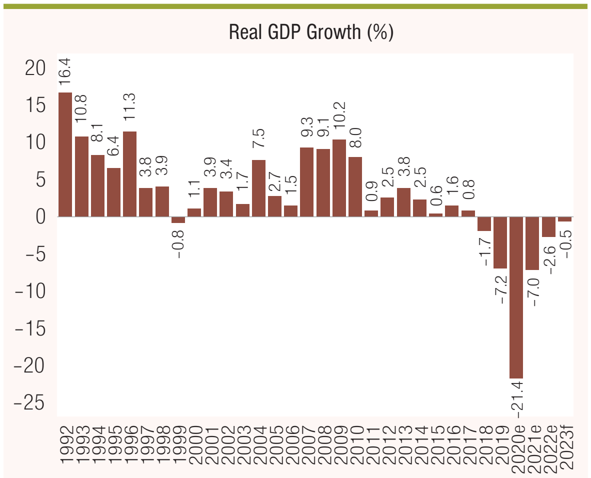
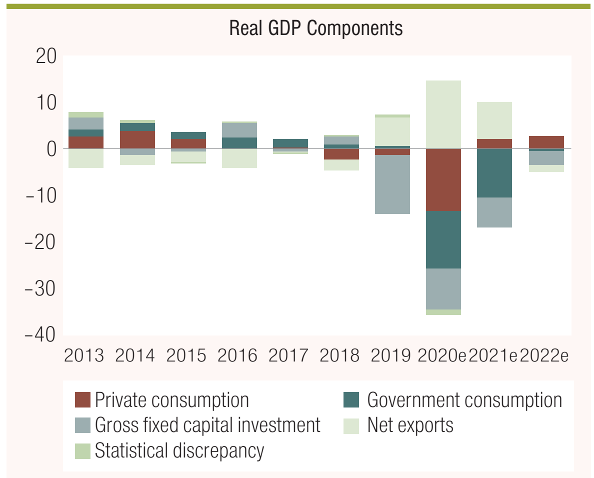


FIGURE 2 • Private Consumption Is the Sole Positive Contributor to Growth in 2022



improvement in the trade in services balance in 2021. However, this trend has reversed in 2022. Despite the continued rebound in the tourism sector in 2022, domestic demand on imported goods has increased to pre-crisis levels, with an adverse impact on the trade in goods balance, resulting in net exports contributing negatively to growth.

Fiscal Developments

A slightly expansionary 2022 government budget only came into effect six weeks before the end of the year, and thus had limited impact on public finances in 2022. In the absence of immediate measures of fiscal consolidation and initiation of debt restructuring in the context of a comprehensive crisis resolution plan, a passive approach to fiscal policy continues to drive a near complete collapse of public finances. The decline in primary spending has led to an acute collapse in public service delivery,[10] while the collapse in revenue generation has hindered financing meaningful wage corrections to offset the dramatic erosion of public sector wages, allowances, and pensions driven by inflation.

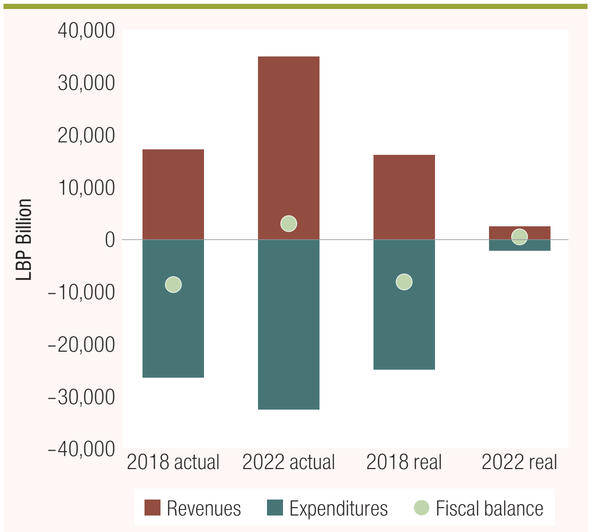
The overall fiscal balance is estimated to have recorded a narrow surplus of 0.3 percent of GDP in 2022, down from a surplus of 1 percent of GDP in 2021. The narrow surplus sustained in 2021 and 2022, obscures a near complete collapse of public finances to the lowest rates globally, and to a fraction of pre-crisis levels. Revenues are estimated to have declined from an already low 13.1 percent of GDP in 2020 to 6.0 percent of GDP in 2022.[11]

Falling revenues were more than offset by a larger decrease in total expenditures, which declined from 16.4 percent of GDP in 2020 to a record low of 5.7 percent of GDP in 2022, pointing to a massive hollowing out of the state amid an unprecedented crisis. To put matters in perspective, in real terms, public expenditures and revenues in 2022 have witnessed a close to 7-fold and 11-fold decrease respectively in real terms compared to 2018 (Figure 3). In nominal terms, revenues and expenditures are estimated to be equivalent to a record low of US$1.3 billion and US$1.2 billion, respectively in 2022

10 See World Bank's 2022 Lebanon Public Finance Review: (Link)

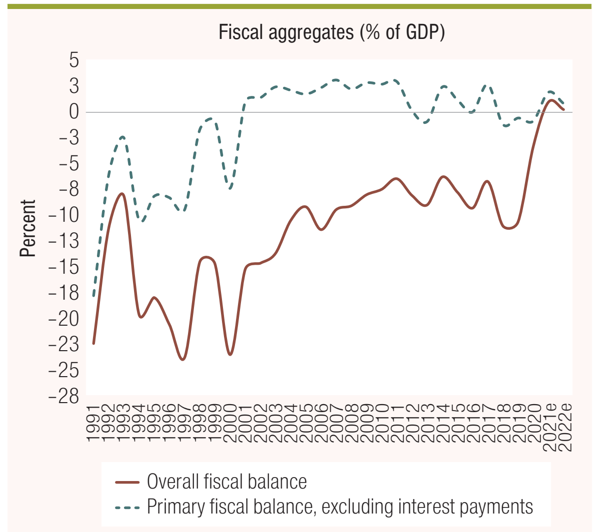
11 World Bank fiscal estimates are based on the latest official Ministry of Finance statistics, and therefore do not include extra budgetary spending, including quasi-fiscal operations conducted by the Central Bank, arrears, usage of IMF SDR allocation for certain fiscal spending, among other expenditures not recorded in official statistics-the fiscal balance is likely to be significantly negative when taking the above-mentioned expenditures into account.

FIGURE 3 • Evolution of Public Finances in Nominal (LBP) and Real Terms, 2018 vs. 2022



Sources: Lebanese authorities and WB staff calculations.

FIGURE 4 • Public Finances Collapse Inducing Positive Fiscal Balance in 2021–2022



Sources: Lebanese authorities and WB staff calculations.

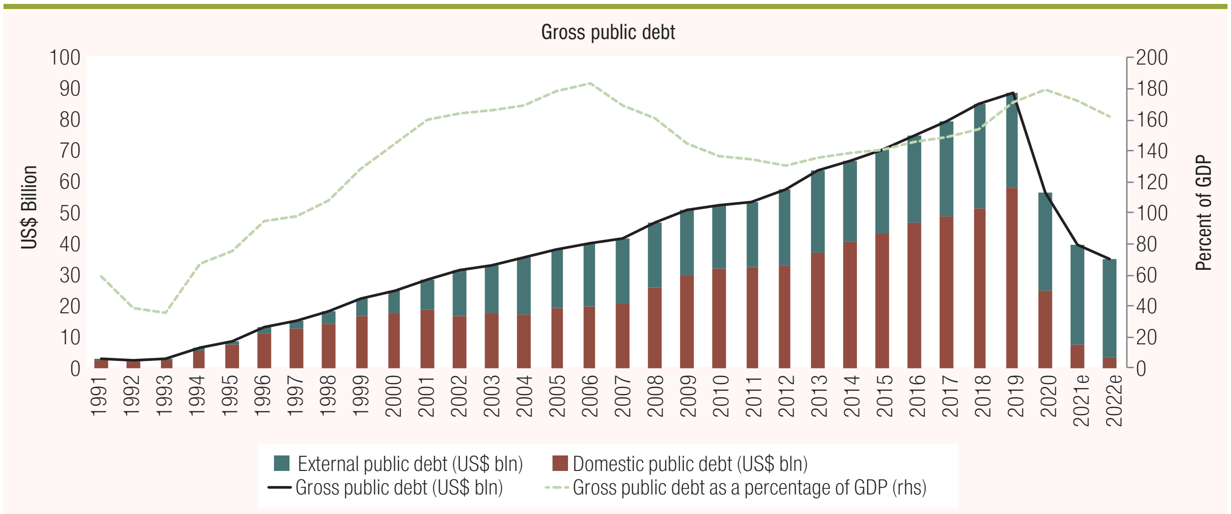
(fiscal surplus equivalent to US$93 million), down from the 2018 pre-crisis revenues and expenditures of US$11.5 billion and US$17.6 billion, respectively (fiscal deficit of US$6 billion).

Primary spending continued to fall as a percentage of GDP in 2022 to a record low of 5.1 percent of GDP, while debt service payments are curtailed by the sovereign default. Although primary spending is estimated to have increased by nearly 100 percent in nominal terms (yoy), it was more than offset by an inflation-driven increase in nominal GDP in 2022 (Figure 4). Between 2019 and 2022, interest payments on foreign debt decreased by 97 percent as a result of the sovereign default, leading to a 56 percent fall in debt service over the same period. In the absence of a debt restructuring plan and fiscal consolidation, the primary balance is estimated to have recorded a narrow surplus of 0.9 percent of GDP in 2022, down from a surplus of 1.8 percent of GDP 2021.

Significant tax revenue losses and an inflation-driven increase in nominal GDP continue to drive a sharp decrease in revenues as a percentage of GDP. Tax revenues are particularly dampened by economic contraction, tax evasion due to a significant shift to a cash-based economy, exchange rate mis-valuation of taxes and fees, and a severe weakening of tax administration capacity as absenteeism spikes due to a collapse in real wages. Authorities have recently attempted to boost revenues by adjusting the former pegged exchange rate. The long-anticipated increase in the customs dollar exchange rate (the exchange rate used to calculate the customs value of imported goods) from 1,500 LBP/US$ to 15,000 LBP/$ came into effect in December 2022. To boost revenues further, amidst an unwavering depreciation spiral, the customs dollar exchange rate was further increased from 15,000 to 45,000 LBP/$ in March 2023, prompting a further increase in the prices of imported goods with custom fees. Nonetheless, in a context of continued currency depreciation, government revenues remain exposed to significant losses. Quick and frequent adjustments to the exchange rate on tax revenues and custom duties to match currency depreciation, are both costly and regressive in the continued absence of a stabilization plan (including the restoration of crucial public services and wage corrections) and daily erosion of purchasing power only compensated for through ad-hoc and temporary salary increases.

Despite a marginal decrease in debt-to-GDP ratios in 2022, debt dynamics remain unsustainable amid a sharp currency depreciation and economic contraction. In 2022, the debt-to-GDP ratio reached 163 percent, a 6-percentage point

FIGURE 5 • Sharp Decrease in Nominal GDP Prompts Erosion of Public Debt as a % of GDP to Pre Crisis Levels



Sources: Lebanese authorities and WB staff calculations.

(pp) decrease from 172.5 percent in 2021. The slight decrease in the debt ratio is a result of the significant erosion of domestic debt due to currency depreciation (the numerator), outweighing the fall in nominal GDP (the denominator), in nominal US$.[12] Exchange rate depreciation of 132 percent (yoy) has led to a 58 percent decrease in domestic debt, while nominal GDP only fell by 7 percent in 2022 compared to 2021. The World Bank debt model assumes a stable foreign denominated debt stock and does not include accumulated arrears. As nominal GDP in US$ continues to decline in the absence of comprehensive reform and economic stabilization, the debt-to-GDP ratio is projected to remain on its structurally unsustainable path, similar to the pre-crisis era (Figure 5).

Through a revaluation operation, BdL added $16.5 billion in assets under "loans to public sector" in its balance sheet; the solvency issue of the sovereign-BdL nexus remains unchanged. The loans to the public sector reflect swaps carried out between BdL and the sovereign from 2007. In exchange for US$ funding, the sovereign deposited the equivalent in LBP at the former exchange rate of 1507.5 LBP/US$. However, along with its new official exchange rate of 15,000 LBP/US$, BdL has revalued those swaps in US dollars, and added them as an asset on its balance sheet, effectively considering them a liability of the sovereign.

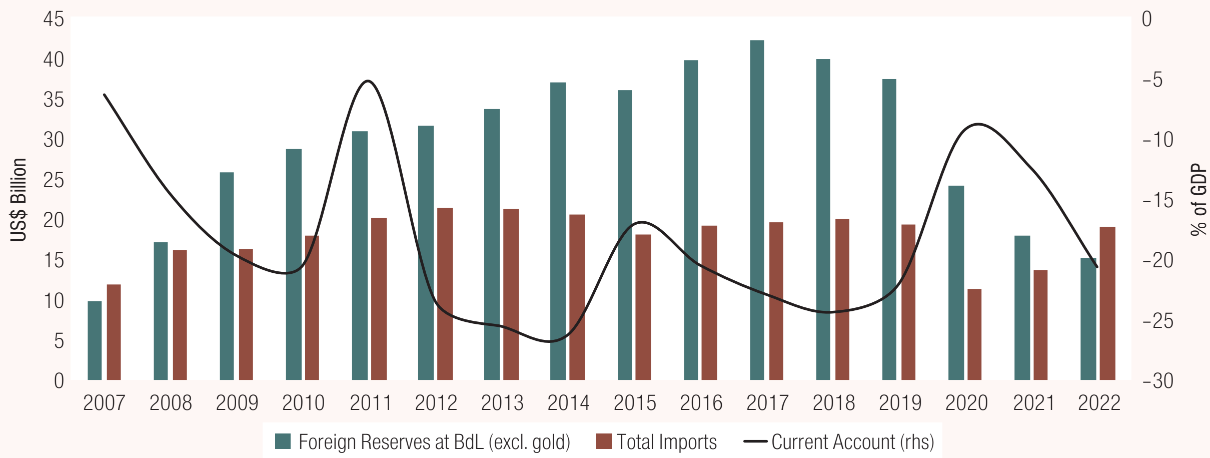
In this reshuffling of the balance sheet, BdL has effectively reduced the losses of the financial sector and possibly substantively increased public debt, severely eroding already unsustainable public debt dynamics. The MoF has not yet indicated how it will treat this addition.

External Sector

A widening trade-in-goods deficit continues to drive a substantive current account deficit in 2022, reflecting historic external imbalances. According to customs data for merchandise goods, imports grew by 39.7 percent (yoy) in 2022, combined with a 10.2 percent decrease in exports. In fact, imports to Lebanon reached US$19 billion in nominal terms in 2022, close to pre-crisis levels. Anticipated increases in the customs duties exchange rate ("the customs dollar"), has likely contributed to the substantive increase in imports of industrial goods (yoy increase of 45.8 percent) and have driven the hoarding of those goods in anticipation of a price adjustment.

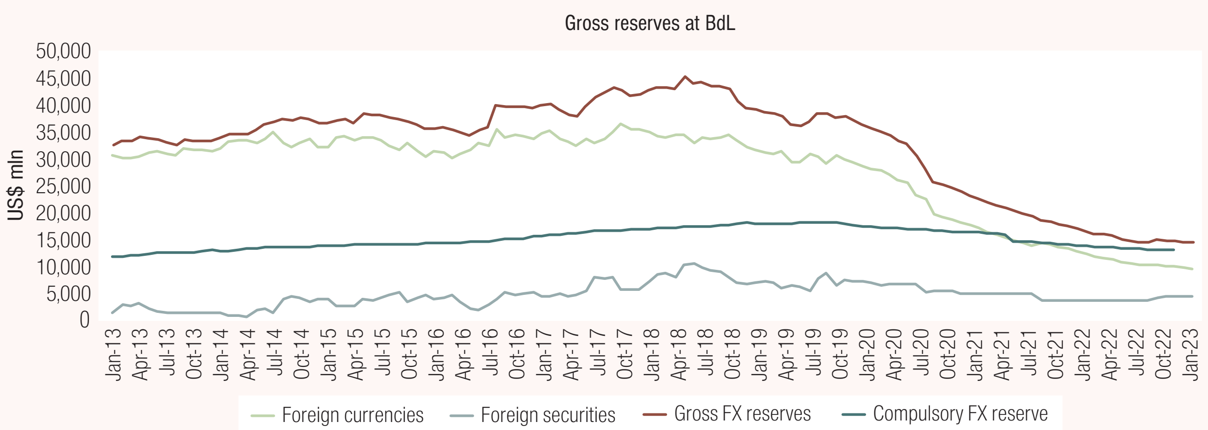
[12] To convert domestic debt to US$, the World Bank Average Exchange Rate for 2020–2022 is used and is estimated at 3,688; 11,755; and 27,309, respectively.

FIGURE 6 • Current Account Deficit Widens in 2022, Registering a Ratio to GDP Similar to Pre-Crisis Years



Sources: BdL, CAS and WB staff calculations.

FIGURE 7 • A Steady Depletion in the Gross Foreign Exchange Position at BdL



Sources: BdL and WB staff calculations.

The trade-in-goods deficit reached 72.2 percent of GDP in 2022, up from 42.2 percent of GDP in 2021 (a widening of the deficit by 59.5 percent in nominal US$ terms).

The current account (CA) deficit's ratio reached 20.6 percent of GDP, almost the level of the pre-crisis medium-term average (2013–2019) of 22.6 percent of GDP (Figure 6)**.** In nominal terms however, the CA deficit reached US$4.4 billion, 57 percent less than the pre-crisis medium term average of US$10.6 billion between 2011–2019. The widening CA deficit as a percentage of GDP continues to be driven by a widening trade-in-goods deficit. The widening trade-in-goods deficit has offset the continued improvement of the trade-in-services balance driven by a persistent rebound in the tourism sector, and the improvement in current transfers driven by the increase in remittances. Tourist arrivals have increased by 57 percent (8M-2022), on top of a 140 percent increase in 12M-2021. Hotel occupancy rates also support this rebound and have increased by 8.7 percentage points in 11M 2022 compared to 11M 2021. The rebound in tourism has increased services receipts by an estimated 59% in 2022 (yoy), increasing the trade-in-services surplus to 17.2 percent of GDP.

Lebanon is estimated to have received a record 31.7 percent of GDP in remittances in 2022, the 2nd highest ratio in the world.[13] Remittance inflows have long been a backbone of the Lebanese economy, averaging US$6.5 billion, between 2012 and 2021. As a percentage of GDP, remittances have increased from an average of 13 percent between 2012 and 2019, to 19.8 percent in 2020, 26.4 percent in 2021, to 31.7 percent in 2022 respectively (largely owing to a denominator led effect of a decrease in US$ nominal GDP). In nominal terms, remittances have increased by 20 percent between 2021 and 2022 (to an estimated US$6.8 billion), only partially offsetting the deficit in the CA balance. In the current crisis, remittances have come to play a crucial role as a safety net for the majority of Lebanese families to finance household consumption and the provision of survival necessities. As the crisis has led to a large exodus of well-educated and highly skilled labor, it is expected to contribute to a further increase in remittance inflow reliance as a safety net in the near future.

The Current Account deficit continues to be financed, for the most part, by the remaining usable gross reserves of BdL. Gross reserves are gradually being depleted; between end October 2019 and end 2022, gross reserves have declined by US$22,745 million, reaching US$15,194 million (including US$4,796 million in foreign securities). BdL's gross position differs widely from its net reserves (i.e., gross FX reserves at the central bank net of FX liabilities to others) and contrary to most central banks, BdL does not publish net reserves, which are estimated to be highly negative and in excess of US$60 billion.[14]

Money and Banking

The Lebanese Pound continues to depreciate sharply, despite having lost more than 98 percent of its value since the onset of the crisis. Between December 2021 and 2022, the Lebanese pound depreciated by 66.5 percent. The BNR (i.e., the Banknote Rate; or parallel market rate) averaged 31,102 LBP/US$ in 2022, while the World Bank-estimated Average Exchange Rate (AER)[15] averaged 27,309 LBP/US$ reflecting a shrinking spread between both rates due to the (disorderly) termination of FX subsidies and pervasive dollarization (or market value) pricing across the overwhelming majority of goods and services.

While the currency has been depreciating for more than three years, episodes of rapid depreciation intensified since February 2023, testament to the continued atrophy of the Lebanese economy. The judicial row over the Beirut blast probe, coupled with repeated banking sector strikes, and political tensions have fueled uncertainty. Persistently high demand for foreign currency to fulfill import obligations and finance foreign currency-denominated expenditures, and continued speculative activity, are further increasing the frequency of episodes of rapid depreciation. While on average, the exchange rate depreciated by five percent on a monthly basis in 2022, it depreciated by 47 percent in February 2023 alone.

Bank strikes have contributed to the sharp deterioration of the BNR as Sayrafa transactions via banks were put on hold by the strikes and foreign currency withdrawals were restricted to ATM withdrawal limits. Increased pressure on ATMs is not always met with adequate replenishment of foreign currency. The BdL's Sayrafa initiative, an electronic currency trading platform for selling US dollars at discounted exchange rates instituted in April 2020, has done little to stem the Pound's decline (see Box 1).

The rapid depreciation in the currency continues to drive triple digit inflation (Figure 12)**.**

13 Remittances Brave Global Headwinds, Migration and Development brief, November 2022, Knomad.

14 World Bank estimates, also see similar estimates in: "Mapping out the path to the Lebanese Economic Recovery", Goldman Sachs International, 2021; "Fitch Downgrades Lebanon to 'CC'", Fitch Ratings, 2019; Moubayed, A., & Zouein, G. (2020).

15 The AER is derived by applying consumption-based weights on the official, the platform and the US$ banknote exchange rates. For a detailed derivation please refer to: World Bank (2020), Lebanon Economic Monitor: The Deliberate Depression, Fall 2020. (Link).

BOX 1: THE SAYRAFA PLATFORM: THE CYCLE OF BUYING TIME

The Sayrafa platform, BdL's Electronic Exchange Platform, has become the central bank's main foreign exchange market operations tool. The platform's viability hinges on BdL's ability to supply dollars from BdL's remaining gross useable reserves. This box provides background on the platform and some empirical analysis of the relationship between the trading volume on Sayrafa, the Banknote (BNR) and Sayrafa rates. It also quantifies the arbitrage profits accruing to those with access to the platform. The foreign exchange interventions via Sayrafa reflect unfavorable monetary tools that led to short-lived appreciations of the LBP at the expense of dwindling reserves and a weakened BdL balance sheet, especially in the absence of a new exchange rate and monetary framework. More recently and starting in April 2022, the analysis suggests that BdL's interventions via the Sayrafa platform have been preceded by a precipitous increase in currency in circulation likely indicating that BdL bought foreign currency in the parallel market to inject them on Sayrafa. Such interventions have contributed to episodes of sharp currency depreciation and volatility, and a further erosion of purchasing power of the LBP. The analysis concludes that the Sayrafa platform is not only an unfavorable monetary tool, but has also morphed into a mechanism to generate arbitrage profits reaching US$2.5 billion since its initiation.

Platform Initiation and Intended Objectives

Circular 149,[a] issued by Banque du Liban (BdL) on April 3, 2020, established the Electronic Exchange Platform, known domestically as Sayrafa. The circular also announced the establishment of a special unit at the central bank whose purpose is to trade foreign currencies. The central bank issued two additional circulars, 157[b] and 159,[c] on May 10 and August 17, 2021, which expand the trading on the Sayrafa platform to commercial banks and require banks to partake in foreign currency transactions solely on the Sayrafa platform.

The establishment of the Sayrafa platform was a bid to bring order to the foreign exchange market. Foreign exchange rate bureaus and agents (many of whom are unlicensed) are the main dealers in the foreign exchange market. As the Lebanese Pound (LBP) continued to depreciate rapidly against the US$ amid a multiple exchange rate system engineered by BdL, the central bank invited legal foreign exchange offices to partake in trading on the Sayrafa platform for the transactions to be "clearly and transparently announced", rather than undertaken in what was dubbed as the "black" or "parallel" market. The ultimate objective of the platform was to (i) arrest the deterioration of the banknote/parallel market exchange rate, and (ii) formalize FX transactions at the market rate in a transparent manner, through the banking sector and official exchange dealers (ultimately cracking down on unofficial market transactions and speculation in the hope of driving down the BNR).

Evolution of the Platform: Interpreting Sayrafa Volumes

Sayrafa swiftly became the central bank's preferred tool to conduct foreign exchange market interventions that aim to shore up the LBP. Following its inception, the trading volume on Sayrafa was very modest and average daily volume over the period July 26 to October 13, 2021, stood at US$1.3 million. Nonetheless, following episodes of rapid depreciation in the LBP, the central bank announced, on multiple occasions, its readiness to supply dollars on the Sayrafa platform without limit in a bid to stem the rapid depreciation of the LBP. In tandem, the BdL, as outlined in the *Fall 2022 Lebanon Economic Monitor*, removed, by issuing circular 161 dated December 16, 2021, all quotas on the monthly US$ liquidity that it provides to the commercial banking sector and expanded the access to Sayrafa to money transfer companies whose annual transactions volume exceeds US$50 million via circular 614 issued on February 21, 2022. These changes made the Sayrafa platform a more potent tool for exchange market interventions.

The volume of transactions on Sayrafa largely depends on BdL providing an adequate level of US$ liquidity on the platform. The volume of transactions on Sayrafa picked up rapidly following BdL's announcement on December 15, 2021, that it stands ready to provide unlimited liquidity in US$ on the platform. Similar announcements were made on May 27, October 23 and December 27, 2022, precipitating a surge in trading volume.[d] Following episodes of rapid depreciation in the LBP in March 2023, the BdL increased Sayrafa rate again to 70,000 LBP/US$ on March 1 and to 90,000 LBP/US$ on March 23. The trading volume on the platform was adversely affected by several bank closures in February and March 2022.

Econometric Analysis: Association between the volume on Sayrafa and the Spread between the Sayrafa and the Banknote Rate (BNR):

The opaque nature of trading on Sayrafa and the complete absence of information on the buy and sell sides of transactions have led to it being perceived as a "black box".[e] Nonetheless, using the available data, a simple empirical analysis of the association between the volume on Sayrafa and the Sayrafa and BNR rates is offered. The analysis demonstrates a statistical relationship between the overall volume of trade on the Sayrafa platform, the value of the Lebanese Pound, and the spread between the official and parallel, or BNR, rates. However, the relationship is a weak one and does not amount to an endorsement of the platform.

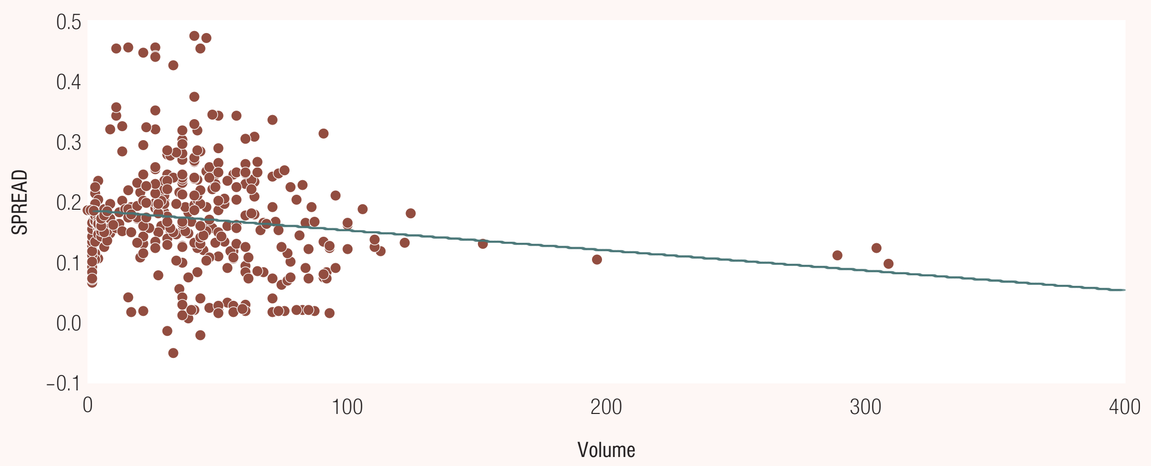
Let s_t and $\tilde{s}_t$ denote, respectively, the BNR and Sayrafa rates, expressed in terms of units of LBP per US$. The spread between the BNR and Sayrafa rates is $sp_t = (s_t - \tilde{s}_t)/ s_t$ The latter computation circumvents non-stationarity in the exchange rates.

First, the relation between the volume of transactions and the spread is examined graphically.

The scatter plot suggests a negative (albeit weak) association between the spread and volume.

(continued on next page)

BOX 1: THE SAYRAFA PLATFORM: THE CYCLE OF BUYING TIME *(continued)*



Second, a Vector Error Correction model (VECM) comprising the natural logarithms of the BNR, Sayrafa rate and transaction volume is estimated.[f]

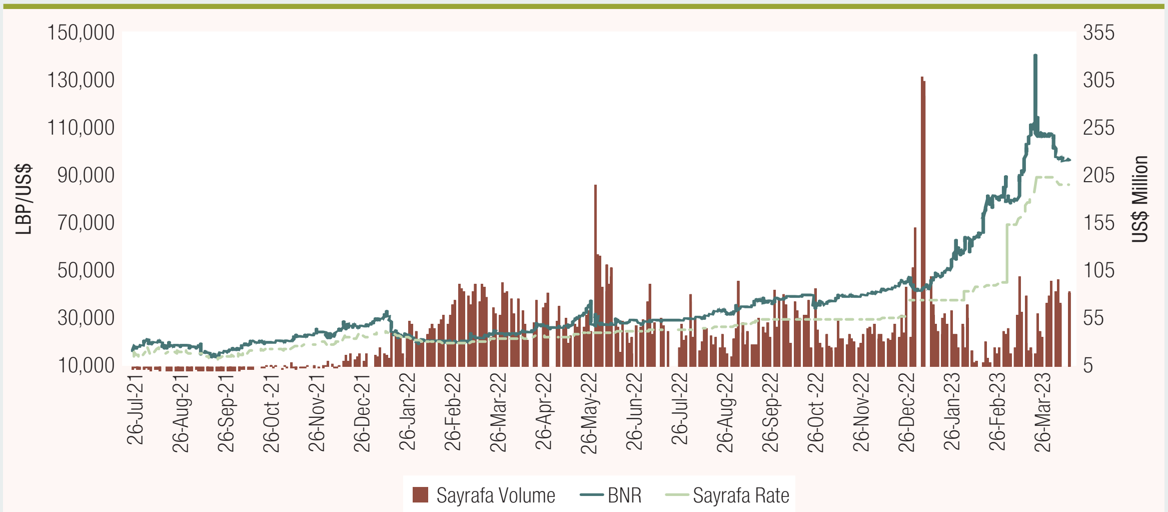
The findings from estimating the VECM suggest that, except for the first lag, the volume on Sayrafa is negatively associated with the BNR and positively associated with the Sayrafa rate. Further, tests of Granger causality indicate that the volume on Sayrafa Granger-causes the BNR. Taken together, these findings point to a narrowing in the spread between the BNR and Sayrafa rates when the volume on Sayrafa increases.

The Source of FX supply through the Sayrafa Platform

Remaining FX Usable Reserves

The survival of the Sayrafa platform hinges on the central bank's ability to supply dollars. As the Sayrafa exchange rate has been consistently below the BNR, very few (if any) businesses, traders, and individuals have an incentive to sell US$ at the Sayrafa rate. Hence, the supply of dollars is likely to originate from BdL's reserves and, because there are no economic incentives to offer US$ at a loss on the platform when they can be sold at a more favorable exchange rate in the parallel market, the functioning of the platform hinges on BdL provisioning US$ liquidity on the platform. For the period December 2021 to August 2022 the palpable increase in Sayrafa volumes (FX interventions by BdL) occurred

FIGURE 8 • Increased Sayrafa Volumes (weakly) Associated with BNR Appreciation & Decrease in the Spread between BNR & Sayrafa Rates



Sources: BdL and WB Staff Calculations.

(continued on next page)

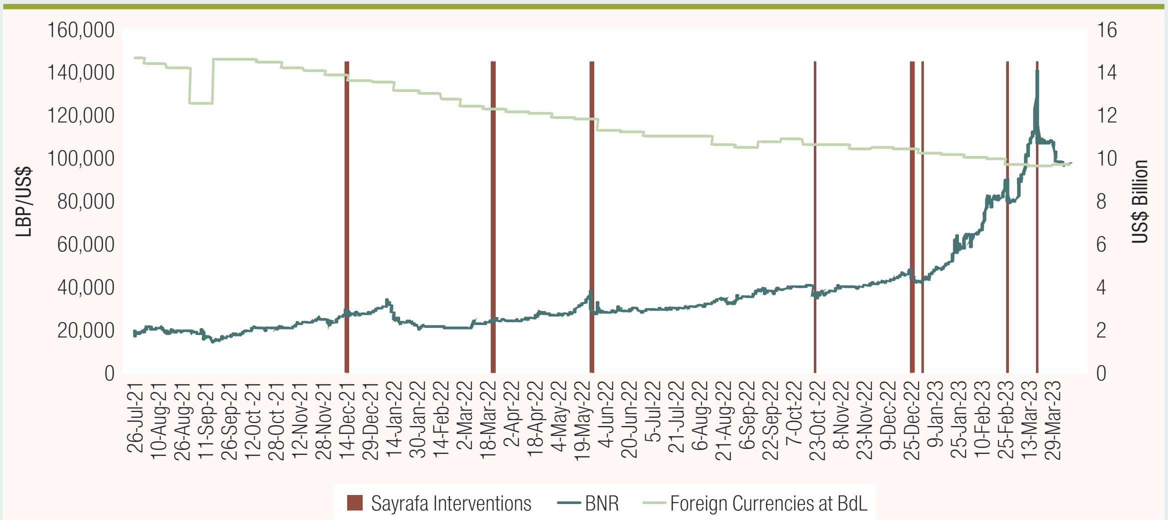
BOX 1: THE SAYRAFA PLATFORM: THE CYCLE OF BUYING TIME *(continued)*

in tandem with a precipitous decrease in remaining gross usable reserves. Indeed, BdL gross reserves have decreased by US$4.82 billion over the period July 2021 to January 2023, likely indicating that the reserves were used, at least in part, to provide liquidity on the platform (Figure 9 below). BdL's interventions, have thus led to short-lived appreciations in the BNR at the expense of depleting remaining gross usable reserves, ultimately weakening BdL's balance sheet position.

Buying Dollars from the Banknote Market

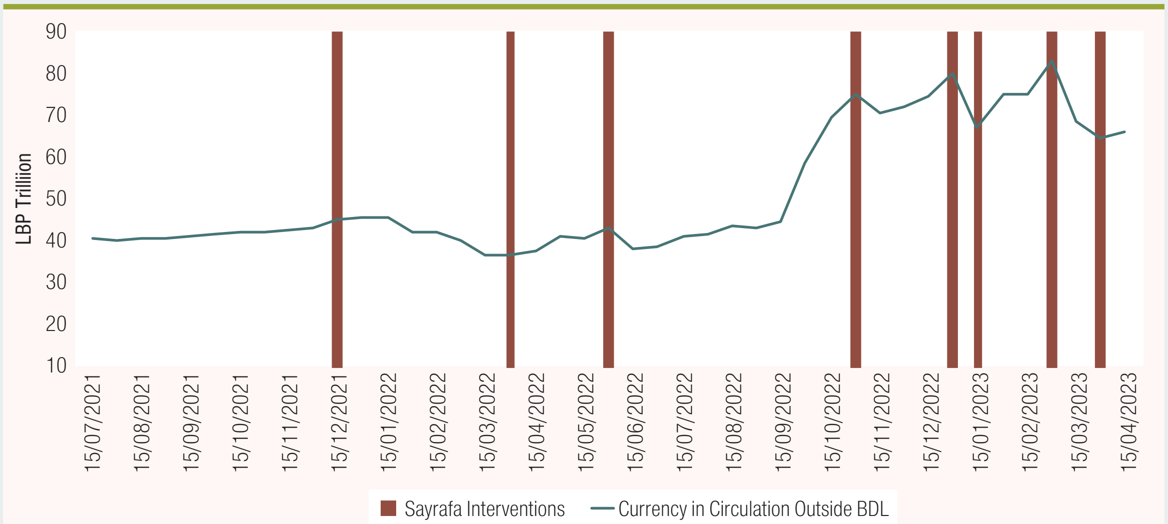
The plateauing of the decrease in BdL foreign currency assets all the while BdL's foreign exchange interventions via Sayrafa are still underway raises questions regarding the source of the liquidity on the platform.[h] Starting in April 2022, the significant increases in the volume on Sayrafa were preceded by surges in currency in circulation (Figure 10 below). The latter actions may be suggestive that BdL purchased foreign currencies outright

FIGURE 9 • Increase of Volume of Transactions on Sayrafa Occurred in Tandem with a Precipitous Decrease in Remaining Gross Usable Reserves[g]



Sources: BdL and WB Staff Calculations.

FIGURE 10 • Increase of Volume of Transactions on Sayrafa Was Preceded by an Increase in Currency in Circulation Starting in April 2022



Sources: BdL and WB Staff Calculations.

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BOX 1: THE SAYRAFA PLATFORM: THE CYCLE OF BUYING TIME *(continued)*

from the market to inject them on the Sayrafa platform. The increase in the currency in circulation has led to rapid episodes of steep currency depreciation, further exacerbating exchange rate volatility and far from succeeding in stabilizing the BNR.

Arbitrage Opportunities

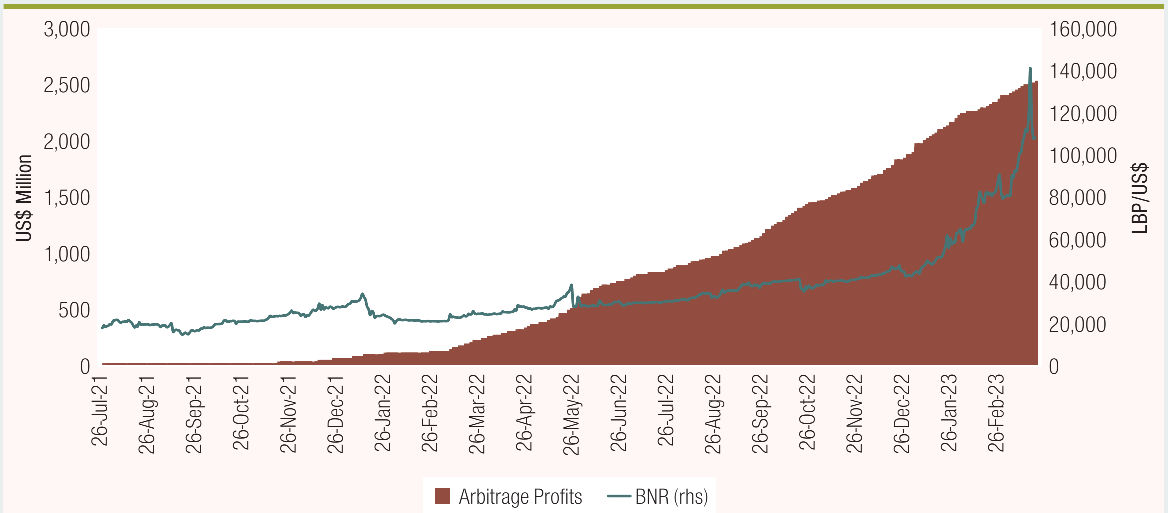
The platform has also proven to be a mechanism to generate arbitrage profits, and provide subsidies to public servants, importers, and select individuals and corporations.[i] In fact, owing to access to foreign currency at subsidized rates, close to US$2.5 billion in arbitrage profits have accrued to those benefitting from access to Sayrafa since the initiation of the platform (Figure 11).[j] Arbitrage profits are computed as the spread between the BNR and the Sayrafa rate, multiplied by the Sayrafa volume, then divided by the BNR. Due to lack of granular data on buy and sell transactions on Sayrafa, it is assumed that the total volume of transactions reported are sell-side transactions, with most FX supply provided by BdL.[k] Arbitrage profits, therefore, are also losses to BdL's balance sheet.

Notwithstanding the sizeable volume of transactions on the platform, the goal of unifying exchange rates continues to be elusive due to the rationing and severe shortage in FX supply on the platform, and the lack of a credible macro-framework. In fact, the platform has added yet another exchange rate to a highly taxing multiple exchange rate system that continues to create distortions and rent-seeking opportunities.

Conclusion

The Sayrafa platform reflects a weak and inefficient monetary tool at best, with the ultimate objective of buying time in the absence of a new exchange rate and monetary framework. BdL's interventions via the Sayrafa platform have only achieved short-lived appreciations in both the Sayrafa and the US$ banknote exchange rates, at the expense of dwindling foreign reserves and/or a rapidly depreciating exchange rate (prompting severe erosion in purchasing power), a testament to the unsustainability of such measures. Burning through foreign exchange reserves to temporarily prop up the national currency is an unsustainable monetary and quasi-fiscal tool that has proven to be costly, as it negatively affects Lebanon's financial position, and long-term prospects of recovery.

FIGURE 11 • Arbitrage Profits Using the Sayrafa Platform Exceed US$2.5 Billion



Sources: BdL and WB staff calculations.

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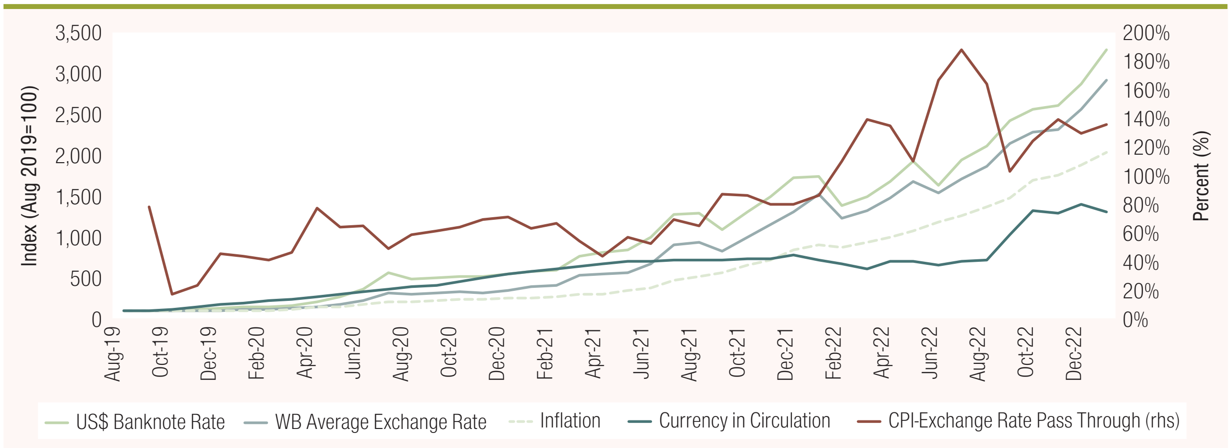
[a] Circular 149.
[b] Circular 157.
[c] Circular 159.
[d] The announcement on December 27, 2022 was accompanied by a change in the Sayrafa rate to LBP 38,000 per US$.
[e] See, for example, Article.
[f] The Johansen (1988) methodology is employed to estimate the VECM. The Sayrafa and BNR are cointegrated and this cointegration relation is exploited in the model.
[g] Burgundy lines represent announcements of BdL interventions that lead to an increase in the volume of transactions or the Sayrafa rate.
[h] A distinction should be made between foreign currency reserves and assets at BdL. The difference between foreign currency assets and reserves is equal to BdL's securities portfolio in foreign currencies. While foreign assets plateaued, foreign currency reserves continue to decrease, albeit the rate of decrease has slowed in 2021 and 2022.
[i] Employees of the public sector are permitted to withdraw their salaries at the Sayrafa rate, effectively constituting an implicit tool to subsidize public sector wages.
[j] The arbitrage profits estimate does not include those profits stemming from the spread between the Sayrafa rate and the preferential Sayrafa rate granted to public sector employees, which means that the estimated cumulative arbitrage profits are likely to be understated.
[k] As mentioned earlier, as the Sayrafa exchange rate has been consistently below the BNR, very few (if any) businesses, traders, and individuals have an incentive to sell US$ at the Sayrafa rate. Hence, BdL is likely the main if not only supplier of FX liquidity on the platform.

Inflation averaged 171.2 percent in 2022 and is expected to remain in the triple digits in 2023. The rise in prices of food and non-alcoholic beverages in the consumption basket was the highest contributor to inflation in 2022, averaging a 240 percent increase throughout 2022, and reaching a maximum of 483 percent (yoy) in January 2022 (Figure 13). In fact, the exchange rate pass through,[16] which measures the extent to which fluctuations in the exchange rate lead to changes in aggregate prices (i.e., inflation), has averaged 133 percent in 2022, up from an average of 61 percent between October 2019 and December 2021. This increase is mainly on account of the near complete removal of FX subsidies on crucial imports by BdL, increased dollarization in the Lebanese economy[17] and unmonitored price increases to hedge against future depreciation episodes.

16 Please see online annex published with this issue for further details on the exchange rate pass-through calculations.

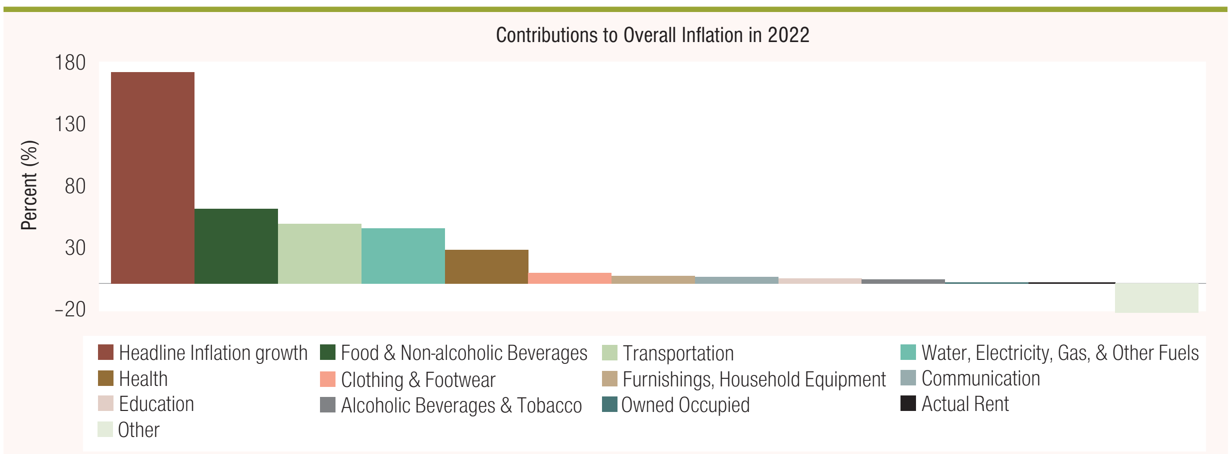
17 The loss of confidence in the LBP has increasingly driven dollarization across several sectors, including tourism. More recently, all supermarkets have also been allowed to price in US$, while customers can pay in dollars or Lebanese pounds at the market rate published by each supermarket.

FIGURE 12 • Exchange Rate Depreciation Drives the Surge in Inflation



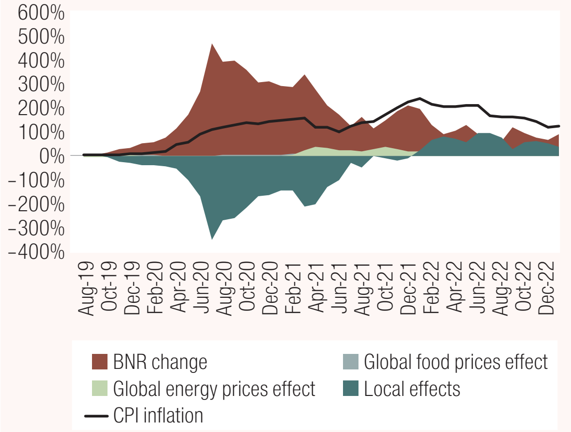
Sources: BdL, CAS and WB staff calculations.

FIGURE 13 • Inflation in Basic Items Has Been a Key Driver of Overall Inflation, Hurting the Poor and the Middle Class



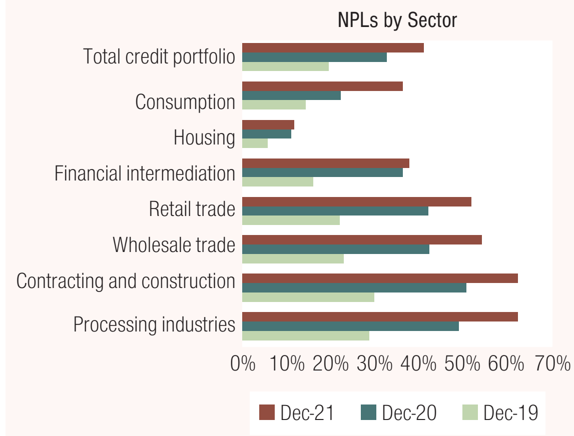
Sources: CAS and WB staff calculations.

FIGURE 14 • Currency Depreciation and Local Factors Are Main Drivers of Inflation



Sources: CAS and WB staff calculations.

FIGURE 15 • A Steady and Sharp Deterioration in Credit Performance as Measured by NPL Ratio for Banks



Sources: Lebanese authorities and WB staff calculations.

In addition to currency depreciation, local factors (such as hedging) have become dominant drivers of core CPI inflation.[18] Local factors refer to increases in headline CPI inflation that cannot be attributed to global food or energy price increases or to changes in the BNR. Figure 14 provides a disaggregation of headline CPI inflation, by global (namely, food and energy prices), exchange rate depreciation, and local factors. Stripping out the short-lived (or transitory) effects of increases in global food and energy prices following the Russian invasion of Ukraine, the rapid depreciation of the LBP was the largest driver of core inflation in Lebanon until December 2021; however, since January 2022, the weight of local factors in headline CPI inflation has increased. It is likely that the residual increase in core inflation (local factors) is due to hedging against future rapid episodes of depreciation, and lack of price monitoring and control by the relevant authorities.

Effective February 1, 2023, BdL has adjusted Lebanon's official exchange rate to 15,000 LBP/US$, a devaluation of nearly 90 percent from the former peg of 1,500 LBP/US$. The new exchange rate replaces the former peg in the context of a multiple exchange rate system that persists. This system provokes distortions in the economy and creates rent-seeking opportunities. The new official exchange rate also applies to the withdrawal rates of pre-crisis deposits (of circular 158 and 151). The change of the exchange rate in the balance sheet of banks prompts the re-calculation of all banking sector assets denominated in LBP but converted to US$ at the former 1,500 rate to the new rate of 15,000-hence, since banks have a sizeable amount of assets denominated in liras (that have to be converted to US$ at the new rate)—banks will incur huge losses in those assets. However, BdL has allowed banks to (1) value their real estate assets at the "fresh dollar" rate and (2) adopt the Sayrafa platform rate of December 31 of each year, and for five years, to value their real estate assets in Lebanon and their long-term contributions and lending related to participations in banks and financial institutions abroad bought or granted with BdL's approval.[19] The BdL has given banks five years to 'reconstitute' losses in their balance sheets, which essentially goes against the upfront realization of losses (as per international best practice and IMF prior actions).

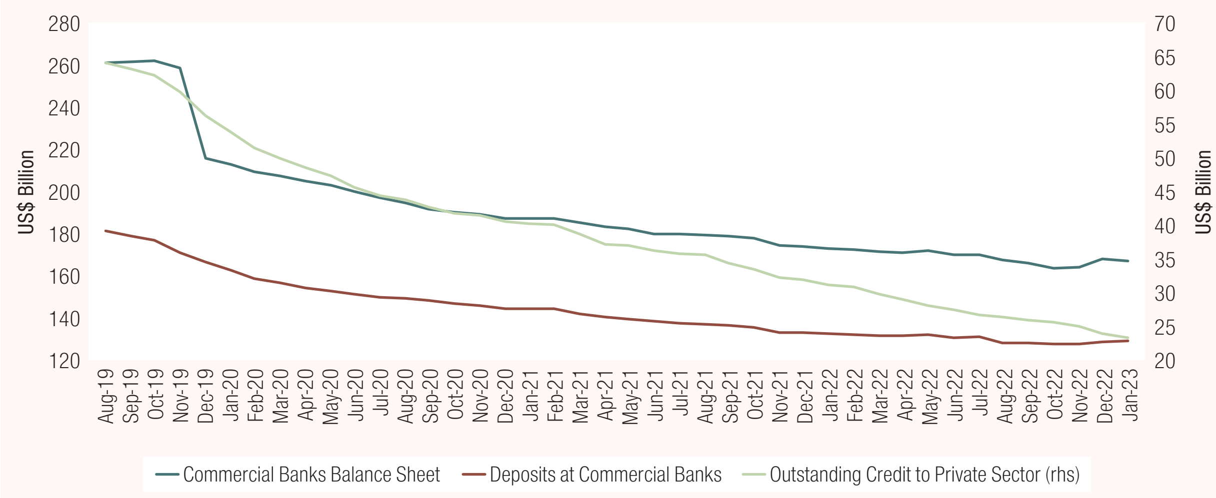
Financial losses in the banking system exceed US$72 billion, equivalent to more than three times GDP in 2022.[20] Combined losses stem

18 Core CPI inflation is defined as the rate of change in the price of CPI basket excluding global food and energy prices, two volatile components. Headline inflation, which measures the change in the price of the entire CPI basket, typically exhibits larger volatility than core inflation.

19 Circular 659.

20 Please refer to: World Bank (2022), Lebanon Economic Monitor, Fall 2022: Time for an Equitable Banking Resolution. (Link).

FIGURE 16 • A Severe Contraction in Loans and a Reduction in Deposits Shrinking Bank Balance Sheets



Sources: CAS and WB staff calculations.

from (1) a sovereign that is in default on its public debt of approximately US$35 billion (163 percent of GDP in 2022);[21] (2) a central bank, Banque du Liban (BdL) that has US$60 billion (259 percent of GDP) in negative net foreign exchange reserves—by far the largest negative reserves of all central banks across the world;[22] and (3) substantive losses in the private sector credit portfolio rendering the oversized banking system insolvent, against pre-crisis equity of US$21 billion.[23] As early as November 2019, the financial sector introduced discretionary and informal capital controls, to conserve their liquidity and capital, as depositors struggled to access the full value of their pre-crisis deposits. A multiple exchange rate system was put in place, governed by ad-hoc Central Bank circulars, in lieu of a new monetary exchange rate framework grounded in the full realization of financial losses. Since June 2021, BdL has formally allowed for a gradual withdrawal of deposits, a lirafication scheme that has resulted in haircuts on deposits between 60–80 percent. The burden of the ongoing adjustment and deleveraging in the financial sector is highly regressive, falling hardest on smaller depositors.

Despite ongoing regressive deleveraging schemes for more than three years, the banking sector balance sheet remains impaired. As of January 2023, 70.1 percent of banking assets are in sovereign securities, 63.3 percent of which are with BdL in the form of deposits, while the remaining 6.8 percent are in government securities (TBs and Eurobonds) and claims on the public sector. As of end 2022, 77 percent of banks' liabilities are private deposits (only down from 90 percent at the onset of the crisis) despite the deposit lirafication scheme.[24] The domestic credit portfolio has further contracted by US$8 billion as of end 2022; this is on top of a contraction by US$8.6 billion in 2021 (Figure 16), bringing the total credit contraction to about 61 percent since the onset of the crisis in 2019. Figure 15 portrays the sharp deterioration in the banking sector's lending portfolio as measured by the ratio of nonperforming loans (NPL).

As outlined in the *Fall 2022 Lebanon Economic Monitor*, divergent views among key stakeholders on how to distribute the financial

21 Based on World Bank estimates; The World Bank debt model assumes a stable foreign denominated debt stock.

22 Based on World Bank estimates, also see similar estimates in: "Mapping out the path to the Lebanese Economic Recovery", Goldman Sachs International, 2021; "Fitch Downgrades Lebanon to 'CC'", 2019; Moubayed, A., & Zouein, G. (2020).

23 Source: BdL.

24 About 77 percent of total deposits (US$98 billion) are in FX; most of them (98 percent) are estimated to be in pre-crisis dollars.

losses remains the main bottleneck for reaching an agreement on an equitable banking resolution. Global best-practice principles endorse a financial sector rehabilitation strategy that recognizes and addresses the large losses in the sector upfront, respects the hierarchy of claims, protects small depositors, and refrains from recourse to public resources. Key stakeholders in Lebanon, however, remain strongly opposed to such a resolution, calling on the State to bear responsibility for the ongoing crisis and to privatize public assets and/or draw on future government revenues to bail-out the financial sector. The magnitude of the holes in the intertwined balances sheets of the Central Bank, the banking sector and the Sovereign, dwarfs the current and future assets that the sovereign could realistically mobilize for a bailout. Not only is Lebanon's banking system *too big to bail*, but a bailout of the financial sector by taxpayers would redistribute wealth from poorer to richer households, as the public would be asked to compensate bank equity holders and wealthy depositors.

3

OUTLOOK AND RISKS

Subject to extraordinary high uncertainty particularly in the context of repeated episodes of sharp currency depreciation, real GDP is projected to contract further by 0.5 percent in 2023.[25] The less severe contraction in real GDP in 2023 owes to a continued, albeit modest, pick up in private consumption and a narrowing of the current account deficit relative to 2022. Further, milder contractions in investment and gross fixed capital formation are also expected to contribute to lessening the economic contraction relative to 2022. Projections (Table 1) pay heed to persistent lack of political will for comprehensive reforms, and institutional vacuum, expected to prolong throughout the whole of 2023. A complete depletion of FX reserves at BdL is not expected in 2023.

Inflation is expected to remain in triple digits, at 165 percent, persistently amongst the highest rates globally. Monetary and financial turmoil are expected to continue to drive crisis conditions. In our next run, our inflation estimates will be revised to account for ongoing episodes of steep currency depreciation-and the persistent sharp interaction between the exchange rate and inflation shaping unstable dynamics (as outlined in *Money and Banking* section).

On the fiscal front, given the significant delay in ratifying a government budget for 2023, we assume that the 2022 budget will continue to have considerable impact on public finances in 2023.[26] As budget 2022 reflects a slightly expansionary fiscal policy, the fiscal balance is estimated to record a deficit of 0.5 percent of GDP for the first time since 2020. The primary balance is projected to also record a deficit of 0.3 percent of GDP. As a result, probable monetization of the fiscal deficit will

[25] Given the lack of data to inform 2023 projections, our projections for the economic growth are based on dynamic forecasts from the econometric models that are outlined in the online Annex published with this issue. Due to parameter and model uncertainty, these forecasts are subject to considerable uncertainty.

[26] In the absence of a ratified 2023 budget, spending follows the 1/12th rule based on the last approved budget law, i.e. spending in 2023 will be based on the budget law of 2022 until a 2023 budget comes into force. The 1/12[th] rule stipulates that for each month of the new year that passes without an updated budget, the government can spend one-twelfth of the annual amount allocated in the last approved budget. With inflation in triple digits, the 2022 nominal LBP budget numbers, translate in a sharp contraction in real terms for 2023.

have implications on the narrow money supply and exacerbate the inflationary environment. Nonetheless, in real terms, both expenditures and revenues in 2023 are on a steep downward trajectory, reflecting an 88.8 and 84.3 percent decrease respectively, since 2018, a reality that points to a massive hollowing out of the state. Debt dynamics are expected to remain unsustainable as a result of both economic contraction and currency depreciation, with the debt-to-GDP ratio projected at 183.5 percent of GDP in 2023.

The current account deficit to GDP ratio is expected to remain sizeable in 2023, although slightly lower than in 2022, reflecting a chronically weak external position. The current account deficit is expected to narrow to 14 percent of GDP in 2023, down from a record 20.6 percent of GDP in 2022. The materialization of the anticipated increase in the custom duties exchange rate was among the main drivers of the record increase in imports in 2022, and the consequent worsening of the trade-in-goods deficit. Following the introduction of the changes to the exchange rate of the custom duties prompting further increases in the price of imported goods, a slight improvement in the trade-in-goods balance in 2023 is projected, driven by a projected decrease in imports. Nonetheless, the current account deficit continues to reflect historic external imbalances and continues to deplete the remaining usable foreign exchange reserves of BdL.

Against this backdrop, the Lebanese economy is markedly distant from a stabilization path, despite the ostensive normalization of crisis conditions. Economic contraction deceleration in 2022 and 2023 respectively, is owed to a technical deceleration tied to consecutive steep contractions in previous years (base effect) and is not an indication of a stabilizing economy. To the contrary, further economic contraction cannot be discounted as foreign reserves run dry, the inflation-depreciation spiral accelerates, and the core functions of the state are further depleted. Therefore, even the technical deceleration in economic contraction witnessed is far from sustainable.

Under current conditions of ever-present financial and monetary turmoil, compounded by political uncertainty, a heavily dollarized and cash economy prevails. As outlined in the *Special Focus* below, the pervasive dollarized cash economy impedes prospects of economic recovery. The prevalence of cash transactions not only heightens the risks of money laundering and tax evasion, but also aggravates informality and has adverse implications on the ability to conduct monetary and fiscal policy. Should BdL's gross foreign exchange reserves run out, a fully dollarized economy whose size will be dictated by foreign exchange inflows will ensue.

Persistent lack of political will for comprehensive and adequate reforms stems from a policy of preservation of interests of a narrow elite base. While Lebanon's pre-crisis unsustainable development model has benefited a few at the expense of the rest of the population, ad-hoc crisis management decisions have also favored an unequal economic adjustment that is setting the premise for long term inequality and a new economic configuration.

Across all economic pillars, ad-hoc crisis management decisions continue to undermine a just and comprehensive recovery plan, ostensibly because of the persistent political deadlock. As outlined in detail in annex I, the continued socialization of financial losses through a multiple exchange rate system, ad-hoc monetary policy and the monetization of fiscal deficits have prompted a deeply regressive inflation-depreciation spiral that has only further depressed economic output and deepened the calamities of Lebanon's residents. In fact, piecemeal interventions, and short-sighted decisions in isolation of a well-carved out comprehensive strategy, have shifted the burden of the economic adjustment to the most vulnerable segments of the population and the majority of the local labor force who earn in national currency and are witnessing a daily, often double-digit erosion to their purchasing power. This is further compounded by a near complete collapse of public finances, driving an acute collapse of public service provision and state institutions atrophy with devastating consequences on state building moving forward. The winners in this case are few.

As repeatedly called for, Lebanon needs to urgently adopt a domestic, equitable, and comprehensive solution that is predicated on: (i) a new and credible exchange rate and monetary framework, (ii) comprehensive bank restructuring addressing upfront the balance sheet impairments, restoring liquidity, and adhering to sound global practices of bail-in solutions based on a hierarchy of creditors (starting with banks' shareholders) that protects small depositors, (iii) a medium-term fiscal strategy to restore debt sustainability, and (iv) key structural and sector-level reforms to enhance governance (see Annex I).

TABLE 1 • Selected Economic Indicators (2015-2023)

	2015	2016	2017	2018	2019	2020	2021 Est.	2022	2023 Proj.
	(annual percentage change, unless otherwise specified)								
Real Sector									
Real GDP	0.5	1.6	0.9	−1.9	−6.9	−21.4	−7.0	−2.6	−0.5
Real GDP per Capita[a]	−1.7	3.8	3.4	0.7	−4.2	−19.7	−5.8	−0.8	−0.5
	(Share of Real GDP)								
Agriculture	3.7	3.8	4.3	4.4	4.7	6.0	6.0	6.0	6.0
Industry	12.7	12.8	12.3	12.0	10.7	12.8	12.8	12.8	12.8
Services	72.0	71.7	71.8	72.2	73.9	76.9	78.6	78.6	78.6
Net Indirect Taxes	11.6	11.7	11.6	11.4	10.6	4.3	2.6	2.6	2.6
	(annual percentage change, unless otherwise specified)								
Inflation (Consumer Price Index)	−3.7	−0.9	4.5	6.1	2.9	84.3	154.8	171.2	165.0
Public Finance	(percent of GDP, unless otherwise specified)								
Revenue	19.2	19.4	21.9	21.0	20.8	13.1	7.5	6.0	6.3
o/w Tax revenue	13.7	13.7	15.5	15.4	15.6	9.0	5.6	4.8	5.0
Expenditure	26.9	28.7	28.6	32.0	31.4	16.4	6.5	5.7	6.8
Current expenditure	21.7	23.2	23.6	26.0	26.1	14.3	5.8	5.2	5.8
o/w Interest payment	5.7	6.0	6.1	5.8	6.0	2.3	0.9	0.6	0.2
Capital expenditure	1.4	1.4	1.5	1.7	1.3	0.4	0.1	0.1	0.2
Overall fiscal balance	−7.7	−9.3	−6.7	−11.0	−10.6	−3.3	1.0	0.3	−0.5
Primary balance	1.2	0.0	2.7	−1.2	−0.5	−0.8	1.9	0.9	−0.3
External Sector	(percent of GDP, unless otherwise specified)								
Current Account Balance	−17.1	−20.5	−22.9	−24.3	−22.0	−9.3	−12.5	−20.6	−14.0
Trade balance	−22.9	−23.7	−24.8	−24.8	−25.1	−20.3	−31.0	−46.8	−41.4
o/w Export (GNFS)	39.7	37.3	36.1	35.7	35.7	28.2	44.9	61.3	68.3
Exports of goods	8.0	7.7	7.6	7.0	9.4	12.9	20.1	21.4	22.3
Exports of services	31.7	29.6	28.5	28.7	26.3	15.3	24.7	39.9	46.1
o/w Import (GNFS)	62.6	61.0	60.9	60.5	60.8	48.5	75.9	108.1	109.8
Imports of goods	35.2	35.1	34.8	34.4	35.3	33.4	55.4	79.2	76.1
Imports of services	27.4	25.9	26.1	26.1	25.5	15.1	20.5	28.9	33.7
Factor services and transfers	5.8	3.2	1.9	0.5	3.0	11.0	18.5	26.2	27.5
o/w Net remittance inflows	7.2	6.7	5.2	4.2	6.1	11.9	17.8	24.0	25.9

(continued on next page)

TABLE 1 • Selected Economic Indicators (2015-2023) *(continued)*

	2015	2016	2017	2018	2019	2020	2021 Est.	2022	2023 Proj.
	(annual percentage change, unless otherwise specified)								
Total Public Debt									
Total debt stock (US$ million)[b]	70,315	74,959	79,530	85,139	88,900	56,813	39,903	35,047	32,948
Debt-to-GDP ratio (percent)	140.8	146.6	150.0	155.1	172.3	179.2	172.5	162.6	183.5
Memorandum Items									
Nominal GDP (LBP billion)	75,268	77,105	79,939	82,764	80,196	116,954	271,916	588,617	1,509,308
Exchange rate, average (LBP/US$)	1,508	1,508	1,508	1,508	1,554	3,688	11,755	27,309	84,068
Nominal GDP (US$ million)[b]	49,929	51,147	53,028	54,902	51,606	31,712	23,132	21,554	17,953

[a] We base our per-capita calculation on population estimates produced by UN population division. These estimates have been significantly revised down, for Lebanon, to 5.5 million, from 6.7 million, in 2022. This change has a prominent effect on Real GDP per capita growth and Nominal GDP per capita.

[b] We use the WB-AER to calculate the total debt stock and nominal GDP in US$ million for 2019 onwards.

SPECIAL FOCUS: GAUGING THE SIZE OF THE CASH ECONOMY IN LEBANON

A complete loss of confidence in an impaired banking sector has precipitated a rapid shift towards hard currency cash transactions. This Special Focus offers estimates of the size of the cash economy over the years 2020 to 2022. The US$ cash economy is defined as total US$ cash in circulation and reflects, for the most part, legal transactions in a highly dollarized economy. The analysis indicates that the cash economy has increased in size from 26.2 percent in 2021 to 45.7 percent of GDP in 2022. The bulk of the increase in the size of the cash economy in 2022 (vis-à-vis 2021) can be ascribed to a slowdown in capital flight and a decrease in GDP in US$ - a denominator effect. In the absence of adequate reforms and crisis resolution measures, a growing cash economy is a major impediment to Lebanon's economic recovery, as it has adverse implications on conducting fiscal and monetary policy, significantly heightens the risks of money laundering, increases informality, and facilitates tax evasion.

Background and Rationale

In the wake of Lebanon's unprecedented financial crisis, a cash economy has come to gradually replace the banking sector. Indeed, the bulk of financial transactions are settled in cash and lines of credit offered by the banking sector are fully cash-collateralized.

Sizing the cash economy is essential to understanding the evolving nature of transactions and assessing the potential implications of a pervasive cash economy on the conduct of fiscal and monetary policy. A growing cash economy implies that fiscal policy is less potent. On the one hand, a pervasive cash economy would be detrimental for tax buoyancy and effort. On the other hand, the cash economy creates incentives for tax avoidance. Further, the prevalence of cash transactions complicates the conduct of monetary policy given that the conduit for maintaining a nominal anchor and exchange rate stability is the banking sector. Because the cash economy replaces banking transactions, monetary policy will also become less effective.

The root cause of a pervasive cash economy is the loss of confidence in the insolvent banking sector. Unlike other countries, where cash transactions are mostly driven by tax avoidance (or in which cash may have originated from illegal activities), the cash economy in Lebanon reflects a loss of confidence in an insolvent banking sector. This reality has implications on measuring the size of the cash economy, as contrary to other countries, cash transactions are part and parcel of both illicit and informal activities as well as the majority of transactions in the formal (i.e., legal) economy.

Measuring the Size of the Cash Economy

The US$ cash economy is defined as total US$ cash in circulation. For the period 2020 to 2022, the US$ cash in circulation (a flow variable) is estimated. In that sense, the cash economy in Lebanon refers to, for the most part, legal transactions occurring in a highly dollarized economy.

Empirical methodologies to estimate the size of the legal cash economy can be classified into direct and indirect approaches (Medina and Schneider, 2018; Schneider and Buehn, 2018)**.**[27] The indirect approaches proxy for the size of the cash economy using the discrepancy between national expenditures and income as well as the difference between the official and actual labor forces. In addition, the transaction, currency demand and multiple indicators, multiple causes approaches offer an indirect method to measure the size of the cash economy. The direct approaches rely on surveys of company managers and labor markets to gauge the size of the cash economy. The data limitations in Lebanon constrain the use of the econometric techniques that may be useful to gauge the size of the cash economy.

Nonetheless, the discrepancy between the income and expenditure sides of the national accounts can be used to establish a lower bound on the size of the legal cash economy in Lebanon for 2020:

Starting from the identities of the national accounts, Gross National Income (GNI) is:

$$GNI = GDP + NFI$$

where NFI is net factor income from abroad. Gross National Disposable Income (GNDI) is:

$$GNDI = GNI + TR,$$

where TR are net transfers from abroad.

Prior to 2020, the difference between GDP from the expenditures side and GNDI published by Central Administration of Statistics (CAS), peaked at US$2.8 billion in 2015.[28] In 2020, the difference between GNDI and GDP stood at US$4.5 billion. The size of the cash economy is estimated as the difference between GNDI and GDP in both years. Following the indirect approach, this provides a lower bound for the size of the cash economy in 2020.

Owing to the lack of national accounts and other data that can be helpful in estimating the size of the cash economy in 2021 and 2022, the methodology of Pickhardt and Sarda (2012),[29] which the authors propound to circumvent the difficulties associated with estimating the size of the cash economy econometrically, is adapted to Lebanon's unique case.[30]

For 2021–2022, measuring the size of the US$ cash economy requires identification and accounting for the different sources of cash in US$. Six sources of US$ cash in circulation are identified. These are: (i) withdrawals of pre-crisis foreign currency denominated deposits, and BdL foreign exchange (FX) interventions from remaining reserves, including through the Sayrafa platform, as dictated by various BdL circulars; (ii) US$ remittances from abroad; (iii) US$ cash hoarded at homes since the onset of the financial crisis; (iv) US$ cash entering via official and unofficial entry points; (v) humanitarian

[27] Medina, L., & Schneider, F., (2018). Shadow economies around the world: What did we learn over the last 20 years?, IMF working paper, WP/18/17, Washington DC. Schneider, F., & Buehn, A. (2018). Shadow economy: Estimation methods, problems, results and open questions. *Open Economics*, 1(1), 1–29.

[28] More specifically, the difference between GNDI and GDP stood at US$ 1.38, 1.78, 1.63, 1, 0.25 and 1.56 billion in 2013, 2014, 2016, 2017, 2018 and 2019, respectively.

[29] Pickhardt, M., & Sardà, J. (2011). Cash, hoarding and the underground economy, Discussion Paper No. 56, Centrum für angewandte Wirtschaftsforschung Münster (CAWM), Universität Münster.

[30] Pickhardt and Sarda (2012) argue that their proposed method accounts for cash hoarding which may arise because of "fundamental distrust in the banking system". As such, their approach would be the most relevant to Lebanon.

and development cash assistance provided by international organizations (including to refugee communities); and (vi) post-crisis bank deposits in US$, i.e "fresh" US$ deposits that are not subject to the bank-imposed informal capital controls (i.e., restrictions on withdrawals and international transfers.); fresh US$ deposits mostly consist of salaries and international transfers that are assumed, for the most part, to be accessible quickly and withdrawn by depositors.

Gauging the size of the cash economy in Lebanon for 2021-2022 presents several challenges. First, data on the exceptional cash withdrawals in foreign currency since the issuance of basic circular 158 on June 8, 2021, are not available. Second, while the total volume of transactions on Sayrafa is available, more granular data on buy and sell transactions are not. Third, estimates of cash hoarding at homes or cash being brought in by individuals via official or unofficial border crossings are highly speculative and subject to considerable uncertainty.

Several assumptions are required to estimate the size of the cash economy in 2021 and 2022. These include:

1. Currency in circulation is exchanged into US$ at the prevailing banknote rate (BNR) for precautionary demand motives. As the national currency has lost its function as a store of value (and, to a certain extent, as a medium of exchange), it is assumed that, in an economy undergoing rapid dollarization, cash in LBP is immediately exchanged for US$ to preserve purchasing power.
2. The substantial (non-cash) deleveraging in the banking sector is accounted for by netting out foreign currency claims/loans (both resident and non-resident) from foreign currency deposits.
3. The remainder (i.e., deposits that are net of loans) of the foreign currency deposits are either withdrawn according to circular 158 and channeled to the cash economy or withdrawn through discounted cheques and channeled to the cash economy. More specifically, according to information provided by the Banque du Liban (BdL), 120,000 accounts benefitted from circular 158 in the first three months following the issuance of circular 158 in 2021.[31] This amounts to US$ cash withdrawals of US$288 million.[32,33] The latter figure is netted out from the net-of-loans cumulative decrease in deposits over the period July to December 2021 and a discount rate of 30 percent is applied to the balance,[34] which effectively is assumed to be converted into US$ cash via discounted cheques. Further, the average discount rate of 30 percent is applied to net-of-loans deposits for the period January to June 2021.
4. Under the assumption that the same number of accounts benefited from the provisions of circular 158 in 2022 as in 2021; US$ cash withdrawals related to circular 158 are therefore estimated at US$576 million in 2022. A discount rate of 20 percent is applied to the balance of the net-of-loans deposits, effectively assuming that they are converted into US$ cash via discounted cheques.[35]
5. Remittances are assumed to flow directly into the cash economy (and are therefore not saved). As mentioned earlier, the unprecedented financial crisis has made Lebanon even more reliant on remittances to finance household consumption and

[31] https://www.bdl.gov.lb/news/index/8/251 and https://www.bdl.gov.lb/files/circulars/158_en.pdf.

[32] Circular 158, issued on June 8, 2021, allows depositors to withdraw US$800 on a monthly basis split between US$400 in US$ banknotes and US$400 in LBP at an exchange rate of 12,000 LBP/US$, which was amended to be 15,000 LBP/US$ as of February 1st, 2023. (Link)

[33] Those withdrawals are assumed to have taken place between July and December of 2021. The starting date of July for the withdrawals supposes that depositors require three weeks to comply with the stipulations of circular 158 and become eligible for withdrawals according to it. The withdrawals in US$ cash according to circular 158 is also assumed to only apply to resident deposits while non-resident deposits are converted into US$ cash via discounted cheques.

[34] The average cheque discount rate for 2021 is 30 percent (source: lebaenselira.org).

[35] It should be noted that the LBP portion of the withdrawals according to circular 158, and all withdrawals according to circular 151 would be reflected in currency in circulation.

the provision of necessities. Net remittances (i.e., remittance inflows minus outflows) obtained from BdL's data on the balance of payments is included.

6. The portion of the reserves that is injected into the economy is computed as the change in reserves that are net of essential subsidies (i.e., wheat, fuel and chronic medication). That is, for both years (2021 and 2022), the portion of reserves that is used to import essential goods is netted out, as these funds are not channeled to the cash economy. As no granular data on Sayrafa transactions exist, it is assumed that the net reserves includes both FX interventions of BdL in the market and via the Sayrafa platform. Withdrawals in cash US$ are also netted out in accordance with circular 158 from BdL's remaining reserves (article 5 of circular 158) to avoid double counting.
7. Non-Lebanese tourists bring in cash that must be accounted for as part of the cash economy. Lebanese tourists are assumed to be withdrawing from their bank accounts (or exchanging dollars, which would appear in currency in circulation). Spending of non-Lebanese tourists is measured by multiplying non-Lebanese tourist spending in 2020 by the year-on-year growth in tourist spending as obtained from BLOMINVEST's BRITE database.
8. In principle, the portion of "fresh" US$ deposits (i.e., that are not subject to the ad-hoc capital control imposed by the banks or post-2019 US$ deposits) which is withdrawn must be accounted for. However, the data provided by BdL does not include a delineation between pre-crisis and fresh US$ deposits. Further, the size of fresh deposits making their way into the cash economy is likely to be small relative to the above-mentioned sources. Therefore, the latter are not included in the computations.
9. Humanitarian and development cash assistance disbursed in US$ to refugee communities and Lebanese poor households are estimated at US$127.8 million in 2021 and US$340 million in 2022.[36]
10. Net errors and omissions of the balance of payments for 2021 are assumed to be indicative of capital flight and are thus deducted from the US$ cash economy for that year.[37] Although admittedly an imperfect proxy for capital flows, the existing studies (IMF, 2019; Bank of Iceland, 2005)[38] suggest that an increase in net errors and omissions is indicative of capital outflows.

Building on these assumptions, the size of the cash economy for both 2021 and 2022 is estimated as:

$$\Sigma_{t=0}^{T} \Delta C_t + \Sigma_{t=0}^{T} D_t + REM_T + \Sigma_{t=0}^{T} \Delta R_t + HA_T + TS_T - CF_T,$$

where C_T is currency in circulation in US$ in month t, computed by dividing currency in circulation by the BNR, C_0 is currency in circulation in US$ in the base period, D_T are net-of-loans foreign currency (resident and non-resident) deposits that are converted into US$[39] and REM_T are net remittances at year end, R_t and R_0 are, respectively, net-of-essential subsidies foreign currency reserves at the BdL in month t and the base period, HA_T is humanitarian assistance in cash US$ at year end, CF_T denotes capital flight at

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36 The estimates are derived from various humanitarian and development programs across different response frameworks in Lebanon, namely: Lebanon Crisis Response Plan (LCRP), 3RF, the UN Emergency Response Plan (ERP), and cash programs under other frameworks. The estimates also include cash assistance provided to Lebanese households as part of the World Bank financed Emergency Social Safety Net Program (ESSN) for 2022. The estimates only include those programs disbursing cash assistance in US$; cash assistance disbursed in LBP is assumed to be included in currency in circulation.

37 Capital flight in 2022 is likely to be negligible. Our method for establishing a lower bound for 2020 accounts for capital outflows.

38 Bank of Iceland (2005). Monetary Bulletin, 2005–3. A Quarterly Publication of the Central Bank of Iceland. International Monetary Fund (2019). Analysis of net errors and omissions. Thirty-Second Meeting of the IMF Committee on Balance of Payments Statistics, Thimphu, Bhutan.

39 The dollarization rate of deposits exceeded 80 and 77 percent in 2021 and 2022, respectively. Hence, foreign currency deposits account for the bulk of the deposit base. It is assumed that the withdrawals in local currency deposits will be reflected in currency in circulation.

TABLE 2 • Breakdown of the Components of the Cash Economy in 2021 and 2022

	2021	2022
US$ Cash from Deposit Withdrawals (US$ Billion)		
Resident Deposits Minus Claims in Foreign Currency	0.734	0.634
Non-Resident Deposits Minus Claims in Foreign Currency	0.523	0.185
	1.261	**0.819**
Other Sources of US$ Cash (US$ Billion)		
Currency In Circulation	0.926	0.809
Net Remittances	4.25	4.53
Change In Reserves Net of Essential Imports	1.81	2.18
Tourist Spending	1.46	1.18
Humanitarian Assistance	0.12	0.34
Capital Flight	(3.77)	0
Total *(US$ billion)*	**6.06**	**9.86**

TABLE 3 • Size of the Cash Economy

Year	Estimated Size of the Cash Economy	Percent of GDP
2020	US$ 4.5 billion (lower bound)	14.2%
2021	US$ 6.06 billion	26.2%
2022	US$ 9.86 billion	45.7%

year end and TS_T is an estimate of non-Lebanese tourist spending at year end. The base period for the computations (t=0) is December of the previous year.

Abstracting from the cash inflows via official and unofficial points of entry, the latter computation provides an approximation for the size of the cash economy.

Table 2 provides a detailed breakdown of the components of the cash economy for 2021 and 2022.

Table 3 provides a summary of the estimates size of the economy in 2020, 2021 and 2022 in nominal US$ terms and as a percent of GDP in US$.

Conclusion

The cash economy increased in size in 2021 and 2022, albeit the year-on-year increase in the size of the cash economy is larger in 2022 than in 2021. Based on the nominal GDP projections, the size of the cash economy stood at 26.2 percent and 45.7 percent of GDP in 2021 and 2022, respectively. The bulk of the increase in the size of the cash economy in 2022 (vis-à-vis 2021) can be ascribed to a slowdown in capital flight. In fact, BoP data for H1-2022 show that, for the very first time since the onset of the crisis, net errors and omissions are close to zero. Therefore, the assumption that most of the capital flight occurred in 2020 and 2021 is plausible, particularly that 2022 generally witnessed tighter informal controls. The size of the cash economy relative to GDP is also noticeably larger in 2022 than 2021 owing to the decrease in GDP—a denominator effect.

It is important to underscore that the cash economy is not a net contributor to growth. In fact, transactions in the cash economy are reflected in GDP. That is, while the nature of settling transactions did change since the onset of the crisis, this change does not prop up economic growth.

The prevalence of cash transactions significantly heightens the risk of money laundering, increases informality, and creates space for further tax evasion. An increasing reliance on cash transactions threatens to completely reverse the progress that Lebanon made towards enhancing its financial integrity by instituting robust anti-money laundering controls in its commercial banking sector (IMF, 2017) before the current crisis.[40] Cash economies make it easier to conceal the source of funds for illicit and illegal activities. Cash economies also incentivize informality by small and micro businesses, lower productivity due to the absence of economies of scale and will likely compound longstanding weaknesses in Lebanon's tax code as they pertain to property, capital gains and income taxes (IMF, 2023).[41] Cash transactions exacerbate the distortions in the lump sum regime for business profits and facilitate tax evasion. This, in turn, erodes the tax base and diminishes tax buoyancy, effort and compliance.

[40] International Monetary Fund (2017). Lebanon: Financial System Stability Assessment, IMF Country Report No. 17/21, Washington DC.

[41] International Monetary Fund (2023). Lebanon: Technical Assistance on Putting Tax Policy Back on Track, IMF Country Report No. 23/8, Washington DC.

ANNEX I. FEW WINNERS, MANY LOSERS

Equitable & Comprehensive Macroeconomic Stabilization Plan Pillars	Expected Outcome	Substitute Ongoing Crisis Resolution Measures	Winners and Losers	
I. Exchange Rate and Monetary Policy				
New Exchange Rate & Monetary Framework: Gradual free floating of the exchange rate, unified exchange rate & a new monetary policy with clear objectives of reducing inflation.	1. Preservation of BDL remaining usable FX reserves	**1. Multiple Exchange Rate system put in place:** A. Creates arbtirage opportunities & encourages speculative activities B. Prompts huge distortions and losses C. Depletes remaining FX reserves as BDL intervenes unsustainably to prop up the currency	**Winners:**	Financial sector that benefits from lower than market value withdrawal exchange rates of pre-crisis deposits-regressive deleveraging schemes-to dissolve financial losses
	2. Correction of real exchange rate misalignment	**2. Creation of a Sayrafa Platform managed by BDL as main vehicle of intervention in the FX market:** No granular data on buy & sell transactions, and exchange rate setting-platform became a vehicle for arbitrage profits and public wage subsidization.		Exchange Rate Bureaus, money exchangers & speculators (especially those with inside information on monetary policy)
	3. Current Account Deficit on a structurally sustainable path	**3. Distortionary & regressive subsidy scheme for crucial imports (2020–2021)***		Smugglers, business & individuals with access to subsidized exchange rates earning higher profits Heavily Indebted businesses & individuals who repaid their FX loans at the former pegged exchange rate (substantive decrease in the real value of their debt)
	4. Medium-term improvement of competitiveness, boosts production & Exports		**Losers:**	Bussinesses with lack of access to credit; Industries (due to hindered competitiveness); Small and medium sized depositors. The bulk of Lebanon's residents, as they grapple with a multiple exchange rate system
Adoption of Formal Capital Controls	A vehicle that would have limited capital outflows, and sustained foreign currency in the country in defense of the exchange rate, and in preservation of Central Bank FX reserves.	**Informal Capital Controls,** prompting unequal treatment across depositors and select individuals/entities ability to engage in capital flight.	**Winners:**	Individuals, elites, corporations, shareholders with influence and power, who were able to engage in capital flight
			Losers:	The bulk of the depositors-the more capital flight, the less FX resources there is to protect small and medium sized depositors
Full Assessment of the financial position of BDL	Restores the Central Banks capital, and ensures ability to conduct effective monetary policy moving forward.	**Political decision to hinder audits at BDL** resulting in the lack of transparency in financial sector losses in BDL balance sheet	**Winners:**	Powerful political and economic elites with vested interests in prohibiting a comprehensive bank restructuring strategy, and BdL restructuring/governance reform.
Governance Reforms in BDL-strengthening financial sector supervision and control (including AML/CFT regime)	Strengthening AML/CFT Frameworks to enhance transparency & accountability	**No reform-**governing through ad-hoc BDL circulars.	**Losers:**	All depositors, and the majority of the local labor force struggling with daily erosion of purchasing power as a result of an ensuing inflation-depreciation spiral. SMEs, businesses adversely affected by the lack of capital markets and financial stability.

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Equitable & Comprehensive Macroeconomic Stabilization Plan Pillars	Expected Outcome	Substitute Ongoing Crisis Resolution Measures	Winners and Losers	
Enhance Macroprudential Policy and Regulatory Oversight in the Financial Sector	Delineate financial sector regulatory oversight responsibilities and segregate, to the extent possible, regulatory oversight from the conduct of monetary policy-to foster financial stability and the use of capital markets.	The main financial regulatory oversight responsibilities remain with the Banking Control Comission, the Special Investigation Committee and the Capital Markets Authority-all three are overseeen by BdL's governor.		
II. Public Debt Sustainability				
Implementation of a Public Debt Restructuring Strategy (for both domestic debt (treasury bills) & foreign debt (eurobonds, that requires negotiations with foreign investors)	Restores debt sustainability & Instills Credibility	**Unstructured default on foreign debt (eurobonds);** Commercial banks who held the majority of the eurobond porfolio, sold off holdings to foreign investors & vulture funds giving foreign creditors more leverage in the restructuring discussions as they effectively hold a blocking stake and may file potential lawsuits against the Lebanese state that may take years to resolve.**	**Winners:**	Commercial banks who sold their eurobond portfolios, vulture funds abroad.
	Lebanon reaccesses international financial markets in the medium-term	**Continued payments of interest on domestic debt (treasury bonds) to commmerical banks-**interest payments often financed through monetization.	**Losers:**	Rest of the population, that is subject to possible litigation, is axed from financial markets, and is faced with zombie banks. Vulnerable and Poor families disproportionally affected as monetization of debt servicing is inflationary, and inflation is a regressive tax.
III. Financial Sector Comprehensive Restructuring				
Adoption and Implementation of a Bank restructuring strategy that: (i) addresses upfront the balance sheet impairments & financial losses, (ii) restores liquidity, and (iii) adheres to sound global practices of bail-in solutions based on a hierarchy of creditors (starting with banks' shareholders); **Strategy to be supported by an effective bank resolution framework**	Restoration of banking sector solvency, that is pivotal for recovery and sustainable economic growth Protection of small and medium depositors, in dollars and in cash	**Socializing of Financial Losses:** Instilling a pre-crisis deposit lirafication scheme (financial sector regressive deleveraging) that has disproportionally burdened small and medium depositors and implied haircuts on deposits reaching 80 percent. **Monetization to finance withdrawal scheme prompting an unwavering Inflation-Depreciation Spiral** (increase in currency in circulation, that has an inflationary-depreciation impact)	**Winners:**	1. Financial sector that benefits from lower than market value withdrawal exchange rates of pre-crisis deposits-to dissolve financial losses 2. Bank Shareholders whose capital was not wiped out based on a hierarchy of creditors (best practice) 3. Big Depositors, bank shareholders, and powerful elites that have vested interest in recourse to public assets to cover (even if not viable) financial losses.
Initiation of an externally assisted bank-by-bank evaluation for the 14 largest banks to inform banking sector restructuring	Identification of financial losses per bank, to support mergers, acquisitions, and liquidations	**Severe delay in bank by bank audits, in the context of Zombie Banks**		
Recapitalization of Viable Banks	Inject fresh capital, bail-in solutions			

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Equitable & Comprehensive Macroeconomic Stabilization Plan Pillars	Expected Outcome	Substitute Ongoing Crisis Resolution Measures	Winners and Losers
Limit any recourse to public assets and resources	Fostering equitable burden sharing, preserving shared resources for generations to come	The pending bank restructuring strategy includes the creation of a Deposit Recovery Fund (DRF). The DRF aims to compensate depositors by issuing bonds/securities that will be partly financed through banks' assets (such as Central Bank Certificate of Deposits), state assets, and potential future government revenues.	**Losers:** 1. Small and medium sized depositors who have endured 60–80 percent haircuts to their deposits as a result of the regressive deleveraging scheme. 2. The majority of the local labor force, pensioners, and retirees who have witnessed a severe erosion of purchasing power as a result of the inflation-depreciation spiral. 3. Generations of Lebanese citizens to come, who may be potentially rid of public goods and assets to recover financial losses. 4. SMEs, businesses, corporations,individuals who suffer from lack of financing in the banking sector (zombie banks)
Governance Reforms: strengthening the banking supervision, resolution and deposit insurance frameworks	Maintain a sound banking system and restore confidence in it.	Lack of any governance reforms, and changes to bank supervision governance.	
Reformed bank secrecy law to bring it in line with international standards	Fight corruption and remove impediments to effective banking sector restructuring and supervision, tax administration, as well as detection and investigation of financial crimes, and asset recovery.	Passing of amendments to the banking secrecy law by parliament in October 2022—amendments fell short of international standards, and several shortcomings still need to be overcome to ensure that the banking restructuring strategy has necessary safeguards.	
IV. Fiscal Reform			
Timely ratification of consecutive government budgets with immediate corrective revenue and spending measures	A. **Preservation of government revenues to provide basic public services,** through correct valuation of exchange rate in all revenue components & tax valuations B. **Preservation of public sector human capital, and avoiding state atrophy** through provision of immediate and sustainable financial support to crucial civil servants.	1. **Near complete collapse of public finances**, resulting in an acute collapse of public service provision. 2. **Ad-hoc and piecemeal measures on both the Expenditure and revenue side of government budget:** a. Financing fiscal deficit through monetization b. Ad-hoc temporary social assistance to civil servants (also partly financed through monetization) that fail to protect against erosion of purchasing power due to rampant inflation c. Misvaluation of VAT, customs, excises, and lack of correction for inflation in specific excises resulting in losses to revenues equivalent to 5.6 percent of GDP in 2022 (IMF, 2023).***	**Winners:** 1. Private providers of public services (private generators for example) 2. Political elite providing basic services in their areas strengthening clientelist networks
Medium-term Fiscal Strategy: Fiscal Consolidation Plan	**Achieves equitable economic adjustment and burden-sharing** (creates fiscal space for additional social and infrastructure spending while ensuring fiscal sustainability.) **Improves efficiency and effectiveness of public expenditure** and identifies possible avenues for spending prioritization and streamlining.		**Losers:** 1. Civil servants, pensioners, retirees, whose wages have been eaten up by inflation. 2. The entirety of the Lebanese population (and consecutive generations) as a result of state atrophy and collapse of public services.

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Equitable & Comprehensive Macroeconomic Stabilization Plan Pillars	Expected Outcome	Substitute Ongoing Crisis Resolution Measures	Winners and Losers	
Expenditures Side-Medium Term Reforms: a. Public Sector Census to target wage bill reduction b. Pension Reform c. Tackling NSSF Arrears d. Reforming Transfers to SOEs e. Creating fiscal space for Social Safety Nets f. Support public procurement	• Potential savings identified through Public Sector reform, consistent with the effective delivery of Public services • Complete review of pension and retirement schemes for civil servants and private employees • Developing rules and procedures for new procurement methods			
Revenues Side-Medium Term Reforms: a. Broadening Tax Base b. Improving tax collection c. Abolishing tax exemptions (including property taxation) benefitting well-off individuals and corporations d. Reforming income tax	Moving towards a progressive tax system that offsets income and wealth inequality			
V. Governance & Sector Specific Reforms (top two reforms)				
Electricity Sector Reform	Restores electricity production, distribution, and tarrif collection. Electricity sector no longer a drag on Lebanon's public finances. Supports transition to renewable energy alternatives.	Rise of a 'generator economy' that is costly, pollutative, and unregulated.	**Winners:**	A largely unregulated private generator industry amassing substantive profits: the supply-demand gap allowed diesel generator owners to expand their subscription-based businesses, creating a complex informal economy that has been resistant to regulations and government oversight.
			Losers:	• Poor and vulnerable households rid of very basic access to electricity, and unable to afford private generators. • Most of Lebanon's residents grappling with skyhigh energy bills
Independence of the Judiciary	Protection of public funds, holding corrupt officials, organizations, and entities to account, and preserving citizen rights.	Consistent undermining of the principle of the seperation of powers (between the judiciary and executive branches) resulting in blocked lawsuits and cementing a culture of impunity and lack of accountability remains far from independent.	**Winners:**	Powerful Entities and individuals evading fair trials
			Losers:	The entirety of the Lebanese population whose rights are undermined by the lack of independence of the judiciary.

[a] Subsidy Reform Note.
[b] In 2019, out of $86 billion in government debt, only between 5–11% of total public debt was held by foreign entities; thus, domestic debt restructuring with commercial banks and BDL was a viable option prior to the Eurobond sell-off to foreign investors.
[c] Technical Assistance on Putting Tax Policy Back on Track, IMF.

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