



REPUBLIC OF LEBANON

MINISTRY OF FINANCE

COUNTRY PROFILE

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GENERAL BACKGROUND

Area and Population

According to a survey conducted by CAS, the number of Lebanon's permanent residents was estimated in June 1997 at 4,005,000, 92.4 per cent. of whom were Lebanese. This number does not include temporary residents such as migrant workers.

The following table shows the breakdown of population by age:

| | <u>Total</u> <i>(per cent.)</i> |
|------------------|------------------------------------|
| Under 20..... | 38.9 |
| 20-59..... | 51.2 |
| 60 and over..... | 9.9 |

Source: CAS—Conditions de Vie des Ménages en 1997—February 1998 (the "CAS Survey").

The population is composed of Christians, Muslims, and minorities and is Arabic speaking, with French and English being widely used. In the period 1975-1993, a decline in population of about 300,000 occurred, as a result of relocations mainly to North and South America, Europe, Africa, Australia and the Arabian Gulf States.

The main cities are Beirut, the capital, Tripoli, Sidon, Jounieh, Zahle and Tyre. Approximately 32 per cent. of the population lives in Beirut and its suburbs.

History

Overview

From 1516 to 1918 Lebanon was under the administrative rule and political sovereignty of the Ottoman Empire. In 1920, the territory defined by the present-day boundaries became a state called "Grand-Liban" (Greater Lebanon) by decree of General Gouraud, head of the French troops in the Levant. The state remained under French Mandate until November 26, 1941. A constitution was adopted on May 25, 1926 establishing a democratic republic with a parliamentary system of government. Effective political independence of the Republic occurred on November 22, 1943 (Independence Day). In 1945 Lebanon became a founding member of the League of Arab States, then of the United Nations. Departure of the foreign troops then on the Republic's territory was completed on December 31, 1946.

Over the next 30 years, Lebanon became a melting pot with a diverse cultural heritage. The instability in surrounding countries caused Lebanon to experience large waves of immigration from neighboring countries and attracted thousands of skilled laborers, entrepreneurs and intellectuals. The economic force of the Republic has mainly revolved around its entrepreneurs. In addition, Lebanon's democratic traditions, its attachment to freedom of speech and expression and its educated population enabled the Republic to become the cultural, academic and medical center of the region.

A combination of internal and external factors led to the outbreak of conflict in 1975. The regional instability and conflicting relations between neighboring countries contributed to destabilizing the domestic political and economic situation. Successive rounds of fighting took place, aggravated by two Israeli military invasions in 1978 and 1982. The period of conflict witnessed a significant reduction of government authority, large losses in human lives, substantial physical and infrastructure damage and a considerable emigration of skilled labor from the country.

In the aftermath of the Taif Reconciliation Accord (the "*Taif Agreement*") signed in Saudi Arabia in 1989, military hostilities effectively came to an end in October 1990. President Elias Hrawi assumed office with Dr. Salim Al Hoss as Prime Minister. In 1992 Mr Rafik Hariri was appointed as Prime Minister and the first parliamentary elections in 20 years were held. In 1995, President Hrawi's term of office was extended for an additional three year period, after a constitutional amendment.

In October 1998, General Emile Lahoud was elected President and appointed Dr. Salim Al Hoss as Prime Minister. Parliamentary elections were held in Lebanon on August 27, 2000 and September 3, 2000 and, in accordance with the Constitution, mandatory consultations between the President and members of Parliament regarding the designation of the Prime Minister took place in October 2000, following parliamentary elections. 106

members of Parliament designated Mr. Hariri as their choice for Prime Minister and the President thereafter appointed Mr. Hariri as Prime Minister. Following consultations between Mr. Hariri and members of Parliament, a new Government was formed in October 2000.

Israeli Occupation

An armistice agreement was signed between the Republic and Israel in 1949. The agreement governs the security issues related to the southern border. However, since then Israeli attacks on Lebanese territory persisted, culminating in several Israeli invasions of the Republic's territory.

In 1978, Israel invaded the southern part of Lebanon and declared that part of the country a security zone for its border. In 1982, Israel invaded Lebanon up to and including Beirut. The United States, France, Italy and the United Kingdom sent a multi-national force to provide security while Israel pulled back and Palestinian forces left for Tunis. The multi-national force left Lebanon in 1984. Israel partially withdrew from central Lebanon in 1984 and 1985 but enlarged its occupation of the southern part of the country up to the area of Jezzine.

On April 11, 1996, June 24, 1999, February 7, 2000, and May 5, 2000, Israeli military aircraft attacked southern Lebanon and several power stations and bridges near Beirut.

On May 24, 2000, Israel withdrew its troops from territory in southern Lebanon, which it had been occupying since 1978, in fulfillment of United Nations Resolution 425 which was passed by the Security Council in 1978, following the first Israeli invasion of Lebanese territory. The Government is reasserting its authority over that territory. Several issues relating to the withdrawal remain unsettled: an issue concerns certain villages and adjacent land on the eastern side of Alsheikh Mountain, known as the "Shebaa Farms", which have been occupied by Israel since 1967. The Government advised the United Nations that it considers the area to be Lebanese territory and that, as such, the withdrawal must encompass it. Other issues relate to minor disagreements regarding border delineation and to the release of Lebanese nationals held in Israeli jails.

There exists a United Nations Interim Force in Lebanon (UNIFIL) of approximately 4,500 personnel deployed in southern Lebanon with a mandate to help the Lebanese Government restore security after the Israeli withdrawal requested in Resolution by 425 by the Security Council.

A preliminary conference on the reconstruction of southern Lebanon was held in Lebanon on July 27, 2000 and was attended by representatives of a large number of countries, multilateral financial institutions (including the World Bank and European Investment Bank), United Nations agencies (including the United Nations Development Program and ESCWA) and Arab funding agencies. The principal objective of the conference was to secure funding and other assistance (including grants, loans and technical assistance) to cover medium and long-term development projects in southern Lebanon. Following the preliminary conference, the Government received grants from various Arab countries in an aggregate amount of U.S. \$148 million.

Constitutional System

Three laws have governed the constitutional system of the Parliamentary democracy. The first was promulgated in 1926, the second in 1943 and the third in 1990, following the Taif Agreement.

The Constitution of September 21, 1990 (the "*Constitution*") amended the 1926 Constitution and reiterates the principle that the Republic is an independent, united and internationally acknowledged sovereign state. It also confirms the Republic's Arab identity and involvement in both the Arab League and the United Nations, as a founding and active member. Furthermore, the Constitution emphasizes the respect for freedom of speech and belief and the Republic's commitment to human rights and parliamentary democracy, private ownership, free market economics and balanced regional development and emphasizes the firm support for peaceful co-habitation between the various religious communities.

The Republic's political system is based on the separation of executive, legislative and judicial powers and a system of checks and balances. The Government determines overall policy, appoints senior administrators and submits proposed legislation to Parliament. Parliament, which is elected every four years, proposes and adopts laws and supervises government policy. Judicial power is fully vested in the courts and is autonomous.

The Taif Agreement provided the framework for a two-stage process of political reform. The first stage resulted in improving the distribution of political power among representatives of the various religious communities:

seats in Parliament are equally divided between Christian and Muslim communities and the powers of the Council of Ministers and of Parliament have been reinforced. The second stage calls for the elimination of the sectarian political system.

The Executive Branch consists of the President of the Republic and the Council of Ministers (the Cabinet). The President, currently Emile Lahoud, is the Head of State. The President is elected for a six-year term by a two-thirds majority of Parliament in the first voting round and by a simple majority if a subsequent round is required. The President appoints the Prime Minister, currently Mr. Rafik Hariri, following consultations with Parliament. The President must appoint the prime ministerial candidate who has the greatest level of support in Parliament. The Legislative Branch consists of a single-chamber Parliament of 128 members. Members are elected for four-year terms in regional ballots, with the number of members for each region determined on the basis of the size and population of each region, subject to an overall number of members for each religious community. Parliament may be dissolved by the Council of Ministers, acting by vote of a two-thirds majority of the Ministers, upon request of the President of the Republic only on the basis of one of the following grounds:

- if the Parliament fails to meet during one ordinary session or two extraordinary sessions (except in the event of *force majeure*); or
- if the Parliament fails to pass a budget law.

The court system consists of one administrative court, the State Council Court ("*Conseil d'Etat*") and civil courts (which include commercial courts and criminal courts). The Supreme Court is the highest court of appeal for civil and commercial matters. Constitutional matters and conflicts relating to elections are referred to the Constitutional Council discussed above. The judges of the various courts (excluding certain members of the Constitutional Council) are appointed by the Government after favorable recommendation of the Supreme Council of Justice.

Elections

The term of office of the former President, Elias Hrawi, came to an end in November 1995. Under the Constitution, President Hrawi could not be re-elected at the expiration of his initial term in November 1995. However, in October 1995, Parliament approved an amendment to the Constitution permitting a one-time extension of the presidential term for three years. Presidential elections took place in October 1998 and Emile Lahoud, the then Commander in Chief of the Army, was elected President. His election was preceded by a constitutional amendment approved by Parliament granting a one-time exemption to certain civil servants from the requirement of being out of service for at least two years prior to election to public office.

Parliamentary elections took place in 1992, 1996, and 2000, the last one resulting in the election of 128 members of Parliament of whom 45 are new members. The 1992 parliamentary elections were the first such elections in Lebanon since 1972. In May and June 1998, municipal elections took place for the first time since 1963. All political parties participated. There are 624 municipal councils with a total of 7,401 elected members.

Legal System

The Republic's legal framework is based on the Constitution and on a body of well-established laws, dating back to 1930. The Constitution and the laws thereunder guarantee the private ownership of property, the free flow of funds and currencies in and out of the country and the freedom of contract between parties (so long as contracts do not contravene public policy).

Lebanese civil law is mostly based on the Code of Obligations and Contracts (which is based on the French Civil Code and was promulgated in 1932) and the Land Ownership Law. Other major legislation includes the Commercial Code (promulgated in 1942), the Code of Money and Credit (promulgated in 1963) and the complementary legislative decrees (issued in 1967) related to commercial agency representation, stock exchange, limited liability companies and business concerns and the New Code of Civil Procedure (promulgated in 1983).

An active legislative reform movement is taking place both in Parliament and through special committees formed by the Central Bank and the Ministry of Justice to modernize Lebanese law following the end of the period of conflict. Significant laws and regulations have been adopted in various areas, including a law authorizing and regulating fiduciary activities, a law regulating the issuance of bonds and other debt securities by banks and

authorizing the public placement and listing of shares representing up to 30 per cent. of a bank's capital, and a regulation by the Central Bank relating to the activities of financial intermediaries.

International Relations

Lebanon is a founding member of the United Nations and the League of Arab States and is a member of all international organizations under the auspices of the United Nations (United Nations Educational, Scientific and Cultural Organization, Food and Agriculture Organization, International Fund for Agricultural Development and others), the International Bank for Reconstruction and Development (the "*World Bank*"), (and its affiliates, the International Finance Corporation and the Multilateral Investment Guaranty Agency), the International Monetary Fund and the International Development Association.

The Republic maintains diplomatic relations with 86 countries and has 80 diplomatic and consular missions abroad. It hosts a similar number of missions in its territory. The Republic also hosts international organizations such as the United Nations Regional Office for Education, Science and Culture in the Arab Countries, the United Nations Commission for Refugees, Food and Agriculture Office of the United Nations, the World Health Organization, the United Nations Fund for Childhood, United Nations Development Program and the Arab Center for Legal and Judicial Research affiliated to the Arab League. The Economic and Social Commission for Western Asia (ESCWA), an agency of the United Nations, relocated its headquarters to Beirut in October, 1997 and the World Bank opened an office in Beirut in January, 2000.

The Republic's policy is to co-exist in peace and harmony with all its neighbors within the context of a comprehensive, just and lasting peace settlement in the Middle East.

The Republic has a long tradition of openness to the international community with close ties to the Arab world, Europe and America. The Government is implementing a comprehensive strategy for trade liberalization. The Republic is committed to democratic principles.

The Republic has entered into free trade agreements with Syria, Egypt, Kuwait and the United Arab Emirates. In addition, in February 1988, an agreement was entered into between Lebanon and Syria pursuant to which tariffs on industrial goods are being reduced by 25 per cent. per year, commencing in January, 1999. A similar agreement for the reduction of tariffs on agricultural goods was entered into in September, 1999 pursuant to which tariffs have been reduced by 50 per cent. effective November, 1999, with an annual reduction of ten per cent. over a period of five years. The Republic is also a party to the Arab Free Trade Agreement and, effective January 1, 1998, tariffs on certain goods are being reduced by 10 per cent. annually among 14 Arab countries.

Since 1992, the Republic has entered into, or initialed, a number of treaties for the promotion and protection of investments and the avoidance of double taxation. Treaties for the promotion and protection of investments have been signed with each of Armenia, Azerbaijan, Benelux, Bulgaria, Canada, Chile, China, Cuba, Czech Republic, Egypt, Finland, France, Germany, Greece, Iran, Italy, Malaysia, Morocco, OPEC Fund, Pakistan, Romania, Russia, Spain, Switzerland, Syria, Tunisia, United Arab Emirates, United Kingdom, Ukraine, and Yemen. Similar treaties have been initialed with each of Austria, Bahrain, Hungary, Indonesia, Kuwait, Netherlands, Poland, Qatar, Oman, and Sweden. Treaties for the avoidance of double taxation have been signed with fifteen countries, and initialed with an additional fifteen countries.

The Republic has applied for membership in the World Trade Organization (WTO) and was granted observer status in April, 1999.

The Republic is currently negotiating a partnership agreement with the European Union ("*EU*"), as part of the EU's Euro-Mediterranean partnership framework. The EU is one of the Republic's major trading partners.

THE ECONOMY

Economic System

Lebanon has a long tradition of domestic free trade and investment policies, with free market pricing for most goods and services, an unrestricted exchange and trade system and extensive links with the developed world in practically all economic activities. The Government has maintained a generally non-interventionist stance toward private investment, and public ownership has generally been limited to infrastructure and utilities. There are no restrictions on the movement of capital and goods by residents and non-residents of the Republic, including on entry or exit of firms or on access to foreign exchange, which makes Lebanon a supportive system for private sector development.

The Government continues to favor a strong role for the private sector in a liberal policy environment. It welcomes foreign investment in the economy. There are no legal restrictions on setting up and operating private businesses in Lebanon, subject to limited exceptions (See "External Sector—Foreign Direct Investment"). Investment in infrastructure activities historically has been undertaken by the public sector. The absence of exchange controls in Lebanon allows foreign investors freely to import and export capital in any form they wish.

The Lebanese economy, characterized by freedom of exchange and transfers, is based on private initiative. The private sector is estimated by CAS to contribute over 80 per cent. to aggregate demand and includes industries such as agriculture, manufacturing, construction, trade and tourism, in addition to services such as banking and finance, hotels and restaurants, media and advertising, and consulting and engineering. The manufacturing and industrial sectors are estimated by the CAS to contribute approximately one-fifth of the national income. They are provided only with a limited level of protection from international competition.

Recent Economic History

The Republic had developed into a prosperous, lower middle income country by the mid-1970s. Economic growth averaged 5 per cent. per year during the period 1960-1970 and then accelerated to 7 per cent. per year in the period 1970-1975. The main source of growth was the services sector, in particular, tourism, banking, insurance and free port activities. The banking sector, aided by a stable and liberal regime, a freely convertible currency, favorable regulations and skilled management, permitted Beirut to serve as a financial center to the Middle East. This environment allowed Lebanese entrepreneurial and financial skills to evolve to a high degree, and in the 1970s its bankers and traders enjoyed an excellent reputation in the region. Although smaller in size than the services sector, the export-oriented agricultural and manufacturing sectors also grew (at annual rates averaging between 4 per cent. and 6 per cent.), contributing to overall growth of income. Having grown at an average of 3 per cent. per annum since 1960, per capita gross national product ("GNP") was estimated at U.S. \$1,070 in 1974, just prior to the outbreak of the conflict in April 1975.

Estimates put the Republic's GNP per capita at about U.S. \$820 in 1990, barely one third of its 1975 level in real terms. Damage to infrastructure and physical assets due to the conflict amounted to U.S. \$25 billion, according to United Nations estimates, with none of the principal sectors emerging from the conflict unscathed. While limited investment and maintenance expenditure led to the erosion of the capital base, the sizeable emigration of skilled manpower constituted a major loss to the economic potential of Lebanon. As a result, from 1975 to 1990, aggregate national output steadily declined. In addition, the confidence in, and credibility of, the Lebanese Pound and economic stability began to erode. The shift in authority from the Government to non-official entities gave rise to a parallel economy that severely hampered the Government's ability to collect revenues as most trading was conducted through unofficial ports of entry. This dearth in Government revenue and the growing expenditure on public services led to large and rapidly growing Government budget deficits. These negative developments, along with the prevailing political uncertainty, plunged the Lebanese economy into a vicious cycle of large budget deficits leading to monetary expansion and inflation, which translated into dollarization of the economy and capital flight. This in turn led to a dramatic depreciation of the value of the Lebanese Pound and further inflation.

The cessation of hostilities was followed by a recovery in the economy in 1991; according to IMF estimates, GDP rose by almost 40 per cent. and inflation moderated in the course of the year. Large capital inflows, along with a partial recovery of exports, resulted in an overall balance of payments surplus of over U.S. \$1 billion. However, the fiscal deficit remained high in 1991 (56 per cent. of expenditures). At the start of 1992, public confidence in economic management was shaken by what was perceived as a weak budget incorporating, inter alia, large wage increases in the public sector and a large deficit. This led to economic stagnation with an intensification of inflationary pressures reflecting both exchange rate depreciation and the resort to central bank finance to cover the budget deficit. By the beginning of 1992, the Central Bank stopped supporting the Lebanese Pound, the value of which declined to all-time lows. The cycle of deficit financing, dollarization and capital outflows led to escalating inflation and exchange rate depreciation, with the value of the Lebanese Pound reaching LL 2,420 per U.S. Dollar in September 1992.

Following the appointment of the first Government led by Mr. Rafik Hariri in October 1992, there was a significant increase in confidence that allowed the Government to take measures to restore economic stability and renew confidence in the Lebanese Pound.

Between 1993 and 1998, the economic program of the successive Hariri Governments rested on the dual, and sometimes conflicting, tasks of economic revival and stabilization. This framework aimed to rehabilitate the country's damaged infrastructure, replenish the depleted capital stock, reinstate traditional public services, and implement programs for the return of displaced persons to their villages and provide a conducive environment for the return of the expatriate Lebanese community, while pursuing exchange rate stability and anti-inflationary

policies. This strategy has been successful to a certain extent. As the Government-led reconstruction program got underway and with the normalization of the economic environment, real economic growth averaged 5.7 per cent. over the period from 1992 to 1997. At the same time, the foreign exchange rate gradually appreciated, reaching LL 1,516 per U.S. Dollar at the end of 1998. The inflation rate was reduced from over 120 per cent. in 1992 to approximately three per cent. in 1998. Interest rates have gradually declined since 1995 but remained high. As at December 31, 1997, the budget deficit represented 23.48 per cent. of GDP. For the years ended December 31, 1998 and December 31, 1999, the budget deficit (excluding foreign financed expenditures of the Council for Development and Reconstruction ("*CDR*")) represented approximately 13.8 per cent. and 14.5 per cent., respectively, of GDP and debt service represented approximately 75 per cent. and 81 per cent., respectively, of total revenues. Net Public Debt (consisting of Net Domestic Debt and Public External Debt) represented approximately 105 per cent. of GDP as at December 31, 1998 and 120 per cent. of GDP as at December 31, 1999.

The previous Government headed by Dr. Al Hoss, which took office in December 1998, had continued to foster monetary stability. Inflation was further reduced to 0.25 per cent. in 1999, the foreign exchange rate remained stable and the balance of payments registered a surplus in 1999.

The balance of payments was in overall surplus during the period from 1993 to 1997, despite growing trade deficits. The balance of payments was U.S. \$1.13 billion in surplus for 1994. In 1995 and 1996, the balance of payments registered a surplus of U.S. \$256 million and U.S. \$786 million, respectively. In 1997, the balance of payments registered a surplus of U.S. \$420 million. However, the balance of payments registered a deficit of U.S. \$487 million for 1998. In 1999, the balance of payments registered a surplus of U.S. \$261 million.

Role of the Government in the Economy

Lebanon has a long and established tradition of having an open and free market economy. The state sector has traditionally been small, with the Government having a history of minimal intervention in economic activity.

For the first eight years of the conflict (until 1983/84) Government authority was still present, albeit in a much weaker form than before the conflict began, and some tax revenue was forthcoming. From 1983/84, the Government effectively lost control of all ports, and non-payment of direct taxes and bills to state-owned utilities became widespread, leading to a financing of current Government expenditure through money creation.

After the conflict, the Government continued the policy of reliance on private sector initiative, which had served the country well in the pre-conflict era. However, the Government has assumed a larger role than it has done historically by making substantial investments in infrastructure needed to create an environment conducive to long-term growth based on private sector activity. However, the various post-conflict governments have also been seeking to increase the private sector participation in infrastructure financing.

Privatisation

In May, 2000, Parliament adopted a privatization law, which sets the framework for the privatization of state owned enterprises. The privatisation policies are aimed at re-establishing the preeminence of the private sector as the main contributor to economic growth. The privatization law establishes a Higher Privatization Council and provides that the proceeds from privatization will be applied towards debt repayment. A law regulating the water sector, in anticipation for its privatization, was adopted by Parliament in May, 2000. Other sector laws relating to telecommunications and electricity are in the process of preparation by the Government and submission to Parliament. While the state sector in Lebanon does not account for a large portion of GDP (7.4 per cent. of GDP in 1995, excluding certain government agencies), it nevertheless includes several enterprises and types of assets which have been successfully privatized in other emerging markets. The Government owns Electricité du Liban (which supplies virtually all electricity in the Republic), Société des Eaux de Beyrouth and other water companies, the airport and port companies, the fixed-line telephone monopoly and other assets, many of which may be eligible for privatization. The Central Bank also owns significant commercial assets, including substantially all of the shares of the national air carrier, Middle East Airlines. With the exception of the sale in 1997 by the Central Bank of its shares in Credit Libanais S.A.L., a commercial bank, prior governments did not conduct sales of state-owned enterprises. The Government believes that privatization is likely to result in significant economic benefits, including a reduction in public debt levels, and a consequent decrease in the budget deficit, an increase in capital inflows, the acquisition of new technology and a broadening of domestic capital markets.

Gross Domestic Product

With the restoration of peace and stability, the GDP registered high growth rates for the period from 1993 to 1995, averaging an estimated real growth rate of 7.2 per cent. per annum. Real GDP grew at slower estimated rates of 4 per cent. in 1996 and 1997, 3 per cent. in 1998 and 1 per cent. in 1999.

The following table shows estimates of gross domestic product for the years 1995-1999:

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|--|-----------------------|--------|--------|--------|---------|
| GDP (at market prices) billions of LL..... | 18,028 ⁽¹⁾ | 20,417 | 22,880 | 24,509 | 24,816 |
| Exchange rate, LL per U.S. \$ (period average)..... | 1,621 | 1,571 | 1,539 | 1,516 | 1,507.5 |
| GDP (at market prices) million of U.S. Dollars ⁽¹⁾ | 11,122 | 12,996 | 14,867 | 16,167 | 16,462 |
| Growth of Real GDP..... | 6.5% | 4.0% | 4.0% | 3.0% | 1.00% |
| Growth of Nominal GDP..... | 17.8% | 13.2% | 12.1% | 7.1% | 1.27% |
| GDP Inflation..... | 10.6% | 8.8% | 7.8% | 4.0% | 0.25% |

Source: Ministry of Finance/Banque du Liban.

Note:

⁽¹⁾ The GDP figure as published by the CAS for 1995 was LL 17,775 billion. The CAS is in the process of calculating the GDP for subsequent years.

Principal Sectors of the Economy

At the end of the conflict, all sectors of the Republic's economy were characterized by widespread damage to physical assets and an obsolescence of remaining facilities, given the reluctance during the years of conflict to invest in new capital or spend funds on maintenance. In addition, there was an outflow of professional and entrepreneurial skills from Lebanon. A lower production capacity, together with rigidities in internal flows of goods and labor, led to very low levels of output.

The end of the conflict in 1990 marked the unification of the internal market and an upsurge in output in most sectors of the economy. Since then, there has been an increase in investment and a gradual return of skilled workers to the country. However, the economy suffered slow-downs in 1998 and 1999.

The following table sets forth selected indicators of economic activity in significant sectors:

Selected Indicators of Economic Activity

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|-----------------------|--------|--------|--------|--------|
| Industry | | | | | |
| Recorded Exports (million of U.S. Dollars)..... | | 919.5 | 513.0 | 715.9 | 676.8 |
| Electricity Production (million kwh)..... | 5,006 | 7,492 | 8,364 | 9,009 | 9,025 |
| Cement Production ('000 tons)..... | 3,968 | 3,812 | 3,654 | 3,514 | 2,970 |
| Construction | | | | | |
| Construction Permits..... | 48,076 ⁽¹⁾ | 17,433 | 17,787 | 15,060 | 14,349 |
| Area ('000 sq. meters)..... | 34,950 | 13,487 | 11,397 | 9,817 | 8,422 |
| Commerce | | | | | |
| Port of Beirut (no. of ships)..... | 3,429 | 3,279 | 3,117 | 2,892 | 2,796 |
| Beirut Airport(no. of passengers '000s)..... | 1,673 | 1,715 | 2,007 | 2,060 | 2,222 |
| Documentary Credits for Imports | | | | | |
| (million of U.S. Dollars)..... | 2,736 | 2,882 | 2,960 | 2,766 | 2,369 |

Source: Ministry of Finance/Banque du Liban.

Note:

(1) A sharp increase in construction permits in 1995 was to a large extent due to the regularization of previous construction violations.

Services

The Lebanese economy is based primarily on the service sector, which accounts for approximately 60 per cent. of GDP (down from approximately 70 per cent. in the 1970's). Major subsectors are commerce, tourism and financial services. Other components include health care and higher education.

Commerce

The Port of Beirut plays an important role in Lebanon's commercial activities. After World War II, Beirut became the most important Arab port on the Eastern Mediterranean serving the Arab world. A free-port area for re-exports added to Beirut's success. During the conflict, the Port of Beirut virtually closed down and related commerce ground to a halt.

Work has been completed on the reconstruction of the Duty Free Zone at the Port of Beirut to restore its pre-war capacity and a project for the rehabilitation and expansion of the Port of Beirut is underway.

The following table sets forth data concerning trade activity at Beirut Port for the years 1995-1999:

| Trade Activity at Beirut Port | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|-------------|-------------|-------------|-------------|-------------|
| No. of ships..... | 3,429 | 3,279 | 3,117 | 2,892 | 2,796 |
| Incoming freight ⁽¹⁾ | 6,368 | 5,859 | 5,612 | 5,283 | 5,248 |
| Outgoing freight ⁽¹⁾ | 306 | 285 | 270 | 279 | 307 |
| Freight in transit ⁽¹⁾ | 230 | 163 | 146 | 144 | 126 |

Source: Ministry of Finance/Banque du Liban.

Note:

(1) In thousands of metric tonnes.

Tourism

The strategic position of Lebanon, its mild climate and natural beauty, consisting of snow-capped mountains, valleys and the Mediterranean Sea, make it a natural tourist attraction. Apart from its privileged geographical and natural situation, Lebanon benefits from qualified and experienced human resources in the tourism industry.

Prior to the outbreak of the conflict, tourism (including hotels and restaurants) contributed approximately 20 per cent. to Lebanon's GDP. This is notable given that, at that time, the international tourism industry was not as developed as it is today.

Significant private investment is currently being made in the modernization and expansion of this sector and international hotel companies have returned to Lebanon. Casino du Liban, which historically constituted a major tourist destination, reopened in 1996. Lebanon is the only country in the Arab world that offers skiing and related winter sports activities. The largest ski resort in the country has been expanded and modernized. The Government believes that, because of the return of peace and stability to the country and with the development of the necessary infrastructure, tourism will again contribute significantly to Lebanon's economy. Lebanon's tourism industry also relies on the large number of Lebanese living abroad, who return regularly to the country during the summer season.

Financial Services

From the 1950s to the start of the conflict in 1975, Beirut was the region's financial services center. At the onset of the oil boom starting in the 1960s, Lebanon-based banks were the main recipients of the region's petrodollars.

Currently, the main financial services offered are commercial banking, investment banking and insurance. Despite the conflict and a crisis in the late 1980s involving a small number of banks, the commercial banking sector remains a centerpiece of the Republic's service-oriented economy. The Lebanese banking sector witnessed unprecedented growth during the period from 1992 to the present. Total deposits with commercial banks increased from U.S. \$6.5 billion at the end of 1992 to U.S. \$33.9 billion at the end of 1999. In addition, since 1996, Lebanese banks have been successfully accessing the international capital markets. Specifically, since 1996, several banks raised over U.S. \$2 billion on the international debt markets and three banks raised approximately U.S. \$300 million through the issuance of global depositary receipts on the international equity markets. The banking system is seen as having a key role by being the entry point for capital inflows for the region's development. At the same time the authorities are aiming at widening and deepening the financial sector by facilitating the establishment and evolution of, and providing a regulatory framework to, more diversified private financial institutions. Several investment banks, with capital raised offshore, have been established in Beirut and offer a variety of traditional investment banking services, including debt and equity raising and corporate finance advisory services. Several commercial banks have established investment banking subsidiaries offering similar services.

As part of the Government's strategy of reestablishing Beirut as a regional financial services center, the Central Bank established in 1994 a central depository, settlement and clearing agency, MIDCLEAR, which is a joint stock company organized under the laws of the Republic. The Government reopened the Beirut Stock Exchange in 1996.

Construction

Prior to the conflict, the property sector had always been important, with a substantial portion of the activity concentrated in Beirut, where the housing needs of the city's rapidly increasing urban population had to be met. Beirut saw an almost uninterrupted boom from the late 1950s to the early 1970s, when it expanded dramatically, eventually to house half of the country's population. Mountain towns and villages close to Beirut favored by tourists, such as Aley and Bhandoun, also experienced a boom.

The post-conflict era has witnessed a significant construction boom. Real estate prices have risen steeply, especially for prime property, but have recently stabilized. The boom has been fuelled by a mixture of local, expatriate and Gulf Arab funds. With respect to residential property, it has been concentrated mostly at the upper end of the housing market. As the stock market has resumed its operations only recently, land and construction have been viewed by many as attractive investment opportunities. Construction projects are financed mainly by equity investments. In 1995, construction activity accounted for 9.2 per cent. of GDP, a significant increase from approximately 4.5 per cent. in 1972. Since 1996, this activity has slowed, as witnessed by decreasing cement deliveries and number of construction permits.

Industry

In 1995, the industrial sector (mainly production of cement, furniture, paper, detergents, cosmetics, pharmaceuticals, batteries, garments and processed foods) accounted for 17.3 per cent. of GDP, an increase from 15.9 per cent. of GDP in 1972. Virtually all industry is privately owned.

Exchange rate and price stability coupled with the gradual fall in Lebanese Pound interest rates have contributed to a better environment for investment and growth in industry. Infrastructural bottlenecks resulting from the conflict are being addressed as improvements in roads, telephones and electricity supply are realized. IDAL is in the process of establishing free industrial zones in several areas around the country. The Government provides various incentives for the establishment of industrial facilities in Lebanon, including fiscal incentives in the form of reduced customs duties and tax exemptions.

From 1993 to December, 1999, the International Finance Corporation ("*IFC*") carried out 31 investment and financing projects in Lebanon in an aggregate amount of U.S. \$316 million, with an additional U.S. \$256 million raised by the IFC through loan participations. Investments during 1999 included loans to three companies for U.S. \$50 million. As of December 31, 1999, U.S. \$237 million representing IFC loans, loan participations and equity investments had been disbursed and remained outstanding.

Energy

Lebanon has no known fossil fuel resources. Apart from relatively modest hydroelectric resources and the import of 50-100 megawatts of electricity semi-annually from Syria, all energy needs are met with imports of petroleum products, which represented over 4.2 million TOE (tonnes of oil equivalent) in 1995. Two state-owned refineries (one in Tripoli and one in Zahrani) are currently non-operational. The power sector accounts for about one-third of fuel imports.

Lebanon's energy sector is dominated by the state-owned Electricité du Liban ("*EDL*"). EDL is a vertically integrated utility with approximately 900,000 customers. Lebanon's energy production facilities include three thermal power stations, two gas turbine stations in each of Baalbek and Tyre and seven hydroelectric stations. In addition, two new combined cycle power plants have been constructed. Besides its own plants, EDL purchases power from four independent hydroelectric power producers and sells wholesale to four private distributors. EDL is also the majority shareholder in the previously private-owned Kadisha company, a thermal and hydro power producer and distributor to about 100,000 customers in North Lebanon.

The power sector sustained severe physical damage to all its production transmission and distribution facilities during the conflict. EDL also incurred financial losses resulting from low tariffs, high technical and non-technical losses, including widespread illegal connections, and loss of control over its commercial operations.

EDL has been regaining control over its operations. Following the rehabilitation of existing plants, tariffs were increased significantly, and, commencing in 1996, steps are being taken to address billing and collection weaknesses as well as non-technical losses. The program for the rehabilitation of the Republic's energy sector is further described under "Reconstruction—Electricity Generation."

The Israeli attacks on power stations near Beirut in June, 1999 and February, 2000 resulted in damages estimated at approximately U.S. \$40 million. Required repairs to the power stations as a result of the latest attacks have been substantially completed.

Agriculture

Approximately one third of the Republic is arable. The most fertile areas are located along the coastal strip and in the Bekaa valley. The diversity of the Republic's topography and climate enables cultivation of a wide variety of vegetables, fruits, industrial crops and cereals. In 1995, agriculture contributed approximately 12 per cent. to the Republic's GDP, as compared to approximately 9.9 per cent. in 1972. Food and agricultural exports, which include forestry products, provide about 10 per cent. of merchandise export earnings.

RECONSTRUCTION

The Council for Development and Reconstruction and the Reconstruction Program

The CDR is a government agency entrusted with a key role in the process of reconstruction and economic recovery. It was established in 1977 in response to the needs of reconstruction as a successor to the Ministry of Planning and was reorganized in 1991. The CDR is an executive agency for the Council of Ministers. It is responsible for formulating and monitoring the implementation of public investment projects as well as seeking foreign funding.

Proposals for projects forming part of the reconstruction program are submitted for Parliamentary approval on a project by project basis. Approximately 1,664 contracts with a total value of approximately U.S. \$5.4 billion were awarded by the CDR for the period since reconstruction efforts started in 1992 to the end of 1999.

CDR expenditures on reconstruction and development programs are financed partly by grants and borrowings from international development agencies and other overseas entities and partly by appropriations from the budget. The Government's strategy is to finance the reconstruction and development program principally through the use of external financing, preferably concessionary financing (in the form of grants and soft loans). Other sources of external financing include commercial loans with export credit guarantees and the issuance by the Government of eurobonds and other international debt securities. As discussed elsewhere, the Government also seeks to partially finance the reconstruction program through participation by private sector companies.

Infrastructure

As a major regional entrepot and financial center, the Republic had a well-developed infrastructure prior to the conflict. The country's ports (Beirut, Tripoli, Sidon and Junieh) and Beirut International Airport were especially productive assets of the economy operating under a free exchange system. Catering to the large number of residents, businesses and international visitors, the housing and telecommunications sectors had been built up to high standards. The development of the road network had not, however, kept pace with the growth of the economy. The years of conflict exacted a heavy toll on the infrastructure. Since 1992, significant progress has been made in restoring and upgrading the infrastructure: electricity is available on a 24-hour basis to most users, telecommunications systems have been significantly upgraded and are functioning better, emergency water supply repairs have been undertaken, road networks are being upgraded, and collection of solid waste has markedly improved.

Electricity Generation

Work on a rehabilitation program for power plants with a cost of U.S. \$410 million started in 1993 and is now completed. This program involved the repair and reconstruction of existing generation, transmission and distribution facilities so that a nominal production capacity of 1,250 megawatts could be attained. Except for temporary interruptions caused by Israeli air attacks, electricity is now available to consumers in all of Lebanon 24 hours a day, with the power supply temporarily being augmented by the purchase from Syria of between 50 and 100 megawatts semi-annually. Another program, aiming to modernize the electricity sector, began in 1996, with a cost

estimated at U.S.\$1 billion. This program included the installation of four gas turbines in Sour and Baalbeck, with a capacity of 140 megawatts. These turbines became operational in 1996. In order to meet increasing demand and to anticipate the replacement of some older units, two combined cycle power plants providing additional production capacity of a total of approximately 900 megawatts are also being installed with approximately 600 megawatts currently operational. In addition, a new national 220KV network is being installed.

A Power Sector Restructuring and Transmission Expansion Project has been agreed on between the Government and the World Bank. The project calls for the implementation of a set of sector-wide restructuring and reform actions designed to introduce competition and private sector participation in utility operations and to reorganize EDL.

Water and Wastewater Sectors

A rehabilitation and development program for the water and wastewater sector, which is estimated at approximately U.S. \$1 billion, is underway.

The rehabilitation program began in May 1993 at a cost of some U.S. \$60 million in the first year. This included urgent repairs related to existing networks throughout Lebanon. Extension of the water treatment plant at Dbaye, which supplies clean water to a large part of Beirut was completed at a cost of approximately U.S. \$5.7 million. The rehabilitation program for Greater Beirut (Beirut & Ain al Delbeh Water Authorities) is currently being executed at a cost of approximately U.S. \$50 million. Rehabilitation and replacement of main water treatment plants and pumping stations in the rest of Lebanon is underway at a cost of approximately U.S. \$43 million.

Contracts for the rehabilitation and development of water and wastewater systems in North and South Lebanon, Mount Lebanon and the Bekaa were awarded between 1996 and 1999 at a value of U.S. \$214 million. These contracts comprise feasibility studies, environmental impact studies, design and preparation of tender documents, works and supervision.

Telecommunications

Work on the expansion of telephone exchanges commenced in November 1993. 200,000 mechanical lines out of the existing 450,000 system capacity were taken out of service and replaced by electronic lines, and an additional 800,000 new digital lines were commissioned in July 1993 so as to create a total fixed system capacity of 1,250,000 lines, bringing the total value of rehabilitation and extension contracts signed to some U.S. \$800 million. The strategy behind the project is to reconstruct the telephone system using modern technology such as digital switching and fiber-optic transmission. Work on the system was completed in 1999, including the rehabilitation and extension of the network. To date, equipment for approximately 980,000 of the planned new lines has been installed and a further 87,000 lines are about to be installed. A new program to add approximately 650,000 additional lines over a three year period was launched in April 1997 and has now been completed. International telephone capacity has been increased with the construction of two new earth stations and the laying of new submarine optical cable linking Saida, Beirut and Tripoli to Tartous in Syria and Alexandria in Egypt. Additionally, two compatible mobile phone networks currently aggregating over 600,000 lines are now operational. The mobile telephone networks are privately financed through two BOT contracts awarded to different operators.

Transportation

The first phase of road projects is currently being undertaken. Works started include the rehabilitation of the capital's road network, the completion of extensions started before the conflict and the extension of the coastal highway system north to Tripoli and south to Sidon was completed in 1996.

Current cost estimates for the extension of Beirut's international airport, with targeted passenger movement of 6 million persons per annum by the year 2000, amount to U.S. \$526 million. Two major contracts totaling some U.S. \$446 million have been awarded under a multi-year project approved by Parliament. Financing of U.S. \$179 million has been secured from the European Investment Bank, the Kuwait Fund for Arab Economic Development and the French Government, and a number of the airport's facilities (for example, the car park) are intended to be financed through BOT contracts reducing the portion of the costs to be funded by public expenditure. At the end of 1998, work related to the extension of the airport was approximately 81 per cent. complete. A new passenger terminal was put in service at the beginning of 1998 and completion of the project is expected by the end of 2000.

A project for the rehabilitation of the Port of Beirut, estimated at a cost of U.S. \$150 million, is intended to restore port capacity to pre-conflict levels. Contracts relating to the first sections of the civil works component of this project were awarded in October 1996 for an amount of U.S. \$102.8 million, subsequently reduced to U.S. \$90

million. Partial financing for this project amounting to the equivalent of U.S. \$54 million has been secured from the European Investment Bank.

A contract for the purchase of 200 new buses to improve public transport for the Beirut area has been entered into at a cost of some U.S. \$20 million. The buses are currently in operation.

SOLIDERE

Following the end of the period of conflict in 1990, the Government was confronted with the issue of how to redevelop areas in Lebanon that had suffered damage during the hostilities. Redevelopment was particularly critical for the Beirut Central District (the "*BCD*"), which had been the historical center of government and commercial activity and which had also been the subject of extensive damage during the hostilities. The BCD is considered the heart of Beirut. The area contains many important government buildings and the Lebanese Parliament. It has traditionally been considered the center of banking and commerce in Lebanon. The hotel district, internationally renowned before the hostilities, lies at the western edge of the BCD.

In 1992, the Government created a legal framework that would allow for the establishment of private real estate companies to carry out the redevelopment of damaged areas in accordance with a master plan approved by the Government. Parliament established the foundation for this legal framework with the enactment in 1991 of Law 117 ("*Law 117*").

SOLIDERE is the first real estate development and reconstruction company created pursuant to Law 117, in July 1992, and the only such company with responsibility for the development and reconstruction of the BCD (the "*Project*"). The entire area is approximately 1.8 million square meters, consisting of the traditional BCD and the Reclaimed Land. The traditional BCD constitutes the area of the BCD which existed prior to the hostilities in Lebanon and covers a surface area of approximately 1.2 million square meters. Under the master plan for the Project, the aggregate permitted built-up floor space in the entire BCD (including certain exempted lots which do not belong to SOLIDERE) and the Reclaimed Land is limited to 4.69 million square meters.

SOLIDERE's capital is composed of real estate of the original owners and the lessees in the BCD, who received 65 per cent. of SOLIDERE's shares in compensation for their properties and rights, and cash contributions from Lebanese and Arab investors, who subscribed to the flotation of shares in SOLIDERE, which closed on January 10, 1994. On September 30, 1996, the shares of SOLIDERE, previously listed on the Beirut Secondary Market, were listed and began trading on the Beirut Stock Exchange.

On December 3, 1996, 6,700,000 Global Depositary Receipts representing fractional economic interests in SOLIDERE shares were issued and currently are trading on the London Stock Exchange. In September 1997, SOLIDERE amended its by-laws and, in October, 1997, it obtained the necessary governmental approval to permit foreign investors to own shares in SOLIDERE.

HUMAN RESOURCES

Lebanon's human resources have traditionally been the backbone of its economy. The Republic's human resources had been developed to levels comparable to, or higher than, those of lower middle-income countries. Prior to the conflict, Lebanon was endowed with a well-trained population and labor force with adequate health facilities. The conflict resulted in setbacks for the human resources of the Republic. A significant emigration of skilled labor took place with large numbers of professionals, traders, industrial workers and construction workers leaving the country. The educational system also suffered (See "*-Educational System*", below).

However, a significant reversal of emigration has been observed since the end of the conflict and the installation of the Hariri government in October 1992. A large number of families living abroad have now returned, as well as young persons, who have been educated and have worked abroad, and who have either entered, or are looking to enter, the workforce. They are expected to contribute positively to the economic development of the country.

EDUCATIONAL SYSTEM

The variety of Lebanese educational institutions (schools as well as universities) is a reflection of the openness of the Republic to the international community. Private schools have a long and strong tradition in Lebanon. Aside from private schools established by western clerics (French, Anglo-Saxons, Germans, Italians), there are many and diverse local and foreign religious and secular schools. The Educational Center for Research and Development has recently revised and updated the national curriculum for schools.

According to the CAS Survey, the literacy rate was 88.4 per cent. in 1997, as compared to 68.2 per cent., the literacy rate in 1970.

The Republic traditionally had an advanced educational structure, and well-trained technicians and engineers. Prior to the conflict, Beirut served as an educational center for the region. However, a substantial part of this human capital was reduced during the conflict, and the educational system suffered damage and lack of investment. In spite of the turmoil, however, the educational system has survived and still retains high standards.

The following table gives a summary of the school system during the academic years 1994-1995, 1995-1996, 1997-1998 and 1998-1999.

| School System | 1994-95 | 1995-96 | 1997-1998 | 1998-99 |
|---|----------------|----------------|------------------|----------------|
| Total number of schools | 2,469 | 2,639 | 2,771 | 2,719 |
| Public schools (as a percentage of total) | 51.3% | 50.0% | 49.0% | 45.71% |
| Private commercial schools (as a percentage of total) | 33.8% | 34.9% | 36.4% | 36.23% |
| Private non-commercial schools (as a percentage of total) | 14.9% | 5.1% | 14.6% | 10.07% |
| Total student enrolment in schools | 799,905 | 829,338 | 878,102 | 871,580 |

Source: Ministry of Finance.

Lebanon's universities had a total of 87,957 students during the academic year 1996 – 1997. In 1998-1999 the total number of students enrolled at university were 101,400.

The principal universities in Lebanon consist of the Lebanese University, with five branches (59,728 enrolments in 1998-1999), the Arab University (sponsored by the Egyptian University of Alexandria) (11,356 enrolments in 1998-1999), Université Saint Joseph (USJ) (founded and run by French Jesuits) (6,667 enrolments in 1998-1999), American University of Beirut (AUB) (4,700 enrolments in 1998-1999), Lebanese American University (4,292 enrolments in 1998-1999), Notre Dame University (2,966 enrolments in 1998-1999), Kaslik University (3,819 enrolments in 1998-1999), the recently established Balamand University (Hybrid System) and Haigazian University College. The Lebanese University, the USJ and the AUB have medical schools.

The Government's emphasis on education is evidenced by the existence of three active ministries with responsibilities relating to educational matters. They are the MNEYS, the Ministry of Vocational and Technical Education and the Ministry of Culture and Higher Education.

EXTERNAL SECTOR

Balance of Payments and Foreign Trade

Lebanon is a predominantly importing country and is characterized by large trade deficits; however, net foreign income earnings, remittances and earnings from tourism, banking, insurance, and other services help offset the trade deficits. The trade balance recorded a deficit of approximately U.S. \$5,529 million for the year ended December 31, 1999 and a deficit of approximately U.S. \$6,399 million for the year ended December 31, 1998. Substantial capital inflows and continuing remittances from the Lebanese diaspora financed these deficits, typically resulting in a balance of payments surplus. Even during the conflict, the balance of payments was generally in surplus.

The balance of payments recorded a surplus of U.S. \$786 million in 1996 and U.S. \$420 million in 1997. However, the balance of payments registered a deficit of U.S. \$487 million for 1998, due in part, to the turbulence in certain financial markets in 1998 and a consequent withdrawal of funds by foreign investors in Lebanese treasury bonds as part of an overall reduction of exposure to emerging markets, and to increase foreign borrowings. The balance of payments recorded a surplus of U.S. \$261 million in 1999.

The following table indicates the principal destinations of exports for the years 1995 to 1999.

| Destinations of Exports⁽¹⁾ | | | | | |
|--|--------------------|--------------|--------------|--------------|--------------|
| | 1995 | 1996 | 1997 | 1998 | 1999 |
| | <i>(per cent.)</i> | | | | |
| Industrial Countries | 21.3 | 22.3 | 32.9 | 36.9 | — |
| Italy | 1.5 | 3.8 | 3.3 | 2.6 | 2.8 |
| United States | 3.7 | 3.0 | 6.0 | 6.6 | 6.2 |
| Switzerland..... | 1.1 | 1.5 | 2.4 | 3.4 | 6.6 |
| France | 6.0 | 4.6 | 7.2 | 8.7 | 7.7 |
| Germany | 2.2 | 2.3 | 2.2 | 3.2 | 3.6 |
| United Kingdom..... | 1.7 | 1.6 | 3.1 | 3.0 | 3.6 |
| Other | 5.1 | 5.5 | 8.7 | 9.4 | 9.9 |
| Developing Countries | 78.7 | 77.7 | 67.1 | 63.0 | 59.6 |
| Middle East..... | 59.7 | 62.4 | 54.1 | 43.4 | 43.2 |
| Saudi Arabia..... | 11.0 | 13.7 | 15.1 | 12.1 | 10.5 |
| Syria..... | 8.4 | 6.9 | 5.9 | 6.5 | 4.8 |
| Jordan..... | 4.0 | 4.9 | 3.9 | 3.6 | 4.0 |
| Kuwait | 3.9 | 7.7 | 4.5 | 4.2 | 4.5 |
| U.A.E | 28.8 | 23.4 | 9.0 | 9.9 | 8.0 |
| Egypt..... | 1.9 | 1.7 | 2.5 | 2.4 | 2.3 |
| Other | 1.7 | 4.2 | 13.2 | 4.6 | 9.3 |
| Africa | 5.3 | 3.4 | 4.8 | 5.0 | 5.5 |
| Other Europe | 8.2 | 4.1 | 1.2 | 6.0 | 4.2 |
| Other | 5.5 | 8.0 | 7.0 | 8.6 | 6.7 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |

Source: Higher Council of Customs/Banque du Liban.

Note:

(1) Minor discrepancies in the figures appearing in this table are due to rounding.

The following table sets out the major sources of imports for the years 1995 to 1999.

| Sources of Imports⁽¹⁾ | | | | | |
|---|--------------------|--------------|--------------|--------------|--------------|
| | 1995 | 1996 | 1997 | 1998 | 1999 |
| | <i>(per cent.)</i> | | | | |
| Industrial Countries | 65.8 | 69.1 | 68.2 | 66.8 | 66.4 |
| Italy | 13.0 | 12.1 | 13.2 | 11.5 | 10.9 |
| France..... | 7.5 | 7.8 | 9.5 | 9.7 | 9.6 |
| Germany | 8.4 | 8.5 | 8.7 | 8.7 | 8.9 |
| United States..... | 10.5 | 10.9 | 9.2 | 9.3 | 8.1 |
| Japan..... | 4.0 | 3.9 | 4.1 | 4.2 | 4.2 |
| United Kingdom..... | 3.9 | 4.0 | 4.4 | 4.5 | 4.4 |
| Switzerland..... | 4.7 | 3.4 | 6.6 | 6.3 | 7.1 |
| Belgium-Luxembourg..... | 1.9 | 1.5 | 1.9 | 1.9 | 1.9 |
| Other..... | 12.0 | 17.0 | 10.6 | 10.7 | 11.3 |
| Developing Countries | 34.2 | 30.9 | 31.8 | 33.1 | 33.6 |
| Middle East | 7.5 | 8.3 | 9.4 | 8.7 | 9.4 |
| Saudi Arabia | 1.8 | 1.5 | 1.7 | 1.7 | 1.7 |
| Syria | 3.4 | 4.1 | 4.4 | 3.7 | 3.6 |
| Bahrain..... | 0.0 | 0.1 | 0.1 | 0.1 | 0.4 |
| Kuwait..... | 0.1 | 0.1 | 0.1 | 0.1 | 0.2 |
| Other | 2.1 | 2.6 | 3.2 | 3.1 | 3.6 |
| Africa | 2.2 | 1.0 | 0.8 | 0.5 | 0.7 |
| Europe..... | 12.5 | 8.5 | 5.3 | 5.5 | 5.3 |
| Romania..... | 0.9 | 0.8 | 0.6 | 0.5 | 0.6 |
| Turkey..... | 2.1 | 2.3 | 2.1 | 2.5 | 2.6 |
| Cyprus..... | 0.4 | 0.4 | 0.5 | 0.2 | 0.2 |
| Other | 9.1 | 5.1 | 2.1 | 2.2 | 1.9 |
| Others..... | 12.1 | 13.1 | 16.3 | 18.4 | 18.2 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |

Source: Higher Council of Customs/Banque du Liban.

Note:

(1) Minor discrepancies in the figures appearing in this table are due to rounding.

Foreign Direct Investment

Prior to 1975, foreign direct investment was substantial. It was concentrated in property, services, banking and tourism. Predictably, foreign direct investment was weak during the period of conflict.

The onset of peace marked a reversal of this trend. Since 1990, considerable amounts of private Arab capital have been invested in real estate. Two principal sources for foreign direct investment have been the substantial funds held by Lebanese abroad and the large pool of private Arab wealth.

The Government continues to favor a strong role for the private sector in a liberal policy environment and welcomes foreign direct investment in the economy. The legal framework is sound and conducive to foreign investment. There are no special financial provisions for, or constraints on, foreign investors in the Republic, except that certain restrictions exist on foreign ownership of banks and companies involved in media activity, land ownership (both directly and when holding shares in companies owning real property) and the employment of foreign labor. A government agency, the Investment Development of Lebanon which has been established in 1994 currently assists foreign direct investors in setting up their activities in Lebanon.

Lebanon's membership in the Multilateral Investment Guarantee Agency was ratified by Parliament as a means of reinforcing the confidence of foreign investors wishing to invest in Lebanon. In addition, the National Institute for the Guarantee of Investment makes insurance coverage available to investors, in the form of compensation, for losses resulting from non-commercial risks.

MONETARY SYSTEM

Role of Banque du Liban

The Central Bank is the sole custodian of public funds, supervises and regulates the banking system and is vested by law with the exclusive authority of issuing the national currency. Banque du Liban's primary role is to safeguard the currency and promote monetary stability, thereby creating a favorable environment for economic and social progress. The Central Bank also advises the Government on various economic and financial matters. In conducting its monetary management function, the Central Bank utilizes a wide range of instruments, including reserve requirements on Lebanese Pound deposits with commercial banks, liquidity requirements on U.S. Dollar deposits in commercial banks, Treasury Bill repurchase and swap agreements with commercial banks, as well as Lebanese Pound denominated certificates of deposits issued by Banque du Liban.

As a result of high inflation prior to 1992, the Lebanese economy became substantially dollarized. Since October 1992, monetary policy has been targeted at stabilizing the Lebanese Pound exchange rate and controlling the inflation rate and money growth. The return of confidence in monetary stability and the high returns on investment in LL-denominated financial securities led to a significant decline of the dollarization of deposits in the economy and to a build up in foreign exchange reserves until the end of 1996. Thus, the proportion of foreign currency deposits decreased from 73.6 per cent. in December 1990 to 56.3 per cent. in June 1997 before increasing to 63.9 per cent. at the end of 1997 and 65.5 per cent. at the end of 1998 due in part to the turmoil generally affecting emerging markets following the Asian crisis. In 1999, the proportion of foreign currency deposits declined gradually to reach 61.8 per cent. at end-December, with a further decline to 61.0 per cent. at end-March, 2000.

Banking Sector

As at December 31, 1999, there were 66 active commercial banks, 723 branches in Lebanon, 24 financial institutions and seven specialized medium and long-term credit banks in Lebanon. Foreign banks are well represented in Lebanon and maintain branches in the Republic or equity stakes in several local banks.

Unlike the banking sector in some other emerging market countries, the banking sector in Lebanon is generally acknowledged to be stable and financially strong, and plays a critical role in the economy as a whole.

The banking sector currently offers services related to short-term and, increasingly, medium-term financing. As medium-term funds become available to Lebanese banks (by way of loans from international organizations, such as IFC and the European Bank for Reconstruction and Development, or the issuance of debt securities on the international capital markets), commercial banks have begun to offer a variety of medium-term loans, such as residential mortgage loans, other consumer loans and several types of loans to corporate investors. The return of foreign banks to the Republic is seen as a key step to diversifying the financial sector and strengthening competitive forces. Foreign banks are gradually re-establishing themselves in Lebanon, with ING and Citibank having each received a banking license in 1996, Nova Scotia in 1997 and Banque Nationale du Canada in 1998 and Cairo Amman Bank in 1999 and other foreign banks acquiring participations in the capital of Lebanese banks.

From March 1995, commercial banks were required to meet a minimum capital adequacy ratio of 8 per cent. in line with the Basle Accord. In September, 1999, the Central Bank required banks to raise their capital adequacy ratios to 10 per cent. by end 2000 and 12 per cent. by end 2001. A law facilitating bank mergers by, among other things, making banks eligible for soft loans from the Central Bank, was passed in 1993 and renewed in 1998 until 2003. During the past three years, commercial banks' capital increased substantially, and at June 30, 1999, their average capital adequacy ratio was approximately 17.85 per cent.

In addition, Parliament passed legislation to revitalize specialized banks (for housing, agriculture and industry). State participation in the shareholding of these banks has been reduced to a minority stake. In addition, Parliament passed laws relating to the listing of bank shares on stock exchanges and several banks currently list their eligible shares on the Beirut Stock Exchange.

The following table sets out the combined balance sheet of the commercial banks at December 31 for the years 1995-1999.

Balance Sheet of Commercial Banks in Lebanon

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|---|-----------------|-----------------|-----------------|-----------------|
| | <i>(in billions of Lebanese Pounds)</i> | | | | |
| Assets | | | | | |
| Reserves | 3,541.5 | 4,377.9 | 6,224.6 | 6,513.3 | 6,826.6 |
| Currency | 81.6 | 96.4 | 114.8 | 111.3 | 146.1 |
| Deposits with Banque du Liban | 3,459.9 | 4,281.5 | 6,109.8 | 6,402.0 | 6,680.5 |
| Claims on private sector | 10,320.0 | 12,687.0 | 15,451.3 | 18,681.5 | 20,994.3 |
| Lebanese Pounds | 1,278.3 | 1,622.6 | 1,987.2 | 2,073.5 | 2,473.7 |
| Foreign currency | 9,041.7 | 11,064.4 | 13,464.1 | 16,608.0 | 18,520.6 |
| Claims on public sector | 7,948.9 | 12,060.3 | 13,234.2 | 17,942.1 | 21,840.80 |
| Treasury Bills | 7,892.4 | 11,954.2 | 13,125.3 | 17,796.2 | 21,499.4 |
| Other | 56.5 | 106.1 | 108.9 | 145.9 | 341.4 |
| Foreign assets | 6,337.3 | 6,718.9 | 9,184.0 | 9,984.2 | 8,910.4 |
| Fixed assets | 738.5 | 1,150.5 | 1,271.6 | 1,637.9 | 2,033.6 |
| Unclassified assets | 168.8 | 188.4 | 267.1 | 271.7 | 364.9 |
| Total Assets | 29,055.0 | 37,183.1 | 45,632.7 | 55,030.7 | 60,970.6 |
| Liabilities | | | | | |
| Private sector deposits | 21,805.8 | 27,504.6 | 33,306.9 | 38,825.5 | 43,303.7 |
| Lebanese Pounds | 8,601.1 | 12,815.6 | 13,277.1 | 15,249.9 | 18,794.2 |
| Sight | 508.0 | 568.7 | 685.5 | 758.4 | 845.7 |
| Term | 8,093.1 | 12,246.9 | 12,591.6 | 14,491.5 | 17,948.5 |
| Foreign currency | 13,204.7 | 14,689.1 | 20,029.8 | 23,575.6 | 24,509.5 |
| Sight | 1,930.4 | 2,030.4 | 2,376.2 | 2,604.8 | 2,644.5 |
| Term | 11,274.3 | 12,658.7 | 17,653.6 | 20,970.8 | 21,865.0 |
| Public sector deposits | 261.0 | 285.1 | 216.6 | 346.1 | 701.7 |
| Liabilities to non-resident banks | 1,214.9 | 1,459.7 | 1,134.7 | 1,621.9 | 1,780.6 |
| Bonds | — | 325.9 | 327.9 | 370.6 | 167.5 |
| Deposits of non-residents | 2,078.3 | 3,180.1 | 5,262.4 | 7,287.6 | 7,856.1 |
| o/w: in Lebanese Pounds | 392.6 | 535.3 | 657.7 | 646.9 | 846.4 |
| Capital accounts | 1,145.9 | 1,943.5 | 2,990.0 | 3,619.9 | 4,019.3 |
| Unclassified liabilities | 2,549.1 | 2,484.2 | 2,394.1 | 2,959.1 | 3,141.7 |
| Total Liabilities | 29,055.0 | 37,183.1 | 45,632.7 | 55,030.7 | 60,970.6 |

Source: Ministry of Finance/Banque du Liban.

Interest Rates

Prior to 1993, interest rates on Treasury Bills were fixed by the Ministry of Finance in consultation with Banque du Liban. In May 1993, the Central Bank began selling 3-month Treasury Bills in a multiple price auction. The authorities subsequently extended this system to 6- and 12-month Treasury Bills in June and September 1993, respectively. In October 1994, the auction system was extended to 24-Month Treasury Bonds. Interest rates declined significantly in 1993 and 1994 in response to increased domestic and external demand for Lebanese Pound assets. The first three quarters of 1995 witnessed an increase in interest rates, reflecting a number of factors, including the policy objective of maintaining stability in the foreign exchange market in the face of political uncertainties associated with the end of the President's term of office. Interest rates experienced a steady decline from the fourth quarter of 1995 to the date of this Offering Circular, reflecting increased confidence in the strength and stability of the Lebanese Pound. The Central Bank also affects interest rates through its treasury bill discount and repurchase operations on the secondary market.

The gradual decline in interest rates on Treasury Bills has been accompanied by a decrease in the spread between U.S. Dollar and Lebanese Pound lending and deposit rates. The spread between deposit rates in Lebanese Pounds and in U.S. Dollars narrowed from 11.7 per cent. in December 1995 to 6.94 per cent. in December 1998, further declining to 5.67 per cent. in December, 1999 and 5.18 per cent. in March, 2000, and the spread between lending rates in Lebanese Pounds and in U.S. Dollars narrowed from 16.8 per cent. in December, 1995 to 8.74 per cent. in December, 1998, 7.51 per cent. in December, 1999 and 7.18 per cent. in March, 2000.

Foreign Exchange Rates and International Reserves

The currency of the Republic is the Lebanese Pound. The Lebanese Pound is convertible and its exchange rate is generally determined on the basis of demand and supply conditions in the exchange market. Bankers are allowed to engage in spot transactions in any currency. However, they are prohibited from engaging in forward transactions in Lebanese Pounds for speculative purposes. Banque du Liban intervenes when necessary in order to maintain orderly conditions in the foreign exchange market. There are no taxes or subsidies on purchases or sales of foreign exchange.

Foreign exchange rate stability is a primary policy objective of the Government and of Banque du Liban. Banque du Liban's exchange rate policy since 1993 has been to anchor the Lebanese Pound nominal exchange rate to the U.S. Dollar. This appreciation was limited to 0.03 per cent. in 1999 and the Lebanese Pound exchange rate remained unchanged during the first quarter of 2000. Although several external factors can influence the exchange rate, including general investor confidence in the economy, the authorities expect to continue to gear their monetary policy towards maintaining strength and stability in the exchange rate. Direct intervention in the currency markets supplements this policy when necessary to smooth excessive volatility of the exchange rate. Exchange rate stability over time should enable Banque du Liban to lower gradually domestic interest rates.

Foreign currency reserves are generally placed by Banque du Liban outside the Republic with other central banks or with highly rated international banks. They include a limited amount of highly rated foreign debt securities. Although not legally obligated to do so, Banque du Liban has been pursuing a policy of setting aside, and segregating from its foreign exchange reserves, certain foreign currency amounts corresponding to the maturing external public debt obligations of the Republic. These foreign currency amounts are being made available to the Republic for payment of its external public debt obligations, against payment to Banque du Liban of equivalent amounts in Lebanese Pounds. See "Monetary System—Role of Banque du Liban".

Securities Markets

The Beirut Stock Exchange was created in 1920 by the French mandate authorities in order to privatize public utilities, railways, telecommunications and the post office. Companies from the industrial, banking and tourism sectors were gradually added. The Beirut Stock Exchange flourished from 1954 to 1975. It ceased trading in 1983.

In August 1994, the Government set up the Beirut Stock Exchange Committee to supervise and manage the reopening of the Beirut Stock Exchange. Trading on the Stock Exchange commenced on January 22, 1996 when the shares of three previously listed Lebanese companies were re-admitted to trading. On September 30, 1996, the shares of SOLIDERE, previously listed on the Beirut Secondary Market, were listed and began trading on the Beirut Stock Exchange.

Market capitalization of companies listed on the Beirut Stock Exchange rose from approximately U.S. \$386 million in January 1996 to approximately U.S. \$3,193 million in December, 1999, due in large part to the listing of SOLIDERE shares. The number of authorized brokers rose from five to fourteen and the number of listed companies rose from three to twelve over the same period.

The Government regards the re-establishment and development of organized capital markets, including markets for the issue and secondary trading of equity and debt securities, as being of significant importance for the financing of Lebanon's reconstruction and economic expansion.

In addition, since 1996, several Lebanese companies raised funds (both equity and debt) in the international capital markets.

SUMMARY

SELECTED LEBANESE ECONOMIC INDICATORS ⁽¹⁾

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|---------|---------|--------------------|-------------------------|-----------------------|
| The Economy | | | | | |
| GDP (at current market prices in billions of Lebanese Pounds)..... | 18,028 | 20,417 | 22,880 | 24,509 | 24,816 |
| GDP (at current market prices in millions of U.S. Dollars) ⁽²⁾ | 11,122 | 12,996 | 14,867 | 16,167 | 16,462 |
| Real Growth Rate (per cent.)..... | 6.5 | 4.0 | 4.0 | 3.0 | 1.0 |
| Balance of Payments (in millions of U.S. Dollars) | | | | | |
| Current account | (4,587) | (4,507) | (4,153) | (5,863) | (5,626) |
| Capital account..... | 4,843 | 5,293 | 4,573 | 5,375 | 5,887 |
| Overall balance of payments | 256 | 786 | 420 ⁽³⁾ | (487) ⁽³⁾⁽⁴⁾ | 261 ⁽³⁾⁽⁴⁾ |
| Reserves | | | | | |
| (in millions of U.S. Dollars) | | | | | |
| Foreign Exchange ⁽⁵⁾ | 3,026 | 3,935 | 2,959 | 3,318 | 4,968 |
| Gold ⁽⁶⁾ | 3,572 | 3,410 | 2,670 | 2,651 | 2,678 |
| Gold (Thousands of Troy Ounces)..... | 9,222 | 9,222 | 9,222 | 9,222 | 9,222 |
| Public Finance | | | | | |
| (in billions of Lebanese Pounds) | | | | | |
| Central Government Revenues | 3,033 | 3,533 | 3,753 | 4,449 | 4,868 |
| Central Government Expenditures ⁽⁷⁾ | 5,856 | 7,225 | 9,162 | 7,906 | 8,454 |
| Central Government Overall Deficit..... | (2,823) | (3,692) | (5,409) | (3,457) | (3,586) |
| Primary Deficit/Surplus ⁽⁸⁾ | (948) | (1,039) | (2,031) | 691 | 888 |
| Public Debt | | | | | |
| Net Domestic Public Debt | | | | | |
| (in billions of Lebanese Pounds)..... | 9,287 | 13,358 | 18,381 | 19,544 | 21,377 |
| Public External Debt | | | | | |
| (in millions of U.S. Dollars) ⁽⁹⁾ | 1,332 | 1,883 | 2,402 | 4,166 | 5,539 |

Notes:

- (1) Certain figures differ slightly from previously published data.
- (2) Translated at period average exchange rates.
- (3) Includes a U.S.\$500 million deposit from Saudi National Commercial Bank made in December 1997.
- (4) Includes a U.S.\$100 million deposit from the Kuwaiti Investment Authority made in February 1998.
- (5) Foreign exchange reserves are owned by Banque du Liban and do not include foreign exchange deposits held at Banque du Liban by banks and other financial institutions.
- (6) Parliament passed Law No. 42/86 dated September 24, 1986 forbidding dispositions of gold reserves without parliamentary legislation.
- (7) Not including expenditures by the Council for Development and Reconstruction financed with foreign funds (See "Public Finance—Operations of the Central Government").
- (8) Budget surplus or deficit, excluding domestic and external debt service and net treasury operations for 1998 and 1999.
- (9) Calculated at end of period exchange rates, commencing in 1998.