

New economic plan details ambitious goals

Bloomberg

Lebanese officials promised to tax banks and slash their own pay as they unveiled an unprecedented package of measures to avert a financial meltdown and appease tens of thousands of protesters demanding they leave power. The emergency plan, announced Monday by Prime Minister Saad Hariri, includes the approval of a 2020 budget targeting a deficit of 0.6 percent of economic output with no other taxes or borrowing and more aid to poorer families.

The vision was met with skepticism by economists, not least because Lebanon's budget deficit stood at just under 12 percent of gross domestic product in 2018. And while the plans appear to meet demands for change that have gone unanswered for decades, including an end to electricity blackouts, they did little to calm tempers in the street.

The stakes are high for Lebanon, which straddles the region's geopolitical fault lines and has often been a proxy battleground for the Middle East's broader conflicts. The 15-year Civil War ended in 1990 but still haunts a country where the warlords became the rulers and have remained in power ever since.

It's that class that protesters say has plundered the state, leaving it unable to provide basic services and close to bankruptcy.

Time isn't on Lebanon's side. One of the most indebted countries in the world, it needs to find fresh sources of funding as the foreign inflows on which it has traditionally relied have dried up.

Even after Hariri's speech, the yield on Lebanon's Eurobonds due in 2021 was up more than 300 basis points Monday to almost 24 percent, a record.

"The deficit target is both unrealistic and unnecessary," said Ziad Daoud, Dubai-based chief Middle East economist, Bloomberg Economics. "It's just short of fantasy to expect it to go from near double-digits to zero in one year. Fiscal sustainability requires a reduction of the deficit, but not necessarily to this extent. The goal was likely chosen for theatrics."

With financial pressures rising, Hezbollah and its allies have opposed Hariri's push to impose taxes and take other measures they fear will harm low-income families that form a large section of their support base. The reform package promises to impose a one-off tax on bank revenues and cut ministers' salaries by 50 percent.

It also promises to implement the much-delayed restructuring of an electricity sector that loses \$2 billion a year and to look at the possibility of selling off part of the telecoms sector, where a lack of competition has led to some of the highest costs in the region.

The government also pledged to meet the conditions required to unlock about \$11 billion in international aid pledges made at a donor conference in Paris 18 months ago - key to reviving a moribund economy and averting a debt crunch.

The International Monetary Fund projects Lebanon's current-account deficit will reach almost 30 percent of GDP by the end of this year. It predicts that economic growth, stagnant at 0.3 percent in 2018, would continue to be weak. Public debt is projected to increase to 155 percent of GDP by the end of 2019.

"None of this satisfies the protesters' core demands: removal of a deeply corrupt, sectarian and inept oligarchy whose systemic function is to divide, exploit and profit off of a subjected society," said Paul Salem, president of the Middle East Institute in Washington, D.C. "They've had enough; they want fundamental change: This is not it."

Against this backdrop, banks, schools and the stock market were shut Monday, as were many businesses. Protesters blocked roads around the country as protesters filled the streets waving the flag.

The financial crisis has been years in the making. For months, sporadic protests and strikes have erupted as a shortage of dollars squeezes businesses and threatens a currency peg in place for more than two decades.

In the plan, Lebanon's Central Bank will slash \$2.9 billion from the country's local-currency interest payments and commercial lenders will pay a one-time tax under a government plan to wipe out the budget deficit almost entirely next year.

Hariri, the finance minister and Central Bank governor will see the program through, the Secretary-General of the Cabinet Mohammad Makiyeh said in a televised news conference Monday.

The government will also impose a 2 percent tax on banks' revenue in 2019 that would amount to nearly LL600 billion (\$397 million), Minister of State for Information Technology Adel Afiouni told Bloomberg.

"This will give us fiscal space to have enough time to get our reforms in place," the minister, who is also a former Credit Suisse banker, said. The government won't borrow and is committed to paying maturing debt next year.

While the plan to slash debt costs may appease the protesters, many of whom accuse banks of profiting from the nation's financial trouble, investors will be assessing the implications on Lebanon's credit.