

INTERNATIONAL CONFERENCE FOR SUPPORT TO LEBANON - PARIS III

SECOND PROGRESS REPORT



INTERNATIONAL CONFERENCE
FOR SUPPORT TO LEBANON - PARIS III
SECOND PROGRESS REPORT
2nd of July 2007

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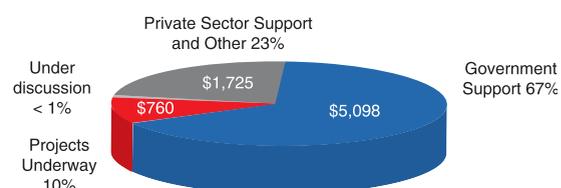
This is the second progress report since the International Conference for Support to Lebanon “Paris III - Rafic Hariri conference ” was hosted by President Jacques Chirac in Paris on January 25, 2007. The first progress report published in April 2007 provided background information on the conference and the available data at that date. For the first report please refer to the document “International Conference for Support to Lebanon Paris III First Progress Report” on www.finance.gov.lb. This report provides an update on progress achieved since then and the status of discussions with donors. In summary:

1. Since the Paris III Conference, the Government has achieved significant progress in setting up the institutional structure to implement and monitor the reform program. The Program Coordination Office and the three Inter-Ministerial Committees IMCs (Social, Economic and Infrastructure and Privatization) were formed and commenced their activities. The Program Coordination Office reviewed with the “Natural Owners” or concerned ministries and public institutions the reform program. 316 reform initiatives were allocated to 12 “Natural Owners”. The social cluster has the most initiatives at 41 percent of the total, the economic 35 percent and the infrastructure and privatization 27 percent of initiatives.
2. Ministries and public institutions have progressed in the implementation of the reform program. To date, 64 reform initiatives have been launched under the purview of the IMCs and another 41 are expected to be launched during the third quarter of 2007. By end of November, 116 initiatives will have had a tangible impact.
3. In parallel, the Ministry of Finance has worked closely with donors on the programming of their pledges. Of the total \$7,613 million pledged in

the Paris III Conference, 67 percent is estimated to be for project financing, support for reforms, balance of payment support and technical assistance channeled through the government. Over \$1,000 million are expected to be received in 2007 for reform in form of budgetary support, of which \$177 million were transferred to date. Discussions with donors are underway regarding \$1,472 million for budgetary support, in line with the reform agenda.

4. Several agreements to provide support to the private sector have been reached with local financial institutions, making \$840 million available to SMEs.
5. Discussions with donors have provided a clearer picture regarding sector allocation of funds. The power and social sectors were a focus of many donors as per the priorities set by the Government.
6. An IMF mission to hold discussions for the 2007 Article IV consultations and for the first quarter assessment under the Emergency Post Conflict Assistance (EPCA) concluded that Lebanon’s performance under the program is on track.

Updated Distribution of Pledges (US\$, million)



Source: Collected data by June 19, 2007

UPDATED RESULTS OF CONFERENCE

Table 1: Updated Paris III Pledges (Greater than \$10 million; in US\$ million)

Country	Total	Private Sector Support	UN/ UNI- FIL/ NGOs	TA/ In-Kind	To BDL	Grants to Government		Loans to Government		Projects Underway
						Budget Support	Project Financing	Budget Support	Project Financing	
European Investment Bank	\$1,248	\$709		\$20					\$260	\$260
Saudi Arabia	\$1,100					\$100			\$1,000	
World Bank	\$975	\$275						\$300	\$400	
United States	\$890	\$120	\$235	\$286		\$250				
Arab Fund for Economic & Social Development	\$750								\$550	\$200
France	\$650	\$163						\$488		
European Commission	\$486					\$39	\$243	\$65		\$139
United Arab Emirates	\$300							\$300		
Islamic Development Bank	\$250						\$30		\$215	\$5
Arab Monetary Fund	\$250	\$100						\$150		
Italy	\$156		\$26				\$33		\$98	
Germany	\$134						\$91			\$43
United Kingdom	\$115		\$35							\$80
International Monetary Fund	\$77				\$77					
Spain	\$53		\$16	\$2			\$3			\$33
Egypt	\$44			\$15			\$29			
Belgium	\$26	\$13					\$13			
Turkey	\$20			\$20						
Canada	\$17		\$13	\$4						
Norway	\$15		\$8				\$8			
Oman	\$10					\$10				
Others*	\$47		\$14	\$1		\$1				
Total*	\$7,613	\$1,379	\$346	\$347	\$77	\$400	\$449	\$1,303	\$2,523	\$760

Source: Collected data by June 19, 2007

*Others include \$31 million still under review; a report detailing "Others" is included in the appendix

A. Government Support

1. Total government support is estimated at \$5,098 million, of which, 77 percent is in the form of loans.

(a) **Budgetary support** stands at \$1,703 million or 33 percent of the total pledged to the government:

(i) Loans for budgetary support stand at \$1,303 million and include those from the World Bank, France, European Commission (EC), United Arab Emirates, and the Arab Monetary Fund (AMF).

(ii) Grants for budgetary support total \$400 million which include contributions from Saudi Arabia, United States, European Commission, Oman and Malaysia.

(b) **Project Financing** totaled \$2,972 million or 58 percent of total pledged to the government:

(i) Loans for project financing totaled \$2,523 million including loans from

European Investment Bank, Saudi Arabia, World Bank, Arab Fund for Economic and Social Development (AFESD), Islamic Development Bank (IDB), and Italy.

(ii) Grants for project financing totaling \$449 include the EC, IDB, Italy, Germany, Spain, Egypt, Belgium, and Norway.

(c) **Loans to BDL** stand at \$77 million which were transferred from the IMF. The loan was provided at the signing of the EPCA agreement (Please refer to the section "Update on the IMF EPCA Program").

(d) **Technical Assistance and In-Kind Contribution**, totaling \$343 million, was added as a new category as some donors have expressed interest in supporting Lebanon in this form. Technical assistance is expected from EIB, Canada, Spain and Denmark. In-kind contributions are expected from the United States, Egypt and Turkey.

Table 2: Summary of Government Support (US\$, million)

	<i>Budgetary Support</i>	<i>Project Financing</i>	<i>BDL</i>	<i>TA / In-Kind</i>	<i>Total</i>
Grants	400	449	-	347	1,196
Loans	1,303	2,523	77	-	3,902
Total	1,703	2,972	77	347	5,098

Source: Collected data by June 19, 2007

2. Donations Received to Date

Of the total pledged for government support, \$177 million was received to date:

(a) \$100 million grant from Saudi Arabia. The \$100 million grant in budgetary support was received on April 11th 2007. The funds were used to repay \$76 million in Eurobond interest, \$9 million for foreign loans, and \$15 million for treasury bills interest in Lebanese Pounds.

(b) \$77 million from the IMF was received on April 4, 2007. As with all IMF loans, the loan is actually in the form of a currency swap, where the borrowing member exchanges its own currency for reserve currencies it needs for balance of payments purposes.

Lebanon pays quarterly charges on its outstanding Fund credit at the weekly determined adjusted rate of charge, as posted on the Fund's website.

UPDATED RESULTS OF CONFERENCE

In addition, some agreements were signed while others are under progress:

- (a) An agreement for the \$300 million soft loan from the UAE was completed on the 20th of February. The loan is allocated for debt replacement and bears an interest rate of 2.5 percent per annum. (for further details please refer to the Paris III First Progress Report).
- (b) Discussions are underway with the other donors. Details are available in the sections “Sector Allocation” and “Details of Pledges”.

3. Budgetary Support Expected in 2007:

Although discussions are still underway with many of the donors, the Ministry of Finance estimates that over \$1,000 million will be received by the end of 2007. In addition to the \$100 million grant from Saudi Arabia and the \$77 million loan from the IMF, a first tranche of the following contributions is expected in 2007:

(a) **World Bank:** The Lebanese Government is in the process negotiating two Development Policy Loan (DPL) agreements with the World Bank. The DPLs are loan agreements for budgetary support with the disbursement based on the fulfillment of agreed to triggers or actions in a certain sector:

(i) The power sector \$100 million DPL was agreed to between the Lebanese Government and the World Bank with a policy note sent to the World Bank on June 13, 2007. The loan agreement will be presented to the World Bank board in mid-July. Disbursement is expected immediately after the Board approval.

(ii) Work is currently progressing toward the social sector DPL of \$75 million.

The Social Inter-Ministerial Committee in charge of monitoring reforms under the Ministry of Social Affairs, Health, Education and Labor/NSSF is meeting regularly and discussions to finalize an agreement with

the World Bank are underway. The DPL is expected to be presented to the World Bank Board of Directors in September 2007.

(b) **UAE:** The agreement signed for \$300 million debt replacement loan is expected to be disbursed in tranches in the second half of 2007.

(c) **France:** A mission was in Lebanon during the week of April 23rd to hold initial discussions regarding the budgetary support loan of €375 million. The agreement will be based on conditions discussed during the mission and expected to be finalized and approved by the two governments. Disbursement will take place in three tranches. The first tranche is estimated to be in the second half of 2007 following French Parliament ratification.

(d) **US:** On May 24th, the US Congress approved a bill containing Lebanon's total contribution of \$770 million (the \$120 million for private sector was allocated previously). The funding included the budgetary support of \$250 million as a support to the implementation of the EPCA program. The Ministry of Finance held several meetings with representatives from the American Embassy in Beirut in addition to meetings held during the IMF / World Bank meetings on April 14 – 15th in Washington between the Lebanese Minister of Finance and officials from the State and Treasury Departments. Based on these meetings, a memorandum of understanding is under discussion to finalize the timing and triggers for disbursement of funds and is expected to be signed shortly.

On June 25th, 2007 the Council of Minister reviewed a proposed MOU and assigned the Ministry of Finance to negotiate the final terms of agreement with USAID. Partial funding is expected in the second half of 2007.

(e) **EC:** A total package of \$104 million (€80 million) for Micro-financial assistance, subject to approval by EU Parliament, is expected to be reviewed by the second half of 2007. The package includes a \$65 million (€50 million) loan and a complementary grant estimated at \$39 million (€30 million) to pay the interest on the loan. Subject to the timing of the EU Parliament approval, the first tranche of this loan may be available at the end of 2007.

(f) **Arab Monetary Fund:** Discussions are underway to determine best structural adjustment measures to be supported by the AMF. Although tranching, the first tranche is expected to be upon the signing of an agreement.



In addition to the above support pledged during the Paris III Conference, the **Government of Malaysia** indicated its support and willingness to restructure existing debt. Since then, the Central Bank of Malaysia has worked with the Ministry of Finance in Lebanon on restructuring \$500 million in existing loans through decreases in coupon rates and lengthening of maturities and/or grace periods. The agreement is subject to approval by the Malaysian Ministry of Finance.

UPDATED RESULTS OF CONFERENCE

B. Support to the Private Sector & Other

Donor institutions have made significant progress on reaching agreements with financial institutions to provide support to the private sector. In fact, approximately \$840 million in loan agreements have been signed or close to being final. The disbursement will depend on the applications of the private sector and the banks' processes.

1. **European Investment Bank (EIB):** \$709 million (or 57 percent of EIB's total contribution) was dedicated to the private sector. The following table summarizes the expected allocation of these funds.

Table 3: Updated summary of EIB's Paris III pledge for private sector support

	<i>Amount in original currency (€ million)</i>	<i>Amount in \$ million</i>	<i>Description</i>
SME Reconstruction Facility (Guaranteed by government with BDL)	100	130	Facility that targets the reconstruction and recovery of SMEs whose businesses were affected by the recent conflict. The agreement should be signed with BDL in the third quarter of the year.
Multi-sector global loan (already signed) (Guaranteed by government)	60	78	Line of credit will provide long term projects in industry, agro-industry, IT, financing for SME investment services, health and education. It will be channeled through 14 top-tier banks in Lebanon.
Non-sovereign corporate and private bank loans	200	260	
Public-privatepartnerships Private investment energy & Transport	150	195	
Private Equity Operations local venture	35	46	
Total	€545	\$709	

Source: Collected data by June 19, 2007

2 **World Bank:** Through the IFC, \$225 million in loan agreements have been signed with local financial institutions. This includes:

- (a) Credit line facilities with BLOM Bank, Fransabank and Credit Libanais in the amounts of \$50 million, \$25 million and \$15 million respectively
- (b) Trade Finance agreements with Bank Libano-Francaise, Bank of Beirut, and Fransabank in the amount of \$30 million each
- (c) Risk sharing facility with Bank of Beirut of up to \$25 million
- (d) An investment of \$20 million was made in a retail institution.

The remaining amounts are under discussions with various institutions.



3 **United States:** Agreements with financial intermediaries have been signed for the total amount pledged of \$120 million.

- (a) Citigroup and The Overseas Private Investment Corporation (OPIC), extended \$20 million and \$50 million 15-year term loan facilities to Banque Libano-Francaise SAL (Lebanon) and Byblos Bank. These funds will be used for small and medium-sized enterprises (SMEs), real estate and consumer finance.
- (b) An agreement for a \$50 million facility has been reached with an undisclosed financial institution.

4 **France:** Through the Agence Française de Développement (AFD), €125 million is being provided to financial intermediaries to support SMEs. So far the AFD has signed agreements with Byblos Bank for €25 million, Société General de Banque au Liban (SGBL) for €10 million, Fransabank for €10 million, Libano-Francaise for €15 million, Banque Audi for €25 million totaling €85 million (\$111 million). AFD is in discussions with other banks for the remaining amount.

5 **Arab Monetary Fund:** In April 2007, The Arab Trade Financing Program (ATFP) signed credit line agreements with Credit Libanais s.a.l., Fransabank s.a.l., BankMed s.a.l. and Banque Libano-Francaise s.a.l. for a total of \$57 million. This agreement aims to help finance foreign trade deals. In March 2007, ATFP also signed an agreement with Byblos Bank for \$25 million.

UPDATED RESULTS OF CONFERENCE

Table 4: Updated summary of support to the private sector & other (US\$ million)

	<i>Support to the Private Sector</i>	<i>UNIFIL / UN / NGOs</i>
Grants	-	346
Loans	1,379	-
Total	1,379	346

Source: Collected data by June 19, 2007

In parallel to the Paris III pledges, and on January 16, 2007 the **Arab Fund for Economic and Social Development** signed with the Council for Reconstruction and Development an \$86 million loan agreement for support to rehabilitation of damages in the private sector. The law was sent to Parliament for approval.

In addition to private sector support, donors have pledged \$346 million to be channeled through multilateral organizations and NGOs. The largest of these are a US contribution of \$185 million to support UNIFIL and \$50 million to support developmental activities through USAID. The remaining amount includes support from Italy, UK, Spain, Canada, Norway, Sweden, Denmark, Japan, Austria, and Finland.

C. Projects Underway

Approximately \$760 million of the funds pledged in Paris III represent contributions that were in the process of being allocated at the outset of the Conference. Of these pledges approximately, \$185 million are from Stockholm Conference for Lebanon's Early Recovery.

D. Under Review

The remaining \$31 million are under review and their programming is yet to be finalized. These include support from Jordan, Greece, Australia, China, Ireland, Cyprus, Brazil, South Korea, Luxembourg, Portugal, and Slovenia. This support is expected to be in the form of grants.

SECTOR ALLOCATION

The following table details available allocation of pledges.

Table 5: Sector allocation of pledges (US\$ million)

Country	Total Pledged	Sector	Intended Uses of Funds
European Investment Bank	\$1,248	Private Sector, Power, Water, Ports, Roads	<ul style="list-style-type: none"> - Private Sector support: \$709 million (€545 million) - Waste water, ports and roads: \$260 million (€200 million) in existing projects - Waste water: Project under discussion for an approximated \$86 million (€66 million) - Power Sector: Project under discussion for approximately \$182 million (€140 million) - Technical Assistance: \$19.5 million (€15 million) which maybe used for implementing privatization
Saudi Arabia	\$1,100	Budgetary Support, Other projects	<ul style="list-style-type: none"> - Budgetary support: \$100 million - Project financing \$1,000 million under discussion
World Bank	\$975	Private Sector, Water, Social, Power	<ul style="list-style-type: none"> - Private Sector Support: \$275 million - Loan agreements under negotiation for the power and social sectors
United States	\$890	Budgetary support, Private sector, Security, Development	<ul style="list-style-type: none"> - Private sector, \$120 million - UNIFIL: \$184.5 million - Armed forces: Total \$285.5 million - Budgetary support: \$250 million - Development support: \$50 million through USAID
Arab Fund for Economic & Social Development	\$750	Power, Water, Administration reforms	<p>Several Loans were under preparation at the outset of the Paris III Conference:</p> <ul style="list-style-type: none"> - Public administration development: \$31 million (KWD 9million) - Water and waste water: \$86 million (KWD 25 million) - Rehabilitation of Damages in Private Sector SMEs: \$86 million (Kuwaiti Dinar \$25 million) - Power Sector: \$120 million (Kuwaiti Dinar \$35 million) <p>The remaining funds are under discussion with additional funds dedicated to the power sector a possibility</p>
France	\$650	Budgetary Private sector Support,	<ul style="list-style-type: none"> - Budgetary Support: \$488 million (€375 million) - Private sector: \$163 million (€125 million)
European Commission	\$486	Recovery, reform, budgetary support	<ul style="list-style-type: none"> - Stockholm humanitarian pledge: \$139 million (€107 million) - Grants in the framework of EC cooperation with Lebanon for the period 2007-2010: \$243 million (€187 million) - Micro-financial assistance package: \$104 million (€80 million)

Source: Collected data by June 19, 2007

Table 5: Sector allocation of pledges (US\$ million)

<i>Country</i>	<i>Total Pledged</i>	<i>Sector</i>	<i>Intended Uses of Funds</i>
United Arab Emirates	\$300	Budgetary support	Debt reduction
Islamic Development Bank	\$250	Social, Infrastructure	Agreement under discussion for the full amount. Expected: - Social sector projects: \$30 million - Infrastructure including water, roads and other projects: \$215 million
Arab Monetary Fund	\$250	Budgetary support, Private Sector	Budgetary support in the context of support to fiscal adjustment reforms: \$150 million loan - Private sector: \$100 million for trade financing from the Arab Trade Financing Program
Italy	\$156	Social sector, infrastructure	Mission visiting Lebanon to finalize programming of funds
Germany	\$134	Security, Education, Water	- Vocational training sector: \$17 million (€13 million) - Water supply and wastewater: \$56 million (€43 million)
United Kingdom	\$115	Humanitarian	- European Commission pledge: \$80 million - UNRWA: \$30 million - Implementation of UNSCR1701/UNIFIL: \$5 million
International Monetary Fund	\$77	Balance of payment	Loan under the EPCA Program. Final uses of funds are under discussion
Spain	\$53	Humanitarian Solar energy	- United Nations Agencies, Lebanon Recovery Fund (through UNDG) and NGOs: €36.34 million or \$48 million - Technical assistance: \$2.3 million (€1.76 million) - Project financing: \$2.5 million (€1.9 million)
Egypt	\$44	Power	In-kind grant to rehabilitate the Jieh Power plant for a total of \$14.6 million was committed
Belgium	\$26	Reconstruction	Health / reconstruction: Re-equipment of the Tibnin civil hospital for \$6 million (€4 million) The remaining amount under review
Turkey	\$20	Social Sector	
Canada	\$17	Governance, Social	Mission in Lebanon reviewed needs with various ministries Possible allocation to refugee issues
Norway	\$15	Environment, Humanitarian	

Source: Collected data by June 19, 2007

SECTOR ALLOCATION

Table 5: Sector allocation of pledges (US\$ million)

<i>Country</i>	<i>Total Pledged</i>	<i>Sector</i>	<i>Intended Uses of Funds</i>
Oman	\$10	Budgetary Support	
Sweden	\$6	Peace building, Infrastructure, Humanitarian	UNDP for peace building and municipalities; Swedish NGOs for projects in Lebanon
Denmark	\$3.5	Security, Humanitarian	UN Agencies and NGOs including Danish Refugee Council, UNMAS, UNRWA Security: \$1 million in support to implementation of UNSCR 1701, including border management
Japan	\$4	Humanitarian	UN Agencies and NGOs: including UNRWA, UNMAS and several Lebanese and Japanese NGOs
Austria	\$	Humanitarian	UN Agencies including UNDP and UNRWA
Finland	\$1	Humanitarian	UN Agencies
Brazil	\$1	Infrastructure	
Malaysia	\$1	Budgetary Support or Housing	

Source: Collected data by June 19, 2007

The above table does not include countries where sector information is not available as of publication of the report.

UPDATE ON THE IMF EPCA PROGRAM

The Government of Lebanon entered into an Emergency Post Conflict Assistance agreement with the IMF. As such, On April 9th, 2007 the IMF board approved a \$77 million emergency loan. The agreement is based on the government's reform program but has specific monitorable actions and quantitative indicative targets to be completed by the government during the year 2007.

Since then, an IMF mission visited Lebanon on May 14 - 28, 2007 to hold discussions for the 2007 Article IV consultation, for the first quarter assessment under the EPCA program and prospects for the remainder of 2007. The mission met with government officials including the Minister of Finance, the Central Bank Governor, the Ministers of Economy and Trade, Tourism, and Energy and high officials from the office of the Prime Minister and various public agencies. In addition, the IMF team held discussions with officials from the private and banking sectors. The IMF's mission assessed the economic situation and concluded that as expected, 2007 is a difficult transition year. However, performance under EPCA is on track and the reform program offers a viable solution to the debt issue. The mission stressed the importance of timely disbursement of the Paris III pledges in support of the reform plan. On the monetary side, the IMF indicated that a stable environment will also allow for reform of monetary policy instruments and improving the Central Bank balance sheet. Finally, the statement indicated that the banking sector's expansion into the region decreases the local risk but may require new regulations. (Please refer to IMF Article IV Concluding Statement in the Appendix). The next mission is expected in July 2007.

DETAILS OF PLEDGES

To the largest extent possible, below are the details of the status of discussions with the various donors:

A. European Investment Bank

The total amount pledged by the EIB is \$1,248 million.

1. The largest part of this contribution at \$709 million is dedicated to the private sector. Please refer to section "Private Sector Support".
2. Technical assistance is anticipated to be at \$19.5 million (€15 million) and may be dedicated to implementation of privatization.
3. \$260 million (€200 million) is expected to be spent on waste water (€66 million) and power projects (€140 million).
4. \$260 million (€200 million) are for projects underway in the waste water, ports and roads sectors.

A technical mission visited Lebanon to determine best uses of these loans the week of January 29th. A loan agreement for a project in the water sector is being finalized with CDR. Once an agreement is signed, it will be sent to Parliament for ratification. On the power sector front, an Independent Power Producers proposal developed by the Government of Lebanon was sent to EIB for consideration.

B. Saudi Arabia

Saudi Arabia's contribution consists of \$100 million as a grant in budgetary support and \$1,000 as a soft loan for project financing.

1. The \$100 million grant in budgetary support was received on April 11th 2007. (Refer to "Government Support" section).
2. High level meetings were held during April 2007 in Beirut and in Washington DC on the occasion of the IMF/World Bank meetings between Saudi and Lebanese authorities to discuss possible allocation of the \$1,000 million loans for project financing. Currently, CDR and the Ministry of Finance continue holding discussions with the Saudi Fund for Development regarding the programming of the loans. The power sector Independent Power Producers proposal was sent to the Saudi Fund for Development for consideration.

C. World Bank

The total World Bank contribution amounted to \$975 million.

1. Private Sector support through the IFC who is extending credit lines and risk sharing facilities with partner banks with a target amount of \$250 - \$270 million. (for more details review section "Private Sector Support").
2. Two Development Policy Loans estimated for a total of \$175 million in the power and social sector. (for more details review section "Budgetary Support Expected in 2007").

The remaining funds will be discussed at a later stage.

D. United States

Support from the United States totals \$890 million with the following allocation:

1. Support to the private sector for an amount of \$120 million through Citigroup and The Overseas Private Investment Corporation (OPIC). Please refer to the section titled "Support to the Private Sector & Other".
2. Budgetary support estimated at \$250 million. This budgetary support is expected to be based on certain actions to be agreed upon between the Lebanese Government and the US Government. These reforms are modeled on the IMF EPCA Program. (please refer to the section titled "Budgetary Support Expected in 2007").
3. Support to UNIFIL estimated at \$185 million.
4. Development support through USAID for approximately \$50 million.

5. The remaining amount is expected to be for support of the armed forces including Internal Security Forces.

E. Arab Fund for Economic and Social Development

The total AFESD contribution is expected to reach \$750 million. Initial discussions were held between H.E. Prime Minister Siniora and the Director General Mr. Abdulatif Y. Al-Hamad regarding the allocation of these funds on April 11th, 2007. The Lebanese Government has proposed to the AFESD financing the Independent Power Producers project. Loans from the AFESD are usually based on agreements for financing certain projects proposed by the Lebanese Government. Several Loans from the Fund were under preparation at the outset of the Paris III Conference for \$203 million in the areas of public administration, water and private sector rehabilitation.

DETAILS OF PLEDGES

F. France

The French contribution of \$650 million (€500 million) will be channeled through the AFD according to the following:

1. A loan to the private sector for \$163 million (€125 million) through intermediary banks. Please refer to the section "Support to the Private Sector & Other".
2. The remaining \$488 million (€375 million) is expected to be for debt replacement similar to the transaction performed at Paris II. French Parliamentary approval is required for this support and is expected to take place during Parliamentary extraordinary session this summer. A mission was in Lebanon headed by Mr. Jean-Pierre Jouyet, then *Chef de l'Inspection Générale des Finances* and now Minister of European Affairs on April 26, 2007. The mission discussed the possible terms and triggers of disbursements. These triggers are modeled on the IMF EPCA Program. The agreement is expected to be finalized in the second half of 2007 following the French Parliamentary approval.

These grants are governed by the EU Neighborhood Policy and are focused on support for political reforms, support to social and economic reforms, and support to reconstruction and recovery.

3. A micro-financial assistance (MFA) package of \$98 – 104 million (€75 - €80 million). The package consists of a \$65 million (€50 million) loan and \$33 - \$39 million (€25 - 30 million) grant to offset the interest payments related to the loan. The aim of the loan is budgetary support with the disbursement taking place in two to three tranches upon completion of certain reforms agreed to by the Lebanese Government and the EC. These terms are currently under discussion.

In parallel to discussion regarding the terms of the package, the EC will be presenting the MFA to member states starting June 2007 with the final approval required from EU member states' Ministers of Finance. EU Parliamentary approval is expected by the end of 2007. Disbursement will take place over a two year period.

G. European Commission

The total European Commission support of \$486 million (€374 million) comprises:

1. Relief and humanitarian support in the context of the Stockholm Conference for Early Recovery in the amount of \$137 million (€107 million). These grants were used for various relief efforts after the Israeli July War.
2. Grants in the framework of EC cooperation with Lebanon for the period 2007-2010 amounting to \$243 million (€187 million).

H. United Arab Emirates

On February 20th, 2007, the first agreement after the Paris III Conference was signed with the United Arab Emirates through the Abu Dhabi Fund for Development. The agreement was for a loan totaling of \$300 million for budgetary support. Details of the loan are provided in the first progress report.

- 2 \$100 million from the Arab Trade Financing Program (a subsidiary of the AMF) aimed at supporting the private sector.

Please refer to the section titled “Support to the Private Sector & Other”. Discussions are underway with the majority of the remaining donors with information available in the table of sector allocation.

I. Islamic Development Bank

An IDB mission visited Lebanon the week of February 26th and reviewed possible projects for financing. Loans for projects in the social sector have very preferential terms at 1 percent of interest and a grace period, making these loans almost a grant. Projects under consideration in the social sector include hospitals and schools. In addition, part of the loans will be allocated to infrastructure including projects in water and waste water and for roads. The allocation between the two sectors is still under discussion and the list of project is not final. A follow-up mission from IDB to finalize the agreement is expected in the third quarter of 2007.

J. Arab Monetary Fund

The Arab Monetary Fund total contribution of \$250 million is allocated to:

1. \$150 million in budgetary support for structural adjustment (public finance and financial markets sectors). A mission to discuss and agree on the structural adjustment measures is expected to visit Lebanon in the second half of 2007. The structural measures are expected to be in the fiscal domain.

INSTITUTIONAL STRUCTURE FOR IMPLEMENTING REFORMS

The Government of Lebanon has set up an overall structure to conduct and supervise the implementation of the Paris III reform program. This structure envisages a Government Reform Program Coordination Office (GR PCO) based at the Office of the President of the Council of Ministers. The GR PCO has the responsibility for the overall coordination of the implementation of Paris III socio-economic reform program. The GR PCO liaises with and supports the work of three Inter-Ministerial Committees (Social, Economic, Infrastructure & Privatization) chaired by the President of the Council of Ministers. The three IMCs include Ministers and Heads of Public Sector Entities that are directly involved in the implementation of Paris III reform initiatives.

The Government has set a socio-economic reform plan consisting of more than 316 initiatives grouped into 50 programs. It has prioritized these initiatives based on their socio-economic impact, legislative requirements and ease of securing budget. As a result, it has identified 116 short-term initiatives that could be implemented by November 2007. These are split as 40 social initiatives, 39 economic initiatives and 37 infrastructure and privatization initiatives.

A. Progress to date

1. The three IMCs organized their first round meetings from May 15th to 17th, 2007 and appointed Secretaries which would provide administrative support. They have started the process of allocating Paris III reform initiatives to "Natural Owners", endorsing and determining resource requirements (technical assistance and financial). It was agreed that these IMCs will meet on a monthly basis to resolve issues escalated from line Ministries and Public Sector Entities.

The IMCs will also re-calibrate and re-prioritize sector initiatives, as necessary and oversee coordination and integration within ongoing Government activities. Finally they will report progress to Council of Ministers and escalate any unresolved issues. The IMCs can also engage external constituents to seek formal input on specific policy areas, such as private sector or civil society associations, or Public-Private Partnerships. These external constituents will act as consultative entities to IMCs.

(a) **Social Inter-Ministerial Committee**, includes the Ministers of Social Affairs, Health, Education, Labor in addition to the Director General of the National Social Security Fund (NSSF). The Paris III social reform program includes 129 social initiatives constituting 41% of the reform program initiatives committed during the International Donors Conference. Each "Natural Owner" has developed initiatives to improve and promote the performance of the social sector. The Ministry of Social Affairs assumed the Social IMC Secretariat.

(b) **Economic Inter-Ministerial Committee**, includes the Ministers of Finance, Economy and Trade as well as the Minister of State for Administrative Reform, and Central Bank Governor. The Paris III economic reform includes 112 initiatives constituting 35% of the total number of initiatives committed during the International Donors Conference. Each "Natural Owner" has developed a series of short-term initiatives to reform the economic and fiscal sectors. The Ministry of Finance assumed the Economic IMC Secretariat.

(c) **Infrastructure and Privatization Inter-Ministerial Committee**, includes the Ministers of Telecommunications, Energy and Water, Transportation, in addition to the Secretary General of the Higher Council for Privatization (HCP) and the President of the Council for Development and Reconstruction (CDR). The Paris III infrastructure and privatization reform program includes 75 initiatives constituting 24% of the total number of initiatives committed during the International Donors Conference. Each "Natural Owner" has developed a series of short-term initiatives to improve public infrastructure and service levels, as well as progress on privatization efforts. The Prime Minister's Office assumed the Infrastructure and Privatization IMC Secretariat.

2. Each "Natural Owner" has assigned a Monitoring & Support Unit (M&S) to develop its Paris III reform plans into Program Charters and detailed work plans, with the technical assistance of the GR PCO. The "Natural Owners" will report progress on a monthly basis to their respective IMCs and will liaise closely with the GR PCO through the M&S Unit. They are in the process of developing charters and detailed work plans for implementation. Program charters and detailed work plans will include objectives, key implementation risks, resource requirements (technical assistance, budget & team), work plan, milestones of key deliverables, and key performance indicators (KPIs) that assess the efficiency, impact and sustainability of the reform initiatives. Moreover, "Natural Owners" will determine Technical Assistance requirements with the support of their M&S Unit and the GR PCO and they will assign resources to implement Paris III initiatives. Finally, they will manage conflicts around inter-dependencies with other "Natural Owners", resolve issues

within their own authorities and escalate unresolved issues to the GR PCO and the IMC.

B. In the medium term

1. Each M&S unit will finalize program charters and resource plans, supported by GR PCO.
2. Identify and approve funding and technical assistance needed. These needs once finalized will be communicated to the Inter-ministerial Committees.
3. To formalize the structure, the Natural Owners will finalize and endorse a Paris III commitment document (PCD). This document will be the basis on which the IMCs will follow-up on the reforms with each ministry / institution.
4. IMCs will filter requests for technical assistance and decide on TA/funding allocation.
5. Review monthly progress of implementation and start steady-state implementation progress reporting.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

A. Social Reform Program

Social Affairs

The Ministry of Social Affairs (MoSA) is focusing on the short term on three work streams:

1. Enhancement of the management of the social sector through elimination of duplication in service delivery and program implementation among the Ministries of Social Affairs, Education and Public Health, through increasing coordination in the implementation of local development projects, as well as formulating a social strategy to act as framework for all social related actions and interventions.
2. Reform and restructuring of the Ministry of Social Affairs by reviewing the mandate and programs of MoSA, revisiting the organizational structure, and implementing process re-engineering and automation of MoSA.
3. Establishment of a targeting mechanism (proxy means testing) as a first step towards the implementation of a number of social Safety Nets aimed at assisting the very poor and vulnerable population.

The Ministry of Social Affairs is working towards enhancing the management of the social sector through the following concrete measures.

Firstly, formulation of a comprehensive social strategy is underway. An advisory board was created to provide guidance and technical support in the elaboration of a social strategy. The board is led by MoSA and will provide a strategy framework by end of July 2007, to be later developed into a comprehensive social strategy.

Secondly, eliminating duplication in service delivery between ministries in order to identify all duplicated or overlapped programs and

services in each ministry (MoSA, MoH, and MEHE) including budget, administrative structure, beneficiaries; etc. has been launched. In June 2007, a staff member was assigned from each concerned ministry to follow-up with the Social IMC on the overlap in the provision of social services between ministries. Identification of duplicated programs and services is underway and a draft report is expected in July 2007. Bilateral meetings will then be organized between social ministries and recommendations will be prepared for efficient roles of each duplicated program in the third quarter of 2007. Building on recommendations, a time bound action plan for the duplication of services will be prepared. It is expected that the Social IMC will approve a time based action plan that eliminates duplication between MoSA, MOH and MEHE by September 2007.

MoSA is addressing the **coordination of local development projects**. An expert was subcontracted to map existing local development projects to provide a solid base for identifying overlaps and gaps in their implementation. The expert is expected to submit a final draft of mapping before end of July 2007.

MoSA has already achieved some progress in the **reform of certain programs (Care and Local Development)**. The Ministry has formulated improved procedures for the implementation of local development projects in partnership with concerned stakeholders. In addition, it developed a new system and a set of eligibility criteria of NGOs and welfare institutions wishing to be subcontracted by MoSA. Both items are expected to be finalized and approved by the Minister before December 2007.

Preparations for the implementation of social safety nets are underway.

Within the context of Social Protection DPL, an activity has been launched to **establish a targeting mechanism for strengthening poverty and vulnerability focus of the social safety net programs.** To date, processing and analysis of the 2004 multi-purpose household survey are underway. Furthermore, preparations for developing a roadmap for implementation of a new targeting mechanism have been progressing. It is expected that the Social IMC will have issued a decree introducing targeting mechanisms with a roadmap for its implementation by September 2007.

Health

The Ministry of Health (MoH) is developing a reform program, in alignment with the World Bank's Social Protection Development Policy Loan. In the short term, the Ministry of Health is focusing on the following work streams:

1. Upgrading of primary healthcare (PHC) services
2. Targeted interventions for maternal and child mortality reduction
3. Implementation and institutionalization of public hospital accreditation program
4. Development of common health insurance standards, procedures and functions
5. Enhancement of public health functions and programs
6. Undertaking pharmaceutical reform through updating the re-pricing of all drugs registered between 2000 and 2006.

The MoH is implementing a reform program, within the context of the planned Social Development Policy Loan, to **upgrade primary healthcare services.** The initiative aims to revitalize primary healthcare through the implementation of a five year action plan based on a recently developed primary healthcare strategy for the country. The proposed action will focus on improving the effectiveness and quality of primary healthcare services provided by the network service providers currently being overseen and supported by the Ministry of Health. As a first step, this program will be carried out through:

- (i) Defining catchment areas for 120 centers, and linking the primary healthcare centers with referral public hospitals in each catchment area as part of a new district health management system
- (ii) Developing a health card system
- (iii) Expanding IT infrastructure of 120 catchment areas. This activity is expected to be launched in Q4 2007, contingent on the availability of funds.

In parallel, the **development and implementation of PHC accreditation program** has commenced in June 2007, funded by the Italian Cooperation and Development is expected to be finalized in December 2007. Expected outputs are: quality assurance performance indicators and accreditation standards. This will followed by an implementation phase.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

The roll-out of the targeted interventions program for maternal and child mortality reduction is to be launched contingent on the availability of funding. Then, the successful pilot project of Wadi Khalid (Akkar) is planned to be rolled out, in collaboration with public hospitals in 10 areas: Akkar, Tripoli, Dennyeh, Baalbeck, Hermel, Rachaya, Hasbaya, Marjeyoun, Bint-Jbeil, and Nabatiyeh with the support of UNICEF. This activity is expected to be launched in Q1 2008.

MoH is implementing and institutionalizing a public hospital accreditation program, in collaboration with the Ecole Supérieure des Affaires (ESA). The contract was signed in May 2007, is pending approval of the court of accounts and is funded from the Ministry of Health's 2007 budget. Experts of the French Health Authority (HAS) are expected to be mobilized in Q3 2007, to undertake the following:

- (i) Conducting training on accreditation to 25 public hospitals
- (ii) Establishing a short list of "accredited" certification companies
- (iii) Updating and upgrading accreditation standards
- (iv) Conducting a survey to public hospitals.

The expected timeline for completion is Q4 2008, eighteen months following commencement.

MoH is **developing common health insurance standards, procedures and functions.**

Short-term initiatives activities include:

- (i) Completing the pilot testing of the visa billing system
- (ii) Updating the National Health Accounts (NHA) to make health expenditure data available for appropriate and targeted health policies

Completing the pilot testing of the visa billing system is currently underway by the Ministry of Health and expected to be completed in October 2007. Furthermore, the Ministry of Health is currently working on developing National Health Account matrices for 2004 and 2005 and preparations are underway to institutionalize the collection and extraction of data at each public fund for 2006 and 2007. Subsequently, a WHO expert will be mobilized for installing the appropriate software and template.

On the other hand, the **re-commissioning of the work on the standardization** of codes, forms, and payment methods, and the integration of the Health Management Information System (HMIS) across funds has commenced within the context of the Social Protection Development Loan. A consultant funded by the World Bank is currently conducting situational analysis to redefine common business procedures and advise on utilization control mechanisms for both MOH and NSSF mainly relating to contracting with private providers and integration and upgrade of health management information system and insuring an effective utilization review. The proposal is expected to be finalized in July 2007, to be followed by an implementation plan.

The reform effort to fully develop and operationalize the **National Expanded Program on Immunization (EIP)** will be initiated by the Ministry of Health with close support from UNICEF, the World Health Organization and the World Bank. The envisaged 5 year reform effort will build on existing support provided by UNICEF and WHO in order to scale up current activities towards a fully institutionalized national EPI program. The MOH and UNICEF have agreed on a one year work plan focused on strengthening routine and supplementary immunization services with five different components: program management, service delivery, communication, capacity-building, and monitoring and evaluation. This activity is expected to be launched in Q3 2007, contingent on the agreement between MOH and MOF to finance this activity under a separate program budget.

Another critical aspect of a health system – a core public health function of the state – is **integrated disease surveillance and response**. The Ministry of Public Health in Lebanon has made great improvements over recent years in working towards the establishment of such a system. The Ministry of Health has submitted a workplan to the World Bank within the context of Social Development Policy Loan to:

- (i) Build capacity of MOH on communicable diseases surveillance
- (ii) Set up an institutional mechanism for electronically networking focusing on diseases reporting, information sharing and use of GIS
- (iii) Develop a national reference laboratory at Beirut Rafic Hariri Governmental Hospital to conduct biological tests required for notifiable communicable diseases. This activity is expected to be launched in Q3 2007, contingent on the availability of funding.

MoH is undertaking pharmaceutical reform, by re-pricing all drugs registered from 2000 to 2006. The activity has been progressing with the completion of re-pricing all drugs registered after the year 2001 in December 2006. The expected date for re-pricing all drugs registered between year 1996 and 2000 in July 2007. For products registered before the year 1995, documents will have to be submitted before July 2008.

Education

The educational sector is undergoing significant strategic changes, in line with a 3-year reform program undertaken by the Ministry of Education and Higher Education (MEHE). Several initiatives have been ongoing for several months, with some streams showing significant progress. The short term programs include:

1. Consolidation of policy, planning and resource allocation
2. Improvement of efficiency, effectiveness and competence level of the teaching workforce
3. Enhancement quality of education
4. Enhance strategic management of educational facilities through consolidation of small unviable schools

A number of initiatives are currently underway to consolidate policy, planning and resource allocation.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

Education Sector Strategy was completed in April 2007. The document was approved by MEHE stakeholders, submitted to the Council of Ministers for endorsement and expected to be finalized by September 2007. The strategy aims at providing:

- (i) Education on the basis of equal opportunity
- (ii) Quality education that contributes to building a knowledge society
- (iii) Education that contributes to social integration
- (iv) Education that contributes to economic development
- (v) Governance of education

Implementation of the 3 year strategy will be launched in the third quarter of 2007, with MEHE planning to integrate and implement policy, planning, and Information Management functions at MEHE.

A comprehensive study on “**Rationalizing the Financing of the General and Vocational Education System in Lebanon**” was completed in April 2007. The study identified and documented all monetary and non-monetary resource flows within the public and private sectors in Lebanon. This permitted the assessment of efficiency and equity of the current distribution of resources across schools, sectors, regions and socio-economic cohorts in addition to the public management of resources. An important output of the study was the development of a financial model for estimating required expenditures for education policies. This model is providing guidance for high-level decision makers through development of framework and methods necessary for evaluating policy options that improve the efficiency and equity of resource allocation.

To provide continuity of measures and methods over time and facilitate monitoring policies and benchmarking results, additional steps are currently undertaken to support the reform process. A technical assignment was launched to integrate the methods and strategies into an ongoing **Financial Planning and Decision Making Function** at the Ministry of Education and Higher Education. This phase will commence in July 2007 as the consultant to undertake this activity will be mobilized then.

MEHE has started the process of developing and disseminating **model performance-based budget for 2008-2009** in coordination with the Ministry of Finance. A committee was established at MEHE to be the core counterpart in preparing the **Medium Term Expenditure Framework** and is expected to prepare the ingredient lists and relevant costs for all required activities and functions based on priorities extracted from the education sector strategy, by November 2007. This will permit the analysis of the relative efficiency of policy alternatives in producing educational outcomes.

MEHE is implementing Education Management Information Systems (EMIS) at the Ministry, and School Information Systems (SIS) at schools. A school information system (SIS) should be installed in 1500 schools and EMIS contract should be signed by September 2007.

An **organizational audit** was completed, examining the mandate, structure, efficiency, staffing and decision making process at MEHE. A Joint Committee chaired by the Director General (DG) of Higher Education and comprised of representative from OMSAR, the Civil Service Bureau, the Directorate of Vocational Education, the Minister's Advisors and the DG of Education was established by a Ministerial Decree in order to provide recommendations on developing a revised organizational structure and was based on results from MEHE's Organizational Audit. The Joint committee submitted a draft of the Restructuring Action Plan and Monitoring for restructuring assignment in May 2007.

A firm was selected and will commence by end of June 2007 on developing a **revised organizational structure** that will detail the functionality of all MEHE units, develop position descriptions, revise relevant decrees and regulations and formulate and deliver professional development activities.

MEHE has also embarked on improving the efficiency, effectiveness and competence level of the teaching workforce through the leadership and instructor development programs.

The first phase of **Leadership Development** was completed with 121 school principals completing a professional development program designed to improve leadership, motivational and management skills, together with improved understanding of international trends in competency based contextualized learning (October 2006). Each candidate prepared and is implementing a school development plan for his/her school. 303 candidates who are currently enrolled in the second phase of the program are implementing the self guided

modules and practicum phase which is expected to be completed in October 2007. Progress towards institutionalizing the Leadership Program within MEHE and the Lebanese University is ongoing to maintain sustainability and development of the leadership training program for school principals. In this respect, the Lebanese University is to be mandated, through the Faculty of Education, to provide in-service professional development for School Principals.

With regards to instructor development, **15 regional resource centers have been established throughout** Lebanon for in-service training. 270 have been selected and trained to become Master Trainers. 24 candidates are being trained by NGOs to provide support to students with special needs. Since 2004, 11000 teachers have received training through the Instructors Continuous Program.

Enhancing the assessment of academic achievement has been progressing. MEHE teams have developed Evaluation Kits to provide a basis for the assessment of student learning. Over 1000 kits have been prepared and validated. An Exam Generation System has been developed, and consultants have been recruited to develop a Question Bank System, and Examination Management System which are expected to be ready by November 2007.

In order to enhance strategic management of educational facilities, criteria for school consolidation (# of students, student/teacher ratios, constructed area, distance...) have been set and a total of 20 primary non viable will be consolidated as soon as MEHE reach an agreement with respective Parliament members on consolidation.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

Labor

The main initiatives of the Ministry of Labor (MoL) revolve around streamlining laws and regulations to facilitate access to skills and increase employer flexibility MoL is considering to:

1. Streamline work permit procedures for skilled foreign workers and executives, and simplify duplicative pre-approval of Ministry of Labor
2. Revise labor laws to facilitate employment of temporary and seasonal workers, and youth labor
3. Review procedures for termination of employment agreements to allow simple notification, and consider removing MoL approval and investigation

These initiatives, expected to start in July 2007, depend on the availability of funding.

Social Security

The National Social Security Fund (NSSF) is developing a reform program in coordination with the World Bank, and part of the Social Development Policy Loan. Reform initiatives revolve around rationalizing and expanding the coverage of social insurance system, strengthening NSSF governance and administration, improving NSSF financial sustainability, and strengthening income protection policies.

Most of these initiatives are expected to be formulated by September 2007, in close consultation between the NSSF and the World Bank.

B. Economic and Fiscal Reform Program

The Paris III economic reform program includes around 35% of the total number of initiatives committed during the International Donors Conference. This program will be implemented by the Ministry of Finance (MoF), Ministry of Economy & Trade (MoET), the Central Bank (BDL), and the Office of the Minister of State for Administrative Reform (OMSAR). Each “Natural Owner” has developed a series of short-term initiatives to reform the economic and fiscal sectors.

Finance

In addition to its responsibility in the negotiation and implementation of the Paris III pledges, most especially the currently-under-negotiation US\$ 1.47 billion in budgetary support loans and grants, and its donor coordination role, the Ministry of Finance has developed an ambitious reform program for the 2007-2009 period. In the short-term, MoF initiatives will focus on:

1. Rationalizing expenditures
2. Enhancing government revenues
3. Undertaking budget and financial reform
4. Undertaking revenue management and tax administrative reform toward a function-based structure
5. Strengthening debt management
6. Reforming capital markets

The Ministry of Finance is working towards the rationalization of expenditures which has included the following three concrete measures in the first six months of 2007. Firstly, expenditures on travel and communication have been restricted as communicated in the 2008

budget circular which was issued in May 2007. Second, a decree was issued in the second quarter of 2007 to pay the “Council of the South” and the “Fund for the Displaced” the first LL 100 billion out of their dues needed for closing the funds (decree # 292 dated 27/04/2007). To date, 35% of this LL 100 billion have been paid in total. Third, to contain the wage bill in the medium term, a hiring freeze was put in effect as issued in the 2008 Budget Circular, stipulating the need for a Council of Ministers’ decision for any urgent hiring need.

In addition, the Ministry of Finance has embarked on **enhancing revenue** collection. Despite the currently existing political situation, total revenues have increased by around 9 percent for the first four months of 2007 when compared against 2006. More specifically, on the short term revenue enhancement front, since the beginning of 2007, the Treasury's share of Casino du Liban revenues has been expanded from 30% to 40%. Revenues from Casino du Liban have increased by 38% in the January to May period 2007 compared to the same period in 2006. Also as part of a revenue enhancing and administrative reform, the built property tax database has been linked to the Cadastre's database since January 1st, 2007. The update of the database is an ongoing process. Comparative figures indicate that as a result, revenues of property tax during the first five months of 2007 have increased by 36% compared to the same period of 2006. Another major revenue collection enhancement policy planned for by MoF is to lift the cap on domestic car gasoline prices to align domestic prices with international prices and to gradually increase the excise rate to reach the pre-cap rate starting with the excise rate floor at LL 300 per liter for 2007.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

The uncapping mechanism has been proposed and an internal study on the distributional impact of the uncapping has been completed. A Council of Ministers decision remains to be adopted in this regard. A study on the possible needs and ways to subsidize the most affected income groups is required prior to the uncapping.

A number of initiatives are being implemented by MoF in its bid to **implement a full fledged public financial management reform by undertaking budget and financial reform**. For the first time, actual steps for adopting a top-down budgetary process has been taken, by including the medium-term expenditure framework as part of the budget circular for 2008 May 20th, 2007, a process that is expected to continue until 2011. For budget year 2008, the Medium Term Expenditure Framework will constitute a general guideline for the spending agencies, in order not to exceed the proposed global budget envelope. MoF is preparing for a second step in this process, that will be concluded in March 2008, to prepare a medium term expenditure framework with a budget ceiling for each Ministry, and to be discussed in the Cabinet by then. The new budget preparation techniques were presented to around 200 high level representatives from spending agencies in a workshop in May 2007. As part of a series of planned ongoing workshops, two have been held in the second quarter of 2007 with MoF officials to discuss the reform plan and to seek the participation from different working groups. On another front, in preparation for the MTEF in coordination with spending agencies and in preparation for the introduction of performance-based budgeting, the Ministry of Education was chosen to serve as a pilot (June 2007). A core unit has been formed at the Ministry of Education for this purpose and a team from this Ministry was sent on a study tour

to Morocco, to get acquainted with the Moroccan experience in this context. In addition, MoF has prepared and submitted to Cabinet a draft 2007 budget law consistent with the targeted primary balance of the central government including HRC spending and CDR foreign-finance expenditures.

In terms of improving **revenue-management and administrative reform**, an administrative reform towards a function-based structure that has been initiated is the reorganization of the regional tax offices along function-based operations. The Council of Ministers had signed a restructuring decree in this regard. By the end of 2007, it is expected that clarifying instructions for the newly established departments, such as prerogatives, in the regional tax offices are issued and that the follow-up collection function is moved from the Treasury to tax offices. In addition, the restructuring decree approved the organizational structure of satellite offices. As such, it is expected that taxpayer services are established in satellite offices gradually starting with the most important sub-regions in terms of fiscal coverage (by end-2007).

On the tax administration front and modernizing legislation, the MoF has introduced the Tax Procedure Code that unifies and harmonizes various tax procedures. The TPC draft law has been finalized, was approved by the Council of Ministers, and is presently being negotiated at Parliamentary Committees. The development of implementation decrees is expected to be completed by end-2007. In addition, an internal version of the Global Income Tax draft law to replace the current schedular income tax system has been finalized. The draft law is currently undergoing final stakeholder consultations before submission of the Council of Ministers, which is expected to take place in Q3 of 2007.

The preparation of related regulations and procedures is expected to be completed by the end of 2007.

In terms of improving the delivery of services and administrative reform, the introduction of electronic registration of taxpayers has been initiated. Registration forms and documents have been finalized, the necessary decrees and decisions were issued (in 2006), and systems and procedures have been developed. By the end of 2007, it is expected that the systems and procedures are finalized, that the registration team within tax roll are trained, the necessary equipment is installed, and that a communication campaign and registration process are launched. In addition, progress has been achieved to put in place a new audit strategy based on risk selection criteria, new audit techniques and procedures, and the development of an audit manual. Central audit and compliance teams were formed in March 2007. The following month, the annual audit budget plan and program was prepared. Progressive implementation has been in place in four pilot sites (Beirut, Mount Lebanon, Value Added Tax department, Large Taxpayer's Office). The development of a procedure manual, of scoring system and criteria and other deliverables is expected by end-2007. In addition, a 24/7 call center to provide around the clock serves for all taxpayer inquiries was launched in May 2007, reflecting the focus on client-oriented services by improving communication with clients. As a testament to the efforts of the Ministry of Finance's innovation and reform in this area, MOF was awarded the prestigious United Nations Public Service Award in 2007 for the category "Improving the Delivery of Services" for Taxpayer Services.

To **strengthen debt management**, the Ministry of Finance has initiated a number of reform

measures. In this regard, one draft law to establish an integrated debt management unit at MOF and to create a "Higher Council for Debt Management" to formalize and enhance coordination between MOF and BDL awaits parliamentary approval. On another front, in order to improve debt reporting and transparency, MOF has already issued an internal debt report and expects to regularly publish quarterly debt publications by end-2007. Preparations for developing a formal debt management strategy have been completed with the circulation of a quarterly internal financing strategy report prepared since May 2006. MoF has also initiated the development of secondary market liquidity in LL by introducing five-year treasury bills (in Q1 2006); an instrument aimed at organizing and lowering the frequency of market auctions. The study of introducing further longer maturity TBs is an ongoing process and is highly dependant upon the prevailing political environment.

In contributing to the **improvement of the business environment**, the Ministry of Finance has provided tax incentives for enterprises affected during the war as undertaken in the second half of 2006. The installment of dues for VAT and DASS for Q2 2006, the exemption of penalties, and the extension of filing deadlines were implemented. Following up on these measures, it is expected that development procedures to verify the declared damage and to reconstitute lost tax records as well as to increase the period allowed for loss carried forward is expected by end-2007. In addition, the loan-guarantee agency Kafalat, raised the ceiling of guaranteed loans to LL 600 million in mid-2006. Kafalat which covers the industry, agriculture, tourism, traditional crafts and high technology sectors also made provisions for small and medium enterprises affected by the war.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

With BDL, three options for damaged SMEs were developed by Kafalat and administered on a case by case basis: rescheduling of the loan, granting an additional grace period, and re-injecting funds to purchase damaged equipment/machinery. Another measure to improve the business environment through capital market reform, has been the drafting of a draft capital markets law which awaits parliamentary approval.

An IMF mission, concluded on May 28, 2007, held discussions for the 2007 Article IV consultation and reviewed performance under the EPCA program. The mission mainly concluded that 2007 continues to be a difficult transition year, Lebanon is on target under the EPCA program, and the authorities have managed skilfully the financial and fiscal pressures from the July 2006 war with Israel.



Economy and Trade

Ministry of Economy and Trade (MoET) has developed a reform program along 4 axes:

1. Encourage investment
2. Promote and strengthen Intellectual Property
3. Further facilitate trade and enhance trade competitiveness
4. Enact laws to improve the business environment

In the short-term, MoET is **encouraging investment** by taking measures to streamline business registration & licensing, and eliminate minimum capital requirements. The current business registration process is complex, lengthy and time consuming. In addition it is a costly process involving multiple payments at every step. The Government, in cooperation with the IFC and key stakeholders is engaged to streamline business registration and licensing. Its aim is to reduce the time it takes to obtain a business license, to reduce the cost of opening and closing a business, as well as to facilitate the process to ensure more transparency and efficiency. For this purpose, MoET has completed the mapping of Business Registration Procedures, undertaken a study on streamlining administrative barriers to investment in coordination with the Foreign Investment Advisory Service (FIAS), and issued recommendations about new and improved business registration procedures as presented in a workshop held on the 22nd of June 2007. The design of an action plan to implement the study findings is under discussion and has not yet formally begun.

In order to achieve a simpler, transparent, fast and reasonably priced registration process, a number of initiatives are being planned for 2007. Short term implementation initiatives that do not require parliamentary approval are expected to be accomplished by the end of Q3 2007. These measures include the consolidation of all fees upfront, the standardization of forms and applications, the creation of a user guide detailing required steps for registration, and the finalization of a Memorandum of Understanding with LibanPost to allow for one package consisting of one application, one payment and one contact point in the process. The Ministry of Justice, Ministry of Economy and Trade, Ministry of Finance, Commercial Registries, National Social Security Fund, and the Prime Minister's office are engaged in this measure. Longer term initiatives in the pipeline require legal changes. By the end of 2007, a matrix identifying all laws to be amended should be completed.

Another initiative to encourage investment has been the successful establishment of 4 Business Development Centers (BDCs) by MoET in 2006-2007 in Beirut, Saida, Tripoli and Zahle. By September 2007, MoET will engage in extensive training program for BDC managers on incubation and working with companies. It will also propose an accreditation system to BDCs for business councilors.

MoET is **promoting and strengthening Intellectual Property (IP)**. MoET drafted amendments to the Copyright Law, and sent it to concerned ministries for review and feedback on April 20th, 2007. The Ministry also drafted the new Trademark Law, and had sent it to the Council of Ministers in March 2006. The Council of Ministers in turn, forwarded the Trademark draft Law to the relevant Ministries for review. MoET received the feedback end of

April 2007. Also, MoET is strengthening the capabilities of the Intellectual Property Protection Office (IPPO) in the fields of IP enforcement and development of human resources. This activity requires Technical Assistance to undertake IP training and develop job description for IP inspectors. The expected timeframe for the IPPO project extends until Q4 of 2008.

To **further facilitate trade and enhance trade competitiveness**, MoET has activated the existing National Committee on Trade and Transport Facilitation. However, it requires technical assistance to draft a three-year master plan.

Finally, MoET is working on **improving the business environment**, by preparing Laws on Standards, on Technical Regulation & Conformity Assessment, and Competition. Technical assistance is needed to finalize the drafting of some of these Laws. The draft Laws on Standards and draft Law on Technical Regulation and Conformity Assessment await Ministry of Industry signatures before being sent to the Council of Ministers. The competition Law is expected to be finalized by experts in mid-July 2007. Implementation of the Protection of National Production Law, issued by Parliament in Q4 2006, is expected to begin by end-2007.

Central Bank

In the short-term, the Central Bank is contributing to the Paris III reform program, by undertaking the following activities:

1. **Maintain floor on BDL gross reserves** (On-going activity)
2. Undertake measures to **enhance access of businesses to credit**

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

In the longer term, the Central Bank is planning to:

1. Transfer regulatory control from BDL for MIDCLEAR, and for securities business
2. Divest BDL's portfolio by selling part of its shares in MEA and Intra Investment Corporation

Administrative Reform

The Office of the Minister of State for Administrative Reform (OMSAR) is **modernizing the procurement code** to help bring procedures to international standards. The draft law for public procurement and the draft law for the reorganization of the public procurement administration will be finalized by end-August 2007. Following approval of the Economic Inter-Ministerial Committee (IMC), these draft laws will be submitted to the Council of Ministers for endorsement.

OMSAR is also **addressing corruption in the administration**. To this end, it is in the process of identifying candidate ministries to be subjected to the anti-corruption project and is developing Terms of Reference (TOR) for the consultancy firm. By September 2007, TORs for the consultancy firm will be ready and candidate ministries identified. However launching the bidding process is subject to the availability of funds which have not yet been identified.

OMSAR is **developing modalities for outsourcing tasks carried out by the public sector**. By September 2007, OMSAR will identify, in coordination with concerned Ministries, the tasks to be outsourced to the private sector. OMSAR will develop the TORs and scope of work for the consultancy firm which will analyze findings and identify priority activities, and propose a mechanism to such outsourcing based on international best practices.

In addition, OMSAR is preparing an **action plan for the implementation of the e-Government strategy**. OMSAR is currently in the process of developing TORs for consultants to review and update the e-government strategy and develop a high level national action plan, and update the e-readiness assessment. By September 2007, TORs will be completed. However, the launch of the bidding process will be subject to availability of funds. Projects are being implemented depending on the availability of incoming funds. An e-procurement development project funded by a mini-grant has been initiated with results expected in mid-2008.

Finally, OMSAR is **implementing a training program for the Ministry of Health (MoH)**, particularly in Information Technology. By September 2007, the preliminary assessment of MoH training needs will be completed and the preparation of TOR kicked-off.

C. Infrastructure and Privatization Reform Program

The Paris III Infrastructure and Privatization reform program includes around 24% of the total number of initiatives committed during the International Donors Conference. In order to oversee the implementation of this program, an Infrastructure and Privatization Inter-Ministerial Committee (IMC) has been established. The program will be implemented by the Ministry of Telecommunications (MoT), Telecommunications Regulatory Authority (TRA), Ministry of Energy and Water (MoEW), Council for Development and Reconstruction (CDR), Electricité du Liban (EDL) and the Higher Council for Privatization (HCP). Each “Natural Owner” has developed a series of short-term initiatives to improve public infrastructure and service levels, as well as progress on privatization efforts.

Telecommunications

The telecommunications sector reform plan entails three major programs:

1. Establishment of the Telecommunications Regulatory Authority (TRA) to regulate the telecommunications sector in order to achieve a competitive market delivering state-of-the-art services at affordable prices to the broadest spectrum of the Lebanese population
2. Corporatization of Liban Telecom (LT) in order to prepare the ground for privatization, hence implementing an important phase of the Telecom Law enacted in July 2002
3. Privatization of mobile telecommunications in order to improve service quality, offer a broader variety of services, alleviate public debt and budgetary deficit, and open access to best practice management and operations for the Lebanese mobile telecommunications sector

To-date, the **TRA has been established**, decrees defining its organizational and financial structures issued, its Board appointed, and its budget drafted and sent to the Ministry of Telecommunications and the Ministry of Finance for approval. Moreover, the TRA regulatory functions have been defined, and it has signed a Memorandum of Understanding with HCP on allocation of regulatory responsibilities in June 2007. (Please refer to Appendix D for TRA Progress as of June 28th). By the fourth quarter of 2007, all telecommunications regulatory functions would be transferred from the Ministry of Telecommunications to TRA, including radio frequency allocation. TRA has issued three regulations for consultation: Significant Market Power (SMP) Guidelines, Interconnection Guidelines, and Consumer Affairs Guidelines. The deadline to receive comments on all regulations is August 10, 2007.

As part of the **corporatization process of Liban Telecom**, the Council of Ministers issued a decree to establish Liban Telecom in January 2005 as a merger of Ogero and two divisions of MoT. An international consultant was appointed in November 2006 to assist in the establishment of LT, and a steering committee has been designated to oversee the implementation, pending the appointment of a board of directors for LT. The legal due diligence is underway, and a statistics company, human resource consultant and independent auditor have been retained to complete all the necessary groundwork. Finally, MoT launched broadband services in the Beirut area in May 2007.

PROGRESS ON IMPLEMENTING THE REFORM PROGRAM

Finally, the privatization of mobile telecommunications through the issuance of two mobile licenses is expected to be launched by mid-September 2007. Transaction advisors, along with a technical consultant and a financial auditor, were officially appointed in June 2007. Legal due diligence has been completed for one mobile operator, and is being completed for the other. The transaction design is currently being finalized.

Power Sector

The Power Sector reform plan first consists of three pillars:

1. Strengthening sector policy-making capacity
2. Enhancing the operational efficiency of Electricite Du Liban (EDL) to supply electric energy that is socially, economically and environmentally sustainable
3. Corporatization and privatization of EDL

In order to **strengthen sector policy-making capacity**, consultants have been selected to provide technical assistance to the Ministry of Energy and Water (MoEW). At the operational planning level, Electricité de France (EdF) has been hired to develop a Master Plan for the Power Sector, including a Public Investment Plan (PIP) for generation and transmission, and will start in July 2007.

To **enhance the operational efficiency of Electricite Du Liban**, a consultancy team has been selected to perform operational, financial, accounting, legal and contract management activities at EDL. Moreover, the government is working on reinforcing the capacity of the EDL finance department, and a financial auditor was appointed to audit 2002-2006 EDL financial statements. In addition, the operation and maintenance of Zahrani and Beddawi plants has

been subcontracted to a private company, and another private company has been contracted to supervise these operation and maintenance activities. Finally, a contract was signed with Egypt in April 2007, committing the supply of Natural Gas to the Beddawi plant starting the second quarter of 2008. The Government of Lebanon is also examining the provision of the Zahrani power plant with Liquefied Natural Gas (LNG) through a floating storage and re-gasification unit. Finally, a contract was signed and work has started since July 2006 on the establishment of a National Control Center (NCC) to audit grid performance and enable electricity import from neighboring countries.

In order to **corporatize and privatize EDL**, consultants have been selected to assist the Government of Lebanon in power sector restructuring. In addition, the Government of Lebanon is working to establish a power sector regulatory agency. In June 2007, a contract was signed between the Lebanese Government and the International Finance Corporation (IFC) to appoint IFC as an advisor in the transaction to license Independent Power Producers (IPPs) in Lebanon. An IPP Working Group has been formed, and the process should be fully launched by the fourth quarter of 2007. Finally, an international consultancy was appointed in November 2006, and is performing the groundwork for the tendering of licenses to private companies to install and operate meters.

APPENDICES

Appendix A: Key Initiatives undertaken and planned in 2007

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007		
	Status	Milestones
Fiscal Adjustment		
<i>I. Expenditure Measures</i>		
Reduce travel and communication expenses	Initiated	-Restriction of expenditures on travel and communication set in 2008 budget circular (Q2 2007)
Work on phasing out the "Council of the South" and the "Fund of the Displaced"	Initiated	-Decree issued to pay these two funds the first LL 100 billion out of their dues out of the LL 750 billion (Q2 2007) -First step towards closing the two funds performed by paying LL 35 billion of these due amount in May and June 2007 to date
Contain the wage bill in the medium term through reducing the size of the public sector by attrition and by limited hiring	Initiated	-Hiring freeze in effect and issued in Budget 2008 circular instructions which includes need for Council of Ministers' decision for any urgent hiring need (Q2 2007)
<i>II. Revenue Collection Enhancement Measures</i>		
Start expansion of Treasury's share of Casino du Liban revenues	Completed	-Expansion of Treasury's share of Casino du Liban's from 30% to 40% applied since Q1 2007 -Revenues from Casino du Liban increased by 38% Jan-May 2007 vs. same period 2006
Increase Casino du Liban revenue collection	Initiated	Expected by end-2007: -Council of Ministers' decision to settle Casino's past dues required
Enhance built property tax revenues through administrative reform of building up a comprehensive database on built properties	Initiated	-Property tax department information system linked to that of Cadastre since 1/1/2007. -Update of database is ongoing -To date 2,500 files have been updated -Revenues from property tax January – May 2007 have increased by 36% year on year
Prepare for lifting the cap on domestic car gasoline prices	Completed	-Uncapping mechanism proposed -Internal study on the distributional impact of uncapping completed
Lift the cap on domestic car gasoline prices, and set the excise rate floor at LL 300 per liter for 2007	Initiated	-Council of Ministers decision required -Study on possible needs and ways to subsidize most affected

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

income groups required

Structural Reform Measures under the Reform Program

I. Structural Fiscal Measures

A- Implement a full fledged public financial management reform

Prepare for the adoption of a top-down budgetary process linked to medium-term expenditure framework	Completed	<ul style="list-style-type: none"> -Detailing steps for implementation of reform prepared -Presentation of new budget preparation techniques to spending agencies in workshop (May 2007) -Workshop held with MOF Officials to discuss reform plan and to seek participation from different working groups (Q2 2007 and ongoing) within MOF and with spending agencies
Adopt a top-down budgetary process linked to medium-term expenditure framework	Initiated	<p>Expected 2007-2011:</p> <ul style="list-style-type: none"> -Preparation of priority sector distribution, based on which to distribute budget ceilings -Holding of successive workshops and training sessions to train spending agencies on new budget preparation techniques -Continue to communicate reform efforts within MOF and with spending agencies
Prepare for linking the budget preparation to a medium-term expenditure framework (MTEF) prepared by MOF	Completed	<ul style="list-style-type: none"> -2008 Budget Circular issued including reform measures Q2 2007 -Global budget ceiling as a guide for spending agencies
Link the budget preparation to a medium-term expenditure framework (MTEF) prepared by MOF	Initiated	<p>Expected by end-2007 and ongoing:</p> <ul style="list-style-type: none"> -Review spending agencies' budgets ensuring they reflect reform measures
Prepare for the introduction of a pilot to MTEF in coordination with spending agencies in preparation for the introduction of performance-based budgeting	Completed	<ul style="list-style-type: none"> -Ministry of Education chosen as pilot to prepare MTEF (June 07) -Programs, objectives, indicators and performance measurement introduced -Committee/unit formed in Ministry of Education to be core counterpart in preparation for performance-based budgeting (June 2007) -Team of Ministry of Education to participate in study tour to get trained on similar experience in Morocco

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

Introduction of MTEF (spending agencies)	Initiated	Expected (2007 – 2011): -Completion of MTEF by Ministry of Education -To build capacity of Ministry of Education and Higher Education to meet requirements of new budget preparation techniques -Selection of other ministries depending on availability of relevant sectoral strategies and based year data and performance data
Prepare and submit to Cabinet a draft 2007 budget law consistent with targeted primary balance of central government including detailed HRC operations and CDR foreign-financed expenditures	Completed	-HRC and CDR spending during 2007 estimated and included in 2007 budget (Cabinet of Ministers' decision # 51 dated 25/06/2007)
Submit to Parliament a draft 2007 budget law consisted with targeted primary balance of central government including detailed HRC operations and CDR foreign-financed expenditures	Initiated	
Continue the process of coordinating with CDR and HRC to produce annual budgets	Initiated	Expected end-2007: -HRC and CDR to produce yearly spending projections to be consistent with government's medium term framework under EPCA
<i>B. Revenue management and administrative tax reform</i>		
Prepare for the introduction of the "Tax Procedure Code" that unifies and harmonizes various tax procedures	Completed	-TPC draft law finalized and approved by Council of Ministers -Submitted to parliament for review
Introduce "Tax Procedure Code" that unifies and harmonizes various tax procedures	Initiated	Expected by end-2007: -Law finalization in parliamentary committees -Development of regulations -Council of State to approve regulations
Prepare internal Global Income Tax Law	Completed	-Draft law prepared (internal version)
Finalize draft Global Income Tax law and submit to parliament for approval and prepare related regulations and procedures	Initiated	-Draft law among final stakeholder consultations before submission to Council of Ministers (Q3 2007) Expected by end-2007: -Decide on major tax policy issues

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

		<ul style="list-style-type: none"> -Submit law to Council of Ministers -Develop regulations and tax policies -Develop forms and guides -Develop business procedures and processes -Launch consultations with sectors' representatives
Prepare for the reorganization of tax offices along function based operations	Completed	<ul style="list-style-type: none"> -Restructuring decree signed by Council of Ministers -Departments organized according to regions: Mount Lebanon, North, South, Bekaa, Nabatieh -Heads of departments appointed -Sections in Beirut tax office and LTO have been established in line with the created departments in regional tax offices -Staff allocated according to new functions/departments
Reorganize regional Tax Offices along function based operations	Initiated	<p>Expected by end- 2007:</p> <ul style="list-style-type: none"> -Issue necessary clarifying instructions for the newly established departments in the regional tax offices (ex. prerogatives) (July 2007) -Decide on transactions to be processed in satellite offices and related procedures -Move follow-up collection function from treasury to tax offices
Establish taxpayer services in satellite offices	Initiated	<ul style="list-style-type: none"> -Organizational structure of satellite offices approved according to restructuring decree <p>Expected by end-2007:</p> <ul style="list-style-type: none"> -Launch satellite offices gradually starting with most important sub-regions in terms of fiscal coverage
Prepare for the introduction of electronic registration of tax payers	Completed	<ul style="list-style-type: none"> -Registration forms and documents finalized -Necessary decrees and decisions issued (2006) -Systems and procedures developed
Introduce electronic registration of taxpayers	Initiated	<p>Expected by end- 2007:</p> <ul style="list-style-type: none"> -Finalize systems and procedures -Train registration team within tax roll -Install necessary equipment

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

		-Launch communication campaign -Launch registration process
Operationalization of call center for tax enquiries	Initiated	-Dedicated call center launched (21 May 2007) -Operation models for the call center have been defined -Front line services have been contracted to a specialized firm -Coordination with the supplier and building the tree of information by tax type in order to feed the knowledge base (ongoing)
Put in place new audit strategy based on risk selection criteria, new audit techniques and procedures, and develop an audit manual	Initiated	-Central audit and compliance teams formed (Q1 2007) -Preparation of the annual audit budget plan and program (April 2007) -Progressive implementation in 4 pilot sites (Beirut, Mount Lebanon, VAT, LTO) Expected by end- 2007: -Develop scoring system -Develop scoring criteria (based on risk analysis) -Develop audit procedure manual -Develop audit techniques, performance indicators, business processes and procedures, necessary automate functions
<i>II. Debt Management</i>		
Improve debt reporting and transparency through debt publication – Step 1	Completed	-First quarterly debt bulletin internally devised, reviewed and published
Improve debt reporting and transparency through debt publication – Step 2	Initiated	Expected end-2007: -Publish the quarterly debt publication in a timely manner
Introduce the necessary preparations for developing a formal debt management strategy	Completed	Quarterly internal financing strategy report prepared (since May 2006)
Develop a formal Debt Management Strategy	Initiated	Expected end-2007: -Finalize a formal debt management strategy
Formalize and enhance coordination between MOF and BDL and create a “Higher Council for Debt Management”	Initiated	-Law creating Higher Council drafted and awaiting parliamentary approval
Establish an integrated debt management unit at the Ministry of Finance	Initiated	-Law authorizing the creation of the integrated debt management unit drafted and awaiting parliamentary approval

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007		
Develop secondary market liquidity in LL by introducing longer maturity instruments with a low frequency of auctions – Step 1	Completed	-Five-year Treasury Bills introduced (Q1 2006)
Develop secondary market liquidity in LL by introducing longer maturity instruments with a low frequency of auctions – Step 2	Initiated	-Study introduction of longer maturities Treasury Bills and ways of enhancing their market appeal (ongoing)
Maintain floor on BDL gross reserves	Initiated	- Ongoing
<i>III. Privatization Program</i>		
Establish inter-ministerial infrastructure and privatization committee chaired by the Prime Minister	Completed	
<i>Telecommunications Sector</i>		
Establish Telecommunications Regulatory Authority (TRA) and appoint its Board	Completed	-TRA Board was appointed on February 21, 2007, and TRA began its regulatory work as of April 2007
Transfer all regulatory responsibilities to TRA	Initiated	-TRA signed Memorandum of Understanding with HCP to assign responsibilities in June 2007 -TRA issued three regulations for consultation (Significant Market Power Guidelines, Interconnection Guidelines, Consumer Affairs Guidelines); Deadline for consultations: August 10, 2007
Issue two mobile licenses	Initiated	-Transaction advisors appointed in June 2007 -Technical consultant and financial auditor appointed in June 2007 -Legal due diligence completed for one mobile company and is being finalized for the second -Transaction structure has been designed
Establish Liban Telecom (LT) as a merger of Ogero and two directorates at the Ministry of Telecommunications	Initiated	-Contract signed with international consultant to assist in creation of LT in November 2006 -Steering committee to oversee corporatization has been designated -Statistics company has been retained to conduct a market study of the telecommunications sector

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

			<ul style="list-style-type: none"> -Human Resources consultant has been retained to define job descriptions and compensation at LT -Legal due diligence for the establishment of LT is underway -Government in the process of appointing transitional Board of Directors
Launch Broadband services in Beirut	Completed		- Services launched as of April 2007
<i>Power Sector Reforms</i>			
Hire consultant team to provide technical assistance to Ministry of Energy and Water	Completed		-Report to evaluate offers and select winning bidder completed on June 12, 2007
Hire <i>Electricité de France</i> (EdF) to develop Power Sector Master Plan, and Public Investment Plan (PIP) for generation and transmission	Initiated		-Contract expected to be signed by July 2007
Hire consultant team to strengthen operational, financial, legal and contract management at EdL	Completed		-Report to evaluate offers and select winning bidder completed on June 12, 2007
Reinforce capacity of EDL finance department	Initiated		<ul style="list-style-type: none"> -Brainstorming meetings held regularly between EDL and MOF -Consultant selected to strengthen financial management at EdL -Consultant selected to assist GOL in EDL restructuring
Audit EdL accounts 2002-2006	Initiated		-EDL board approved hiring auditing company for 2002-2004 on June 1, 2005 and extended its contract to cover 2005 and 2006 on April 20, 2007
Finalize financial terms with private company to operate and maintain Beddawi and Zahrani power plants	Initiated		-Contract signed and private company started operations in 2006
Appoint private company to supervise the operation and maintenance of Beddawi and Zahrani power plants	Completed		-Contract approved by EDL board on June 30, 2007
Secure Natural Gas to Beddawi power plant	Completed		-Agreement signed with Egypt in April 2007; delivery to start in Q2 of 2008
Establish a National Control Center to audit grid performance and enable power import	Initiated		<ul style="list-style-type: none"> -Contract signed and execution started in July 2006 -Center expected to be completed by 2009
Hire consultant team to assist GOL in power sector restructuring	Completed		-Report to evaluate offers and select winning bidder completed on June 12, 2007
Establish power regulatory agency	Initiated		-Interviews currently being held

KEY INITIATIVES UNDERTAKEN AND PLANNED IN 2007

		with candidates
Launch IPP process to purchase current facilities and install additional capacity at Beddawi plant	Initiated	-Contract signed with IFC to advise on transaction on June 15, 2007
License private companies to install and operate meters, and enter into service contracts for distribution	Initiated	-Contract signed with international consultant in November 2006
<u><i>IV. Social Sector Reforms</i></u>		
<u><i>Enhance Management of the Social Sector</i></u>		
Formulize and Activate a Social Inter-Ministerial Committee for Social Policy Supported by a Technical Secretariat	Completed	-Social IMC established and activated (May 2007) -Social IMC meeting up on a regular base to set overall sector strategies and priorities and monitor and evaluate the implementation of social strategies. -Social IMC is supported by a technical secretariat that resides within the Ministry of Social Affairs.
Prepare a Social Development Strategy for Lebanon under the auspices of the Inter-Ministerial Committee	Initiated	-MoSA in the process of developing the social strategy with support from a team of experts (Q2 2007) -Previous studies undertaken by the concerned ministries have been reviewed (Q2 2007) -An advisory board was created to provide guidance and technical support in the elaboration of a social strategy. The board is led by Ministry of Social Affairs and strategy framework is currently being developed. -Components of the Strategy to be ready by July 2007
<u><i>Social Safety Nets</i></u>		
Time-bound Action Plan for elimination of duplication in services between MOSA, MOH, and MOE adopted by IMC-SP	Initiated	-A staff member designated to follow-up, with the social IMC, on duplication and overlap in the provision of social services between ministries (June 2007) -Identification of programs and services that are duplicated or linked to other currently underway and draft report expected in July 2007. -Bilateral meetings will be organized between social

		<p>ministries to discuss duplication and come out with concrete recommendations for efficient division of roles of each duplicated program (Q3 2007)</p> <ul style="list-style-type: none"> -Time bound action plan for elimination of services will be prepared, building on recommendations -A time based action plan that eliminates duplication between MoSA, MOH and MEHE expected to be approved by the council of Ministers by September 2007
Roadmap for implementation of new targeting mechanism (proxy-means testing targeting) and safety net programs	Initiated	<ul style="list-style-type: none"> -Expenditure data finalized and delivered to MoSA (June 07). -Proxy means testing formula for targeting poor households to be developed (August 07) -Establish the necessary set up for implementation of proxy means testing (software, human resources, printing of manuals and application forms, information campaign, etc.) (Q3 2008) -Revisit suggested safety net programs and recommend and endorse prioritized program (Q3 2008) -Initiate implementation of safety net programs (Q1 2009)
Improved procedures for implementing local development initiatives at MoSA	Initiated	<ul style="list-style-type: none"> -MoSA formulated improved procedures for implementing local development projects in partnership with concerned stakeholders (completed) -Improved procedures for implementation of local development projects finalized and issued by Ministers (Sept. 07)
Mapping of local development programs completed	Initiated	<ul style="list-style-type: none"> -An expert contracted to map existing local development projects -Mapping expected to be completed by July 2007.
Minister issues decree adopting new standards and criteria for Welfare Institutions providing in house care to specific groups (children, elderly, disabled)	Initiated	<ul style="list-style-type: none"> -MoSA developed a set of eligibility criteria of NGOs and welfare institutions wishing to be subcontracted by MoSA (July 07) -Eligibility criteria for Welfare Institutions and NGOs to be signed and issued by Minister (Sept 07)

<u>Health</u>		
Institutionalization of public hospital accreditation with the Ecole Supérieure des Affaires(ESA)	Initiated	-Contract signed, pending approval of court of accounts. The activity is expected to commence in Q3 2007 when French experts (of the HAS) will have been mobilized
Develop and implement PHC accreditation program	Initiated	-Activity commenced in June 2007, funded by the Italian Cooperation. -Development of PHC accreditation program will be completed in December 2007, to be followed by implementation.
Define catchment areas , design referral system, expand IT and institute payment card system	Not initiated	-Activity has not been launched to due to lack of funding
Re-commission the work on the standardization of codes, forms and payment across funds	Initiated	-A Consultant funded by the World Bank conducting situational analysis to redefine common business procedures between MoH and NSSF mainly relating to contracting with the private providers and integration and upgrade of health management information. -Activity was launched in Q2 2007 and proposal expected to be completed by Q4 2007, to be followed by implementation.
Integrate Health Management Information System (HMIS) across funds	Initiated	-Consultant funded by the World Bank is conducting situational analysis to redefine common business procedures between MoH and NSSF mainly relating to contracting with the private providers and integration and upgrade of health management information. -Activity was launched in Q2 2007 and proposal expected to be completed by Q4 2007, to be followed by implementation.
Complete the pilot testing of the visa billing system	Initiated	-Pilot testing of the visa billing system currently underway by the Ministry of Health. -Testing expected to be completed by October 2007.
Upgrade and institutionalize National Health Accounts (NHA)	Initiated	-Activity is currently underway for developing NHA matrices for 2004 & 2005. -Preparations to institutionalize the collection and extension of data at each public fund for 2006 & 2007 are underway.

		-TA will be provided by WHO for organizing the NHA team and installing the appropriate software and template (for 2006 & 2007 figures)
Re-price pharmaceuticals registered between 2000 and 2006	Initiated	-Activity of re-pricing pharmaceutical products was launched (i) for products registered after 2001, documents were submitted on December 2006 (ii) For products registered between 1996 and 2000, documents are to be submitted before July 2007 (iii) for products registered before 1995, documents shall be submitted before July 2008.
<u>Education</u>		
National Education Strategy was finalized	Completed	-National Education Sector Strategy was completed (April 2007). -National Strategy document was approved by MEHE stakeholders and was submitted to the Council of Ministers for endorsement, expected to be in September 2007. -Implementation of the 3-year strategy is to be launched in Q3 2007.

Firm selected to undertake organizational restructuring and staff development of MEHE	Completed	<ul style="list-style-type: none"> -An organizational audit was completed, examining the mandate, structure, efficiency, staffing and decision making process at MEHE -A Joint Committee (chaired by the DG of Higher Education and comprised of representative from OMSAR, the Civil Service Bureau, the Directorate of Vocational Education, the Minister's Advisors and the DG of Education was established by a Ministerial Decree) in order to provide recommendations on developing a revised organizational structure (& based on results from MEHE's Organizational Audit -The Joint Committee submitted a draft of the Restructuring Action Plan and Monitoring for restructuring assignment (May 2007) -TA consultant was selected to undertake restructuring and staff development pf MEHE (May 2007) -Commencement of services is expected by end of June 2007; the consultant is expected to develop, building on Joint Committee's recommendations, a revised organizational structure that will detail the functionality of all MEHE units, develop position descriptions, revise relevant decrees and regulations and formulate and deliver professional development activities.
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<p>Comprehensive study on the financing of general and vocational education streams</p>	<p>Study: Completed Implement- ation: Initiated</p>	<ul style="list-style-type: none"> -A comprehensive study on the financing of general and vocational education streams was completed (April 2007). -Terms of reference were prepared for the development of an integrated financial planning and monitoring function at MEHE (March 2007). -The consultant to undertake the activity will be mobilized in August 2007. -The consultant will work with the team mobilized to develop performance based budgeting for the sector (Q3 2007) -Develop and support with training, systems and technology a core planning team within MEHE to enable them to evaluate the economic and financial analysis of policy options and the measurement of educational outcome indicators (Q3 2007) -Perform information audit to identify the data sources internal and external to MEHE that are necessary for the development, implementation and monitoring of goals (Q3 2007). -Develop a financial software tool that will automate the mechanics of the estimation of unit costs and evaluating the impact of policy choices on the total financial resources required (Q4 2007) -Establish priorities and rationalize investment in VTE (Q1 2008)
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<p>MTEF methodology agreed upon and technical work underway</p>	<p>Initiated</p>	<ul style="list-style-type: none"> -Ministry of Education was chosen as a pilot to prepare Medium Term Expenditure Framework. This activity was launched in June 2007. -A Committee was established at MEHE to be the core counterpart in developing and disseminating model performance-based budgeting. The team is working in coordination with a team from the MOF. -Ingredients lists and relevant costs for all required activities and functions in the sector are being prepared based on priorities extracted from the education sector strategy (ongoing- expected to be completed in November 2007) -A team from MEHE is participating in a study tour to train on similar experience in Morocco (June, 2007).
<p>School Mapping Exercise launched</p>	<p>Completed</p>	
<p>EMIS contract signed and SIS installed in 1500 schools</p>	<p>Initiated</p>	<ul style="list-style-type: none"> -A thorough analysis of school information requirements and management information systems at MEHE was conducted. -A school information system (SIS) is under implementation and should be installed in 1500 schools by September 2007 -EMIS contract should be signed by September 2007

<p>Leadership Development Program for School Principals underway</p>	<p>Initiated</p>	<ul style="list-style-type: none"> -First phase of Leadership Development was completed with 121 school principals completing a professional development program -20 of those participated in a study tour in Canada (October 2006) -Second phase of Leadership Development Program is currently underway with additional 303 school principals currently implementing the self-guided modules and practicum phase -20 of those will be participating in a study tour in Canada in October 2007. -Progress towards institutionalizing the Leadership Program within MEHE and the Lebanese University is ongoing
<p>Instructor Development</p>	<p>Initiated</p>	<ul style="list-style-type: none"> -15 regional resource centers have been established throughout Lebanon for in-service training. -270 have been selected and trained to become Master Trainers. -24 candidates are being trained by NGOs to provide support to students with special needs. -Since 2004, 11000 teachers have received training through the Instructors Continuous Program.
<p>Enhance Learning Achievement</p>	<p>Initiated</p>	<ul style="list-style-type: none"> -MEHE teams have developed Evaluation Kits to provide basis for the assessment of student learning. -Over 1000 kits have been prepared and validated. -Consultants were recruited to develop a Question Databank System, Exam generation System and Exam Management System -Examination Generation System (EGS) and Question Bank System (QBS) to be ready by November 2007

Enhance strategic management of educational facilities through consolidating unviable schools in both the GE and VTE sectors	Initiated	<ul style="list-style-type: none"> -Criteria for school consolidation were set -Priority non viable and receiving schools have been identified -A total of 20 primary unviable schools will be consolidated by September 2007 (for the academic year 2007-2008.)
<i>V. Social Security and Pension Reform</i>		
Law reforming End of Service Indemnity and introducing new fully funded defined contributions pension system finalized by Parliamentary approval	Completed	
Board of the NSSF agrees to assessment of the current situation by external experts and preparations reforms	Completed	
Validate government arrears with NSSF and agree on refinancing plan	Initiated	<p>Expected by end-2007:</p> <ul style="list-style-type: none"> -Audit government arrears with the NSSF and the NSSF accounts payable. -Based on discussions with MOF agree on a refinancing plan for arrears with proper documentation. -Liquidate other arrears -Auditor will conduct due diligence on NSSF assets, bank deposits and dormant accounts. -Normalize payment schedule for government dues to the NSSF according to requirements of law. -Prepare plan to implement accounting on an accrual basis and prepare balance sheet following acceptable accounting standards.

Reform program to restore financial equilibrium of health insurance branch of NSSF submitted to cabinet	Initiated	Expected by end-2007 -Conduct a preliminary actuarial valuation of health insurance funds -Adopt steps to control and contain medical payments -Permanently close "voluntary insurance program" to avoid further adverse selection that would further add to the deficit Submit proposal to the Cabinet aiming to bring NSSF health insurance fund to financial equilibrium over the medium term as stipulated under Article 66.
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Revised implementation plan for second phase of the Master Plan to reform business and administrative process approved by Board of NSSF	Initiated	<ul style="list-style-type: none"> -Activities to be completed by December 2007 -Recruit a technical management team within NSSF to oversee the implementation of the Master Plan -Conduct assessment of (i) core business processes and administrative systems (registration, collection, reconciliation, record keeping, benefit liquidation, payment/reimbursement) and (ii) NSSF initiatives for administrative reform in the context of the reform of health insurance and end-of service indemnity systems. -Identify necessary adjustments to the Phase 2 of the master Plan -NSSF to build strong IT capacity by establishing a directorate level IT department and through recruitment of a mix of internal and external skills to include IT Leadership (managerial and technical), business analysis, and sourcing management -Implement Phase 1 of Master Plan, while ensuring consistency with envisioned reforms in the health insurance and end-of-service indemnity branches. -Prepare terms of reference and bidding documents for implementation of the second phase of the master plan -Consultancy companies contracted.
<i>VI. Growth-Enhancing Structural Reforms</i>		
<i>A. Governance</i>		
New draft public procurement law and draft law for setting up the Public Procurement Management entity	Initiated	<ul style="list-style-type: none"> -Draft laws being finalized inter-ministerial committee -Draft laws will be shortly submitted to the Council of Ministers for approval before parliamentary submission.
Identify ministries and draft TOR for anti-corruption project	Initiated	<ul style="list-style-type: none"> -TOR for consultancy firm ready and candidate ministries identified (Q3 2007) -Bidding process subject to availability of funds
Identify opportunities and modalities for outsourcing of public services	Initiated	<ul style="list-style-type: none"> -Some tasks for outsourcing will be ready by Q3 2007

		-TOR and the scope of work to analyze findings, identify priority activities and propose a mechanism to such outsourcing to be developed (Q3 2007)
Action plan preparation for the implementation of the e-Government strategy	Initiated	-Bidding process subject to funding -Projects being implemented depending on incoming funding -E-procurement development gateway project initiated (expected results mid-2008)
<i>B. Improving the business environment</i>		
Provide tax incentives for affected enterprises	Initiated	-Undertaken Q3, Q4 2006: Installment of dues for VAT Q2 2006 -Installment of dues for DASS Q2 2006 -Penalties exemption -Filing deadlines extended Expected by end- 2007: -Develop procedure to verify declared damage -Develop procedure to reconstitute lost tax records -Increase the period allowed for loss carried forward
Encourage investment by reducing time required to obtain a business license and cost of opening and closing a business. Enact measures to streamline business registration and licensing and eliminate minimum capital requirements	Initiated	-Timeframe: Q1 2007 – Q1 2008 -Methodology for simplifying Business Registration procedures developed -InfoPro survey completed Expected short term implementation (by Q3 2007): -Consolidation of all fees upfront -Standardization of forms and applications (requires cooperation from Ministry of Justice) -Memorandum of Understanding with LibanPost being finalized -Creation of user guide to required steps Expected Long term (Q4 2007; requires parliament) : -Complete matrix identifying laws to be amended
Establish Business Development Centers	Initiated	-Four centers established -Close follow-up required with 4 BDCs and appropriate coordination with EU (Q1 2007 – Q3 2007) -By September 2007 MOET will engage in extensive training programs for BDC managers
Develop action plan for	Initiated	-Report and recommendations of

implementation of FIAS Administrative Barriers study findings		FIAS study presented in workshop (22 June 2007) -Next steps for action plan under discussion (Q4 2007)
New Intellectual Property (IP) laws drafted and sent to relevant administrations for feedback, IP Protection Office (IPPO) strengthened (TA needed for training)	Initiated	- Draft Copyright Law sent to concerned ministries for review and feedback (April 2007) -New Trademark Law drafted and sent to Council of Ministers (March 2006). MoET received feedback (April 2007) -Requires involvement of the Ministries of Justice and Interior (Q1 2007 – Q4 2008)
Further facilitate trade and enhance trade competitiveness	Initiated	-Activate and implement National Committee on Trade and Transport Facilitation (Q1 2007 – Q3 2009) -Public awareness program about export market opportunities aimed at private sector being developed (Quality program supported by EU) (by Q2 2008) (Law awaiting Parliamentary approval)
Laws on standards, technical regulations, conformity assessment, competition and protection of national products drafted; Committee on Trade and Transport Facilitation (TA needed to draft three-year master plan), Information Technology Law, draft insurance law	Initiated	-Law on standards and Law on Technical Regulation and Conformity Assessment drafted (await Ministry of Industry signatures before being sent to Council of Ministers); -Modern Competition Law to be finalized by experts (mid-July 2007); -Implementation of Law of Protection of National Production to be implemented by end-2007 (Law issued by Parliament Q4 2006)
Strengthen commercial legal framework aimed at encouraging investment	Initiated	Initiated initiatives include: -Review liquidation/bankruptcy laws and procedures (Q1 2007- Q4 2008) -Harmonize policies and procedures for foreclosure across Lebanon (Q1 2007-Q4 2007)
Expedite clearance of imports, including by increasing automation at the port, and lowering related costs.	Initiated	-Number of steps reduced from 14 to 4 (pre-2007) -Standardized automated document issued -One-stop shop at Port of Beirut established with presence of customs (other Ministries not present except for Agriculture) -Testing of programs ongoing

Kafalat credit limit increased to LL600 million	Completed	<ul style="list-style-type: none"> -Credit limit increased to LL 600 million (mid-2006) -Sector coverage: Industry, agriculture, tourism, traditional crafts, high Technology -Guarantee of total loan increased from 75% to 85% -No other collateral requested by banks -EU support on above garnered -Rescheduling of previous loans for SMEs affected by war on a case by case basis. Three avenues determined with BDL: rescheduling, granting an additional grace period, re-injecting money to buy damaged equipment/machinery.
Promote the creation of venture capital funds to facilitate financing	Initiated	<ul style="list-style-type: none"> -“Building Block Equity Fund”, an initiative by BADER, a young entrepreneurs program launched (Q4 2005) Expected by end-2007: -Closing of BADER fund at \$ 20 million commitments from 10 Lebanese banks, EIB, AFD, private investors (Q3 2007) -Starting BADER investments (Q4 2007)
<i>C. Capital Market Reform</i>		
Enactment of Capital Markets law	Initiated	<ul style="list-style-type: none"> -Being discussed in Commissions -Awaits parliamentary approval

Appendix B. IMF 2007 Article IV Consultation Mission - Concluding Statement

International Monetary Fund
Lebanon
2007 Article IV Consultation Mission
Mission Concluding Statement
May 28, 2007

1. **An International Monetary Fund (IMF) mission visited Beirut May 14-28, 2007 to hold discussions for the 2007 Article IV consultation.** The mission also reviewed performance under the 2007 program that was the basis for the IMF's Emergency Post-Conflict Assistance (EPCA) and prospects for the remainder of the year. The mission met with the Minister of Finance, the Governor of the Central Bank, the Ministers of Economy and Trade, Tourism, and Energy, high officials from the prime minister's office, various ministries and agencies and the public electricity company (EdL), as well as representatives of the banking sector, the industrialists association and the labor union. The mission wishes to thank the authorities for the open and constructive discussions and their warm hospitality.

I. Overview

2. As anticipated, 2007 continues to be a difficult transition year beset by continued political uncertainty and uncertain market condition. Performance under EPCA is on track, but financial and fiscal risks remain. The Paris III reform program offers a promising way out of the large debt overhang and financial vulnerabilities, and the 2008 budget as well as implementation of the structural reforms now being launched in the telecom, power and social sectors will be key in generating a clear forward momentum. Still the strategy is not without risks, and to sustain adjustment and reform over the medium-term it will be important to: generate a broad consensus behind the reform objectives; ensure that spending priorities and structural policy are supportive of high private sector growth; and reform institutions to improve the effectiveness of policy making. The success of the program also depends on the timely disbursement of pledged donor support. An improvement in the fiscal situation should also provide the opportunity to reform monetary policy instruments. A retrenchment of the central bank from quasi-fiscal activities (including direct financing of the government) is also needed to strengthen its balance sheet. The rapid expansion of Lebanese banks into the region will help diversify their large asset base and will require an adaptation of banking supervision to minimize exposure to new and unforeseen risks.

II. Recent Developments and Short-term Prospects

3. **The authorities managed skillfully the financial and fiscal pressures from the July 2006 conflict with Israel.** The Banque du Liban (BdL) intervened successfully to maintain financial stability and the deposit outflow observed during and the immediate aftermath of the conflict was fully recovered by end-2006. Likewise, the government was able to contain the conflict's impact on debt by containing discretionary spending and mobilizing generous grant support from donors.

4. **The ongoing political stalemate and recurrent outbreaks of violence are the key obstacle to economic recovery.** First quarter developments and a positive external economic

environment point to a real GDP growth of at least 2 percent or higher for 2007. However, there is a large degree of uncertainty around this projected growth, with downside risks linked to the political and security situation but also a significant higher growth potential, if the country were able to capitalize on the strong regional demand. Depositors and financial markets seem to have largely factored in the political uncertainty, and the financial impact of the recent flare up of violence appears to have been contained. Still, financial risks remain high.

5. **Notwithstanding a difficult financial and economic context, the authorities met all of the end-March 2007 targets under EPCA, except for the ceiling on government borrowing from the BdL which was exceeded only by a very small margin.** Stronger than projected revenue collection helped contain the primary deficit and the accumulation of net debt in the first quarter. However, in the absence of any readjustment of domestic fuel prices, the recent increase in international oil prices has reduced excises on gasoline products to zero. If not reversed, this trend could lead to a shortfall of revenue from excises of more than ½ percent of GDP for the year as a whole. An early announcement of a floor for gasoline excises would help safeguard the authorities' fiscal objectives for 2007. In view of the exposure of public spending to unexpected demands, such as from heightened security measures, achievement of the fiscal target for 2007 calls for continued strict expenditure discipline.

6. **The authorities' financing strategy for the remainder of 2007 remains vulnerable to shocks to market confidence and delays in the disbursement of donor support.** Commercial banks were reluctant to roll over maturities in the first quarter. This was partly offset by increased subscriptions by the National Social Security Fund which is reallocating its portfolio from deposits to treasury bills, and also some additional borrowing from the BdL. However, the authorities have restated their commitment to rely on market financing, and, in recent weeks, commercial banks have returned to treasury bill auctions. The government also issued a \$400 million Eurobond at end-May despite the tense security situation. To the extent that central bank financing becomes again necessary in the current uncertain environment, it should be circumscribed to short-term bridge financing.

III. Implementation of the Paris III Program

7. **The 2007 program is the first step in the long process of adjustment and reform outlined in the authorities' Paris III document, the main aims of which are to restore the foundations for solid growth and reduce the risks of a financial crisis stemming from the large debt overhang.** The strategy envisions the implementation of fiscal measures equivalent to around 10 percent of GDP over five years. In combination with privatization and external donor support, this large scale adjustment would bring down government debt to under 130 percent by 2012. Restored confidence and structural reforms would in parallel contribute to improve the GDP growth outlook. To enhance the chances of success, it will be important that reforms be properly sequenced so that policies can reinforce each other.

8. **While the strategy remains the most promising way forward, it is not without risks.** These include political implementation risks, shocks to the macroeconomic environment, uncertainty about the yield of reforms, and risks stemming from contingent fiscal liabilities. Contingent liabilities may arise from actuarial imbalances in the public and private pension systems, the open-ended nature of transfers to the health and family allowance funds, and unforeseen costs from power sector reform

9. **Timely and flexible disbursement of Paris III pledges is another important element of the strategy.** Welcome progress has been made in locking in the terms and conditions for the release of funds from some key donors. Negotiations are still under way with others and the mission fully supports the authorities' request that donors convert their pledges from project to budget support, or at least align their project disbursements to the government's own spending priorities.

Setting fiscal and structural policy priorities for 2008

10. **The Paris III program envisions a strong acceleration of fiscal adjustment in 2008.** Encouragingly, the draft 2007 budget law already precommits the increase in the value-added tax and the tax on interest income. Preparations for introducing a global income tax as of 2008 are advancing, but require legislative approval before the end of 2007. Ongoing efforts to strengthen tax administration and non-tax revenue collection should further boost revenues. The program also envisions further adjustment in gasoline excises. On the expenditure side, containment of current spending will continue to be necessary, but, as recognized by the authorities, implementation of energy and social sector reforms with the assistance of the World Bank will be key to achieving durable adjustment. The success of power sector reforms will require a careful sequencing of infrastructural and governance initiatives to avoid compounding the existing problems. The audits of EdL and NSSF and the ongoing computerization of NSSF are important steps in this process.

Mobilizing domestic support for adjustment and reform by protecting the most vulnerable

11. **Public and political support will need to be mobilized to sustain reform and adjustment over the medium term.** The financial support of the international community (through phased disbursement of financial assistance) provides incentives for successive governments to continue on the reform path. However, unless the reforms also enhance social and economic conditions for the population at large, it may prove difficult to maintain the reform momentum. Sustaining high economic growth (through the policies discussed below) is key in this regard, but the most vulnerable also need to be protected by effective social safety nets. The social pillar of the Paris III strategy addresses this important concern, and the authorities are encouraged to implement swiftly their plans of reallocating social spending toward better targeted redistribution schemes.

Aligning public spending and policy priorities to growth objectives.

12. **On the fiscal front, the structure of current spending needs to move toward more productive expenditure choices.** Outright transfers account for a large share of current spending, and even the wage bill contains a large redistribution component in as much as it is not allocated on the basis of public sector needs. The planned phasing out of some extra budgetary funds is an important step in this direction and should not be delayed beyond the planned horizon. Structural reforms in the power sector are also expected to reduce considerably non-productive public spending, and to improve the reliability of energy supply. Once these reforms are launched, attention should be turned to civil service reform to address ingrained governance and efficiency problems., including through revisiting staffing and remuneration.

13. **Privatization remains a core element of the overall strategy and should be seen first and foremost as an instrument to raise growth.** Telecom privatization will have a direct impact on debt and thereby can be expected to improve confidence. Beyond that, it offers the opportunity to liberalize the sector and introduce greater competition under the supervision of the newly established telecom regulatory authority. Under the current duopoly in mobile telecommunication, Lebanon has lost ground to other countries in the region in terms of telecommunication costs and

service. The Paris III growth objective require that this sector become again a dynamic contributor to the economy.

14. **The authorities have begun to address problems in the business environment by reducing red tape, streamlining business licensing procedures and targeting improvements in public services to enterprises.** Reducing the costs of doing business is important, but these actions should be complemented by measures to reduce rent-seeking behavior in the public and private sector. In many sectors, oligopolistic market structures still inhibit competition and need to be dismantled, and the competition law needs to be backed by proper enforcement mechanisms.

Developing stronger institutional mechanisms to improve the control over budgetary outcomes and the quality of spending.

15. **Planned reforms in public financial management will help enhance the effectiveness of policies.** The planned establishment of debt management institutions within the ministry of finance should contribute to lowering the government's debt service burden. Timely implementation of the action plans to improve cash management functions (including the Treasury Single Account) and the budgetary process will be equally important to achieve the objectives discussed above, notably to direct scarce public resources to priority sectors, and reduce inefficiencies in public financial management. By linking current policies to medium-term objectives, a medium-term budget framework is essential to keep the process on track and contain the risks of backtracking. The decision to introduce the notion of medium-term budget planning and to provide a top down budget envelope for the 2008 budget preparation process is very encouraging in this regard. Building on these reforms, a fiscal rule or a fiscal responsibility law could eventually help provide self-correcting mechanisms in the budget process to safeguard overall fiscal objectives against unforeseen deviations.

IV. Monetary and Exchange Rate Policy

16. **Successful fiscal adjustment will provide an opportunity to reform the monetary policy framework.** In the current fiscal situation and unpredictable financial environment, monetary stability objectives have been well served by deploying a range of special intervention instruments. More stable and predictable market conditions should enable the central bank to refocus on guiding interest rates through short-term transparent instruments,. Interest rate and exchange rate stability cannot be pursued simultaneously, and the current premium placed on the stability of the T-bill rate as the main indicative interest rate overly constrains monetary policy management. By using its own short-term instruments, the central bank will gain flexibility in responding to balance of payments and dollarization objectives. Such an environment would also create the conditions for the government securities market to develop, thereby attracting a wider range of investors and helping the government diversify its financing base. In the short term, the interlinkages between the government's cash and debt management and the BdL's liquidity and reserve management call for close cooperation between the two institutions to increase the efficiency of financial policies. The establishment of a working group at the technical level to exchange relevant information on a high frequency basis would be a very welcome step in this regard.

17. **The BdL also needs to make progress on strengthening its balance sheet to preserve the effectiveness of monetary policy over the medium term.** In large part, the BdL balance sheet has been weakened by measures taken to replenish reserves and maintain financial stability during

the recent crises episodes. However, the cost of sterilizing government financing in the past and the indirect costs associated with quasi fiscal activities in support of specific objectives and sectors have also contributed. Going forward, it would be important to scale back quasi-fiscal activities, such as selective reductions in reserve requirement and the recent scheme to provide below-market loans for banks with an exposure to businesses who have been affected by the conflict. To the extent that these activities merit public support, they should be funded explicitly by the budget. Over the medium-term, an improvement in the economy's financial situation and de-dollarization will help strengthen the BdL's balance sheet. Privatization of the assets held by the central bank will also help its financial balance, while contributing to the government's growth agenda.

18. **The exchange rate peg has served the authorities well in maintaining financial stability, and the exchange rate does not appear to be misaligned.** The exchange rate peg has served as a nominal anchor, fixing expectations including during times of financial pressures. International reserves held by the BdL combined with the banking system's liquidity cushion appear sufficient to meet temporary pressures on the exchange rate, should they occur. Lebanon's strong export performance is an indication that the exchange rate is not misaligned, with the depreciation of the U.S. dollar against major currencies broadly offsetting the impact of the spike in inflation in the aftermath of the 2007 conflict. However, the expectation of private-sector led growth in the Paris III medium-term program requires steady improvements in competitiveness. In the absence of adjustments in the exchange rate, the onus will be on realizing productivity gains through improvements in the business environment supported by the structural reforms discussed above.

V. Banking Sector

19. **Commercial banks are diversifying their asset structure through regional expansion and focusing more on private sector lending, in particular retail lending.** The diversification strategy is welcome both from a risk management point of view, and given the projected decline in government financing needs. Moreover, the banking system appears ready to meet the Basel II capital adequacy standards, which the authorities plan to introduce on January 1, 2008. The changing business model of the domestic banking system will require a parallel adaptation of banking supervision to ensure that new activities, including activities abroad, do not create new and undue risks. While most banks seem well placed to adjust to these changing circumstances, some consolidation of the sector seems likely over the medium term. It is important that the mechanisms put in place to facilitate consolidation minimize moral hazard and increase banks' management accountability and shareholder responsibility. The reform of the deposit insurance fund that is being contemplated would provide an opportunity to develop a more comprehensive bank resolution mechanism.

Appendix C: Paris III Detailed Division of Grants and Loans

Country	Total Pledged	Projects Underway	Private Sector Support	UN System/ UNIFIL/ NGOs	Technical Assistance / In-kind	To BDL	Grant to Government		Loan to Government		Under Review	Sector
							Budgetary Support	Project Financing	Budgetary Support	Project Financing		
European Investment Bank	\$1,248	\$260	\$709		\$20					\$260		Power, Water, Ports, Roads
Saudi Arabia	\$1,100						\$100			\$1,000		
World Bank	\$975		\$275						\$300	\$400		Social, Power, Water
United States	\$890		\$120	\$235	\$286		\$250					Security
Arab Fund for Economic & Social Development	\$750	\$200								\$550		Power, Admin reforms
France	\$650		\$163						\$488			
European Commission	\$486	\$139					\$39	\$243	\$65			Political reforms, Social, Economic and Recovery
United Arab Emirates	\$300								\$300			
Islamic Development Bank	\$250	\$5						\$30		\$215		Social, Infrastructure
Arab Monetary Fund	\$250		\$100						\$150			Fiscal reform
Italy	\$156			\$26				\$33		\$98		Employment, Social, Infrastructure

Country	Total Pledged	Projects Underway	Private Sector Support	UN System/ UNIFIL/ NGOs	Technical Assistance / In-kind	To BDL	Grant to Government		Loan to Government		Under Review	Sector
							Budgetary Support	Project Financing	Budgetary Support	Project Financing		
Denmark	\$3.5			\$2.5	\$1							Security, Humanitarian
Ireland	\$3										\$3	
Japan	\$4			\$4								
Austria	\$1			\$1								
Cyprus	\$1										\$1	
Finland	\$1			\$1								
Brazil	\$1										\$1	
Malaysia	\$1						\$1					
South Korea	\$1										\$1	
Luxemburg	\$1										\$1	
Portugal	\$1										\$1	
Slovenia	\$0.13										\$0.13	
Total	\$7,613	\$760	\$1,379	\$346	\$347	\$77	\$400	\$449	\$1,303	\$2,523	\$31	

Appendix D: TRA Progress as of June 28, 2007¹

Introduction

The Telecommunications Regulatory Authority Board was appointed on February 21, 2007, and the TRA began its regulatory work as of March 1, 2007. The TRA has embarked on building the institution and establishing a sound regulatory environment, with a focus on preparing for the mobile privatization and licensing in Q4 2007. The report gives a brief description of each task that the TRA has worked on in the last three months, identifies the progress to date, and highlights the key milestones going forward for each task.

Building the TRA Institution

1. Code of Practice

The TRA has issued its Code of Practice which sets out the procedures and principles governing its work.

2. Preparing the 2007 Budget

The TRA budget for its first year of operation (2007) has been drafted and submitted to the Minister of Telecommunications and the Minister of Finance for approval on May 18, 2007. The Council of Ministers has issued a decision approving the TRA budget of L.L. 20 billion (equivalent to US\$ 13.3 million) for 2007. Prior to the approval of the budget, the Council of Ministers (COM) had granted the TRA an advance payment on its budget of L.L. 4.5 billion (COM Decision 20/4/2007). The payment was transferred to the TRA on June 2, 2007.

3. Organizational Structure

The TRA prepared an organizational chart and submitted it to the Minister of Telecommunications for approval and forwarding to the Council of Ministers. The organizational chart has been designed in accordance with the requirements of the TRA Administrative and Financial Decree (COM Decree 14264/2005). The TRA has been working with seven staff, including the board members, during the covered period. It plans to have 20 professionals by end of July 2007, and 80-100 professionals by the end of 2007.

4. Financial Procedures

As required by TRA Administrative and Financial Decree (COM Decree 14264/2005), the TRA has finalized its Financial Procedures and will be submitting them to the Minister of Telecommunications and the Minister of Finance for approval.

5. Transfer of Regulatory Functions

Regulatory functions to be transferred to the TRA from the Ministry of Telecommunications (MOT) are divided into five categories:

1. Licensing
2. Radio Frequency Management (assignment, monitoring, etc.)
3. Number Management
4. Import Authorizations
5. International Relations

¹ This write-up is an excerpt of the first TRA Quarterly Report

TRA and MOT have been meeting regularly to facilitate the transfer since April 2007. A committee of MOT and TRA staff officials has been established to prepare a list of all the information and documentation that is to be transferred to the TRA. The complete transfer is expected to take place by the last quarter of 2007.

6. Human Resource Management

a) HR Policies and Procedures

Draft HR policies and procedures are ready for Board approval.

b) HR Regulation

Draft HR rules and regulations are being prepared by TRA's legal advisors.

c) Job Descriptions

Job descriptions for vacancies in the TRA have been drafted.

d) Recruitment Process

TRA has advertised for managerial, senior and administrative positions in all national newspapers and websites, and in two magazines. TRA has received around 600 applications in the last two weeks.

e) Interviews

TRA has prepared detailed questionnaires and interview guides. Applications will also be assessed through written tests of communication, writing and analytical skills.

7. Securing International Assistance

TRA has held discussions with various international donors and has secured the following commitments:

- EU commitments: financing of technical assistance (approximate budget 1.5 million)
- US Commitments: financing of technical assistance and training to TRA senior management, and light equipment acquisition (approximate budget US\$ 2 million)
- Partnership for Lebanon: Financing of technical assistance for broadband strategy (approximate budget: undetermined)
- Others: TRA is further exploring other international assistance

8. Public Consultation Procedures

TRA has issued guidelines for the conduct of a public consultation process. These Guidelines are designed to serve industry stakeholders in understanding the process by which public consultations are conducted, and to serve a model for all TRA public consultations.

TRA Work Plan

1. Mission Statement

TRA has defined its mission statement as follows:

To establish a regulatory environment that enables a competitive telecommunications market to deliver state-of-the-art services at affordable prices to the broadest spectrum of the Lebanese population

2. Strategic Objectives for 2007

TRA has highlighted several strategic objectives for the first year of operations. These objectives constitute major milestones in the Lebanese government's reform program in the telecommunications sector:

- Liberalization mobile communications (2G/3G) by Q407
- Liberalization of Broadband by Q407
 - Providing the regulatory framework for the launch of ADSL services
 - Regularizing existing DSP licenses

- Launching the process to issue new broadband licenses (including IP backbone and International gateway services)

3. Annual Work Plan (Assignment of responsibilities)

TRA is finalizing a detailed Action Plan that assigns roles, responsibilities and timelines, in order to deliver its strategic objectives. The Action plan covers:

- Drafting new regulations and decisions
- Drafting the mobile and broadband licenses
- Drafting the auction rules and request for applications (RFA)
- Transition and handover by MOT of regulatory documentations and functions to the TRA
- Building institutional capacity
- Conducting market analysis
- Drafting telecommunications policy

4. Establishing a Sound Regulatory Framework

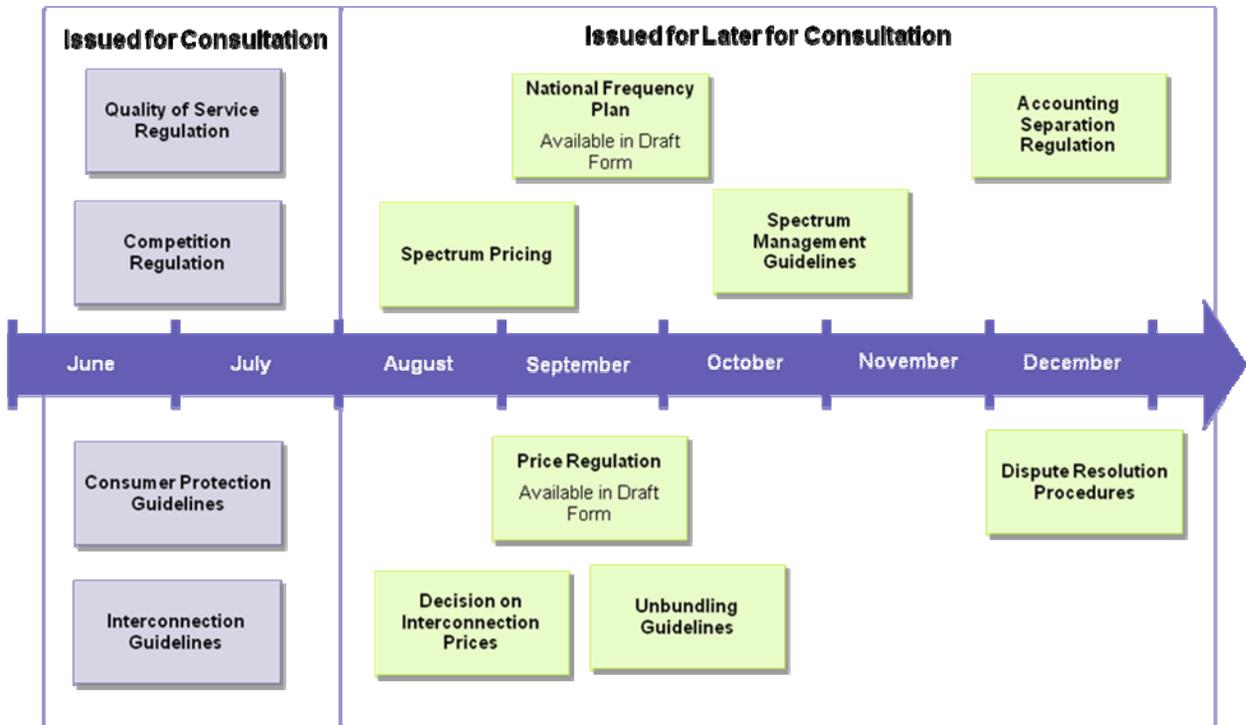
TRA has made significant strides towards establishing a best-in-class regulatory framework. TRA has already issued four draft regulations for consultations (refer to figure 1):

- Interconnection Guidelines
- Significant Market Power Guidelines (Competition)
- Consumer Affairs Guidelines
- Quality of Service Guidelines

TRA has prepared the following draft regulations:

- Spectrum Pricing Regulation
- National Frequency Plan
- Spectrum Management Guidelines
- Unbundling Guidelines
- Interconnection Pricing Decision
- Accounting Separation Guidelines
- Price Regulation

Figure 1 – Regulation Roadmap



1. Mobile Licensing:

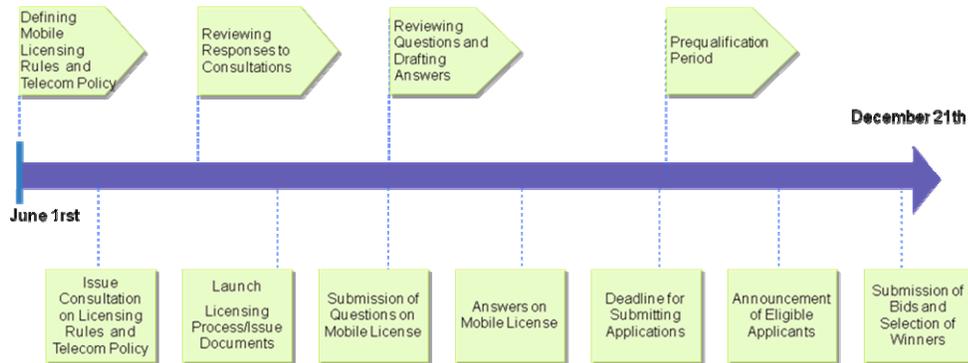
TRA is working with the Higher Council for Privatization (HCP) and the Ministry of Telecommunications (MOT) to ensure the success of the licensing/privatization of the two incumbent mobile networks, in line with the Government of Lebanon's commitments in the context of the Paris III donor conference. TRA is taking the lead in preparing the licenses, the auction rules (in consultation with HCP), and the relevant regulations, while HCP and MOT are working on preparing the expected transfer of mobile network assets. The mobile licensing/privatization will be carried out in a transparent, competitive auction. It is the first step in the liberalization of the mobile telecommunications market.

In the mobile licensing process the TRA has accomplished to date the following:

- a. Timeline for licensing and privatization of the two mobile operations (refer to figure 2)
- b. Detailed task allocation table to coordinate between the various stakeholders: MoT, HCP, TRA, CoM, etc... (Annex 1). This task allocation has been discussed and approved with the Investment Banks and the HCP
- c. Drafting MoU with the HCP: TRA has drafted a detailed MoU to ensure a smoother and coordinated privatization and licensing. Draft has been finalized with HCO and HCP legal counsel and awaits signature of PCM and Chairman of TRA.
- d. Mobile Financial models: The TRA, with its financial advisors and consultants, is working on a financial model of the mobile licenses
- e. Drafting of Request for Applications and Information Memorandum: TRA and its advisors have started drafting the RFA and IM
- f. Establishing legal basis for the transaction of the sale of mobile assets: TRA has provided legal opinion that no further legislation is required to sell the Mobile network Assets this opinion has been submitted to the Minister of Telecommunications and is to be forwarded to the Minister of Justice for review
- g. Review and Comment on various drafts of mobile privatization law

- h. Review and comments on alternative transaction structure proposed by HCP legal advisors
- i. Contracting with legal and regulatory consultants to assist in the preparation of the mobile license documentation.

Figure 2 – Mobile Licensing Timeline



2. Broadband

In addition to the identification of the broadband objectives (licensing of IP backbone and international gateway), TRA has started working on a broadband strategy. In addition, TRA has been closely monitoring the ADSL market. Finally, TRA is drafting unbundling guidelines in compliance with Law 431 and its competition provisions as well as internationally recognized competition principles.



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