

**Rating Action: Lebanon**

**Moody's changes outlook for Lebanon's sovereign ratings to positive from stable**

DIFC, December 11, 2008 -- Moody's Investors Service has today changed the outlook on Lebanon's sovereign ratings to positive from stable. These ratings are the country's B3 local and foreign currency government bond ratings, the B3 country ceiling for foreign currency bank deposits, and the B2 country ceiling for foreign currency bonds.

"The change in outlook was motivated by the proven resilience of the public finances to shocks, which have been severe in recent years. The improvement in Lebanon's political and economic environments since the signature of the Doha Agreement in May are also reassuring," explains Tristan Cooper, a Vice President-Senior Analyst in Moody's Sovereigns Group. Under the Doha Agreement, Lebanon's hostile political factions agreed to: (i) elect a new president; (ii) form a national unity government; and (iii) pass a new electoral law in advance of the 2009 parliamentary elections.

All three actions have been achieved: a consensus president was appointed in late May (the presidency had been vacant since November 2007); a new government that includes Hezbollah and representatives of other opposition parties was formed in July; and a revised electoral law was approved by parliament in September. These actions appear to have assuaged Lebanon's volatile political environment, which was nearing civil war in May.

"Moody's recognises that Lebanon's calmer political environment has allowed the country's economy to regain momentum but also notes that the public finances would likely be durable should the improvement falter, as shown during previous episodes of political turmoil," says Mr. Cooper. This summer was Lebanon's best in terms of tourism inflows since 2004. The IMF is projecting that the Lebanese economy will grow by 6% this year and the country's very large public debt overhang has continued to ease.

Furthermore, Moody's notes that Lebanon is one of the few countries to have so far benefited from the global financial turmoil, as members of the large Lebanese diaspora have moved funds into Lebanon's banks, viewing them as relatively safe havens. Due to strict regulation, Lebanese banks have not been exposed to toxic sub-prime assets and did not hold significant assets with failed Western banks. Thus, largely due to these deposit inflows, the central bank's foreign currency reserves jumped by 57% over the first nine months of this year. At end-September, they amounted to US\$15.3 billion or 60% of 2007 GDP. Lebanon's commercial banks also retain a high level of foreign currency liquidity. Moody's notes the banking system therefore remains willing and able to roll over and buy new government paper in both local and foreign currency.

Despite these improvements, Moody's points out that Lebanon still has substantial credit risks. The political situation is fragile and tensions could well resurface before the parliamentary elections next May. There is also the looming threat of renewed conflict between Israel and Hezbollah. A return to serious political turmoil would quickly set back the economy and could lead to a withdrawal of bank deposits, although these have been highly resistant to political shocks in the past, as have the government's poor finances. Lebanon's economy is also likely to be negatively affected by the global economic downturn, as external demand falls and remittances and inward investment potentially suffer. The level of remittances from Lebanese workers in the Gulf are already reported to be falling. Nevertheless, Moody's believes that these downside risks are already well captured by Lebanon's low ratings.

Moody's would upgrade Lebanon's sovereign ratings if the current relative political calm can be sustained through the electoral cycle, some much-needed economic reforms are passed and the public debt burden continues to ease.

Lebanon has a GDP per capita in purchasing power terms of around US\$12,000, mid-range among countries rated by Moody's, although the absolute size of the economy is relatively small.

The last rating action took place on 25 March 2008 when Moody's changed the outlook on Lebanon's ratings to stable from negative owing to the resilience of Lebanon's public finances in the face of numerous political shocks.

The principal methodology that Moody's uses in rating the Government of Lebanon is its Sovereign Bond Methodology, which can be found at [www.moody.com](http://www.moody.com) in the Credit Policy & Methodologies directory. Other methodologies and factors that may have been considered in the process of rating this issuer can also be

found in the Credit Policy & Methodologies directory on Moody's website.

Any impact on other issuers resulting from today's rating action will be announced separately.

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