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Sovereigns

International Credit Analysis

Republic of Lebanon

Ratings

	Current Ratings
Foreign Currency	
Long-Term IDR	B-
Short-Term IDR	B
Local Currency	
Long-Term IDR	B-
Country Ceiling	B-

Outlook

Foreign Long-Term IDR	Stable
Local Long-Term IDR	Stable

Financial Data

Lebanon

	2007	2008
GDP (USDbn)	24.7	27.7
GDP per head (USD)	6,033	6,671
Real GDP (% change)	4	4
Consumer prices (% change)	4.5	9.5
Government debt (% GDP)	169.9	163.4
Net external debt (% CXR)	-38.2	-37.1
International liquidity ratio	182	193

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Rating Rationale

- Lebanon's 'B-' rating reflects the highest public debt burden and budget deficit of any sovereign rated by Fitch Ratings and acute political instability which has stymied plans to reduce them. Government debt of 724% of revenue is over five times the 'B' category median. Moreover, even if the government succeeds in reducing debt to a planned 130% of GDP by 2011, this would still be extremely high — exceeded only by Japan at over 170%. The budget deficit was 11.1% of GDP last year (the official figure of 10.3% excludes some capital spending).
- Lebanon retains an impeccable debt service record, despite the shocks suffered since 2005. Important rating supports are the resilience of the economy and especially the banking system, a supportive diaspora and donor community, and skilful management of public finances and debt. Despite war with Israel in 2006 and an 18-month political standoff between government and opposition which brought government to a virtual halt, GDP growth could exceed 4% this year, non-resident deposits are up 23% yoy, and the budget deficit and debt burden are declining. Normal access to the eurobond market has been restored.
- Critically, pressure on public finances has never led to calls to redirect debt service spending to other uses. Strong donor support is focussed primarily on preserving Lebanon's fragile political system with its multi-confessional character. There are no signs of recent political developments bringing any change here, but such developments cannot be totally ruled out in future.
- Receipts from tourism and private transfers help offset a very large trade deficit while inward FDI of over 11% of GDP, mainly construction and real estate, together with donor support, finance a double-digit current account deficit. Lebanon's gross external financing need is well below 'B' and 'BB' category medians and although the current account deficit could rise to over 13% of GDP this year, gross reserves are still rising. Lebanese banks' aggregate balance sheet is very large relative to GDP and banks hold around 60% of government debt. This explains Lebanon's ability to support an apparently huge debt burden and also its net external creditor status (residency basis) despite one of the highest ratios of government foreign-currency (FC) debt to FC receipts in the 'B' category.
- Lebanon's rating is also supported by a high per capita income in peer group terms and a supportive business climate. Although inflation has risen this year, the long-standing USD peg has proved robust, not suffering any sustained pressure. Nevertheless, the combination of the USD peg, potentially volatile non-resident deposits and over 70% dollarisation is a major systemic risk given Lebanon's susceptibility to shocks. Although gross reserves have reached an all-time high this year, liquidity is relatively weak in peer group terms.

Key Rating Drivers

- The rating Outlook is Stable. The May Doha Accord has given Lebanon a president and new government and holds out the possibility that key reforms will be implemented. These include privatisation of mobile telephone services, tax increases and action to stem losses at the state electricity company. Active reform implementation would bring positive rating action. By contrast, renewed political turbulence or heightened geopolitical tensions that triggered sustained falls in non-resident deposits and a rising debt burden would bring negative rating action.

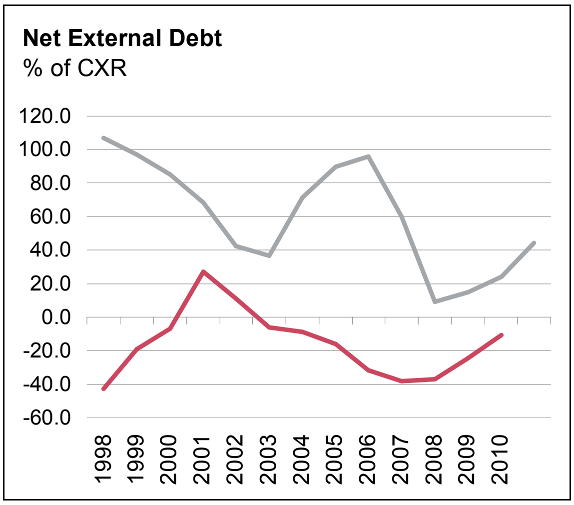
Key Indicators for Lebanon

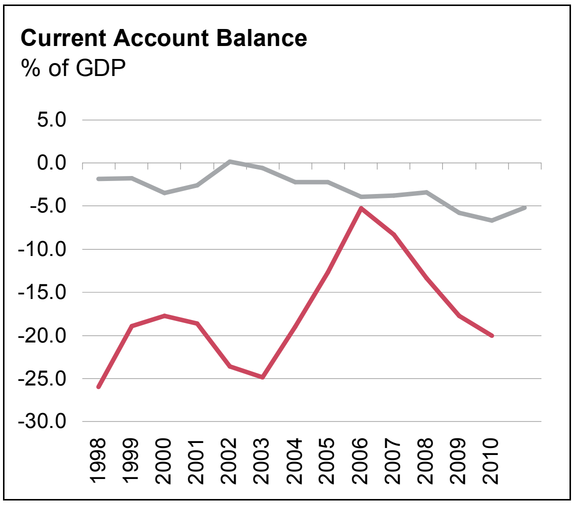
Population (2007): 4.1m
Population growth rate (2002-2007): 1.2% p.a.
GDP (2007): USD24.7bn
GDP per head at market exchange rates (2007): USD6,033
GNI per head at purchasing power parity (2006): USD5,460 (= 12% of USA level)
Modern sovereign rescheduling history: None

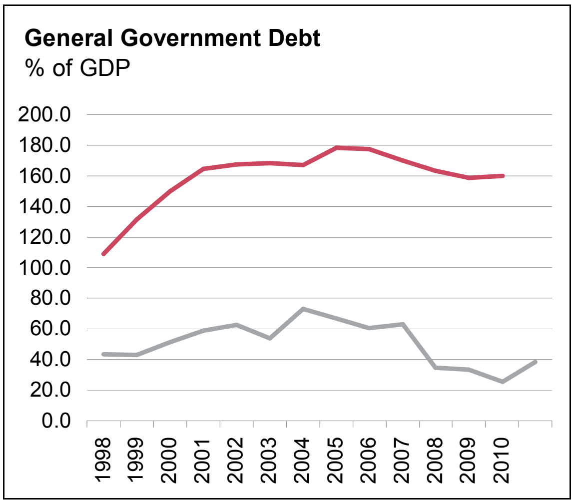
	2004	2005	2006	2007e	2008f	2009f	2010f
Domestic economy and finance							
Real GDP growth (%)	7.5	1.1	0.0	4.0	4.0	3.5	4.0
Unemployment (% of labour force)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Consumer prices (annual average % change)	1.7	-0.7	5.6	4.5	9.5	7.0	3.0
Gross domestic savings (% of GDP)	-5.7	-3.6	-9.9	-14.6	-16.4	-17.7	-18.1
Gross domestic investment (% of GDP)	22.0	21.1	13.6	14.3	15.0	16.0	17.0
Short-term interest rate (%)[a]	5.3	5.2	5.2	5.2	5.2	5.2	5.2
Broad money (% change Dec to Dec)	10.1	4.5	7.8	12.4	15.3	12.9	9.3
LBP per USD (annual average)	1,507.5	1,507.5	1,507.5	1,507.5	1,507.5	1,507.5	1,507.5
REER (CPI, 2000=100)	82.3	79.0	80.6	77.4	72.7	79.0	80.6
REER: % change (+ = appreciation)	-6.9	-4.1	2.1	-4.0	-6.1	8.7	2.0
Public finances							
General government balance (% of GDP)	-10.2	-9.1	-14.5	-11.1	-11.4	-10.9	-11.7
General government debt (% of GDP)	167.1	178.4	177.4	169.9	163.4	158.4	159.6
General government debt maturities (% of GDP)[b]	62.6	42.2	50.4	41.1	30.4	28.5	24.7
General government debt/revenue (%)	722.4	783.0	831.8	724.2	673.9	653.5	659.7
Interest payments/revenue (%)	52.4	46.0	59.9	50.6	45.2	44.1	44.4
Balance of payments							
Current account balance (USDm)	-4,080	-2,748	-1,201	-2,045	-3,716	-5,430	-6,572
Current account balance (% of GDP)	-19.0	-12.7	-5.3	-8.3	-13.4	-17.7	-20.0
Current account balance plus net FDI (USDm)	-2,300	-79	1,468	1,033	84	-2,130	-3,272
Current account balance plus net FDI (% of GDP)	-10.7	-0.4	6.5	4.2	0.3	-7.0	-10.0
Gross financing requirement (% of official reserves)[c]	54.6	40.5	33.0	26.9	42.6	41.3	46.0
Current external receipts CXR (USDm)	18,139	19,642	22,265	24,486	27,224	29,702	31,927
Current external receipts CXR (annual % change)	8.8	8.3	13.4	10.0	11.2	9.1	7.5
Current external payments CXP (USDm)	22,219	22,390	23,466	26,531	30,940	35,132	38,499
Current external payments CXP (annual % change)	2.9	0.8	4.8	13.1	16.6	13.5	9.6
External assets and liabilities							
Gross external debt (USDm)	25,209	24,042	25,088	27,536	30,486	31,936	33,386
Gross external debt (% of GDP)	117.4	111.5	110.2	111.3	110.2	104.3	101.8
Gross external debt (% of CXR)	139.0	122.4	112.7	112.5	112.0	107.5	104.6
Net external debt (USDm)	-1,612	-3,168	-7,108	-9,362	-10,107	-7,306	-3,364
Net external debt (% of GDP)	-7.5	-14.7	-31.2	-37.8	-36.5	-23.9	-10.3
Net external debt (% of CXR)	-8.9	-16.1	-31.9	-38.2	-37.1	-24.6	-10.5
Public external debt (USDm)	9,562	9,395	9,886	10,100	10,300	10,500	10,700
Public external debt (% of GDP)	44.5	43.6	43.4	40.8	37.2	34.3	32.6
Net public external debt (% of CXR)	-20.4	-23.2	-26.5	-24.9	-42.5	-37.1	-29.3
Public FC denominated & FC indexed debt (USDm)	18,375	19,133	20,330	21,221	22,266	23,328	24,389
Short-term external debt (% of gross external debt)	55.1	53.4	56.4	54.4	57.9	59.0	60.0
External debt service (% of CXR)	22.0	19.4	20.6	14.3	15.2	15.6	13.9
External interest service (% of CXR)	3.7	6.1	5.3	5.3	3.5	3.5	3.5
Liquidity ratio (%)[d]	140.9	151.6	156.2	182.4	193.2	182.1	168.5
Official international reserves including gold (USDm)	13,269	13,947	15,780	16,188	21,882	21,532	20,040
Official international reserves in months of CXP cover	7.2	7.5	8.1	7.3	8.5	7.4	6.2
Official international reserves (% of broad money)	28.1	28.3	29.7	27.1	31.7	27.7	23.6

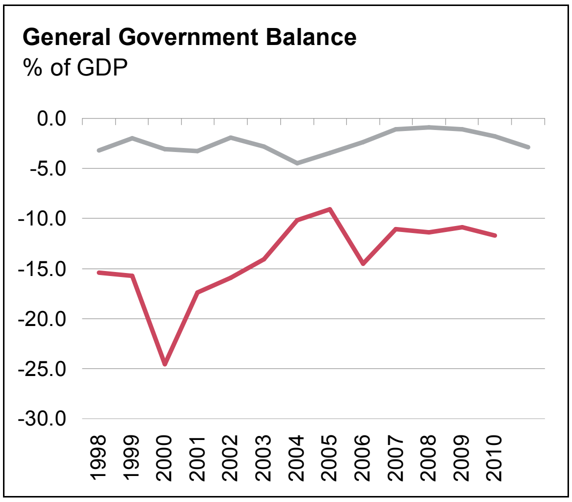
[a] Three LBP T-bills
[b] Maturities of medium- and long-term debt during year plus short-term debt outstanding at the beginning of the year
[c] Current account balance plus amortisation of medium- and long-term debt, over official international reserves
[d] Official reserves incl. gold plus banks' foreign assets/debt service plus liquid external liabilities

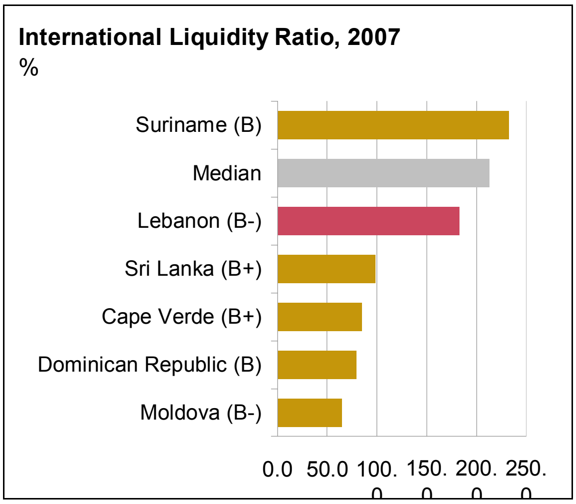
Peer Comparison

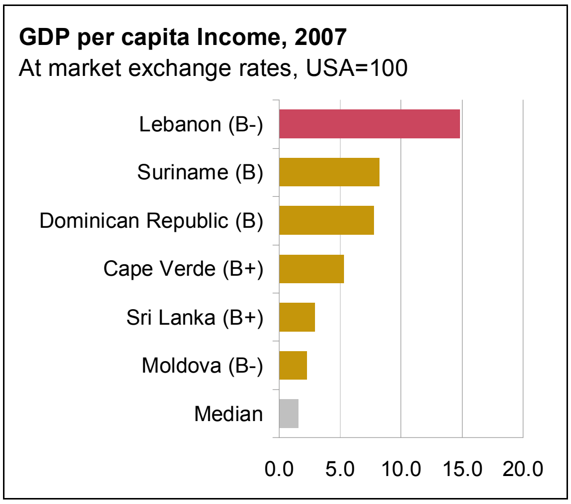












Lebanon

B Median

Peer Group

Rating	Country
B	Benin
	Cameroon
	Dominican Republic
	Mozambique
	Suriname
	Uganda
B-	Bolivia
	Lebanon
	Malawi
	Mali
	Moldova
	Rwanda
CCC	Ecuador

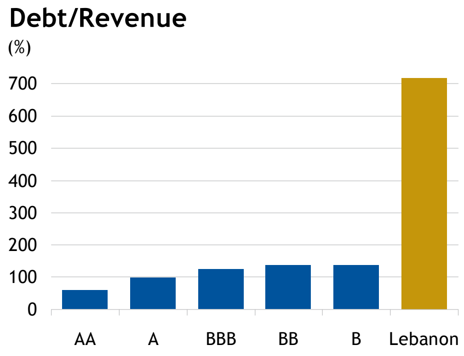
Rating History

Date	Long-term foreign currency	Long-term local currency
Sep 2001	B-	B-
Feb 2001	B+	B+
Jun 1999	BB-	BB
Jun 1998	BB-	BB+
Feb 1997	BB	BBB-

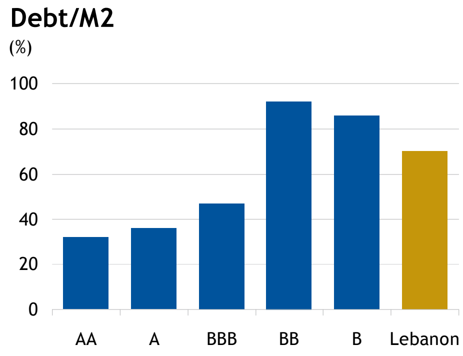
Rating Analysis

Lebanon's 'B-' rating reflects the highest public debt burden and budget deficit of any Fitch-rated sovereign and acute political instability which has prevented implementation of plans to reduce them. Government debt of 724% of revenue is over five times the 'B' category median and higher even than Japan ('AA') and Sri Lanka's ('B+') ratios (both over 500%). Moreover, even if the government were to succeed in its plan to reduce debt to 130% of GDP by 2011, this would still be exceeded only by Japan's ratio of over 170%. The budget deficit was 11.1% of GDP last year. (The official deficit figure excludes some foreign-financed capital spending and is slightly lower at 10.3% of GDP.)

Lebanon's Government Debt Ratios



Source: Fitch sovereign comparator, June 2008



Source: Fitch sovereign comparator, June 2008

Despite such high debt ratios and a history of political turbulence, Lebanon has managed to avoid default due to the resilience of the economy and especially the banking system, a supportive diaspora and donor community, and skilful management of public finances and debt. Despite war with Israel in 2006 and an 18-month political standoff between government and opposition which brought government to a virtual halt, GDP growth bounced back to 4% last year and could exceed that this year, non-resident deposits have reached new records, and the budget deficit and debt burden are declining.

Critically, pressure on public finances has never led to calls to redirect debt service spending to other uses. And strong external donor support is focussed primarily on preserving Lebanon's fragile political system with its multi-confessional character. There are no signs of recent political developments bringing any change here, but such developments cannot be totally ruled out in the future.

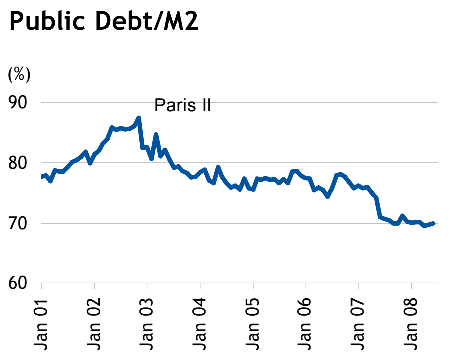
Lebanon receives important external support from the Lebanese diaspora and friendly Arab and Western governments. Receipts from tourism and private transfers help offset a trade deficit of around 30% of GDP. The current account deficit narrowed to an all-time low in 2006, despite the war with Israel, and the increase in the deficit to 8.3% of GDP last year mainly reflected higher imports, partly financed by donor grants. The deficit was more than covered by inward FDI of over 11% of GDP, mainly construction and real estate, especially from the Gulf. Lebanon's gross external financing need of 27% of reserves last year was well below the 'B' category median and the forecast increase to 42% this year is still in line with the 'BB' median. Gross reserves rose USD2.5bn in H108 and by almost USD5bn in the year to August, including valuation gains.[1]

Non-resident deposits help give Lebanese banks an aggregate balance sheet second only to Luxembourg and Hong Kong relative to GDP. M3 is equivalent to 242% of GDP.

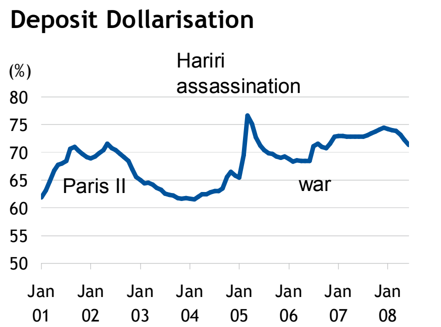
[1] Lebanon's reserves include substantial gold holdings, worth USD7.7bn at current prices. However, these cannot be sold without a constitutional amendment.

This is an important reason why Lebanon is able to sustain an apparently huge debt burden, since at 70% of M2 Lebanon's debt is well below 'B' and 'BB' medians. With domestic lending opportunities limited, banks hold around 60% of government LBP and FC debt, helping explain Lebanon's net external creditor position on a residency basis, despite one of the highest ratios of government FC debt to current account receipts (CXR) in the 'B' category.

Banking System Pressure Points



Source: BdL



Source: BdL

The downside is that banks' exposure to the government is large: direct debt to government is equivalent to about 25% of assets and exposure to the central bank (BdL) is similar. This means that any default by the government would have severe implications for banks. However, it also means that it is in banks' collective interest to support the government by at least maintaining their exposure to government debt. This does not mean that banks have an unlimited appetite for government paper, however. In the past, when the government debt burden and banks' exposure to government have been rising, banks have become increasingly reluctant to take on more government paper. This was most vividly demonstrated at the end of 2002, when debt reached an all-time high of almost 90% of M2. That prompted banks to withdraw from the market and heralded the Paris II donor conference. Debt to M2 has fallen fairly consistently since then, to its current 70%. Deposit dollarisation is another key indicator of market stress and was on a rising trend until earlier this year, but has now begun to decline again.

Lebanon has maintained access to the eurobond market throughout most of the recent political turbulence, with over USD3bn of maturing eurobonds rolled over or re-financed over the past 18 months. However, for most of 2007 the central bank was the primary buyer, distributing the bonds to banks in the secondary market. BdL's active and adept operations in the government debt market are an important near-term support for government creditworthiness. Most of the reduction in government debt last year reflected valuation gains on BdL gold holdings, 80% of which were passed to the government. But BdL's balance sheet has weakened and its ability to provide FC support is limited. Eurobonds issued this year – totalling USD2.3bn – have been through normal market channels.

Lebanon's rating also reflects a relatively high per capita income and supportive business climate in peer group terms. Although inflation has risen this year, the long-standing USD peg has proved robust, not suffering any sustained pressure. Nevertheless, the combination of the USD peg, potentially volatile non-resident deposits and over 70% dollarisation is a major systemic risk given Lebanon's susceptibility to shocks. Although gross reserves have reached an all-time high this year, liquidity is still relatively weak.

Local Currency Rating

The Local Currency Rating is the same as the FC rating given the high degree of dollarisation and banks' heavy participation in both local and FC debt markets, making it difficult to differentiate between the two in any default.

Country Ceiling

The Country Ceiling is the same as the FC IDR despite the virtual absence of exchange controls. A government debt default would inevitably affect the banks as major holders of government debt.

Political Situation

The Doha Accord of May 2008, brokered by Qatar's prime minister, has ended an 18-month political vacuum in which Lebanon's parliament did not meet, the government's policy agenda was severely curtailed and, since November, the country was without a president.

Key Dates in Lebanon's Recent Political History

2004

September: UN Security Council resolution 1559 demands the withdrawal of Syrian troops from Lebanon and respect for Lebanese sovereignty. Under Syrian pressure, the Lebanese parliament votes to extend incumbent President Émile Lahoud's term of office for three years.
October: Prime Minister Rafik Hariri resigns

2005

February: Assassination of former Prime Minister Hariri
April: After major demonstrations in Beirut and strong international pressure, Syrian troops withdraw from Lebanon
May: Parliamentary elections bring in a new government under Fouad Siniora

2006

July: War with Israel
August: UN-brokered ceasefire establishes UN peacekeepers on Lebanon's southern border with Israel. UN Resolution 1701 calls for the disarmament of militias and the setting up of an international tribunal to try suspects in the Hariri assassination.
November: Hizbollah withdraws its ministers from the cabinet

2007

January: Paris III donor conference
April: IMF programme signed
June: UN tribunal established to investigate the Hariri assassination
November: President Lahoud's term expires. Parliament unable to agree a successor.

2008

May: Confrontation between the government and Hizbollah comes to a head. Qatari mediation under the auspices of the Arab League leads to agreement of a new government of national unity in which Hizbollah has a blocking minority of 11 out of 30 seats. Parliament convenes and elects former army chief General Michel Suleiman as president. Prime Minister Siniora re-appointed.
July: New cabinet announced
August: New government wins a parliamentary vote of confidence

2009

May: Parliamentary elections to take place under a new electoral law

Since the war with Israel in summer 2006, political tensions had gradually increased between the majority March 14th bloc, consisting of Saad Hariri's Future Movement and other mainly Sunni and Christian allies, and the opposition March 8th bloc, comprising Hizbollah and other Shiite and Christian groups. Hizbollah pulled its ministers out of the government in November 2006 in protest at what it saw as the majority's hostility to it during the war. It demanded a broader-based government of national unity in which it would have a blocking minority. The stand-off came to a head in May this year, triggered by a government attempt to dismantle Hizbollah's telecommunications network and to reassign the chief of airport security, who was a Hizbollah supporter. Hizbollah militia overran West Beirut, including the downtown area, and closed Beirut airport, demonstrating its power to challenge the Western-supported government. Fears of worsening violence and perhaps a relapse into civil war prompted mediation by the Prime Minister of Qatar under the auspices of the Arab League. Agreement was reached on a new president, formation of a government of national unity, and new parliamentary elections to be held in May 2009 under a new electoral law. Long-running protests that had closed parts of the downtown area for several months have ended, although sporadic violence continues outside Beirut.

Key Parliamentary Factions

- The Future block, led by Rafik Hariri's son Saad, elected mainly from Beirut, North Lebanon and West Bekaa (mostly Sunni Muslim)
- The Lebanese Forces/Qornet Shahwan/Phalangists (mainly Christian) elected from various areas and allied with the Future block
- The two blocks Amal and Hizbollah (mostly Shiite Muslim), elected mainly from the south of Lebanon, southern Beirut and the North Bekaa
- Former general Michel Aoun's block (mostly Christian), elected mainly from the northern part of Mount Lebanon

The Doha Accord allocates 16 ministers to the parliamentary majority, 11 to the opposition and three to the president to appoint. In subsequent negotiations, senior positions allocated to the majority include the finance ministry while the opposition provides the deputy prime minister and foreign minister and minister of telecommunications. Within the opposition, Hizbollah was allocated three seats but gave two of them to its allies in other parties. The opposition's 11 seats out of 30 give it a blocking minority on decisions needing a two-thirds majority, for example amending the constitution, adopting the budget, some high level appointments, the dismissal of ministers, amendment of electoral laws and the dissolution of parliament. If the opposition withdraws the government is not quorate.

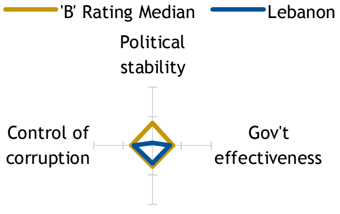
The government received a parliamentary vote of confidence for its programme in August, including economic reforms agreed at the January 2007 Paris III conference. In practice, however, the focus in the short term is likely to be on political rather than economic issues. The Doha Accord tasks the president with initiating a dialogue on national defence strategy, to address amongst other things the issue of Hizbollah's weapons; agreeing a way forward on the UN tribunal into the assassination of former Prime Minister Hariri; and regularising relations with Syria. President Suleiman has made a start with the first visit of a Lebanese president to Syria since Syria withdrew its troops in 2005. His position as a consensus candidate puts him in a stronger position to intermediate between opposing government parties than his predecessor. However, outstanding issues are highly contentious, with compromise difficult to envisage. The new government will be the broadest in recent history, but while in theory it therefore attracts widespread support, its effectiveness remains to be seen. It is probably best seen as a caretaker administration, to take Lebanon through to next year's elections. In preparation, it will have to agree a new electoral law, which will also raise sensitivities. Against this background, little substantive economic legislation is likely to be agreed.

Distribution of Seats by Confession

Muslim	**64**
Shia	27
Sunni	27
Druze	8
Alawite	2
Christian	**64**
Maronite	34
Greek Orthodox	14
Greek Catholic	8
Armenian	6
Protestant	1
Other	1

Source: MEED

Governance Indicators



Source: World Bank and Fitch

Political convention requires that the president, prime minister and speaker of parliament are reserved respectively for Christian, Sunni and Shia representatives. In addition, Christian and Muslim MPs always have equal representation (see table). The issue in next year's elections therefore is what balance of forces within these constraints will form a majority. Currently, Christian MPs are split into two main factions, the Aoun block of former general Michel Aoun, allied with the opposition March 8th bloc, and the rest allied with the majority March 14th bloc. Sunni and Shia factions are more homogenous but on opposing sides of the political divide.

In light of Lebanon's recent turbulent political history, it is no surprise that governance indicators, as measured by the World Bank annual survey, are weaker than the median for Lebanon's 'B' category peers. Indeed, Lebanon's score for "political stability" is the lowest of any country reviewed in the World Bank study, just below Nigeria and Sri Lanka. The only indicator in which it scores better than the 'B' median is "regulatory quality" — also reflected in a ranking in the World Bank's 'Ease of Doing Business' survey of 85 out of 178 — better than the 'BB' median.

Structural Comparisons

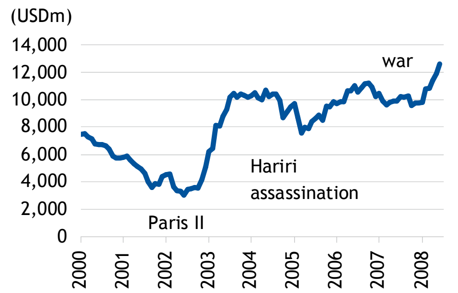
	Lebanon (B-)	Cape Verde (B+)	Sri Lanka (B+)	Jamaica (B+)	B median	BB median
GNI per capita, USD (PPP, 2006)	5,460	5,980	5,000	4,030	2,640	5,880
GDP per capita, USD (market rates)	6,033	2,716	1,677	4,220	1,254	3,146
Real per capita GDP growth, 5-year average (%)	2.2	4.3	6	1.2	3.3	4.7
UN Human Development Index (rank of 177)	88	102	99	101	117	93
Inflation, 5-year average (%)	2.5	1.9	11.3	11.4	7.9	8.0
Gross domestic savings (% GDP)	-14.6	-2.2	17.6	11.2	11.2	20.8
Gross domestic investment (% GDP)	14.3	44	27.9	33.8	22.1	23.1
CXR (% GDP)	99.0	73.9	38.6	66.4	43.5	41.3
Commodity dependence (% exports)	30	12.3	29.8	35.5	83.0	47
Private-sector credit (% GDP)	74.4	47.9	32.8	12.4	19.5	30.0
Ease of doing business (rank of 178, 2008)	85	132	101	63	118	102

Data for 2007 unless noted otherwise
Source: Fitch Sovereign Data Comparator - June 2008; UN; IMF; World Bank

Macro and Structural Issues

The main anchors of macroeconomic policy remain the long-standing peg of the Lebanese pound to the USD and the five-year programme of fiscal and structural reforms presented by the government to the January 2007 Paris III donor conference in the aftermath of the summer 2006 war with Israel. Monitoring of the 2007 programme was via an IMF Emergency Post-Conflict Assistance (EPCA) programme agreed in April 2007, which has concluded with Lebanon in full compliance. A follow-on programme is possible, but for the moment the IMF is merely engaged in quarterly monitoring.

Gross Foreign Currency Reserves



Source: Banque du Liban

Lebanon received substantial grant aid in 2006 and 2007, helping it finance the immediate fiscal impact of the war (see *Public Finance* section below). However, the major reduction in the fiscal deficit and public debt envisaged under Paris III has not proved possible because of the political stalemate.

Political instability has not brought any sustained pressure on the peg, however, and gross reserves have risen to new highs over the past year. Interest rates have not moved in parallel with US rates because of the authorities' desire to insulate, as much as possible, the government, banks and the private sector from higher rates. This has required active money market intervention by BdL to offset government funding shortfalls and consequent short-term liquidity pressures and to minimise international reserve loss. The central bank has often been the principle buyer of new government debt issues, although these have for the most part been passed on to banks. The BdL balance sheet contains USD8.75bn equivalent of government securities. The IMF has expressed concern about the weakness of BdL's balance sheet and the lack of flexibility of LBP interest rates.

Inflation has increased to a decade high this year — reaching 13.9% in the year to July and averaging 7% yoy in the first seven months.[2] Fitch forecasts an annual average for 2008 of 9.5%. Inflation is mainly imported, though the disruption during the summer 2006 war also raised the price level. As in many emerging markets, higher food and fuel prices are the main culprit, rising by 20.7% and 16% respectively over the past year. Gasoline prices have been increased, although they remain heavily subsidised. Current brisk GDP growth of at least 4% is not felt to have had a major inflationary impact, given that the growth to a large extent represents recovery from the war. However, investment rates are very low and would need to rise to support sustained growth at this rate. National accounts data remain weak, but a key growth driver has been construction and real estate, which is the target of much FDI, especially from the Gulf. Property prices have risen rapidly this year.

Public Finance

Most measures of the strength of public finances show Lebanon in a very weak position compared to rating peers. As well as the highest deficit and debt/revenue ratios amongst rated sovereigns, budgetary pressures are also evident in a high interest burden that consumes half of all budget revenue and accounts for a third of budgetary spending. Nevertheless, the authorities have done well to contain the budget deficit and debt burden since 2005 in the face of political turbulence and outright war in 2006. Debt management has also been adept. These institutional strengths provide important support for Lebanon's rating, albeit at a low level.

Public Finance Comparisons, 2007

	Lebanon (B-)	Cape Verde (B+)	Sri Lanka (B+)	Jamaica (B+)	B median	BB median
General government balance (% GDP)	-11.1	-2.1	-6.9	-5.8	-1.1	-1.1
Interest (% revenue)	50.6	5.2	30.7	43.2	5.2	8.7
GG debt (% revenue)	724.2	246.7	515.5	414.9	136.6	136.6
GG debt (% GDP)	169.9	76.8	85.8	125.8	33.4	32.7
Domestic debt (% total debt)	49.5	43.8	50.2	48.7	39.2	40.8
GG debt maturities (% GDP)	41.1	1.8	17.9	n.a.	2.6	3.7

Source: Fitch

In 2007, public finances recovered from the material deterioration they suffered in the wake of the war with Israel in summer 2006. Rather than widening as expected, the (official) fiscal deficit narrowed from 13.3% of GDP in 2006 to 10.3% of GDP in 2007,[3] owing mostly to a 20% increase in revenues that in turn reflected resurgent economic activity, administrative tax reforms and inflation. Even so, revenues and grants fell short of target. However, spending increases were also modest, due to a decline (as % of GDP) in transfers to municipalities and EdL, leading the primary

[2] There is no official consumer price index. The figures quoted are published by the Consultation and Research Institute (CRI).

[3] Fitch's figures for the primary and overall fiscal balance, +0.7% and -11.1% of GDP respectively, are weaker than official figures, since Fitch includes the foreign-financed capital expenditure of the Council for Development and Reconstruction (CDR). This amounted to 0.8% of GDP in 2007.

balance (excluding CDR expenditure and grants) to improve from -1.2% of GDP in 2006 to 0.5% of GDP. Spending was below target, largely due to slower-than-expected disbursement of budgetary support from Paris III donors, reflecting the 18-month political vacuum. In 2007, Lebanon received USD565m in budgetary support (2.3% of GDP, of which 1% of GDP was grants).[4] But to date the government has received only about USD1.3bn of the USD5.6bn pledged towards the public sector at the conference in 2007. The debt/GDP ratio fell from 177% in 2006 to 170% in 2007. However, most of this reduction is attributable to a transfer of unrealised gold valuation gains, amounting to 6% of GDP, from the central bank to the government.

Fiscal Projections, 2007-2008

	2007			2008
(% GDP)	Paris III Jan 07	IMF EPCA May 07	Outturn	IMF EPCA May 08
Revenue and grants	25.8	26.7	23.5	24.0
Expenditure	39.3	39.1	33.8	34.3
Interest	13.2	12.4	11.9	12.3
Primary balance	-0.3	0.0	1.6	2.0
Overall balance	-13.5	-12.4	-10.3	-10.3
Public debt	170	176	170	167

Source: "*Recovery, reconstruction and reform*", MoF, Jan 2007; IMF report no. 08/150; MoF; and Fitch estimates

The most recent official projection for 2008 is contained in the May IMF EPCA review. This sees the overall deficit contained to last year's 10.3% of GDP, with revenue and spending both up by a modest 0.5% of GDP. Within this, interest payments are likely to grow less quickly as a result of lower government debt, so the primary surplus is expected to rise to 2% of GDP, but with the debt ratio falling only slightly. First-half outturns are consistent with this and Fitch projects a further fall in debt to 163% of GDP. However, much will depend on the actions of the new government and the speed of disbursement of Paris III funds.

The medium-term goal remains to reduce government debt to below 130% of GDP by 2012. This is largely reliant on privatisation (31% of GDP), but fiscal adjustment (7% of GDP) and Paris III donor assistance (6% of GDP) also make a contribution. The biggest ticket item available for privatisation is the mobile telephone system, which could realise as much as USD6bn or about 25% of GDP for the public exchequer. A number of regional companies have expressed interest. However, its sale has been repeatedly stymied by the political situation and was interrupted yet again by security events in May 2008. The groundwork for privatisation has been completed, although the procedure will still take about five months to complete once final go-ahead is given. It is intended that this should be completed prior to the elections, but further delay is possible. A provision in the IMF programme to set a floor for petrol excise has not been implemented.[5] Planned increases in VAT from 10% to 12% and in the tax rate on interest income from 5% to 7%, and the introduction of a General Income Tax (GIT), also remain on hold. On the expenditure side, a key objective is to make long-planned efficiency gains at EdL.

A positive primary balance undoubtedly alleviates the immediate pressure on debt dynamics. Revenues are also buoyant, despite the absence of planned new tax measures. Nevertheless, spending pressures are rising — expenditure grew 13.3% in H108 — not least due to the surge in global oil prices that will result in substantially higher payments to the loss-making EdL. Transfers to EdL were 3.2% of GDP in 2007 but were running at an annual rate of over 5% of GDP in H108. The outgoing

[4] In addition, Malaysia agreed to exchange USD0.5bn in debt for a bond with longer maturity and lower interest.

[5] Subsidies on domestic petrol sales are netted off excise taxes, which have fallen to zero.

government also agreed an increase in the minimum wage.[6] Notwithstanding these increases, in October the government hopes to table a budget that will see 1% lower spending in 2009 than in 2008, thanks mainly to a public-sector hiring freeze (not extending to the civil service) but also to the re-prioritising of capital spending and transfers. Fitch believes that given the resolution of the political stalemate, the government's adeptness at fiscal control over 2001-2005, and its demonstrated commitment to reform in the face of conditional donor support over 2007, fiscal rationalisation is likely to continue and the overall deficit should be at least contained. However, inflation-led demands for greater social spending, a rising oil bill and an impending parliamentary election could weigh on fiscal adjustment.

Any prolonged slippage in reforms and fiscal adjustment would be severely detrimental to debt sustainability. According to an IMF analysis,[7] full implementation of the Paris III reforms could see debt falling to as low as 93% of GDP by 2026. And a primary surplus maintained at 1.3% of GDP would be sufficient to keep the ratio on a downward trajectory. But less than full implementation of reforms or a shock to growth or real interest rates would set the ratio on an unsustainable rising path once more (see table below).

IMF Debt Sustainability Analysis

Variable	Assumptions	Debt/GDP ratio by 2026: Baseline	Shock	Historical scenario[a]
Real interest rate (%)	Baseline= 4.9 Shock= 6.7 Historical= 8.6	93	141	240
Growth rate (%)	Baseline= 4.0 Shock= 3.2 Historical= 2.8	93	159	217
Primary balance (% GDP)	Baseline= 3.2 Shock= 1.3 Historical= -1.0	93	134	180
Partial adjustment and no privatisation	Interest rate spread= 220bp Growth rate = 3 Primary balance= 3.0 by 2012	93	230	Not applicable

[a] Historical scenario has variables equal to their decade average
Source: IMF Article IV Report, December 2007

A greater share of deficit financing in 2007 came from Paris III disbursements. This allowed government liabilities to BdL to shrink, even though banks withdrew from the government debt market for much of the year. However, the reduction in BdL holdings of T-bills mainly reflected use of the proceeds of revaluing BdL's gold holdings in June. Its T-bill holdings rose again in Q3 and only fell in Q4. Banks' T-bill holdings fell through the year until Q4. During 2007 Lebanon carried out eight eurobond transactions totalling USD2.7bn. However, all but a five-year issue for USD400m in May was taken up by BdL, though ultimately sold on to banks.

Central Government Financing

(LBPbn)	2004	2005	2006	2007
Central government deficit	3,056	2,798	4,564	3,838
BdL	654	602	-2,342	-2,280
Commercial banks	3,614	2,587	4,247	205
Government institutions (pension fund etc.)	-352	245	835	1,740
Other creditors	-1,163	-465	1,067	24
Bilateral and multilateral creditors	84	-133	39	2,352
Other	219	-38	718	1,797

Source: MoF, IMF, BdL and Fitch estimates

[6] Subject to ratification by the parliament, the government has decided to increase the monthly minimum wage from LBP300,000 to LBP500,000, at an estimated cost of 1.5%-2% of GDP per annum. However, given the sharp increase in inflation, labour unions are agitating for an increase to LBP1,100,000.

[7] 2007 Article IV Report: December 2007.

In the first half of 2008, commercial banks returned to their role of financing most of the budget deficit, accounting for 87% of the increase in gross debt in that period, mainly in the form of LBP T-bills. In addition, four maturing eurobonds have been refinanced through three new issues. The first, in March, was for USD875m over five years; the second, in April, for USD882m over six years, in exchange for three maturities totalling USD1bn in May, June and August; and the third, in August, for USD500m over seven years.

Market issued Eurobonds: maturities and recent Issues

(USDm)	Maturities	New issues	
2007	**1,219**	**2,238**	
February	750	1,000	Initially issued to BdL
May		400	
July	100	138	Initially issued to BdL
October	369	400	Initially issued to BdL
November		300	Initially issued to BdL
2008	**2,119**	**2,257**	
March	869	875	
April		882	
May	250		
June	250		
August	750	500	
2009	**2,376**		
May	338		
August	352		
October	636		
November	625		
December	425		

Source: MoF

The 18-month political stalemate resulted in a reduction in the average maturity of Lebanon's debt to 4.3 years as at June 2008. Eurobond debt now has an average maturity of just over four years and T-bill debt just under two years, although this has now begun to increase again.

Central Government Debt

(LBPbn)	2005	2006	2007	Jun 2008
Total	**57,985**	**60,851**	**63,364**	**67,060**
By residency of holder				
Domestic	44,468	49,238	51,701	55,096
Foreign	13,517	11,613	11,663	11,964
By place of issue				
Domestic	34,925	35,988	37,157	40,456
o/w LBP T-bills	3,325	4,129	5,474	5,563
Foreign	23,060	24,863	26,207	26,604
o/w market eurobonds	18,729	20,399	20,780	20,927
By currency denomination				
Local currency	29,141	30,204	31,373	34,672
Foreign currency	28,844	30,647	31,991	32,388
USDbn equivalent	19.1	20.3	21.2	21.5
Market-held debt[a]	34,721	38,670	39,221	42,635
By maturity				
Less than 12 months (residual maturity)	7,960	6,609	4,098	4,550
Average maturity (years)	5.7	6.0	5.0	4.3
T-bills	2.6	2.9	1.61	1.73
Eurobonds	6.2	6.6	5.92	4.94

[a] Gross debt less that held by public institutions and bilateral and multilateral lenders
Source: Mof, BdL and Fitch estimates

Banking System

The banking system continues to play a key role in financing the government. Banks hold around 60% of marketable government debt — both eurobonds and T-bills. The proportion of T-bills held was as high as 80% in 1999 but fell sharply up to 2001 — a move which precipitated the government's previous financing problems in 2001-2002 and made the Paris II conference necessary. The proportion reached a low of just under 50% in 2003 and has subsequently increased gradually. Bank holdings of eurobonds have shown a similar pattern, peaking at 80% in the late 1990s, then falling to around 50% on the eve of Paris II and then gradually climbing to current levels. When banks have wanted to reduce their holding of government debt, the official sector has ultimately had to step in — the central bank in the first instance followed by friendly governments.

Given the role of the banking system as the largest single holder of public debt, a critical ratio to monitor is the ratio of debt to M2.[8] This encapsulates the large size of the banking system relative to the economy, with M2 equivalent to 242% of GDP — the largest such ratio outside Luxembourg and Hong Kong. Public debt rose from 40% of M2 in the early 1990s to 88% on the eve of Paris II. It then fell to a 75%-80% range but dropped sharply last year to its current 70%. This is below the median for 'B' and 'BB' rated sovereigns (see earlier chart).

At 74% of GDP, private-sector credit is less than one-third of the M2/GDP ratio. Whether this is viewed as crowding out or reflecting the dearth of domestic lending opportunities, it helps explains why banks are such large holders of government debt. Government debt comprises 26% of banks' balance sheets, which is high compared to an emerging market average of 15%, but by no means the highest. It is a similar level to Egypt and Mexico and lower than in India and Turkey. However, taking account of holdings of BdL debt and other BdL liabilities raises broader "sovereign" exposure to 53% — similar to Argentina's.

Key Facts: Banking System, 2007

M2 (% GDP) - including FC deposits	241.7
Deposit dollarisation - residents (%)	74.4
Private credit (% GDP)	74.4
Exposure to government debt (% assets)	26.1
Exposure to BdL (% assets)	27.0
NPL ratio (% loans)	10.1
Capital adequacy ratio	25.0
Public ownership (% of assets)	0
Foreign ownership (% of assets)	<20
Banking System Indicator (BSI)	D
Macro-Prudential Indicator (MPI)	1

Source: IMF, BdL, MoF, Fitch estimates

Given Lebanon's fragile political and financial situation, the combination of 74% deposit dollarisation and potentially volatile non-resident deposits (14% of deposits[9]) in the context of an exchange rate peg represents a further systemic weakness of the banking system. Although none of the major banks are government owned, the authorities are highly likely to support them in the event of a sovereign crisis.[10] Loan quality is also low, with borrowers highly indebted and gross NPLs at 10.1% of total loans at end 2007. This ratio has improved, however, and fell further to 8.5% in mid-2008. Apparently high capitalisation of almost 25% is also flattered by the zero risk weight applied to LBP government debt. However, under Basel II guidelines, introduced from 2008, the risk weighting of eurobonds rises to 100%.

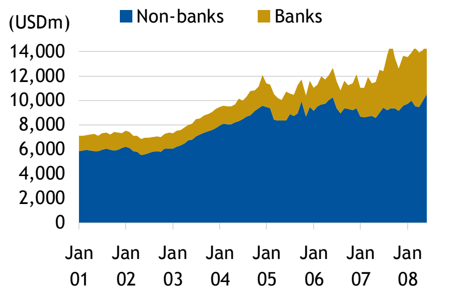
[8] This is equivalent to BdL's M3 aggregate, which includes FC deposits.

[9] This is likely to be an underestimate. The residency qualification requires only an address in Lebanon. Many non-residents will have properties in Lebanon used for only part of the year but they will be officially classed as resident

[10] Their ability to do so, however, is reduced by already fragile public finances. This explains the relatively low Support Rating of '5' that Fitch assigns to some major banks, encapsulating both the sovereign's willingness and ability to provide support.

Fitch lowered the Individual Ratings of major Lebanese banks to 'D' ('weak') at the end of 2006, in the wake of the war. The Banking System Indicator (BSI) is 'D', denoting a weak system.[11] Risks are mitigated by the historical resilience of non-resident deposits and by banks' high liquidity. The biggest fall in deposits in any year was 20%. By contrast, liquidity substantially exceeds this: the formal requirement is for banks to hold 15% of deposits in BdL and a further 15% in other external liquid assets. In practice, liquidity currently exceeds 50%. The fall in deposits after the Hariri assassination was a relatively modest 5%.

Non-Resident Deposits



Source: Banque du Liban

Information about the structure of non-resident deposits is hard to come by due to bank secrecy laws. However, the majority — 70% — are from non-banks, largely non-resident Lebanese and other Arab depositors, which have traditionally been quite stable. However, the share of potentially more volatile interbank deposits is growing.

In an effort to diversify out of the volatile Lebanese operating environment, banks are increasing their operations overseas. Among the larger banks, 20% of assets are now in foreign operations, with the objective of generating half of profits abroad within three years. Target markets include Algeria, Egypt, Iraq, Jordan, Nigeria, Sudan, Syria, Tunisia and the Gulf.

External Finance

Lebanon's balance-of-payments figures are rudimentary. Although they have improved, the openness of the capital account and limited information on non-bank private-sector flows means that the main components are merchandise trade, official and banking sector flows. The trade deficit is around 30% of GDP and although exports have been growing strongly, helped by the weak USD, to which the LBP is fixed, merchandise exports remain among the smallest relative to GDP of any rated sovereign. The trade deficit is offset by large surpluses on transfers and services, reflecting remittances from and visits home by the large Lebanese diaspora. Last year's current account deficit of 8.3% of GDP was modest by comparison to its most recent peak of over 23% of GDP in 2003. The improvement reflects increased net transfers and a move of the income account from deficit to surplus, reflecting lower non-interest debits. However, the current account deficit increased last year as imports rose, mainly due to reconstruction needs, but higher

Current account finance: Cumulative 2002-7 USDm

Current account	**-19.3**
FDI and other equity	17.8
Repatriation of assets	11.4
Net borrowing	7.8
Errors and omissions	-12.5
Other	-0.2
Reserve increase	5.0

Source: IMF

The large current account deficit has generally been almost covered by FDI, largely reflecting inflows into construction and real estate, especially from Gulf countries. Net equity inflows have averaged over 15% of GDP for the last three years. Net portfolio equity inflows alone were almost 3% of GDP last year, with the Lebanese stock market rising strongly towards the end of the year. However, identified and unidentified outflows also increased sharply in 2006 and 2007, and reserves were broadly unchanged despite an increase in borrowing, especially by banks.

[11] See "*Assessing Bank Systemic Risk*", July 2005. Banking systems are categorised on a scale from 'A' (very high quality) to 'E' (very low quality), with most emerging markets falling into the 'D' category.

External Finance Comparisons

	Lebanon (B-)	Cape Verde (B+)	Sri Lanka (B+)	Jamaica (B+)	B median	BB median
Current account balance (% GDP)	-8.3	-9.2	-4.2	-14.5	-5.4	-3.4
Current account balance plus net FDI (% GDP)	4.2	-0.2	-2.8	-8.3	-1.6	1.8
Inward FDI (% GDP)	11.5	9.0	1.6	10.8	3.0	4.0
External finance need (% FX reserves)	26.9	52.5	150.7	188.7	67.3	37.3
Gross external debt (% CXR)	112.5	116.6	134.1	106.8	77.1	81.8
Net external debt (% CXR)	-38.2	44.5	97.1	62.8	15.3	-3.6
Sovereign external debt (% CXR)	41.2	62.8	109.8	79.7	55.3	44.1
Net sovereign external debt (% CXR)	-24.9	16	84	54	16.0	-0.4
Public debt (% total external debt)	36.6	53.8	81.9	74.6	68.0	59.1
Debt service ratio (% CXR)	14.3	5.4	9.9	18.0	7.0	9.9
Interest service (% CXR)	5.3	3.1	3.5	7.3	1.8	4.1
Liquidity ratio (2008)	182.4	95.7	102	126.9	274.2	218

Data for 2007 unless noted otherwise
Source: Fitch Sovereign Data Comparator, June 2008

Developments in H108 point to a major widening of the current account deficit this year. Exports and imports both rose by over 30%, but with imports now four times bigger than exports, the latter have to grow much faster to prevent the trade deficit from widening. Tourist receipts will be higher following the easing of political tensions — arrivals were up 28% in the year to July — and remittances are likely to rise again. Even so, the current account deficit could exceed 13% of GDP and rise higher still next year. Nevertheless, reserves were up by USD2.6bn in the first half (transactions basis) and by USD4.5bn by August (including valuation gains), so capital inflows have clearly more than matched the increased current account deficit. Banks attracted a further USD1.3bn in non-resident deposits in H1 and their overseas assets continue to be drawn down to fund domestic operations. Equity investment is likely to have increased, judging from the behaviour of the stock market and property prices. Net government FC issuance was small. Errors and omissions are assumed to have fallen, after the easing of political tensions.

Disbursements of Paris III donor support from now on will be increasingly linked to policy implementation. A reactivation of the reform process would be associated with both a reduced fiscal deficit, which will contribute to lowering the current account deficit, and a more comfortable financing position. Total donor assistance received in 2007 was USD565m. This is just a small fraction of the USD7.5bn pledged at the Paris III conference. Signed agreements now amount to USD4.7bn, of which USD1.9bn is for budget support and of which USD1.5bn has been received. Remaining disbursements of at least USD2.4bn and a maximum USD5bn will be spread over several years.

Paris III Pledges and Disbursements

(USDm)	Pledged	Signed	Received
Budget support	1,737	1,857	1,477
Project support	3,499	1,030	Ongoing
Private-sector support	1,463	1,266	576
Other	833	556	n.a.
Total	**7,532**	**4,709**	**n.a.**

Source: Paris III June 2008 progress report, MoF

Fitch estimates Lebanon's gross external debt rose slightly last year to USD27.5bn — the first significant increase since 2004. However, the rise was confined to private-sector borrowers; public-sector external debt on a residency basis is estimated to have remained stable at USD10bn. The banking system remains the largest external debtor with USD13.6bn, 70% of this representing non-resident deposits. Overall gross external debt has remained stable at around 111% of GDP since 2003 and has been declining as a share of CXR.

The public sector's modest external debt should be contrasted with its much larger FC debt of over USD21bn. The difference between the two reflects residents' holdings of USD10bn of this debt, which on a residency basis does not constitute external debt. Most of this USD10bn reflects banks' holdings of 60% of outstanding eurobonds. Non-resident market holdings of Lebanese eurobonds amount to little more than USD2bn.

Reconciliation of Sovereign Foreign Currency and External Debt

(USDbn)	2007
Government FC debt	**21.2**
Eurobonds	17.7
Held by banks	11.1
Held by BdL	2.6
Held by others (mainly non-resident)	4.0
o/w Paris II (foreign governments)	**1.9**
Market holders	**2.1**
Non-eurobond FC debt	**3.5**
Non-resident T-bill holdings (est.)	**0.2**
Government external debt	**7.7**
BdL liabilities	2.4
Sovereign external debt	**10.1**

Source: Mof, BdL and Fitch estimates

Lebanon's gross FC reserves of USD9.7bn at end-2007 fall just short of sovereign external debt. However, gold holdings are a substantial USD6.4bn, making the sovereign a net external creditor.[12] Having said that, BdL's liquid FC reserves are more than accounted for by banks' reserve requirements on FC deposits. A minimum of 15% of deposits must be held at BdL and a further 15% in other liquid external assets. In practice, banks observe a liquidity ratio of nearer 50%, with the equivalent of about 30% of deposits kept with BdL. This boosts BdL's apparent reserves, but in fact, net FC reserves are negative to the tune of USD6.5bn.

Despite BdL's negative net FC reserves, the country as a whole remains a net external creditor. This takes account of BdL's gold holdings, as well as banks' FC assets held overseas, as opposed to at BdL. The non-bank private sector has external debt of USD3.8bn. It also has sizeable external assets, but these are not included in Fitch's definition of the overall net external position. (Lebanon does not compile an International Investment Position.)

Lebanon's External Balance Sheet

(USDbn)	2007
Public-sector net liabilities	**-6.0**
Liabilities	10.1
Non-resident held eurobonds	4.0
Other government debt	3.7
BdL external liabilities	2.4
Assets	16.1
Foreign-exchange reserves	9.7
Gold	6.4
Banks' net liabilities	**-7.1**
Liabilities	13.6
Assets	20.7
Private non-bank liabilities	**3.8**
Total (net)	**-9.3**

Source: Mof, BdL and Fitch estimates

Of most relevance to the Foreign Currency Rating, however, is the overall FC position. The sovereign has net FC liabilities of USD18.2bn (74% of GDP) largely comprising the government's FC debt of USD21.2bn. BdL's gross FC assets of USD19.2bn are not far short of government FC debt, but netting off banks' reserve requirements and other BdL foreign liabilities (including USD1.5bn in deposits from Saudi Arabia and Kuwait made during the war with Israel) reduce BdL's net FC assets to just USD3bn. Banks are overall net FC creditors. Bank's net external assets of USD7bn are largely a counterpart to the portion of domestic FC deposits not matched by FC lending or deposits at BdL.

[12] Wider measures of Lebanon's international reserves, including those published by the IMF, include BdL holdings of eurobonds. However, although these may be a liquid FC asset in normal circumstances, they are not an external asset and Fitch does not include them in its reserve total. Moreover, their liquidity would be doubtful in a sovereign external crisis. There is also a question about the liquidity of gold holdings, since these cannot be sold without a constitutional amendment. However, they could be used as collateral for foreign loans.

Lebanon's Foreign Currency Balance Sheet, 2007

(USDbn)	Liabilities	Assets	Net liabilities
Sovereign	**37.4**	**19.2**	**18.2**
Government FC debt	21.2		
Gross FX reserves		9.8	
Gold holdings		6.4	
Other FX assets		3.0	
Banks' FX reserve requirements	12.8		
Other BdL liabilities	3.4		
Banks	**56.1**	**59.5**	**-3.4**
External assets		20.7	
Reserve requirements in BdL		12.8	
Domestic FC lending		26.0	
Domestic FC deposits			
o/w resident	42.9		
non-resident	13.2		
Total (net)			

Source: Mof, BdL, Association of Banks in Lebanon and Fitch estimates

Of the government's USD21.2bn in FC debt at end 2007, USD13.2bn (62%) comprises market-issued eurobonds. A further USD4.1bn are concessional low-coupon, long-maturity bonds issued as eurobonds to donor governments and to BdL under the Paris II and Paris III conferences. The rest is mainly concessional multilateral and bilateral loans. Eurobond amortisation was quite light in 2007 at USD1.2bn. But although new issues were more than double this, only USD400m was issued to the market, the rest being taken up by BdL and bilateral donors. Market amortisation rises to USD2.1bn in 2008 but all issues have already matured. The next maturity is not until May 2009, giving the authorities considerable debt management flexibility.

Annex

Fiscal Accounts Summary

(% GDP)	2005	2006	2007	2008f	2009f	2010f
Revenue & grants	**22.8**	**21.3**	**23.5**	**24.2**	**24.2**	**24.2**
o/w VAT	5.2	4.9	5.4			
Expenditure & net lending	**31.9**	**35.5**	**34.6**	**35.6**	**35.2**	**35.9**
Interest	10.5	12.8	11.9	10.9	10.7	10.7
o/w foreign currency	6.2	6.4	6.5	6.0	5.8	5.7
Primary spending	21.4	22.7	22.7	24.7	24.5	25.1
Personnel	9.8	9.7	9.6			
Other current	9.4	10.6	10.8			
Capital spending	2.2	2.5	2.4			
o/w CDR[a] (externally financed)	0.5	0.9	0.9			
Primary balance (excl. interest)	**1.4**	**-1.4**	**0.7**	**-0.4**	**-0.2**	**-0.9**
Overall balance	**-9.1**	**-14.2**	**-11.1**	**-11.4**	**-10.9**	**-11.7**
Financing						
Local currency	5.6	8.9	7.5	7.6	7.5	8.5
Foreign currency	3.5	5.3	3.6	3.8	3.5	3.2
Public debt	**178.4**	**177.4**	**169.9**	**163.4**	**158.4**	**159.6**
Local currency	89.7	88.0	84.1	82.8	82.3	85.3
Foreign currency	88.8	89.3	85.8	80.5	76.2	74.3
o/w eurobonds	75.0	75.8	71.6	64.0	57.8	54.0
Public debt (% of M2)	78.0	75.9	70.3	65.5	62.3	61.6
Public debt (% of revenue)	783.0	831.8	724.2	673.9	653.5	659.7
Memo						
Balance excluding CDR[a] (official definition)	-8.6	-13.3	-10.3	-10.0	-9.6	-10.5
Interest (% of revenue)	46.0	59.9	50.6	45.2	44.1	44.4

[a] CDR — Council for Development and Reconstruction
Source: Ministry of finance, Fitch estimates and forecasts

Public-Sector Foreign-Currency Debt Service (Medium- and Long-Term Debt)

(USDm)	2005	2006	2007	2008f	2009f	2010f
Amortisation (all foreign currency)	**2,230**	**3,029**	**1,819**	**2,750**	**3,100**	**2,800**
Eurobonds	1,800	2,499	1,219	2,119	2,376	2,043
Other foreign-currency debt	430	530	600	631	725	757
Interest (all foreign currency)	**1,328**	**1,452**	**1,609**	**1,668**	**1,779**	**1,879**
Total foreign-currency debt service	**3,558**	**4,481**	**3,428**	**4,418**	**4,879**	**4,679**

Source: Ministry of Finance, IMF, Fitch

Balance of Payments

(USDm)	2005	2006	2007	2008f	2009f	2010f
Current account balance	**-2,748**	**-1,201**	**-2,045**	**-3,716**	**-5,430**	**-6,572**
% of GDP	-12.7	-5.3	-8.3	-13.4	-17.7	-20.0
% of CXR	-14.0	-5.4	-8.4	-13.6	-18.3	-20.6
Trade balance	**-6,587**	**-6,138**	**-7,849**	**-10,000**	**-11,725**	**-12,795**
Exports	2,652	3,207	4,077	5,504	6880	8,600
Change (%)	29.4	20.9	27.1	35.0	25.0	25.0
Imports	9,239	9,345	11,926	15,504	18,605	21,395
Change (%)	8.7	1.1	27.6	30.0	20.0	15.0
Services, net	**2,963**	**2,831**	**2,541**	**3,500**	**3,500**	**3,500**
Services, credit	10,858	11,565	12,527	14,500	15,000	15,500
Services, debit	7,895	8,734	9,986	11,000	11,500	12,000
Income, net	**-186**	**295**	**377**	**-216**	**-206**	**-277**
Income, credit	1,733	2,440	2,663	1,720	1,822	1,827
Income, debit	1,919	2,145	2,286	1,936	2,027	2,104
o/w: interest on public debt	696	457	529	545	546	579
Current transfers, net	**1,062**	**1,811**	**2,886**	**3,000**	**3,000**	**3,000**
Non-debt-creating flows, net	**3,954**	**3,017**	**3,786**	**4,600**	**3,600**	**3,600**
Direct investment, net	2,669	2,669	3,078	3,800	3,300	3,300
Portfolio equity investment, net	1,285	348	708	800	300	300
External borrowing, net	**-756**	**1,611**	**2,933**	**3,850**	**2,350**	**2,350**
Net lending abroad	**3,698**	**-1,646**	**1,053**	**2,000**	**1,000**	**1,000**
Net errors and omissions	**-3,718**	**-3,575**	**-6,905**	**-3,500**	**-2,000**	**-2,000**
Change in reserves (-=inc)	**-458**	**-250**	**588**	**-3,824**	**-110**	**1,032**
Memo						
Gross borrowing (incl. short-term)	15,743	17,842	19,283	22,004	23,608	24,524
Gross external financing requirement	5,369	4,596	4,244	6,901	9,035	9,908
Stock of international reserves, excl. gold	9,845	10,207	9,778	13,602	13,712	12,680

Source: IMF, MoF, Banque du Liban, Fitch estimates and forecasts

External Debt and Liquidity (Residency Basis)

(USDm)	2005	2006	2007	2008f	2009f	2010f
Gross external debt	**2,4042**	**25,088**	**27,536**	**30,486**	**31,936**	**33,386**
% of GDP	111.5	110.2	111.3	110.2	104.3	101.8
% of CXR	122.4	112.7	112.5	112.0	107.5	104.6
By maturity						
Medium- and long-term	11,206	10,937	12,567	12,832	13,097	13,362
Short -term	12,836	14,151	14,968	17,653	18,838	20,023
Total debt (%)	53.4	56.4	54.4	57.9	59.0	60.0
By debtor						
Public sector	9,395	9,886	10,100	10,300	10,500	10,700
o/w Eurobonds (held by non-residents)	5,055	4,035	4,015	4,015	4,015	4,015
non-res holdings of T-bills	950	591	205	205	205	205
Non-bank private sector	3,013	3,020	3,796	4,046	4,296	4,546
Banks	11,633	12,182	13,640	16,140	17,140	18,140
o/w non-resident deposits	9,466	9,351	n.a.	n.a.	n.a.	n.a.
Gross external assets[a]	**27,209**	**32,195**	**36,898**	**40,592**	**39,242**	**36,750**
International reserves, incl. gold	13,947	15,780	16,188	21,882	21,532	20,040
Deposit money banks' foreign assets	13,262	16,415	20,710	18,710	17,710	16,710
Net external debt	**-3,168**	**-7,108**	**-9,362**	**-10,107**	**-7,306**	**-3,364**
% of GDP	-14.7	-31.2	-37.8	-36.5	-23.9	-10.3
% of CXR	-16.1	-31.9	-38.2	-37.1	-24.6	-10.5
Debt service (principal & interest)	**3,817**	**4,579**	**3,496**	**4,133**	**4,643**	**4,451**
Debt service (% of CXR)	19.4	20.6	14.3	15.2	15.6	13.9
Interest service (% of CXR)	6.1	5.3	5.3	3.5	3.5	3.5
Liquidity ratio (%)	**151.6**	**156.2**	**182.4**	**193.2**	**182.1**	**168.5**
Excl. banks' foreign assets	75.0	80.1	89.4	84.7	98.1	92.5

[a] Non-bank private-sector external assets are not taken into account
Source: Banque du Liban, Ministry of Finance, BIS, IMF, Fitch estimates and forecasts