

Country Diagnostics for Lebanon

Lebanon's private sector development and investment activity is hampered by a number of political, institutional and macroeconomic challenges. These include a complex institutional, political and macro-economic environment; substantial infrastructure gaps, limited access to finance, deficiencies in unleashing Lebanon's innovation potential and important inequalities.

- **Political, institutional and macroeconomic challenges:** Lebanon's complex political system, reflecting its multi-confessional structure and long-standing regional tensions, complicate the implementation of much-needed reforms to promote investment and private sector development. Weaknesses in the rule of law and complex administrative procedures make it difficult for businesses to start, invest and close. Moreover, macroeconomic imbalances expose investors to substantial uncertainty. Fiscal and current account deficits are large and the public debt to GDP ratio is the third highest in the world. The banking sector is highly dependent on deposit inflows from the Lebanese diaspora and heavily exposed to the sovereign, which adds to uncertainty and systemic risks.
- **Infrastructure gaps:** Economic activity in Lebanon is undermined by poor infrastructure quality, notably in energy, transport, water and waste treatment and ICT. These infrastructure gaps reflect under-investment, limited technical capacity and have been aggravated by the large refugee population hosted by Lebanon. The government's Capital Investment Plan (CIP) aims at raising 3.2 per cent of GDP annually over the next decade to invest in physical infrastructure. For the CIP to be successful, it requires strong donor support and needs to be accompanied by far-reaching structural reforms, for instance in the power sector and to improve public investment management and infrastructure.
- **Access to Finance:** Lebanon has a large and sophisticated banking sector compared to regional peers. Nonetheless, access to finance remains problematic for many firms, notably for SMEs and enterprises outside the capital city. Banks' large holdings of sovereign debt, risks crowding out credit to the private sector. Moreover, stringent collateral requirements; the limited availability of credit information; and the small size of the non-bank financial sector represent important constraints to financial inclusion.

- **Innovation:** Innovation activity in Lebanon compares favourably to regional peers. Nonetheless, a substantial catch-up potential remains compared to more advanced economies. Innovation activity in Lebanon mainly suffers from regulatory deficiencies, costly brain drain and market failures. More efforts are needed to promote knowledge transfers and spending on education and R&D.
- **Social Inclusion:** Income inequalities are pronounced and were further aggravated by the Syrian refugee crisis. High unemployment, a high share of low-skilled workers and gender inequalities undermine economic and social inclusion. The limited availability of high quality jobs results in substantial brain drain entailing important costs in terms of forgone growth and innovation potentials. Substantial efforts are needed to address skill mismatches, reform the TVET system and address regional disparities and gender imbalances.

About the Country Diagnostics Project

This Country Diagnostics Report for Lebanon was jointly produced by the EBRD and EIB. The report aims at identifying the key challenges and opportunities in promoting private sector development and investment in Lebanon. This collaboration between the EBRD and EIB builds on the Country Diagnostic Working Group, which was created jointly by EBRD, IFC, WB, the Swedish International Development Cooperation Agency (SIDA) and the UK Department of International Development (DFID) in 2017. The Country Diagnostic Working Group helps IFIs and DFIs to share perspectives and experiences of preparing Country Diagnostics and develop cross-institutional collaboration where possible. The full report is forthcoming and will also be made available on the Country Diagnostics w