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Lebanon's Political-Economic Crisis: Ramifications for Israel

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The waves of protests in Lebanon in recent weeks and the country's political instability stem primarily from fundamental problems in the local economy, including the absence of reforms and the rampant corruption among the ruling elite and all government institutions. The downgrading of Lebanon's credit ratings, lower growth rates, and high unemployment have sent the Lebanese economy to its lowest point since the end of the civil war. These developments are highly problematic for the country's decision makers, including Hezbollah. Israel, for its part, is monitoring the developments, which inter alia could lead to a strengthening of Hezbollah.

The crisis rocking Lebanon in recent months stems in part from deep economic problems that have afflicted the country for many years. These are joined by new problems that have arisen over the past decade and exacerbated an economic crisis seen by many as the worst since the end of the civil war in 1990. The immediate trigger for the outbreak of the popular protest in October 2019 was a proposal to tax social media.

Lebanon's GDP was estimated at \$56 billion in 2018, with an average annual growth of 1 percent reported over the last three years. Despite early forecasts of higher growth in 2019, an International Monetary Fund report gave an updated and reduced forecast, and currently only 0.2 percent growth is expected. In recent years Lebanon's economy has depended on banking (40 percent of GDP), as well as agriculture, industry, and tourism, which according to the IMF is at its strongest since 2010. In 2019 Lebanon's debt-to-GDP ratio exceeded 150 percent and heralds a major crisis and swift downgrading in the country's credit rating, with serious harm both to banking and currency strength, as well as to the ability to secure loans for debt redemptions.

The two deep problems weighing on Lebanon's economy are inter-linked. The first is endemic corruption: the organization Transparency International ranks Lebanon 138 among 175 countries assessed. Corruption in Lebanon is manifested especially in nepotism and budget-inflation to line the pockets of those close to power. Thus, for example, in July 2017 public sector salaries rose by dozens of percentage points, while private sector salaries did not enjoy any increase. The only way to fund the higher

salaries and inflated budgets is through taxes on the population, which have ballooned in recent years and burdened the private sector.

The second problem is political instability, which is linked to Lebanon's community structure and greatly limits the Lebanese government's freedom of action and ability to implement reforms. The instability makes it hard for the government to meet the public's basic demands, including sanitation services and electricity supply. As a result, there is a burgeoning market in private generators, though even this phenomenon is arguably linked to corruption: politicians are aligned with the generator suppliers, and thus, in fact, profit from government inaction. Furthermore, the absence of reform in the political system has created a weak tax collection mechanism, such that Lebanon's tax revenues are at just 50 percent of their potential. The political instability and lack of reform ward off foreign investors from Lebanon, and over the last decades the country has dropped 40 places in the ease-of-doing-business ranking and is now ranked 143 in the world. External aid to Lebanon has dwindled in recent years, in part due to a reduction in remittances by Lebanese expatriates who in the past sent large sums of money to the motherland.

New difficulties have compounded these problems. The civil war in Syria has had a negative effect on Lebanon's economy. Since 2011 there has been a reduction in agricultural exports to Syria as well as other markets that must be reached via Syria, including Iraq and Jordan. Furthermore, the war generated a severe refugee problem. In recent years, approximately one million refugees from Syria sought refuge in Lebanon, and their presence is a strain on the economy. In addition, the American sanctions on Iran indirectly harm Lebanon. The "maximum pressure" policy pursued by the US administration against Iran has harmed the Iranian economy and prompted a decline in Iranian aid to Hezbollah, heightening the motivation on the part of the organization to increase revenues derived from the privileges of political power, which means a cost to the Lebanese taxpayers. Furthermore, the decline of the Iranian economy has caused a significant reduction in Lebanese exports to Iran over the last year. Beyond that, in the summer of 2019, as part of its policy against Iran, the US administration imposed direct sanctions on Lebanese terrorism figures and banks. The consequences of the sanctions compound those created by the cessation some years ago of investment by Saudi Arabia, which had enlisted to help Lebanon but now prefers not to invest there so long as key positions are filled by figures close to Iran.

The banking system and the status of the central bank, a pillar of the Lebanese economy for many years, have suffered an additional significant blow. Beyond the downgraded credit rating, the banking system currently faces a liquidity problem and the lack of cash deposits, and these have triggered caps on withdrawals and a significant reduction in the Lebanese lira's exchange rate on the open market – the first in many years. The current

wave of protests has also contributed to a loss of trust in the banking system, both in the international community and among the Lebanese public, as many bank branches closed for long periods and cash withdrawals were limited.

This cluster of longstanding and new problems has brought Lebanon to a precipice. The downgrading of Lebanon's credit rating over the last year stems from the consequences of these same economic problems: a reduction in growth, some 40 percent unemployment among young Lebanese, a decline in investment in the country, the world's third-highest debt-to-GDP ratio (152 percent), and a deficit of more than \$1 billion that is due to be paid in March 2020. It now appears that many fear an extreme scenario: failure by Lebanon to guarantee its debt payments and an announcement of insolvency. This scenario could well be a realistic possibility already in 2020, unless decision makers in Lebanon take bold steps to stem this derailment.

A technocrat government, elected on the basis of professionalism and expeditiousness, with members free of salient political allegiance or obligation, would likely help achieve stabilization and, with time, perhaps even improve Lebanon's economic situation. This could also temper sectarian tensions that, were they to escalate, could drag Lebanon into renewed civil war. Clearly, technocrat government-led developments on a positive vector would also be positive for Israel, which has for years been threatened by the possibility of Lebanon's destabilization, given that the attendant violence could spill over Lebanon's southern both (even if the recent months of domestic ferment in Lebanon have a patriotic rather than sectarian flavor).

Yet an attempt to install a technocrat government in Lebanon that would strive for economic and political reform would be paved with difficulties and highly difficult to implement. Political operatives who currently enjoy access to the country's resources and coffers would do everything in their power to make it fail. Such a struggle against reform and change to the political and economic system would be waged, first and foremost, by Hezbollah. A foreshadowing of this was provided by the Cedar Conference of April 2018, where the organization opposed terms set by French President Emmanuel Macron for granting Lebanon loans to pay off debts: sweeping economic reforms, transparent conduct, and the acceptance of international oversight.

In any event, the establishment up a technocrat government that would carry out required reforms and circumscribe Hezbollah is not realistic in the current Lebanese climate. The situation can thus be expected to deteriorate, with various political players vying for the levers of power and economic power nexuses, and perhaps even trying to take over banks, media companies, gas franchises, and more. In parallel, various players will attempt to enlist the support of actors with interests in the region – whether Russia or

China, which want to increase their regional clout, or France, which has a historical link to Lebanon – with the aim of addressing the debts that beset the country.

Israel has no interest in meddling in Lebanon's internal affairs and wields no means of influence there, except indirectly, should a broad conflict with Hezbollah erupt. The foreseeable future does not appear to hold any realistic opportunity for improved relations between Israel and Lebanon, even if only to advance a compromise regarding the dispute over economic waters, which could provide Lebanon with an important source of income. However, Lebanon's desperate need for extra aid may provide Israel with an opportunity to try to shape the terms of the aid, inter alia by demanding a reduction in Hezbollah's militarization and access to the public coffers.