

**Notre Dame University
Louaize – Lebanon**

**Faculty of Political Science, Public administration, & International
Affairs and Diplomacy**

Rafic Hariri: A controversial Lebanese Leader

The Rise and Fall of Rafic Hariri

(1944-2005)

M.A. Thesis in Public Administration

By

Marc-Antoine R. Zabbal

June, 2005

The Rise and Fall of Rafic Hariri

(1944-2005)

By

Marc-Antoine R. Zabbal

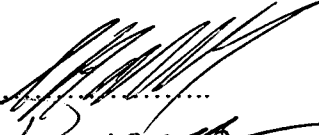
Submitted to the faculty of political science, Public administration, & International
Affairs and Diplomacy


In Partial Fulfillment of the Requirements for the Degree of Master of Arts Public
Administration

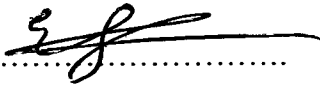
Notre Dame University

Louaize-Lebanon

June 6, 2005

Approved by: Advisor: Dr. Simon Haddad 

First Reader: Dr. Akl Keyrouz 

Second Reader: Dr. Edward Sayyah 

In memory of Leila and Carole, I dedicate this work.

Acknowledgment

I would like, first of all, to thank my Lord for granting me such kind and supportive parents, Rosario and Elhame, as well as my brother and my fiancé Cynthia, whose advice are always important.

I would like to thank my elder brother Dr. Simon Haddad for his support and help. I am also grateful to both of my academic advisors Dr. Akl Keyrouz and Dr. Edward Sayah.

Thank you, all for making my work as enjoyable as possible...

Marc-Antoine.

Table of contents

| | |
|---|-----------------|
| Abstract | 2 |
| | |
| Chapter one: the four theories of leadership: | 4 – 14 |
| Relevant Theoretical Considerations | 4 |
| Section 1 – Transformation leadership | 5 |
| Section 2 – Stogdill theory | 5 |
| Section 3 – E.A. lock theory | 7 - 9 |
| Section 4 – Emotional Intelligence..... | 9 - 14 |
| | |
| Chapter two: First mandate of Hariri (1992 – 1998) | 15 - 30 |
| Section 1 – Taïf Agreement..... | 15 – 16 |
| Section 2 – Reaching power | 16 – 17 |
| | |
| Chapter three: Second mandate of Hariri (2000 – 2003)..... | 31 - 46 |
| | |
| Chapter four: Last mandate of Hariri (2003 – 2004)..... | 47 - 62 |
| | |
| Conclusion | 63 - 65 |
| | |
| Annex 1: Paris I and Paris II agreements..... | 66 - 97 |
| | |
| Bibliography: | 98 - 104 |

Abstract

A name that will re-echo throughout Lebanese history, that of Rafic Hariri, a giant who gave his all to his country and sacrificed his very self at the end. His name is mentioned in every household and will be remembered by Lebanese.

Rafic Hariri came from a Sunnite family of living in the outskirts of Sidon, where he spent his childhood years. Later, he traveled to KSA and executed brilliant projects which rendered him a billionaire.

Backed up by his wealth and experience, Hariri chose to fulfill his youthful dreams of building up his country developing his country and finally gave his life for his ideal.

The most outstanding project Hariri implemented was the reconstruction of Beirut during the decade following the war. He actually earned his initial fame as the single most successful entrepreneur in Lebanon's recent history. Another interesting example that reflected his patriotic attitude was the efforts he made during the Taïf conference, in order to come to resolve the Lebanese conflict.

The negotiations involved considerable risk but resulted in ending 17 years of war with the conclusion of the Taïf Agreement. In fact he accomplished positive social, political and economic changes in Lebanon; despite many internal and external obstacles that he faced.

Now there is much discussion about the reconstruction process and Hariri's policies in addition to his quest for leadership and its bases.

Four relevant theories of leadership are listed and explained followed by a study to see of how they applied in the case of Hariri. Then the political history of the late Prime Minister is revived, starting with time when he was at the peak of his power and

continuing with the economic problems he faced till the last mandate, accompanied by an analysis of his leadership skills.

Chapter one

Relevant Theoretical Considerations:

Needless to say leadership has always been “the target” most public servants aim at; but the problem was constantly been the means and ways of achieving such status.

For many, trust comes as the first attribute needed for leadership; it signifies a psychological energy for the followers. In areas of tension and in the Third World countries, people tend to perceive “aggressive power” as a normal alternative to democracy. During the war, waged on its soil Lebanon provided as an excellent example of aggressive power and use of force. The latter constituted for a long time period the major factors of militia leaderships.

Democratic societies are possible only if trust binds both the government and the people so as to be effective. Trust can have an important influence on others’ visions and performances; hence, it can be considered as an expectation or belief which both sides can rely on, each by referring to their words, actions or assumptions.¹

The importance of trust was emphasized by Locke, whose main argument was that Governments are trusted by the people and respond likewise. This is based on the political process, whereby people award trust along with some of their freedom, accepting such limitations by laws, order taxes, etc...This is in return for security, prosperity and many other considerations.

¹ Cook and wall , journal of occupational psychology, 1980, P. 46

In his book “Trust as Commodity” (1988), Dasgupta defines trust as a product that is increased rather than depleted with frequent use. In this sense, trust would tend to be a complete process, a tradition, a variable depending on one’s actions carefully investing it towards positive ends resulting in a better state along with stability. The opposite of this process would eventually lead to distrust; by which most of the leaders lose their credit and popularity.

Transformational leadership

Transformational leadership² examines deeply the role that leaders play through the concept of trust in people’s life and future. This theory is verified when people are in need of a leader to reconstruct and reorganize their environment.

Once trust is acquired, the leader uses this effective means to increase the overall performance... The reorganization plan covers the daily tasks people perform to create a general economic policy for the country, taking into consideration the expectations of the followers and making them accordingly feasible. First, the leader must study the general situation to try to find a common ground for his followers. Studying the situation enables him to have a general idea of the overall state through an overlook on people’s needs. After their needs are understood, a plan is created that will eventually ameliorate the situation and assure a better quality of life. This process is measurable with the general outcome performance of the society in the near future.

Stogdill’s theory

On the other hand Stogdill’s theory (1948)³ investigates the general traits shaping a leader. His argument is that leaders are generally identified by their leadership traits

² E. Yulk , transformational leadership , journal of applied psychology (1992) P. 24

enabling them to assume more responsibilities; these traits are indispensable to the making of a leader who simply possesses what is called “the right stuff”.

“Capacity” is the second important attribute, one that involves the ability to think straight and in a focused manner. First, there are the intelligence and alertness factors which are usually and easily expressed in verbal mastery, second there is the capability to make a “just judgment” which is also necessary when seconded with “originality” that consists of a new model of thinking and inspiration for many. For this theory, a true Achievement walks hand in hand with capacity, it is the visible result people often see when considering a potential leader.

Knowledge is essential for achievements (information is power); for this matter scholarly and athletic accomplishments count in the general view of a leader, according to Stogdill, some of a person’s achievements can reflect his inner personality and qualities.

Status also plays a vital role in generating the leader’s image, involving his socioeconomic status, financial and personal history. This helps in creating a competitive popularity which serves as a measure of the likely success of a leader.

According to the theory, Responsibility demands dependability, initiative and self-confidence. These characteristics are translated into affirmative actions. In any given situation, a leader should have the initiative and self-confidence to resolve the problem. Such attributes, along with many others such as aggressiveness and persistence, ensure a certain degree of the confidence people always want to place in a leader.

³ R.M. Stogdill: Stogdill Handbook of leadership: A survey of the literature, new York, Free press, 1974 PP.127-138

Another factor making up the status frame is the participation trait, taking part in various social, political, and religious activities. The level of sociability and cooperation with different entities reflects a leader's ability to adapt to all parties.

E.A Locke theory

According to E.A Locke⁴, traits do not work alone; a leader must have other characteristics such as achievements, initiative ambition and energy.

Leadership motivation plays a vital role in the desire to influence and lead others.

Influencing people comes from the ability to affect others by defending a certain argument or exceeding the normal limit. It simply supposes above-average intelligence; the passion to gain power and the art of exercising influence on others⁵.

In this theory, E.A Lock introduces a series of virtues to the leadership style.

As for "Honesty and integrity", leadership is no more a solo action process or reaction; it is something to be looked at and admired. Honesty and integrity would ensure a transparent rule which eventually reflects the internal personality of a leader.

People often demand honesty since they simply need to know what "is really going on".

These two virtues help build-up a strong image of a leader.

Effective leaders are ones who are credible with an excellent reputation; as a conclusion, leaders are ideals.

The introduction of virtues into this theory conveys has many implications especially as the traditionally leader is represented as a "tough guy" with the ability to manage almost anything. E.A Lock re-introduced a modified traits theory with a more "human" touch that would eventually bring the leader more closely to people.

⁴ E.A Lock "do trait matters?", Academy of management executive,5,2 (1991)PP.48-60

⁵ Bennis and Bert, "trust in leadership and team performance", journal of psychology,85,6 (2001) PP. 1004-1012

Going back to the general traits of a leader, “cognitive ability” he discusses the ability of a leader to gather, integrates and interprets as much information as possible.

The modern and fast evolving world demands a highly modified leader who has the capability of know and interpret news and events differently in order to reach a positive outcome for his people.

“Charisma” plays a big part in this theory. Combining the previously mentioned traits and eliminating the charismatic (traditional) portrait does not work for a leader. A leader should be a sort of “ideal” to his followers.

Finally, this theory introduces two different types of dominance:

1. Personalized power motive.
2. Socialized power motive.⁶

1-Personalized power motive means that “a leader would seek power as an end in itself”. He works on possessing power as an end to dominate others in an irrational and wrongful way. Usually this type of leaders ends with the full or partial destruction of himself. In this case most leaders take power as their first and last resort. Their feelings of insecurity and the primary fear of losing power makes them unworthy of leadership.

Leaders of this category often base all their judgments and actions on a profound “self-doubt” situation. This is due to the emotional instability or “vicious circle” they often peace themselves in.

Unfortunately such leaders often attract dependent and submissive followers who do not have enough personality for initiative thinking, freedom of expression or even liberty of action. Socialized power motive is the contrary of personalized power motive; it is the use of power as a mean of achieving the desired goals.

⁶ David MC Callend: “socialized power motive”, Journal of applied psychology, 16.5(2001) PP. 98-102.

In this second model, leaders tend to listen to their followers, allowing them the opportunity to express their opinions and plans. Leaders belonging to this model are generally more transparent and work for the benefit of all.

This category illustrates how leaders play the mediator role, by which they encourage their followers to accept responsibility and express their opinions, which are really valued; followers of leaders of this category are empowered and independent in addition to being respectful and loyal to their leader.

Emotional intelligence

The fourth style of leadership is the theory of “emotional intelligence” which wins the leader into the hearts of his followers. This technique is mainly based on manipulating the followers’ emotions and getting them to fulfill the wishes of the leader. It can be ethnic, religious or in extreme cases racist. This also means the dual direction of influence - Implemented on both leader and followers.

Unless the leader follows a rational thinking along with emotional intelligence, this matter remains negative.

As a right measurement of any leadership style, emotional leadership is “the ability to perceive emotions, to access and generate them so as to assist thought, to understand emotions and their knowledge, and to reflectively regulate emotions so as to promote emotional and intellectual growth”⁷. The role of the emotional intelligence is the logical use of emotions to reach the target.

Usually people differ in knowledge and the use of their emotional intelligence.

Mainly, people search for leaders who are witty and use this character in favor of their political principals.

⁷ Mayer & Salovey, 1997: 5: “emotions”, academy of manager executive, 7.87(1989) P.53

This theory is specifically emphasized because of the social structure of the Arab culture in general and the Lebanese socio-cultural background in particular. Arab people tend in general to be more emotional and less rational; a fact well-known in our culture, religion and especially family and societal structure. In brief, emotional intelligence plays the most important role in any political figure.

The main criteria of emotional intelligence are the following:

The detection of emotions along with the right way of expressing them comes first. Not all people are aware of their emotions, and further not all of them are willing to express them. A leader always acknowledges his emotions and the perfect way of showing them.

This explains why certain leaders tend to raise the voices in an interview or make various gestures with their hands to attract attention. These techniques have one objective: to captivate and mobilize followers.

As a leader, emotional intelligence is not strictly being able to manage own feelings but also those of others. After identifying emotions and using them in a positive manner, thinking correctly and avoiding mistakes comes next.

So “emotional intelligence” means being able to excite and move people or even make them feel cautious. In other words, it is manipulating the thoughts and actions of others.

The theory of emotional intelligence and effective leadership identifies the right type of leaders who should possess:⁸

a-The and development of common objectives

b-the generation of knowledge

C-maintenance of “high steam” excitement and optimistic environment

⁸ J.M George : emotions and leadership: the role of emotional intelligent, Sage publications, LTD, Human relations, 2000,53.8 PP.1027-1055

d- The ability to fix a unified identity.

Emotional intelligence means being able to create a new foundation based on the power of intelligence to generate in others a certain level of awareness and comprehension, in this case, leaders start questioning themselves: on what common grounds do we really deal with followers? There is a clear fundamental fact which states that both leader and followers need each other and a mutual collaboration should take place.

The leaders aim to unify the followers with certain goals and objectives, mainly subjective, to change and develop the common environment. With reference to the four fundamental points that constitute emotional intelligence; leaders have to create a “collective sense” for their followers to share a common view and go in one direction. This technique means less time is wasted on identifying each ones view.

Leaders tend to create a “vision” for their plans based on their targets and achievements. Once they establish a collective sense of objectivity for their followers, realizing them is easier; this is based on the common thinking generated in the leader’s first construction model.

A- “A compelling” vision for an organization based on creativity, flexibility and positive thinking surely unites followers.

The three mentioned qualities are advantages if a leader possesses them. They differentiate him from others. Creativity is an extremely important attribute which leads to the rise or fall of leaders.

Furthermore, leaders should be flexible and tolerant of others’ mistakes, but not to the extent of weakness or just the opposite, being a tyrant.

Third, positive thinking is vital in many ways such as for raising the moral or giving self-esteem to followers. Applying flexibility through positive thinking creates a healthy working environment and moreover stability and continuity of the leader's path.

B-Sharing of knowledge or information: leaders must share information with their followers since the latter have the right to know. Leaders must make sure that their followers are aware of the problems facing the country. Wrong information wrecks leadership credibility and followers standard.

Another important point is giving the opportunity to followers to suggest solutions that the leader may explicitly present; encourages flexibility and positive thinking.

C- The maintenance of "high steam" excitement and optimistic environment assures the continuity of the idea and vision of the leader. Followers cannot achieve all their goals alone; they need someone to trigger some enthusiasm in them therefore, leaders should be motivators for their groups. The two important ensuring successes are cooperation and trust.

These two factors come in a "two way sense": from point A (leader) to point B (followers) and vice versa. Trust guarantees solidity for both sides, creating cooperation, leading to hard work and positive results for both.

The fourth and last point is the creation of a unified identity, leaders create shared models of values, adding their own to those of their society and environment.

The importance of moral values in every society is the main reason behind the previously-mentioned issue, based on this fundamental concept, leaders elaborate more on the target they hope in achieving. The concern of any leader remains completing his plans to success, therefore he raises moral quests to provide strong backup.

There are many expressions appealing to moral values for political ends such as “war on terror”⁹, “war against evil”¹⁰ and many more combinations which definitely assist any leader to obtain what he wants. That’s mainly from a leader’s point of view.

Sharing a meaningful common value facilitates collaboration and creates a collective sense of common goals. The creation of an identity creates solidarity and loyalty among members of the same group, sect and nation.

The present analysis suggests that emotional intelligence is worthy of consideration in the leadership domain. Emotional intelligence and the two other theories have the potential to contribute to effective leadership in multiple ways.

The special relevance to leadership revolves around the fact that it is an “emotion-laden” process; both from a leader and a follower perspective. Clearly, what is needed now is an empirical research in order to test the three theories more efficiently.

Given the complexity of the issues, both qualitative and quantitative methods give the most promising results.

Additionally, it would be interesting to explore how interaction between leaders and followers results in creating a new style of management in a setting.

Through a detailed plan, this knowledge will be used to explain the Lebanese former Prime Minister Rafiq Hariri on both the political and economical levels. The latter lead to the reconstruction process in Lebanon and created out of Hariri a strong “unbreakable” political leader.

⁹President Bush addressing the nation in the memory of victims of the 9/11,new York, 2002 : www.9-11commission.gov

¹⁰President Bush addressing the nation in the memory of victims of the 9/11,new York, 2002 : www.9-11commission.gov

All in all, investigating how this leader's capabilities in the emotion domain, traits or cognitive ability, contributes in the effectiveness which seems worthy of future empirical research.

Chapter TWO

In this chapter we examine the achievements of Rafiq Hariri during the first tenure as Prime Minister (1992 till 1998). This era earned him his reputation as a Tycoon¹¹ after he led the country on both the economic and political levels.

The various theories of leadership cited earlier in chapter one are used as an instrument to measure the great leadership capabilities of Prime Minister Hariri during that period.

“Short nights, long days starting with a power breakfast”

The Financial Times.¹²

Hariri not only was in attendance throughout the Taif Agreement in 1989, but also played a major role in organizing the general preparations, allowing it to take place. The fact that he could not assume power in 1990 did not stop him from extensively breaking into the Lebanese economic arena. In 1991 he established and managed Solidere¹³ - the foremost company of the reconstruction of the center of Beirut.

Two years prior to becoming a Prime Minister, Hariri had already begun implementing his concrete plans for the new millennium. It was in 1991 and during the first mandate of Omar Karami that Hariri had signed up the Solidere project, creating his private company as a legal module for reconstruction.

Hariri's plan was to privatize the center of the capital of Lebanon in order to transform it into a modern metropolis worthy of its former reputation in the region. As both leader and businessman, Hariri knew that the only way to recover from the ravages of the past

¹¹ An Nahar, Beirut, 19/6/1994.

¹² The Financial Times, March 22nd 1993

¹³ "Solidere": a private company owned by Prime Minister Hariri whose task was the investment and reconstruction process in downtown Beirut.

war and its notorious merchants was through a quick revival: the new plan was to restructure a healthy society based on a powerful market economy that would provide new work opportunities and assurance for foreign investment.

Solidere was created in 1991, but the project had to remain pending until October 22nd of 1992, when Hariri finally took over as PM, to be fully launched and executed.

Hariri's first task was to put Solidere and his restructuring plan on track, which would be the concept of his national economy plan.

The scope of Hariri's infrastructure projects was defined as follows: "By employing various agencies, the government of Lebanon has focused on two main areas of post-war transportation improvements a major, systemic project of road repairs and the design and completion of several hundred kilometers of new roads and highways."¹⁴

The most important elements of the reconstruction plan were:

- A new road network within Beirut central district that covered an area of 4.4 million square meters.
- A new three-lane express highway at the Ouzai road south Beirut, which is eight kilometers long.
- The establishment of a road system in northern Beirut which would include 25 kilometers of urban motor ways, 12 major interchanges and 10 overpasses.

Three airports, modern ports, an international road and rail networks and numerous free-zone areas for industry and trade were part of Hariri's international reconstruction objective. The plan for the complete reconstruction of Lebanon during the first years of Hariri's sentence culminated in the Horizon 2000 plan, an ambitious development

¹⁴ Hariri's official site: www.rHariri.com/economicplans.

scenario that would eventually lead to the recognition of Lebanon as the center of regional business, especially in the Middle East.

With a "total of USD 34 billion invested, half of that amount was to come from the public, half from the private sector."¹⁵

The aim of the plan was the recreation of the center of Beirut, a task already given in 1991 to Solidere. In parallel with this massive project, two other urban construction plans were to take place:

The first project was LINORD, the construction and creation of a business, touristy and residential development in the northwestern Christian section of the metropolitan area.

The other project, ELISSAR, foresaw the creation of a whole district of affordable accommodation between the refurbished and expanded *Cité Sportive* and the airport.

The above-mentioned was only the start of the development journey. Hariri could handle everything, the economic plan, the contacts, the strategies, etc. His stature grew to colossal proportions. He was heralded as Lebanon's "savior" – "the phoenix rising out of its ashes". People still recall when he first appeared in 1992 on *Télé Liban*; they all gathered near the television waiting for "this myth to speak out".

Hariri's financial state was the primary strength of his success along with many other factors.

In 1992, Lebanon's potential growth was undermined by a stagnating legal and regulatory system that was issued back in 1974 and restrained any restructuring plan under a complexity of laws and regulations; in other words, red tape bureaucracy. In response to that, Hariri created a legal independent entity called the CDR (Council of

¹⁵ The Executive "An overlook on Hariri's economic plan", Beirut, issue 1236, March 2004

Development and Reconstruction) whose task was to supervise and execute reconstruction projects all over Lebanon.

The CDR was accountable only to the prime minister himself and had separate budget and constructive working plans. With a fiscal budget reaching four billion dollars, the CDR financial process relied on both an internal monetary support (the state annual fiscal budget) and an external one (grants and donations from Arabic and foreign states).

According to Hariri, such a step ensured quick action and less time consumption as in any developed state, a necessity for Lebanon after 25 years of war.

The two institutions (CDR and Solidere) were the “weapons” of the direct intervention of Hariri into the reconstruction course. Another important innovation Hariri came up with was the new Ministry of Displaced. One of the many problems Hariri faced during his first term in power was the problem of the Displaced which blocked the reconstruction process; that most of these Displaced were located in Beirut suburbs where most of Hariri's plans were laid. Hariri saw his plans for the central business district grow to fruition in the first three years. He believed obviously in what he had to sell, making great efforts to mobilize funds from local shareholders and international investors to the extent that he was ready to personally invest in his projects.

Once the BCD started to make a profit, Hariri “sometimes dipped into his private funds to speed up the work program.”

His company paid about \$2.5 to \$3 billion for the master plan for the redevelopment of downtown Beirut, which aspired to remold the city into the Paris of the Middle East”¹⁶

The result which occurred by late 1997 made it hard for any returning emigrant to recognize the new Beirut. The latter progressed vastly and can now be described as a

¹⁶ The Times issued on 22nd March 1993.

modern “eastern” Paris surprising than any other city that suffered from war. The question then rose: at what price? (This matter, including Solidere’s various critics, is discussed in the upcoming chapter).

Through this major economic breakthrough, Hariri was able to quell the doubts of many anxious Lebanese and showed them a quick recovery after the long years of civil strife. The significant issue would be the stability of the Lebanese pound (Lira). Two important factors were the key to resolving this situation:

- 1- the general monetary and financial policy set out by the government
- 2- the confidence people had in Hariri (both nationally and internationally)

Those two direct factors helped in stabilizing the monetary situation and creating a suitable environment for investment.

That was the first step among many. Besides the Beirut central periphery, roads and infrastructure, the government completed three main projects between autumn 1997 and summer 1998. They were the landmarks of the new reconstruction process in Lebanon: the Camille Chamoun sports stadium, Beirut International Airport and the Grand Serail.¹⁷ Restoring The Camille Chamoun Stadium cost over USD 100 million dollars. It hosted the 2000 Asian Games as well as Pan Arab sports events. (Other stadiums were built or were in the process of reconstruction but none had the same prominence.)

Beirut International Airport was the major welcoming point of the city and its heralded reconstruction was greatly welcomed. That was as far as the economic level went, but there is an important observation to be made about Hariri’s personality. There was an immense power which he possessed along with the obscure mixing of personal, public,

¹⁷ An Nahar, Beirut July 12, 2000

business, political and his peculiar role as entrepreneur/premier, which was controversial from the very start.

His personal riches were invested in his private companies, costing him USD2.5-3 billion dollars. Many saw this as the fruit of his passion but presumed that he would have to pay a high price on the political level. He was accused of being a politico-economic tycoon and there were fears that he would sweep the whole Lebanese dynamic. The facts were completely different when he went into politics.

During the first six years of his mandate, Hariri headed three different cabinets.

What was the unique proposition that Hariri offered that was not available in Lebanon?

What makes his name to stand out among others as one of Lebanon's greatest

Leaders during the most difficult times? Is it true that everyone admired him yet tried to stop him?

It was obvious that the first six years of Hariri's term did not face much opposition; on the contrary, he had received international and local support. 28th October, 1992 was the beginning of a new era in Lebanon. The civil war officially ended on 13th October, 1990 after a brutal Syrian assault on Baabda Palace. The prime minister at the time, of the interim government, General Michel Aoun¹⁸, whose person was perceived as "rebellious", had to go away and the post war epoch began.

Omar Karami became prime minister for the first two years when Lebanon had a weak government with very little support and recognition. The future was recklessly unknown.

Omar Karami resigned from office paving the way for Mr. Rafiq Hariri who got appointed in 1992. Born in Sidon, Lebanon 1944, Rafik El Hariri studied at the

¹⁸ Former army commander and prime minister for what was called "transitional period" back in 1988, Aoun's official task was to ensure happen a free election and to pass on the government and the executive power to the newly elected parliament.

elementary school of Sidon and pursued his studies at the Arab university of Beirut majoring in commerce. He then moved to Saudi Arabia in 1965 in search for a better life where he taught in a school and worked as a part time accountant before opening his entrepreneur company.

After establishing his private company, Hariri was able to impress the royal family by building a hotel in Taïf in six months and broke the record. This project permitted a new tight business relation with the royal family before moving into bi-political concerns.

Hariri already had previous political experiences starting by establishing a welfare social institute in 1979 under the name “Hariri Foundation”, whose task was mainly to help and educate the less fortunate (33000 students graduated with the help of this foundation). In 1982 after the Israeli invasion on Lebanon, Hariri’s private company “OGER” became actively involved in the elimination of demolished buildings and opening of streets and roads which were littered with roadblocks and sand bags.

It was in 1984 that Mr. Hariri got engaged for the first time in the Lebanese internal political scene, during the Geneva and Lausanne conference. He attempted (on behalf of the KSA) to bring about inner reconciliation in Lebanon and terminate the civil war. Despite all the efforts made, war proceeded for another six years. It was in 1989 when Hariri (and again on behalf of KSA) stood out as the “power behind the Taïf agreement¹⁹; which succeeded in ending the war and drafting a new constitution for Lebanon.

Once in power, Hariri did not benefit from the many international factors which played positive roles in backing up his fresh start:

¹⁹ The Taïf agreement : signed by deputies representing various confessions in Lebanon in 1989, the Taïf agreement was mainly invented to try to put an end to Lebanon's devastating civil war

1- The Taïf Agreement, a new Lebanese constitution signed in 1989 and agreed upon by different Lebanese parties, concluded the civil war and declared several new principles; the most important two were:

First: Equality for Christians and Muslims in terms of political representation (before 1989, Muslims had 5 seats for every six Christian ones). The new agreement offered security for the Muslims in terms of political identification and further complete equality. Rafic Hariri was perceived by many Lebanese Muslims as a savior who gave them back their political rights.

Second: The executive power, which was earlier invested in the President of the Republic, was now to be handled by a body of ministers, or in other words the prime minister.

Working closely with the Saudi royal family for over 15 years, Hariri was able to gain Arab support (especially Saudi, which helped to promote Lebanon's credibility. This was after the monetary situation was stabilized and new investors gained who eventually helped him in rebuilding the country literally from ashes. It was the realization of Hariri's dream.

With national and international support, Hariri's first six years in power were sufficient to position him as leader of the reconstruction process in Lebanon and one of the founders of the "the New Lebanon".²⁰ With this kind of geo-political support during the first six year of his tenure, Hariri's power confirmed him as founder of the New Lebanese era.

Hariri was able to create a certain pact called the Troika based on the three main confessions in Lebanon – himself, the President of the Republic Elias el-Hrawi (a Christian) and the speaker of the parliament Nabih Berry (a shiite Muslim) -.

²⁰ Al Moustakbal, Beirut in a special document published in October 15, 2000

Hariri's political and international influence allowed him to plan and lead this Troika and enabled to achieve his political ambition: "creating a strong, centralized Sunni leadership"²¹ (something which historically did not exist in Lebanon); that was along with primary economic plan which is highlighted previously in this chapter.

With the help of considerable number of consultants, Hariri managed in those six years to create a "political frame" which no Sunni individual had ever achieved. He secured himself with the "Troika" measures, which allowed him easy access to everything and the application of any political tactic that would eventually succeed. This point of intelligent management is clearly visible in the "resignation process" which Hariri employed successfully; such as the case in 1994.

Similar unexpected attempts caused some negative impacts, such as the government treasury bonds withdrawn by one third in the BDL²² assets (Banque du Liban). This froze many construction plans and further proved that Hariri was indispensable for the rebuilding process.

Needless to say, additional factors gave Hariri the legitimacy at the time, such the Syrian intervention, which strengthened and encouraged his political presence. He greatly influenced their "brotherhood" treaty with Lebanon.

The mentioned reasons revealed Rafiq Hariri as the "invincible man" in Lebanese internal politics especially that everything in Lebanon during those six years was divided into three "non-equal" parts.

²¹ Deputy Mohammad KABANI in a special interview on Future T.V , Sunday 21st May, 2005

²² Banque du Liban: the official bank of the state.

After reaching the high point of his political journey, Hariri made a certain mistake or rather a false assumption during an interview in February 1993²³; PM Hariri outlined some parameters for negotiations with Israel: "Lebanon is willing to sign any agreement with Israel, short of a peace treaty, based on the United Nations Security Council Resolution 425."²⁴ During a talk show on LBC with Marcel Ghanem in 1996, he showed his reliance on the peace process in the region as an automatic certainty.

It was very clear that Hariri aimed to impose the reconstruction plan as the primary task of Lebanon after the peace process in the region. Another aim of Hariri put was to repatriate the Palestinian refugees (their number reached up to 400,000)²⁵ a move that would have an immediate positive impact on the local economy.

He also saw peace as eliminating the guerrilla campaign of Hizbollah, the Lebanese Resistance in south Lebanon, after the full Israeli withdrawal. That was in addition to the redevelopment of the southern area and the return of its dispossessed. This would have brought prosperity and stability to Lebanon. Hariri further assumed that Syria would have no role to play after the withdrawal of the Israeli army and the end of their strikes.

The political platform of Hariri may be summarized thus;

1. Lebanon would become sovereign and free from any direct military occupation
2. The state would control all Lebanese territory
3. There would be no militia presence after the Israeli retreat
4. The Taïf agreement was to be fully implemented.

²³ Simon Haddad, *the Palestinian's impasse in Lebanon*, Sussex, Portland, 2003, P.16

²⁴ The resolution 425: calls for an immediate withdraw of Israeli forces from Lebanon.

²⁵ Simon Haddad, *the Palestinian's impasse in Lebanon*, Sussex Portland, 2003, P.44

5. The question of Palestinians refugees would have to be resolved (this issue was very controversial since their presence created an unwelcome demographic imbalance for the Christians and the Shiites)

On the economic platform there were many advantages:

1. Stability would lead to prosperity meaning more revenues for Lebanon
2. Ending the military and financial support to parties fighting against Israel would help in reducing costs.
3. As Lebanon has always depended on tourism as a main resource income; the more stability it possesses the more tourists will come and further increase revenues.

Despite above the mentioned forecasts, the situation remains vague until this day as Prime Minister Hariri's plans for a quick peace were frustrated. Hizbollah remains armed and active at the borders despite Israeli's withdrawal and the Palestinians linger in the camps to the number of 300,000.

After the year 1996, Hariri began to face criticism Peace was not finally achieved in 1996 which created a situation of spiraling debt in Lebanon. Hariri's opponents were questioning the intelligence of his policies, especially the extensive level of corruption that was increasing during the final stage of his mandate. These factors are examined in the next chapter.

If one relates the peak phase to the theory body of leadership discussed in chapter one, some relevant information can be found about the leadership skills and qualities that Hariri possessed.

The first theory is simply that there is a need for trust, an important feature that would facilitate the type of "Transformational Leadership" which the post-war period required.

The mechanism and reputation that identified Hariri greatly helped in affirming his position and persona as leader and “savior” during that period. Nevertheless, regardless of his “perfect economic plan” and business achievements, Hariri would always be known as the man who fostered the Taif Agreement and the end of the civil war.

Many factors shaped the above-mentioned trust which was created before Hariri’s nomination. This trust was molded by an efficient monetary policy, a stable Lebanese pound and above all (and perhaps the most relevant) the erasure of all visible aspects that had to do with the war. Literally, Beirut underwent a surgical process, a face-lift.

The reconstruction plans offers new job opportunities which revived the building sector with an overall 26% of Lebanon’s GDP.²⁶ At this stage we can easily apply the “Transformational Leadership” theory to Hariri’s performance.

If one considers the “Stogdill’s theory”, numerous resemblances can be found especially that it investigates the general characters leaders possess. In other words, it means having “the right stuff” from public image to social belonging, to the ability to make right and fair judgments, to the participation trait, till to the affirmative action, all the way to achievement and the power of focus. The portrait or figure of Prime Minister Hariri conveys “a calm yet dynamic person, a man full of confidence and a light smile.”²⁷

As for social belongingness, Hariri “is a philanthropist, a self-made man who built his business single-handedly on the basis of his reputation...”²⁸ It is well-known that Hariri is from Sidon and a middle-level family that he traveled to KSA where he became a successful billionaire and then returned to Lebanon as an investor who served his society

²⁶ The Executive Gazette Number 4113 published on April 25th 1995

²⁷ CNN special edition Christmas 2000/inside Asia, 2000.

²⁸ Hariri official site: rHariri.com/biography

well through his association (The Hariri Foundation). This is all reflected in his public image

During his six-year term, Hariri relied on advisors, specialists and his own intuition in order to make the right decision. Hariri brought the country to a new era of high development status through major reconstruction plan for the country.

On the internal political front, general conditions and foreign interventions were the main obstacles to this radical change.

This political tactic served as an example of Hariri's correct affirmative action: Having created his electoral base in the capital, Hariri won a seat as a Beirut Member of Parliament in the 1996 parliamentary elections, and consolidated one of the strongest political blocs in the following parliamentary period.

As for the appliance of the "cognitive ability" theory, it was specifically used during the period of Hariri's governance from 1992 till 1998 where he first based his work and actions on honesty and integrity the "ingredients" of the cognitive theory. "The most important thing is honesty and loyalty. The intelligent man is honest; it is the liar who is the dumb one. You can lie to people some of the time but not all of the time, but you can tell the truth to all the people all the time"²⁹

The other aspect of this theory would be the ability to influence and then implement the social power motive thus, maintaining the same level of power and public respect.

Hariri acquired several methods of control. One can clearly cite the social work of his foundation and the help he brought to the less fortunate.

Other key factors were his appearance as a media personality and his ability to communicate a new vision, and further attract people to his sphere by that personal vision

²⁹ Prime Minister Hariri during a special report of BBC, June 2002.

for the future. As for the mechanism of organizing his teamwork on the simple concept of social power motives, the Prime Minister was actively involved in talk shows and student debates to propagate and persuade. I was personally involved in one of these sessions at the American University of Beirut.

In the next chapter, there will be more details about the prime minister's tendency to always take counseling from his advisors, which mainly led to his resignation in 1998.

According to the latest leadership studies, emotional intelligence is the main concern for any leader to influence more effectively. This will be the last theory in this study; as emotional intelligence is "the capability to manage the moods and emotions of others."

This theory holds true, especially in our Mediterranean society where emotions and moods play a major role in the effectiveness and functionality of daily life. Hariri was aware of this fact and was abiding by it:

- One: the creation and development of common objectives. His common objectives were widely approved by both his followers and friends from one side, and his opponents from the other.

By carefully choosing those objectives and ranking these choices as "public good", Hariri created a situation where he would be untouchable on any moral basis (creating a safe and prosperous political environment to guarantee institutional reorganization including the stabilization of the currency, etc); any opposition to this program would be opposition to the "public good".

His speeches used to carry phrases such as: "Who could stand in the face of modernization" and "We all have to work for a better Lebanon"³⁰

³⁰ Hariri's speech during the opening of the regular meeting of Lebanese council, October 1994)

- Two: the knowledge generation: Hariri had no truth-telling problem during his first term. For one thing, he was the sole reorganizer, holding significant information on the monetary status for example. Being given this “green light” from regional and international supporters, he had no relevant obstacles or problems to face with his followers or critics. It was in the next period that the concealment begins.

Three: the point was characterized quite famously by Rafik el Hariri himself. His high-maintenance stand and constantly optimistic mood, despite any problem, were shown in his now famous statement “El balad machi wala y himak!” (The country is doing fine, there’s nothing to worry about!). This saying was even humorously turned into a song broadcast by many television networks.

Hariri knew the complications facing every facet of the Lebanese society and mostly was aware of his growing status and perceptions. For many he was a “saving grace” in the first six years of his term. His self-confidence was quite obvious in his plans and actions which he announced at various dinners and social events. It never waned even in the most difficult years in office, all through to 1997 and eventually the final political collapse in 2004.

The creation of a “unified identity” was Hariri’s main objective all the way until 1998: uniting the people under one flag, one nation. Things, however, did not work out as planned; for many reasons, the sectarian identity in social life remained greater and more influential than that of a national identity with no defined terms.

These would be the factors which influenced his strategy for the 2000 elections (chapter 3).Hariri's leadership skills appear in these four main theories; but like any other man, this leader was not perfect or faultless.

In the upcoming chapter the second part of Hariri's governance in Lebanon is discussed, studying all its facets and factors including the reasons for his brief retreat from the political scene prior to his reappearance and applying the same methods and theories. It would be an experiment to test if this leader can ultimately control the situation and flip issues into his benefits. On the other hand, the situation, circumstances and environment may be the determining factors of the rise and fall of a political powerhouse.

Chapter THREE

This chapter provides more information about the second half of Hariri's political era in Lebanon in addition to direct examples about his strategy within government as well as in oppositional. Furthermore this chapter includes, the various leadership theories will have been reexamined and implemented relative to Hariri's political plan and frame of action; it will assess his success as a leader.

In 1998 after the election of President Emile Lahoud as a result of a Syrian initiative and pressure, Hariri retired shortly from the political scene. Many agreed that this step caused a significant loss of political rank and influence, rendering the former Prime Minister an important, yet not exclusive, leader in the parliamentary opposition.

Observers remark that this was the first the head of the opposition, a title he always rejected. In return, the Lebanese and Syrian secret services began to generate a "counter-opposition" to the movement of Hairi and his ministerial allies, legitimizing it under the banner of ending Hariri's "corruption and misuse of power" .

However, in fact this was a war against a policy, an economic plan and a person.

Salim El Hoss took over the post of Prime Minister after Hariri's resignation in 1998. He led the cabinet for two years, waging an "anti-corruption" campaign, starting with a judicial hearing and imprisonment of Fouad El Senyora, Hariri's former Minister of Finance.

In order to reduce the public debt, Hoss applied his general economic guideline based on a conservative economic plan, calling major construction plans to a sudden end. He halted the Beirut International Airport project and a new road in northern Kesrouan and Metn, and delayed many other fundamental plans. Hoss also cut down the annual budgets

of various ministries, except for the Ministry of the Displaced. Reducing the budget have been considered a dangerous political move since it concerned the right of return of many families to their villages and the reconciliation of former factions in the civil war. It also would have negatively affected the application of a major clause in the Taïf Accord.

The budget for the CDR and the Council for the Redevelopment of the South was also cut down. As mentioned earlier, the CDR was responsible for major reconstruction facilities while the Council for the Redevelopment of the South presented both monetary and logistical assistance to an area that was still under Israeli occupation.

Hoss' plan to "cut down expenditure" had an adverse effect on the economy; the reduction, delay and cancellations of many projects caused a lack of investor assurance and further a recession due to a lack of cash flow.

While it may be true that Hoss' plan stabilized the national debt situation, it also created a scenario of withdrawal in the Lebanese economy as no progress was made to increase governmental revenues. It was clear at that point that Hariri had succeeded in terms of economic strategies, since this era required a man who was not "timid" in his actions towards growth and countering recession. That man would instill both investor and consumer confidence and widen the avenue to a futurist Lebanese development. Apparently, Hoss was not of that kind.

As mentioned earlier, Hoss's campaign against Prime Minister Hariri was carried in by two means: economic and political.

Politically, Hariri was under pressure mainly from:

- 1st- President Lahoud.
- 2nd- A joint Lebanese-Syrian Secret Service campaign.

3rd- Hoss's cabinet.

The three fronts "opened fire on Hariri" due to "his immense wealth, strong ties to the international business community and connections to the Saudi royal family"³¹, a combination that posed a real and vital threat to Syria and its allies' and their dominion in Lebanon. At the political level, Hariri's former ministers presented themselves to justice without formal accusation, it was a fiasco.

One more assault on Hariri's political position emerged via the media.

On that front, the official state television, Télé Liban, was used to destroy Hariri's political platform through a series critical reports and false rumors. For example the station imported to present proof that Hariri caused an increase in the national debt which would be later negated by the nationalization of Palestinian refugees, thus serving the interest of the American/Israeli agenda.

It was another unsuccessful attempt by the government; on the other hand, the Sunni population grew anxious at this wave of attacks on their most promising Sunni leader and quickly creased their support to him.

This reaction surprised the tripartite attackers of Hariri, whose efforts obviously had a reverse effect. The final straw came with the 2000 Electoral Law, which was tailored by the Syrian/Lebanese intelligence apparatus, splitting Beirut into three different electoral districts and dwarfing Hariri's concentrated electoral power.

Along these various pronged attacks; Hariri made a glaring comeback depending on the following: his opposition to the two year term of Hoss, the people's weary response to the government's reform initiatives and its largely inactive cabinet.

³¹ Middle East Intelligent Bulletin, Vol4. No.9 (September 2002) p.1

As a result of the bad economic condition along with the over-pushed aggressive policy against Hariri in autumn 2000, the electorate granted an absolute victory to Prime Minister Hariri and his list of candidates gaining all seats in the Beirut electoral district.

Additionally, Hariri stood out strongly in Tripoli, gaining half the parliamentary seats while his sister Bahia won the southern parliamentary seat in Sidon.

This triumph enabled Hariri to enter the parliament with one of the largest support; therefore, President Lahoud renamed him as Prime Minister for a fourth term.

Another factor contributing in his return was a Syrian decision to quell the popular tensions created after the unsuccessful economic policy of Selim El Hoss. The Syrians accepted to deal with Hariri for a short period.

“The people gave their final vote: the winner, Hariri”³² with this huge of public support Prime Minister Hariri formed his fourth cabinet, with new individuals and only a few “old-Guard” political affiliates (that he was always forced to include in order to appease regional powers). Regaining his position as Prime Minister, Hariri had a new task was divided into two main objectives:

- 1- The continuity of the reconstruction plan
- 2- The resolution of the public debt, which exceeded \$30 billion.

Once he came back, Hariri directly began managing all the reconstruction projects in order to respect contracted deadlines and regenerate of the economy. Most of these projects were ready to be used directly after completion, such as the athletic stadiums with the hosting of the 2000 Asian Cup in addition to the hotels and conference halls which welcomed several international diplomats during the “Sommet De La

³²Al Moustakbal , Beirut, October 24th ,2000

Francophonie”, the first summit to be held in Lebanon. These projects induced the reopening of the Beirut International Airport.

As mentioned earlier in Chapter 2, the construction sector holds an overall 26% of Lebanon’s GDP. During the term of Hoss this rate was down by 11%. By the year 2000, an increase of development projects, backed with foreign loans and long term credit facilities, was started.³³

Many negative points marked of Hoss’s mandate: a recession in growth, an increase in the unemployment rates, a lack of confidence in the economic future and sustainability, and reduction of investors, in addition to a huge public deficit and accumulation of the public debt. Hariri started working instantly on a recovery program that would ensure a sustainable growth level; Hariri based his proposal on three pillars in order to achieve his objective:

First: developing a new aspect for the Lebanese economic structure which would allow it to abide by the international global standards set by the WTO.

Second: the establishment of a clear and transparent “fiscal financial policy” in order to help boost economic growth as well as restructuring the sector and improve its productivity and self-sufficiency; in addition to privatizing a number of public facilities in order to reduce public debt and budget deficit.

Third: working on stabilizing the monetary system to avoid inflation and preserve a good exchange rate for the Lebanese currency (the Lira).Internally, Hariri would be able to improve the situation; yet he would destroy his relationship with the Syrians, who exercised all kinds of power and had a negative influence in Lebanon’s political and economic affairs tending to hinder any development.

³³ See Annex 1: Paris one meeting, pp.78-80

As a successful businessman, Hariri believed that only political stability would allow economic prosperity Lebanon's only hope.

After the Israeli withdrawal and the full implementation of U.N. Security Council 425 President Emile Lahoud and Hizbollah (following Syria's instructions) refused to acknowledge Israel's retreat as complete. The Shebba farms scenario was created wherein Lebanon claimed that a small strip of farm land was still under Israeli control thus still considered to be an "occupied territory". On the other hand, U.N. experts consider this area as Syrian. This Shebba issue was judged by the Resistance to justify their continued attacks against Israel. This matter jeopardized the economic growth plans and left Hariri's projects pending once again.

Hariri aimed to stop the Hizbollah operations on the Lebanese-Israeli front. This goal caused "President Bashar Assad angrily to cancel a scheduled meeting in Damascus and to refuse to speak with him for over month."³⁴

The political instability and the ongoing corruption at the institutional level caused a large deficiency in the economy. Hariri, "who had lot of friends, a lot of very powerful, wealthy friends in France, Saudi Arabia and the Gulf in particular,"³⁵ had to take appropriate measures to convince these states the need to invest. This provided the Lebanese government with a large funding for redevelopment and economic assistance, as these states were reminded of their responsibilities in the matter which were stated clearly in the Taïf agreement back in 1989.

A global meeting was to be held in Paris known as "Paris I". It was the first step towards a wider economic assistance to come in "Paris II".

³⁴Middle East Intelligence Bulletin, Vol.4 No. 9 (September 2002) p.1

³⁵Simon Williams, "Lebanon's economic Champion" for BBC news , (Monday, 14 February,2005), p.1

The international community holding the meeting demanded several guarantees from the Lebanese government and required their implementation for the following two reasons:

- 1- According to some specialists, it would have a direct “relief” impact on the Lebanese economy, enabling it to reduce inflation and start a positive growth process.
- 2- There was a series of demands that, once approved, would offer a great deal of reliability and trust for the international community and allow it to continue providing Lebanon with other sources of recovery assistance (to be implemented as recommended by Paris II summit).

The government was asked to adopt a total of 32 measures. A few were not fully implemented. Here is a list of the most important conditions:

- 1- For Télé Liban, the international community asked for the lay off of 500 employees to help relieve the channel’s debt. It always suffered from a lack of equipment and an inefficient role in the media sector.
- 2- Concerning customs tariff reduction, Lebanon was asked to reduce its rate from 12% till 6% (this step among others would guarantee the process of globalization and its entry in a world trade economy.)
- 3- The Lebanese state should provide tax breaks as well as creating investment zones to attract and raise the number of investments
- 4- New anti-corruption measures should be introduced to reduce money-laundering.
- 5- A new Value Added Tax should be introduced in order to increase tax revenue sales on all commercial items.
- 6- An open air policy should be adopted.
- 7- The Euro Med Agreement should be applied.

8- A suitable legal-commercial environment should be created that would facilitate Lebanon's entry to the WTO.

This all went along with other fundamental economic reforms such as privatization of the electric, telecommunication and water industries in Lebanon.

The direct implementation of almost all of the above-mentioned conditions allowed Lebanon to enjoy a slow but certain growth rate from 0 in 2000 to 1% in 2001 and 2002, all the way to 4% in 2003 and 2004.

These achievements paved the way for Paris II. To this very day, there is always a mention of Paris 2 in all economic or political debates reflecting its feasibility, impact, and obligations. It was definitely a controversial topic, for this conference always carried the potential for shifting and determining the economic and future development of Lebanon.

In November 2002, Rafiq Al Hariri met the representatives of the following countries: France, Lebanon, Germany, Saudi Arabia, Bahrain, Belgium, Canada, Denmark, United Arab Emirates, and Spain, the united state of America, Great Britain, Italy, Japan, Kuwait, Malaysia, Oman and Qatar. Then he represented himself to international financial institutions including: the International Monetary Fund, the World Bank, the E.U Commission, European Investment Bank, Saudi Development Fund, Kuwaiti Development Fund, Arab Development Fund and the Arab Monetary Fund.

In his introductory speech, Hariri briefly specified the terms and objectives of the meeting: the initial loans donated from the international community to Lebanon over the span of the 12 year post-war period of reconstruction had been quickly transformed into a spiraling debt that the small country would not be able to payback. These loans were

short-term and at high interest, an issue that required from Lebanon a quick recovery. The idea behind this conference would be to “swap” those existing loans with a more suitable and less aggressive way that would help Lebanon to reduce its debt by granting it longer-terms dates and lower interest rates.

After introducing the above-mentioned “swap” technique that, Hariri’s cabinet laid down three main objectives:

- 1- Fiscal adjustment that would lead to a reduction in public debt.
- 2- The privatization process
- 3- The external support process

Regarding the fiscal adjustment, Hariri knew that the only way to radically change the composition of the public debt was to set out a general plan that would prevent probable future losses in the Lebanese market.

This plan was to focus on reducing corruption through using a specific program which the Ministry of Public Reform would implement with the help of the Ministry of Finance. They would monitor and eliminate all kinds of misuse of the public money and all forms of corruption.

“The primary fiscal balance has improved by 10% points of GDP during 2001-2002”³⁶, with a target of 19% by year 2006. As for the privatization process, it was a plan to assure the world that Lebanon is on the right track to globalization and to implement certain rules and regulations in order to enter the WTO.

This process started back in 1995 with the privatization of the mobile telephone networks in Lebanon.

³⁶The Lebanese Republic official transcript on Paris 2 meeting, “Beyond reconstruction and recovery.... Towards sustainable growth”, a request for international support. p.90

Further steps were taken to ensure the success of Paris I. By late 2002 many local industries and facilities were privatized: the Zahrani power plant,³⁷ the national telephone network³⁸ and the national postal service.³⁹ Privatization would guarantee higher state revenue, better service and performance, and less corruption; through strict private employee monitoring.

In 2003, Lebanon was expecting a \$5 billion dollar loan from external support which would assist it in achieving a more reliable and sustainable growth.

This amount would allow the government “to borrow from supporting countries markets at low spread, using the proceeds solely to substitute such external loans for existing high interest short-term debt.”⁴⁰ This plan, according to government officials, would drastically reduce the total GDP growth that would affect the time period profile of the public debt.

In early 2003, Paris II turned out to be a success with the emergence of the \$5 billion dollar loan in the form of long term credits and low interest rates; as well as a plan for “swapping” old loans with for ones resulting in a positive 4% GDP growth in 2003.⁴¹

Hariri saw this as the only way to salvage a severely damaged economy taking into consideration the political conflict that started between himself and all the Syria loyalists such as President Lahoud and the Speaker of The House Nabih Berri.

The deteriorating relationship with the Syrian regime initiated many rumors about Hariri during that period. A particular incident created to damage his image was a Syrian

³⁷Privatized by “Uroum Co.” (Iranian company)

³⁸privatized by “OGERO Co” Lebanon

³⁹privatized by Liban post (Canadian post- Canada)

⁴⁰The Lebanese republic official transcript on Paris 2 meeting, “Beyond reconstruction and recovery.... Towards sustainable growth”, a request for international support. p.99

⁴¹The Lebanese Republic official transcript on Paris 2 meeting, “Beyond reconstruction and recovery.... Towards sustainable growth”, a request for international support. p.100

security measure to arrest 250 opposition activists while Hariri was out of the country. Hariri seemed genuinely surprised when the media asked him to comment, and claimed: "I had no idea about this development." It was an incident set up by the Syrian forces in conjunction with the Lebanese security apparatus to tarnish Hariri's image especially among the Christians.

Early September 2002, the Syrians started seriously considering a successor to Hariri who would be a powerful and wealthy ally, similar to Hariri. This person was the Saudi royal prince Al Walid Bin Talal.

Al Walid's mother was of Lebanese origin and the daughter of Lebanon's first post-independent Prime Minister. The prince is of Lebanese origin and well-connected in the international business milieu (thus possessing the required trust by the international community), and well "mediatized" as a potential Prime Minister. He was also a close friend of the President and willing to abide by the Syrian framework for Lebanon.

This political attempt was raised publicly during an interview in which Bin Talal was asked if he would consider the post of Lebanese Prime Minister. He replied: "We'll cross that bridge when we come to it."⁴² This new political deception provoked Hariri to reply: "We don't have time for that we have an economy to take care of"⁴³.

Along with all the political pressure and nearly personal assault, Hariri remained steadfast and determined, starting with the Paris 2 initiatives to go forward. Surprisingly, on the 15th of April 2003, Hariri submitted the government's resignation; the President immediately accepted it.

⁴²Middle East Intelligence Bulletin, Vol.4 No. 9 (September 2002) p.11

⁴³Special interview and meeting with AUB graduates, December 2002

After almost all the economic and political parts of Prime Minister Hariri's term are cited, they will be examined based on the four theories stated earlier in Chapter 1.

Unlike his first term when he enjoyed major local and international support, Hariri's second one faced vicious political and social challenges orchestrated by the Syrians, the media, the state and the public.

The first concept, once again, is "trust", a thing that Lock emphasizes as an essential ingredient in the creation of a bond between the leader and his followers. The theory of transformational leadership strongly relies on Lock's "trust" concept.

Hariri's reliance on the "trust" issue is widely proven. Going back to his resignation in 1998, a "cold war" started on his person in order to reduce the chances of his return.

With Lebanon suffering from a stagnation period, a plan was required to transform the condition into a new reform policy. The leadership value, highlighted previously, is very important in this regard. Hariri was intent on taking drastic measures to that degree through the application of the Paris I and II accords as a foundation in that process. One of his first actions was to negotiate for large reductions of import tariffs.

On the basis of on Stodgill's theory, Hariri's leadership traits would be defined by "consistency", meaning that Hariri would retain the same qualities he possessed during his early term as Prime Minister.

His achievements are the measure pole of any leader's power and legitimacy. By that standard, Hariri has no rival especially in the Sunni camp. His legacy in the economical and political domains allowed him to tower over others in such a remarkably short period of time. Hoss's failure over the last two years in the economic sphere caused weariness among voters. His era was marked by inaction and political disinterest.

This served as an additional reason for supporting the Hariri camp while also helping Hariri in reevaluating his leadership strategy.

It was clear that Hariri had the ability to adapt to different political situations by seriously analyzing past strategies and events to avoid the previous errors. Hariri's aim to reappear in the political scene is associated with another of Stodgill's theories, the "just judgment" character. Undoubtedly, Hariri had a share of political missteps and erroneous maneuvers, but his "just judgment" in presenting his resignation in 1998 was an overwhelming success. Accordingly, he was able to create a "popular" reaction among the Beirut Sunni. The community thought of his resignation as an attack on the power of the Sunni sect as a whole.

The proof of the success of this maneuver was Hariri's sweeping victory in the 2000 parliamentary elections. Hariri applied Stodgill's third principle, which is participation. Despite the fact of several resignations particularly in 1998 and 2003, Hariri's loyalty to serve his nation and people remained unaltered, "I highly value my friendly relationship with the Lebanese people for they are my only asset"⁴⁴.

Hariri's social activities during that period remained highly-profiled. He used to welcome guests and social movements from all sectarian backgrounds and assist them financially and morally; he used to invite people from struggling social classes in Ramadan for every night of the month while personally attending the dinners.

This was a constant strategy in keeping touch with his "only asset", the people.

The third theory of leadership is "cognitive leadership" which implies the method of "influencing" people, as a key to advance any political or economic program. This is

⁴⁴ A special interview with Marcel Ghanem from Kalam Al Nass (word of the people) , LBCI Co., June 5, 2003.

accompanied with honesty and integrity; trust issues that would allow any leader to launch or prolong his political position.

Hariri used several forms of influence during his resignation and comeback period

In 1991, one third of Hariri's personal money was moved to Lebanon. He used his wealth as a political power platform to directly influence people and correspond with important allies. At the personal level, many people were employed at Hariri's institutions; on the other hand and at the economic level, a web of limited investments was formed with local businesses and monetary institutions.

At the social/economic level, Hariri aided the less fortunate families of Beirut whose numbers had risen to 4000, beside his academic initiatives which helped over 33,000 students.

As for the "honesty and integrity" concept, Hariri was relentless in defending his social/political plan through various media. It was a contentious "defensive" propaganda campaign that vocalized his honest stance on all current economic issues.

The last point in this leadership theory was the method Hariri used to dominate over every move of his parliamentary team and cabinet members, all the way to his personal consultants, Hariri's attitude and working approaches illustrated how the socialized power motive was behind this successful man.

Hariri was always ready to engage in any debate with whoever wants to: academics, businessmen, students, or political movements. He was the leader who always had "something useful to say". The Prime Minister's one and only resolution to political or economic crisis "was and always will be dialogue".⁴⁵

⁴⁵ Middle East Intelligence Bulletin, Vol.4 No. 12 (October 2003) p.7

As mentioned earlier in the chapter, Hariri suddenly created a new cabinet of many unknowns: “fresh blood”; changing his “old guard”, after intense consultations.

This went along with Hariri’s formation of various political and social entities such as the “Future Youth Movement” and the “Hariri Foundation”. This allowed them total independence in internal elections and other private tasks.

Finally, the fourth and final theory, “emotional intelligence”, could be divided as follows: First: the creation and development of common objectives. The latter shifted mainly from reconstruction process plans to the reviving of the Lebanese economy.

Generally, objectives change to coincide with the shift of priorities; a matter that Hariri perfectly was aware of. Citizens wanted to improve their financial status and reduce the public debt during the second term of Hariri. Both issues caused massive problems in the domestic economy of the country. Hariri used all his personal contacts in order to find a feasible solution.

Second: the knowledge generation. In his second era, the generation relevant to the information age strongly opposed Hariri and accused him of hiding vital data about the economic situation; an allegation which he strongly denied. This social reality was used as new offensive form on the Prime Minister.

Alternatively, Hariri used to share information with his followers since his main concern was “to inform the people about the reality of the situation in order for them to react in a positive way hence reducing the problem”⁴⁶.

⁴⁶ M. Al Barazi, *Chourakaa fi ightiyal al Hariri* (partners in Hariri’s killing) Middle Eastern Center for Strategic Studies ,1st edition (2005), p.217

After the 2000 parliamentary elections, Hariri found the need to shift from a united Lebanese identity to creating a unified Sunni situation that is in accordance with a new, regressive and political atmosphere.

It was this sectarian identity maneuver that helped Hariri to regain the seats of Beirut and Saida ; especially that the Taïf accord, along with the social structure in Lebanon, perceived sectarianism as a positive structure in Lebanon and its survival.

Based on this information, Hariri remained a leader worth observing and following.

In the fourth and final chapter, Hariri's political terms are combined using the four leadership theories to test the similarity of the results; in addition to studying the reasons of his resignation in 2003.

How would Hariri be measured according to the standards he set for himself as Lebanese leader and world figure?

Chapter FOUR

The last chapter assesses Hariri in two spectrums: the last term as a Prime Minister and the role he played after the 2004 resignation. The Lebanese political arena was going through one of its most intricate crises under international pressures. At the same time, a United Nations resolution demanded drastic changes and reforms at all political levels.

Hariri's role in this transitional period is examined with a review of his strategies and plans; to form a conclusion on the status of his leadership.

Accordingly, we separated this chapter from previous ones to respect the importance of this period of Lebanon's history. The era coincided with international pressures and potential sweeping changes occurring 15 years after the Taif accords.

After the September 11th terrorist attacks, the United States declared its "war on terrorism" from Afghanistan to Iraq. The US decided on a radical change in its foreign Policy towards the Middle East.

On April 17th, 2003, Rafiq Al Hariri was asked (for what would be the final time) to form a new cabinet. In less than one week he had managed to reshuffle his old cabinet, concluding a two-day parliamentary debate on policy which gained a vote of confidence. "The process had been faster than ever before."⁴⁷

Hariri was aware of the difficulties facing Lebanon. On the other hand, the Bush Administration's increased criticism on Syria's role in the Middle East and its involvement in the Lebanese domestic issues and political affairs eventually led up to

⁴⁷An Nahar Beirut , April 23, 2003

Congress's "Syria accountability act"⁴⁸, which imposed strict sanctions against Syria in the event of non-compliance.

This was a clear sign that Syria's "historical relations"⁴⁹ with the Americans was deteriorating rapidly. Through this Congressional act, Washington was demanding Syria's military withdrawal from Lebanon and closer coordination in anti-terrorist activity.

Finally, the United Nations translated this act into a resolution; giving the Lebanese issues an international scope once again.

This drastic change in relations between the world superpower and Syria had enormous effects on Lebanon. The United States perception regarding the Syrian military and political involvement in Lebanon had changed 180 degrees from its previous endorsement (post-war period). It claimed that there was no necessity for Syria's presence after complete Israeli military withdrawal from the South in accordance with the UN Resolution 425.⁵⁰

Syria and its supporters in Lebanon strongly rejected this approach and warned that it would increase an already tense and complicated situation in the region.⁵¹ The true underlying motive for this rejection was the threat posed on the bilateral Syrian/Lebanese political relationship which would damage the personal interests of members of certain political classes from both countries.

⁴⁸On October 15, the U.S House of Representatives passed the Syria Accountability and the Lebanese Sovereignty Restoration Acts of 2003.

⁴⁹Due to the immense help Syrians used to provide the US during the Gulf War and other intelligence and military information sharing.

⁵⁰The Times, 129 (December 4th 2003)

⁵¹Demonstrations were organized against what they called "the US intervention in Lebanon", most of those demonstrations being located in areas which were under direct Syrian military supervision.

The internal player possessing the most firm and unwavering Syrian support was Hezbollah, God's Party. The United States asked for the disarming of the party and the handing over its weapons to the Lebanese government.

Based on the fundamental nature of its purpose as national liberators⁵², the logical conclusion would be for Hezbollah to hand in its weapons after the liberation of the South. But the official Syrian and Lebanese position strongly opposed this argument, alleging that there were still territories under Israeli occupation (The Shebaa Farms area); that was despite the fact that United Nations experts did not recognize them as Lebanese territory, but rather according to regional maps as Syrian.

This unsettled issue proved to be very problematic for the United States and the international community, as Hezbollah's military activity resumed at the Shebaa Farms border, a matter that the US administration found "extremely dangerous". The Bush administration was now searching for alternative measures to disarm the Iranian-supported militia, and to put an end to this instability factor.

This all had a negative impact on Lebanon's economic prosperity, considering also the dire economic straits Lebanon had been in over the last few years.

On the economic platform, Hariri's strategies were to reduce the budget deficit, increase the primary surplus and gradually reduce the interest rate. This plan was to be put into effect by curbing the increase in public debt and then reducing it, using privatization.

As for the private sector (Hariri's base), an increase of productivity was necessary in order to create new job vacancies for the new generation. This increase occurs strictly if the government takes initiatives in the taxing system encouraging investment. In the

⁵² "Ending the occupation over our territory" Hezbollah official statement: www.hezbollah.org/frontpage.statement

public sector, according to the recommendations drawn up in Paris I and II, the government should cut down cost and increase productivity.

The economy in Hariri's government turned around five concepts:

One: achieving a significant and sustainable reduction in the overall public expenditure in a way that "boosts efforts to curb expenditure and limit allocations."⁵³

Two: privatization of mainly official institutions that would turn losses into gains and assure certain fixed revenues and profitable returns. This process would be done in accordance with international laws and regulations along with transparent advisory boards and committees.

Three: preserving monetary and financial stability

Four: continuing with the plan of economic development and growth by capitalizing on funds and agreements offered by international organizations and friendly countries.

Five: dealing with economic problems by improving the Lebanese taxing system, cutting unnecessary expenses and completing the reform policy drawn up in the Paris II conference.

These major steps had to be taken along with a local and international propaganda campaign that assured the interested parties a controllable situation in Lebanon.

Economic reform was Hariri's main concern in order to enter the Euromed agreement which would enable Lebanon to develop its export web to include a greater number of countries.

Other steps would be taken to improve tourism, one of Lebanon's basic economic pillars.

Efforts were to be made to encourage investment through promotional advertising abroad and expanding the market to include educational, medical and conference aspects through

⁵³The Executive, Beirut, April 2004

“adopting legislation and measures that would contribute to the development of that sector.”⁵⁴

Hariri realized the delicacy of the period under all the international pressure accumulating on Lebanon and Syria; including the resolution adopted by Congress for Syria’s withdrawal. At that time, Syria had enjoyed complete domination over Lebanon and all officials in power and vehemently rejected the United States outlook and thought of it as a threat to their long standing interests.

Hariri took very quick steps towards influencing the political policy of the upcoming government by stating to the Parliament on April 24th, 2003: “The Government assures, above all, that Lebanon is committed to implementing international resolutions. These include resolutions aimed at achieving a comprehensive, just and lasting peace in the Middle East.”⁵⁵

Hariri publicly intended, along with the cabinet, to regain international consideration by agreeing to adhere and comply with the international resolutions. This facilitated the implementation of the controversial future resolution 1559.

After the Syrian Accountability Act was created and implemented, the Syrian reaction was obstinate. It refused to move out of Lebanon, whether militarily or politically. More pressure by Syrian officials was placed on Hariri to change the US⁵⁶ attitude towards Syria’s influence on Lebanon. Syria still could not clearly perceive the shift in US policy towards the Middle East, as it always believed this would be a temporary phase.

⁵⁴www.rhariri.com/tourism

⁵⁵www.rhariri.com/policy statement in brief

⁵⁶Like we already mentioned in chapter 3: Hariri had great connections through out the world the thing Syria at that time didn’t have.

“We will do what it takes to bring peace into this blessed region.”⁵⁷This briefly covers the new US stance towards the region. Another statement by the Secretary of Defense: “It’s time to change 60 years of wrong US policy in the region”.

Another internal factor was the local one. The internal movement facilitated the realization of an important objective, which was the withdrawal of the Syrian forces from Lebanon. The demonstrations of Lebanese student movements demanding the immediate withdrawal of Syrian forces was labeled as a “phenomenon” by some local newspapers. This is worth noting especially considering the number of demonstrators that was constantly growing. In an unprecedented move that appeared to protect their rights and civil liberties,⁵⁸ the US State Department declared it was closely watching the demonstrations and guaranteeing respect for the basic rights of the students and their freedom of expression.

Hariri remained neutral during this period in order to calm the situation. He focused more on the economic condition. Despite this position of neutrality, his assistance in dealing with the complicated international pressure against Syria and his maintenance of the economic factor made him appear as the main culprit in the local and international debacle.

Hariri’s foes attempted to divert people’s attention away from politics (where major changes were coming into play) to the economy (where Hariri’s actions were partially responsible). In an interview broadcast on Future TV⁵⁹ with host Zahi Wehbe on Friday, January 20th, 2004, Hariri declared that “an organized political war” was launched against

⁵⁷ Colin Powell Speech, M. Al Barazi, *Chourakaa fi ightiyal al Hariri (partners in Hariri’s killing)* Middle Eastern Center for Strategic Studies ,1st edition (2005),pp.36-41

⁵⁸With reference to the incident whereby students were beaten up in front of local and international media on august 7th 2003

⁵⁹A TV broadcasting company owned by Prime Minister Hariri

him in order to make him look guilty and conceal the responsible party from the eyes of the public.

This propaganda campaign did not put an end to Hariri's desire to accomplish his duties towards reform. Another serious development taking place that would definitely threaten Hariri's projects capabilities was the following. During a meeting with university students, President Emile Lahoud declared: "I am ready to do whatever it takes to better serve my country and if the people will grant me this opportunity I'll be more than glad..."⁶⁰

Many analysts thought that this was a turning point leading to the definitive resignation of Prime Minister Hariri. The latter had a seriously deteriorating relationship with the President. Then again, the differences he held concerning fundamental political and economical issues were too wide to bridge.

The main point of Hariri's political view in 1993 and 2000 was that Lebanon's role in the peace initiatives should be separated from all other Arab processes. He was well aware that Syrian intervention and Israeli occupation created a steady level of instability. Hariri believed in diplomatic means to resolve these issues and insisted on applying them to end the Shebaa Farms problem. The President, however, thought that the Arab/Israeli struggle preceded any economic reform initiative.

Those contradictory theories lead to a clash of interests. It reached a point where Hariri clearly saw a continuation of the Lebanese problem if there was any extension for Lahoud's term in office. He was clearly evaluating this situation when he declared: "The

⁶⁰ During a special visit to the Presidential Palace, June 16th 2004

United States sanctions aren't a maneuver and I am afraid more pressures would be exerted on Lebanon and Syria."⁶¹

His opposition to the extension of Lahoud's term reached its zenith when he openly declared that he would "rather cut off his arm than sign the (extension) decree"⁶² for President Lahoud.

This statement caused a private uproar, urging Syria to bluntly demand Hariri to sign the decree; it was Hariri's final severing from Lahoud. The Prime Minister resigned for the last time on October 20th, 2004. ⁶³

During this phase Hariri became merely a viewer "watching the game not controlling it."⁶⁴ But a final plan was made. Hariri's intuition led him to create a strong and unified Lebanese oppositional movement, binding Christian and Muslim opposition figures. This formed a counter-balance to the Syrian sponsored state and guaranteed his comeback victory via an international support system and domestic popularity, only this time on a national level, as opposed to a reduced sectarian level.

Hariri's ally was the leader of the Druze sect, Walid Joumblatt.⁵⁶ He asked him to lead the first Opposition Front meeting in the Bristol Hotel (what came to be known as the Bristol meeting ⁵⁷ back in December 2004). Then, subsequently, in his first public act of resistance against the Syrians, Hariri dispatched two of his Beirut deputies to the meeting. It was an extremely controversial move.

Along with these rapid developments, another factor coming from outside the local context speeded up the "liberation process".

⁶¹ Middle East Intelligence Bulletin, Vol.8 No. 11 (September 2003) p.1

⁶² Al Massira, Beirut, 275 August 2004

⁶³ Two decrees were issued by the cabinet calling to convene as from Monday and stay until its scheduled session began in October and urging legislators to approve the amendments of the 49th article of the Lebanese constitution, to extend the President's mandate until November 23, 2007.

⁶⁴ An Nahar, Beirut 21st December, 2004

On September 2nd, 2005, the United Nations Security Council announced Resolution 1559⁶⁵ asking for the withdrawal of “all foreign forces” and for the disarmament of all “Lebanese and non-Lebanese militias”. It was a clear signal for Syria to pull out its remaining 27,000 soldiers and security apparatus from the Lebanese soil.

On the eve of the resolution, Syrian Vice-president Abdul Halim Khaddam, emphatically denied all allegations against Lebanon and Syria stating: We do not interfere in Lebanon’s domestic affairs.

This statement did not deter the pressures that would finally force Syria to withdraw. The cost of this withdrawal would be extremely high for Rafiq El Hariri. An endless propaganda campaign continued to target Hariri’s achievements, political rights and opinion. The vicious nature of this campaign would later be examined by the “International Independent Investigation Commission”⁶⁶, for the campaign would pave the way for Hariri’s assassination.

Just a few weeks after passing of Resolution 1559, parliamentarian Marwan Hamade escaped from a car-bomb assassination attempt. A veteran politician known for his moderation, Hamade was an effective go-between between Hariri, and Druze leader Walid Jumblatt and the Christian opposition. The investigation of Hamade's assassination attempt led nowhere, like others of political assassinations in pre- and post-war Lebanon. The Hamade incident carried an unambiguous message: the political assassinations made to preserve the status quo of Syrian hegemony over Lebanon were still part of the

⁶⁵ The full text is available at Wikisource: [UN Security Council Resolution 1559](#).

⁶⁶ Security Council Resolution 1559 (April 7, 2005): The Security Council has established an international independent investigation commission based in Lebanon to investigate the killing of former Prime Minister Hariri. To ensure an effective probe into Hariri’s murder, the Council calls on Lebanese authorities to grant the commission full access to information relevant to the inquiry. If Beirut fails to cooperate with the UN investigation team into the “terrorist act”, it could face UN sanctions which seek to root out terrorism.

"political process", in defiance of the renewed international focus on Lebanon. This unstable situation remained until it exploded on February 14th, 2005, with a car blast killing the Prime Minister along with 19 people. The tragedy caused a shockwave all over Lebanon. The Hariri assassination has unleashed sociopolitical forces that will take Lebanon into a new era. Between the Opposition's determination to confront Syria and the willingness of pro-Syrian forces to vigorously support the status quo, Lebanon's political future has become unpredictable. The moment was ripe for active international action to press Syria to end its occupation. Once again, the 'myth of the phoenix from the ashes' emerged, thanks to a series of youthful demonstrations uniting all political and sectarian fronts and calling for the full sovereignty and liberation of Lebanon and a complete Syrian retreat. On April 28th 2005, the last Syrian soldier crossed the border from Anjar to Syria; finally realizing Hariri's dream of a sovereign Lebanon.

Going back to the four theories of leadership, we can see how Hariri changed his tactics to preserve his leadership. Through "Transformational Leadership", Hariri was conceived to be a "savior"⁶⁷ based on values of "trust" through complicated socio/political times. During this new geopolitical crisis that was centering on Lebanon's future, Hariri switched his priorities from economic stability and revival to a platform of freedom and liberation in order to build a stable democratic state and society. Leaders study the general situation to find common ground with their followers, Hariri understood the demands of his followers, especially that the trend of demonstrations mentioned before started to affect all of his decisions. In order to gain his country and his followers, Hariri

⁶⁷See chapter 2 PP. 25-28

had to execute a drastic change in his leadership decisions. At this stage, the transformational leadership theory can be easily applied to Hariri's new outlook.

According to the Stodgill theory, personal traits play an important role in the decision-making process. The issue of social belongingness helps the leader to take risks or drastic steps perceived to be revolutionary by his followers. And Hariri surely did that.

Through his continuous charity work, Hariri explained his position to his followers. His affirmative action plan of changing policy enabled him to gain a considerable number of new supporters and earn the respect of his main political rivals, thus, creating a real sense of national unity.

This drastic change in political attitude "granted Hariri an advanced position in the front lines of the Lebanese opposition",⁶⁸ along with the increased respect of rivals and a high degree of honesty while dealing with other issues concerning Lebanon.

This is part of the third theory, "Cognitive Leadership", which is mainly based on respect, honesty and influence.

From the perspective of the third point in the theory, "influence", Hariri's move towards the local opposition parties threatened the regime. Hariri, through his international credibility, could create a very effective and powerful league within the Opposition.

This coalition created a delicate⁶⁹ counter-balance to the traditionally weak Lebanese regime, a natural alternative to the deplorable status quo. This was all prior to the 1559 U.N. resolution.

⁶⁸Al Anbaa (Kuwait), 23 April, 2005.

⁶⁹Delicate period: a word often used by Lebanese officials that became a "jock-word" in the Lebanese political dictionary.

As for the fourth and last theory, emotional intelligence was a main decree in Hariri's tactics. His objectives targeted a familiar issue with an added political risk: liberation and freedom for true democratic change by resisting the Syrian-controlled regime. Hariri's initial motives in 1993 had been to create a sovereign state and sign peace accords with Israel. Then again, the conditions back then were not in his favor.

On Friday, March 23rd, D. Hamadeh, in a profile on Rafiq El Hariri's political life for the University of Texas, wrote: "Lebanon has been under the influence of Syria. Hariri has accepted this reality, and like other politicians have tried to turn it to his advantage to a point where he tried to turn it into Lebanon's advantage by proclaiming the full independence and sovereignty status."⁷⁰

Hariri would remain connected to the "power on the ground" through his political association, the "Future Youth Movement", during weekly meetings and seminars, where they would brief each other on the present situation. This was the basis of his electoral groundwork and future campaign hopes.

Along with his high esteem and constant smile, the Prime Minister continued to have faith and further remain strong facing perceived injustices: "Have faith in God, He will definitely come to our rescue."⁷¹ This trait ("hope and confidence") infused power into the will of his followers even and especially after his death in March 2005.

Hariri was aware that "emotional intelligence" requires the creation of a "unified identity" and this objective could finally be reached through this following. The new international attention spotlighted Lebanon with a U.N. resolution and constant U.S.

⁷⁰D. Hamadeh "Rafiq Hariri: role profile" for the university of Texas, USA, 23rd march 2001.

⁷¹Future TV an electoral shot taken from the minister speech, 2005.

administrative motions and declarations. He forecast the “light at the end of the tunnel” and the period of “self rule” in Lebanon.

Hariri’s involvement in the Bristol meeting, re being the most powerful Sunni leader, gave the needed impression to the world community. The impression was formed of a unified Lebanese opposition joining the Christian and Druze communities and even a few important Shiite figures that were able to pull away from the traditional political movements.⁷²

For the majority of the Lebanese, Hariri’s decision was mostly heroic, since no Sunni leader in his position had ever historically dared to stand up to Syria. The latter always kept a tight grip around the Sunni community in Lebanon and prevented it from ever gaining solid political or militant power.⁷³

Furthermore, the Bristol coalition of many communities was original and the first of its kind since 1943, when a national majority gathered to resist the French colonial power in a move for independence.

According to the four theories, this turning point of ideas, plans and actions could be applied to the issue of flexibility and projection. Leaders had to be able to project the needs and desires of their followers and then turn them into reality, having the flexibility to carry out plans that required a change in course. Hariri had the power of perceiving change and adapting to it by applying the three phases discussed in the first three chapters, including “emotional leadership” theory.

⁷²Hizbullah and the Amal movements both criticized as being the two only Chiit superpowers.

⁷³Al Safir (Beirut) November 25th 2004

Emotional intelligence urges the leader to assimilate a large amount of information, accompanied with knowledge, of the basic needs of his followers. Hariri exercised this ability by shifting strategies through each political stage.

In the first phase Hariri tackled the “reconstruction” issue. Lebanon had been through 15 years of devastating war and chaos and Hariri offered a restructuring plan linked with his business savvy.

The second phase required resolving the economic issue. Through his vast global connections, Hariri created a system that advocated a plan of economic rescue reform.

In the third and final phase, Hariri embraced the Lebanese opposition because of local and international pressure of political and state reform. It would be a process of freedom and liberation, but the heroic Prime Minister would end up a martyr for it.

Throughout these phases, Hariri’s leadership skills never diminished or changed; only circumstances modified his acts. He used each new phase to learn from his errors and avoid making them again. They required him to draw up new economic and political plans that would increase his chances of attaining heights of the leadership once more, something which he would not always achieve. The important factor being detected through the careful study of these four different theories was that of circumstance.

For example, in the first phase of Hariri’s political journey the circumstances were to his benefit while in the second the regional political currents (Syrian inspired) were running against him.

The same factor reveals itself in the third and last phase, this time with local and international forces favoring Hariri’s oppositional stand. Through his leadership skills, he was able to take advantage of these circumstances to return to prominence.

Apparently, Hariri was a leader who knew how to read and respond to circumstances through every phase of his political voyage.

Finally, to judge by the facts presented in this study along with other case studies and theories, Hariri's leadership skills were extremely high and the benefits of our late Prime Minister which are current political and economic work will show themselves in full clarity in the near future.

The leadership skills shown by Rafiq Hariri were very fine, resulting in his adapting to all challenges that helped him shape those skills as shown below in the awards for his achievements:

- Chevalier de la Légion d'honneur (1981)
- Chevalier of the Italian Republic (1982)
- Cedar National Medal / Rank of Commodore (1983)
- Saint Peter and Paul Medal (1983)
- Save the Children 50th anniversary award (1983)
- Medal of King Faysal (1983)
- Médaille de la Ville de Paris (1983)
- Golden Key of Beirut City (1983)
- Chevalier des Arts et des Lettres (1983)
- Officier de la Légion d'honneur (1986)
- Doctor Honoris Causa of Boston University (1986)
- Doctor Honoris Causa de l'Université de Nice (1988)
- Doctor Honoris Causa of the Arab University of Beirut (1994)
- Golden Key of Sao Paulo City/Brazil (1995)
- Medal of the Liberator of Argentina- General José St. Martin (1995)
- Prix Louise Michel-France (1995)
- Doctor Honoris Causa of Georgetown University-Washington USA (1996)
- Grande Croix de la Légion d'Honneur (1996)

- Le Grand Cordon (1996)
- The Order of Diplomatic Service Merit Grand Gwang Hwa Medal- Korea (1997)
- Doctor Honoris Causa of the University of Ottawa, Canada (1997)
- Doctor Honoris Causa of the University of Montreal, Canada (1997)
- Le Grand Collier du Trône- Morocco (1997)
- Cavalier du Gran Croce (1997)
- Al Nahda Medal, First Category, Hashemite Kingdom of Jordan (2001)
- Medal of Honor of the Arab Union/ the Trade Union of Veterans Associations (2001)
- “Star of Romania”, rank of The Grand Cross (2002)
- Union Medal / Republic of Yemen (2002)
- Honorary Doctorate in Human Letters, Lebanese American University, Beirut, Lebanon (2003)
- Orient Doctorate Degree, Moscow State Institute for International Relations (2003)
- UN-HABITAT Scroll of Honor Special Citation for Post Conflict Reconstruction / World Urban Forum, United Nations-Barcelona, Spain (2004)
- King Faysal International Award for Serving Islam, equally with the Islamic Bank for Development (2005).⁷⁴

At all times, Hariri’s skills evolved to reach a stage of perfection while he collaborated with his Christian compatriots to focus on all main political and economic targets. Hariri declared this ultimate mandate: “Reaching a free democratic Lebanon”.

This analysis about leadership skills Hariri possessed, beginning at a young age then making out of him a successful business man and enabling him to enter the Lebanese political scene from a wide experienced perspective, resulted in creating a political leader Lebanon has not witnessed for quite a long time.

⁷⁴ www.rhariri.com/awards

Conclusion:

Hariri's main concern and objective was the reconstruction of the country. This goal was shared by most Lebanese groups who proclaim their unwillingness to re-live the trauma of the civil war. This environment or "positive circumstance", ⁷⁵created after the Taif agreement, helped Hariri realize the dream of every Lebanese.

Apparently his task was harder than he had thought; he obviously came up with wrong predictions concerning peace and stability in the region. This was due to the internal political instability, elite unaccountability, poor cabinet solidarity and competing sectarian visions. All of these factors helped to create the "other face"⁷⁶, a description made by his political opponents.

Despite this fact, the challenge of rebuilding Lebanon was the main feature behind this great man's vision and action. Back in 1993, he openly tried to regain Lebanese sovereignty by assuring Lebanon's presence on the international map as an independent unit, taking unilateral decisions. This initiative created for Hariri some enemies who were in reality enemies of Lebanon.

Then in year 2000, the prime minister had tried again to focus on the domestic economic problems which would enable the country to resist firmly any regional threat. His call was in vain and as a result, Hariri's loyalty to his country was in doubt.

However, Hariri created a possible solution for the public debt by managing through the web of his personal connections, to call an international conference, hence, allowing several states to provide and put into effect their announced offers back in 1990.

⁷⁵See Chapter four pp. 62-64

⁷⁶ Najah wakim, Al Ayadi as- soud (the black Hands), Beirut : Sharikat al- matbuat lil- tawzi wal nasher, 1998, p.4

Because of the corruption and direct foreign intervention, Hariri aim was not fulfilled and Lebanon, until the present day, has barely recovered.

He spent nine years in office and 35 years of hard work to reestablish and reconstruct his country. In accordance with the four theories of leadership and Hariri's achievements, the importance of that man whose target was the reunification of all Lebanese was immense. The target was reached even after his assassination.

Reaching his primary task of reconstructing Lebanon along with laying a firm foundation for the Lebanese economy, Hariri managed to assemble the Sunni community under his leadership. Throughout Lebanese history, this community has never had a unified leader and was always under the "mercy of other Sunni community dominance especially Syria".⁷⁷

In order to be able to measure the grandeur of his leadership, two main criteria are presented in order to better understand this man's vision and leadership achievements.

After his death Hariri transferred some of his leadership legacies to his son Saad El Dinn Al Hariri, as ALJAZIRA points out in its latest news: "Al Hariri is expected to sweep the Beirut poll on 29 May 2005 with an ultimate result of 94% of the total vote in favor of Hariri's son"⁷⁸

This evidence is a living fact about the legacy of Hariri's leadership and his realization of mobilizing the Sunni sect under his control, along with the emotional feeling locked inside every Lebanese in response to his brutal assassination.

By coming to acknowledge his contribution to the decade of reconstructing both society and economy, but also by gaining the best possible understanding of the obstacles and

⁷⁷ An-Nahar (Beirut) august 4th, 2002

⁷⁸ file:///A:/Aljaziera_net-Lebanon_leader_weight_poll.htm

problems of the reconstruction years, the Lebanese can use lessons of the past decades as a vital tool in helping to determine the nation's impending course.

Annex 1:



LEBANESE REPUBLIC

LEBANON: PARIS II MEETING

November 23, 2002

**BEYOND RECONSTRUCTION AND RECOVERY.....
TOWARDS SUSTAINABLE GROWTH**

A request for international support

ABBREVIATIONS AND ACRONYMS

| | |
|--------------|--|
| BdL | Banque du Liban (Central Bank of Lebanon) |
| CDR | Council for Development and Reconstruction |
| EdL | Electricité du Liban |
| EU | European Union |
| EIB | European Investment Bank |
| FATF | Financial Action Task Force |
| FX | Foreign Currency |
| GAFTA | Greater Arab Free Trade Area |
| GCC | Gulf Coordination Council |
| GDP | Gross Domestic Product |
| GNP | Gross National Product |
| GPRS | General Packet Radio Service |
| GSM | Global System for Mobile |
| IDAL | Investment Development Authority of Lebanon |
| IMF | International Monetary Fund |
| INSEE | Institut National de la Statistique et des Etudes Economiques |
| LL | Lebanese Pounds |
| MEA | Middle East Airlines |
| MW | Megawatt |
| NERP | National Emergency and Reconstruction Program |
| NDIF | National Deposit Insurance Fund |
| NSSF | National Social Security Fund |
| SME | Small and Medium Scale Enterprise |
| VAT | Value Added Tax |
| WTO | World Trade Organization |

LEBANON: PARIS II MEETING
BEYOND RECONSTRUCTION AND RECOVERY.....
TOWARDS SUSTAINABLE GROWTH

Contents

PREFACE

| | |
|---|----------|
| INTRODUCTION | 1 |
| Graphs: Fiscal Developments and Debt (2000-2003) | 2 |

| | |
|---|----------|
| INDEBTEDNESS AFTER A DECADE OF RECONSTRUCTION AND RECOVERY | 3 |
| Box 1 Lebanon 1990: After Fifteen Years of War | 3 |
| Box 2 Lebanon 2000: After Ten Years of Reconstruction and Recovery | 5 |

| | |
|---------------------------------|----------|
| THE GOVERNMENT'S PROGRAM | 6 |
| Introduction | 6 |

| | |
|---|-----------|
| PROGRESS MADE DURING 2001-2002 | 6 |
| Fiscal adjustment | 6 |
| Public Debt | 7 |
| Table 1 Fiscal Developments and Debt 2000-2002 and Budget 2003 | 8 |
| Privatization | 9 |
| Structural Reforms | 10 |
| Growth and Exports | 11 |
| Recent Developments | 11 |

| | |
|---|-----------|
| THE PROGRAM FOR 2003 AND BEYOND | 12 |
| Introduction | 12 |
| Fiscal Adjustment | 12 |
| Privatization | 13 |
| Cost of Debt | 14 |
| Debt Reduction, Growth and External Support | 14 |
| Table 2 Fiscal Developments and Debt 2002-2007 | 16 |
| Graph: Domestic Effort | 17 |
| Table 3 Composition of Public Debt | 18 |

| | |
|-------------------------|-----------|
| EXTERNAL SUPPORT | 18 |
|-------------------------|-----------|

POSTSCRIPT

| | |
|---|--|
| ANNEX I PARIS II: THE GOVERNMENT'S PROGRAM FOR 2003 AND BEYOND | |
| ANNEX II PARIS I: A MATRIX OF STRUCTURAL REFORMS | |

LEBANON: PARIS II MEETING

BEYOND RECONSTRUCTION AND RECOVERY..... TOWARDS SUSTAINABLE GROWTH

PREFACE

At the time that the current Government took office in late 2000, Lebanon faced a difficult situation arising from debt accumulation that had its origins in a decade of reconstruction and recovery after 15 years of war and civil strife and amidst continued attacks from abroad. There had been a lack of national consensus on how to address an evolving debt problem and delays in domestic action. Fiscal deficits and debt had reached unsustainable levels and the economy was stagnating. On the occasion of the Paris I meeting in February 2001, the Government of Lebanon presented its strategy for addressing the situation with fiscal adjustment to reduce the rate of accumulation of debt, privatization to reduce the stock of debt, and structural and institutional reforms to lay the basis for growth. It requested support from the international community to complement the Government's effort and bring about a virtuous cycle of lower fiscal deficits, declining debt ratios, and lower interest rates that can unleash the potential of Lebanon's private sector. The meeting agreed to convene a follow-up meeting to assess the progress that Government had made towards the objectives of its strategy and to agree on external support to ensure its success.

This document presents the progress that has been made since the Paris I meeting and the program that the Government has adopted for the next years. In the meantime, the fiscal deficit has been reduced (with revenues now exceeding non-interest expenditures), major privatizations are about to be launched, and the structural reforms are largely in place, but debt ratios have continued to rise as a result of high interest rates, with interest payments on the net debt of about US\$30 billion now absorbing about 80% of Government revenues. External support is the missing link to creating the virtuous cycle. The Government of Lebanon does not expect that the support it is requesting will be available mainly in the form of grants and soft loans. The Government requests external support to change the composition, reduce the cost, and lengthen the maturity of its debt through instruments such as sovereign guarantees, investments by Governments and Central Banks in new Lebanese Government foreign currency bonds, and similar arrangements that would allow Lebanon to borrow in supporting countries' markets at low spreads, using the proceeds solely to substitute such external debt for existing high interest short-term debt. Such substitution would result in a sharp reduction in the level of domestic interest rates, with a consequent further reduction in the overall fiscal deficit and Government financing needs, and lay the basis for solid private sector-led growth and recovery.

The Government is committed to its program of fiscal adjustment, privatization and structural reform. If the overall program was not to be successful in the absence of external support, economic and social stability in Lebanon could be undermined. The Government of Lebanon is therefore most appreciative of the initiative of the President Chirac of France to convene the Paris II meeting and the willingness of friends of Lebanon in the international community to participate and consider Lebanon's request for assistance.

LEBANON: PARIS II MEETING

BEYOND RECONSTRUCTION AND RECOVERY..... TOWARDS SUSTAINABLE GROWTH

INTRODUCTION

1. In early 2001, after a new Government had taken office in Lebanon, President Chirac of France convened a meeting in Paris, with the presence of the Presidents of the European Union (EU) and the World Bank and the Vice-President of the European Investment Bank (EIB) with a view to discussing support for the Government's economic program. The meeting indicated that support would be considered once progress had been made on the implementation of the program. It was agreed to convene a broader follow-up meeting to assess progress made and to agree on future external support to ensure successful implementation of the Government's program over the 2002-2004 period.

2. At the time of the Paris I meeting, Lebanon faced a difficult economic situation. Real Gross Domestic Product (GDP) growth had stagnated, the overall fiscal deficit had reached close to 25% of GDP in 2000, with interest payments on public debt absorbing the bulk of Government's total revenues, and total net public debt had reached about US\$23 billion, equivalent to close to one and a half times Lebanon's GDP in that year. Facing the dual challenge of the need for fiscal adjustment and debt reduction and for stimulating economic growth, the Government took immediate steps to decrease the rate of accumulation of public debt through fiscal adjustment—in particular moving the primary balance from a deficit to a surplus—and to prepare for debt stock reduction through privatization. It also initiated structural measures to stimulate economic growth and exports.

3. The Government's initial efforts, the progress achieved to-date, and its program for the next few years are discussed in the section "The Government's Program" below (page 6). During 2001-2002 there has been some recovery of growth and strong export performance resulting from the incentives and structural measures taken by Government since early 2001. Despite significant fiscal adjustment during 2001 and 2002—with an improvement in the primary fiscal balance¹ equivalent to about 10% points of GDP—, total net public debt has risen further, however, to US\$30 billion² (of which the equivalent of US\$17.8 billion is net domestic currency debt³), or 173% of Lebanon's estimated GDP⁴. At the same time, interest

¹ Government revenues less non-interest expenditures.

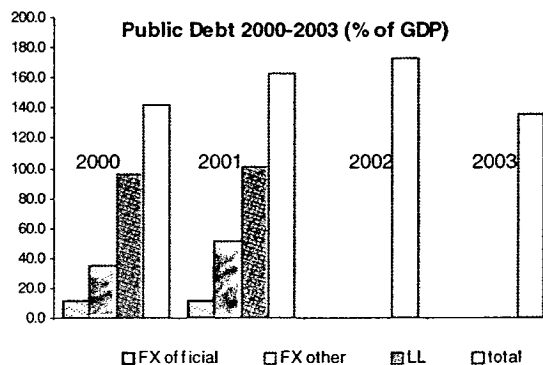
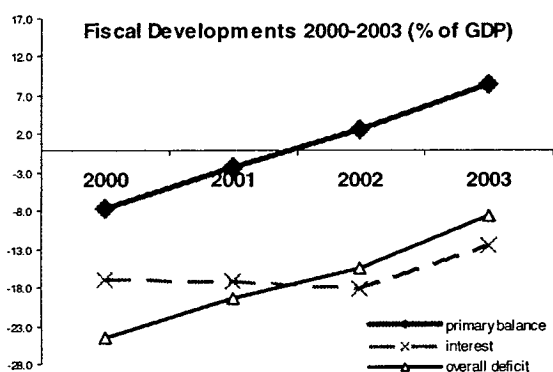
² This is the level of net public debt (as of end-2002), which includes net domestic debt (gross domestic debt, excluding accrued interest on discount Treasury bills, less public sector deposits with the Banque du Liban—BdL—and commercial banks) and total outstanding and disbursed foreign debt. Unless indicated otherwise, references to domestic and total debt in this document are to the net public debt, excluding accrued interest on discount Treasury bills.

³ Debt denominated in Lebanese Pounds (LL)

⁴ There is a broad consensus that Lebanon's GDP is likely to be higher than indicated in current estimates, and that the Gross National Product (GNP) is larger than GDP. Government will update

payments on the debt have reached a level of nearly 18% of GDP and absorbed about 80% of total Government revenues in 2002, even exceeding its tax revenues.

4. The graphs below present the evolution of fiscal and debt situation: (i) as of end-2000, after a decade of reconstruction and recovery, subsequent to 15 years of war; (ii) as of end-2002, after the fiscal adjustment that was implemented during 2001 and 2002; and (iii) the situation expected as of end-2003, after the planned continued fiscal adjustment, based on the budget for 2003, and the implementation of the privatization program, on the assumption that the external support that is requested will be forthcoming. Detailed information on fiscal developments and debt for 2000-2003 is presented in Table 1 (page 8). The Government's program for 2003 is presented in the section "The Program for 2003 and Beyond" below (page 11).



5. Despite the initial progress that the Government has made with fiscal adjustment, privatization and structural reforms, sustained growth will not be achieved unless Lebanon, with external support, is able to create a virtuous cycle of lower fiscal deficits, declining debt ratios, and lower interest rates that can unleash the potential of Lebanon's private sector supported by more efficient public institutions, in the context of stable economic and social conditions. The Government is committed to its program of continued fiscal adjustment, privatization and structural reform. If the overall program was not to be successful in the absence of external support, economic and social stability in Lebanon could be undermined.

6. Delays in policy actions to address the evolving debt issue during the 1990s, because of political or institutional constraints, or adverse external circumstances, undoubtedly have contributed to the situation that the country finds itself in today. Nevertheless, much of its origin goes back to the particular circumstances that Lebanon faced as it sought to reconstruct after 15 years of war and civil strife, with continued occasional external hostilities throughout the 1990s. This background is provided in the section "Indebtedness after a Decade of Reconstruction and Recovery" below (page 3) to set the stage for today's situation and the proposed Government response for which it seeks external support on the occasion of the Paris II Meeting.

GDP and GNP estimates in early 2003 with the help of Eurostat and INSEE and hence debt ratios would likely be smaller, but obviously still too high.

INDEBTEDNESS AFTER A DECADE OF RECONSTRUCTION AND RECOVERY

Box 1 Lebanon 1990: After Fifteen Years of War

In the early 1990s, Lebanon faced the multiple challenges of post-war reconstruction and economic stabilization after fifteen years of war and civil strife. The hostilities had left massive destruction of infrastructure and housing, displacement of population and weakened institutions:

- Damage to physical assets was estimated, by the United Nations, at US\$25 billion—with much of the physical infrastructure destroyed or inoperative
- A quarter of the population was displaced, with their houses destroyed, and one in five Lebanese—many professionals and skilled workers—left the country
- Public institutions were severely weakened
- Per capita income—at the level of Portugal in 1974—had fallen by two-thirds in real terms by 1990 and stood at US\$1000—one seventh of Portugal's

7. Initial circumstances were not conducive to rapid reconstruction. Domestic conditions were chaotic as national reconciliation took hold and the regional situation remained highly unsettled. With a revenue base and institutional capacity that had been eroded after 15 years of war, and limited external support, Government initially relied heavily on domestic currency financing for its expenditures, with increased recourse to monetary financing in the course of 1992. By late 1992 (before major reconstruction had even started), total public debt already stood at the equivalent of 40% of GDP. This was the background to the severe economic instability in that year with sharp exchange rate fluctuations and inflation at triple digit levels.

8. To address the unstable situation that had evolved in 1992, a new Government that took office in late 1992 adopted exchange-rate based stabilization policies that helped restore confidence, caused a rapid decline in the rate of inflation to single digit level by 1994, and encouraged private capital inflows. The reconstruction program took off in earnest in 1993. The Government's initial National Emergency and Reconstruction Program (NERP), initiated with support from external donors, was expanded into a broader and larger program for reconstruction and infrastructure expansion in 1994 as Lebanon sought to reposition itself as an international economic and services center in the Arab region that had increasing prospects of prosperity based on developments ongoing at the time. The Government's program focused in particular on rehabilitating, reconstructing, and expanding infrastructure with a view to providing the basis for the private sector to lead the reemergence of Lebanon as a regional hub for trade and services and a link between the region and Europe.

9. In addition, in the aftermath of the war, the Government took on the task of investing in social peace, taking care of the incorporation of the war militia, and providing for resettlement and social assistance to the displaced, many of whom could not return to their homes as a result of the continued occupation of the South. At the same time, regional

security conditions remained unsettled throughout the 1990s, requiring expenditures for security as well as the repair of damages that were caused by bombings, particularly on the occasion of the major Israeli attacks in 1993 and, again, in 1996 and 1999. On the latter occasions, part of the rehabilitated infrastructure was again destroyed or damaged.

10. As domestic normalization took hold and rehabilitation and reconstruction took off, there were great expectations in Lebanon for sizable external support in the form of grants for the reconstruction program to supplement the role of the Lebanese Diaspora in reviving Lebanon's private sector. In the event, the magnitude of the support, while important, fell far short of those expectations, and was mainly in the form of soft loans from the countries and institutions of the Gulf Coordination Council (GCC) and Europe, and loans from international financial institutions. Undoubtedly, some of this was a consequence of the emergence of other priorities that arose in the region for potential donors from 1990 onwards and the absence of progress on a comprehensive settlement, beyond Lebanon's control. The shortfall in external funding was compounded by Lebanon's failure to rapidly utilize the support that was provided (mainly in the form of project-specific loans for the NERP from GCC funds and countries, European institutions and a number of EU countries, and the World Bank) as the weak public institutions often found it difficult to meet the requirements associated with these loans.

11. Moreover, access to medium-term external loans at market terms was initially limited, even though Lebanon had a solid track record of meeting its external debt obligations throughout its history, even at war times, during the darkest days of violence, and the option of borrowing in foreign currency domestically was not available to Government at the time. Nevertheless, from 1994 onwards Lebanon was increasingly successful in tapping international capital markets, with lengthening maturities, declining spreads, and diversification of sources, but the amounts available fell short of the overall financing needs that were rising rapidly.

12. Finally, a greater role for the private sector in the reconstruction and expansion of infrastructure was limited by a host of factors. These included not only the absence of a appropriate legal framework and of institutions or political consensus, but also the state of the devastated infrastructure and public institutions operating it, and most importantly, the reluctance of the private sector to take on major infrastructure investments in Lebanon in the aftermath of the war, amidst continuing insecurity in the region, including bombings of infrastructure facilities. Thus, the Government undertook most of the task of restoring basic services to support private sector recovery. In the cases where public private partnerships were feasible, such as in the case of the cellular phone system, Government did proceed on this path.

13. Against the above background, Government initially relied heavily on borrowing in local currency in the domestic market for its overall financing requirements. The domestic currency debt had average maturities of less than a year with high interest rates as a consequence of the stabilization policies and the risk premia that investors demanded. With high cost of borrowing, the overall fiscal deficit expanded rapidly, even though as a result of the revenue effort initiated in 1993 the ratio of Government revenues to GDP had by the mid-1990s risen nearly three-fold from the post-war level. The rise in the overall fiscal deficit not only reflected the reconstruction outlays and the post-war social and security expenditures, and high interest rates on the budget's financing, but also the fiscal costs of the occasional sterilizations by the Central Bank (Banque du Liban—BdL) of short term financial capital inflows as part of the stabilization policy, in order to avoid exchange rate volatility, in particular a sharp appreciation of the currency. Thus, the stabilization policy that had major benefits in terms of confidence, capital inflows, replenishment of reserves, and price stability, had its unavoidable fiscal costs. The overall fiscal deficit reached about 20% of GDP by the mid-1990s, with interest payments absorbing about three-quarters of total revenues.

14. With fiscal deficits rising, Lebanon's public debt increased rapidly and by 1996, total net debt stood at US\$11 billion, equivalent to about 85% of GDP, with all but about US\$2 billion in the form of local currency domestic debt. In the meantime, the reconstruction and recovery program that was underway and the stabilization policies contributed to rapid economic recovery, with real GDP increasing to about 80% over its 1990 level by 1996, with a per capita income of around US\$3000— equivalent to about one-third of Portugal's. Indeed, the International Monetary Fund (IMF) was quoted in that year as "Lebanon has made considerable progress since 1992. Economic growth was sustained...inflation brought down...basic infrastructure restored...As a result, the economy is much better placed now to exploit its considerable potential through adjustment and reform. Looking forward, there is considerable potential for the Lebanese economy."⁵

15. During the latter part of the 1990s, Lebanon entered into a cycle of rising deficits and debt and lower growth. International developments made it increasingly difficult for Lebanon to access international capital markets, particularly in the aftermath of the East Asia financial crisis and its effects on emerging markets debt, and Government turned increasingly to borrowing domestically in foreign currency, tapping the significant pool of financial savings, including those of the Lebanese Diaspora, in the domestic banking system. With increasing concerns over rising fiscal deficits and levels of public debt, spreads on this borrowing steadily increased. The steady rise in interest cost accelerated the increase in the level of fiscal deficits and debt

Box 2 Lebanon 2000: After Ten Years of Reconstruction and Recovery

By 2000, Lebanon's war-damaged physical infrastructure had been substantially rehabilitated and reconstructed, although new rehabilitation challenges evolved with the liberation of the occupied South. Public services were operating, basic education and health care was being provided, internal security was fully restored, and the displaced had returned to their homes. Real GDP had about doubled from the post-war level.

However, after the rapid growth during the first half of the 1990s, the economic situation had worsened in the latter part of the decade. The overall fiscal deficit had reached close to 25% of GDP in 2000, with even the primary balance (revenues less non-interest expenditures) in deficit (by 7.5% of GDP), Lebanon's total public debt had risen further to US\$23 billion (or close to one and a half times Lebanon's GDP), real GDP had stagnated, and per capita real income had declined. Private sector confidence was at low levels and private investment was depressed, in part because of the effect that the fiscal deficits and public debt accumulation had on availability of credit and domestic interest rates. It was against the background of worsening trends that Government set out in late 2000 to develop a comprehensive strategy to resolve the debt dilemma through a sustained domestic effort with external support, and that the Paris I Meeting took place in early 2001.

⁵ From a World Bank publication on Lebanon (September 1996)

THE GOVERNMENT'S PROGRAM

16. *Introduction.* Government initially faced a dilemma with respect to fiscal adjustment in the context of a stagnating economy, and declines in per capita real income. With an economy drifting into a recession, and thus threatening the already narrow Government revenue base, and stagnating exports in 2000, Government took a number of fiscal stimulus measures to revive domestic production and exports, and also initiated structural reforms aimed at further liberalizing and deregulating the economy. At the same time it began to develop a program for medium term fiscal adjustment and privatization so as to reverse the trend of rising public debt. The Government's program was presented on the occasion of the Paris I Meeting (see Annex II: Paris I Meeting—A Matrix of Structural Reforms), during which it was agreed that external support would be considered once Lebanon had demonstrated progress in the implementation of its program. Progress made during 2001-2002 and the Government's program for 2003 and beyond are presented below.

PROGRESS MADE DURING 2001-2002

17. *Fiscal adjustment.* On the revenue side, the fiscal measures taken in late 2000 to stimulate the stagnating economy and exports included a targeted reduction in import duty rates. Since customs revenues accounted for more than half of tax revenues in 2000 (and about one-third of total revenues), tax revenues rose only modestly in 2001, with increases in income taxes offsetting the decline in customs revenues. Government overall revenues declined by about 2% in 2001, as non-tax revenues were also lower because of the weak economy. The lowering of duty rates was not only aimed at reviving a stagnating economy, but was also consistent with the overall objective of relying relatively less on international trade related taxes for fiscal purposes, and improving the efficiency of domestic production, in line with undertakings envisaged under the international agreements that were being prepared, in particular the Association Agreement with the EU. During the first three quarters of 2002, however, total revenues rose at a rate of about 28%, with a major contribution from the Value Added Tax (VAT) that was introduced in early 2002, after careful administrative preparation in the course of 2001. As a result, the revenue to GDP ratio has risen from 19.2% of GDP in 2000 to 22.3% in 2002 to-date, with the ratio of tax revenues to GDP rising from 11.9% in 2000 to 15.4% in 2002.

18. Fiscal adjustment in 2001 was achieved primarily through strict control over non-interest expenditures. Despite the need for fiscal outlays to address critical needs in the South after its liberation in 2000, and selective incentives to stimulate the stagnating economy and exports, overall non-interest expenditures were as much as 22% lower in 2001 than they had been in the previous year. Part of this outcome reflected a spillover of expenditures against the 2001 budget and some delayed payments to private contractors into 2002. However, even without this, the reduction in expenditures in 2001 would still be sizable. Moreover, despite the spillover of expenditures from 2001 and the payment of the end-2001 arrears during 2002, the ratio of non-interest expenditures to GDP is expected to be further reduced to less than 20% of GDP in 2002, from more than 27% of GDP in 2000.

19. The fiscal adjustment during 2001 and the first three quarters of 2002, as measured by the primary fiscal balance, amounted to the equivalent of 9.8% points of GDP, with the primary balance moving from a deficit of 7.6% of GDP in 2000 to a surplus of 2.2% in 2002 to-date (and an estimated 2.6% for the year as a whole). This is well in line with the Government's target of a 20% points cumulative fiscal improvement over a five year period, with frontloading. The reduction in the overall fiscal deficit was somewhat smaller than the improvement in the primary balance as interest payments rose further from 17.0% of GDP in

2000 to an estimated 18.1% in 2002, even though average rates on outstanding debt moderated somewhat with a further shift from domestic currency debt to US\$ denominated debt, within the limits that existed. For 2002 as whole, the overall fiscal deficit is estimated at 15.6% of GDP⁶, or about 9% points below the 2000 level. The actual fiscal performance in 2001 and 2002 exceeded the targets envisaged in the informal Medium Term Economic Framework that had been developed in collaboration with the IMF 2001 Article IV Consultations mission.

20. The improvements on the revenue side are a result of a range of revenue measures. By far the most important recent development was the introduction of the VAT (at a rate of 10% on goods and services, with few exemptions), which accounts for a significant part of the increases in revenue in 2002, as well as the increases envisaged for 2003. Taxes on income and profits in 2002 are expected to be up by 60% over the 2000 level, in part as a result of tax audits of large tax payers carried out in 2001 and the tax regularization law that was adopted in 2001. Gasoline taxes were raised three times during 2001-2002 and this year are yielding 50% more than in 2001. The results on the revenue side are also a reflection of the institutional strengthening that has taken place in the area of tax administration, including the establishment of automated customs and land registration administrations, and a widening of the income tax base and a strengthening of tax administration.

21. The efforts to reduce Government expenditures also reflected the results of the initial structural measures taken to rationalize public sector employment and redefine the role of the state. The Government's television station, Tele-Liban, and the national airline, MEA, were restructured, with layoffs totaling about 2000 staff. Surplus employees in a number of public institutions are being redeployed to fill civil service vacancies elsewhere. At the same time, basic legislation is being updated to modern standards to improve public sector efficiency and transparency. A new public accounting law, which streamlines budgetary procedures and strengthens treasury controls, and a new procurement law, which would establish a public procurement regime based on international standards, were approved by Cabinet and are now before Parliament. The major reduction in the role of the public sector that is envisaged by Government underlies the privatization drive that is now underway (see paragraph 25 below).

22. Major improvements in the performance of the public power company (Electricité du Liban—EdL), which now covers its operating costs before debt service, contributed to the fiscal outcome for 2002 and facilitates the planned privatization. The focus of the company's new management has in particular been on improving revenue collections, with the installation of new meters and inspection of existing ones, resulting in revenues increasing by close to 40% over last year. The privatization of EdL and other public companies now planned for 2003 and beyond will also play a key role in reducing the stock of public debt.

23. *Public debt.* With the overall fiscal deficit still at high levels, driven in large part by very high levels of interest payments, the accumulation of debt continued, albeit at a somewhat slower rate. Whereas financing during the latter part of the 1990s had relied heavily on intermediation of the deposits of the domestic banking system, a considerable part of which is held by the Lebanese Diaspora, this pool of domestic financial savings (amounting to about twice the level of Lebanon's annual GDP), became increasingly difficult to tap during 2001 and the first half of 2002, and, instead, the Central Bank increasingly provided resources to the Government for the financing of its deficit.

⁶ The overall fiscal deficit includes the operations of public enterprises and municipal finances. The overall public sector deficit for 2002 is about 0.8% of GDP lower than the fiscal deficit, equivalent to the surplus of National Social Security Fund (NSSF).

Table 1. Fiscal Developments and Public Debt 2000-2002 and Budget 2003

| | 2000 | 2001 | 2002 Jan-Sep | 2002 Estimate | 2003 Projected |
|---|-------|-------|-----------------|------------------|-------------------|
| Fiscal Developments | | | | | |
| <u>% of GDP</u> | | | | | |
| Revenues and grants | 19.6 | 18.7 | 22.3 | 22.3 | 23.7 |
| Tax Revenue | 11.9 | 11.8 | 15.4 | 15.6 | 16.1 |
| Non-tax Revenue | 7.3 | 6.7 | 6.9 | 6.7 | 7.6 |
| Grants | 0.4 | 0.1 | 0.0 | 0.0 | 0.0 |
| Expenditures | 44.2 | 38.1 | 36.9 | 37.9 | 32.4 |
| Non-Interest | 27.2 | 20.9 | 20.1 | 19.7 | 19.5 |
| Interest | 17.0 | 17.2 | 16.8 | 18.2 | 12.6 |
| Primary Balance | -7.6 | -2.3 | 2.2 | 2.6 | 4.2 |
| Overall Deficit | -24.6 | -19.4 | -14.6 | -15.6 | -8.4 |
| Public Debt | | | | | |
| <u>US\$ billion</u> | | | | | |
| Domestic Currency Debt (net) ^a | 15.7 | 16.8 | 17.3 | | |
| Domestic Currency Debt (gross) | 17.4 | 18.1 | 18.6 | | |
| Banks and Private Sector | 14.5 | 11.9 | 12.7 | | |
| Public Sector | 3.0 | 6.2 | 5.9 | | |
| BdL | 1.1 | 4.1 | 3.8 | | |
| Other | 1.8 | 2.0 | 2.1 | | |
| Public Sector Deposits | -1.7 | -1.3 | -1.3 | | |
| Foreign Currency Debt | 7.5 | 10.3 | 12.3 | | |
| Official Creditors | 1.7 | 1.8 | 1.8 | | |
| Other ^b | 5.8 | 8.5 | 10.5 | | |
| Total Public Debt (net), incl. accr. interest | 23.2 | 27.0 | 29.6 | 30.7 | 25.0 |
| Total Public Debt (net) ^c | | | | 30.0 | 24.7 |
| <u>% of GDP</u> | | | | | |
| Domestic Currency Debt (net) | 95.7 | 100.8 | 100.9 | | |
| Foreign Currency Debt | 45.9 | 61.6 | 71.9 | | |
| o/w Official Creditors | 10.6 | 10.6 | 10.7 | | |
| Total Public Debt (net) | 141.6 | 162.4 | 172.8 | 173.0 | 135.8 |
| <u>Composition (%)</u> | | | | | |
| Domestic Currency Debt (net) | 67.6 | 62.1 | 58.4 | | |
| Foreign Currency Debt | 32.4 | 37.9 | 41.6 | | |
| o/w Official Creditors | 7.5 | 6.6 | 6.2 | | |
| Total Public Debt (net) | 100.0 | 100.0 | 100.0 | | |
| <p>(a) The net domestic debt equals gross domestic debt less Government deposits with the BdL and commercial banks. It includes accrued interest on discount Treasury bills.</p> <p>(b) This includes about US\$1.0 billion in Eurobonds held by BdL at end September 2002</p> <p>(c) Excluding accrued interest on discount Treasury bills</p> | | | | | |

24. Total net debt outstanding is projected at the equivalent of US\$30 billion at end-December 2002 (equivalent to 173% of GDP). This includes debt held by public institutions in amount of US\$5.8 billion equivalent gross, or US\$4.8 billion net⁷, so that the net consolidated public sector debt is about US\$25.2 billion, or 145% of GDP at end-December 2002. Net domestic currency debt, at the equivalent of US\$17.8 billion, represents about 60% of total debt, and foreign currency debt amounts to US\$12.2 billion. The latter amount includes both debt owed to Lebanese residents and resident financial institutions, and outstanding and disbursed public debt owed to foreign creditors. Debt owed to foreign creditors, i.e. external public debt as normally defined, is still relatively modest, accounting for a little over one-third of the total foreign currency debt. Of this amount, only US\$1.8 billion represents outstanding debt to official creditors (multilateral and bilateral). In the meantime, at current levels, interest payments on the public debt are absorbing the bulk of Government revenues (and exceed all of tax revenues), indicating the need to both reduce the stock of debt and the cost of servicing it.

25. *Privatization.* Government has set out to undertake a major program of corporatization and privatization of public infrastructure to bring about a reduction in the stock of debt, as well as improvements in efficiency of operations, that will also have a positive fiscal effect (by reducing Government outlays for infrastructure operations and investment or increasing net contributions to the budget) and will reduce the cost of services to business. This program will also lay the basis for a deepening of Lebanon's capital markets. Reflecting an evolving national consensus, and recognizing the need for privatization as an integral part of a comprehensive effort to address an increasingly difficult fiscal and debt situation and of a viable growth strategy, Parliament had adopted a framework privatization law in 2000 that formed the basis for developing sector specific laws to underpin specific privatization operations in various sectors. The law provided for the establishment of a Higher Privatization Council, in the Office of the Prime Minister. The Council became operative in 2001. Three specific laws were enacted in 2002 to set the stage for privatization of two existing cellular phone systems, to corporatize and privatize the fixed line telecommunications, and to corporatize and privatize the power sector. These two sectors represent by far the largest components of public infrastructure, other than roads, in terms of assets. Both laws provide for the establishment of regulatory bodies for the respective sectors.

26. Preparation for privatization in two key sectors—telecommunications and power—, with the help of international investment banks and financial and legal advisors, are thus well underway by now. The specific privatization plans and next steps and timetable are discussed in the Section on the “Program for 2003 and Beyond” below. As mentioned above, Government has already implemented a program of restructuring of the national airline, providing the basis for attracting a strategic investor. Preparations are also underway for legislation to support privatization in the water and waste water sectors, through concessions, following the consolidation of the sector which established four regional companies from as many as 21 entities existing before. In the case of ports and the Beirut Airport initial preparations are underway for privatization through concessions. Finally, legislation has been adopted in 2002 that authorizes the establishment of special accounts for privatization proceeds, which, in accordance with the 2000 framework privatization law, can be used exclusively for purposes of debt reduction. The same legislation also authorizes Government to establish special accounts for certain revenues to be used for securitization, and for the receipt of loans to be used solely for debt payment and servicing.

⁷ This includes both LL and US\$ denominated debt, held by the BdL, the NSSF, and the National Deposit Insurance Fund (NDIF).

27. The stage has thus been set for privatization to make a significant contribution to the resolution of the current debt dilemma. Yet, the combined effects of the major fiscal adjustment together with the comprehensive infrastructure privatization program that is underway will not be sufficient by themselves to reverse the current cycle of fiscal deficits, rising debt and slow growth, into a virtuous one of declining debt, lower interest rates and growth. Such growth would be underpinned by the structural reforms that the Government is undertaking.

28. *Structural Reforms.* The privatization strategy aims not only to reduce the current stock of debt and help achieve the fiscal adjustment targets, but is also to improve the reliability and quality of provision of public services and reduce costs through increased efficiency of operations. As such, it is an integral part of the Government's broader program of structural reforms, which are aimed at promoting growth by further liberalizing the economy, in particular trade, modernizing the legal framework for production and trade, and removing administrative obstacles and disincentives. These reforms are expected to reduce the cost of doing business and hence improve competitiveness of the economy.

29. The reforms focus in particular on promoting exports of goods and services. While Lebanon has traditionally had an open economy, the legal framework, dating from the 1950s and 1960s, had become outdated. In addition to membership in the Greater Arab Free Trade Area—GAFTA (since 1997), in early 2002 Lebanon entered into an Association Agreement with the EU, which, as part of a broader partnership and program of cooperation, provides for free access of Lebanon's industrial exports, most agro-industrial exports and a large number of agriculture exports. In view of the difficult fiscal situation, the EU granted a five-year grace period on the dismantling of Lebanese tariffs (in any event, most categories of imports—86% of the number of all items—have rates of 0 and 5% only). At the same time Lebanon is advancing towards membership of the World Trade Organization (WTO), with the first Working Party meeting held in Geneva in October 2002 and membership now expected in late 2003. These agreements are being underpinned by an updating of legislation, including a WTO-compatible customs law that came into effect in December 2000, and trade liberalization measures, including the introduction of an open skies policies in late 2000, liberalization of oil products in early 2002 and the planned liberalization of pharmaceutical imports and elimination of exclusive agencies for which draft laws are now in Parliament. Further legislation now under preparation includes a competition law, a law on licensing procedures to streamline trade licensing and abolish ad-hoc administrative requirements, a consumer protection law, and further legislation required in connection with WTO accession.

30. In order to promote private investment, and in particular to attract more foreign investment, an investment promotion law was adopted in 2001 that establishes a one-stop agency for investors and selective tax incentives, while another law eased limitations on foreign ownership of land. The adoption of strict new law for fighting of money laundering in 2002, enhanced the international standing of Lebanon's banking system, and encourages bona-fide foreign financial investments. With a view to reducing labor cost and enhancing formal employment creation, employer's contributions to the NSSF were reduced in 2001 from 38.5% to 23.5%. Government subsidies for production and trade, at low levels overall, have been reoriented to enhance their impact. While subsidies for sugar beet production were abolished, selective and transparent subsidies are being provided for reducing transportation cost of fresh produce exports, and lowering interest rates, particularly for small and medium size enterprises (SMEs), complemented with a guarantee scheme to facilitate their access to bank financing. These subsidy measures must be seen as temporary as the structural reform measures lead to a reduction in the cost of doing business in Lebanon. The structural reform measures, which are summarized in Annexes I and II, have already had positive effects, but their full impact on growth will not be felt as long as the issue of the public debt overhang with its consequent effects on private investment is not resolved with external support.

31. *Growth and Exports.* The incentives that Government introduced in late 2000 and the reforms undertaken during 2001 and 2002 to stimulate growth and exports have helped to reverse the downward trends. While overall growth has remained modest— with real GDP growth of about 2% in 2001 and 2002—, export performance has been encouraging, with exports increasing by 25% in 2001, despite a weak international economy following the nine-eleven events, and at a rate of 19% during 2002 to-date.

32. Although exports grew from low levels, the increases registered over the past two years (in the context of a sluggish world economy) suggest that Lebanese exports can be competitive provided structural constraints are addressed, as Government is committed to doing. In this context, the Association Agreement with the EU that was concluded in early 2002 will greatly help Lebanon realize its export potential. By far the greatest constraint now remaining to accelerated growth are the high levels of public sector borrowing which crowd-out the private sector and the high levels of interest rates that deter non-financial investments. Building on the progress that has been made during 2001-2002, the Government's program for 2003 and beyond aims at removing this key constraint to growth.

33. *Recent Developments.* Despite the signs of some recovery in terms of GDP growth and exports, the economic and financial situation has been difficult in 2001 and the first part of 2002. A host of factors contributed to significant pressures on BdL's international reserves and pushed interest rates on new Government debt upward. On the domestic side, delays in enacting the legislation required for the privatizations, and the increased Central Bank financing of the Government, reduced confidence that Lebanon's debt situation would be resolved notwithstanding Government's stated commitments. A number of external factors compounded the situation, including the perception that the Paris I meeting had not resulted in specific commitments to support Lebanon, as well as the 9-11 events and their immediate aftermath and impact on economies and financial markets around the world.

34. Since about the middle of 2002, there has been a reversal of the negative trends, resulting again from a combination of domestic and external factors, with some recovery of reserves. The fiscal outcome for 2001 and for 2002 to-date (including in particular the successful introduction of the VAT) and the enactment of legislation allowing for privatization in the telecommunications and power sectors, reflecting the national consensus that had finally evolved, demonstrated the seriousness of Government's intentions with respect to fiscal adjustment and privatization. Geopolitical developments subsequent to the 9-11 events increased the interest of regional investors in Lebanon, and the de-listing of Lebanon by the Financial Action Task Force (FATF), after the adoption of a strict new law for fighting of money laundering, enhanced the international standing of Lebanon's banking system. Finally the successful Francophone Summit in October 2002 and indications that a Paris II meeting would indeed be convened before year's end further improved market sentiment and enhanced confidence. Nevertheless, these recent trends can only be sustained if public debt levels are reduced by a combination of further fiscal adjustment, as envisaged in the 2003 budget, major privatizations and external support, as was also concluded by the recent IMF 2002 Article IV Consultations Mission (paragraph 36 below).

THE PROGRAM FOR 2003 AND BEYOND

35. *Introduction.* Government's strategy for addressing the debt situation reflects a major domestic effort to further increase public savings (increasing the primary surplus), while protecting expenditures for basic social services, and to reduce the stock of debt through privatization, complemented with a change in the composition of debt in order to reduce interest rates on the public debt and domestic interest rates generally, so as to

encourage private investment and growth. Lower interest rates will complement the public savings effort in bringing down the overall fiscal deficit, and thus the rate of accumulation of further debt. The Government also plans further reforms to underpin a resumption of growth, which would help bring down debt to GDP ratios. Structural reforms are also aimed at improving public sector performance, which would also lead to improved utilization of external project support already committed. External support is needed to ensure reductions in the cost of servicing the debt so as to bring the rate of growth of the stock of debt remaining after privatizations to levels that are lower than the rate of GDP growth.

36. The IMF Article IV Consultations mission that visited Lebanon in October 2002 has reviewed recent developments and the Government's program. The mission indicated that economic performance and confidence have improved significantly in recent months. It also noted that in the absence of actions to materially reduce the stock of debt and its servicing cost, these improvements would be short-lived and trends in the economy would remain unsustainable. In this context the mission noted that privatization and external support of the type requested at the Paris II meeting would be critical to the future evolution of the economy. The illustrative five-year scenario prepared by the mission based on the Government's program (with external support) indicated a significant upfront reduction in public debt and a downward path of the public debt ratio in the medium term. The mission stressed that the Government's strategy of fiscal adjustment and privatization would lead to a viable scenario only if external support of the magnitude and type requested at the Paris II Meeting would be forthcoming. It indicated that with the domestic effort and the external support in the magnitudes envisaged, public debt would be put on a downward path, and reductions in interest rates would contribute to a sustained improvement in growth performance. It noted that a viable alternative scenario to the Government's program with external support is not available. In this respect the mission welcomed the Government's planned approach to the Paris II Meeting.

37. *Fiscal Adjustment.* As mentioned above, the Government has set out to undertake a major fiscal adjustment, resulting thus far in an improvement in the primary fiscal balance by about 10% points of GDP since 2000. For 2002 as a whole the overall fiscal deficit is estimated at 15.6% of GDP, comprising a primary surplus of 2.6% of GDP and interest payments of 18.2% of GDP.

38. The budget for 2003 that has already been submitted to Parliament is an austerity budget that envisages a further 11% increase (from the estimated actual 2002 level) in Government total revenues, and a further reduction in the ratio of non-interest expenditures to GDP⁸. Expenditures are being reduced across the board, except for social sectors expenditures so as to protect those most affected by the worsening of the economic situation in recent years.

39. As in other countries, raising revenues in the context of slow economic growth is not an easy task, and it is compounded in the case of Lebanon by the inability to rely on additional import duties because of the commitments made in the context of the Association Agreement with the EU, and the high level of international oil prices which initially limits the scope for raising taxes on petroleum products beyond the increases already effected during 2001 and 2002. Nevertheless, with the full implementation of the VAT for the whole year in 2003, the effects of the income tax measures taken in 2001 and 2002 and the improved

⁸ The Government's budget does not include certain revenues and expenditures (e.g. expenditures by the Council for Development and Reconstruction—CDR—that are funded by external project loans). However, unless indicated otherwise, all references to revenues and expenditures in this document are to total revenues and expenditures (both budget and non-budget) as per definitions used in the IMF's Article IV Consultations Reports. The targets for fiscal adjustment and the various fiscal ratios are based on this comprehensive coverage of revenues and expenditures.

administrative and collection capacity for income taxes, additional property taxes, and a number of other measures, including increases in fees, a strong revenue effort will be undertaken in 2003. The Government is committed to further reducing expenditures in case of any shortfall in projected revenues in 2003. As a result the overall primary surplus is expected to rise further to 4.2% of GDP (representing an overall improvement in the primary balance by 11.8% points over 2000), and the overall deficit would be reduced further to 8.4% of GDP, predicated on a reduction in interest payments resulting from the implementation of the other components of the Government's program and the availability of external support.

40. The Government's target for 2004 is to reduce the overall fiscal deficit by more than half from the 2003 level, which would bring it down to below the level of nominal GDP growth⁹, while the target for 2005 is to bring the overall fiscal deficit down to about 1%, with overall balance in the budget¹⁰, (or well below the EU Maastricht Treaty target level). This compares to a deficit of close to 25% of GDP in 2000. With declining debt levels, it is envisaged that the overall fiscal deficit would be eliminated by 2006. These targets reflect significant further increases in the primary surplus—which is already high by international standards—, but at a somewhat more moderate rate after 2004 as public expenditures cannot be reduced much more if Government is to carry out, and improve, its basic functions, as well as the decline in interest rates that would result from debt reduction and substitution on account of the implementation of the privatization plans and the external support that is being requested for 2003. Whereas the improvement in the primary balance accounted for all of the reduction in the deficit during 2001-2002, the further reductions during 2003-2007 would result mainly from lower interest payments (see Table 2 below).

41. *Privatization.* Apart from the other benefits associated with the planned privatizations as discussed above, privatization is the main vehicle for initially bringing down the level of outstanding debt and the debt to GDP ratio. The components of the privatization program that are expected to contribute directly to a reduction in the stock of debt during 2003 include the telecommunications and power sectors.

42. In the case of telecommunications, the sale of licenses for two existing mobile systems to provide GSM and GPRS services for a period of 20 years is now underway. An information memorandum has been approved by Cabinet on October 24 and pre-qualification of bidders¹¹ is to take place in November with a view to inviting bids to be submitted before the end of 2002, and the transaction to be completed before the end of the first quarter of 2003. Bidders will be asked to offer for the license either without or with revenue sharing (of 40%) with the Government. The latter option has been added in part in view of the current difficult situation in the international telecommunications industry, so as to enhance investors' interest. While this option may bring disproportional lower privatization proceeds, it would allow Government to benefit to a larger degree from the future potential of the sector in Lebanon. Government would proceed to securitize its 40% share of revenues under offshore arrangements and the overall effect on the stock of public debt could well be greater than under the first option.

43. The ongoing fixed line operations of the Ministry of Telecommunications will be transferred to a new commercial corporation (Liban-Telecom) to be established in the second half of 2003, once the regulatory agency is operative. The (initially) public corporation will

⁹ Based on a conservatively projected recovery of real growth (see Table 2 below) with continued low inflation. Inflation as measured by the CPI is estimated at 4% in 2002, most of which reflects the one-time effect of the introduction of the VAT. Inflation as measured by the GDP deflator is about 2%. Inflation (GDP deflator) forecasts of about 2% for 2003 and beyond are based on the IMF mission forecast.

¹⁰ The budget excludes foreign financed expenditures by the CDR of about 1% of GDP.

¹¹ A total of 19 international and regional companies or consortia have expressed interest.

have a monopoly for five years and also receive a license for providing mobile services, using the infrastructure of the existing two systems. Government intends to sell a 40% share (the initial maximum envisaged under the law) to a strategic investor before the end of 2003. Once a track record has been established, Government would proceed to sell additional shares to private investors, as allowed for under the law. This is expected to enhance the value of the shares that initially remain with Government.

44. In the case of the power sector, Government will proceed to establish a commercial public corporation for power generation and distribution and one for transmission, transferring the assets of the EdL which currently owns and operates all of Lebanon's 2000 MW generating capacity and transmission, as well as most of the distribution. The generation and distribution company would have a monopoly on generation for seven to ten years, after which the sector would be opened up in line with current EU Directives. Establishment of the two companies, and a regulatory agency for the sector, is to take place during the first quarter of 2003, subsequent to which the Government intends to sell a 40% share (the initial maximum envisaged under the law) of the generation and distribution corporation to a strategic private investor before the middle of 2003. Government intends to contract operations of the transmission corporation with the same strategic investor. As in the case of telecommunications, Government would subsequently proceed to sell additional shares to private investors, as allowed for under the law, once a track record has been established.

45. Overall, based on current estimates, which are supported by the analytical work carried out by specialist firms engaged by Government, the total privatization proceeds, including a combination of outright sales and securitization, are expected to reach about US\$ 5 billion in 2003, which would be applied in full to Government debt reduction. As the privatizations are now underway, specific estimates of each transaction are not provided, as it could affect the bidding process. For 2004 and 2005, privatization proceeds in the order of US\$1 billion per year are envisaged, primarily from the subsequent sales of shares in the telecommunications and power corporations, as discussed above. These subsequent sales would result in further reducing the total debt to GDP ratio. Moreover, they would promote a deepening of Lebanon's capital market.

46. *Cost of Debt.* Levels of total public debt that exceed GDP are not unique to Lebanon, and indeed can be found also in a number of EU countries. What is unusual however is an interest burden equivalent to 18% of GDP (at current levels of debt and interest rates), which is simply not sustainable. The origin to this situation that evolved during a decade of reconstruction and recovery after a fifteen year war has been discussed above. At present, the average interest rate on outstanding domestic currency debt is close to 14%, while the average interest rate on foreign currency debt is a little over 9%, with a higher rate for domestic foreign currency debt. The average interest rate on total debt is about 12%, equivalent to a spread of around 1000 basis points over US\$ and Euro LIBOR rates. Given current rates in the domestic market, the cost of new debt is even higher.

47. As indicated in Table 1 above, domestic currency debt held by public institutions accounts for nearly one-third of total net domestic currency debt, and about one-fifth of total gross public debt as of end-September 2002, or about US\$5.9 billion. This debt currently carries full market rates, and, as all domestic debt, has relatively short maturities. The BdL held the equivalent of about US\$4.8 billion of total foreign and domestic currency debt. The Government and the BdL have agreed to reduce the level of this debt by the equivalent of US\$1.8 billion as of early 2003 as an offset against a special Government account held at the BdL representing the difference between the market and book value of Government assets, and to convert a similar amount (comprising a combination of domestic and foreign currency short term debt) into a long-term debt in US\$ at an interest rate of 4%.

48. **Private Sector Contribution.** In addition to the envisaged agreement with the BdL, the Lebanese private banking community has indicated its willingness to contribute to the major ongoing macroeconomic adjustment initiative through an interest cost reduction effort that complements the Government's program of fiscal adjustment, privatization and the external support. This could be achieved through voluntary reverse swap operations that reduce the rates on the existing stock of debt held by banks, and through a proactive role, on their part, in the Treasury paper market that would result in rates on new Government issues that reflect the impact of the overall adjustment. The mechanics of this contribution as well as its effect on interest rates and debt service will be detailed in a separate paper.

49. **Debt Reduction, Growth and External Support.** Lebanon's total net public debt is expected to reach US\$30.0 billion by the end of 2002, equivalent to 173% of GDP. With the implementation of the Government's plans for further fiscal adjustment (increases in the primary surplus), privatization, and the above-mentioned agreement with the BdL, debt reduction would take place in 2003 even in the absence of external support. As a result, rates on domestic currency borrowing could decline somewhat and spreads on foreign currency borrowing ease a little in 2003, but in the absence of external support, average interest rates on the debt would remain high (above 10%), and remain so after 2003. Therefore, only a very modest further reduction in the overall fiscal deficit would be feasible in 2004 and beyond, and the stock of debt would rise again from 2004, with the debt to GDP ratio remaining at close to one and half times GDP. Thus, the reductions in the debt to GDP ratio and in the cost of servicing the debt as a result of the Government's plans for fiscal adjustment and privatization, while sizable, are not enough, by itself, to create a virtuous cycle of debt reduction, lower interest rates, and growth, enabling sustained economic and social development. Table 2 below shows the scenarios that would evolve if the domestic effort is or is not complemented by external support in the amount and of the type requested as indicated in the section "External Support" below (page 18).

50. Without external support, the debt to GDP ratio would decline in 2003 as a result of the privatizations that are envisaged (albeit that privatizations are likely to yield less because of the greater country risk to be perceived by investors in the absence of external support), and the agreement with the BdL. The ratio would barely decline further thereafter, however, as interest rates would not decline further. Consequently, notwithstanding the improvements in the primary balance, further reductions in the overall fiscal deficit would be limited, and the overall deficit as a % of GDP would remain in excess of the rate of nominal GDP growth. Similarly private investment would remain constrained on account of the debt overhang and level of domestic interest rates, and consequently growth would be low, at best.

51. The above "without external support" scenario is a positive perspective on possible outcomes in the absence of external support. With large gross borrowing needs of the Government in 2003—because of the short term maturity of existing debt—, financial markets may in the absence of demonstrated external support again turn negative, and consider the Government's program not to be feasible in terms of reaching its basic objective of resolving the debt dilemma. The resulting Government reliance on financing of part of its deficit by the Central Bank could put further pressure on reserves and interest rates. Subsequently, this could undermine financial and economic, as well as social and political, stability.

Table 24 Fiscal Developments and Public Debt, 2002-2007

| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|--|-------------|------------|------------|------------|-------------|-------------|
| without external support ^a | | | | | | |
| GDP (US\$ billion) | 17.3 | 18.0 | 18.8 | 19.6 | 20.4 | 21.2 |
| real GDP growth | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% |
| fiscal deficit (% of GDP) | 15.6 | 13.0 | 8.5 | 7.0 | 5.7 | 4.6 |
| total net debt (US\$ billion) ^b | 30.0 | 26.3 | 26.9 | 27.2 | 27.8 | 28.2 |
| net debt to GDP ratio (%) | 173 | 146 | 143 | 139 | 136 | 133 |
| with external support ^c | | | | | | |
| GDP (US\$ billion) | 17.3 | 18.2 | 19.2 | 20.3 | 21.4 | 22.7 |
| real GDP growth | 2.0% | 3.0% | 3.0% | 3.5% | 3.5% | 4.0% |
| nominal GDP growth | 4.0% | 5.1% | 5.6% | 5.6% | 5.6% | 6.1% |
| as % of GDP | | | | | | |
| Primary fiscal surplus | 2.6 | 4.2 | 6.1 | 7.4 | 8.3 | 9.1 |
| Interest on public debt | 18.2 | 12.6 | 9.5 | 8.2 | 7.4 | 6.4 |
| fiscal deficit | 15.6 | 8.4 | 3.4 | 0.8 | -0.9 | -2.7 |
| budget deficit ^d | 14.9 | 7.6 | 2.6 | 0.0 | -1.6 | -3.4 |
| US\$ billion | | | | | | |
| fiscal deficit | 2.7 | 1.5 | 0.6 | 0.2 | -0.2 | -0.6 |
| privatization | 0.0 | 5.0 | 1.2 | 1.3 | 0.7 | 0.7 |
| total net debt ^b | 30.0 | 24.7 | 24.2 | 23.1 | 22.2 | 21.0 |
| consolidated net debt | 25.2 | 21.7 | 21.2 | 20.1 | 19.2 | 18.0 |
| net debt to GDP ratio (%) | 173 | 136 | 126 | 114 | 104 | 92 |
| consolidated net debt (%) | 138 | 113 | 104 | 94 | 85 | 74 |
| Interest rate public debt % ^e | 12.0% | 8.0% | 7.0% | 6.5% | 6.5% | 6.5% |
| Interest savings (US\$ million) | | 1144 | 1286 | 1369 | 1316 | 1257 |
| o/w from external support | | 704 | 729 | 803 | 741 | 673 |

(a) This scenario assumes the same improvement in the fiscal primary balance as the scenario with external support, but privatization proceeds at 15% less because investors are likely to reflect a greater country risk in their offers.

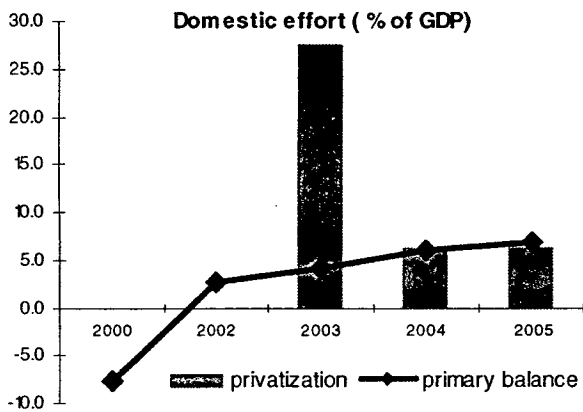
(b) Excluding accrued interest on discount Treasury Bills

(c) The scenario that is presented here for 2003-2007 is basically the same as the scenario developed by the IMF Article IV Consultations mission based on the Government's program, except that: (i) privatization and securitization proceeds are US\$250 million higher in 2003, and include the further sale of all remaining shares in the telecommunications and power corporations during 2004-2007; (ii) the debt is US\$1.8 billion lower in 2003 on account of the agreement with the BdL; and (iii) most importantly, that overall fiscal adjustment is greater, as the average rate of interest on public debt is projected to decline more in 2003 and to continue to decline through 2004-2006, and hence, reductions in the debt are at a faster rate.

(d) Equals fiscal deficit less foreign financed expenditures by the CDR

(e) The 2002 rate is of end September.

52. With external support, the request for which is summarized on page 18, Lebanon



would be in a position to substitute US\$5 billion in external debt, contracted at terms (interest rates and maturities) available to prime sovereign borrowers, for existing public debt (with an average rate of 12% as of end-September 2002). Just by itself, this substitution would have an immediate effect of savings in interest in the order of US\$400 million per annum (over 2% of GDP)¹². However the combination of continued fiscal adjustment and privatization, in 2003 and beyond, along the lines discussed above (and shown in the graph above), and the

external support would bring about a steady reduction in the debt to GDP ratio and interest rates on the public debt. While the total interest savings in the order of US\$1.25 billion a year on average during 2003-2005 are the result of the combined and mutually reinforcing effect of the domestic effort and the external support, the with and without external support scenarios indicate that over half of it, or around \$725 million a year on average during 2003-2005, is attributable to the external support. Underpinned by the structural measures that have been taken, the reduction in interest rates of the magnitude that would result with external support would contribute to a recovery of growth to at least the conservatively projected levels indicated in Table 2, thus further enforcing the downward trend in debt indicators.

53. Except for the projected real GDP growth rates, which are modest, the scenario of steadily declining interest rates (during 2003-2005), sharp reductions in the overall fiscal deficit and declining debt stocks and ratios, as discussed above and presented in Table 2, represents an achievable and sustainable outcome in the case that external support is provided in the magnitude and nature envisaged (paragraph below)¹³. If the amount of the support in 2003 were to be much less, or the terms much harder, larger public borrowing in the domestic market and higher interest rates would limit the decline in the overall fiscal deficit and the stock of public debt could not be reduced after 2003, while private investment and growth would not take off. Lebanon would find itself in a “muddling through” situation at best, unable to realize its growth potential, and vulnerable to possible shocks arising from changes in confidence, with its effects on domestic financial markets, or exogenous events.

¹² This estimate is based on the average interest rate on debt of 12% as of end-September 2002 and an interest rate of 4% on the debt instruments of the external support. The immediate impact would be larger (as much as \$500 million) to the extent that these instruments substitute for domestic currency debt that had an average rate of 14%.

¹³ To check the robustness of the scenario a sensitivity analysis was done that assumed interest rates at 0.5% point higher, privatization proceeds at 10% less, and the improvement in the primary fiscal balance at 1% of GDP less in 2004 and 2005. With a combination of all those factors, the fiscal deficit would be eliminated by 2007, debt stocks would not rise after 2003, and the debt to GDP ratio decline, albeit slower.

54. Table 3 below shows the composition of the total gross public debt as of end-September 2002 in some detail.

| Table 3 Composition of Public Debt (end-2002) | |
|--|------|
| (US\$ billion) | |
| Total gross public debt ^a | 31.3 |
| Total gross debt held by public sector | 5.8 |
| o/w BdL | 3.7 |
| o/w Other institutions | 2.1 |
| Total gross debt held by private sector | 25.5 |
| FX debt, excl. public sector | 11.8 |
| LL debt, excl. public sector (gross) | 13.7 |
| LL debt, excl. public sector (net) | 13.4 |
| Consolidated public sector debt (net) | 25.2 |

(a) The net public debt (gross less public sector deposits) is US\$ 30 billion, excluding accrued interest on discount Treasury bills.

The projected end-2002 public debt is US\$31.3 billion gross (and US\$30.0 billion net). The stock of debt will be reduced by US\$1.8 billion in early 2003 on account of the agreement with the BdL (paragraph 47). For 2003, Government's financing needs for its budget (a fiscal deficit equivalent to \$1.5 billion) would be met primarily by new, mainly domestic, debt contracted at lower rates (in addition to disbursements from existing external project loans). *The external support that is requested and the privatization*

and securitization proceeds would be earmarked for paying off debt held by the private sector (primarily commercial banks) that matures in 2003 and other high interest debt. In particular paying off maturing domestic debt is expected to contribute to the projected decline in interest rates that would underpin the recovery of growth in conjunction with the structural measures that are in place and underway.

EXTERNAL SUPPORT

55. In order to create a virtuous cycle leading to sustained economic and social development, Lebanon needs the support of the external community to complement its major domestic effort now underway. The domestic effort includes a 16% of GDP fiscal improvement during 2001-2003 and privatizations, to be applied to Government debt reduction, in an amount of about US\$5 billion in 2003. This reduction in debt is separate of Paris II proceeds.

56. Lebanon devotes 80% of rising Government revenues to pay interest on its net debt of about US\$30 billion. The Government of Lebanon realizes that the support it is requesting will not be available in the form of grants and soft loans from bilateral and multilateral sources in the magnitude that would be required and for the purpose of changing the composition of its debt. Government therefore requests external support to change the composition, reduce the cost, and lengthen the maturity of its debt through instruments such as sovereign guarantees, investments by Governments and Central Banks in new Lebanese Government foreign currency bonds, and similar arrangements, for a total amount of US\$5 billion in 2003, that would allow Lebanon to borrow in supporting countries' markets at low spreads, using the proceeds solely to substitute such external debt for existing high interest short-term debt. Such substitution would result in a sharp reduction in the level of domestic interest rates, with a consequent further reduction in the overall fiscal deficit and financing needs. It would sharply reduce the Government's gross financing needs for 2003 and 2004 and significantly improve the maturity profile of the debt. It would, through lower interest rates and increased availability of financial sector domestic financial savings for the private sector, also help trigger a revival of private investment to underpin a recovery of GDP growth.

57. *In order to allow Government to achieve a sustainable reduction of its fiscal deficit and a recovery of growth, the request for the terms of the support in the amount of US\$5 billion is for long term maturities, with a grace period of five years (for principal only), during which time the Government intends to eliminate the overall fiscal deficit, and a repayment period of 10 years, during which time Governments expects to generate fiscal surpluses in the amount of the support, at interest rates similar to the supporting countries' cost of domestic or external borrowing, which are estimated at around 4% on average. These surpluses will be used to repay the obligations arising from Paris II.*

58. ***Special Account for debt service.*** Government has established by law a special treasury account at the Central Bank that is earmarked exclusively to service the interest and principal of outstanding debt obligations including forthcoming resources from the Paris II process. The above-mentioned law stipulates that all privatization and securitization proceeds must be channeled fully to this account for the exclusive purpose of debt reduction. Also, the law stipulates that all primary surpluses will be channeled to this special account for the purposes of meeting Lebanon's debt service obligation. In addition, Government is committed, fully, to introduce additional revenue measures to ensure that debt service obligations are met in a timely and orderly fashion. This special account provides a transparent and monitorable mechanism of Government's ability to meet its outstanding obligations.

59. The International Monetary Fund has reviewed the Government's program on the occasion of the recent Article IV Consultations. It has indicated that the Government's strategy of fiscal adjustment and privatization would lead to a viable scenario only if external support of the magnitude and type requested at the Paris II Meeting would be forthcoming. It concluded that with the domestic effort and the external support in the magnitudes envisaged, public debt would be put on a downward path, and reductions in interest rates would contribute to a sustained improvement in growth performance. It also noted that a viable alternative scenario to the Government's program with external support is not available. The Government of Lebanon therefore hopes that participants at the Paris II Meeting will agree to ensure that a viable scenario of stability and growth will ensue in Lebanon.

LEBANON: PARIS II MEETING

BEYOND RECONSTRUCTION AND RECOVERY..... TOWARDS SUSTAINABLE GROWTH

POSTSCRIPT

Lebanon 2005

After Five Years of Adjustment, Reforms, and External Support—A Vision

By the time of the Paris II Meeting in late 2002, Lebanon faced the prospect that economic stability could be undermined, notwithstanding the adjustment and reforms that had been undertaken since late 2000, arising from a large debt overhang that had accumulated as the country had recovered during the 1990s from 15 years of war. Rising outlays for interest on public debt absorbed an increasing share of rising revenues and of Government expenditures. There was a possibility that, in the absence of a reversal of trends with external support, sustained social stability could be at risk. The Government's program for further fiscal adjustment, large privatizations, and reforms, despite its scope and depth, by itself was unlikely to result in a resolution of the debt dilemma and sustainable growth.

The external support that was provided in late 2002 and early 2003 (mainly in the form of financial instruments that enabled Lebanon to substitute debt at market terms of the supporting countries for part of its high interest short term, mainly domestic, debt), in conjunction with the implementation of the Government's program for further fiscal adjustment, privatization, and structural reforms, had led to a steady reduction in the cost of servicing the debt and declining debt ratios from 2003 onwards.

By 2005, the budget was in balance and the overall fiscal deficit had been nearly eliminated, and the debt to GDP ratio had fallen since 2002 by the equivalent of more than to half of total GDP. Most of the public infrastructure services were operated by the private sector, which owned large parts of them. Government no longer required access to concessional external loans or to the Central Bank, and did not need to absorb the bulk of savings in Lebanon's financial system, to meet its steadily declining financing needs. Interest rates had fallen sharply and, with the private sector no longer crowded out by public sector borrowing needs and structural reforms to liberalize the economy and support the private sector in place, private investment was booming. International trade and services blossomed in a liberal trade environment, with close ties to the EU, and regional investors had put their confidence in a modern version of the Lebanon they had known in the 1960s and early 1970s. GDP growth was accelerating and per capita incomes were steadily rising, and with Government focusing on its basic functions and essential social programs, sustainable broad based socio-economic progress was being made. There were good prospects that in real terms Lebanon's per capita income would by about 2010 recover to the pre-war level.

Annex I Paris II Meeting

The Government's Program for 2003 and Beyond

| Objectives | Background and Status | Key Targets |
|--|--|---|
| Reducing Public Debt and Interest Rates | Rising levels of public debt, much of it accumulated during 10 years of reconstruction and recovery, have created a vicious circle of high fiscal deficits, rising interest rates, declining private investment, and economic stagnation. | Fiscal deficit was 25% of GDP and real GDP growth 0 in 2000. |
| Fiscal Adjustment | The primary fiscal balance has improved by 10% points of GDP during 2001-2002 on account of a major revenue effort, particularly with the introduction of the VAT and expenditure control, including restructuring of public entities. | Primary balance from deficit of 7 ½% of GDP in 2000 to surplus of 5% in 2003 |
| Privatization | Further increases in primary surplus, particularly in 2003 (budget approved by Cabinet) on account of continued revenue effort (in particular VAT and income taxes) and reductions in expenditures (including reductions in public employment), facilitated by planned privatizations, so as to reduce the overall fiscal deficit to below EU norms by 2005 and eliminate it by 2006. Reduction is predicated on reducing interest rates on public debt with external support to complement the fiscal adjustment and privatization. | Overall fiscal deficit: -10% in 2003 -1% in 2005 -surplus in 2006 |
| External Support | Public sector had traditionally operated basic public services, and reconstructed infrastructure after the war. Level of services has remained substandard, cost recovery has been insufficient, and all sectors, except for telecommunications have been a significant drain on the budget. An outdated legal framework and lack of political support were not conducive to privatization. A national consensus on an increased role of the private sector has now evolved. | Parliament adopted legislation in 2002 to allow privatization in telecommunications and power sectors |
| External Support | Telecommunications and power sector are key to short-term debt reduction on account of privatization because of size of assets and investors' interest. | Target of US\$5 billion in privatization and securitization proceeds in 2003, and about US\$1 billion per year 2004-2005: -Sell mobile licenses first quarter 2003 -Sell 40% of power corporation first half 2003 -Sell 40% of telecom corporation second half 2003 -Sell remainder 2004-2007 |
| External Support | --Sale of two mobile system licenses is now underway --Corporatization of telecommunications company, and unbundling and corporatization of power company, and establishment of regulatory agencies is now being prepared prior to privatization | Award concessions during 2004-2005 following establishment of legal framework in 2003 |
| External Support | Privatization of water sector and ports and airports through concession arrangements are being planned for 2004-2005 | During first half 2003 Reduction in interest rate on public debt by about one-third in 2003 and 1% more in 2004 |
| External Support | Substitution of US\$5 billion in external debt at | |

| | | |
|--|--|--|
| | <p>prime market terms for existing high interest debt, through guarantees, Central Bank deposits, investments in Lebanese Government bonds and bills, and similar arrangements requested at Paris II meeting</p> | |
|--|--|--|

| Objectives | Background and Status | Key Targets |
|------------------------------------|---|--|
| Promoting Growth | After a rapid recovery of the economy during the first half of the 1990s, GDP growth slowed down, reflecting the effects of the evolving fiscal deficit and debt situation, as well as the structural constraints. Concurrently with the implementation of a debt reduction strategy, Government is taking structural measures that lay the basis for a recovery of sustained growth, once the key constraint to private investment—excessive public sector domestic borrowing and high interest rates—is removed as a result of the fiscal adjustment, privatization and external support. | Real GDP growth at 0 in 2000 and low growth in 2001-2002 |
| Trade Liberalization | | |
| <i>International Agreements</i> | Lebanon's traditional liberal and open trade regime, a model in the 1950s and 60s, had not adapted to the global developments in trade that had taken place during the war, and the legal framework had become outdated. This limited the effort to reestablish Lebanon as a center for regional trade and provision of services and a link between the region and Europe. | Increase in exports to GAFTA area Increase in exports to EU |
| <i>Modernizing Legal Framework</i> | Lebanon became a member of the <u>Greater Arab Free Trade Area</u> (GAFTA) in 1997, which is now in its 6th year of tariff dismantling. An <u>Association Agreement with the EU</u> was completed in January 2002 and signed in June 2002. Pending ratification of the agreement by all States, an interim trade agreement is already in effect which provides for duty free access of all industrial exports, and most agricultural and agro-industrial exports from Lebanon. Because of the heavy reliance on import tariffs for fiscal purposes, and the difficult fiscal situation, Lebanon has a five year grace period for dismantling its tariffs. Lebanon is seeking membership to the <u>World Trade Organization</u> . The first Working Party meeting was held in October 2002 A new, WTO-compatible Customs Law was enacted in June 2001 which, among others, simplifies procedures and introduces modern information technology for customs declarations, and international standards for clearance. Imports of oil were liberalized in 2001 and legislation to liberalize imports pharmaceuticals was submitted to Parliament Legislation is under preparation to abolish exclusive agencies and commercial representation, which limit competition, and to streamline licensing requirements for trade. Competition law and consumer protection law being prepared A number of other laws are being prepared in line | WTO membership Present to Parliament early 2003 Present draft legislation in conjunction with WTO membership to Parliament |

| Objectives | Background and Status | Key Targets |
|---|---|--|
| <p>Promote Private Investment</p> | <p>A new Investment Promotion Law was adopted in August 2001. The Investment Development Authority of Lebanon (IDAL) has been designated as a "one-stop shop" to support investors. The law provides financial and tax incentives depending on the location (in one of three investment zones in the country), size of investment, and type of activities, with the most incentives for information technology projects</p> <p>The laws for the telecommunications and power sectors that were adopted in 2002 (see above), and the laws that are being prepared for the water sector will increase private investment in basic infrastructure</p> <p>A Foreign Ownership Law was adopted in March 2001 that eases limits on foreign ownership of land</p> <p>A Money Laundering Law was adopted in April 2002 to meet requirements of FATF, resulting in Lebanon being de-listed. This enhanced international standing of Lebanese banking system. Law on bank shares (April 2002) facilitates trading in shares of Lebanese banks.</p> | <p>Increase in investments in sectors other than real estate by regional investors, and, supported by the Association Agreement, a major increase in number of European investors</p> <p>Establish regulatory agencies in first half of 2003. Limit role of Government in public services to regulator only by 2005</p> <p>Increased financial investments, particularly from region</p> <p>Increase share of private sector in total banking system credit, with sharp increase in credit to SMEs</p> |
| <p>Improve Public Services and Reduce Cost of Business</p> | <p>Private investment is limited by access to domestic credit and high interest rates, as well as conservative nature of Lebanese banking system. In particular SMEs, which offer the largest potential for employment growth, are affected. In early 2001 Government increased loan limits in "Kafalat" guarantee scheme and introduced interest rate subsidies for SMEs.</p> <p>Large segments of the public coast around the Beirut area have been illegally developed during the war. This had had negative environmental effects and discouraged new investments in tourism. Government is preparing legislation for the settlement of violations of public coastal properties, which will also result in additional Government revenues.</p> <p>The privatization of basic public services will improve the quality of services, and through greater efficiency and improved cost recovery from non-business consumers, reduce the costs of provision of basic services to business</p> <p>Public institutions remain weak. A program of administrative reform supported by the EU, the Arab Fund and the World Bank is underway. The more limited role of Government in the economy will allow Government to deploy its scarce human and financial resources to improving the provision of basic functions of the State. This is a medium term endeavour.</p> <p>A new public accounting law, streamlining budgetary procedures and strengthening treasury controls, and a</p> | <p>Government revenues from 2003, and new tourism investment in areas concerned from 2004.</p> <p>No claims on budget for basic public services from 2004</p> |

| | | |
|--|---|--|
| | <p>procurement law, incorporating best international practices, so as to increase transparency and competition, have been presented to Parliament.</p> <p>Employers' contributions of 38.5% of wages to the National Social Security Fund have been reduced in March 2001 to 23.5% so as to encourage employment creation and reduce business cost</p> <p>Temporary subsidies are being provided under the "Export Plus" program adopted in June 2001 to exporters of fresh produce to reduce transportation costs. At the same time, subsidies to sugar beet production were abolished in early 2001</p> | |
|--|---|--|

**ANNEX II PARIS I MEETING
GOVERNMENT OF LEBANON**

A MATRIX OF STRUCTURAL REFORMS¹⁴

Measures Already Adopted (December 2000-February 2001)

| MEASURE | ACTIONS | IMPACT | STATUS |
|-------------------------------------|--|--|---------------|
| 1. State Media Reform | <ul style="list-style-type: none"> Lay off 500 workers from Tele-Liban, cancel workers collective bargaining contracts and restructure the sector | <ul style="list-style-type: none"> Contain public expenditures | done |
| 2. Civil Service Reform | <ul style="list-style-type: none"> Reassign surplus workers to Civil Service Board and fill new civil servants posts through the Board | <ul style="list-style-type: none"> Restrict the growth of public sector employees and contain expenditures | done |
| 3. Customs Tariff Reduction | <ul style="list-style-type: none"> Reduce effective customs tariff from 12% to 6% | <ul style="list-style-type: none"> Liberalize trade and reduce the price level in the economy | done |
| 4. Customs Law | <ul style="list-style-type: none"> Simplify and streamline customs procedures | <ul style="list-style-type: none"> Facilitate trade | done |
| 5. Investment Law | <ul style="list-style-type: none"> Create a one-stop-shop for investors, provide tax breaks and financial incentives to projects, and create investment zones | <ul style="list-style-type: none"> Attract and raise the level of investments | done |
| 6. Open Skies Policy | <ul style="list-style-type: none"> Introduce competition and provide unrestricted entry into Lebanon | <ul style="list-style-type: none"> Render Beirut International Airport as regional travel hub Lower airfares | done |
| 7. Land Acquisition by Non-Lebanese | <ul style="list-style-type: none"> Provide greater access for non-Lebanese to acquire real estate property and lower registration fees | <ul style="list-style-type: none"> Enhance investment in the real estate sector | done |
| 8. Public Accounting Law | <ul style="list-style-type: none"> Streamline and simplify budgetary procedures and strengthen treasury functions | <ul style="list-style-type: none"> Facilitate Central Government financial activities | done |
| 9. Money Laundering Law | <ul style="list-style-type: none"> Take new measures to guard against money-laundering activities | <ul style="list-style-type: none"> Comply with international standards and regulation for combating money laundering activities | done |
| 10. Sugar Beet Subsidies | <ul style="list-style-type: none"> Terminate subsidies on sugar beet and wheat production | <ul style="list-style-type: none"> Liberalize agricultural sector and reduce expenditures | done |

¹⁴ As presented to Paris I Meeting. Page 2 provides the status of measures that were to be adopted during March 2001-December 2002, and Page 3 lists other measures taken during March 2001-October 2002, not included in Matrix as presented to Paris I Meeting

Measures To be Adopted (March 2001-December 2002)

| MEASURE | ACTIONS | IMPACT | STATUS |
|--------------------------------------|---|---|--|
| 1. Value Added Tax | <ul style="list-style-type: none"> VAT draft law approved by COM VAT law ratified by parliament VAT Implementation | <ul style="list-style-type: none"> Enhance revenue collection and widen the tax base | Implemented VAT first quarter 2002 |
| 2. Global Income Tax | <ul style="list-style-type: none"> Draft law presented to COM Law ratified by parliament (2003) Implementation of law (2004) | <ul style="list-style-type: none"> Improve tax collection capabilities Expand taxpayer base Streamline tax collection | Draft law being prepared. Tax to be effective 2004 |
| 3. Privatize Middle East Airlines | <ul style="list-style-type: none"> Strategy presented to COM Staff redundancy package Initiation of privatization of MEA | <ul style="list-style-type: none"> Resolve MEA high-wage bill Limit expenditure drain | Restructuring, including lay-offs completed. Airline now profitable. |
| 4. Privatize Telecom Sector | <ul style="list-style-type: none"> Telecom law approved by COM Telecom law ratified by parliament Settlement of contractual disputes with Cellular Operators Convert BOT into licenses Parliamentary approval of license agreements Initiate privatization of Liban Telecom | <ul style="list-style-type: none"> Improve efficiency Allow for the introduction of state-of-the-art technology Lower rates Generate revenues for debt retirement | Law approved. Sale mobile licenses underway. Liban Telecom and regulatory agency being created. Privatization 40% 2003. |
| 5. Privatize Electricite du Liban | <ul style="list-style-type: none"> Approval by COM of draft law to convert EDL into a joint stock company Ratification of draft law by Parliament Initiate tender for management contract and 10% equity share | <ul style="list-style-type: none"> Limit expenditure drain Improve provision of services Generate revenues Eliminate leakages | Law approved. Companies and regulatory agency being created. Privatization 40% 2003 |
| 6. Privatize Water | <ul style="list-style-type: none"> Beirut Water Authority concession approved by COM Beirut Water Authority concession ratified by Parliament Tripoli Water Authority concession approved by COM Tripoli Water Authority concession ratified by Parliament | <ul style="list-style-type: none"> Enhance effective cost recovery Revenue generation Enhance efficiency | Draft legislation allowing concessions approved by Cabinet |
| 7. Reform of the Army Pension Scheme | <ul style="list-style-type: none"> Readjust army retirement benefits and settle accrued retroactive benefits | <ul style="list-style-type: none"> Reduce current expenditures and drop in future liabilities | Done |
| 8. Social Security Reform | <ul style="list-style-type: none"> Reduce social security contributions, settle arrears and provide alternative schemes | <ul style="list-style-type: none"> Retire contingent liabilities, lower cost of labor and promote employment | Done (from 38.5 to 23.5%) |
| 9. Municipality Law | <ul style="list-style-type: none"> Promote decentralization and normalize financial accounts of municipalities | <ul style="list-style-type: none"> Provide efficient municipal services with positive fiscal externalities | Draft legislation presented to Parliament |
| 10. Euro-Med Trade Agreement | <ul style="list-style-type: none"> Sign the Euro-Med Trade Agreement, accede to the WTO and execute GAFTA | <ul style="list-style-type: none"> Liberalize trade and generate economic growth | EU agreement signed June 2002 WTO Working Party held Oct. 2002 |

Other Measures Adopted (March 2001-October 2002)

| MEASURE | ACTIONS | IMPACT | STATUS |
|--|---|--|-------------------|
| 1. Establish Special Accounts for Debt Management | Law adopted May 2002 allowing Government to open special accounts for privatization proceeds and revenues to be used for securitization, and for loans, all to be used solely for debt reduction and substitution | <ul style="list-style-type: none"> • Reduce stock of debt • Improve structure of debt • Lower interest rates | done |
| 2. Settlement of violations of public coastal properties | Draft law presented to Parliament (September 2002) | <ul style="list-style-type: none"> • Environmental protection of coast • Promote tourism investment • Additional fiscal revenues | done |
| 3. Liberalize oil imports | Government decision effective February 2002 | <ul style="list-style-type: none"> • Reduce cost of imports of oil and oil products | done |
| 4. Liberalize imports of pharmaceuticals | Draft Law approved by Cabinet (February 2002), now being considered in Parliament | <ul style="list-style-type: none"> • Lower prices through increased competition • Lower cost of private and public health care | done |
| 5. Abolish Exclusive Agencies | Draft legislation approved by Cabinet, now being considered in Parliament | <ul style="list-style-type: none"> • Lower prices resulting from increased competition | done |
| 6. Guarantee scheme for loans to SMEs | Approved by Cabinet in February 2002 and operative for selected loans by private banks | <ul style="list-style-type: none"> • Increased access by SMEs to investment credits • Increase in SME investments • Employment generation | done |
| 7. Interest rate subsidies for SMEs | Effective January 2002 for limited amounts in selected sectors | <ul style="list-style-type: none"> • Increase in SME investments • Employment generation | done |
| 8. Export Plus Program | Effective August 2001. Provides limited subsidies to exports of fresh produce to compensate for high cost of transportation and provides for quality control | <ul style="list-style-type: none"> • Increased exports • Employment generation, particularly in rural areas | done |
| 9. Law on banks shares | Effective April 2002. Facilitates trading in shares of Lebanese banks | <ul style="list-style-type: none"> • Increased foreign investment in financial sector | done |
| 10. Professional tax | Tax effective after the ratification of tax regularization law (budget 2002) | <ul style="list-style-type: none"> • Increased revenue | done |
| 11. Tax regularization | Law ratified by Parliament (budget 2002) | <ul style="list-style-type: none"> • Increased revenue | done |
| 12. Securitization of the customs revenues from Tobacco | Under preparation | <ul style="list-style-type: none"> • Debt retirement • Interest payment reduction • Fiscal consolidation | Under preparation |

Bibliography

Abu Khalil, A. (1994) 'Determinants and characteristics of Syrian policy in Lebanon', in: D. Collins (Ed), *Peace for Lebanon: From War to Reconstruction* (New York, Lynne Rienner)

Al Anbaa (Kuwait), "Lebanon's way to freedom", 23 April, 2005.

Al Massira, Beirut, 275 August 2004

Al Moustakbal, Beirut in a special document published in October 15, 2000; October 24th, 2000

Al Safir (Beirut) November 25th 2004

An Nahar, Beirut, 19/6/1994, July 12, 2000; April 23, 2003; 21st December, 2004; august 4th, 2002

Banque du Liban: the official bank of the state.

Beetham, D. (1992) *the Legitimation of Power* (London Macmillan Education).

Bennis and Bert, "*trust in leadership and team performance*", journal of psychology, 85, 6 (2001)

Bert Frydman, Iva Wilson, Joanne Wyer (2002) *the power of collaborative leadership: Lessons for the learning organization* (London, Butterwoth)

Bok, D. (1997) '*Measuring the performance of government*', in J.S.Nye, Jr., P.D. Zelikow and D.C.King (Eds), *Why People Don't Trust Government* (Cambridge, Harvard University Press).

CNN special edition Christmas 2000/inside Asia, 2000.

Colin Powell Speech, M. Al Barazi, *Chourakaa fi ightiyal al Hariri* (partners in Hariri's killing) Middle Eastern Center for Strategic Studies ,1st edition (2005).

Collins, D. (1994) '*Peace for Lebanon? Reflections on a question*', in: D. Collins (Ed).*Peace for Lebanon: From War to Reconstruction* (New York, Lynne Rienner)

Cook, J. and Wall, T. (1980), *New work attitude measurer *****, organizational commitment, and personal need fulfillment. *Journal of occupational psychology*.

Crow, R. (1962) '*Religious sectarianism in the Lebanese political system*', *Journal of Politics*, 24(3).

D. Hamadeh "*Rafiq Hariri: role profile*" for the university of Texas, USA, 23rd march 2001.

Dasgupta, P. (1988) '*Trust as a commodity*', in: D.Gambetta (Ed), *Trust: Making and Breaking Cooperative Relations* (New York, Basil Blackwell)

David MC Callend: "*socialized power motive*", *Journal of applied psychology*, 16.5(2001)

Deputy Mohammad KABANI in a special interview on *Future T.V.*, Sunday 21st May, 2005

E. Yulk, *transformational leadership*, *journal of applied psychology* (1992)

E.A Lock "*do trait matters?*" *Academy of management executive*, 5, 2(1991)

El -Khazen F. (1993) '*The making and unmaking of Lebanon's political elites from independence to Taïf*': *TheBeirut Review*.

El-Hoss, S. (1992) '*Horizons of perspective change in Lebanon*', *The Beirut Review*, 3.

El-Khazen F. (1992) '*Lebanon's communal elite-mass politics*', *The Beirut Review*, 3.

Fukuyama, F. (1995) *Trust: The Social Virtues and the Creation of prosperity* (New York, Free Press)

Gambetta, D. (1998) 'Can we trust?' in: D.Gambetta (Ed), *Trust: Making and Breaking Cooperative Relations* (New York, Basil Blackwell)

Ghassan Diba, "Al-Bu'd al-ijtima'I wa al-inma'I fi siyasat al-ifaq" (The Social and Developmental Dimension in the Expenditure Policy), Ab-aad 6 (May 1997).

Hamdan K. (1997); *Le Conflit Libanais: Communautés Religieuses, Classes Sociales et Identités Nationales* (Paris Garnet Editions)

Harik, I. (1972) 'The ethnic revolution and political integration in the Middle East', *International Journal of Middle Eastern Studies*, 3.

Harik, I. (1975) 'Political elite of Lebanon', in: G.Lenczowski (Ed), *Political Elites in the Middle East*.

Hariri cultural Center Hariri (2003) *Hariri's Government, principal decisions and actions* (Paris, Hariri cultural Center service of documentation)

Hariri's official site: www.rHariri.com

Hetherington, M.J. (1998) 'The political relevance of political trust', *American Political Science Review*, 92.

Hizbullah and the Amal movements both criticized as being the two only Shiit superpowers.

Hudson, M. (1968) *the Precarious Republic: Political Modernization in Lebanon* (New York, Random House)

J.M George: *emotions and leadership: the role of emotional intelligent*, Sage publications, LTD, Human relations, 2000, 53.8

Jon L. pierce, John W. Newstrom (2000) *leaders & the leadership process*, third edition (New York, Mcgraw-hill Irwin editions)

Khashan, H and Haddad, S. (2000) '*the coupling of the Syrian- Lebanese peace tracks: Beirut's options*', *Security Dialogue*, 31.

L;owenberg, G.(1971) '*The influence of parliamentary behavior on regime stability*', *Comparative Politics*, 3.

Lijphart, A. (1997) *Democracy in Plural Societies: A Comparative Exploration* (New Haven, Yale University Press).

Lipset S.M. (1981) *Poiltical Man: The Social Bases of Politics* (Baltimore, Johns Hopkins University Press)

M. Al Barazi, *Chourakaa fi ightiyal al Hariri (partners in Hariri's killing)* Middle Eastern Center for Strategic Studies, 1st edition (2005).

Maila, J. (1994) '*The Taïf Accord: an evaluation*', in: D. Collins (Ed), *Peace for Lebanon: from War to Reconstruction* (New York, Lynne Rienner)

Mansour, A. (1993) *Inqilab Ala Al-Taïf (Revolt Agaist Taïf)* (Beirut, Dar Aj-Jadid)

Marry parker Follett, (1973) "*Power*" in *dynamic administration: the collected papers of Marry parker Follett*, Elliot M. fox and L. Urwick, eds.(London: Pitman,1973)

Mayer & Salovey, 1997: 5: "*emotions*", *academy of manager executive*, 7.87(1989)

Middle East Intelligence Bulletin, Vol.4 No. 9 (September 2002)

Middle East Intelligent Bulletin, Vol4. No.9 (September 2002); Vol.8 No. 11 (September 2003); No.12 (October 2003)

Miller, A. (1974) '*Political issues and trust in government: 1964-1970*', *American Political Science Review*, 68.

Najah wakim, *Al Ayadi as- soud* (the black Hands), Beirut : Sharikat al- matbuat lil-tawzi wal nasher, 1998.

Najib 'Issa, *al-Qiwa al-'amila was siyasat al-'amala fi lubnan* (Labor Forces and Labor Policy in Lebanon) (Beirut: Lebanese Center for Policy Studies, 1996).

Perthes, V. (1993) '*Problems with peace: postwar politics and parliamentary elections in Lebanon*', *Orient*, 3.

Picard, E. (1996) *Lebanon: A Shattered Country* (New York, Holmes & Meier).

Putnam, R.D. (1993) *Making Democracy Work* (Princeton, Princeton University Press).

R.M. Stogdill: *Stogdill Handbook of leadership: A survey of the literature*, New York, Free press, 1974

Salameh, G. (1991) '*Beyond Lebanese political reform: reconciliation with basic values*', *The Beirut Review*, ½.

Salem, E.A. (1973) *Modernization without Revolution: Lebanon's Experience* (Bloomington, Indiana University Press).

Salem, P. (1998) 'Democracy in Lebanon: between political science and the elections of 1996', in: P. Salem and F. Al-Khazen (Eds), *The Parliamentary Elections of 1996 and the Crisis of Democracy in Lebanon* (Beirut, Center for Lebanese Studies).

Sassine, F. (1999) *'The legislative power in Lebanon'*, paper presented in the Conference on the Document of National Understanding 'The Taif Accord: A National Critical Evaluation'.

Seligman, A.B. (1997) *the Problem of Trust* (Princeton, Princeton University Press).

Simon Haddad, *the Palestinian's impasse in Lebanon*, Sussex, Portland, 2003.

Simon Williams, *"Lebanon's economic Champion"* for BBC news , (Monday, 14 February,2005).

Sleiman, I. (1999) *'The Lebanese President'*, paper presented in the Conference on the Document of National Understanding 'The Taif Accord: A National Critical Evaluation'.

Smock, D.R. and Smock, A.C.(1975) *The Politics of Pluralism* (New York, Elsevier).

Special interview and meeting with AUB graduates, December 2002

The Economist (1999) 'Silent clapping. an investigation into political corruption in Lebanon may not be all it seems to be', *The Economist*, 352.

The Executive "An overlook on Hariri's economic plan", Beirut, issue 1236, March 2004; April 2004

The Executive Gazette Number 4113 published on April 25th 1995

The Financial Times, March 22nd 1993

The Lebanese Republic official transcript on Paris 2 meeting, *"Beyond reconstruction and recovery.... Towards sustainable growth"*, a request for international support

The Times issued on 22nd March 1993; 129 (December 4th 2003)

Thomas R.Linlof (1995) *qualitative communication research methods* (SAGE Publications)

Trendle, G. (1993) '*The grass root of successes*', *The Middle East*, February.

•
www.9-11commission.gov.