

# Lebanon Revisited

## A Concept for a 2003-2005 Strategy

*“The most open, tolerant places in the Muslim world today are all trading centers: Dubai, Istanbul, Bahrain, Amman, Beirut, and Jakarta.”*  
Thomas L. Friedman. March 2002.

### I. Summary

Lebanon, perhaps the oldest trading center in the world, is facing enormous challenges to its economy, brought on by a host of domestic, regional, and global issues. USAID, over the past four years, has been effective in addressing rural poverty, local governance, and the environment, and has made inroads in advancing economic policy reform and building the capacity of Lebanon's American universities. During the next three years, USAID will build on these gains, creating economic opportunities in areas with high growth potential; accelerating reform and global competitiveness; strengthening economic and democratic governance; and promoting sustainable environmental and water management practices. Key to success will be partnerships that fuse the interests, expertise, and resources of the business, government, university, NGO, and donor communities; and mechanisms that allow a small mission to manage its substantial investments efficiently.

### II. Lebanon Today

Lebanon, like its neighbors, lives in very challenging times. Just two years ago, in May 2000, Lebanon was celebrating the withdrawal of Israeli forces from the south after two decades of occupation and a devastating civil war. People were excited about resettling, reintegrating, and reviving the south, and bringing stability, security, and sovereignty to the entire country. These goals, however, proved short-lived when Lebanon and Syria disputed the U.N.'s "Blue Line" border with Israel, reviving the "resistance" movement and putting recovery on hold. September tragedies -- Jerusalem in 2000 and New York and Washington in 2001 -- saw the respective launching of the Palestinian *intifada* and the "War against Terrorism." Both affected Lebanon profoundly, the latter highlighting Hizballah on America's list of global terrorists, putting considerable strain on Lebanon's relationship with the United States. Today, as Arab leaders prepare for their late March Summit in Beirut, our hope is that the region, and the world, will finally witness the birth of a viable and comprehensive plan for peace in the Middle East, and that Lebanon will above all become known for its launching.

#### ... the glass half-empty

Even with the chance for peace on the horizon, the current situation makes it easy to be down on development. South Lebanon, for example, remains not fully integrated, with periodic cross-border violations and confrontations; unsafe habitats riddled with mines; and minimal government presence and investment. The national economy is stagnant, with an alarming level of public debt whose servicing, together with the costs of

government operations, consume an astounding 94% of the tax revenues. Political machinery, mired in religious and various other cleavages, often undermines nation-building and collective action for the common good, making “political will” hard to define and slowing the institutional and structural reforms needed to put Lebanon on a sound footing. External influences, primarily Syrian, affect all major decisions in Lebanon.

### **... and the glass half-full**

But there is reason for optimism and no reason to jettison a future anchored in sustainable development. The reform-minded government of Prime Minister Hariri, in place since November 2000, is making good moves – advocating economic growth and investment nationwide; promoting competitiveness and globalization with a Euro-Med Partnership and planned WTO accession; making 2002 the “Year of Privatization”; introducing key revenue-enhancing reforms and a value-added tax; supporting sound budget management, and promoting good governance, and administrative and municipal reform. Anchoring them is a very diverse Christian-Muslim-Druze population that comprises one of the most educated, talented, entrepreneurial workforces in the Arab world, in a capital that has long served as a regional hub for business and banking, in a country that has long been a mecca for travel and tourism. Equally significant are the estimated 16 million Lebanese around the world – five times the resident population. Many of them have maintained close ties with Lebanon and have created vibrant social and economic networks, vital safety nets, and a pool of resources and wealth that has kept many Lebanese and the country afloat, especially during difficult times. While we don’t pretend to understand fully how this “second” or “shadow” economy works, it is unquestionably an integral ingredient of Lebanon’s resilience.

### **III. Where We’ve Come From**

Nearly five years ago, following a near shut-down of U.S. development assistance in Lebanon, the USG decided to revive its bilateral assistance program. Much of it was a reaction to the Israeli occupation and continued conflict in South Lebanon, as well as the widening and very apparent social and economic disparities, especially in rural areas. There was also growing recognition of Lebanon’s role in building regional economic cooperation and achieving Middle East peace. The outcome: USAID put in place a five-year \$60 million strategy aimed at

- revitalizing and expanding economic opportunities in rural areas, through small-scale infrastructure and income-generating activities;
- promoting democracy and good governance, building capacity of local municipalities to plan and manage resources efficiently and transparently; and
- improving environmental practices, particularly community-based approaches that promote sustainable agriculture and environmental health.

Over time four other activities were added: a WTO accession program to encourage trade and investment, globalization, and broad-based policy and legislative reform; an “industry cluster” program, to identify and promote productive sectors for investment; a water resource management program, to make agriculture more productive and ensure that water pricing is efficient and equitable; and a landmine action program, to make all Lebanese aware of hazardous areas and assist survivors in productive enterprises.

Nearly five years later, having operated in an increasingly difficult development context, we can say, with conviction, that this strategy was sound and tailor-made to USAID’s strengths. Indeed, USAID has built a reputation as one of the top donor programs in Lebanon, viewed by many as one of the most responsive, expansive, resilient, targeted, high-performing, and quick-disbursing – though far from the largest. We attribute this to our *purpose* -- promoting equitable, sustainable development in Lebanon over the long-term; our *products* -- demand-driven, people-focused, affordable, effective, appropriate, visible and accomplishable in the short-term; our *partners* – PVOs, NGOs, foundations, universities, business associations, and corporations -- who together, often in partnership with the public sector, form a multi-faceted, highly-talented, experienced group capable of navigating effectively at the highest governmental, corporate, and diplomatic levels, as well as at the community level; and our *procedures* -- user-friendly, promoting extensive collaboration with all relevant public and private entities and, in contrast to most donor programs, channeling resources directly to implementing partners.

Most important are the significant achievements produced by these “4 Ps”, which include improving living standards among the rural poor; stimulating economic policy reform and growth-oriented industry clusters; supporting Lebanon’s accession to the WTO; strengthening municipal governance; promoting advocacy among NGOs and civil society organizations; improving environmental practices and technologies for environmental health; raising awareness of landmines and helping mine survivors and their families rebuild productive lives; and strengthening Lebanon’s American educational institutions, to name a few.<sup>1</sup> The program has also created important spread effects. With an average of only \$15 million a year for the first four years, USAID leveraged another \$60 million of complementary World Bank and European Union funding for rural community-based development activities. These, in turn, have become a model for at least three other AID programs intent on bringing economic opportunities and social services to disadvantaged communities, often in conflict or post-conflict settings.

#### **IV. Where We Want to Go**

We thus have a relatively nascent but high-performing program, now earmarked at \$35 million annually, operating in a middle-income country where economic disparities are often pronounced, but whose social indicators – health, education, nutrition – are among the highest in the region. The program, well-focused on the Agency’s EGAT and DCHA Pillars, is not heavily directed.<sup>2</sup>

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<sup>1</sup> For details of these and other accomplishments, see the “Performance Narrative” and Congressional Budget Justification Sections of USAID/Lebanon’s *FY 2002 Annual Report*.

<sup>2</sup> EGAT: Economic Growth, Agriculture, Trade; DCHA: Democracy, Conflict Prevention, Humanitarian Assistance.

Our intention in this next phase, as discussed below, is to build on our success, melding elements of the current strategy into one that fuses expansion with integration, targets value-added and growth-oriented sectors and reforms, and fosters economic and political governance that will enhance Lebanon's competitiveness as a regional and global player, all the while keeping the focus on the ultimate prize: a prosperous Lebanon embarked on a path of sustainable development.

#### **A. Key Planning Assumptions**

With all its strengths and advantages, Lebanon today is confronted by regional instability, internal political stalemate, and deteriorating economic performance. These and related factors could, in the worst case, result in economic collapse. They also apply downward pressure on standards of living, particularly among the rural poor. At this point we do not expect a political or economic breakthrough that would usher in any significant gains. We also believe that the Lebanese may be able to avoid a cataclysmic breakdown. We are "sober" and assume the following:

**External Political and Security Status.** Political and security conditions in the Middle East have become more volatile. The perspectives and approaches of key actors seem to have hardened; terrorist incidents have increased. All these have had a negative impact on Lebanon's economy. Success at the "Beirut Summit" would certainly be positive but, given the complexity of issues, not translate into immediate benefits for Lebanon.

**Internal Political Situation.** Lebanon's political system is designed to maintain stability among different confessional groups. The structure and processes of government are tied closely to that system. The over-riding desire for political balance has thus far stymied efforts to implement major institutional or electoral reform. However, there is support for municipal development and local-level planning and resource mobilization, backed by a revised municipal and new decentralization laws, currently in draft.

**Domestic Economic Performance.** Lebanon's GDP growth over the last three years has been weak, a condition that will likely continue for at least another year. Quick economic reform is unlikely in the near-term, unless an imminent threat of crisis incites the GOL to adopt appropriate reforms and longer-term structural adjustments. WTO accession will progress and support the new Euro-Med Agreement. Cost-cutting austerity budgets will decrease investment in infrastructure and public services, particularly in rural areas.

**International Economic Performance.** Lebanon's trade deficit widened considerably in 2001, with higher imports spurred by lower tariffs. Public debt increased significantly. Reversing this will depend on a comprehensive reform program that includes such things as aggressive privatization measures, collection of the VAT, and removal of subsidies. The Lebanese pound's peg to the dollar is under increasing pressure; it will remain fragile as investor confidence in the pound, and the GOL's ability to prop it up, decline.

**South Lebanon.** The initial jubilation surrounding the May 2000 Israeli withdrawal has not translated into resettlement, revival, and reintegration of South Lebanon. USAID's and other donors' investments, while making a difference in infrastructure and demining, are not able to stimulate economic activity on any significant scale. This will not happen until border incursions cease and the GOL takes full control of the south, at a minimum.

**Life Beyond Beirut.** Lebanon is often compared to a "City-State" with all economic, social and political roads leading to Beirut. Out-migration from rural areas increased during the civil war and occupation, creating a band of heavily-populated communities around Beirut. Urban centers exist along the coast -- Tripoli, Sidon, Tyre -- but economic activity is limited. Countering this trend depends on developing competitive advantages in these secondary cities, with strong linkages to surrounding towns and communities.

**Lebanese Initiative and Outlook.** Whatever growth Lebanon can muster will be driven by the private sector. Commercial banks, while holding considerable government debt, are liquid; they will lend for growth sectors. Lebanese have extensive family, business and educational ties to the United States, which have a positive effect on Lebanon and will continue. Politics aside, the Lebanese look to the U.S. presence in Lebanon for technical leadership, business connections, and economic opportunities. Their overall view of the United States is favorable.<sup>3</sup>

Thus, looking at the situation today and speculating on tomorrow, we see a "**status quo**" **scenario** as most likely emerging, characterized by gradual economic deterioration that is somehow managed by the GOL and private sector players. Economic policy reforms will be implemented gradually; the political and security milieu will not change significantly. Lebanon will face resistance by international creditors to extend additional credit and debt relief, but steps will be taken to avoid acute financial crisis, mainly through credits, deposits, and other help from the Gulf states and overseas Lebanese. In sum, Lebanon will have its share of challenges over the next 2-3 years.

## **B. Investment Opportunities**

The Mission, in close collaboration with AID/W and Embassy and State colleagues, and with extensive input from a host of local experts and partners, proposes focusing on six strategic areas in this next phase. Collectively, they support the Embassy's core MPP goals of promoting regional stability and economic prosperity; and USAID's economic growth (EGAT) and democratic governance (DCHA) pillars. They also dovetail nicely with the Secretary's "Middle East Partnership for the Future", targeted at reducing social and economic inequities, improving the economic and business climate, and building human capacity across the region.

The ideas presented below represent the evolution of what USAID has done well for the past four years, adapted to today's realities and future prospects. They reflect, in various

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<sup>3</sup> A March 2002 Gallup Poll in nine Islamic countries showed that Lebanon has the highest favorable opinion of the U.S. at 41%, followed by Turkey at 40%; Kuwait at 28%; Indonesia at 27%; Morocco and Jordan at 22%; Saudi Arabia at 16%; Iran at 14%; and Pakistan at 9%.

ways, value-added, integration, consolidation, and expansion. Together they reflect:

1. A transition -- from alleviating poverty to creating economic opportunity
2. A focus – on strengthening growth areas, both geographic and productive
3. A link – between the rural and urban, inland and coastal
4. An emphasis – on governance, reform, and sustainability
5. A reliance -- on new partnerships and models for economic growth

The following six “strategic areas” will:

- **Expand Economic Opportunities**

The Lebanese need good jobs and incomes, not just in Beirut, but in other cities, towns, and communities. Melding the two “cluster components” of the current program – rural development clusters and industry clusters – will make this happen by integrating those productive sectors and locales that have the greatest potential for growth. The sectors, which together comprise about 35% of Lebanon’s GDP, are: agribusiness, catering to “niche markets” for high-value fresh foodstuffs and processed foods, to replace imports and expand exports; tourism, by far the best prospect for near-term growth, particularly ecotourism and cultural/historical tourism; and information technology, a value-added industry for a wide range of economic activities. The locales: “Growth Poles”, outside Beirut and within or linked to rural clusters, that have the economic foundation (natural and human resources, technology, capital, infrastructure) to capitalize on these productive sectors. Regional hubs-with-spokes, linked to key Beirut-based industries, will stimulate rural-urban linkages that favor balanced, equitable, and sustainable development.

Anticipated results: The growth of employment and income-generating activities in, and reduction in migration from, rural areas; increased trade, investment, and export earnings; reduced food imports and deficits.

- **Accelerate Economic Reform**

This scenario for expanding economic opportunities will not get beyond second-gear if the enabling environment for trade and investment, and growth and services industries, is disabled. USAID’s principal vehicle for economic reform is WTO accession, for which we provide core technical assistance to an inter-ministerial WTO Unit, as well as advice to the business, university, and NGO communities. We expect the pace of accession to accelerate this year, not only because the GOL is nearly ready to start negotiations, but because the current economic situation, coupled with the desire to move ahead on the agriculture and services components of Lebanon’s newly-minted Euro-Med Partnership Agreement, make WTO membership a necessity. The major focus for the next 18-24 months will be legal reforms for goods and services, intellectual property, international trade, competition policy, agricultural standards and safeguards, customs, and foreign investment. We anticipate the reform agenda will continue beyond accession.

Anticipated results: WTO accession by the end of 2003; increased trade and investment with appropriate legal guarantees and protections; a business environment in line with best international practices, i.e., predictability, stability, transparency, and accountability.

▪ **Strengthen the Foundations for Governance**

The above foundations for economic governance go hand-in-glove with democratic governance, especially as the benefits of a performing economy spread through society, with people and structures empowered to make decisions on capturing and investing resources for the common good. In this respect much of Lebanon's strength lies in local government, the 712 recently-elected municipal councils. USAID has both a partnership and mandate to help provide them with e-government-friendly planning and management information systems, which we have developed and installed in over 100 municipalities. Good councils are key to successful rural cluster activities; their entrepreneurship, which we will strengthen, is key to creating "growth poles" and stimulating local investment. We will also consider expanding our "transparency and accountability" grant program, to build the capacity of NGOs, civil society organizations, the media, and private groups to advocate openness and combat corruption.

Anticipated results: Municipal councils nationwide engaged in effective planning and management by 2005, supporting rural cluster activities and collaborating with industry growth action plans in "growth pole" regions; citizens more informed about corruption.

▪ **Improve Environmental Policies and Practices**

USAID is developing three "niches" in the environmental sector that have the potential for high economic and health-related pay-offs. One targets solid waste/water disposal in rural areas, where USAID is developing innovative, appropriate, and cost-effective technologies for small municipalities and communities. Another focuses on-farm water management and "collaborative planning" among users and providers, to maximize the use of scarce water resources, particularly in South Lebanon. The third, just beginning, aims at broadening private sector participation among Lebanon's four water authorities and developing water pricing policies for full cost recovery. GOL is looking to USAID's success in Jordan as a possible model for water pricing. All three issues – waste disposal, wasting water, and wasting money – are key constraints to developing this sector.

Anticipated results: Nationwide dissemination of appropriate solid waste/water disposal technologies; municipalities fully engaged in environmental planning and management; on-farm water management systems in place and replicated in targeted areas; water revenues cover water distribution costs.

▪ **Promote Landmine Awareness and Victims Assistance**

Widespread landmines and other unexploded ordnance in South Lebanon and the West Bekaa are killing or injuring an average of nine people a month. They undermine safety, security, and resettlement, and dampen economic revival. They are nothing less than the

“silent killer” of people and development. USAID, with over \$20 million of investments in the South, leads the GOL/Donor/NGO “International Support Group for Mine Action” in focusing attention on socio-economic constraints in mine-affected areas. With support from the War Victims Fund, USAID plays a major role in promoting landmine awareness activities; helping landmine survivors and their families rebuild productive livelihoods; and strengthening the capacity of Balamand University’s “Landmine Resource Center” to conduct surveys and analysis integral to our programs. Continuing these activities, in close coordination with deminers from the Lebanese Armed Forces, U.N. Peacekeeping Forces (UNIFIL), and private companies, is critical to our interests in South Lebanon.

Anticipated results: An increase in higher-impact, growth-oriented investments in South Lebanon and the West Bekaa; a reduction in mine-related deaths and injuries.

#### ▪ **Strengthen American Educational Institutions**

Lebanon’s American Educational Institutions (AEIs), notably the American University of Beirut (AUB) and the Lebanese American University (LAU), are two of the premier institutions of higher learning in the region, let alone Lebanon. Over the past three years USAID has cultivated an excellent partnership with AUB and LAU, based on common development priorities that span the entire USAID program. Faculty are fully integrated into WTO, ICT, tourism, rural development, governance and environmental initiatives, adding considerable added-value to various partners and projects. Equally important, these AEIs are fully committed to values of tolerance, free inquiry, and critical thinking. They enjoy substantial support from many constituencies – Congress, and the American Task Force for Lebanon, to name two. Support to AEIs for USAID program priorities, with modest funding for scholarships and other AEI initiatives, are a good investment.

Anticipated results: Faculty and staff increasingly engaged in public policy and programs that support development assistance; student body diversity, focusing on disadvantaged communities in rural areas.

### **C. Partnerships and the Global Development Alliance**

The impact of this new phase rises and falls on the quality of our partnerships. USAID’s current partners - PVOs and NGOs, private companies, business associations, donors and government agencies, foundations, and American educational institutions are strategically engaged in our program and instrumental in helping us achieve results. We will continue capitalizing on their strengths and their resources.

The business model reflected in the Agency’s “Global Development Alliance” (GDA) is especially relevant as we strengthen and expand public-private partnerships. We have one GDA activity under our belt – a “Mobile Education Center” for South Lebanon which was developed under our rural cluster program and co-financed with Microsoft and AUB. This kind of multi-purpose “internet for development” activity holds great promise for expanding community-based information technology activities in high priority areas, i.e., those where rural and industrial cluster activities come together. We view the GDA as an

integral, value-added part of our program, and will seek to tap into the Bureau’s “Mission Incentive Fund” this year and throughout the strategy period.

#### **D. Other Scenarios**

The Mission will analyze “trigger points” that could lead to Breakthrough/Breakdown scenarios. For the moment we see the following:

**Breakdown.** The trigger would be increased conflict in the region that spills over to Lebanon, an economic meltdown, or in the worse case, both. Drastic cutbacks would be required by the GOL, leading to major economic dislocations and social strife. USAID would likely concentrate first-and-foremost on safety net activities (e.g., quick income-generating activities, micro-credit facilities) in poverty-prone rural areas. We are well positioned to do this through the rural cluster program. There is also the possibility of providing emergency policy reform/adjustment assistance, depending on circumstances.

**Breakthrough.** The trigger would be economic recovery through a confluence of positive factors – comprehensive peace or debt relief being the most robust. We would expect increases in domestic and regional stability, tax revenues from privatization and the VAT, pledges from donors and investment from overseas, etc. USAID would like focus on improving the capacity of key public and private sector institutions, as well as on policy refinements to support sustained growth.

#### **E. Dealing with Conflict and Terrorism**

Our program thus far, notably the rural cluster and municipal governance activities, has had some success in promoting collaborative decision-making and mitigating conflict in several conflict-prone areas. Our tack is to work with communities and municipalities to identify activities that they want and that cross-cut the myriad of socio-political-religious cleavages. We then help mobilize them to contribute to, implement, and in the end own the products as part of the common good. This approach has also worked in communities with Hizballah presence, where USAID activities – known for their social, political, and religious neutrality -- serve as a counterweight to many of Hizballah’s social projects. The continued presence of their militia, however, and occasional cross-border incursions, act against resettlement, revival, and reintegration of South Lebanon -- limiting the range, location, and type of programs we and other donors can effectively implement. We also view our support to and relationship with Lebanon’s AEs in some respects as “bridging a cultural gap”, fostering the kind of mutual respect and understanding that is critical to our long-term interests in Lebanon, and throughout the region.

#### **V. Proposed Parameters**

##### **▪ Management and Resources**

The strategic areas proposed above, together with the partnerships and scenarios that will give them life, can, we believe, be implemented within the Mission’s current staffing and

resource levels. This consists of (1) 1 USDH, 6 FSN professionals, 3 of whom will be on-board by June 2002, and 3 support staff;<sup>4</sup> (2) RLA, RCO, EXEC, and CONT support from USAID/Jordan, in addition to ICASS services already provided by the Embassy; (2) program resources of at least \$35 million annually, reflecting FY 2001-2002 appropriated and FY 2003 proposed ESF levels; and \$10-20 million of PL 480 resources, preferably monetized; and (3) operating expense resources of at least \$900,000 in FY 2003.

▪ **Duration and Focus of the Next Phase**

Given the many uncertainties in Lebanon and the region at the moment, and the risk that they will continue for some time, we propose a 3-year FY 2003-2005 planning horizon for the next phase of assistance – recognizing that the “status quo” and “breakthrough” scenarios are embedded in a longer-term sustainable development vision. We would organize the six strategic areas into three strategic objectives, with American Educational Institutions integrated across the portfolio as a core implementing partner:

SO1: Expanded Economic Opportunities, which would combine rural/industry clusters, economic reform, and landmine victims assistance

SO2: Strengthened Foundations for Governance

SO3: Improved Environmental Practices and Policies

▪ **Proposed Timing for Strategy Submission and Review**

The strategy review would take place after the departure of the current Mission Director (o/a June 15) and the arrival of the new Mission Director (June 28). Both will be present at the review.

Strategy Submission: May 24<sup>th</sup>

Strategy Review: June 24-27<sup>th</sup>

▪ **Other Decisions for the Parameters Meeting**

1. Whether the mission should produce a new strategy or a revision to the current one.
2. Whether the Mission can issue a “Request for Assistance” (RFA) by the end of April for the “clusters” portion of the strategy -- prior to approval for the new or revised strategy. Delaying the RFA until July would jeopardize an FY 2002 obligation for this component and affect the continuity and momentum of the program.

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<sup>4</sup> USAID and the Embassy are discussing the possibility of adding another USDH or USPSC. The issue is not whether the position is needed for program management, but rather adequate housing on the Embassy compound.