



MIDDLE EAST/ LEBANON
COUNTRY RISK PROFILE:
PARLIAMENTARY ELECTIONS IN FOCUS

JUNE 2009



Marker Global Ltd

Finsgate
5-7 Cranwood Street
London EC1V 9EE

Telephone: (0044) 020 8133 2704
Email: info@markerglobal.com

Despite the recent instability, Lebanon has enjoyed a period of relative economic growth over the last year.

SUBJECT: POST-ELECTION COUNTRY RISK OUTLOOK

- The victory of the pro-Saudi and US March 14 block in Lebanon's parliamentary elections held on 7 June 2009 is unlikely to result in any major change.
- In the short-term, the country will face challenges such as the formation of a new cabinet, Hizbullah's right to a veto vote and the appointment of a new prime minister. The break-down in negotiations could result in a return to political deadlock.
- In the long-term the country's deep-rooted economic and social problems will continue to go unaddressed as the new government is unlikely to have the power or will to bring in major reform or new legislation.
- However, despite the uncertainty, the staging of peaceful elections is a positive achievement for a country that was overcome by a round of street fighting between the two sides just over a year ago.
- Moreover, the economy has performed well over the last year and the stronger diplomatic skills of the Obama administration could result in a more stable period over the short to mid-term.

FACTBOOK

The March 14 alliance (March 14)

March 14 is an alliance of various Lebanese political parties united by an anti-Syrian and pro-Saudi Arabia and the US stance. Its name derives from the anti-Syrian demonstration held on 14 March 2005 in response to the assassination of Rafic Hariri, the former Prime Minister, the previous month. The alliance is led by Rafic Hariri's son, Saad Hariri, and consists of the Future Movement party, which mostly has Sunni supporters, the Kataeb and Lebanese Forces parties, both of which represent Christians, the Progressive Socialist Party of Druze leader Walid Jumblat as well as other smaller groupings.

The March 8 alliance (March 8)

March 8 was named after the pro-Syrian demonstration that took place on 8 March 2005. The demonstration was called to show support for Syria whose forces occupied the country. The alliance is led by Hizbullah, whose supporters are Shia Muslims, and consists of Amal, another main Shia party, the mainly Christian Free Patriotic Movement led by General Michel Aoun as well as smaller groupings. The alliance is pro-Iranian and Syrian.

Parliamentary seats:

From a total of 128 seats, March 14 won 69 seats.

ANALYSIS

STEP 1: Business risk outlook

Poll result calms business fears of isolation

Prior to the polls, Lebanese businesses were unnerved by fears that a victory by the March 8 block could result in a western backlash, materialising into cuts in aid or even financial sanctions. The victory of the March 14 alliance is a positive result for the country's trade and commerce. Brokers on Beirut's stock exchange reported strong demand for stocks on 9 June, the first day of trading after the elections. Since then stocks have continued to make gains.

Economically Lebanon has enjoyed a period of relative stability over the last year. The growth rate for 2009 is predicted to be around 4%¹ and the country has showed resilience to the global recession. The country's key banking sector is managed conservatively, many banks reported good results² for the latest financial year and managers are adept at weathering conflict and economic uncertainty.

However the private sector still faces a number of obstacles. Previous Lebanese governments have shown little understanding of the needs of the private sector and investment in infrastructure is badly needed.

Infrastructure in Lebanon is outdated and in need of investment. In the telecoms sector, mobile phone call rates are some of the most expensive in the world, installation of landlines is complex, internet penetration rates are low and high-speed internet access is expensive. Plans to introduce a third telecommunications licence and to privatise the fixed line operator Oger Telecom have been stalled. Currently the two mobile licences are managed on behalf of the government by Zain Group and Egypt's Orascom Telecom under a one-year contract, to be renewed in early 2010. Lebanon has strong demand for improved internet speeds and currently bandwidth speeds are below regional standards. Although some progress has been made, the government could facilitate improvements by liberalising this sector and encouraging more competition.

One of Lebanon's biggest assets is its population of well-educated and polyglot youth. However the rates of emigration are very high and although no official studies have been conducted, it is estimated that around one fifth to a half of graduates emigrate to the GCC, Europe or the US. The Lebanese Emigration Research Centre conducted a study in 2007 which found that 60% of university students intended to leave Lebanon after they graduated.

However despite the instability and inadequate infrastructure, Lebanon's wealth of human resources and low costs gives Lebanon good potential as a location for business. Several call centres³ have expressed interest in locating to the country and some Gulf businesses have moved their back house activities to Lebanon to avoid the high-costs of GCC countries.

Fundamental economic shortcomings are deep-rooted

Despite the relatively good performance of the economy there are still fundamental economic problems. The country's national debt of US \$47 billion continues to increase and is now 162% of the GDP.⁴ This has accumulated since the early 1990s when the government borrowed to fund post-war reconstruction projects. Most of the debt is owed internally to Lebanon's banks but the government has not defaulted on repayments. However economists and international financial institutions question how much further this debt can continue to grow before it reaches crisis point.⁵

Government run utilities and services continue to hemorrhage money, and in the case of Electricite du Liban (EDL) it is estimated that around US \$1 billion is lost every year⁶, through inefficiency, theft and corruption. EDL offers poor service and all parts of the country are subject to power cuts of between 3-12 hours a day. However attempts at privatising public-owned companies such as EDL, in a bid to raise state revenues and improve service for the consumer, fall victim to political bickering and often do not succeed.⁷ Assets that could be privatised or sold-off are the mobile phone licences, transport and health care facilities.

1. Salameh sees Lebanon's growth rate at 4 percent by end-2009, The Daily Star, May 29, 2009

2. In their annual reports, Bank Audi and Byblos Bank, two of Lebanon's largest banks recorded an increase in net profits of 19.1% to US \$238.5 million and 23% to US \$122 million respectively.

3. Lebanon's Bassil signs call-centre contracts with five firms, The Daily Star, 26 March 2009

4. Shatah warns delays in reforms will scupper international aid, The Daily Star, April 09 2009

5. Lebanon—2009 Article IV Consultation Mission, Mission Concluding Statement, March 5, 2009

A system of exclusive agencies that give import rights to only one individual hinders Lebanon's ability to offer consumers competitive prices. These exclusive agencies have been in the hands of the same families for several generations. Attempts to tackle this system and liberalise import rights in order to make Lebanon eligible for World Trade Organisation (WTO) membership have been met with strong lobbying by the families who retain the exclusive rights and rely on their strong political influence.

Two sectors that have experienced growth over the last decade are tourism and real estate. The Ministry of Tourism has said that it is expecting a record 2 million tourists in Lebanon this year, after 500,000 visitors were recorded by May. Tourism in Lebanon has been gradually increasing since the end of the civil war but has been hit by the instability that the country has experienced in the last five years. However hotel occupancy of 55 percent is still below the Middle East average of 69 percent.⁸

The real estate sector in Lebanon has experienced a boom despite the instability and a number of new developments are taking place across the country. Real estate prices in Lebanon are famously resilient and there is an adage that properties never lost value throughout the 1975-1990 civil war. Although there are no official figures or reliable studies, real estate prices have increased by around a third in Beirut over the last few years. The reconstruction of the Downtown area is gathering pace and projects that have been in the pipeline for years are getting closer to realisation. Much of the demand for real estate in Lebanon is coming from Gulf Arabs, who like to summer here and Lebanese expatriates.

STEP 2: Short-term outlook

Long-drawn negotiation to form new cabinet expected

The March 14 coalition must negotiate a new cabinet, appoint a prime minister and respond to a March 8 demand that it retain its veto vote.⁹ Following the political deal brokered by the Qatari government in Doha last year, Hizbullah was granted a veto over cabinet decisions. March 14 have said they will reject any demand for a veto. Potentially, negotiations over this issue could risk a return to the crisis that resulted in political deadlock between 2006-2008. It is likely that the formation of a new government will take weeks or even months of negotiation.

Hizbullah to maintain key role in the balance of power

Despite Hizbullah's loss in the elections they remain extremely powerful in Lebanon. Support for them has not waned among their Shia Muslim constituents, and disarmament of their armed-wing, a previous demand of the March 14 alliance is unlikely to be addressed. The outbreak of fighting between the two sides in May 2008 in which Hizbullah and its allies fought a decisive victory, has effectively forced the March 14 alliance to tone down any demands that it makes on the party.

In some respects Hizbullah's loss in the elections suits the party as it does not have to take responsibility for governance nor risks a western backlash like what was seen when Hamas won elections in the Palestinian Authority areas in 2006.

STEP 3: Long-term outlook

Fractious political system cause for future instability

In the long term the risk of serious instability remains high given the country's inherently fractious political system and the volatile nature of the region's politics. Internally, key issues such as Hizbullah's arms, reform of the sectarian political system, and the status of the country's 300,000 Palestinian refugees are unlikely to be on the table anytime in the near future.

Lebanon has a sectarian system of government in which representation in parliament is on the basis of confessional background. Each sect is given representation on the basis of the Taif Accord in 1989, which gives Maronite Christians 34 seats, the largest number of seats in parliament. Sunni and Shia Muslims have 27 seats each. The presidency is reserved for a Christian Maronite, the prime minister must be a Sunni and the speaker of the house a Shia.

6. Electricity: a financial abyss and a nightmare for the Lebanese, Agence France Presse, June 23, 2008

7. In 2008 the scheduled auction of the mobile phone licenses failed to take place due to the divide between March 8 and March 14 politicians.

8. Lebanon may be set to welcome a record number of tourists this summer, Zawya, May 22, 2009

9. Hizbullah, allies to boycott government without veto, Reuters, June 13, 2009

This representation is theoretically on the basis of the size of these sects' populations in Lebanon. However a census has not been conducted in Lebanon since 1932 and population numbers have changed substantially since then. Many Shias claim that they are now the largest religious community in Lebanon and that therefore they should receive more representation.

For long-term stability in Lebanon to be secured, reform of the political system must take place. The current sectarian system is inherently unstable and was a main factor in the 1975-1990 civil war. Many activists in Lebanon call for an end to the sectarian system of government, however those who benefit from this system are reluctant to relinquish their control and reform is unlikely to happen in the near future.

Increased Rights for Palestinian Refugees Essential

Lebanon is home to around 300,000 (some estimates put this number at 400,000) Palestinian refugees who fled their homes in Palestine in 1948 and 1967. Most of these refugees live in overcrowded camps with inadequate services. The refugees are banned from working in around 20 professions, owning property and do not have access to state healthcare and are marginalised in every aspect of Lebanese society. As a result of these restrictions unemployment rates among Palestinians are high.

Many Palestinian camps are off-limits to Lebanese security services and are policed by militias of Palestinian factions. In 2007 the Lebanese Army launched an offensive on Nahr al-Bared refugee camp in the north of Lebanon following an attack on the army by the Fatah al-Islam group who were based in the camp. The subsequent battle resulted in the deaths of more than 400 people, the destruction of the camp and a bombing campaign by Fatah al-Islam elsewhere in the country.

The current conditions for Palestinian refugees could lead to further conflict. The poor conditions in which refugees live leaves them prone to radicalisation and the destruction of the Nahr al-Bared camp has resulted in further resentment between the Lebanese authorities and the Palestinians. The camps themselves are lawless and tensions between the factions who control them often leads to armed battles. Although some Lebanese politicians support measures that would ease living conditions for Palestinians, such as giving them more rights without full citizenship, these are unlikely to be implemented.

Regional and international conflicts

Elsewhere in Lebanon there are other flashpoints. The northern town of Tripoli has seen regular gun battles between Sunni and Alawi Muslims. Many areas of the country are essentially fiefdoms of the local political strongman. The Lebanese Army's ability to intervene and quell communal unrest is limited in case it is seen as being too harsh on one side, resulting in its neutrality being questioned and therefore risking the unity of the force.

Regionally, another conflict between Israel and Hizbullah is a strong possibility. Hizbullah is militarily stronger than it was in the 2006 conflict and Israel will eventually be forced to address this threat to their regional hegemony. The party's armed wing has probably relocated its positions in south Lebanon to areas north of the Litani River as well as increased its weapons stockpiles. There is a risk of a conflict either between Iran and the US or between Iran and Israel both of which would risk embroiling Lebanon as Hizbullah could support its Iranian allies by attacking the Jewish state.

The tensions between the two sides can be seen in the recent arrest of a number of Lebanese citizens, some of who were officers in the Lebanese Armed Forces, who authorities in Beirut accuse of being part of a spying network run by Israel.

Lebanon's relations with Syria have improved over the last year following the opening of embassies in Beirut and Damascus but Syria still has extensive influence in Lebanon. Syria has allies in Lebanon and is likely to have an on the ground presence that stems from its former occupation of the country. How Syria chooses to use this influence given the changing foreign policy of the Obama administration remains to be seen but decisions made in Damascus have the ability to cast sway in Lebanon and Syria's authority here remains strong.

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About the report's author

Christian Henderson is a business intelligence director at Marker Global and the head of its Middle East practice. Prior to becoming a consultant he was a journalist in the Middle East for five years and worked at the Daily Star and Al Jazeera. He is based in the region and regularly travels across the Middle East.

Further information

For further information please contact the report's author, Christian Henderson (c.henderson@markerglobal.com).