

RISK REMAINS IN LEBANON DESPITE CALM ELECTIONS

BEIRUT, 10 June 2009: The victory of the pro-Saudi and US March 14 block in Lebanon's parliamentary elections is unlikely to result in any major change in a country that for the last five years has been dogged by the worst instability since the 1975-1990 civil war. The formation of a new cabinet, Hizbullah's right to a veto vote and the appointment of a prime minister represent challenges in the short-term. 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, 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.

Business risk outlook

Prior to the polls, fears that a victory by the pro-Syria and Iran March 8 block could result in a western backlash, which could have extended to cuts in aid or even financial sanctions, unnerved businesses in Lebanon. The victory of the March 14 politicians 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. Stocks of Solidere, the real estate developers responsible for the reconstruction of the Downtown area, rose by 15%.

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

Short-term outlook

The March 14 coalition must negotiate a new cabinet, appoint a prime minister and respond to a possible Hizbullah demand that it retain its veto vote. Following the political deal brokered by the Qatari government in Doha last year, Hizbullah was granted a veto over cabinet decisions. Hizbullah sources have signalled that they want to retain that veto should they enter a national unity government, although no clear statement has made to this effect. The March 14 block 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.

Long-term outlook

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, the status of the country's 300,000 Palestinian refugees and fiscal management are unlikely to be on the table anytime in the near future.

Socio-economic problems such as unemployment and poverty persist. The country's national debt of US \$47 billion continues to increase and is now 162% of the GDP. All parts of the country are subject to power cuts of between 3-12 hours a day. Corruption and the weakening of some state institutions pose serious problems.

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 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.

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.

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. 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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FURTHER INFORMATION

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