REPUBLIC OF LEBANON

MINISTRY OF FINANCE

Public Finance Prospects

Ministry of Finance Quarterly Report

QI 2004

Fiscal Overview:

The total deficit decreased by 38 percent reflecting the 15 percent upsurge in total revenues and the 5 percent decrease in total expenditures between QI 2003 and QI 2004. The consolidation of the fiscal position also appears in the 321 percent increase of the total primary surplus which totaled LL 221 billion (section 1).

Revenue and Expenditure:

Total receipts amounted to LL 1,719 billion compared to LL 1,486 billion in QI 2003. The amelioration of the economic environment in QI 2004 fueled the overall improved performance across all revenue categories. Both tax and non tax revenues grew by around 20 percent when compared against QI 2003; tax revenues reached LL 1,163 billion and non tax revenues amounted to LL 471 billion by the end of March 2004. Total spending reached LL 2,298 billion, LL 123 billion less than the first three months' spending of the preceding year. This decline is due to a 19 percent lower debt service payment (sections 2 and 3).

Public Debt:

The stock of gross debt reached LL 50,677 billion as of March 2004, a 0.6 percent increase compared to December 2003. The slowing down in the total debt stock increase resulted from the 3.2 percent reduction of the foreign debt, following the repayment of USD 555 million, representing the amount of the two Eurobonds repaid on March 2004. Net market debt totaled LL 47,565 billion, registering a 0.5 percent increase (section 4).

External Trade:

The trade balance marked a USD 1,421 million deficit, or a 9 percent increase compared to the first three months of 2003. The increase in the trade deficit shadows the 34 percent jump in Lebanese exports which totaled USD 471 billion by the end of March 2004 as a result of the significant increase in the exportation activity to Iraq. Imports witnessed a 14 percent increase, attributed in large to increases in the value of imports from the Euro-zone and China (section 5).

Privatization & securitization developments:

The tender for the management contracts of the telecommunication mobile network was completed in March 2004 with the selection of a German company, Detecon International, and a Kuwaiti company, MTC as successful bidders (section 6).

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Section 1. Fiscal Overview

Between QI 2003 and QI 2004, the **total deficit** decreased by 38 percent to reach LL 579 billion. This decrease resulted from a 5.1 percent decrease in total expenditures which stemmed from a 19 percent decrease in the debt service and reached LL 800 billion by the end of QI 2004 compared to LL 987 billion by the end of QI 2003.

The total budget decrease was also the consequence of a LL 233 billion or a 15.1 increase in **total revenues** which had reached by the end of March 2004 LL 1,719 billion as opposed to LL 1,486 billion a year earlier. The increase in total revenues is explained by a better performance across all revenue categories.

The **total primary surplus** amounted to LL 221 billion, increasing by 321 percent from its March 2003 level when it stood at LL 52 billion.

Table 1. Summary of Fiscal Performance

(LL billion)	2003 March	2004 March	2003 Jan-Mar	2004 Jan-Mar	change 2003-2004	% change
Budget revenue	417	582	1,366	1,634	268	19.6%
Budget expenditures *of which:*	624	628	1,644	1,550	-94	-5.7%
Debt service	*336*	*277*	*987*	*800*	*-188*	*-19.0%*
Budget deficit/surplus	-207	-47	-278	84	362	130.1%
in % of budget expenditures	-33.1%	-7.4%	-16.9%	5.4%		
Budget primary deficit/surplus	130	230	709	883	174	24.5%
in % of budget expenditures	20.8%	36.7%	43.1%	57.0%		
Treasury receipts	49	25	120	85	-34	-28.8%
Treasury payments	242	168	777	748	-29	-3.7%
Total budget and treasury receipts	466	607	1,486	1,719	233	15.7%
Total budget and treasury payments	867	797	2,421	2,298	-123	-5.1%
Total cash deficit/surplus	-400	-189	-935	-579	356	-38.1%
in % of total expenditures	-46.2%	-23.8%	-38.6%	-25.2%		
Primary deficit/surplus	-64	88	52	221	168	321.0%
in % of total expenditures	-7.4%	11.0%	2.2%	9.6%		

Source: Ministry of Finance (MOF), Directorate General of Finance (DGF)

Section 2. Revenue Outcome

For the first quarter of the year, **total revenues** amounted to LL 1,719 billion, a 16 percent increase compared to the first quarter in 2003.

Budget revenues, the largest component of total revenues, cumulated at LL 1,634 billion by the end of March 2004, a 20 percent increase compared to the same period in 2003. With LL 1,163 billion collected, **tax revenues** also increased by 20 percent and represented 71 percent of the quarterly budgetary revenues. They were the main reason behind the increase in budget revenue which resulted from an overall improved performance across all tax categories. On the other hand, **non tax revenues** increased by 19.2 percent,

Table 2. Total revenue

(LL billion)	2003 Jan-Mar	2004 Jan-Mar	% change
Budget Revenue	**1,366**	**1,634**	**19.60%**
Tax Revenue	971	1,163	19.80%
Non-Tax Revenue	396	471	19.20%
Treasury Receipts	**120**	**85**	**-28.80%**
Total Revenue	**1,486**	**1,719**	**15.70%**

Source: MOF, DGF

Table 3. Tax revenue

(LL billion)	2003 Jan-Mar	2004 Jan-Mar	% change
Tax revenue	**971**	**1,163**	**19.76%**
Tax on income, profits, & capital gains, *of which:*	**130**	**192**	**48.39%**
Income Tax on Profits	*59*	*68*	*15.03%*
Income Tax on Wages and Salaries	*62*	*43*	*-31.56%*
Income Tax on Capital Gains & Dividends	*6*	*13*	*136.04%*
5% Tax on interest income	*-*	*60*	*100%*
Income Tax Penalties	*2*	*7*	*299.61%*
Tax on property	**74**	**98**	**32.13%**
Domestic taxes on goods & services, *of which:*	**353**	**425**	**20.28%**
Value Added Tax	*316*	*380*	*20.04%*
Other taxes on goods and services, of which:	*33*	*40*	*23.11%*
Private car duties	*18*	*23*	*26.93%*
Passenger departure Tax	*14*	*17*	*18.69%*
Taxes on international trade	**369**	**390**	**5.63%**
Customs	*100*	*117*	*16.78%*
Excise, of which	*269*	*273*	*1.47%*
Petroleum Tax	*190*	*188*	*-1.33%*
Tobacco Tax	*47*	*42*	*-11.79%*
Tax on cars	*30*	*42*	*39.50%*
Other tax revenue *of which*	**45**	**58**	**28.69%**
Fiscal stamp fees	*45*	*58*	*28.79%*

Source: MOF, DGF

cumulating at LL 471 billion by the end of March 2004 (see Table 4 for details). This resulted mainly from the 27.2 percent augmentation in **income from public institutions and government property** observed in the first quarter of 2004.

• Development on the Tax Revenue Front:

Taxes on income, profits and capital gains amounted to LL 192 billion by end of March 2004 compared to LL 130 billion for the same period of 2003. This 48 percent increase, however, was not homogenous across all income tax categories and each type of tax marked the first quarter differently.

Collection of income **tax on profits** progressed by 15 percent, increasing from LL 59 billion in Jan-March 2003 to LL 68 billion in Jan-Mar 2004. This has been partly fueled by the lowering of the VAT threshold in April 2003 which widened, *de facto*, the base of taxable profits. Indeed, newly registered contributors to the VAT are receiving registration numbers that are signaling them to the Revenue Directorate and making their eventual evasion from the income tax on profits much more difficult. Another factor lying behind this increase is a recrudescence of the auditing activity.

Income tax on capital gains, with a total collection of LL 13 billion by the end of March 2004, more than doubled when compared to the same period in 2003. The increase in income tax on profits and capital gains may imply that the economy in 2003 was more profitable to enterprises than in 2002.

The **5 percent tax on interest income**[1] allowed the collection of a total of LL 60 billion and became, therefore, the second source of income tax revenue in the first quarter of 2004. The 5 percent tax on interest income collected for the first quarter of 2004 represented a 100 percent increase with respect to the same period in 2003 as the tax started to be collected in April 2003[2].

Income tax on wages and salaries assured the collection of LL 43 billion in the first quarter of 2004, a 32 percent decrease compared to the same period one year earlier. The decrease reflects the impact the amendment that the **Income Tax Law on Wages and Salaries**[3] had on the collection schedule of this tax: whereas QI 2003 amount of tax collected accounts for a semi annual bulk payment, QI 2004 amount of tax collected reflects only a one quarter payment amount.

Income tax penalties have also increased from LL 2 billion in Jan-Mar 2003 to LL 7 billion in Jan-Mar 2004, or a 300 percent increase.

Taxes on property increased by 32 percent: from LL 74 billion in the first quarter of 2003 to LL 98 billion in the first quarter of 2004. Increases were recorded for all three main property taxes.

(a) **Built property tax**, the recurrent component of the tax, increased by 42 percent from LL 31 billion during 2003 to LL 44 billion this year. This is explained by the issuance of the year 2001 assessment schedule, and by the amnesty granted on due penalties.

(b) **Real estate registration fees** improved by LL 10 billion by the end of March 2004 compared to the level of last year's first quarter, and reached LL 45 billion. This is attributable to:

(1) A more active real estate market. In fact, the number of real estate properties sales transactions went up by 9 percent, reaching 9,830 transactions in the first quarter of 2003 compared to 8,990 during last year's first quarter.

(2) Prices of real estate properties have also gone up reflecting an increased market demand. This effect is particularly visible for the month of January 2004, when despite a 3 percent decrease in the real estate property sales transactions, the real estate registration fees collected from sales transactions went up by 23 percent and reached LL 15 billion compared to LL 12 billion in January 2003. This is further confirmed by the 30 percent increase in the price value of the sales transactions which reached LL 707 billion in the first quarter of 2004 compared to LL 543 billion during last year's first quarter.

(3) Another reason behind the increase in **real estate registration fees** is the 215 percent increase in real estate registration fees paid by foreigners which reached LL 7 billion despite a substantial drop in the real estate property sales transactions carried on by foreigners in the first quarter of 2004. The increase in real estate registration fees paid by foreigners can be explained by the general increase in market prices that has been observed lately in the real estate market in Lebanon but also by the fact that foreigners have purchased real estate properties located in very expensive areas.

Domestic Taxes on Goods and Services increased by 20 percent, reaching LL 425 billion for the first quarter of 2004 as compared to LL 353 billion over the same period a year earlier. The upsurge in domestic taxes on goods and services can be mainly attributed to higher receipts from **VAT** and to a lesser extent to **other taxes on goods and services**. The VAT receipts increased by LL 63 billion or 20 percent in Jan-Mar 2004 reaching LL 380 billion compared to LL 316 billion in the first quarter of 2003. On the one hand, VAT collected at imports amounted to LL 250 billion compared to LL 197 billion a year earlier reflecting the increase in imports witnessed during the first quarter of 2004. On the other hand VAT collected on the internal operations totaled LL 130 billion (of which LL 122 billion from the fourth quarter of 2003 activities) as opposed to LL 119 billion in 2003. Other taxes on goods and services represent the bulk

[1] The 5 % tax is levied on all sources of interest income (including interest on deposits accounts in all currencies, fund management accounts, Certificates of Deposit, debt securities issued by private sector entities, and Treasury bills), and banks are required to collect and forward this tax to the Treasury on a monthly basis.

[2] No 5 percent income tax on interest income were collected in QI of 2003 because the tax became effective in February 2003 and started to be collected in April 2003 and, therefore, the 5 percent interest income collected for February and March 2003 were included in 2003 second quarter figures.

[3] Amendment of Article 21 of the Budget Law 2003

of the secondary sources behind the increase in domestic taxes on goods and services. They increased by 23 percent and reached LL 40 billion for the first quarter of 2004 as opposed to LL 33 billion in the first quarter of 2003. This was generated by: (a) a LL 5 billion increase in car duties which culminated at LL 23 billion and (b) a LL 3 billion increase of passenger departure tax, which amounted to LL 17 billion.

Taxes on international trade (both excises and custom duties) collected LL 390 billion during the first three months of the year compared to LL 369 billion during Jan-Mar 2003. The composition of revenues from trade has stabilized and excises represent around 70 percent (versus 30 percent for custom duties) of international trade taxes for 2003 and 2004 respectively.

Custom duties collected LL 117 billion for the first three months of 2004 compared to LL 100 billion one year ago. The increase in revenues from custom duties can be attributed to the 15 percent rise in imports during QI 2004 as compared to QI 2003.

Excises did not vary significantly and assured LL 273 billion for the Treasury in the first quarter of the year compared to LL 269 billion one year ago. This is to be found in the import patterns of the three main excisable items, namely, petroleum, tobacco and cars.

Excises on **Petroleum** decreased from LL 190 billion in QI 2003 to LL 188 billion in QI 2004. This decrease is due to the suppression of excises on petroleum gases and other gaseous hydrocarbons such as propane, butane and ethylene in October 2003. Petroleum excises collected in QI 2004 were, therefore, levied mainly on car gasoline.

Car Gasoline imports increased from LL 143 billion to LL 151 billion between QI 2003 and QI 2004. However, this increase in import has resulted from a price effect due to the increase in the average price of oil per liter, at customs, from LL 368 to LL 392 between QI 2003 and QI 2004 while the quantities imported have decreased from 0.389 billion liters to 0.385 billion liters during the same period. Therefore, in the first quarter of 2004, the market continued to react to the increase in prices by contracting further its demand for car gasoline. As a result of this slight decrease in the quantity imported, excises levied on car gasoline stagnated at LL 186 billion.

Between QI 2003 and QI 2004, Lebanon's imports of tobacco declined from LL 40 to 50 billion. This is due to the increase in the price of imports which led to a substantial decrease in the quantity of imported boxes of cigarettes. Indeed, while Lebanon was importing 347,200 boxes at an average price of LL 408 per packet in QI 2003, imports decreased to 162,800 boxes at an average estimated price of LL 496 in 2004. As a result of this substantial decrease in the quantity of tobacco imported, excises levied on tobacco decreased from LL 48 billion in the first quarter of 2003 to LL 42 billion by the end of March 2004.

Cars imports value increased from LL 120 billion in Jan-Mar 2003 to LL 157 billion in Jan Mar 2004. This reflects an increase in the quantity of cars imported from 5,631 units up to 7,540 units in the considered period. This increase in the demand for cars is partly explained by the slight decrease in the average price of imported cars from LL 21,384 million to LL 20,822 million between QI 2003 and QI 2004. Therefore, excises collected on cars registered a remarkable 40 percent increase, reaching LL 42 billion by the end of March 2004 and offsetting the decreases in excises collected from petroleum and tobacco. The suggested improvement in the car business is further reflected in a 27 percent increased collection of car registration fees *(please refer to the paragraph on Other Taxes on Goods and Services)*.

Other tax revenues display a 29 percent increase, registering LL 58 billion for the first quarter of 2004, as opposed to LL 45 billion in three first months of 2003. The bulk of other tax revenues is constituted of **fiscal stamp fees**. Two factors might explain this increase in fiscal stamp fees:

a)-The lowering of the VAT threshold from LL 500 billion to LL 300 billion in April 2003 and later to LL 225 billion in January 2004 which increased the proportion of formally recorded transactions and hence might partially explain the difference in the fiscal stamp fees collected between QI 2004 and QI 2003.

b)-A higher level of transactions in the economy, which will probably positively affect the number of formal recorded transactions independently from the VAT threshold lowering effect.

Table 4. Non-Tax revenue

(LL billion)	2003 Jan-Mar	2004 Jan-Mar	% change
Non-tax revenue	**396**	**471**	**19.20%**
Income from public institutions and government property *of which:*	**289**	**367**	**27.24%**
Income from non-financial public enterprises of which:	*253*	*347*	*37.37%*
Revenue from Casino Du Liban	*9*	*13*	*42.89%*
Budget Surplus of National Lottery	*6*	*8*	*45.45%*
Transfer from the telecom surplus	*238*	*326*	*36.98%*
Income from public financial institutions (Central Bank)	_	_	_
Property income (namely rent of Beirut International Airport)	*32*	*18*	*-45.33%*
Administrative fees & charges *of which:*	**88**	**84**	**-4.41%**
Administrative Fees *of which*	64	62	-3.49%
Notary fees	*3*	*4*	*11.44%*
Passport fees/ public security	*20*	*20*	*-0.38%*
Vehicle control fees	*30*	*27*	*-11.63%*
Judicial fees	*5*	*6*	*10.82%*
Driving license fees	*2.589*	*3.473*	*34.18%*
Administrative Charges	10	10	5.47%
Permit fees (mostly work permit fees)	11	10	-8.92%
Other Administrative fees & charges	2.129	1.668	-21.65%
Penalties & confiscations	**1.039**	**1.257**	**20.98%**
Other non-tax revenue (mostly retirement deductibles)	**18**	**19**	**5.25%**

Source: MOF, DGF

Non tax revenues cumulated at LL 471 billion by the end of March 2004, compared to LL 396 billion registered during the same period of 2003. This 19 percent increase stems primarily from a 27 percent rise in revenues generated by public institutions and government property which offset the 4 percent decrease in administrative fees and charges.

Income from public institutions and government property totaled LL 367 billion by the end of March 2004, of which, LL 326 billion were transferred to the Treasury from the annex budget surplus of telecommunication, a 37 percent increase compared to last year's transfers. Another LL 13 billion and LL 8 billion were transferred to the Treasury from the budget surpluses of the Casino du Liban and of the National Lottery respectively. These represent 43 percent and 45 percent higher transfers over last year's result.
Receipts from rents (namely from the Beirut International Airport or B.I.A) reached LL 18 billion in QI 2004 as opposed to LL 32 billion in QI 2003.

The collection of **Administrative Fees and Charges** witnessed a 4 percent decrease from the first quarter of 2003. It amounted to LL 84 billion by the end of March 2004.

This decrease is mainly attributed to lower collection of vehicle control fees, the main source of public sector fees, by LL 3 billion which is equivalent to a fall of 12 percent.
Other administrative fees like public security fees, the second major source of public fees paid to the Treasury, remained stable at LL 20 billion for the first quarter of the year. Notary, Judicial and driving license fees witnessed substantial increases in percentage but very modest improvements in absolute terms and could not, therefore, counter the decrease in administrative fees that resulted from the drop in vehicle control fees.

Permit fees (mostly work permit fees), produced LL 10 billion by end of March 2004, receding by 9 percent from Jan-Mar 2003 amount[4]. Other Administrative fees and charges and penalties and confiscations maintained their 2003 collection level at LL 2 billion and LL 1 billion respectively.

Treasury receipts[5] totaled LL 85 billion, representing guarantees in the amount of LL 24 billion, LL 13 billion worth of deposits, LL 24 billion of transfers from municipalities and other treasury revenues of LL 23 billion.

[4] *While assessing the performance of public fees, such as passport fees and work permit fees, a year on year comparison would be more relevant due too the irregularity in collection .*

[5] *Please note that Treasury resources are pure cash transactions that are temporary in nature, in the sense that receipts are often reclassified elsewhere (as expenditures, or as budget revenues).*

Section 3. Expenditure Outcome

Table 5. Expenditures by transaction classification

(LL billion)	2003 Jan-Mar	2004 Jan-Mar	% change
Total expenditures	**2,421**	**2,298**	**-5.1%**
Budget expenditures	**1,644**	**1,550**	**-5.7%**
Expenditures excluding debt service	657	751	14.3%
Debt service *of which*:	987	800	-19.0%
Domestic debt	665	467	-29.8%
Foreign debt	322	332	3.2%
Treasury expenditures	**777**	**748**	**-3.7%**
o/w Municipalities	47	174	271.9%
Previous years' appropriations	462	406	-12.1%
Non-Interest Expenditures (Total Expenditures minus Debt Service)	**1,434**	**1,499**	**4.5%**

Source: MOF, DGF

Total expenditures for the period of Jan-Mar 2004 totaled LL 2,298 billion, decreasing by approximately 5 percent from the Jan-Mar 2003 level, mainly on account of lower debt service. Budget expenditures amounted to LL 1,550 billion, a 6 percent decrease compared to the same period in 2003 and treasury expenditures reached LL 748 billion, a 4 percent decrease compared to the first quarter in 2003.

Total primary spending (total expenditures exclusive of debt service) for the first three months of the year reached LL 1,498 billion, a 4 percent increase compared to Jan-Mar 2003. This increase is mainly due to a larger transfer to municipalities.

Table 6. Expenditure by Economic Classification

(LL Billion)	2003 Jan-Mar	2004 Jan-Mar	% change
1. Current expenditures	**1,938**	**1,743**	**-10%**
1.a Personnel cost *of which:*	768	738	-4%
Article 13: Salaries and wages	*483*	*486*	*1%*
Retirement and end of service compensations	*254*	*207*	*-19%*
1.b Interest payments	987	800	-19%
1.c Materials and supplies	28	18	-38%
1.d External services	23	24	5%
1.e Various transfers *of which:*	48	83	72%
NSFF		45	
1.f Other current	66	65	-2%
Hospitals	*52*	*56*	*7%*
Others	*14*	*9*	*-37%*
1.g Reserves	16	16	0%
Interest subsidy	*16*	*16*	*0%*
2. Capital expenditures	**183**	**203**	**11%**
2.a Acquisitions of land, buildings, for the construction of roads ports, airports, and water networks	6	1	-84%
2.b Equipment	15	9	-40%
2.c Construction in Progress	128	154	21%
2.d Maintenance	26	23	-13%
2.e Other Expenditures Related to Fixed Capital Assets	8	16	90%
3. Other treasury expenditures	**290**	**339**	**17%**
Municipalities	47	174	272%
EDL	166	82	-50%
4. Unclassified expenditures	**2**	**6**	**150%**
5. Customs cashiers	**8**	**8**	**-1%**
6. Total expenditures 1/	**2,421**	**2,298**	**-5%**

Sources: Statement of account 36, Cashier spending, Public Debt Department figures, Fiscal performance gross adjustment figures

Notes:
1/ excluding foreign financed capital spending
Please note that previous Budget expenditures is classified according to their economic classification under Budget expenditures

In the first quarter of 2004, **current expenditures** cumulated at 1,743 billion which is 10 percent less than in Jan-Mar 2003. This decrease is mainly due to a 15 percent decrease in interest payments.

Personnel cost reached LL 738 billion for the first three months of 2004, registering a 4 percent decrease compared to QI 2003 because of a lower level of spending on retirement and end of services compensation which amounted to LL 208 billion compared to LL 254 billion in Jan-Mar 2003. Spending on wages and salaries remained almost stable, equaling LL 486 billion compared to LL 483 billion one year earlier.

Interest or debt service payments for the first three months of 2004 amounted to LL 800 billion, LL 187 billion less than the level in QI 2003. This decline is mainly attributed to the large drop in its domestic component, which amounted to LL 467 billion compared to LL 665 billion a year earlier. Foreign currency debt service increased slightly (by 3 percent) and amounted to LL 332 billion in QI 2004 compared to LL 322 billion in QI 2003. The four major developments contributing to this decline in the debt service bill could be summarized as follows:

(a) The issuance of LBP denominated Treasury Bills to the market was halted between February 2003 and November 2003 and, therefore, domestic interest payments due in the first quarter of 2004 were limited to:

(i) Debt committed prior to February 2003.

(ii) The newly issued 3-month securities since November 2003.

(b) The two-time strong decline in the overall level of interest rates since end-November 2002, led to savings in the debt service bill. Indeed, interest rates on the 24-month category declined from 14.14 percent in November 2002 to 9.2 percent in January 2003 and to 7.8 percent by end – March 2004.

(c) The funds raised from Paris II donor countries (at 5 percent) replaced high-cost debt maturing in 2003.

(d) The special scheme conducted with the Banque du Liban (at 4 percent), and the zero interest scheme of the Lebanese commercial banks also led to large savings in the debt service bill in QI 2004.

(e) The continuous trend in achieving primary surpluses during 2003, led to lower borrowing needs and hence lower debt service costs in QI 2004.

Various transfers reached LL 82 billion, 40 percent higher than in 2003. Of this amount, LL 45 billion was already paid to the NSSF in settlement of previous years' budget transfers.

Other current expenditures (such as external services, payment to hospitals and interest subsidies) remained almost stable compared to the previous year while current expenditures on material and supplies decreased by 38 percent and reached LL 18 billion by the end of QI 2004.

Capital expenditures increased by 11 percent compared to their level in the first quarter of 2003, due to higher spending on construction across the following agencies: the Displaced Fund, the Council of the South, and the Council for Development and Reconstruction (CDR).

Other treasury expenditures were 17 percent higher than in Jan-Mar 2003, the increase pertains to treasury transfers to Municipalities, which almost increased three folds from the previous year’s level when municipalities' transfers reached only LL 47 billion. The increase is due to payments made for solid waste management on behalf of the municipalities.

Table 7. Transfers to EDL*

(LL billion)	2003 Jan-Mar	2004 Jan-Mar	% Change
EDL	**166**	**82**	**50.5%**
Debt service**	91	82	50.5%
Treasury advances for fuel purchases	75	0	-100%
Expropriations	0	0	0

Source: MOF, DGF

** Does not include the LL 300 billion loan provided by BDL, and guaranteed by the Treasury*

** *Includes principal and interest payments*

EDL spending was equal to LL 82 billion in January-March 2004, which is almost half that of January-March 2003. This difference is explained by the Treasury advance, worth LL 75 billion, provided last year to EDL to finance the fuel purchases.

The decrease in the Treasury transfers for QI 2004 might be explained by the full disbursement of a LL 300 billion loan granted from BDL to EDL. The loan is guaranteed by the Treasury.

Section 4. Evolution of public debt

Table 8. Public Debt

Public Debt Outstanding by Holder as of End-March 2004
Amounts expressed in LL Billion

	Dec-01	Dec-02	Dec-03	Mar-04	change QI in LL billion	% change QI
Total debt	**42,637**	**47,274**	**50,365**	**50,677**	312	0.6%
Domestic debt	**28,214**	**25,302**	**26,843**	**27,911**	1,068	4.0%
a. Central Bank *of which:*	6,251	723	8,938	8,753	-185	-2.1%
Zero interest T-bills(1)			*3,508*	*3,508*		
Special T-bills issued at 4%			*4,299*	*4,299*		
b. Commercial Banks *of which:*	15,830	17,211	12,303	13,707	1,401	11.4%
Zero interest T-bills			*880*	*880*	*0*	
c. Other Domestic Debt (T-bills) *of which:*	6,133	7,368	5,603	5,455	-148	-2.6%
Public entities	*3,055*	*3,221*	*2,584*	*2,331*	*-253*	*-9.8%*
Foreign debt (2)	**14,423**	**21,972**	**23,522**	**22,766**	-756	-3.2%
a. Bilateral and Multilateral	2,046	2,214	2,582	2,585	3	0.1%
b. Paris II related FX debt		1,432	3,731	3,711	-21	-0.5%
c. BDL Eurobond		2,819	2,819	2,819	0%	0%
d. Market Eurobonds *of which:*	11,477	14,611	13,673	12,814	-859	-6.3%
Zero interest Eurobonds issued						
to Comm. Banks (3)			*1,083*	*1,073*	*-10*	*-0.9%*
e. Other foreign Debt (4)	900	896	717	838	121	16.9%
Public sector deposits	**1,913**	**2,964**	**3,019**	**3,113**	94	3.1%
Net debt	**40,724**	**44,310**	**47,346**	**47,565**	219	0.5%
Gross market debt	**31,612**	**36,866**	**29,712**	**30,479**	767	2.6%

Source: Ministry of Finance, Banque du Liban

Notes:

1. Represents intermediation of the Central Bank in the zero-interest scheme of commercial banks executed between Jan-Aug 2003
2. Certain foreign debt figures differ from previously published data due to the updating of the DMFAS system (debt management system)
3. Variation due to USD/Euro exchange rate fluctuation
4. Includes accrued interest and foreign currency private sector loans

Gross public debt as of end-March 2004 amounted to LL 50,677 billion, an increase of LL 312 billion or 0.6 percent over the debt level as of end-December 2003.

The mere 0.6 percent rate of growth of the public debt in QI 2004 resulted mainly from the 3.2 percent reduction in the foreign debt, following the repayment of USD 555 million, representing the amount of the two Eurobonds repaid on March 10 for USD 184.025 million and Euro 297.756 million.
Financing in QI 2004 was mainly from two sources: (a) LBP Treasury bill issuance (driven by strong demand from domestic commercial banks) and (b) the Treasury's share in the re-evaluation of the gold and foreign currency reserves account at the Central Bank (Account 115).

The treasury did not issue any new Eurobonds in the first quarter of 2004 and, therefore, the stock of outstanding Eurobonds declined from USD 12.70 billion to USD 12.22 billion.

Domestic debt reached LL 27,911 billion by end-March 2004, an increase of LL 1,068 billion or 4 percent over the end-2003 level. As demonstrated in Table 8, commercial banks have participated actively in the T-bill auctions- thereby increasing their portfolio by LL 1,400 billion in QI 2004. Market financing was the only source of financing for the Treasury in QI 2004 as the Central Bank's portfolio of Lebanese Pound T-Bills declined by LL 290 billion. The T-Bill portfolio of public entities also declined by LL 253 billion.

Gross Market debt, defined as gross public debt excluding the portfolios of the Banque du Liban, public institutions, bilateral and multilateral loans, and debt issued to the Paris II lending countries, increased by LL 767 billion or 2.6 percent since end-December 2003 reflecting the strong appetite of the market in subscribing to Government securities.

Net public debt (defined as gross public debt less public sector deposits) amounted to LL 47,565 billion as of end-March 2004, increasing by LL 220 billion or 0.5 percent since year-end 2003. Almost half of this rise is due to EDL's drawing down of the remaining part of a loan (LL 108 billion) extended to it by BDL for fuel purchases. The entire loan of LL 300 billion is guaranteed by the Treasury.

Table 9. Overall Weighted Average Cost of Outstanding Public Debt

	Date	Total Debt	Domestic Debt	Foreign Currency Debt
Before Paris II	Nov. 02	11.97%	13.82%	9.21%
After Paris II	Nov. 03	8.36%	9.23%	7.39%
	Mar. 04	8.15%	8.95%	7.17%
Change	Nov. 02-Nov. 03	-3.61	-4.59	-1.82
Change	Nov. 02-Mar. 04	-3.82	-4.87	-2.04

Source: Ministry of Finance

Table 10. Evolution of Primary Market Treasury Bill Yields

	Pre-Paris II (End-October 2002)	Post Paris II (January/February 2003)	December 31st, 2003	March 31st, 2004
3-months T-Bills	11.18%	6.96%	5.48%	5.29%
6-months T-Bills	12.12%	8.18%	6.53%	6.40%
12-months T-Bills	13.43%	9.13%	6.87%	6.76%
24-months T-Bills	14.64%	9.41%	7.99%	7.80%
36-months T-Bills			8.68%	8.66%

Source: Ministry of Finance

Section 5. Evolution of External Trade

Balance of Trade: The trade deficit marked a 9 percent increase, totaling USD 1,421 billion by the end of March 2004, owing to a 14 percent increase in imports, which in absolute terms outgrew the 34 percent increase in exports.

Table 12. External Trade

(USD million)	2003 Jan-Mar	2004 Jan-Mar	% change
Exports	350	471	34%
Imports	1,652	1,891	14%
Trade balance	-1,302	-1,421	9%

Source: MOF, Directorate General of Customs (DGC)

Imports in the first quarter of 2004 amounted to USD 1,891 million, compared to USD 1,652 million one year earlier. The increase in imports reflects mainly a USD 65 million increase in the imports of base metals and articles of base metals, a LL 53 million increase in the imports of machinery and mechanical appliances, a USD 35 million increase in products of the chemical and a USD 29 million increase in the transport equipment. The total increase in imports was large enough to offset the USD 16 million decrease in imports of mineral products.

Exports in the first quarter of 2004 reached USD 471 million, increasing by USD 121 million with respect to the first quarter of 2003. The increase in exports is mainly owed to the USD 57 million augmentation in the exports of machinery and mechanical appliances and the USD 26 million rise in the exports of base metals and articles of base metals. The significant increase in exports countered the USD 24 million decrease in the exports of pearls, precious or semi precious stones.

Table 13. Imports Distribution by Product

(USD million)	2003		2004			
	Jan-Mar	% share	Jan-Mar	% share	change	% change
Mineral products	343	21%	327	17%	-16	-5%
Machinery and Mechanical Appliances	182	11%	235	12%	53	29%
Products of the Chemical	162	10%	198	10%	35	22%
Base Metal and Articles of base Metal	95	6%	159	8%	65	69%
Transport Equipment	119	7%	148	8%	29	25%
Other Goods	751	45%	823	44%	73	10%
Total	**1,652**	**100%**	**1,891**	**100%**	**239**	**14%**

Source: MOF, DGC

• **Import Distribution by Product**:

Imports of **mineral products** decreased by 5 percent and cumulated at USD 327 billion as opposed to USD 343 million a year earlier. The diminution in mineral products import value resulted from the USD 31 million decrease in the imports of **mineral oils and fuels (other than car gasoline)** which receded to USD 208 million in the first quarter of 2004. This has occurred despite a USD 10 million increase in the imports of **salt, sulfur, earth and stones** which reached USD 19 million and a USD 5 million increase in the imports of **car gasoline** which reached USD 100 million in the first quarter of 2004.

The 29 percent increase in machinery **and mechanical appliances** imports, which reached USD 235 million by the end of March 2004 in contrast with USD 182 million in the first quarter of 2003, is the consequence of (1) a USD 32 million increase in the imports of **reactors, boilers, machinery and mechanical appliances**; **parts thereof** which cumulated at USD 134 million in the first quarter of 2004 and (2) a USD 20 million augmentation in the imports of **electrical machinery and equipment and parts thereof**.

Base metals and articles of base metals imports cumulated at USD 159 million compared to USD 95 million , increasing by 69 percent with respect to the first quarter of 2003. This increase was the outcome of (1) a boom in the **iron and steel imports** which grew by USD 55 million, reaching USD 94 million worth of imports and (2) a USD 4 million augmentation in the imports of **aluminum and articles thereof** which totaled USD 19 million in the first quarter of 2004.

Transport Equipment imports were worth USD 148 million in the first quarter of 2004 as opposed to USD 117 million one year earlier, witnessing a 25 percent increase compared to last year's first quarter. This growth was mainly fueled by the increase in the imports of cars which rose by USD 24 million during Jan-Mar 2004; cumulating at USD 104 million (please refer to Section 2, page 6 for further analysis on car imports).

Table 14. Exports Distribution by Product

(USD million)	2003		2004			%
	Jan-Mar	% share	Jan-Mar	% share	change	change
Pearls, precious or semi-precious stones	145	41%	121	26%	-24	-16%
Machinery and mechanical appliances	31	9%	87	19%	57	185%
Base metals and articles of base metals	25	7%	51	11%	26	105%
Prepared foodstuffs	34	10%	33	7%	-2	-5%
Products of the chemical	29	8%	30	6%	1	5%
Other exports	87	25%	149	32%	62	71%
Total	**350**	**100%**	**471**	**100%**	**120**	**34%**

Source: MOF, DGC

• **Export Distribution by Product:**

Exports of **pearls, precious or semi-precious stones** decreased by 16 percent and totaled USD 121 million during the first quarter of 2004 as opposed to USD 145 million in the first quarter of 2003.

Machinery and mechanical appliances exports increased by 185 percent, cumulating at USD 87 million during Jan-Mar 2004 in contrast to USD 31 million a year earlier. This increase resulted from (1) a USD 7 million rise in the exports of **nuclear reactors, boilers, machinery and mechanical appliances; parts thereof** which amounted to USD 22 million by the end of March 2004 (mainly exported to Iraq and Saudi Arabia) and (2) a USD 49 million increase in the exports of **electrical machinery and equipment and parts thereof** which became worth USD 65 million during Jan-Mar 2004 (mainly exported to Iraq and Kuwait).

Exports of **base metals and articles of base metals** doubled, reaching USD 51 million compared to USD 25 million during Jan-Mar 2003. This augmentation is mainly due to a USD 17 million increase in iron and steel exports, a USD 2 million increase in articles of **iron and steel** exports, a USD 3 million increase in **copper and articles thereof** exports and a USD 3 million increase in the exports of **aluminum and articles thereof**.

Table 15. Regional Distribution of Imports

(USD million)	2003		2004			%
	Jan-Mar	% share	Jan-Mar	% share	change	change
Total	**1,652**	**100%**	**1,891**	**100%**	**239**	**14%**
European Union *of which:*	661	40%	770	41%	109	16%
Euro-zone	*581*	*35%*	*658*	*35%*	*77*	*13%*
Arab Countries	245	15%	257	14%	13	5%
China	107	7%	145	8%	38	35%
United States	92	6%	119	6%	27	29%
Switzerland	60	4%	49	3%	-11	-19%
Other	486	29%	551	29%	64	13%

Source: MOF, DGC

• **Regional Distribution of Imports:**

Imports from the **European Union** increased by 16 percent, cumulating at USD 770 million in the first quarter of 2004 compared to USD 661 million during last year's first quarter. This increase is the outcome of two factors:

(a) A 13 percent nominal increase in the value of imports from the Euro-zone which reached USD 658 billion in Jan-Mar 2004 as compared to USD 581 million in Jan-Mar 2003. The nominal increase in the Euro-zone imports was slower than the appreciation of the Euro exchange rate versus the American Dollar which increased by 16.82 percent[6]. This means that either imports from the Euro-zone have decreased in real prices or that Lebanese importers have shifted their demand to cheaper Euro-zone imports or more plausibly a mixture of both effects.

(b) A 55 percent increase in the imports from the United Kingdom which reached USD 90 million in Jan-Mar 2004 compared to USD 58 million in Jan-Mar 2003. This increase is the result of:

(i) The strong Lebanese demand for the imports of machinery and mechanical appliances. British imports of machinery and mechanical appliances reached USD 28 million in Jan-Mar 2004 compared to an estimated USD 21 million in Jan-Mar 2003.The most imported machinery and mechanical appliance's sub category was the "electric generating sets and rotary converters "sub category whose imports amounted to USD 11 million. It is very interesting to notice that the most exported mechanical appliance's sub category to Iraq was also the" electric generating set

[6] *During the first quarter of 2004, one Euro was traded on average for USD 1.25 compared to USD 1.07 during the first quarter of 2003.*

and rotary converters" sub category with USD 38 billion worth of exports.

(ii) The increase of mineral products imports from the United Kingdom. Imports of mineral products reached USD 13 billion in Jan-Mar 2004 compared to an estimated USD 6 billion in Jan-Mar 2003.[7]

Imports from **Arab countries** augmented by 5 percent, reaching USD 257 million in the first quarter of 2004 compared to USD 245 million last year's first quarter. The main Arab import partners of Lebanon for the first quarter of 2004 were in descending order : Egypt (from where Lebanon imports mainly: base metals and articles of base metals, mineral products and vegetable products); Saudi Arabia (from where Lebanon imports mainly: Mineral products, plastics and articles thereof); Syria (from where Lebanon mainly imports: live stock, mineral products, base metals and articles of base metals); United Arab Emirates (from where Lebanon mainly imports: base metals and articles of base metals and pearls, precious and semi precious stones) and Jordan (from where Lebanon mainly imports vegetable products and products of the chemicals).

Imports from **China**[8] ranked as the third source of Lebanese imports in QI 2004, rose by 35 percent and moved up from USD 107 million in the first quarter of 2003 up to USD 145 million the first quarter of 2004. Lebanon mainly imported from China the following products: machinery and mechanical appliances, textiles and textiles articles and base metals and base metals articles.

Imports from the **United States** increased by 29 percent, amounting to USD 119 million compared to USD 92 million in Jan-Mar 2003. Lebanon imports from the United States the following products in descending order: vegetable products, prepared foodstuffs, machinery and mechanical appliances, transport equipment and products of the chemical.

Imports from **Switzerland** went down by 19 percent and reached USD 49 million in the first quarter of 2004 compared to USD 60 million one year earlier. The main imports from Switzerland are (in descending order): pearls, precious and semi precious stones, products of the chemicals and optical instruments and apparatus.

Table 16. Regional Distribution of Exports

(USD million)	2003		2004			%
	Jan-Mar	% share	Jan-Mar	% share	change	change
Total	**350**	**100%**	**471**	**100%**	**120**	**34%**
Arab Countries	103	29%	233	50%	130	126%
Switzerland	125	36%	101	21%	-24	-19%
European Union	37	10%	35	7%	-1	-3%
United States	21	6%	11	2%	-10	-50%
Other	65	18%	91	20%	25	38%

Source: MOF, DGC

• Regional Distribution of Exports:

Exports to **Arab countries** increased by 126 percent, totaling USD 233 million in Jan-Mar 2004 compared to USD 103 million in Jan-Mar 2003. This increase is the result of the export boom to Iraq. Lebanon's exports to Iraq reached USD 98 million during the first quarter of 2004 compared to USD 9 million in the first quarter of 2003 or an eleven fold increase, replacing Saudi Arabia as Lebanon's first export destination. The main exports to Iraq were machinery and mechanical appliances, mineral products, and prepared foodstuffs. Another reason behind this upsurge in Lebanese exports is the increase in exports to the United Arab Emirates which progressed by 45 percent, reaching USD 29 million in Jan-Mar 2003 compared to USD 20 million a year earlier. Lebanese exports to the United Arab Emirates consisted mainly of pearls, precious and semi precious stones. Exports to Syria continued to improve and registered an 80 percent increase. Exports to Syria cumulated at USD 27 million in Jan-Mar 2004 compared to USD 15 million in Jan-Mar 2003 and consisted of paper and paperboard articles thereof and mineral products.

[7] It should be noted that the British pound depreciated by 1.6 percent with respect to the US dollar between QI 2003 and QI 2004 and hence did not inflate nominally the value of imports from the United Kingdom.

[8] China was singled out in this report as it is becoming a major source of imports for Lebanon.

Exports to **Switzerland** receded by 19 percent, amounting to USD 101 million compared to USD 125 million. This decrease is perfectly correlated with the decrease in the exports of Lebanese pearls, precious and semi precious stones observed above.

As witnessed throughout last year, the depreciation of US dollar with respect to the Euro did not help Lebanon increase its exports to the European Union exports to the European Union slightly decreased from USD 37 billion to USD 35 billion.

Exports to the **United States** receded by 50 percent, reaching USD 11 million in Jan-Mar 2004 compared to USD 21 million in Jan-Mar 2003. Lebanese exports consisted mainly of prepared foodstuffs.

Section 6. Developments on Privatization/Securitization Fronts

Telecommunication Mobile Network:

Pursuing its drive for private sector's participation, and due to unsatisfactory bids for the Sale Auction of the two mobile licenses, alternatively, the Ministry of Telecommunications launched a successful tender for the management of the two mobile networks, for a period of four years, based on a new Tender Rules and Procedures (which among others includes tougher prequalification criteria regarding the subscribers' base). After distributing the tender documents to thirteen companies for participation, the tender for the management contracts was successfully completed in March 2004, with the selection of a German company, **Detecon International**, and a Kuwaiti company, **MTC** (Mobile Telecommunications Company) as successful bidders. MTC and Detecon who manage LibanCell and Cellis mobile networks respectively started operating their respective networks as of June 1st 2004. It will cost the Treasury $201 million and $209 million in management fees for Detecon and MTC respectively, over the 4 years contracts period. Both companies have in mind the modernization and the upgrading of the networks, which experienced over the last couple of years a relative setback in terms of development. It is worthy to note that both management contracts include an exit clause based on a six-month prior notice which allows the Lebanese government to launch a possible sale for licenses prior to the expiration of the four year management contract.

Appendix. Developments in the Electricity Sector

Pursuant to the failure of the tender launched by Electricite du Liban (EDL) on July 8, 2003 for the operation and maintenance of Deir Ammar and Zahrani power plants due to the lack of competition as only one company (Ansaldo-Sagem) had submitted an offer, EDL relaunched the same tender with modified terms on November 19, 2003. In this second attempt, Shanahan was the only qualified bidder to whom EDL granted a two-year operational and maintenance contract at a value of USD 26 Million. This contract was cancelled by the Council of Ministers for the lack of competition. In the meantime and in order to secure the continuity of operation, the contract of the current Italian operating company, ENEL, (which expired on November 15, 2003), was renewed twice for three months each time, rendering May 15, 2004 the new expiry date. On February 17, 2004, EDL launched the tender for the third time and three companies namely, Siemens (Germany), Ansaldo-Sagem (Italy) and Taamirat Niroo (Iran) submitted their offers on March 8, 2004. Taamirat Niroo was awarded the contract for the price of USD 20.86 Million, compared to a price of USD 22.8 Million offered by Ansaldo-Sagem, the only competitor after the withdrawal of Siemens. On May 12, 2004, after having signed the contract and paid all required stamp fees, Taamirat Niroo withdrew from the process forfeiting its performance bond. Taamirat Niroo justified its withdrawal by citing misinterpretation on its behalf of the tender rules and procedures document. On May 21, 2004, the board of directors of EDL awarded the contract to the second best bidder, Ansaldo-Sagem, for the operation and maintenance of the two plants for two years at a value of USD 22.8 Million.

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