REPUBLIC OF LEBANON
MINISTRY OF FINANCE

Public Finance Prospects 2006
Ministry of Finance Yearly Report

- **General Fiscal Developments:** The year 2006 may be divided in two parts separated by the July Israeli War. The first part of the year was characterized by a strong fiscal performance and growth - estimated at 5-6 percent - while the second part starting with the War and the subsequent political situation suffered significantly. The first half of 2006 was characterized by a strong performance in the primary surplus which reached LL 994 billion. In fact, the primary surplus in the first six months of 2006 exceeded the full year 2005 and almost equaled that of total 2004. However, as a direct impact of the July Israeli War, the primary balance ended the year registering a deficit - amounting to LL 25 billion - the first time since 2000. In terms of GDP, the small primary deficit (almost zero percent of GDP) compared to a surplus of approximately 2 percent of GDP in 2005. In turn, the total fiscal balance by the end of the year registered a deficit of LL 4,582 billion, deteriorating by 64 percent from LL 2,798 billion in 2005. In terms of GDP, the total deficit reached 13 percent of GDP after it had decreased to one of the lowest post-war levels at 8 percent of GDP in 2005 also despite difficult circumstances (please refer to Public Finance Prospects 2005 on the Ministry of Finance's website). **(section 1).**

- **Revenues and Expenditures:** The higher deficit resulted from an increase of 16 percent in total payments and a decrease of 2 percent in total receipts. Total expenditures registered an amount of LL 11,877 billion in 2006 mainly due to a rise in both interest payments and non-interest expenditures by approximately 29 percent and 10 percent respectively. Total revenues for 2006 yielded LL 7,295 billion, with the slowdown attributed to the War of July and blockade's impact on the Lebanese economy during the subsequent months as well as the difficult political environment which prevailed during the last quarter of the year. The decline in revenues can be explained by the 8 percent decrease in non-tax revenues despite the 1 percent and 2 percent increases in tax revenues and treasury receipts respectively. **(sections 2 and 3)**.

- **Public Debt Developments:** In 2006, net debt increased to 165.0 percent of GDP from 161.5 percent of GDP by end-2005. Gross public debt, which cumulated at LL 60,880 billion, decreased from 178.7 percent of GDP in 2005 to 177.7 percent of GDP in 2005. **(section 4)**.

- **External Trade:** The deficit in the trade balance reached USD 7,115 million in 2006, narrowing by 5 percent compared to the year 2005. Despite the July War and the interruption of exports and imports during the two-month blockade, exports rose by 21 percent or LL 403 billion, while imports increased by 1 percent or LL 58 billion. **(section 5)**.

- **VAT Developments:** In 2006 VAT developments included: (a) a 2.9 percent increase in the amount of VAT declared by businesses, with wholesale trade and retail trade being the highest contributors. (b) a 1 percent drop in the amount of VAT declared at customs from the import of merchandise, due to slight decreases in the import of several product categories. **(section 6).**

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Section I: Fiscal Overview 2006

Table 1. Summary of Fiscal Performance

(LL billion)	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	Change 2005-2006	% Change
Budget Revenue	568	562	6,984	6,867	-117	-1.7%
Budget Expenditures	649	813	7,802	8,641	839	10.7%
o/w Debt Service	395	478	3,534	4,557	1,023	28.9%
Budget Deficit/Surplus	**-81**	**-251**	**-818**	**-1773**	**-955**	**116.8%**
in % of Budget Expenditures	-12.5%	-30.8%	-10.5%	-20.5%		
Budget Primary Deficit/Surplus	**314**	**227**	**2,716**	**2,783**	**67**	**2.5%**
in % of Budget Expenditures	48.3%	27.9%	34.8%	32.2%		
Treasury Receipts	37	30	421	427	6	1.5%
Treasury Payments	363	468	2,401	3,236	835	34.8%
Total Budget and Treasury Receipts	605	592	7,405	7,295	-111	-1.5%
Total Budget and Treasury Payments	1,013	1,281	10,203	11,877	1,673	16.4%
Total Cash Deficit/Surplus	**-408**	**-689**	**-2,798**	**-4,582**	**-1,784**	**63.8%**
in % of Total Expenditures	-40.2%	-53.8%	-27.4%	-38.6%		
Primary Deficit/Surplus	**-13**	**-211**	**737**	**-25**	**-761**	**-103.4%**
in % of Total Expenditures	-1.2%	-16.5%	7.2%	-0.2%		

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

At the end of 2006, the **total deficit** (budget and treasury) deteriorated by 64 percent, reaching LL 4,582 billion from LL 2,798 billion in 2005. In terms of GDP, it was equivalent to 13.4 percent of GDP[1], increasing from 2005's level of 8.6 percent of GDP which was one of its lowest post-war levels. This deterioration was due to the impact of the July War and the maturing of some of the Paris II debt which had a positive effect during 2004 and 2005.

In terms of GDP, while revenues decreased to 21.3 percent of GDP in 2006 from 22.8 percent in 2005, expenditures increased to 34.7 percent of GDP in 2006 from 31.4 percent in 2005. The year 2006 ended with a **primary deficit** of LL 25 billion, dropping from the previous year's primary surplus of LL 737 billion or 2.3 percent of GDP.

[1] *The Economic accounts for 2004 were released in February 2007. Based on the published 2004 GDP of LL 32,357, and based on growth estimates (MOF, BDL, IMF) GDP for 2005 is calculated at LL 32,446 billion and GDP for 2006 at LL 34,**263** billion.*

Box 1: Real Impact of July War on Public Finances

The Lebanese economy's performance during the first half of 2006 signaled that annual real GDP growth would attain 6%. The impact of the 34-day war beginning in July and the near-two-month air and naval blockade as well as the tense political environment during the last couple of months of 2006 was such that a 0% rate of real GDP growth resulted instead. At an estimated LL 34,263 billion, Lebanon's GDP in 2006 was around LL 990 billion lower than what had been projected.

The war's impact was also reflected in public finances leading to a primary deficit of LL 25 billion in contrast to the LL 1,271 billion surplus projected for 2006 prior to the war. The primary deficit was mainly due to a LL 805 billion revenue loss and a LL 466 billion increase in primary expenditures as compared to 2006 pre-war projections.

The fiscal balance also underperformed in relation to the pre-war 2006 forecast. At a deficit of LL 4,582 billion, the fiscal balance was 35.2% worse than what had been expected for 2006. In addition to the LL 805 billion loss in revenues, the loss in the deficit of LL 1,193 billion was due to a LL 388 billion increase in expenditures.

Fiscal Impact of the July War - Historical Evolution of Fiscal Performance

(LL billion)	2003	2004	2005	2006 Pre -War	2006 Actual	Difference 2006 Pre-war and Actual	% Difference 2006 Pre-war and Actual
Revenues	6,654	7,514	7,405	8,100	7,295	-805	-9.9%
Expenditures	10,592	10,540	10,203	11,489	11,877	388	3.4%
of which Primary Expenditures	5,718	6,519	6,669	6,854	7,320	466	6.8%
Fiscal Balance	-3,938	-3,026	-2,978	-3,389	-4,582	-1,193	35.2%
Primary Balance	936	995	736	1,246	-25	-1,271	-102.0%

Source: Ministry of Finance

** This box is an update to Table 2 from the Ministry of Finance's publication Impact of the July War on the Public Finances. 2006 published on MOF's website.*

Section II: Revenue Outcome

Table 2. Total Revenue

(LL billion)	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	% Change
Budget Revenues, of *which:*	**568**	**562**	**6,984**	**6,867**	**-1.7%**
Tax Revenues	*378*	*383*	*4,867*	*4,922*	*1.1%*
Non-Tax Revenues	*190*	*179*	*2,117*	*1,945*	*-8.1%*
Treasury Receipts	**37**	**30**	**421**	**427**	**1.5%**
Total Revenues	**605**	**592**	**7,405**	**7,295**	**-1.5%**

Source: MOF, DGF

Total revenues in 2006 were LL 7,295 billion equivalent to 21.3% of GDP (LL 7,216 billion net of the LL 79 billion grants or 21.1% of GDP); a loss of around LL 111 billion compared to the collected LL 7,405 in 2005 or 22.8 percent of GDP in 2005 (a 1.5 percent decline). However, the decrease in revenues is more pronounced if the one off exceptional inheritance tax amount of approximately LL 164 billion is excluded, in which case total revenues for 2006 are LL 7,131 billion or LL 274 billion below the collection level of 2005. This 4 percent drop in revenues is due to the July War, the near two-month blockade, the subsequent political instability, and the hike in international oil prices during the second and third quarter of the year. In the first half of the year, revenues were experiencing a healthy growth rate of 15 percent compared to the first half of 2005. However, this growth was reversed in the second half of the year, when revenues decreased by 17 percent compared to the second half of 2005.

In terms of the breakdown of revenues, non-tax revenues decreased by 8 percent (equivalent to LL 172 billion), tax revenues rose by 1 percent, and treasury receipts increased by almost 2 percent

Budget revenues decreased by 1.7 percent in 2006, reaching LL 6,867 billion in 2006 (or 20 percent of GDP) down from LL 6,984 billion (or 21.5 percent of GDP) in 2005. As with almost all revenue items, the deterioration is mainly due to the second half of the year's collection performance. During the first six month of 2006, budget revenues had increased by 17 percent. This increase was reversed in the second half of the year where budget revenues decreased by 18 percent. Within budget revenues, non-tax revenues decreased by 8 percent while tax revenues declined by 1 percent in 2006**.**

Tax revenues (as part of budget revenues) totaled LL 4,922 billion in 2006 or 1 percent higher than the outcome of 2005 where tax revenues were LL 4,867 billion. However, this indicates a deterioration as a percentage of GDP, where tax revenues represented 14.4 percent of GDP in 2006, compared to 15 percent of GDP in 2005. During the first half of the year tax revenues had increased by 16 percent, however, the events of the second half of the year, led to this result. The total increase of LL 55 billion in tax revenue reflects of an increase in tax on income, profit and capital gains and the tax on property by 11.4 percent and 39.6 percent respectively which offset the decrease in domestic taxes on goods and services and taxes on international trade by 2.8 percent and 15.3 percent respectively:

Tax on income, profits and capital gains Income taxes generated LL 1,166 billion or 3.4 percent of GDP; 11 percent higher collection than in 2005 which reached LL 1,047 billion or 3.2 percent of GDP for 2005. This improvement represents higher collection from all income tax sources (with the exception of penalties on income tax which represents a small percentage of the total and which is due to amnesty on penalties, Decision 827, dated September 14, 2006 (note that the timeframe of the amnesty was extended several times reaching mid-July 2007.)

(a) Collection of the **income tax on profits** in 2006 increased by 8 percent, amounting to LL 442 billion by December 2006, compared to LL 409 billion by December 2005. Most filing and payment took place in May-June prior to the break of the July war, and 90 percent of the total amount was collected in the first half of the year and hence limited impact in the second half of the year. Compared to 2004 which is considered a better fiscal year than 2005, collection in 2006 is approximately 6 percent higher.

(b) The **income tax on wages and salaries** for the year 2006 collected LL 196 billion, up 5.3 percent from the LL 186 billion collected in 2005. Since the implementation of the DASS reform, and with the continuous build up of the wage earner database, the average collection amount from the withheld tax on wages and salaries per declaration period (quarterly) has risen from approximately LL 30 billion in 2003, LL 33 billion in 2004, LL 41 billion in 2005, to around LL 42 billion in 2006. The DASS reform has so far resulted in an overall 35 percent improvement in collection since the start of this administrative reform process.

(c)With revenues amounting to LL 98 billion in 2006, **income taxes on capital gains and dividends** witnessed a 3.5 percent increase compared to the LL 95 billion collected in 2005. The majority of this tax is collected in the first half of the year (70 percent) and had experienced a growth of 22 percent. The decrease of 21 percent in the second half of the year led to an overall limited growth.

(d) The **5% tax on interest income** collected LL 415 billion by December 2006, witnessing 23.3 percent higher revenues than the LL 337 billion collected in 2005. The interest income tax has witnessed a 186 percent rise in collection since its implementation in 2003. The collection has risen from LL 145 billion in 2003 to LL 229 billion in 2004 to LL 338 billion in 2005 to reach LL 415 billion in 2006. In regards to source by currency, 60 percent of the total collection in 2006 came in LL and the remaining 40 percent came in foreign currency. Around 60 percent of this amount was collected from the commercial banks, and 40 percent was received from the BDL.

Table 3. Tax Revenue

(LL billion)	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	% Change
Tax Revenues:	**378**	**383**	**4,867**	**4,922**	**1.1%**
Taxes on Income, Profits, & Capital Gains, *of which*:	**45**	**57**	**1,047**	**1,166**	**11.4%**
Income Tax on Profits	*13*	*17*	*409*	*442*	8.0%
Income Tax on Wages and Salaries	*4*	*3*	*186*	*196*	5.3%
Income Tax on Capital Gains & Dividends	*3*	*5*	*95*	*98*	3.5%
Tax on Interest Income (5%)	*22*	*29*	*337*	*415*	23.3%
Penalties on Income Tax	*2*	*2*	*17*	*13*	-25.3%
Taxes on Property, *of which:*	**71**	**57**	**414**	**579**	**39.6%**
Built Property Tax	*9*	*15*	*90*	*94*	4.7%
Real Estate Registration Fees	*60*	*36*	*291*	*281*	-3.3%
Domestic Taxes on Goods & Services, *of which:*	**134**	**144**	**1,896**	**1,844**	**-2.8%**
Value Added Tax	*114*	*127*	*1,693*	*1,659*	-2.0%
Other Taxes on Goods and Services, of which:	*20*	*16*	*192*	*175*	-9.0%
Private Car Registration Fees	*11*	*7*	*108*	*109*	1.4%
Passenger Departure Tax	*9*	*9*	*83*	*64*	-22.7%
Taxes on International Trade, *of which:*	**107**	**109**	**1,268**	**1,074**	**-15.3%**
Customs	*42*	*43*	*481*	*461*	-4.1%
Excises, of which:	*65*	*67*	*787*	*613*	-22.1%
Petroleum Tax	*22*	*35*	*362*	*230*	-36.4%
Tobacco Tax	*17*	*16*	*189*	*162*	-14.4%
Tax on Cars	*26*	*15*	*231*	*217*	-6.3%
Other Tax Revenues (namely fiscal stamp fees)	**21**	**17**	**241**	**259**	**7.6%**

Source: MOF, DGF

Proceeds from the **Taxes on Property** witnessed an overall increase of almost 40 percent, at LL 579 billion in 2006 (or 1.7% of GDP), compared to LL 414 billion in 2005 (1.3% of GDP which was the average collection over the past years). This increase is due to a one time exceptional increase in inheritance tax (in the amount of approximately LL 164 billion) which outgrew the 3 percent decline in real estate registration fees.

(a) **Recurrent Built Property Tax,** the recurrent component of the tax**,** generated LL 94 billion in 2006, almost 5 percent higher than the LL 90 billion collected over January-December 2005. This overall rise in collection stems from the 18 percent year on year improved performance in the first half of the year, and the 75 percent year on year rise in collection during the month of December 06. This latter may be attributed to the amnesty on due penalties granted post war (decision 827, dated September 14, 2006).

(b) **Real Estate Registration Fees,** the non-recurrent taxes on property, collected LL 281 billion in 2006 compared to LL 291 billion for 2005, representing a decrease of 3.3 percent. As is the case with many items in revenues, the decrease stems from a slower second half of the year. In this case, real estate registration fees had increased by 40 percent during the first half of the year. The results of the year reflect the 2.8 percent decrease in sales transaction to 50,140 operations for the year 2006 down from 55,099 transactions in 2005.

Total receipts from **domestic taxes on goods and services** (exclusive of excises) equaled LL 1,844 billion by December 2006 or 5.4% of GDP, 3 percent below the collection level in January-December 2005 at (or 5.8% of GDP). This is mainly due to near 2 percent lower revenues from the VAT and around 23 percent lower receipts from passenger departure tax.

The year 2006 collected LL 1,659 billion or 4.8% of GDP from the **Value-Added Tax**, almost 2 percent below the LL 1,693 billion (5.2% of GDP) collected during the year 2005.

- ⇨ Of this amount LL 1,153 billion were collected at customs, compared to LL 1,177 billion in 2005 mirroring a 2 percent drop in non fuel imports in 2006[2] which is explained by the war of July and the near two months blockade (please refer to trade section for the 2006 trade outcome); and
- ⇨ LL 506 billion were collected from internal economic activity, compared to LL 516 billion in 2005 i.e. a 2 percent decline in revenues. This may be a reflection of the general slowdown in consumption following the war in July, the blockade, the deteriorating political situation and the demonstrations. Note that decision number 826 dated September 14, 2006 granted taxpayers the possibility of settling their second quarter 2006 VAT on installment over November-December 2006 and February-March 2007, meaning that on accrual basis, QII VAT dues will still flow to the Treasury in the first quarter of 2007.

It is worth nothing that VAT collection had increased by 15 percent in the first half of the year compared to 2005 reflecting the resumption of economic activity in the first half of the year (indeed, it was estimated that the economy during the first half of the year was growing at more than 5%), as compared to the first half of 2005 where activity was severely impacted by the assassination of Prime Minister Rafic Hariri.

Other taxes on goods and services (namely include car registration fees and the passenger departure tax) collected a total of LL 175 billion for 2006, 9 percent less than the amount collected in 2005. This overall decrease resulted mainly from the 23 percent decrease in departure tax which overshadowed the increase in receipts from car registration fees by near 1 percent:

(1) Private car registration fees[3] collected LL 109 billion during 2006, 1.4 percent higher than the collection level in 2005. This result reflects a combination of strong car trading activity in the first half of the year and a significant slow down in the second half of the year. By June 2006, private car registration fees had witnessed a 38 percent increase in revenues, in line with a 40 percent rise in the number of cars imported during that same period. This trend was reversed after the July War with the year ending with lower car imports by 5 percent.

(2) The passenger departure tax collected LL 64 billion in 2006, 23 percent lower than 2005. The July War and subsequent political situation led to lower number of tourists in the second half of the year with 2006 ending the year with 1,062,635 tourists, a decrease by 6.7 percent compared to 2005. It is worth noting that at the eve of the War, 2006 was expected to be a record year for the

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[2] *The impact of the nominal rise in fuel prices on VAT collection at imports did not compensate for the VAT loss from the drop in non fuel imports.*

[3] *One time fee paid upon the purchase of a car.*

number of tourists. In 2005, 1,139,524 tourists visited Lebanon, compared to 1,278,469 tourists in 2004.

Taxes on international trade (custom duties and excises) collected LL 1,074 billion (3.1% of GDP) by December 2006, down nearly 15 percent from LL 1,268 billion (3.9% of GDP) by December 2005. The performance of taxes from international trade in 2006 lags behind the 2004 collection at 5% of GDP, and well behind an average of 6% of GDP in the subsequent years (prior to the capping of domestic prices of car gasoline). For 2006, the nearly two-month disruption of trade activity in the midst of the July war, the resulting blockade (which induced a 2 percent drop in non fuel imports), and the hike in international oil prices significantly impacted revenue collection. Excises decreased by approximately 22 percent and customs receipts declined by 4 percent.

Excises[4] generated LL 613 billion in the year 2006 (1.8% of GDP), 22 percent lower than the LL 787 billion collected during 2005 (2.4% of GDP). In addition to the July War and two month blockade, the hike in international oil prices experienced in the spring-summer of 2006, whereby the crude oil barrel reached a peek at around $73 per barrel, negatively affecting excise revenues from car gasoline (given the capping regime). The year 2006 further witnessed a drop in the revenue collected from the excises on tobacco (by almost 14 percent) and on cars (by 6 percent).

Car Gasoline: Excises from car gasoline decreased to LL 230 billion (0.67% of GDP), 32 percent below 2005 collection level (1.1% of GDP) which is equivalent to LL 132 billion less revenues. The decrease is due to lower volume of imports and lower effective excise per liter due to the cap on the retail price of gasoline and a hike in import prices. In 2006, Lebanon imported 1.624 billion liters down from 1.666 billion liters in 2005 and 1.665 billion liters in 2004; however at a value of LL 1,183 billion in 2006 compared to LL 1,051 billion in 2005 and LL 770 billion in 2004. The higher nominal value of car gasoline import is due to higher average import price per liter which increased by 16 percent to LL 729 per liter in 2006 up from LL 631 per liter in 2005, (note that the average import price was LL 462 per liter in 2004). However given the capping structure, the average effective excise rate collected decreased to LL 140 per liter in 2006 down from LL 217 per liter in 2005 (the average effective excise rate was LL 386 per liter in 2004, and LL 489 per liter prior to the capping of domestic prices in accordance to a Council of Ministers' decision on May 20th, 2004).

Tobacco: Receipts from excises on tobacco imports for the year 2006 totaled LL 162 billion dropping by 14 percent compared to the year 2005. The decrease was consistent with the decline in the value of tobacco imports in 2006 to LL 159 billion down from LL 185 billion worth of tobacco products imported in 2005. The decline was a result of a decrease of imports in tons by 17 percent.

Cars: With LL 217 billion of excises collected, the year 2006 witnessed a drop of 6 percent in receipts from excises on cars, explained by a 5 percent decline in the number of cars imported (41,986 car imported in 2005 compared to 39,852 car imported in 2006). However, the slight rise in car registration fees collected in 2006 (a 1.4 percent rise from 2005 collection level) in the context of a slower imported car market may hint at the fact that the second hand car market was more active this year. The total value of cars imported decreased by 4 percent totaling LL 810 billion for 2006 compared to LL 847

[4] *Excises are collected at imports on car gasoline, tobacco and cars mainly, and on alcoholic beverages.*

billion for 2005. The average price per car imported in 2006 was 1 percent higher than that of 2005.

Customs revenues amounted to LL 461 billion (1.3 percent of GDP) by December 2006, 4 percent lower than the LL 481 billion (or 1.5 percent of GDP) collected in 2005. Imports, as is the case with most economic activity, were robust in the first half of the year and sluggish in the second half of the year, ending the full year with a 1 percent increase compared to 2005 (please refer to the trade section for a more comprehensive overview of international trade performance). Although total imports for 2006 increased to USD 9,398 million compared to USD 9,340 million in 2005, the 0.6 percent rise is explained by a 9 percent nominal rise in fuel imports (from USD 2,151 million in 2005 to USD 2,348 million in 2006) due to the hike in international oil prices experienced during the second and third quarter of the year. Note that very little custom duties are levied on the import of fuel products, and therefore custom revenues did not rise with the nominal rise in fuel imports. On the other hand, non fuel imports totaled USD 7,050 m in 2006 compared to USD 7,189 m in 2005 witnessing a drop of 2 percent.

Other tax revenues (mainly fiscal stamps) reached LL 259 billion in the year 2006, registering an 8 percent increase from the level of collection in the previous year. Fiscal stamp revenues for the first half of the year registered LL 148 billion, a 35% increase compared to the same period in 2005, a further indication of the economy's strong performance. In contrast, the decline in other tax revenues during the second half of 2006 reflects the subsequent slowdown of economic activity. At LL 111 billion, other tax revenues in the period July-December 2006 were 15% lower than those during the same period in 2005.

Table 4. Non-Tax Revenue

(LL billion)	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	% Change
Non-Tax Revenues	**190**	**179**	**2,117**	**1,945**	**-8.1%**
Income from Public Institutions and Government Properties, *of which*:	**135**	**133**	**1,663**	**1,428**	**-14.1%**
Income from Non-Financial Public Enterprises, *of which*:	131	131	1,614	1,394	-13.6%
Revenues from Casino Du Liban	*5*	*6*	*51*	*42*	-17.9%
Revenues from Port of Beirut	*0*	*0*	*58*	*0*	-100.0%
Budget Surplus of National Lottery	*10*	*0*	*47*	*53*	12.8%
Transfer from the Telecom Surplus	*116*	*125*	*1,456*	*1,298*	-10.9%
Property Income (namely rent of Rafic Hariri International Airport)	*4*	*2*	*44*	*29*	-34.2%
Other Income from Public Institutions (interests)	*1*	*1*	*6*	*5*	-3.9%
Administrative Fees & Charges, *of which*:	**46**	**39**	**365**	**426**	**16.6%**
Administrative Fees, *of which*:	36	30	290	342	17.8%
Notary Fees	*2*	*1*	*17*	*17*	-0.8%
Passport Fees/ Public Security	*8*	*6*	*88*	*111*	26.2%
Vehicle Control Fees	*19*	*17*	*129*	*156*	20.2%
Judicial Fees	*2*	*2*	*20*	*19*	-3.5%
Driving License Fees	*2*	*2*	*16*	*23*	42.3%
Administrative Charges	5	5	25	19	-24.9%
Sales (Official Gazette and License Number)	1	1	3	3	9.5%
Permit Fees (mostly work permit fees)	4	3	39	50	27.8%
Other Administrative Fees & Charges	1	1	8	12	56.0%
Penalties & Confiscations	**1**	**0**	**4**	**4**	**4.9%**
Other Non-Tax Revenues (mostly retirement deductibles)	**7**	**6**	**85**	**87**	**2.4%**

Source: MOF, DGF

Non-tax revenues generated LL 1,945 billion in 2006, decreasing by 8 percent compared to 2005. Non-tax revenues' share of GDP also deteriorated to 5.7 percent of GDP compared to 6.5 percent of GDP in 2005.The lower revenues are mainly attributed to a slower second half of the year. During the first six months of the year, non-tax revenues had increased by 19 percent, however events in the second part of the year led to a 26 percent decrease in the last six months of the year compared to 2005. The 8 percent decrease represents 14 percent lower revenues from public institutions and government properties and 17 percent higher administrative fees and charges.

Income from public institutions and government property reached LL 1,428 billion in 2006 (4.2% of GDP), compared to LL 1,663 billion for 2005 (5.1% of GDP), representing a 14 percent decrease in receipts. This decline is due to lower revenue collection from several components under this category, the main of which being transfers from the **telecom budget surplus.** In effect, revenues from the telecom budget surplus for 2006 amounted to LL 1,298 billion, compared to LL 1,456 billion in 2005, representing an 11 percent decrease in transfers to the Treasury from the Ministry of Post and Telecommunication. This decline is due to the payment of the arbitration settlement to France Telecom in the amount of LL 48 billion in the first half of the year, and to the arbitration settlement to Libancell in the amount of LL 226 billion in the second half of the year[5]. This lower transfer may also be explained to a certain extent by the damages to the mobile and fixed networks incurred during the war.

Furthermore, revenues from the **Casino du Liban** decreased by nearly 18 percent as compared to the year 2005, reaching LL 42 billion at the end of 2006, a direct impact of the war in July and the disruption of tourism activity,

On a cash basis, no collections were received from **Port of Beirut** by end of 2006 (the cash transfer was made in the beginning of 2007) compared to LL 58 billion in 2005 (which represents the transfer of the budget surplus of the Port of Beirut for the years 2005 and 2004).

The only item under income from public institutions and government properties that exhibited an increase was revenues from budget surplus of the **National Lottery**. This revenue amounted to LL 53 billion in 2006, representing an increase of almost 13 percent compared to the previous year.

Administrative fees and charges collected LL 426 billion in total for 2006 (1.2% of GDP), rising by 17 percent from the 2005 levels (1.1% of GDP). This increase is attributed to the strength of the first half of the year where administrative fees and charges rose by 56 percent offsetting the weakness in the second half of the year where these revenues decreased by 14 percent.

Administrative fees increased by LL 52 billion to reach LL 342 billion in 2006 up from LL 290 billion in 2005. Again, the first half of the year increased by 56 percent offsetting the 12 percent decrease in the last six months of the year. The total rise represents higher revenues from **passport fees** by LL 23 billion and LL 26 billion additional revenues from **vehicle control fees**. Passport fees increased by 47 percent during the first half of the year and 8 percent in the last six months of 2006. Figures show that the increase in passport fees was more acute in July and August which could be explained by increased demand to travel out of Lebanon during the war. The increase in vehicle control fees may be explained by the Article 29 of Budget Law 2005 (Law 715, February 3rd, 2006) which granted 85% amnesty on due penalties on vehicle control fees outstanding till end of 2005, with a period of settlement extending till end of May 2006 (therefore part of the LL 155 billion collected in 2006 is an amnesty amount on past due penalties).

[5] *France Telecom and Libancell were two mobile operators with BOT contracts with the Lebanese Government. In June 2001, the Government notified the two mobile operators of the early termination of their BOT contracts in accordance with their respective terms and the BOT Contracts were terminated effective on August 31, 2002. Following this dispute, each of the mobile telephone network operators initiated arbitration proceedings. The arbitration proceedings between each of the former mobile operators in the Republic and the Government resulted in two arbitration awards in favor of the former operators. The transfers mentioned refer to the settlement of the arbitration amount.*

Work permit fees further witnessed LL 11 billion additional revenues in 2006, compared to the collection level in 2005 again due to the strength of the first part of the year.

Treasury revenues for the year 2006 amounted to LL 427 billion, increasing by 2 percent compared to last year's collection level. This amount includes LL 79 billion grants received for humanitarian aid and relief purposes during the war that were transferred to the High Relief Council[6]. It is worth noting that Municipalities' revenues declined by LL 50 billion in 2006 compared to their 2005 level.

[6] *Refer to expenditure section, p.18.*

Section III: Expenditure Outcome

Table 5. Expenditures by Transaction Classification

(LL billion)	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	% Change
Total Expenditures	**1,013**	**1,281**	**10,203**	**11,877**	**16.4%**
Budget Expenditures	**649**	**813**	**7,802**	**8,641**	**10.7%**
Expenditures Excluding Debt Service	254	335	4,268	4,084	-4.3%
Debt Service, *of which*:	**395**	**478**	**3,534**	**4,557**	28.9%
Local Currency Debt	190	279	1533	2,368	*54.5%*
Foreign Currency Debt, of which:	205	201	2002	2,189	*9.3%*
*Eurobond Coupon Interest**	153	145	1709	1,838	*7.5%*
*Specialbond Coupon Interest**				13	
Concessional Loans Principal Payments	39	43	179	223	*24.6%*
Concessional Loans Interest Payments	13	13	114	116	*1.5%*
Treasury Expenditures , *of which*:	**393**	**468**	**2,401**	**3,236**	**34.8%**
Municipalities	*49*	*39*	*384*	*405*	*5.4%*
Previous Years' Appropriations	*177*	*187*	*648*	*656*	*1.3%*
Non-Interest Expenditures (Total Expenditures minus Debt Service)	**618**	**803**	**6,669**	**7,320**	**9.8%**

Source: MOF, DGF

** Includes general expenses related to Eurobond transactions*

Total Expenditures (budget and treasury) for the year 2006 reached LL 11,877 billion, 16.4 percent higher than expenditures in 2005. In terms of GDP, total expenditures represented 34.7 percent of GDP in 2006, up from 31.4 percent of GDP in 2005. The increase came in major part as a result of the July war. In fact, in the first half of the year, the government was able to limit the increase in total expenditures to 7.5 percent compared to 2005, however, expenditures had to be increased significantly during the second half of the year (by approximately 33.6 percent). Most importantly, the increase in the first half of 2006 was basically driven by the rise in interest expenditure which rose during the first half of June 2006 by 38 percent, meanwhile non-interest expenditure, as a result of the tight control on spending, dropped by 7.2 percent (please refer to PFM of June 2006 for further details).

Total Primary Expenditures (Non-Interest Expenditures) represented 21.4 percent of GDP in 2006, up from 20.6 percent of GDP in 2005. These expenditures amounted to LL 7,320 billion in the year 2006 compared to LL 6,669 billion in 2005. The government had managed to curb primary expenditures in the first half of the year to the extent that primary expenditures were decreased by 7.2 percent compared to the first half of the year in 2005. However, during the last six months of the year, spending increased by 26.5 percent compared to the second half of the year 2005. The LL 651 billion increase in primary expenditures mainly resulted from two major factors:

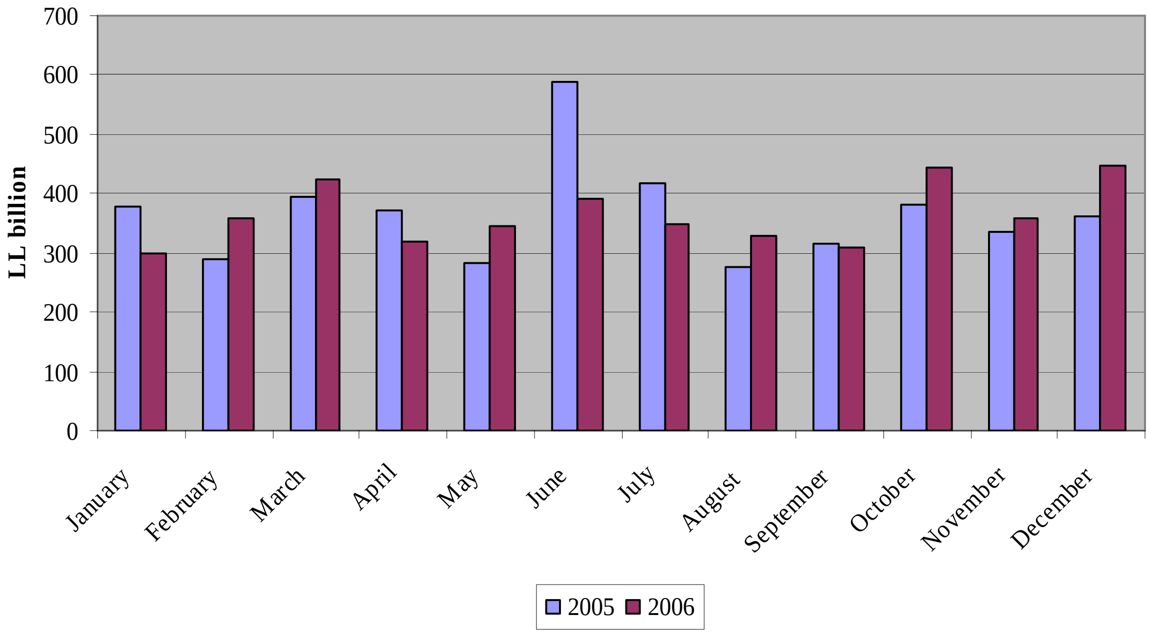
i) An increase of LL 396 billion in spending on or on behalf of EDL by the Treasury: As guarantor of EDL oil purchase agreements with Sonatrach and Kuwait Petroleum Corporation that have been effective as of January 2006 and September 2005 respectively, the Treasury started paying for EDL's oil purchases when they started falling due in June 2006.

ii) The direct war-related impact that led to an increase of LL 114 billion in personnel cost, and a transfer to the High Relief Council of LL 98 billion.

Looking at expenditures from an economic perspective, the year 2006 witnessed an increase in current and capital expenditures, as well as treasury spending.

Current expenditures for the year 2006 amounted to LL 8,927 billion, compared to LL 7,925 billion in 2005, representing an increase of 12.6 percent, which was mainly due to higher debt service by LL 1,023 billion.

Monthly Primary Current Spending



Primary current expenditures amounted to LL 4,370 billion in 2006, slightly lower than 2005 when primary current expenditure registered LL 4,391 billion. Further details on current expenditures are highlighted in what follows *(also please refer to table 6)*:

Personnel cost in 2006 amounted to LL 3,307 billion, LL 114 billion higher than the level of 2005. The 3.6 percent increase resulted from higher retirement and end-of-service compensations by LL 63 billion, and from a rise in salaries and wages by LL 59 billion. It should be noted that there is no patterned trend for the retirement and end-of-service indemnity growth, as they depend highly on several factors that affect this trend. For instance, employees have the right to choose to have their benefits paid as a lump sum without having any pension pay; in this case, the end-of-service part will increase more than the increase in the retirement amount. The higher salaries and wages are mainly due to the additional recruitment in the army and the security forces after the July Israeli War and in response to the implementation of resolution 1701. *(For more information on salaries and wages please refer to box 3).*

Interest payments registered LL 4,557 billion in 2006, compared to LL 3,534 billion in 2005, an increase of 29 percent. This increase resulted from the 55 percent higher local currency debt service and 9 percent rise in foreign currency debt service. The main reasons behind this increase in the debt service for 2006 stems from the matured stock of:

- ⇨ Domestic currency zero-rated special treasury bills and
- ⇨ Foreign currency zero-rated special bonds.

These bonds were issued by the commercial banks in the context of their contribution to the Paris II Conference and matured during the period January-July 2005. *(For more details, please refer to the Debt Section).*

Materials and supplies reached LL 140 billion by December 2006, LL 73 billion lower than their level at the end of 2005. The higher spending in 2005 is due to the near LL 93 billion payment of public administrations' electricity bills to EDL, in accordance with Law # 672 enacted on February 17th, 2005 which opened an additional allocation in 2004 Budget Law, under the Ministry of Finance's budget to reimburse accrued electricity bills on behalf of public administrations.

External services (rent, postal services, insurance, advertisement and public relations) amounted to LL 87 billion, up by LL 5 billion from their end-2005 level.

Various transfers reached LL 498 billion in 2006, down from LL 569 billion in 2005. The main reason for the lower expenditures is the lower NSSF transfers by LL 90 billion. NSSF payments in 2006 totaled LL 200 billion compared to LL 290 billion in 2005. The transfer in 2005 was based on Law 671 issued in February 5, 2005 stipulating the opening of LL 240 billion additional Budget allocation in the 2004 Budget. This allocation is earmarked to reimburse government contributions to NSSF on account of 2003 & 2004.Meanwhile, the transfer in 2006 was based on decision made by Council of Ministers in settlement of previous year's accumulated appropriations.

When excluding the transfers made to the NSSF, expenditures under this article increased by LL 19 billion compared to 2005.

Table 6. Expenditures by Economic Classification

(LL billion)	2005 Jan-Dec	2006 Jan-Dec	% Change
1. Current expenditures	**7,925**	**8,927**	**12.6%**
1.a Personnel cost, *of which*	3,193	3,307	3.6%
Article 13: Salaries and wages	*2,129*	*2,188*	*2.8%*
Retirement and end of service compensations	*864*	*927*	*7.2%*
1.b Debt Service payments	3,534	4,557	28.9%
1.c Materials and supplies	213	140	-34.3%
1.d External services	82	87	6.0%
1.e Various transfers	569	498	-12.5%
o/w NSSF	*290*	*200*	*-31.0%*
1.f Other current	258	258	*0.0%*
Hospitals	*192*	*223*	16.0%
Others	*66*	*33*	*-50.1%*
1.g Reserves	75	80	7.0%
Interest subsidy	*75*	*80*	*7.0%*
2. Capital expenditures	**534**	**551**	**3.3%**
2.a Acquisitions of land, buildings, for the construction of roads, ports, airports, and water networks	15	12	-23.5%
2.b Equipment	25	25	-2.4%
2.c Construction in Progress	413	435	5.4%
2.d Maintenance	46	48	5.7%
2.e Other Expenditures Related to Fixed Capital Assets	35	32	-8.7%
3. Other treasury expenditures, *of which*	**1,701**	**2,365**	**39.0%**
Municipalities	384	405	5.5%
EDL*	833	1,370	64.4%
Transfers to High Relief Council		98	
Treasury advances for water authorities	48	0	-100.0%
Treasury advances for diesel oil subsidy	14	52	269.0%
Treasury advances for Telecom companies	15	0	
4. Unclassified expenditures	**5**	**1**	**-75.6%**
5. Customs cashiers	**39**	**32**	**-16.3%**
6. Total expenditures (excluding CDR foreign financed)	**10,203**	**11,877**	**16.4%**

Source :Statement of Account 36, cashier spending, Public Debt Department figures , Fiscal performance gross adjustment figures
** EDL figure for 2005 excludes Treasury advances to water authorities for their accrued electricity bills (LL 48 billion) and Budget transfers (LL100 billion) under the line item "Materials and Supplies" for the settlement of public administrations' accrued electricity bills. Table 7 below includes these transfers.*

Box 2. Salaries and Wages in 2006

Salaries and wages cover the salaries and wages of all employees (such as full-time and part-time employees, consultants, advisors, workers earning a lump-sum-amount), compensations (such as family, overtime, transportation), allowances (including sickness and maternity, marriage, birth, death, hospitalization, schools, social spending, treatment in medical centers), bonuses, contributions to mutual funds (such as those of COOP employees, members and employees of parliament, judges and judges of the religious courts, and contributions to the Lebanese University).

In 2006, salaries and wages increased by 2.85% compared to 2005 from LL 2,275 billion to LL 2,340 billion in large part due to the hiring of approximately 15,000 army troops within the last three months of the year, and to the hiring in the Security Forces throughout the year. The share of salaries and wages as a percentage of total expenditures decreased from 22.3 percent in 2005 to 19.7 percent in 2006. The share of salaries and wages as a percentage of total primary expenditures similarly decreased over the same time period from 29.1% to 27%.

The three major components of salaries and wages are:

1) The salaries of military personnel (includes armed forces within the government such as the Lebanese Army, the Internal Security Forces, the General Security Forces, and the State Security Forces) made up 51% of the total wage and salary bill for 2006. The 8.3% (or LL 91 billion) increase over 2006 was mainly due to a 7.7% increase in the salaries of the army, and an 18.2% increase in the salaries of the Internal Security Forces, reflecting both categories' increased hiring.
2) In 2006, the salaries of education personnel (including salaries of teachers, contributions to salaries/wages of Lebanese University) constituted 30% of the total salaries and wages bill. At LL 701 billion end-2006, the salaries of education personnel decreased by 5.3% (or LL 40 billion) from LL 741 billion in 2005. Most of this reduction (65.5%) is due to a decrease in the salaries of contractual teachers.
3) At LL 448 billion end-2006, the salaries of civil personnel increased by 3% (or LL 13 billion) from LL 434 billion. Their share of the total salaries and wages bill at 19.1% is constant compared to 2005.

Breakdown of Salaries and Wages

(LL billion)	Jan - Dec 2005	Jan - Dec 2006	Percentage change over 2006
Militaries Personnel	**1,100**	**1,191**	**8.29%**
Army	739	784	6.16%
Internal Security forces	276	316	14.44%
General Security forces	63	65	4.31%
State Security forces	22	25	13.57%
Education Personnel	**741**	**701**	-5.34%
Civil Personnel	**434**	**448**	3.06%
Grand-Total	**2,275**	**2,340**	**2.85%**

** The grand total differs from the total for the item "Article 13: Salaries and Wages" in table 6 because the amounts listed in this box for Education personnel include contributions to the salaries of Lebanese University staff.*
Source: MOF, DGF

Other current expenditures for 2006 amounted to LL 258 billion, remaining at the same level as 2005. Hospital spending increased by LL 31 billion because of a large number of casualties during the war that offset the decrease in "other" items under this category.

Interest subsidies for loans to the productive sectors (agriculture, industry, tourism, technology and crafts) increased by LL 5 billion or by 7 percent from their level in 2005, reaching LL 80 billion in 2006.

Capital expenditures for the year 2006 amounted to LL 551 billion, increasing by LL 18 billion (3.3 percent) compared to 2005. This represented:

- An increase in construction in progress by LL 22 billion to reach LL 435 billion in 2006.
- An increase in the transfers to the Displaced Fund by LL 50 billion on an annual basis hence reaching LL 70 billion in 2006.
- Lower transfers to the Council of the South by approximately LL 30 billion to reach LL 36 billion in 2006.
- CDR local financing in 2006 was approximately LL 239 billion, almost equivalent to last year's level (LL 235 billion).

Other treasury expenditures were the main driver for the increase in primary spending as they increased by LL 664 billion (or 39 percent) during 2006 reaching LL 2,365 billion. The main items classified as part of "the other treasury expenditures" are Municipalities, EDL, and transfers to the High Relief Council.

(a) In 2006, spending on **municipalities** was 5.5 percent higher than in 2005 reaching LL 405 billion compared to LL 384 billion in 2005. Municipalities' spending had decreased in the first half of the year by 1.7 percent. Post War recovery necessitated higher spending in the second half of the year.

(b) Table 6 shows that Treasury transfers to EDL increased by 64% from 2005 to 2006. However, including Treasury advances to water authorities for their accrued electricity bills and budget transfers, transfers to **EDL** from the treasury were 40.7 percent higher in 2006 than in 2005, amounting to LL 1,370 billion in 2006 compared to LL 974 billion in 2005 (refer to Table 7). A total amount of LL 217 billion was disbursed during the period of August **-** December 2006 to settle arrears for oil suppliers as per Treasury Advance decrees issued in 2005. The rise in EDL costs is also attributed to higher payments to fuel oil and gasoil suppliers. In 2006, LL 920 billion were directly allocated to fuel purchases compared to LL 637 billion in 2005 (includes repayment of loans for oil purchase). *(please refer to table 7).*

(c) Transfers to the **High Relief Council** of LL 98 billion. During the war, a total amount of LL 19 billion was transferred in the form of treasury advances to the High Relief Council in order to allow the relief operations to take place. In addition, a special donations account was created in order to support the Lebanese Government in relief operations. The total donated amount of LL 79 billion was transferred in September 2006 to the High Relief Council.

Table 7. Transfers to EDL

(LL billion)	2005 Jan-Dec	2006 Jan-Dec	% Change
EDL *of which:*	**974**	**1,370**	**40.7%**
Debt Service *of which:*	**245**	**249**	**1.8%**
C-Loans and Eurobonds, *of which:*	**196**	**228**	**16.2%**
Principal Repayment	143	*181*	**26.6%**
Interest Payment	53	*47*	**-12.1%**
Loans for Oil Payment	49	17	**-65.7%**
BDL Guaranteed Loan Payment	0	5	**100.0%**
Oil purchase payments*	**588**	**903**	**53.6%**
Material and Supplies (Electricity bills)	**93**	**0**	
Treasury advance to Water Authorities	**48**	**0**	
Repayment of oil suppliers arrears **	**0**	**217**	

Source: MOF, DGF

** In 2005, oil purchase payments consisted of a treasury advance of: LL 130 billion paid for Fuel /From Decree #14310 date 2/4/2005; a treasury advance for EDL's losses of LL 220 billion paid from decree # 14561 (220 billion LL), LL 155 billion paid from decree # 14917, and LL 83 billion paid from decree #15542 for normal investment expenditure payments dated Oct 2005 (total decree amount LL 150 billion) . In 2006, oil purchase payments of LL 903 billion were made directly to Sonatrach and the Kuwait Petroleum Corporation against letters of credit signed by MOF.*

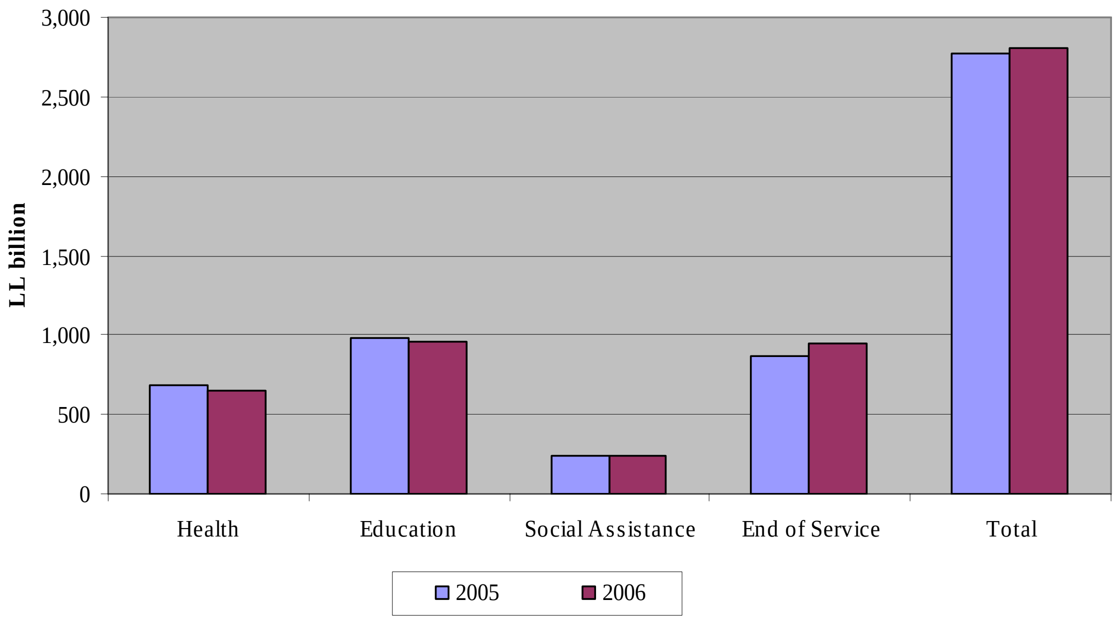
***Paid from decree Nbr.16084 Dec 2005(152 billion LL) & disburse an amount of 64 billion LL from the TA no. 14308 dated 02/04/05 LL 90 billion,*

Details of Social Expenditures

Overall expenditures on the social sector witnessed a slight increase of 1 percent in 2006 compared to 2005. This spending includes the two fundamental social services of (a) education health, (b) pension and end-of-service indemnity, as well as other areas of interventions classified as social assistance.

Of the total LL 2,801 billion of social spending in 2006, education accounts for the largest bulk, at 34 percent of total spending, covering mainly the Ministry of Education and Higher Education, in addition to educational allowances paid to security forces. Spending on pension and end-of-service ranked second, representing 34 percent of total social expenditures. As for spending on health, it accounted for 23 percent of total social spending.

Allocation of Social Spending



Source: MOF, DGF

Table 8. Social Spending for 2005-2006

(billion LL)	2005	2006	Magnitude of change 2006 over	Percentage change 2006 over
Health				
Hospitalization in the private sector	192	223	31	16%
Purchase of Medication	55	64	9	15%
Hospitalization of public sector employees in private sector	85	71	-15	-17%
Maternity and sickness allowance	17	33	16	99%
Other	49	66	16	33%
Sub-Total	**398**	**455**	**57**	**14%**
Education				
Ministry of Education and Higher Learning, *of which*	882	854	-28	-3%
Wages and Salaries of the General Directorate of Education	*534*	*478*	-56	-11%
Wages and Salaries of the General Directorate of Higher Learning	*0*	*1*	0	26%
Wages and Salaries of the General Directorate of Technical Education	*61*	*71*	10	17%
Contributions in the salaries of the Lebanese University	*146*	*152*	6	4%
Contributions to non profitable organizations (private schools)	*29*	*45*	16	56%
Construction under execution (construction and restauration of schools)	*40*	*29*	-11	-27%
Education allowance in private sector	101	106	5	5%
Sub-Total	**983**	**960**	**-23**	**-2%**
Other Social Spending				
Marriage allowance	2	3	1	74%
Birth allowance	*2*	*3*	2	102%
Death allowance	2	4	2	112%
Other social spending allowance	4	8	3	73%
Participation in several pension funds	21	21	0	-1%
Ministry of Social Affairs, *of which*	69	65	-4	-6%
Transfers to non profitable organizations	*67*	*65*	-2	-3%
Ministry of Displaced	3	5	1	35%
Transfers to employees' cooperative	135	135	0	100%
End of service & Pensions	864	942	78	9%
NSSF	290	200	-90	-31%
Sub-Total	**1,392**	**1,385**	**-7**	0%
Grand-Total	**2,774**	**2,801**	**27**	**1%**

Source: MOF, DGF

Section IV: Public Debt Developments

Table 9. Public Debt Outstanding by Holder as of End-December 2006

Assumes full LL Replacement	Dec-03	Dec-04	Dec-05	Dec-06	Change Dec 05 - Dec 06	% change Dec 05 - Dec 06
Gross Public debt	**50,285**	**54,048**	**57,985**	**60,880**	2,895	4.99%
Local currency debt	**26,843**	**26,371**	**29,141**	**30,204**	1,063	3.65%
a. Central Bank (including REPOs and Loans to EDL to finance fuel purchases)*	8,938	10,652	11,686	9,588	-2,098	-17.95%
b. Commercial Banks (Tbills and other loans)	12,303	12,220	14,130	16,487	2,357	16.68%
c. Other Local Currency Debt (T-bills)	5,603	3,500	3,325	4,129	804	24.18%
o/w Public entities	*2,564*	*2,187*	*2,446*	*3,313*	867	35.45%
Foreign currency debt	**23,442**	**27,677**	**28,844**	**30,676**	1,832	6.35%
a. Bilateral, Multilateral and Foreign Private sector loans	2,934	2,970	2,789	2,884	95	3.41%
b. Paris II related debt (Eurobonds and Loans)*****	3,731	3,814	3,682	3,721	39	1.06%
c. BDL Eurobond (Paris II)	2,819	2,819	2,819	2,819	0	0.00%
d. Market Eurobonds	13,631	17,686	18,729	20,399	1,670	8.92%
e. Accrued Interest on foreign currency debt	327	388	406	434	28	6.92%
f. Special Tbls in Foreign currency**			419	419	0	0.00%
Public sector deposits	**3,019**	**4,360**	**5,590**	**4,324**	-1,266	-22.65%
Net debt	**47,266**	**49,688**	**52,395**	**56,556**	4,161	7.94%
Gross Market debt* **	**29,638**	**31,861**	**34,726**	**38,676**	3,950	11.37%
% of total debt	**59%**	**59%**	**60%**	**64%**		6.08%

Source: Ministry of Finance, Banque du Liban

Notes:
* The BDL has extended loans to EDL for the equivalent amount of US$ 300 million to purchase fuel oil. These loans are listed as Public debt as they are government guaranteed.
** Special Tbs in Foreign currency (expropriation bonds).
*** Gross market debt equals gross debt less the portfolios of the BDL, NSSF, bilateral and multilateral loans, and Paris II related debt.
**** Figures of Dec 03- Dec 04 -Jan 06 change because of exchange rate of Euro
***** Paris II related debt (Eurobonds and Loans) decline on August because payment of first principal 30M EURO

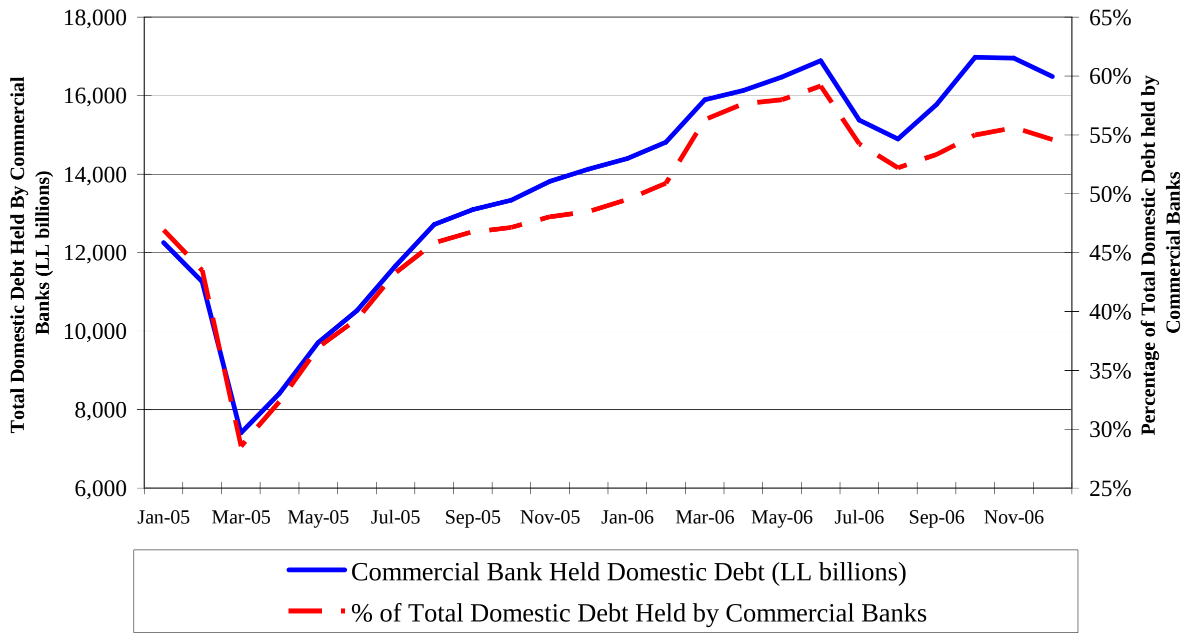
Gross public debt amounted to LL 60,880 billion (USD 40.4 billion) as of 31st December 2006, which is equivalent to 177.7 percent of GDP. Despite an overall deficit of LL 4,582 billion, increasing by 63.8 percent compared to 2005, gross public debt increased by LL 2,895 billion or 4.99 percent over the December 2005 level.

Net public debt amounted to LL 56,556 billion (USD 37.5 billion) registering an increase of LL 4,161 billion or 7.94 percent since end-December 2005.

Domestic currency debt as of end-December 2006 amounted to LL 30,204 billion, registering an increase of LL 1,063 billion (or approximately 3.65 percent) over the end-2005 level. This was mainly due to an increase in the Lebanese Pound Treasury bill portfolios of commercial banks in the first half of 2006. Also, the portfolio of the Central Bank in Lebanese Pound Treasury bills decreased over the end-2005 level. Central Bank financing decreased steadily from the beginning of the year to reach a low of LL 7,852 billion in June. However, in the aftermath of the July War, market demand was subdued and Central Bank financing became dominant reaching LL 9,569 billion in August and remaining steady at around that level for the rest of the year. Commercial banks' appetite for Lebanese

Pound denominated Treasury bills resumed in September 06 and domestic debt held by commercial banks increased from a trough of LL 14,896 billion in August 2006 to 16,487 billion in December 2006 (a 16.68 percent increase for the year).

Commercial Bank Financing of Domestic Debt
(2005-2006)



Weighted average cost of debt as at end December 2006, increased from a level of 7.23% as at end December 2005 to 7.59%. The weighted average cost of outstanding domestic debt increased from a level of 7.85% in December 2005 to 7.23% in end-December 2006. As for the weighted average cost of foreign debt, it registered 7.20% in December 2005, down from 7.23% a year earlier.

Table 10. Evolution of Weighted Average Cost of outstanding Public Debt

Date	Total Debt	Domestic Debt	Foreign Debt
Dec-03	8.34%	9.18%	7.39%
Dec-04	6.56%	6.04%	7.05%
Dec-05	7.23%	7.85%	7.23%
Dec-06	7.59%	7.99%	7.20%

Primary market interest rates currently range between 5.22 percent for the 3-month t-bills to 9.32 percent for the 36-month t-bills. As compared to 2005, all market interest rates remained the same, except for the interest on the 36-month t-bill which declined slightly, as is apparent in the table below.

Table 11. Evolution of Primary Market Treasury Bills Yields

Maturity	Dec. 31, 2004	Dec. 31, 2005	Dec. 31, 2006
3-month	5.22 percent	5.22 percent	5.22 percent
6-month	6.31 percent	7.24 percent	7.24 percent
12-month	6.69 percent	7.75 percent	6.75 percent
24-month	7.74 percent	8.50 percent	8.50 percent
36-month	8.68 percent	9.34 percent	9.32 percent

Source: Ministry of Finance

Average time to maturity of domestic debt, as of 31st December 2006, equaled 1.6 years and the average maturity of issued instruments was 35 months. In contrast, the average time to maturity of domestic debt as of 31st December 2005 was 1.6 years and the average maturity of issued instruments was 31 months. As for foreign debt, and as of 31st December 2006, the average time to maturity of Eurobonds and Concessional Loans was 6.3 years and the average maturity of issued Eurobonds instruments was 9.48 years. In contrast, as of 31st December 2005, the average time to maturity of Eurobonds and Concessional Loans was 4.9 years and the average maturity of issued Eurobonds instruments was 8.33 years.

Table 12. Net Issuance of Eurobonds in 2006

US$ million

Eurobonds Issued	**3,536**
Eurobonds Redeemed	**3,072**
Net Issuance	**464**

Source: Ministry of Finance

Foreign currency debt by end-December 2006 amounted to LL 30,204 billion (equivalent to USD 20 billion), increasing by LL 1,063 billion (or 3.65 percent) since the beginning of the year. During 2006, the Ministry of Finance issued an aggregate amount of Eurobonds equivalent to USD 3.54 billion. During the year, the total amount of Eurobonds redeemed amounted to USD 3.07 billion. Therefore, the net issuance of Eurobonds in the year 2006 amounted to USD 464 million.

Table 13. Terms and Conditions of Eurobonds issued in 2006

	Issue Size	Curr	Coupon	Issue Date	Maturity Date
Apr-06					
	676,902,000	USD	7.375%	04/12/06	04/14/14
	911,469,000	USD	8.25%	4/12/2006	4/12/2021
	149,542,000	EUR	5.88%	4/12/2006	4/12/2012
	750,000,000	USD	8.25%	4/25/2006	4/12/2021
	175,000,000	EUR	5.88%	4/25/2006	4/12/2012
Aug-06					
	206,591,000	USD	7.500%	08/02/06	08/03/09
	450,000,000	USD	7.500%	08/02/06	08/02/11
Dec-06					
	145,000,000	USD	7.500%	12/29/06	08/03/09

Source: Ministry of Finance

Table 14. Performance of Lebanese Eurobond Secondary Market

(Prices and yields as of the closing of 03-Jan-2007).

Republic of Lebanon Eurobonds	Mid- Price	Mid-Yield
Euro		
LEB 8.875 06	101.25	6.64%
LEB 7.250 09	94.88	7.07%
US Dollars		
LEB 6.500 07	99.88	7.24%
LEB 8.625 07	100.29	7.95%
LEB 7.375 08	98.88	8.49%
LEB 10.125 08	102.75	8.23%
LEB 10.250 09	104.25	8.47%
LEB FRN 09	99.12	8.59%
LEB 7.000 09	96.25	8.47%
LEB 7.125 10	96.25	8.50%
LEB 7.875 11	97.50	8.57%
LEB 7.750 12	96.25	8.60%
LEB 8.625 13	99.25	8.78%
LEB 8.500 16	97.00	9.00%
LIBAN 10 15	106.50	8.88%
LEB 11.625 16	116.00	9.05%
LEB 8.250 21	93.75	9.04%

Source:CSFB

For information on Eurobonds Outstanding and Eurobond issues visit the Ministry's website www.finance.gov.lb

Table 15. Public Debt Outstanding by Instrument as of End-December 2006

LL Billion	2003 Dec	2004 Dec	2005 Dec	2006 Dec	Change Year-to-date	% Change Year-to-date
Total Debt	**50,285**	**54,061**	**57,985**	**60,880**	**2,895**	**4.99%**
Domestic Debt	**26,843**	**26,371**	**29,141**	**30,204**	**1,063**	**3.65%**
1. Long Term Bonds, *of which:*	**24,691**	**20,766**	**23,384**	**26,862**	**3,478**	**14.87%**
a- 60 Months Bonds	650	650	1,772	2,172	**400**	**22.57%**
b- 54 Months Bonds	616	616	616	616		
c- 48 Months Bonds	0	0	633	633		
d- 36 Months Bonds	884	8,943	14,521	21,093	**6,572**	**45.26%**
e- 30 Months Bonds	3,033	3,033	3,033	0		
f- 24 Months Bonds	18,986	7,281	2,385	1,751	**-634**	**-26.58%**
g- Coupon Interest	522	243	425	597	**172**	**40.47%**
2. Short Term Bills, *of which:* *1/*	**1,799**	**5,102**	**5,246**	**2,839**	**-2,263**	**-43.14%**
a- 12 Months Bills	796	2,887	3,023	1,579	**-1,308**	**-43.27%**
b- 6 Months Bills	424	2,103	2,067	1,117	**-986**	**-47.70%**
c- 3 Months Bills	579	112	156	143	**31**	**19.87%**
3. Other Domestic Debt 2/	**353**	**504**	**511**	**503**	**-1**	**-0.20%**
Foreign Debt	**23,442**	**27,690**	**28,844**	**28,983**	**1,293**	**4.48%**
1. Eurobonds, *of which:*	**19,566**	**23,682**	**24,743**	**26,441**	**2,759**	**11.15%**
Paris II related Eurobonds	2,789	2,789	2,789	2,789		
2. Loans, *of which:*	**3,876**	**4,008**	**3,682**	**3,816**	**-192**	**-5.21%**
a- Paris II Concessional Loan	942	1,026	893	932	**-94**	**-10.53%**
b- Bilateral and Multilateral Loans	2,595	2,728	2,626	2,763	**-70**	**-2.60%**
c- Foreign Private Sector Loans	338	255	163	121	**-58**	**-22.70%**

Source: MOF, Banque du Liban
1/ Includes Accrued Interest on Short-Term Bills
2/ Mainly composed of loans extended to EDL to finance fuel purchases

Table 15 above demonstrates the **evolution of public debt by instrument**. On the domestic debt front, the demand for long-term bonds increased as compared to December 2005, while that for short-term bonds decreased. On the long-term bonds, the increase mostly occurred in the 36-month category, while the 24-month bonds witnessed a slight decline.

Moreover, commercial banks have over-subscribed in the 36-month Treasury Bills and substituted their shorter term Treasury Bills by this category. This shows the commercial banks' strong appetite for longer term Lebanese Pound denominated Treasury Bills.

Domestic debt subscription trends over the period January-December 2006 show that most investors continued showing **a special interest in the 36 month category**, which can be explained by the yield it is currently offering at 9.58 percent. The 6 month category is also attracting considerable interest amongst the shorter term instruments being offered. Over the January-December 2006 period 55 percent and 21 percent of all subscriptions were made in the 36 month and 6 month categories, respectively.

Over the same period, the least attractive maturities are the 24-month, the 12-month category, and the 3 months (all showing deficits). Only 3.6 percent, 9 percent and 10 percent of all subscriptions were made in the 24 month, 12 month and 3 month categories, respectively.

Over this period, there was an overall deficit in subscriptions (i.e. subscriptions minus maturities) amounting to LL 132 billion, with a deficit of LL 1,261 billion in short term maturities and a surplus of LL 1,130 billion in relatively longer dated instruments.

Section V: Evolution of External Trade

Table 16: External Trade

US$ millions	2005 Dec	2006 Dec	2005 Jan-Dec	2006 Jan-Dec	Change	% Change
Exports	217	206	1,880	2,283	403	21%
Imports, *of which*	872	904	9,340	9,398	58	1%
Mineral products	237	245	2,226	2,413	187	8%
Trade Balance	**-655**	**-698**	**-7,460**	**-7,115**	**345**	**-5%**

Source: MOF, Directorate General of Customs

Balance of trade:

In January-December 2006**,** the trade deficit decreased by 5 percent compared to January-December 2005. The improvement in the trade balance was a result of a (1) 21% increase in **exports** and (2) modest 1% increase in **imports**. The upsurge in exports of USD 403 million was due to the significant increase in the value of exports of **pearls, precious stones and metals** that was due to the increase in the prices of such products, particularly gold.

By the end of 2006, **imports** amounted to USD 9,398 million, compared to USD 9,340 million in 2005. From a product perspective, the increase in imports of **mineral products, machinery and electrical instruments**, **products of the chemical or allied industries** and **base metals and articles of base metals** was matched by a decrease in imports of **vehicles, aircraft, vessels and transport equipment** and other goods. From a regional distribution perspective, the huge increase in imports from the **United States** was matched by a significant decrease in imports from **Switzerland**.

On the other hand, **exports** reached USD 2,283 million in 2006, increasing by USD 403 million compared to 2005. From a product perspective, the significant increase in exports is mainly owed to a (1) USD 331 million increase in the exports of **pearls, precious or semi precious stones**, (2) USD 45 million increase in the exports of **base metals and articles of base metal** and (3) USD 20 million increase in the exports of **machinery and electrical instruments**. From a regional distribution perspective, the upsurge in the value of exports reflects a (1) USD 326 million increase in exports to **Switzerland**, (2) USD 97 million increase in exports to the **European Union** and (3) USD 20 million increase in exports to **China**.

Table 17: Import Distribution by Product

US$ millions	2005 Dec	2006 Dec	2005 Jan-Dec	%Share	2006 Jan-Dec	%Share	Change	% Change
Mineral products	237	245	2,226	24%	2,413	26%	187	8%
Machinery and electrical instruments	99	126	1,061	11%	1,123	12%	62	6%
Vehicles, aircraft, vessels and transport equipment	83	56	809	9%	764	8%	-45	-6%
Products of the chemical or allied industries	75	74	820	9%	887	9%	67	8%
Base metals and articles of base metals	63	60	651	7%	682	7%	31	5%
Other goods	314	343	3,773	40%	3,529	38%	-244	-6%
Total	**872**	**904**	**9,340**	**100%**	**9,398**	**100%**	**58**	**1%**

Source: MOF, Directorate General of Customs

Import distribution by product:

Imports of **mineral products** increased by 8 percent and cumulated at USD 2,413 million in 2006 as compared to USD 2,226 million in 2005. The increase in the import value of mineral products resulted from:

1) A USD 120 million increase in the imports of **gasoil**, which reached USD 938 million for 2006 compared to USD 818 million for 2005. This 15 percent increase was constituted of:
   a. 11% increase in price of **gasoil** from 624 LL/liter to 691 LL/liter
   b. 4% increase in the quantity imported of **gasoil** from 1.98 billion liters to 2.05 billion liters

2) A USD 88 million increase in the imports of **car gasoline**, which reached USD 785 million for 2006 compared to USD 697 million for 2005. This 13% increase was due to a 15% increase in the average price of **car gasoline** from 631 LL/liter to 729 LL/liter, which offset a 3% decrease in the quantity imported of **car gasoline** from 1.67 billion liters to 1.62 billion liters.

3) A USD 10 million decrease in the imports of **fuel oil**, which amounted to USD 442 million in 2006 compared to USD 452 million in 2005. This 2% decrease was due to the 10% decrease in the quantity imported of **fuel oil** from 1.56 billion liters to 1.41 billion liters, which was largely offset by an 8% increase in **fuel oil** prices from 437 LL/liter to 474 LL/liter.

Table 18: Breakdown of Mineral Product Imports

	2005 Jan-Dec	2006 Jan-Dec	Change	% Change
Import value details (US$ millions)				
Car gasoline	697	785	88	13%
Gas oil	818	938	120	15%
Fuel oil	452	442	-10	-2%
Import quantity details (millions of liters)				
Car gasoline	1,666	1,624	-42	-3%
Gas oil	1,977	2,047	70	4%
Fuel oil	1,561	1,406	-155	-10%
Import price details (LL/liter)				
Car gasoline	631	729	98	15%
Gas oil	624	691	67	11%
Fuel oil	437	474	37	8%

Source: MOF, Directorate General of Customs

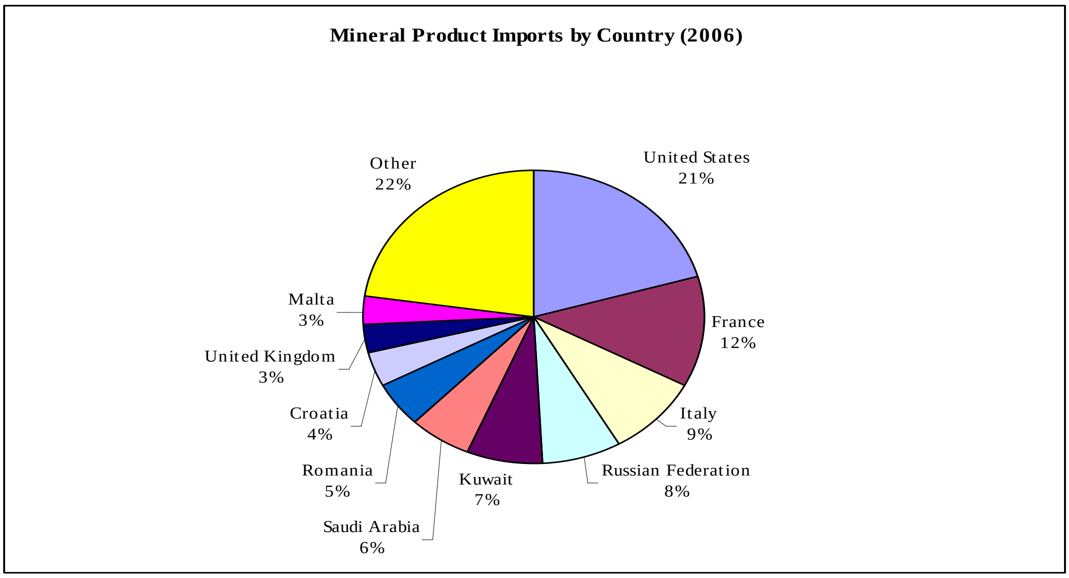
The 12 percent increase in imports of **machinery and electrical instruments**, which reached USD 1,123 million by the end of December 2006 in comparison to USD 1,061 million by the end of December 2005, was the consequence of an increase in the imports of **reactors, boilers, machinery and mechanical appliances** (or what can be described as electrical materials for industrial use) of USD 218 million that offset a USD 155 million decrease in the imports of **electrical machinery and equipment and parts thereof** (or what can be described as electrical appliances for household use)**.**

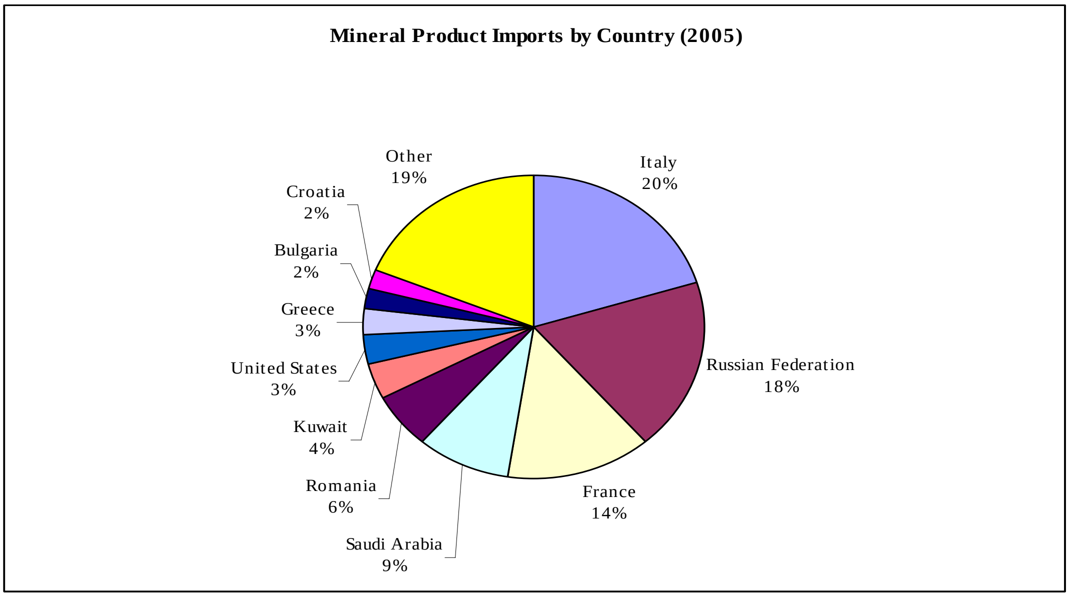
Imports of **vehicles, aircraft, vessels and transport equipment** were USD 764 million in 2006, as compared to USD 809 million in 2005. This 6% decrease was mainly due to a decrease in the imports of **vehicles** by USD 45 million. The decrease in the imports of vehicles could be explained by the decrease in the value of **car** imports from 2005 to 2006 by USD 25 million, or 2,134 **car** units.

Imports of **products of the chemical or allied industries** reached USD 887 million in 2006 compared to USD 820 million in 2005, thus registering an 8 percent increase. This increase can be attributed to a USD 82 million increase in the imports of **pharmaceutical products**.

Base metals and articles of base metals imports cumulated at USD 682 million by the end of December 2006 compared to USD 651 million by the end of December 2005. This increase could mainly be attributed to an increase in **imports of copper and articles thereof** of USD 25 million from 2005 to 2006.

Below are two pie charts that explore mineral product imports by country in 2005 and 2006.





Source: MOF, Directorate General of Customs

Table 19: Export Distribution by Product

US$ millions	2005 Dec	2006 Dec	2005 Jan-Dec	%Share	2006 Jan-Dec	%Share	Change	% Change
Pearls, precious stones and metals	61	29	224	12%	555	24%	331	148%
Machinery and electrical instruments	27	35	314	17%	334	15%	20	6%
Base metals and articles of base metals	25	39	276	15%	321	14%	45	16%
Products of the chemical or allied industries	22	16	163	9%	162	7%	-1	-1%
Prepared foodstuffs, beverages and tobacco	17	18	191	10%	187	8%	-4	-2%
Other exports	66	69	712	38%	724	32%	12	2%
Total	**217**	**206**	**1,880**	**100%**	**2,283**	**100%**	**403**	**21%**

Source: MOF, Directorate General of Customs

Export distribution by product:

Exports of **pearls, precious or semi-precious stones** increased by a remarkable 148% percent and totaled USD 555 million in 2005, compared to USD 224 million in 2005. This increase was mainly triggered by the upsurge in the value of **gold ingot** exports, from USD 120 million in 2005 to USD 445 million in 2006.

Exports of **base metals and articles of base metals** increased by USD 45 million from 2005, to reach USD 321 million in 2006. This was mainly due to a (1) USD 18 million increase in exports of **copper and articles thereof**, (2) USD 12 million increase in exports of **aluminum and articles thereof** and (3) USD 10 million increase in exports of **articles of iron or steel**.

Machinery and electrical instrument exports increased by 6 percent or USD 20 million, cumulating at USD 334 million in 2006, in comparison to USD 314 million a year earlier. This increase was mainly due to a (1) USD 7 million increase in the exports of **insulated wire, cable and other insulated electric conductors and optical fiber cables** and (2) USD 4 million increase in the exports of **electric generating sets and rotary converters**.

Table 20: Import distribution by region

US$ millions	2005 Dec	2006 Dec	2005 Jan-Dec	% Share	2006 Jan-Dec	% Share	Change	% Change
European Union 1/	333	339	3,597	39%	3,778	40%	181	5%
Arab Countries 2/	176	169	1,322	14%	1,449	15%	127	10%
China	68	78	734	8%	752	8%	18	2%
United States	45	122	548	6%	1,016	11%	468	85%
Switzerland	15	18	422	4%	212	2%	-210	-50%
Other	235	179	2,717	29%	2,191	23%	-526	-19%
Total	**872**	**905**	**9,340**	**100%**	**9,398**	**100%**	**58**	**1%**

1/ The European Union included as of January 1, 2007 the following countries: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom

2/ Arab Coutries includes the following countries: Algeria, Bahrain, Djibouti, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Palestinian Autonomous Territories, Qatar, Saudi Arabia, Sudan, Syria, Tunisia, United Arab Emirates, Yemen

Source: MOF, Directorate General of Customs

Import distribution by region:

Imports from the **European Union** increased by 5%, from USD 3,597 million in 2005 to USD 3,778 million in 2006. Four countries originated 67% of Lebanon's imports from the **European Union** in 2006, and these were **France, Italy, Germany** and **United Kingdom**. Comparing 2006 to 2005:

1) The increase in imports from the **European Union** was triggered by the enlargement of the bloc in 2006, with the new members exporting around USD 497 million worth of goods to Lebanon. New member **Romania** was the number five **European Union** exporter to Lebanon in 2006 with USD 161 million worth of goods, replacing **Belgium** whose exports to Lebanon dropped from USD 175 million in 2005 to USD 154 million in 2006. The top two imported goods from **Romania** in 2006 were **mineral products** at USD 121 million and **wood and articles thereof** at USD 26 million.

2) In fact, had the European Union not been enlarged in 2006, imports from the **European Union** would have decreased by USD 315 million between 2005 and 2006.

3) In 2005, **Italy** topped **European Union** countries in terms of exports to Lebanon, which dropped by USD 266 million from USD 976 million to USD 710 million in 2006, pulling **Italy** down to second place after **France** in the ranking of European Union exporting countries to Lebanon in 2006. The top two imported goods from **Italy** in 2006 were **mineral products** at USD 206 million and **reactors, boilers, machinery and mechanical appliances** at USD 71 million.

4) In 2006, **France** topped **European Union** countries in terms of exports to Lebanon, which dropped by a slight USD 27 million from USD 788 million in 2005 to USD 761 million in 2006. The top two imported goods from **France** in 2006 were **mineral products** at USD 289 million and **pharmaceutical products** at USD 92 million.

Imports from **Arab countries** augmented by USD 127 million or 10 percent and reached USD 1,449 million for 2006 compared to USD 1,322 million in 2005. Five countries originated 81% of Lebanon's imports from the **Arab Countries** in 2006, and these were **Egypt, Saudi Arabia, Kuwait, Syria** and **United Arab Emirates**. Comparing 2006 to 2005:

1) The increase in imports from **Arab Countries** was mainly triggered by the increase in imports from **Kuwait** by USD 82 million, **Egypt** by USD 76 million USD and **Bahrain** by USD 25 million. This offset the decrease in imports from **Saudi Arabia** by USD 33 million and **Syria** by USD 18 million.

2) In 2005, **Saudi Arabia** topped **Arab Countries** in terms of exports to Lebanon, which dropped by USD 33 million from USD 329 million to USD 296 million in 2006, pulling **Saudi Arabia** down to second place after **Egypt** in the ranking of **Arab Countries** exporting to Lebanon in 2006. The top two imported goods from **Saudi Arabia** in 2006 were **mineral products** at USD 138 million and **plastics and articles thereof** at USD 56 million.

3) In 2006, **Egypt** topped **Arab Countries** in terms of exports to Lebanon, which increased by a USD 76 million from USD 303 million in 2005 to USD 379 million in 2006. The top imported goods from **Egypt** in 2006 were **iron and steel** at USD 167 million, **copper and articles thereof** at USD 38 million, **soap and washing agents** at USD 24 million and **mineral products** at USD 23 million.

4) Imports from **Syria** decreased by 9% from 2005 to 2006, moving Syria from third place to fourth place in **Arab Countries** exports to Lebanon by country in 2006. This was mainly due to the decrease in imports of **iron and steel** from **Syria** by USD 11 million, from in USD 24 million 2005 to USD 13 million in 2006.

Imports from **China** registered a 2 percent increase, rising from USD 734 million in 2005 up to USD 752 million in 2006. The top two imports from China were **reactors, boilers, machinery and mechanical appliances** at USD 134 million, and **electrical machinery and equipment** at USD 95 million.

Imports from the **United States** increased by a remarkable 85% percent, amounting to USD 1,016 million in 2006 compared to USD 548 million in 2005. This significant increase was mainly fuelled by the increase in **mineral product** imports from the **United States** by USD 419 million, from USD 65 million in 2005 to USD 483 million in 2006.

Finally, imports from **Switzerland** decreased by a hefty 50%, from USD 422 million in 2005 to USD 212 million in 2006. This huge drop was mainly due to the decrease in imports of **pearls, precious and semi-precious stones** from **Switzerland** by USD 203 million from USD 315 million in 2005 to USD 112 million in 2006.

Table 21: Regional Distribution of Exports

US$ millions	2005 Dec	2006 Dec	2005 Jan-Dec	%Share	2006 Jan-Dec	%Share	Change	% Change
European Union 1/	14	31	178	9%	275	12%	97	54%
Arab Countries 2/	90	95	1,006	54%	999	44%	-7	-1%
China	1	8	26	1%	46	2%	20	77%
United States	4	5	58	3%	53	2%	-5	-9%
Switzerland	52	20	125	7%	451	20%	326	261%
Other	55	47	486	26%	459	20%	-27	-6%
Total	**217**	**206**	**1,880**	**100%**	**2,283**	**100%**	**403**	**21%**

1/ The European Union included as of January 1, 2007 the following countries: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom

2/ Arab Countries includes the following countries: Algeria, Bahrain, Djibouti, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Palestinian Autonomous Territories, Qatar, Saudi Arabia, Sudan, Syria, Tunisia, United Arab Emirates, Yemen

Source: MOF, Directorate General of Customs

Export distribution by region:

Exports to **Arab countries** decreased by 1 percent, totaling USD 999 million in 2006 compared to USD 1,006 million in 2005. Comparing 2006 to 2005:

1) There was a remarkable increase in exports to **Djibouti**, **Qatar** and **Morocco**. Exports to **Djibouti** increased by a significant 175%, to **Qatar** by 75% and to **Morocco** by 45%.

2) There was a remarkable decrease of exports to **Libya**, **Mauritania**, **Yemen** and **Iraq**. Exports to **Libya** decreased by 66% from USD 16 million in 2005 to USD 5 million in 2006. Exports to **Mauritania** witnessed a 34% decrease, whereas those from **Yemen** witnessed a 33% decrease. Exports to **Iraq**, which had surged to USD 178 million in 2005, dropped to USD 136 million in 2006.

Exports to the **European Union** increased by 54%, from USD 178 million in 2005 to USD 275 million in 2006. The top two export destinations in 2006 were **Belgium** **France** and the **United Kingdom** with USD 47 million, USD 39 million and USD 32 million worth of exports respectively. The top two exports to Belgium were **pearls, precious and semi-precious stones** and **articles of iron and steel**, at USD 10 million and USD 8 million respectively. The top export to France in 2006 was **aluminum and articles thereof** at USD 6 million, whereas the top export to the United Kingdom in 2006 was paper and articles thereof at USD 7 million. Comparing 2006 to 2005, exports to **Belgium** increased by USD 24 million. Exports to **Netherlands, Italy, Greece, France, Cyprus, Germany, United Kingdom** and **Ireland** all increased remarkably contributing to 35% of the total 54% increase in exports to the **European Union** from 2005 to 2006. These increases more than offset the decrease of exports to **Hungary, Czech Republic, Romania, Portugal, Spain** and **Malta** by an aggregated 47 %.

Exports to **Switzerland** increased by a huge 261%, from USD 125 million in 2005 to USD 451 million in 2006. This was mainly due to the increase in exports of **pearls, precious and semi-precious stones** by USD 327 million, from USD 120 million in 2005 to USD 447 million in 2006.

Exports to the **United States** decreased by 9 percent, reaching USD 53 million in 2006 from USD 58 million in 2005. Exports consisted mainly of **furniture, bedding and mattresses** at USD 11 million, down by USD 1 million from 2005, and **pearls, precious and semi precious stones** at USD 8 million, down USD 2 million from 2005.

Exports to **China** increased by 77%, from USD 26 million in 2005 to USD 46 million in 2006. The main export to **China** remained copper and articles thereof, and witnessed a 79% increase from USD 22 million in 2005 to USD 39 million in 2006.

Section VII: Value Added Tax Developments

Please note that most of the VAT figures mentioned in this section are extracted from declarations/claims processed. As such, these figures depend on the number of processed declarations at a given date (in this case the figures for 2006 are as of February 2007). Given that the process of entering data in the system is ongoing, figures may be subject to change in the future as more declarations/claims are processed.

Three sources of Value Added Tax (VAT) statistics are reported: VAT collected from internal economic activity, VAT from imports collected at customs, and VAT declarations. Tax revenues from the Value Added Tax (VAT) are outlined in the following section as broken-down by economic activity[7].

Due to the July 2006 war, the Ministry of Finance stipulated an exceptional tax measure concerning the settlement of VAT. Decision number 826 dated September 14, 2006 extended the filing and declaration deadline and allowed for a four-installment VAT settlement according to the following schedule: first installment due by November 20th, 2006; second installment due by December 20th, 2006; third installment due by February 20th, 2007; and fourth installment due by March 20th, 2007. In addition, the Ministry of Finance approved of a 100% amnesty on penalties arising from unsettled tax payment dues since 2002, and 90% amnesty on penalties arising from faulty tax filing on all tax types and fees since 2002. (*Please refer to Box 3 on Post War Tax Measures.*)

VAT: Internal Activities

In 2006, declared VAT from **internal activities** totaled LL 521.3 billion[8]. This amount is 2.9% higher than the 2005 total of LL 506.9 billion. The modest increase in VAT revenues can be partly attributed to the slowdown in economic growth during the second half of 2006, during and following the July war. The first half of 2006 saw a total of LL 262.3 billion declared VAT from internal activities, 19.1% higher than for the same period in 2005 at LL 220.2 billion.[9] The second half of 2006 however, at LL 259.1 billion, was 9.6% lower than for the second half of 2005 which registered LL 286.7 billion.

The highest VAT-generating economic activity in 2006 was from **wholesale trade** which contributed 18% to VAT revenues from internal operations. At LL 92.2 billion, wholesale trade registered 14.8% higher collection than in 2005 at LL 80.3 billion. Wholesale trade overtook retail trade, the historical leading contributor to VAT declared internally, in 2006. This could be attributed to the fact that retail trade and other economic activities were inversely affected from the war. In addition, since wholesale trade was the economic activity that grew the most in value terms in the first half of 2006 at LL 12.6 billion higher than for the first half of 2005, it is likely that wholesale was very high before the war due to the build up of stocks in expectations for a record tourist season and high economic growth.

Retail trade was the second highest VAT-generating activity in 2006. Although it maintained its 17% share of contributions, it was not the highest generating activity as in the past. At LL 89.4 billion, VAT revenues from retail trade were 6.3% higher than those from 2005 at LL 84.2 billion. This masks: a) the growth of retail trade in the first half of 2006 at LL 43.1 billion which was 19.3% higher than the first half of 2005; and b) the negative impact of the

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[7] *Taxpayers' economic activity are classified along the Ministry of Finance's Business Activity Code which adopts the ISIC nomenclature.*

[8] *Please note that the amounts of VAT declared (extracted from declaration forms) differ from VAT amounts actually collected on a cash-basis (Fiscal Performance figures). As such, and as mentioned in the Revenues Section, internal VAT cash collected decreased by 2.0 percent in 2006 compared to 2005.*

[9] *This may not capture all Quarter II declarations, the deadline for which to declare was extended as per decision 826 dated September 14, 2006 mentioned earlier.*

July war which resulted in 3.5% lower VAT generated in the second half of 2006 at LL 46.3 billion as compared with the second half of 2005.

At 12% share of VAT revenues from internal operations, **business activities**, mainly advertising, architectural and engineering activities, and legal consultancies, recorded LL 63.0 billion. This is 5.4% higher than the contribution of business activities in 2005 at LL 59.8 billion.

Hotels and restaurants recorded LL 41.7 billion in VAT revenues from internal operations, 1.8% higher than in 2005. A record number of arrivals to Lebanon in the first half of 2006 is reflected in the LL 24.2 billion amount of VAT revenues (40.8% higher than for the first half of 2005). The reverse trend is also true for the second half of the year where VAT revenues from hotels and restaurants decreased by 26.6% to LL 17.4 billion following a significant decrease in the number of tourists.

The 19.3% decrease in VAT revenues from **construction activity** indicate a contraction of the construction sector which contributed LL 39.8 billion in 2006 down from LL 49.4 billion in 2005. Although construction activity was 3% lower in the first half of 2006 as compared to the same period in 2005, it was reflected in the months during and after the war leading to a 31.5% reduction in contribution activity in the second half of 2006.

The **sale of cars, maintenance and repair of vehicles**, increased by 17.8% to LL 24.8 billion, up from LL 21.0 billion in 2005. Its share of VAT revenues from internal activities increased by one percentage point to 5% but it retained its rank as the 6th largest contributing economic activity.

VAT generated by the **manufacture of food products and beverages,** namely the manufacture of malt liquors and malt, sweet confectioneries, and bakery products, increased by 3.8% to LL 23.8 billion in 2006 as compared to LL 22.9 billion in 2005. The category maintained its 5% share of VAT declared from internal activity but slipped in rank to 7th from 6th place.

With LL 17.5 billion declared as VAT, **real estate** activities retain their 8th rank and 3% share of declared VAT although at 0.9% lower than their 2005 contribution of LL 17.6 billion. This only reflects VAT collected on commercial rent as the sale of real estate is VAT exempt.

The **post and telecommunications**[10] sector contributed LL 13.1 billion, or 3% of VAT revenues from internal activities to occupy the 9th rank. This amount is 5.8% higher than in 2005 where the sector contributed LL 12.4 billion and was ranked 11th.

Sewage and refuse disposal, sanitation and other activities registered LL 12.2 billion, or 2% of VAT revenues in 2006. The industry retained its 10th place position although at 3.0% less contribution than in 2005 which recorded LL 12.6 billion.

[10] Note that the VAT contribution figure from Post & telecommunication here is understated as it does not capture all the VAT raised from the telecommunication sector. As per the VAT law, a large fraction of VAT on telecom is directly transferred to municipalities, and hence is not captured in these figures.

Table 22: VAT Revenues from Internal Operations (10 Largest Contributing Activities)

(LL billion)

	Economic Activity (ISIC Nomenclature)	2005	% Share	Previous Rank*	2006	% Share	% Change
Rank	**VAT from internal activity**	**506.9**	**100%**		**521.3**	**100%**	2.9%
1	Wholesale trade and commission trade, except of motor vehicles and motorcycles	80.3	16%	2	92.2	18%	14.8%
2	Retail trade, except of motor vehicles and motorcycles; repair of personal and household goods	84.2	17%	1	89.4	17%	6.3%
3	Other business activities	59.8	12%	3	63.0	12%	5.4%
4	Hotels and restaurants	40.9	8%	5	41.7	8%	1.8%
5	Construction	49.4	10%	4	39.8	8%	-19.3%
6	Sale, maintenance and repair of motor vehicles and motorcycles; retail sale of automotive fuel	21.0	4%	7	24.8	5%	17.8%
7	Manufacture of food products and beverages	22.9	5%	6	23.8	5%	3.8%
8	Real estate activities	17.6	3%	8	17.5	3%	-0.9%
9	Post and telecommunications	12.4	2%	11	13.1	3%	5.8%
10	Sewage and refuse disposal, sanitation and similar activities	12.6	2%	10	12.2	2%	-3.0%
Other		105.7	21%		103.8	20%	-1.8%

Source: MOF, VAT Directorate, VAT Declaration Forms

(Please note that VAT figures in this table represent declared amounts whereas VAT figures in the Revenue section are cash collected amounts. Note that VAT declaration amounts may vary depending on the number of processed declarations at a given date.

** In 2005, the Manufacture of non-metallic mineral products (glass, ceramic, concrete, cement and plaster) occupied the 9th rank*

VAT Revenue Collected At Customs

Table 23 : VAT Revenue Collected At Customs (Five Largest Contributing Items)

(LL billion)	2005		2006		
	Jan-Dec	% Share	Jan-Dec	% Share	% Change
VAT customs collection,* of which	**1,181**	***100%***	**1,168**	***100%***	**-1%**
Mineral fuels and oils	351	*30%*	366	*31%*	4%
Vehicles other than railway	145	*12%*	136	*12%*	-6%
Reactors, boilers, other machinery	88	*7%*	87	*7%*	0%
Electrical Machinery	70	*6%*	65	*6%*	-7%
Iron and Steel	52	*4%*	51	*4%*	-1%
Others	475	*40%*	464	*40%*	-2%

Source: Directorate General of customs (DGC), Import Declarations, by HS chapter

** Please note that VAT collected at Customs in this table may differ from the amount previously mentioned in the Revenue Section as this data is captured from the Customs Administration Declaration forms whereas VAT in the fiscal performance is on a cash basis amount.*

*** Table displayed by HS chapter of the customs nomenclature and not by section as published in the Anuual Reports of previous years.*

VAT revenues collected at customs decreased by 1% in 2006 at LL 1,168 billion in contrast to the 1% increase in imports. This difference could be attributed to the imports of VAT exempt goods contributing to humanitarian relief that occurred during and after the war. Council of Ministers' Decisions 240 and 247 exempted VAT on a number of items for humanitarian relief effective until 31 October 2006 including on grants and donations of tents, mattresses, blankets, clothing, and other basic needs. In addition, there was an increase in imports of chemical products (namely pharmaceuticals) which are mostly VAT exempt.

In general, VAT revenue collected at customs reflects the top 5 imports except for chemical products:[11]

With a 31% share of VAT revenue collected at customs, **minerals fuels and oils** continue to lead the list of items most contributing to VAT collected at customs, mirroring the category's top rank in imports in 2006. Mineral fuels and oils were the only item in the top five contributing products' ranking whose contribution increased in value since 2005. At LL 366 billion, VAT customs collection of mineral fuels and oils in 2006 surpassed the 2005 contribution at LL 351 billion. This can be mainly attributed to increased cost of gasoil and car gasoline as reported on in the trade section (*Section V*).

Vehicles other than railway, such as tractors, their parts and accessories, and bicycles, was the second most VAT generating import category. The category maintained its 12% share of VAT revenues collected at customs and accounted for LL 136 billion. This represents a 6% decrease compared to the LL 145 billion in 2005 at, reflecting their 6% decrease in imports.

The third product category contributing to VAT revenues collected at customs was **reactors and boilers,** mainly machinery and mechanical appliances, with a LL 87 billion contribution, unchanged from 2005. Similarly, this product category continued to reflect a 7% share of VAT revenues collected at customs in 2006 as in 2005.

Electrical machinery ranks fourth in the five largest import VAT contributing list with a 6% contribution as in 2005. This product category however witnessed a 7% decrease in revenues with LL 65 billion collected in 2006 as compared to LL 70 billion in 2005 in line with their decreased imports.

At a LL 51 billion contribution to VAT revenues collected at imports in 2006, **iron and steel** maintained a 4% contribution as in 2005. This amount reflects a 1% decrease from the value contributed in 2005.

(*For further details on trade performance, please refer to Section V*).

[11] *Except for chemical products which are the fourth most imported product category, but which do generate little VAT because a large share of chemical products are VAT exempt (including medicine, some pharmaceutical products, fertilizers)*

Table 24: Statistics from VAT Declaration Forms

(Amounts in LL billion – except for first item)	2004	2005	2006	04-05 % Change	05-06 % Change
Number of Declarations Received	63,336	70,745	75,999	11.7%	7.4%
Amount of VAT Declared	527	519	536	-1.5%	3.2%
Total Amount of VAT Claimed for Refund	182	178	245	-2.1%	37.0%
*Diplomats & Int. organization**	*5*	*5*	*7*	7.2%	30.3%
*Exempted sectors***	*25*	*36*	*32*	45.5%	-12.9%
*Exporters****	*71*	*83*	*67*	16.2%	-18.8%
*Semi Annual and Annual Refund claims*****	*81*	*54*	*139*	-33.3%	156.7%
VAT Tourist Refund	11	11	9	6.0%	-15.6%

Source: MOF, VAT Directorate, VAT Declaration Forms as of February 1st, 2007

VAT revenue figures in this table are based on quarterly VAT declaration forms, whereas the VAT revenue figures in the Fiscal Performance represent cash collections. Note that VAT revenues in this Table may also differ from the VAT figures in Table 22 depending on the number of processed declarations at a given date.

** Includes United Nations.*

***Under Article 59 of VAT Law and its amendment in 2004, exempted sectors are granted 100% refund, of VAT input incurred..*

**** Exports are zero-rated*

***** By virtue of VAT Law and its amendment in 2004, VAT creditors/carry forwarders can refund their VAT twice each year.*

The number of **VAT declarations** received in 2006 increased to 75,999, continuing the upward trend since the VAT's introduction in 2002 and mainly due to the successive lowering of the mandatory registration threshold from the original threshold of LL 500 million in 2002 decreasing annually to reach a threshold of LL 150 million in 2005[12].

The total amount of VAT filed and declared by businesses in 2006 increased by 3.2% to LL 536 billion from LL 519 billion in 2005 which itself was a 1.5% decrease from the 2004 amount at LL 527 billion.

The average amount of VAT declared per declaration has decreased from an average of LL 8.3 million in 2004, to LL 7.3 million in 2005, and to LL 7.1 million in 2006 reflecting the decrease in the mandatory registration threshold and thus the higher collection of VAT from smaller taxpayers.

The **VAT tourist refund** decreased by 15.6% in 2006 amounting to LL 9.4 billion. This followed the increase in the VAT tourist refund in 2005 by 6% up to LL 11.1 billion as compared to 2004 which itself witnessed the highest number of incoming tourists to Lebanon since 1975, the beginning of the civil war.

The large decrease in the VAT tourist refund in 2006 reflects reduced tourist activity in 2006 due to the July war which resulted in a two month air and naval blockade. There were a total of 1,062,635 arrivals in 2006, 6.7% less than those in 2005 (themselves 10.9% less than those in 2004). Prior to the war, 1.6 million tourists were expected to visit Lebanon in 2006 as indicated by a strong first half of 2006 which saw 630,804 tourists arriving to Lebanon, 45.3% higher than for the same period in 2005, and 24.6% higher than for the same period of

[12] *The mandatory registration threshold lowered to LL 150 million of annual turnover, has been effective as of January 1st 2005. The voluntary registration threshold was canceled effective 1/1/2004, granting businesses and individuals the right to register in the VAT regardless of the level of their annual turnover.*

2004, itself a record year since the end of the civil war. This was revealed in the VAT tourist refund data for the first half of 2006 at LL 6.2 billion, 34.9% and 35.6% higher than for the same period in 2005 and 2004 respectively. In contrast, the second half of 2006 witnessed a reversal of tourist activity and thus VAT tourist refunds, with a total of 431,831 arrivals and LL 3.2 billion VAT tourist refund. Tourist arrivals for the second half or 2006 were 39.7% lower than in 2005 and 44.1% lower than in 2004. VAT tourist refund in the second half of 2006 was relatively more affected at 51.4% lower than for the second half of 2005, and 46.4% lower than for the same period in 2004.

The total amount of **VAT claimed for refund (excluding tourist refund)**[13] increased by 37% in 2006 to LL 244.5 billion. This was mainly due to the 157% increase in the semi-annual and annual refund claims which amounted to LL 138.9 billion in 2006 from LL 54.1 billion in 2005. This is in line with the increase in the number of refund claims received which amounted to 3, 995 in 2006, up from 3,924 in 2005, and 3,983 in 2004. This may hint at lower investments in those VAT exempt businesses in 2006.

Diplomats and international organizations claimed for LL 6.7 billion worth of refunds in 2006, compared to LL 5.2 billion in 2005, increasing by 28.5%.

Refund amounts claimed by **exempt sectors**[14] decreased by 12.9% in 2006 to LL 32 billion from LL 36 billion in 2005. The number of refund claims presented by refund sectors in 2006 also decreased by 10.7% to 1,360 claims. This led to an average of LL 23.4 million per claim in 2006, compared to LL 23.9 million in 2005, and LL 16.3 million in 2004.

VAT refund claims for **exporters**[15] totaled LL 67 billion, a reduction of 18.8% compared to the 2005 total at LL 83 billion. This contrasts with 21% higher exports in 2006 which was mainly driven by the increase in the value of gold ingots which could be explained by the fact that precious stones are VAT exempt. In 2006, there were 1,779 refund claims presented by exporters, an increase of 5.6% compared to 2005. The average amount per claim presented by exporters decreased from an average of LL 49.1 million in 2005 to LL 37.7 million in 2006.

Refund claims from VAT creditors/carry forwarders registered LL 139 billion in 2006, 156.7% higher than in 2005 at LL 54 billion. The average amount of refund claimed also increased in 2006 to LL 273 million from LL 124 million in 2005 and LL 249.1 in 2004. This comes despite an increase in the number of claims to 509 in 2006 from 436 in 2005 and 326 in 2004 indicating a trend of higher refund claims from VAT creditors/carry forwarders.

[13] *Please note that tourist refund operations are effected by an international company "Global Refund" and not by the Treasury. Thus, tourist refund figures are accounted for separately.*
[14] *Article 59 of VAT Law 379 grants exempt activities, namely exempt industries such as agro food, pharmaceutical, agricultural chemicals, printing and publishing and exempt services such as education and medical services the right to refund the VAT incurred, in order not to add burden on their operating costs.*
[15] *As is consistent with a destination based VAT, the Lebanese VAT Law zero-rate exports.*

Box 3. Post War Tax measures

In September 2006, and following the July 2006 Israeli offensive on Lebanon, the Ministry of Finance stipulated a series of exceptional tax measures with the purpose of easing the fiscal burden on the private sector.

1. Settlement of VAT and the withheld tax on wages and salaries - *Decision number 826 dated September 14, 2006*

The declaration and payment dates for the VAT and the withheld tax on wages and salaries for the second quarter of the year fall due during the first 15 days of the month of July. These dates coincided with the beginning of the war resulting in the incapacity of taxpayers to fulfill their timely tax obligations. Consequently, the Ministry of Finance extended the filing and declaration deadlines to:

⇒ September 19th, 2006 for the withheld tax on wages and salaries and

⇒ September 24th, 2006 for the VAT;

MOF also granted taxpayers the possibility to settle their QII tax dues in four installments according to the following schedule:

- First installment due by November 20th 2006
- Second installment due by December 20th 2006
- Third installment due by February 20th, 2007
- Fourth installment due by March 20th, 2007

2. Amnesty on Due Penalties - *Decision number 827 dated September 14, 2006*

As an exceptional measure, the Ministry of Finance approved the following:

- 100% amnesty on penalties arising from unsettled tax payment[1] dues, across all tax types and fees, since the year 2002
- 90% amnesty on penalties arising from faulty tax filing, across all tax types and fees since the year 2002

The amnesty period extends until the end of 2006.

Through this decision, the Ministry of Finance is hoping to relieve some of the fiscal burden on taxpayers on the one hand, and to settle part of its tax arrears (going back to the year 2002), by providing taxpayers the incentive to clear up past dues.

3. Postponement of filing, declaration, payment dates falling due between July 12th - September 15th 2006 along a new calendar starting September 16th, 2006 - *Decision number 823 dated September 12, 2006*

This decision stipulates that the period extending from July 12, 2006 until September 15, 2006 is put on hold; As a result, filing, declaration, payment and all sorts of obligations falling due within this period shall resume starting September 16, 2006, along a new calendar whereby initial dates are postponed by an equivalent 66 days period.