# Fostering Economic Opportunities in Lebanon:

# A Review of Potential Policy Actions for Increased Competitiveness

## Contents

# Introduction

The Lebanese economy was growing modestly over the past decade. Its performance was impacted by the global crisis and a series of domestic, regional and international events. The private sector, the engine of job creation, has not been able to create enough jobs to keep pace with the rapidly growing young population, and significant numbers of youth and women are pushed to unemployment. The overall unemployment is estimated to have exceeded 20 percent, partly as a result of the large influx of Syrian refugees. Even before the Syrian crisis unfolded in 2011, around 11 percent of the labor force was unemployed, with rates worrisomely high amongst women and youth – 18 percent and 34 percent respectively - and in lagging regions. In this context, supporting private sector job creation, especially in lagging regions, such as North Lebanon which houses almost half of the country's poor, is critical and much needed.

Global integration through foreign investment and trade is key for Lebanon to accelerate its growth and create the much-needed jobs. For a small country with a growing population, such as Lebanon, there is a compelling case to deepen its economic integration with the world, attract more foreign investment, boost its trade, and ultimately create more and better jobs. However, for this to happen, Lebanon needs to improve its competitiveness. This requires actions on many fronts including upgrading its infrastructure by partnering with the private sector through PPPs given the county's fiscal constraints, as well as improving its investment policy, trade facilitation, competition policy and access to finance. The planned Tripoli Special Economic Zone offers an opportunity and useful tool for the Government of Lebanon (GOL) to achieve these results, at the same time focusing on a lagging region. However, its success depends on its ability to implement a good practice framework, including world class trade processes.

The World Bank undertook a diagnostic exercise to examine a range of policy reforms and actions that can contribute to private sector led job creation focusing on how to more effectively promote private investment and leverage private financing, facilitate trade and strengthen competition. This diagnostic served as analytical background to the preparation of the "Creating Economic Opportunities in Support to the National Jobs Program" PforR and formed the technical basis of the project design. The areas of focus were selected based on the following criteria: (i) where the GOL requested a focus and have a pre-existing reform objective; (ii) where global evidence indicates strong potential to foster private investment and job creation; and (iii) where the WBG had not recently undertaken analytical work and needed to update its knowledge.

This synthesis report summarizes the findings of the below technical reports[1]:

(i) Lebanon PPP Country Readiness Diagnostic (2017);
(ii) Investment Policy Technical Note "Leveraging foreign investment for the creation of value added jobs in Lebanon" (2017);
(iii) Competition Policy Technical Report (2017);
(iv) Trade Facilitation Technical Note (2017);
(v) Trade Policy Technical Note "Selected Policy Issues on Trade and Special Economic Zones in Lebanon" (2017);

[1] These documents have been shared with the Government of Lebanon.

(vi) Tripoli Special Economic Zone: Market Assessment and Economic and Financial Assessment Reports (2017); and
(vii) Knowledge and Innovation City in Tripoli Technical Note (2017).

These reports are complementary to other analytical work recently completed, including: (i) the "Financial Sector Assessment Program FSAP" (2016); (ii) "Jobs for North Lebanon: Value Chains, Labor Markets, Skills and Investment Climate in Tripoli and the North" (2016) report; (iii) Access to Finance Assessment – Supply and Demand Assessment (2017), as well as to the ongoing advisory work provided by the World Bank to streamline business registration and construction permits.

# 1. Country Context

1.1 **Lebanon is a small open country of high middle-income status with a population of 4.5 Million people in 2015[2].** Its many advantages include a free-market economy, the absence of controls on the movement of capital and foreign exchange, a well-developed banking system, as well as its highly educated labor force and large successful diaspora. The country benefits from a dynamic private sector, a financially sound banking sector with total assets exceeding 350 percent of GDP, and a large and resilient remittance base that reached 15.9 percent of GDP in 2015.

1.2 **Since the end of the civil war, the Lebanese economy has expanded at a moderate pace, but with high volatility due to frequent shocks, mainly local and regional socio-political and security unrests.** While real GDP grew by an estimated 4.8 percent on average from 1993 to 2015, the volatility around that average was large at 3.7 percent[3].

1.3 **Most recently, the refugee crisis from the Syrian civil war took a toll on the Lebanese economy and dragged down growth significantly.** In 2015 it is estimated that GDP grew by 1 percent[4] and a similar growth rate is projected in 2016 after a real growth of 2.6 percent in 2013 and 8 percent in 2010. According to the World Bank Economic and Social Impact Assessment of the Syrian Conflict (2013), the cumulative losses in economic activity reached an estimated USD7.5 Billion by end-2014. The sudden surge in demand due to Syrian refugee influx has led to a deterioration of all core public services, especially infrastructure. The country's infrastructure, already severely constrained, was ill-prepared to cope with increased use resulting from the surge in refugees.

1.4 **Exports have been an obvious indicator of Lebanon's economic slowdown.** In 2012, Lebanon exported almost $4.5 Billion worth of Lebanese goods. By 2016, the figure had declined to less than $3 Billion in value. The reason for the decline is partially due to the disruption of land routes through Syria to markets in the Gulf and a drop in Lebanese exports to the Syrian market, one of its larger trading partners. Nonetheless, even abstracting from the impact of Syria, the fundamentals such as the overvalued exchange rate in Lebanon is hurting the competitiveness of exports.[5] Services sectors, especially tourism-related services, dominate Lebanon's export basket. In 2014, 79.4 percent of exports were services. Out of this, 44.2 percent was in travel services, mainly tourism; 24.8 percent in ICT services; and the remainder in financial, insurance and transport services. For merchandise exports, jewelry, scrap copper and electric generating sets were the top three exported items.

1.5 **Foreign Direct Investment (FDI) has also been steadily declining since 2010 at a CAGR rate of 9.8 percent.** The volatility in growth levels has been accompanied by a highly volatile investment market in the past few years that is reflected in the country's fluctuating FDI inflows, ranging from USD 2 up to 4.5 Billion per year. Between 2004 and 2009, Lebanon

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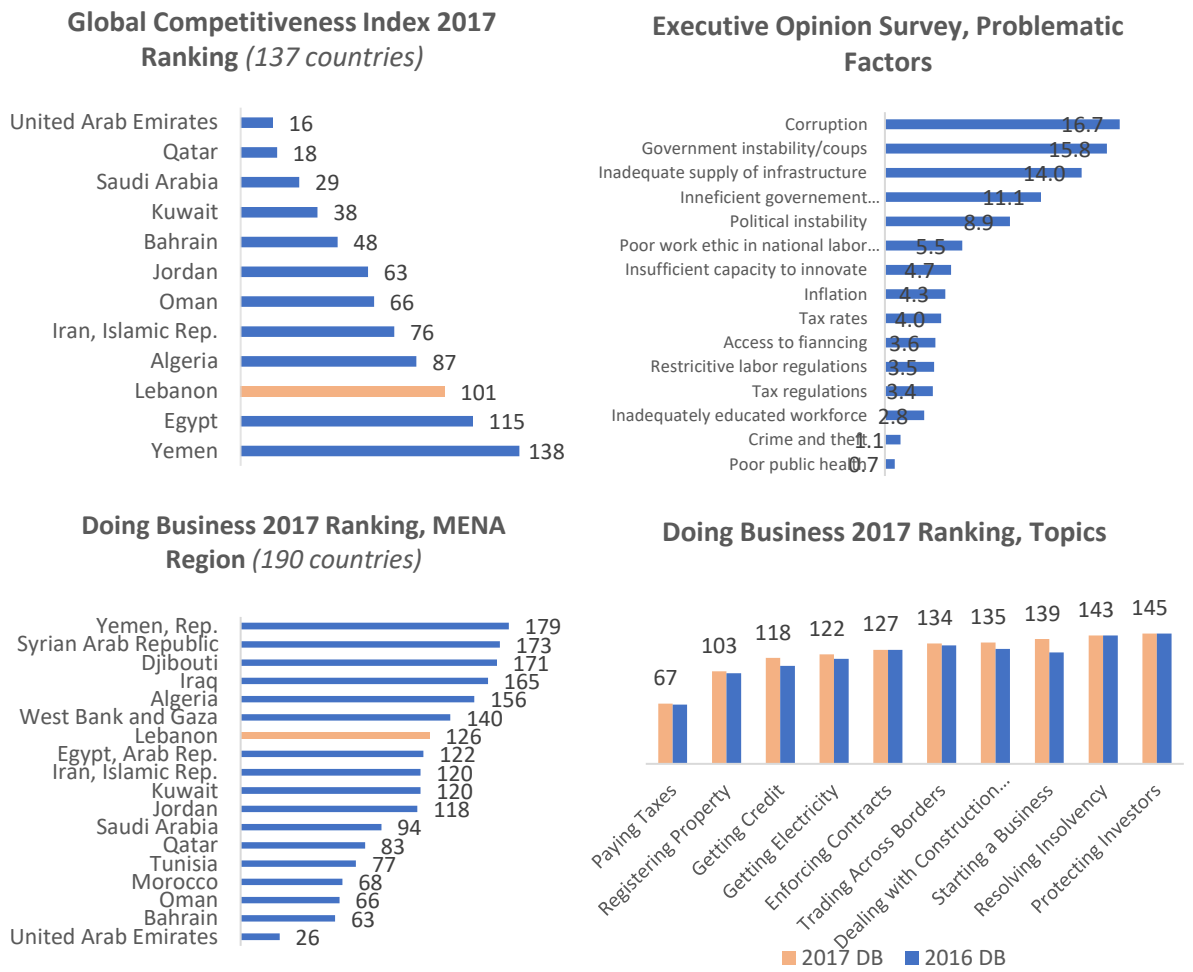
[2] Not taking into account the approximate 1.5 Million Syrian refugees residing in the country
[3] World Bank 2016, Country Partnership Framework for the Lebanese Republic
[4] IMF World Economic Outlook
[5] According to IMF's 2017 Article IV for Lebanon, Lebanon's real exchange rate may be overvalued by anywhere between 0–23 percent.

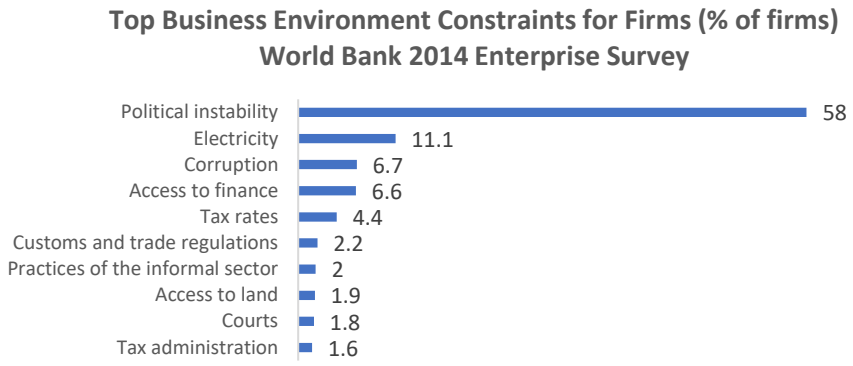
witnessed a surge in FDI inflows that steadily declined since 2010. The main decline in investment inflows was due to the war in Syria, regional turmoil, political instability in Lebanon and the economic slowdown of GCC countries due to lower oil prices.

*Investment Climate*

1.6 **Lebanon's poor investment climate has limited the ability of the private sector to invest, trade and grow.** It has contributed to the decline in investor and consumer confidence. The failure to develop and maintain a quality investment environment over recent decades has undermined the competitiveness of firms and their ability to grow and drive job creation. **Box 1Error! Reference source not found.** summarizes the situation.

**Box 1: Snapshot of Lebanon's Comeptitveness**





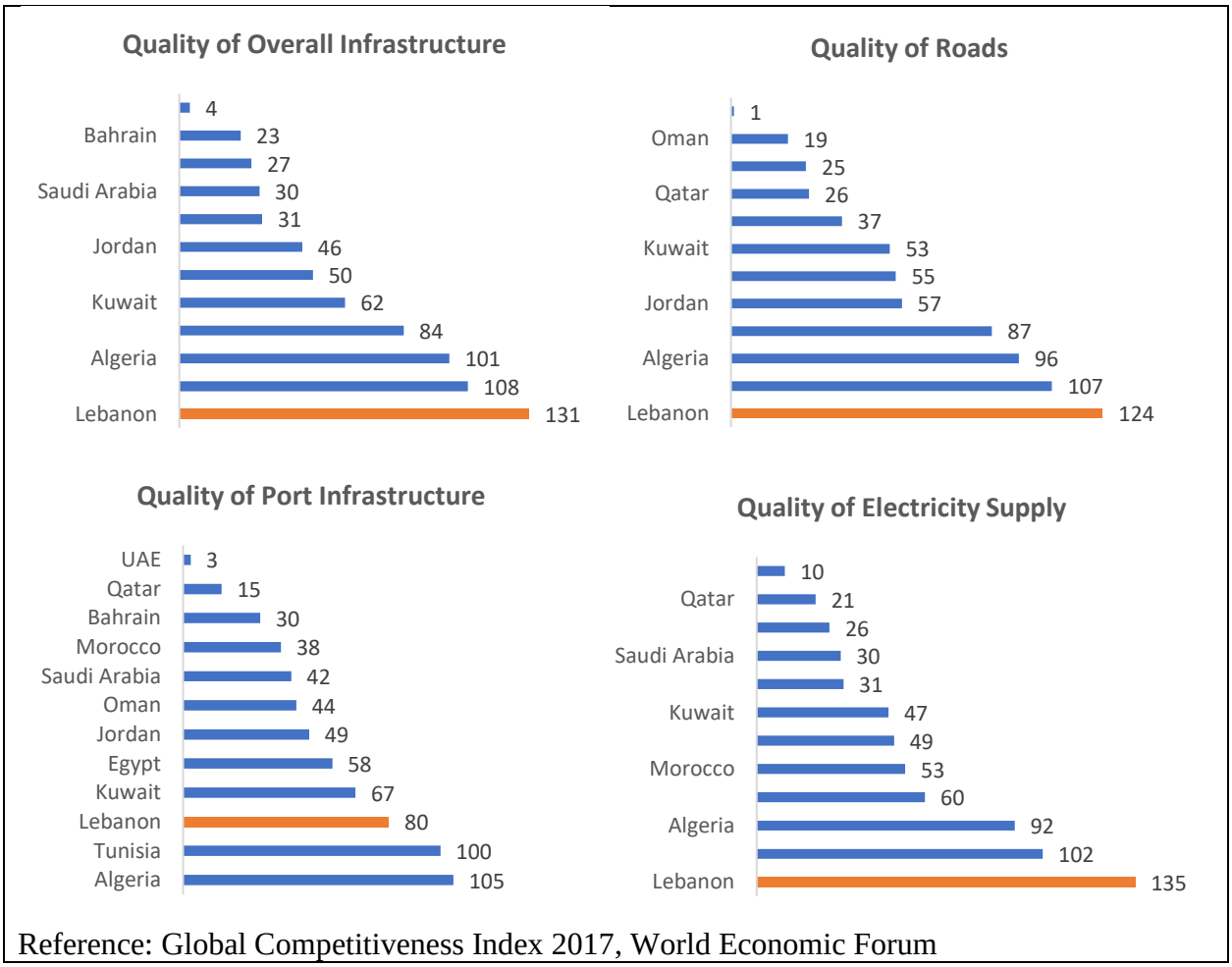

Reference: Global Competitiveness Index 2017, World Economic Forum; Doing Business 2017, World Bank; Enterprise Surveys 2014, World Bank

1.7 **Surveys of business managers highlight national and regional political instability as the most problematic factors impacting their operations**. Instability was rated as the top obstacle by 21% of managers in the World Economic Forum's *Global Competitiveness Index* (2017) and by 58% of firms in the latest (2013) World Bank Enterprise Surveys.

1.8 **Beyond instability, firms also face a wide range of business environment constraints with inadequate supply of infrastructure on the top of the list.** (See Box 2) According to the 2017-18 Global Competitiveness Index, Lebanon scores poorly in terms of access and quality of infrastructure, especially when compared to neighboring Arab countries. Fiscal constraints over the past decade have limited severely the level of public investment available to upgrade the infrastructure; and regulatory barriers have prevented private sector investment. Access to electricity[6] is cited as major constraint by 55% of firms, according to the World Bank Enterprise Surveys (2013). Surveyed firms indicated that losses due to electrical outages reached 5.7% of total sales, more than double the worldwide average. Other critical economic infrastructure – notably the telecommunications networks, trade and transport – are also perceived as major impediments to business operation in Lebanon.

**Box 2: Quality of Infrastructure - Global Competitiveness Index 2017** *(137 Countries)*

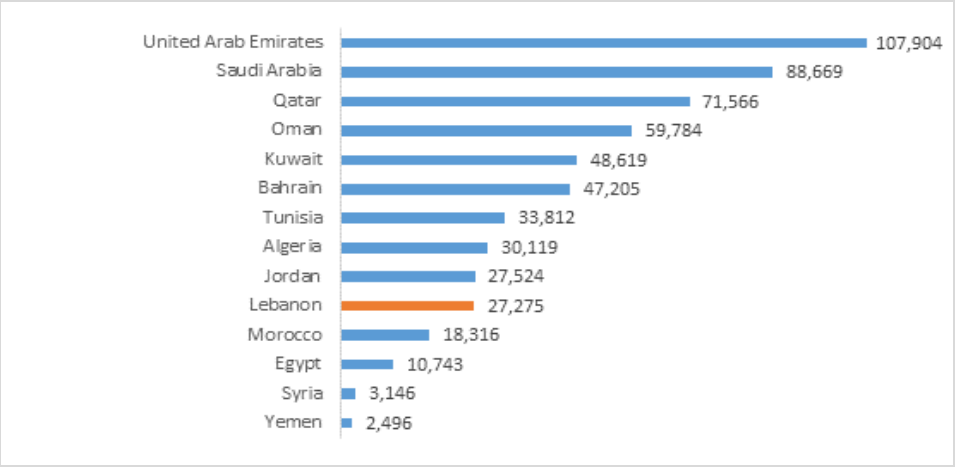
[6] A recent study as shown that the Syrian crisis has deepened the problem of the electricity network due to: (i) increased burden on an already deteriorating network; (ii) negative impact on quality of supplied power due to additional demand in some areas; (iii) indirect impact of additional power consumption of schools hosting displaced Syrians as well as municipalities/water establishments; (iv) damaged to distribution transformers and cables due to overload; (v) rise in non-technical losses and damage to distribution network due to the non-metered connections. Main findings extracted from: *Ministry of Energy and Water and UNDP. (2017). The Impact of the Syrian Crisis on the Lebanese Power Sector and Priority Recommendations.*




Reference: Global Competitiveness Index 2017, World Economic Forum

1.9 **In terms of telecommunications, while access to fixed and mobile broadband has increased significantly in recent years, quality and speed of connections still lag behind.** In fact, Lebanon has one of the lowest internet bandwidth per user in the region according to the World Economic Forum's Network Readiness Index 2016 (Figure 1). Moreover, while prices have come down recently, they remain high in global terms.

Figure 1:International internet bandwidth bits per second per internet user




Source: World Economic Forum, Network Readiness Index 2016

1.10 **Trade infrastructure, including both physical and infrastructure and processes and procedures (soft infrastructure) represents a significant barrier to growth of Lebanon's traded sectors.** Cumbersome processes and procedures, requirements for submission of redundant documents, low levels of customs automation, and excessive inspections of cargo are cited as key sources of inefficiency by the private sector. Lebanon ranks 134th out of 190 countries worldwide in the latest World Bank's Doing Business (2017) - Trade Across Border sub-indicator.

1.11 **Access to finance is also problematic and limits firms' investments and growth potential**. Despite having a large and relatively sophisticated financial sector, worth an estimated 350% of GDP[7], key aspects of the financial sector architecture are missing or insufficiently developed, and credit is not flowing as efficiently as it could to the businesses and sectors that can generate jobs. For example, while SMEs account for 96% of all firms in Lebanon, only 20% of private sector credit is channeled to them[8]. Among the key regulatory barriers contributing to the problem of access to finance are: i) the current insolvency framework, which lacks the provisions that are needed for a dynamic private sector and effective debt recovery, which prompts banks to over-collateralize; and ii) the absence of secured transactions framework, which limits the scope of assets that businesses can use as collateral.

1.12 **A gamut of other regulatory constraints – from business registration and licensing to enforcing contracts – also hamper businesses from expanding.** According to the 2017 World Bank's Doing Business indicator, Lebanon ranks 126th globally and 11th among the 21 MENA countries in terms of ease of doing business. It takes on average 15 days and 8 procedures to start a business in Lebanon at cost equivalent more than 40 percent of per capita income; to start the same business in the average OECD country would cost just 3 percent of per capita income.

1.13 **While many countries are working on improving their investment climate to make their economies more attractive for investments, domestic and foreign, Lebanon has made no substantive progress and regressed according to a number of indicators.** Looking at the 2017 Doing Business, Lebanon scored 54 percent in the Distance to Frontier, which means that

[7] According to the World Bank/IMF Financial Sector Assessment.
[8] 2016 World Bank, Financial Sector Assessment

Lebanon is 46 percent away from the best performer. Lebanon regressed 4 places from its 2016 ranking where it stood at 122, and no improvement has been made in any sub-index. In fact, Lebanon did not enact any reform related to the business environment since 2013, while on average MENA countries implemented five.

*Jobs Challenge*

1.14 **The failure to develop and maintain a conducive investment climate over the years has undermined the competitiveness of the private sector and limited its ability to create sufficient jobs.** Job creation by the domestic private sector is limited and concentrated in low productivity sectors that employ mainly low skilled workers[9]. This trend occurs while Lebanese education system generates high numbers of skilled graduates. Prior to 2011 the unemployment rate stood at 11 percent with 34 percent of the country's youth affected and 18 percent of whom were women.[10] This has been exacerbated in the years that follow due to the refugee influx into Lebanon, with unemployment now estimated to have reached more than 20 percent[11]. The rates are even more acute in lagging regions. It is estimated that around 30,000 to 35,000 young people graduate from university every year and only 5,000 jobs are offered annually, which leaves some 30,000 without jobs[12].

1.15 **As a result, the unemployment rate is the highest for the population with secondary and tertiary degrees, reaching 14 – 15 percent respectively, which explains the high level of highly skilled outmigration.** 44 percent of migrants between 2004 and 2009 held a university degree compared with 16 percent of the total resident population of Lebanon.[13] In other words, young educated Lebanese are contributing to other countries' economies and not Lebanon, and despite the large remittances generated, the brain drain is only partially offset. However, with the significant drop in labor demand from traditional external markets, such as GCC, Europe and the US, and tougher regulation, outlets that have historically eased Lebanese unemployment are getting blocked.

1.16 **Compounded with a rapidly growing young population, unemployment is expected to keep rising in the coming years**. Lebanon is a demographically young country. Prior to the influx of the Syrian refugees, 45 percent of the population was below the age of 24. In the absence of sufficient job opportunities to absorb these new entrants, unemployment will continue to rise.

*Sources of Economic Opportunity*

1.17 **Given the small size and slow growth of the Lebanese economy, access to new sources of demand, outside its confined borders will be key to create new investment and job opportunities.** Global integration through foreign investment and trade is key for Lebanon to accelerate its growth and create the much-needed jobs. For a small country with a growing population, such as Lebanon, there is a compelling case to deepen its economic integration with the world, attract more foreign investment, boost its trade, and ultimately create more and better jobs. However, for this to happen, Lebanon needs to improve its competitiveness. While Lebanon

[9] Low productivity sectors include: low productivity services and trade, and construction
[10] World Bank, 2013, "Republic of Lebanon: Good Jobs Needed"
[11] World Bank, 2013, Lebanon Economic and Social Impact Assessment of the Syrian Conflict
[12] The Arab Weekly, August 2017, Lebanon's youth bearing the brunt of unemployment
[13] CAS, 2012, Population and housing in Lebanon

has traditionally played a leading role as a regional trade hub, exports and FDI have underperformed in terms of job creation. Over the years, both domestic and foreign investment has become increasingly concentrated in the lower labor-intensive sectors of finance and real estate, at the expense of tradable sectors. Raising the competitiveness particularly in Lebanon's tradable sectors, can have a significant impact on investment potential and the creation of quality jobs, given also that a one percent increase in firm productivity generates an increase in job creation of 3.9% in Lebanon[14].

1.18 **This report identifies prospective policy priorities and directions that can improve Lebanon's competitiveness and generate new economic opportunities in the face of the current low growth trend in the economy. It mainly targets actions that are feasible and have significant economywide spillovers, including through both productivity and demonstration effects.** These include:

- **Leveraging PPPs as a potential mechanism for attracting private sector participation to close the country's infrastructure gap**: To upgrade the infrastructure or the delivery of public services without crippling the country's fiscal policy, transportation, electricity telecom, and other government owned and managed services should be open for private funding and participation. The recently passed PPP law sets the proper legal and regulatory framework for the implementation of partnership projects. However, much more work is needed in terms of selection, preparation, negotiation, implementation and fiscal management of private participation, for PPP projects to be materialized.

- **Investment Policy actions that promote FDI and increased integration in global value chains:** In order to create sufficient value-added jobs, Lebanon will need to further attract and retain foreign investments, and promote linkages and business opportunities between domestic businesses and foreign ones. This requires the development of a job centric investment policy, implementation of key investment related legal and regulatory reforms, strengthening the institutional capacity of the investment development authority, and leveraging the Tripoli Special Economic Zone for investment attraction.

- **Pro-competition policies actions**: To establish a well-functioning and efficient market which translates into better market outcomes such as lower prices, better quality products and services for consumers and businesses, the government needs to build an effective antitrust enforcement framework that eliminates barriers to entry and exit of new business entities and curb anticompetitive behavior. It also needs to strengthen market performance and private investment in key sectors. For example, in broadband, the government needs to level the playing field among public and private and illegal service providers in the different segments of the value chain, and allow for fair and non-discriminatory access to essential facilities for all players in order to improve speed, quality and prices.

- **Trade facilitation reform that can improve trade competitiveness:** To increase the competitiveness of Lebanese exports, the government needs to facilitate trade for the private sector, by bringing the country in line with international Kyoto standards including the

[14] World Bank (2016). "Lebanon: Promoting Poverty Reduction and Shared Prosperity, A Systematic Country Diagnostic". Middle East and North Africa Region.

application of trade automation, streamlining import and export processes and procedures covering a number of agencies, and strengthening risk management at the national level.

- **A best practice framework for the Tripoli Special Economic Zone:** In order to ensure the success of the TSEZ in terms of attracting investment in targeted, job-creating sectors (export-oriented, productive sectors) in one of Lebanon's most lagging regions, the zone should adopt a best practice SEZ framework, with world class trade facilitation measures. Moreover, the TSEZ presents an ideal environment to pilot trade facilitation reforms before scaling nationwide. Also, the TSEZ incentives are attractive for new businesses and build a case for establishing an innovation hub in Tripoli.

1.19 The balance of this report summarizes the key aspects of the analysis and findings of the technical reports prepared on the above policy areas. Particular attention is paid, where possible, to the job creation impact of these policies.

# 2. Public Private Partnerships: Country Diagnostic

***Leveraging private sector investment and expertise to meet current and future infrastructure needs, via PPP arrangements, could be a key factor to improving Lebanon's business competitiveness, and help to drive economic growth and development. With the passage of a PPP Law in late 2017, a legal basis is now in place to support greater private sector participation in investment in critical infrastructure. However, taking advantage of this opportunity will require: government-wide ownership of the PPP law, which can serve to more effectively define and drive the PPP process; building capacity of a centralized coordinating agency within government; putting in place standardized institutional processes and methodologies; and building capacity within line ministries/contracting agencies to develop and implement PPPs.***

## A. Role of PPP in Upgrading Infrastructure

2.1 **Lebanon faces growing infrastructure investment needs driven by insufficient prior investment in infrastructure, destruction and damage to infrastructure caused by conflict, and a fast-rising population driven by the Syrian refugee influx.** The World Bank's 2015 Systematic Country Diagnostic lists Lebanon's under-developed infrastructure as a leading factor in lagging and uneven growth, and stagnant poverty levels. In recent years Lebanon's fiscal deficit has widened as sluggish economic growth has led to stagnant revenues, and government expenditures have increased to meet fiscal demands (particularly related to the refugee influx). In addition, the continued import of fuel to meet the country's power supply needs constitutes 15% of total government expenditures. As a result, while rising government expenditures have led to an increased gross public debt, and capital investments remain stubbornly low, constituting only 4% of the annual budget.

2.2 **To supplement public finance, Lebanon has the potential to leverage private finance via PPPs in support of infrastructure investment and economic growth**. The private sector already plays a major role in the Lebanese economy, and the services and financial/banking sectors represent 70% of Lebanon's national income. However, characterized by high liquidity and solid capital adequacy, there is significant scope for Lebanon's commercial banks to provide the financing to underpin infrastructure investment and PPPs. Indeed, Lebanese banks have a private sector loans-to-deposits ratio of only c.30%, and feedback from commercial banks suggests that there is c.30% of additional deposits available for lending. Given this liquidity, banks are interested and willing to participate in PPPs in Lebanon on competitive terms. To capture available private finance for PPPs, commercial banks advise that GoL needs to develop a robustly-prepared, well-structured pipeline of projects that clearly demonstrate financial viability and bankability, within the context of a clearly defined PPP legal framework. In addition, in order to ensure bankability, it is likely that PPP projects will require a range of capital subsidies and guarantees provided by GoL and/or donors to mitigate credit risk. The type and scope of credit support required will depend on the structure and sector of the project—for example, an urban transport project may require significant capital subsidy, while an energy generation project may require a sovereign guarantee, supplemented by a donor guarantee, to backstop GoL offtake obligations and cover the

foreign exchange risk. The provision of credit support will be particularly important with initial projects in order to help Lebanon's PPP program develop and demonstrate a track record of success to private investors.

2.3 **Sustainably meeting infrastructure needs requires a more structured approach to infrastructure planning, prioritization, and financing.** Expanding and improving Lebanon's infrastructure stock is a key priority of Prime Minister Saad Hariri, while the World Bank's 2015 Systematic Country Diagnostic for Lebanon lists under-developed infrastructure as a leading factor in lagging and uneven growth, and stagnant poverty levels. Recently, the government developed a Capital Investment Plan (CIP). The CIP includes over 280 infrastructural projects, divided between energy, transport, water, wastewater, solid waste treatment, telecommunications, special economic zones and culture and tourism. The first phase spans over six years and is estimated to reach USD10.8 Billion, 35 percent of which could come from private investment under the PPP law. Lebanon secured an estimated $11bn in pledges of loans and grants for the CIP at the CEDRE donor conference that took place in Paris on April 6.

2.4 **While PPPs have been identified as one of the potential tools available to GoL to support the realization of the new infrastructure vision, it will be crucial to ensure that the right projects are pursued within the context of a fiscally sustainable investment program**. Lebanon does not currently have a centralized Public Investment Management (PIM) and fiscal and debt management processes required to identify, prioritize, and structure sector investments in a coherent and systematized manner. In addition, there is no standardized framework to understand the fiscal and debt management implications of PPP projects. The development of a robust PIM process would enable GoL to more effectively identify priority infrastructure projects with PPP potential, while a fiscal management framework and debt management strategy would facilitate the required oversight, by the Ministry of Finance (MoF), of GoL financial commitments to PPPs to ensure PPP program sustainability.

## B. Lebanon Experience in PPPs

2.5 **PPPs are not new in Lebanon**. The country has a long history of private sector participation in the delivery of public infrastructure services, which traces back to the concessions of the Beirut water supply and the Port of Beirut in the 1880s. The 1975-1990 civil war weakened the government's ability to provide public services, and provided further space for civil society organizations and the private sector to take on public service delivery roles on a largely informal basis. Subsequently, in 1994 the GoL introduced private sector participation in the telecoms sector, and in 2000 passed the Privatization Framework Law in 2000. This Law provided the framework for the formal expansion of the private sector role in infrastructure provision, and established the Higher Council of Privatization (HCP). Since 2006 the HCP has advocated for the development of a PPP program in Lebanon, and these efforts have led to the enactment of the PPP Law in September 2017.

2.6 **Over the past 25 years, Lebanon has gained PPP experience across a range of sectors.** The World Bank's Private Participation in Infrastructure (PPI). The World Bank PPI Database identifies 44 transactions in Lebanon, generating total investment of US$827 Million. In addition, there have been a small number of PPP transactions in non-core infrastructure sectors and at the

municipal level, which were not tracked by the PPI Database. These projects include the FAL Mechanique vehicle licensing project, LibanPost, Saida-IBC solid waste treatment project, and the Sukleen/Sukomi solid waste management project in Greater Beirut and Mount Lebanon. It should be noted that all of these transactions were processed on a project-by-project basis, prior to the enactment of the PPP Law, and were procured under sector-specific and/or project-specific laws.

2.7 **However, Lebanon's experience implementing PPPs has been mixed. Of the 44 transactions identified by the PPI Database, 20 were canceled, 6 are concluded, and the remaining 18 are operational**. In addition, many tenders have been discontinued or contracts renegotiated. The major lessons learned from this experience relate to:

- **Lack of Standardized Project Preparation and Contract Design:** The number of early terminations and contract renegotiations is a particularly disconcerting feature of Lebanon's PPP experience over the past 25 years. Similarly, the performance of some contracts has also been widely criticized, largely related to weak contract management and enforcement.
- **Inadequate Tender Procedures:** As the PPP Law was only enacted in September 2017, all prior PPP projects in Lebanon have been tendered under the Public Accounting Law. The general procurement procedures under the Public Accounting Law are designed for traditional public procurement processes, and lack the detailed multi-stage PPP-specific processes that can ensure transparency and competitiveness

## C. Institutional Framework and Ownership

2.8 **Lebanon's new PPP institutional framework provides for centralized, coordinated government decision-making and adapts the role of line ministries/contracting agencies in the preparation and procurement of PPPs.** Prior to the enactment of the PPP Law in September 2017, line ministries were able to procure PPPs on the basis of sector laws and policies, and the procurement procedures laid out under the Public Accounting Law. However, while this enabled line ministries to maintain control of the preparation and procurement of PPPs, it led to differentiated approaches and processes, dependent on the lead line ministry. The recent enactment of the PPP Law provides a standardized approach to project development and procurement. It clarifies the roles and responsibilities of the various government entities within the PPP institutional framework. In turn, this should support the delivery of better prepared and procured PPP projects, leading to improved project outcomes. Nevertheless, practical experience of the implementation of PPP projects under the PPP Law will be required to determine whether the PPP Law is able to address vested interests and other political economy constraints to project development.

2.9 **The institutional framework for PPPs does vary across those countries to have enacted a PPP Law, dependent on each country's specific political and bureaucratic context.** However, the most common institutional framework lays out clear roles for three entities in particular:

- Line ministries/contracting agencies: project owners, and responsible for identification, preparation, procurement, and implementation of PPPs;
- MoF: responsible for assessment and management of fiscal implications of PPPs;

- Centralized PPP Entity: responsible for promoting and coordinating PPP activities, and supporting line ministries/contracting agencies in the development of PPPs. This entity is most typically located within the MoF.

2.9 **The PPP Law is designed to ensure that all PPP decision-making is subject to the highest levels of government coordination, inter-ministerial cooperation, and approval, consistent with the consensus-building decision-making that characterizes the Lebanese confessionally-based political framework.** The legislation establishes the High Council for Privatization and PPP (HCP) as Lebanon's centralized PPP champion (replacing the former High Council for Privatization, HCP). The HCP retains HCP's cross-GoL representation, and membership of the HCP still consists of the President, the Minister of Justice, the Minister of Finance, the Minister of Economy and Trade, and the Minister of Labor as permanent members, and the relevant line minister for each PPP project. The cross-GoL nature of the HCP is designed to promote consensus, generate transparency, and ensure a standardized and predictable "Value for Money" (VfM) approach to PPP initiatives in this country.

2.10 **The PPP Law ensures that significant aspects of the PPP project cycle and related GoL functions require the action and consent of other actors within the GoL**. In particular, project identification and project implementation are the responsibility of line ministries/contracting agencies. Public investment management, budget planning, and fiscal management are the responsibility of the MoF, although this could have been more comprehensively laid out in the PPP Law. The law assigns the HCP Secretary General as head of the project steering committee during the preparation and procurement of each PPP, with representation from the relevant line ministry/contracting agency and the MoF, together with the relevant regulatory agency where it exists. This role as head of the project steering committee during the project preparation and procurement process gives HCP a more active role in the PPP project cycle than is the case for equivalent agencies in some other countries, although there are precedents for this type of centralized control of project preparation and procurement, and the optimal arrangement depends very much on specific country contexts. The most important point to note is that the institutional framework requires the support and buy-in of all stakeholders within the PPP project cycle. Particular attention needs to be paid to the perception that procuring a project under a PPP arrangement will result in a loss of control for line ministries/contracting agencies, which is especially sensitive given the country's confessional political system. To mitigate this perception, it should be emphasized that the project steering committee, headed by the HCP Secretary General, reports to and provides recommendations to the higher-level HCP board (with cross-ministerial representation) to make final procurement decisions. The institutional framework in Lebanon's PPP Law is further detailed within draft PPP Guidelines (being updated) and regulations currently before for CoM for approval.

2.11 **Despite the high-level government commitment to PPPs, capacity and ownership of the new PPP program is currently low among several contracting agencies.** There is high-level government support for PPPs as evidenced by the enactment of the PPP Law.

2.12 **In addition, there is clear appetite for PPPs across line ministries/contracting agencies.** With the enactment of the PPP Law, the HCP needs to build traction and support for the PPP program within line ministries/contracting agencies to build a broad-based momentum for the

development and implementation of PPPs in Lebanon. This priority is all the more the case given the objectives of the CIP which identifies private investment as an essential source of funding, with HCP now working closely with a number of government agent in the assessment of some 18 projects for potential PPP procurement. This will require ongoing awareness building and training to ensure that line ministries/contracting agencies fully understand the detail of the PPP Law and PPP Guidelines, and are comfortable with the roles and responsibilities of all entities within the PPP institutional framework. The institutional framework in Lebanon's PPP Law is further detailed within draft PPP Guidelines (being updated) and regulations currently before for CoM for approval.

## D. Recommendations

**2.13 Below is a list of immediate, short and medium-term priority actions that can help Lebanon accelerate its PPP program.**

*Immediate Actions*

**2.14 Update and finalize the PPP Guidelines, and implementing decrees to the PPP law to create a comprehensive enabling framework for PPPs.**

Lebanon's PPP experience to date has been mixed. PPP projects were afflicted by a lack of standardized project preparation processes and contract design, and by inadequate tender procedures. Based on these lessons learned, the GoL has enacted a PPP Law to provide a comprehensive enabling framework for PPPs, and to support improved project outcomes. The GoL now needs to update and finalize the PPP Guidelines, aligned with the PPP Law, to provide a comprehensive legal framework for PPPs. With the enactment of the PPP legal framework, high-level GoL interlocutors should prioritize communicating and educating all stakeholders on the benefits of PPPs in order to facilitate and catalyze the PPP program.

*Short-term priorities*

**2.15 Design and deliver a communications strategy and capacity building program to demonstrate GoL commitment and ownership of the PPP program and increase capacity of key stakeholders.**

The GoL should design and deliver a communications strategy and capacity building program for PPPs, that would be rolled out to both public and private sector stakeholders. The communications strategy should guide internal and external communication of the GoL's PPP program. It should be designed to build awareness, capacity, and commitment, and convey the goals, objectives, and scope of the PPP program to as broad an audience as possible. The communications strategy should contain detailed content on GoL's objectives, an implementation timeline/approach, stakeholder mapping, and key messages for different stakeholders. Now that the PPP Law is enacted, it is also recommended that GoL holds a highly publicized formal launch event for the PPP program to both public and private stakeholders. This would be a major signal that Lebanon is open for business on PPPs.

The capacity building program should be designed for all key stakeholders, and should therefore provide a variety of depth to the material. Short informational sessions should be organized at the Ministerial level. In-depth training should be provided at the bureaucratic level, aimed at

practitioners across line ministries/contracting agencies and other entities who will be responsible for day-to-day implementation and/or oversight of PPPs. This in-depth training can also be provided to private sector stakeholders to both encourage and enable their engagement in the PPP program. The capacity building program should introduce and explain the PPP legal framework, and should cover all aspects of the PPP project cycle, from initial project identification to implementation and contract enforcement.

### 2.16 Develop standardized documents, tools, and templates to support the preparation of high-quality projects.

The development of a robust PPP pipeline will require the development of standardized documents, tools, and template. These materials will promote adoption of international best practices in project preparation and encourage a focus on achieving value-for-money in PPP deals. This will be of particular benefit to line ministries/contracting agencies, who will have responsibility for the identification and implementation of projects, and will also facilitate the oversight role of the HCP and the project steering committees. The HCP should lead the development of a comprehensive set of standardized documents, tools, and templates for use and reference in the PPP project cycle process, as summarized below:

- Needs analysis, project identification and planning
- Developing preliminary business case
- Feasibility studies and risk analysis
- Economic cost benefit analysis
- Value for money assessment
- Financial feasibility assessment
- Affordability and fiscal impact assessment
- Procurement and contract management
- Disclosure policy
- Performance management and audit
- Dispute resolution

### 2.17 Develop a Fiscal Commitments and Contingent Liabilities Framework and debt management strategy to support the long-term sustainability and management of GoL financial commitments to PPPs.

The assessment and management of government financial commitments to infrastructure investments is currently provided for on a project-by-project basis under the Public Accounting Law and the annual Budget Law. Neither of these existing laws, or the PPP Law, provide specific guidance on the institutional process to approve government financial contributions to PPPs. The lack of guidance on GoL financial commitments to PPPs creates a risk that responsible entities (notably the MoF and line ministries/contracting agencies) will lack the capacity and processes to adequately assess and manage financial commitments to PPPs.

Per international best practice, it is recommended that institutional responsibilities and processes for the assessment and management of financial commitments to PPPs are included within the PPP Guidelines. In addition, a Fiscal Commitments and Contingent Liabilities (FCCL) framework and debt management strategy for PPPs should be developed by MoF in order to deliver integrated assessment and management of all PPPs on a programmatic basis, with clear criteria for the approval of all government financial commitments. The roll-out of the FCCL framework and debt

management strategy should be accompanied by significant capacity building and training for the relevant agencies, in order to ensure the effective oversight of GoL's fiscal commitments to PPPs.

**2.18 Prepare specific guidance on municipal-level projects within the PPP Guidelines or as a standalone Municipal PPP Guideline to facilitate the development of municipal-level PPP projects**

The PPP Law provides the option for municipalities to prepare and procure PPPs under the same processes as national-level projects, but does allow for a differentiated approval process for municipal-level PPP projects, in line with the Legislative Decree No. 118, dated June 30, 1977. This differentiated approval process recognizes that the project development and implementation process and annual planning and budget processes for municipal projects are clearly distinct from national-level processes under national line ministries. Specific guidance on municipal-level PPPs should be included either within the PPP Guidelines or as a standalone Municipal PPP Guideline. This guidance material should be prepared in close coordination with the HCP, MoF, and municipalities. This could include streamlined preparation and approval processes for small-scale municipal-level projects.

*Medium-term priorities*

2.19 **Clarify accounting and budget treatment of PPPs to provide comfort on GoL's ability to deliver long-term financial commitments to PPPs.**

The accounting and budget treatment of PPPs in Lebanon requires clarification. As noted above, there is no specific reference to PPPs within the Public Accounting Law or the annual Budget Law, although the PPP Law does note that government commitments to PPPs shall be accounted for within the national budget. In practical terms, this means that GoL contributions to a PPP project will continue to be managed in the same manner as any other infrastructure investment, and must be included within the annual budget plan of the line ministry/contracting agency. This would include both current (e.g. recurring availability payments) and capital (e.g. up-front capital subsidy) expenditure items. While Lebanon's annual budgetary process does allow for multi-year government commitments to PPPs (under the budget annexes), greater clarity and certainty over the budgetary management of government commitments to PPPs would be useful. It is recommended that MoF issues detailed guidance on the accounting and budget treatment of PPPs, and considers legislation for the formal ring-fencing of multi-year government financial contributions to PPPs within the annual Budget Law. In addition, attention also needs to be given to how contingent liabilities would need to be accounted for within the budget plan of the line ministry/contracting agency.

# 3. Investment Policy

***Expanding existing and creating new inflows of foreign investment into Lebanon will be essential for the creation of value added jobs. Foreign investments can come either in the form of foreign direct investment (FDI) or non-equity modes of investments[15] (NEMs), such as contract manufacturing, service outsourcing or franchising. Despite the resilience of the domestic private sector in times of regional and domestic political instability, it alone will not be able to create the required jobs, nor reverse the decline of the country's economic growth and exports. For this to happen, the Government of Lebanon (GoL) needs to develop a comprehensive foreign investment strategy, focus on key competitive sectors primarily in services such as ICT, Business Processing Outsourcing (BPO), but also in High Tech Manufacturing, undertake key legal and regulatory reforms, and strengthen IDAL and its services.***

## A. Benefits of Foreign Investments

3.1 **Foreign investment, FDI and NEMs, can bring significant benefits to host countries especially in terms of job creation, integration in global markets and trade, technological spillovers, human capital formation, increase of competition, and improvement of enterprise development.** Many studies have shown that foreign investment can increase participation in global value chains GVCs, which in turn leads to the creation of more, better paid and inclusive jobs through catalyzing structural transformation and/or generating backward and forward linkages in and around the chain[16]. There is a wide range of country examples where increases in the number of products exported and the number of export destinations can be traced to policies that are successful in the attraction and retention of efficiency seeking FDI. These includes the experiences of China, Czech Republic, Costa Rica, Malaysia, Mexico, Philippines and Vietnam[17]. Evidence also points to a positive link between FDI and higher wages paid by multinational companies relative to domestic firms[18].

3.2 **In the Middle East and North Africa (MENA) region, most countries are at various stages of implementing reforms aimed at growing foreign investment.** United Arab Emirates (UAE), Egypt, Morocco and Tunisia provide examples of various levels of success in attracting efficiency-seeking investors in the last few years. However, the potential benefits of foreign investment have to some extent been by-passing Lebanon. The understandable pre-occupation with security and political priorities to date has, arguably, resulted in insufficient attention to policy making that can serve to better position Lebanon to capture more of the benefits available from the global economy. This has contributed to the paradox that while it is an open economy with not many legal barriers to the entry of investment, it has remained unintegrated with the global economy.

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[15] Non-equity modes (NEMs) are contracts between a foreign player and domestic firms for production of services and goods, either for consumption or export.

[16] World Bank, 2015, The Impact of Investment Policy in a Changing Global Economy

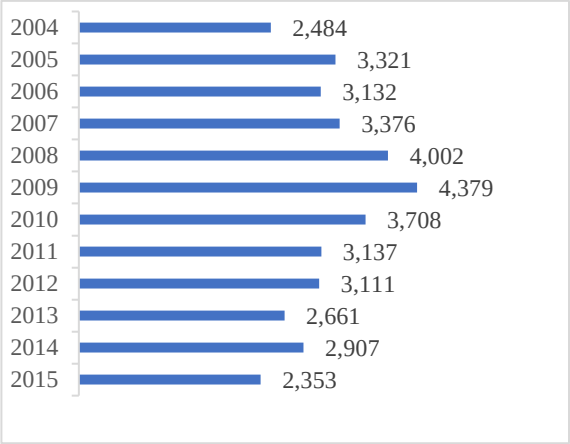
[17] Moran 2014

[18] Heyman, Sjoholm, and Tingvall 2007, and Hijzen and others 2013

## B. Foreign Investment Performance

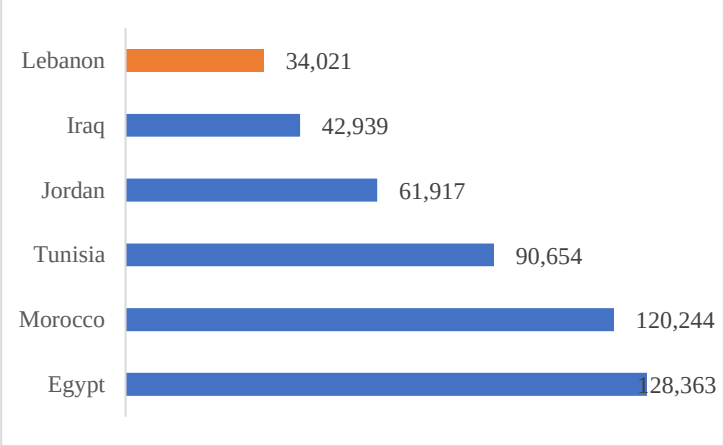
3.3 **Foreign investment inflows have not reached their potential in Lebanon.** Three key observations emerge from an analysis of FDI and impacts on jobs, including: (i) FDI has been declining since 2010 (see Figure 2) at a compounded annual growth rate (CAGR) of 9.8 percent. Regional turmoil, political instability and the economic slowdown of GCC countries contributed to this deterioration[19]; (ii) the number of direct jobs generated by FDI between 2003 and 2017 was significantly lower than in other MENA countries (see Figure 3). During this time, direct jobs mounted to 34,021 - only half of those in Jordan and merely a third of those in Tunisia[20]; and (iii) 44 foreign companies were registered in Lebanon in 2015, in particular in services sectors (financial services, trade/retail, IT) and industry.

Figure 2: FDI Inflows (USD Million)




Source: Central Bank of Lebanon, Balance of Payments

Figure 3: New direct jobs generated by FDI (2003-2017)




Source: FT fDi Markets (2003-2017) database

3.4 **Most investments were not conducive to the creation of value added jobs**. About 70 percent of investment announcements in Lebanon during 2003 to 2017 were in market-seeking sectors[21], while only 16 percent were in efficiency-seeking and 14 percent in strategic asset-seeking sectors (see **Error! Reference source not found.**). The market seeking investments have g enerated benefits, including a good quantity of jobs, namely 22,400, compared to tourism, with 7,500, and efficiency-seeking investment, with almost 4,000 jobs[22]. However, they have not fostered technology and know-how transfer to domestic firms, nor did they increase the volume and sophistication of Lebanon's export basket, which is needed for its international competitiveness and economic growth.

3.5 **A similar pattern can be observed in NEMs, the prevalence of which is a unique feature of the Lebanese economy.** NEMs are mainly concentrated in franchising in hospitality,

[19] Lebanon has not been alone in this downturn, in fact, according to UNCTAD, the entire Western Asia region witnessed a 2% decrease in FDI inflows. 2016 World Investment Report.

[20] FT fDi Markets (2003-2017) database.

[21] Market-seeking FDI includes retail, professional and business services, construction, logistics & distribution. Strategic assets-seeking FDI includes tourism. The majority of export oriented sectors fall under the efficiency seeking FDI - tradable business services or export oriented processing sector are prime examples of this kind of investment.

[22] Estimate using the values for estimated job announcements by FT fDi Markets (2003-2017) database.

services and retail, and management contracts, especially in hotels, telecom (mobile operators), duty free, and infrastructure projects. These are primarily market and partially strategic asset-seeking investors (in tourism) who have chosen to enter through NEMs, either due to their business expansion model or because this form of investment entails less risk. Some export oriented NEMs are present in contract manufacturing or operate under licensing arrangements, mainly pharmaceutical and food and beverage manufacturers[23].

3.6 **Efficiency-seeking investments are particularly important for Lebanon in its effort to create value added jobs, integrate into the global economy and move up the value addition chain.** While typically they are more difficult to attract, they tend to be greenfield and hence a net creator of jobs. Moreover, by integrating the domestic private sector into more sophisticated parts of the global value chain – the jobs created tend also to be both more diversified and attain higher levels of productivity. The export-orientation of efficiency-seeking investment also means it is a generator of foreign exchange. Efficiency seeking NEMs have the added positive feature of mitigating the perception of increased political risk, which is particularly relevant for fragile and conflict-afflicted states with mature private sectors, such as Lebanon. Often, NEMs are the first point of access into global value chains, and gradually local firms (partners) have the opportunity to grow into independent exporters and gain independent access to the global value chains.

## C. Barriers for Foreign Investment

3.7 **Lebanon's potential to attract further foreign investments is partially hampered by the poor perception of its business environment and multiple barriers serve as a deterrent to the entry and growth of foreign investment, including efficiency-seeking types.** In addition to political instability and inadequate infrastructure, focus groups meetings with foreign and domestic companies highlighted several investment climate issues that exist across the investment life cycle that are impeding their decision to invest or reinvest in Lebanon. A summary of the findings is set below.

**Economy-wide constraints:**

- **Investment vision and strategy:** 80 percent of investors in the focus groups rated the clarity and effectiveness of Government's investment policy and strategy as poor.
- **Investment attraction:** 40 percent of investors rate the availability and quality of investment promotion services for investors as average, and 60 percent as poor.
- **Investor entry**: 40 percent of investors disagreed that the process to obtain an operating license was clear and with reasonable time/cost. 40 percent of investors also disagreed that the process to bring in and keep foreign management, or specialized work force, was clear and without unreasonable time/cost.
- **Investor protection and retention**: Unpredictable and arbitrary Government action was among the top concerns raised by investors, in particular, with respect to tax and customs procedures and inspections, but also in other aspects of government conduct. 60 percent of investors rate the effectiveness of tax and customs administration as poor, with concerns

[23] Given the lack of national and international statistics on NEMs, measuring its activity in Lebanon is difficult, except in the franchising sector. Based on available data, contract manufacturing and licensing is most prevalent in the pharmaceutical industry.

related mostly to implementation of law. Per the survey results, 100 percent of investors were not regularly consulted by the Government on proposed regulatory changes.

**Sector-specific constraints:**

- Some multinational, but also domestic, **IT and telecom** companies identified work permits and visa issues to be problematic and unpredictable when recruiting foreign skilled labor. In addition, they highlighted the weak enforcement of intellectual property rights.
- Companies who service or manufacture **high technology products** identified customs procedures to import or export as very complex, lengthy and cumbersome.
- Investors in the **tourism/hospitality** sector stated that the Labor Law is outdated and hiring part time workers during the peak seasons as very costly.
- Foreign **construction** firms indicated that Government procurement practices sometimes indirectly favor domestic firms.

## D. Legal Framework Governing FDI and NEMs

3.8 **In addition to investment climate issues, a review of Lebanon's policy, regulatory and institutional environment for investment, highlights additional challenges and gaps**.

3.9 **An analysis of the Investment Law 360 (IL) has highlighted multiple gaps.** From a good international practice perspective, the IL has several shortcomings, including: (i) it is incomplete, because it fails to address the core principles of good investment legislation: investor rights and asset protection;(ii) contains an inflexible and insufficient legal base for investment promotion and attraction: though IDAL is an autonomous legal entity with its own budget reporting to the Prime Minister[24], the law makes the institution inflexible and ill-prepared to function as an effective investment promotion agency, and; (iii) offers a seemingly generous but untested incentive scheme with no mechanism in place to conduct an effectiveness assessment of incentives in terms of attracting investments of generating jobs. According to IDAL, 73 percent of incentives provided by IDAL are offered to domestic firms, suggesting that locational incentives are not being used as an effective foreign investment attraction tool.

3.10 **In addition, the legal and regulatory framework for NEMs and its implementation are weak.** This is particularly evident in terms of enforcement of contractual rights and the protection of intellectual property. Furthermore, there are no specific programs or incentives that would promote NEMs and link local firms with foreign partners.

3.11 **On the institutional level, benchmarking IDAL against global best practices in investment promotion suggests that IDAL's performance is lagging along some dimensions.** The national investment policy and promotion agenda in Lebanon lies almost entirely with IDAL. However, compared to best practice investment promotion agencies, there are significant areas for improvement. First, it is particularly weak on strategic planning, aftercare and policy advocacy. IDAL provides a limited range of services that do not capture the whole investor life cycle. Second, aftercare services aiming at investor retention and expansion, and promotion of linkages and spillovers to the domestic economy, are not developed at IDAL. Third, reviewing the governance

[24] Art. 3 and 8 of the Investment Law 360

framework will also likely help IDAL to unlock its full potential and maximize its leverage of policy makers to improve the product and investment climate of the country. Fourth, reducing the number of target sectors to those with the strongest value proposition to foreign investors will help to focus the agency's limited resources. In addition, this will aid Government policy and its product development effort on sub-sectors that can become the drivers of future economic growth of the country, such as tradable services.

## E. Sectors of Focus

3.12 **A rapid scan suggests that Lebanon's investment promotion effort should focus on a set of four to five sub-sectors in efficiency-seeking sectors, namely in tradable services (BPOs, ICT) and export oriented high-tech manufacturing**. These are "ready to go sectors" presenting high value added to Lebanon (primarily in terms of jobs creation but also with regards to the whole value chain development and supplier opportunities for domestic firms) that are also likely to be attractive for foreign investors given the country's existing international competitiveness.

3.13 **The second group, "aspirational sectors" for investment promotion, include healthcare, tourism, media and entertainment, pharmaceutical and chemical sector.** These are not yet ready for FDI promotion. For example, two market oriented sectors - tourism and healthcare - are likely to provide a strong value proposition to potential investors. The former, however, depends on the tourism growth trends in the country, and the latter on the healthcare sector's capacity to enlarge the domestic market by attracting foreign clients, i.e. healthcare tourism. Others require improvement of Lebanon's international competitiveness, such as pharmaceutical and chemical industries. This group, however, could present opportunities for NEMs, such as in contract manufacturing and other forms.

3.14 **The remaining sectors, namely agro-processing, agriculture and construction materials, while still presenting considerable value for Lebanon, do not hold a strong value proposition for FDI**. This is because of either: high operating costs and trade barriers (low to mid value-added manufacturing, agro-processing); weak FDI demand (printing, media); or the prevailing investment mode (mergers and/or acquisitions) that usually does not generate new jobs (pharmaceutical, agro-processing sectors). There may be opportunities in some version of NEMs (such as contract farming), however, this assumption would need to be verified through a mapping of available local partners.

## F. Recommendations

3.15 **In summary, opportunities in Lebanon exist in both FDI and NEMs. They are primarily available in services (BPO and ICT), but also in manufacturing via NEMs.** Services sectors are less affected by the limitations of transportation infrastructure, relatively high labor costs and behind the border trade barriers. They are reasonably resilient to these challenges but still require a good investment climate and online connectivity.

3.16 **However, for Lebanon to take advantage of these opportunities and become a significant regional player as a more sophisticated economy that is better integrated with the MENA region, Europe and Asia, GoL will need to take steps to improve the investment**

**competitiveness of the economy, and then focus on facilitating investment in a small group of sectors in which Lebanon is already competitive.** Identified sectors should also be those most capable of providing value added jobs. Accordingly, there are two elements at play. One is improving the value proposition of Lebanon for investors. This involves addressing current shortfalls in the policy, legal, regulatory and institutional environment for investment. The other element is actively targeting and facilitating investment into sectors and subsectors of particular interest for Lebanon.

3.17 Suggested recommendations include:

3.18 **Develop and adopt a job-centric investment policy:**
To address the jobs challenge in Lebanon, the country should target attracting new and growing existing foreign investment. This should be focused particularly in efficiency-seeking sectors, which tend to be better paid, generate knowledge externalities, increase labor productivity and lead to a higher standard of living.

3.19 **Gradually implement a set of key legal and regulatory reforms to facilitate investment and jobs:**
Legal and regulatory reforms are an integral part of investment competitiveness. Based on private sector feedback and a legal review, identified reform priorities include: (i) update the Investment law, as well as new decrees, to strengthen IDAL and include investor protection guarantees important for foreign investors; (ii) implementation of a one-stop shop for investors at IDAL; (iii) streamline processes for the administration of investment incentives and the receipt of an operating license for investors; (iv) adjust visa and work permit rules to attract foreign skilled labor, especially in specialized GVC tasks; and (iv) conduct steps to take stock and address grievances impeding expansion of existing investors, initially through IDAL.

**3.20 Strengthen institutional capacity and sector focus of IDAL:**
IDAL's performance can be improved by strengthening several of its institutional dimensions (such as mandate, strategy and governance) and core competences, including a greater focus in a narrower set of sectors that can create value-added jobs. This includes, in particular, strengthening investor aftercare and outreach, and policy advocacy aimed at investment climate improvement.

**3.21 Utilize Tripoli Special Economic Zone for investment attraction:**
TSEZ provides an opportunity for the government to advance investment attraction as a part of GoL's foreign investment vision. Consideration should be given to three areas, namely ensuring a best practice business environment for foreign investors, focusing on a subset of competitive efficiency-seeking sectors named above for which the zone conditions would provide an advantageous setting, and articulating and communicating Lebanon's value proposition for foreign and domestic investors within the TSEZ, coupled with proactive outreach, which should be an integral part of services provided by a relevant government agency such as IDAL.

# 4. Competition Policy

***Designing and implementing a comprehensive competition policy is key for Lebanon's ambition to boost private investment and create more and better jobs. Competitive pressure matters for achieving greater innovation and productivity. It is a market efficiency pre-requisite which translates into better market outcomes such as lower prices, better quality products and services, and greater choice for the Lebanese consumers and businesses. As such, it is key to build an effective antitrust framework and strengthen the current competition draft law for Lebanon. Effective competition is particularly important in sectors such as Broadband and Cement as they are key drivers of efficiency and productivity growth in downstream sectors that use these inputs. Currently, Lebanon's poor performance in broadband is a drag on economic growth. To improve speed, quality and price of internet, the government needs to level the playing field among all service providers and encourage competition on the merits, allow for fair and non-discriminatory access to essential facilities and promote competitive neutrality between the state-owned operators and private players. Also, the government needs to strengthen market dynamics in the cement sector and review the price setting mechanism. In the absence of sound competition policies and antitrust enforcement, efforts to attract and retain investments might be impaired by anti-competitive practices of firms.***

## A. Benefits of Competition

4.1 **The economic benefits from competition are substantial and well documented. Firms operating in a competitive environment are more likely to innovate[25] and to increase their productivity[26]. Competition boosts investment[27], generates employment and ultimately speeds up economic growth and improves overall welfare.** Competition in input (upstream) markets, such as transportation, financial services, energy, telecommunication and construction services, is a key driver of efficiency and productivity growth in downstream sectors—the users of these inputs. Empirical evidence strongly supports the positive effects of competition policy enforcement on productivity growth[28]. Increased international competitiveness - and therefore more favorable terms of trade - is another important and positive effect associated with increased competition in domestic markets. Finally, consumers benefit from lower prices, direct savings and improvements in the variety and quality of goods and services. Consumers also find enhanced job opportunities and additional income as investors. Also, anti-competitive practices result in welfare losses for the economy as a whole. Price-fixing agreements among competitors impose significant costs on society.

4.2 **Recent evidence from Lebanon suggests that the entry of politically-connected firms (PCFs) in markets reduces job creation in Lebanon**. The existence of PCFs in a sector reduces net job creation by reducing sharply the growth of non-PCFs due to unfair competition by PCFs which hurts their direct competitors and reduces their incentives to invest and innovate. On a net basis, the effect of this misallocation of resources towards PCFs is that each additional PCF reduces

[25] Bassanini and Ernst, 2002, Bloom et al, 2011
[26] Acemoglu et al. 2006 or Aghion and Griffith, 2005
[27] Alesina et al, 2005
[28] Voigt, 2009 or Buccirossi et al, 2009

jobs created by 7.2 percent at the sector level and reduced jobs created by non-PCFs by 11.3 percent. [29]

## B. State of Competition Policy in Lebanon

4.3 **Unlike many of its peer countries, Lebanon lacks a competition law and an antitrust enforcement framework.** A draft law was first drawn up in 2005, and in 2012 Lebanon introduced an updated draft, however its enactment has been delayed. In 2017, work on the Draft Competition Law by the Ministry of Economy and Trade (MoET) has been initiated again in recent months. The draft law is the first in Lebanon that simultaneously prohibits anticompetitive agreements, abuse of a dominant position, and anticompetitive concentrations (mergers). It establishes a national Competition Authority (CA) in Lebanon, granting it exclusive jurisdiction over the application of the competition law and laying out a system of appeals regarding decisions of the Competition Authority.

4.4 **The draft law is fairly comprehensive but could be strengthened with a number of amendments which would allow it to be more effectively implemented such as:** (i) clarifying whether the law intends to prohibit "monopolies" per se or to prevent "monopolistic practices, (ii) making exemptions from penalties and provisions for leniency obligatory and not discretionary if a party comes forward and provides evidence on anticompetitive behavior, (iii) including a specific list of sectors that are exempt from the application of this competition law versus open broad open ended exceptions, (iv) ensuring that merger notification criteria are optimally set using clear criterion, (v) revisiting the ability of national competition authorities to engage in enforcement against state aid control, and (vi) specifying in the law that the competition authority will report to the Cabinet or Prime Minister directly in order to strengthen independence.

4.5 **There are a number of government interventions that affect the economy in a cross cutting way or that affect several sectors at once, such anti-dumping measures, exclusive agencies and price controls.** A review of 20 industrial sectors is currently underway by the Association of Lebanese Industrialists (ALI) at the request of a Prime Ministerial Committee on Anti-Dumping, to determine whether dumping is taking place and assess the need for protections. When not appropriately applied, anti-dumping measures and industry protections, can cut off a strong source of competitive pressure in markets thereby dampening incentives to seek efficiency and to innovate. It may also facilitate collusive behavior. Where they occur in consumer goods it is consumer that are harmed directly – in particular any measures that affect basic food markets and raise prices for consumers are likely to hurt the poor disproportionately. Similarly, Lebanon's Legislative Decree No. 34 of 1967 grants exclusive agencies and sole distribution rights to importers of all products with the exception of foodstuffs, washing products (detergents), and cleaning material. Exclusive rights granted to some importers, with state protection, can also hinder competition. Moreover, despite enjoying a free market economy where sellers of locally produced or imported goods set freely the prices of their products, some goods prices are directly regulated by the government[30].

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[29] Diwan and Haider, 2016

[30] 5.1 The government sets prices especially in the utilities sector, such as energy products, electricity, telecommunications, in addition to pharmaceutical drugs and Lebanese bread. In addition, the technical center for pricing policies at the Ministry of Economy and Trade (MoET) controls and monitors price fluctuations of consumer

## C. Key Competition Issues in the Telecommunications Sector, with Specific Focus on the Broadband Sub-sector

### a. Overview of Broadband in Lebanon

4.6 **Both mobile and fixed broadband services in Lebanon appear to perform below potential in terms of initial indicators of competition compared to regional peers.** World Bank 2014 classes Lebanon as a country with a "developing" fixed and mobile broadband markets. Its prices are relatively high but penetration rates are low. Lebanon is the only market in the development phase in MENA that has a monopoly ownership in the mobile segment, in this case held by the state. Mobile networks in Lebanon are owned and regulated by the Ministry of Telecommunications, and managed on a fee basis by 2 private operators: Orascom Telecom of Egypt who operate Alfa (MC1), and Zain of Kuwait who operate Touch (MC2).

4.7 **Broadband access, on the other hand, is open to a level of competition**. A large number of Data Service Providers (DSPs, facilities-based operators), and Internet Service Providers (ISPs) - using the infrastructure of Ogero or licensed DSPs - are operating in this market segment. They all compete with state-owned Ogero who not only operates the fixed line on behalf of the MoT, but also acts as a DSP and an ISP. In addition, many unlicensed operators are also offering high-speed internet (grey market). Despite this entry in this segment, there are several regulatory issues that are preventing the full benefits of competition in this segment. First, while DSPs have the right to build their own backbone infrastructure, *de facto*, over 90 percent of the backbone/backhaul market is provided by MoT/Ogero. Second, the terms and conditions of the different licensees are not consistent and Ogero also offers retail internet services, commanding over half of the market share. These constraints do have an impact on the technology options available to the consumers and, indirectly on average broadband internet prices and speed.

4.8 **Mobile penetration and prices in Lebanon lag behind some regional peers.** Mobile phone subscriptions witnessed a sharp increase in the past few years registering a 94 percent penetration rate. Mobile broadband penetration rates have also been on the rise, reaching 53.5 percent in 2015 up from 43 percent in 2013. Despite the increase in penetration, Lebanon stands behind some regional peers, especially GCC countries with penetration rates above 100 percent for some. In terms of prices, Lebanon's operators charge the highest prepaid average minute rates in the Arab World according to the 2016 Networked Readiness Index and ranks 120 out of 139 worldwide countries[31]. However, mobile international termination rates are lower than benchmark countries like Egypt and Tunisia. These prices are set and controlled by the government.

4.9 **Lebanon also trails behind other countries in the region in regard to quality and speed of broadband network and services.** Despite being the regional pioneer in introducing

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goods mainly in supermarkets. However according to MoET regulations, Legislative Decree No. 73/83, the ministry has the right to set a ceiling on prices or profit rates where price should not exceed double the cost, but in practice this is not being enforced.

[31] The 2016 Networked Readiness Index does not take into account the latest mobile price reduction that happened in July 2017.

internet in 1996, fixed broadband internet services, using Digital Subscriber Line (DSL) technology, were not launched until 2007 and broadband has been available only at low speeds and at, until more recently, high prices. This has changed in the past few years due to proactive measures to reduce prices, increase speed and to upgrade the infrastructure, mainly through the deployment of fiber optics cables and increased international bandwidth. These efforts have led the penetration rates to increase significantly from 9.85 percent in 2013 to reach 22.76 percent in 2015, making broadband penetration rates the highest in the region. Fixed broadband internet tariffs reached on average USD 30.4 per month in 2015, according to the 2016 Networked Readiness Index[32], significantly cheaper than regional peers, particularly GCC countries. However, despite improved affordability and infrastructure upgrade over the years, Lebanon has one of the lowest bandwidth per user in the region.

### b. Status of Reform of the Telecommunication Sector

4.10 **In 2002 the GoL issued the Telecommunications Law No. 431 which aimed to transform the telecommunications sector in Lebanon from a state-owned fixed monopoly to a competitive market, open to private participation**. It provided the framework for a new telecommunications private operator "Liban Telecom" to replace Ogero –the MoT owned wireline provider. Liban Telecom would initially be state-owned but eventually be privatized, bringing in a strategic investor and offering shares to the public. It would operate fixed international and local lines, internet and data services and a third mobile phone network.

4.11 **The law also established an independent regulator, the Telecommunications Regulatory Authority (TRA), who was assigned to liberalize, regulate and develop the sector by promoting competition, however its powers were suspended in 2011 and MoT assumed the role of a de facto regulator.** The TRA's mandate include issuing licenses and regulatory decisions; managing the wireless spectrum and numbering plan; monitoring the market for any abuse of dominant market position and anti-competitive practices; and taking remedial action. In June 2011 the State Council issued a verdict stipulating that Law 431 has been suspended, as such TRA's power was curtailed. Since then MoT took over the responsibilities of the TRA. This represents a significant challenge to the sector given that MoT remains the owner of the dominant incumbent in every segment of the broadband value chain.

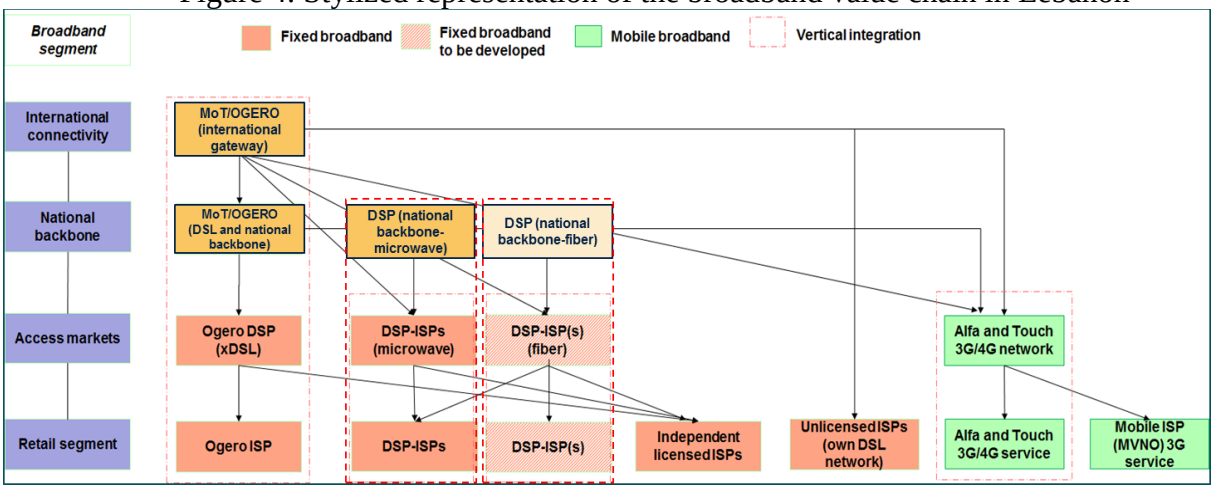
4.12 **Currently, there are efforts by the MoT to develop a new vision to revamp the telecom sector and increase private sector participation.** In February 2017, the new Ministry of Telecommunications promised to renovate the landline communication network, upgrade fiber optic networks, and improve internet services. In the same context, the Council of Ministers issued a decree in June 2017 cutting the prices of DSL internet services by more than 50 percent. It has also agreed to open international gateway and bandwidth capacities for all users, and to reduce the prices of international lines around 300 percent from USD250 per line per month to rates starting from USD110 per line per month, with discount brackets for wholesale and heavy users. In addition, the same decree allows for the first time, a private data service provider to deploy its own fiber optic cables.

[32] The 2016 Networked Readiness Index does not take into account the latest mobile price reduction that happened in July 2017.

### c. Development of the Broadband Value Chain and Key Competition Constraints

4.13 **State owned firms Ogero, Alfa and Touch are the dominant player in all segments of the value chain, acting as both an upstream provider of essential facilities to private firms, as well as a rival downstream (see Figure 4)**. This is evident in all four segments: international connectivity, national backbone, access markets, and the retail segment. This situation can leave scope for reductions in competition and have detrimental effect on the quality, access and pricing of broadband if not adequately regulated.

Figure 4: Stylized representation of the broadband value chain in Lebanon




Source: Authors' own elaboration

4.14 **International Connectivity[33]:** The MoT owns all elements of the international connectivity value chain, sub-marine cables, landing stations and international gateways[34], and thus the state is the monopoly provider of international data connectivity (provided through 2Mbps E1 lines) to Ogero and private Data Service Providers (DSP). Prices of the E1 lines are set by MoT without using cost based measures and unlike private DSPs, state owned Ogero pays MoT for E1 lines at the real cost level.

4.15 **National Backbone[35]**: The passive infrastructure of the national backbone in Lebanon consisting of the traditional copper network as well as fiber optic backbone network are owned by MoT/Ogero. With the saturation of the MoT network used for Asymmetric Digital Subscriber Line

[33] An international gateway is a facility through which data communications can be sent between the domestic networks of different countries. This is the starting point for Lebanon's connection to the World Wide Web.

[34] The MoT owns stakes in three international fiber-optic cable systems: Syria-Lebanon ('Berytar', 46.9 percent), launched 1997, 5Gbps, 134km, Tartous (Syria) to Beirut; Cyprus-Lebanon ('Cadmos', 38 percent), launched 1995, 2x622 Mbps, 230km, Pentaskhinos (Cyprus) to Beirut; and Egypt-Syria ('Aletar', 6.25 percent), launched 1997, 5Gbps), 787km, Tartous (Syria) to Alexandria (Egypt). Two satellite earth stations also provide international links.

[35] The national transmission network refers to large inter-city capacity used to connect different service areas to provide the internet connection. The lack of a high speed/high capacity national transmission network is considered one of the biggest bottlenecks to high speed internet in Lebanon.

(ADSL[36]), the MoT started expanding and modernizing its national transmission network by laying down a fiber optic backbone. This was initially scheduled for completion in 2012, but, despite the laying of at least part of this network, there were delays in switching on the connections over the network. The upgrade of the fiber backbone was later accelerated in the second half of 2015 after the MoT presented a new five-year '2020' strategy in July 2015 envisaging nationwide fiber access coverage. Currently a tender for a new investment, estimated at US$300 Million, to upgrade the Fiber to the Cabinet (FTTC/FTTH) infrastructure, by bringing fiber to all cabinets, was launched by MoT/Ogero. The lack of competition in the provision of national bandwidth can act as a bottleneck to lower priced broadband services and can hinder the roll out of the national network.

4.16 **Local segment (including activities of Date Service Providers)**37**:** The local loop in Lebanon (traditional copper last mile) is owned by Ogero. Since this gives the incumbent the ability to control access to customers, in many countries where the local loop is owned by the incumbent, regulators have required "local loop unbundling" or LLU. This is where incumbents provide competitors with access to local loops, allowing them to offer broadband and other advanced services to existing users of the fixed line. In Lebanon, Local Loop Unbundling (LLU) regulations drawn up by TRA have remained in draft since 2007 but LLU has not been implemented. LLU is particularly relevant where there is a lack of significant competition between different types of access network for broadband. In the absence of LLU, DSPs in association with ISPs offer internet services to final customers by buying wholesale services from Ogero on the local network, which accounts for a high proportion of their costs. There are around five major active DSPs (although the MoT listed ten licensed DSPs as at 2016), with Ogero being the dominant DSP. Most DSPs are vertically integrated with an ISP. DSPs have also been assigned spectrum and operate certain infrastructure-based services including wireless access (microwave based services). Spectrum is assigned without a competitive process and players pay a very low flat fee (US$ 60,000) for spectrum regardless of the amount or band of frequency assigned. Moreover, in June 2017, a decision was made to provide the right to roll out local fiber networks to 2 private DSPs with no competitive tender process. These two DSPs were the only two players with the right of way to build a fiber network in their license terms (other DSPs only have right of access in their license terms). That decision was subsequently called into question by other DSPs who filed a claim at the State Council based on the proposal that DSPs license terms should be harmonized so that all players have the opportunity to compete in terms of facilities. The discrepancy in licensing terms for private DSPs is not only limited to the right way and the ability to deploy fiber optic, it also entails different revenue sharing models. This can provide some DSPs with an undue advantage[38].

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[36] Asymmetric digital subscriber line (ADSL) is a type of digital subscriber line (DSL) technology, a data communications technology that enables faster data transmission over copper telephone lines than a conventional voiceband modem can provide.

37 The term "local loop" traditionally refers to the circuit wiring (copper wire, cable, optical fiber or wireless) that links a telecommunication network with a customer's home or business. Local loop unbundling (LLU or LLUB) is the regulatory process of allowing multiple telecommunications operators to use connections from the telephone exchange to the customer's premises.

[38] In addition to the prospective disparity in treatment of different private DSPs, they must all pay yearly fees to MoT in order to renew their initially issued licenses by the Council of Ministers while Ogero is exempt

4.17 **Fixed broadband retail (fixed ISP segment):** ISPs rely on DSPs and Ogero for wholesale services and resell subscriptions to end users by providing the necessary equipment for connection. Ogero is dominant in the ISP market despite the presence of legal and grey-market competitors. There are around 43 licensed ISPs (as at June 2016) – six of which are considered major market players - and around 70 unlicensed DSP/ISPs. As well as being the primary provider of essential facilities, Ogero is thought to hold around 50 percent market share in the DSL market. There have been complaints of an unlevel playing field between licensed, unlicensed ISPs and Ogero. Unlicensed ISPs are thought to provide internet service to up to 100,000 households. They access international capacity from Ogero but have built their own local DSL facilities to reach the end consumer (something which licensed players are not able to do). Unlike licensed ISPs, they do not share revenue with the MoT and do not pay licensing fees. In March 2017, the MoT indicated that they intended to implement a plan to license unlicensed players, although it was not clear how the playing field would be levelled between licensed and unlicensed players given the existing difference in infrastructure.

4.18 **Mobile Broadband**: The state holds the monopoly on mobile broadband service provision. The state has two mobile network operators (MNOs), Alfa and Touch holding around 47 percent and 53 percent of the MNO market respectively. The two are under management contracts with the private sector but the MoT continues to be the key strategic decision maker for the two firms. For example, the MoT makes key decisions regarding the roll out of new services and sets the final retail prices for both MNOs services. The mobile firms generate a combined total of roughly USD1.2 to 1.4 Billion in revenues for the state each year, making the sector the third-largest government income earner after VAT and customs. Mobile broadband services can compete with fixed broadband services (particularly for household use), but the benefits of this may be limited in Lebanon by a lack of independent regulation of the state monopoly. Some private fixed broadband ISPs have complained that the state-owned MNOs benefit from subsidized antenna rental space and electricity, a lack of license fees, lower taxes and lower prices for international bandwidth from MoT. MNOs are also thought to highly cross-subsidize 3G services with their voice profits. All of which undermines effective competition in the market and reduces public access to choice and quality services.

## D. Development of the Cement Sector and Key Competition Constraints

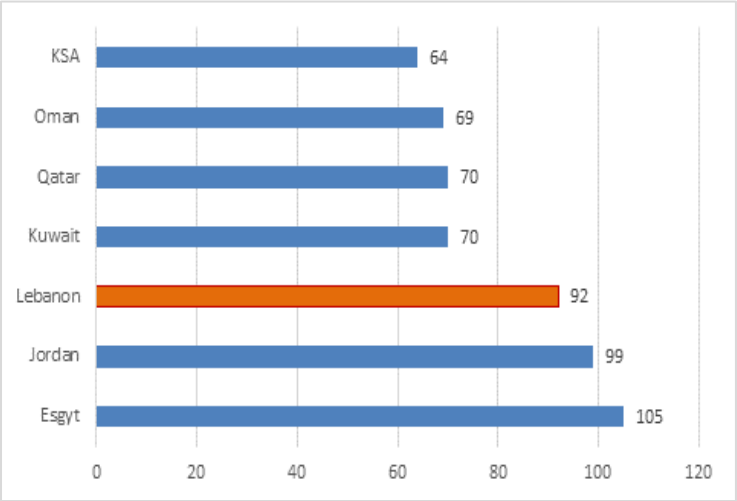
4.19 **Lebanon's cement supply is provided by three fully backwards integrated cement plants:** Cimenterie Nationale accounts for 41 percent of total cement sales, Holcim holds 40 percent, while Ciment de Sibline has the remaining 19 percent market share (figures as at 2015). All produce grey cement (42.5 grade), while only Holcim produces white cement. All producers have access to their own limestone mines, and tend to supply to all regions of Lebanon.

4.20 **There are additional limestone reserves in Lebanon that would allow for entry, although the attractiveness of these sites is not equal.** The Council of Ministers holds a "quarry masterplan" showing the location of these reserves that can be used by investors to understand whether new entry would be feasible and desirable. At least one prospective investor holds a license for establishment of a new plant but has not started operating yet, ostensibly largely due to environmental concerns.

4.21 **Cement imports can be a significant source of competition to incumbent producers but are now de facto prohibited**. In Lebanon import licenses for Portland cement and clinker are no longer issued by the Ministry of Industry and tariffs reach 75 percent on Portland cement and clinker, and 25 percent on white cement. The rationale for this de facto ban on imports is that Lebanon currently has excess production capacity in place. In turn, producers have agreed not to export cement unless there is significant excess capacity in the market.

4.22 **In return for import protection for incumbents, wholesale cement prices in Lebanon are not set by the market but through a negotiation between producers and the government.** Prices are set through negotiation with the Ministry of Industry at around USD90 per ton against USD50 per ton for imported cement from Turkey. This price has not changed since 2009 despite fluctuations in energy prices. Costs of production in Lebanon could be between USD20-50 per ton implying healthy margins for producers. In fact, wholesale cement prices in Lebanon are amongst the highest in the region with only Jordan and Egypt being more expensive (see Figure *5*: Wholesale prices of cement in Lebanon and peer countries (USD000), 2014Figure *5*).

Figure 5: Wholesale prices of cement in Lebanon and peer countries (USD000), 2014




Source: "Lebanon's Cement Sector: A Progress to Continue" Blominvest Bank Lebanon, 2016

4.23 **One reason for the price differential between domestic and imported prices could be higher energy prices or less efficient technology** (e.g. the industry in Turkey is highly competitive and makes effective use of alternative energy sources such as toxic waste). However, the industry in Lebanon considers Turkeys prices to be highly subsidized or for producers to be engaging in dumping in Lebanon.

4.24 **At the domestic market level, some recorded practices further diminish effective competition:**

- **There may be some advantages provided to certain players at the local/municipal level.** One cement producer may benefit from a cost advantage over the other two cement producers since it benefits from direct electricity lines to its plant provided by the municipality while the other two must be connected to the grid or produce their own energy.
- **Firms appear to practice customer allocation.** Market shares on national basis have been stable over the last decades with no significant entry or exit. In practice, market shares are

agreed between the three producers. Customers (concrete producers) are generally not able to switch between suppliers due to these agreed market share arrangements, meaning some bulk buyers have not switched cement suppliers in close to 40 years despite attempts to renegotiate with other cement producers.

- **All cement producers are integrated into concrete production and there are reports they have used exclusionary strategies to foreclose independent rivals from the concrete segment**. This is not necessarily anticompetitive and integration can be efficient but will depend on the exact effects and circumstances of the case. Some independent concrete producers that did survive appear to have been able to maintain their position in the market by striking deals with cement producers allocating them a share of the downstream concrete market.

## E. Recommendations

4.25 Based on the findings outlined above, the GoL may wish to consider the following recommendations:

**4.26 Building an effective antitrust framework:**

- Strengthen current provisions in the draft law and determine institutional arrangements for the Competition Authority in a way that maximizes its independence while ensuring it has the necessary strength to enforce decisions.
- In parallel it will be key to build broad support for an effective antitrust framework in Lebanon. Generating evidence on the potential benefits of competition can help build backing for the passage and effective implementation of the antitrust framework.
- Engage with various stakeholder groups beyond policy makers, including conducting training with civil society and media on the benefits of competition for consumers, entrepreneurs and for job creation, in order to build demand for enforcement of competition rules.

**4.27 Strengthening market dynamics in the broadband sector:**

- Consider developing a feasible strategy for promoting competition in the sector to complement the MoT's plans to issue a new vision for the sector (or specific revisions to Law 431) - which acknowledges the suspension of privatization plans - to allow for a more level playing field even in the absence of privatization.
- Complete the proposed functional separation of Ogero into an "infraco" and a commercial arm.
- Consider developing and issuing guidance on the definition of an essential facility to be used by the MoT in determining access conditions for private sector players to the state owned essential facilities (e.g. international gateway, national backbone, certain 3G/4G networks) in a fair and non-discriminatory way.
- Complete the proposed harmonization of DSP/ISP licensing terms to i) bring licensed and unlicensed players under the same framework and tackle illegal behavior of unlicensed players; and ii) harmonize licenses terms and fees.
- Consider whether DSP/ ISPs could be subject to a general authorizations scheme rather than licensing and increase the period of validity of DSP/ ISP authorizations / licenses to ease entry into the sector and increase certainty for players.
- Finalize, publish and implement the spectrum roadmap aligning spectrum bans with ITU allocations, and considering measures to assign spectrum in a way that promotes new entry

and greater competition. The ad hoc assignment of frequencies amongst DSPs creates an unleveled playing field and does not create value for the state. Spectrum released through digital switchover and refarming should be assigned through a competitive process which allows for new entry (e.g. through an auction with caps in place).

- Consider implementing a competitive neutrality framework to allow for competition between private DSP/ISPs and state-owned operators on a level playing field. This would include understanding and reforming, where possible, specific advantages received by the state, such as subsidized antenna rental, subsidized electricity, lower taxes, differences in licenses fees and differences in cost of bandwidth.
- Allow for facilities-based competition between last mile fiber networks: Competition between private players in the laying of last mile fiber networks is viable and can have significant benefits in promoting investment, innovation and improving quality/prices. Despite earlier moves to select one private player selected to lay last mile fiber, there has been recent direction to ensure that the right to lay fiber is not given exclusively to one player.
- Consider ways to rebuild the TRA as an independent regulator in the medium term. Consider ways to strengthen market intelligence, including of the unlicensed players (since all players contract with Ogero/MoT).

**4.28 Strengthening market dynamics in the cement sector:**

- Consider whether the price setting mechanism could be made more market-based with a direct link to international and/or energy prices, whether they could be time bounded to encourage a move towards price competition, or whether prices could be set independently of operators.
- Consider the value in developing a feasible plan to actively promote new investment in the sector in anticipation of future increases in demand (e.g. from reconstruction efforts in Syria) using the quarry masterplan held by the Council of Ministers to understand whether new entry would be feasible and desirable.
- Examine the costs and benefits of import protections taking into account the effect that exposure to imports could have on incentivizing greater efficiencies and the use of more innovative technology, as well as on costs for local businesses that use cement as an input. Also consider monitoring effects of such measures.

**4.29 Reform of cross cutting economic policies to boost competition:**

- Review the benefits of current exclusive agency provisions and consider resuming efforts to enact a law abolishing exclusive agencies.
- Develop guidelines for implementing antidumping measures and imposing infant industry protection in a way that avoids conflict of interest in the review process, that takes into account spillover effects on industries that use products as inputs and guidelines for application (e.g. include ensure measures are proportionate and time bounded).

# 5. Trade Facilitation

***Facilitating trade is vital for Lebanon to improve its integration with the world, unlock foreign investment opportunities, improve exports' competitiveness and create jobs. Moving goods efficiently and predictably across borders is necessary if Lebanon is to expand its exports, attract and retain efficiency seeking foreign investments and tap into global value chains. If shipments are consistently delayed at ports or if the paperwork needed to clear goods for export are overly cumbersome or not clear, investors will turn towards other opportunities. Moving forward, it is recommended that GoL implements reforms to bring customs agency performance in line with the Revised Kyoto Convention (RKC), including the simplification of trade procedures, increased automation, and strengthening of risk management.***

## A. Benefits of Trade Facilitation

6.1 **Trade facilitation can yield significant benefits to economies. It raises productivity and improves export competitiveness, which in turn expands trade and result in job creation.** The OECD estimates that for every extra day required to ready goods for import or export decreases trade by around 4.5 percent. In the same context, studies found that exporters in African countries with more efficient customs agencies export more products[39]. Other studies estimate that significant trade facilitation reforms could cut trade costs by almost 14.5 percent for low-income countries and10 percent for high-income countries. Also, evidence suggest that jobs that are tied to trade tend to pay better than those that are not. For example, in Western Europe, those working in export-oriented companies collect a 10-20 percent wage premium over the average wage. In the United States, the premium is 6 percent and in Sub-Saharan Africa the figure is 34 percent[40]. Trade facilitation allows for easier access to imports which result in cheaper intermediate goods and access to better technology, with spillovers into the wider economy. This in turn will also lead to lower prices for domestic consumers and job creation. In addition, simplified import, export and customs procedures benefit traders, but also improve government administration, revenue collection and controls, while contributing to an improved climate for inward investment.

## B. Overview of Border Management Performance

6.2 **Trade processes and procedures conducted by Lebanese border inspection agencies are complex and time-consuming.** This is confirmed by Lebanon's low ranking in the Trade Across Border (TAB) indicator of the latest Doing Business Report, in which Lebanon ranks 134$^{th}$ out of 190 countries worldwide and the World Bank's Logistics Performance Index (LPI) which ranks Lebanon 82$^{nd}$ out of 160 countries. Lebanon lags behind in all six categories of LPI when compared with the Middle East and North Africa (MENA) region's best performing country: The United Arab Emirates (UAE). The gap becomes very apparent when it comes to Customs performance and adequacy of infrastructure. Moreover, Lebanon's score in logistics competence is also low. The status of the Border agencies' performance in Lebanon was further confirmed by the Lebanese trading companies and logistics service providers. Cumbersome processes and procedures, requirements for submission of redundant documents, and excessive cargoes

[39] Yoshino 2008
[40] WTO, The WTO can ... stimulate economic growth and employment

inspections were identified as key operational inefficiencies. These inefficiencies lead to increased costs, and longer time to import and export, thus hurting the national trade sector. In some cases, unofficial payments were also required to speed the process.

6.3 **Private sector's negative perception of border agencies performance is concentrated to the Customs agency.** Operating more as a revenue collection rather than a trade facilitation entity, it hesitates to remove red tape, expressing a pronounced concern for security concerns given regional threats. Additionally, other key border functions i.e. those of the quarantine or standards agencies also lag both in terms of procedural simplification and application of automation. Lack of systematic coordination among the control agencies complicates the day-to-day business of Lebanese traders who spend disproportionate amounts of workhours to process their declaration packages.

## C. Economy-Wide Constraints

6.4 **Lebanon is not a contracting party to the Revised Kyoto Convention (RKC), under the World Customs Organization (WCO), therefore, it is not legally bound to comply with the WTO's Trade Facilitation Agreement (WTO –TFA)**. However, efforts to implement some trade facilitation reforms in line with the RKC have been made by all border agencies, yet these were sporadic and had limited impact.

6.5 **To improve border agencies performance, trade facilitation efforts should be focused on addressing economy wide constraints identified in three thematic areas:** simplified processes and procedures, inspection and risk management practices, and trade automation systems and interoperability.

**6.6 Simplified processes and procedures:** Processes and procedures are complex resulting in inefficiencies. Past initiatives – funded by the EU and the WCO - developed capacity building programs for the simplification and streamlining of import and export processes however the results were limited so far. A more results based operational approach is needed. The Lebanese customs office is currently drafting the new Customs Law with the help of the Italian Customs under an EU-funded Twinning project and will, allegedly, incorporate several procedural simplification measures into it.

**6.7 Inspection and risk management practices:** According to preliminary information collected from traders, more than 50% of imports and exports undergo inspections. This percentage is partially explained by the region's geopolitics and the high levels of security due to the ongoing Syrian conflict. Nonetheless, even if this factor is taken under consideration, current control levels are far behind the internationally accepted best practice of 5 percent. Quarantine, security and other border control agencies do not apply risk management in their operations. Their attention is focused on the development of specialized databases and on the procurement of equipment which will enhance the levels of control. To address this issue and save time on border entry points, Lebanon attempted to develop a Golden list program "Trusted Traders Program" that provide a faster processing service to companies that adhere to certain criteria set by the customs. Despite the fact that traders seem to be aware about it, there are only a few of them – if any- actively using it. There is appetite to review the performance of the existing program, identify determining factors for non-performance and take corrective measures to increase its utilization.

**6.8 Trade automation systems and interoperability:** The level of information technology used to handle trade processes and procedures, varies across cargo control agencies. On one hand, the Customs have already introduced their own Customs Information System (CIS) and have plans to further strengthen its efficiency via several automation and IT interconnectivity initiatives. On the other hand, there are other agencies- especially those under the Ministry of Agriculture (MoA) - which have not migrated to an automated system yet and still require all import and export documents and procedures to be processed manually. Looking at the totality of compliance, there is currently a complex nexus of manual and electronic processes which are not well aligned. Some initiatives to share information and data between the Customs and other agencies have been already been implemented, however, they have been applied in a sporadic manner without following an integrated approach. There are opportunities for developing a trade electronic single window (eSW) platform, based on international best practices, which aims at connecting all trade related agencies. Improving automation levels, will have a direct impact on the cost and time of trade and an ancillary effect on the government efforts to combat unofficial payments and delays at the borders.

## D. Recommendations

6.9 **To address these constraints and in order to improve border agencies performance at the national level and advance with trade facilitation reforms, the government will need to develop and adopt a new Customs Strategic Plan that supports the application of trade automation, including the development of a eSW, simplifies processes and procedures, strengthen risk management, and upgrades existing Trusted Traders Program.** The GoL has already embarked in a wider reform initiative being led by the Lebanese High Council for Customs (HCC), including: (i) the updating of the Customs Law and developing a new strategy to simplify customs procedures and modernize the risk management system; (ii) updating the existing ASYCUDA-based system to support e-payments; (iii) introducing "single window" systems at the Beirut port, the TSEZ, and other key border posts, allowing seamless integration of Customs, Health, and other relevant authorities; and (iv) introducing a full-fledged Authorized Economic Operator (AEO) Program, which will enable proven, low-risk traders to avoid overly-burdensome inspection procedures. However, progress with these initiatives will require the adoption of the Customs Strategic Plan under preparation, coordination with other key ministries and agencies, the approval of a new Customs Law to Parliament, and the articulation of a clear implementation plan. Piloting a number of those initiatives in the TSEZ with the possibility of subsequent scale-up at the national level could be an option for the government. Reform requirements at the TSEZ are fully aligned with the national level trade facilitation reforms. Below is one key recommendations for government's consideration.

# 6. Special Focus: Tripoli Special Economic Zone

***This section of the report focuses on the Tripoli Special Economic Zone (TSEZ), Lebanon's flagship economic development project. It establishes its economic viability and potential to attract private investors and create jobs, and details the prerequisites that are vital to the zone's success and attractiveness. These include implementing a good practice SEZ framework and adoption world class trade facilitation policies and measures. The section also highlights key considerations for the creation of a Knowledge and Innovation City in Tripoli and within the TSEZ framework.***

## A. Market and Feasibility Assessment

6.1 **In the context of wide-ranging constraints in the broader national investment climate, special economic zones (SEZs) can be an effective instrument to catalyze trade and investment.** With multiple binding constraints (including both infrastructure and regulation) to investment and a fragile political economy that makes it difficult to achieve robust national reforms, Lebanon represents an ideal environment in which SEZs might be effective: i) in the short term, to catalyze investment into an enclave with a high-quality business environment; and ii) in the longer term, to provide demonstration effects for the type of business environment that can be rolled out into the national economy. SEZs may also offer the potential to address both growth and macroeconomic vulnerability issues linked to weak industrial sector performance. To the degree that they attract new investments – particularly from foreign enterprises – that introduce new technologies to the domestic economy, industrial parks and SEZs support growth both through an accumulation of physical capital as well as an increase in productivity. Moreover, the shift in economic activity toward the more resilient industrial sector, will help establish a more diversified economy, enabling Lebanon to better absorb shocks. SEZs may also offer a strategy to mitigate macroeconomic vulnerabilities through raising net exports and increasing FDI.

6.2 **The Tripoli SEZ represents a flagship economic development project for Lebanon, and is at the heart of efforts to support job creation in one of the country's most lagging regions.** The GoL established its first type of SEZ – the Logistics Free Zone - at the Port of Beirut in 2007. This zone operates under the 'free economic zones' model, which aims to attract foreign and domestic investment in trade-related activities, including transport, transit, and logistics. In 2008, the government passed a law for the establishment of the Tripoli Special Economic Zone (TSEZ), to be established on a 55-hectare site adjacent to the Port of Tripoli. This SEZ is expected to go beyond the trading and logistics role of the Logistics Free Zone in Beirut and develop an industrial park to attract foreign and domestic investments on manufacturing and related activities. It is also intended to play a significant role in stimulating job creation in the regional economy through both labor market and supply chain linkages. After a delay, the GoL appointed a board and established and funded the TSEZ Authority (TSEZA) in 2016 and the project is moving quickly, with the expectation of having investors operating in the zone by 2021.

6.3 **Yet, its success in attracting investments and creating jobs is dependent on the implementation of a good practice SEZ framework.** This involves creating an enabling business environment and resolving current bottlenecks in the ease of doing business in Lebanon, including burdensome business formation and licensing processes; complex and time-consuming trade

processes and procedures; and prohibitive costs and limited availability of serviced land, facilities, and utilities. Addressing the above-noted constraints is a pre-condition for TSEZ to realize its full potential for investment and enhance its regional competitiveness as an attractive business location.

6.4 **Two feasibility studies have confirmed the market and employment creation potential of the TSEZ, and established its economic viability and potential to attract private investors.** An initial pre-feasibility study, carried out in 2010 through support from USAID, concluded that the site was commercially viable. This was confirmed in a recent market assessment and pre-feasibility study carried out in 2017-18 by the WBG.

6.5 **According to a market analysis undertaken by WBG, particular sectors for which the TSEZ would be a particular useful setting and which may derive extra benefit from the special conditions in the zone include Chemical Products, Food Products and Beverages, Metal Products, Rubber and Plastic Products, Electrical Machinery and Apparatus, Pulp, Paper and Paper Products, and Logistics and Warehousing.** The analysis suggests that these high potential industry sectors are the most suitable for the TSEZ and are likely to drive demand for serviced land at the zone, based on key sector performance parameters such as sector exports, sector exports as a proportion of output, sector labor intensity, sector value added, size of establishments[41], and revealed demand from investor interviews and surveys. Logistics and warehousing in the only non-manufacturing sector, however evidence shows that better logistics performance is strongly associated with trade expansion, export diversification, ability to attract foreign direct investments[42]. The TSEZ should be pro-active in targeting promotion efforts at these sectors. Most of these sectors have already revealed potential demand for plots in the TSEZ. However, the TSEZ should not refuse investment applications outside these sectors, if the investment meets the environmental and social safeguards standards set by the TSEZ.

6.6 **To be successful in attracting investors, TSEZ should be particularly competitive in in terms of operating costs.** A comparative benchmarking between Lebanon and the TSEZ with special economic zones and free zones in the region, in terms of production factor costs, uncovers exiting weaknesses that should be addressed to realize new investments and job creation under the TSEZ regime. Foreign investors seeking to establish a production or logistics facility will compare the TSEZ with alternative locations in the nearby region and around the Gulf. All benchmarked zones offer serviced infrastructure. They provide fully equipped industrial estates comprising roads, power, water, sewer and telecommunications connections, and leveled land or pre-fabricated buildings, inclusive of maintenance, utility and security services. Below is the summary of the benchmarking exercise.

- **Land prices**. The cost of land for industrial use is very high in Lebanon compared to the benchmarked economic zones. The TSEZ, however, could consider adopting lower rates that those that are charged in other formal industrial estates in Lebanon.
- **Electricity prices and supply**. The electricity rates are broadly in line with those in Turkey

[41] Typically, an SEZ is specifically designed for larger enterprises which for the purposes of the analysis is determined to be enterprises employing more than 49 workers. The market analysis study determined that sectors with less than 10 enterprises employing more than 49 workers would not qualify for targeting by the TSEZ.
[42] World Bank's 2010 Logistics Performance Index and Its Indicators report

and UAE, although substantially higher than in Saudi Arabia where power is heavily subsidized. Electricity in Lebanon is also heavily subsidized. The fiscal sustainability of these subsidies is a question mark. If the subsidies are stopped, tariffs may to be doubled and will be substantially higher than those seen in the benchmarked zones. Moreover, supply of electricity is insufficient and many consumers resort to own generators or to private generators. While TSEZ is able to ensure electricity supply at competitive prices using its own generation, this would not be sufficient to make the zone attractive for energy-intensive sectors such as aluminum smelting and other basic metal and chemical production.

- **Labor costs and supply**. Lebanon has an overall highly educated, but also relatively expensive workforce. International investors looking for low labor costs have other alternatives in the region (Egypt, Jordan). To be attractive, the TSEZ must aim for sectors that can make use of Lebanon's educated and versatile workforce.
- **Transport accessibility**. TSEZ can boast direct access to a well-equipped container terminal, which is essential for an export-oriented zone. At the moment, the frequency and number of connections is much lower than in some other benchmarked zones, (like the zones in the UAE, but also Port Said and Aqaba). The attractiveness of TSEZ for international investors will be co-determined by the success of the terminal operator in expanding its business.
- **Attractiveness of incentives**. The TSEZ incentive package - both financial and non-financial - is important and in line with the international practice. It plays a key role in the attraction of inward investment to Tripoli. However other matters including international location (logistics), internal market size, natural competitive advantages, availability of specialist skills, proactive commitment of government, and professionalism of the TSEZ Authority and IDAL staff will also play important roles in the attraction of investment to the Tripoli Special Economic Zone.

6.7 **Assuming the TSEZ adopts a good practice SEZ framework, it is estimated that the zone will be filled in around 10 years and 3000 direct jobs will be created (base estimate).** The results are in line with the international experience in the growth of specific SEZs across the globe. Demand forecasts suggest that under a cautious scenario it will take 20 years to fill the zone which is typical of many existing zones; the base estimate will take just over 10 years and the optimistic scenario just over 5 years. Job creation forecasts suggest that between 3000 (base estimate) to 5000 (optimistic estimate) direct jobs will be created after 5 years of operation. Both direct and indirect job creation will result as a consequence of TSEZ investment and development in Lebanon, generating residential demand for dwelling units (DUs) in a variety of housing configurations (*e.g.*, workforce incremental housing units/apartments, row houses, and villas). Assuming the optimist scenario is realized and estimating a conservative 1.5 multiplier for the indirect jobs, it is estimated that in year 5 the TSEZ can create more than 7500 direct and indirect jobs, and more than 30,000 direct and indirect jobs in 20 years. The results of the site-level demand and jobs projections appear in **Error! Reference source not found.** and **Error! Reference source no t found.**.

Table 1: Cumulative TSEZ Demand Forecasts Across Time

| TIME PERIOD | Cumulative TSEZ Demand Forecasts (Hectares) |
|---|---|

| (Years) | Optimistic Estimate | Base Estimate | Cautious Estimate |
|---|---|---|---|
| **1** | 10 | 10 | 5 |
| **2** | 15 | 10 | 5 |
| **5** | 30 | 20 | 10 |
| **10** | 40 | 30 | 15 |
| **20** | 175 | 100 | 35 |

Source: WB estimates

Table 2: TSEZ Direct Job Forecasts

| TIME PERIOD (Years) | TSEZ Direct Jobs Forecasts (Jobs) | | |
|---|---|---|---|
| | Optimistic Estimate | Base Estimate | Cautious Estimate |
| **1** | 3000 | 1750 | 750 |
| **2** | 3500 | 2000 | 750 |
| **5** | 5000 | 3000 | 1000 |
| **10** | 6000 | 3750 | 1250 |
| **20** | 19250 | 9750 | 2500 |

Source: WB estimates

*PPP Options for TSEZ*

6.8 **The Zone could be totally developed by a Private Sector Developer, however, given the perceived high risk of international investors for Lebanon this is not very likely to happen.** A private developer could expect to borrow 70 percent of the total cost of some USD 270 and earn an IRR of approximately 20 percent. However, there exist a very real possibility that experienced international developers would find the project too risky, given international investors apparent very high perceived level of risk inherent in investments in Lebanon in general and Tripoli specifically as demonstrated in an international survey undertaken by the Study.

6.9 **To lower the perceived level of risk it is recommended that the zone be developed and managed as a variation on a DBFMO[43] PPP.** Given the circumstances it is recommended that **the TSEZA forms the Tripoli SEZ Development Corporation (TSEZDC) as a wholly owned subsidiary of the TSEZA with an independent board and which enters into a concession agreement with a private sector partner.** The TSEZDC would build a Chinese Wall between the TSEZA primary role as the regulatory of the TSEZ and its responsibility for developing and operating the TSEZ. The TSEZA would develop the site to fully serviced plots and then lease the site to a Private Sector Partner who would construct Factory Buildings as required by tenants and

[43] Design, Build, Finance, Maintain and Operate

lease both buildings and serviced plots at market rates and promote, manage and administer the site. The government lease rate to the Private Sector Manager would be established by tender for the concession. Under such an PPP concession the Private Sector Partner would not have to carry any of the inherent risk attached to the initial site development and provided the Government lease rates are appropriate both parties could expect to make satisfactory profits: the Government largely because of its ability to borrow at below market rates and the Site Manager because of the opportunity offered by the PPP to lease the site from the GOL at below market rates

6.10 **This scenario directly addresses the issue of perceived security risks by appropriately apportioning risk and reward to the appropriate agents**. The TSEZA accepts the initial risk of financing and developing the zone through its subsidiary the TSEZDC. The Private Sector Partner leases the site from the TSEZDC and accepts responsibility for the management, maintenance and operation of the zone and in doing so does not immediately place its own equity at risk. The Private Sector Partner can immediately earn income from serviced plots; an income which requires no significant investment and from the Administration Building which while requiring an initial investment by the Private Sector Partner guarantees immediate income from TSEZA. Further, Private Sector Partner can delay investments in the construction of SFBs until it has a clear expectation that tenants will lease such facilities in the very near term. Thus, such an agreement would provide the TSEZA with an experienced international partner and minimize both the risk and the cost of the partner's investments.

6.11 **Finally, to increase early incomes the Private Sector Partner could consider selling user rights to serviced plots and SFBs for an upfront, one off discounted payment**[44]. A possible price for a 30-year lease would be the Net Present Value of the stream of future lease payments discounted by the developer's weighted average cost of capital. It would not be necessary to make serviced plots available only through such a purchase of 30-year use rights but rather to offer it as an option.

6.12 **The TSEZDC as Master Developer can expect an IRR of 9% - entirely satisfactory for a public investment - against an investment of USD 10 Million with a Payback Period of 11 years fueled by USD 6.75 per sq. meter lease payment from the Private Sector Partner for the serviced plots.** Given that the IRR of 9% exceeds the WACC for the proposed TSEZDC of 7.3%, the Net Present Value (NPV) of the Cash Flow is positive and hence the investment would be justified.

6.13 **Further the Private Sector, for an equity investment of USD 70 Million over 8 years to construct SFBs and an Administration Building would expect an IRR of 20 per cent and a Payback Period of 6 years.** As the Private Sector Partner would be in full possession of a fully developed site, facing a stream of investments driven only by demand from tenants and not dependent on any Government payments for viability, this would be an attractive option to global developers. Finally, it would be politically very attractive as it promises positive returns to both parties to the PPP concession – the Government and the Private Sector Partner.

[44] This is not a new proposal. A number of zones around the world sell use rights for a defined period for an upfront payment e.g. Tan Thuan Export Processing Zone, the oldest EPZ in Vietnam, sells a 50 year lease for a serviced plot for an upfront payment of USD 108 / square meter.

## B. Trade Facilitation in the Context of the TSEZ

6.14 **While implementing nation-wide reforms is necessary and timely, using the Tripoli Special Economic Zone (TSEZ) as a model for the initial application of reforms, with a possibility of scaling-up at a national level, is an excellent starting point.** So far, the economic zone is not yet developed, however the authority in collaboration with different partners is in the process of preparing and finalizing a Master plan and a licensing regime. At this stage, it is critical and timely to integrate international best practice trade facilitation reforms to the master plan and zone regime to ensure having the enabling system for the implementation of simplified processes and integrated risk management that are attractive for investors.

6.15 **In fact, many countries use Special Economic Zones as vehicles to test and improve trade facilitation and border management modernization policies prior to their application at a national level**. The rationale behind this approach is based on the fact that a typical SEZ - being geographically and procedurally confined- constitutes an ideal low-risk environment, conducive for the implementation of small-scale programs. The TSEZ, which is adjacent to the Port of Tripoli could be ideal for this purpose.

6.16 **Moreover, how quickly and predictably goods are cleared across borders within the TSEZ is vital for attracting investments, particularly foreign investments.** For the TSEZ to meet its target of 50 to 70 tenant companies and employ around 3,000 people, it will need to have, among other things, efficient trade measures in line with best practices especially in terms of the complexity of processes and procedures, inspection and risk management practices, and Information Technology (automation). For this to happen, several steps on the regulatory, institutional and operational levels need to be implemented.

### a. Simplification of Processes & Procedures

6.17 **Simplification of processes and procedures have been recognized as a priority reform on a national and regional levels, particularly at the TSEZ.** In the context of the TSEZ, focus should be placed on specific customs procedures including the description and standards for Temporary Storage of Goods, Outright Exportation, Duty Free Zones, Customs Transit, Inwards Processing, Outwards Processing, Temporary Admission and other specific procedures.

6.18 **In comparison to the RKC, there are gaps in the provisions and requirements of the existing legal framework for the Customs and the TSEZ**. Specifically, five custom procedures require further consideration to reflect best practice.

- **Free Zones:** It is currently unclear whether domestic goods could be sold to the TSEZ and whether goods within the zone can be imported into the Lebanese customs territory. According to the provisions of the RKC the sale of domestic goods to economic operators within the TSEZ and the sale of TSEZ goods into the Lebanese economy should use standard import procedures.

- **Outright Exportation**: In comparison to the related article in the RKC, the current process for exporting goods can be further simplified. The regulatory procedures are still to be developed however the process will be impacted by the development at Port of Tripoli.
- **Customs Transit**: There is a need to take into consideration within the regulatory framework the national movement of goods imported into Lebanon at another point of entry, such as goods imported through Beirut International Airport for transport to the TSEZ
- **Temporary Admission:** The temporary admission procedure allows goods to be imported for a limited period of time (six months, one year, *etc*.) for defined purposes without the payment of import duties and tax. The *draft* master plan for Port of Tripoli includes the development of a dry dock for the repair of vessels, however the dry dock is outside the TSEZ. It is possible to source parts from within the TSEZ to repair the vessels, however, it is unclear whether they can benefit from a temporary admission.
- **Inward Processing:** There are small or medium operators in Tripoli who import raw material and export them as finished good after value added processing. It is unlikely all will seek to relocate to the TSEZ and depending on their actual operations it may be useful for Customs to make available the customs procedure for Inward Processing. The RKC describes Inward Processing as it 'provides for conditional relief from import duties and taxes for goods that are to be exported after having undergone specified manufacturing, processing or repair[45].

6.19 **Trade procedures related to flow of goods in and out of the zone need to be further defined in the legal and regulatory framework.** The current legal and regulatory framework which governs the TSEZ's trade procedures include provisions that dictate the relationship between the TSEZ and the Customs authority only, with no reference to the rest of the border inspection agencies, for instance quarantine or standards authorities. In addition, some key secondary legislation are missing and need to be issued. These include (i) the definition of the control and leakage prevention methods and tools, (ii) definition of the procedures for entry, exit, receipt, delivery, sorting, storing, maintenance and transport of goods from one place to another, (iii) establishment of Customs Office at the entrance of the zone territory, (iv) customs office staff and modus operandi, (v) simplification of Customs procedures in special entry, temporary entry, temporary export, transit and import regimes for local consumption and (vi) development of Entry/Exit registry templates.

6.20 **Moreover, the TSEZ Authority needs to ensure that the infrastructural design of the zone facilitates the inflow and outflow of goods.** The Port of Tripoli is undertaking a major expansion with a new container terminal to be operated by a new container terminal operator. The TSEZ will be developed adjacent to the new container terminal. The Port, with advice from the TSEZ Authority, plans to have one gate for the entry and exit of cargo and trucks and is considering a second entrance for vehicle traffic. However, there does not appear to be an integrated border inspection facility in the port's master plan. In summary, there is a need for installing container weighbridges to facilitate export trade, enhance security via modern Closed Circuit Video Surveillance (CCVS) systems, procurement of fixed scanners and ramps, and the installation of sophisticated gate automated system both at the port and at the SEZ territory.

[45] IPCSA Simple, efficient solutions for swift and smooth supply chains: How to develop a Port Security System

6.21 **As such, a thorough review of the existing masterplan needs to be undertaken, in coordination with the regulatory agencies and the TSEZ Authority.** The objective is to confirm regulatory agency requirements including the place/places for inspection, re-engineer the process to open-up gates, fit scanners and other trade compliance equipment and re-engineer the process to create an express lane for TSEZ cargo. Moreover, it is recommended that a full-fetched procedural mapping assessment is conducted in order to identify bottlenecks in the trade process at the port.

### b. Inspection and Risk Management Practices:

6.22 **Inherent in free or special economic zones operations is a wide range of risks for all trade related regulatory agencies.** Risks include: revenue leakage (for Customs), the use of the zone territory for the movement of illegal goods (for all regulatory agencies), the risk that trade within the zone is a pathway for the entry of harmful pest and disease (MOA and Ministry of Health) and the cross contamination of export agri-food product resulting in the refusal of entry at the destination market (MOA and Standards).

**6.23 In order to reduce border risks, the TSEZ can consider the below initiatives:**

- Authorized Economic Operator under the WCO SAFE Framework of Standards to manage security risk and Authorized Operator with appropriate facilitation benefits applied to the authorized operator;
- Border Agency Partnership arrangement to raise awareness for personnel within TSEZ on harmful pest and diseases, reporting unusual bugs to MOA, voluntary disclosure of undeclared goods and illegal goods within any consignment;
- The establishment of a TSEZ Risk Management Committee;
- Priority access to technical advice on matters relating to import and export including a one-stop-shop for information;
- Disaster recovery and business continuity in times of disruption including response plans for failures associated with dangerous goods, presence of a harmful pest or disease, failure of TSEZ or regulator agency systems.

6.24 **Sanitary and phytosanitary control is also important for the zone.** Some goods entering the zone might have higher risks than others, such as animal and plant imports that could carry different pests and diseases. A control mechanism should be in place to prevent the spreading of such infiltrations into the country.

6.25 **There are a few unexplored areas mainly related to the current levels of compliance with standards (sanitary, phytosanitary, health and other standards) for TSEZ and TSEZ operators that need to be determined once the target-sectors for the TSEZ are confirmed.** Under RKC, customs can implement general authorizations for the movement of goods from the Port of Tripoli to the TSEZ without requiring prior authorization for each consignment. However, it is important to identify how will this procedure impact MOA's management of plant and animal risk, and what are the challenges for MOA with general authorizations.

6.26 **Access to treatment facilities – fumigation, heat or other treatment – should be defined and managed appropriately since the service provider will be outside the TSEZ**. According to the plant and animal quarantine, they have legal jurisdiction in free zones. However, the plant quarantine law is itself silent regarding free zones. Furthermore, according to the law establishing the Tripoli Economic Zone, the Authority may be exempt from complying with national legislation which therefore could include plant and animal quarantine laws. However, since Lebanon is a member of the IPPC[46], the MOA as the recognized competent Authority will be the issuing authority for phytosanitary, sanitary and health certificates to goods produced within the TSEZ. Therefore, the following actions are suggested:

- Conduct an assessment of TSEZ trade identifying the specific sanitary and phytosanitary (SPS) risks presented by the trade and activities within the TSEZ;
- MOA to undertake an evaluation of the SPS market access requirements for exports originating from the TSEZ as a resource for TSEZ operators;
- Develop, implement and review MOA surveillance and incursion readiness and response procedures and protocols in coordination with the TSEZ Authority and operators within the TSEZ

### c. Trade Automation Systems and Interoperability

6.27 **Interoperable IT systems support both the simplification of procedures and effective border risk management and reduce time, cost and risk.** The ultimate goal is to develop the enabling environment for paperless processes that will reduce the time and cost to all participants and ensure transparency and data collection which will reduce risk significantly[47]. This process requires a coordination between the TSEZ, and each of the Port, the customs, and the other relevant ministries (Health, Economy and Trade, and Agriculture).

6.28 **The TSEZ is an ideal environment to pilot, review and amend interconnectivity of information systems and identify critical success elements for future national reforms.** Therefore, it is suggested that a detailed evaluation exercise is conducted in order to assess interconnectivity of information systems (e.g. port community system[48], port centric Electronic Data Interface (EDI) system or a form of e-SW) that links the port, TSEZ, transporters, traders and related the regulatory agencies. However, the development of a port community system (PCS) or similar port centric coordination and information sharing platform should be considered on the basis of cost-benefit analysis and should fit into the IT strategies of the various port stakeholders. Nonetheless, there are many advantages for piloting a PCS in the port of Tripoli under controlled operational environment and then scale it up as a nation-wide initiative.

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[46] International Plant Protection Convention of which the recommended practice for phytosanitary measures for imports says: "For the purpose of this standard, import is considered to cover all consignments moving into the country (except in transit), including movement into free trade zones (including duty free areas and consignments in bond) and illegal consignments detained by other services.

[46] ISPM 20 Guidelines for Phytosanitary import regulatory system https://www.ippc.int/static/media/files/publication/en/2017/06/ISPM_20_2017_En_2017-06-26.pdf

As advised by the Port of Tripoli manager

ng the average time to import and export of manual processes, combination of manual and electronic and paperless shows a reduction in time for paperless

[48] *IPCSA Simple, efficient solutions for swift and smooth supply chains: How to develop a Port Security System*, IPCSA http://www.ipcsa.international/armoury/resources/ipcsa-guide-english-2015.pdf

6.29 **In order to reduce border risk the TSEZ will need to invest in an automated gated system that records cargo movements in and out of the zone.** The current port expansion master plan envisages a 'smart-port' with high use of technology. This is planned to be materialized through the development of a port information system[49] as well as a new port management system that fits with the future strategy of being a 'technology-enabled' port. The adoption of new technology at the Port will lead to a change in the volume and categories of goods moved through the port and therefore increase border risk. The installation of gated automated systems with the latest license plate reading technology and the use of GPS to track container movements are some of the options to be considered by the TSEZ and the Tripoli Port.

### C. Preferential Trade Agreements and TSEZ

**6.30 While overcoming non-tariff trade barriers that hinder trade in the wider economy and adopting efficient and streamlined trade processes and procedures are key for the success of the TSEZ, ensuring that goods produced in the zone are considered originating from Lebanon and benefit from the preferential access offered under the GAFTA and EU trade agreements is very useful.**

6.31 **Lebanon has traditionally been a country with a free and open trade regime.** Efforts towards trade liberalization were focused on Europe and the Arab world. Lebanon signed Regional Trade Agreements with the European Union – Association Agreement (AA), with Switzerland, Lichtenstein, Norway and Iceland - European Free Trade Agreement (EFTA), and is a member of the Greater Arab Free Trade Area (GAFTA) which includes 17 Arab countries. Under these agreements, most imports and exports benefit from tariff-free market access conditional on compliance with the specific Rules of Origin (RoO) under each[50].

6.32 **Preferential Trade Agreements (PTAs) do not guarantee preferential treatment in special economic zones (SEZs).** In fact, many preferential Trade Agreements exclude SEZ processed products from their preferential treatment or establish special stringent conditions relating to the Rules of Origin, to limit trade triangulation and to safeguard the competitiveness of local producers among other reasons. In the same context, an issue arises when assessing the eligibility of goods produced in the TSEZ, to benefit from the same tariff-free market under the GAFTA and the AA.

6.33 **In the case of GAFTA, the agreement does not include any provisions on free zones or special economic zones operating in member countries.** It only specifies that a product is considered originating if it was wholly produced or obtained in a GAFTA country or if 40 percent of its value added is accrued in a GAFTA country. Thus, in principle MFN tariffs should apply to exports from SEZs in GAFTA countries to other GAFTA countries. Yet, it is worth noting that GAFTA countries exhibit relatively low MFN tariffs ranging from 5 percent to percent at a maximum (see **Error! Reference source not found.**).

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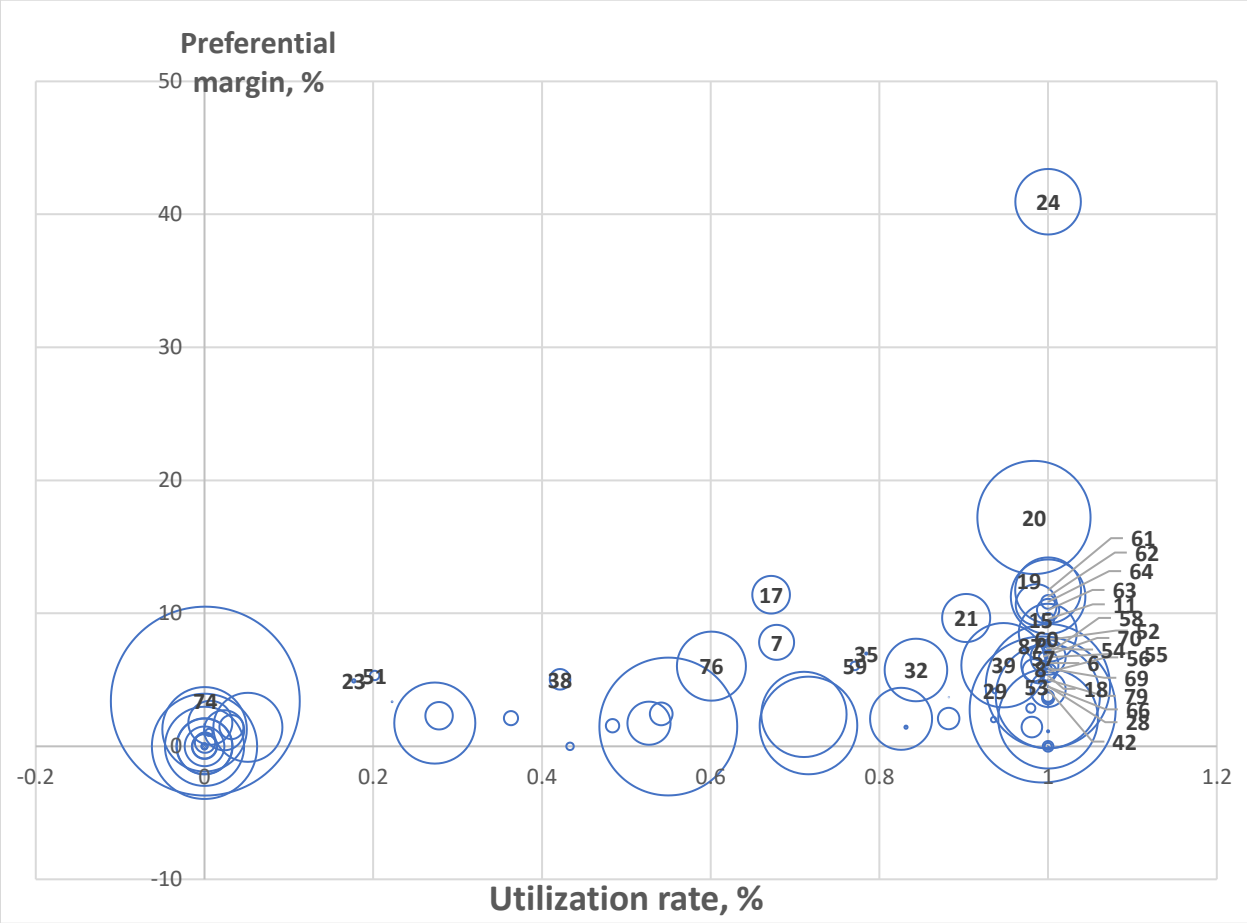
[49] Funding has already been secured from the Islamic Development Bank (IDB).

[50] Rules of Origin (RoO) are the set of criteria a product being processed or produced in a preferential trade agreement member country must undergo to be recognized as originating in the country and benefit from preferential access.

6.34 **In the case of the EU AA, treatment of zone produced goods is not explicit**. Article 35 of the EU AA states, "when products originating in the Community or in Lebanon are imported into a free zone under cover of a proof of origin and undergo treatment or processing, the authorities concerned shall issue a new movement certificate EUR.1 or EUR-MED at the exporter's request, if the treatment or processing undergone complies with the provisions of this Protocol". First, the text implies that a product or input produced/processed in a Free Zone (FZ) must already be compliant with RoO to be considered originating in Lebanon. In addition, any subsequent transformation taking place in the FZ would also need to comply with specifics laid out in the agreement. Nothing is said about producing a good from non-originating inputs. Second, the text does not mention Industrial Parks or SEZs. Also, worth noting, that the overall utilization of EU preferences in Lebanese exports ranged between 42 percent and 58 percent in the last years (See Figure 6**Error! Reference source not found.**). A possible explanation for the suboptimal share of Lebanese exports entering the EU under preferential treatment could be the complexity of the RoO.

Figure 6: Utilization of preferences against preferential margin by HS sector, 2015




Source: Staff estimates using data from EUROSTAT

## D. Knowledge and Innovation City (KIC)

6.35 **To support job creation and entrepreneurship in Tripoli, the GoL is exploring the possibility of the creation of a Knowledge and Innovation City (KIC) based at the Rashid Karami fairground in Tripoli, as part of the establishment of the Tripoli Special Economic Zone (TSEZ)[51].** Innovation hubs, incubators and accelerators can contribute to job creation, level the playing field between those with advanced degrees and those without university degrees, and help people with more basic skills in lower income communities connect to better jobs.

*Challenges in the entrepreneurial ecosystem*

6.36 **In the past few years, the GoL has taken significant steps to support entrepreneurship and start-up creation in the country.** In Beirut alone, the World Bank found that, each year, an average of 12 more start-ups are created than in the previous year, resulting in a 24 percent compound growth rate in startup creation since 2009. About two-thirds of the start-ups surveyed by the World Bank in Beirut reported hiring at least one employee, with a median of three jobs per startup, which were primarily early stage. This is characteristic of an entrepreneurial ecosystem that has passed its nascent growth stage but is far from maturing, and suggests a need for the further development of start-ups and the broader entrepreneurial ecosystem to also help maximize the potential for job creation.

**6.37 Research and surveys conducted by the World Bank[52] and by InfoPro and City Trends Consult, commissioned by the TSEZ, identified the following, high-level challenges in the entrepreneurial ecosystem in Lebanon.**

- Low knowledge-based economic activities and the relatively small size of the ICT sector, paired with low commercialization of innovation and patenting compared to peer countries.
- Low degree of collaboration between universities and industry, which affects both research and development initiatives as well as university students' skills development. A further challenge is the insufficient exposure of fresh graduates to industry practices and the lack of relevant professional and technical skills.
- Significant brain drain whereby young graduates are leaving the country to find employment or entrepreneurial opportunities elsewhere.
- Challenging business environment, including processes to create new businesses as well as regulatory challenges that result in low-speed internet and lagging infrastructure.
- Accelerator programs do not seem to provide enough quality training for entrepreneurs to be sustainable and quality mentors are scarce, with few instances of angel investors.
- The innovation community is still in its early stage and clusters do not connect easily with each other, suggesting a silo approach among ventures from different networks.
- Obstacles for seed stage funding and exit: compared to other early and middle stage ecosystems (such as in Tanzania and Palestine), despite abundant funding thanks to Circular 331, processes in Lebanon for start-ups are lengthier for credit and funding (compared with Palestine), suggesting more difficulties (linked to procedures or access to finance requirements) in obtaining funding for start-ups.

[51] In 2018, the COM approved the expansion of the mandate of the TSEZ to Rachid Karami Fair.
[52] Beirut Tech Startup Ecosystem Report, World Bank, 2017.

**6.38 In the context of Tripoli, these challenges are arguably even more acute, paired with additional socioeconomic challenges, such as the high youth unemployment rate, poverty, low economic activity with lagging, traditional industries, and increased security risks brought on by the Syrian conflict.** Entrepreneurship is nascent and limited in Tripoli, with much of the start-up ecosystem concentrated in Beirut.

6.39 **However, the Tripoli area offers opportunities to stimulate economic activity and innovation and access to the TSEZ incentives could be encouraging for new businesses.** Tripoli is the country's second biggest city, about 80 kilometers from Beirut, requiring a relatively short drive depending on the capitol's traffic, however the cost of labor and living are much lower. It is home to a number of universities including Balamand University, one of the top universities in the country, offering a potential pipeline of skilled talent most of whom currently move to Beirut or elsewhere abroad after graduation. The diaspora from the Tripoli area, whether they are successful members of the start-up ecosystem based out of Beirut, or abroad, offer a further potential opportunity to catalyze interventions to expand and enhance the start-up and innovation ecosystem in the Tripoli area. Moreover, the inclusion of Tripoli's in the India Middle East Western Europe Fiber Optic Submarine Cable System allowing the city to deliver high speed internet capacities at low cost is highly attractive for digital startups. In addition, TSEZ's incentives including the ease of administrative procedures, economic and tax incentives, and flexible labor regulations are very appealing to entrepreneurs.

*Business models and key innovation factors*

6.40 **Innovation facilities also have different management options and business models depending on the driving factors for their creation and the need for profitability**. The different options vary based on the mission, drivers and business model for the innovation entity. Innovation hubs can be community driven, real estate driven, private or government driven. Founders have different expectations for the facilities depending on their orientation. Foundations and government agencies primarily expect development and economic impacts rather than direct financial reward. Investment funds and real estate firms tend to expect equity in start-ups and rental income from the property. Table *3* presents examples of successful global innovation hubs which have different approaches to sustainability and profitability, and whose business model may be applicable for the KIC.

6.41 **A high-level demand assessment conducted by InfoPro and City Trends Consulting in Lebanon found that 63 percent of companies surveyed had an interest to relocate to a future KIC in Tripoli and pay office rental fees**. However, they would need not only access to the infrastructure of the SEZ, such as low-cost and reliable Internet, but access to talent and other amenity which could require upfront investment from the KIC and the city. Furthermore, given the nascent start-up ecosystem and the poverty-stricken context of Tripoli, if the KIC wishes to benefit the local economy, it will may need to consider offering programs that directly impact the local community beyond just hosting new companies in the area. This may require a mixed business model whereby it subsidizes certain activities oriented towards local development through membership or office rental fees or through government subsidies, and explore the possibility to graduate to a for-profit model over time.

Table 3: Examples of innovation hubs around the world

| | iHub (Nairobi, Kenya) | DUMBO Incubator (New York, United States) | In5 (Dubai, United Arab Emirates) |
|---|---|---|---|
| **Profit/non-profit** | Originally non-profit, then transformed into for profit | Mixed | Non-profit |
| **Drivers** | Community-driven | Real estate- driven | Government-driven |
| **Founders** | Omidyar Network[53] and Hivos (foundations) | New York City Economic Development Corporation (NYCEDC), New York University (NYU), and Two Trees Management Co. (a real estate firm) | Dubai Internet City (DIC) |
| **Management** | Originally Ushahidi (non-profit software company), but since its founding it has included equity investors | NYU & Two Trees | DIC |
| **Business model** | The founders originally did not expect a financial return but rather social impact. Ushahidi generated some revenue from operation of the space but it was not its sole source of income. Four of their six initiatives were profit-oriented and they put 20% of their profits back into the co-working space. In 2016, iHub amended its strategy and secured private investment. | NYCEDC does not expect a financial return but rather economic impact for the city. NYU also does not expect financial return but rather linkages with the university. NYU will accept equity in exchange for space rental. The real estate company earns revenue. | The founder does not expect a financial return but rather economic impact. The real estate company earns revenue from rentals. |
| **Other supporters** | Google[54] provided funding for the UX Lab and Cluster. Corporate partners include Intel, | | |

[53] Press Release, 2009, "Omidyar Network Commits $1.4M to Ushahidi to Broaden Crowdsourcing Platform's Impact," December 2. https://www.omidyar.com/news/omidyar-network-commits-14m-ushahidi-broaden-crowdsourcing-platform%E2%80%99s-impact.
[54] http://www.itnewsafrica.com/2012/04/kenyas-ihub-gets-google-funding/.

| | | | |
|---|---|---|---|
| | Microsoft,[55] Samsung, and Nokia. InfoDev at the World Bank supported the m:lab through a grant. Currently, they also have other private investors. | | |

Reference: World Bank

6.42 **In terms of offering from an innovation facility, most facilities include the following elements include:** (i) amenities such as good transport and minimal business complication; (ii) the potential market for the start-up's services as well to supply talent; (iii) relevant and inexpensive space to work; (iv) availability of funding; (v) networking opportunities; and (vi) support services such as lawyers, accountants, advertising agencies, mentors and Internet access. The KIC would need to take into account how to ensure the appropriate supply of these elements especially as its activities and reach scale. Box 3 includes high level implementation steps for the KIC.

**Box 3: Implementation Steps for KIC**

Recommendations for high-level steps to establish the KIC are presented below, including key decisions on the mission, model, and management of the facility.

1. Continue to assess demand, and review models for sustainability.
2. Conduct a SWOT analysis for the KIC in Tripoli.
3. Carry out a cocreation exercise with key stakeholders to validate vision and programs, and develop mandate and model.
4. Based on the agreed mission and prior analysis, develop the model for the KIC.
5. Finalize funding plan and secure financing.
6. Establish the KIC legally, including any legal agreements needed between the TSEZ and the KIC, and the KIC and the board.
7. Hire the KIC executive director and finalize operationalization, organizational key performance indicators (KPIs) and annual budget.
8. Commission design and architecture services to configure the KIC based on the vision, model, and programs.
9. Finalize programs, staffing, and secure key partnerships for the activities.
10. Start hosting first tenants, kickoff networking, and pilot programs.

## E. Recommendations

Below is set of recommendations on how to move forward with a good practice framework, how to proceed with trade facilitation in the TSEZ, and considerations for the creation of a KIC in Tripoli as part of the TSEZ, with the objectives of boosting innovation and entrepreneurship for increased employment and productivity.

### 6.43 Implement a good practice TSEZ framework

[55] http://news.microsoft.com/2013/03/20/microsoft-unveils-strategic-cooperation-with-ihub-and-mlab-to-accelerate-innovation-in-east-africa/.

The implementation of a good practice framework is a precondition for the success of the zone. Addressing investment constraints and bottlenecks at the legal, regulatory and institutional level would enhance TSEZ's regional competitiveness as a business location and spur investment. As such, it is recommended for TSEZ to move forward with the following next steps:

- Develop the value proposition of the TSEZ.
- Develop TSEZ Implementation Strategy and Business Case.
- Present the designed Master Concept Plan and Business Case to potential private developers for initial reaction.
- Provide for an onsite/offsite Independent Power Producer. Design incentive scheme to operate solar rooftops on leased factory warehouses. Encourage energy efficiency in tenant firms. Include energy efficiency requirements in developer/operator agreements.
- Work with Customs to develop streamlined procedures in line with customs law.
- Ensure immediate/eventual private sector operation of TSEZ with TSEZ Authority as regulatory body only.
- Develop arrangements with qualified private sector technical training institutes in order to help tenant firms. This can be done prior to operation of TSEZ through coordination with potential anchor investors.
- Adopt a unified Regulatory Framework, including expedited process for business set-up/licensing for SEZ developers/operators and tenants (i.e., de facto "Account Executive" "one-stop" model)
- Consider offering regionally competitive lease rates initially to attract good, large anchor tenants. These possible low lease rates will rise over time as the TSEZ value proposition is tested in the market and TSEZ becomes more attractive higher-value industries.

*Trade facilitation*

6.44 **Strengthen the TSEZ legal and regulatory framework for simplified procedures**

Even though the envisioned SEZ is outside the Customs territory, regulations and procedures which define the seamless inflows of inputs and outflows of final goods must be developed in the form of decrees and decisions. The Customs authority has the technical capacity to assist the TSEZ authority to develop these legislative pieces. In practice, these should be developed in close coordination with the rest of the port stakeholders.

**6.45 Enhance coordination between the different border management bodies for broader integrated risk management**

In order to strengthen the coordination between the TSEZ Authority, the Customs and the Port of Tripoli and to facilitate the quick undertaking of a number of joint reform actions, it is recommended to establish Tripoli Trade Facilitation Working Group (TFWG) that will include representatives of the Authority, the Customs and the Port of Tripoli. The recommended work plan of the TFWG include: (i) establishing the TFWG, (ii) aligning infrastructure design with trade facilitation, (iii) defining the level of automation at the port, (iv) decide on the provision of AEO status to TSEZ investors, and (v) draft decisions and decrees.

**6.46 Apply a trade automated system**

The design and implementation of an electronic interoperable IT system at a special economic zone level would greatly benefit the simplification of processes of imports and exports.

**6.47 Revisit GAFTA and AA to ensure products processed in the TSEZ are eligible to preferential treatment when complying with rules of origin, while evaluating potential negotiation costs**

The Government of Lebanon (GoL) should seek eligibility to GAFTA preferences for goods produced or processed in a free zone or SEZ and ensure that the Association Agreement (AA) with the EU provides Lebanese SEZ-processed products the same treatment than Lebanese products produced elsewhere in the country. The latter could be achieved, for instance, by amending Article 35 of the AA. Yet, even if GAFTA and the AA would end-up fully recognizing products processed in SEZs/FZs as eligible to preferential treatment when complying with rules of origin, exporters facing low market access in the respective destination countries would not trouble to comply with RoO when the compliance costs outstrips the benefits of preferential market access. Thus, the GoL should also evaluate the potential negotiation costs of pursuing full recognition of SEZ-processed products in both agreements.

*Knowledge Innovation Center (KIC)*

6.48 **Develop community building and networking programs**

In order to address the challenges mentioned earlier concerning communities and networks, and to further encourage their development, it is important to strengthen coordination mechanisms within the entrepreneurial and innovation ecosystem in Lebanon and between Beirut and Tripoli. This could include incentives and support for networking events and joint activities among ecosystem actors in both cities and internationally. The KIC could kickstart activities by partnering with the local start-up community to organize networking events and bringing international actors to enrich the networking that is already taking place in Tripoli. This could also inform the approach to a possible advisory board for the KIC and secure commitment from board members.

**6.49 Link start-ups, academia and industry**

By linking innovative, tech-enabled start-ups with the larger and more traditional firms in as structured program, the ecosystem can expand and help boost productivity and innovation in traditional industries. Policy makers can help kickstart such programs through catalytic actions, including convening key stakeholders and ecosystem players, and providing funding to test and pilot such initiatives. The KIC can act as a coordinator and host for such programs, collaborating with key hubs and other ecosystem players from around the country and abroad.

In order to catalyze the highly educated young population and fill the practical skills gaps that may constrain entrepreneurs and technical talent, policy makers are encouraged to explore increasing practical education in university and incentivizing rapid and applied technical skills training programs. By bridging academia to industry and incentivizing the creation of a special internship program whereby students get to work on real projects for private companies, students can increase their practical experience and companies can benefit from lower costs, innovative talent, and new ideas. Policy makers can take further catalytic action by offering seed funding or initial subsidies to kick-start such programs, which tend to turn self-sustainable after three-four years, primarily through fees from private sector partners.

**6.50 Implement bootcamps for rapid upskilling**

By expanding rapid, demand-driven, applied-skills training, the talent pipeline can increase in an accelerated manner, meeting unfilled demand by startups and industry. However, this kind of

training often has prohibitively high tuition fees for those with low or even middle income. Policy makers can consider investments to either subsidize or offer loans on favorable terms to increase participation by qualified candidates in such trainings. Furthermore, they can incentivize the expansion of such trainings to key subsectors of the economy, such as light manufacturing, through market research, private partnerships, and seed funding for the development of appropriate curricula. The KIC could play a leading role in market research and connecting training providers to private sector demand, which can inform training providers of key skills gaps and strategic subsectors. It could help in coordinating stakeholders to convene a public-private partnership to catalyze such programs through job placements and private investment. It could support the expansion of bootcamps to Tripoli through donating space or other key infrastructure and amenities.

### *6.51 Strengthen the start-up support infrastructure*

To address the constraints in supply of suitable mentors and to strengthen support services in Tripoli, and in the Lebanese ecosystem, policy makers need to consider how to catalyze further capacity building of mentors in accelerators and to attract international talent (as mentors, entrepreneurs, or capacity builders) to the ecosystem. Performance contracts, whereby funding is attached to set targets in terms of improvements in the organization's business model, services or other targets, can offer an instrument whereby accelerators, incubators, or hubs who receive funding are set objectives and yield results that are aligned with the policy goals.

Policy makers should also carefully examine key factors that would attract accelerators and incubators to effectively reach start-ups in the Tripoli area, as well as attract existing ecosystem actors in Tripoli to the KIC. They need to prioritize other programs focused on skills development and pre-acceleration to boost the start-up and talent pipeline in Tripoli, described above, which could make Tripoli a more attractive recruitment/scouting ground for such organizations. This would need to be supplemented by substantial communication and branding efforts to showcase the KIC as well as efforts to boost networking opportunities at the KIC for key stakeholders and ecosystem actors. These suggestions, along with recommendations to support community development and networking, may also help address funding issues.

# 7. Conclusion

7.1 **Lebanon is facing a considerable employment challenge.** The private sector, the main job creator, has not been able to create enough jobs to keep pace with the rapidly growing young population, as such significant numbers of youth and women are pushed to unemployment. The massive influx of Syrian refugees and the regional political instability have aggravated the situation. In the absence of appropriate policies unemployment is expected to continue rising. In face of such a major challenge, there is a critical need to create value added jobs in Lebanon, building on the country's educated human resources that are widely known to be talented, competent, multilingual and resilient.

7.2 **the analysis conducted under the LECOD initiative identifies a range of policy options, already in the government's sights that can improve competitiveness and integration with the world which in turn leads to improved employment outcomes.** Such policies include encouraging private participation in investment in critical economic infrastructure through PPPs, attracting additional foreign investment to the country in priority sector that can create values added jobs, and addressing constraints for private sector growth such as trade barriers and competition. Progress on these fronts would help push Lebanon to realize a more job-focused growth.

7.3 **PPPs can be an excellent means to deliver or upgrade infrastructure in Lebanon, and attract investments under the CIP**. Lebanon faces a pressing need to improve and expand access to basic infrastructure services, while also facing increasingly severe fiscal constraints. The recent passage of the PPP law and the development of the CIP opens opportunities to make significant gains in closing Lebanon's infrastructure in the coming years by leveraging of private sector financing. What is now key is mobilizing the institutional infrastructure to support PPPs, including: government wide ownership, capaciting the centralized coordinating agency within government, mainstreaming standardized institutional processes and methodologies, and capacity within line ministries/contracting agencies to develop and implement PPPs.

7.4 **Foreign investment has the potential to be an important driver of economic growth and job creation in Lebanon**. It can help Lebanon integrate into global production value chains and shift the country's workforce from lower to higher value-added jobs. Attracting FDI in services sectors such as ICT and BPO, and promoting manufacturing outsourcing options through NEMs can be a way to create the required jobs, upgrade domestic firms and help Lebanon move towards more sophisticated tasks of value chains. To make this possible, ideally a suitable investment policy framework that leverages the TSEZ and includes effective investment services aimed at attracting, retaining and linking FDI with the domestic economy are needed.

7.5 **In today's increasingly competitive environment, it is necessary to ensure fair and open competition where market forces could create opportunities for a more efficient allocation of resources and support private sector investment and growth.** Boosting domestic competition would increase efficiency and productivity. It would enable more productive firms to enter the market and place downward pressure on high markups. Strengthening competition in the broadband value chain can accelerate the deployment of high-speed broadband networks including

fiber, and impact penetration, speed, and cost which in turn will improve productivity, foster job creation and develop the knowledge economy. As such, levelling the playing field among all service providers and allowing for fair and non-discriminatory access to essential facilities and promote competitive neutrality between the state-owned operators and private players is key.

7.6 **Facilitating trade across borders is necessary if Lebanon is to boost its exports.** Lebanese policymakers are aware of the need to reignite export growth. In fact, the government has called for doubling exports over the coming few years. Complex and lengthy clearance processes, and multiple procedures and requirements, increase the costs and time of doing trade. Today these obstacles may be posing greater barriers to trade than tariffs, especially for SME exporters. Hence, it is important to accelerate trade facilitation efforts and enhance administrative efficiency and effectiveness, reduce costs and time to markets by simplifying and automating processes and procedures and improving risk management. Using the TSEZ as a model for the initial application of reforms, with a possibility of scaling-up at a national level, is an excellent starting point. It is also important to ensure preferential treatment for zone processed goods under Lebanon's multilateral trade agreements.

7.7 **The planned TSEZ can play an important role in the attraction of investments, growth of exports, and outward orientation of the Lebanese economy**. **It also can contribute significantly to addressing the jobs challenge.** However, its fate, to a great extent, is determined from the outset, by the choices made in the adopted policy frameworks, incentive packages, and various other provisions and bureaucratic procedures such as business registration/licensing, trade procedure and processes, and the supply of high-quality serviced land, pre-built facilities, and utility services. These elements will impact the likely scale and scope of investor demand, and investors will carefully weigh them in their investment decision. Moreover, experience suggests that maximizing the benefits of zones depends on the degree to which they are integrated in an overall investment and trade reform agenda.

7.8 **Combined these policy actions have the potential to make a significant impact on job creation and developing economic opportunities for the Lebanese.** Evidence world-wide also shows that these policy interventions have led to positive labor effects, and contribute to output growth in the long run.

7.9 **However, efforts should not be limited to this.** While recognizing that national and regional political instability remains the most critical constraint to investment, addressing chronic constraints for private sector such as electricity, and improving access to finance by enacting key laws such Secured Transaction and Collateral Registries law, and improving the regulatory framework for businesses, are key to improving the investment climate in Lebanon. Ideally, all these policies should be implemented in an integrated manner.