

# Reform, Modernization and Growth •

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The year 2000 and beyond must be made competitive, we must have an environment which is favorable for the return of entrepreneurs as well as our Lebanese financial capital that is abroad, but also have an economy capable of producing jobs, productive jobs for our young population. So I've entitled my little talk : Reform, Modernization, and Growth, as being basic issues we need to address over the next few years. There are five policy areas which I would like to discuss and then want to comment on some of the specific issues emerging from the important research project that was undertaken by SRI and LAU. There are four major areas I would like to discuss:

1. Administrative reform,
2. Monetary and Exchange Rate Policy
3. The fiscal policy,
4. International commercial policy,
5. Competition and competitive policy.

I- Let me start first with administrative reforms. You have followed our newspapers and our public statement, our media is very active -thank God- it could be one of the most promising industries for the future, that could be one of the clusters in which I think we have a comparative advantage. The media have kept you informed of the first steps in terms of administrative reform. What is the true meaning of administrative reform? The true meaning has 3 aspects:

We need to have and achieve **transparency** in the way government conducts its business, and the way the government conducts its relations with the private sector and our citizens.

We also need to have an **accountable** government. Accountability and transparency are basic to any relation between government and its citizens, between government and the international stance with Lebanon.

So this government is here to undertake deep and lasting administrative reform, with the purpose of making government efficient, transparent, and accountable.

The transparency, accountability and increased efficiency of the government, along with the change in the political regime, I believe reduces economic risk and makes the government more productive; and importantly by reducing economic risk, we can also reduce political risk.

The international evidence is very clear. Corruption, waste and bribery diminish economic growth. Transparency, accountability, good governance, efficient governments promote economic growth. This is an important challenge but we need to achieve that.

I'm here to announce that this government is serious about economic reform and administrative reform. And just to remind you, this is the first time this happens in

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35years. So in the series of changes you've heard of and seen, as well as those that were announced yesterday, will continue, they will not end here, until the time when we have the transparency, accountability and efficiency in the government that is desirable.

II- Second set of issues has to do with the economic stance of government, fiscal policy, and the public debt. We're designing at the moment an economic policy package that is meant to do the following:

It's intended to promote private sector activity. Let the private sector be the main engine of growth over this next period, and review the role of government over the coming 5 years.

In terms of the budget deficit, the current levels are clearly too high. Over the next few years, we need to think of reducing the budget deficit from current levels - close to 15% of GDP- down to 5-6% of GDP. I'll also make a side remark that is important, the GDP is lower than GNP in Lebanon. You need to be careful when assessing the situation, always keep that in mind. When discussing some numbers people get alarmed, but when you look at the numbers relative to GNP and therefore including net income from the rest of the world that we receive, the numbers are substantially less, the deficit relative to GNP is substantially less and the level of debt relative to GNP is substantially less, because GNP is larger than GDP by ~10%, so it is not as alarming as otherwise. Nevertheless, we need import and economic reform.

Second, you cannot reduce the budget deficit on a permanent and sustainable basis unless you address the public debt issue. The two, of course, are intertwined. Unless you address the issue of the public debt and have a clear economic policy as to what you're going to do to the level of the public debt, you cannot really hope to address the issue of the budget deficit. The reason is that given the size of the debt, debt service consumes, more than 75% of government revenue. Therefore, unless you address the public debt issue, you cannot seriously hope to address the budget deficit issue.

In addition to that, this government does not wish to reduce the budget deficit and therefore, as a result, merely do that to service debt. That would be a mistake both in terms of social and economic policy.

As you know, our regions in Lebanon are in need of infrastructure, a large number of them are impoverished. So any program to reduce the budget deficit and reduce the budget debt has also got to be accompanied by a program that will address the needs and requirements of the regions of Lebanon. Any reconstruction cannot be successful in Lebanon unless all Lebanese, in all the areas and regions of Lebanon, of all walks of life, feel that they are concerned by the reconstruction and can benefit from it. The reconstruction cannot be the reconstruction of cities, but the reconstruction of Lebanon across all the territory of Lebanon. Everybody needs to feel that they benefit from the reconstruction of Lebanon, otherwise we would have failed in our reconstruction. So what you need to do is achieve a balance between the different objectives of economic and social policy. On the infrastructure side, we will be accelerating the loans that were already in place, and discuss with a number of institutions, such as the various Arab funds, development banks, and the World Bank. Most of those are infrastructure and development projects. There are over 400 projects that are lying dormant, we will accelerate the implementation of those. Those will help the regions of Lebanon, we'll help our rural areas. They will be directly productive, in other words, most of these infrastructure and development projects can go hand in hand with private sector investment; therefore, you'll get a

double impact of both increased public sector investment in the areas where we need it, accompanied by private sector investment.

Let me give an example, if you address environmental issues by cleaning up our beaches, our coast, our rivers, and the rest of our environment, you are also making it a more conducive environment for tourism. Tourism, the environment, and agriculture are strongly linked. There's a golden triangle there. A country like Switzerland is extremely successful. It subsidizes its agriculture, and as a result, it also has a clean and healthy environment that improves tourism. People think of Switzerland as a clean green place, and indeed it is. So if you accelerate environmental investment issues, you are also giving incentives for the private sector to invest in tourism, which helps generate growth overall. So that's another cluster.

In terms of reducing the level of the public debt, the government has announced a program of privatization. This is the first time in the history of Lebanon that this issue is being addressed in a serious fashion. So we've announced that the government will propose a comprehensive law on privatization, that will provide the regulatory environment. We need to ensure that privatization takes place in a transparent fashion, with at least three bodies being created: a policy-setting privatization council; an executive privatization team and unit that will assess any institutions that are to be privatized. The law would also institute a regulatory agency supervising any privatized entities to make sure that pricing, quality and extent of services and investments are well provided for. We will make sure that you're not going to transform what is now a public monopoly into a private monopoly. We're also going to make sure that if you privatize any entities, that they will be providing services efficiently, at non-monopoly prices, but more importantly, across all the areas of Lebanon. You don't want to run the danger of having a privatized entity that will just provide services where it's most profitable; you also have to think of all the regions of Lebanon. That will have to be part of any privatization brief. As a result of these concerns and more generally, to ensure a competitive environment, we are preparing an anti-trust legislation.

The most important thing from a fiscal point of view, is that any privatization proceeds will be used to reduce the size of the public debt. As you do that, you enter a soft-landing scenario policy package, namely by reducing your budget deficit and taking a number of steps to do so, and reducing the size of your public debt, you'll be reducing debt service, meaning the overall budget deficit will start declining, and as a result, the crowding out that government is now imposing on the private sector will diminish. This will provide the scope for lower interest rates both in Lebanese pounds as well as in US dollars. As interest rates start declining, the private sector will find it more profitable to do two things: to increase expenditure on consumption and invest in productive projects and investments. They will also turn towards the financial markets and invest in equity instead of investing in treasury bills and debt. Investment projects in productive sectors will become more profitable, and therefore this will accelerate private sector lead economic growth.

Our aim then is, through privatization, through reducing the budget deficit, to reduce the size of the government; through administrative reform to make government more efficient so that government itself becomes a more efficient provider of services. In turn, this reduces the costs of inputs to business, and increases productivity of the private sector. I think we need to end the concept that a citizen is there to serve the government. You have to reverse it and have the government serve the private sector and the citizens; make government productive.

III- Third major area: if you want to increase your exports and export growth, you need to rethink your international commercial policy. That is currently happening. As you know we are in negotiations with the European union on a partnership agreement, that can open up substantial markets for the Lebanese industry, agriculture and service industry. But in addition, we also have to think locally. We do not want to be exposed to trade diversion. If we have too many links through a European partnership agreement, this could divert trade away from potentially more competitive areas. So we're also accompanying negotiations with the European Union with steps that have already started to be implemented, trade agreements with our Arab neighbors. Starting January 1<sup>st</sup> 1999, tariff barriers between Lebanon and Syria have been lowered by 25% on a fairly large number of industrial products. As Syria opens up and liberalizes its economy allowing the entry of Lebanese products, and as you increase trade between the two countries, that would be the beginning of a medium-sized economy with around 21 million people. This provides opportunities for Lebanese agriculture, in particular the agro-industrial sector, industry as well as services. This will also be accompanied by increased openness in the Arab free trade area and the common Arab economic zone. This is the beginning of a trading bloc developing in the Arab world; and this is excellent news for Lebanon and the skills of the Lebanese who are entrepreneurs and know how to market and sell.

Clearly now, if you want to be successful in exporting, you need to adopt international standards and norms. And in that we have a number of institutions, and I appeal to you not only to support them but also to use them: LIBNOR, and the Industrial Research Institute. Perhaps you are not too familiar with these 2 institutions, but they are there and I'm going to make sure that you become more familiar with them - they fall under the control of the Ministry of Industry. LIBNOR will help you impose international standards, ISO norms and standards. As we impose them, our products and services will become more competitive internationally, and we'll also be able to compete with imports domestically because the quality of our goods and services will also increase.

My appeal to you as agro-industrialists, as service providers, think of putting together a program whereby you'll increase the quality of your goods and services; use these institutions, they are there to help you. It's this marriage between public institutions and the private sector that will make us successful.

In terms of international commercial policy, Lebanon will have to renew its tradition of being open, of competing internationally. Our trade liberalization agreements with Syria, Egypt, Kuwait, Jordan, the Arab Free Trade Area agreement, the European Partnership Agreement and others all imply a reduction in tariff and non-tariff barriers to trade. This obviously will involve changes in our tariff policy. Tariff policy has to be reviewed and studied so that it is no longer a burden on the private sector. At the moment, for example, our tariffs are also imposed on raw materials and intermediate goods that are used by our industry. This makes our industry non-competitive. If we have alternative forms of taxation, we can reduce those tariffs on raw material and intermediate goods and therefore make our industry much more competitive. Our policy will be to reduce tariffs on raw materials and intermediate goods.

IV- In terms of competitive policy, our ministerial declaration had a one-liner in it, many people perhaps did not notice it. It said that we will be developing a law, an anti-trust law and to improve competition, and a law for consumer protection. That also will certainly be on our agenda. And this I believe is important because restoring

competitiveness to our economy is certainly one of the main engines of economic growth.

What you have the beginning of, and I'm trying to give you just the broad outline, is an overall package in terms of government reform, in terms of commercial policy, in terms of fiscal policy and debt management, international commercial policy, competition policy. The package, I believe will be the beginnings that will allow the Lebanese economy to takeoff again. I believe that this package needs to be supported by a number of laws. I will mention them briefly, but they are important. Some of them are measures that will directly spur economic growth.

- The first law concerns small and medium sized businesses. A recent industrial survey shows that 90% of our businesses have 15 employees or less; so SMB's are really the backbone of the Lebanese industry and business. You need to address their requirements in terms of finance, and currently there is a law proposed to parliament to make sure-we're hoping that it will pass very quickly<sup>1</sup>- which will create an institution that guarantees small and medium sized credits. That is important because by guaranteeing up to 75% of principal plus interest on these small and medium sized loans, they will reduce the risks of those loans. Banks and financial institutions will find it profitable to extend more loans to small and medium sized businesses, and will be able to do so at lower interest rates because they have the guarantee of the institution. We are strongly supportive of such lending.
- Another law concerns **leasing** activities. The law on leasing is important in providing medium and long term finance to Lebanese industry and particularly to agro-industrial projects, as well as to contracting companies.
- We're also going to be proposing a law to the parliament that will address and modernize our **insurance industry**. That law hopefully again will be passed in 1999. Our insurance industry at the moment is not playing its full role and potential in both providing insurance services, nor playing its role in providing long-term financing to the Lebanese economy. The insurance industry abroad, pension funds, insurance companies, are normally the major investors in assets like real estate and housing, because they have long term sources of finance, and therefore they can provide finance for long term requirements. We will propose a law that will modernize our insurance industry. The law will also provide for better regulation of the insurance industry, by having a separate commission similar to our banking control commission, there will be an insurance control commission to regulate the insurance industry.
- Another law, which I believe, is extremely important and that is currently in parliament, is the law on the protection of intellectual property rights and patents. Intellectual property is an area in which I believe Lebanon has a comparative advantage. We are providers of services, we can in our small country be the location for businesses that wish to provide products and services requiring the protection of laws on copyrights, intellectual property and patents. They will not do so unless we can provide them with the protection of a patent, property rights, and intellectual property law. This will be in our long-term interest.
- The final law I wish to mention is the law that will create **an independent capital market authority**, similar to the SEC in the United States, and the French Commission des Operations de Bourse, or the SFA in the UK. We need a separate capital markets authority. This law would privatize the stock exchange,

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<sup>1</sup> The law was approved by Parliament in February 1999.

which is exactly what it should be, it should be privately run and managed. However, you need a separate regulatory authority. Promoting the financial markets and the stock exchange is extremely important, in order to be successful in privatization, which effectively returns to the citizens part of the assets that the state was controlling or owning. It can only be successful in doing so if the financial markets are efficient. Privatization and efficient capital markets are a policy package. You need the capital markets authority to have efficient financial markets, which allow a smooth process in terms of transferring shares and rights to the private sector.

Let me end my talk with a number of basic comments. We are at a crossroad, and we face some serious issues and challenges. I believe what government is proposing in terms of administrative reform, is a new policy regime that is promising the rule of law, transparency and accountability to make the government more efficient. The economic package that I've outlined will also make sure that the public sector and government does not stand in the way of private sector growth and development. As we do so, as we remove corruption, waste, and the bribery, I believe this will provide a better investment climate, and let our Lebanese business people be even more ambitious and confident for the future and accelerate their investments. I think it will also attract more investments from the rest of the world. With more trade opportunities, with better investment horizons, I think we'll achieve Lebanon's true economic potential. We can only do so if the public sector, government and the private sector cooperate together.

I hope you will join me, in achieving Lebanon's true potential.  
Thank you.