

IMPACT OF THE JULY OFFENSIVE ON THE PUBLIC FINANCES IN 2006

Brief Preliminary Report

August 30, 2006

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Executive Summary

1. The Israeli offensive of July 2006 has resulted in severe repercussions on the Lebanese economy as a whole. Notwithstanding their immediate impact, these ramifications will most likely continue to be felt in the years ahead. In fact, while the full picture of the physical damage assessment will shortly be clearer and quantified, the impact of the offensive on the economic, financial and public finance indicators will span over the short and medium term, especially with the continuing blockade and the breach of the cessation of hostilities by Israel.

2. Prior to the offensive, on the public finance front, the government was able to raise revenues, decrease primary expenditures, and therefore improve the deficit and the primary surplus. Indeed, despite the difficulties which faced the country following the assassination of Prime Minister Hariri in February 2005, all public finance indicators were showing improvements in the one-year period spanning from June 2005 to June 2006 due to the efforts that were exerted by the government to tighten the grip on the fiscal situation. As a strong sign of this amelioration, the **primary surplus more than quadrupled during the first half of 2006 compared to the first half of 2005.**

Table 1: Public Finance Results until June 2006

(LL billion)	HI 2005	HI 2006
Revenues (1)	3,533	4,063
Expenditures	4,856	5,230
Debt service	1,555	2,161
Primary Expenditures	3,301	3,069
EDL	433	151
Municipalities	166	163
Fiscal Deficit	-1,323	-1,167
Primary Surplus / Deficit	232	994

Source: Ministry of Finance

(1) Total revenues do not include grants

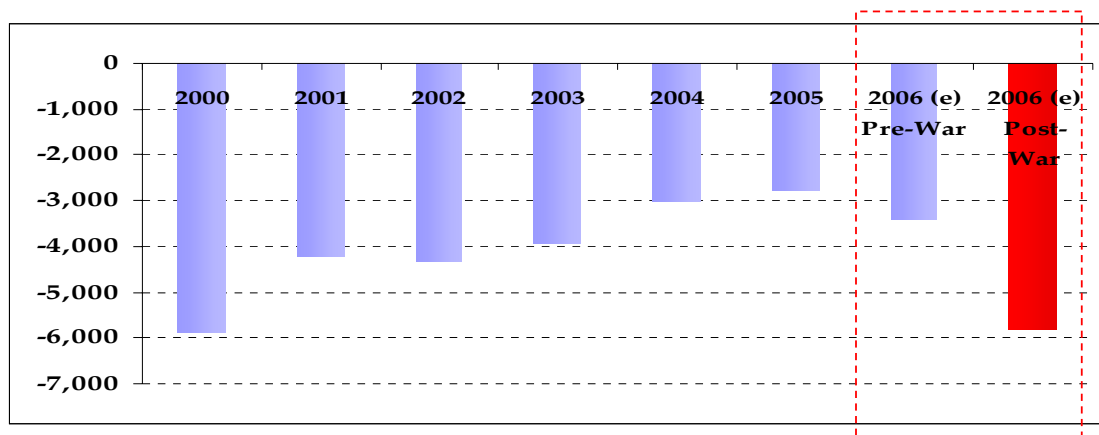
3. The improvement in the primary surplus in the first half of 2006, prior to the Israeli offensive on Lebanon, was due to increased efforts to raise revenues, through enhancing collection and regularizing transfers from public entities and utilities. The revenues were 4,063 billion L.L. for the first half of 2006, which marks a 15% increase compared to the first half of 2005. Not only did the government enhance revenues, but it also controlled expenditures through better management, particularly non-interest expenditures. Non-interest expenditures dropped by 7% from 3,309 billion L.L. (US\$ 2,195 million) in the first half of 2005, to 3,070 billion L.L. (US\$ 2,036 million) in the first half of 2006.

4. Also, the progress on the debt management front helped decrease the financing risk and the government was able to raise financing solely through the market, without any reliance on the Central Bank. In fact, between the time it took office and the launch of the offensive, the government was able to repay slightly less than US\$ 3 billion (4,523 billion L.L.) to the Central Bank through a reduction of its treasury bills portfolio.

5. However, the offensive of July 2006 has put an end to this amelioration. While growth looked poised to grow at 5% in 2006, with a record of 1.6 million tourists anticipated to visit Lebanon, the heavy destruction and loss of capital and human resource base will surely result in a loss of output as per preliminary expectations from INSEE.

6. In sum, the loss in public finance due to the Israeli offensive against Lebanon in July 2006 is estimated at around US\$ 1.6 billion (2,419 billion L.L.) until the end of 2006, taking into consideration the Israeli blockade which lasted for a two-months period, barring the full impact of the infrastructure cost on public finances, and keeping in mind that the full impact will be felt throughout 2007 and the medium-term.

Figure 1: Evolution of Total Deficit – Pre and Post War Assumptions

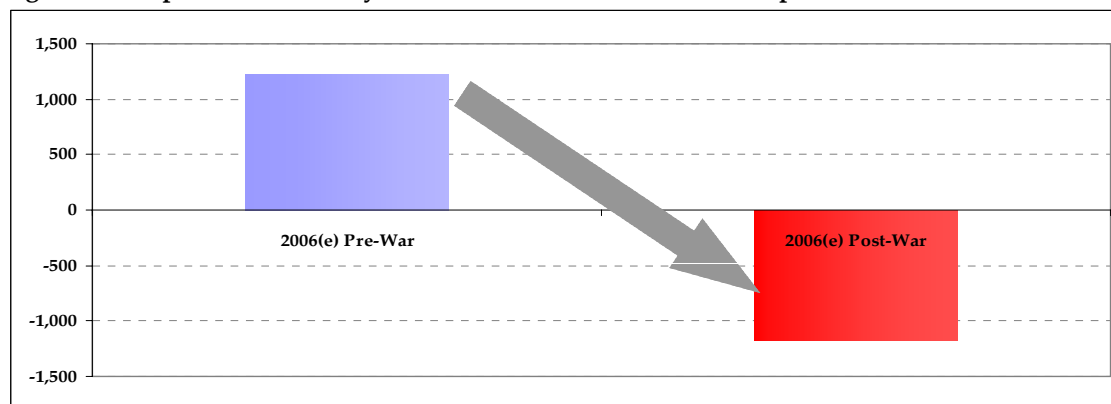


7. More specifically, for the two months of July and August, the **slide in revenues** has already amounted to around US\$ 314 million (473 billion L.L.) (according to preliminary estimates), which is equivalent to 1.44% of GDP¹, and is expected to sum up to more than US\$ 920 million (1,386 billion L.L.), only in 2006 when compared against previous expectations, taking into account the spanning of the blockade for a period of two months. The offensive has resulted in lower tax and non-tax revenues, mainly trade and international exchange duties, the value-added tax.

8. At the same time, the **increase in primary public spending** will amount to around US\$ 800 million (1,218 billion L.L.), which is additional spending of around 3.7% of GDP², only in 2006 when compared against 2005. The reasons behind skyrocketing expenditures are to compensate for the heavy toll in human life, to cover for the profound destruction in housing and infrastructure, to finance health and relief needs arising from the offensive, and to pay for the security expenses resulting from the implementation of UN Security Council Resolution 1701.

9. The end result is expected to be worsening fiscal dynamics and the emergence of a **primary deficit** for the first time in six years, following years of exerting efforts towards containing the fiscal situation. The primary surplus of 994 billion L.L. (US\$ 659 million) that was recorded for the first half of 2006 is now estimated to be reversed into a primary deficit of 1,173 billion L.L. (US\$ 778 million) by the end of 2006 – 1,909 billion L.L. (US\$ 1.266 billion) higher than 2005 and far from the original target of a primary surplus of 1,246 billion L.L. (US\$ 827 million), in the absence of external shocks. As a result of the offensive, the Ministry also estimates, for 2006, a total deficit of 5,808 billion L.L. (US\$ 3.85 billion), which is almost twice the total deficit for 2005. Rising deficits will call for additional financing needs, and worsening debt dynamics, in a country which was already battling to redress its fiscal imbalances.

Figure 2: Comparison of Primary Balance – Pre and Post War Assumptions



¹ The post war GDP forecasted for 2006 is LL 32,765 billion (please refer to the table of GDP estimates 2003-2006)

² Please refer to the previous footnote

Table 2: Fiscal Impact of the July Offensive – Historical Evolution of Fiscal Performance

LL billion	2003	2004	2005	2006	2006
				Pre -War	Post- War
Revenues	6,654	7,514	7,405	8,100	6,714
Expenditures	10,592	10,540	10,203	11,489	12,522
of which Primary Expenditures	5,718	6,519	6,669	6,854	7,887
Fiscal Balance	-3,938	-3,026	-2,978	-3,389	-5,808
Primary Balance	936	995	736	1,246	-1,173

Source: Ministry of Finance

Table 3. Fiscal Impact of July Offensive (Historical Evolution of Fiscal Performance in % of GDP)

In % of GDP	2003	2004	2005	2006	2006
				Pre -War	Post- War
Fiscal Balance	-13%	-9%	-9%	-10%	-18%
Primary Balance	3%	3%	2%	3%	-4%
Total Revenues	22%	23%	22%	23%	20%
Primary Expenditures	19%	20%	20%	19%	24%
GDP (in billion LL)	29,846	32,655	33,081	35,603	32,765

Source for GDP: National account data 2003, BDL estimates for 2004 and 2005, Real growth 2006 preliminary forecast (INSEE consultant)

Note:

1/ Post war Inflation estimates in 2006 is assumed to be similar to 2005

2/ Post conflict real growth 2006 is estimated between - 0.5 percent and -2 percent

Box 1: Financial Assistance from Friendly Countries

Significant confidence in the system was injected with the transfer of US\$1.5 billion from the Kingdom of Saudi Arabia and Kuwait. In fact, in early August, Saudi Arabia provided financial support through a US\$ 1 billion deposit at the Central Bank of Lebanon accompanied by a commitment of US\$500 million as a grant for reconstruction. Kuwait also deposited US\$ 500 million at the BDL and committed a grant of US\$ 300 million for reconstruction. Saudi Arabia and Kuwait's grants for reconstruction will constitute the seed money for a reconstruction fund.

To address immediate early recovery needs amounting to US\$ 537 million, a donors' conference organized by the Swedish government took place on August 31, 2006 in Stockholm and resulted in around US\$ 900 million of assistance. The largest donors were Qatar with slightly more than 33% of contributions, the Arab Fund for Economic & Social Development with around 13%, the Kingdom of Saudi Arabia with 6.7%, and the EC & USA with around 6%.

In addition to funds spent to date by the Lebanese Government on relief, the Lebanese Government - High Relief Committee has received a total of US \$103 million as of August 29th in terms of cash donations (excluding in kind donations). These funds are for the sole purpose of relief and will be spent accordingly. These funds do not include donations channeled through non-governmental and multinational organization such as the International Red Cross and the United Nations. The main sources of funding are governments, multilaterals, companies, individuals and embassies and organizations. As expected, governments are the largest donors accounting for 97% of all donations (mainly Saudi Arabia, Iraq, & Kuwait).

I – Projected Revenues in 2006

10. By June 2006, revenues totaled 4,063 billion L.L. (US\$ 2,695 million) rising by 15 percent compared to the first half of 2005, i.e. 531 billion L.L. (US\$ 352 million) of additional revenues, 390 billion L.L. (US\$ 259 million) of which stemming from most tax fronts, namely income taxes, property taxes, VAT and fiscal stamps; and 161 billion L.L. (US\$ 107 million) originating from non tax revenue items, namely income from government properties (telecommunications) and administrative fees and charges (vehicle control fees).

11. This positive environment was expected to continue throughout the year, and revenues were therefore assumed to end the year 2006 at 8,100 billion L.L. (US\$ 5,373 billion). However, the Israeli offensive against Lebanon has devastated this projection. Instead, revenues for 2006 are now estimated at 6,714 billion L.L. (US\$ 4.45 billion), which is 1,386 billion L.L. (US\$ 920 million) lower than original projections. This estimate takes into consideration the impact of two months of air and sea blockade imposed on Lebanon and the resumption of trade activities thereafter.

12. When compared to 2005, total expected revenues for 2006 indicate 9 percent lower collection (6,714 billion L.L. versus 7,405 billion L.L.), keeping in mind that the year 2005 also witnessed a series of dramatic events which disrupted economic activity and therefore revenue collection.

13. Tax revenues for 2006 are expected to generate 4,596 billion L.L. (US\$ 3,049 million), which is approximately 6 percent lower than the collection level of 2005, as a result of the interruption of economic activity and the consequent slowdown in consumption. The situation has been further exacerbated by the air and sea blockade which lasted for two months and the resulting interruption of the trading activity for nearly two months.

14. As an immediate impact of the Israeli offensive, revenues from taxes on international trade are expected to fall by 35 percent in 2006. In fact, despite a 33 percent rise in imports in the first half of 2006 compared to the equivalent period in 2005, total imports for this year are anticipated at 15 percent below the import level in 2005. On the other hand, maintaining the capping on the retail price of fuel in the face of rising international oil prices exacerbates the loss in trade revenues. Revenues from fuel excise have plummeted throughout the year, reaching a close-to-zero collection level in June 2006. Consequently, 2006 year-end revenues from fuel excises are projected to be 75 percent less than those for year-end 2005. The share of taxes on international trade out of total revenues is expected to drop from a historical average of 25 percent to barely 12 percent in 2006.

15. Domestic taxes on goods and services are anticipated to collect 7 percent lower revenues in 2006 than total collection in 2005, namely on account of lower VAT revenues. The disruption of economic activity, and namely tourism, the expected slowdown in consumption and the nearly two months of blockade adversely impacted VAT collection. The second half of 2006 is projected to collect 24 percent lower VAT revenues than the first half of 2006, ending the year with 8 percent lower revenues on a year on year basis.

16. Non tax revenues for 2006 are expected to decline by 20 percent compared to the 2005 revenue level. The causes behind the fall in non tax revenues are the settlement to the 2 previous mobile operators as well as lower transfers from the budget surplus of telecommunications and from the Port of Beirut due to the damages to the cellular and fixed line networks, and to the interruption of all trans-boarding activity in the port resulting from the sea blockade.

Table 4: Pre-War and Post-War Revenue Projections

(LL billion)	2005	Expected 2006 Pre War	Expected 2006 Post War	% change 2006
Tax Revenues	4,864	5,579	4,596	-17.62%
Taxes on Income Profits & Capital gains*	1,047	1,161	1,120	-3.53%
Taxes on Property	414	729	637	-12.62%
Domestic Taxes on Goods & services	1,896	2,183	1,761	-19.33%
Value Added Tax (VAT)	1,693	1,939	1,565	-19.29%
Taxes on International Trade	1,268	1,179	828	-29.77%
Excise	787	673	448	-33.43%
Customs	481	506	380	-24.90%
Other Tax Revenues (fiscal stamps)	241	327	250	-23.55%
Non Tax Revenues	2,116	2,089	1,695	-18.86%
Entrepreneurial & Property Income**	1,662	1,490	1,238	-16.91%
Administrative Fees & Charges	365	494	367	-25.71%
Treasury Revenues	421	432	423	-2.08%
Total Revenues	7,401	8,100	6,714	-17.11%

Source: Ministry of Finance

*The taxes on income, profit & capital gains revenue figure shows that the collection of these taxes is not relatively impacted by the Israeli aggression on Lebanon as more than 70% of the expected amount for 2006 was collected during the first half of the year.

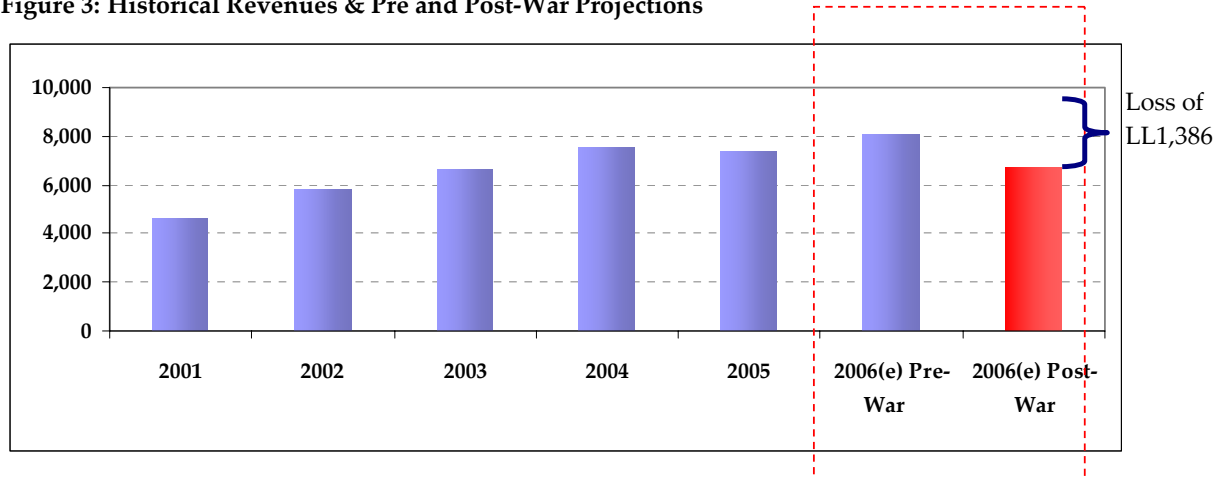
**The 2006 pre-war & post-war projections account for the settlement to the 2 previous mobile operators. The 2006 post-war projection also accounts for the damages to the telephone network resulting from the Israeli offensive.

17. It is worth noting that the offensive against Lebanon will only partially impact total revenues in 2006. This is because income taxes on profits and capital gains and property taxes were largely collected during the first half of the year. This is also because the 15 percent improvement in revenues witnessed during the first half of 2006 will to a certain extent outweigh the expected deterioration for the remainder of

the year. As such, it is expected that the adverse impact of the offensive will be more severe in 2007 onwards, mostly in the first half of 2007.

18. To ascertain the harmful impact of the offensive on public finances, and the corrosion of the revenue base, preliminary figures reveal a 35 percent fall in total revenues for the months of July and August 2006 compared to the cashed amount in July and August 2005. In total, the magnitude of the loss in revenues over the period July-August 2006 is calculated at near 475 billion L.L. (US\$ 315 million), or 1.5% of GDP.

Figure 3: Historical Revenues & Pre and Post-War Projections



II – Projected Expenditures in 2006

19. Total expenditures for January-June 2006 reached 5,230 billion L.L. (US\$ 3,469 million), compared to 4,867 billion L.L. (US\$ 3,229 million) during the same period in 2005, an increase of 7.5 percent. This increase is mainly due to a rise in debt service by 602 billion L.L. (US\$ 400 million) or 38 percent comparing these two periods. Meanwhile, non-interest expenditures decreased by 7 percent (the equivalent of 239 billion L.L. or US\$ 150 million) during the first half of the year compared to the same period in 2005 due to efforts by the Ministry of Finance to curb expenditures and to manage the timing of payments to better meet available liquidity.

20. However the events of July 2006, have reversed the trend of lower primary spending during 2006. In fact, while non-interest spending was originally expected to end the year at 6,854 billion L.L. (US\$ 4.5 billion), post-war projections reveal higher non-interest expenditures – reaching 7,887 billion L.L. (US\$ 5.3 billion) - due to the relief and reconstruction efforts that have started to be undertaken by the Government, as well as the additional security measures required for implementation of UN Security Council Decision 1701. This implies a deterioration

of 1,031 billion L.L. (US\$ 684 million), or around 3 per cent of GDP, compared to the year-end projections prior to the commencement of hostilities. At the same time, total expenditure (including debt service) will reach 12,522³ billion L.L. (US\$ 8,306 million) by end of 2006, an increase of 2,319 billion L.L. (US\$ 1,538 million) compared to 2005 or by 23 percent. These numbers are estimates and do not take into account total additional capital expenditures as estimated by CDR covering the rebuilding of destroyed houses and the complete restoration of the damaged infrastructure.

Box 2: Preliminary Impact of Israeli Offensive

The Israeli offensive against Lebanon has caused immeasurable destruction to the lives, livelihoods and infrastructure of its people. The hostilities have claimed over 1,100 civilian lives, left more than 4,000 people wounded, and displaced more than a quarter of the Lebanese population (close to one million people).

Since the cessation of hostilities, an estimated 500,000 internally displaced people have returned to their areas of residence, in addition to an estimated 150,000 from outside the country. Around 60-70% of returned individuals are currently occupying inhabitable houses. According to estimates by the Order of Engineers, the offensive has lead to the destruction of 30,000 housing and commercial units, mainly in the South and the Bekaa.

The scale and the scope of the damage to infrastructure have also been great. Direct bombardments have targeted all infrastructure sectors from transport, to electricity, telecommunications, water, health and education, directly affecting the livelihoods of hundreds of thousands of Lebanese citizens.

A preliminary assessment by the Council for Development and Reconstruction indicates that 137 roads have been damaged, and 107 bridges and overpasses have been damaged or destroyed. The impact on the health sector has been three-fold: damage to health facilities and infrastructure, lack of access and epidemic risks and exhaustion of supplies. The following table provides a damage assessment based on preliminary estimates from the Council for Development and Reconstruction.

Table 1: CDR Damage Assessment Figures By Field

	Total Damages (US\$ millions)
Transport	484
Electricity	244
Telecommunications	116
Water	80
Health and Education	34
Housing & commercial spaces	2,406
Industry	220
Military	16
Fuel Distribution Stations	12
TOTAL	3,612

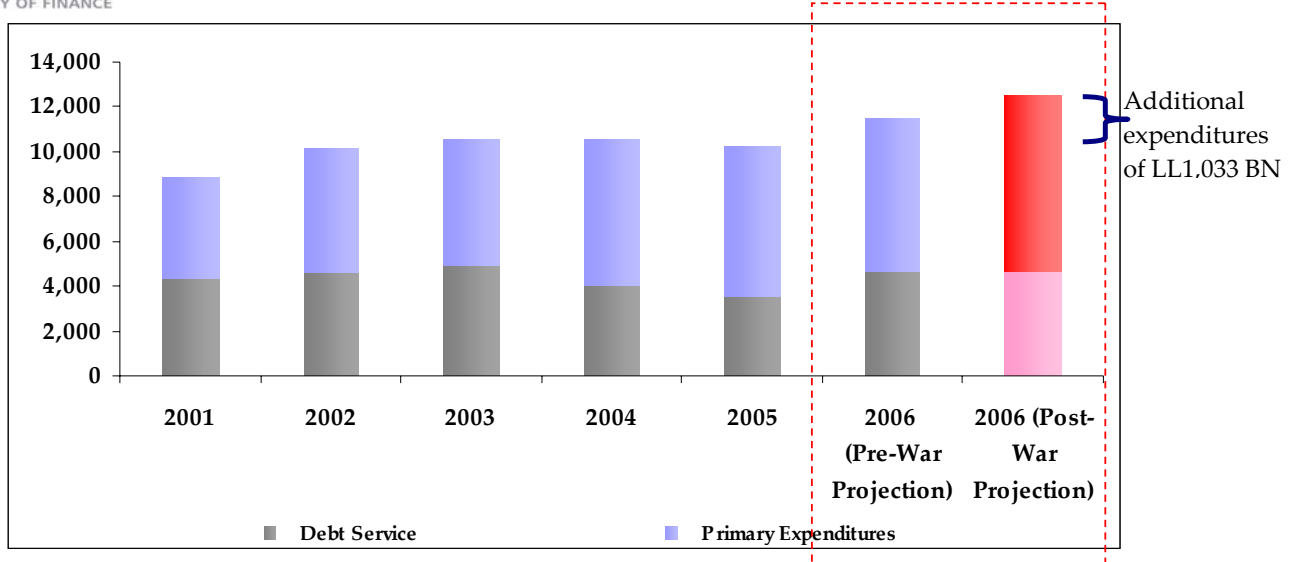
In addition, the Israeli offensive has brought about large environmental damage, due to the oil spill from the bombarded Jiyeh power plant, the widespread destruction that has resulted in massive waste amounts and the use of heavy bombs that have left toxin residues in the air.

³ Includes payments incurred by EDL for purchasing fuel oil and gas oil (Kuwait Petroleum Corporation and Sonatrach Petroleum Corporation.) from July – December 2006.



REPUBLIC OF LEBANON
MINISTRY OF FINANCE

Figure 4: Historical Expenditures and Pre and Post-War Projections



21. The projected increase in expenditures is mainly due to four reasons, namely higher military spending, relief costs, EDL, and reconstruction outlays.

22. In order to meet the requirements of UN Security Council Resolution 1701, military spending is expected to rise to accommodate sending 15,000 troops to South of Lebanon through calling back some of the reservists (retired personnel), in addition to new recruits. The main increases are expected to be reflected in military salaries and wages and other items namely “materials and supplies”, in addition to the rise in capital spending mainly for army-related equipment. The additional military expenditures are estimated at 105 billion L.L. (US\$ 70 million) during the remainder of 2006.

23. Expenditures related to relief efforts include hospital charges for war-related injuries, and expenses incurred by the High Relief Council to accommodate the needs of refugees and compensation for the deceased, injured and disabled. Such expenditures are expected to reach approximately 70 billion L.L. (US\$ 46 million) in the remainder of the year.

24. Initiating the reconstruction efforts particularly those pertaining to basic needs such as main roads, bridges, in addition to rehabilitation of schools and hospitals requires significant additional spending. As a result of these costs, additional capital expenditures are expected to reach a minimum of 500 billion L.L. (US\$ 33 million) in 2006.

25. Debt service expenses are not expected to be impacted by the July hostilities during 2006. Based on available data as of end of July, debt service in 2006 is

expected to reach 4,635 billion L.L. (US\$ 3,075 million), of which 2,375 billion L.L. (US\$ 1,576 million) is for local currency debt and 2,261 billion L.L. (US\$ 1,500 million) for foreign currency debt. The impact of the offensive on debt service will become evident starting 2007 when coupon payments are due for medium and long-term bonds.

26. Electricité du Liban is expected to incur significantly higher payments for the Treasury than initially projected during the remainder of 2006, due to the Utility's inability to cover these payments from its own resources after the damages it has incurred because of the offensive. The main expected payments include: (a) Payment of due amounts for the purchase of fuel oil and gas oil through agreements with Sonatrach (Algeria) and Kuwait Petroleum Corporation (Kuwait) estimated in the amount of 744 billion L.L. (US\$ 494 million) by the end of 2006; (b) Arrear payments for fuel importers in the amounts of 210 billion L.L. (US\$ 139 million); (c) Maturing concessional loans in the amount of 116 billion L.L. (US\$ 77 million).

27. The main impact of the offensive on expenses related to Electricité du Liban will be the Treasury's payment of the company's dues to Sonatrach (Algeria) and Kuwait Petroleum Corporation (Kuwait), due to the company's expected incapability to perform them. In fact, in July 2006, the Treasury paid US\$ 131 million (198 billion L.L.) of the US\$ 133 million (200 billion L.L.) total due for the month. The assumption that Electricité du Liban will not be able to meet its part of the payments is based on the fact that Electricité du Liban has suffered damages amounting to approximately US \$114 million (172 billion L.L.) in the areas of generation, transmission and distribution.

Table 5: Pre-War and Post-War Expenditure Projections (LL billion)

	2005	2006 (e)	2006 (e)	Change 2006	Change 2006 (%)
		Pre-War	Post-War		
Current expenditures, of which	7,925	8,961	9,010	49	0.55%
Personnel Cost	3,193	3,286	3,322	36	1.09%
Debt service	3,534	4,636	4,636	0	-0.02%
Consumption goods	213	165	173	8	5.01%
External services	82	90	90	-1	-1.01%
Other transfers	569	447	468	21	4.76%
<i>of which NSSF</i>	290	150	150	0	0.00%
Other current expenditures	258	261	252	-9	-3.53%
<i>of which hospitals</i>	192	213	230	17	8.13%
Capital expenditures	534	564	1,122	558	98.84%
Other treasury expenditures, of which	1,477	1,701	2,359	658	38.70%
<i>Electricite du Liban</i>	833	1,136	1,433	297	26.14%
<i>Municipalities</i>	384	314	354	40	12.73%
<i>Higher Relief Council</i>			50	50	
Total expenditures	10,203	11,490	12,521	1,031	8.97%

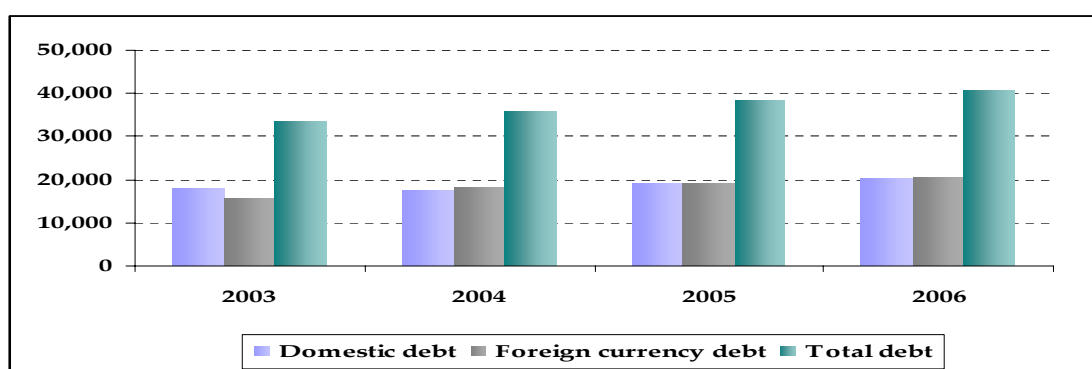
Source: Ministry of Finance

III – Debt Growth Trends till End 2006

28. Before the offensive, public debt was expected to stay below the 60,000 billion L.L. (US\$ 40 billion) mark at the end of 2006. This estimate did not take into consideration potential privatization revenues that would lower the debt stock. At the end of 2005, public debt stood at 58,031 billion L.L. (US\$ 38.5 billion).

29. The July 2006 offensive is expected to accelerate the growth of the debt owing to the expected increase in the overall deficit and the emergence of a primary deficit. The debt is therefore expected to reach 62,000 billion L.L. (around US\$ 41 billion) by the end of 2006.

Figure 5: Post-War Public Debt Growth (2003-2006)



30. The offensive against Lebanon has generated a decline in investor confidence, and has raised refinancing risks in both local and foreign currencies. The Ministry of Finance succeeded in the first half of the financial year in issuing US\$ 750 million and € 175 million worth of new Eurobonds, and in exchanging 71 percent of Eurobonds outstanding for 2006 (US\$ 1.7 billion). These issuances were executed at low coupon rates and long maturities⁴, despite high yield rates prevalent in international financial markets at the time. The Ministry of Finance was planning to issue new Eurobonds in the financial markets towards the end of July. Due to the unforeseen developments, the anticipated launch was not possible.

31. The Israeli offensive against Lebanon has lowered Lebanese Eurobond prices in secondary markets, and increased their yields. In fact, Eurobond spreads rose markedly when the conflict erupted, but have since declined. The average yield increased from 6.99% in end June to 7.63% on August 19.⁵ This is a change in the spread over the 6-month Libor from 135 basis points to 216, an increase of 81 basis points, during this period, reflecting the heightened risk associated with these

⁴ 7.375% for April 2014 maturity, 8.25% for April 2021 maturity and 5.875% for Eurobond in € of April 2012 maturity

⁵ Weighted-average yield from Blominvest Bank

bonds. The international rating agencies FITCH and Standard and Poor's have emphasized these risks by revising Lebanon's credit outlook downwards after the offensive.

32. The negative repercussions of this offensive, most notably the deterioration of the primary surplus and the emergence of a primary deficit, are expected to lead to a significant increase in the overall deficit, and thus to accelerated debt growth. Coupled with the reluctance of local commercial banks to purchase Treasury Bills, this will incur additional interest payments whose financial impact would start appearing by the first half of 2007 at the latest.

Box 3: Impact of July Offensive on Monetary Indicators

The Balance of Payments as of end July 2006 registered a surplus of US\$ 1,373 million as compared to US\$ 2,562 million as of end-June 2006. In July 2006, the balance of payments registered a deficit of US\$ 1,189 million due to a monthly US\$ 735 million deficit from Banks and the US\$ 454 million deficit from BDL.

The Dollarization level increased from 72.76% in June 2006 to 74.81% in July 2006. After Prime Minister Hariri's assassination the dollarization level peaked in March 2005 at 79.2% and then started to decline gradually in 2005 and 2006, to reach 72.52% in January 2006. The dollarization level remained almost stable until end-June 2006, to rise again due to July offensive.

Total private sector deposits were constantly increasing during 2006. However, by the end of July 2006 the trend reversed and private sector deposits registered 88,158 billion L.L. (US\$ 58 million) down from 91,408 billion L.L. (US\$ 61 million) in June 2006, a 3.55 percent decrease. As compared to July 2005, total private sector deposits are still higher by 8 percent. In May 2006 and June 2006 the growth rate of total sector deposits reached 1.43% and 1.55%, respectively. Note that in 2006 and before the offensive of July, the average monthly increase in total private sector deposits was about 1 percent.

Resident private sector deposits registered 74,061 billion L.L. (US\$ 49 million) in July 2006, decreasing by 2.42 percent as compared to the month before, and increasing by 8.57% year on year.

As for non-resident deposits, they amounted to 14,097 billion L.L. (US\$ 9,351 million) decreasing by 9.11% compared to the previous month, and increasing by nearly 5.1% year on year. In 2006 and before the offensive of July, the average monthly increase in non-resident private sector deposits was about 1.5 percent. Some resemblance can be inferred when comparing July 06 decline with March 2005, the month after Prime Minister Hariri's assassination, where non-resident deposits also decreased by 9.64%.

The M3 level in July 2006 was 1.89% lower than the previous month, and 7.98% higher than that of July 2005. After Prime Minister Hariri's assassination the M3 level also decreased by 1.5 percent when comparing March 2005 to February 2005.

Foreign exchange reserves ended the month of July 2006 at US\$ 10,563 million down from US\$ 11,020 million in June 2006, which was the highest level ever attained and constituted about 115 percent of imports.

Monetary indicators

<i>LL billion</i>	June 2005	July 2005	June 2006	July 2006	% change Jun-Jul 06
M3	70,301	71,358	78,540	77,054	-1.89 %
Bank Deposits	80,034	81,632	91,408	88,158	-3.55 %
Deposits of Private Non-residents	12,615	13,414	15,510	14,097	-9.11 %
Dollarization rate (%)	74.51%	73.95%	72.76%	74.81%	-205

Source: Banque du Liban

Appendix: Fiscal Data as of June 2006

Table A-1. Summary of Fiscal Performance

(LL billion)	2005	2006	2005	2006	Change	
	June	June	Jan-June	Jan-June	2005-2006	% Change
Budget Revenue	543	390	3,327	3,877	550	16.5%
Budget Expenditures	933	854	3,653	4,098	444	12.2%
<i>o/w Debt Service</i>	290	409	1,559	2,161	602	38.6%
Budget Deficit/Surplus	-390	-463	-327	-221	106	-32.4%
in % of Budget Expenditures	-41.8%	-54.3%	-8.9%	-5.4%		
Budget Primary Deficit/Surplus	-100	-54	1,232	1,940	708	57.5%
in % of Budget Expenditures	-10.7%	-6.4%	33.7%	47.3%		
Treasury Receipts	25	25	206	186	-20	-9.5%
Treasury Payments	190	189	1,214	1,132	-82	-6.7%
Total Budget and Treasury Receipts	569	415	3,533	4,063	531	15.0%
Total Budget and Treasury Payments	1,123	1,043	4,867	5,230	363	7.5%
Total Cash Deficit/Surplus	-554	-627	-1,335	-1,167	168	-12.6%
in % of Total Expenditures	-49.4%	-60.2%	-27.4%	-22.3%		
Primary Deficit/Surplus	-264	-218	224	994	770	343.6%
in % of Total Expenditures	-23.5%	-20.9%	4.6%	19.0%		

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

Table A-2. Total Revenues

(LL billion)	2005	2006	2005	2006	
	June	June	Jan-June	Jan-June	% Change
Budget Revenues, of which:	543	390	3,327	3,877	16.5%
<i>Tax Revenues</i>	499	335	2,493	2,882	15.6%
<i>Non-Tax Revenues</i>	44	55	834	995	19.3%
Treasury Receipts	25	25	206	186	-9.5%
Total Revenues	569	415	3,533	4,063	15.0%

Source: MOF, DGF

Table A-3. Tax Revenues

(LL billion)	2005	2006	2005	2006	
	June	June	Jan-June	Jan-June	% Change
Tax Revenues:	499	337	2,493	2,882	15.6%
Taxes on Income, Profits, & Capital Gains, of which:	219	51	691	771	11.6%
Income Tax on Profits	181	12	353	397	12.5%
Income Tax on Wages and Salaries	4	3	102	104	1.3%
Income Tax on Capital Gains & Dividends	14	7	54	66	22.2%
Tax on Interest Income (5%)	19	28	173	194	12.0%
Penalties on Income Tax	1	1	6	9	33.3%
Taxes on Property, of which:	33	39	178	398	123.7%
Built Property Tax	5	6	50	63	25.9%
Real Estate Registration Fees	23	28	112	156	39.6%
Domestic Taxes on Goods & Services, of which:	121	133	866	995	15.0%
Value Added Tax	106	114	783	886	13.3%
Other Taxes on Goods and Services, of which:	15	19	79	100	27.8%
Private Car Registration Fees	10	13	47	65	38.0%
Passenger Departure Tax	5	7	31	35	12.9%
Taxes on International Trade, of which:	109	93	648	569	-12.2%
Customs	38	47	228	254	11.2%
Excises, of which:	71	46	420	315	-25.0%
Petroleum Tax	36	0	233	90	-61.5%
Tobacco Tax	18	17	91	93	3.2%
Tax on Cars	18	29	95	130	37.9%
Other Tax Revenues (namely fiscal stamp fees)	18	20	110	148	35.0%

Table A-4. Non-Tax Revenues

(LL billion)	2005	2006	2005	2006	
	June	June	Jan-June	Jan-June	% Change
Non-Tax Revenues	44	55	834	995	19.3%
Income from Public Institutions and Government Properties, of which:	9	11	631	697	10.5%
Income from Non-Financial Public Enterprises, of which:	7	8	609	677	11.1%
Revenues from Casino Du Liban	4	4	31	21	-32.4%
Revenues from Port of Beirut	0	0	33	0	-100.0%
Budget Surplus of National Lottery	3	4	20	40	100.0%
Transfer from the Telecom Surplus	0	0	525	616	17.2%
Property Income (namely rent of Rafic Hariri International Airport)	2	2	19	17	-10.1%
Other Income from Public Institutions (interests)	1	0	2	3	16.8%
Administrative Fees & Charges, of which:	28	35	158	247	55.9%
Administrative Fees, of which:	23	29	125	196	56.3%
Notary Fees	1	2	8	10	19.9%
Passport Fees/ Public Security	8	10	40	59	46.6%
Vehicle Control Fees	9	10	55	94	71.9%
Judicial Fees	2	2	10	11	16.5%
Driving License Fees	1	3	6	13	103.1%
Administrative Charges	1	1	9	9	-3.8%
Sales (Official Gazette and License Number)	0	0	1	2	18.8%
Permit Fees (mostly work permit fees)	3	5	19	32	68.5%
Other Administrative Fees & Charges	1	0	4	9	141.8%
Penalties & Confiscations	0	1	2	3	77.0%
Other Non-Tax Revenues (mostly retirement deductibles)	7	8	43	48	11.2%

Source: MOF, DGF

Table A-5. Expenditures by Transaction Classification

(LL billion)	2005	2006	2005	2006	
	June	June	Jan-June	Jan-June	% Change
Total Expenditures	1,123	1,043	4,867	5,230	7.5%
Budget Expenditures	933	854	3,653	4,098	12.2%
Expenditures Excluding Debt Service	643	445	2,095	1,937	-7.5%
Debt Service, of which:	290	409	1,559	2,161	38.6%
Local Currency Debt	124	221	620	1,108	78.7%
Foreign Currency Debt, of which:	166	188	939	1,053	12.1%
Eurobond Coupon Interest*	148	147	814	916	12.4%
Specialbond Coupon Interest*		13		13	
Concessional Loans Principal Payments	14	23	74	78	6.2%
Concessional Loans Interest Payments	4	4	50	46	-9.3%
Treasury Expenditures , of which:	190	189	1,214	1,132	-6.7%
Municipalities	23	60	166	163	-1.7%
Previous Years' Appropriations	1	1	468	467	-0.1%
Non-Interest Expenditures (Total Expenditures minus Debt Service)	833	634	3,309	3,070	-7.2%

Source: MOF, DGF

Table A-6. Expenditures by Economic Classification

(LL billion)	2005	2006	
	Jan-June	Jan-June	% Change
1. Current expenditures	3,861	4,299	11.3%
1.a Personnel cost, <i>of which</i>	1,540	1,607	4.4%
<i>Article 13: Salaries and wages</i>	1,030	1,056	2.5%
<i>Retirement and end of service compensations</i>	416	446	7.1%
1.b Debt Service payments	1,559	2,161	38.6%
1.c Materials and supplies	121	71	-41.8%
1.d External services	43	53	22.0%
1.e Various transfers	434	247	-43.1%
<i>o/w NSSF</i>	290	100	-65.5%
1.f Other current	127	123	-3.4%
<i>Hospitals</i>	79	105	32.5%
<i>Others</i>	48	17	-64.1%
1.g Reserves (3)	37	38	3.7%
<i>Interest subsidy</i>	37	38	3.7%
2. Capital expenditures	269	336	25.0%
2.a Acquisitions of land, buildings, for the construction of roads, ports, airports, and water networks	3	11	252.6%
2.b Equipment	11	12	11.1%
2.c Construction in Progress	206	254	23.6%
2.d Maintenance	28	30	5.4%
2.e Other Expenditures Related to Fixed Capital Assets	21	29	37.5%
3. Other treasury expenditures, of which	713	579	-18.8%
Municipalities	166	163	-1.7%
EDL	295	151	-49.0%
Treasury advances for water authorities	48	0	-100.0%
Treasury advances for diesel oil subsidy	12	52	345.4%
Treasury advances for Telecom companies	15		
4. Unclassified expenditures	3	1	-73.3%
5. Customs cashiers	21	15	-29.8%
6. Total expenditures (excluding CDR foreign financed)	4,867	5,230	7.5%

Source: statement of account 36, cashier spending, Public Debt Department figures, Fiscal performance gross adjustment figures

Table A-7. Transfers to EDL

(LBP billion)	2005	2006	
	Jan- June	Jan- June	% Change
EDL of which:	434	151	-65.3%
Debt Service of which:	113	112	-0.6%
C-Loans and Eurobonds, of which:	113	96	-15.4%
Principal Repayment	77	68	-12.3%
Interest Payment	36	28	-21.9%
Loans for Fuel Oil Payment	0	17	100.0%
BDL Guaranteed Loan Payment	0	0	0.0%
Treasury Advance for Fuel Purchase	127	0	0.0%
Treasury Advance for EDL's Losses	55	0	0.0%
Material and Supplies (Electricity bills)	91		0.0%
Treasury advance to Water Authorities	48	0	-100.0%
Payments of Sonatrach and Kuwait Oil Agreement⁶	0	38	0.0%
Expropriations	0	0	0.0%

Source: MOF, DGF

⁶ These payments cover principles and interests in relation to KPC (Kuwait Petroleum Corporation) and Sonatrach Petroleum Corporation.

Table A-8. Public Debt Outstanding by Holder as of End-June 2006

Assumes full LBP Replacement	Dec-03	Dec-04	Dec-05	Jun-06	Change Dec 05 - June 06	% change Dec 05 - June 06
Gross Public debt	50,285	54,048	58,018	58,524	506	0.87%
Local currency debt	26,843	26,371	29,141	28,556	-585	-2.01%
a. Central Bank (including REPOs and Loans to EDL to finance fuel purchases)*	8,938	10,652	11,686	7,835	-3,851	-32.95%
b. Commercial Banks	12,303	12,220	14,130	16,910	2,780	19.67%
c. Other Local Currency Debt (T-bills)	5,603	3,500	3,325	3,811	486	14.62%
o/w Public entities	2,564	2,187	2,446	2,957	511	20.89%
Foreign currency debt	23,442	27,677	28,877	29,968	1,091	3.78%
Ratio to total debt	46.6%	51.2%	49.8%	51.2%		
a. Bilateral, Multilateral and Foreign Private sector loans	2,934	2,970	2,822	2,892	70	2.48%
b. Paris II related debt (Eurobonds and Loans)	3,731	3,814	3,682	3,748	66	1.79%
c. BDL Eurobond (Paris II)	2,819	2,819	2,819	2,819	0	0.00%
d. Market Eurobonds	13,631	17,686	18,729	19,684	955	5.10%
e. Accrued Interest on foreign currency debt	327	388	406	406	0	0.02%
f. Special Tbls in Foreign currency**			419	419	0	0.00%
Public sector deposits	3,019	4,360	5,590	5,153	-437	-7.82%
Net debt	47,266	49,688	52,428	53,371	943	1.80%
Gross Market debt***	29,638	31,861	34,759	38,451	3,692	10.62%
% of total debt	59%	59%	60%	66%		

Source: Ministry of Finance, Banque du Liban

Notes:

* BDL has extended loans to EDL for the equivalent amount of US\$ 300 million to purchase fuel oil. These loans are listed as Public debt as they are government guaranteed.

** Special Tbs in Foreign currency (expropriation bonds)

*** Gross market debt equals gross debt less the portfolios of the BDL, NSSF, bilateral and multilateral loans, and Paris II related debt.

**** Figures of Dec03- Dec04 -Jan06 change because of exchange rate of Euro