1,274 pages in 15 pages: The McKinsey Report in a Nutshell

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Abstract

The purpose of this study is to present the now-popular 1,274 page McKinsey report in an illustrative, user-friendly, and shorter version that focuses on the key takeaways for Lebanon's economy and its future potential. This paper aims to render the findings appreciated by economists or policy-makers, but also by citizens, avid readers, students, researchers interested in keeping-up with Lebanon's economic diagnosis.

The original report was thrust centre-stage last month, becoming part of the Lebanese policy-making, the reason why this study will present an overview of McKinsey's line of thought in all 8 sections of the report, for an accurate picture of most content and key findings. However, the paper strictly elaborates on 4 core sections of the McKinsey which we judged are "of utmost relevance" to the priorities of the newly-formed government. The highlighted sections are: "The Vision: Lebanon's Economic Aspirations", "The [six] Sectoral Engines for Lebanon's economic growth" (i.e. the most productive sectors), "Required Enablers to support the aspirations", and the "Flagship projects", as per McKinsey.

This report stays true to the findings of the original McKinsey Report throughout, but it also adds and concludes with the authors' take on some approaches and/or findings.

Context

Overview: The 8 sections of the McKinsey Report

The report frames its findings under 8 sections. The study begins with an executive summary and introduction, followed by a macroeconomic evaluation of Lebanon's economy and its evolution which concludes that Lebanon is caught in a "*vicious economic cycle*". The section further presents a detailed sectorial diagnosis across 15 industries, from which McKinsey's national "*Vision 2025*" for Lebanon is derived.

The chapter delineating the Vision calls for a multi-dimensional, long-term growth instead of 'short term fixes'. In fact, this notion of sustainable growth according to McKinsey's presentation, and other international entities before it, is obtained by tackling the root of Lebanon's economic woes. In this chapter, McKinsey proposes to drive economic growth by revamping & prioritizing six "*sectoral engines*" known as the economy's "productive sectors". As such, the Vision entails "economic targets" and "focus-sectors targets", "priority" projects, and key performance indicators ("KPIs") to track the country's progress on the medium- and long-term. In addition, "government enablers", as per section six of the report, are also an essential portion of the Vision - to make sure all economic and sector specific reforms receive the indispensable government backing via an attractive business climate, public sector efficiency, improved infrastructure and prioritization. In section seven, *McKinsey* presents the institualization mechanisms needed to orchestrate stakeholders' roles in the Vision and to track the progress in implementation. In its final section, the report concludes with 3 specific "flagship projects" that Lebanon "*must immediately adopt*" to jumpstart the economy.

This study presents the line of thought used in the entire report, but elaborates on 4 chosen sections. We identified the bold sub-sections of the adapted McKinsey report below as "essential" and we therefore detail & analyze them in the following sections:

I. Executive Summary
II. Introduction and methodology
III. Context and Diagnostic
    a. Economic perspective
    b. Sector Diagnostics (15 sectors covered in detail)
    c. Institutional and policy enablers (in focus)
IV. The Vision: Lebanon's Economic Aspirations for 2025 and 2035
V. Sectoral Engines for Lebanon's Economic Growth
VI. Required enablers to support the aspirations
VII. Institutionalization Mechanisms
VIII. Flagship projects

In a nutshell: Lebanon's Macroeconomics

McKinsey's 'vicious economic cycle' explores in great detail the key macroeconomic challenges of Lebanon. In fact, a version of Lebanon's key economic parameters in 2018, equally accurate and comprehensive, are summarized in our BLOMInvest study: "The Lebanese Economy in 2018: Time for Drastic Reforms" available on our public corporate blog. Similarly, McKinsey sheds light on the un-tackled macroeconomic parameters, persistent corruption, pending business environment laws and legislations stuck at different stages of the pipeline for 5-10 years, alongside a highly volatile growth, and a reliance on diaspora inflows not channeled into 'productive' sectors rather add to the government's indebtedness. McKinsey then offers its sector-by-sector analysis of Lebanon's 15 core industries: • Oil & gas • Agriculture •

Industry • Tourism • Knowledge-economy • Financial services • Education • Healthcare • Real estate & construction • Retail & commerce • Logistics & transportation • Telecommunications • Power & water • Diaspora • Urban efficiency - of which 6 resurface later in Section "V." of the report, detailed hereafter as "sectoral engines".

The McKinsey "Vision"

McKinsey delineates a "vision", which represents economic aspirations set for Lebanon. The Vision has underlying general economic targets, priority initiatives, & key performance indicators (KPIs) to monitor the country's progress on the medium- and long-term. To overcome the economic challenges, Lebanon should adopt and develop a mid-to-long-term horizon Vision 2025, complemented by long-term Vision 2035.

In a nutshell, the 2025 "economic targets" for Lebanon entail the following: • Lift GDP growth from current (2017) 1% to 6% on average by 2025 i.e. a real GDP at $80B • Create~370,000 new domestic jobs by 2025 • Reduce Unemployment (UE) from current 25% to 8% • Reduce public debt to GDP: from 145% currently to 110% through "*privatization & deficit reduction*" • Reduce the Fiscal deficit from 8% to 3% of GDP via restrained spending, cut subsidies, fighting corruption, boosting resource-mobilization, improving collection • Balance of Payments (BOP) surpluses at approx. 10% of GDP by 2025 • Decrease the time limit for passing legislations: from 2+ years to 6months by 2025.

Vision 2025 entails a jumpstarted "productive economy" and an overhauled business climate. McKinsey pushes for sector prioritization and directing the government's existing resources towards these "priority areas". The "key success factors" of this vision can be summarized as follows:

a. **Productive Sectors:** An "integrated" national vision will reignite the productive economy and improve the business climate. This goes hand-in-hand with diversifying the economy, thereby reducing the current growth volatility linked to external factors while nurturing that nation's self-efficiency.
b. **Business Environment:** Fix the framework of economic competitiveness to render a conducive business environment and rehabilitated infrastructure (through relaxing the costs of doing business, fighting corruption).
c. **Government enablers:** Ensure a healthy public sector alongside efficient management of public finances via fiscal discipline, improved collection, rational spending.

Other targets in the Vision include improving Lebanon's global ranks on several indices and boosting 'sectorial' contribution to GDP. For example, on the Corruption Index, the vision aims to make Lebanon 50th of 180 countries, up from 146th • Ease of doing business (EODB) index: from 133rd to 30th of 190 countries by 2025, among other indices • Most importantly, increase the Productive sector contribution from: 14% to 25% by 2025, as detailed in the next table.

By 2035, the Lebanese economy is envisioned as a "*high income, diversified economy with a unique economic imprint and competitiveness*". Even though most 2035 targets and KPIs are to be determined by 2025, Lebanon's "productive sectors" by then will be areas of excellence, while the country enjoys a healthy macroeconomic position ("government enablers") that can influence neighboring economies.

A crucial element McKinsey emphasizes in both visions are "key performance indicators (KPIs)". According to McKinsey it is indispensible to track the country's progress on the sought-after pillars. Therefore, specific KPIs are crucial to testify for the country's progress (or lack thereof) on the different tackled dimensions.

Sectorial Highlights: McKinsey's "productive sectors" & Required "Enablers"

General Targets: from 2017 to Vision 2025 & 2035

	GDP in real 2017 prices	Job creation	Additional industry-specific Target
Industry	\$4.6B to \$8B to \$11.7B	185K to 240k to 250k	-
Agriculture	\$1.6B to \$2.2B to \$3.2B	210k to 214k	-
Tourism	\$1.6B to \$3.7B to \$5.4B	89k to 185k to 211k	**Total Nb. Of Tourists** 1.9M to 4.2M to 6.5M
Knowledge economy	\$1.4B to \$3.8B to \$5.6B	44k to 105k to 123k	**Innovation capacity** Rank: 58 to 30 to 15
Financial Services	\$4.8B to \$7.8B to \$11.4B	50,000 to avg. 50,000 in 2025/35	-

Source: BLOMInvest Bank; McKinsey Report, 2018

McKinsey identifies six sectors as the "engines" of economic growth. In Section "V." of the report, these 6 core sectors according to the experts are: Agriculture • Industry • Tourism • Knowledge economy • Financial services • Diaspora. The analysis begins with a summary of the sector's contribution to GDP and relevant performance metrics. It then highlights the sector's main challenges and accordingly, it chooses the key performance indicators (KPIs) and "enablers" that can drive growth.

Three criteria identified McKinsey's "productive sectors" as growth-drivers. The first criterion is "historical performance". McKinsey referred to the sector's contribution to GDP and relevant performance metrics in a summary diagnostics. "Assessing the size of the emerging opportunities" was the second criterion used by McKinsey, whereby the firm highlights the sector's main (current) challenges and accordingly, it chose key performance indicators (KPIs) for the sector. Using the third criterion, "global and/or regional trends in that sector", McKinsey complemented its diagnosis and KPIs with indispensible government "enablers" needed to enforce the sectorial growths so that the results fit the Vision of Lebanon's bold macroeconomic and sectorial aspirations.

McKinsey requires Lebanon to launch around 160 priority initiatives across the 6 "productive" sectors. As per the report, these initiatives will help guide the Lebanese government in the implementation of the "Vision 2025" and in monitoring of the country's progress, enforcing accountability and commitment through the KPIs. The initiatives would also ensure "balanced regional development" in different regions of Lebanon whereby each area would act as a "hub" of some sort for one or more of the 6 productive sectors, thereby driving growth.

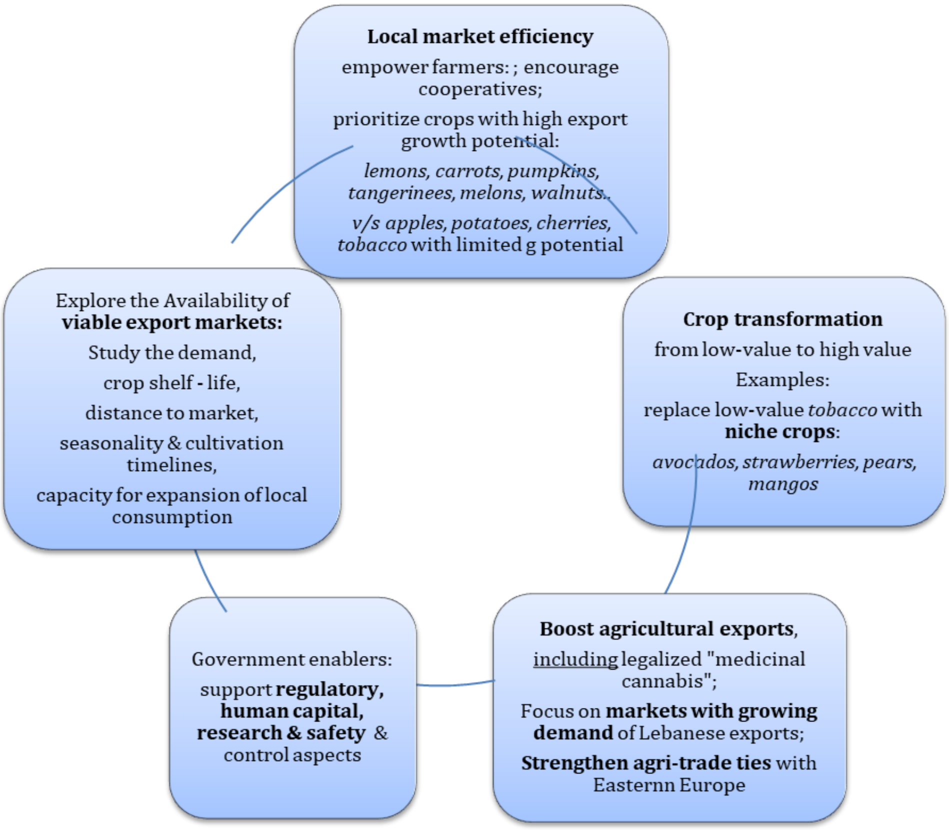
In details, the original report presents the 6 sectors following one structure. • Aspiration statement for the sector • Weaknesses (current performance) • Sector charter & Priority targets (found hereafter as easy-to read illustrative Diagrams) • General targets (contribution to GDP) • KPIs (which can be new or existing targets).

For ease of analysis, the sector priorities and aspiration are summarized in illustrative diagrams, while the main KPIs per sector are summarized in one table hereafter. From the key priority initiatives per sector in the user-friendly charts, the reader can immediately infer the sector's key weaknesses, as per McKinsey, as well as the main sectorial findings and essential KPIs to be tracked as suggested by McKinsey. A table summarizing the major KPIs to be used per sector also follows.

1. Agriculture

Aspiration: "*A high value and quality sector generating sustainable wealth for farmers and rural communities*." (McKinsey Report, 2018)

15 Priority Initiatives & top sector charter summarized below:

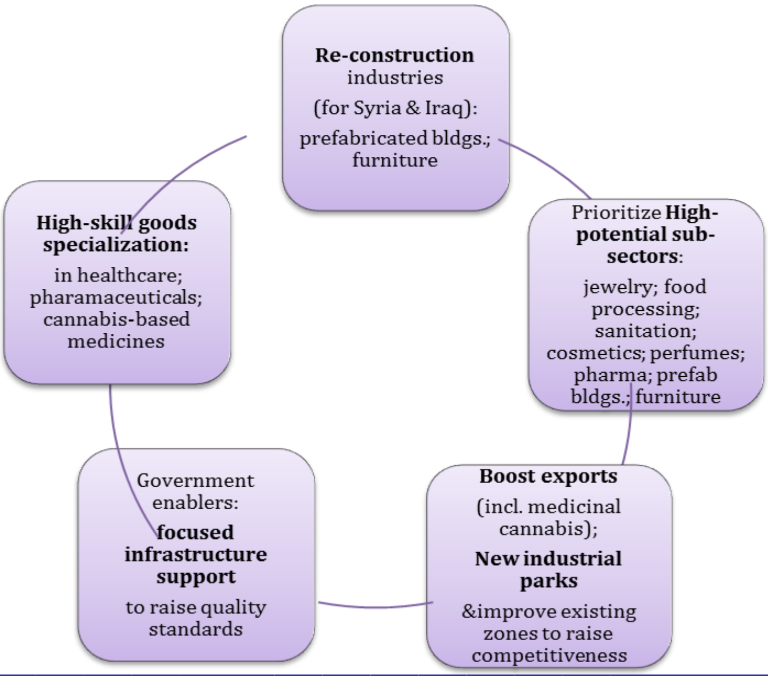


Source: BLOMInvest Bank; McKinsey Report, 2018

2. Industry

"A niche regional leader in creative and high-value industries and hub for regional processing".

12 Priority Initiatives & top sector charter

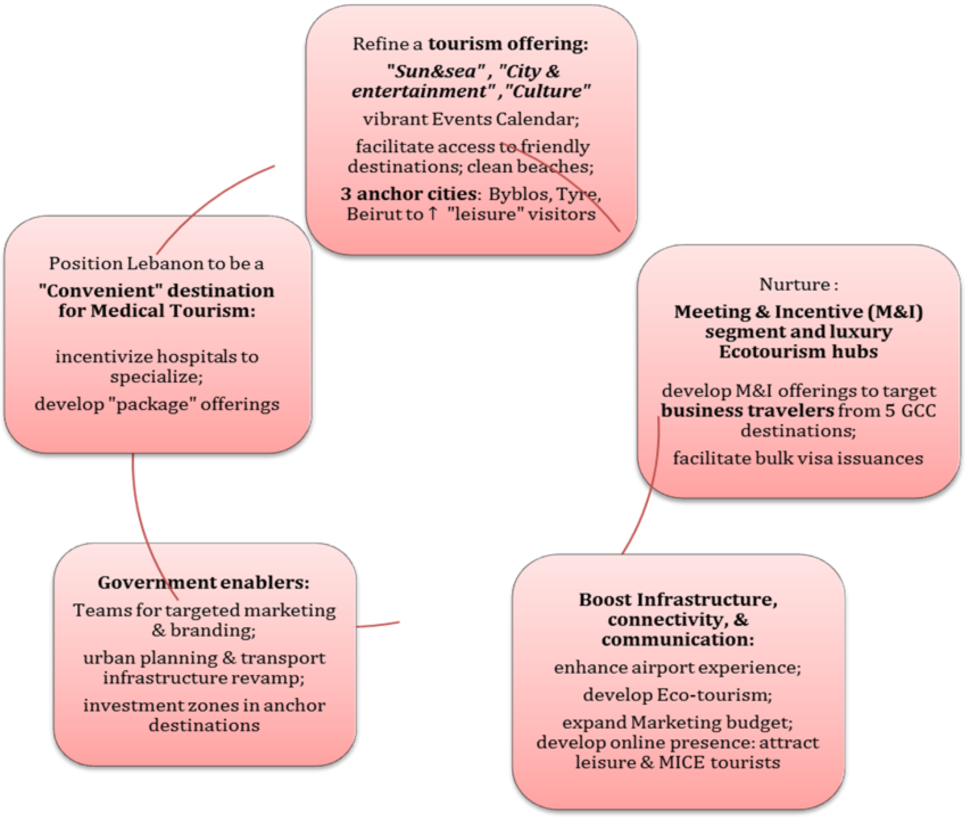


Source: BLOMInvest Bank; McKinsey Report, 2018

3. Tourism

"A revived Riviera destination offering […] unrivalled entertainment, immersive culture, & breath-taking sea- views with regional niche offerings in business and specialized medical tourism."

22 Priority Initiatives & top sector charter



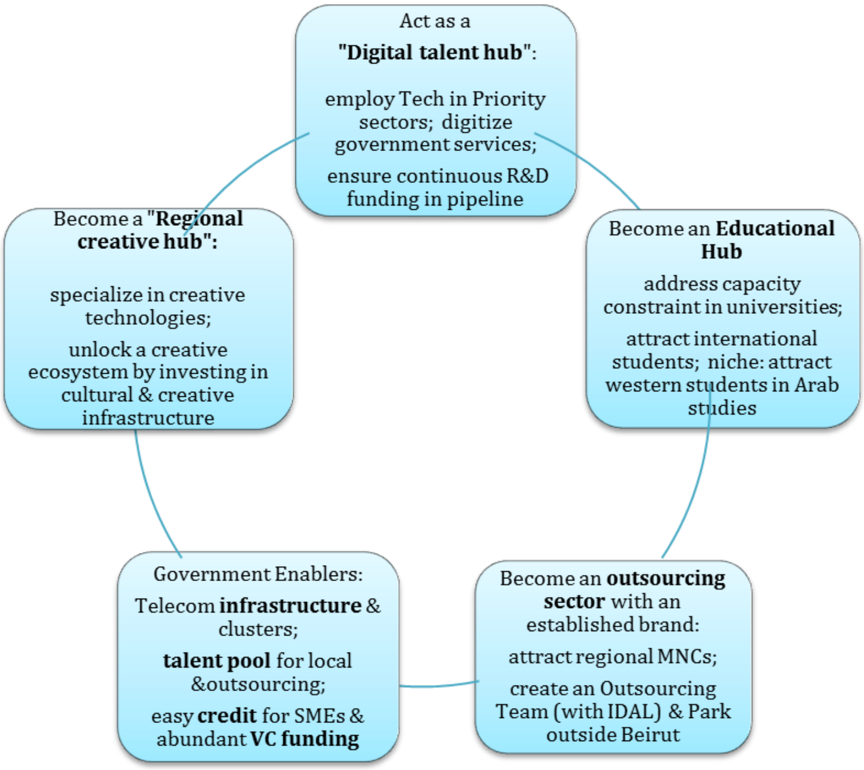
Source: BLOMInvest Bank; McKinsey Report, 2018

It is worthy to mention that the largest number of KPIs, 28 to be exact, was set for each of the Financial services and the Knowledge economy sectors, followed by 22 priority initiatives for Tourism.

4. Knowledge economy

"A knowledge-intensive and digital nation, at the forefront of innovation, acting as a talent hub for technology, outsourcing, creative industries and education".

28 Priority Initiatives & top sector charter

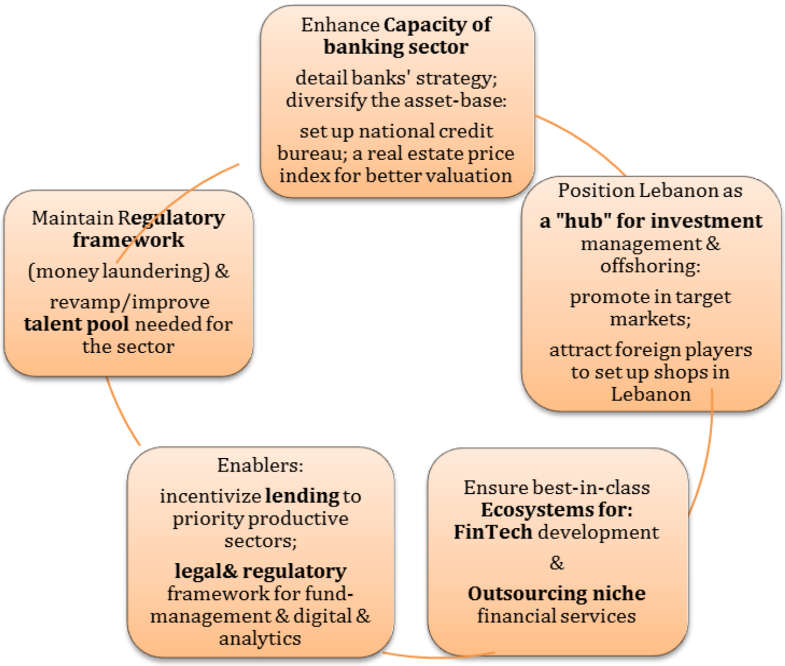


Source: BLOMInvest Bank; McKinsey Report, 2018

5. Financial Services

"... Becoming an "investment management & offshoring hub" while providing exportable centers of excellence across niche services, building on strong and resilient sector foundations".

28 Priority Initiatives & top sector charter

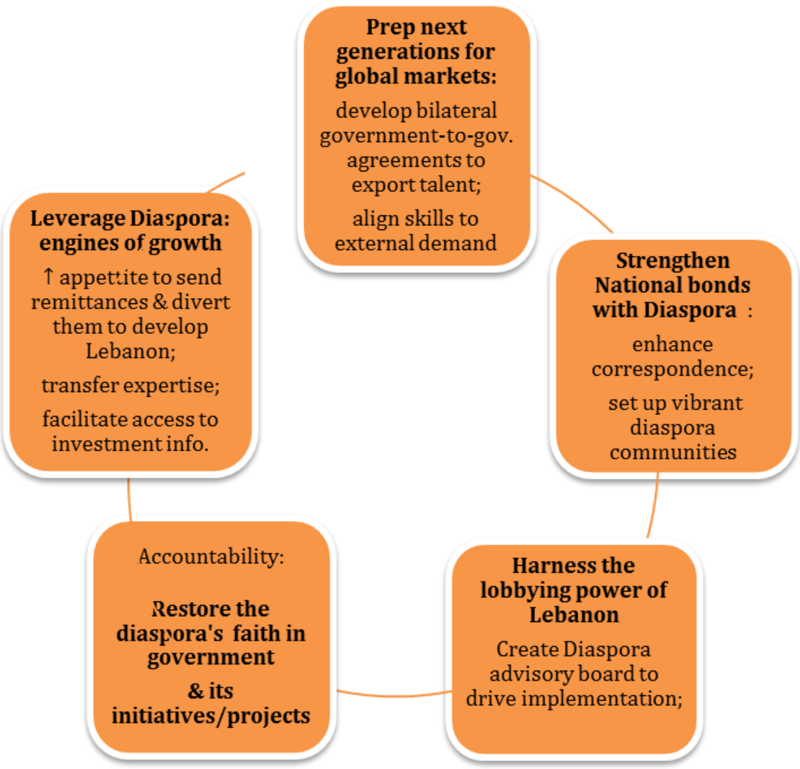


Source: BLOMInvest Bank; McKinsey Report, 2018

6. Diaspora

"A proactive emigration policy, with a highly engaged Lebanese diaspora actively contributing to Lebanon's economic and social development"

16 Priority Initiatives & top sector charter



Source: BLOMInvest Bank; McKinsey Report, 2018

McKinsey's Main Key Performance Indicators (KPIs) per "productive" sector: 2017 v/s 2025 Targets			
Sector	KPI #1	KPI #2	KPI #3
Agriculture	**Agricultural Exports:** ↑ from \$175M to \$750M	**Land transformed to "high-value" crops:** ↑from 0 to 10,000 hectares	**New Metric needed: "Farmer Satisfaction"** (In %)
Industry	**Nbr. of functioning Industrial zones**: ↑from 0 to 6+	**Exports of "Prioritized Goods"**[1] \$828M to \$1,790M	-
Tourism	**Attract "Leisure" Tourists:** (from 15 countries) ↑ from 1.9M to 4M	**"MICE" Tourists:** N/A to 200,000 **"Medical" Tourists:** ↑ from 20,000 to 40,000	**Nbr. of hotel rooms in anchor destinations** ↑from 7,000 to 11,000 -14,000
Financial Services (Numerous KPIs set; 1 from every Priority initiative is chosen.)	**Assets under Management (%GDP)** ↑from 14% to 30% **Stock exchange market cap (%GDP)** ↑from 24% to 60%	**Non-Banking Assets (%GDP)** ↑from 21% to 33% **Global Financial Centre Index (Rank):** N/A to Top 50	**Bank Sovereign Exposure** ↓from 50% to 37% **Nbr. of Fintech** ↑from 15 to 45
Knowledge Economy	**Nbr. Total startups:** ↑from 200 to 2,000	**Yearly R&D spending(\$M)** ↑from 50 to 290 **Total Revenues (\$M)** ↑ from 82 to 906	**Nbr. Int'l students:** ↑from 8,000 to 16,000 **Nbr. Outsourced jobs** ↑from 5,000 to 30,000
Diaspora	**Nbr. of Government-to-Government Agreements** N/A to 10	**Yearly Nbr. of Diaspora Projects** (hotels, factories) N/A to 30	**Diaspora covered in official Directory** N/A to 50 - 60%

Source: BLOMInvest Bank; McKinsey Report, 2018

[1] These include: food processing, furniture, napkins & sanitation, perfumes & cosmetics, pharmaceuticals, prefabricated buildings, soaps & sanitation. *(Source: McKinsey Report, 2018)*

Core Enablers to Support Sector Aspirations

Particular government "enablers" are required to accompany McKinsey's 160 sectorial priority initiatives and pass on urgent legislation. The "institutional and/or policy enablers" are identified by McKinsey as indispensable for sectorial KPIs and sectorial charter/priority initiatives. McKinsey believes these enablers will accelerate the approval of 11 crucial legislations needed in the country to enhance the non-conducive business environment. These are namely: the critical *Code of commerce* revamping, *Bankruptcy law* and the *Closing of a business*.

The enablers can be summarized under 5 fronts. The enablers are: Fiscal policy, Monetary policy, the Ease of doing business in Lebanon, Economic development activation, and Trade & international agreements. These are mentioned throughout the report, with a focus on Lebanon setting achievable but ambitious goals on them. Success stories from governments around the world improving each set of enablers are also mentioned in the report.

Infrastructure is a first key enabler and 11 CIP projects are priority to fit the McKinsey Vision. According to the McKinsey report, the CIP projects should be prioritized to fit Vision 2025 and its aspirations. In fact, 11 CIP projects valued at $3.4B are essential and priority according to McKinsey. These include: the core power projects, expanding Beirut-Tripoli ports, the Fiber network deployment, the industrial zones construction (Tripoli) and in additional zones, the Beirut knowledge "*hub park*", and the urban improvement of Tyre, Byblos, and Beirut.

The reform of the public administration is also key for the Vision. These enablers entail: fighting corruption, digitizing the government and boosting productivity. Moreover, fiscal policy enablers would include a spending framework that eliminates 1% of fiscal deficit annually, while boosting revenues and collection for the government.

Accelerating legislation to improve the business environment and enablers on **country Branding & export promotion are crucial.** McKinsey calls for cross-cutting urgent legislations in the Code of commerce, competition law, closing a business, bankruptcy law and in sector-specific legislations, such as passing 4 agriculture laws, 4 in each of the tourism sector and knowledge economy, 2 laws in financial services and 1 in the industry sector. Moreover, close collaboration among all stakeholders is indispensible for optimal impact and results from the productive sectors.

The "Quick Wins" suggested: McKinsey's Flagship projects

McKinsey suggests 3 projects must be launched "*immediately*" to jump start the momentum of the Vision. Besides the long term growth sought in the Vision, McKinsey suggests 3 initiatives to be launched "*immediately*", to jump start the momentum of the Vision for Lebanon, while the overhauling works begin on the country's promising potential of the identified productive sectors.

1. **Construction technology zone:**

The reconstruction cost is valued at approx. $100-300B, and industrial construction can carry value to Lebanon. The project on the border with Syria aims to capitalize on Lebanon's proximity to Syria and the ongoing reconstruction in the country and in Iraq as well. The reconstruction is mainly advised via pre-fabricated housing for millions of returning refugees, given the estimated required reconstruction ranges between 200-300k homes per year and Syria's domestic construction can only meet an estimated 20-30% of total demand.

This will carry a comparative advantage to Lebanon mainly because of the country's:

- Geographic proximity
- Availability of high skilled labor: Architects, engineers, and their deeper understanding of Syrians' preferences due to similarity of preferences
- Strong cultural and language ties.

Industrial construction[2] is preferred saves cost and time, albeit being more productive and maintaining high quality. Moreover, Lebanon would capture reconstruction value by creating high-skill employment opportunities as jobs move from on-site to factories inside Lebanon. In addition, prefabricated material in Lebanon, according to McKinsey, is one of the fastest growing exports so the sector is considered well established. Besides, the industrialized construction takes less time to completion, reduced cost, and requires fewer personnel yet is more productive.

An industrial construction zone can help attract players across the value chain. For example, the suggested zone on the border for example in El Qaa region would bring together real estate developers, architects/engineers, suppliers, manufacturers of industrial input, distributors, tech provides, sales entities.

2. **Tourism end-to-end journey**

This project entails an overhauled airport experience to tourists from pre-arrival to departure and post-departure services. This can tackle the challenges of tourists in pre-arrival, at arrival, in-country experience, upon departure, and encouraging return or referrals especially through social media channels. The initiative entails expanding the airport capacity, better managing customs control and queuing, taxi, public transport, maintenance of cultural sites, unclear check-in process, aftercare services that can encourage tourist referrals, returns, and data collection/integration to fortify and drive decision-making.

3. **"Smart Lebanon" knowledge hub**

Hosting creative technology, for licensing and clusters in Lebanon can enhance its competitiveness. As per McKinsey, from global experience, hubs can drive more innovation, healthy competition, boosts future

[2] Industrial construction: the report defines it as a sector that entails, "large-scale, centralized production of units using automated and optimized industrial technologies that allow for integration across the value chain."

productivity, better access to talented pool, reduces transport costs, and enhance competitiveness. The hub in Lebanon will entail: physical and virtual clusters, infrastructure that serve as the flagship of the country's knowledge economy agenda.

Final thoughts: Our Observations & Comments

KPIs have historical evidence of helping countries keep track of progress (deterioration). In general, KPIs are considered as booster of governments' transparency and accountability amid economic or socio-economic overhauls. McKinsey details KPIs per sector and elaborates in depth. In fact, KPIs have proved to be a useful tool for countries in distress or in trouble. When they requested the assistance of the International Monetary Fund (IMF) for instance, countries like Egypt, Cyprus, or other European states post-the 2008 global crisis (Ireland, Portugal, Greece, Iceland, etc.) were dispatched IMF packages (conditioned financial assistance), which came with a set of periodically reviewed country KPIs. Doing so allowed the IMF to keep track of socio-economic progress and enabled the country itself get back on track, or require further assistance at times of slow progress. As such, KPIs served as a constant reminder or whistleblower of the need for concrete action, results, or for needed re-adaptation of set targets according to the country needs.

In fact, the McKinsey report emphasizes sectorial KPIs for each of the 6 growth engines of Lebanon. As explored in-text, the original report emphasizes detailed KPIs per productive sector. The notion of KPIs is essential to set a timeframe for a potential resolution(s), as well to track the government's willpower and accountability through measuring essential targets reached (or missed) to readapt and re-tailor alternate ways to move forward in the next phases. And this has indeed proved useful when it comes to tracking the performance of international economies after the dispatch of an IMF package to them.

Lebanon needs to tackle the root problems of its economic woes, not quick fixes. The McKinsey report brings forth Lebanon's known corruption, fiscal woes, high debt, and inefficient public administration among other weaknesses. However, it also presents the drastic reforms we need in Lebanon at this point, as referred to in our 2018 BlomInvest report on Lebanon.

Some of McKinsey's targets are too ambitious, but the assessment of an "outsider" can entail "key takeaways" for the Lebanese government. Perhaps McKinsey's perspective on the Lebanese economy represents an external viewpoint, given it is a bit more detached from local political constraints and political bickering embedded within the economic canvas of the country. Indeed, some of the suggested targets are too ambitious, while some of the policy prescriptions are unrealistic or numerous, but the assessment is that of an "outsider" and can represent "key takeaway" for the Lebanese government.

"Key takeaways" from such a detailed report can trigger national dialogue and self-made policies, given national leaders know the country intimately. Key lessons can be learned from the report and they can empower Lebanon's government to call for dialogue or suggest policies it can accommodate, knowing the vulnerabilities of the country more closely than any external party. The Lebanese political leaders can infer main takeaways from the presented analysis. McKinsey actually details weaknesses and targets and presents global or regional examples of success stories that Lebanon can aspire to emulate. In fact, McKinsey's vision on the country's productive sectors calls for a national dialogue between the private sector and the government. Being so, the Lebanese can therefore come up with their own vision and policies to reach the end results suggested by McKinsey.

An interesting observation is that McKinsey righteously focuses on "productive" sectors to ensure sustainable growth, while leaving out real estate. Productive sectors can actually jumpstart economic and business cycles in a country because they involve multiple stakeholders, including the national labour market, financial systems, and the public sector in terms of needed capital spending. Traditionally, Lebanese plans have focused on localized, and/or short-term boosts to a particular arm of the economy over another. A case in point is how huge efforts in Lebanon are still focusing on incentives to lift up the real estate (RE) sector. On the contrary, McKinsey does not highlight RE as a productive sector and an engine of growth at this point. By doing so, the report highlights some false Lebanese misconceptions about certain sectors and their usefulness, to carry Lebanon out of its current national economic slowdown.

Moreover, the legalization and export of "medicinal cannabis" in the report was only one measure of many others suggested to drive growth from Lebanon's agricultural sector. The buzz in the Lebanese media on the McKinsey report came strictly around the "legalization of cannabis" for medicinal export purposes, even though it represents only one recommendation of many others. The report also classified Lebanon's agricultural sector as a "productive engine" (visit 'agriculture' diagram page 6 of the previous section). As such, *McKinsey* thoroughly analyzed the sector, assigning multiple KPIs and priority actions. Besides medicinal cannabis export, the report's suggestions included action to introduce technology and modern techniques into agriculture, to substitute low-value crops with high value ones, to focus on the export of crops with rising demand and to prioritize high growth export-markets. McKinsey also presented successful global agricultural models used by other countries, which can act as a mere guide for Lebanon's future models of success.

However, the McKinsey Vision does not account for the regional context, instability, or Lebanon's exponential refugee crisis when it compares it to some countries or their growth models. Lebanon is located in a region that has its own specificities. It is surrounded by war zones and by ongoing conflicts like the Israeli-Palestinian, among others, which can introduce changes to the timeframe set for reform and even to some targets set. For instance, McKinsey's classification of countries like Switzerland, among others, as "similar to Lebanon" in terms of similar small territory and limited population, is a flawed comparison because Lebanon is actually the 2nd largest recipient of Syrian refugees in the MENA region, with national officials and the World Bank estimating total refugee population at least at 1.5M by 2017 including non-registered Syrians, and more than 40,000 Palestinians from Syria. Similarly, McKinsey's reference to global, successful models used in the productive sectors of different European (or other) countries must account for changes in the achievements across a timeframe that goes with Lebanon's specificities. Yet, aspiring to successful worldwide models can serve Lebanon well in tailoring its own models and targets and aspire to the success of others while at it.

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