IIF: Lebanon at a Crossroads – Navigating Limited and Deep Reform Paths

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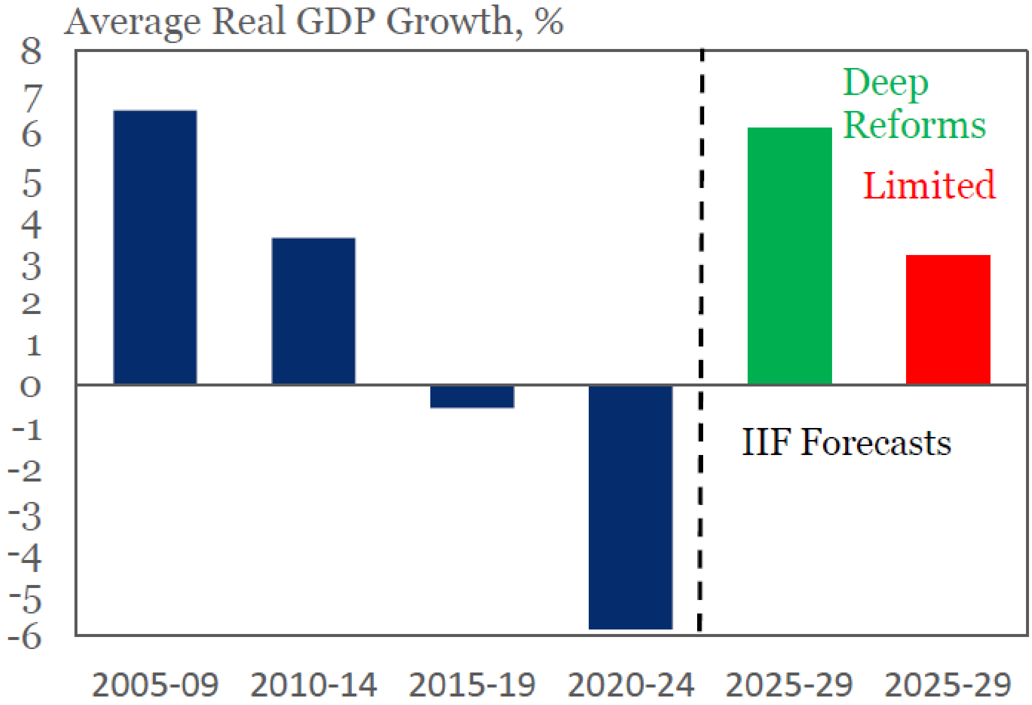
Lebanon has faced a multitude of crises since 2019, ranging from financial collapse and political instability to a devastating war that continues to inflict damage. Consequently, the economy contracted by a cumulative 38% from 2018 to 2024, with the Investment to GDP ratio plummeting from around 21% in 2018 to below -9% in 2024, according to the Institute of International Finance' s (IIF) calculations. Recently, some corrective measures have been taken. The exchange rate has stabilized, a ceasefire with Israel has been implemented, and the election of a new president, a new prime minister, and a new cabinet, believed to be pro-reform, has given some hope. However, poor governance, political and sectarian divisions, widespread corruption, and mismanagement of public policy continue to hamper potential reforms. Despite these challenges, the IIF' s Research Note on Lebanon, titled 'New Era: The Urgency for Deep Reforms' (February 16, 2025), asserts that there remains hope for Lebanon' s future. The report anticipated two equally probable outcomes: a limited reform scenario and a deep reform scenario.

In its **limited reform scenario**, the IIF predicted that the newly elected governmental leaders will encounter various obstacles, such as the delicate relationship with Hezbollah, making it harder to abide by the ceasefire agreement and UN Security Council Resolution 1701. The parliamentary elections set for May 2026 are important, but political parties still present in the current parliament might keep getting in the way of needed economic reforms until then. If no major political transformation occurs in the forthcoming Parliamentary elections, it is improbable that the new Cabinet and President will successfully implement deep reforms and decrees in the parliament. Thus, securing an IMF-supported economic program will remain out of reach, and international aid will predominantly consist of humanitarian assistance, insufficient to meet even half the financial requirements for reconstruction.

In this scenario, the economy is projected to grow at an average rate of only 3% between 2025 and 2029, with the market exchange rate continuing to weaken and inflation possibly rising again. The current account deficit is expected to stay at a high level, ranging from 9% to 10% of GDP, and foreign exchange reserves may gradually decrease from $10.1 billion by the end of 2024 to slightly below $7 billion by 2029. Moreover, a greater proportion of deposits will remain out of reach.

Exhibit 1: Real GDP growth averages 3% in the Limited Reform Scenario for 2025-2029 and 6.2% in the Deep Reform Scenario



Source: Authorities and IIF

Graphic: IIF

Under the **deep reform scenario**, Lebanon is projected to receive $12.5 billion in financial assistance from multilateral institutions and official donors, distributed as follows:

- $3 billion from the IMF in the context of a four-year Extended Fund Facility (EEF) arrangement
- $3 billion from the World Bank for certain projects
- $4.5 billion from the Gulf Cooperation Council (GCC)
- $2 billion from major European countries

Moreover, Lebanon could secure $10 billion in foreign direct investment from the GCC between 2025 and 2029, which falls under non-debt creating capital flows.

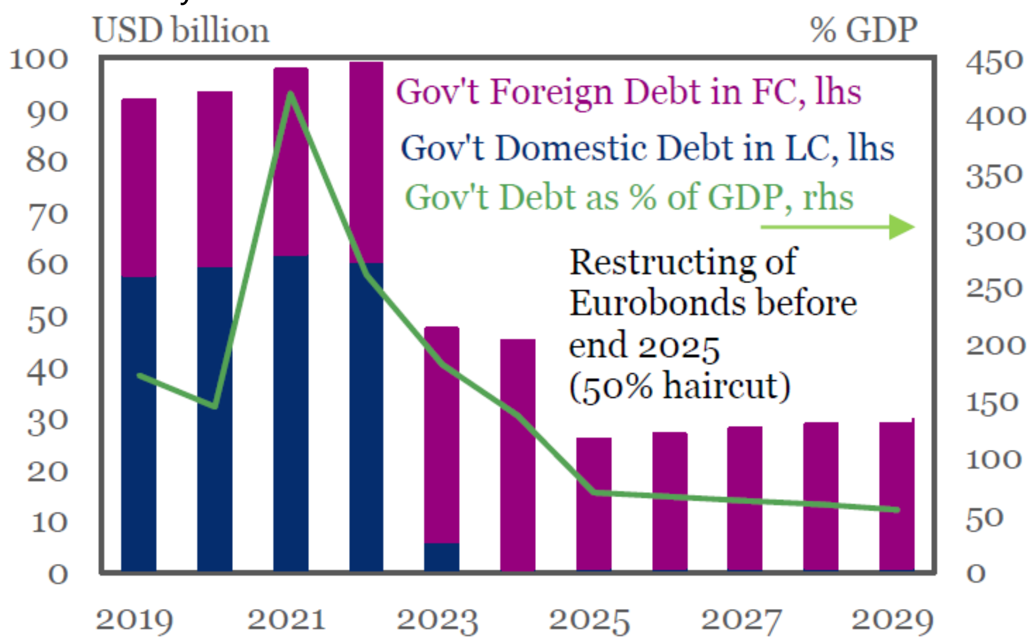
In this scenario, Lebanon's future looks promising with its strong entrepreneurship and talented people. Its real GDP is expected to get back to its 2017 peak by 2031, with the 2018 GDP peak of $54 billion expected by 2028. Deep reform scenario projections indicate 6.2% average GDP growth from 2025-2029, driven by FDI, public investment, and tourism revenues. A BIS study (2016) and Cyprus's example show that falling bank credit won't hinder recovery after crises. Lebanon's private consumption, strengthened by remittances and tourism, will support the economy. Construction will recover through FDI and loans, with Lebanese banks needed for real estate financing.

Inflation is expected to continue its downward path and decrease from an average of 45.2% in 2024 to 16.9% in 2025 and 3.4% by 2029, amid a stable exchange rate and better economic prospects.

As for the current account deficit, it is anticipated to decrease from an estimate of 10.8% of GDP in 2024 to 7.6% by 2029. This decline is supported by the restoration of exports to Saudi Arabia, recovery in tourism receipts due to the lifting of travel bans, and decreased re-exports or smuggling of goods to Syria.

Government debt to GDP ratio is expected to drop from 136% in 2024 to 53% by 2029 aided by Eurobonds haircut, budgetary tightening and better growth levels.

Exhibit 2: Government debt to GDP ratio is expected to drop from 136% in 2024 to 53% by 2029



Source: Haver and IIF

Graphic: IIF

The primary surplus is projected to rise from 0.4% of GDP in 2024 to 2.5% by 2029. The overall balance, excluding foreign-financed capital expenditures, is expected to rise from a negative 0.5% of GDP in 2024 to a positive 3.3% by 2029. This increase will be fueled by less tax evasion, better tax collection, and strong economic growth.

Regarding Eurobonds, assuming necessary reforms and the IMF agreement are executed, they are projected to climb from about 19 cents to approximately 30 cents by June 2025.

Lebanon stands at a crossroads with two possible economic paths: limited reforms with 3% GDP growth in 2025-2029 or deep reforms with 6.2% growth, both having a 50% probability according to the IIF. Deep reforms rely on securing international aid and an IMF agreement, which requires progress on seven key pillars: political and security stability, banking sector restructuring, adopting a flexible exchange rate, fiscal consolidation through improved tax systems, restoring confidence in the Lebanese pound, judicial reforms, and strengthening social safety nets. Achieving these reforms is more challenging than the report suggests, given the deep-rooted corruption and political/security barriers, making the 50% possibility of this scenario seem optimistic. In fact, Israel's daily ceasefire violations have resulted in over 830 breaches, around 60 civilian deaths, and numerous injuries since November 27, 2024. Israeli soldiers have also remained in five locations in southern Lebanon past the deadline to withdraw, breaching Lebanon's sovereignty. Judicial reform is equally tough as many staff members in public institutions were appointed by corrupt politicians. However, there is hope: Lebanon may have hit rock bottom, offering a chance for recovery if reforms are pursued boldly. It's important to note that both the limited reform and deep reform scenarios present improvements compared to Lebanon's current dire situation. While deep reforms offer a more optimistic growth outlook, even the limited reforms signify progress from the present economic conditions.

Exhibit 3: Main Economic and financial Indicators

	Actual				IIF Estimates			IIF Deep Reform Scenario, 50%				
Indicator	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Nominal GDP (LP trillion)	83	80	97	246	675	2,082	2,943	3,608	4,114	4,681	5,252	5,792
Nominal GDP ($ billion)	54.9	53.2	25	19.8	24.9	24.3	32.8	38.3	41.5	45.5	49.4	52.9
Real GDP growth, % change	-1.9	-6.8	-24.6	2	1.3	-1.1	-7	5.3	4.8	6.5	7	7.2
Private consumption	-2.6	-1.4	-22.5	-7.2	2.5	-3.2	-14.9	1.8	2.6	4.8	5.4	6.3
Public consumption	5.3	2.8	3.6	-101	2.5	2	14.6	14.9	13.9	8	9.5	9.6
Private fixed capital	3.4	-39.7	-70	123.5	-16.7	6.1	-30.6	20.6	20.5	22.8	18.3	14.9
Public fixed capital	26.2	-20.3	-3.9	-81.1	93	27.7	105.1	182.8	56.4	22.5	14.6	3.6
Exports of goods & services	-4.6	-2.2	-39.4	11.9	11	-3.7	-20.8	12.7	12.5	12.1	10.9	10.2
Imports of goods & services	1.3	-9.6	-33.4	8.1	22.3	-3.8	-22	15.2	12.8	11.8	10.8	9.8
Gross investment, % GDP	21.1	13.5	11.8	9.7	9.6	10.4	8.7	11.8	14.6	16.8	18.3	19
Private excluding FDI, % GDP	14.6	8.5	5.5	6.1	6.6	6.5	6.3	6.7	6.2	6.1	6.8	6.8
FDI, % GDP	4.8	3.6	4.4	3	2.1	2.7	1.4	2.5	4.7	6.3	7	7.9
Public investment, % GDP	1.7	1.4	1.8	0.5	0.9	0.8	1.1	2.6	3.7	4.2	4.5	4.4
GDP deflator, % change	5.5	4.1	60.1	148.4	171.3	211.6	51.9	16.5	8.8	6.8	4.8	2.9
CPI inflation, %, average	6.1	2.9	84.9	154.8	171.2	221.3	45.2	14.6	8.7	6.8	5.1	3.4
CPI inflation, %, end of period	3.9	3.2	146	224.4	122	192.3	18.1	11.6	7.8	6	4.2	3.2
Weighted average exchange rate, LBP/US$	1,508	1,576	4,203	12,446	27,087	85,805	89,700	94,281	99,171	102,840	106,234	109,421
Current account, $ billion	-13.4	-11.1	-2.8	-4.6	-7.3	-5.6	-3.5	-3.7	-3.8	-3.7	-3.8	-4
Current account, % of GDP	-24.3	-20.8	-11.1	-23	-28.6	-23.3	-10.8	-9.7	-9.2	-8.2	-7.8	-7.6
Fiscal balance, % GDP	-11.4	-11	-7.4	-2.7	-6.4	-0.4	-0.6	-1.6	-3.8	-2.8	-1.8	-0.6
Primary balance, % GDP	-1.2	-0.5	-4.2	-1.4	-5.4	0.7	0.4	-0.1	0.2	0.9	1.5	2.4
Government debt as % of GDP	155	172	145	418.2	260.1	181.6	136.8	69.3	65.7	62	58.9	54.5
Official FX reserves, USD bn	32.5	29.6	18.6	13.6	10.4	9.6	10.2	10.7	13.7	17.6	21.9	26.4
Gold reserves, USD bn	11.8	13.9	17.3	16.6	16.7	18.7	24.4	26.7	26.7	26.7	26.7	26.7

Source: Lebanese authorities and IIF estimates and projections

Graphic: IIF

Exhibit 4: Balance of payments and External Debt, in USD billion, unless otherwise indicated

	Actual						Est	IIF Deep Reform Scenario, 50%				
Indicator	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Trade Balance	-15.1	-13.4	-6.5	-8.8	-13.6	-12.7	-9.5	-11.1	-12.7	-14.5	-16.3	-18
Merchandise exports	3.8	4.8	4.1	4.1	4.5	4.1	3.7	4.1	4.7	5.3	6.1	7
Merchandise imports	-18.9	-18.2	-10.6	-12.9	-18.1	-16.9	-13.2	-15.2	-17.4	-19.8	-22.4	-25.1
Net services	1.4	0.4	0.1	0.8	1.5	1.2	0.6	1.4	2.7	4.6	6.1	7.5
Exports of services	15.8	13.6	4.9	5.7	8.1	7.8	6.1	7.5	9.4	11.7	13.8	15.8
ow: Tourism	8.4	8.6	2.4	3.1	5.3	5.4	3.9	5	6.3	8	9.2	10.2
Imports of services	-14.3	-13.1	-4.8	-4.9	-6.6	-6.6	-5.5	-6.1	-6.6	-7.2	-7.7	-8.3
Net income	-1.1	-1.2	-1	-1.9	-0.8	-0.1	-0.6	-0.3	-0.3	-0.3	-0.3	-0.3
Receipts	2.8	3.1	1.6	0.1	0.8	0.9	0.3	0.6	1.7	1.7	1.6	1.6
Payments	-3.9	-4.3	-2.6	-1.9	-1.6	-0.9	-0.9	-0.8	-1.9	-1.9	-1.9	-1.9
Net current transfers	1.4	3.1	4.7	5.3	5.7	5.8	5.7	5.9	6	6.2	6.3	6.4
Current account balance	-13.4	-11.1	-2.8	-4.6	-7.3	-5.6	-3.5	-3.7	-3.8	-3.7	-3.8	-4
Current account as % of GDP	-24.3	-20.8	-11.1	-23	-28.6	-23.3	-10.8	-9.7	-9.2	-8.2	-7.8	-7.6
Nonresident capital flows	3	-5.1	-5.6	-5	-4.7	-3.8	-0.1	1.1	3.3	4.1	4.7	5.1
Foreign direct investment	2.7	1.9	1.6	0.6	0.5	0.7	0.5	1	1.9	2.9	3.5	4.3
Portfolio investment	-4	-2.3	1.4	0.9	-3.9	-2.3	0.1	-0.6	-0.5	-0.7	-0.8	-0.7
Other investment	4.4	-4.7	-8.5	-6.4	-1.4	-2.1	-0.6	0.7	1.9	2.0	2.1	1.5
of which: official loans	0.2	0.2	0.3	1.3	0.2	0.2	0.2	1.6	2.8	2.9	3	2.4
Resident capital flows+E&O	-1.2	8.7	1.2	3.8	5.9	5.1	5.6	4.7	3	1.6	1.4	1.4
Capital account	1.4	1.4	1.7	1	1.5	0.6	0.7	1	1.1	1.3	1.4	1.4
Official FX reserves, USD bn	32.5	29.6	18.6	13.6	10.4	9.6	10.2	10.7	13.7	17.6	21.9	26.4
External debt in USD bn	112	107	97.5	92.8	92.2	90	91.1	68.5	66	63.6	61.1	58.4
Eurobonds	31.3	31.7	31.3	33.6	36.1	38.8	41.7	20.8	20	18.9	17.6	16.4
Official debt	2.2	2.1	2.1	2	2.2	2.4	2.6	4.2	5.9	8	10.2	12.2
Nonresident FC deposits	47.5	41.7	34.3	29.7	28	24.2	23.5	21.9	20.2	18.5	16.8	15.1
30% of resident FC deposits	27.1	27.7	26.5	24.5	22.7	21.4	20.4	18.9	17.4	15.9	14.4	12.9
External debt, % of GDP	204.2	201.0	390.2	469.2	369.8	371.2	277.8	179.0	159.2	139.7	123.5	110.3

Source: BdL through 2023; IIF estimates for 2024 and forecast for 2025-2029

Graphic: IIF

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