

The Levant: Problematic politics stifling growth

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- Lebanon has been under political and economic duress for some time now. While reforms are under way, politics may hinder the beleaguered country's development.
- Its business environment faces similar challenges. Nonetheless, optimism is reflected in Lebanon's PMI figures, which reached a seven-month high in January 2022.
- Jordan's markets are looking steady. The kingdom seeks to boost exports with new trade deals, while all the while the monarchy continues to consolidate its rule.

Lebanon: No room for growth

Political discord and lagging reforms continue to threaten Lebanon's growth prospects. The path towards recovery requires heavy intervention from international organisations, which are beginning to step in.

- Although elections are set for May 2022, the supervisory commission remains doubtful that it will be able to monitor the process successfully.
 - This calls into question the legitimacy of not only the electoral process but also the results.
 - The commission has not been able to hire the necessary media observers because it does not have the means to do so.
 - The commission has no independent funding and parliament is reluctant to recognise its powers.
- As we have seen across the MENA region this year, political parties may push to postpone the elections.
 - Nabih Berri's Amal Movement and President Michel Aoun's Free Patriotic Movement stand to lose the most seats and could opt for postponement.
 - Both are key allies of the Shia movement Hizbullah, and both have weakened since 2019.
 - Hizbullah will look to retain its parliamentary majority.
- Failure to hold elections on time risks straining ties with Western nations which are keen to help Lebanon to emerge from its severe economic crisis.
- According to the World Bank Lebanon Economic Monitor (LEM), Fall 2021, the country's economic crisis is one of the top ten, and possibly even one of the top three, most severe economic collapses in the world since the 1850s.
 - While the government has attempted to pass a draft budget, this has received much pushback.
 - Included within the draft are plans to hike regressive taxes on customs duties, as well as import and trade fees.
 - Increasing import taxes could lead to another spike in inflation by driving up the cost of imported goods and services.

Another government rescue plan involves returning around USD 25B (of USD 104B) to depositors over 15 years. The payments will be made in USD.

Figure 1 - Lebanon GDP growth (%)¹

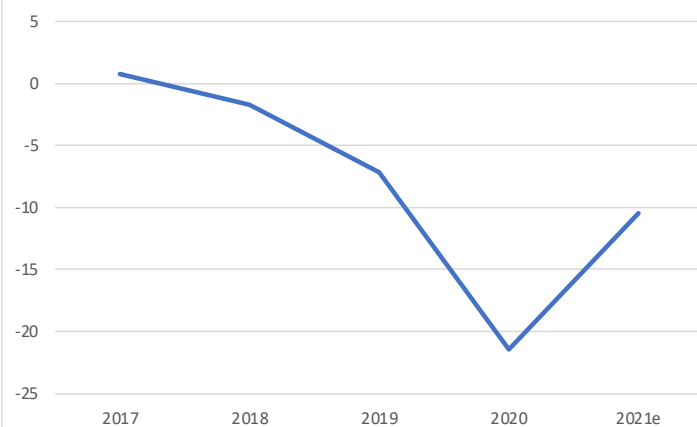
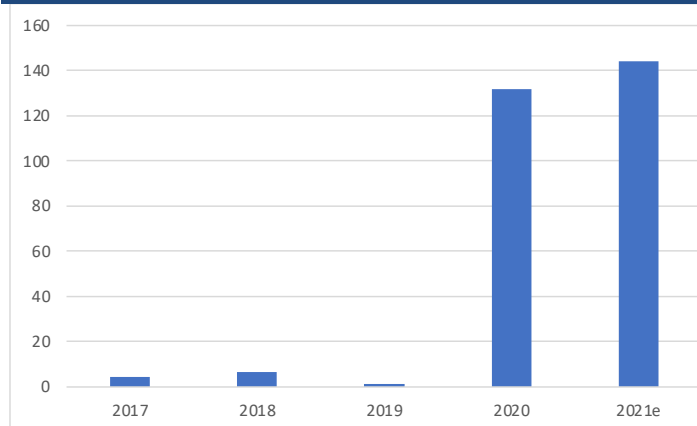


Figure 2 - Lebanon inflation rate (%)²



- Most of the remainder is set to be converted to Lebanese pounds (LBP) at several exchange rates, which would wipe around 75% off various deposits.
- The plan projects a 93% devaluation of the LBP.
- Although the Association of Banks in Lebanon (ABL) has since rejected the plan, it may yet move ahead.
- A reprieve may be provided if a deal is reached with the International Monetary Fund (IMF).
 - Talks between IMF representatives and the government of Prime Minister Najib Mikati resumed earlier this year. They addressed issues such as the budget, the banking sector and the exchange rate.
 - The IMF is reluctant to extend financial aid to a government that is seemingly incapable of resolving its own structural and institutional woes.
- If Lebanon wants to recover economically, there are several issues which must be tackled. Restructuring and reform measures are key for even limited success.
 - Governance throughout the country is opaque, particularly in the banking sector. The IMF has called for more transparency, though such efforts could be futile.
 - Additionally, the World Bank and the GCC demand a forensic audit of Lebanon's central bank (Banque du Liban).
 - Previous auditing attempts by Alvarez and Marsal failed in 2020 due to a lack of co-operation on behalf of Lebanon's central bank. Although these auditing efforts resumed in November 2021, there is still a significant lack of transparency. There is no

¹ Arabia Monitor; The World Bank.

² Arabia Monitor; Blom Bank.

data with regard to the actual value of the central bank's reserves and the losses accrued by the financial sector.

- Ghada Aoun, a judge and state prosecutor, issued a subpoena for the central bank's governor, Riad Salameh, after he failed to appear for questioning over corruption allegations made against him.
- Debt restructuring and an overall renovation of the banking sector is vital for the protection of depositors' wealth. Such measures will also help to regain Lebanon's credibility and to earn trust across the international community.
- Multiple exchange rates are significantly impacting Lebanon's economic and financial performance. A unified system coupled with temporary capital control may be necessary.
- While the outlook is not wholly promising, there is some cause for optimism. Lebanon's Purchasing Managers' Index (PMI) rose to 47.1 in January 2022, the highest figure for seven months. Nevertheless, this indicates that challenges remain for the business environment.
- If the same leadership and political factions continue to take charge, we assess that reforms may lag and that a bailout could fall flat.

Jordan: Trade ties pave path for growth

Following the easing of COVID-19 restrictions, growth in Jordan was catalysed by an expansion in the services, industrial and agricultural sectors. These sectors are set to grow even further due to trade deals with allies which have helped to nurture exports.

- Jordan is seeking to deepen trade ties with the UK by strengthening the existing 'association agreement', which makes it easier for both countries to do business.
- Jordan wants to increase exports to the UK, including processed and halal meats, as well as fruits and vegetables.
- The trade agreement between the UK and Jordan came into effect in May 2021. As part of the deal, Jordan benefits from lower tariffs.
 - The agreement primarily relates to goods, services and intellectual property.
 - It ensures total trade between the UK and Jordan exceeds GBP 561M annually.
- To help boost trade, AD Ports Group, a leading trade and logistics company, signed four strategic deals and a Head of Terms Agreement (HoT) with the Aqaba Development Corporation (ADC). As part of the arrangement, AD Ports Group will support the development of tourism, logistics, transport and digital infrastructure within Aqaba.
 - The arrangement will help to streamline Jordan's exports.
- In January 2022, the IMF approved the disbursement of around USD 335M to Jordan, bringing its total pay-outs to the kingdom since the start of 2020 to around USD 1.23B.
- The IMF assesses that Jordan's recovery remains on track due to continued progress regarding reforms; these have ostensibly helped the kingdom to maintain macroeconomic stability.
- Potential headwinds include high unemployment and low labour force participation.
 - Jordan is set to continue with structural reforms so as to boost jobs. If these reforms continue, unemployment is set to dip in 2022 after peaking last year.

Figure 3 - Jordan GDP growth (%)³

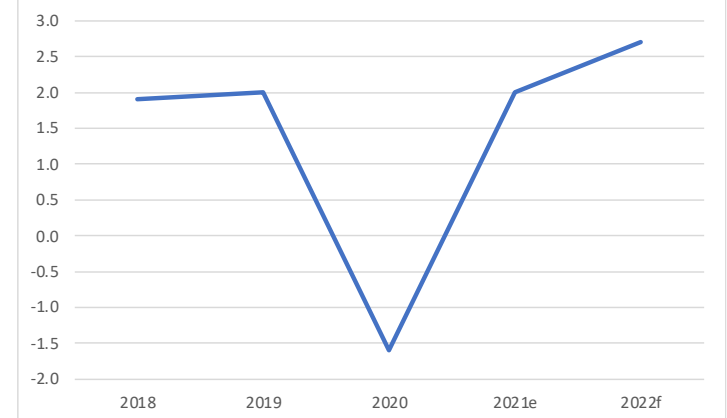
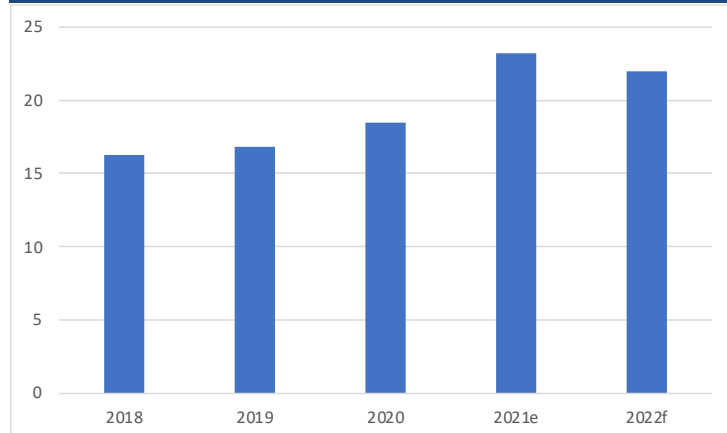


Figure 4 - Jordan unemployment rate (%)³



- As for Jordan's politics, King Abdullah II put forward constitutional changes last month which have since been ratified into law.
 - The king already has the power to appoint or dismiss governments. He also commands the military and directs foreign policy.
 - The changes include the creation of a security council that reports directly to the king.
 - The new security council comprises members of the intelligence services and the army. The council specialises in security, defence and foreign policy; it will meet whenever the king demands.
 - The amendments also make it difficult for parliament to remove governments. The removal of the government now requires a motion for a vote of confidence to be approved by 25% of the legislature. This is significantly higher than the previous 7% threshold.
 - The move makes what is already a largely ceremonial government body even more ineffectual.
 - The king also wants to increase the number of women in the labour force by encouraging employers to make special considerations vis-à-vis their hiring decisions.
- The king's moves come as no surprise; following the alleged attempted coup last year, we anticipate the introduction of further reforms that aim to consolidate his authority.

³ Arabia Monitor; IMF.

⁴ Arabia Monitor; Trading Economics.

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