The Politics of International Assistance in Lebanon: An Evaluation of the IMF's Loan Conditions as a Pathway to Inclusive Growth

Working Paper

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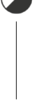

ABSTRACT

Four years into Lebanon's crippling economic crisis and the country's ruling political parties are yet to agree on a path towards financial and economic recovery. With declining support from international donors, Lebanon has sought an IMF loan in an attempt to partially cover the banking sector's losses and boost local economic growth. Questions remain, however, about whether an IMF loan programme will help situate Lebanon on a pathway to prosperity in light of the country's history of elite wealth capture and dependence on international aid. Based on a qualitative assessment of the conditions set forth by the IMF through its Staff-Level Agreement (SLA) with the Lebanese government in 2022, the article argues that although the IMF has recently made significant commitments to promoting inclusive growth, its approach in the SLA still leaves ample possibilities for ruling political parties to exploit a future loan at the expense of the public. The paper concludes with a set of recommendations for amendments to the IMF's conditioned reforms to ensure that the IMF loan, if granted, will secure greater protection for members of the public, rather than becoming a tool for advancing the interests of Lebanon's political and economic elites.

INTRODUCTION

Lebanon is in the midst of a major financial and socio-economic crisis, and a loan from the International Monetary Fund (IMF) appears to be a vital and necessary resource for getting the economy on track to recovery. Lebanon has a long history of receiving support from the international donor community, largely as a measure of ensuring that local economic and political turmoil does not escalate and spill over into regional destabilisation. Although the Lebanese government has never before opted for a loan from the IMF, it has received support from several donor conferences, unlocking billions of dollars in investments to assist the country's economy (Sherry, 2014). From 1991 to 2022, successive Lebanese governments received development assistance amounting to approximately $22.6 billion in the form of grants and loans from the international community. Assistance on such a scale is quite significant considering how small Lebanon is, and it has arguably become a fundamental pillar of the country's post-war economy (Mahmalat et al., 2023). In the context of post-conflict volatility, loans and grants have been offered and received in response to various specific political developments. From the need for reconstruction after the end of the Lebanese Civil War in 1990, to the withdrawal of Syrian troops in 2005, donor countries have consistently been willing to assist Lebanon, mainly because of its geopolitically strategic location, and their vested interests in promoting the neoliberal agenda (Sherry, 2014; Mahmalat et al., 2023).

However, the current prospects for an IMF loan look bleak due to multiple very challenging political and economic circumstances. A prolonged political impasse in Parliament has meant that governors have stalled on the vital political and economic reforms that are needed to respond to the current crises (Gharib, 2022). At the economic level, the country's stability has been consistently deteriorating for years, with a particularly rapid decline after 2018, when the government declared that the public debt has to be restructured – an indication that the country is unable to repay its debt, which consequently discouraged international creditors from loaning Lebanon anew. Donor countries are now insisting on various reforms as a prerequisite for offering any financial assistance package, marking a stark contrast from their generous development assistance in previous years. This was evident in the last international conference in 2018, formally known as CEDRE, where donors pledged $11 billion in soft loans and grants, contingent upon implementing administrative reforms and measures against corruption (Merhej & Ghreichi, 2021). Political and economic reforms, however, were not even up for discussion in Parliament, and this made negotiations with the donor community fail. At the same time, the governmental reserves were dwindling gradually. By 2020, then-Prime Minister of Lebanon, Hassan Diab, began to seek an IMF bailout, which was also dependent on multiple preconditioned reforms, including auditing the banking industry, lifting the banking secrecy law, and implementing further fiscal/structural reforms (Mehrej & Ghreichi, 2021; Jbeili et al., 2022).

There is a strong case to be made that agreeing to the reforms and taking a loan from the IMF is necessary for Lebanon's economic recovery. If the government implements the IMF's preconditioned reforms, this will serve as reassurance to the international community that the country is committed to a democratically robust and fiscally disciplined pathway to socioeconomic development. Furthermore, Lebanon's international financial standing has been severely downgraded in the last few years, and this can only be remedied if

the government shows readiness to commit to an international loan programme. The problem, however, is that the Lebanese public is already suffering from a deeply rooted financial and socioeconomic crisis, and this raises concerns about implementing the kinds of austerity measures that usually accompany an IMF package. The overlapping crises have driven poverty rates to 85 percent and unemployment above 30 percent (Sherry, 2023). More dangerously, the number of families that live in abject poverty – people unable to secure their daily sustenance – has increased from 10 percent before 2019 to 30 percent at the present (ibid). The Central Bank has also stopped subsidising imports which, coupled with fuel shortages and supply-chain bottlenecks, have caused a 483 percent hike in food prices in just in the one year prior to January 2022, and, subsequently, a 42 percent increase in acute food insecurity (World Food Programme March Situation Report, 2023; Human Rights Watch, 2022a). The subsidies were also lifted on the import of vital goods such as fuel, which in turn exacerbated the prices of electricity, water and gas (Human Rights Watch, 2023a). These findings concur that any further austerity measures resulting from an IMF deal will likely prove devastating for the public, and especially for the growing number of people living in poverty.

The crucial question that emerges in this context is if and how an IMF loan programme can be implemented in a manner that steers away from elite wealth capture, while protecting the most vulnerable from further austerity measures and supporting the transition to tangible improvements to people's quality of life. Put in slightly different terms, we must ask if and how an IMF loan can translate into a pathway to prosperity, understood in terms of equitable investments in the services and provisions that people need for a decent quality of life – jobs with a living wage, good quality education, and affordable and reliable utilities such as electricity and water (Moore et al., 2023; Jallad et al., 2022). One of our key arguments in this paper is that any policy programme – and especially that of the IMF in the present moment – must directly prioritise quality of life for the wider public, beginning with the most vulnerable, and it ought to take into account the pathways through which the reforms can steer away from the exploitation of the political elite and instead focus on benefitting the public.

THE IMF: FROM STRUCTURAL ADJUSTMENT PROGRAMS TO A DISCOURSE OF INCLUSIVE GROWTH

The IMF was formed in 1944 at the Bretton Woods Conference and established as a major inter-governmental institution for supporting international economic cooperation after the Second World War (IMF, 2023a). The Bretton Woods conference resulted in the creation of an international system of exchange rates backed by the US dollar (as opposed to gold) in an effort to facilitate global monetary cooperation. At the time of its foundation, the membership of the IMF consisted of 44 nations. Since then, this number has increased more than four-fold and currently, with a membership of 190 member states, the IMF is one of the most comprehensive and powerful institutions globally (Kentikelenis et al., 2016; IMF, 2023a). The Fund has eight main functions as per its mandate, including the 'surveillance of member states' economic policies, the dissemination of information and research, mobilising external financing, and increasing the global supply of international reserves' (Abdo et al., 2020, p. 12; Kentikelenis et al., 2016). Among its various functions, the IMF's lending programmes have been the most controversial (Kentikelenis et al., 2016; Williamson, 1983). The IMF's standard practice is to attach a set of obligatory policy reforms for the borrowing country to gradually implement in exchange for financial assistance (Williamson, 1983). The content of the IMF's conditionality, however, has attracted a full range of perspectives and debates. These are beyond the scope of this paper, but they have been reviewed elsewhere (Babb, 2005; Babb and Carruthers, 2008; Dreher, 2009; Nelson, 2014). The focus of this article, instead, is on the social consequences of the IMF's conditionality when implemented in the context of the Lebanese political economy.

Ever since its formation, the IMF has upheld a vision of economic growth as a key mechanism for improving living standards in developing countries, especially via promoting macroeconomic policies' (IMF, 2002). The Fund has mainly relied upon GDP to measure if an economy is growing or contracting (Callen, 2012), and also as a metric for assessing whether or not to intervene in developing countries. This was especially the case during the 1980s when the Washington Consensus was developed by the Bretton Woods institutions in conjunction with the United States Department of Treasury. In broad terms, the Washington Consensus represented a 'set of professionally-sanctioned prescriptions' to assist governments of developing countries to counter their debt and economic troubles (Babb, 2013). The principles reflected a kind of 'market fundamentalism' with economic growth as the main priority and little to no consideration for social protection (Diab & Hindy, 2021). The assumption was that if national income increases, wealth would 'trickle down' to all income groups and make everyone much better off than before (ibid). The Consensus was also a vehicle for international financial institutions, mainly the IMF and the World Bank, to practise conditional policy-based lending, and to reform the governance of developing countries (Babb, 2013; Sherry, 2017). The Fund's reforms were then found to be disastrous for public spending and inequality: labour market deregulation; privatisation of state-owned assets; requesting large reductions to governmental expenditures and cutting down subsidies on basic services including healthcare and education; lowering marginal tax rates and increasing positive interest rates; demanding trade liberalisation, mainly through eliminating non-tariff measures and devaluing local currencies to increase exports and make

national products more competitive (Sherry, 2017; Willamson, 2003).

The IMF employs two types of conditionality in its lending programmes: quantitative and structural (Kentikelenis et al., 2016). When the IMF was initially formed, its conditions were mainly based on quantifiable macroeconomic targets that the government of the borrowing country needed to reach for sustaining financial assistance from the Fund (e.g. decreasing governmental debt). This type of conditionality was not structural because it still gave the governments of borrowing countries, the freedom to choose the means to reach the macroeconomic goals in question (ibid). However, with the advent of stricter neoliberal reforms inspired by the Washington Consensus, the Fund's practices often ventured into what critics saw as abandoning the 'economic neutrality zone'. The IMF was now accused of interfering in non-economic areas that are relevant to policy-making such as when demanding trade and financial liberalisation (Abdo et al., 2020; Kentikelenis et al., 2016; Nunn & White, 2016; Sherry, 2017). By the late 1990s, it had become clear that the conditions of the IMF's 'structural adjustment lending programs' were being imposed on developing countries in a standardised form – namely, without taking into consideration the intricacies of each context – and this was leading to poor and at times disastrous results (Ban & Gallagher 2015). While Lebanon never went through an SAP, other countries in the region, most notably Egypt and Jordan, witnessed significant social unrest as a result of the structural reforms required by the SAPs (Abdo et al., 2020). This led to a wave of backlash against the IMF, with critics claiming that the free-market fundamentalism and the one-size-fits-all strategy followed by the Fund fail to efficiently respond to the diverse crises in the borrowing developing nations (Ban & Gallagher 2015).

The criticism directed towards the Fund led to a unique shift in its rhetoric, especially following the Asian financial crisis of 1997 and the Arab Spring of 2011. IMF conditionality was once again re-packaged in an attempt to redirect policy towards fiscal consolidation – helping to reduce government deficit and debt – as a substitute for uniform, market-oriented structural reforms (Sherry, 2017; Nunn & White, 2016; Kentikelenis et al., 2016). The rebranding of the Fund's lending programmes sought to emphasise the post-Washington Consensus's focus on transitioning from a donor-led development process to one where local stakeholders play a much greater role in managing the loan, and where a greater focus is placed on the social impact of economic reforms (Nunn & White, 2016). The Fund even came up with new lending arrangements such as the Flexible Credit Line scheme which enabled countries with 'very strong economic fundamentals and institutional policy frameworks' to meet balance of payment needs without recourse to explicit conditionality (IMF, 2023). There was even a shift in how the Fund assessed inequality, as it adopted the concept of inclusive growth. In 2012, the IMF Deputy Managing Director, Nemat Shafik, elaborated on this commitment by claiming that the IMF would henceforth focus on five key areas that are critical for achieving socially inclusive growth: "job creation, better-targeted social safety nets, strong governance and business environments, access to finance, and greater trade access and integration" (Shafik, 2012). Opinions differ on whether the IMF has made any significant advances towards implementation of an inclusive growth or sustainable prosperity agenda. Abdo et al. (2020), for example, claim that under the leadership of Christine Lagarde

(2011-2019), the IMF produced extensive empirical research on how inequality and neo-liberal market reforms hamper growth, but they still concur, after looking into several IMF arrangements executed post-2011, that there remains a clear gap between the Fund's changing rhetoric and its policy design for recipient countries in the developing world.

The Fund's work on fostering inclusiveness through reducing inequality and increasing social protection is still found to be lacking in both the IMF's soft policy advice to member states (Article IV reports) and its 'harder policy advice' that is associated with its lending programmes and structural conditionality (Nunn & White, 2016; Kentikelenis et al., 2016). This has also been concurred by the IMF's recent periodic policy reviews in which the Fund stated that there has been a limited focus on social spending, social protection and inequality in the IMF programmes initiated between 2011 and 2017. The policy reviews further advocated for specific frameworks to expand the agenda of inclusive growth, highlighting that this has been a long-overdue project (IMF, 2019a; IMF, 2022). However, the essence of the problem remains that the IMF approaches social protection from the standpoint of fiscal policy (IMF, Independent Evaluation Office, 2017, p.11). Instead of assessing people's needs and engaging with them to understand their hardships, the IMF would generally recommend specific fiscal policies to the borrowing government with hopes that this would create the needed space for social spending. In addition, social protection is viewed as mainly revolving around social insurance (such as pension schemes), social assistance (cash transfers) and labour market interventions (Alston, 2018). In the context of Lebanon, as we argue in this paper, such an approach is only a short-term fix that will not redress the severity of social conditions in the longer term, given the prevalence of elite wealth capture and the service-based nature of the Lebanese political economy. Long-term social protection, we argue, has to be a core pillar in any macroeconomic framework rather than simply a tool to temporarily mitigate the adverse short-term effects of fiscal adjustment on the most vulnerable.

THE IMF AND THE UNFOLDING OF THE LEBANESE CRISES

Lebanon has been a member state of both the World Bank and the IMF since 1947. Its membership in the IMF entitles it to access technical assistance from the IMF, information on economic policies of member countries for trade enhancement, and financial support in times of balance of payment difficulties (IMF, 2022). Lebanon has never received a loan from the IMF, but it has received Special Drawing Rights (SDRs), with the last arrangement being in August of 2021. The IMF uses SDRs as a way of supplementing the foreign exchange reserves of its member states to help them avoid resorting to loans when in need of increasing governmental reserves (IMF, 2022). In addition, every member country is entitled to Article IV consultations which are a key instrument through which the IMF influences policy making in its member states. The IMF has been conducting Article IV consultations and publishing reports annually on Lebanon since 2006. The last report, however, was published in 2019 before the current crisis unfolded and the economy began deteriorating (Abdo et al., 2020).

Over the last two decades, the IMF has praised the ability of the Lebanese banking sector to withstand exogenous internal and regional shocks, particularly following the 2008 global financial crisis

which affected Lebanon only mildly (Finger & Sdralevich, 2009). However, the factors influencing the apparent financial stability in Lebanon had no grounds in the real economy (this point will be elaborated shortly). The IMF only recently became sceptical about the possibility of the Lebanese economic system to remain intact. In the Article IV report published in 2019 (prior to the unfolding of the October 2019 Uprising), the IMF warned about the extreme volatility of the Lebanese economy, claiming that any 'moderate negative external or domestic event can precipitate a fall in confidence and thus, an economic and financial crisis' (IMF, 2019b, p.8). Nevertheless, the suggestions of the IMF in response to the vulnerability of the Lebanese economy were limited to fiscal adjustment, increasing reserves and decreasing the Central Bank's involvement in quasi-fiscal operations. While these measures may have appeared to be effective for covering up the gaps in the Lebanese economy in the short turn, they would, even if implemented, fail to rectify a flawed economic model which was, and still is, in need of bottom-up refurbishing (Abdo et al., 2020).

In the meantime, the rift between the public and the political establishment was continuing to grow. High levels of income inequality, inadequate investment in basic services, scarce opportunities for secure and well-paid employment, and widespread political and economic clientelism were all contributing to a general sense that the country's economic and political models could not offer a decent quality of life for the majority of people, and there was no serious prospect for positive future change. Then, on October 17, 2019, the tensions between the wider public and the political establishment reached a breaking point. In a bid to raise additional revenue, the Lebanese government announced proposals for a number of new taxes, including a monthly tax on the use of WhatsApp, which is a highly popular and almost universally used service in Lebanon (International Crisis Group, 2021). The tax was seen as 'the last straw' in a long history of political impunity and indifference, leading to a public backlash that was both immediate and on a massive scale. The protests condemned the rampant corruption, deteriorating living conditions, and inequality that people in Lebanon were subjected to, and called for the toppling of the government and of the whole political establishment. It was an unprecedented moment in the history of Lebanon as it encompassed people from all ages, factions and backgrounds, leading to months of civil unrest (ibid). The protests were able to dismantle the cabinet headed by then-PM Saad Hariri, but lost momentum before achieving any other major political change.

PM Hariri's resignation took place in what was an already-volatile economic context that was showing signs of decay long before the uprising began. Those in power have attempted to frame the country-wide protests as the instigator of the socio-economic crisis, when, in fact, records show that Lebanon has not been creditworthy (considered suitable to receive credit by international credit agencies) for at least four years prior to the uprising (Noe, 2022). The IMF had even reported to the Central Bank (BdL) that the latter had a US$4.7 billion gap in its reserves as a result of the 'unconventional practices' initiated by its governor Riad Salameh since 2016, but this report was never officially released due to the protests (Noe, 2022; for more information on BdL's unconventional strategies, see Abdel Samad 2021 and Bifani 2022). Moreover, Lebanon's external debt had been growing at an unsustainable rate for years and was becoming increasingly incapacitating, reaching about 190

percent of GDP in 2018 (IMF, 2019b). This meant that most of the country's outputs were directed towards debt servicing – a problem that wreaked havoc on real economic growth. The burden of the debt became imminent in 2019, when rating agencies such as Moody and Fitch Ratings downgraded Lebanon's debt, which in turn translated into a decrease in the price of Lebanon's Eurobonds (a debt security issued by a government to support government spending). In addition, the sovereign downgrade caused the Lebanese financial sector to be side-lined from international financial markets and this also affected the public's confidence in the system and contributed to a wave of deposit withdrawals throughout 2019 and especially after the October 17 protests (Makari, 2021; Noe, 2022).

Domestically, for people in Lebanon, it was evident that the economic crisis was worsening by the day. First, in mid-2019, commercial banks started imposing informal restrictions on depositors' withdrawals (Bifani, 2022). Then came the October 17 uprising and the forceful release of the Lira peg which vanquished public confidence in the economic stability of the system, despite repeated assurances from the Governor of the Central Bank, Riad Salameh, that the Lebanese Lira is strong and stable. To make matters worse, the caretaker cabinet (the resigned Hariri-led cabinet), decided to pay a maturing $1.6 billion Eurobond in November 2019, which put extreme pressure on the Central Bank's foreign reserves, and necessitated the implementation of a Capital Control bill to prevent capital flight in light of the socioeconomic instability (Bifani, 2022). Instead, commercial banks prevented most people from withdrawing their foreign currency deposits on no legal grounds while politically and financially connected individuals made the needed arrangements to secure the flight of their money abroad (ibid). Nevertheless, despite the economic and social havoc locally, the Lebanese establishment refused to take responsibility or initiate any meaningful reforms (Noe, 2022). Seeing that the situation was headed towards a financial collapse with no proper political plans in sight, the top management of several Lebanese banks started selling the rest of their banks' Eurobonds to foreigners between October 2019 and January 2020, ultimately leading to the enormous transfer of sovereign USD-denominated debt to foreign investors. This meant more 'fresh' dollars for banks but lower hopes of negotiating debt restructuring since the government debt was now sold to numerous different foreign parties (ibid).

The compounding economic problems of 2019 – currency depreciation, immense capital flight in the absence of a regulatory capital control bill, a Eurobond sell-off and civil unrest – caused government reserves to dwindle to a point where the government had to prioritise subsidising living costs at the expense of paying back the next maturing Eurobonds (an amount of $1.2 billion due in March 2020). This marked the first default in Lebanon's history (Bifani, 2022; Noe, 2022). The default meant that Lebanon would endure a further sovereign downgrade and lenders would afterwards impose higher interest rates and stricter conditions on debt repayment methods. In principle, when a government is en route to default, it should at least communicate with bondholders several months in advance to negotiate the terms of the default or have an agreement with the IMF or donor countries for assistance that will minimise the costs of the default (Makari, 2021). However, the post-Saad Harriri cabinet headed by PM Hassan Diab announced the default before even reaching out to the IMF or having a well-thought-out economic plan that could gain the approval of Parliament. This worsened the liquidity problem significantly because the default meant that banks could

not receive any interest on their Eurobonds investments and that the government will now face stricter financial constraints (Makari, 2021). The cabinet headed by Diab wanted to prioritise spending money on subsidies to help alleviate the social burden of the crisis on the public, but this action was akin to sticking a band aid on a bullet wound.

Approximately two months after the default, the Diab cabinet formally requested the IMF's assistance on May 1, 2020. Initially, the cabinet announced that there is an estimated net loss of $90 billion on the balance sheets of banks – a figure that the IMF confirmed (Jbeili et al. 2022). However, the Central Bank, the Association of the Banks of Lebanon, and several parliamentary members refuted this number, while concurrently refusing to investigate he banking sector, under the protection of Lebanon's banking secrecy law. The failure to agree on the losses incurred, and subsequently on how the burden of the losses should be distributed, meant that negotiations with the IMF had to be halted for the time being.

NEGOTIATIONS WITH THE IMF AND LEBANON'S POLITICAL ECONOMY

Two years would pass by before the negotiations with the IMF resume in January 2022, with the spread of Covid-19 and the Beirut Port explosion being major reasons for the delay. The Beirut Port explosion on August 4, 2020 incapacitated the government and compelled the cabinet headed by Diab to resign, leading to a 10-month ministerial vacuum, further crumbling of the banking sector and continuous political deadlock in Parliament (Jbeili et al., 2022). The first substantial milestone, when negotiations with the IMF resumed, was reaching a non-binding Staff Level Agreement (SLA) in early 2022. The agreement delineated the roadmap set by the IMF and agreed upon by the negotiating group from Lebanon. The two parties agreed on an "Extended Fund Facility" designed to help countries facing severe ruptures in their balance of payments and general macroeconomic instability, through a comprehensive economic reform program. The agreement was not as comprehensive as the Article IV reports which the IMF was conducting annually since 2006, but it devised a roadmap of reforms for the Lebanese government

Figure 1. Timeline of IMF discussions with the Lebanese authorities. The green panels represent the resumption of negotiations after the disruptions caused by Covid and the Beirut Port Explosion.

to receive the needed funds. The loan, if awarded, will amount to SDR 2,173.9 million, or approximately 3 billion USD, to be paid in several instalments over three to four years. Although the loan is relatively small compared to the losses suffered by the Lebanese economy since 2018, it could nevertheless prove to be a crucial lifeline if Lebanon hopes to attract investors and regain the reputation of its banking system on international financial markets.

Nonetheless, a general survey of the dominating political and economic environments locally – and taking into account Lebanon's history of borrowing from the international community – indicates that the IMF loan negotiations will likely end up in one of two scenarios: either (1) the ruling political-economic elite will continue stalling on the preconditioned IMF reforms and use ad hoc policies to manage what is left of the economy, (e.g., minimising the losses by collecting additional revenue at the expense of the public, while shying away from the IMF loan); or (2) the government may claim to be implementing the reforms, but it would do so only in a way that keeps its interests, and the interests of its members and their networks, at the core of any new economic or political arrangement. For example, one of the main preconditions of the IMF is amending the banking secrecy law to allow the Central Bank, Banking Control Commission (BCC), and the National Institute for the Guarantee of Deposits (NIGD) to request and investigate banking information (Badil, 2022). To appease the IMF, the Parliament purports to have amended the law which, when closely examined, appears to be riddled with loopholes. The amended law allows the relevant institutions to review bank budgets and balance sheets, but it still prohibits them from investigating individual accounts. In addition, the IMF specifically requested the operational independence of the Central Bank, BCC and NIGD, but the amended law states that access to specific banking information is contingent upon a ministerial decree (i.e., it has to be granted by the Finance Minister and accepted by the Cabinet) (ibid). These are two of many examples that illustrate how the political/banking elites have no real intent in executing reforms that conflict with their own interests. It is in this particular context that any policy programme suggested to Lebanon should be read (Bifani, 2022).

Furthermore, foreign assistance schemes have had mixed consequences for Lebanon. On the one hand, they have kept Lebanon's economy going, but on the other hand, they have been continuously used to boost the disastrous policies and corrupt system of power-sharing (Gharib, 2022). In 2001, at the Paris I donor conference, Lebanese officials pledged to liberalise and further facilitate trade, in addition to privatising the electricity, water and telecommunications sectors, limiting governmental expenditures through decreasing subsidies on services, and reforming the tax system (Sherry 2014; Bifani, 2022). The reforms essentially targeted the most vulnerable as they required a decrease in social protection whilst still stalling on the need to change the persistent service-based economic model. In addition, the ruling parties proceeded with the reforms which align with their interests such as increasing indirect taxation over wealth taxation. Lebanon opted for another loan the year after, amid stagnant economic growth. This led to a second donor conference, dubbed Paris II, where the Lebanese government presented a mere repackaging of the conventional market-oriented policies with special emphasis on increasing tax revenues through VAT and reducing capital expenditures (Sherry,

2014). Again and again, the government favoured those who are already benefiting from the neo-liberal model, enabling them to acquire further financial gains from international assistance schemes that were skewed towards open economies and free trade. Following this borrowing facade, public debt increased from $15 billion in 1998 to $38 billion in 2004 (ibid). To make matters worse, the money borrowed was not spent on development projects that could potentially create job opportunities and income for the government. Instead, they were allocated to debt servicing and financing the service sector, encouraging dependency on foreign capital and impeding sustainable development growth (Sherry, 2014; Bifani, 2022). As such, the intervention of the donor community has provided Lebanon with exogenous shocks which helped in retrieving short-term economic growth and partial confidence in the system, but ultimately failed in placing Lebanon on a pathway to sustainable prosperity.

The history of Lebanon's dependence on foreign support and the analysis of how this support has been used and captured by local elites indicate that Lebanon's economic and political models will likely undermine the ability of an IMF deal to boost inclusive and sustainable recovery without carefully planned measures that prevent the political-financial class from exploiting the loan. The donor community and international financial institutions have promoted liberalisation and deregulation, along with the increasing dependency on the services sector (personal/business services, financial operations, trade, real estate, food service activities) at the expense of the productive sectors and social protection (Sherry, 2014). As a result, the country witnessed significant social and economic setbacks up until the eventual collapse in 2019. Lebanon has continuously failed to invest in the real economy even with all the funds that were transferred in the past few years as a result of the Beirut Port Explosion, the pandemic and the large scale of Syrian refugee displacement. Instead, those in power capitalised on the semblance of economic success, while neglecting to undertake reforms that could have generated real capital, especially concerning the livelihoods of small depositors and the most vulnerable (Gharib, 2022). The political-banking establishment has lost the trust of the public, as well as that of foreign depositors and the international community, leaving the IMF package as one of few options, if not the only option, left for speeding up financial recovery.

HOW CAN THE IMF LOAN PROGRAMME LEAD TO INCLUSIVE GROWTH?

In this final section of the article, we consider the IMF's proposed reforms for Lebanon and make a number of recommendations for creating pathways to more inclusive and sustainable recovery. The IMF has been vocal about the need to integrate a more inclusive approach when intervening in middle-to-low-income countries, especially with regard to the growing evidence that a lack of inclusion can be macroeconomically harmful (IMF, 2017). Nevertheless, when it comes to its recently made agreements, from the loan agreement with Egypt in 2022 to the SLA reached in Lebanon, the Fund has not been adequately focused on incorporating social protection schemes. The IMF believes that governments can create space for social protection through maintaining sound fiscal policies which is very often infeasible as borrowing countries tend to suffer from systematic flaws in their fiscal system,

mainly as a result of existing debts and the mismanagement of public funds (Alston, 2018). The Fund also views social protection as consisting of social safety nets, social insurance policies and an increase in social spending on a governmental level (IMF, 2019a; Alston, 2018).
While this looks good on paper, it still falls within the top-down approach to preserving the quality of life of people, without taking into account if and how the strategy will meet people's needs and respond to their experiences. For instance, in its recent loan to Egypt (the fourth loan since 2016), the IMF prioritised the need to increase government social spending through a cash transfer program. However, the depreciation of the Egyptian currency has erased the gains to cash transfer recipients, rendering the program insufficient in protecting people from further austerity measures (Human Rights Watch, 2023b). Therefore, the IMF approach to social protection ought to be customised according to a deep policy diagnosis of the area being intervened in to comprehend the patterns and mechanisms through which social policies may lead to inclusive growth and prosperity. An increase in social spending or social safety nets does not necessarily translate to better welfare for the people, especially if the socio-political context of the country being intervened in is not taken into consideration.

In what follows, we list a number of factors that should be taken into consideration for the preconditioned reforms set forth by the IMF to lead to inclusive growth and reduce the risk of contributing to Lebanon's debt and austerity. The country's public debt has already reached around 163 percent of GDP (according to figures for 2022), the central bank has US $60 billion in negative net reserves and the banking sector is insolvent, which has resulted in arbitrary capital controls, 'haircuts' on deposits and a multiplication of exchange rates that are simultaneously in operation for different purposes (World Bank, 2023). Recapitalizing banks is a necessity for service operations to become partially functional again and for that, huge funds are needed. The Lebanese government may continue normalising the crisis and creating severe ad hoc measures to stabilise the situation, or it may eventually acquiesce to the IMF's preconditioned reforms and reach a comprehensive loan programme. In either case, the common denominator remains the need to protect the wider public, which is already bearing the brunt of the collapse, from further austerity measures and erosion of basic quality of life. The IMF has taken an important step in terms of prioritising social spending in the SLA to Lebanon; but in light of the current socio-political context, the reforms remain insufficiently detailed as a pathway to enhancing social protection and ensuring that the loan is fully invested in livelihoods and vital services and provisions. The SLA outlines five 'pillars' of restructuring that need to take place:

- 'Restructuring the financial sector to restore banks' viability and their ability to efficiently allocate resources to support the recovery;
- Implementing fiscal reforms that coupled with the proposed restructuring of external public debt will ensure debt sustainability and create space to invest in social spending, reconstruction and infrastructure;
- Reforming state-owned enterprises, particularly in the energy sector, to provide quality services without draining public resources;
- Strengthening governance, anti-corruption, and anti-money laundering/combating the financing of terrorism (AML/CFT) frameworks to enhance transparency and accountability, by modernising the central bank legal framework and governance and accountability arrangements;
- Establishing a credible and transparent monetary and exchange rate system' (IMF, 2022).

The social impact of the IMF agreement with the Lebanese government is not yet clear

since the negotiations have only reached the SLA with the above-mentioned requisite reforms. However, a close examination of the proposed preconditions in light of Lebanon's current political economy and history of dependence on foreign support allows us to anticipate their possible socio-political impact. We argue for a number of additional amendments through which each of the five pillars could ensure that a future IMF loan secures greater protection for the most vulnerable and contribute to sustainable and inclusive prosperity.

With regard to the first pillar, restructuring the financial sector, there ought to be a clear emphasis on the 'bail-in' strategy as the only equitable plan to restructure the banking industry in Lebanon. Restructuring the financial sector includes conducting audits on the Central Bank's accounts, restructuring commercial banks and the Central Bank, passing the Capital Control Law, amending the Banking Secrecy Law and recapitalizing the banking sector. As mentioned previously, the banking sector in Lebanon has been dependent on the inflow of foreign deposits for its survival and continuation. To maintain this inflow, banks have set high interest rates that have lasted for decades. It is worth noting that 1 percent of depositors own 50 percent of the total amount of foreign currency deposits in the commercial sector (World Bank, 2022). This means that very few individuals, mostly politically connected and financially well-off, were benefiting from the unsustainable and unreasonable policies of banks (phantom returns from large interest rates). At the same time, commercial banks were depositing this money in the Central Bank and also benefitting from the high returns that the latter was granting. This exposed banks to huge risks as BdL was loaning a failing state that was slowly showing its inability to pay back, especially after first announcing the need to restructure the state's debt in 2018 (Noe, 2022).

As the economic situation deteriorated, the Central Bank became unable to give commercial banks their deposits which made them freeze the deposits of people and impose informal capital controls. Currently, there is a $72bn hole in the balance sheets of banks (amounting to 311 percent of GDP), suggesting logically only one thing: bankruptcy and insolvent banks (World Bank, 2022). So far, to recapitalise banks, the Central Bank has been coming up with numerous ad hoc policies such as the Sayrafa platform – an electronic payment platform, which primarily serves as a subsidy for banks and businessmen to trade US dollars at a substantial premium in comparison with the parallel market exchange rate (Cole, 2023). Civil servants and public sector employees have also been allowed to withdraw their salaries on the Sayrafa rate (86200 L.L/USD as of June 27, 2023) in an effort to increase their income since the official exchange rate is at 15,000 L.L/USD. However, according to cumulative figures, the Sayrafa appears to benefit a fraction of civil servants whilst generating more than $2.5 billion in arbitrage profit (namely, profit earned from buying and selling the same security at different prices) for the financial class (Cole, 2023). It is thus solely a tactic that helps the political-financial elites buy time with the public's money while failing to respond to the systematic flaws that have caused the current economic crisis. This is also apparent in the unconventional operation of banks as more than 60 banks froze all foreign deposits and implemented informal capital controls and haircuts that made the value of any "pre-crisis dollar" equal to the devalued Lebanese Lira (Ghanem & Ray, 2022). This meant that people who had foreign currency deposits prior to 2019 were not (and still aren't) allowed to withdraw their money anymore unless they agree to withdraw them with extreme haircuts while politically and financially connected individuals made the needed arrangements to secure the flight of their money abroad

(Bifani, 2022). The IMF ought to dismiss such inequitable and severe measures that are mainly affecting middle-to-low-income citizens and emphasise the need to move with the bail-in option as a precondition for any loan programme. The bail-in requires 'cancelling, writing down or converting liabilities into equity', which means that banks' shareholders along with the largest creditors – those who majorly benefitted from the huge interests that banks were giving – have to use their savings to prevent their institutions from becoming bankrupt, merging or closing (World Bank, 2022, p:6). This is also in line with Lebanon's Intra Law (No.2/67) which clearly states that a defaulting bank has to go through an insolvency procedure and when a bank is declared insolvent, the board of directors, auditors and any authorised signatories may be held liable for their personal assets to cover the bank's debts (Kanso, 2022).

In the second SLA pillar, it is expected that a few fiscal reforms along with external public debt restructuring will help Lebanon spend more on the real economy and on social spending. However, for decades, the Lebanese government has continuously neglected an orderly and disciplined fiscal policy to serve the interests of the ruling financial-political bloc. Those in power have vested interests in the service-based rentier economic model and have always tailored the fiscal policy accordingly. This is no longer an accusation, as one can clearly see the accumulation of debt – beyond fiscal needs – solely to maintain an overvalued fixed exchange rate that attracted deposit inflows and generated the illusion of wealth. In addition, the ruling power-bloc has hollowed out the state through making service provision the duty of confessional leaders, public-private partnerships and elite wealth capture (World Bank, 2022). In light of this socio-political context, any hopes of fiscal consolidation (reducing deficits and the accumulation of debt) is a far-fetched strategy. More importantly, relying on fiscal consolidation to 'create space for social spending' is likely going to leave the people high and dry in the face of further austerity measures. As such, a more feasible strategy to create fiscal space for investing and social spending would be debt relief which may take the form of either debt cancellation and/or debt rescheduling. It is through public debt relief that the IMF loan might actually lead to inclusive growth; otherwise, it will only add to the already existing debt and lead to further austerity measures.

In addition, the IMF has advocated for the gradual increase of value-added taxes – especially on gasoline, tobacco, and alcohol – until they reach 20 percent. Yet, there has been less emphasis on income taxation and corporate income tax. This directly translates to higher social costs for middle and lower-income consumers. Lebanon has always suffered from an unequal and corrupt tax system that does not generate enough revenue. Also, tax evasion is very common as the fiscal law is riddled with loopholes, deductions and exemptions (Assouad, 2021; Atallah et al., 2021). The revenue collected from taxation in 2017 amounted to 15 percent of the total GDP since most of the revenue comes from indirect taxation (Assouad, 2021). It is thus important to situate wealth taxation at the heart of any fiscal strategy provided for Lebanon. Wealth taxation, in a country where about 10 percent of the population monopolises 75 percent of the nation's wealth, is very much needed to mitigate the extreme levels of inequality and finance welfare services (Assouad, 2021; Atallah et al., 2021). Hence, what is required in the medium to long term is a move towards a progressive tax system that offsets income and wealth inequality.

In line with the need to reduce inequality, the IMF ought to advocate for the unification of

exchange rates to end arbitrage but only if this is accompanied by proper social protection schemes. Ever since the forceful release of the Lebanese Lira peg, the multiple exchange rate system that was put in place has been governed by ad hoc circulars coming from the Central Bank. The multiple exchange rate system has generated arbitrage profits in light of the dwindling of foreign reserves and the insolvency of the banking sector (World Bank, 2023). The multiple exchange rates in operation enlarged the revenue of the political-financial elites more so than of anyone else. The customs dollar exchange rate increased from 1500 LBP/USD to 15,000 LBP/USD in December 2022 and more recently to 45,000 LBP/USD, which primarily targets Lebanese consumers. Meanwhile, banks are only allowing depositors to withdraw their money (pre-crisis dollar) at the rate of 15,000 LBP/pre-crisis USD (World Bank, 2023). This is a basic example of how the Lebanese government is arbitrarily using numerous exchange rates that help in collecting more revenue with little to no consideration of the impact caused by austerity on members of the public. Therefore, a unified exchange rate is indeed necessary, but only if it is accompanied by social protections measures and exemptions for staple health and food products, which will prevent it from causing damage to the general public.

The IMF's third pillar – 'reforming state-owned enterprises, particularly in the energy sector' – also needs to be elaborated. When it comes to privatisation, the IMF is recommending a comprehensive plan for the energy sector which relies on implementing public-private partnerships. In reference to the government's book, most of the public resources in Lebanon are being drained annually over inefficient public sectors, especially energy and telecommunications (Jbeili et al., 2022). However, privatisation in the current political economy may lead to a reinforcement of clientelism in local service provision, which will end up transferring more power to an oligopolistic private sector, where actors are more likely to be politically affiliated, due to the difficulty of finding reputable apolitical companies willing to invest in this financially difficult environment. Given the lack of adequate regulatory frameworks and the low level of liquidity, Lebanese consumers might be left worse off when proceeding with privatisation, since the price they pay will be at the mercy of private companies seeking profit maximisation (Ray, 2023). As such, it is more advisable to look into regulatory measures that would help manage state-owned enterprises to limit the drainage of resources. A comprehensive plan for the energy sector, including a transition to renewable energy ought to be prioritised. Major steps have been achieved to develop Lebanon's energy sector in the direction of renewable sources (Moore & Collins, 2020; see also Moore et al., 2023). However, the full transition to renewable energy is also lacking the needed legal and regulatory frameworks that would encourage investment in renewable energy infrastructure (ibid).

At the same time, job creation should be prioritised as a third of Lebanon's labour force are out of work (ILO, 2022). Job creation can be accomplished through the structural transformation of the economy and a reconceptualization of its priority from accumulation of financial wealth into the development of high-productivity services and integration of technologies in the production process (Dibeh, 2021). For instance, investment in renewable energy infrastructure, agriculture and the environment could potentially unlock myriad job opportunities for people in Lebanon (Moore & Collins, 2020). Emphasis should be made on linking the skills of the growing labour force with the needs of the market to cover the existing labour market skills gap locally. A number of

strategies may be identified to help in this regard: (1) starting with directing public investments toward infrastructure, and incentivizing the creation of energy efficient technologies and green jobs; (2) supporting local production and the expansion of existing businesses; (3) providing entrepreneurship training for start-ups and existing small and medium-sized enterprises (SMEs) to further their competitive edge; (4) facilitating the access of local enterprises (and especially SMEs) to financial benefits such as access to credit and foreign currency deposits (ILO & UNICEF, 2022).

Finally, to address the IMF's fifth pillar, accountability must remain at the core of any comprehensive recovery plan set forth for Lebanon. Without accountability, any pathway towards inclusive growth will be hampered by the constant abuse of power in government along with the interference in the judiciary. The IMF's SLA recommends the creation of anti-corruption and anti-money laundering frameworks, but this will be rendered futile in light of the political interference in the judiciary. Therefore, a good course of action would be to lobby for the existing draft law which ensures the independence of the administrative courts (Ray, 2023). When the independence of administrative courts is achieved, a separate judicial independence law should support the independence of the judiciary across all branches, in line with Article 95, Section B of the constitution (ibid). There is no 'good governance' without having an effective and independent judiciary that abides by the rule of law.

CONCLUSION

Four years into Lebanon's crippling crisis and the political class is yet to reach a consensus over the most crucial economic, financial and political reforms. The intransigence in finding a consensus has become the best strategy for the elites in power to try to evade bearing the responsibility for the current crisis. Almost all of the ruling parties are benefitting from the political and economic systems locally and none of them wish to see the system restructured. The cost of this prolonged impasse, however, is rising by the day with devastating effects on the public and especially on the most vulnerable. Although this is the first time that Lebanon is filing an IMF loan request, the country has historically received international assistance from the donor community on multiple occasions in times of political and financial turmoil. Yet, such assistance has consistently failed to be invested in a better quality of life. Instead, it has been exploited for the benefit of the financial-political class and international donors' neoliberal agenda. In light of the current context, receiving a loan from the IMF may either situate Lebanon on the pathway to inclusive growth or prove to be devastating for the general public.

A growing body of literature has noted the shift in the IMF's narrative on loaning conditionality, moving from heavy market fundamentalism to a more equal and socially inclusive discourse. Yet, as we argue in this article, the IMF's work on fostering inclusiveness, reducing inequality, and strengthening social protection faces challenges and still seems to be rather vulnerable to elite wealth grabs. The IMF still approaches social protection from the lens of fiscal policy and targeted social assistance programmes rather than a deep policy diagnosis of people's needs. Social protection ought to be a core pillar of any macroeconomic strategy suggested to Lebanon. We acknowledge that the

SLA is a steppingstone towards a more comprehensive IMF loan programme which fully details the approach of the Fund. However, understanding and highlighting the loopholes in the SLA at an early phase is of crucial importance if a future loan is going to benefit the wider public rather than enabling the political and financial elites to continue business as usual.

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