

Lebanon Crisis Update

August 2022

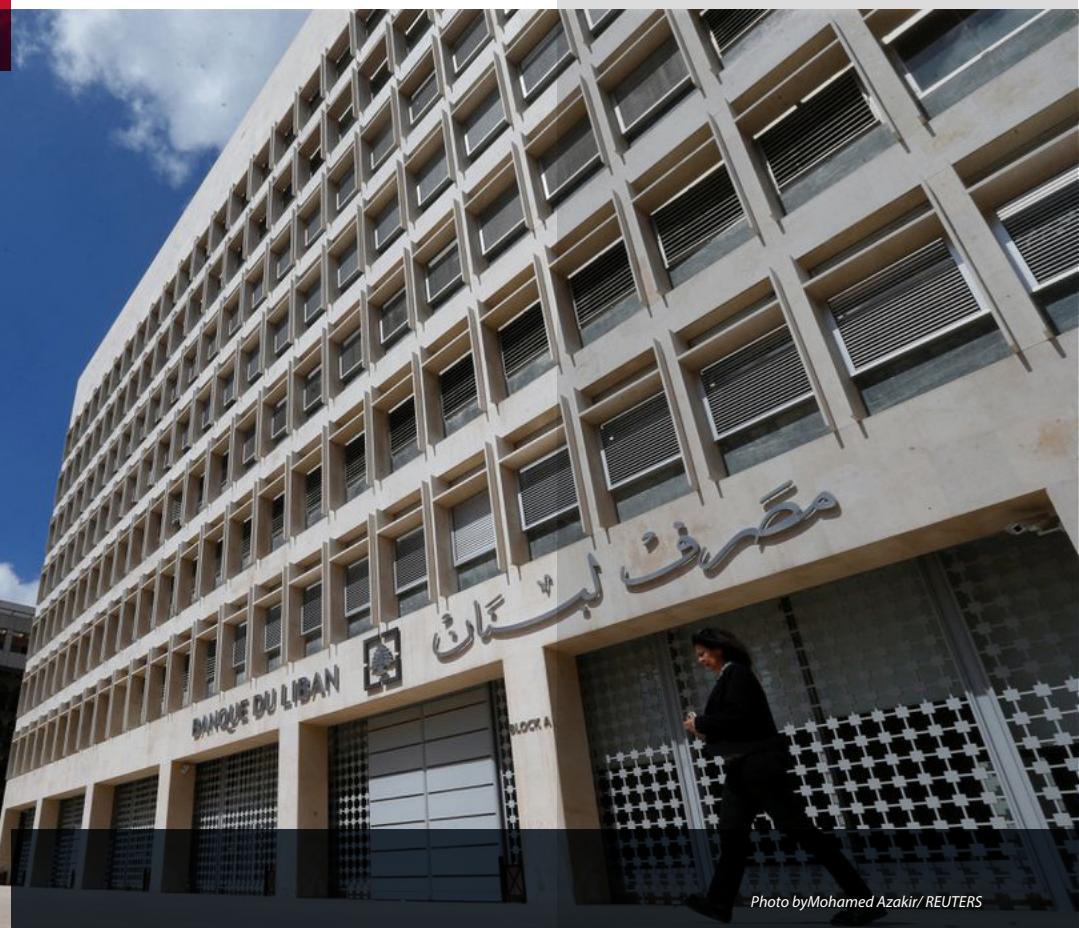


Photo by Mohamed Azakir/ REUTERS

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The Monthly Lebanon Crisis Update provides an overview of economic and political developments to alert the international aid response to new and emerging challenges that could impact the humanitarian situation in Lebanon. In the context of the multiple crises affecting Lebanon, the update tracks the impact of political developments on the economy, relevant international developments, updates on service delivery and governance issues, and analysis of the drivers of humanitarian need as they develop. The report also aims to provide nuanced forecasting on contextual shifts relevant to shifting needs and the implementation of humanitarian programming. The report draws upon a desk review of currently available literature, analysis of relevant quantitative data, and key informant interviews with a range of experts and individuals with knowledge of Lebanon's economy.

The Lebanon Crisis Analytics Team (LCAT) provides reactive and in-depth context analysis to inform the humanitarian community in Lebanon. The information and analysis contained in this report is strictly to inform the humanitarian response and policymaking on Lebanon.

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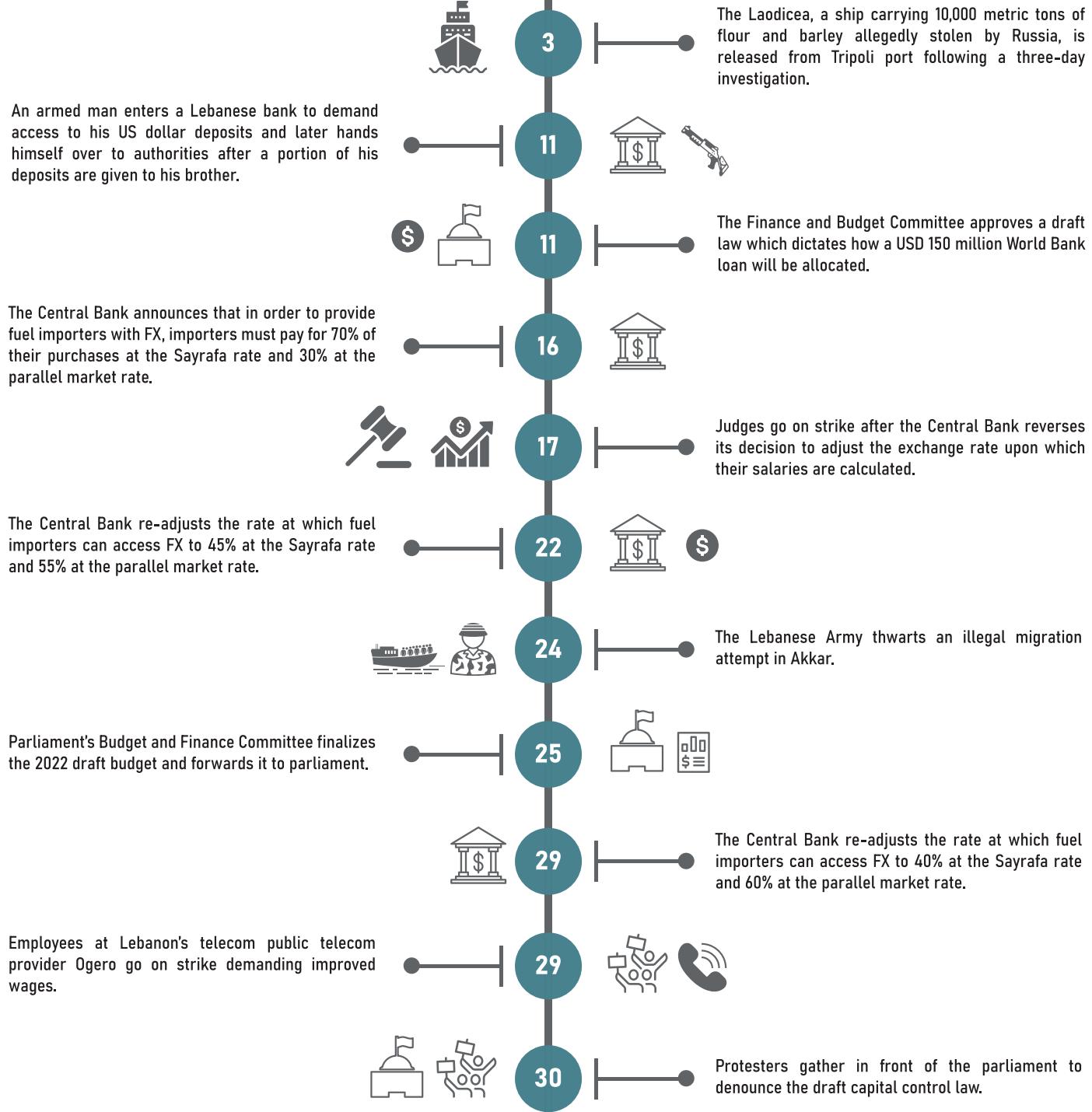


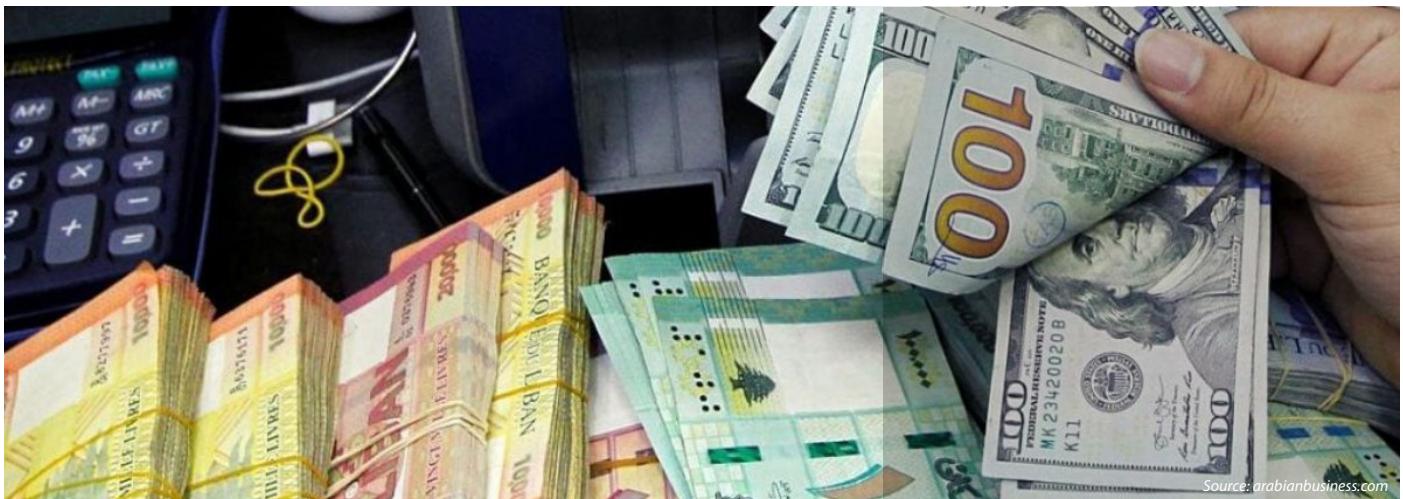
Key Findings

- The value of the Lebanese Pound (LBP) fluctuated against the US dollar (USD) throughout August and by the end of the month depreciated to about LBP 33,000. The depreciation appears to have been triggered by a continued decline in Sayrafa exchanges compared to previous months and a record amount of LBP in circulation. It is likely that the LBP will depreciate further in September, driven by fewer Sayrafa transactions, high amounts of LBP in circulation, and changes to import financing by the Central Bank.
- The Central Bank is steadily reducing credit lines for importers through the Sayrafa platform. Throughout August, the Central Bank decreased this effective subsidy three times over the span of three weeks by adjusting the percentage of foreign exchange provided to fuel importers via Sayrafa to 70%, then 45%, and then 40%. The rest is paid via the parallel market rate. This led to minor disruptions in the market and queues of cars formed around petrol stations as fuel prices increased, specifically 95-octane, 98-octane, and diesel.
- The Budget and Finance Committee completed its review of the 2022 draft budget and sent it to the parliament for approval. Notably, the draft budget does not contain a specific customs tax rate, fostering uncertainty about whether the budget will be passed or returned for another round of review. Changes to the exchange rate at which custom tariffs are calculated will likely lead to further inflation. Further delays in ratifying the budget will prevent officials from addressing the open-ended public sector strike and present additional challenges to unlocking IMF funding.
- A parliamentary session focusing on the capital control law was halted by MPs and met with protests outside the parliament, further delaying prospective implementation of the long-awaited law, which doubles as a requirement for a deal with the IMF. A separate IMF requirement, an amended the banking secrecy law, was sent back to the parliament by President Michel Aoun despite being approved by the parliament in late July. The IMF stated that the draft banking secrecy law does not meet its requirements and the parliament is expected to revisit the law in the coming month.



AUGUST





Source: arabianbusiness.com

Economic and Financial Updates

The Lebanese Pound (LBP) depreciated slightly against the US dollar (USD) throughout August and closed the month at about LBP 33,000. The LBP traded at 30,000 per USD 1 at the start of August and slightly depreciated early in the month, likely due to the August 5 Association of Banks in Lebanon (ABL) announcement stating that banks would go on strike on August 8 and August 9. ABL denounced the arrest of the Chairman of Lebanon's CreditBank Tarek Khalife in the first week of August and asserted that the strike was in response to "harmful stances" against the sector. Despite the ABL statement, banks decided to end their strike on August 9. The LBP-USD exchange rate reached LBP 31,000 after banks announced that they would not continue the strike, before dropping again on August 11, when depositor Bassam al-Sheikh Hussein stormed the Federal Bank in Hamra. Hussein held bank employees and clients hostage for several hours and demanded access to his dollar account to pay for his father's medical bills totalling USD 50,000.¹ The LBP-USD rate depreciated from about LBP 30,500 to LBP 32,000 after the event and continued depreciating thereafter, reaching LBP 34,000 on August 20 before appreciating to about LBP 32,000 on August 25. The LBP-USD exchange rate remained at about that level through the end of the month but depreciated again on the last day to close the month at around LBP 33,000.

USD 665 million was exchanged via Sayrafa during August. Despite a slight increase in comparison with the USD 619.1 million exchanged during July, August's total amount was about USD 298 million less than the USD 963 million exchanged in June and USD 400 million less than the USD 1.065 billion exchanged in May (see figure 2). During the second half of August, Lebanon's foreign currency reserves dropped by USD 400 million, reaching USD 9.8 billion, including USD 1.1 million in Special Drawing Rights. The Central Bank increased the amount of Money Supply² in July and August, reaching a record LBP 61.25 trillion on August 14, after decreasing to LBP 55.3 trillion in June, surpassing the previous all-time high of LBP 60 trillion in May. Money supply then dropped to 59.2 trillion LBP on August 25 (see figure 3).

¹ Hussein then handed himself over to authorities after the bank delivered USD 35,000 to his brother, out of the USD 210,000 that Hussein holds in deposits at Federal Bank.

² M1 Money Supply: LBP in circulation + Sight Deposits in LBP

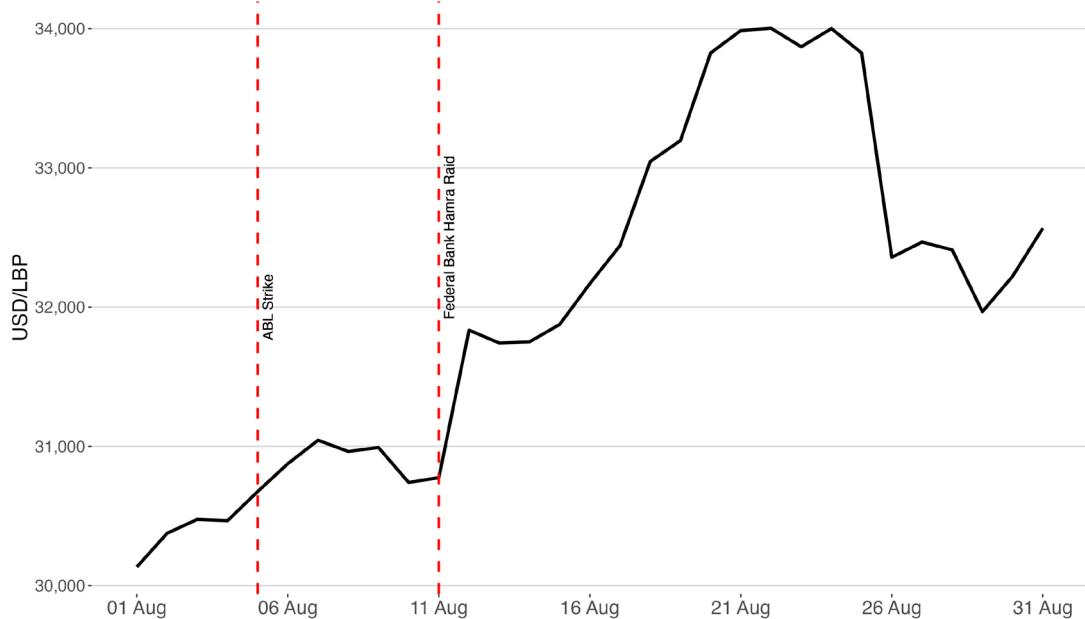
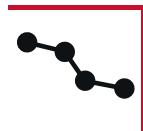


Figure 1: Parallel Market Rate VS Events in August

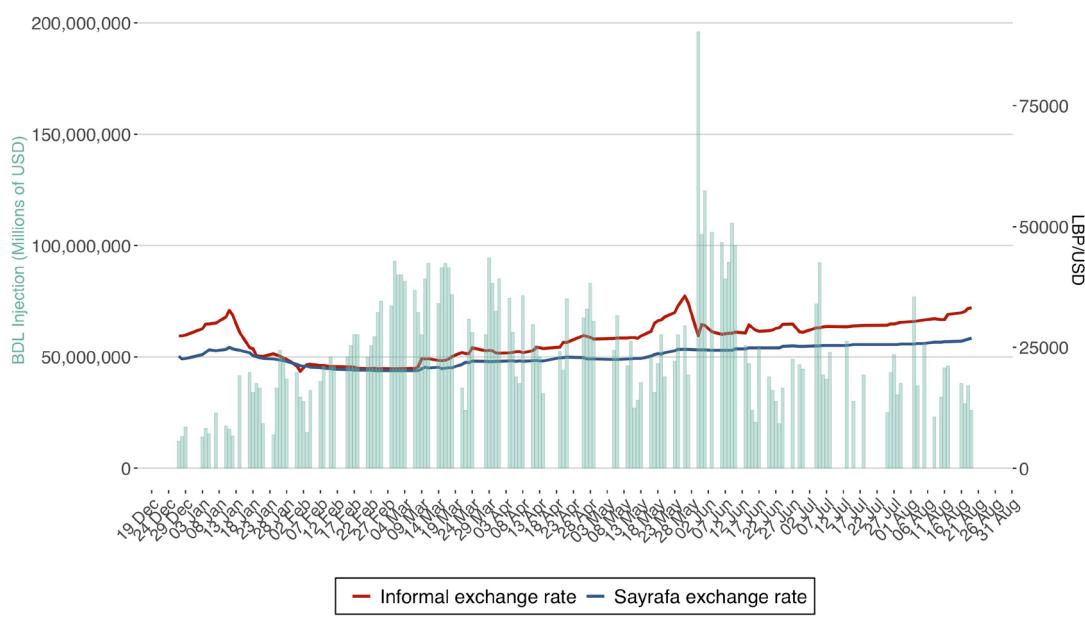


Figure 2: Sayrafa transactions VS Market Rates³

³ Source: Central Bank - [lirarate](#)

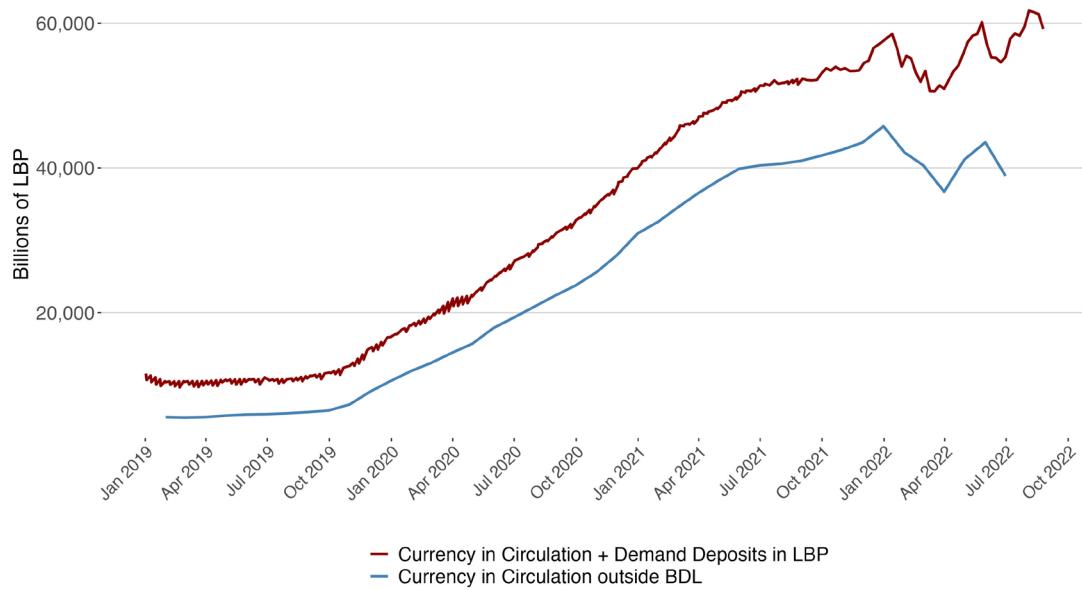
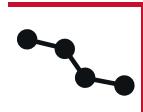


Figure 3: Money Supply and Money in Circulation⁴

The Central Bank announced major changes to the way it provides credit to importers, reducing the percentage of FX provided to fuel importers via the Sayrafa exchange platform three times in August. Queues formed at some petrol stations across the country and prices increased as the Central Bank announced the reduction of effective fuel “subsidies” throughout August. In May, fuel imports were entirely paid at the Sayrafa rate, when the Minister of Energy met with Central Bank Governor Riad Salameh and proposed that fuel imports be effectively subsidized fully for another two months via Sayrafa.⁵ However, on August 16, the Central Bank announced that fuel importers are required to provide 30% of FX import payments in USD (at the parallel market rate) while 70% would be exchanged at the Sayrafa rate.⁶ This policy remained in place for only one week, as the Central Bank decreased the rate at which fuel importers could access FX via Sayrafa to 45% on August 22. This rapid shift in strategies led to further questions over the Central Bank’s ability to continue providing USD for fuel importers at the Sayrafa rate with rumors circulating that the Central Bank will completely end fuel importers’ access to Sayrafa, leading to lengthy queues at petrol stations. The Central Bank released a statement on August 25, denying that it plans to entirely lift effective fuel subsidies. Despite this announcement, the Central Bank continued to reduce fuel importers’ access to foreign currency on the Sayrafa platform. On August 29, the Central Bank announced that fuel importers could exchange 40% of their foreign fuel purchases via Sayrafa. This impacted the prices of 20 liters of 95-octane, 98-octane, and diesel as highlighted in the following table.

⁴ Source: [Central Bank](#)

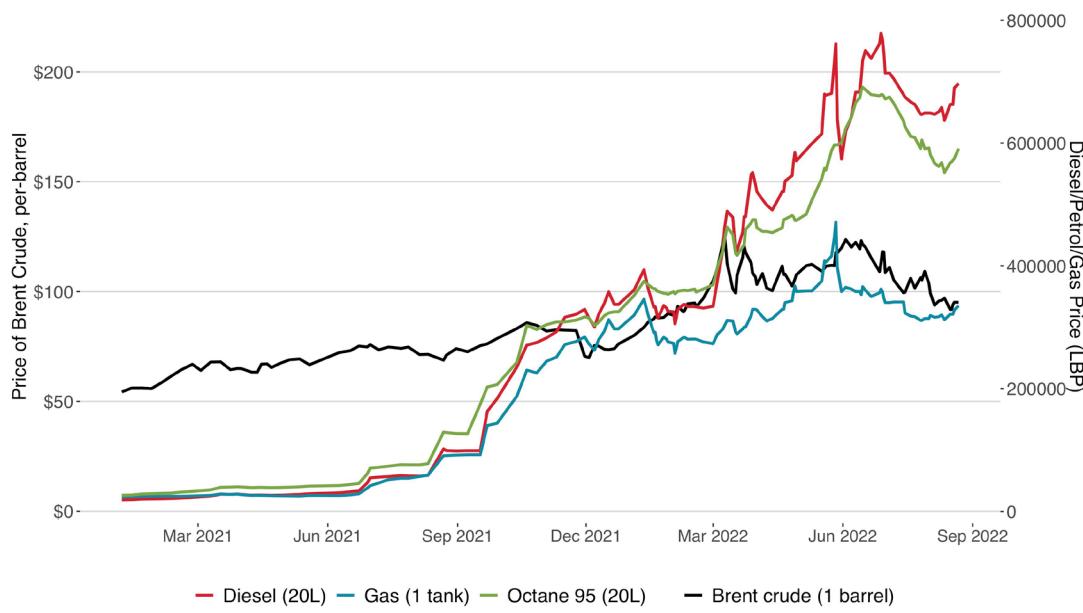
⁵ [Gasoline now 100 percent subsidized at BDL's Sayrafa rate - L'Orient Today](#)

⁶ Previously, importers were required to pay 15% up front in hard currency, with 85% provided through Sayrafa. This went to 100% through Sayrafa in May and June, before being amended downwards in August.



	20L 95-octane	20L 98-octane	20L Diesel	Gas-cylinder
Before august 16	552,000	564,000	637,000	312,000
August 16	568,000	580,000	663,000	321,000
August 22	584,000	597,000	709,000	330,000
August 29	589,000	602,000	705,000	319,000

*Table 1: Impact of Central Bank strategies on Fuel Prices*⁷



*Figure 4: Fuel Prices from March 2021 to August 2022*⁸

Debate over the exchange rate according to which import tariffs are calculated is threatening to stall passage of the 2022 national budget. Parliament's Budget and Finance Committee announced on August 25 that they finalized the 2022 budget and sent it to the parliament, despite not agreeing on the exchange rate on which import taxes will be based after initial proposals were shot down. Pressure has been mounting on Lebanese officials to finalize the budget amid a public sector strike. Talks over increasing public revenues are ongoing, with a focus on increasing import tariffs that could be used to fund a public sector wage increase. The initially proposed tariff rate would have brought it in line with the Sayrafa rate set by the Central Bank. However, the Budget and Finance Committee shifted towards introducing a new exchange rate specifically used to calculate customs taxes at LBP 20,000 per USD 1.

On August 24, the government engaged in talks over whether to increase the customs exchange rate directly or gradually. No decision was made and the Budget and Finance Committee approved the budget one day later without specifying an exchange rate. Various politicians have expressed concern over the impact of changing the customs exchange rate, as it could drive further inflation, with some speculating LBP prices could rise by as much as 30%.

⁷ August 16: 70% on Sayrafa -30% on Parallel-market rate
 August 22: 45% on Sayrafa - 55% on Parallel-market rate
 August 29: 40% on Sayrafa -60% on Parallel-market rate

⁸ Source: [lirarate](#)



Minister of Economy and Trade Amin Salam made what appeared to be contradictory statements on the impact of changing the customs exchange rate, first stating that the impact would be insignificant on August 18,⁹ while on August 21, he reportedly said that such a change would cause a 30% increase in inflation.¹⁰ According to a study conducted by LBCI, if custom tariff rates are calculated at LBP 20,000 per USD 1, prices of some goods will rise. Most importantly, the study projects a 27.48% increase in canned vegetable prices (a household essential) and a projected 25.35% increase in the price of imported cheese.¹¹

A joint parliamentary session convened in late August to discuss the long-awaited capital control law, as President Michel Aoun returned the draft banking secrecy law to parliament. The capital control law would legalize and standardize banking restrictions that were implemented at the beginning of the fiscal and monetary crisis in 2019. MPs decided to halt a session on August 30 and send the draft law back to the cabinet due to disagreements between MPs over the law itself and calls among lawmakers for Central Bank Governor Riad Salameh to attend sessions during which the law is debated and discussed. The session was held amid protests by a group of depositors. The draft capital control law was last discussed prior to parliamentary elections, but those deliberations were halted due to protests by depositors and civil society groups, who prevented parliamentarians from entering the sessions. Depositors claim the law is unjust, as it favors banks and would provide further powers to the Central Bank governor. On August 31, President Aoun returned the draft banking secrecy law to parliament - after the parliament had approved amendments to it on July 26 - over concerns that the IMF would not accept the draft legislation. In order to access IMF funding, the international financial institution requires Lebanon to pass a banking secrecy law "in line with international standards to fight corruption and remove impediments to effective banking sector restructuring and supervision, tax administration, as well as detection and investigation of financial crimes, and asset recovery." On September 2, the IMF announced that the current draft law does not resolve key deficiencies and called for further amendments.

⁹ www.arabnews.com/node/2145796/middle-east

¹⁰ [Salam: Prices of goods will increase 30% if custom tariffs are increased to 20,000](#)

¹¹ [Will raising price of customs dollar affect prices of goods-\[REPORT\] - Lebanon News](#)



Impact and Analysis:

Foreign exchange provided to importers via the Sayrafa platform are regularly being referred to as “subsidies” in the media, as the Sayrafa rate has been, on average, about 15% stronger than the parallel market rate (see figure 2). Forcing traders to purchase much of their required USD on the parallel market will lead in turn to price increases, some of which are already being realized. Heightened demand for USD in the market will likely lead to further LBP depreciation, compounding the inflationary effects of tightening importers’ access to Sayrafa. It is possible that newly implemented Central Bank policies regarding importers are part of a wider effort to draw more dollars out of the market towards import financing and reduce reliance on credit lines that are heavily, if not nearly entirely, dependent on dwindling FX reserves. Central Bank policy may stem from an assumption that the summer months led to an influx of foreign currency into the Lebanese market due to remittances and tourism. Of note, despite the expected influx of foreign currency, the exchange rate did not appreciate. However, some expect severe LBP depreciation, oddly enough, both despite and due to Central Bank policy. Without IMF funding, the Institute of International Finance warns that the parallel market LBP-USD exchange rate would reach LBP 110,000 by the end of 2026.¹²

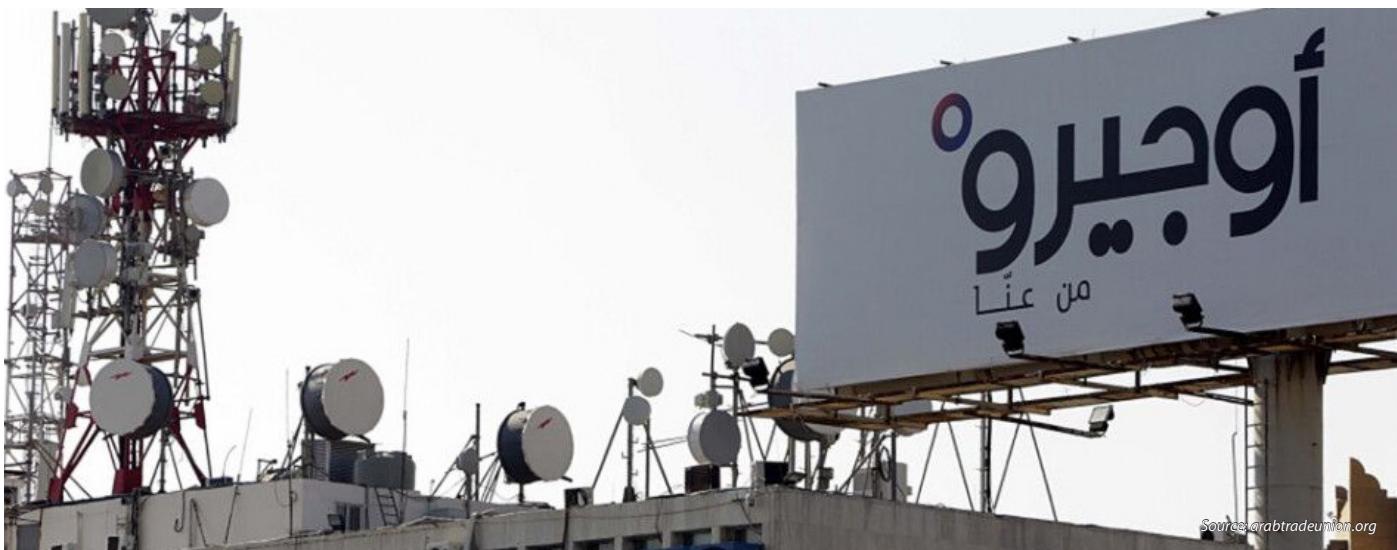
Expected increases in tariffs will also fuel inflation, while bringing much needed revenue to the state. Fitch Solutions recently revised Lebanon’s forecasted inflation for 2022 from 155.7% in 2021 to 178%, stating that this is due to the government’s proposal to adjust the customs FX rate.¹³ Additional revenue would be important for the Lebanese state to address its balance of payments, possibly mitigating negative effects on the LBP-USD exchange rate should public sector salaries be increased without corresponding revenue generation. The previous decimation of tariff revenues caused by calculating them at the LBP 1507 to USD 1 exchange rate has also had the effect of both significantly reducing the cost of imported luxuries, as well as critical commodities. This is likely reflected, for example, in data on imported cars, reaching USD 835 million in the first seven months of 2022.¹⁴ The prospect of imminent tariff increases may be driving importers to frontload stock, which in turn will impact demand for FX on the market. While luxury car owners previously paid an additional 50% tax on imported vehicles, this has dropped considerably in USD terms.

Calculating tariffs at LBP 20,000 to USD 1 raises separate concerns, given that this would run counter to IMF requirements outlined in the staff level agreement about unifying LBP-USD exchange rates. Should the tariff be calculated at the LBP 20,000 rate, it would bring the total number of exchange rates in use to nine. This also potentially sets the stage for recurrent political battles over subsequent changes in the rate, should further depreciation continue to eat at government revenues. As has been observed regarding price controls for fuel and other items, this could have a disruptive effect on market activity, as buyers and sellers moderate their actions according to expected changes, rather than through normal market dynamics. It is therefore likely that market actors will adjust their habits ahead of the actual implementation of these decisions.

¹² [Without IMF aid, exchange rate could exceed LL 110,000 by end of 2026, finance institute warns - L'Orient Today](#)

¹³ [Lebanon Set For Second Highest Inflation Rate Globally In 2022](#)

¹⁴ [Customs.gov.lb/Trade Statistics](#)



Access to services

Many public sector employees remain on strike, despite some branches ending their work stoppages, others have joined. About 350 judges, some 62% of judges in Lebanon, announced that they joined the public sector strike on August 17, after the Central Bank decided not to grant them a “raise” it had previously stated would be implemented in July. The effective raise would have entailed calculating judges’ salaries according to an exchange rate of LBP 8,000 per USD 1 instead of LBP 1,507. Judicial sector employees remain on strike as well as those at the Ministry of Education, impacting thousands of students’ ability to register at universities. An ongoing strike by professors at the Lebanese University has prevented students from finishing their exams originally scheduled for earlier in 2022. Talks over increasing Lebanese University tuition are ongoing. The Lebanese University is the only public university in Lebanon that is affordable for most students (in lira-denominated terms), including the most vulnerable, but remains heavily underfunded despite generally maintaining a reputation of providing a high-quality education. The judicial strike adds to the list of public services and state institutions to which residents have limited access, if any at all. Public documentation is becoming extremely difficult to access and the latest judicial strike prevents people from obtaining needed legal papers, in addition to slowing or effectively halting progress in multiple court cases. Closing the courts leaves detention hearings on hold, which presents significant protection risks - including those held in detention ahead of trial or individuals in gender-based violence cases that are unable to obtain restraining orders against their abusive partners.

The increase in telecommunication prices in July was not met with an increase in salaries for either the state internet provider Ogero or telecommunication service providers Touch and Alfa, prompting employees to go on an open-ended strike and negatively affecting service. On August 25, employees at Lebanon’s only two telecommunication service providers, Touch and Alfa, announced that they were going on strike and demanding wage increases. On August 28, the employees halted their strike after they verbally agreed to terms, without announcing these terms to keep the deal confidential.



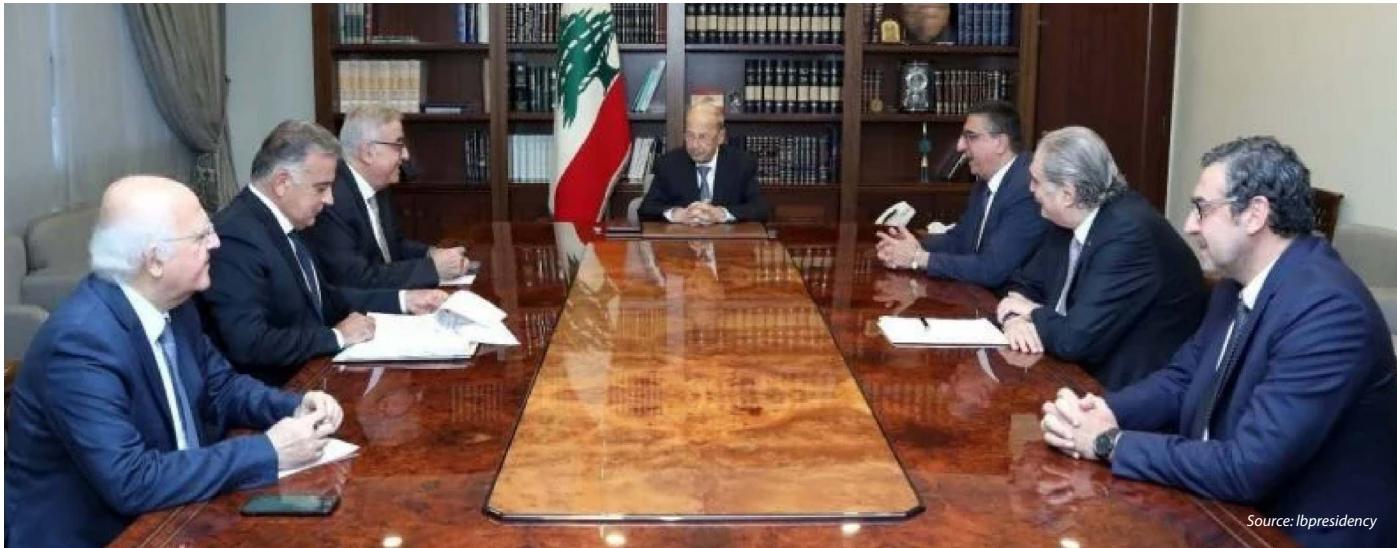
The verbal agreement is now in the Ministry of Telecommunications' hands, with employees threatening to go back on strike if a favorable agreement cannot be reached. On August 29, employees at state telecommunications provider Ogero joined public sector employees in demanding better wages and living conditions and went on strike. Shortly after the strike began, telecommunications services deteriorated across the country and completely stopped in the south on the last day of the month. According to Mercy Corps' focus group discussions held in August, telecoms price hikes from Touch and Alfa have driven many who cannot afford the service into depending solely on Ogero internet for connectivity. Therefore, disruptions to Ogero landline services will likely have a disproportionate impact on those unable to afford alternative access.¹⁵

Lebanese residents and citizens continue to attempt unsanctioned migration abroad via boat, driven by the continuing impact of the economic crisis. On August 6, more than 75 Lebanese citizens, mainly residents of the largely impoverished northern city Tripoli, were rescued off the coast of Turkey and taken to Spain. The incident prompted the Lebanese Intelligence services to arrest four Lebanese accused of operating a smuggling business and having connections to the rescued Lebanese migrants. These incidents appear to be becoming more frequent, particularly as deteriorating living conditions are prompting many to attempt unsanctioned migration. In January, 82 Lebanese migrants were captured by Greek and Turkish authorities and handed over to Lebanese authorities.¹⁶ In April, a migrant boat capsized just a few kilometers off Lebanon's northern shore, where 10 bodies were recovered that night, while 48 survivors were rescued. According to navy estimates, 30 people were believed to have gone down with the boat.¹⁷ On August 22, four months after the disaster, the rescue submarine funded by AusRelief arrived in Lebanon. The sunken migrant boat was discovered at a depth of 450 meters below sea level on which 10 bodies were identified.

¹⁵ For more on the impact of telecoms price hikes, see our recent [LCAT report](#).

¹⁶ [Dreaming of Europe ... 82 Lebanese went through hell in the Mediterranean - L'Orient Today](#)

¹⁷ [Lebanese submarine finds 10 bodies on sunken migrant ship - ABC News](#)


Source: lbpresidency

Political Updates

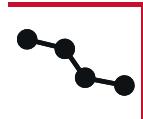
A Ministry of Displaced plan to repatriate Syrian migrants in Lebanon is fuelling intra-government tensions. After announcing the plan to repatriate Syrian refugees in early July, Minister of Displaced Issam Charafeddine arrived in Damascus on August 14 to head a delegation to discuss his plan with several Syrian officials. The Syrian Minister of Local Administration and Environment Hussein Makhlouf claimed during talks with Charafeddine that “the doors are wide open for a return of Syrian refugees, and the state is ready to provide them with everything they need”. He added that many displaced people have already returned and that he hopes “all displaced people” can return. Charaffedine and caretaker Prime Minister Najib Mikati reportedly disagree over the plan, with the former accusing Mikati of wanting to please donor countries. In a statement, Charafeddine stated that Lebanon has not ratified the 1951 United Nations Refugee Convention or the 1967 protocol. The minister claims this enables the Lebanese and Syrian governments to exclusively agree on a framework to return Syrian refugees and migrants without appealing to the international community or the United Nations.

Progress on forming a new government appears stalled, as President Aoun and caretaker Prime Minister Mikati remain divided on a prospective cabinet makeup. Despite multiple consultations between the president and prime minister in August, Mikati’s proposed ministerial lineup has not been met with Aoun’s approval. According to media reports, Aoun favors a government lineup largely similar to the caretaker cabinet, with six ministers being replaced. Mikati does not appear to favor these changes, particularly as many believe Aoun’s proposed changes would result in the Free Patriotic Movement controlling or effectively controlling one-third of ministers, a so-called “blocking third”. Aoun’s term ends on October 31, meaning the forthcoming government, if formed, would assume presidential powers until the next president is elected. Speculation over government formation delays have focused on this point as well as the fact that it is uncertain whether presidential elections will be held on time.



Looking Forward

- As Lebanon's FX reserves decline, it is likely that the Central Bank will continue to restrict the amount of FX being provided to importers through the Sayrafa platform. In this context, the LBP would depreciate in value, portending accelerated inflation in the coming period. This would result in ongoing price increases for critical commodities such as fuel, offsetting recent and ongoing global commodity price reductions, themselves driven by fears of global recession.
- Expected tariff increases could prompt changes in market behavior - such as preemptive price rises or hoarding - given the significant impact this will have on the cost of imported goods. The expectation of tariff hikes may have even triggered heightened levels of imports in recent months, as importers seek to stock their inventories amid lower taxation levels.
- The impact of price hikes and strikes on access to telecoms services will likely worsen in the coming weeks, notably if the Ogero network continues its service cuts. Already many have shifted to a dependence on Ogero landline internet to make up for an inability to afford Touch or Alfa mobile lines following the July rate increases.
- The 2022 budget likely requires further amendments before it can be ratified by the parliament, specifically due to outstanding questions over increasing public sector wages and changing the customs tariff exchange rate. Increasing public sector wages will likely bring an end to the ongoing public sector strike that has been disrupting state institutions and worsening service delivery. However, this may come at the cost of increasing LBP in circulation, which would drive further LBP depreciation and inflation.
- Further delays in government formation and prospective delays in the election of a president will slow progress on reforms needed to meet IMF benchmarks. Critical issues such as the 2022 budget, capital control law, and banking secrecy law remain outstanding. Other important IMF requirements such as bank restructuring, as well as auditing the Central Bank and top commercial banks in the country, will likely remain on hold.



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