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# Linking Economic Growth and Social Development in Lebanon

For

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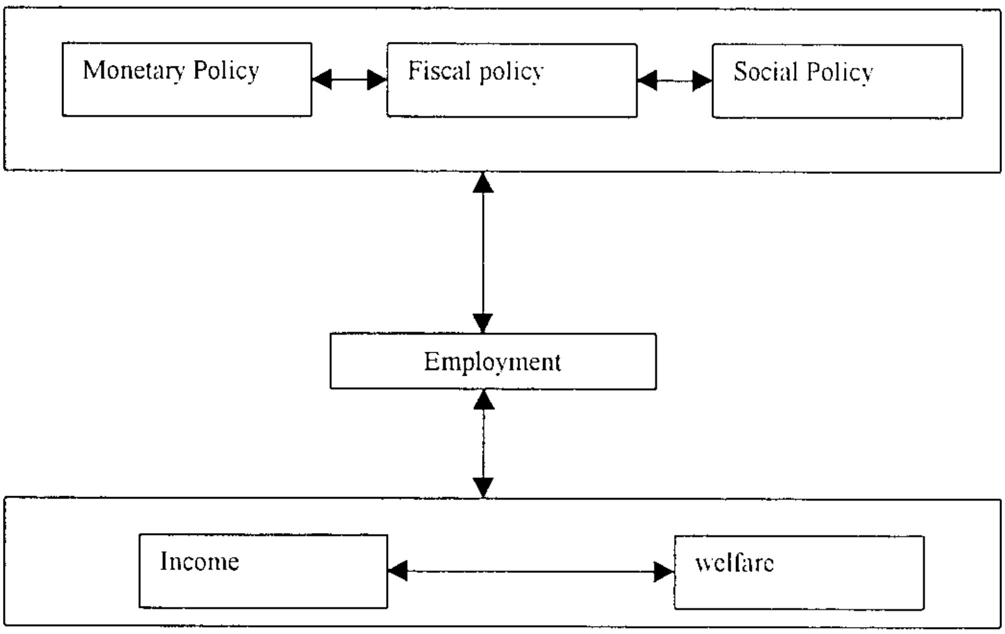
A link between economic growth- an increase in the rate of a country's output- and social development- a betterment of the quality of life- has been established. But how and to what extent does this macroeconomic variable affect social reality and vice versa?

The conference 'Linking economic growth and social development in Lebanon' held from January 11-13, 2000 in Beirut, Lebanon, attempted to examine this relationship in light of the growing international efforts to address the issue of poverty alleviation and improving social conditions of the residents, through the interaction of economic and social policies in developing countries in general, and Lebanon in particular. Fiscal policy, debt management, monetary policy, labor markets, and social sectors in Lebanon were discussed. Despite the relevance of the individual presentations on these topics, the main objective of the conference, the linkage among them was not clearly established, and remained elusive. Several factors limited the possibility of highlighting efficiently the link between macro-economic growth and social development:

- The first constraint is mainly methodological. In fact, the correlation between growth and social development could not be measured at one point of time, and needs some empirical evidence to be traced. Lebanon, lacks supporting data in this regard and most of related conclusions would be based upon observations or qualitative measurement.

- Most of the presented papers did not touch upon the linkage directly (though some of them did). In fact, the linkage between economic growth and social development can not be seen only as a vertical relationship between the two themes, it is, in addition, an interaction among the different agents involved whether at the macro level or at the social level, in light of the system of policies and regulations controlling these interactions.



An alternative approach for realizing this linkage could be by having the whole elements involved in this relationship, and analyzing the different possible interactions among them, the policies organizing these interactions, and the outcome of the whole system from the viewpoint of the different stakeholders: the state, the private sector, the civil society, the donors, etc....

Based on the presented papers, this report attempts to link economic policies to the social sphere, by focusing on the implications of the former on the latter, and vise versa (whenever possible). It is divided into three main parts. The first section is a brief overview of the theory underlying the link between economic growth and development. The second examines the current economic policies and the extent to which they yielded growth and promoted social development in Lebanon. The last section looks at prospects to reinforce the transmission of growth into development, which was mainly found to be weakened by institutional impediments, for Lebanon to be able to meet current domestic challenges and future global ones.

## I. Theoretical framework

At first glance, economic growth seems to only involve investment in physical capital. However, without a counterpart investment in human capital and skills, economic performance may not be as fruitful. Although the direction of the relationship between both is still subject to controversy, it is certain that additional resources created by economic growth, if any, trigger down to labor, the factor of production in question, only if employment opportunities are created across all factions of the population and sectors. The extra income generated to households improves their quantitative living standard (income), and if private resources are spent accordingly, their qualitative living conditions (health and education). The outcome is a more educated, empowered and productive labor force. Note that social development is not necessarily undertaken for economic purposes only but is also an end in itself.

A main party involved in facilitating the interaction between the economic and social spheres and paving the way for balanced and sustainable development is the State. First, through its economic, fiscal and monetary policies, the state is able to ensure that (i) economic growth occurs, a pre-requisite of which is a stable macroeconomic environment, and that (ii) economic growth is translated into social development through an equitable distribution of resources and access to public assets. Second, through its social policies, whether as provider promoter or regulator, the state could insure the accessibility to and the affordability of social services.

The provision of a favorable macroeconomic environment occurs through the adoption of economic policies that are growth-enhancing, coupled with social policies that ensure the benefits of growth are actually reaped in terms of better standards of living. Able to affect the consumption pattern of households, it can also ensure that private resources are spent in accordance with its vision of promoting human capabilities and ultimately social development. The implications of macro policy choices on micro variables thus become clear.

## A. Economic growth and social development: Which way is which?

Much debated is the issue of what comes first: Economic growth or social development? Alternatively, could they occur simultaneously? Research shows that no one country was able to reach what Prof. Amartya Sen, Nobel Prize winner of economics for 1998, calls the 'virtuous cycle of growth' by accelerating growth first without having advanced social development previously or simultaneously. But how could social realities initially be improved in an environment where growth is absent and resources scarce?

### *1. From growth to development*

In effect, what matters is not the level of income- though it is important- as much as the efficiency with which resources are used and income transformed into social development. This is where the role of the State is most needed. First, economic policies should provide a well-suited environment for economic growth. Second, social policies aiming at the distribution of public and private resources, the allocation of public expenditures, and the accessibility to public assets by various income groups regions and social segments, should ensure that additional income translates itself into balanced growth.

The extent to which economic growth would influence poverty reduction is still a controversial issue, and considered as the onset of the modern economic development. It is evident that decline in economic growth leads to an increase in the extent of poverty, meanwhile achieving certain levels of economic growth might and might not influence poverty reduction. Some observers would argue that attaining economic growth is a necessary but not a sufficient factor for improving living conditions of the population- mainly the poor. While some others argue that growth, regardless of its structure, is good for the poor. A study conducted by the World Bank using a sample of eighty countries over four decades, shows that income of the poorest bottom fifth of the sample population increases one-for-one with per capital GDP. Thus, income of the poor does rise with economic growth[1]. Other empirical analysis, however, suggests that initial income inequality influences the degree to which economic growth would reduce poverty. A more biased judgment could suggest that under certain circumstances growth could be accompanied with a transfer of wealth from the most poor to the most rich.

Generalization these observations might be misleading since the interaction between growth and poverty reduction is somehow subject to country specific policies and factors that mainly affect the distribution of income, the opportunities of the poor to contribute to growth, as well as the composition of growth.

Each of these suggestions could be valid given the targets set by the government, whether to achieve growth, or to limit budgetary deficit and control indebtedness. Whatever the objectives of the government would be, adequate social policies have to be there, whether

[1] Dollar, D. and Kraay, A., ' Growth is good for the poor', *The World Bank*, March 2000.

to insure a fair distribution of the outcome of growth, or to reduce the negative impact upon disadvantaged groups.

Government guidance may also be needed to overcome market failures resulting in under-investment in education and health by households, two main pillars of social development. This is so because household spending also plays a role in affecting social development. Notwithstanding the size of family income, what is of importance to sustainable and balanced development is the manner in which this income is spent to improve human capabilities rather than to plunge into conspicuous consumption. To which extent the government guidance could be fruitful in this regard is a matter of controversy, however could be indirectly reached, for instance, through better women education, given that the education and autonomy of women is crucial to the role women play in the household- mainly in identifying priorities of consumption- and defines their contribution to the process of development.

## *2. From development to growth*

The fruits of social development, mainly through better health and educational attainments, and its contribution to growth could be mainly tackled through the quality of labor the betterment of these conditions could result in. Quality of labor could be measured through not only level of skills but also through relative productivity.

While new growth theories have admitted the role social development plays in promoting economic growth, a skilled labour force alone is a necessary but insufficient condition for growth. This however does not undermine the significance of a better skilled population as a catalyst to growth.

In addition to higher levels of skills, the economic benefits of better health and education can be perceived through increased productivity once integrated in the job market as workers, managers or policy makers.

Various research and studies have examined the link from nutrition, health and basic schooling to GDP growth. Examples of some results include[2]:

- Increased calorie intake can lead to gains in labour productivity of up to 47% *(Doreid, 7)*
- A 10% increase in life expectancy raises the growth rate by an estimated one percentage point per year*(Doreid, 7)*
- A one-percentage point increase in the share of the labour force with secondary education leads to increases of 6-15% points in the share of income received by the poorest 40%. *(Doreid, 7)*

However, the smoothness of the link between better health and education, and growth highly depends on the state's social vision in formulating and implementing its policies,

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[2] The below mentioned figures are taken from Moeiz Doreid's paper.

and the ability of its apparatus to manage factor market policies to meet the needs of the economy and promote opportunities of employment. In most developing countries, the risk of lack of social vision and of comprehensive and coordinated policies should be taken as a possible institutional barrier in the transmission mechanism.

**B. Growth, employment and development**

Economic growth can improve people's lives through not only job creation, but also through the adaptability of created opportunities to the existing and prospective labor supply. Here, the problem of education, the output of which is basically the input to the labor market, would be raised, mainly as to its being a demand-driven or supply-driven education.

Employment is a major node in the link between growth and development. Even if additional income is generated by economic activities, it does not automatically generate employment, but may do so unevenly, leaving a likelihood of inequitable distribution of income in the absence of a trickle down effect. Hence the need for a sound employment policy that ensures well functioning labour markets.

Evidence from the experience of about one hundred countries in the eighties substantiates this claim. It revealed that in only one third of the cases did growth yield an expansion in employment opportunity. In almost one fifth of the cases, employment opportunities contracted despite growing income[3]. *(Doreid, 3)* Once income is not equally distributed, economic growth would tend to widen the disparities among various social factions rather than narrow them, thereby accentuating existing problems. Government action becomes highly crucial to correct market failures that tend to distort the distribution of employment opportunities. The form of government intervention depends upon their social strategies and is in reality relevant to some built-in factors in the countries themselves. For instance, at the supply level, this intervention might take the form of unemployment allowances, strict laws controlling competition with foreign labor, and other measurement. At the demand side, the government, as a promoter, could intervene in identifying the most suitable model that the country should adopt, and hence the areas of competitiveness of the economy and to translate its vision into practical measures that would yield employment generating and higher income activities.

**C. Economic policies, growth and development**

A stable macroeconomic environment that is conducive to economic growth is not the outcome of pure market forces. It is rather that of the interaction of government policies directed towards that end, such as growth enhancing fiscal and monetary policies that indirectly yield social development, or social policies that directly touch upon social development. However, policy makers should be careful when designing what they may see as suitable policies to foster economic growth. What is currently adopted by developing countries is "tailoring" the experience of developed countries to fit their

[3] These results can be found in Moeiz Doreid's paper.

current needs. This could be as dangerous as leaving the market forces to determining the path of growth. It might be true that no big variety of choices could be available, mainly when setting fiscal and monetary policies (either expansionary or contractionary), however, the accompanying social policies are relative to the country itself and must take into consideration the specificity of the country in question, and could never be "generic" policies.

### *1. Fiscal policy-growth-development*

The relevance of fiscal policy to social development rests on its ability to contribute to an environment that fosters economic growth generating an income effect and that promotes social justice through a welfare effect. The logic underlying the link between the fiscal situation and these effects is the following:

a) In the event of a balanced budget or budget surplus, in theory, the government need not incur any cost to cover for any deficiencies in its finances. If any, public debt does not impose a debt service burden nor does inflation pull up interest rates. Accordingly, fiscal policy does not hinder investment and growth is possible.

b) In the event of a budget deficit, debt is incurred in order to finance the deficit assuming that inflationary pressure is to be avoided. The increase in borrowing needs pulls up debt service. As more resources are allocated to financing the budget, less liquidity is available for productive investments thus forgoing growth and possible development related benefits. Also, social expenditures are curbed to contain the deficit thereby affecting the satisfaction of basic needs provided by the State, and decelerating social development. Moreover, taxes may be increased to generate public revenues and usually governments tend to resort to indirect taxation, being easiest in collection and could generate higher revenues. However the burden of this taxation burdens mostly the low-income segments. Further increase in taxation, given a declining trend of economic growth, would not result but in a further decline in economic growth.

How could fiscal policies generate income effect and welfare effect:

a) The income effect occurs through a release of resources to the private sector – or abstinence from taxing it- to be used in productive investment that would manifest itself as economic growth. Releasing resources will not be a sufficient incentive for channeling additional income into productive investment. Other measurement will be required in this regard, mainly as to providing the suitable investment environment. This additional income yields an improvement in social conditions assuming it is spent on health and education. The level of household disposable income is also affected by taxation. Accordingly, a balanced fiscal policy need not increase taxes – mainly indirect- on households thereby avoids a reduction in their spending on social services and living standards.

b) The welfare effect does not involve a pecuniary release of resources but directly increases availability and access to social services. When available, the public sector can

allocate resources to priority social spending from which all factions of society benefit. As a result, living conditions are ubiquitously enhanced.

Therefore, ensuring that sound fiscal measures are in place is a backbone to the process of development without which economic growth becomes increasingly more difficult and social justice less attainable.

*2. Monetary policy- growth-development*

A complement to balanced fiscal policy in promoting a favorable environment for economic growth is monetary policy. Notwithstanding the differences in monetary policy objectives across countries, the main purpose of such policy is to ensure price stability. Internal price stability aims at achieving low inflation rates. Accordingly, real prices of factors of productions, namely capital and labor, do not deteriorate in value. Lower interest rates will be conducive to investment and growth, which in turn will produce additional resources to be invested in social development. Real wages would not have to be eroded and result in a worsening of living conditions of workers.

External price stability ensures a stable exchange rate, something, which enhances the confidence in the domestic economy. This, in turn, favors investment and economic growth. However, sustainable price stability cannot be reached in the presence of fiscal imbalances, whereby deficit financing is inflationary or public expenditure money generating; should it co-exist with fiscal imbalances in the short run, it imposes a high economic and social cost. Nor can fiscal balance be reached with a monetary policy imposing high interest rates, which increase the cost of borrowing. Thus, coordination among policy objective is necessary for the desired objectives be harmoniously attained.

*3. Social policy - development*

Social policy is the tool by which the fruits of growth are, to the extent possible, evenly distributed in favor of all factions of society so as to establish social justice. Two main subsets falling under its umbrella are education and health, the two basic pillars of social development.

**a. Education**

Education is a crucial component to the transmission from social development to economic growth to social development. Through the educational system, the relevant skills and qualification needed by the labor market are extended to the potential labor force. Hence, economic growth is accelerated and additional resources are available for further promoting this aspect of social development. This highlights the necessary link between the educational system (supply of labor) and the labor market (demand for labor), which allows the latter to create its own flexibility to absorb people when employment is created by the investment of additional resources in productive sectors. It of course presumes that education is equally available to all and that it does equip students with quality skills to meet the needs of the market. It also assumes that the employment criteria are solely a function of qualifications. Nonetheless, education as such could not be considered as a basic tool for generating qualified labor. Other factors are to be considered such as the adaptability of the curricula to the market need, the cost of education and the accessibility to education by different social groups, regions and income levels.

**b. Health**

Investment in health is a basic component of social infrastructure that is most needed for development. Thus, any additional resources generated by economic growth, if channeled to that sector through an effective and well-managed health policy, will yield a direct return in terms of a more health population. In economic terms, this enhanced productivity will feed in the growth cycle thereby further accelerating it. However, unless access to basic health services is universal, equally available to all the population, a balanced social development cannot be pushed forward in the presence of disparities.

The role of the state is also crucial in health care provision, control and financing. Health care is a very sensitive issue that could no be left to market forces.

***4. Globalization- growth and development***

In an environment where economies are increasingly integrated, globalization affects all national policy choices, including their impact on social development. In developing countries, much attention has been drawn to trade liberalization as one aspect of globalization. The other two aspect, often less addressed initially, are capital mobility and labor movements.

Increased openness is seen to create wider markets, capital flows and technological transfers, thus increasing investment, productivity, growth and employment opportunities. The Hecksher-Ohlin model proposes that trade liberalization in specific, relates economic growth to social development through its effect on narrowing income gaps within the country- and with others- of the more abundant factor of production, whether skilled or unskilled labor[4]. Thus wage inequalities are deemed to shrink in favor of the more abundant factor whose wage and living standards thus increase. If the extra income is spend by the relevant households on basic social needs they failed to meet before the wage increase, then improvement in the social sphere is noted.

In most developing countries, labor is unskilled when compared with the skills of the labor force in developed countries. The mechanism by which this wage adjustment occurs is the increase in the demand for unskilled labor in the export sector if the ratio of skilled to unskilled labor is lower for exports than imports. This is to say that trade liberalization expands the production of export goods using intensively unskilled labor,

[4] This assumes that international capital movements are allowed, otherwise, the comparison would be between labour and capital as factors of production.

thus promoting growth through the channeling of resources to the export sector in light of increased trade.

Therefore, opening up the domestic economy has a positive impact on income distribution. However, a concurrent rise in growth and productivity in the export sector is necessary for liberalization to yield an increase in investment and employment. It is therefore crucial to invest in education for the efficient and effective use of technology and the upgrading of skills, apart from its benefit to the international competitiveness of the labor force, for income gaps to shrink and social improvements to be realized.

## II. Case Study: Lebanon

The relevance of the link between economic growth and social development is to be highlighted for today's Lebanon. The main challenge is not only to accelerate economic growth but also to translate it into social development, especially with the widening regional social disparities that have emerged since independence, and accentuated thereafter.

The 8.5% economic growth of the post independence era (1950-1974) was not balanced *(Charafeddine, 1)*, nor was the harsh economic reality of the civil war (1975-1990) a catalyst for an equitable and sustainable development. At the end of the war, Lebanon was faced with economic difficulties and a deterioration of social conditions. Economic policies, often uncoordinated and contradictory, were designed to redeem the economic prosperity of the pre-war period and stimulate economic growth. However, despite political statements highlighting the importance of balanced development across regions and sectors, attention as to how the benefits of potential growth could be evenly distributed was not adequately effected, as evidenced by the historical absence of a national development policy. What was and still, to a certain extent, prevalent is the focus on programmes benefiting Beirut and Mount Lebanon, rather than marginalized areas of the South, North and Bekaa. This has hampered the growth-development-growth cycle from generating a balanced distribution of resources regionally and sectorally.

**The concept of balanced regional development could be treated in a different dimension than the traditional one, i.e., providing geographic divisions with basic services and infrastructure and even investment incentives so that they can achieve a kind of self-satisfaction. Given the size of the country, regional development would rather have to take into consideration the de-facto concentration of services in Beirut and Mount Lebanon, and attempt at easing accessibility to the capital, whenever possible, rather than duplicating these services all over the country.**

### A. Diagnosis of the economic growth-social development link

#### *1. From economic growth to development*

Although much ambiguity surrounds GDP figures, there is a general consensus that Lebanon has witnessed high growth rates in the first half of the post war era due to the real estate and construction boom. Estimates suggest an average of 6.5% between 1992 and 1995, culminating at 8% in 1994. The second half witnessed a slowdown as the average for the period 1996-1998 decelerated to 3.5%, and a deep recession thereafter with a rate of 1% for 1999 and a forecast of 1.8% for 2000[5]. *(Doreid, 2).*

Official real GDP growth in Lebanon has been calculated by deflating the nominal GDP figure with the Consumer Price Index (CPI). The CPI could not be the best estimate of GDP deflator. Accordingly, a correction should be made by weighting the partial indexes of internal prices based on the structure of value added, instead of the structure of the consumer basket which includes a large imported component. Adopting this deflator, real GDP growth recorded in the 90's might have recorded far lower levels than the declared ones.

However whatever was the growth level, neither the acceleration of economic growth nor the subsequent recession was translated into an improvement in the quality of life for all factions of the population, leaving social development far behind. Additional income generated by economic activity, whether substantive or minute, was not equally distributed among factors of production, greatly disadvantaging labour as the share of interest in the national income bill more than doubled- while that of labour remains ambiguous- in an economy heading towards recession. In other words, the distribution was biased to those who are already in the higher income groups, i.e., debt instrument holders at the expense of lower income group of wage earners.

Given that Lebanon experiences a high concentration of income, with 20% of families earning 50% of income *(Maroun, intro, ii)*, it is clear that the unbalanced nature of growth in Lebanon has further accentuated income inequalities thus impairing equitable development rather than promoting it. In effect, the purchasing power of higher income groups increased by 4.8% annually between 1992-1999 while that of the middle income and lower income groups dropped by 8.4% and 4.6% respectively *(Maroun, intro, i)*. This erosion of income also manifested itself with the contraction of the middle class Lebanon was known for, with 61.9% of Lebanese families now belonging to lower income strata as opposed to 20.4% in 1974 only. *(Maroun, intro, i)*.

The unbalanced economic growth that led to a regression in the living standards of most Lebanese was paradoxically accompanied by a progress in the social indicators despite the slowdown since 1995 and the stagnation since 1998. Although still deficient relative to the needs of the people, the improvement does not reflect an advancement in social development as an outcome of the transmission from growth to development, but rather a uniform pattern of private spending on social services irrespective of the level of income.

Households of a lower income bracket allocate a higher share of their income to meet basic needs. They spend more than 40% of their income to meet basic nutrition needs *(Maroun, intro, ii)*, and around 8.1% on heath care. Around 15% of Lebanese population benefit from the health insurance provided by the State through the National Social Security Fund (NSSF). Moreover, two third of pre-university students is enrolled in

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[5] These figure are from Moeiz Doreid's paper.

private schools, thereby denoting the burden on families with limited income seeking quality education in light of the poor quality of the public schooling system and their limited supply despite increased social spending by the State.

Public provision of social services has proved poor and highly bureaucratic, reflecting the reluctance of those who can afford private services- and sometimes who can not afford- to resort to them. Even low income groups tend to use private educational services seeking quality of education, noting that around 51.1% of students living in households earning between LL 500,000 and 800,000 resort to private schooling. The higher the income bracket, the higher the likelihood that the more affluent use private social services.

This distinction between public and private has become a reflection of growing income disparities. Given the historically uneven distribution of income and the absence of a social policy, economic growth thus mainly benefited those who initially were at a regional advantage, reducing the quantitative and qualitative living standards of those already marginalised. In light of this reality, social development cannot said to have been enhanced despite the noted improvement.

*2. From social development to growth*

The conclusion that growth in Lebanon does not efficiently result in social development would hinder the possibility of measuring the impact of social development upon growth. In reality, this might be one of the factors that resulted in retreat in growth during the recent years. However, reverse direction of the cycle growth-development-growth could be traced as a simulation of what could have happened if growth was translated into social development.

Given the existing regional income and social disparities in Lebanon, we can deduce that the most healthy and well-educated faction of the population is concentrated in the area where most economic activity occurs. Note that not all of these skills are transferred to the production sphere given the lack of employment opportunities even within the more affluent areas. Although Lebanon does have high literacy rate in that respect (84%), the question is not only one of enrolment and dropouts but mainly of quality of education, which is directly associated with private schooling. The same logic applies to health services, which are mostly concentrated in Beirut and Mount Lebanon.

**The issue is that it the contribution of education to growth is uneven given the initial inequitable distribution of human resources ranging from the most skilled in Beirut and Mount Lebanon to the less skilled in the rest of the country. The benefit from economic growth to which this human input contributed self-sustains this unequal pattern of distribution of resources through the unbalance distribution of growth. It is therefore up to the State to implement a social policy that can change the pattern of growth and social development.**

**B. Diagnosis of growth-employment-development link**

Economic growth of the post war era was not accompanied by adequate job creation, thus the link to social development was insignificant, as the mechanism of transmission itself was absent. Official figures reveals that the unemployment rate in Lebanon reached 8.5%, which could not be considered as a very high rate. However the massive waves of migrations recorded during the period 1993-1999 suggested that the unemployment rate could have been much higher.

Some claim that it is not the link from growth to employment that was inoperative as much as the failure of government policy to effectively generate economic activity that is to blame for the lack of employment creation[6]. Whatever the argument is, the final outcome is that employment opportunities did not increase over the past years, leading to a deterioration of living conditions. One question could be asked which is whether the input to the labor was very high and could not be met, or it is the shortage in employment opportunities. Another question also could be asked whether the characteristics of supply were matched with those of demand. Again, whatever the argument would be, one conclusion could be made: labor market demand and supply were far from being matched.

The main reasons underlying the worsening of labour conditions partly relate to the general economic situation and partly to labour market specific distortions. The distribution of growth was unbalanced in its job creation effect, if any. As the service sector absorbed 65.1% of 1.36 million labour force at the expense of industry (14.7%) and agriculture (12%) in 1997, most of the employment opportunities generated were concentrated in that sector. This effect was also biased to the post war reconstruction boom, such that the construction sector, mainly a low-skill labour intensive sector, witnessed an increase in employment at the expense of trade and industry sectors which had the highest sectoral unemployment rate.

However, employment in construction was mostly captured by cheaper migrant Syrian labour, whose entrants reached around 450,000 between 1994-1996 *(Dagher, 7)*. The total number of foreign entrants to the Lebanese market ranged between 500,000 and 700,000 in 1993 and 1995 *(Dagher, 7)*. Foreign labour, which accounted to 34% of the domestic labour force, has put pressure on low skilled Lebanese workers- mainly on wages- or those who are more skilled but accepts to take a low skill job in light of the worsening labour conditions. These are reflected by an income level that is 30% that of the level of the 1974 level, average wages that dropped by 87% in the period 1984-1992 compared with 1974 figures *(Dagher, 8)*, and high lay-off rates in light of the economic recession.

Another controversial issue could be raised here also: does the market fail to create opportunities for high skill labor causing them to migrate, or the migration that occurred created a shortage in supply of high skill labor.

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[6] This view was expressed by Albert Dagher.

Some observers might see the massive waves of migration that took place during the war period created a shortage in the supply of skilled and educated labor. It was estimated that around 79% of who migrated were looking for employment *(Dagher, 9)*. This might have resulted in unmet demand for skilled labor.

The problem might be the other way around. As a matter of fact, the post-war economy might have failed, to some extent, in creating enough job opportunities for skilled labor. Also, the relatively low wages that skilled labour seems not to match their cost of living and the value of self-investment in education. Both these factors were push factors for the Lebanese skilled labor to migrate seeking better job opportunities and higher returns. The economic recession since 1996 deepened this phenomenon with the immigration of the labor force averaging 160,000 person per year. Many believe that this immigration tradition has avoided substantial increases in the unemployment rate, which in the post war period was about 8.5% in 1997, after having ranged between 20-40% between 1992-1990. *(Dagher, 5)*.

The migration of skilled labor has made Lebanon a transfer economy with transfer per year amounting to US$ 1.8 billion i.e. around 45% of GDP in early eighties *(Dagher, 14)* dropping 8-11% GDP for 1995 *(Dagher, 7)*. Thanks to these transfers, workers whose real wages persistently dropped were able to survive harsh economic realities.

Thus, transfers contributed to the maintenance of living standards of most families, something that has allowed the poorer faction to maintain a high share of their income allocated to the satisfaction of basic needs, namely health care and education. Accordingly, the improvement in social conditions was not the result of a growth transmission mechanism as much as it was partially externally induced. The sustainability of this reliance on transfers is however questionable as far as the consumption and production patterns are concerned. The presence of these transfers further highlights the distortion in the labor market as they suggest that wages need not necessarily be related to labor productivity.

**The problem could also have a totally different dimension: the time lag between the adaptability of supply to the demand and the volatility of demand could have together deepened the imbalances tin the labor market. As an illustration, the post-war growth have created a volatile demand for some high-skill jobs, for instance engineers, as a result of the construction boom. However, this boom did not last for more than 2-3 years, during which the supply for this category of professions increased significantly, resulting in a high unemployment rate among engineers afterwards.**

## C. Diagnosis of economic policies-growth-development link

### *1. Fiscal policy*

1.1 The expansionary period: 1992-1996

The economic model for post war Lebanon formulated by the 1992 Hariri government included an expansionary fiscal policy, able to meet the reconstruction needs of a country whose infrastructure was destroyed by 16 years of civil war. The increase in government spending in the reconstruction boom did stimulate aggregate demand, promoting economic growth, albeit inequitably in favor of Beirut and Mount Lebanon. Moreover, it occurred at the expense of increasing fiscal imbalances and accumulation of public debt, something that subsequently became an obstacle to growth. With increased spending and low revenues, the budget deficit to GDP widened to reach a record high of 23.6% in 1997 *(Deebeh, 5)*, while constantly being financed by increasing debt. Accordingly, the debt to GDP ratio increased from 56% in 1992 *(Doreid, 2)* to 113% in 1998 *(Azouri, 1)* with the debt service accounting for 26% in 1993 to 42% 1998 of total expenditures *(Azouri, 1)* and 88% of the scant public revenues *(Doreid, 2)* , the latter estimated at less than 18% of GDP in 1998 *(Azouri, 1)*.

Although wage adjustments were implemented in the post war era to compensate for the worsening of living conditions of workers, the absence of a well-defined wage policy discarded the cumulative drop in real wages incurred in the civil war. Thus, the increase in the wage level initially sought to improve the quality of life of workers did not necessarily reflect an improvement in social development.

Concurrently and controversially, increased public spending on wages was accompanied by tax policies focusing on revenue generation and overlooking social issues thereby increasing rather than reducing social gaps. Government measures aimed at promoting investment and increasing tax collection. For that, it lowered the ceiling of taxes on profit and income in 1993 to 10% to promote compliance to tax payments, and increased indirect taxes including basic utilities and services. Knowing that middle and low income brackets consume a higher share of their income on taxed goods, the regressive nature of indirect taxation made the lower income group worse off. Services most consumed by upper income groups were not subject to taxation. Thus, the tax burden mostly fell on lower income groups, worsening their quality of life, which was meant to improve with the increase in wages. This highlights the lack of coordination among different policy objectives.

This quantitative effect of fiscal policies on development was however complemented by a qualitative one. Public expenditures on basic social services maintained a good share of 22.2% total public spending i.e. 6.1% of GDP. Despite high social spending on education and health, the social outcome remain relatively poor.

At the heart of the problem are the quality, effectiveness and cost efficiency of public provision of social services, rather than the absence of resource allocation to these social sectors. Although the level of high social expenditures reflects the intention of the government to tackle social development through its fiscal policy, the issue is one of efficient and effective management rather than initial allocation of resources and falls outside the realm of fiscal policy per se.

1.2 The austerity period: 1996-to date

This expansionary fiscal policy created fiscal problems that substantially drained public resources to unproductive debt repayments, leaving less and less resources to be allocated to productive investment in the non-reconstruction sectors, thus undermining future growth. As such, the new government formed in 1998 devised a 5-year fiscal adjustment plan that sought fiscal sustainability as a catalyst to growth, in light of growing fiscal deficit and public debt accumulation. Four targets had been set:

a) First, a reduction of the budget deficit to 4.5% of GDP by 2003 *(Azouri, 2)*, something, which contains borrowing needs and releases resources to the private sector for investment thus promoting growth. This is expected to occur via an increase in revenues by 4.5% of GDP 2003, through tax reform and modernization (income and property tax law, VAT by 2001, global income tax, reform of tax administration, etc...) *(Azouri, 2)* that caters more attentively to equity issues. Concurrently, public expenditures are rationed such that real current expenditures go down to 28.6% of GDP by 2003, including a reduction by 5.3% of GDP of debt servicing cost over the five years. *(Azouri, 3)*

Privatization was also presented as a budget financing option that reduces the debt repayment burden. The proceeds are expected to be around US$ 4-5 billion *(Azouri, 3)* and the main sectors involved are telecommunications, electricity and airlines. However, although privatization does yield fiscal benefits, it is not a solution to fiscal problems per se as much as it is an incentive that promotes efficiency and ultimately growth. In Lebanon, the extent to which these efficiency related benefits can be reaped and transformed into growth are undermined by the prevalence of monopolistic market conditions. Moreover, a strong regulatory structure and sound macroeconomic conditions are needed, without which risk aversness may predominate on behalf of investors thus undermining the expected benefits and associated fiscal impact. Given that the current economic situation is very much handicapped, the potential yields of privatization are questionable[7].

b) Second, a debt of 96.3% of GDP by 2003 *(Azouri, 2)* whose management and structure is to be improved, with external foreign debt being contained at 35% of outstanding debt *(Azouri, 7)*. This goes, hand in hand, with the shift the government undertook in 1998 from domestic to foreign debt in order to reduce the high cost of borrowing, by taking advantage of the interest rate differential of around 5-6% *(Deebeh, 5)*. This strategy has however overlooked possible implications as to the hazards of a currency crisis and likelihood of default that could jeopardise the domestic economy and its growth.

[7] The above views about privatisation were expressed by Ghassan Deebeh.

Moreover, the substitution for foreign debt disregards the possible long run resource constraint on development finance.

c) Third, a decrease in interest rates on local and foreign debt that reduces the cost of borrowing to the private sector and enhances productive investment. *(Azouri, 2)*

d) Fourth, a growth rate of 5% by 2003 *(Azouri, 2)*, which, with increased focus on social and regional development programmes and a more balanced tax system, will trickle down to the majority poor of the population. Still, it is too early to assess the outcome of the current programme in its contents, deemed too austere by some, and with respect to its implications on social development.

### 2 Monetary policy

The hyperinflation of the war years was also accompanied by a depreciation of the exchange rate of the Lebanese Lira against the US Dollar, both of which has substantially reduced purchasing power in 1999 to 20.9% of what it was in 1974 *(Maroun, intro, i)*. As such, the post war monetary policy followed a stabilization programme, aimed at containing the inflation rate, bringing it down from a three-digit to a one-digit rate, and stabilizing the exchange rate. The impact of monetary policy on the general macroeconomic and accordingly on social environment was mixed.

Monetary policy did meet its target of gradually reducing inflation from 100% in 1992 to 10% in 1996 to around 4.5% in 1998. This has positively affected real wages whose erosion had thus decelerated. However, wage levels did not recuperate to the level that existed in the pre-war era, despite the various wage adjustments that took place in the nineties. Average individual wages stood at US$ 1,100 in the pre-war era as opposed to US$ 218 in 1997 *(Dagher, 7)*. Consequently, overall wages and purchasing power of wage earners remained low.

The restrictive monetary policy produced high interest rates that eliminated the positive effects created by the reduction in inflation on the macroeconomic environment. The interest rates on Treasury Bills were high so as to absorb liquidity from the economy and maintain a contractionary stance. On the one hand, this increased the cost of borrowing to finance the budget. Notwithstanding its non-inflationary impact as opposed to the pre-1992 money printing budget-financing practice, it thus imposed a high debt service burden on the government, further accentuating fiscal imbalances and negatively affecting prospects for growth. On the other hand, investment in productive sectors became increasingly expensive and undesired. In light of high return on Treasury bills, investment shifted from employment generating to lucrative, non-productive investments earmarked to finance the budget deficit. As a result, failure to absorb resources into productive sectors and the ensuing handicap in creating jobs broke the link to social development. Despite the intention to gradually reduce interest rates to foster economic growth, the contraction in the inflation rate brought down nominal rates while real interest rates remain high. Thus, the positive effects of reduced inflation did not translated into growth and development.

Faced with an exchange rate of the US$ vs. The Lebanese pound that had depreciated from LBP 3.25 in 1974 to 1838 in 1992, post war monetary policy sought to establish a stable exchange rate that fosters macroeconomic stability that encourages investment and growth. The adoption of an exchange rate peg resulted in the gradual appreciation of the Lebanese LBP to the US Dollar to 1500 in 1999.

The appreciation of the national currency vis a vis the US Dollar was coupled with a rise in the real effective exchange rate, the ratio of the price of non tradables to the price of tradables. This fact had a negative impact upon the international competitiveness of Lebanese good in international markets. Thus, investment in tradables fell causing economic contraction in light of growing trade deficits. These external imbalances further aggravated the worsening economic situation.

### *3. Social policy*

The post war era involved the formulation of a policy mix that was aimed at promoting economic growth. However, a social policy that effectively distributes this growth was not devised. Despite the allocation of additional resources generated by growth to basic social services, around 6.1% of GDP *(Issa, 2; A. Haddad, 1)*, the perceived improvement in basic social indicators (education and health) since the seventies, was not accompanied by an improvement in the quality, effectiveness, and access to the public provision of these services. Thus, the absence of social policy, and the prevalence of widening regional disparities undermined the impact of economic growth on balanced social development.

### 3.1 Education[8]

The education sector absorbed substantive resources, 9.3% of GDP, a ratio higher than the OECD average of 5.2% for the nineties *(data from LCPS report, 9)*. However, in light of the lack of social and developmental vision in the prevalent education policy, these additional public resources were not effectively channelled into social development, despite the noted improvement. The main reasons are threefold:

a) First, the absence of a link between the educational system and the needs of the labour market. Indeed, there was a mismatch between demand and supply in the labour market. The demand in the reconstruction boom was mostly for low skilled labour, which was captured by low skilled foreign workers. However, the demand for highly skilled labour was unmet, the reasons being that most had immigrated, were not specialised enough, or under-qualified. Thus, although the Lebanese are known to be educated, it appears that most of the existing range of more than fifty specialisation was not in demand by the labour market, given the lack of guidance to students. Specialisation as a pre-requisite for employment was also substituted for favouritism, something that introduced distortions to the employment mechanism.

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[8] Basic educational needs include pre-schooling, elementary and secondary schooling, and level of adult literacy.

b) Second, the low quality and high cost of education. Apart from the issue of lack of needed specialisation is the issue of under-qualification. Although **scant** data exists about the quality of education, the general impression is that it has been regressing since the outbreak of the war if one considers the component rather than the outcome of quality as such i.e. teachers, curriculum, methods, and school. The under-supply of high skilled people reflects the failure of the Lebanese educational system to deliver qualifications required today. The government's effort to improve the existing curriculum still fails to create a coherent, well managed and well taught system. The lack of unified criteria in private schools, deemed superior to public schools, also questions its quality with regards the need of the labour market. This low return from public education in specific is matched with a high cost. In 1998, the average cost per student per year stood at about LL1.9 million, a level comparable to LL2.2 million in private schools *(data from LCPS report, 9)*. The problem of quality of education also extends to universities and vocational training. For the former, this is reflected by the weakness of research, the lack of unification among different curricula and under one higher educational body, and the lack of supervision of quality following the granting of an operating license and the establishment of the university. For the latter, deterioration in quality in terms of curricula, management and the focus on theory rather than practice fails to meet the demands of the market, thus hampering the transmission from growth to development.

c) Third, the absence of social justice in the access to education. As previously mentioned, the initial regional differences in terms of human resource distribution and income inequality has been a main barrier to reaching an equitable social development especially with the absence of effective corrective policy measures. About one third of the population can hardly meet its basic needs *(31.2% in Amine, 7)*. Given the high cost of education, be it private or public, household spending on basic education remains low for the poor majority, although it takes a good part of their income. The outcome: 13.6% of the population aged more than 10 years old are illiterate in today's Lebanon *(Amine, 7)*. Despite high public spending on education, the coverage is limited to only one third of students. Basic education thus remains inaccessible to most children as dictated by the regional distribution and income group; 20% in the North as opposed to 9% in Beirut. *(Amine, 7)*

### 3.2 Health[9]

Mainly provided by the private sector, health services absorb a good share of GDP, around 9.2% of GDP in 1997 *(Azar, 13)*. Left unregulated by the State, the health sector in highly unbalanced in supply and access, oversupplied with irrelevant infrastructure and technologies, and is expensive. Being liberal in nature, it lacks universal coverage.

The lack of universal access to health services in Lebanon reflects the social injustice in the access to these services by all factions of the population, most of who are poor, as

[9] Basic health needs comprise basic health services, pregnancy and family planning, nutrition, provision of drinking water, low cost medication for poor people

accentuated by the concentration of the supply of these services according to regional disparities. Doctors, whose number has been growing overtime, are concentrated in Beirut (32.6%) and Mount Lebanon (34.7%), leaving the rest of Lebanon to be covered by 32.7% *(Azar, 6)*. Such oversupply of doctors as noted by a ratio per person of doctors falling within the OECD range (2.8 per 1,000) is coupled with an oversupply of unnecessary hospital infrastructure *(Azar, 6)*. These include hospital beds, 15,000 when the actual need is 9,000 most of which provided by private hospitals, and equipment and high tech units[10] that do not meet, if not exceed, the needs of the market *(LCPS report, 10)*. The reason for the divergence of the health sector from such needs is, not only the absence of government regulation, but also of the pursuit of profit making, the sector being dominated by private institutions. With their scant presence, public hospitals seem unable to compete due to high cost and inefficiency, which is directly related to the centralised nature of their administration and finances.

Given the commercial aspect of health services, the market structure of the health sector has been very oligopolistic since governed by commercial company legislation. More specifically, the ensuing exclusivity given for the import of pharmaceuticals, some of which are not registered, is at the heart of the high cost of medicine, and thus health care, as spending on medicine ranges between 30-40% of total health expenditures *(Azar, 8)*. In addition, the private doctors' charge is arbitrarily determined by the market and exceeds the ceiling imposed on public health consultations.

The charge for health related services, has been mostly borne by households, although the state does subsidise some. 53.8% of health related expenditures was borne by households, 16.1% by the ministry of health, and 11.2% by the NSSF *(Azar, 13)*. In 1998, around two third of these expenditures went to hospitalisation, with the share of hospitalisation accounting for more than 80% of the budget of the ministry of health *(Azar, 9)*, and 75.5% of NSSF's *(Azar, 14)*. This underlines the high reliance of public financing bodies on private hospitals, with which they contract thus imposing a high cost. Fewer resources were allocated to other needed health services such as basic health services and preventive health, the latter accounting for less than 2% *(Azar, 9)*.

Despite high expenditures on health services, the State leaves 58.2% of households with no coverage for health services *(Direction centrale de stat. in Azar, 14)*. In effect, the public sector only covered 13.1% of households, the NSSF 15.2%, and insurance companies 13.8% *(Direction centrale de stat. in Azar, 14)*. Because of the lack of distributive vision by the State and its regulatory weakness which resulted in half of firms not registering their employees with NSSF, effective and equal access to health services, specifically basic health needs, were not addressed. Rather, access was confined to those who had the income or political affiliation to received them.

10 High technology centres include 12 open heart surgery units, 12 in-vitro fertilisation centres, 39 center for renal hospitals in Beirut and Mount Lebanon

*4. Trade strategy*

Lebanon has shown commitment to follow up the globalisation trend that has dominated the international economic scene, as a means to promote sustainable economic growth which, coupled with increased employment, would positively affect social development. However, despite its intention and recent efforts undertaken in trade liberalisation, Lebanon suffers from the absence of a coherent and clear trade policy, often contradicted by other policies. Capital mobility is often unaddressed while lax labour movements have been confined to neighbouring Arab regions, as evidence by the unregulated flow of Arab workers to Lebanese labour markets.

Efforts towards the accession to the Euro-Mediterranean Free Trade Agreement and WTO are hoped to provide Lebanon with a wider market, larger capital inflows and enhanced access to technology, all of which would accelerate growth and advance social development. In the absence of an education policy that improves the quality of education and the competitiveness of the Lebanon labour force, a fiscal policy that reduces reliance on income generated by trade barriers[11], and a monetary policy that promotes internal and external stability in line with other policy objectives, the benefits from liberalisation cannot be reaped. It is worth noting that the benefits from liberalising trade with EU under the Euro-Mediterranean agreement seem scant as EU tariffs on Lebanese products are already low. It would therefore not expand the investment in the export sector as much as it would increase the import from the EU, Lebanon's main source of imports.

In general, Lebanon is more open than the average of developing countries in terms of trade, with a ratio of trade to GDP exceeding 100% for the period 1991-1995 *(M. Haddad, 2)*. This however, is not matched by export competitiveness as Lebanon imports are ten times more than it exports. In terms export structure, manufactured export accounted for about 70% of total exports*(M. Haddad, 2)*, an indication of a skilled labour force compared to the region but not the global economy. The export sector remains small as exports per capital stood at $330 in 1996, around the average for developing countries[12]*(M. Haddad, 2)*. Accordingly, Lebanon's trade structure, although orientated towards the production of skill-intensive goods mostly absorbed by Saudi Arabia and UAE, is highly unbalanced with more-skill intensive imports, which far exceed exports. Thus, the small size of the export market undermines the potential benefits that can be reaped in the event of higher economic growth and employment opportunities.

## D. Institutional barriers to growth-development link

Economic growth and social development are not solely the outcome of economic and social policies. Equally important is the institutional framework within which these

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[11] The weighted average tariff stood at 24% in 1996, **while ...% of government revenues were from custom duties in 19?** *(M. Haddad, 2)*

[12] Jordan had a per capital exports ratio of $1,034 compared to Israel's $ 3,615 ratio for 1996. *(M. Haddad, 2)*

policies interact and growth and development are fostered. In Lebanon, the transmission of growth through the various economic and social policies into social development have not been successful not because of policy specific ineptitude per se, but more because of a political, economic, legal, and social institutional settings that are impaired.

### *1. The State and public governance*

The role of the State, its embeddedness, and legitimacy are matters of importance to economic and social development. Without a clear vision for policy formulation and a coherent network for policy implementation, coordination, and supervision, economic growth cannot be effectively accelerated, nor can social development be advanced.
A developmental State would devise a comprehensive and harmonious policy mix bearing a social vision. Its provision of social goods is essential to transform economic gains to development benefits. A predatory state overlooks the provision of such goods. Lebanon is more of an intermediate state, where policies have been initially geared towards promoting economic growth and high public spending was channelled to the social sectors. The former proved uncoordinated while the latter inefficient and ineffective.

Because the state remains fragmented and lacks cohesion, it was unable to formulate harmonious policies, let alone ones with a developmental vision. Economic policies did aim at promoting investment and growth, but were often stifled by red tape and political balance of power. These policies also suffered from lack of coordination among ministries due to poor administration and/or lack of clarity of objectives. A classical example is that of fiscal and monetary policies, whose high interest rates used to provide stability accentuated fiscal imbalances. Some complementary policies, such as social policy, were ignored while a sectoral policy was absent.

The ensuing inefficient allocation of resources to different sectors, the lack of competence in public administration specifically debt management, the lack of transparency and data, the inefficient handling of daily work, the absence of objective standards in the regulatory and monitoring mechanisms, resulted in the inefficient conversion of economic growth to social development.

Despite the sizeable involvement of the State in the economic sphere (45% of GDP) *(LCPS report, 19)*, its social impact has been very minimal in terms of effectiveness, as state provision of social services only reached **one third of the population**. Thus, the state as an institutional mechanism has been a hindrance to the transmission of growth into development rather than a catalyst, in light of its uncoordinated and ambiguous policies, weak administration and control, and absence of national development objectives.

*2. Economic institutions*

The economic system in Lebanon is highly unbalanced and political. This has introduced market distortions to the economic sphere as an institutional barrier to first, generate balanced growth and then transmit it to development.

The income disparities have favoured Beirut and Mount Lebanon as opposed to the South, North and Bekaa regions. Having existed since independence and accentuated since, they represent a major hindrance for economic growth to be balanced. This is so because most investment benefited the regions that were most politically backed thus widening the economic inequalities depending on political affiliation. Investment in general has not been equitable. Bank credit was highly biased to few big customers, leaving smaller and medium enterprises less capable of accessing credit to finance investment, contributing to growth and reaping its benefits.

In the labour markets, such market distortions are evident by the employment mechanism governed by political favouratism and family ties, and the gap between the educational system and the needs of the labour market, which was maintained by government apathy in orientating the youth.

The government's failure to devise a clear trade strategy has resulted in a trade sector that has a structural bias in favour of imports, especially in light of the sustained appreciation of the Lebanese Lira against the US Dollar, something that has resulted in chronic trade deficits. The export market remains relatively small. In light of trade liberalisation, should the export sector maintain its size, with only imports growing, productivity gains and social benefits will be forgone.

Lebanese financial markets remain underdeveloped to be able to handle large privatisation flows and the ensuing legal handling of operations.

*3. Legal infrastructure*

The legal structure adopted in Lebanon is one of the major institutional barriers to growth and social development. First, most laws are outdated. Second, regulatory structures are absent or weak. Rigid and outdated legal structure are mostly observed in the minimum wage law, taxation and social protection laws. The first sets minimum wages at a very low scale. More importantly, the second, disadvantages those with lower income through high reliance on indirect taxation, and the tax exemption on interest earned from financial investment, which redistributes wealth from workers/taxpayers in favor of debt instrument holders, the more affluent faction of society. This is accentuated by the fact that corporate profits, capital gains and wealth are not adequately taxed. The implications of these legal deficiencies on social development are self-evident. The social protection policies in Lebanon the universal coverage, inadequate targeting criteria, multiplicity of the system, and high and replicated administrative cost (NSSF, Ministry of Health, Ministry of social affairs,..).

The absence of an effective regulatory framework has undermined various economic and social links:

a) First, the absence of control and supervision of public expenditures, in addition to the evaluation of the outcome. This has resulted in great inefficiencies and ineffectiveness, especially with regards the high social expenditures, whose return was minimal. It also imposed a high opportunity cost for the government in terms of tax revenue collection, something that harms the fiscal situation.

b) Second, the absence of standards for employment selection, replaced by favoritism, undermines the productivity of the labor force and consequently growth.

c) Third, the absence of standards to control the quality of education has greatly lead to its deterioration, something, which not only undermines growth but the quality of the progress in social indicators achieved.

d) Fourth, the absence of a control mechanism in the health sector, especially with regards the prices of services and their quality. Fifth, effective regulatory bodies do not exist to meet the ongoing trend of globalization and privatization. The lack of such institutional legal structure highly undermines potential benefits.

### *4. Social infrastructure*

The structure of Lebanon suffers from many drawbacks in terms of social issues. First, and complementary to income disparities, are regional disparities in human resources. As has been previously mentioned, household spending is highly crucial for access to education given that public spending only reaches one third of the population. Knowing that the majority of the population falls in the lower income bracket, those who are in the less affluent regions of the South, North and Bekaa are less privileged in terms of this access. Thus, with the more educated and skilled residing in the more affluent areas, Lebanon's social infrastructure proves highly unbalanced, making harder for growth and development to be balanced in the absence of an active role of the State with a social vision.

## III. Recommendations and their applicability

After having presented the main issues facing the economic and social sectors and defining the nature of the relationship between economic growth and social development in Lebanon, recommendation were brought forward to examine the alternatives to the worsening economic situation. First, economic policies that are growth-enhancing and forward looking, something which necessitates an effective state apparatus. Second, a national development policy that incorporates social vision to the economic policy mix and promotes the effectiveness of social service provision.

### 1. General State capacity

The question of the economic model needed for Lebanon highly relied on the future role and objectives of the State, requiring a dynamic vision that follows the rapidly changing global environment. Economic objectives were to be clear and harmonious and the state apparatus reformed, ensuring sound policy formulation, implementation and coordination among various ministries while improving public governance and competence. The State has to take active role in implementing legal reform so as to follow up international development, while adjusting existing legal deficiencies that hamper social development, and installing regulatory bodies that increase transparency and effectiveness. It is only then that economic growth is accelerated and its transmission into social development smoothened.

The applicability of such a framework highly depends on Lebanon's willingness to set clear objectives, embrace a developmental stance, and gain legitimacy and independence from political interest. The success of policy recommendation rests on state capacity to insulate itself from political conflicts, have competent policy markers and evaluators, and an efficient and modern apparatus that generates information for sound policy making.

### 2. Harmonised economic policies

#### *a. Fiscal-monetary policy mix*

A sound policy mix between fiscal and monetary policy is needed for macroeonomic stability to occur and economic growth to accelerate. The 5-year adjustment plan devised by the Hoss administration is too austere to generate growth in light the existing recession. The increase in taxes, the privatisation that potentially decreases aggregate demand, coupled with a contractionary monetary policy will not yield growth but rather ensure the economic recession continues to the end of the plan in 2003. The following four points were suggested[13].

First, fiscal policy must act as the steering policy of the economy towards growth through stimulating aggregate demand via increased public investment. Monetary policy is unable to undertake such role by fear of jeopardising exchange rate stability. This remains

[13] This view was expressed by Ghassan Deebeh.

debatable in light of the need to rationalise public expenditures, increase the revenue base and contain public debt, the latter having culminated in light of the high interest rates imposed by monetary policy. Second, monetary policy must abandon its strict anti-inflationary policy and shift towards the accommodation of the fiscal stimulus, thereby enhancing policy synchronisation. This ought to reduce interest rates and debt service while promoting investment. Third, quick fix solutions such as privatisation or borrowing should be replaced by a comprehensive modernisation of the tax system, an institutional structure for risk management and efficient debt management, coupled with a clearly defined debt strategy. In effect, attention should be drawn to the inherent risk of the debt substitution strategy undertaken in order to reduce the cost of borrowing as it increases the vulnerability of the domestic economy to currency crises. Fourth, privatisation should be postponed and should follow, not precede, economic recovery. A favourable macroeconomic environment is needed for its related non-debt relief benefits to be reaped.

However, economic policies should not only aim at promoting growth as such, but more importantly the pattern of growth, one that is job creating. Employment policy is thus crucial for allowing economic growth to meet social objectives.

*b. Employment policy*

To date, employment policy has been marginalised, as evidenced by the fact that the ministry of labour does not take part in economic policy making. Thus, the involvement of this ministry in the economic ministerial council, the main body defining economic policies, should be supported. This will allow the consideration of employment issues in national policy making and the formulation of an employment policy able to address the needs of the economy. It will also re-activate the role of state in establishing the link between the labour market and educational qualifications needed through its Employment Bureau, whose research department would act as a facilitator of information exchanges on the needs of the market and the available skills.

The formulation of an employment policy needs to be accompanied by a change in the current labour legislation that may hamper its effective implementation. Labour laws are outdated, overlooking labour working conditions, rights and security. In addition, the condition of Lebanese labour has been negatively affected by the flow of foreign labour, something that indirectly increased unemployment rates. Thus, labour and immigration laws should be subject to re-examination so as to promote the domestic labour condition, especially in light of the increased openness and future challenges.

It is important to re-emphasise that an employment policy, when devised, can only be useful if operating under a broad comprehensive strategy aimed at accelerating growth and promoting development.

## 2. A comprehensive social policy

So far, Lebanon had implemented economic policies that lacked social vision. The growth pattern focused on physical infrastructure especially with the reconstruction boom, something that brought less attention to enhance the efficiency of investment in human capital and the promotion of balanced development. This trend was maintained by the absence of comprehensive and complementary social policy that would channel resources effectively and evenly into the education and health sectors. Today, Lebanon needs to analyse the current conditions, challenges and prospects of social sectors, have a vision for socio-economic development, political commitment towards it, and formulate a comprehensive national social policy with clear objectives. The role of the State in this progression is pivotal. It should prioritise basic social services in public spending, identify those deprived or in the lower income brackets as the primary beneficiaries[14], work towards increasing the capacities of the ministries, reinforcing the coordination mechanism among them, and regulating them. The State should also seek to use the NGO network in the management and financing of public institutions providing social services.

### *2.1 Education*

The Lebanese education sector mainly suffers from deterioration in the quality of education in general and unavailability of equal access to schools. A main reason for this is the lack of a well-defined education policy, set standards and active supervision from the State. This is so because the actual strategy was to subject the education system to markets forces, where the role of the State was very much contained. To render more effective and qualitative educational services, the State needs to incorporate education policy in its economic adjustment plan while and strengthen its role through the active presence of the ministry of education.

a) First, the ministry should become less fragmented as an entity to improve its effectiveness. This suggests the merging of the three ministries of higher education and culture, vocational and technical training, and education. By doing so, decisions are more centralised and effective. Moreover, the ministry should act as an adaptation mechanism between the need of the labour market and the educational qualification offered by the system. This means that it should contain the expansion of university specialisations that are irrelevant to the job market.

b) Second, a national education plan should be devised with focus on the improvement of the quality of and access to education. The former imposes the adoption of standards such as the average of student per teacher ratio, number of students per classroom etc. The latter could be achieved by promoting free and compulsory education. This will allow

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[14] These include the following regions: Akkar, northern Baalbeck, Hermel, Marjayoun, Bent Jbeil, some regions of Tripoli and Beirut)

universal access to education for all children and need not be a costly option as funds currently granted to the education of civil servants' children, could be shifted to finance it. Concurrently, the minimum age for education should be raised from 12 years to 15 years so as to ensure that basic education is achieved by all.

c) Third, the supervisory authority of the state over the education sector should be enhanced so to so ensure that the quality is maintained according to the set standards.

d) Fourth, and a complement to the increase in quality of education, an effort should be directed towards maintaining the educational comparative advantage Lebanon is **known** for i.e. foreign languages, especially in light of globalisation and potential opening **up** of labour movements.

### *b. Health*

The dominance of the private sector undermined the role of the so-far ineffective State in the provision and regulation of the health service market. This resulted in a sector that was driven by the interest of suppliers rather than that of people, by high prices and limited access, thus yielding an inequitable distribution and access to all, in line with the existing regional disparities. To fall in line with the social vision to be adopted by the State, within the framework of a national development strategy, health policy makers ought to prioritise the efficiency and effectiveness of health services, equity and social justice.

Given that no ideal health system exists, due to the inherent moral hazard characteristic of insurance in general, Lebanon should work towards finding a system that is compatible with its needs and falling within its institutional reach. Recommendations[15] included the establishment of a compulsory health insurance scheme, the strengthening of the supervisory role of the State and the limitation of its role to this function only, the participation of the State in the insurance premium payment to ensure 'optimal protection', and an increase the independence of NSSF.

These measures however do not solely rely on State capacity but mostly on the people's willingness to buttress the capacity of the State. A starting point would be for households and firms alike to assume their responsibilities by paying their social obligations to the State.

## 3. A globalisation-oriented strategy

Lebanon's expectations that increased openness will yield and sustain a high path of growth while narrowing the widening gaps that have ravaged it, should be actively coupled with a dynamic strategy that is well-managed, comprehensive and forward looking. For that, a global and coherent national policy should be devised, taking into account the needs of the various sectors, in order to generate balanced growth. This

[15] These recommendations were suggested by Suzanne Azar.