

# Reconstructing Lebanon: Short- and Longer-Term Challenges

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## ABOUT THE AUTHORS



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## Brief Analysis

Lebanon has secured pledges for assistance roughly equal to its \$3.6 billion estimate of what is required to rebuild from the recent war. Though foreign assistance will be an important element in the short-term physical reconstruction, it will do little to help Beirut contend with the longstanding structural maladies afflicting the economy -- particularly \$40 billion in government debt. Lebanon also faces the challenge of how to reinforce central government authority in the face of Hizballah's efficient reconstruction efforts.

## Aid Pledges

Even before the fighting had ended, several Arab states had committed at least \$1.1 billion in grants -- \$500 million from Saudi Arabia, \$300 million each from Kuwait and Qatar, and smaller sums from other states. They also committed \$1.5 billion in loans to Lebanon's Central Bank -- \$1 billion from Saudi Arabia and \$500 million from Kuwait. Similar loans in the past have typically not been repaid. Further, several Arab States followed Lebanese prime minister Fouad Siniora's recommendation to "adopt a village." In addition to pledging \$300 million, Qatar said it would rebuild the southern Shiite Lebanese villages of Bint Jubayl and Khiam, while Abu Dhabi vowed to reconstruct and rehabilitate schools in south Lebanon and hospitals in Bint Jubayl, Marjayoun, and al-Arqub, and to provide compensation to some fishermen. More recently, Syria announced it would rebuild the towns of Qana, Siddiqin, and al-Qalilah.

Western and international pledges to reconstruct Lebanon have been equally impressive. On August 31 in Stockholm, Western government and international institutions committed \$940 million toward the reconstruction of Lebanon, surpassing the \$500 million target set earlier by Siniora. The accounting is a bit unclear; some of the pledges made seem to have included earlier announced aid. That said, the total pledged is at least \$230 million from the United States; \$112 million from the International Monetary Fund; \$91 million from the European Union; \$34.5 million from Spain; \$38 million from Italy; \$25 million from France; \$22 million from Canada; and \$20 million from Switzerland.

## The Hizballah Challenge

The funds raised at Stockholm should help insulate the Siniora government against some internal political challenges. In recent weeks, the government has increasingly come under pressure from Hizballah and its Christian ally, Michel Aoun, leader of the Free Patriotic Movement. Aoun, who signed an agreement with Hizballah in February 2006, continues to press his bid for the presidency -- a move opposed by the ruling coalition. Looking to capitalize politically from the war, in late August Aoun called for the Siniora government to "peacefully" step down, threatening: "If this change does not happen . . . there are other ways to escalate from now on."

To a large extent, opposition critiques of Siniora have been related to the government's handling of the war and the subsequent ceasefire agreement defining the mandate for international forces. But there has also been a good deal of criticism focused on the slow pace of government reconstruction efforts -- particularly when compared to the swift and comprehensive rehabilitation program currently being implemented by Iranian-backed Hizballah. Indeed, in addition to the \$12,000 Hizballah has already provided to each of 5,000 homeless families, press accounts indicate that Hizballah has nearly completed its own damage survey of the Beirut suburbs led by Hizballah's new organization Jihad al-Bina (the Jihad for Reconstruction). In addition to serving Shiite areas, Hizballah is also working in predominately Sunni areas, like the northern area of Akkar, where the Shiite militia reportedly recently repaired some two-hundred houses in thirteen villages.

The Siniora government's preliminary fundraising successes and the announcement last week that it would disburse \$33,000 to each family whose home was destroyed during the war may help to improve local perceptions of government effectiveness. But the real test in the coming months will be the government's performance in rebuilding Lebanese infrastructure and getting services back up and running.

During an August 23 speech on LBC television, Siniora announced the Lebanese government's reconstruction strategy. At the August 31 Stockholm Conference, the Lebanese government presented a paper detailing the "early recovery process," the national plan focused on preliminary reconstruction requirements, and cited several priority sectors for funding, including electricity (\$114 million), telecommunications (\$134 million), transport (\$484 million), and government infrastructure (\$4 million). This work, according to the report, is seen as a "stepping stone" to a forthcoming "comprehensive national reconstruction and development program."

#### Longer Term Challenges

Even if the Siniora government demonstrates itself to be an effective and credible agent of reconstruction, questions will remain concerning the central government's ability to rebuild the Lebanese economy. Indeed, the estimated reconstruction costs only amount to about 10 percent of Lebanon's current debt of \$40 billion -- roughly twice the country's 2005 GDP of \$22 billion.

Shortly after the Syrian withdrawal from Lebanon in March 2005, the Bush administration started discussions with the Lebanese government and the Europeans about convening an international conference focused on Lebanon's economy. The war delayed the conference, which was slated to discuss economic reform and debt relief among other topics, but it may be rescheduled for November 2006.

Given the current political and economic situation in Lebanon, however, it is difficult to envision the Siniora government committing to the type of deep structural reforms likely to be pressed at this conference. Initial Lebanese government figures suggest that Lebanon's GDP will shrink by 7-8 percent this year as a result of the war; prewar forecasts had predicted growth of 6 percent. (Other reports predict that GDP will fall by 10 percent this year.) In this context, the government will have a hard time pursuing the kind of economic reforms needed to resolve the debt crisis. Some of these steps, which the government had earlier considered, include cutting government fuel subsidies and raising value-added taxes on consumer goods. These moves would be very unpopular with the Lebanese public and would be exploited for political gain by Siniora's rivals.

Another important element in Lebanon's economic revitalization will be confidence in long-term stability. In a recent report, the Beirut Chamber of Commerce's Center for Economic Support estimated that the war will cost Lebanon \$3 billion in Arab investment this year -- nearly 14 percent of the 2005 GDP -- in addition to lost investments from Western nations. Lebanon is not likely to be able to attract the high levels of foreign investment it enjoyed before the war until the government takes steps to ensure that another war is not around the corner. Essentially, the large-scale return of foreign capital will depend in no small part on Lebanon finding a long-term solution for the disposition of Hizballah's weapons. Economic reconstruction, as well as regional stability, depends on resolving the issue of Hizballah's arms.

## Conclusion

Through the years, the Lebanese economy has proven resilient in the face of adversity. Even in 2005 -- the year that former Lebanese prime minister Rafiq Hariri was assassinated -- the economy grew by 1 percent. Going forward, however, the calculation is different. Not only has the regional environment changed, so have domestic Lebanese politics -- the most important aspect of which has been the emergent political clout of Hizballah.

If the past month is any indication, the Siniora government will not have a problem raising enough money for the physical reconstruction of Lebanon. More difficult, however, will be tacking economic reforms and generating confidence in Lebanon's stability. In this regard, Lebanon's long-term economic rehabilitation cannot be divorced from the status of Hizballah. In the aftermath of the war, the anomaly of Lebanon's economy thriving despite political uncertainty can no longer hold.

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