ECONOMIC AND SOCIAL CONSEQUENCES OF THE ESCALATING HOSTILITIES IN LEBANON

October 2024 - Rapid Appraisal

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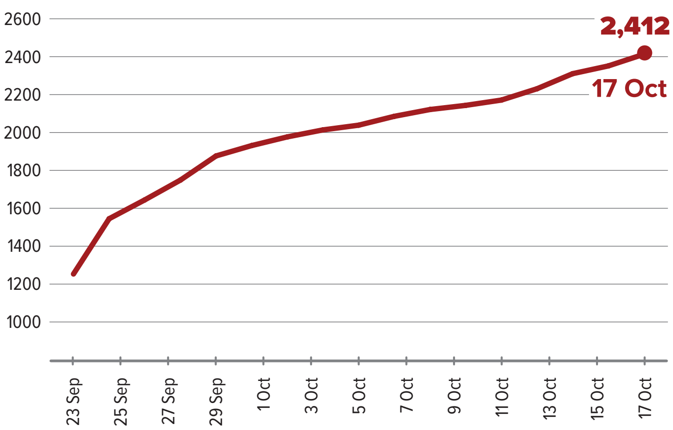
The escalating hostilities in Lebanon in 2024 strike while Lebanon is already weakened by years of political, economic, and social crises. Since 2019, Lebanon's economy has been severely impacted by a series of successive crises, resulting in a 28% contraction in GDP (at constant price of 2019) between 2018 and 2021[1]. The Lebanese pound lost over 98% of its value, triggering hyperinflation and significantly diminishing the country's GDP in dollar terms, while eroding purchasing power across the population.

The scale of the military engagement, the geopolitical context, the humanitarian impact and the economic fallout in 2024 are expected to be much greater than in 2006. The risk of broader regional involvement and the advanced military technologies employed in 2024 further distinguish it from the earlier conflict. As such, the escalating hostilities in Lebanon will have profound and far-reaching impacts on the country's GDP and employment.

Short-term Impacts:

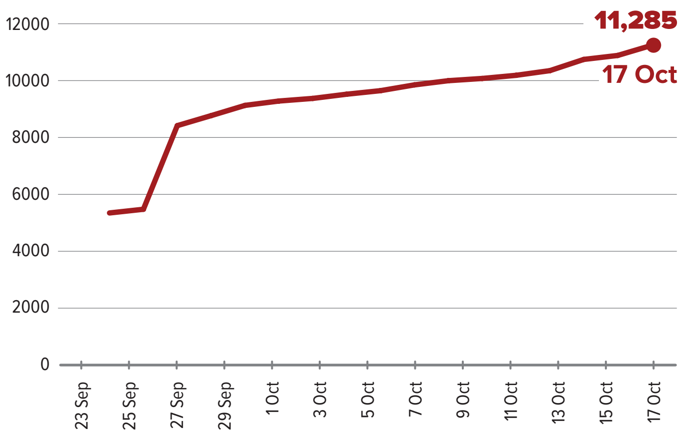
In addition to the tragic loss of **2,412** lives and **11,285**[2] injured, the ongoing conflict threatens to further destabilize Lebanon's already fragile economy.

Death toll in Lebanon since the start of the war in Oct. 2024



Source: PCM, Sitrep series no 2 – no 17

Number of injured since the start of the war in Oct. 2024



Source: PCM, Sitrep series no 2 – no 17

1 Central Administration of Statistics, National Accounts for 2018-2021.

2 Presidency of the Council of Ministers, Situation Report #21: Israeli Hostilities on Lebanon, October 17, 2024.

3 Team assumptions.

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Methodology

The report follows conservative economic modeling based on most available recent data especially for tourism and transportation sectors. Estimations were generated using a Computable General Equilibrium (CGE) model calibrated for the Lebanese economy. It is assumed that, in the absence of the conflict, the Lebanese economy would have followed the growth trajectory outlined in the most recent IMF review from June 2023.

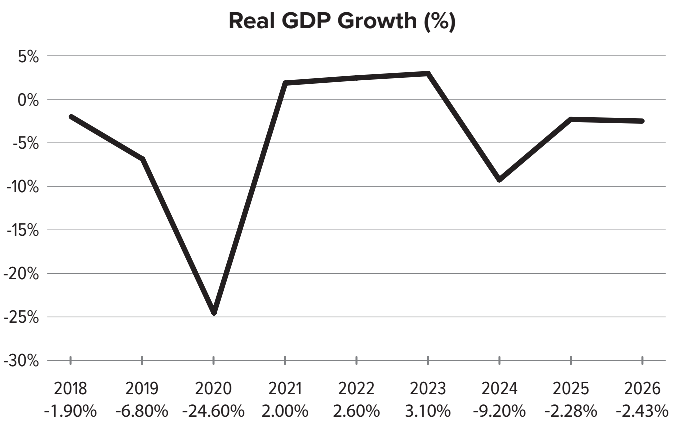
Estimations are based on two key assumptions:[3]

- **The conflict will persist through the end of 2024**, leading to a 20% decline in trade activities due to the closure of the Lebanese Syrian border, which is critical for trade routes. Additionally, the transport and communications sectors are expected to shrink by 10%, mainly due to reduced airport traffic. The broader services sector, including hospitality, recreation, and tourism, is anticipated to contract by 4%.
- **Capital destruction is assumed to be relatively limited across sectors.** The agriculture and livestock sector may face a 20% decline, while smaller reductions are expected in energy and water (2%), industries (2%), construction (4%), transport and communications (1%), merchant services (4%), trade (4%), and public administration (1%) .

The Short-Term Implications

The short-term implications are important and will affect all economic and social dimensions:

- **Economic Contraction: GDP is projected to decline** by **9.2%**[4] compared to a no-war scenario, indicating a significant decline in economic activity as a direct consequence of the conflict **(around 2 billion dollars)**. The **total economic damage** will not be far from the one estimated for the 2006 war which was around \$2.5 to \$3.6 billion (equivalent to **8% and 10% of Lebanon's GDP** at the time). The largest share of losses came from physical infrastructure, housing, and productive capacities (factories, power stations, etc.).



Source: 2018-2021: CAS National Accounts; 2022-2023: IMF staff review; 2024-2026 model estimate.

- **Job Losses in Key Sectors: Unemployment is expected to rise by 2.3 basis points (to reach 32.6 basis points in 2024)**, reflecting significant job losses and economic displacement. This decline is mainly due to the loss of labor demand in the following sectors:
  - **Tourism and hospitality:** The war caused widespread cancellations of hotel reservations and the collapse of tourism-related businesses, leading to significant job losses in this sector (5.1%).
  - **Agriculture:** Farmers and rural laborers lost jobs as agricultural production in war-affected areas plummeted. Many lost their livelihoods as the war destroyed farms and agricultural infrastructure (around 7%).
  - **Construction:** Although this sector eventually saw a boom during the reconstruction phase, in the immediate aftermath of the war, many laborers and workers in construction found themselves without work as new projects were halted and ongoing ones were destroyed (3%).
- **Micro, Small, and Medium Enterprises (MSMEs) Heavily Impacted**: The Central Bank estimates that MSMEs represent approximately 90% of the Lebanese economy, "with two-thirds of MSMEs concentrated in the Beirut and Mount Lebanon"[5]. MSMEs across the country have now been forced to close or suspend their businesses due to direct shelling, economic uncertainty, displacement, security risks, disruption in supply chain, in addition to decreased demand. Additionally, damage to essential infrastructure, such as electricity, communications, water supply, roads, and drainage, complicates business operations and access to workplaces, further reducing production capacity. Still under the ongoing burden of the economic and financial crisis, these MSMEs are likely to suffer indebtedness, inability to pay salaries, low production, business downsizing, and failure to meet financial obligations. As such, it is expected that rising unemployment among full-time, part-time, and daily workers will affect approximately 1.2 million employees in the country.
- **Negative Impact on Households' Welfare:** Consumer Price Index is projected to increase by 6%, while the exchange rate could depreciate. Private consumption could fall by 14.8%, a significant contraction in household spending, while private investment could drop by 2.77%, indicating a sharp decline in investor confidence.

4 These estimations are realized using a Computable General Equilibrium Model calibrated for Lebanon, while the no-war scenario was based on the last IMF review conducted in June 2023.

5 Market Overview of Small and Medium Enterprises in Beirut and Mount Lebanon- ICR- 2016.

- **Distribution of International Trade:** Exports are expected to decrease by 9.84%, mainly due to physical infrastructure damage and trade restrictions. Imports could decline by 10.87%, reflecting weakened domestic demand and challenges in accessing global markets.
- **Fragilization of Public Finance:** Total government revenue is projected to fall by 9.16% and increase financing needs by 30%.
- **Destruction and Strain on Infrastructure and Public Services:** Roads were heavily damaged, disrupting trade and economic activities for months after the war ended. Bridges, airports, and power plants are still at risk. This will contribute to a slower-than-expected recovery in GDP as reconstruction took years. Total investment could drop by 6.3% in 2025 and 6.3% in 2026, with private investment experiencing similar declines (6.6% and 6.7%, respectively).
- **Decline in Key Sectors:** The conflict will affect all the economic sectors. Agriculture and livestock are expected to see a 6.25% reduction, while the energy and water sector faces the largest decline at 24.5%, severely affecting utility supply. Industries may contract by 3.87%, and construction output could shrink by 1.2%. The transport and communications sector anticipates a 12.04% drop, highlighting major disruptions, while merchant services are projected to decline by 8.06%. Trade is expected to suffer a sharp 21.18% decrease due to logistical challenges and border closures. Lastly, public administration may experience a minor reduction of 0.95%.
- **Environmental Losses and Damages:** Since the outbreak of the conflict in 2023 and further to the recent escalation, massive environmental losses across different sectors including land use and land cover, biodiversity, and protected areas, agriculture, tourism, air quality, ground and surface water, soil, solid waste, in addition to the mounting volumes of debris. Contamination with unexploded ordnances (UXOs) and potential hazardous material further complicates these environmental challenges and could also be a threat to public health, particularly further to the use of white phosphorous and other chemical materials.
- **Internal and External Displacement** is expected to have affected over 20% of Lebanon's resident population (1.2-1.5 million by mid-October 2024). In addition, from September 23 to October 15, 2024, General Security has recorded the crossing of 329,386 Syrian citizens and 126,842 Lebanese citizens into Syria. However, the destruction of key Lebanese-Syrian border crossings will likely restrict further external displacement, increasing pressure on local communities and exacerbating humanitarian needs within the country.
- **Tensions on the Rise:** Alongside the significant displacement, tensions continue to emerge in many forms: inter-communal tensions fueled by existing anti-refugee sentiments; intra-Lebanese tensions stemming from perceived political and religious differences; community insecurity linked to the current displacement context; and vertical tensions directed at shelter management, partners, and local authorities. So far, local actors and authorities have managed to contain incidents, with no large-scale conflicts reported. However, the risk of further tensions remains high, as the ongoing crisis unfolds within an already strained environment marked by pre-existing inter-communal conflicts, rising hate speech, and unstable intra-communal relations, exacerbated by disagreements over involvement in the war.
- **Institutional Stability:** This violence has further compromised institutional capacities at all levels, with many institutions at both national and sub-national level now unable or seriously hampered to ensure crisis response, deliver essential services, and manage the mass displacement. As winter approaches, additional challenges in service delivery will arise at the subnational level. Compounding the situation are the exceptional challenges faced by security institutions. The economic and financial downward spiral has dramatically impacted their operational capacities and affected personnel's availability, with the concern now too often shifting from "inefficient" service delivery to "incapacity" to ensure basic security services. This is also applicable for key institutions playing a frontliner role to the response, including civil defense and fire brigades.

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The Long-Term Economic Consequences

Even if it ends in 2024, the consequences of the escalation of hostilities in Lebanon are expected to persist for years. Without substantial international support, Lebanon's economic outlook remains grim:

- **GDP** is projected to contract by **2.28% in 2025 and 2.43% in 2026** compared to a no-war scenario, signaling a prolonged economic downturn.
- **Unemployment** could rise by **1.3 basis points in 2025** and **1.4 basis points in 2026,** reflecting increased job losses and limited opportunities for employment recovery.
- **Private consumption** is expected to decline by **3.6% in 2025 and 2.8% in 2026,** as households continue to experience reduced incomes and heightened economic uncertainty.
- **Total investment** could drop sharply by **6.3% in both 2025 and 2026,** with private investment facing similar declines of **6.6% in 2025 and 6.7% in 2026**, reflecting low investor confidence.
- **Exports** are projected to decrease by **1.25% in 2025 and 1.39% in 2026,** while imports could fall by **3.07% in 2025 and 2.74% in 2026,** as economic activity slows and trade continues to be disrupted.
- **Public revenue** may decline by **3.22% in 2025 and 3.11% in 2026,** limiting the government's ability to fund public services and essential programs. **Financing needs** are expected to remain high, at 21.08% of GDP in 2025 and 27.49% in 2026, indicating a growing reliance on domestic debt to cover the government's funding gaps.


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Beyond Humanitarian Aid: What is Needed from the International Community

The ongoing hostilities will have significant impact on Lebanon with long-term economic and social consequences. Lebanon's Human Development Index (HDI) trend has been affected by the major internal crisis hitting the country since 2019. The impact of such crisis generally takes a few years to reflect on the HDI, affecting both present and future generations.

With living conditions in Lebanon severely affected and rising poverty and vulnerability rates, it is imperative for the international community to mobilize immediate humanitarian relief support. In parallel, development assistance needs to be mobilized to support economic, social, and institutional stability in areas such as water, food, health, sanitation, and infrastructure. International support, in line with the Lebanon Response Plan (LRP), should pave the way for future medium- to long-term recovery efforts whilst addressing the immediate needs.

Specific elements of this approach should include:

- **Prioritizing Stabilization of Key Institutions:** this includes supporting local authorities in effectively managing the high influx of displaced persons and ensuring their access to essential services such as waste, energy, and water. At the macro level, main services such as health and education need to be maintained. With a new task at hand, there is also a need to strengthen local authorities' capacities to manage and respond to the mass displacement crisis while adopting sustainable lasting solutions. This includes support to vwwv such as municipalities, the civil defense, and the Disaster Risk Management units. Finally, there is a need to enhance the operational capacities, territorial coverage, and effective security service delivery.

- **Support for Private Sector Recovery:** Lebanon's private sector, which includes key industries such as agriculture, tourism, and services, has been severely affected by the conflict and economic crisis. Investment levels have plummeted, and many businesses have shut down. Productive sector should be prioritized, particularly those providing the survival essentials such as agro-food and hygiene products, in addition to those directly attacked and suffering physical damages. **International financial assistance, including climate financing** and investments will be necessary to restore confidence in the private sector, facilitate access to credit for small and medium-sized enterprises (SMEs), and revitalize key industries. This could come in the form of **direct foreign investments**, soft loans, or credit guarantees to stimulate growth. Support MSMEs is also needed, through grants, provision of equipment, direct rehabilitation activities and technical support. Businesses also need to be supported to adapt to the changing market: including adapting their business models including exploring new markets, diversifying products or services, linking up to broader markets, and adopting innovative approaches to ensure business continuity.

- **Investment in Human Capital:** The war and economic collapse have resulted in a significant loss of human capital, as professionals and skilled workers have emigrated in large numbers. Educational institutions and healthcare services are underfunded and unable to meet the needs of the population. International financial support for education, healthcare and social protection systems is critical to prevent further erosion of human capital. This would include funding for healthcare infrastructure, and programs to retain skilled workers in the country.

- Lebanon's domestic and international financing instruments and policies need to be reviewed and made "fit for purpose" – in particular in the areas of **humanitarian aid, reconstruction, private sector revival, and currency stabilization**. For Lebanon to rebuild its economy and emerge from the conflict and crisis, a coordinated effort from international financial institutions, donor countries, and private investors will be essential. Such efforts need to be underpinned by a transparent and accountable nationally led aid coordination system. Capacities for evidence-based policy making, regulation, and coherent and integrated delivery of priorities need to be ensured. Without this support, Lebanon risks further economic collapse, exacerbated poverty, civil unrest and continued political instability.

- **Balance of Payments Support:** Lebanon has a severe **balance of payments crisis** due to declining exports, reduced **financial flows**, and falling capital inflows. The war has exacerbated this, further limiting the country's ability to earn foreign currency and service its external debt. **International financial assistance**, such as loans or grants from the IMF, World Bank, or regional partners, will be necessary to provide **balance of payments support** and ensure that Lebanon can meet its short-term import needs (food, fuel, medicine) while addressing its long-term external financing gap.

- **Reconstruction and Infrastructure:** The conflict and previous crises have devastated Lebanon's infrastructure, with the 2020 Beirut explosion alone causing between $8.5 and 10 billion in damages and economic losses. The current conflict has caused further destruction to roads, schools, hospitals, and other critical infrastructure. **International financing** is needed for large-scale reconstruction projects, including rebuilding the transport system, power grids, water facilities, and telecommunications infrastructure, in addition to addressing environmental damages in key areas such as agriculture, forests and land cover, protected areas, and solid waste, particularly for the debris management. Long-term financial commitment from international donors and institutions, such as the World Bank, IMF, and regional development banks, will be essential for sustainable recovery.

- **Need for Support to Social Stability and Ensuring a Conflict-sensitive Approach**: Within this volatile context, there is a risk that tensions could become heightened around aid as well driven by political divisions. Moving forward, competition over assistance could rise even further and become a major trigger of tensions. Therefore, it is crucial that partners coordinate with each other and with local authorities and apply conflict-sensitive approaches in their different work streams while responding to the emergency. Applying a tensions risk in targeting is of essence, ensuring that localities with pre-existing vulnerabilities and high levels of tensions are prioritized. There is also a need to strengthen local mechanisms for peacebuilding and conflict mitigation.