Socialist People’s Libyan Arab Jamahiriya
A Public Expenditure Review

(In Three Volumes) Volume I: Synthesis
September 30, 2009

Social and Economic Development Group
Middle East and North Africa Region

Document of the World Bank
CURRENCY EQUIVALENTS
(As of September 30, 2009)
Local Currency Unit = Libyan Dinar
Exchange Rate (1.27 LD per USD)

FISCAL YEAR 2009
July 1–June 30

WEIGHT AND MEASURES
Metric System

ACRONYMS AND ABBREVIATIONS

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ABC</td>
<td>Activity-based costing</td>
</tr>
<tr>
<td>AMR</td>
<td>Automatic Meter Reading</td>
</tr>
<tr>
<td>BCM</td>
<td>Billion cubic meters</td>
</tr>
<tr>
<td>BPC</td>
<td>Basic Public Congresses</td>
</tr>
<tr>
<td>Bpd</td>
<td>Barrels per day</td>
</tr>
<tr>
<td>CAPEX</td>
<td>Capital expenditures</td>
</tr>
<tr>
<td>CBL</td>
<td>Central Bank of Libya</td>
</tr>
<tr>
<td>CCGT</td>
<td>Combined Cycle Gas Turbine</td>
</tr>
<tr>
<td>CERA</td>
<td>Cambridge Energy Research Associates</td>
</tr>
<tr>
<td>CFL</td>
<td>Compact fluorescent lamp</td>
</tr>
<tr>
<td>CMM</td>
<td>Collection management and metering</td>
</tr>
<tr>
<td>CPI</td>
<td>Consumer price index</td>
</tr>
<tr>
<td>DBO</td>
<td>Design-build-operate</td>
</tr>
<tr>
<td>DPAT</td>
<td>Territorial divisions in charge of planned investments</td>
</tr>
<tr>
<td>DSM</td>
<td>Demand-side management</td>
</tr>
<tr>
<td>ECA</td>
<td>Energy conservation agreements</td>
</tr>
<tr>
<td>EPA</td>
<td>Effective project approval</td>
</tr>
<tr>
<td>FAO</td>
<td>UN Food and Agriculture Organization</td>
</tr>
<tr>
<td>FSA</td>
<td>Fiscal sustainability analysis</td>
</tr>
<tr>
<td>GBHCN</td>
<td>General Body for Health Care Planning</td>
</tr>
<tr>
<td>GCHU</td>
<td>General Corporation for Housing and Utilities</td>
</tr>
<tr>
<td>GCP</td>
<td>General Counsel for Planning</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross domestic product</td>
</tr>
<tr>
<td>GEA</td>
<td>General Environment Authority</td>
</tr>
<tr>
<td>GECOL</td>
<td>General Electricity Company of Libya</td>
</tr>
<tr>
<td>GER</td>
<td>Gross enrollment rate / gross enrollment ratio</td>
</tr>
<tr>
<td>GFS</td>
<td>Government Financial Statistics</td>
</tr>
<tr>
<td>GMMR</td>
<td>Great Man Made River</td>
</tr>
<tr>
<td>GMMRA</td>
<td>Great Man Made River Authority</td>
</tr>
<tr>
<td>GNI</td>
<td>Gross national income</td>
</tr>
<tr>
<td>GoL</td>
<td>Government of Libya</td>
</tr>
<tr>
<td>GPC</td>
<td>General People’s Committee</td>
</tr>
<tr>
<td>GPCA</td>
<td>General People Committee of Agriculture</td>
</tr>
<tr>
<td>GPCEWG</td>
<td>General People Committee of Electricity, Water, and Gas</td>
</tr>
<tr>
<td>GPCF</td>
<td>General People’s Committee for Finance</td>
</tr>
<tr>
<td>GPCHE</td>
<td>General People’s Committee for Health and Environment</td>
</tr>
<tr>
<td>FSA</td>
<td>Fiscal sustainability analysis</td>
</tr>
<tr>
<td>GBHCP</td>
<td>General Body for Health Care Planning</td>
</tr>
<tr>
<td>GCHU</td>
<td>General Corporation for Housing and Utilities</td>
</tr>
<tr>
<td>GCP</td>
<td>General Counsel for Planning</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross domestic product</td>
</tr>
<tr>
<td>GEA</td>
<td>General Environment Authority</td>
</tr>
<tr>
<td>GECOL</td>
<td>General Electricity Company of Libya</td>
</tr>
<tr>
<td>GER</td>
<td>Gross enrollment rate / gross enrollment ratio</td>
</tr>
<tr>
<td>GFS</td>
<td>Government Financial Statistics</td>
</tr>
<tr>
<td>GMMR</td>
<td>Great Man Made River</td>
</tr>
<tr>
<td>GMMRA</td>
<td>Great Man Made River Authority</td>
</tr>
<tr>
<td>GNI</td>
<td>Gross national income</td>
</tr>
<tr>
<td>GoL</td>
<td>Government of Libya</td>
</tr>
<tr>
<td>GPC</td>
<td>General People’s Committee</td>
</tr>
<tr>
<td>GPCA</td>
<td>General People Committee of Agriculture</td>
</tr>
<tr>
<td>GPCEWG</td>
<td>General People Committee of Electricity, Water, and Gas</td>
</tr>
<tr>
<td>GPCF</td>
<td>General People’s Committee for Finance</td>
</tr>
<tr>
<td>GPCHE</td>
<td>General People’s Committee for Health and Environment</td>
</tr>
</tbody>
</table>
Vice President: Shamshad Akhtar  
Country Director: Mats Karlsson  
Sector Director: Ritva S. Reinikka  
Sector Manager: Farruk Iqbal  
Lead Economist and Task Team Leader: José R. López-Cálix
# Table of Contents

**Acknowledgements** ...................................................................................................................... III

**Synthesis** ........................................................................................................................................ 1

**Main Messages of the Report** ......................................................................................................... 7

**Message 1: Make Public Expenditure More Accountable** ................................................................. 8

**Message 2: Preserve Fiscal Sustainability in the Medium Term** ...................................................... 11

**Message 3: Achieve High-quality Public Expenditure Management** ............................................. 13

  - Level 1. Setting an Aggregate Expenditure Ceiling Target ............................................................. 14
  - Level 2. Allocating Resources to Sectoral Priorities Efficiently ..................................................... 16
  - Level 3. Modernizing the Public Investment Management System for an Enhanced Technical Efficiency ................................................................................................................. 16

**Message 4: Raise Selectiveness with a Pro-Productive Bias in Choosing Public Projects** ............ 23

**Balancing the Efficiency and Quality of Education** ............................................................... 25

**Improving Health Services for All** ................................................................................................. 27

**Increasing the Efficiency of the Power Sector in Libya** ................................................................. 29

**Rebalancing Road Maintenance and Network Development** ....................................................... 31

**Making Water Use Efficient and Sustainable** .................................................................................. 33

**Final Remarks and Next Steps** ..................................................................................................... 35
ACKNOWLEDGEMENTS

This review is the result of a significant team effort. As such, it has benefited from an array of invaluable contributions. The review is based primarily on data collected during November 2007 and April 2008 World Bank missions and extensive comments provided by Libyan Authorities during a December 2008 seminar held in Tripoli.

The Synthesis Report, Volume I, was prepared by José R. López-Cálix (Task Team Leader), based on contributions from the team and following valuable suggestions from multiple peer reviewers and Bank management. He also wrote Chapters 1, 2, 4, and 10 in the Main Text contained in Volume II, while benefitting from contributions of Jorge Shepherd (fiscal trends), Khalid El Massnaoui (poverty map), Mouloud Mokrane (public investment management), and Olivier Le Ber (intersectoral prioritization) who provided valuable written contributions. Moataz El-Saïd and Khaled Sakr wrote Chapter 2 on fiscal sustainability. Khalid El Massnaoui wrote Chapter 3 on civil service reform. Hafedh Zaafrane, with contributions from Adriana Figueroa, wrote Chapter 5 on education. Heba Elgazzar wrote chapter 6 on health. Paul Noumba and Mohab Awad Mokhtar Hallouda wrote chapter 7 on power. Terje Wolden, with contributions from Olivier Le Ber, wrote Chapter 8 on roads. Nabil Chaherli and Mohamed Lahouel wrote Chapter 9 on water. Chapter 10 was a truly collective effort with all sector specialists, who provided written inputs. Mats Karlsson, Ritva Reinikka, and Marouane el Abbasi provided priceless guidance and enthusiasm throughout the process (all World Bank). Sheldon Annis and Diane Stamm edited the English version. Bank services edited the Arabic draft version of Volumes I and II. Volume III has the annexes (several contributors) and statistical appendix (prepared by Soumia Driouch and Khalid Alouane with contributions from Bachir Abdaym, Jorge Shepherd, and Khalid El Massnaoui).

Salvatore Schiavo-Campo (public investment), Ajay Tandon (health), Caroline Van den Berg (water), Robert Beschel (civil service reform), Ahmed Shawsky (water), Ananda Covindassamy (power), Sajitha Bashir (education), and Henry Keralli (roads) provided precious guidance and multiple suggestions as internal peer reviewers of the draft chapters. Valuable input and suggestions were also received at various stages of the project from Roberta Gatti, Farruq Iqbal, Mira Piqato, Mustapha Nabli, Paola Ridolfi, Philippe de Meneval, Mehdi Benyegoub, and Michel Bellier. The draft report was also reviewed by a Bank quality learning review team, which found it of good quality. Production support at various stages was provided by Soumia Driouch, Khalid Alouane, Sheela Reddi, Angela Hawkins, and Ludmila Melnikova. Marouane El Abassi provided excellent operational support to field research in Tripoli.

Warm thanks go to the Libyan counterpart team headed by Dr. Mahmoud Gebril, former Secretary of the Libyan National Planning Council, whose detailed guidance and suggestions were priceless, and Dr. Abdelhafid Mahmud Zlitini, Secretary of the General People’s Committee for Planning and Finance, for its enthusiastic support to the refining of the content and finalization of the work. Many thanks, as well, to the team in charge of providing extensive analytical support, data, and written input to this report, headed by Eng. Khaled El-Ghuel, Under-Secretary of the General People’s Committee for Planning and Finance, whose astute remarks contributed greatly to raising the quality of the report and ensuring that it reflects Libyan reality. Many thanks also to the rest of the counterpart team integrated by Dr. Ahmed Jallala and Ahmed Jehani, extraordinarily supported by Al Mois Ben Mostafa Ben Esmael. The review also benefited from multiple contributions from the following Libyan counterparts:

Secretary of the Libyan National Planning Council: Dr. Mahmud Gebril Ibrahim.
Secretary of the General People’s Committee for Planning and Finance: Dr. Abdelhafid Mahmud Zlitini.
Secretary of the General People’s Committee for Education: Dr. Abdelgader Mohamed Albagdadi.
Secretary of the General People’s Committee for Electricity, Water and Gas: Eng. Omran Abukrae.
Secretary of the General People’s Committee for Transportation: Dr. Mohamed Abuagela Elmabruk.
Secretary of the General People Committee for Agriculture, Animal and Marine Wealth: Dr. Abubaker Al Mabruk Al Manssuri.
Secretary of the General People Committee for Health and environment: Dr. Mohamed Abuagela Rashed.
Secretary of the General People’s Committee for manpower, training and employment: Eng. Maatoug Mohamed Maatoug.
Secretary of the General People’s Committee for of Educational Technologies Authorities: Dr. Abulgassem Al Badri.
Secretary of the Administration Committee of the General Union of Commerce and Industry Chambers, Jumah Ali Al Usta.
Former Secretary of the General People's Committee for Finance: Mohamed Ali El-Huwej.
Secretary of Control Center of Private schools, Dr. Idriss Hafid Al Mabruk.
Secretary of the General People’s Committee for Firms Privatization and Economic Public Institutions, Dr. Mahmud Ahmed Al Ftessi.
Secretary of Administration Committee of the General Company for Gas, Lotfi Abdelkrim Liyass.
Secretary of the Administration Committee of the Execution Board of Renewable Energy Eng. Fathi Mohamed Abugrad.
Secretary of the Administration Committee for Roads and Bridges Authority Dr. Mohamed Ashtewi Ben Omar.
Secretary of Administration Committee of Financial Money Markets, Soleiman Salim Ashahumi.


Finally, special thanks to Dr. Ali Khuderi Merza, UNDP advisor to the General People’s Committee for Planning and Finance.
SYNTHESIS

1. Since the lifting in 2003/04 of the United Nations (UN) embargo, and particularly the presentation of the 2008–12 Development Program (DP), the Libyan Arab Jamahiriya has reaffirmed its intention to shift its economic strategy. So far, hydrocarbon wealth has supported living standards and socioeconomic development that compares favorably with other Middle East and North Africa (MENA) and oil-producing countries. On the economic front, strong growth is supported by fiscal and balance-of-payment surpluses. On the social front, a Wealth Distribution Program (WDP) aims to distribute part of the hydrocarbon wealth to the population; however, in a context of declining oil prices, details on the size, form, and other modalities of the program were postponed by the General People’s Congress in its March 2009 meeting. In any case, the country now aims to optimize its public expenditure to create more and better-paid jobs, manage its oil wealth for the long term, fill its severe infrastructure gaps, transfer its oil revenues in ways that improve people’s income, and accelerate its transition to people’s capitalism.

2. Libya’s 2008–12 Development Program is the biggest and most ambitious Public Investment Program (PIP) ever. The PIP included in the 2008–12 Development Program originally projected an unprecedented cost of LD250 billion over 2008–12 (about US$225 billion). However, as a consequence of domestic concerns over absorptive capacity and in the context of falling oil prices, such figure has been revised down, first to LD150 million overall, and more recently to LD100 billion overall (or LD25 billion per year) over 2009–12 (GPCP 2008b). In a context where Libyan public investment rates are among the highest in the world (21 percent of gross domestic product [GDP] in 2007), the PIP projects an annual average investment rate of 20 percent of GDP in the next five years. Among those resources, investments in basic infrastructure represent about two-thirds of the pipeline, which reveals a shift from prioritizing social needs toward the financing of productive activities.

3. Libya has many assets to fulfill its dreams. Libya holds the largest oil reserves in Africa, with proven reserves of 43.7 billion barrels in 2007. Libya also has vast natural gas reserves, estimated at 52.8 trillion cubic feet (TCF), which with new discoveries will probably reach 70 TCF to 100 TCF. Despite falling oil prices since the second-half of 2008, strong prospects for higher oil prices in the medium term and increased production, along with new discoveries, would enable Libya to generate sizable revenues into the future.

4. Supported by hydrocarbon wealth, Libya has reached living standards and socioeconomic development that compares favorably with other MENA and oil-producing countries. According to the 2007 United Nations Development Program’s (UNDP’s) human development index, Libya is ranked 59th among 162 countries. It has universal enrollment in primary education and an adult literacy rate of 91 percent. Secondary school enrollment rose from 21 percent in the 1970s to 105 percent in recent years, and tertiary enrollment has recorded a similar pattern. Life expectancy at birth is 73 years (70 for males and 75 for females), on a par with most middle-income countries. The total fertility rate is 5.2 children per woman of reproductive age, and one-third of the population is below age 15. Infant and under-5 mortality rates are lower than in most MENA countries, at 18 to 19 per 1,000 live births. Access to improved sanitation is 96 percent in both rural and urban areas. There is almost universal access to primary health facilities at the local level, and there are 1.25 physicians and 4.8 nurses per 1,000 people.

5. Strong economic performance has also been shaped by changes in oil revenues and, to a lesser extent, the political cycle, all this in a context where public expenditure has been highly procyclical over almost two decades. Correlation and regression analyses confirm that public expenditure—and
more in particular public investment—have been procyclical. During 1990–2007, the correlation coefficient between public investment and growth is moderately high at 0.5. And regression analysis between growth and public investment (in logarithms) finds a high and significant coefficient that reveals that growth elasticity to public investment is above three (actually 3.4), while growth elasticity to public expenditure is 1.\(^1\) These findings are not exceptional, but rather a frequent result among developing—and oil-producing—middle-income economies like Libya. In this context, however, implementing a countercyclical fiscal policy—as the country is now proposing to do under falling oil prices—will rather be an innovative, but desirable move.

6. **Public expenditure has also been pro-poor.** At first sight, Figure 1a, which depicts the crossing of poverty rates (mean consumption per person) and budget expenditure allocations in 2007 (measured in per capita terms) per Shaabia, shows little (if not marginally negative) correlation. However, this picture markedly improves once the main outliers (exceptional cases of Shaabiat—often urban—obtaining above-average high amounts of resources) are excluded. As a result, a second look that excludes outliers, in Figure 1b, shows a clearly positive relationship between poverty rates and budget allocations, thus confirming the pro-poor bias of public outlays. In this way, with a few exceptions (outliers), it can be safely said that in Libya the poorest Shaabiat tend to receive the highest development budget allocations.

**Figure 1a: Per Capita Investment Allocations and Poverty Rates per Shaabia**

<table>
<thead>
<tr>
<th>Per capita public investment in LD</th>
<th>Mean poverty headcount</th>
</tr>
</thead>
<tbody>
<tr>
<td>30,000</td>
<td>DJF = 0.002</td>
</tr>
<tr>
<td>25,000</td>
<td>DJF = 0.002</td>
</tr>
<tr>
<td>20,000</td>
<td>DJF = 0.002</td>
</tr>
<tr>
<td>15,000</td>
<td>DJF = 0.002</td>
</tr>
<tr>
<td>10,000</td>
<td>DJF = 0.002</td>
</tr>
<tr>
<td>5,000</td>
<td>DJF = 0.002</td>
</tr>
</tbody>
</table>

District acronyms are as follows: BAT = Batnan, DAR = Darana, AKH = Jabal Akhdar, ALM = Al Marj, BEN = Benghazi, AID = Ajdaya, SIR = Sirt, ALJ = Al Jafrah, ALK = Al Kafra, MUS = Musrata, MAK = Al Markab, TRI = Tripoli, IAF = Irafah, ALZ = Al Zawia, KHA = Al Negat Al Kums, GHA = Al Jab Al Gharbi, NAL = Nalut, SAB = Sabha, ALS = Wadi Al Shatia, MER = Merzeg, ALH = Wadi Al Hayat, ALW = Al Wahat, and GHT = Ghat.

Sources: Bank staff estimates; based on GPCP data.

---

\(^1\) Both correlation and regression estimates are available from the author upon request.
7. **However, there is room for improved targeting of public investment.** Figure 2 depicts the most recent poverty map for Libya. This presentation updates previous efforts done by Libyan authorities in 2000 for both the 1969 and 1992/93 household surveys to estimate poverty lines at the national and regional level (per Shabia). Figure 2 also has the per capita development budget allocations disaggregated per Shaabia. The map ranks Shaabiat per poverty level (for 32 Shaabiat) and per expenditure allocations (for only 22 Shaabiat). Details on the design and estimates of the poverty map are contained in Annex L, Volume III of this report. The map is an extremely powerful analytical tool that indicates that (a) some of the poorest Shaabiat (for example, Mizdah, Ghat, and Sabha Wadi Al Shatli) receive among the highest per capita amounts of budget allocations; (b) some mid-poor Shaabiat also receive budget allocations that roughly correspond to their status; (c) some of the richest Shaabiat receive low budget allocations, another indication of a pro-poor bias (for example, An Nuqat, Al Jfara, and Al Jufrah); but (d) some of the richest Shaabiat receive exceptionally high budget allocations, which reveals room for an enhanced targeting of expenditure allocations (for example, Sirt, Az Zawiyah, Murzuk, and Tarabulus).

---

2 The title of the two surveys are: Household Budget Survey in Tripoli and Benghazi (1969) and Family Expenditure Survey 1992-93. Authorities also point out that an “estimation was carried out in December 2000 using a similar approach as in this review” and that “attempting estimation for people under the poverty line in the 2003 Project (LIB/97/005), using data from the 2002/03 survey, resulted in figures that were inconsistent with those of 1969 and 1992/93.” A more recent estimation was done by Salem Abouaisha Khalifa in his thesis for a master degree on “The Impact of Population Growth on Levels of Income Distribution in Developing Countries: Analysis for the Calculation of Poverty Thresholds in Libya between 1970-2006.”
<table>
<thead>
<tr>
<th>No</th>
<th>Name</th>
<th>Poverty Rates</th>
<th>Per capita Invest.</th>
<th>Ranking</th>
</tr>
</thead>
<tbody>
<tr>
<td>21</td>
<td>Mizdah</td>
<td>34.9</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>17</td>
<td>Ghat</td>
<td>30.9</td>
<td>17,164</td>
<td>2</td>
</tr>
<tr>
<td>7</td>
<td>Al Kufrah</td>
<td>28.1</td>
<td>13,691</td>
<td>3</td>
</tr>
<tr>
<td>30</td>
<td>Wadi Al Hayaa</td>
<td>21.3</td>
<td>6,875</td>
<td>4</td>
</tr>
<tr>
<td>2</td>
<td>Al Butnan</td>
<td>20.0</td>
<td>2,912</td>
<td>5</td>
</tr>
<tr>
<td>31</td>
<td>Wadi Al Shatii</td>
<td>18.9</td>
<td>3,239</td>
<td>6</td>
</tr>
<tr>
<td>8</td>
<td>Al Marj</td>
<td>18.1</td>
<td>6,718</td>
<td>7</td>
</tr>
<tr>
<td>9</td>
<td>Al Murgub</td>
<td>17.7</td>
<td>3,582</td>
<td>8</td>
</tr>
<tr>
<td>1</td>
<td>Ajdabiya</td>
<td>16.5</td>
<td>3,397</td>
<td>9</td>
</tr>
<tr>
<td>27</td>
<td>Sabha</td>
<td>15.7</td>
<td>23,939</td>
<td>10</td>
</tr>
<tr>
<td>25</td>
<td>Tarhuna Wa Msalata</td>
<td>15.4</td>
<td></td>
<td>11</td>
</tr>
<tr>
<td>4</td>
<td>Al Jabal al Akhdar</td>
<td>15.1</td>
<td>4,564</td>
<td>12</td>
</tr>
<tr>
<td>23</td>
<td>Nalut</td>
<td>14.3</td>
<td>6,164</td>
<td>13</td>
</tr>
<tr>
<td>22</td>
<td>Mraelata</td>
<td>14.3</td>
<td>7,854</td>
<td>14</td>
</tr>
<tr>
<td>12</td>
<td>Al W chal</td>
<td>13.6</td>
<td>6,912</td>
<td>15</td>
</tr>
<tr>
<td>24</td>
<td>Tajura W a Al Nawahi Al Arba'</td>
<td>13.1</td>
<td></td>
<td>16</td>
</tr>
<tr>
<td>19</td>
<td>Gharyan</td>
<td>11.8</td>
<td></td>
<td>17</td>
</tr>
<tr>
<td>3</td>
<td>Al Hizam Al Akhdar</td>
<td>11.1</td>
<td></td>
<td>18</td>
</tr>
<tr>
<td>14</td>
<td>Benghazi</td>
<td>10.9</td>
<td>8,733</td>
<td>19</td>
</tr>
<tr>
<td>29</td>
<td>Sabratha Wa Surman</td>
<td>9.1</td>
<td></td>
<td>20</td>
</tr>
<tr>
<td>11</td>
<td>Al Qubah</td>
<td>9.0</td>
<td></td>
<td>21</td>
</tr>
<tr>
<td>26</td>
<td>Tarabulus</td>
<td>8.7</td>
<td>10,093</td>
<td>22</td>
</tr>
<tr>
<td>5</td>
<td>Al Jfara</td>
<td>8.5</td>
<td>3,827</td>
<td>23</td>
</tr>
<tr>
<td>32</td>
<td>Yafra</td>
<td>8.4</td>
<td></td>
<td>24</td>
</tr>
<tr>
<td>20</td>
<td>Murzuq</td>
<td>8.0</td>
<td>8,960</td>
<td>25</td>
</tr>
<tr>
<td>10</td>
<td>An Nuqul al Khams</td>
<td>6.2</td>
<td>2,915</td>
<td>26</td>
</tr>
<tr>
<td>16</td>
<td>Darnah</td>
<td>6.1</td>
<td>7,074</td>
<td>27</td>
</tr>
<tr>
<td>15</td>
<td>Bani Walid</td>
<td>5.8</td>
<td></td>
<td>28</td>
</tr>
<tr>
<td>6</td>
<td>Al Jufrah</td>
<td>5.7</td>
<td>5,688</td>
<td>29</td>
</tr>
<tr>
<td>18</td>
<td>Ghadames</td>
<td>4.4</td>
<td></td>
<td>30</td>
</tr>
<tr>
<td>28</td>
<td>Sirte</td>
<td>3.8</td>
<td>18,101</td>
<td>31</td>
</tr>
<tr>
<td>13</td>
<td>Az Zuwilah</td>
<td>1.5</td>
<td>9,716</td>
<td>32</td>
</tr>
</tbody>
</table>
8. Libya’s performance in executing public investment also reveals marked improvements. In 2007, the actual/budgeted execution ratio for capital expenditures rose to a high 92 percent, well above the 74 percent of 2004. This is the highest rate of execution achieved in more than 25 years in Libya! In doing so, Libya has reached a level of public investment execution that is considered as reasonably high by international standards. Recent efforts at improving the public investment management system explain this positive outcome (see para. 40). However, not all sectors reviewed by this report improved their performance in similar terms. Figure 3 depicts a 2x2 decomposition per level of execution (on the left, above and below 90 percent) and per the size of the sector in the total pipeline (above and below 20 percent of the total number of projects). The figure shows that (a) only one big sector (housing) also achieved a high rate of execution—the other two sectors above the average level of execution—electricity and higher education—had a small pipeline; (b) general education had a level of execution below 90 percent, but somehow this can be explained by its big size; and (c) three sectors—health, technical and vocational training, and communications and transport, did not achieve a high performance, despite their small size, which points to the need to focus capacity building in these sectors.

9. And at the decentralized level, a mild improvement in the performance of project execution is also observed. Among Shaabiat, the overall execution implementation record (measured by the percentage of finished projects) remained constant: it increased to only 32 percent in 2007, from an average 31 percent during 1999–2006. But in some sectors, it did improve. This was the case of communications and transport (47 percent up from 27 percent), and health care (57 percent up from 45 percent). General education and technical and vocational training also improved, but modestly. As an exception to this general trend, project completion in the electricity sector deteriorated among Shaabiat (Figure 4).

10. On the social front, a Wealth Distribution Program (WDP), announced by Colonel Muammar Gaddafi in March 2008, intends to distribute part of the hydrocarbon wealth to the population. The program had originally planned cash transfers of LD25 to LD30 billion (US$20 to US$25 billion) to benefit every Libyan household. So far, however, only LD4.6 billion (US$3.8 billion) has been approved in the 2008 budget, and, in a context of falling and low oil prices, the March 2, 2009, People’s Congress indefinitely postponed further details on the size, form, and other modalities of the implementation of the
Furthermore, the alternative of transferring public assets ownership is also being considered. On the institutional front, however, the country is indeed proceeding with another major institutional restructuring. Colonel Gaddafi charged the Government with failing to manage the hydrocarbon wealth well and announced the phasing out of all but five ministries by the end of 2008. Such institutional restructuring actually started on March 2, 2009, with the following measures adopted by the People’s Congress: (a) the Ministries of Finance and Planning were merged (one of the recommendations of this report—see Chapter 4); (b) all sectoral ministers involved in this PER were removed; (c) the former head of the National Planning Council was removed from his position and appointed to be in charge of the design of the institutional reorganization of the government; (d) a new organization of the government was announced (a draft proposal expected in May); and (e) a second stage of civil service reform is unfolding.

11. In this way, Libya’s oil windfall—through the implementation of the 2008–12 Development Program—is already transforming its economic, institutional, and social landscape. On the economic front, real growth is expected to be close to 7 percent in 2008, with sizable fiscal and balance-of-payment surpluses. The Government also intends to modernize and expand public services and to fill pressing infrastructure gaps in basic infrastructure and social services.

12. Taking into account these assets, this report summarizes the main findings and recommendations of a Public Expenditure Review for the Libyan Arab Jamahiriya General People’s Committee for Planning. This review—the first ever produced for Libya—focuses on assessing recent public expenditure patterns and on building a modern framework for public investment management. At the Government’s request, it carefully analyzes past and present government spending trends, reviews present management practices, and suggests a comprehensive program for reform. Its more specific goals are to review the most recent performance of public expenditure; estimate the fiscal sustainability of public expenditure plans over 2008–12; identify the contribution of the Government’s ongoing civil service reform to fiscal sustainability; identify the main shortcomings of the public investment management system; improve investments in five important sectors—education, health, power, roads, and water; and introduce alternative best practices in the definition of inter- and intrasectoral criteria for project selection in those sectors, with a view to prioritize public projects addressing productive activities.

13. The reports builds upon the framework of fiscal management in oil-dependent economies, which features three parts (Figure 5). The first deals with collecting and saving oil revenues, leading to one stream of a large literature exploring both fiscal sustainability and the pros and cons of alternative models of an Oil Stabilization Fund. The second deals with development spending, leading to a second stream of a large literature assessing standards in public investment and the many effects of sizable public investment programs. The third deals with

**Figure 5: The Three Parts of Fiscal Management in an Oil-Dependent Economy**

![Figure 5: The Three Parts of Fiscal Management in an Oil-Dependent Economy](image)

*Source: Bank staff elaboration based on a Libya GCP presentation.*
financing current spending, such as wages, subsidies, or social programs, addressing the ongoing civil service reform and the proposed WDP. This review deals with all three parts, except for two topics that are treated in depth elsewhere: alternatives for Oil Stabilization Funds and cash transfer mechanisms that could be adopted for the WDP. The former topic was addressed by a previous World Bank report (World Bank 2006c) and the latter topic was briefly treated in a separate workshop held with Libyan authorities in April 2008. The PER brings four main messages next.

Main Messages of the Report

14. **Message 1: Make Public Expenditure More Accountable.** The accountability of Libya’s public expenditure management can improve if the country solves its “institutional gap” and makes its expenditure (and investment) decisions and follow-up with solid institutions and enhanced transparency. Despite multiple improvements in public investment management, severe weaknesses still hamper efficient service delivery along the accountability channels involving three players: policymakers, service providers, and clients. Filling these gaps and setting a solid accountability framework for governance and public service delivery rests on strong and solid institutions and on defining proper incentives and responsibilities among the three players.

15. **Message 2: Preserve Fiscal Sustainability in the Medium Term.** Libya’s revised fiscal position in early 2009 is sustainable at current oil prices of US$60-80 per barrel in the medium term, even though some deviations from the sustainable path may occur (and are desirable) in the short term for supporting a countercyclical policy. This conclusion is based on several assumptions: (a) future average oil prices above US$60/barrel; (b) estimated oil output; and (c) moderate spending (and investment). Such a hypothetical stance should be adjusted to the ongoing changes in oil prices, to changing rates of return of public investment, to an eventual high cost of the WDP, and to an eventual accelerated implementation of public investment, which may somehow contribute to increase inflation and reduce the quality of public investment.

16. **Message 3: Achieve High-quality Public Expenditure Management.** The overall quality of Libya’s public expenditure (and investment) management can be improved if the country moves to comply with the three levels of a sound public expenditure management framework. Level 1 is aggregated fiscal discipline, integrating sectoral ceilings under a medium-term expenditure horizon; Level 2 is allocative efficiency, assigning resources according to sectoral priorities; and Level 3 is technical efficiency, implementing public projects according to solid technical standards.

17. **Message 4: Raise Selectiveness with a Pro-productive Bias in Choosing Public Projects.** Basic infrastructure projects have, in general, higher rates of economic return than projects in the social sectors. At the macro level, the 2008–12 PIP deepens the ongoing shift toward basic infrastructure projects initiated in the post-embargo era, with increased budget allocations. At the micro level, Libya must establish a culture of “quality at entry” in project selection that prioritizes sound projects in basic infrastructure. Past generalized practice of massive project approval with little or no supporting feasibility studies is in the process of being eradicated. Quality at entry implies introducing proper methodologies for selecting public projects in accordance with well-defined criteria—methodologies that give a higher weight to the economic rate of return of projects in mutually complementary intra- and intersectoral project selection processes as described below.

18. **The articulation of the main text of this report around those four main messages is straightforward (see Volume II).** Two chapters focus on two main messages: Chapter 2 examines fiscal sustainability and Chapter 10 develops selectiveness in public projects. Chapters 3 and 4 assess current and capital expenditure trends and administration, the two key components of quality expenditure
management. Chapters 5–9 explore the accountability framework and the quality and efficiency of each sector pipeline. To do this, sectoral chapters follow a common structure combining the analysis of each sector performance, its institutional accountability framework, its public expenditure patterns, and its quality assessment, mostly measured by internal and, whenever available, external efficiency indicators. All chapters include detailed policy recommendations, also summarized in a matrix of policy recommendations. Volume II is complemented by several technical annexes and a statistical appendix in Volume III.

19. As stated above, Libya not only has many assets but does not start from a policy and organizational vacuum. On the contrary, Libyan authorities have already been working on the four messages addressed by this report: institutional accountability, fiscal sustainability, high-quality fiscal management, and pro-productive bias on project selection. This report builds upon the early positive achievements obtained by Libya’s most recent efforts.

**Message 1: Make Public Expenditure More Accountable**

20. What incentives do Libyan public servants have to comply with delivering high-quality public projects and services? According to the Authorities interviewed, very little, and to improve this markedly, Libya must solve its institutional gap. There is ample quantitative evidence of a positive correlation between the quality and resilience of central institutions and economic growth worldwide: On average, countries that obtain higher scores in institutional development are associated with higher rates of growth (see Burki and Perry 1998). In the same vein, resource-exporting countries with good governance grow more rapidly not only in the long term, but in the short term (Collier and Goderis 2008).

21. Following the framework of World Bank (2004), accountability for governance and public service delivery rests on the relationships and interactions among policymakers, services providers, and clients. Public accountability’s definition is based on the idea that authorities should fully disclose and explain their actions (transparency) and should abide by legal or administrative sanctions if their actions are judged not in the public interest (contestability). Figure 6 shows the three optimal dimensions of accountability:

a) Between politicians/policymakers and clients (citizens’ voice).

b) Between politicians/policymakers and service providers (the so-called compact).

c) Between service providers and clients (client power).
Accountability works better when these three dimensions—disaggregated in six indicators, voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, and corruption—are improved. But how is this happening in a unique country like Libya?

22. **Compared with other MENA countries, Libya’s performance in two of six areas, voice and accountability and government effectiveness, is weak.** Of the six governance indicators for Libya measured by the World Bank, two—government effectiveness, and voice and accountability—are in the bottom 20 percent range of the world ranking of countries and declining. This reflects marked weaknesses in the citizen’s voice and client power dimensions of the channels of accountability. Three of them—rule of law, control of corruption, and regulatory quality—are in the next-to-bottom 20 to 40 percent range of the world ranking, and only one (political stability) is above the 60 percent range of the world ranking (Figure 7). These outcomes are consistent with findings published by other international organizations. In 2008, Transparency International placed Libya in the 126/180 position in the corruption perception index (a key feature of accountability), and in 2009, the Heritage Foundation corruption index also placed Libya in the bottom 25th quartile in terms of perception of the country’s freedom from corruption.

23. **Improving both dimensions of voice and accountability and government effectiveness requires addressing the institutional gap.** Libya’s institutional gap is the lag between the quality of its public institutions and their capacity to deliver services efficiently and respond to citizens’ needs. Libya’s institutional policymaking aims to reflect the principle that citizens should participate in government, from the grassroots to the highest levels, in a bottom-up approach. In 1977, the Declaration of People’s Power established local officials as the foundation of the political system. Authority was delegated to the General and Local People’s Conferences and to the General and Local People’s Committees in the localities. The 26 municipalities were abolished in 1998 and replaced by 31 Shaabiat administrative regions and 415 popular conferences. The number of Shaabiat was subsequently reduced to 22.

24. **Since the late 1990s, putting into practice the Declaration of People’s Power has provoked continual redefinitions of the state, resulting in changing relationships between central and local authorities.** Multiple manifestations of an unstable institutional environment have followed. First, two
highly complex institutional processes—accelerated decentralization followed by forced recentralization—have taken place in less than a decade. Experience indicates that completing both processes successfully can take decades before actually harvesting their full benefits, and suspending them leads to discontinuous policy initiatives. For instance, recentralization suddenly suspended the experience of delegating expenditure responsibility (decentralization) to the Shaabiat during 1999–2005. Second, a weakened central government has resulted from the continual change in the number, coverage, and institutional heads of ministries. Since the late 1990s, the number, functions, and names of the highest authorities of ministries have varied from year to year, and this process is far from over with the state reform announced for the end of 2008. Third, in a context of permanent redefinition of the state, discrete policy interventions have been continually improvised in a vacuum of sectoral strategies until recently. Fourth, even if the General People’s Congress is responsible for passing on the decisions of the lower levels and turning them into laws and policy initiatives, the government and ministries can pass decrees on specific issues, which frequently causes tensions between the Government and the Congress. In this kind of institutional context, policy decisions are frequently made in non-transparent processes.

25. A concrete, and certainly not unique, example is illustrative of the existing shortcomings. In the health sector, the governance structure is unclear about which health care functions are to be fulfilled at what level, and how the lines of authority and accountability on technical and fiduciary matters are aligned. While hospitals receive their budgets directly from the Ministry of Finance, other facilities such as health care units and centers receive budgets from the Shaabiat health secretariat. Of 99 hospitals, 21 have a high degree of autonomy to use their budget, hire and fire health professionals, or provide them with much higher salaries, while other hospitals do not have that privilege. The private sector operates under unclear conditions on the basis of licenses granted to them by individual Shaabiat, rather than through a national system of licensure overseen by the General People’s Committee for Health and Environment centrally. Information on health is scarce, and the voice of stakeholders is limited. These conditions concern physicians, health professional associations, labor unions, and civil society groups representing beneficiaries. While in theory the population is involved in decisionmaking through People’s Congresses, there is no information or mechanism in the health sector for helping them participate in the governance of facilities or indirectly through premium or out-of-pocket payments, thus limiting their incentives to expect accountability from providers. And providers are not directly involved through any professional association in decisions regarding their licensing, wage negotiations, or other issues pertaining to human resources management.

World Bank Recommendations

26. Given the high political sensitivity of this topic and the lack of a detailed institutional diagnostic, the Public Expenditure Review contains only general, but fundamental, recommendations for revamping the institutional environment in Libya. Institutional development is essential for promoting economic change and modernization and implementing social policies. However, the government’s accountability is undermined by its image not only of technical weaknesses, blurred responsibilities among agencies, and continuous institutional changes, but more fundamentally of its unclear and somehow erratic overall governance framework.

- At the onset of another comprehensive reorganization, the Government should define its new structure, but this time with a long-term vision. The new institutional framework should define and strengthen the core roles, technical capacity, and leadership of ministries, and it should not deal only with institutional reorganization, but with the way officials interact with one another, actions are coordinated, norms and contracts are issued and enforced, and rent-seeking behavior is discouraged. Given the institutional changes adopted in March 2009, this is an ongoing urgent task.
• The central government should strengthen its role in supervision, regulation, acquisitions of goods, and contracting of services, while also exploring partnerships with the private sector in the provision of direct services. Incentives and contracting out are important prerequisites of convergence toward reducing bureaucratic delays, monitoring project implementation, eliminating corruption-prone practices, and minimizing the risk of expropriation and contract repudiation, all central elements of efficient public service delivery.

• Public sector reform should particularly focus on upgrading the technical capacities of middle-tier management, which is mainly responsible for implementation capacity. This involves the strengthening of the quality of high-skilled civil servants, especially through selective hiring, rigorous staff evaluation, and continuous training.

• Some degree of decentralization should be preserved, but doing so requires detailed planning and technical preparation and coordination with central authorities (the ministries). Its forced implementation in the past was a recipe for failure, overwhelming capacities at the local level. In any case, under any intergovernmental framework, decentralization will deal with four challenges: defining the functions and competencies to be transferred; deciding on the amount of resources to be shared; delineating the fiscal responsibility local governments will assume; and setting up a direct link between policymakers, service providers, and users to improve quality at the local level. Attempting to find a single recipe for dealing with these four challenges worldwide would be counterproductive. Instead, defining specific modalities to implement proposals on each of these four dimensions would require not only a tailor-made design and sequencing adapted to the unique conditions of Libya’s political economy, but a separate study.

Governance reforms are never easy tasks. The incoming new institutional framework should be part of an integral plan that relies on a governance pact among the different actors of the state and, perhaps more difficult in the Libyan context, also taking into account representatives of the private sector and civil society.

Message 2: Preserve Fiscal Sustainability in the Medium Term

27. Libya’s macroeconomic performance has been strong in recent years. Supported by high oil prices and high and rising public spending, real GDP growth averaged 7 percent in the last four years until 2008. New hydrocarbon production fields will increase capacity and volume. Libya is planning to produce 2.4 million barrels of oil a day by 2014, up from 1.8 million barrels today. Assuming no new discoveries, Libya’s oil and natural gas reserves would last for about 65 years and 50 years, respectively. And non-hydrocarbon activities, though small, are expanding at 11 percent a year, particularly in construction, transportation, and trade. But inflation has increased substantially since 2007, due to rising import prices and, to a much lesser extent (an 18 percent contribution in 2008, according to official estimates), higher public spending. The external current account is running large surpluses, and net foreign assets are accumulating rapidly.

28. Libya’s overall fiscal position has also been strong despite a significant narrowing of the fiscal surplus in 2007 and 2008, thanks mainly to rising outlays to implement the Public Investment Plan. Propelled by the oil windfall, the fiscal surplus registered a record high of about 36 percent of GDP in 2006. But it narrowed to about 26 percent of GDP in 2007 (and 25 percent in 2008), due to a rapid increase in virtually all expenditure items. There was a sharp —58 percent—increase in capital spending and a 50 percent rise in public wages, the first since 1981, part of the civil service reform. The latter

3 Had fiscal revenues considered the portion of oil receipts that do not go to the budget (the so-called “sterilized part”), the hypothetical fiscal surplus would have increased again in 2009.
increase was smaller than the budgeted increase of 60 percent due to the initiation of an ambitious civil service reform, with about one-third of public employees being transferred to a central labor office for retraining or retrenchment.

29. **Libya manages its hydrocarbon revenues prudently with the support of Al-Mujanab (an Oil Reserve Fund).** So far, the Fund protects public finances from the volatility and uncertainty of oil revenues, and since June 2007, its assets have been managed by the Libyan Investment Authority. This report introduces a standard quantitative model applied worldwide to estimate how Libya’s proposed public expenditure plans could be financed from its oil proceeds, while preserving a constant per capita income for many years, that is, intergenerational equity. The fiscal sustainability analysis (FSA) finds that Libya could achieve intergenerational equity for its hydrocarbon assets and savings in deposit in the Oil Reserve Fund in the medium term by using as broad guidance the findings of the FSA methodology. Under this partial equilibrium model, public expenditure is sustainable if the projected non-hydrocarbon primary deficit (the difference between non-hydrocarbon government revenue and primary government expenditure) does not exceed the implicit return on projected government wealth (from estimated hydrocarbon and financial assets). The results show that continuing average oil prices (on average on or above US$60-80/barrel) and an expected increase in oil output would have sustained projected non-hydrocarbon primary deficits (and produce sizable fiscal surpluses) in 2009 and over the medium term.

30. **The analysis also shows that in the present context of oil prices at US$60-80 per barrel, the current fiscal position is inside the estimated sustainable ceiling.** Expenditure in 2009 show a small decline compared to 2008. This is a clear break with the very large increases in past years and is consistent with Libya’s policy to rationalize public investment. Had the earlier plans formulated in early 2008 remained in effect, an oil price around $80 per barrel would have been necessary to ensure sustainability. In addition, the sustainability ceiling would also be reduced if the implicit rate of return on assets declined by more than 1 percentage point (from the baseline assumption of 5 percent). Even though the definition of such thresholds is merely indicative for policy purposes, the uncertainty about the duration of declining oil prices and future rates of return calls for caution.

31. **In the short term, however, the Authorities have the choice to preserve an expansive countercyclical fiscal policy, which would be desirable.** This would be mainly justified by their massive investment needs required to fill the inherited infrastructure gap from the embargo years, while gradually reversing such acceleration in later years toward the sustainable envelope. In this way, in the short term, a countercyclical policy would use revenues to promote growth and investment in the domestic economy, and thereby preserve consumption on a rapid growth path, perhaps under the expectation that oil prices reverse in a few years. An effective countercyclical policy would be contingent on the government’s ability to assess and implement spending plans (implementation capacity) and the ability of the economy to accommodate additional spending without damaging the other sectors of the economy (absorption capacity). Collier and Venables (2008) justify such policy on the need to find a middle ground between two extremes: devoting all proceeds from the oil windfall to current consumption and investment would be wasteful and inequitable for future generations, but postponing the consumption and investment benefits just for the sake of a far-distant future would be a suboptimal policy as well. Instead, they find room for an optimal policy that involves saving some of the oil proceeds for distant generations, but that does not necessarily require obtaining a constant per capita income for future generations. Such a countercyclical policy would rather put immediate current consumption and investment on a rising path, and by this token bring forward the economy’s growth trajectory, but under the condition of relying on sound project selection that guarantees high rates of returns from projects for future generations. And this is particularly true for countries either having a low share of public spending devoted to infrastructure or experiencing a large infrastructure gap, like Libya.
**World Bank Recommendations**

32. **Libya’s public expenditure plans at current oil prices of $60-80 per barrel are sustainable.** The results show that Libya’s revised public expenditure plans remain sustainable even if oil prices decline to $60 per barrel over the medium-term. At $60 per barrel, the sustainable public expenditure envelope is about LD 43 billion in 2009. This is similar to the present expenditure level for 2009. Other key policy recommendations arising from the above analysis are:

- The recent slowdown in public expenditure growth is a welcome step. However, in cutting back public expenditure, focus should be on completing key projects that are already under way. Current expenditures, including wages, need to be contained.

- The estimated overall expenditure envelope should be reviewed periodically as key variables change, particularly the price of oil. This chapter provides the sustainable expenditure levels at different oil price scenarios. The analysis is, however, also sensitive to other variables. The results should, therefore, be interpreted with caution.

- Deviations from the sustainable expenditure benchmarks in a countercyclical policy could in fact be desirable. However, these should be limited, temporary, and well-justified by economic conditions. In addition to sustainability considerations, the fiscal stance also needs to be guided by the objective of maintaining overall macroeconomic stability and social development goals. If oil prices decline below $60 per barrel, the authorities would need to revisit their public expenditure plans, taking into consideration all of the above objectives and not only the long-term sustainability indicative benchmarks. Given the exchange rate peg, fiscal policy remains the main tool for ensuring price stability. The fiscal stance would, therefore, need to be assessed periodically, taking into consideration the overall economic conditions facing Libya.

- In considering public expenditure plans within the overall sustainable envelope, provisions should be made for the relatively large contingent fiscal liabilities such as the non-performing loans of state-owned commercial and specialized banks.

- WDP disbursements plans should be within the overall sustainable expenditure envelope. WDP disbursements should be limited and aimed whenever possible at replacing existing transfers and explicit subsidies in the context of a comprehensive expenditure reform program that enhances pro-poor and productive targeting and efficiency, with a net positive effect on the budget.

- The emphasis should be placed on the quality of public investment in order to ensure that mineral wealth is transformed into high quality assets, as explained elsewhere in this report.

- Public savings remaining after meeting the sustainable expenditure benchmarks should be wisely invested abroad by the Libyan Investment Authority on conservative investments following commercial objectives. This usually helps prevent a suboptimal domestic investment of these resources due to political pressure. It would also help avoid complicating the macroeconomic management of the domestic economy. However, this
does not totally exclude the use of such resources to finance domestic projects in exceptional cases or for short term counter-cyclical stabilization purposes.

**Message 3: Achieve High-quality Public Expenditure Management**

33. **Three levels of sound public expenditure management promote quality investment.** Reform in all areas is needed to bring a significant and lasting modernization of the public investment system, thus improving the efficiency of public spending and obtaining value for the money of the Libyan people (Table 1).

<table>
<thead>
<tr>
<th>Table 1: The Three Levels of Sound Public Expenditure Management</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Level 1. Aggregate Fiscal Discipline</strong></td>
</tr>
<tr>
<td><strong>Level 2. Allocative Efficiency</strong></td>
</tr>
<tr>
<td><strong>Level 3. Technical Efficiency</strong></td>
</tr>
</tbody>
</table>


34. **The public investment plan presents an opportunity to build a new framework for managing public spending while accelerating growth, creating jobs, and transferring wealth.** Based on the three-level framework, there are three goals:

- Support the preparation of an aggregate expenditure (and investment) ceiling, drawing lessons from the fiscal sustainability analysis, other macroeconomic models, and Libya’s implementation capacity—proxied by the past actual/budgeted execution ratios—for public expenditure.4
- Introduce high technical standards in public investment management while improving the effectiveness of investments in five important sectors: education, health, power, roads, and water.
- Deepen the Government’s strategic approach in adopting specific sectoral investment decisions.

**Level 1. Setting an Aggregate Expenditure Ceiling Target**

35. **To catch up with the infrastructure gap inherited from the decade of embargo, Libya set up impressive multiyear 2008-12 public spending (and investment) rates for the first time.** Public

---

4 This report estimates the “implementation” capacity of the Government, measured by the level of execution of annual budgeted outlays. However, it is important to distinguish such concept from the “absorption” capacity of the economy, a familiar term used by the Government to define the level of public investment that “at the micro level leads to a lower rate of return and, at the macro level (when replacing the rate of return by the rate of growth of GDP), to accelerating inflation.” Both concepts are of dynamic nature. This report deals with the first one, for estimating the absorption capacity would require previously building a proper macroeconomic model of the Libyan economy, which is beyond the terms of reference of this study. Moreover, the Government has already developed its own model to assess the absorption capacity, a model that it keeps continuously updated (see Merza, 2008a,b; GPCP 2008a).
spending in Libya has been high by international standards. At 39 percent of gross domestic product (GDP) during 2003–05, consolidated public spending was among the highest in the world. In international comparisons, its public investment ratio is also very high—it almost quadrupled from 5.8 percent of GDP in 1999. And in 2007, it was almost three times the average for MENA countries—oil rich and oil poor—and for world oil-exporting countries. Only wartime Algeria, Iraq, and Qatar have double-digit public investment rates ranging around 12-13 percent of GDP.

36. But four caveats point to lower, if still high, investment ratios. Because of dual budgeting, capital expenditure includes misclassified current spending, especially maintenance (on average about a third of total investment according to the authorities, a number that has to be taken with a grain of salt and mostly including the operating costs of public projects). Moreover, there is incomplete and untimely financial accounting and reporting in the Libyan system. Thus, resources registered as “executed” in Libyan fiscal accounts represent those recorded as actual budget authorizations by Planning, later approved by Finance to be transferred from the Central Bank of Libya to the numerous bank accounts of executing units. However, no one knows whether these amounts are spent over the year because these units do not regularly report accurate data on their use of resources. Moreover, the Libyan budget allows carryovers of public investment outlays, which blurs their accurate planning and recording on a regular annual budget cycle. Finally, the absence of a commitment control system—which ensures cash resources are available before issuing a check—leads to the potential accumulation of a stock of arrears, ineffective forward expenditure planning, difficulties prioritizing planning, and information gaps during budget preparation (IMF 2006).

37. Despite these shortcomings, the performance of public investment in Libya has been steadily improving in recent years. Public investment execution ratios are reasonably high by international standards—and improving. This ratio reached 92 percent in 2007—the highest ratio in more than 25 years—despite an increased development budget. But the average mixes good performers (power, gas and water, higher education, and housing) with lesser performers (health, and communications and transport). This outcome corresponds to international experience. Indeed, the implementation capacity of sectoral ministries is unequal, and while there is no doubt agencies’ capacity to prepare good project proposals, launch new projects, and execute a much larger expenditure envelope is improving, their learning process is slower than necessary to accommodate such a large absolute increase in budgeted investment.

World Bank Recommendations

38. Further pressure for faster implementation of the 2008–12 pipeline contained in the draft development program would be counterproductive. There are strong political pressures to accelerate completion of projects by 2009, the 40th anniversary of the revolution. In addition, abundant resources have already been authorized, with a booming development budget. In the meantime, government institutions, not good at project execution, need to be strengthened. Forced execution that shortcuts minimum standards in cost-benefit analysis, social returns, and project profiles could waste resources, duplicate activities, and lead to procurement failures. A smooth pace (in terms of constant or declining public investment/GDP ratios) from 2008 onward is a normal expected outcome that would allow the Government to increase outlays (in absolute terms) while gradually improving institutional capabilities and choosing projects more carefully to achieve better results.

39. More specifically, while there is no rule of thumb for defining an optimal size for public expenditure, ongoing trends could bring the public expenditure ratio to an arbitrarily defined medium term benchmark of around 30 percent of GDP (down from 35 percent of GDP in 2007).\(^5\)

---

\(^5\) The eventual medium-term benchmark finally adopted should also be consistent with the absorption capacity of the economy (as defined by the Authorities), but given that the 16-18 percent benchmark is a rather conservative figure based on past time series, it should satisfy such constraint.
This would give medium term visibility to fiscal policy. And such reduction would reflect the expected gains from the second stage of civil service reform (target savings of about 1 percent of GDP in payroll); and a possible return to normal levels of the public investment ratio (target savings of 4 percent of GDP) in agreement with Libya’s historic pre-windfall average (16 to 18 percent of GDP, gradually down from 21 percent of GDP in 2007). It would also gradually introducing minimum requirements of quality investment management; and a realistic view of what can be achieved in terms of improved implementation capacity, especially regarding minimum requirements to be respected in terms of project contracting, procurement, and supervision.

Level 2. Allocating Resources to Sectoral Priorities Efficiently

40. **Rationalization of resources is perhaps the most difficult concept to introduce in a spending-prone budgeting culture of an oil-dependent economy.** It involves linking scarce and cost-effective resources (inputs) to outputs. In Libya, this spending-prone pattern is also associated with the unique institutional context of the decentralization period and the continuous elimination and recreation of line ministries over many years. During that period, preparation of the development budget followed a bottom-up approach reflecting social and political considerations rather than standard criteria for the selection of projects. Only in May 2007, did recentralization bring an attempt to develop a complementary top-down approach in the definition of multiyear, but not annual, sectoral ceilings for a few sectors (see above). In a circular issued by the General People's Committee for Planning, for the first time a five-year Public Investment Plan was requested from each sectoral people’s committee. To do so each committee had to fill out a special form defining priority objectives and quantified targets for their sectors in support of budget requests. As a result, projects started to emanate from strategic sectoral guidelines.

**World Bank Recommendations**

41. **Authorities should make progress toward linking more closely comprehensive sector strategies to multiyear and annual resources allocated.** This is particularly critical for sectoral ministries engaged in mega projects, because the large sums of money involved in those projects risk engaging in “white elephants.” Sectoral strategies should also define inter- and intrasectoral priorities (see Message 4 below). Intersectoral priorities should ideally be accompanied by annual and not only multiyear budgetary ceilings, revised annually on a rolling basis. Such action would frame the negotiation between the planning and sectoral ministries over new projects, given a maximum sectoral allocation that is consistent with the aggregate expenditure. Each ministry would know in advance the projected size of its investment envelope for the following years, and government priorities regarding the investment program would be transparent. The definition of intrasectoral priorities can facilitate the process of project selection (see below).

Level 3. Modernizing the Public Investment Management System for an Enhanced Technical Efficiency

42. **In recent years, the Libyan Government has made remarkable efforts to improve the public investment management system (PIMS).**

- The system has been governed by a comprehensive planning law since 2000 that mandates clear functions and roles to all public institutions in charge of the preparation and implementation of the capital budget.
- The Planning Ministry was the first to be re-created in 2003, reflecting its importance in Libyan society.
The development budget is almost fully financed by its own earmarked resources from hydrocarbon exports (in 2007 representing about 90 percent).

The use of extra-budgetary resources to finance public investment, a major issue until the mid-2000s, has been considerably diminished since the merging of several funds under the Libyan Investment Authority in March 2007.

The preparation of the annual dual budget addressing separate recurrent and development outlays is done under a joint exercise by a macro-fiscal unit integrated by the now merged General People’s Committees for Planning and Finance (GPCP and GPCF).

The General People’s Committee for Planning has elaborated a multiyear development program for 2008–12 to introduce a modern tool for investment planning that complements annual budgeting with indicative sectoral ceilings.

The institutional cycle of the budgeting process is standard, with well-defined autonomy of the budget officers within line ministries, a secured payment procedure requiring two different signatures for the issuance of the check, and a low occurrence of fraudulent practices.

An initial effort at biannual reporting has been introduced with promising response from line ministries.

The General People’s Committees for Planning and Finance have been merged.

Given these achievements, it is not surprising that the overall performance at executing public investment has improved in the last few years (see para. 8).

43. Despite these very positive efforts, Libyan authorities acknowledge the national PIMS is in need of an overhaul. Indeed, according to the 2007 public expenditure execution report, the execution of the PIP faces numerous challenges that affect the level and quality of public spending (GPCP 2008d):

- Weak technical capabilities and expertise of domestic execution bodies;
- Lack of administrative stability at some agencies and sectors;
- Excessive focus on the quantitative side of investment (input) rather than on its qualitative side (output), especially on education and health projects;
- Low level and quality of training and high dropout of trainees;
- No maintenance program for physical assets, and deviation of project-earmarked resources to other needs;
- High amount of outstanding resources for halted projects, and contracted but not launched projects;
- Low level of supervision of project implementation and management;
- Delays in contracting procedures and approval of development projects;
- Low quality and quantity of data and follow-up reports;
- Inadequate level of coordination among sectors regarding project implementation and the provision of utility services;
- Delays in preparing social and economic feasibility studies for many projects;
- Delays in the payment of contracts of national execution agencies due to lengthy and complex procedures.
44. **In response, the Authorities aim to gradually introduce minimum standards in their quest to move toward a modern budgetary system that will support quality investment management.** First and foremost, the new PIMS will face three structural weaknesses inherited from an outdated budgetary system. These are: dual budgeting, the misleading generalized use of contracts to designate projects, and an outdated budget classification. Dual budgeting in a continuously changing institutional environment (the number of ministries and appointed ministers varies from year to year) prevents integrated programming of current and capital expenditures, leading to overlaps and waste. The extensive use of contracts leads to fragmentation of “mini projects” and complicates their management—another consequence of budgeting current and capital expenses under separate classifications, the current budget one, administrative and financial; and the capital budget one, per sector.

45. **The PER shares many of the Authorities’ findings, while focusing on the next systemic issues:**

- **At the macro level,** efforts made in past years to use a macroeconomic model to prepare the annual budget with a medium-term, broad outlook in mind, and to use such model to project scenarios for adjustments to the 2008–12 Development Program under different oil price assumptions, are very positive. The forecasting performance of the Libyan macro model in 2006 and 2007 also appears reasonably good. Authorities have also set ceilings for sectoral investment envelopes. However, those ceilings are indicative and loose, and while significantly increasing sectoral envelopes to record-high levels, they can hardly be considered as a tight budget constraint. Deviations from budgeted resources are also not revised on a rolling basis. In addition, the assumptions supporting the macroeconomic framework of the annual budget are not regularly published yet; but recent efforts done to share the model with Libyan academics and practitioners as well as with international consulting firms and international organizations are very promising steps in such direction.

- **Despite remarkable recent efforts,** some sectoral strategies are still nonexistent or incomplete, thus resulting in projects with little strategic content (see Level 3 below). Among five sectors examined in the PER, only two strategies appeared reasonably well developed (power and health); other sectors appeared with partial, but worthy strategic components (education at all three levels: general, higher, and voluntary education) and two with a list of general sector objectives that can be considered, at best, as strategic guidelines (roads and water).\(^6\) In addition, there is an implicit bias toward approving the already existing projects pipeline.

- **At the micro level,** many steps of the project cycle have important shortcomings: until very recently, there was a generalized absence of feasibility studies even for large-scale, mega projects, slow project implementation, little or no project reporting, and no ex post evaluation. The Authorities, however, are making significant efforts to gradually overcome these issues. Since 2007, a few quality-at-entry mechanisms to filter project proposals have been introduced; basic follow-up tools like the software-based design of a virtual central database of public projects are under preparation; and reporting from executing units has been enforced with some degree of success. Consequently, the number of public projects (1 out of 10 in 2007) stopped is decreasing (better than 3 out of 10 in 2006), despite abundant additional resources.

- **The technical expertise of personnel in charge of executing projects is generally weak.** Shaabiat show similar shortcomings. Initial project costs are commonly underbudgeted, and final costs might actually be much higher. These weaknesses entail substantial risks that projects could not be delivered on time or at costs that could be excessive.

- **So far,** the presence of private financing in public infrastructure projects is limited, in part resulting from an opaque legal framework for public and private partnerships.

---

\(^6\) Indeed, officials from these two sectors have required urgent technical assistance from the Bank to prepare their sector strategy.
World Bank Recommendations

46. In general terms, Libyan authorities recognize the need to move toward a modern public investment system, supported by sound budget management policies that would enhance the quality of public projects and improve service delivery. But public investment management systems reform requires implementing parallel budget reform, which calls for budget unification accompanied by a new budgetary classification that introduces 2001 IMF-GFS standard classification (economic, functional, administrative, and program-oriented) categories. And in doing so, the reform will rigorously redefine the concept of a public project.

47. Quality public investment management results from higher standards at every stage of the project cycle. The reform of the public investment system would require six interrelated tasks:

- The introduction of explicit and public global and sectoral annual fiscal targets, annually revised on a rolling basis. Such targets should be consistent with benchmark medium-term targets, and fiscally sustainable in the medium term, even though they admit temporary deviations under countercyclical policies in the short term.

- The complete design of comprehensive sectoral strategies for the missing sectors, to tighten the framework of the priority pipeline and strengthen the link of resources to objectives (see below on Level 3 of the PIMS).

- Gradual introduction of “quality-at-entry” standards in project selection. This can be done through the preparation and enforcement of a manual of technical standards on public projects, and the development of massive and continual training of budget officers in line ministries and executing units on project appraisal, implementation, and monitoring and evaluation.

- Taking advantage of the recent merging of the Ministries of Finance and Planning, the definition of an upgraded role for the new Ministry as the pivotal point for strategic decision-making, norms preparation, and introduction and follow-up project implementation. This would also involve the introduction of parallel project-tracking procedures. Indeed, given the myriad contracts and their varied sizes, careful consideration should be given to establishing three parallel tracks for processing projects depending on their size. This would involve creating a special technical unit, reporting directly to the General Planning Council, to deal exclusively with mega and special projects and two other tracks, one for midsize projects and another with simplified procedures for mini projects (eventually grouping contracts in conglomerates). This reform would strengthen technical requirements for submitting projects and also bring lighter project preparation and procurement procedures. Figure 8 describes the institutional framework of the proposed PIMS.

- Timely compliance with deadlines and projected costs cannot be achieved unless project execution and evaluation has adequate and periodic monitoring and reporting tools. The creation of an IT-supported single database for public projects is just the first step. A set of incentives should be designed for timely collection of information on project implementation by project-executing units. In doing so, project results will feed back into the investment cycle.

- Reviewing the legal and regulatory framework for public-private partnerships (PPPs) would help
attract domestic and foreign investors. Potential for PPP projects should be examined and programmed as part of the budget, be consistent with overall government and sectoral policies, have specific benchmarks to measure progress, and have their fiscal and governance risks carefully assessed.

**Figure 8: The Proposed New Institutional Framework of the Public Investment Management System for Libya**

48. **Making fiscal space available from a streamlined civil service.** Overstaffing makes Libya’s wage bill one of the highest in the world. In 2005, 6 of 10 Libyans were public employees, and the payroll represented about 25 percent of non-hydrocarbon GDP. These high ratios are essentially explained by the historically small size of the private sector and the failed experience of the uncontrolled appointment of a large number of public servants during the 2001–05 period of decentralization, in which Shaabiat assumed primary responsibility for human resources management. As a result, public employment more than doubled, absorbing the country’s overabundant supply of underemployed labor. Hydrocarbon surpluses have helped offset the immediate fiscal impact of the expensive payroll, but such a heavy burden uses resources that could be devoted to public investment (fiscal space). Overstaffing has encouraged moonlighting and absenteeism and led to inefficiency, low productivity, and deterioration in the quality of public services. In addition, uniform salary levels are distorted, with all public servants governed by almost identical terms and conditions irrespective of their jobs and skills. Frozen public salaries from 1981 to 2007 were eroded by inflation, which has justified continual nontransparent promotions and fringe benefits entirely delinked from merit-based performance. Finally, there is no training of public servants and no capacity-building strategy.

49. **In 2006, the Libyan authorities sought to recapture control of human resources with a remarkable civil service reform, including drastic involuntary retrenchment and significant wage**
increases. The objective was to reduce civil servants by two-thirds in the medium term while improving remuneration for the best employees. The results of the first phase (2006–07) have been relatively successful, with nearly a third of the civil service laid off and partial wage reform implemented. The second phase of the reform should continue the retrenchment program.

**World Bank Recommendations**

50. **The Libyan Authorities should build on the momentum initiated by the first stage of the reform, especially the strong political will, to undertake and sustain the next phase of the reform.**

The objectives of the second phase are to deepen ongoing reforms in promotions and remuneration, introduce performance-based management in the central government, and build human resources management capacity in the Shaabiat. More concrete recommendations follow:

- The selection criteria for the second phase of retrenchment should be refined. Retrenchment in the second phase will be more difficult than the first because redundant personnel and illegal hires have mostly been laid off. Remaining civil servants are now likely to be performing at their best to avoid losing their jobs. The criteria for the next phase will need to be fair, precise, and objective (for example, holding a diploma, level of experience, and effort and ability to excel at the job).

- Authorities should target the larger sectors, where most remaining redundancies will need to come from—higher education, general education, finance, manpower, agriculture, and health.

- Reform of the wage and compensation system should be deepened to attract and retain the best staff with the required skills. The current wage schedule does not do so, despite recent wage adjustments. Wages should be set to at least their 1981 real levels, and the higher-wage scales will need to be adjusted more than the lower ones. The current incentive allowances must be reoriented toward merit and transparency. Allowances must reward productivity, efficiency, and results, not just seniority and allegiance. Discretionary allowances should be abolished.

- Another need is to enforce existing human resources management regulations and introduce results-based management. Libya has a good system in place for designing sectoral staffing structures and managing recruitments, pay, and promotions. Enforcement is now needed at all levels, and this requires continual training, especially for human resources managers at the sectoral ministries and at the Shaabia level.

- It is advisable to establish a supervisory authority to monitor human resources management of the Shaabiat and have veto authority over Shaabiat hiring decisions. The central body would insulate human resources managers from political pressures and interest groups. Staff deployment should be progressive over time, and a central authority should remain in place. Such a supervisory authority would ensure that Shaabiat continue to implement civil service reform and comply with new regulations.

51. **Ultimately, the success of the second stage of the reform will depend on four factors.** Proper handling of the social impact of the program would require preparing a policy social impact analysis to evaluate the impact of the program on the retrenched and devise mitigating measures accordingly, including enhanced unemployment benefits, job search assistance, training, and relocation assistance. The reform should avoid rehiring of the retrenched under political pressures and instead make greater efforts to assist workers in the transition to the private sector. New hires should only replace those retiring and must have the necessary skills. Success of the reform also depends on the timely completion of a pay
reform that rewards merit and productivity and prevents public salaries from eroding, to make it possible to hire and retain qualified workers. Finally, the reform would not be complete without a genuine effort to reduce the politicization of the bureaucracy, enhance accountability, and strengthen managerial efficiency.
Message 4: Raise Selectiveness with a Pro-productive Bias in Choosing Public Projects

52. At the macro level, Libya’s 2008–2012 PIP already contains a significant bias toward productive activities, that is, projects on basic infrastructure that, together with an active public sector role, are critical for the desired productive diversification of the Libyan economy. This is inherited from the post embargo years that left a significant gap of infrastructure that will require several decades to fill. Consequently, resources allocated under the 2008–12 PIP give top priority to investments in basic infrastructure, while projects in the social sectors experience a decreasing share, coupled with closer scrutiny than in the past, as reflected by the significant share of projects dropped in the education and health sectors in the past two years with available information, 2006 and 2007.

53. However, at the present stage, the application of any methodology of project prioritization can, perhaps, only be applied to a minority share of the 2008–12 PIP. On the one hand, the PIP already gives priority to ongoing projects. On the other hand, barely about one-quarter of the total pipeline remained available as “new projects under study” by end-2008. All other remaining projects have been contracted and a significant amount of resources (above 85 percent) remained undisbursed by such date.

54. Prioritizing public projects with a view to benefiting investments in productive activities requires the following steps:

• A prerequisite for selectivity is that the pipeline of projects be anchored. Three factors delineate the framework for selectivity: (a) the amount of available resources, determined by the size (ceiling) of the sectoral and overall expenditure envelopes; (b) the link between the project’s objectives and the broader sectoral and national strategies (if any); and (c) the objective assessment (reality check) of the implementation capacity of the executing units.

• At the micro level, a pro-productive bias in project selection requires first and foremost sound technical projects. High economic rates of return (ERRs) are the most important criteria to create such bias. This is critical, especially in basic infrastructure projects that require sound feasibility studies to guarantee the achievement of high internal rates of return in standard cost-benefit analysis. Furthermore, large and more complex projects might require the support of a specialized agency to do those detailed technical estimates.

• Intrasectoral prioritization follows in second place. There is no unique methodology for intrasectoral projects prioritization and the report provides complete and detailed sector-specific approaches (see Chapter 10 in Volume II). However, common features are: (a) the policy objective searched, (b) the effectiveness potential, (c) linking measurable inputs to outputs/outcomes, and (d) the cost-effectiveness analysis that uses cost-benefit analysis only as its starting point. The number and mix of sector-specific intrasectoral criteria vary per sector, but this is where the ERR becomes an important determinant criterion to be considered. Methodologies then range from one central criterion, like the “levelized energy cost” in the power sector, to a broader range of multiple criteria, like in water.

• As a complementary rather than a substitutive approach, intersectoral prioritization comes in third place. Indeed, worldwide experience shows that there is no unique methodology for intersectoral projects prioritization. However, all approaches have a single common feature: they rely on the pre-definition of weighted criteria. The number of criteria can be small (below 5), which is generally the case of countries having scarce and poor-quality data, or they can be large. Criteria chosen also represent a mix of technical and
political considerations, but again, a productive bias would place the ERR with a higher weight than other criteria.

55. Intra- and intersectoral prioritization can be complementary and not necessarily mutually exclusive. On the one hand, intersectoral prioritization often intervenes in countries suffering severe fiscal constraints. On the other hand, intrasectoral prioritization often takes place in governments featuring strong ministerial entities, but little coordination among themselves and weak planning (or finance) ministries. Ultimately, this is a political decision that the country should take.

56. Often, many countries worldwide have introduced an IT-supported system to minimize the influence of political considerations and make the selection process more objective. The definition of intra- or intersectoral priorities can facilitate the process of project selection through the introduction of a scoring system that quantitatively ranks projects according to preestablished criteria. New projects are listed and rated according to those criteria, and those with the highest rates are selected, minimizing discretion and political interference in project selection.

57. Productive diversification will not result spontaneously just from a deliberate pro-productive selection bias of public investment unless there is an active and complementary public sector role. Slow productive diversification, as Libya features, is also the consequence of so-called market failures; which can be of three types: information, coordination and learning negative externalities. Information externalities arise from the fact that it is easier to copy or imitate than it is to create. This means that part (often most) of the returns to innovate in a new business is likely to decline as they spill over to other firms, especially if the capital required to open such businesses is small, thus contributing to keep diversification initiatives limited to low value added investments. Coordination externalities point out to inefficient and partial government intervention that leads to an incomplete and untimely support required by businesses, thus resulting in their lack of competitiveness. Coordination externalities must be addressed with direct and effective government intervention in all required fields (infrastructure, transport logistics, Customs, human resources, capital access, subsidies, etc) so as to provide all required inputs needed to the success of emerging private activities. Finally, learning externalities constrain private businesses through the lack of a critical input: human (often qualified) professionals, having the proper skill mix and experience required by new businesses. Identifying in the case of Libya what type of externalities is more important as a constraint to productive diversification would require a particular analysis that is beyond the purpose of the present report.7

Summary Sectoral Reviews

58. The development of badly needed basic and social infrastructure represents a major challenge for Libya in the years to come and should be sustained. This challenge exists because of the significant investment gap incurred during the embargo years and its direct impact on growth, poverty levels, and quality of life. The key sectors chosen for this review—education, health, power, roads, and water—confront common problems. Although access has reached remarkable levels and nascent efforts are made in terms of completing sectoral strategies, four major shortcomings are that (a) the institutional and regulatory sectoral frameworks are in many cases incomplete, changing, and with blurred responsibilities; (b) data for planning purposes are poor and scarce; (c) the quality of services is poor, despite heavy subsidies; and (d) private participation is low. The central government should address these challenges by promoting accountability under a new institutional framework (see above) and seeking increased private-sector participation (under alternative schemes of public-private partnerships). And to

---

7 For a detailed analysis of the role of such externalities in the case of Morocco, refer to World Bank (2006), Fostering Higher Growth and Employment in the Kingdom of Morocco, Washington D.C.
introduce accountability the Government should encourage introducing contracting arrangements between policymakers (central authorities) and service providers to facilitate service provision under measured performance (dimension (b) of the channels of accountability—see Figure 6 above). In response to these difficulties, the PER proposes a framework/road map with detailed sectoral policy matrices and institutionally-tied policy recommendations, which should facilitate the task of defining implementation responsibilities, and preparation of concrete manuals for actions per ministry in subsequent and tailored-made technical assistance.

Balancing the Efficiency and Quality of Education

59. Libya’s education system has achieved impressive accomplishments and seems close to achieving the Millennium Development Goals. Supported by sizable public investment, the Government has achieved universal access for primary and secondary education and a 46 percent enrollment for tertiary education. Enrollments in higher education are comparable to middle-income countries. Gender achievements are also high: in secondary and tertiary education girls outnumber boys by 10 percentage points. Despite these impressive achievements in access to education, the poor quality and unplanned investments of the education system are its biggest concerns. There are no systematic assessments to monitor student learning under international standards or to assess the percentage of graduates who find jobs, which complicates measuring the impact and returns of these investments.

General Education

60. Quality is poor. This is due to the fact that the education system gives too much priority to inputs, (teachers, buildings, textbooks), with little attention to outputs and outcomes, little respect for standards, policies, monitoring and evaluation, and a lack of accountability at all levels. The most important shortcomings of the education system are: (a) low internal efficiency rates seen in high repetition rates, a student-teacher ratio among the lowest in the world, a proliferation of small schools, and poor results in learning outcomes; (b) lack of coordinated investment planning and management with three uncoordinated ministerial agencies resulting in waste of resources; (c) very high school unit costs (the current estimate cost of a classroom for basic education reached LD175,000, equivalent to the cost of an average standing apartment in Tripoli and up to four times the construction costs of classrooms in Tunisia and Morocco); (d) a high recurring cost of teachers’ salaries, leaving little room for funding other inputs; and (e) an oversupply of professionals in many disciplines. On the high-school unit costs, there is no evidence that these investments will have an impact on improving access or on learning outcomes. Currently, there are a number of schools that are using classrooms on a double shift seeking to use existing resources in a more efficient way.

61. Although there is equity in access to schools, there is considerable inequity regarding learning outcomes among Shaabiat, measured by the exit exam at the end of secondary school and illiteracy rates. The decentralization period aggravated the lack of accountability and worsened these trends, in particular, the uncontrolled hiring of staff. Higher-education enrollments are high, but a significant number of graduates do not meet labor market needs. Finally, there is an embryonic private sector participation in education, accounting for less than 2 percent in general education and barely reaching 4 percent in higher education. Private sector education is developing fast, but is still embryonic and needs to be encouraged.

62. Teachers’ reallocation is an issue. The Government aims to reduce teachers in basic education by 35 percent and in secondary education by 25 percent, and has included a measure to triple salaries for teachers that will locate to schools more than 120 kilometers away from their homes. As the Government deploys a voluntary departure program, the reallocation of remaining teachers should have to follow a
per-student allocation formula. It is clear that teachers concentrated in urban areas will have to be redeployed to rural and underserved areas. The current goal is to reduce the pupil-teacher ratio to above 7 in basic education and to 6 in secondary education. However, this reduction is modest; the target could be doubled without posing any risk to the quality of education.

World Bank Recommendations

63. The vision for Libya is a new governance structure introducing new accountability and incentive mechanisms, efficient use of human and physical resources, and a program to improve the quality and relevance of education. The education system should give lower priority to the provision of expensive inputs (teachers and buildings) and more attention to outcomes, supported by sound standards, monitoring and evaluation, and increased accountability at all levels. The Government is also seeking ways to improve private sector participation in primary and secondary education. To this end, World Bank recommendations are:

- Develop a program to improve the quality and relevance of education by monitoring and evaluating student learning. An improvement program should include a comprehensive set of reforms that gives teachers and students the skills to perform in a knowledge-based economy. Numeracy and literacy alone are not enough to be productive in modern societies. Instead, knowledge of foreign languages, science proficiency, and problem-solving skills are part of the repertoire of students around the world. Achievement of these goals requires a solid curriculum and sound pedagogy, well-trained and motivated teachers, a good monitoring and evaluation system, and competent school managers.

- Promote sound investment planning and management. In order to have a sound analysis of the investment needs of the sector, it is important to do school enrollment projections. In its 2008–12 PIP, the government has an ambitious construction program with a goal to build 15,580 classrooms. Key areas for technical assistance to make sure that this program is successful are the following: (a) an analysis of the sustainability of those investments; and (b) a capacity-building program for planning and management for the Shabiaat, including data collection, information processing, school mapping, and management of construction and rehabilitation of school buildings.

- Develop a teacher professionalization program. A technical assistance program could provide elements to identify adequate incentive mechanisms to relocate teachers. One positive aspect of the 2008–12 program is that it includes teacher training on a wider spectrum of courses, promoting various teaching skills of teachers, and helping solve the problem of a lack of teachers for certain disciplines. While careful analysis of the criteria, incentives, and opportunities should be given to those that would voluntarily leave their posts, this program should combine with upgrading the skills of those remaining and requiring them to upgrade their qualifications in the system. This would lead to defining performance criteria, assessment methodologies, and the corresponding performance-based incentives.

Higher Education

64. Higher education poses the most difficult challenge, since its graduates do not meet labor market needs. Enrollment rates are already the highest in the region, but graduation rates are low because the unemployment rate of graduates is pretty high and will only continue to grow. Investments planned in the 2008–2012 PIP represent an increase of more than 100 percent of the investments in previous years. There are currently 28,000 enrolled teacher students that will graduate in 2009, for an average maximum capacity of 14,000 new jobs. Given the lower number of jobs available in other sectors, unemployment is likely to rise.
**World Bank Recommendations**

- It is critical to have a new admissions policy consistent with the needs of the labor market, and providing the right incentives to shift enrollments from higher education into technical and vocational programs.
- In addition, it is important to reinforce the quality-assurance system. This is in order to evaluate current institutions and the programs they offer.
- A detailed technical assistance program could help identify the most cost-effective ways to improve the quality and relevance of higher education to market needs. The analysis also needs to assess the likelihood of introducing cost-sharing mechanisms for public universities.

**Vocational Training**

65. **The technical and vocational education policy needs adjustments.** The goal of a minimum of about 200,000 students is ambitious and represents an investment about 10 times higher than in recent years.

**World Bank Recommendations**

- A strategy to increase enrollments and improve the quality, relevance, and linkages with the private sector and industry is a priority for this sector.
- Massive efforts in capacity building and infrastructure are needed to improve the performance of this sector. A cost-benefit analysis of expenditures in vocational training is also needed to make informed decisions in terms of investments per subsector.

**Improving Health Services for All**

66. **The performance and development of the Libyan health sector reflects both the country’s commitment to social welfare and its heavily decentralized political and administrative systems.** In principle, all Libyans are covered by public health insurance, and their benefits package covers nearly all curative and preventive care. Immunization, prenatal coverage, and births attended by a qualified health care worker are also universal. The infant mortality rate was halved from 35 per 1,000 children in 1990 to 18 per 1,000 in 2005. Life expectancy in 2005 was 74 years, higher than in many comparable countries. The country seems well advanced into its epidemiologic transition from infectious diseases to noncommunicable diseases as the main causes of deaths.

67. **While Libya appears to provide universal access to care, outcomes are more problematic when it comes to quality and regulations.** On average, about a fifth of Libyan expenditures on health are out-of-pocket, a significant amount despite free access to a generous package for all citizens. Specifically, the health system has important shortcomings. First, it lacks a strong national institutional and informational base for effective health policy and planning, regulations, and quality assurance and quality control. Allocative efficiency appears very low, since there is very little information on the burden of disease and risk factors, and on their distribution by age, gender, location, and income distribution by quintiles, which points toward misallocation of financial resources. There is a wide supply of public
health services available to citizens, which leads to maldistribution of public and private expenditures across income and regions because there is no gatekeeping and no hierarchy in access to care and patient referral. Financing of health facilities is input-based and providers have no incentive mechanisms for productivity or performance. There is an attitude that access to health care is “a free lunch” that should be used as often and as much possible, with little regard to adequacy of treatment or to costs. There are almost no programs for noncommunicable disease prevention, even though 53 percent of the years of life lost are due to noncommunicable diseases. The financing system also prioritizes the provision of inputs, and is not output-based, with payment to hospitals based on ex ante agreements among the Ministry of Health, the Ministry of Finance, and the hospitals themselves. Libya spends somewhat less on health and health care than countries of comparable socioeconomic level, with total government expenditure on health recently decreasing to about 7.5 percent of total government expenditures—well below the levels of other middle-income countries. The Libyan health system has low internal technical efficiency, no human resources management policy, and no explicit standards for licensing health professionals, for licensing and accrediting facilities, or for treatment protocols or disease management. Since all physicians are salaried, there is no inherent financial incentive to increase productivity or provide better care.

68. **The General People’s Committee for Health and Environment 2008–12 Development Program is a comprehensive document.** It reviews the 2002–06 allocation of resources and outcomes and sets priorities. It captures the need to improve the quality of services in Libya, including an emphasis on primary health care, the development of social health insurance, a review of health legislation, improvement in pharmaceutical and medical equipment procurement and distribution mechanisms, and improvement in medical education and training.

World Bank Recommendations

69. **Libyan authorities understand the challenges facing the health system, but their desire to carry out reforms is slow in translating into concrete measures.** The recommendations that follow address the issues identified in the 2008–12 Development Program and areas that were not explicitly addressed.

- In the short term, (one year), build a national health management information system. While establishing the system may take time, the necessary policy decisions need to be made and resources allocated as soon as possible in order to support the quality-oriented goals and strategies highlighted in the development program.
- Establish a health policy and strategy unit in the Ministry of Health with strong capabilities in policymaking, policy analysis, and monitoring and evaluation.
- In the medium to long term (beyond three years), review medical school admissions criteria and align admissions with long-term physician needs. Introduce licensing and accreditation criteria applicable to both the private and public sectors.
- Develop standard treatment protocols and disease management programs for the most prevalent and/or costly medical services. Ditto for a list of essential and negative drugs.
- Review existing budgeting and payment models with a view to moving toward output-based payment. Consider the pros and cons of nominal user charges to curtail unnecessary use of services while promoting necessary services.
- Introduce gatekeeping and a rational patient referral system across the four levels of health care.
• Review the mapping of health facilities in line with demographic transition and household and health surveys.

• Diminish the role of the state as a purchaser of services, which may contribute to supporting an increasing efficiency and improved health outcomes throughout the system. This might involve establishing a separate health fund or agency and service provision by making the management and funding of state-owned health facilities more autonomous and by introducing output-based payment for health services. International lessons of introducing these innovative schemes are available worldwide.

70. **To support the previous efforts, several technical studies need to be carried out**, including: (a) a review of the curriculum of medical school training, including admissions criteria in line with physician needs, leading to new licensing and accreditation criteria; (b) a review of the list of essential positive and negative drugs based on cost-effectiveness to enable a more rational use of medications; (c) a mapping of the health facilities in line with demographic-cum-epidemiologic transition; (d) new manuals on standard treatment protocols and disease management programs for the most prevalent and/or costly medical conditions; (e) a user’s satisfaction survey to inquire about citizens’ perceptions; (f) a provider’s behavioral survey, exploring Libyans’ attitudes toward piloting performance-based payment schemes); and (g) a public expenditure tracking survey, verifying whether public resources are leaked in their use by the Shaabiat.

### Increasing the Efficiency of the Power Sector in Libya

71. **Universal electricity service has been achieved in Libya and the Government’s redistributive policies have ensured that electricity tariffs remain affordable to most households.** The state has consistently intervened throughout the production chain. In 1983, it established a publicly owned company (the General Electricity Company of Libya, GECOL) to operate the country’s power grid and deliver electricity to consumers. Downstream, the state decides on GECOL tariffs and keeps them affordable to consumers, while it compensates the utility for operating deficits resulting from below-cost end-user tariffs. The state also ensures that GECOL is supplied with fuel oil or natural gas by the National Oil Company at prices below international levels. These interventions have a high cost, which reflects an inefficient allocation of resources in the industry and does not promote high performance.

72. **The vision for the sector now seems to have a clear diagnostic, goals and accompanying resources.** A sector strategy was prepared in 2008. Given the strong prospects for economic growth in Libya, the power sector faces daunting challenges in coping with growing electricity demand, ensuring the sector’s financial sustainability, and achieving its vision of a system that can provide reliable electricity services on competitive terms. The challenges are huge: data show a maximum demand of 4,310 megawatts in 2007, but the investment plan highlights an increase in generation capacity to 12,000 megawatts by 2012. Electricity tariffs in Libya are very low compared with other countries, and subsidies in Libya represent a huge fiscal cost and do not encourage efficient use of energy. In total, electricity subsidies represented approximately 6 percent of GDP in 2007. Low tariffs are justified in Libya by the low income of most households. The 2006 electricity tariff reform sent the wrong signal to consumers about the need to use electricity efficiently when the Government increased the social “threshold” (minimum level of consumption for a household to benefit from a subsidy) from 500 to 1,000 kilowatt-hours. It also led to a deterioration of the financial situation of GECOL, provoking calls for more subsidies. Implicit subsidies and hidden costs are significant. The former increased from 1.4 to 4.6 percent of GDP between 2001 and 2007, and the latter decreased from 2.7 percent of GDP in 2000 to 1.1 percent of GDP in 2007. At present, most consumers, poor or not, benefit from subsidized electricity.
Reducing subsidies captured by non-poor households should be the priority of tariff reform, but this has to be done gradually and with sensible considerations to political constraints.

World Bank Recommendations

73. **Reforming the power sector in Libya is crucial for sustained high growth and development.** Adding an average of 1,450 megawatts generation capacity yearly—while only an average of 100 megawatts per year was added during 2000–06—not only requires quick and well-designed contracts, but will also need mobilization within the company and its local suppliers. It also entails general policies to:

- Improve the institutional framework and accountability;
- Collect and manage sector statistics to guide planning, operations and maintenance, and monitoring and evaluation;
- Adjust low and highly subsidized tariffs;
- Make energy subsidies more transparent and reduce hidden costs;
- Increase private-sector participation and competition in the delivery of electricity services;
- Reduce electricity consumption.

74. **More specific reform challenges calling for actions include the need to:**

- On the accountability front, validate the sector strategy and separate policymaking from regulation and service provision. The Ministry of Water, Electricity, and Gas (MWEG) sets policies, performs as the regulator, and is closely involved with the operations of GECOL. Likewise, GECOL is closely associated with policymaking and regulation. This lack of clarity in the roles and responsibilities of different sector players hampers accountability and transparency in the sector. In addition, the sector has yet to validate and implement its 2008 strategy.

- Enhance the fiscal discipline and fill information gaps in the sector supported by the creation of a sector Observatory. The current institutional arrangement does not induce greater efficiency in the sector. GECOL has little accountability regarding its capital investment program, whereas the Government has yet to condition its capital contribution to the performance achieved by the company. The Ministry of Planning should condition the disbursement of its capital budget allocation against the achievement of specified performance indicators—availability of power plants, ratings of power plant capacity, distribution and transmission losses, and commercial losses. Improved forecasting of future demand and alternative options to lower investment costs are needed. Because accurate information is critical to effective decision-making, a sector Observatory could be created within MWEG to collect, store, analyze, and publish sector statistics while ensuring data consistency from year to year.

- Reform low and heavily subsidized electricity tariffs. Although electricity subsidies can help protect consumer purchasing power, share the oil rent with the whole population, and achieve other socioeconomic goals, there is an urgent need to target subsidies because the current system is highly regressive, that is, it benefits households earning higher incomes. A radical change in how energy subsidies are channeled to the power sector is urgently needed to enable GECOL to make decisions about the allocation of economic resources on the basis of market prices, not on administered prices, while preserving the social tariff on the poorest. The Government could also
improve its pro-social tariff policy by targeting consumption subsidies and making them more transparent. Overall, the electricity subsidy reform for households will have to be gradual and accompanied by an adequate safety net. For large consumers, the Government will need to study tradeoffs stemming from the restructuring of electricity tariffs. To date, Libyan low electricity tariffs make Libya an appealing destination for foreign investment in industries that are heavy consumers of energy. There is consequently a need to ensure consistency between the country industrialization strategy and any future reform of electricity tariffs for industrial users.

- Design a fuel energy price formula linking the evolution of GECOL energy prices to international market fluctuations and implement an aggressive program to reduce commercial and technical losses.

- Introduce the private sector into the electricity sector. To date, private sector participation remains at an early stage. The current regulatory framework provides GECOL with a nationwide monopoly over the provision of electricity services. But GECOL can enter into joint venture operations for production or any other activity in the sector as appropriate. New sector legislation authorizing private-sector participation is highly recommended. One option the Government might consider, in addition to devising and implementing demand-side management measures, is to solicit the private sector to develop independent power projects (IPPs)—for instance, by promoting self-generation by large consumers such as cement factories, or by introducing the private sector in collecting and computerizing bills, and in billing customers.

- Fill the gap of investment in renewable energy, energy efficiency, and demand-side management. In the renewable energy sector, the renewable energy authority should become fully operational. A sound wind and solar atlas should be prepared and promising areas identified. Wind and solar technology are considered a competitive future source of power generation in the region. Libya should explore its options and develop a plan with projects to be developed with private sector participation. The Government should also launch energy-efficiency and demand-side management programs. Such programs can include codes and standards for new buildings and appliances, solar water heating to equip households, compact fluorescent lamps for commercial buildings, and incentive programs to induce industrial site audits.

- Prepare a demand management program that introduces and enforces new building codes, and new standards for electrical appliances, street lighting, and industrial sites.

**Rebalancing Road Maintenance and Network Development**

75. **The transport sector is one of the keys to the future development and well-being of Libya.** The country’s desert and long coast give rise to high transport costs, leaving many inland communities profoundly isolated, and pose a challenge to national cohesion and unity. The road sector is the dominant mode of transport in the absence of any railway, and Libya should be credited for having developed a respectably sized non-urban road network of about 30,000 kilometers, of which 90 percent is paved. The road density is thus generally satisfactory considering the size of the population, the vehicle fleet, and the fact that a large part of the country is uninhabitable semidesert.

76. **The road sector is exceptionally well organized with the equivalent of a central Ministry of Transport in charge of all transport subsectors.** An external highway directorate (Road and Bridge Department) was recently established to manage the road network outside urban areas. Considering the lack of qualified technical staff and other human resources constraints, the limited decentralization of road management to eight regional offices seems appropriate, and the sector has an overall staffing level
that seems adequate, although on the low side. Consequently, the reliance on consulting firms to undertake studies, design, and construction supervision and on private contractors to undertake most road works is also an institutional strength and commendable.

77. However, there are other current arrangements in the sector that do not promote efficiency and often also make it difficult to effectively address matters of public interest. The evidence may be seen all over the country: roads have not been maintained as well as they should, road construction projects are delayed and contracts sometimes cancelled, transport services leave a lot to be desired, and road traffic safety is poor. This situation is not only a result of the past conflicts and lack of funds; it derives mostly from inadequate policies and institutional weaknesses.

78. The formulation of a long-term vision (10 to 15 years) is critical. An overall strategy for the development of the road sector would provide a good framework for the identification of key actions required for transforming the road sector in a first phase encompassing the period up to the end of 2012.

79. The key elements of such a vision for the road sector are next. The national road network has to be rehabilitated, and where required, upgraded. It will be managed by an autonomous road agency and its preservation and further development financed by road-user charges, which are not part of the consolidated budget. Local roads will be managed by local road agencies under the Shaabiat, and a substantial part of their costs will also be financed by road-user charges. A road maintenance fund (or any adequate earmarking arrangements to secure uninterrupted financing for maintenance) will have been established to collect road-user charges and to serve as the procurer of road maintenance services from the central road agency and local roads agencies. Budget funds will be directed only to the development of rural roads required to improve rural accessibility and new highways. Road works will mainly be carried out by private contractors, including under long-term contracts for performance-based maintenance management where appropriate. A substantial amount of work will be contracted out to small local contractors under competition. Consultants would carry out most technical studies, prepare tender documents, and assist in procurement and construction supervision, much as is the case today.

80. The vision formulated above is ambitious; it will be a challenge to Libya to restructure the transport sector accordingly. In the short-term perspective, it is important to embark on a process of change that will eventually lead to the realization of the vision. Challenges facing the sector include:

- The Department for Roads and Bridges faces limited human and financial implementation capacity.
- Lack of a comprehensive sectoral strategy. Road construction programs are not prioritized based on a Master Transport Plan.
- There is insufficient knowledge of the pavement conditions due to a lack of regular road condition surveys. Traffic safety is deteriorating.
- Whereas Libya increased road investment in the 1990s, the transport sector’s share of the budget has been low. Libyan road expenditures will increase under the PIP, but the Government has difficulties in executing the projected expenses as planned.
• The neglect of preventive maintenance has resulted in an overall deterioration of a major part of Libya’s road network. This shouldn’t happen again.

• High fuel subsidies and relatively low road charges and truck tariffs are not financially sustainable.

**World Bank Recommendations**

• It is urgent to carry out an organizational review to address overlaps and gaps in roles and responsibilities and to make the road administration more autonomous.

• There is a critical need to prepare an updated Transport Master Plan with a 15-year time horizon following technical and economic feasibility and other agreed criteria.

• Authorities should consider increasing budgetary allocations, especially for regular maintenance and rehabilitation of existing road assets not covered by the PIP.

• There is a need to implement a Road Asset Management system.

• It is advisable to explore financing arrangements, that is, a gradual reduction of fuel subsidies, increases in road-user charges, and private sector financing.

• Authorities need to continue to pilot private-public partnerships to operate and maintain tolled highways, and to finance timely regular maintenance through multiyear, performance-based contracts.

• It is crucial to review legislation on axle load limits and amend the structure of fines for overloading and enforcement arrangements to reduce the risk of road damage by overloaded trucks.

• Carry out a safety management capacity assessment as a first step in addressing the poor traffic safety situation in Libya.

**Making Water Use Efficient and Sustainable**

81. **Libya has adequate levels of water, but its production is stressed and has sharp geographic and year-by-year variations.** The country is relying on nonrenewable groundwater, despite having augmented its supplies by the Great Man Made River (GMMR) and, to a lesser extent, projects to desalinate seawater. Agriculture uses 78 percent of water withdrawals. But like other Middle East and North Africa (MENA) countries, Libya lacks sufficient water to grow its own food, which makes trade vital.

82. **The country also stands out in the MENA as a low performer in water-sector management.** The sector’s governance is weak because of limited accountability, lack of transparency, and little participation by users. Even with the relaxed fiscal space of today, there is an urgent need to improve water-sector performance and reduce its dependence on public funds. Subsidies are high and untargeted. Based on an assumed long-run marginal cost (LRMC) of LD1.15 per cubic meter for urban water and LD1.01 per cubic meter in irrigation, the water sector absorbed approximately 1.4 percent of GDP in subsidies in 2006. About 90 percent of these subsidies went to urban water supply and sanitation. These subsidies are likely to expand in absolute terms and as a relative share of GDP as access to urban water and sanitation grows and as substantially more water is made available to farmers. Although the water infrastructure needs to be rehabilitated, too little is spent on operation and maintenance.
83. **The water sector is at the beginning of a transformation.** The sector is emerging from a period characterized by low performance in urban service delivery; poor water quality; limited ability to valorize the large GMMR investment that was intended for irrigation; low utility revenues due to low tariffs, poor collection, and high operating costs; and increasing losses because of inefficient management and poor demand management. There is no universal metering, and water utilities do not recover the high costs they incur. With consumers paying minimal amounts, utilities are totally dependent on public funds. Finally, private sector participation in the sector is low.

**World Bank Recommendations**

84. **As part of the process of building and implementing a vision for the sector, three key actions are needed.**

- First, a comprehensive strategy and action plan is needed for irrigation, water supply and sanitation, and water management. The existing draft water sector and strategy proposal for 2025 needs to be updated and ratified (based on previous reviews and in consultation with stakeholders). In support of the draft sector strategy, an ambitious LD15 billion investment program is planned for 2008–12. It has two objectives: to improve access and service quality for water supply and sanitation and to make more water available for irrigation. The massive investment in production, transfers, and distribution should help compensate for the drying out of wells in the coastal zones. In general, public investment in the sector needs to consider that large water projects often face delays and difficulties of financial sustainability. Preparing this plan would provide an opportunity for water users, service providers, and the Government to reach a consensus on tradeoffs for developing and allocating water, and on the sequencing of reforms to improve the governance of the sector. A full range of economic, social, and environmental implications would also need to be considered.

- Second, improving the incentive framework in urban water supply and sanitation will require authorities to gradually raise tariffs in order to recover at least maintenance costs and a small portion of the investment. As an alternative to the current blanket of free water for all, a targeted subsidy could be focused on the poor. Collection rates need to be increased, and universal metering needs to be introduced. The private sector could help create a modern irrigation utility dependent on user fees rather than public subsidies.

- Third, the reliance on the public purse for GMMR water should be reduced. Necessary improvements include an effective cost-recovery mechanism for GMMR water that would maximize crop value per drop; appropriate water pricing for GMMR users; improved returns for irrigated farming, which are particularly low where GMMR water is used; a crop-productivity enhancement program (especially for cereals) to complement the GMMR water provision package for farmers, which would require commensurate investment in agricultural research, extension, marketing, and post-harvest support; and private sector help to create a modern irrigation management utility dependent on user fees, not public subsidies. If these plans do not materialize, the subsidies that will be necessary for water usage—estimated to reach the
cumulated sum of LD800 million for the whole 2008–12 Development Program—will increase, an outcome that would not be an efficient use of public resources.

Final Remarks and Next Steps

85. **Public expenditure needs to foster the comparative advantage of the Libyan economy that lies in oil and non-tradables.** This means a broad range of labor-intensive activities, such as construction in infrastructure and residential housing, oil-related services, banking and finance, and health care. Though wages are still low, Libya’s per capita income is more than five times above China and Morocco, which feature similar productivity in agriculture and manufacturing, likely indicating limited potential for competitiveness in many tradable sectors, excepting possible niches.

86. **The service sector is the global economy’s largest jobs generator and this could be replicated by Libya.** Over the last ten years, virtually all growth in employment in countries with income similar to Libya – or higher – has been in services. Libya already has higher exports per capita than the US, a country four times richer and with 85% of its employment in services. This suggests that modern Libya’s economic opportunities, other than oil and niche agriculture and manufactures, lie in services, domestic and international. The service sector in Libya is undeveloped, repressed by large government, weak incentives and competition in the private sector, and constrained by severe infrastructure gaps and limited exposure to international business practices. Dealing with these constraints will mainly require not only a sustained and well designed public investment program as the one examined in this report, but domestic reforms such as those allowing WTO accession which can help in strengthening investment in services, affirming commitment to economic integration, increasing transparency and predictability, and bringing incentives to the private sector.

87. **Libya needs a growing, diversified and competitive private economy to generate employment and benefit consumers.** Although Libya’s economic structure and recent history is in many respects unique, much can be learned from international experience. The transition from a state-dominated economy to a more private-based and diversified economy implies changing government functions, but certainly not the disappearance of government. In some sectors, such as health and education, public services should remain the leading form to service the nation.

88. **While the Libyan Government reduces its role as economic controller and operator, it must strengthen its roles to foster competition, regulate markets where essential, and provide high quality institutions and investments under new public-private partnerships, as well as to provide essential public services and an improved infrastructure.** A variety of new contractual, ownership and regulatory relationships will need to emerge to create successful public-private partnerships to deliver services and products formerly delivered exclusively by the public sector. While there is great promise in private delivery of services, the challenge, capacity and time taken to properly design and implement public-private partnerships should not be underestimated. Policies and programs should encourage the expansion and formalization of the domestic private sector, while also taking advantage of foreign direct investment. The tax and regulatory burden, as well as the provision of services, are key determinants for firms in the transition from informal to formal status. Allowing new entry of businesses in protected or monopolized markets is likely to be the single most powerful force in
driving transition, so barriers to entry are particularly important to dismantle.

89. **This report highlights the broad agenda of reforms that Libyan authorities need to consider to revise their 2009-13 public investment program with the aim to foster productive diversification.** The proposed agenda requires correct prioritization and sequencing, beginning with the measures that will have a short-term impact in 2009/10. At the same time, groundwork must be laid that will sustain medium-term (up to 2013) efforts and beyond. The Government should send a clear signal that it intends to define new rules of the game for selecting with a productive bias, preparing, and managing public projects, reinforcing messages of commitment, better governance, transparency, and quality of spending. Mere public promises of more resources would be meaningless because the capacity to implement them is limited. Both the design and implementation of this strategy must be consistent across line ministries. The process must be transparent, open, and participatory.

90. **This ambitious reform agenda will require strong leadership of all parties involved, but especially the recently created GPCPF, as well as the line ministries involved.** An important rule of thumb in the process of change, perhaps quite relevant to a changing society such as Libya, is the need to adopt key selective institutions in place, while keeping decision-making as a “learning by doing,” well-monitored process. The future development agenda is less about pouring in huge investment resources and more about improving quality and selectiveness toward high-return investments that will support productive diversification. In general, quality investment is essentially a matter of adopting a few smart policies and projects, setting realistic standards with capable staffing, and steering solid project implementation.