

Executive

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SPECIAL REPORT

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SEEKING CLARITY

■ “Lebanon’s geographic location and trading history dictate the need for three basic premises in terms of its Economic Policy: a strong and stable currency, advantageous trading facilities and low taxes.”

Michel Chiha

The Lebanese banking sector, a long view

Once there was a time when a Lebanese banker had a national vision. Whether a contemporary citizen agrees with this vision or not is immaterial for recognizing its historic influence. Even the question whether or not this banker was consciously intending—as some Western academics speculate—to steer the economy in a direction that was optimal for the interest of the financial bourgeoisie in the early and mid-20th century, is unimportant for the consideration that the vision shared by this banker and by his intellectual and social peers has played a profound role in writing the story of this country. It has determined the Lebanese national narrative and the country’s broad economic course for almost a century—the entire period since the adoption of modern Lebanon’s first constitution and the achievement of independence later on.

The historic fact is that the visionary banker, patriot, and influencer, Michel Chiha, was among the key shapers of not only the 1926 constitution but also of post-independence politics and the Lebanese merchant-republic paradigm. Chiha’s credo was that a nation is created by “the desire and the will to live together.” For him, Lebanon was a composite country dependent on internal balance, a nation of many “associated confessional minorities,” and a nation whose fortune was determined by a confluence of geographic givens—the mountain and the sea—with part mythical, part historic factors, namely the Phoenician heritage of seafar-

ing trade. The nation’s economic policy would have to incorporate a freewheeling market system, Chiha believed, because to his mind “even a moderate version of a tightly controlled economic system is not a rational option for Lebanon.”

Whether one agrees with or disdains the invention of a nation state narrative grown on Lebanese territory from an essentially European historicist seed, it is a truth not to be ignored that this country was shaped by a *laissez-faire* commercial culture mingled with a quasi-mythical tale of entrepreneurial spirit, trader mentality, and prowess in financial intermediation. In a competition over economic direction that a century ago juxtaposed industry and agriculture to trade and services, the course of modern Lebanon was effectively set from its first charting toward a type of economic give-and-take activity that would be nurtured by, and be attractive to, bankers in a mutually profitable symbiosis with landed gentry—or, to put it more accurately in local terms, the traditional *zu’ama* with all their pseudo-feudal webs of tribal privileges, emotional interactions, and social obligations—and that allowed for some seriously oligopolistic cultural traits of communal and religious tribalism.

TESTS OF FORTUNE

All this made Lebanon flourish in the ways it did from the 1950s onward (when it did blossom radiantly for substantial periods of relative peace and growth of, admittedly uneven, wealth) in ways



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that regional peer countries didn't manifest and that Lebanon could not have achieved without its traders, middlemen, and bankers. This history and merchant-republic paradigm with confessional and oligopolistic patterns, however, also played a massive role in bringing on the tests and temptations of the Lebanese fortune in the context of its detrimental exposure to geopolitical interests in the years of imported and indigenous internal violence and in feeding social imbalances in application of this economic model in the last 30 years.

Long before there were 20th century-type bankers in Lebanon, there were farmers, tribal warriors, seafaring traders, artful crafts people, small but enterprising producers, hospitable innkeepers, money lenders, healers, drafters of contracts, useful scribes, religious and cultural adopters and educators, rebellious and brilliant poets, non-conformist sculptors, painters, and thinkers, monastic minds, and even hermits and spiritual visionaries.

With this historic mental wealth of note, it would be a mistaken belief to think that Lebanese, like human beings in general, should or could be molded into a homogenous group—say, a two-layered and egalitarian sort of society composed largely of an internationally competitive agrarian producer class and an equally competitive urban class of industrial producers, a small society with a superstructure of, however ideologically aligned, administrative mandarins. It, by contrast, deserves to be acknowledged that Lebanon is a prime (and indeed exceptional beyond the confines of the Arab region) incarnation of a nation whose human diversity is its engine and capitalist division of labor is the transmission.

Tapping into this diversity, but capitalizing on it only with deteriorating efficacy, the private sector is the historic main conduit of progress and social reality in Lebanon, with all the advantages that this has generated. But the private sector has been an imperfect engine, with deteriorating strength and, by global comparison, dwindling productivity, with all that this means in terms of impaired developments of public goods, for the concentration of capital and market power, and for harmful paralyzes of social mobility reflected in economic inequality and expressed through rentier and entitlement mindsets that infested society from the very top deep down into the sectarian upper, middle, and even lower-middle classes.

These detriments of the Lebanese model—impaired social mobility, entrapment of wealth, power

and freedom in the hands of a few, and horrible underinvestment in public goods—have been visible for the entirety of the past three decades. They have been criminally ignored and those who benefited from them are now facing the consequences of their moral failings. The people cannot but be applauded for insisting, in the demonstrations of the *thawra* (revolution), that Lebanon's political and financial failings have to be remedied. And as many see and say clearly, this restoration of Lebanon requires a redesign of the moribund political system, judicial restitution of illicit gains, and strenuous social efforts and economic sacrifices of many coming years.

But it is also of paramount importance—and vital in charting the next phase of Lebanon's national course—to acknowledge and take into account that the country is inextricably embedded in the structures of a capitalist world, a world that has for the last 40 years not been challenged by any credible alternative. As it did the world's economically leading societies, and perhaps much more so than for many small economies in culturally less exposed positions, capitalism has shaped this country and, to rely on a keen observation of political economist Joseph Schumpeter, it has created the interests that are reflected in the "manufactured will" of the populace in this Lebanese democracy.

This has to be recognized if one wants to embark on changing the Lebanese model. One can argue with Schumpeter (who highlighted this point in his seminal book *Capitalism, Socialism and Democracy*) that capitalism, due to the fascination created by the tangible success of entrepreneurial activity, has acted over centuries as "the

propelling force of the rationalization of human behavior." One can then subsume in local application of this thought that all that is rational as a determinant in the evolution of the Lebanese merchant republic has, since this state's formative years, been inseparable from the DNA of capitalism—which means that banking, trade, and private entrepreneurialism can in no way be behaviorally cut out, economically amputated, or genetically eliminated from the overall DNA of Lebanese society, irrespective of its sad secto-political reality and all that is in need of rectification and healing in this polity.

■ It deserves to be acknowledged that Lebanon is a prime incarnation of a nation whose human diversity is its engine.



LEBANON'S FINANCIAL VITALITY

This entwinement of the banking and commercial DNA with the viability of Lebanon as late-emerging state in the context of early 20th century geopolitics means that it is futile to think Lebanon could exist in any contingent future without this banking ingredient in the national political identity. It is simply not possible to retain Lebanon in the sense of its history and functional organization of society and take the banker out of Lebanon. In this sense, it serves well to remember what Chiha emphasized to his compatriots of 75 years ago—that the Lebanese banker needed to be neither a gold-encrusted Croesus nor a money-worshipping “Mammonist” but fulfills his role best as simply a “talented money technician” when combined with the crucial human qualification of “someone who embodies confidence.” (Chiha apparently expounded this insight years before it became a hollow stock phrase in teaching economic fundamentals at b-schools and a boilerplate cliché thrown around by banks’ PR departments.)

On one hand, this country’s human talent reservoir means the Lebanese are much more than just a gaggle of bankers and their subservient economists, of monopolist traders and their obliging marketers, of rentier landlords and corruptible rentier politicians who (while they instinctively and dishonestly denounce rentierism) press down on the collective neck of a vast proletarian rest. The talented, educated, and underemployed Lebanese women (and even some males) can be top agrarian and industrial producers as well as excel in all of the economic callings mentioned above. Lebanese talent and human capital should not be viewed

solely or even primarily through the 20th century societal stratification lens of the western liberal market economy that, as a model, has advanced far into old age of its civilizational lifecycle.

It would on the other hand also be delusional, however, to assume that Lebanon will thrive by ideologically or operationally reining in its talents in trade, banking, and marketing or by artificially limiting the strength of its banking sector by means of either politics of ideology. In absolute terms, the Lebanese banking sector—like this entire polity—is small, with an exceedingly small contribution to global GDP (even in pre-2020 terms) and a minuscule role in international financial markets. In relative terms of size to the local economy and strength of its human capital, however, the Lebanese banking sector has been growing surprisingly well over the post-conflict decades from 1990.

NEED FOR RENEWAL

This relative increase of banking is all the more notable when financial sector performance is compared with the insufficiently growing professionalism and productivity of many other specializations in the economy. The extent and exceptional scope of this banking growth is further accentuated when examined by the harsh lights of the severe external shocks that the country was exposed to in these three decades, not to speak of the fact that ethics and law as enforced by the state were politically and societally insufficient in the past three decades.

In the global sense and also by its internal coherence, legal, regulatory, and informal Lebanese solidarity, the country’s entire banking sector has been regarded by some local economists as if it were a single bank, and rightly so, given the tight knit identity and extensive formal and even unspoken alignment of local banks with their supervisors and regulators at the central bank. This very intimate alignment is by ethical, psycho-social, societal, and commercial standards not perfectly desirable and has not panned out over the past decade. Thus the need for digital renewal, for mental challenging of entrenched thought patterns in the top banking stratum, and for corruption-resistant managerial change and infusion of fresh minds into decision-making ranks of local banks has been building and has become ever-more unmistakable by time of this writing, judging from the evidence of listening to those who have long, often too long, occupied positions of influence.

For the last nine months, this evidence has been overwhelming—senior bankers (with very few ex-

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ceptions, see Obegi interview page 28) have either been totally silent or exceedingly defensive in their media statements and interactions. They have been found wanting in policy declarations and in their attempts to deflect public attention—quite understandably, but not productively so—from the realities that Lebanese are facing when attempting to access their money at their banks. This is not to say that sole responsibility lies on the banking sector. It has been clear over these past few months that two conflicting narratives have been gaining traction dependent on political leanings: one that lays the blame of Lebanon's economic crisis at the door of an intractable and corrupt political elite, and one that has been throwing increasing ire and vitriol toward the banking sector, in particular the governor of the central bank, laying the blame firmly at the feet of Lebanon's financial sector. The reality, as it often is, is being obscured by the rife rumors and political machinations that are occurring in the country. What can be said, without any equivocation, is that there is plenty of blame to pass around. Amid these competing narratives and ideologies, too many in the banking sector have—perhaps fearing the inevitable backlash—stayed silent, and, by not speaking up at all, and doing so for weeks

and months, up to mid this month, sent out the worse kind of message.

Lebanese banks need digital transformation, internal renewal, and a move to the future—but the mechanism and method for organic change has to be what Schumpeter called capitalism's “perennial gale of creative destruction;” it cannot be forced

■ Experience shows how risky government action is and how this role must be surgical in method, ideology-free, informed by facts, and collaborative instead of interventionist.

by the ideology of a temporary government or state intervention. Recent years—especially the time since after the Great Recession of 2007-2009—have been marked

internationally by an increasing understanding that states and governments need to play roles in political economy that go beyond the blind belief in markets preached by economic theorists late in the last century under some neoliberal ideologies and the older “hands-off” thinking of laissez-faire capitalism. But experience of many economic ac-



tions by governments and central banks in the past 100 years—from Keynesian deficit-spending recipes to protectionist experiments, government bail-outs, and quantitative easing that under the impact of the new coronavirus recession have in recent months proliferated exponentially—also shows how risky government action is and how this role must be surgical in method, ideology-free, informed by facts, and collaborative instead of interventionist.

OBJECTIVE AND CONSTRUCTIVE

EXECUTIVE editors have to admit that we have no indication what Chiha would have thought about the sorry state of the Lebanese condition of 2020 or what the Lebanese would think of this current society for whose independence they strove, sacrificed, and even bore martyrdom. One suspects that they would not have been idle or fallen into shock at witnessing the dismal state of the country they loved (notably, a young Chiha's 1919 return to Beirut from Egypt was to a city in "ruins, sadness and silence," a city devastated by the wars of others).

But it is with immensely greater sadness that we confess to our current ignorance. We believe that our assessments of the Lebanese economy, and specifically the banking sector, in our coverage of the past 22 years have been accurate and analytical to the best of our journalistic abilities, collectively as magazine and individually as writers. We have been, and still are, relentlessly striving for an objective and constructive approach in our particular focuses on Lebanese banking, finance, feeble capital markets, policy-making, and political economy.

Thus it is with a sadness that is incomparable to accepting that we cannot divine the thought, feelings, and ambitions of this republic's forebears that we say this: as of mid-2020 the future and productive utilization of the Lebanese banking sector is obscure to our view. Not because of the sector's reduction in size. As Association of Banks in Lebanon board member Waïl Raphaël noted in the association's one interactive on-the-ground meeting with journalists in June 2020, this reduction is happening and driven by rational depositor behaviors and market logic. What is obscure is the rationale, presented by the government in its financial recovery plan, for banking sector restructuring. Introduced with the ominous note that "complacency or partial solutions are not an option" and an apparent determination to allow buildup of risk (the management of which is the existential business

of banks), the government plan declares that "The authorities will elaborate a comprehensive strategy for the restructuring of banks balance sheets in due course," before hinting that "a full restructuring of the banking sector will require new legal powers for the government."

In the testing times of the Lebanese crisis, it is uncertain what the comprehensive strategy and the new legal powers given to the government will look like. Why would the plan further mention new legal powers for relevant supervisory bodies (without naming any)? Were the old powers not sufficient? Why would the plan say that the Lebanese government will contemplate the issuance of five new commercial banking licenses? Is the intention to create specialized sectoral banks, e.g. for agriculture, reminiscent of dated finance models that have not become known for their successes in other jurisdictions? Are the real intentions for the future of banking in Lebanon for a well-regulated, market-driven and efficient banking sector, or are they dreaming a different banking dream, one that was last dreamt in this part of the world in 1963?

The uncertainty over the accurate data points in banking, finance, and debt realities will be resolved, as the numbers on the first part of the year have recently begun to come in, albeit a bit later

■ The uncertainty over the accurate data points in banking, finance, and debt realities will be resolved.

than journalists and analysts might wish for. The uncertainty over eventual mergers and consolidations in the banking sector will vanish with time if market

forces and the banking regulator—Banque du Liban—are allowed to do their job along the same consolidation logic that has been applied in the past decades, and improve on this practice. The uncertainty over the political economy strategy of the Lebanese state is the component that by mid-2020 appears farthest from resolution. The mindset, however, that might be most productive for this economic future, could very well be the mindset of national independence, interdependence, and responsibility—shown before Lebanon gained its statehood and self-determination in the first half of the 20th century—that might be suitable to guide constructive communication between bankers and their political counterparts, something that is urgently needed but has not been in evidence during the past five months.



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By Thomas Schellen

TALKING BANKERS

Banking economists on the Lebanese banking sector

Bankers are people. Brothers, sisters, mothers, fathers, spouses, children, cousins, clients, business advisors, financial partners, and friends of other Lebanese people. Given that over 25,000 individuals are employed in the local banking sector, with high percentages of them being women (in comparison to most not “traditionally female” professions) in a banking workforce that is composed overwhelmingly of university graduates in their most productive years, it would be strange if most Lebanese were not either connected to a banker themselves or by one or a few degrees of separation to someone else who has a personal connection to someone in the banking industry. Young bankers with positions of responsibility were among the peaceful and cheerful Martyrs’ Square crowds shouting *thawra* (revolution) last November that today seem like a distant dream of hope of a reformed Lebanon that belongs to its people.

But in the public discussions that have been raging for many months—a period in which bankers have and continue to be publicly blamed for their roles—the Lebanese banker has been reduced from a living and breathing human being to a cut-out figure in a shadow play.

Mistakes have been made in Lebanese finance over the past three decades. Honest mistakes. Undeniably things need to change. To facilitate and spur on productivity-enhancing behavior and the migration of banking culture into a new and more socially beneficial pattern, better interpersonal communication is needed. Even in normal times, the personal connection between average retail customers and local finance houses are subjected to pressures that easily can make them drift apart. Much worse impairments of trust and increases in the emotional distance between Lebanese citizens and their banks, though, have been the result of the financial and economic crisis of 2019/2020. One collateral impact of the crisis and the, at times, overheated animosities affecting banks and their customers was an unprecedented reticence of banks to communicate.

In response to our outreach to banks since early May 2020, however, two major Lebanese lenders,



Bank Audi and Byblos Bank, directed EXECUTIVE to their lead economists to ask our questions. Both chief economists preferred to answer our questions in writing. In the following we present the answers of Marwan Barakat, group chief economist and head of research at Bank Audi, and Nassib Ghobril, chief economist and head of the economic research and analysis department at Byblos Bank Group.

Presenting our list of questions, we noted, by way of introduction, that a central pillar in the government’s financial rescue plan famously calls for a comprehensive restructuring of the banking sector to decisively address the accumulated “FX mismatches at the central bank,” reveal embedded losses, and refocus “a resized banking system on the distribution of credit to the private sector.” Noting the obvious political economy and



economic policy implications in this narrative, stretching from a need and form of a “haircut” to issues of state intervention in the design of the Lebanese economic system for the coming 20 years or more, led EXECUTIVE to ask about banks’ views regarding the real size of impairments of their assets, the issue of recapitalization of banks, and the acceptable levels of debt that Lebanon can shoulder. Below are the questions posed and the answers received in writing.

E *What are your views with regards to the size of the hole in the banking sector and your views on the need and optimal available means for sanitizing balance sheets?*

MB: While the economic recovery plan contains some positive points and tangible public sector soft landing measures, it also contains some

weaknesses in our opinion, mainly at the level of the banking system restructuring. The figures provided are of course estimates, and might be exaggerated. For instance, one should not forget that the losses attributed to banks’ credit portfolio to the private sector do not at all take into account that when and if borrowers fail to repay banks their dues, banks themselves already have collateral and real guarantees, such as property assets they could seize and monetize. Hence, losses might very well be lower than envisaged in the government’s plan.

It would be wrong to restructure banks without knowing the real amount of losses, and, even more so, wrong to penalize depositors in one way or the other based on inflated or inaccurate loss estimates. Speaking of depositors, it would also be wrong for banks and depositors to bear the burden of the state’s default. When a borrower defaults, lenders seize their assets rather than the borrower (in this case the state) seizing banks’ and depositors’. On another note, looking at the plan put forth by the Association of Banks in Lebanon (ABL) shows that it is possible for the central bank, Banque du Liban (BDL), to avoid losses thanks to a defeasance fund valued at \$40 billion, and that would avoid banks having to incur losses related to their exposure to BDL. Sanitizing balance sheets should take place in close coordination with the BDL and banks themselves and would be in the interest of all stakeholders.

E *What would be the best mechanisms of asset protection in the interest of future generations and for banks’ recapitalizations?*

MB: If all means to protect depositors’ money prove to be insufficient, the best mechanism would be to establish a sovereign fund where part of large depositors’ money is transferred against shares or stakes. Privatizations and selling of state assets would help depositors recoup those funds. We do not believe that all banks’ equity should be wiped out as suggested by the government plan. In line with the ABL’s own plan that is being currently discussed, banks can save part of their equity and thus continue to operate in the future. Once a consensual plan is put in place, and an International Monetary Fund (IMF) agreement is underway, the economic cycle can start again, confidence can resume, and fresh funds inflows might follow from existing and perhaps new shareholders, thus ensuring banks’ recapitalization. The ABL plan mentioned a voluntary deposit-to-capital conversion for those large depositors who believe that banks that are equity-positive once the restructuring is over can ensure share appreciation for them in the future.

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NG: Lebanese citizens lost confidence in the ability and willingness of the executive branch and of political parties in power to deliver public services and to improve their standards of living, as reflected by the Byblos Bank/AUB Consumer Confidence Index. Amid these developments, it is normal that confidence in the banking sector gets affected, as banks are a key part of the Lebanese economy and are the most affected stakeholder of the Lebanese economy by developments, due to the fact that it is the only sector that lends to the entire economy. So it was expected that banks will be impacted by the crisis more than other sectors. However, the perception about banks was affected by a massive campaign that started in November 2019 to put the blame of the crisis on the banking sector in order for political parties in power to evade responsibility. This campaign, which is still ongoing, has affected the perception of citizens toward banks.

Therefore, confidence in the banking sector is closely tied to confidence in the ability and willingness of the executive and legislative branches to implement much-needed structural reforms. The best way to restore confidence is for a government reform plan with sequenced priorities that would create a positive shock in the market, prioritize growth, tackle the size of the public sector, and address the liquidity shortages in the market. The plan that the government issued at the end of April has faced significant criticism from various stakeholders, and did not result in the positive shock that citizens, the private sector, and the diaspora have been waiting for. But an agreement with the IMF on a funded program will be the start of the long road to restoring confidence.

E *What do you see as the best way forward in terms of recovering or rebuilding trust in the banking sector and how much time do you anticipate will be needed until a working level of trust with banks is restored locally and among Lebanese expatriates?*

MB: Building back trust will take time; that is for sure. In order for that to happen, the government must implement an economic recovery plan ensuring an equitable distribution of losses among economic agents. Burdening depositors is certainly not going to bring back trust, on the contrary [it would] damage it for a long period of time. Once a credible plan is put in place, and IMF and perhaps CEDRE funds are on their way, restrictions on withdrawals and transfers might be lifted and trust restored gradually.

E *There seems to be no large disagreement that the banking sector will lose some players by market-driven consolidation or under some form of merger policy that could be implemented in various ways—for example imposed through new laws or guided by the central bank under use of its regulatory toolkits; the government mentions a downsizing of 50 percent in the number of banks and quite a few independent analysts also seem to think that up to half of the banking sector is slated for a rational reduction in terms of total assets. What do you think?*

MB: With a banking sector nearly 5 times larger than pre-crisis GDP, it is normal to say that the local banking sector is overcrowded. The BDL Governor [Riad Salameh] has long advocated that the number of banks should be reduced. In the current conditions, banking institutions more hit than others and/or unable to raise capital in accordance with BDL regulations, might be forced to merge with others. This would ensure the reduction of the number of banks in the market. Only a handful of larger banks would remain, although it is difficult at this point in time to say how many.

NG: There is a large difference between a market-driven consolidation of the banking sector and the imposition of consolidation as stipulated in the government's financial plan. It is market dynamics, economic conditions, and competition among banks that determine the size of the sector and the number of banks, not government interventionism. There are several factors that are having an impact on the banking sector. First, the current

■ “It is market dynamics, economic conditions, and competition among banks that determine the size of the sector and the number of banks, not government interventionism.”

government's decision to default on the foreign obligations of the Lebanese state in March will inevitably result in heavy losses for banks. Second, deposits have declined by \$25 billion between the end

of August 2019 and the end of April 2020. Third, loans to the private sector have regressed by nearly \$6 billion in the first four months of 2020 and by \$15.5 billion since the start of 2019. Fourth, the severe economic contraction and very low level of household confidence have put on hold any prospects of demand for new loans.

Three of these factors are putting pressure on banks, but three of them are market-driven factors that will push the boards of directors of banks to examine the value-added of merging with or ac-

GLOBAL RISKS ARE COMING

In the long term, the current Lebanese crisis will by all historic experiences of other jurisdictions be a traumatic memory but a memory nonetheless. However, the financial landscape for the remainder of the 21st century is likely going to be informed by the impact of the combination of what the International Monetary Fund (IMF) has called “The Great Lockdown” and the impact of new risks that have been highlighted in 2020 and led to what will be remembered as the deepest correction to developed world financial overconfidence and shakedown of socioeconomic complacency in the annals of Western-dominated capitalism. In assessing global macro-financial reality, the Bank for International Settlements (BIS) has very recently expanded its perspective on predictable but immeasurable global risks that originate in humanity’s overlong dismissal of natural risks. Specifically, the risks labeled Green Swans—a term that was the title of a joint publication of BIS and Banque de France, the French central bank, in January 2020—have now been expanded to prominently include the COVID-19 pandemic, adding to the previously identified Green Swan of climate risk. Green swans are “highly likely” but unpredictable in terms of time and

“too complex to fully understand,” the deputy general manager of BIS Luiz Awazu Pereira da Silva emphasizes. To address the new, radically altered global risk landscape, BIS sees the need for proper measurement and pricing of emerging global risks and the need for strengthening resilience of systems and institutions for avoiding/mitigating Green Swans. As already established in climate risk scenarios, such risk management involves multilateral development banks (MDBs), regulators, and the financial sectors of countries around the world. Collaboration between local and international banks has become instrumental in moving economic agents in less developed countries in direction of adoption and promulgation of the environmental, social, and governance (ESG) standards that can contribute to increased efforts in managing environmental risks. In recent years, Lebanese banks that entered SME financing partnerships with International Financial Institutions and MDBs have begun to steer their SME loan applicants toward prudent climate practices and environmental standards. Thus the following question by EXECUTIVE was posed to 15 banks via email, with the option to respond anonymously. Bank Audi’s Marwan Barakat answered.

E How much of a role does the Lebanese banking sector play in contributing toward the creation of not just more short-term productive but long-term sustainable economic sectors in Lebanon that are viable under increased Green Swan risks, and how can the banking sector’s functioning be improved for the development of the productive sectors in a sustainable economy under new macro-social paradigms and trade-offs between economic efficiency and societal resilience that are being anticipated by leading global banking institutions such as BIS?

MB: Of course banks operating in Lebanon have a big role to play as they are the ones ensuring financial intermediation and channeling liquidity toward productive sectors of the economy in order to contribute to their growth. What is required is for the public sector authorities to ensure a conducive investment climate, a proper macroeconomic background, and, above all, political stability, in addition to implementing a credible economic recovery plan, in order for investors to come back to the country and have faith again in its financial system. Once this is ensured, and the public sector has lower financing needs, banks can benefit from more opportunities to lend to the productive sectors of the economy and contribute to their development.

quiring other banks. Also, historically, the banking sector has seen a gradual and orderly consolidation under the supervision of BDL. In the early 1990s, there were about 82 banks in the country. So BDL provided incentives to banks to merge, acquire other players, be acquired by another bank, or exit the market altogether. There are currently 47 commercial banks in the country, in addition to 16 medium- and long-term banks, also known as “investment banks,” that are owned by the commercial banks. Market factors and BDL incentives are the only logical and healthy way to determine the size of the banking sector and the number of banks. And it is up to boards of directors of banks to explore, examine, and determine

the best course for their bank, and it is up to the shareholders through general assemblies to vote on these measures. Therefore, some of the other ideas that have been suggested sound obsolete and out of touch with realities, and have already negatively affected confidence.

E Noting that the discussion over this topic of the optimal number of banks in the country has seen a wide variety of views for the last 20 years, how many banks are appropriate for Lebanon when considering all future expectations from our local economic outlook to the global recession, goals of financial inclusiveness and open-banking-related trends of digital disruption?

MB: See [answer to previous question] above.

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NG: There is no need to venture onto this obsolete path, as there is no such thing as an “optimal” number of banks. Market forces determine the number of banks in any economy, not theoretical assumptions and abstract notions, and certainly not pervasive opinions about the redistribution of income and about punishing banks because they generate income. A small economy can absorb a large number of banks if it is posting healthy growth rates, if it is attracting capital and investments, if it is transparent and has a developed statistical system, if it has an efficient legal system and its political parties respect and abide by the rule of law, and if it provides the proper investment climate and business environment to encourage investments, risk-taking, and expansion by the private sector. Conversely, a large economy that lacks transparency, that suffers from the government’s intrusion and meddling into the private sector, that endures from a large and costly public sector and inefficient bureaucracy, that applies laws arbitrarily, will not have a developed banking sector and will not attract foreign banks or expertise, and, most importantly, will not gain the confidence of potential depositors and borrowers.

E *How large do you think the banking sector asset base will be in relation to Lebanese GDP at the end of this year, next year, and five years from now? How many large banks will remain, and how extensive do you expect the branch networks of the largest banks to be by 2025?*

NG: It is very ironic that the asset base of the Lebanese banking sector will be large relative to the size of the Lebanese economy at the end of 2020. The banking sector’s assets-to-GDP was about 382 percent at the end of 2019. But despite the ongoing decline in deposits and in credit to the private sector in 2020, and despite the “netting” operation on the assets and liabilities’ sides of the consolidated balance sheet of banks as part of the implementation of international accounting standard IFRS 7 that reduced the assets of banks by about 19 percent year-on-year as at April of this year, the economy is shrinking at a much faster rate. The sector’s assets have declined by 5 percent in the first four months of this [year and] deposits regressed by 7 percent [whereas] loans shrank by 12 percent in the first four months of 2020. However, preliminary projections show a contraction in real GDP of about 14 percent for this year, but I believe the economy will contract by 18 percent based on the current trends. Still,

even with a contraction of 14 percent, nominal GDP will shrink from \$52.3 billion in 2019 to about \$33 billion in 2020. As such we estimate the assets-to-GDP ratio to reach about 270 percent of GDP at the end of 2020.

Therefore, these facts and figures discredit the theories and statements by some public officials about the large size of the banking sector relative to the size of the economy and of the need to downsize it through a centrally-planned process. Instead, they should spend their time producing a blueprint for downsizing the size of the bloated, inefficient, unproductive, mismanaged, overstaffed, and costly public sector. This is the most important factor and a *sine qua non* condition to restore the confidence of Lebanese citizens, of the private sector, of the banking sector, of the Lebanese diaspora, and of the Arab and international community.

E *How do you see the idea that banks should strengthen their “distribution of credit to the private sector”? What needs to be changed in the risk approach to productive sector lending?*

MB: Banks have indeed contributed a lot to supporting the economy and its private sector in difficult times by extending credit. No need to expand further on that, you are right. The government seems to believe that banks have a lot of exposure to BDL, which is an indirect exposure to the state itself. They believe that part of such funds should be allocated to the private sector. However, banks have been very cautious with regards to extending new loans to the private sector in the past couple of years due to the accentuated economic slowdown from 2016 to 2019, and private sector borrowers themselves reduced demand for new loans as they scaled down their expansion plans amidst the prevailing conditions. At the same time, political bickering took a toll on reforms and policy-making and BDL and banks had to come to the rescue of the public sector once again, hence the increased sovereign exposure lately. Once the economic cycle starts again, we would like to lend more to the private sector, but the government needs to create the proper macroeconomic conditions for that.

NG: The notion that Lebanese commercial banks do not lend to the private sector is politically-motivated and displays a deliberate lack of knowledge about the functioning and operations of Lebanese banks, as the numbers speak for themselves. Figures issued by BDL show that utilized credits by the private sector totaled \$59.6 billion at


the end of 2019, despite a decrease of \$10 billion, or 14.3 percent from \$69.5 billion at end-2018.

Further, lending to the private sector exceeded 100 percent of GDP, which shows that banks have reached the prudential limit to lend to the private sector relative to the size of the economy. Still, banks would have liked, and still want, to lend even more to the private sector. But the very large size of the informal economy has prevented such lending. According to the IMF's estimates and to the Central Administration of Statistics' national accounts, the size of the informal economy is about 30 percent of nominal GDP or about \$15 billion based on the size of the economy in 2018.

Last but not least, the executive branch and the political class should realize that they are the reason for the increase in interest rates through politically and electorally-driven decisions that widened the fiscal deficit and increased the borrowing needs of the government. Therefore, a sustained effort to reduce public expenditures drastically is the fastest way to produce market-driven low interest rates, as the current forced and administrative measures to have reduced rates are artificial, temporary, and will not restore the confidence of borrowers.

E *The vision for the Lebanese economy is to return to growth. Banking has not been mentioned as much as agriculture and industry in this context. In the past,*

banking had a big role not just in financing of the public and private sector but also in terms of contribution to taxes and employment. How large do you estimate can the contribution of banking to GDP and fiscal revenue be in the future and how does this compare to the average of the five years until 2018? How many jobs will a restructured banking sector provide and how many new hires can be expected from the sector per year between now and 2025?

MB: A downsized banking sector in a smaller-sized economy will definitely bring some changes. While efforts to promote the primary and secondary sectors of the economy are welcome, and we have been calling for supportive government policies for those sectors for a long time, Lebanon will remain services-oriented to a large extent. Hence, banking and financial services will continue to play an important role in economic activity. However, with much lower banking sector activity and higher corporate tax rates, [the] earnings generation capacity of banks will be affected and their contribution to government revenues will unfortunately be much lower than in recent years. Banks have been one of the most important taxpayers and perhaps because of their transparency, they have been penalized by the government that saw an easy way of raising revenues. Government efforts should be geared toward raising tax collection and fighting tax evasion. 

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TO BANK OR NOT TO BANK



Questions on data, policy design, and usefulness of assumptions

Economic man is a curious construct. Once thought to be a being superior to the common human in his pursuit of value creation and profit generation, the image of this specialized imaginary human subspecies has fundamentally changed. In fact, economic man has reached a point where some contemporary economists describe this model as emotionally dysfunctional—proposing that economic behavior today requires old paradigms of social paternalism to be replaced by models of social maternalism that might have the power to heal societal cleavages.

Such a genderized ideological spin, however superior a social maternalism model could turn out to be in comparison with the historic male economic models and their many inequities, entails its own riskiness if one considers that any exclusionary assumption of absolute or merely relative superiority engenders dangers for social integrity—whether under current strivings for improved gender sensitivity, greater economic equality, and elimination of racism, or under older concepts of

socialization of private property. Strong notions for the need of new paradigms in economy and finance notwithstanding, the fact is that, by today's realities, economic man and his financial sub-variety, banking man (uncovered by this magazine's anthropological research team as *homo banco bancorum*, who originated in the eastern Mediterranean but has spread all over the world) have culturally evolved by historic necessity.

WIDENING THE PERSPECTIVES

The anthropological assumptions of economic and banking man have morphed into modern concepts of economic agents that require a base of inclusiveness and openness to diversity to achieve their purpose of individual profit optimization within the context of social productivity and integrity. Even the dinosaur-like clinging stakeholders in corporate and financial life who—by the clear evidence of the male-dominant composition of boardrooms (around the world, not just in Arab countries)—have desperately resisted to go as far

really accepting women as their equals, have long been forced to change their tune to, albeit only verbal, affirmations of inclusiveness and social integrity in diverseness.

In addition to the widening of the perspectives with regard to banking and organized or formal economy from the particular, exclusionary, and self-interested focuses to their importance for and orientation upon inclusive growth as core attitudinal component, the other core element necessary for the sustenance and redemption of both the modern economic person and homo banco is data. Data related to the business cycle, the financial market, and all kinds of economic risks have to be properly collected, organized, and interpreted.

Relatively sparse and hard to acquire before the arrival of the digital era, such data has become the life blood of economic existence and has been, for the last 20 or so years, turned into virtual torrents that nurture economic planning and reinforce understanding. Data thus demonstrates tangibly that it is, for example, better for a society, specifically any society that aims for broad economic growth, to develop its banking further than to artificially, ideologically restrain financial markets.

As the data experiences of the year 2020 are underlining with their uncertain and, in hindsight, faulty assumptions about the coronavirus threat and modeling of this threat and economic ramifications, collection of correct and complete data and its proper evaluation is vital for preserving the intactness of the entire social body and the individual social cell, and is crucial for protecting national and individual fortunes.

The same point of the importance of data is being driven home with full force also by the Lebanese economic and financial crisis. In all efforts to assess and address this crisis, there have been huge problems related to the disagreement on data, the interpretation of data streams, and the general insecurity over historical economic data as well as the particular uncertainty over the speed and accuracy of computation of very recent financial and monetary data.

This uncertainty affects both the necessary exceptional analyses relating to the emergency situations on the fiscal, central bank, and commercial banking levels and to the reading and contextualization of the regular data streams of banking, financial markets, public finance, and real economy indicators that have been flowing, albeit persistently less perfectly than desirable, for many years (and that have often been reported and commented on in EXECUTIVE, for example in our mid-year banking focus coverages and end-of-year analysis and outlook issues).

Additionally, the recent months and days have been illuminating the questionable validity of narratives that are incessantly being concocted around data. Such narratives are spread indiscriminately, often without any prior examination and scientific process of verification. In this sense, fake data and also incomplete or misunderstood data has proven to be the opposite of the stabilizing and correct-

ing informational factors that data should be. Fears created by misleading and fake data narratives in Lebanon are actually proving to be even more damaging than the existing data uncertainties, a problem that is further exacerbated by the wielding of fake data as a

weapon in the creation of panic and the instigation of excessive mass fearfulness.

Not to forget, there already are devastating and highly warranted fear factors in the real economy of 2020. These fears and the underlying existential threats are bad enough. But it is precisely those circumstances of real existing economic and social threats to the people that make the addition of fake data narratives such potent dangers that can lead to either unjustified depression and economic paralysis or to confrontation and violence as seen in the first two weeks of June which—if building up much farther—could ultimately escalate into self-destruction of Lebanese society.

THE CRUCIAL ROLE OF ASSUMPTIONS

The data assumptions in the government's economic rescue plan in this context are critically important and need to be beyond reproach as they will inform the way in which the immediate course of financial rescue is pursued. As Dany Baz, chief executive officer of analysis provider and consultancy Bankdata speaks to EXECUTIVE about the veracity of the data used for assessing the Lebanese financial hole, the underlying numbers on the size of banking deposits are based on solid information published regularly by Banque du Liban (BDL), Lebanon's central bank. "BDL publishes its balance sheet fortnightly and total bank deposits are clearly highlighted in the breakdown by currency is based on estimates and obviously USD exposure is paramount," she says. "Figures of \$75-80 billion of foreign currency deposits are realistic."

Also in terms of the impairments of banking assets, she considers the three main sources of impairment to be real, namely the exposure, mainly

■ In all efforts to assess and address this crisis, there have been huge problems related to disagreements on data.

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in hard currency, of banks to BDL, the exposure of banks to eurobonds, and their loan exposure on the domestic private sector. “However, there are some details that need to be taken into account when calculating total impairment [as] I believe the government estimate was more in terms of stock than in terms of flows,” she adds (stock being a snapshot of time as opposed to flow being over time).

Baz points out that regarding banks’ exposure to BDL, no reference to the average duration of these deposits, estimated at seven and a half years, was clearly presented by the Lebanese government in its financial rescue plan. “Was duration taken into account?” she asks, noting that within the current economic and political context, calculation of net present value (value over a certain time period) of this exposure would be much lower than the government assumed, irrespective of what discount rate is used. “Consequently, the total stated impairment would be reduced, bearing in mind that according to international accounting standards, [estimation of expected credit loss] on this exposure should be undertaken, translating into obvious provisioning requirements that would represent a material portion of the stated exposure,” she explains. Or simply put, under accounting rules banks must assume that some money owed to them will not be paid back and so they put aside a provision (a projected expense recorded on their books) to cover this eventuality, meaning that when they reassess the likelihood of repayment, the amount written off is lowered by the difference between the new expected loss and the previously assumed loss already accounted for on their balance sheets.

Uncertainty in terms of the size of eurobond exposure relates, according to Baz, to the question of if and how the residual value (the value after an event) was taken into account, noting that current prices of eurobonds in secondary markets are not reflective of the residual values today and the outcome of negotiations with bondholders have to be waited for to have a real assessment of residual values. Also concerning the size of banks’ loan exposure to the private sector, Baz sees a need for clarification. “It was probably based on flat percentage assumptions and we don’t know if such a figure includes existing cash collaterals and real guarantees on impaired loans (loans that lenders think will likely not be paid in full), which would revise the total downward,” she tells EXECUTIVE (for Q&A in interview see box on page 25).

CONCERNS BEYOND BANKING MATTERS

The need to further examine and evaluate the government’s rescue plan extends beyond the questions concerning materially important aspects of the assumed banking exposure and related data. This has been pointed out by many interested parties to the rescue mission, premier among them the Association of Banks in Lebanon (ABL), in its “Contribution to the Lebanese Government’s

Financial Recovery Plan.” Describing the government’s plan as a mere “accounting exercise,” the contribution consists of two pillars (immediate response action and long-term structural reforms) and five priorities, the first (debt restructuring) and

■ The ABL’s most notable diversion from the government plan is the affirmation of the principle of market integrity as paramount for any banking sector restructuring.

fourth (financial sector restructuring) of which are most material to the future of banking in Lebanon.

The contribution’s sharpest and most noteworthy conceptual divergence from the government plan’s assumptions is the affirmation of the principle of market integrity as paramount for any banking sector restructuring and recapitalization. A “one-size-fits-all approach” to this task would be detrimental to the entire economy, ABL emphasizes, and recapitalization needs to adhere to the principle of “case-by-case” guidance by the central bank as a regulator, under the “aegis of the Basel III systemic event forbearance system.” The regulator alone should decide if any banking entities need to be resolved.

“The plan anticipates that the regulator may also encourage some of the more weakly-capitalized financial institutions to merge,” ABL allowed. Elaborating further on the association’s perspective, ABL board member Tanal Sabbah pointed out to media in a rare June 2020 gathering that an approach such as merging two banks that have become problematic because of imposition of a haircut would not solve anything because “as they say, two chicken don’t make an eagle.” (For further banking opinions on the restructuring topic see story page 16).

Questions on the government plan have come as well from less-directly affected stakeholders in the economy, a good example of which is a paper

Q&A WITH DANY BAZ

In order to better comprehend what data-related factors in banking might have contributed to the buildup of Lebanon's factual crisis of the century, EXECUTIVE sat down virtually with Dany Baz, general manager of Bankdata.

E Were banks in your opinion aware of the building of imbalances and the dimensions of the shortfalls now reported?

Banks were definitely aware of the many challenges ahead since their job is to buy risks while ensuring that they are well-monitored, priced, and covered. Nonetheless, the sustainability of the system, within the transition management toward the long-awaited improvement of the economic situation, would have entailed maintaining, at all times and by any means, a sufficient foreign liquidity cushion placed with correspondent banks abroad. In order to keep servicing customer requests, mainly in terms of transfers abroad and cash withdrawals, we estimate the cushion at 20 percent of the foreign currency deposit base. This would have prevented everything we are witnessing from happening. Exacerbation of internal political tensions and weakness in political speech and response heavily impacted confidence, which led to the blowing up of the rapidly deteriorating situation.

E Was there an effort to hide these problems from analysts such as Bankdata and from the general public?

Bankdata does not express any opinion on the financial situation of banks. We require audited financial statements that are undergone by the big four audit firms operating in Lebanon. That said, banks were transparent in their three exposures and figures are correct and available to all. If extraordinary events led to the sudden deterioration of the underlying quality of such exposures, the normal evolution was to reach the situation today.

E What do you think of the explanation that the high influx of funds into the banking system in 2007-2010 was the sole or main reason for the later buildup of financial and currency imbalances?

This is the classical debate between an oversized financial system and an undersized economy. The answer is yes if the abundant liquidity was misused by not channeling it into productive investments to grow the GDP or bridge the gap between actual and potential GDP. Our GDP should have been at \$120 billion if not for the numerous setbacks we have been through. Had the funds been channeled toward productive investments and job creations, then they would have been salutary.

E Did the various governments in power since 2007 have a fiduciary duty to examine and restrain BDL exposure and fulfill such a duty?

Monetary authorities in Lebanon are independent by law. The government's interaction/supervision is delimited by its representation in the Banque du Liban (BDL) Central Council and in the Higher Banking Commission, where all executive powers are embedded, through the memberships of the Director General of the Ministry of Finance, the Director General of the Ministry of Economy and Trade, and the judge approved by the Higher Judicial Council and appointed by government decree. Should each party fulfill its role, then the government should have been aware as it participated in major decisions via these three representatives.

E What can be said about the basic idea of banking sector restructuring and the organizational aspects of such a project from the viewpoint of the sector's role in employment of Lebanese?

Any bank restructuring is salutary as long as it translates into a higher



access to finance, mainly from SMEs, MSMEs, and the youth, as well as more efficient services at a lower cost.

E What is the size of the ancillary economic activities that feed into banking as menial, clerical, and professional services?

It is difficult to estimate ancillary economic activities, mostly in terms of outsourcing, at this stage.

E What do you expect the impact of a banking sector restructuring or eventually forced consolidation to be on the ancillary economy, the work prospects of a company like Bankdata and the capacity of Lebanon as financial analysis center in the region?

Lebanon's banking sector represented four times its GDP and therefore should have two to three mega entities ranking in the top 10 to 15 regional banks. At a decent horizon, this should attract more funds into Lebanon and create more jobs and opportunities in the sector and the economy. As for prospects, companies will certainly struggle to adjust and survive in the short term and I am confident that the renowned resilience and creativity of the Lebanese will allow us to rebound. As for Bankdata, our 38 years of collaboration with the banking sector through highs and lows is nurturing both our energy to overcome this phase and our hope to perpetuate the transparency and professionalism that has made our financial sector unique.

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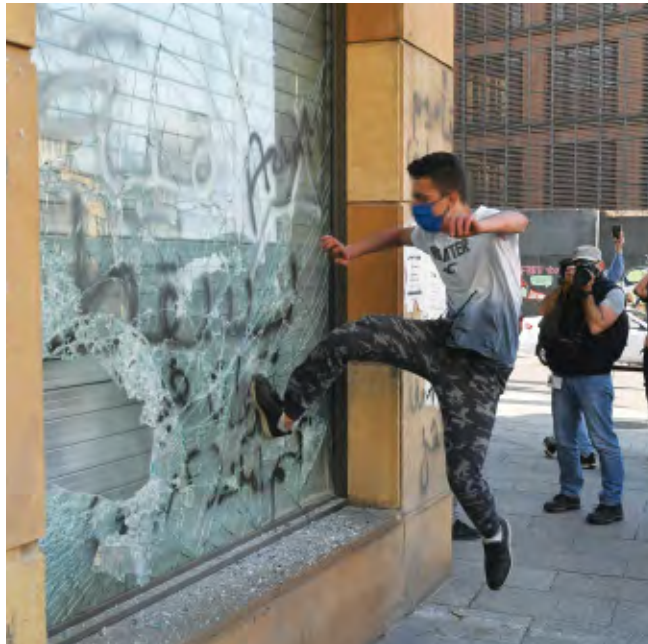
produced by academic researchers affiliated with the Issam Fares Institute for Public Policy and International Affairs at the American University of Beirut. “The plan raises several questions regarding its many assumptions and the calculation of its values,” writes Nasser Yassin, Professor of Policy and Director of IFI, in an introduction to short analyses produced individually by nine different experts.

Poring over aspects of the plan, these researchers voiced their concerns over the governmental concepts in the areas of the time frame of reforms, monetary policy, perspectives on spending reduction and increasing of state revenue, the proposed creation of a Public Asset Management Company, attempts to improve competitiveness, energy sector reform, the social component, and the necessity of the alignment with the International Monetary Fund (IMF). Among many other points, the academics noted the discrepancies between figures presented in the plan’s April 30 version with those used in a previous version, the nature of the plan as political statement, many promises for enhancement of competitiveness that are not accompanied by concepts of their financing, and the dichotomy between the plan’s list of desirable outcomes and its absence of plans for sequencing in form of a roadmap with metrics, a convincing timetable, and an assertion of accountability.

MANY REASONS TO DELIBERATE FAST AND CAREFULLY

This discussion is healthy and necessary even as it requires time and places the stakeholders in positions of having to elaborate on their visions and explain them—specifically the government with its agenda of presumably very serious reforms and the banking sector with its presumed interest in cleaning up and improving its practices as the primary concerned parties, but also all the academics, compassionate business leaders, and organizations. What is neither healthy nor helpful, however, but instead an objectionable waste of time, is any obsessing of primary stakeholders at the top of national decision chains with defensively-minded attributions of guilt to other primary stakeholders for their alleged past sins.

Despite all presumed educatedness and sophistication attained under the power of modern human development, dependence on data and tendency to blindly rely on it have been revealed during the coronavirus crises for their fatal potential to instigate and exaggerate herd behavior



of the 21st century economic person. Even in our time, data pretensions can cause fears and amplify them rapidly. Fake data, and quite transparently fake data at that, have been factors in the escalation of fears and unrest on Lebanese streets in the month of June.

■ A combination of incomplete data, its premature interpretation, instantaneous transmission, and human herd behavior makes for a lethal cocktail with the potential to kill any economy.

It is therefore not only that data and its exaggerated assessments under the impact of fearful biases have arguably stoked the fires of meta-physical economic uncertainty during the trajectory of the

Lebanese economic crisis over the past nine or ten months. In regarding the contribution of fake data and malicious rumors to the outbreak of violent fears in the distressed Lebanese population groups in the course of the country’s existential crisis, the conclusion could be the same as it also suggests itself globally from the 2020 coronavirus crisis: a combination of incomplete data, its premature interpretation, instantaneous transmission, and human herd behavior makes for a lethal cocktail with the potential to kill any economy. To avert this risk requires maturity of vision and clarity of confirmed data.





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DOUBLE JEOPARDY



Q&A with Riad Obegi, chairman of Banque BEMO, on banking sector challenges

First published online on May 28

At a time when banking is materially challenged by economic and financial stresses, and is faced with extreme criticism from distressed depositors and the explosion of economic commentators and activists of all colors in the country, EXECUTIVE wanted to know what local banking leaders have to say about the quagmire and the way forward. Riad Obegi, chairman and general manager of Banque BEMO, was ready to answer.

E Where is the banking sector situated in terms of the short-term crisis and of the long-term economic recovery, rescue, or revival of Lebanon?

Let me start with a more basic consideration of banking. Any economy is based on trust and banks are traders of trust. People prefer to put their money in a bank rather than lending it directly to persons who need the money. So you have people who have savings and people who need funds for investing in the future. To put those two together, you need someone of trust in the middle. When you have lack of trust, or lack of trusting this middleman, the whole system is compromised.

In Lebanon specifically, the situation in my opinion is not really a question of total bankruptcy. There is no bankruptcy, but there is a lack of trust. Unfortunately, the people whose role it is to [instill] trust, are in fact doing the opposite. Everybody is a little guilty—[including] banks of course. They made a mistake closing for two weeks [last October]; they made a mistake by not expressing themselves clearly; they made a mistake in not being very transparent in their policy, and they made a mistake not defending themselves when they were attacked.

E Only the banks?

Banks are a little bit guilty but the government is extremely guilty. I am not talking about the previous governments. This present government is saying we are bankrupt and cannot do anything without the International Monetary Fund (IMF). It says: 'The IMF is requesting that we do a haircut and we are going to do a haircut. We don't know how much but we are going to do it.' So they are creating uncertainty. Uncertainty does not generate trust. Adding to that is that they are saying there are too many banks in Lebanon. Forty is too much, 20 is better, they say. Why should it be bad for Lebanon to have the second [highest] ratio of deposits to GDP in the world? The first country in this regard is Luxembourg and I don't think it is bad for any country in the world to aim to be like Luxembourg. They have the highest GDP per capita in Europe.

When the government is saying that banks are bad or banks should close, I think it is destroying the trust and also destroying the possibilities of recovery. In the theory of [American economist Ben] Bernanke, the Great Depression of 1929 was so deep and so long because the authorities in the United States allowed banks to go bankrupt and disappear. This has crippled the credit channel. The information [stored] in the banks disappeared and the recovery took much longer. This is very well known but apparently not by our government and not by the advisors of this government.

E *What can be done as an alternative to having our finance and economy exposed to the state?*

I think the most important thing is to bring back trust. I don't know what the government is going to do but if he [Prime Minister Hassan Diab] does a haircut, I don't think trust will come back very soon. This [government narrative] is very absurd because he, and experts around him, say we do a haircut and decrease the debt of the government and then the IMF is going to give us money, and then people are going to trust us. I am a banker. If a client [takes a loan] and then finds ways not to pay me back, I am sure that I am not going to lend to him again. Not only am I not going to lend to him again, bankers usually have a long memory and they talk together. I do not expect this recovery plan, except for picking [funds] from one pocket to the other, to give good results.

E *If we are looking at the proposed recapitalization of banks, do you think banks will be interested in adopting the government's idea on recapitalization?*

The government is saying: 'Do recapitalization.' Suppose you have just been robbed by the Mafia and then the Mafia tells you: 'This is the last time. Come back, bring in your money again.' I don't know. I am not sure.

E *It seems that some of us do not care to reflect on how we as consumers have been benefiting from the elevated value of the lira in the past decade. Could we blame the banks for making us consume?*

There is something that is more serious in that the government should normally be an entity that creates coordination between people, not cause problems among people. This government is saying there is this category of people; these are bad people. Thus they are creating animosity between the people.

E *We could debate for hours if banks are just the intermediaries between savers and investors or if banks have a societal role to play beyond this function.*

They do of course. They are the depositories of trust.

E *What is the role of banks today in recovering and protecting assets of the Lebanese people, not just financial assets in the short term but also environmental assets, assets of civil peace among diverse population groups, or assets of Lebanese identity?*

I think the Lebanese banks don't have much of a say in these things now. They cannot do much.

E *But they could?*

Yes. Again, let us go back to the assumptions of the government of Lebanon. These assumptions are that the state of Lebanon is bankrupt, that Lebanon is bankrupt, that the Lebanese lira is overvalued, and that the banks are bankrupt. Everything is bankrupt, and whatever we do, it doesn't matter. We cannot do anything. For us, this is wrong because the state of Lebanon is not bankrupt. It has assets. [We should tell the world:] 'The state of Lebanon has liquidity problems but it has the assets and can pay—however, not now. We are not the type who does not pay our obligations.' If we can make this point, everything goes up.

E *Even the lira?*

Even the lira. Another assumption [of this government] is that Lebanon is consuming much more than it is producing. This assumption is based on wrong figures that do not make sense. We are importing \$20 billion dollars in goods and ex-

porting \$3 billion in goods. But the services are not counted in this equation. If, for 50 years, we had been consuming more than we were producing, we would not be here. You can see from the figures in the banks that savings are in-

■ "The government is saying: 'Do recapitalization.' Suppose you have just been robbed by the Mafia and then the Mafia tells you: 'This is the last time. Come back, bring your money again.'"

creasing year after year since we are producing more than we are consuming. In the last few years, because of the financial engineering, we perhaps received some money that was opportunistic but over 50 years or 70 years? This does not make sense. It is impossible.

Based on these wrong assumptions [the government] concluded with our foreign friends that the Lebanese lira should be devalued. I think this is a political decision in order to take back from the public servants what was given to them perhaps somewhat too generously. But there is no reason [for a devaluation because it would help us to export more], because we are mainly exporting services and services are not very elastic in terms of price changes. If you are a lawyer you are not going to get more business if you are going to say my hour is no longer costing \$200 but only \$100 from now. People would ask: 'What type of lawyer are you when you are pricing yourself at \$100?'

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E *In that sense it is almost a Veblen good (based on the theories of American economist and socialist Thorstein Veblen) where the demand and price are positively correlated.*

Exactly. So I think that it is a wrong decision; wrong assumptions and wrong decisions. What can banks still do? I will tell you what we as bank [BEMO] are doing. I cannot talk for all other banks. We decided that we will lend again to our clients because our job is to take deposits and lend money.

E *You resumed lending actively as of when?*

We resumed lending as of April.

E *How much demand did you encounter?*

There is not a lot of demand, frankly, because people feel uncertain. But there are still people who are saying: 'They are lending to me at a lower price than the bank from whom I am borrowing now, so let me go to them.' All of this is progressing little by little as we decided to lend.

E *How much of a percentage contribution to GDP do you see banks make by 2025?*

The progression of loans follows the progression of GDP everywhere in the world. You might have temporary distortions, but on the long term, you see a very strong link between progression of GDP and progression of loans and as everything is going to reduce bank loans [in Lebanon], you have to expect a reduction of GDP. What can banks do? I think that banks, as much as possible, should resume lending. This is what we have done.

E *Are there other things banks can do beyond their core financial business?*

Banks can also help their clients to become more productive. How can they do this? I think that one of the weaknesses in Lebanon is that people do not like to work together. So we have to push them to work together, to make partnerships. Not necessarily to become public [as listed companies] but at least to partner together. I think the current situation pushes people to work together and also to try and look outside of Lebanon, because Lebanon is not [a territory of] 10,000 square kilometers; it is much more. You have Lebanese everywhere and Lebanese companies everywhere. They are using Lebanon as a base. The government does not like that, but that does not matter. [People] will continue working

until this government goes away and somebody else comes and understands what Lebanon truly is. As banks, we need to help our clients to become more efficient, not necessarily to hire more people.

We need to help [with regard to] the basis of the wealth of Lebanon, which is education. Today, universities and schools have very big problems in collecting tuitions. So we are going to develop financial products where tuitions are going to be financed partly by our bank and paid back over a long period of time. This [type of education finance] does not really exist now but we are going to do that. We are also going to—and are announcing this week—support mediation. This is because we have to expect a lot of bankruptcies very soon, which means that the judiciary system, which is already not very efficient, is going to be overburdened. What we as bank would do is encourage mediation, which might solve 20 to 30 percent of the problems [which otherwise would end in court]. It won't solve all of them; mediation is not the judiciary.

E *Would that be mediation in the sense of an arbiter or perhaps offer mediation to people who seek extensions of loan maturities?*

A mediator is not a judge and not an arbitrator. He just puts people together and helps them to close the distance between their positions. A mediator gets active when there is a conflict,

■ “We have to expect a lot of bankruptcies very soon, which means the judiciary system, which is already not very efficient, is going to be overburdened.”

for example you call a mediator when there is a conflict between you and your banker who is saying I will not finance this need *etcetera*. So you call a mediator and the bank should accept

this mediator who asks both sides what they can offer and tries to facilitate the dialog between the conflict parties. A mediator has a moral authority; however, he has zero power to force anything on you or the second party. There are universities that teach mediation. We are partnering with the Professional Mediation Center at Saint Joseph University (USJ) in Beirut. We are a bank but we can support mediation and push our clients perhaps to have a mediation clause in their contracts. ■