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Overview of the Recent Monetary, Banking, and Financial Developments in Lebanon

2007

Following the July 2006 war, the Lebanese economy started to recover in 2007, despite persistent political and security challenges. Real GDP growth reached 3% and inflation did not exceed 4%. Interest rates remained stable and the BOP posted a surplus of USD 2 billion, despite the unprecedented oil price increase and appreciation of the Euro against the US dollar.

The BDL commitment to the stability of the pound's exchange rate against the dollar continued to play a pivotal role in maintaining financial stability. At end-2007, BDL foreign assets exceeded USD 12 billion, and gold reserves were over USD 9 billion, due to rising gold prices.

The well-capitalized and profitable Lebanese banking sector continued to show a remarkable resilience, an inherent feature stemming actually from a dedicated investors' base, a pool of highly skillful bankers, and an integrated set of sound and strict banking regulations. In this respect, it is noteworthy that the US subprime crisis had no impact on Lebanon, since the BDL had, five years ago, prohibited banks from purchasing structured products.

At end-2007, total banking assets reached USD 97 billion, including deposits in commercial and investment banks, a total equity exceeding USD 6 billion, and USD 12 billion of deposits in Lebanese banks operating abroad. Customer deposits, which grew by 10.5% in 2007 and attained about 300% of GDP, are the main driving force behind banking activities in Lebanon. Besides, annual remittances from the large and wealthy Lebanese diaspora, which exceeded USD 5 billion, represent a strong and continuous capital inflow that spurs the economy.

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In January 2008, Lebanese banks started to implement the Basel II principles, as required by the BDL. Having successfully met the tightened capital adequacy standard (Pillar 1), they were given an additional five years to reinforce risk management and adopt Pillars 2 and 3. In parallel, many Lebanese banks are pursuing a strategy of regional expansion and engaging in new cross-border activities, while focusing on private and retail lending. This process is being supported by the BDL and the Banking Control Commission through regulatory and supervisory reforms. Thus, Lebanese banks operating abroad are expected to increase their activities and realize, within 3 years, more than half their profits from such activities. This would lead to upgrading theirown ratings, independently from the country's sovereign rating.

Facing the domestic political stalemate and the recent turbulence in global finance, Lebanese capital markets remained resilient, with a wait-and-see attitude prevailing in both equity and Eurobond markets. Nonetheless, the cut in interest rates abroad will boost demand for Lebanese debt instruments, because domestic risks prevent a possible reduction in local interest rates.

Finally, the Government remains committed to its comprehensive five-year reform program, submitted to the Paris-III donor conference for reducing the country's large public debt. Though Lebanon had met all end-2007 indicative targets under the IMF Emergency Post-Conflict Assistance program, further progress in implementing reforms, aligned with timely disbursement of donor funds, hinges on an improved political and security situation.