مصرف لبنان
BANQUE DU LIBAN

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

2021

Unstable political circumstances in the country, along with security challenges and regional unrest have impaired the Lebanese economy for more than a decade now. The outbreak of nationwide anti-government protests in October 2019 has further exacerbated the economic environment, cutting deeper into Lebanon's pre-existing economic imbalances, and leading to political paralysis. Economic imbalances have intensified deeply in 2020-2021 and vulnerabilities have continued growing, thus giving rise to severe financial challenges.

In summary, Lebanon has been living multiple shocks in the past two years, starting with the liquidity crisis that erupted in the last quarter of 2019, followed by the government's decision to discontinue payments on all its outstanding US dollar-denominated Eurobonds in March 2020-first sovereign default in Lebanon's history, the COVID-19 pandemic imposing lockdowns in the country starting the second quarter of 2020, and the Beirut port explosion in August 2020 which caused major destruction in the Lebanese capital and left the country without a government for more than a year.

The Lebanese economy has indeed plunged into a severe contraction across all economic sectors, combined with an unprecedented surge in prices. According to BDL forecast, Real GDP is believed to have contracted by 11% in 2021, after registering a real contraction of 22% in 2020. The average inflation rate for 2021 has been forecasted at 154.76% against an average rate of 84.86% in 2020.

At the monetary level, Lebanon continues to suffer from contracting capital inflows, a massive shortage of US dollars and a sharp depreciation in the value of the local currency against the

US dollar in the parallel market, hitting as high as LBP/USD 27,000 in December 2021. Currency in circulation outside BDL increased by 48 % during 2021 reaching LL 45,731 billion at end-December 2021. BDL's exceptional measures initiated at end of year were able to lower money expansion and to curb currency swings in the parallel market. The LL/USD rate stabilized at around LBP/USD 21,000 in the first two months of 2022, converging closer to BDL "Sayrafa" rate, after hitting LL/USD 33,000 early January.

The Central Bank is still maintaining the official rate of LBP 1507.5 in bank transactions and for some critical imports such as medicine and wheat, while allowing bank withdrawals at an increased rate of LBP 8,000 to the dollar. As a result, BDL's assets in foreign currencies continued their downward trend in 2021, reaching USD17.8 billion at end of year as compared to USD 24.1 billion at end of 2020.

As for the banking sector, total banking activity registered a decline of 7% with the consolidated assets of banks recording USD 175 billion at end December 2021, down from USD 188 billion at end December 2020. Contractions were registered in both banks' deposits and loans, though at a slower pace as compared to the previous year.

Total customers deposits declined by 7% in 2021, with the deposit dollarization ratio witnessing a slight decline from 80.4% at end December 2020 to 79.4% at end December 2021. Bank loans to the private sector dropped by 23% to reach USD 29.3 billion at end December 2021, with the loan dollarization ratio dropping to 56.3%. In terms of capitalization, capital accounts figures witnessed a wider contraction over the past year, with total banks shareholders equity dropping by 11% to reach USD 17.7 billion at end December 2021.

In the midst of these challenging circumstances, BDL is still deploying all measures to ease the burdens of the consecutive shocks on businesses and individuals, as well as strengthening the conditions of banks in terms of securing liquidity and capital requirements.

In the past year, BDL has issued a series of circulars from which we can highlight the following:

Due to the exceptional circumstances in the country and in an effort to organize foreign exchange operations, BDL established an electronic exchange platform "Sayrafa" that includes BDL, banks and licensed money dealers. Based on this platform, banks were allowed to conduct foreign exchange operations including the buying and selling of foreign currencies in exchange for other foreign currencies or Lebanese pounds. This new tool provides a transparent setting for the exchange rate and for the participants in the platform. Market dynamics will help determine the exchange rate and BDL may intervene when necessary, based on the existing laws and regulations, in order to control sharp fluctuations in the exchange rate.

The "Sayrafa" platform is part of BDL's initiative that aims to ease the pressure on citizens amid the prevailing crisis that has been exacerbated by the absence of a functioning government that would implement the necessary reforms, reestablish Lebanon's regional and international relations, and restore domestic confidence.

BDL also took a series of exceptional measures related to cash withdrawals at banks, in its ongoing efforts to preserve depositors' rights and help them access their funds in foreign currencies. As per basic circular 158 issued in August 2021, BDL allowed the gradual disbursement of deposit funds up to USD 50,000, over a period of 5 years, from bank accounts opened prior to October 31, 2019.

Moreover, based on a circular issued in December 2021, BDL increased the rate of withdrawals from foreign currency accounts to LBP 8,000 per one US dollar, up from LBP 3,900, within the ceiling of USD 3,000 per account per month.

In the same context, and in an effort to absorb liquidity in Lebanese pounds, BDL issued basic circular 161 in December 2021. As per this circular, BDL provides banks with cash US dollars at the "Sayrafa" rate. As a result, banks must pay their customers Banknotes in US dollars at the "Sayrafa" rate instead of paying the amounts belonging to them in Lebanese pounds.

Despite all BDL efforts to reestablish financial stability, there are other factors that play an important role: the need for political stability and for the government to undertake a number of structural reforms and set a viable economic plan in coordination with international institutions.

The situation in Lebanon is becoming very difficult, and it could worsen in the absence of a comprehensive and credible medium-term reform program, supported by the IMF and international community, to restore confidence and put the economy on a recovery path.

Fiscal adjustment and structural reforms are necessary to alleviate the burden on BDL policies to maintain macroeconomic stability and promote sustainable growth.