



**Bank earnings from financial engineering:
numbers on books in Lebanese pounds**

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After banks' earnings from financial engineering became a tool to express a point of view for some analysts, and after some others found it easy to throw out numbers without verifying their accuracy, it is important to clarify the following details:

- Alvarez report determined banks' earnings from financial engineering at 7,300 billion L.L. (Alvarez report, p. 156).
- These earnings have not been converted into dollars and are still in Lebanese pounds till date, with no impact on the reserves of the Central Bank of Lebanon.
- Banks paid 1,275 billion L.L. from these earnings as taxes for the year 2016 according to the statement of the Association of Banks dated 3/3/2017, exceeding the projected amount of tax collection from the financial engineering in the 2017 draft budget, which estimated the tax revenue at 1,000 billion L.L.
- Alongside the launch of financial engineering, the Central Bank had requested banks to increase their equity in Lebanese pounds after raising the Capital Adequacy Ratio (CAR).
- The Central Bank of Lebanon prohibited banks from distributing any profits resulting from financial engineering through its circulars, particularly intermediate circulars 440 and 446 dated 8/11/2016 and 30/12/2016 respectively.
- In accordance with the circulars of the Central Bank of Lebanon, banks added net profits to their capital accounts in Lebanese pounds and formed provisions in Lebanese pounds. Consequently, no profits were distributed to shareholders, neither in Lebanese pounds nor in dollars.
- If banks had violated any of the circulars issued by the Central Bank of Lebanon, the Banking Control Commission would have intervened to prevent them from doing so.
- Since the increase in capital and the formed provisions remained in Lebanese pounds, it has lost 98% of its value in dollars so far.
- Financial engineering was based on the principle of the Central Bank of Lebanon raising interest rates on the dollar to attract dollars available in the market for the sole purpose of financing the State and maintaining an artificial exchange rate for the Lebanese pound against the dollar, as stated in the introduction of the financial sector rehabilitation strategy previously proposed by the government:

"The massive losses incurred by the Central Bank of Lebanon are the result of its financial operations aimed at attracting capital inflows to maintain the fixed exchange rate, which is overvalued, and to finance the budget deficit."

- It is acknowledged that banks only retain the difference between the interest received on their deposits at the Central Bank of Lebanon and the interest paid to depositors. Thus, the majority of the returns from financial engineering has gone to those who benefited from the high interest rates and not to the banks themselves.

Note: This article is part of a series written by the Secretary General of the Association of Banks in Lebanon as part of his introductory articles to a number of periodicals issued by ABL. It represents his own opinion and personal analysis of the developments, without committing ABL to its content, which remains the sole responsibility of the Secretary General.