Bridging Turmoil and Transformation: A Comprehensive Review of the Lebanese Banking Sector from 2000 to 2018

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Abstracts: This article provides a thorough analysis of the Lebanese banking industry from 2000 to 2018. It looks at the major innovations, difficulties, and changes that have shaped the sector and shed light on the technological, economic, and regulatory factors that affect how well it performs. This study offers insights into opportunities and challenges faced by Lebanese banks within the domestic and regional financial landscape by analyzing trends, policies, and reforms. Between 2001 and 2019, data from published Bilanbanques were gathered, and this information is now being used to build theoretical foundations, empirical models, and a practical understanding of banking systems in emerging economies. The article's importance stems from its coverage of a crucial time in Lebanon marked by political transitions, economic downturns, and regional instability. It highlights how banks navigated difficult times and underwent transformative changes by thoroughly examining the banking industry within this context. Lebanese banks remained liquid, managed risks, and embraced modernization despite the recessionary conditions, positioning themselves for further expansion. Their perseverance during political unrest and economic downturns highlighted depositors' and investors' confidence, which was supported by adherence to international best practices. The Lebanese banking industry played a crucial role as a financial intermediary, catalyst, and partner throughout the years under consideration, promoting the expansion and stability of the economy. It was able to investigate domestic and international expansion opportunities thanks to its strong financial position, dedication to ethical business practices, and commitment to risk management. The sector's performance demonstrates how important it is to Lebanon's economy, serving as a rock of confidence and support for customers and investors in the face of local and regional unrest.

Keywords: Lebanese Banking Sector, Comprehensive Review; 2000 – 2018, Economic Challenges, Political Instability, Regional Instability, Transformative Changes, Resilience; Adaptive Strategies.

1. INTRODUCTION

Only a few studies reported the performance of the Lebanese banking sector for a trend of years. For instance, Peters et al. (2004) analyzed the balance sheet characteristics and performance of Lebanese banks for the years 1993 to 2000 (post-war). Their research showed that while Lebanese banks are successful, they are not as profitable as a control group of banks from five other Middle Eastern nations. Moreover, Khatib (2020) conducted a study that spanned the years 1990 to 2004 and looked at the 15 years following the end of the Lebanese civil war. However, no previous paper, article, or publication reviewed highlights the performance of Lebanese banks for a span of 18 years. Thus, this literature review shall redeem this gap.

This paper provides a comprehensive overview of the Lebanese banking sector, spanning the years 2000 to 2018. It aims to examine the key developments, challenges, and transformations that have shaped the industry over the years, offering insights into the economic, regulatory, and technological factors that have influenced the sector's performance. By analyzing the trends, policies, and reforms implemented during this timeframe, this overview sheds light on the opportunities and challenges faced by Lebanese banks, as well as their position within the domestic and regional financial landscape. The data presented in this paper was collected from the series of published Bilanbanques between the years 2001 till 2019. This paper holds significant added value in academic research and literature. It fills a gap in the existing knowledge by providing comprehensive insights into the sector's evolution, contributing to theoretical frameworks, empirical models, and practical understanding of banking systems within emerging economies.

In addition, the timeframe of the study is crucial as it covers significant events and developments in Lebanon, including political changes, economic crises, and regional instability. By examining the banking sector within this context, the study sheds light on how the sector has navigated through turbulent times and undergone transformative changes. Lebanon has faced numerous challenges, including political instability, social unrest, and economic crises during the period under review. The study's focus on the banking sector allows for an in-depth understanding of how banks have functioned in such a crisis-prone environment. It explores the sector's resilience, adaptive strategies, risk management practices, and policy responses to external shocks, providing insights into the dynamics of a banking system operating within a volatile economy.

1.1. Resilience and Reform: Unveiling Lebanon's Banking Sector in 2000

The Lebanese banking sector was impacted by the continuing sluggishness of aggregate demand in 2000. The stagnation in consumption and investment weighed on banking activity, which reported lower growth and shrinking margins. The Lebanese government, appointed in late 2000, has formulated a macroeconomic adjustment program based on sustaining monetary and financial stability, attaining sustainable growth rates, and ongoing reforms that tackle fiscal imbalances. Such policies, which translated into a slightly positive real GDP growth over the first half of 2001, needed to be supported by a net improvement in the political environment, both on the domestic and regional fronts.

Within this context, banks' efforts were targeted toward ensuring all essential criteria for an optimum financial standing, even at the expense of sacrificing further profitability. The analysis of the major risks related to the Lebanese banking sector revealed, first of all, a persistently well-contained liquidity risk, thus mitigating concerns about a confidence crisis. Banks' net liquid assets accounted for 72.9% of deposits in 2000, against 44.2% and 36.7% for Middle Eastern and World averages. The ratio of loans to deposits recorded a low of 37.4% within the context of conservative bank lending policies. As to foreign exchange risk, it remained well contained within the strict regulatory framework imposed by banking authorities, with consolidated net foreign exchange position which represented only 23% of shareholders' equity at year-end 2000. Efficiency was on a relative decline this year. Faced with an increasingly competitive environment where the extra costs of investing in technology, human resources, and broader product lines were coupled with temporarily depressed profitability, the sector's cost-income ratio edged up by 5.4%, moving from 62.4% in 1999 to 67.7% in 2000. The analysis of the quality of loans showed that non-performing loans and doubtful loans represented 18.4% of total loans (15.5% in 1999), rising as a result of the recessionary conditions, yet matched with a surge in the risk coverage ratio. Provisioning constituted 59% of non-performing loans and doubtful loans at year-end 2000, up by 4% with respect to 1999.

Over the past year, a number of laws and regulations were ratified to further strengthen the Lebanese banking sector and improve its risk profile. First, the Central Bank has pursued a policy to reinforce the adequacy of banks' capitalization, requiring banks to raise their capital adequacy ratios to 10% by year-end 2000 and 12% by year-end 2001, with most banks satisfying this minimum requirement and with an average ratio for the sector standing close to 19% in December 2000. In the same token, the Lebanese Parliament ratified on March 20, 2001, a law concerning bank ownership, unifying all categories of banks' shares and facilitating banks' efforts to increase capital in addition to allowing the issuance of preferred stock and stock options.

At the regulatory level as well, a law on fighting money laundering was ratified by Parliament on April 10, 2001. The new law, which is compliant with the 40 recommendations of the Financial Action Task Force (FATF), established a Special Investigation Committee with extended prerogatives and with a task to investigate money-laundering operations and to monitor compliance with the rules and procedures stipulated in the Law. Moreover, Lebanon passed a law repealing legislation that allowed offshore banking activities, intending to discharge reasons that allow anyone to doubt any improper transactions that were taking place in Lebanon. Other new laws aiming at improving the soundness of the banking system were the law regulating the Profession of Financial Intermediation and the Law on Decision and Internal Audit.

The reinforcement of the regulatory framework was coupled with various initiatives to upgrade the banks’ activity infrastructures at the levels of IT and electronic banking platforms, the diversification of their service and product lines, and the corollary development of their human capital. All these moves impacted relatively the banks’ cost bases while giving them significant competitive edges, thus strengthening their franchises. Lebanese banks which operated at much below their supply capacity, were undeniably well-positioned to take advantage of a dear-cut trend reversal in domestic aggregate demand. They were well positioned as well benefiting from a large cross-border expansion potential, bridging the existing gaps in neighboring markets that are increasingly embarking on serious financial and banking reforms.

1.2. Resilient and Prudent: Unveiling Lebanon's Banking Sector in 2001 for Soundness, Profitability, and Economic Growth

In 2001, banks in Lebanon continued to carry out their activities and operations prudently and efficiently according to sound banking practices guided by the set of prudential rules and regulations that comply with international best practices and standards. Most importantly banks adhered to international standards of capital adequacy, loan classification and provisioning, accounting, and internal audit. In 2001, the soundness of the banking system was maintained as measured by the capital-to-risk weighted assets ratio which stood at 19.2 percent. In that year also banks were able to better manage their assets. The efficient use of assets was gauged by the ratio of the net return on average assets which increased from 0.71 percent in 2000 to 0.74 percent in 2001.

As the economy continued to relatively slow in 2001, asset growth at banks decelerated (but profitability increased, pushed by lower net allocation to provisions for doubtful debt and on financial fixed assets in addition to reduced general operating expenses and income tax). In 2001, total assets of banks increased by 6.5 percent (11.3 percent in 2000) and that was associated with an increase in claims on both the private and public sectors by 0.5 percent and an increase in total deposits by 6.2 percent. In this environment, it was obvious that doubtful and substandard loans slightly increased in relation to gross loans from 18.6 percent in 2000 to 19.4 percent in 2001 and the loan loss provisions to gross loans slightly rose from 12.15 percent to 12.17 percent but the loan loss provisions on doubtful loans to doubtful loans decreased from 74.5 percent in 2000 to 71.4 percent in 2001. It was evident also for banks to hold more liquid assets on their balance sheet with loans in FC to deposits in FC decreasing from 50.3 percent in 2000 to 43.5 percent in 2001. These developments contributed to a lower interest margin of 225 percent in 2001 compared to 2.54 percent in the previous year but this was offset by improved cost efficiency as the ratio of cost to income decreased from 67.4 in 2000 to 65.3 percent in 2001. The result was improved profitability with an increase in net return on average equity from 10.44 percent in 2000 to 11.03 percent in 2001.

With the ongoing restructuring and modernization banks in Lebanon looked into promoting financial and economic development. Success in achieving these targets required at all times sound banking practices, more disclosure of information, the efficient coordination of efforts between banks through the Association of Banks in Lebanon, and professional cooperation with bank regulatory and supervisory authorities.

1.3. Lebanese Banking Sector: Thriving in 2002 - Resilience, Modernization, and Dynamic Partnerships

During 2022, the banking sector in Lebanon continued to effectively meet the financing needs of the nation's economy and offer the best services to its clients domestically and worldwide. These clients were becoming more demanding in terms of high-quality - low-cost banking and financial services. The Lebanese banking industry, which was exposed to worldwide competition due to the trend toward globalization and the historical openness of local markets, continued to adapt by undergoing constant institutional and organizational change. Lebanese banks were actively involved in modernizing their financial services and operations and incorporating cutting-edge technology and information systems into their daily operations. Although this investment increased operational expenses relative to their income, banks, were well-positioned to conduct business both domestically and regionally.

The Central Bank of Lebanon, the Banking Control Commission, and the Association of Banks in Lebanon worked closely together to implement appropriate and strict bank regulation and supervision in 2002, which helped the Lebanese banking sector perform reasonably well in accordance with best business practices. The ratio of total assets to GDP reached almost 300% in 2002, as banks total assets continued to grow faster than the GDP. According to Bilanbanques, the average return on assets and equity was 0.6% and 8.4%, respectively. Liquidity was close to 30% in terms of loans to deposits, while BIS-based solvency ratios topped 20%. Except for the strong liquidity in Lebanese banks (due to market conditions), these levels were consistent with those reported by the top 100 foreign banks. The sector's capital adequacy ratio was significantly higher than the minimal 8% needed by the Bank for International Settlements (BIS) Basel Committee and the 12% required by Lebanon's monetary authority. As a result, banks' capital positions were enough to handle credit and market risks.

The Lebanese banking sector was providing during this year to all investors all the functions needed for an efficient, dynamic, and modern banking sector, playing the roles of financier, catalyst, consultant, and partner:

- Financier as it is the principal source of financing the Lebanese economy due to many reasons, among which, is its capacity of accessing the international financial markets;

- Catalyst due to its credibility and active participation in the financing operations of the economy encourage domestic and foreign investors to get involved and invest in the economy in turn;

- Consultant due to its capacity to provide domestic and foreign investors with a reliable and accurate assessment of Investment Opportunities in Lebanon and beneficial information on the financial capacity and soundness of potential local business partners;

- Partner as the capital of Lebanese banks is open to outside investment, either directly or through the purchase of bank shares listed on domestic and foreign markets.

1.4. Thriving Resilience: Lebanon's Banking Sector Soars in 2003

In 2003, banks in Lebanon had a better operating environment as the overall economic activity in the country fared better in relation to the previous year and the outlook for the Lebanese economy improved considerably after the success of the Paris II conference of foreign donors in November 2002. Participants agreed to pledge a total of USD 4.3 billion in financial support most of which had been disbursed to help restructure the public debt and address fiscal Imbalances. Pledges had been accompanied by additional support from banks in Lebanon which agreed to receive a zero percent interest on USD 3.6 billion claims on the public sector either in the form of cash placed at the central bank or government securities. The central bank provided also financial support by writing off some government debt according to Article 115 of the Code of Money and Credit and accepted a lower yield on government securities it held and subscribed to. This package of measures created a positive economic climate and increased confidence in the Lebanese economy. The short-term outcome was a marked fall in interest rates and the strengthening of the Lebanese currency with the considerable conversion of the denomination of deposits at banks into the Lebanese Pound. Regional developments and the low international interest rate environment contributed also to the strengthening of the Lebanese economy.

Against this background, the Lebanese banking sector performed relatively well in 2003 and much better than the preceding year while carrying out activities and operations in a very prudent, sound, and efficient manner guided by the comprehensive set of rules and regulations that move hand in hand and comply with international best practices and standards. Balance sheet and income statement figures in Bilanbanques showed that the total assets of all banks and the net profit after taxes increased by 13.3 percent and 50.8 percent in 2003 respectively. Net return on average equity and net return on average assets jumped from 8.28 percent and 0.55 percent in 2002 to 11.17 percent and 0.75 percent in 2003. In 2003 also, the cost-to-income ratio decreased substantially to 64.66 percent from 71.28 percent in 2002, liquidity measured by net liquid assets to deposits reached 82.52 percent against 78.01 percent one year back, and the capital adequacy measured by the central bank BIS risk asset ratio stood at 23.10 percent against 20.08 percent a year earlier. Net doubtful loans to equity decreased from 22.96 percent in 2002 to 20.52 percent in 2003.

The process of restructuring and modernization continued and banks kept on financing the needs of the domestic economy in its private and public sectors by providing the best possible high-quality services to local and abroad customers. Obviously, much work was needed to be done to sustain the progress and prosperity of the

Lebanese banking sector seen year after year and which was much due to the good corporate governance and the efficient coordination of views and efforts between banks through their association and the professional cooperation with bank regulatory and supervisory authorities.

1.5. Thriving Through Transformation: Lebanon's Banking Sector Triumphs in 2004

The macroeconomic environment under which banks operated improved significantly in the year 2004 and the Lebanese economy strengthened with real output growth estimated between 4 and 5 percent against an estimated 3 percent in 2003. The acceleration in the economic activity contributed to fiscal and economic measures taken earlier to larger tax collection and government revenues but primary expenditures increased rapidly as well and higher than budgeted. Fortunately, the increase in expenditures was offset by a sharp decrease in debt service; largely attributed to the financial contributions of the different parties and mainly banks following the success of the Paris II conference, which led to a significant drop in the overall deficit as a percent of total public expenditures. Interest rates on LBP-denominated deposits and loans decreased by almost 80 bps and 84 bps respectively and a more moderate decrease in the interest rates on USD-denominated deposits compared to a much larger drop in rates on USD-denominated loans took place These resulted in a narrower spread between lending and deposit interest rates in USD. In the same year also most of the government debt coming to maturity was rolled over at longer maturities and lower interest rates.

The Lebanese banking sector rapidly and successfully adapted to these recent market orientations and trends and carried its activities and operations as in the preceding years in a very prudent and professional manner guided by the comprehensive and up-to-date set of rules and regulations that adhere to international best practices and standards. The structure of bank assets and the underlying returns in addition to the cost of funds reflected the above-mentioned developments and the relatively large exposure of banks to the central government and the central bank.

The consolidated balance sheet and income statements in Bilanbanques showed that the asset quality improved in 2004 and the liquidity and capital adequacy remained high, net doubtful loans to equity sharply decreased from 25.02 percent in 2003 to 18.73 percent in 2004. The liquidity position as measured by net liquid assets to deposits increased to 83.81 percent against 82.52 percent one year back. The capital adequacy measured by the central bank BIS risk asset ratio decreased to 21.03 percent against 23.00 percent a year earlier. Financial statements indicated also that the banking industry as a whole was slightly less profitable and cost-efficient. The total assets and net profit after taxes of all reporting banks increased by 14.5 percent and 4.7 percent respectively in 2004 but the net return on average equity decreased from 11.14 percent to 10.42. The net return on average assets dropped from 0.75 percent to 0.69 percent in 2004 and the cost-to-income ratio slightly increased to 64.96 percent against 64.52 percent in 2003.

1.6. Resilient and Resurgent: Lebanon's Banking Sector Defies Challenges in 2005

Unlike in 2004, economic growth decelerated considerably in 2005 and the macroeconomic environment deteriorated drastically, particularly in the two to three months that followed the tragic assassination of PM Hariri. A temporary financial turbulence ensued and market confidence was affected and further undermined by the political assassinations and series of explosions that followed along with political tensions. The financial shock was rapidly absorbed and financial pressures were alleviated by the availability of high international reserves and a series of coordinated efforts and actions between the Central Bank and banks of which swap operations and the issuance of dollar CDs were welcomed by market participants. Market stabilization and confidence were gradually restored and the deposit base resumed its growth after it had shrunk earlier, particularly following the withdrawal of Syrian troops from Lebanon, the June parliamentary elections, the rise in interest rates on the Lebanese pound, and the talk about a promising financial and non-financial support of the international community for a new economic reform and adjustment program which adoption was repeatedly delayed.

The above-mentioned developments influenced asset expansion and structure and also the liquidity, solvency, and profitability of banks. The consolidated balance sheet of banks regressed during the period extending from mid-

February to mid-May and the same applies to credits granted to both public and private sectors. But after this period, assets resumed growth to compensate for the setback. In 2005, therefore total assets increased by around 6.8 percent, and claims on government and central bank accounted for around 54% of the total at year-end. In the mentioned year banks were highly liquid and solvent. Net liquid assets to deposits were 85.19 percent compared to 84.23 percent a year earlier and the capital adequacy measured by the central bank BIS risk asset ratio increased to 23.41 percent against 21.35 percent, reflecting a larger holding of low-risk weight assets from one side and high capital accumulation from another side. In fact, capital accounts increased by 10.4% in 2005, with banks taking advantage of abundant excess liquidity in the Gulf region to raise more capital. This enhanced confidence in banks, supported regional expansion, increased incentives for prudent risk management, and prepared banks for implementing Basel II standards in 2008. With profitability increasing at a faster rate than assets and equity; i.e., by 25 percent in 2005, largely supported by cash premium to rollover maturing treasury bills and bonds, the net return on average equity and assets increased from 10.22 percent in 2004 to 10.70 percent in 2005 and from 0.68 percent to 0.77 percent respectively. These measures were considered low by international standards though they could be much higher for a few large banks. In 2005 also, the cost-to-income ratio fell to 61.93 percent compared to 65.25 percent in the previous year, and the asset quality improved with the ratio of doubtful and substandard loans to gross loans decreasing to 24.05 percent from 26.11 percent.

The Lebanese banking sector proved, once again, and in close coordination with the monetary and supervisory authorities, its soundness, resistance, and ability to adapt to market changes, reconcile between risks and profitability guided by the set of practices, rules, and regulations that adhered to international best practices and standards. The unfavorable events in 2005 also showed the level of confidence granted by Lebanese depositors and investors to this sector on the basis of its capability to successfully adapt to changes.

1.7. From Promise to Peril: Lebanon's Economic Rollercoaster Ride in 2006

Strong economic recovery and positive prospects typified the first half of 2006 with the Lebanese economy benefiting from high oil prices and abundant liquidity in the region, translated into large capital inflows, foreign direct investment, and transfers along with important tourism and exports activities that strengthened altogether the domestic financial and fiscal situations. Regrettably, July hostilities, the two months-long blockades, and the political tension that followed dashed hopes for strong economic growth in 2006 and put an end to this recovery. Economic and social damage was huge and undermined strong first-half performance to the extent that economic and fiscal indicators deteriorated for the year as a whole and the real GDP was flat compared with a pre-war projected growth of around 6 percent. Inflation also accelerated due to supply shortages. Stockholm donor conference and other local and international financial and reconstruction assistance generated significant support for the Lebanese people.

Financial markets had to face, therefore, another difficult year and were able to weather the situation very well. Financial stability was maintained and confidence was rapidly regained thanks to the skillful management and foresight at the central bank and banks alike. the banking system's strong liquidity position, and the timely foreign financial assistance in the form of deposits of around USD 1.5 billion from Saudi Arabia and Kuwait with the central bank. Official foreign exchange reserves were protected throughout the conflict period and deposits outflows not exceeding 5 percent of the deposit base were recouped by year-end, evidencing the large confidence of Lebanese depositors and investors in their resilient financial sector.

Under this challenging operating environment banks performed very well in 2006 and not at the expense of their risk exposure nor the international best practices and standards to which they adhere. The good performance was largely attributed to the booming domestic economy in the first half of the year before hostilities, ground-gaining regional or cross-border expansion and income diversification, and the strengthening of banks of the range of their corporate, retail and private products and services in addition to exerting more control on their operating expenses. The consolidated balance sheet of all banking groups increased by 13 percent in 2006 to reach around USD 87.8 billion and this growth in total assets was mainly driven by a 12.3 percent rise in deposits from customers and an 18.5 percent enlargement in investment capital, partly in the anticipation of Basel II Implementation. Loans and advances expanded by 16 percent whereas liquid assets by 12.4 percent.

Net profit after taxes for the year 2006 was close to USD 758 million, increasing year-on-year by 30.5 percent. Thus, both net return on average equity and net return on average assets improved from 10.71 and 0.77 percent respectively in 2005 to 11.06 and 0.92 percent in 2006. The capital adequacy measured by the central bank BIS risk asset ratio increased to 25.34 percent against 23.55 percent whereas net liquid assets to deposits were stable at 85.13 percent. In 2006 also, the cost-to-income ratio fell to 55.09 percent compared to 57.24 percent in the previous year, and the asset quality improved with the ratio of doubtful and substandard loans to gross loans decreasing to 21.14 percent from 24.24 percent.

1.8. Thriving Against Odds: Lebanon's Resilient Economy and Robust Banking Sector in 2007

The year 2007 was another challenging year for the Lebanese economy as the political and security framework continued to be unpredictable and unresolved. It was characterized by an escalating political situation and a four months military confrontation in the North of the country between the Lebanese Army and extremist insurgents. The tense security conditions, the political unrest, the almost idle legislative activity, and the absence of major government policy initiatives impeded to a certain extent economic activity, which yet performed better than it was previously estimated, with a marked improvement in the fourth quarter of the year. The estimated real growth in GDP of around 4 percent in 2007 against a weak base in 2006 was mainly driven by the services and construction sectors, which benefited to a certain extent from the rise in regional oil revenue and abundant liquidity that tend to stimulate foreign inflows and foreign demand for goods and services. Post-war reconstruction spending following July 2006 war added an extra stimulus. The Lebanese economy faced international price increases and a devaluation in the US dollar, which together contributed to higher inflation and a widening current account deficit. The balance of payments was, however, in surplus due to a larger increase in net exports of services, remittances, transfers, and capital inflows, and fiscal indicators improved with the rapid growth in revenues.

Financial markets once again showed resilience to political and security uncertainties and were able to withstand the situation very well despite the slow disbursing of external support. Actual disbursements of Paris III pledges of USD 7.6 billion amounted to around USD 1.0 billion in 2007. Financial resilience was attributed to the banking system's strong liquidity position in foreign currencies, strong deposit inflows, and skillful handling of financial pressures and external shocks at the central bank and banks alike. There were no major pressures on the exchange rate, international reserves were almost constant, and nominal interest rates remained broadly stable. Given the political impasse, spreads over international interest rates, however, increased. It is important to mention in this respect that Lebanese banks were not affected by the US subprime crisis as by regulation they had no such exposure to sophisticated structured products nor they relied heavily in their daily operations on financing from international money markets.

In light of the above politico-economic developments, the Lebanese banking sector was able to perform very well in 2007 and reported solid growth in challenging times and more importantly not at the expense of its financial standing, risk exposure, and international regulation and best practices to which it adheres. Annual growth rates of 15.1 percent in consolidated assets and 27.5 percent in consolidated net profits have been reported for all banks and all their subsidiaries. Such achievement was largely due to the regional expansion policies and considerable profits generated by cross-border entities, the more diversified and improved business lines, and better control of operating expenses. The consolidated balance sheet of all banking groups reached around USD 101 billion at the end of 2007 driven by a 16.1 percent rise in deposits from customers and an 8.8 percent expansion in investment capital. Loans and advances expanded by 30.7 percent, reflecting the large increase in banks' resources, the financing of foreign investments of domestic Lebanese businesses, foreign currency lending to the corporate sector of regional countries, and refinancing schemes to help clients who suffered from the July 2006 war. Liquid assets grew by 11.6 percent.

Net profit after taxes for the year 2007 amounted to nearly USD 961 million. Net return on average equity and net return on average assets improved from 10.98 and 0.91 percent respectively in 2006 to 11.83 and 1.02 percent in 2007. The capital adequacy measured by the central bank BIS risk asset ratio stood high at 22.21 percent and the net liquid assets to deposits slightly retreated to 81.37 percent, reflecting mainly the aggressive growth in loans. In 2007 also, the cost-to-income ratio fell to 54 percent and the asset quality continued to improve with the ratio of net doubtful and substandard loans to net loans sliding along its downward path to 4.6 percent from 7.2 percent in 2006. The loan portfolios at banks were even more provisioned and collateralized with loan loss provisions on doubtful loans covering 84.14 percent of doubtful loans and the ratio of net doubtful loans to net loans contracted to 2.5 percent from 4.2 percent in 2006.

1.9. Lebanon's Economic Triumph: Defying Odds and Soaring to New Heights in 2008

Counter to what was earlier projected, the Lebanese economy achieved record growth in 2008 of 8.5 percent in real value as economic activity expanded robustly after the Doha agreement in May and the resulting election of a new president, the formation of a national unity government, and the reinstatement of the legislative activity. The Doha agreement and the positive developments that shortly followed were crucial to this output growth as they improved drastically the political and security situation, restored the confidence of market participants and businesses, and reduced uncertainties. Strong economic growth was driven by high aggregate demand in general and buoyant tourism and construction activities in particular, largely influenced by favorable economic conditions in the Gulf region and other Arab neighboring countries which were before the outbreak of the international financial crisis. During 2008, economic and financial indicators proved that economic and financial developments in the country were favorable since the emergence of the international financial turmoil, contrary to earlier expectations, and that Lebanon has effectively mitigated the potential impact and well-managed to maintain financial stability with the absence of pressures on the exchange rate, the rapid accumulation of international reserves, large deposit inflows, and declining deposit dollarization.

In this respect, the Lebanese banking sector demonstrated in 2008 once again its resilience to financial shocks irrespective of their origins and was able to isolate itself to a large extent from the global credit crisis and its repercussions for many good reasons. It was highly liquid and well-capitalized thanks to banks and regulatory authorities' skillful management and foresight and had very limited exposure to international wholesale funding markets given its traditional heavy reliance on deposits as the main source of funds. The Lebanese banking sector had also limited exposure to failed international banking institutions and sophisticated structured products as effective and prudent bank regulation and supervision largely discouraged such exposure and high-risk activities. Therefore, there was no need for emergency liquidity provision or any other kind of public intervention as opposed to what happened in many countries abroad. On the contrary, the Lebanese banking system was perceived as a regional haven for stable placements and may have attracted more deposits during the global financial crisis than before.

In this context, the Lebanese banking industry fared exceptionally well in 2008 in terms of growth, profitability, and operating expense control while balancing risk-taking and return and complying with worldwide best practices and standards. In 2008, the consolidated balance sheet of all reporting banks and subsidiaries increased by 12.9 percent to about 114 billion USD at the end of the year, while net profit increased by 26.7 percent to 1219 million USD, with a significant part of profits earned by cross-border entities. This increased the return on average assets and equity from 1.02% and 11.79%, respectively, in 2007 to 1.13% and 13.20% in 2008. The cost-to-income ratio has also decreased from 54.02% to 52.64%.

The banking industry also performed well in terms of capital adequacy, solvency, and asset quality. The central bank's BIS risk asset ratio estimated capital adequacy at 22.39% in the year 2008 and the liquidity gauged by primary liquid assets to foreign currency deposits remained robust at 54.25%, but lower than in 2007 due to aggressive loan expansion. The ratio of net questionable and net substandard loans to net loans fell from 3.88% in 2007 to 2.47% in 2008, during a period when loan portfolios were better provisioned and collateralized. The ratio of loan loss provisions on questionable loans to questionable loans climbed from 84.7% in 2007 to 87.4% in 2008, while the ratio of net doubtful loans to net loans decreased from 2.4% to 1.5%.

1.10. Lebanon's Resilience Shines in 2009: Surpassing Expectations, Navigating Challenges, and Paving the Way for Growth

Contrary to many developed and developing countries, the Lebanese economy succeeded for the third year in a row in performing exceptionally well and in achieving a high real GDP growth rate of 9 percent in 2009 while inflationary pressures were limited. Rising confidence among Lebanese residents and non-residents, as well as foreign investors, in the Lebanese economy and markets as a result of the country's relatively stable political and security environment and improved macroeconomic management, as well as booming activities in the construction, tourism, trade, and financial services sectors, led to higher aggregate demand. Large financial inflows under a relatively favorable domestic interest rate structure constituted a key characteristic of the year 2009 and were translated into the rapid growth of deposits at banks, abundant liquidity, a record surplus in the overall balance of payments, and a surge in the International foreign exchange reserves at the central bank to very comfortable and unprecedented levels. Strong economic growth and adequate fiscal management contributed also to achieving a higher primary surplus and to a further decline in the public debt to GDP ratio and thus to a reduction in the underlying vulnerabilities though still considered high.

The Lebanese banking sector and after it has weathered pretty well the global financial crisis, thanks to its conservative assets/liabilities structure and management and prudent bank regulation and supervision, had to cope with and adjust to the low international interest rate environment and the gradual domestic policy rate cuts associated with the rapid financial inflows, large currency conversion into LBP, and massive liquidity in the domestic currency. The ensued narrower net interest rate margins pressured banks' profits and all of these developments along with some regulatory and supervisory measures, including incentive schemes that provided exemptions to reserve requirements, encouraged banks to expand credit to the private sector and to seek further growth opportunities through abroad operations and entities.

Under such internal and external operating conditions, the Lebanese banking system performed extremely well in 2009. In terms of asset growth, profitability, and operational expense control, particularly when compared to the performance of many other regional and worldwide counterparts, always balancing risk-taking and return and complying with international standards and regulations. The consolidated balance sheet of all reporting banks and subsidiaries increased by 21.6 percent in 2009 to around 138.6 billion USD at the end of the period, while net profits increased by 17.4 percent to 1427 mill USD, with cross-border branches, subsidiaries, and affiliated companies accounting for a significant portion of profits. Despite declining spreads, the sector was able to preserve the return on average assets ratio at 1.13 percent but the higher equity growth compared to the liabilities expansion reduced the leverage multiplier and contributed to a slight decrease in the return on average equity from 13.19 percent in 2008 to 12.95 percent in 2009. The cost-to-income ratio retreated further from 52.98 percent to 51.79 percent.

Measures of capital adequacy, liquidity, and asset quality in Lebanese banking improved. Equity as a percentage of total assets was 8.79% in 2009 (8.63% in 2008), capital adequacy as defined by Basel II was over 12%, and liquidity, as measured by the ratio of primary liquid assets to foreign currency deposit balances, hit a new high of 54.29% (up from 53.83%). As a result of maintaining heavily provisioned and collateralized loan portfolios, the asset quality was significantly better, with the ratio of net doubtful and net substandard loans to net loans dropping from 2.44 percent in 2008 to 1.88 percent in 2009. In this regard, the loan loss provision on doubtful loans to doubtful loans ratio grew from 87.66 percent in 2008 to 88.88 percent in 2009. However, the ratio of net doubtful loans to total loans decreased from 1.46 percent to 1.15 percent.

1.11. Thriving Against the Odds: Lebanese Economy and Banking Sector in 2010

Despite rising tensions in the fourth quarter, the Lebanese economy fared admirably in 2010 by attaining robust real GDP growth of about 8% in a reasonably stable and manageable political context and prudent macroeconomic management. Solid confidence and substantial capital inflows, notwithstanding their decrease relative to the previous year, maintained pace and boosted activity in the construction, tourism, commerce, and financial services sectors, resulting in the economy's excellent performance. Both the balance of payments and the primary fiscal balance showed significant surpluses, while the central bank's foreign exchange reserves remained at a high and unprecedented level. The public debt to GDP ratio further declined, reaching 133 percent, as a result of further interest rate declines and a supportive fiscal situation, which indicated a significant reduction in both the public debt burden and the underlying short-term risks and susceptibilities.

By satisfying related financing needs and other banking requirements on competitive terms, the Lebanese banking sector successfully met the increasing domestic demand, which helped to expand output and bring about the aforementioned developments. Additionally, it had to continue coping with low international interest rates, and slow output, and react to the instability and unpredictability of the world's financial system. With the help of regulatory incentive programs that exempt banks from reserve requirements, banks attempted to take advantage of more business opportunities through international operations and entities as well as to concentrate more on non-interest income and credit extensions to the private sector.

In light of this, the Lebanese banking industry once again made notable strides and produced excellent achievements in 2010, while simultaneously managing the trade-off between taking calculated risks and generating a profit, and adhering to worldwide best practices and rules. Net profits increased by 27.4% to reach 1821 million USD at the end of the year, with a significant portion of the profits coming from cross-border branches, subsidiaries, and affiliated businesses. The overall balance sheet of all reporting banks and subsidiaries increased by 11.7% to reach roughly 155.1 billion USD. As a result, the sector's average return on assets and equity ratios increased from 1.13 percent and 12.93 percent in 2009 to 1.24 percent and 13.90 percent, respectively, in 2010. Furthermore, efficiency and control over operational costs resulted in a significant decrease in the cost-to-income ratio, which went from 51.87 percent to 48.72 percent.

Capital adequacy and asset quality increased as a result of prudent bank regulation and supervision, as well as conservative and innovative management; consequently, liquidity remained relatively excellent in 2010. Equity as a percentage of total assets at 9.01 percent in 2010 (8.81 percent in 2009), while Basel II capital adequacy was over 13 percent. Primary liquid assets to foreign currency deposits indicated 51.53 percent liquidity. In comparison, the ratio of net doubtful and net substandard loans to net loans declined from 1.88 percent in 2009 to 1.33 percent in 2010, indicating improved asset quality. This was made possible by keeping highly provisioned and collateralized loan portfolios, as the ratio of loan loss provisions (reserves) on doubtful loans to doubtful loans increased from 88.76 percent in 2009 to 92.54 percent in 2010.

1.12. Navigating Challenging Waters: Lebanese Economy and Banking Sector in 2011

After four successive years of strong real economic growth averaging 8.25 percent per annum, the Lebanese economy relatively cooled in 2011 and the real GDP growth rate decelerated to 5.2 percent according to official national accounts and to much lower rates based on other reputable international institutions' estimates. Domestic political disagreement and tension manifested, among other things, by the fall of the coalition government and then the long delay in the formation of a new cabinet, along with regional political and security turmoil, particularly in Syria altered adversely the business climate and stalled the momentum. Such developments raised uncertainty and impeded the activities of key growth drivers specifically real estate, tourism, and trade, thus contributing to this outcome, which is still notable when compared to output growth in the MENA region. The widening trade deficit in 2011 mainly driven by rising fuel and raw material prices under moderating financial inflows resulted in a considerable deficit in the overall balance of payments, the first of its kind since 2002. Yet the high level of official foreign exchange reserves was sustained and the fiscal situation reported a significant primary balance under the relatively low-interest rate environment, which permitted a further decline in the debt-to-GDP ratio to reach 134.8 percent, entailing lower core risks and susceptibility.

The Lebanese banking sector adopted a cautious approach and took preventative measures that included collective provisions to maintain or even strengthen the overall risk profile and deal with potential spillover effects of regional development in light of the regional political and security events that have harmed and continue to harm the economies of related countries and the operations of subsidiaries operating there, as well as the domestic situation.

However, collective provisions increased by 44% in 2011. The Lebanese banking sector managed to maintain its strong financial position and produce, on average, less impressive results in 2011 despite the challenging operating environment, which were still favorable and even strong when compared to peers and many other banking sectors around the world.

In 2011, the consolidated total assets of all reporting banks and subsidiaries expanded moderately by 7.7 percent, against a relatively higher 11.9 percent in the previous year, to attain 167.2 billion USD at the end of the period, whereas net profits contracted by 5.1 percent to reach around 1.7 billion USD, driven by rising operating expenses and hardly improved net operating income associated with downward pressures on spreads and interest margins. Subsequently, the return on average assets ROAA retreated to 1.08 percent (1.25 percent in 2010), the return on average equity recoiled to 12.31 percent (13.92 percent in 2010), and the cost-to-income ratio increased a little to 49.85 percent from 48.29 percent. Deposits from customers grew by 7.5 percent in 2011 (12.3 percent in 2010) but still, this growth was sufficient to meet all the domestic financing needs, and loans to customers expanded by 14 percent compared to 25.2 percent in the preceding year.

Measures of capital adequacy and liquidity marginally declined from the prior year, however, they remained strong and acceptable. With practically all of the capital consisting of Tier 1, the capital adequacy ratio according to Basel II was close to 12 percent, exceeding international regulatory standards. The ratio of net primary liquidity to deposits was also much higher than regional and global benchmarks at roughly 29 percent. With the ratio of net doubtful loans and net substandard loans to total net loans standing at 1.96 percent (2.07 percent in 2010), asset quality improved. Parallel to this, the ratio of loan loss reserves on doubtful loans compared to probable loans fell from 83.20 percent to 81.59 percent.

1.13. Navigating Turbulence: Lebanese Economy and Banking Sector in 2012

The same factors that caused the Lebanese economy's sharp slowdown in 2011 still had an impact on it in 2012: domestic political unpredictability, a lack of reforms, vulnerabilities in the public sector's finances, escalating spillovers from the Syrian crisis, in addition to persistent security breaches throughout the nation. Due to this, real GDP growth was predicted to be between 0.6% and 1.5% in 2012 as opposed to 1.5% to 1.8% in 2011. With consumption, commerce, tourism, construction, capital flows, and investment indices all indicating weak economic activity throughout the year, the economic downturn in 2012 was widespread. As the budget deficit increased from 6% of GDP in 2011 to 9.4% of GDP in 2012, public finances also declined. The deficit grew mostly as a result of increases in payments to Electricité du Liban of 1.2% of GDP and staff costs of 1.9% of GDP, respectively. The main budget balance also changed, moving from a surplus of 4.26% of GDP in 2011 to a deficit of 0.26% of GDP in 2012, the first primary deficit since 2006. As a result, the dynamics of the public debt were reversed, and the debt level rose for the first time since 2006, from 137.4% of GDP in 2011 to approximately 140% of GDP in 2012. Parallel to this, the current account deficit increased from 12.1% of GDP in 2011 to an anticipated 16.5% of GDP in 2012, while the balance of payments deficit decreased from $2 billion in 2011 to $1.54 billion in 2012.

The value of Banque du Liban's gold reserves reached $15.3 billion at the end of 2012, representing a gain of 6.3% for the year. The amount of the bank's gross foreign exchange reserves was $30 billion at the end of 2012, down 2.7% from $30.8 billion the year before. At year's end, the total value of Banque du Liban's gold and foreign currency holdings was almost 108.5% of GDP.

In parallel, the operating environment of the various markets where subsidiaries of Lebanese banks were present, especially in the Middle East & North Africa region and in Western Europe, was also volatile given the slow economic growth and the recessionary outlook in many of those economies.

The Lebanese banking sector took the necessary actions to deal with the economic slowdown and the unfavorable external conditions in light of the difficult domestic and international operating environments by reviewing its strategies and priorities, adopting a more conservative risk management approach, and enhancing risk coverage. As a result, in 2012, the sector's special provisions for doubtful loans rose by 74%. Additionally, the actions done by the authorities in charge of bank regulation and supervision contributed to maintaining the resiliency and strength of the Lebanese banking sector.

The available financial statements indicated that the total consolidated assets of all reporting banks and subsidiaries reached $181.3 billion at the end of 2012, which constituted an increase of 8.4% compared to a growth of 7.7% in 2011. The growth in assets was mainly driven by the increase in customer deposits by 9.3% in 2012, along with a rise in loans and advances to customers by 12.5% in 2012. In comparison, deposits grew by 7.2% and loans expanded by 14.0% in the previous year. Also, net profits totaled $1.9 billion in 2012 and grew by 7.4% year-on-year, relative to a contraction of 5.1% in the preceding year. As a result, the return on average assets (ROAA) regressed from 1.08% in 2011 to 1.06% in 2012, and the return on average equity (ROAE) was unchanged at 12.27%; while the cost-to-income ratio increased from 49.77% in 2011 to 50.11% in 2012.

The sector's capital adequacy and liquidity measures remained sound and above international benchmarks. The capital adequacy ratio as per Basel II improved from 11.75% in 2011 to 12.91% In 2012, and the common Tier One capital ratio stood at 9.09%. Also, the net primary liquidity-to-deposits ratio improved from 29.3% in 2011 to 31.42% in 2012. Asset quality changed slightly, with the ratio of net doubtful loans and net substandard bans to total net loans standing at 2.1% in 2012 relative to 1.97% in 2011. Also, the ratio of gross substandard loans and gross doubtful loans to total gross loans reached 7.71% compared to 7.66% in 2011. Further, the ratio of loan-loss reserves on doubtful loans to doubtful loans declined slightly from 81.79% in 2011 to 79.45% in 2012.

1.14. Navigating Challenges: The Resilience of the Lebanese Banking Sector in 2013

Like the previous couple of years, the domestic and regional operating environment in 2013 was not that favorable for banks. The Lebanese economy kept growing for the third consecutive year at a slow pace between 1.5 and 2 percent under weakened and challenging domestic security, rising political tension, and unprecedented inflows of Syrian refugees. These Syrian crisis-related developments heightened uncertainty and risk, discouraged investment, and affected directly and indirectly the chief drivers of economic growth, particularly construction, and tourism. A deteriorating primary fiscal budget and an increase in the total fiscal deficit to about 9 percent of GDP contributed to the widening of the fiscal imbalances in 2013, while the enormous external account deficit, which accounted for about 16 percent of output, remained. Nonetheless, monetary policy was effective in ensuring financial stability, with the central bank maintaining substantial and appropriate foreign exchange reserves and a steady interest rate structure. The operating climate in the different markets where subsidiaries of Lebanese banks were present was not much better given the escalating security situation in some of those countries and the slow or fragile economic growth and prevailing recession in some others.

Against this background of realities and challenges, the Lebanese banking sector was robust and kept supporting the stability of the system through its solid liquidity buffers, sound capital adequacy, and well-established depositor-based funding. It also remained a main contributor to stimulating economic activity by providing the necessary financing to the private and public sectors at the best conditions. Banks stayed as well seriously committed to cautiously balancing the trade-off between risk and return, taking necessary provisions, and complying with international regulations and sanctions of which those on Anti-Money Laundering / Countering the Financing of Terrorism (AML/CFT).

Though the sector's assets expansion was favorable, the profitability measures retreated but were somehow in line with international levels. The enclosed financial statements revealed that the total consolidated assets of all reporting banks and subsidiaries expanded in 2013 by 9.7 percent, against 8.4 percent in the previous year, to reach 199 billion USD at the end of the period. Total assets growth resulted mainly from the increase in the deposits from customers by 9.5 percent (8.8 percent in 2012) and in total shareholders' equity by 8.6 percent (13.4 percent in the preceding year). This was coupled essentially with the upsurge in net loans and advances to customers by 15.2 percent compared to 11.4 percent in 2012 and in debt instruments (mainly governmental) by 7.4 percent (3.2 percent a year earlier). Unlike assets, net profits grew by only 0.5 percent in 2013 (7.6 percent in the preceding year) to attain around 1894 million USD, given the increase in total operating expenses (by 8.4 percent year-on-year) that much exceeded that in total operating income (3.9 percent). Consequently, the return on average assets

(ROAA) shrank to 1.00 percent (1.07 in 2012), the return on average equity dropped to 11.09 percent against 12.08 percent, and the cost-to-income ratio rose to 51.82 percent from 49.65 percent.

Capital adequacy and liquidity measures remained strong and above international benchmarks. The capital adequacy ratio as per Basel II improved to 14.31 percent in 2013 against 13.86 percent in 2012 with a common tier 1 ratio of 10.00 percent, and net primary liquidity to deposits stood at 30.71 percent (31.55 percent a year earlier). Asset quality barely changed, with the ratio of net doubtful and substandard loans to total net loans standing at 2.47 percent in 2013 (2.12 percent in 2012) and the ratio of gross substandard and doubtful loans to total gross loans being close to 7.79 percent compared to 7.80 percent for the two mentioned years respectively. The ratio of loan loss reserves on doubtful loans to doubtful loans diminished to 77.69 percent from 79.61 percent.

1.15. Navigating Challenges: Lebanese Banking Sector Shines in 2014 Despite Regional Turmoil

The protracted crisis in Syria and the associated regional upheaval forced the Lebanese banking sector to deal once more with the muted domestic economic growth, security issues, and volatile political climate in 2014. Nevertheless, despite the ongoing local and regional gridlock, the banking industry was able to maintain its historically demonstrated immunity, retaining the confidence of investors and depositors and posting good profits in 2014. More specifically, the consolidated balance sheet of all banks plus subsidiaries included in Bilanbanques exhibited a favorable growth in total assets of 9.3 percent in 2014, which amounted to 217.5 billion USD at the end of the period. This was mainly driven by an 8.5 percent expansion in the deposits from customers, which constituted 83 percent of total assets, and by a 10.8 percent increase in shareholders' equity, which represented 9.1 percent of the total balance sheet. These developments in the sources of funds were associated essentially with a rise in net loans and advances to customers by 11 percent and to a much lower extent in debt instruments (mainly government securities) by 1.6 percent. Balances with central banks swelled 22.2 percent.

It is worth noting that the challenging business climate and operating environment, not only in Lebanon but also in some countries where subsidiaries and branches operated, required banks to uphold a conservative management strategy and take the necessary precautionary measures to sustain or even strengthen the overall risk profile and confront potential spillover of the regional developments. The challenge for the Lebanese banking sector was to preserve under this tough operating situation, its good financial standing and to achieve good results, which were in fact favorable and even strong when compared to peers and many other banking industries around the world. More particularly, the consolidated income statement of all banks plus subsidiaries revealed a good increase in net profits of 9.7 percent in 2014, which totaled around 2.1 billion USD for the mentioned year. The growth in net operating income (9.3 percent) exceeded that in total operating expenses (8.6 percent) and the share of net interest income of total operating income remained almost stable at 63 percent compared to 16.9 percent share for net fees and commission income and 20.1 percent stake for the remaining operating income such as net gains on financial investments and foreign exchange operations.

The return on average assets and return on average equity for the banking industry were stable at 0.99 percent and 11.04 percent, respectively. Both the interest margin and the spread were stable as well at 2.0 percent and 1.9 percent consecutively while the cost to Income ratio decreased a lithe to 51.57 percent from 51.82 percent. Capital adequacy and liquidity indices improved in comparison to the previous year, indicating that the economy is still strong and optimistic. According to Basel II, the overall capital adequacy ratio was close to 14.61 percent (13.48 percent tier one ratio), above international regulatory criteria, and net primary liquidity to deposits was 32.11 percent (30.81 percent in 2013), greatly exceeding regional and worldwide benchmarks. Asset quality was also somewhat improved, with the net doubtful loan to gross loan ratio being at 1.48 percent and the net doubtful and substandard loan to gross loan ratio standing at 2.15 percent (2.25 percent in 2013At the same time, the loan loss reserve ratio on doubtful loans fell to 77.45 percent from 78.34 percent, and the collective provisions to net loans fell to 0.99 percent from 1.07 percent.

As far as the overall economy was concerned, Lebanon's GDP grew in real terms by only 2 percent in 2014, well below the potential growth estimated at 4 percent, as conventional growth drivers i.e. tourism and construction remained adversely affected by several factors. This was mainly, the uncertainty and low investor and consumer confidence provoked by the Syrian crisis and refugees, the lack of consensus among the different political parties in the country preventing macroeconomic management and the passage of important legislations, and the vacant presidency since May 2014. The external account deficit continued also to be large accounting for around 25 percent of output and the decelerating financial inflows contributed under this situation to a considerable deficit in the overall balance of payments close to 1.4 billion USD. Yet the high level of official foreign exchange reserves was sustained and improved and a stable interest rate structure prevailed reflecting a successful monetary policy in maintaining financial and price stability. In addition, the fiscal situation was exceptionally positive with the public deficit to GDP declining to 6.2 percent from 8.9 percent, which permitted stabilization in the debt-to-GDP ratio at 134.5 percent.

1.16. Navigating Challenges with Resilience: The Lebanese Banking Industry's Strong Performance in 2015

The Lebanese banking industry with its domestic entities and external subsidiaries and branches remained sound and resilient in 2015 and was able to achieve relatively good results despite the weakened and challenging local, regional, and international operating environment. On the domestic level, the negative repercussions on the Lebanese economy of the Syrian crisis and related political deadlock and failure to elect a president for the republic were more felt with real output decelerating to below 1 percent. This induced de facto lower banking activity. Many economies where subsidiaries and branches of Lebanese banks operate had also their own economic and security problems and uncertainties and their output growth was also subdued. Under these conditions, the challenge for the Lebanese banking sector was to efficiently manage all types of conventional and emerging risks and preserve good financial standing. cement investors' and depositors' confidence in their banks and fortify compliance with international regulations especially in the areas of AMUCFT, sanctions, and tax evasion to ensure stability and a good reputation for the Lebanese banking system and Lebanon as a country.

The consolidated balance sheet of all banks and subsidiaries reflected a large extent the above-mentioned economic developments and revealed a major deceleration in total assets' growth, which was close to 4.8 percent in 2015 compared to 9.3 percent in the previous year and 9.6 percent in 2013. The moderate but still considered adequate expansion in total assets to 227.8 billion USD at the end of 2015 was associated with a 4.5 percent increase in the deposits from customers (8.5 percent growth in 2014), representing around 80 percent of the total balance sheet, and 6.8 percent rise in shareholders' equity (10.8 percent increase in 2014), constituting nearly 9.2 percent of all assets. The slowdown in the sources of funds' growth was matched by a reasonable augmentation in loans to customers of 5.6 percent in 2015 (11 percent in 2014) and more placements in debt instruments (mainly government securities) by 8 percent. Balances with central banks increased by 4.4 percent.

In parallel, the consolidated income statement indicated a satisfactory growth in net profits of 7 percent in 2015 (9.1 percent in 2014), which amounted to almost 2.2 billion USD for the mentioned year. Net operating income expanded by 5.7 percent and total operating expenses increased by 5 percent. The share of net interest income of total operating income was maintained at 63 percent against a 16.2 percent share for net fees and commission income and a 20.8 percent stake for the remaining operating income including net profits on foreign exchange operations.

The slower banking activity in 2015 did not translate into considerably poorer performance measures in that year. Instead many performance metrics stabilized while others improved thanks to the skilled bank management and its ability to rapidly adapt successfully to changes and difficulties. In terms of profitability, the return on average assets was stable at around 1 percent while the return on average equity slightly retreated to 10.83 percent compared to 11 percent in 2014. Both the interest margin and the spread were stable as well at 2.0 percent and 1.92 percent consecutively while the cost-to-income ratio decreased a little to 50.81 percent from 51.51 percent. Capital adequacy measures improved about the preceding year, while liquidity remained high. The total capital adequacy ratio as per Basel II progressed to 15.03 percent compared to 14.60 percent in 2014 and the tier one ratio attained 13.72 percent, exceeding international regulatory requirements. Net primary liquidity to deposits dropped to 30.7 percent from 32.1 percent a year earlier and remained far above regional and international benchmarks. Asset quality retreated a little with the ratio of net doubtful loans to gross loans at 1.56 percent (1.49 percent in 2014) and the ratio of net doubtful and substandard loans to gross loans stood at 2.31 percent (2.15 percent a year back). In parallel, the ratio of loan loss reserves on doubtful loans to doubtful loans recoiled to 75.56 percent from 77.31 percent but the collective provisions to net loans increased under the new operating environment to 1.09 percent from 0.99 percent.

1.17. Resilience Rewarded: Lebanese Banking Sector Thrives Despite Challenging Times in 2016

Despite the prolonged exigent operating environment, the activity and performance of the Lebanese banking sector improved in 2016 owing to two main factors. First, the Lebanese Central Bank coordinated operations with banks to reduce vulnerabilities and anchor financial stability, and second, the political settlement was reached in the fourth quarter of the year. This latter led to the election of a President of the Republic and the formation of a new government that is working seriously on reducing uncertainty and getting the economy out of its long-lasting low economic growth cycle. As the Syrian crisis continued to distress economic activity and outlook and given that financial inflows slowed markedly in the first half of 2016, under tightened regional financial conditions, the Central Bank of Lebanon had to react to reverse the drop in official reserves, the considerable deficit in the balance of payments and the slowdown in deposits' growth. Central Bank swap operations with banks were dictated by exceptional circumstances and high political uncertainty and came before the achievement of the political settlement, which was reinforcing gradually the confidence of consumers and investors necessary to activate consumption and investment and boost economic output.

The financial statements reported in the Bilanbanques reflected to a large extent the above-stated developments in the Lebanese economy and financial sector. The total consolidated assets of all reporting banks plus subsidiaries expanded by 5.9 percent in 2016, compared to 4.8 percent in the previous year, and reached 241.4 billion USD at the end of the period. Total assets growth emanated essentially from the increase in the deposits from customers, which represent more than 78 percent of the total balance sheet, by 3.6 percent (4.5 percent in 2015) and in shareholders' equity by 10 percent (6.9 percent in 2015). Other sources of funds (around 12 percent of the total) played also an exceptional role in assets' expansion as they rose by around 19 percent. The mentioned changes in total liabilities and shareholders' equity were mainly associated with the upsurge in balances with Central Banks by around 26 percent and the slow increase in net loans and advances to customers by only 2.0 percent (5.6 percent in 2015). Debt instruments, mainly governmental, retreated by 0.3 percent.

The consolidated net profits were around 2.5 billion USD in 2016, thus increasing by 12.6 percent in relation to the preceding year (7 percent in 2015). The reported improvement resulted from the considerable growth in net operating income (24.1 percent), largely driven by the net gains on financial assets and investments, which much exceeded that of total operating expenses (16.3 percent). The share of net interest income of total operating income dropped occasionally to 49.1 percent against 19.7 percent share for net fees and commission income and 31.2 percent stake for the remaining operating income including net profits on foreign exchange operations. The income tax expanded in turn to equal 23.6 percent of profit before tax (18.4 percent in 2015).

In terms of profitability, the return on average assets improved to 1.06 percent in 2016 (0.99 percent in 2015) and the return on average equity advanced to 11.23 percent compared to 10.82 percent in the previous year. Both the interest margin and the spread slightly increased to 2.02 percent and 1.94 percent respectively (2.00 and 1.92 percent earlier) while the cost-to-income ratio fell considerably to 44.36 percent from 50.33 percent. The total capital adequacy ratio progressed to 16.51 percent compared to 15.06 percent in 2015 and the tier one ratio and common tier one ratio attained 14.72 percent and 11.58 percent consecutively, exceeding international regulatory requirements. Net primary liquidity to deposits jumped to 35.15 percent in 2016 from 30.70 percent a year earlier and remained in turn far above regional and international benchmarks. Asset quality retreated a little with the ratio of net doubtful loans to gross loans at 1.60 percent (1.56 percent in 2015) and the ratio of net doubtful and substandard loans to gross loans up to 2.83 percent (2.31 percent a year back). Nevertheless, the ratio of loan loss reserves on doubtful loans to doubtful loans increased a lithe to 75.52 percent from 75.44 percent, and the collective provisions to net loans augmented under the new circumstances to 1.55 percent from 1.09 percent.

1.18. Resilience Amidst Adversities: Lebanon's Banking Sector Paves the Way for Stability and Growth in 2017

The Lebanese banking sector tolerated anew in 2017 the protracted strenuous operating environment and proved once again tinder the exigent circumstances its competency in absorbing shocks and sustaining activity and performance, which remain acceptable given the existent adversities and mirror basically two realities The first is the strategic options and flexible asset liability management adopted by banks in adjusting to changes while securing a solid risk profile and the second is the prudent and forward-looking measures implemented by the regulatory and supervisory authorities to maintain and reinforce financial stability under weak economic activity and heightened uncertainty. In fact, economic conditions domestically and in the region remained largely inert with Lebanon's economic growth estimated at around 2 percent, partly related to the conflict in Syria and the region and partially to the lack of momentum in implementing policies and reforms that tackle internal and external imbalances and improve investor and consumer confidence. The public debt to GDP ratio also regrettably progressed and net financial inflows decelerated in turn, affected to a large extent by the November short-lived political crisis that induced a new wave of responsive monetary and financial operations and higher interest rates. The Lebanese banking sector supported and will keep on backing all types of central banks' pre-emptive and reactive initiatives and operations aiming at stimulating the Lebanese economy and anchoring financial stability.

The financial statements included in this new edition of Bilanbanques echo to a large degree the developments that occurred in 2017 some of which were positive such as fortifying the security situation, approving the first budget in 12 years, and passing a new electoral law. The total consolidated assets of all reporting banks plus subsidiaries grew by 6.9 percent in 2017 against 5.9 percent in the preceding year to attain 257.8 billion USD at the end of the period. This expansion in total assets was associated with an increase in the deposits from customers (which represent around 77 percent of the total balance sheet) by 3.3 percent (3.6 percent in 2016) and in shareholders' equity (that constitutes around 9 percent of total assets) by 6.6 percent (10 percent in 2016). Other sources of funds mainly interbank (around 15 percent of the total) played also an exceptional role in assets expansion as they rose by around 26.4 percent. The mentioned changes in total liabilities and shareholders' equity were primarily correlated with the upsurge in balances with central banks by around 28.8 percent and the much less increase in net loans and advances to customers by 2.3 percent (2.0 percent in 2016). Debt instruments mostly sovereign retreated by 8.9 percent.

The consolidated net profits reached 2.6 billion USD in 2017 and thus grew by 4.4 percent with reference to the previous year (12.6 percent in 2016). This modest positive growth resulted mainly from the outcome of discontinued operations as the profits after tax from operating activities retreated in 2017 by 6 percent. In fact, total operating income regressed by 18.3 percent, largely driven by a drop in each of net fees and commission income and net gains on financial assets and investments following their upsurge in 2016 in the wake of the conducted massive financial engineering operations, while net operating income retreated less by 9.3 percent aided by the sharp reduction in net provisions for credit loss by 61.4 percent. In parallel total operating expenses declined by 5.5 percent (of which 2 percent from the drop off in staff expenses). The share of net interest income of total operating income stood at around 65 percent in 2017 against a 15 percent share for net fees and commission income and a 20 percent stake for the remaining operating income. The income tax represented 18.8 percent of profit before tax.

In terms of profitability, the return on average assets slightly went back to 1.04 percent in 2017 (1.06 percent in 2016) and the return on average equity diminished to 10.84 percent compared to 11.23 percent in the previous year. Both the interest margin and the spread advanced a little to 2.03 percent and 1.94 percent respectively (2.01 and 1.92 percent a year earlier) while the cost-to-income ratio rebounded to its normal level at 49.06 percent from 44.30 percent.

In terms of profitability, the return on average assets slightly went back to 1.04 percent in 2017 (1.06 percent in 2016) and the return on average equity diminished to 10.84 percent compared to 11.23 percent in the previous year. Both the interest margin and the spread advanced a little to 2.03 percent and 1.94 percent respectively (2.01 and 1.92 percent a year earlier) while the cost-to-income ratio rebounded to its normal level at 49.06 percent from 44.30

percent. The total capital adequacy ratio advanced to 16.82 percent compared to 16.49 percent in 2016 and the tier one ratio and common tier one ratio attained 15.07 percent and 12.11 percent consecutively, exceeding international regulatory requirements. Net primary liquidity to deposits jumped to 39.75 percent in 2017 from 35.15 percent a year earlier and remained in turn far above regional and international benchmarks. Asset quality retreated a little with the ratio of net doubtful loans to gross loans at 1.63 percent (1.58 percent in 2016) and the ratio of net doubtful and substandard loans to gross loans up to 3.24 percent (2.81 percent a year back). Nevertheless, the ratio of loan loss reserves on doubtful loans to doubtful loans remained almost steady at 76 percent, and the collective provisions to net loans at around 1.6 percent.

1.19. Resilience and Compliance: The Lebanese Banking Sector's Journey in Challenging Times During 2018

The Lebanese banking sector continued throughout 2018 strengthening its compliance with international regulations, more particularly in the areas of AML/CFT and sanctions, aiming to preserve the reputation and credibility of the system to protect access to the international financial markets for the benefit of investors, clients and the Lebanese business community as a whole. The Lebanese Banking sector also supported Central Bank's pre-emptive and reactive initiatives and operations aiming at anchoring financial stability in an environment characterized by weak economic growth, high uncertainty, and low consumer and investor confidence. Such an environment was triggered by waves of political unrest, slowing capital inflows, increased taxes, and delays in implementing administrative and economic reforms. The successful achievement of parliamentary elections and the 2018 budget law, including the success of the CEDRE conference in Paris did not reflect positively on the general economic mood because of other negative aspects that surfaced. Amongst these negative signals are (i) a more than 8-month delay to form a new government that would undertake fiscal reforms and implements capital investment infrastructure programs on projects and (ii) a sharp deteriorating fiscal situation at a time when expectations and sentiments were optimistic. Nevertheless, the Lebanese banking sector tolerated these challenges and proved once again its competency and perseverance in absorbing shocks and sustaining activity and performance, which is self-explanatory, in the data published in the new edition of "Bilanbanques".

The total consolidated assets of banks expanded by 10.6% in 2018, compared to 6.8% in the previous year to attain 285.2 billion USO in December 2018. This growth in the consolidated balance sheet was mainly due to the exceptional arrangements of interbank transactions with the Central Bank, which rose by around 97.3% to represent around 16% of total assets. The increase in other sources of funds was minor as deposits from customers (around 71.4% of the total balance sheet) increased by only 2.0% (3.3% in 2017) and shareholders' equity (that constitutes around 8.7% of total assets) inched by 0.4% (6.6% in 2017). The stated changes in total liabilities and shareholders' equity were primarily associated with the rise in balances with Central Banks of around 33.8% and the much-reduced debt instruments mostly sovereign, by 2.0%. Net loans and advances to customers retreated by -3.8% (+2.3% increase in 2017).

The consolidated net profits reached 2.5 billion USO in 2018, thus a decrease of 5% as compared to the preceding year. This drop was due to a decline in operating income, (particularly in relation to net gains on financial instruments and other operating non-interest income) and to a lesser degree by the decline in profit from discontinued operations captured in the prior year's income. Elimination of the right of set-off applicable to withholding tax along with an increase in the corporate income tax contributed a considerable reason in suppressing profits, as the total amount of withheld tax on interest earned, plus corporate income tax reached around 1.2 billion USD, i.e. an increase of 87.6% relative to 2017. Consequently, the return on average assets dropped to 0.90% in 2018 (1.04% in 2017) and the return on average equity diminished to 9.95% compared to 10.83% in the previous year. Both the interest margin and the spread retreated as well to 1.97% and 1.87% respectively (2.02% and 1.93% in 2017) while the cost-to-income ratio rose from 48.30% to 50.38% in 2018.

The banking system consolidated financial statements reflected an improvement in the capital adequacy ratio which progressed to 17.79% compared to 16.90% in 2017 and the tier one ratio and common tier one ratio attained 15.47% and 12.65% respectively, exceeding the international regulatory threshold. Net liquidity to deposits amounted to 56.54% in 2018 as compared to 44.93% a year earlier, which was ahead of international benchmarks. Asset quality retreated relatively with the ratio of net credit impaired loans to gross loans at 3.98% (3.25% in 2017) and the ratio of allowance for ECL to net loans up to 1.58% (1.52% in 2017). Nevertheless, the ratio of loan loss reserves on credit-impaired loans to credit-impaired loans remained adequate at 61.72%.

CONCLUSIONS

The timeline in Figure 1 highlights the overview of the Lebanese Banking Sector from 2000 to 2018. This overview provides valuable insights into the evolution, challenges, and transformations of the Lebanese banking industry. It fills a significant gap in existing knowledge by contributing to theoretical frameworks, empirical models, and practical understanding of the Lebanese banking system within emerging economies. Throughout the years covered in the report, the Lebanese banking sector demonstrated resilience, adaptability, and prudent practices, navigating through various economic, political, and security challenges.

Despite facing recessionary conditions in the early 2000s, Lebanese banks-maintained liquidity, contained risks, and pursued regulatory strengthening and strategic initiatives to position themselves for future growth. They embraced modernization and technological advancements, improving their operations and adhering to international standards and regulations. The sector played a vital role as a financial intermediary, catalyst, and partner, contributing to the growth and stability of the Lebanese economy. The banking sector's resilience was particularly evident during periods of political tensions, tragic events, and economic downturns. It absorbed financial shocks through coordinated efforts between the central bank and banks, maintaining stability and regaining confidence. Despite setbacks, the sector consistently reported growth in total assets, profitability, liquidity, and capital adequacy. The ability of Lebanese banks to navigate challenges highlighted the trust and confidence of depositors and investors, supported by adherence to international best practices.

The Lebanese banking sector's performance in the years covered by the study underscores its vital role in the economy and its commitment to sound practices, risk management, and collaboration with regulatory authorities. While facing domestic and regional uncertainties, the sector maintained its strong financial position and explored opportunities for expansion and growth, both domestically and internationally. It contributed to the stability, growth, and resilience of the Lebanese economy, serving as a pillar of trust and support for clients and investors.


2000
•Lebanon's banking industry faced weak demand, but reforms and improved regulations empowered banks to pursue growth opportunities through capital raising and infrastructure upgrades.
2001
•Lebanese banks operated prudently, following international standards and maintaining sound financial practices. They achieved improved profitability and focused on modernization and collaboration for continued development.
2002
•Lebanese banks in 2002 were reliable partners for investors, offering effective financing, strong capital adequacy, and modernized operations as catalysts and consultants in the economy.
2003
•Lebanese banks thrived in 2003 due to improved economic conditions, financial support, prudent practices, and adherence to international standards.
2004
•Lebanese banks experienced a prosperous year in 2004, benefiting from a stronger economy, lower interest rates, and robust liquidity and capital adequacy.
2005
•Lebanese banks resilient through 2005's challenges, earning trust amid economic and political turmoil with liquidity, solvency, and improved assets.
2006
•Despite challenges in 2006, Lebanese banks showed resilience, maintaining stability, confidence, and profitability, supported by liquidity, improved asset quality, and prudent practices.
2007
•In 2007, despite challenges, Lebanese economy and banks showed resilience, with solid growth, improved profitability, and better asset quality.
2008
•Lebanon's economy exceeded expectations in 2008, with record growth of 8.5%. The banking sector showed resilience, maintaining stability and profitability while adhering to global standards.
2009
•Lebanon's economy excelled for the third consecutive year in 2009, achieving 9% GDP growth. The banking sector remained strong, with improved asset quality, profitability, and capital adequacy.
2010
•Lebanon's economy thrived in 2010 with strong growth, stable politics, robust banking sector, and improved asset quality.

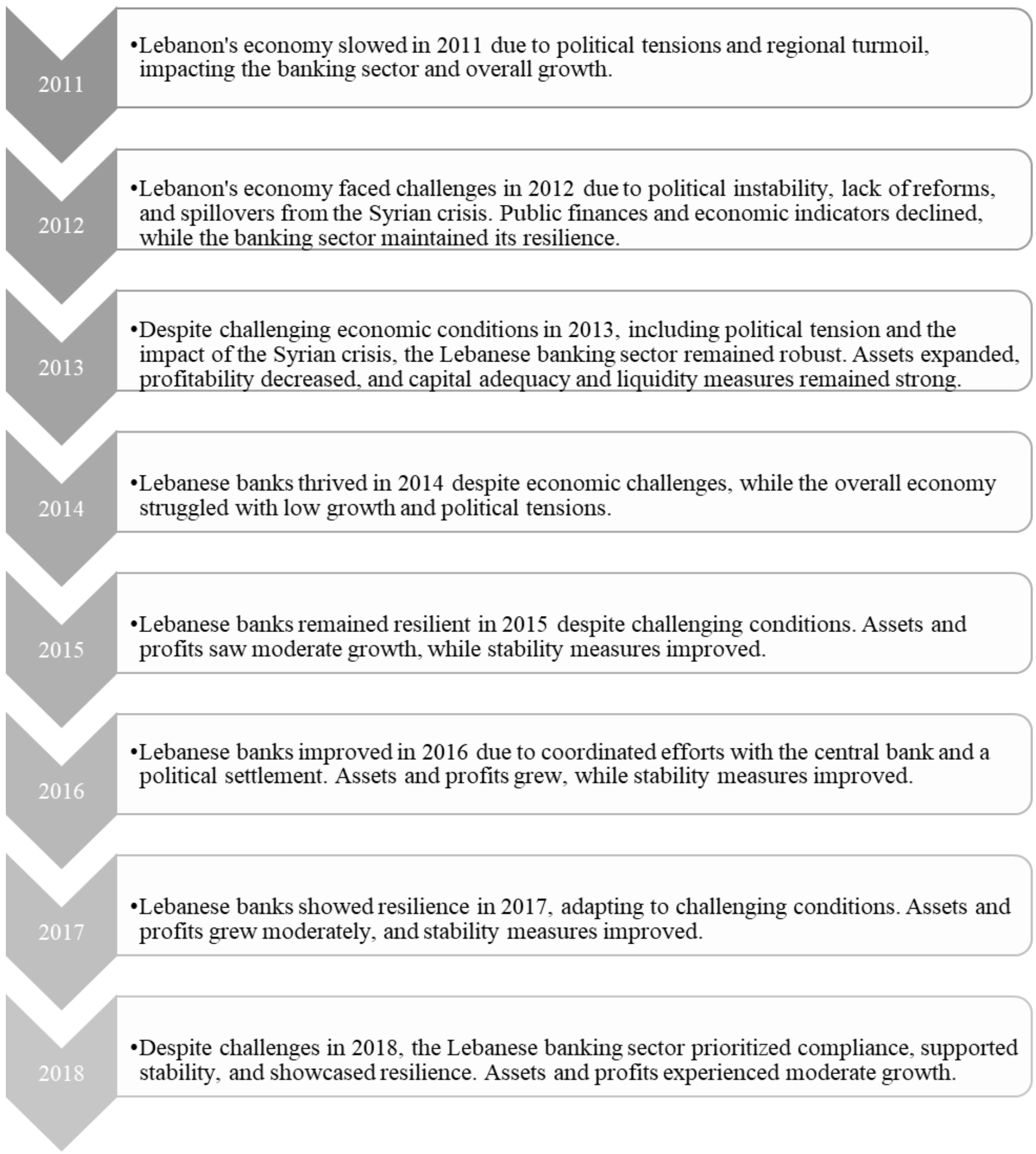

Figure 1: Timeline Highlighting an Overview of the Lebanese Banking Sector

Looking ahead, the report emphasizes the importance of addressing structural weaknesses, implementing necessary reforms, and promoting socio-economic development to sustain economic growth and financial stability in Lebanon. The banking sector is expected to continue playing a pivotal role in supporting government initiatives, stimulating the economy, and instilling confidence in consumers and investors. By leveraging its resilience, adaptability, and commitment to international standards, the Lebanese banking sector can contribute to the country's long-term prosperity and financial well-being.

The Lebanese banking sector's experiences, as explored in the study, can offer valuable lessons for other countries facing similar challenges or operating in volatile regions. By examining the strategies employed by Lebanese banks, their risk management approaches, and the effectiveness of regulatory measures, policymakers and researchers from other economies can draw insights and adapt relevant practices to their own contexts.

The study contributes to the existing body of knowledge on banking and finance by providing a comprehensive review of the Lebanese banking sector. It presents an analysis of the sector's performance, challenges, and transformations during a significant period, adding to the literature on banking in crisis-prone economies. Researchers, scholars, and students interested in banking, finance, emerging markets, and the Middle East region can benefit from the study's findings and use them as a basis for further research.

In brief, the significance of this study lies in its ability to shed light on the performance, challenges, and transformations of the Lebanese banking sector during a period of significant turmoil. Its findings can inform policy decisions, regulatory reforms, and academic research, while also providing valuable lessons for other economies operating in crisis-prone environments.

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