



Lebanese Economic Association

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The Financial Crisis : Its Implications on the Lebanese Economy

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The Financial Crisis

Causes:

Collapse of 2001 Stock market in the US

Specially- Technology and small capital
companies

Speculative elements in financial markets are
significant

Created a shift in demand Toward Real Estate

- Real estate market boom
- Speculative investors invaded the market
- Supply responded to real demand and speculation
- Oversupply when speculators leave the market to reap gains
- Lag in supply response

Easy Credit

- Down payments were not required
- Decline in price implies negative equity for many mortgage holders
- Slow down in the economy due to property market decline
- Foreclosures

Derivatives and related markets

- Wide spread derivatives markets:
 - Credit default swaps
 - Debt guarantees
 - Secondary markets for mortgages in Europe and Asia

Losses in property markets

- Defaults first by speculators and buyers without margins
- Losses in Mortgage companies
Fannie Mae and Freddie Mack

Multiplier effect of Losses

- Banks
- Real estate companies
- Developers
- Industries that supply property

Credit Crunch

- Fear of high risk
- Banks withholding lending/more strict
- Dry up in commercial paper markets

Stock markets react

- Commodity prices up- Speculation a main element
- Signs of recession

Fall in World markets: this year about 60%
30% in Sept/Oct

Rescue Plan

- US Plan
- EU Plan
- British plan
- IMF Plan

Rescue plan-Cont

Government action

- 700 billion by the US
- Near a trillion by EU
- Etc.

Have not been implemented yet

Rescue Plan-Cont.

- Central bank's plan

Quick results

Reduce interest rates

Inject liquidity

Guarantees

Impact

- Global recession likely
 - Liquidity injection is not sufficient
 - Panic in markets remains
 - Speculation remains
 - Not sure Volume and instruments are adequate
 - Response by markets not assuring

Implications for Lebanon

- On Economy

World wide recession will affect economic activity in Lebanon

Production down- sectors decline

-Services decline

Unemployment up

Prices (inflation) down.

Balance of Payments

Exports of goods and services decline
Due to recession and rise in dollar/euro rate
21% to industrial countries
79% to developing and emerging markets

Import of goods and services decline
From recession and oil price
47% from industrial countries
53% from emerging and developing

BOP

- Interest on government debt could increase
As governments need to borrow massive amounts
- Transfers (grants) could decline

From Lebanese abroad

From government pledges- part of Paris3

BOP

- Capital flows will be affected
- Foreign direct investment declines as Global economy is in recession
- Other capital may decline except government
- Government will increase its borrowing
- To finance a larger deficit including from abroad

Government

- Revenues may decline or grow slower
- Grants decline
- Expenditure will increase to support the economy
- Subsidy to EDL declines as oil price declines
- Deficit will likely increase
- Borrowing will increase

Banks

- Net foreign assets 24%
With corresponding banks
- Claims on government 30%
- Claims on BDL 31%
- Claims on private sector 28%
- Equity -13%
- Net foreign assets are placed with corresponding banks in low risk placements

Banks

- Profitability of banks declines
- Non-performing loans increase-
Non performing loans ratio 6.8%
Provisioning 54.2%

Bank's placements in corresponding banks is relatively low risk assets

Banque Du Liban

December 2007

(in billions of LPs)

| | |
|---------------------|------|
| Net foreign assets | 3541 |
| Net domestic assets | 4657 |

Personal wealth

- Will decline from portfolio investments in international markets