

# Remittances in Lebanon: A Lebanese-Dutch Disease?

Mr Kamel Wazne  
Economic Expert

# Capital Inflows in Lebanon

- Capital inflows have a positive effect on the economy
- Capital inflows can take the form of:
  - Foreign Direct Investment
  - Foreign Aid
  - Remittances
- In Lebanon, capital inflows mainly take the form of remittances

# Remittances in Lebanon

- Remittances are the main source of capital to the banking sector
- It is argued that remittances are the backbone of the Lebanese economic and financial system
- Without remittances, the Lebanese model of government funding becomes unsustainable
- Remittances enter the banking system, then feed government financing needs, and the private sectors borrowings

# Remittances in Lebanon

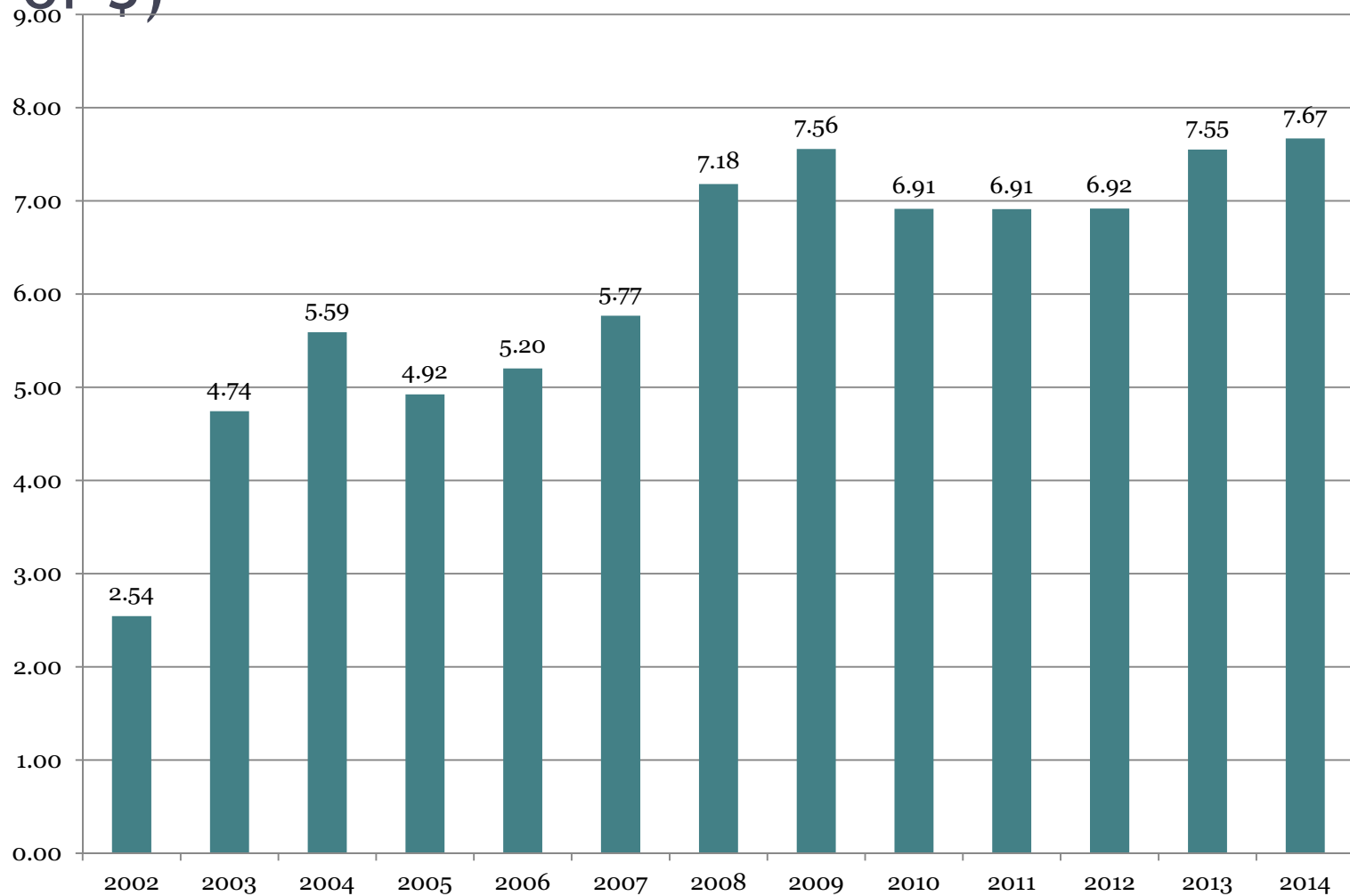
- Lebanon receives large amounts of remittances. An increasing trend but inconsistent growth rate
- The importance of these remittances is seen through their size to GDP. In 2014, Lebanon received more remittances than Russia
- Remittances in Lebanon are approximately 20% of the GDP, one of the highest in the world

# Remittances in Lebanon

However, some crucial questions arise:

- Are remittances actually good for the Lebanese economy?
- Can we consider remittances as a Lebanese Dutch Disease?
- Did remittances bring good or bad to the Lebanese productive economy?
- If bad, is it to be blamed on the banking sector that are misusing these remittances?

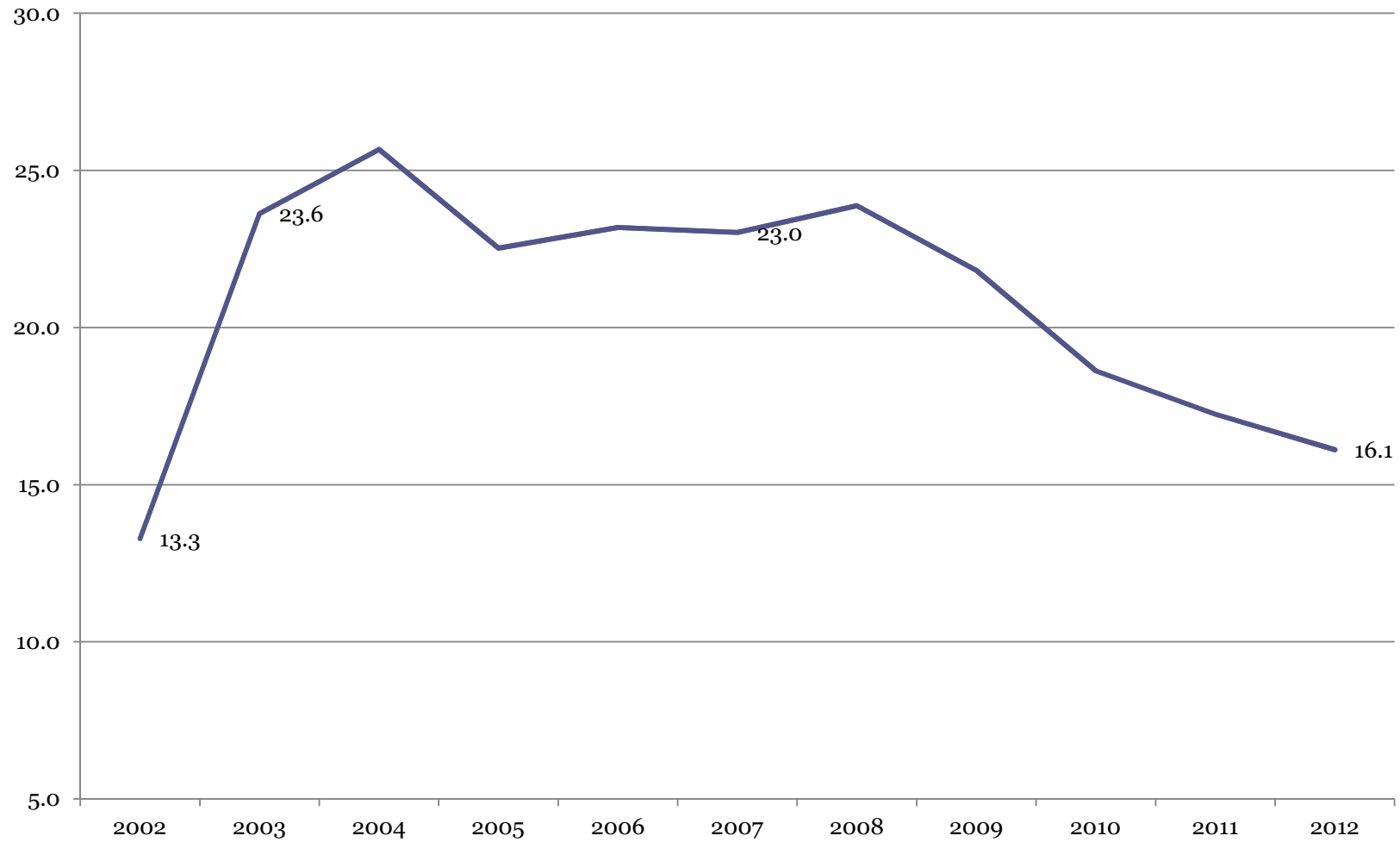
## Remittances in Lebanon 2002-2014 (in billion of \$)



# Remittances as % of Arab World

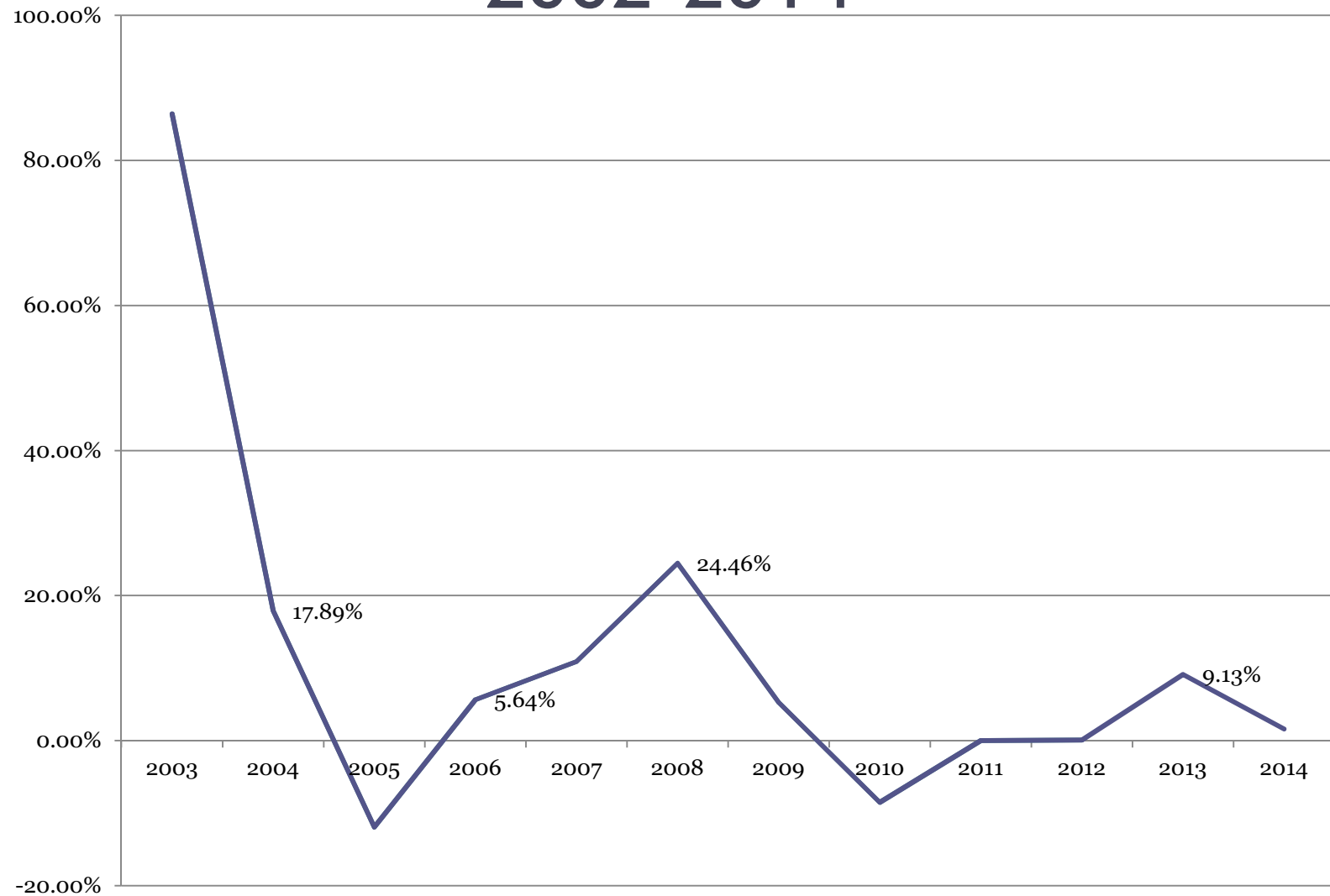


# Remittances as % of GDP

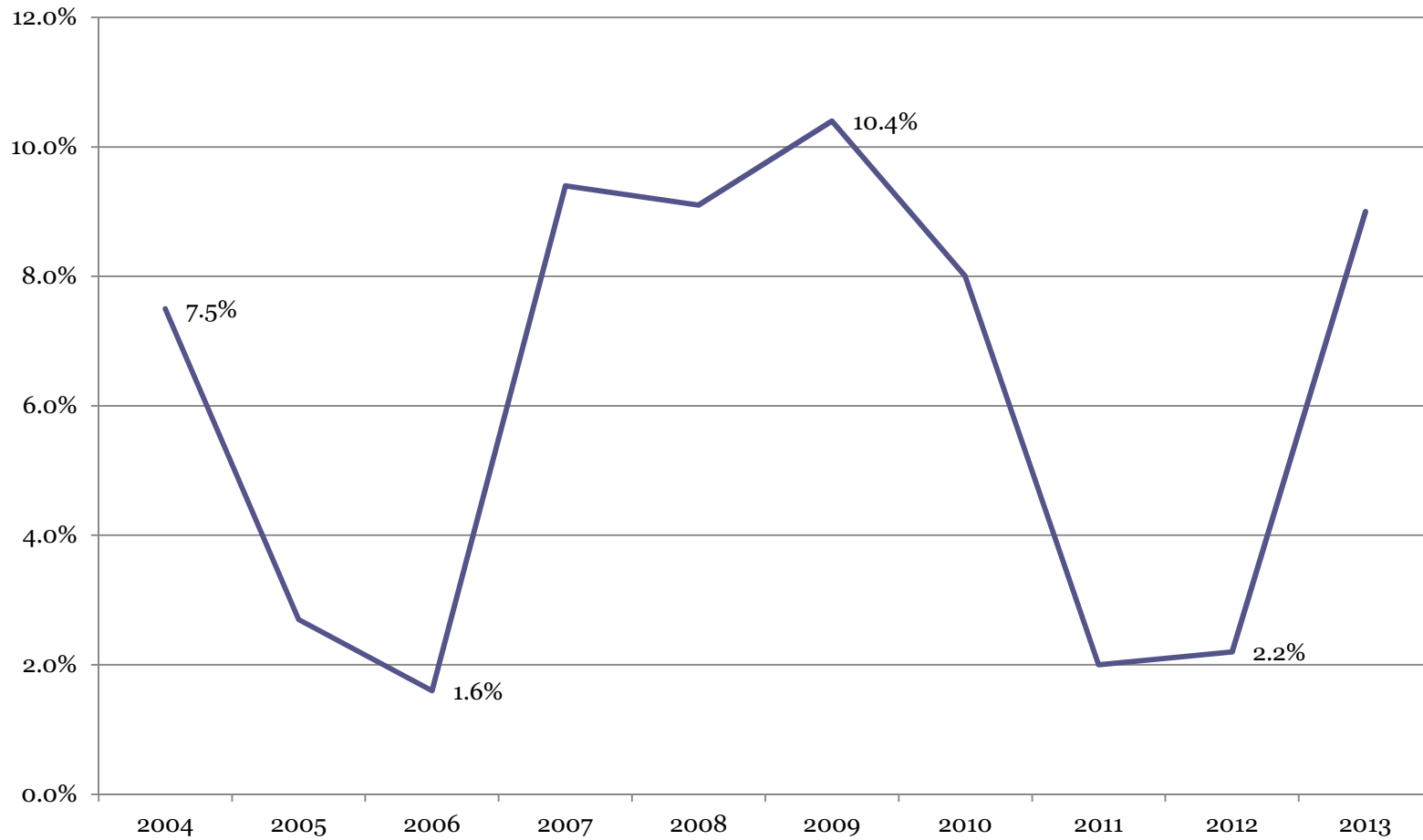




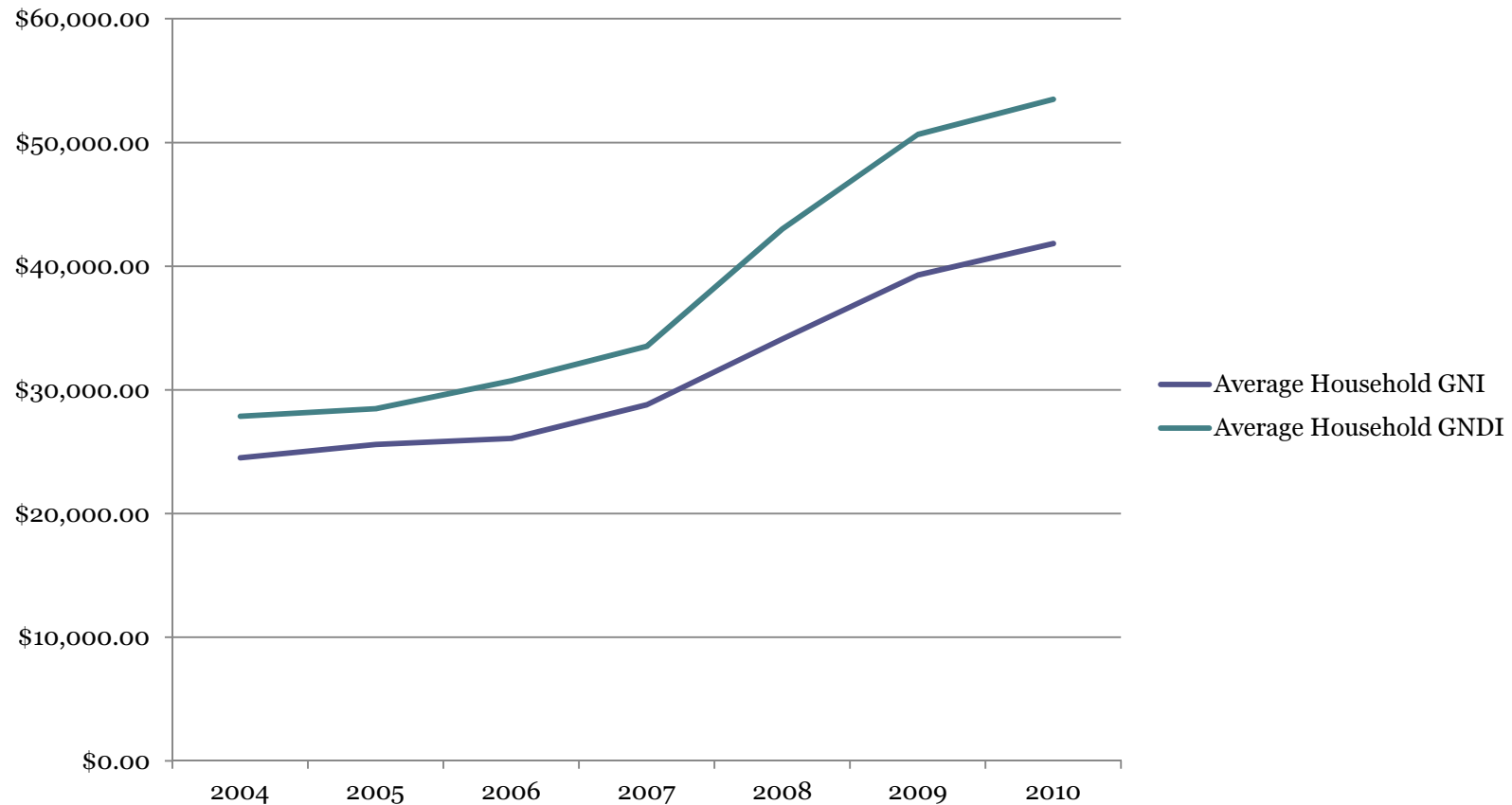
# Growth of Remittances in Lebanon 2002-2014



# Economic Growth 2004-2013



# Impact on Households

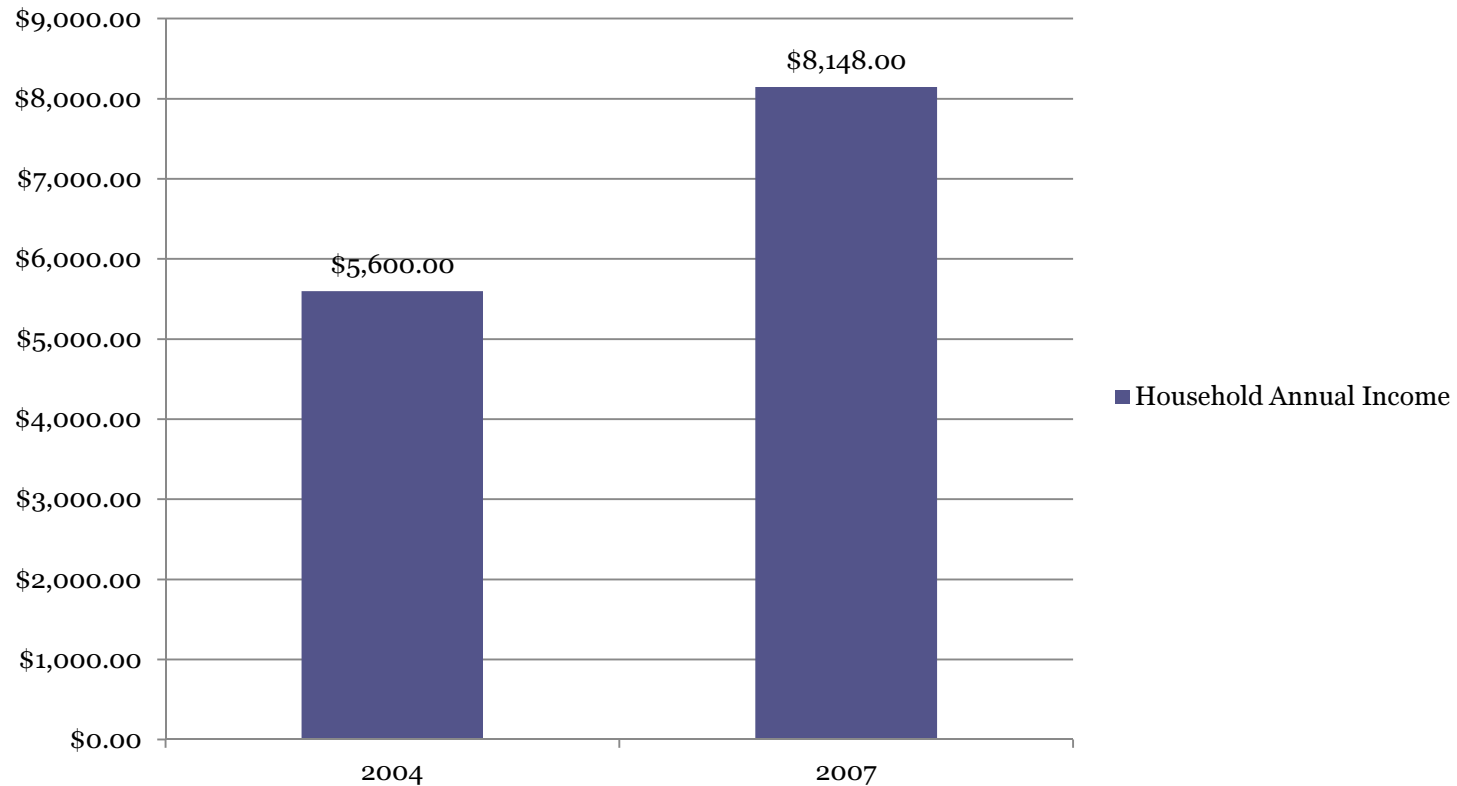


Economic growth was translated into higher average household income, mainly when remittances are taken into consideration. However, how does this translate into welfare and well-being?

These figures hide a dark picture behind.

# Impact on Households

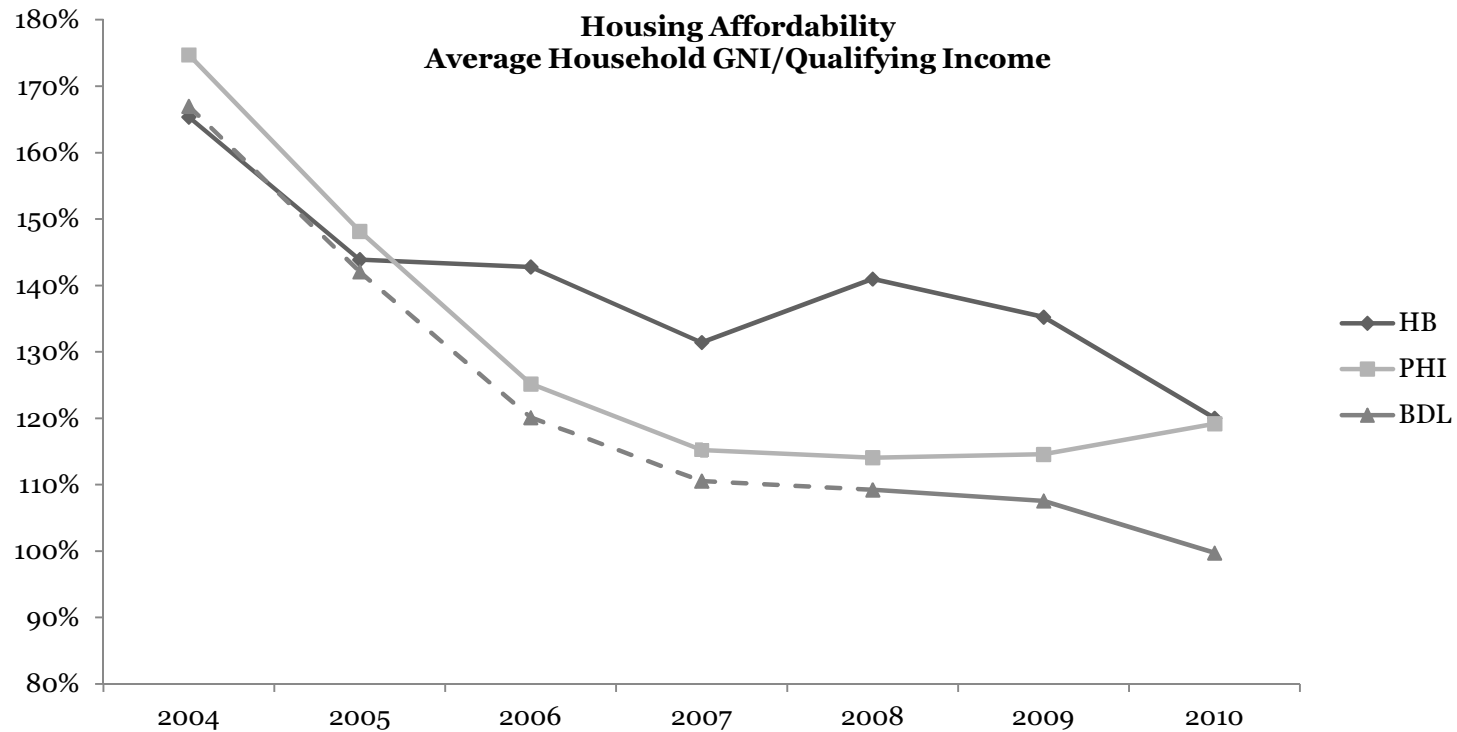
## Household Annual Income



The survey of the CAS shows that Lebanese households are not as well off as the previous aggregated figures show

# House Prices

A house priced at \$60,000 in 2004 increased to circa \$180,000 in 2010: **CAGR 20%**



# Inequality

- Out of 141 countries, Lebanon has the 3<sup>rd</sup> highest degree of wealth inequality in the world with a wealth GINI of 85.7 in 2012
- Housing Affordability has deteriorated sharply
- The PHI, HB, and BDL schemes are improving affordability but ruining individuals finances by generating an indebted population

# Property Prices and Productive Activities

- **Crowd-out effect:** From productive activities that are relatively less profitable to the construction sector and real estate sector (less agriculture and manufacturing, negative environmental impact)
- Higher property prices caused higher rental prices and higher operating cost to SMEs. As a result, there is less profitability and lower potential for further expansion. Slow economic expansion. Future growth prospects are reduced.

## Conclusion 1: Exclusive Growth

- Economic growth in Lebanon funded partly by the inflow of capital and remittances has caused a sharp increase in property prices
- High property prices have impoverished Lebanese households and crowded out productive activities



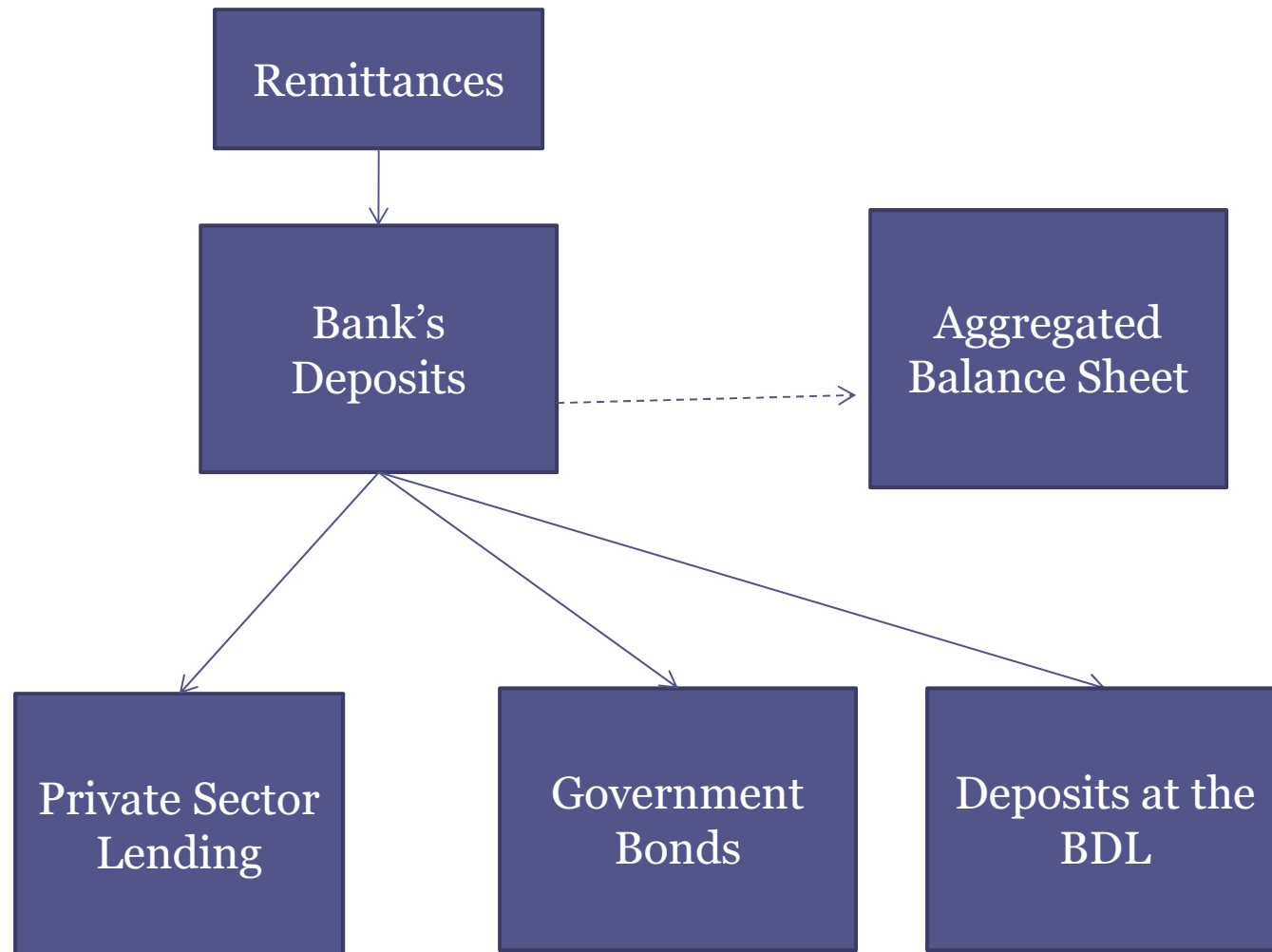
# Lebanese Banks Profitability

- Profitability versus efficiency
  - Lebanese Banks are profitable and make steady progress
    - In 2013, Lebanese Banks registered an estimated profit of \$1.6 billion
    - In 2012, Lebanese Banks registered a profit of \$1.5 billion (despite the Syrian Crisis)
  - However, can we actually say that they are efficient?
- The concept of financial efficiency reflects financing the economic sectors of the economy that are in most need of funding (i.e., infrastructure projects)
- Let's look at the main sources of profits of Lebanese banks

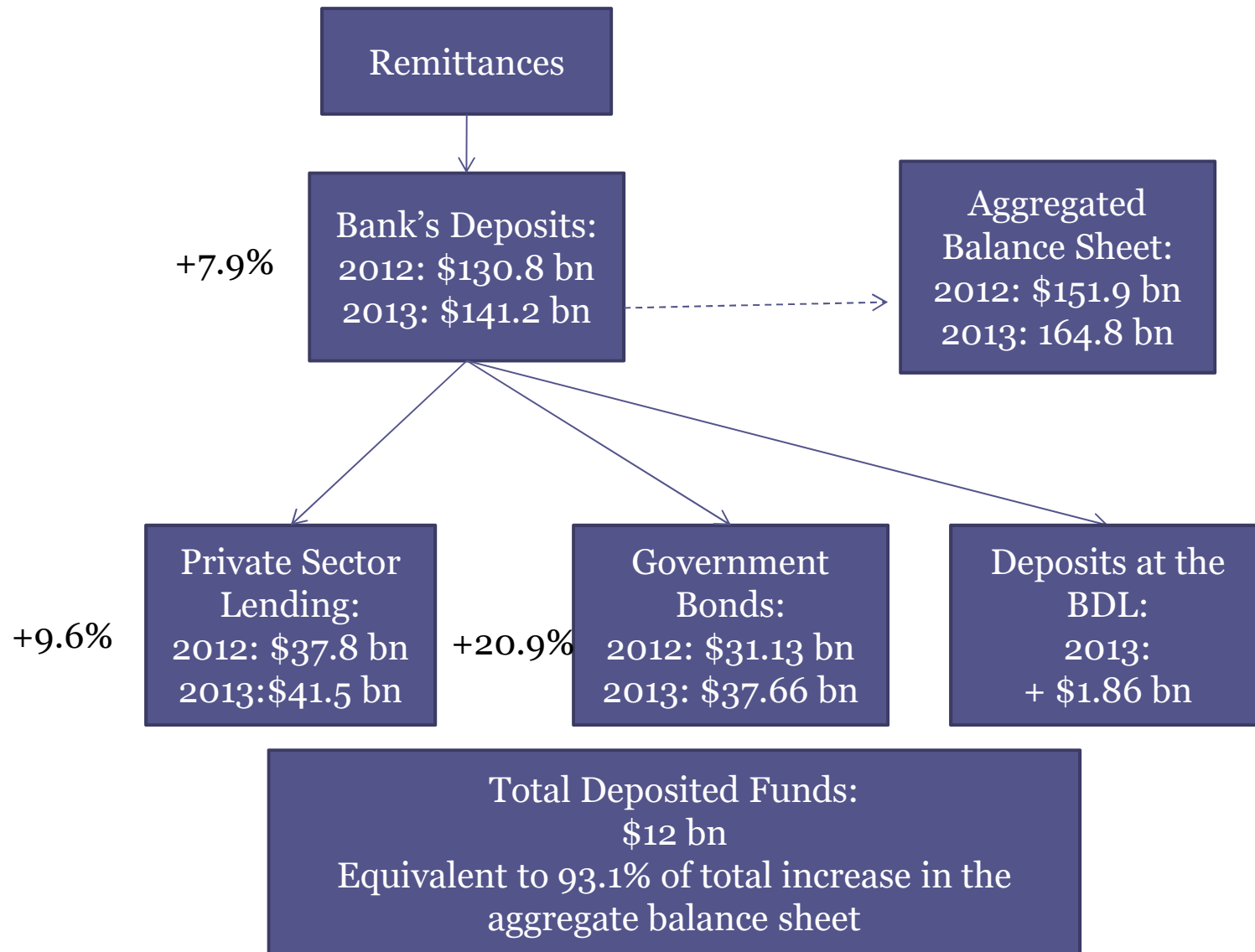
## Sources of Profits of Lebanese Banks

- We have a common Lebanese Model for all banks. At the same time, each bank has its own profit-making method. What is the Lebanese Model?
- According to Joseph Tarabay, former chairman of the Lebanese Banks Association, Lebanese Banks “are still running Arab Wealth”
- More generally, the Lebanese model is based “on running remittances”

# Sources of Profits of Lebanese Banks



# Sources of Profits 2012-2013



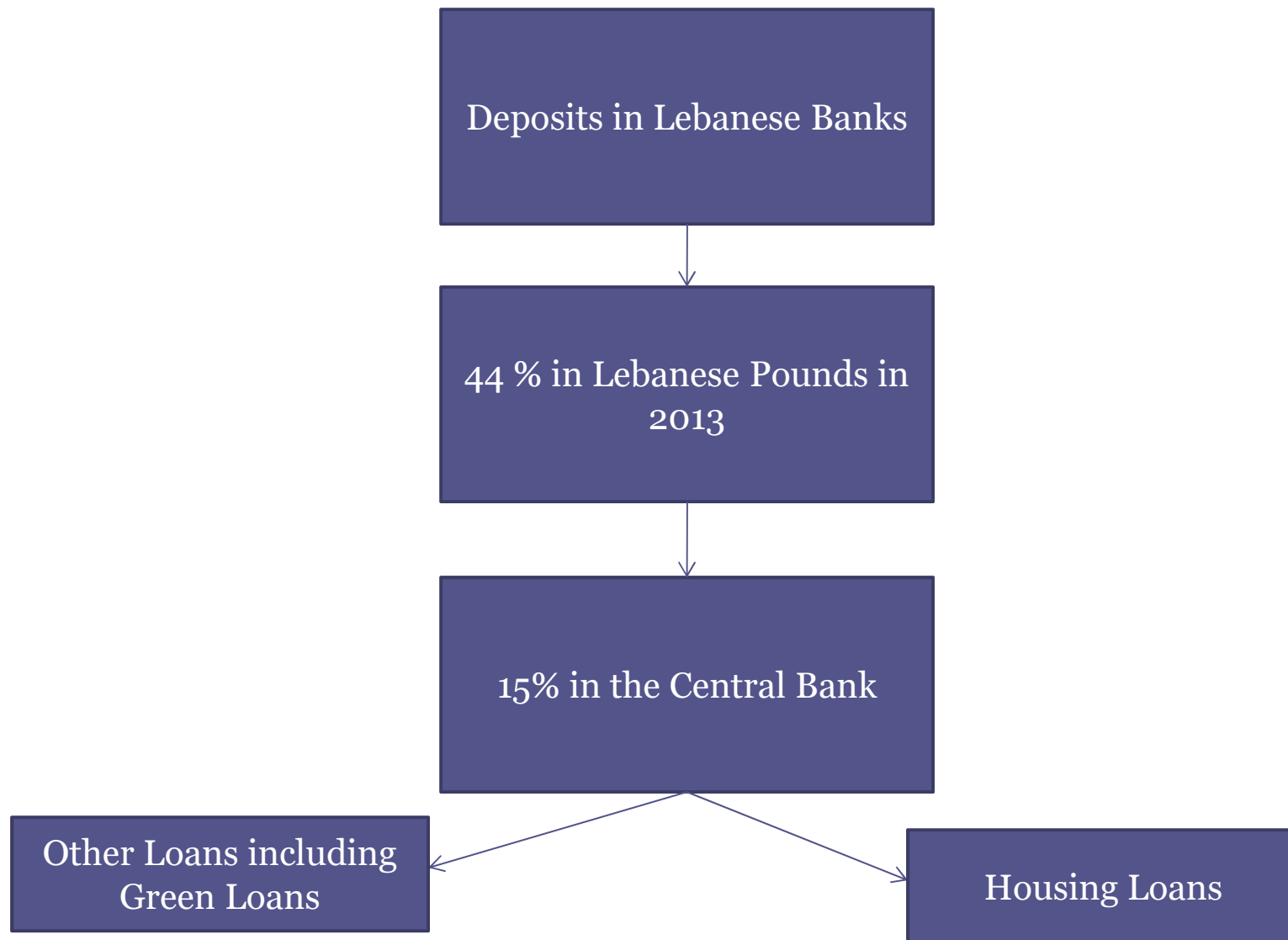
## Profits out of the Three Portals

- In Lebanese Pounds and in Dollars, net profits registered \$1550 million
- Profits Margins
  - In dollars: 1.3%
  - In Lebanese Pounds: 1.26%
- This suggests that total profit from the total deposit portfolio, after calculating the reserve requirement is at least \$1.6 bn in 2013

## The Recent Trend in Sources of Profits

- The share of Treasury Bonds from the profits decreased in 2013
- At the same time, such decrease was compensated with an expansion in funding the economy – the private sector
- Another important source of profits is reserve requirements Exemptions and BDL loans to Commercial Banks

# Reserve Requirements Exemptions



## BDL Loans to Commercial Banks

- In 2013, the BDL offered LBP 2.2 billion (\$1.4 bn with a **1% interest rate**)
- In 2014, this was renewed since only \$ 800 million was used (mainly for housing loans)
- In 2015, the BDL is planning a \$ 1 bn stimulus



## Conclusion 2: Lack of Efficiency

- The Lebanese Banks main source of real profits are those originating from their daily transactions and individual lending (consumption)
- The Remaining profits are earned without effort, they are just on the books between the bank and the state, as well as reevaluation of the price of stocks and bonds based on historical prices instead of market prices
- In that sense, one could conclude that the Lebanese Model lacks efficiency. **Can we blame this lack of efficiency on the banking sector?**
- **Let's have a look at the Market of Loans to the private sector (The Lebanese Economy)**

# Financial Development and Economic Growth

- King and Levine (1993a, 1993b, 1993c) study 80 countries over the period 1960-1989
- They use four measures of “the level of financial development”
  - DEPTH: the size of financial intermediaries (%GDP)
  - BANK: the degree to which the central bank versus the commercial banks are allocating credit
  - PRIVATE: the ratio of credit allocation to private enterprises to total domestic credit
  - PRIVY: credit to private enterprises divided by GDP

# Financial Development and Economic Growth

- Financial systems that allocate more credit to private firms are more engaged in researching firms, exerting corporate control, providing risk management services, mobilizing savings, and facilitating transactions than financial systems that simply funnel credit to the government
- There is strong positive and statistically significant correlation between real GDP per capita and the extent to which loans are directed to the private sector.

# The Size of the Lebanese Banking Sector to the Lebanese Economy



One could argue that the Lebanese Economy is not capable to allow full operation of the banking sector, as such, banks have no alternatives but to lend the inefficient state

# The Structure of the Lebanese Economy

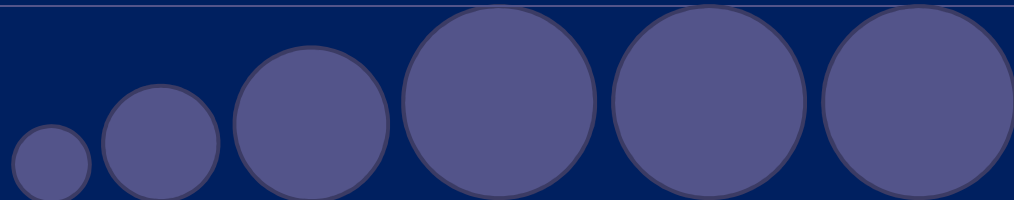
- SMEs (less than 50 workers) accounts for 97% of total enterprises in Lebanese (CAS, 2004)
- These SMEs employ 51% of the working population
- Most of these SMEs, approximately 44% are in the retail trade sector (limited valued added), Sales and maintenance of vehicles 11%, and services to individuals 5.5%
- SMEs with less than 4 workers account for 90.7% of total companies

# Structure of the Economy

**SMIEs 97%**

*SMEs in Lebanon grow in number, not in size*

**Large  
Firms  
3%**



# Constraints of SMEs Development

- Adam Smith: Division of Labor is limited by the size of the market. How?
- The expansion of some economic sectors create new business to cater for the firms of the expanding sector.
- As a result, more specialization, more productivity, and better output
- 
- Lebanon is a small economy in terms of market size. Expansion abroad is needed
- Firms should enter the outsourcing business for Gulf countries.
- However, SMEs blame the lack of sophistication and expansion to the lack of funding. Are businesses in Lebanon qualified for funding?

# Assessment of The Lebanese Economy

- **Competitiveness**

- Global Competitiveness Indicator in 2015

- 113<sup>th</sup> of 144 economies (Drop of 10 places, ahead of Egypt, Mauritania, and Yemen)

139<sup>th</sup>  
Institutions  
Pillar

122<sup>nd</sup>  
Infrastructure  
Pillar

143<sup>rd</sup>  
Macroeconomic  
Pillar

- Global Innovation Index in 2013

- 119<sup>th</sup> of 141 countries

- Technology Level

- Only 25.66% of SMEs use state of the art technology



# Assessment of the Lebanese Economy

- **Ease of Doing Business**
  - In 2015, the rank of Lebanon is 104<sup>th</sup> out of 189 economies (drop 2 places)
  - The business regulations for SMEs in Lebanon are cumbersome
  - Local businesses can thrive in economies where business regulation combines efficiency and quality
  - Examples of Worldwide Improvements: 10 years ago starting a business took 57 days in Senegal. Today it would take 6 days, just one more day than in Norway

# Assessment of the Lebanese Economy

- **Corruption Perception Index (CPI)**
  - 127<sup>th</sup> of 177 countries in 2013, one of the most corrupt public sectors in the World
- **Index of Economics Freedom of Heritage Foundation in 2013**
  - 91<sup>th</sup> of 177 countries
  - Lebanese scores poor on the rule of law and corruption

# Assessment of the Lebanese Economy

Indicator	Score
Global Competitiveness	2015: <b>113/144</b>
Global Innovation	2015: <b>119/144</b>
Ease of Doing Business	2015: <b>104/189</b>
Corruption Perception Index	2013: <b>127/177</b>
Economic Freedom	2013: <b>91/177</b>

# The Lebanese Economy: Activities

- Distribution of economic sectors:
  - Manufacturing 20%
  - Agriculture 4.6%
  - Services 75.4%

Services include banking and tourism

- Most of the productive economy is highly vulnerable to political and security considerations

## Conclusion 3: Poor Matching

- The Lebanese Economy is not ready to absorb the large funds that Lebanese Banks receive through remittances
- Large enterprises (50 and more workers) account for only 3% of total enterprises
- The economic performance of Lebanon is poor by international standards. Competitiveness is below the world average. SMEs can't grow and ace in such an environment.
- As a result, there is little room for financing productive activities

# The Problem

Lack of Loans to Productive Activity or  
Inefficiency of SMEs in Lebanon?

# CONCLUSIONS 1, 2, and 3

