Finance minister says restructuring is needed amid severe economic and financial turmoil

Lebanon is considering using depositors' money to salvage its crisis-hit banks as part of an overhaul of the sector following the country's first sovereign debt default.

Ghazi Wazni, finance minister, said the government was studying examples of other financial restructurings from Greece to Cyprus, with options including a bail-in, where a portion of deposits are converted to shares in the bank. Without such reforms, deposits were at risk, he said in an interview. "To preserve the money of depositors, you need banking restructuring," he said. Other measures being considered included freezing dollar deposits for up to six years before paying them back in Lebanese pounds and creating a fund of state assets that depositors have to buy into. "We have options," said Mr Wazni.#

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Long before coronavirus precautions forced much of Beirut to close down, Lebanon was mired in its worst economic and financial turmoil for decades. The country's economic model had relied on a supply of dollars to its commercial banks, who deposited them at double-digit interest rates in the central bank, which in turn bought government debt. But a severe foreign currency shortage led the fragile system to crash. With depositors panicking about losing their money, Lebanese lenders have imposed tighter restrictions on withdrawals and foreign transfers. While intended to stop a bank run, the capital controls have hurt already struggling consumers and businesses.

The banks are illiquid because more than half of their collective assets are locked in the Banque du Liban. Yet the central bank's foreign currency liabilities to the commercial lenders are more than double its foreign currency assets, leading rating agency Fitch to warn on Tuesday of an "increasing risk of depositor bail-in". If a bail-in is ordered, Mr Wazni suggested it might only affect the wealthiest account holders and said most depositors would be protected, adding that just 8.5 per cent of Lebanese bank accounts hold more than $200,000. But the idea of the government reforming the banking sector was rejected by Salim Sfeir, chairman of the Lebanon Association of Banks. "I address myself to our politicians," said Mr Sfeir, who is also chief executive of Bank of Beirut: "They better not interfere in the banking system." He added that this was a task that should be left to the central bank. Mr Wazni, an economist, is among the technocrats of Lebanon's new cabinet, formed this year after mass protests against Lebanon's postwar political elites brought down the previous administration in late 2019. The new government faces huge challenges, notably shrinking Lebanon's public spending, cutting the cost of paying interest on its debt pile, and curbing its massive current account deficit. For the past three weeks, Mr Wazni said the government had been assembling a "comprehensive plan" to rescue the economy, whose gross domestic product he estimated to have shrunk by 4-5 per cent last year. Although countries restructuring external debts often do so in conjunction with the IMF, Beirut has not asked the fund for anything beyond technical advice. But a full package — usually offering financial support if a government agrees to make economic reforms — is seen as a realistic route for Lebanon to make it out of the crisis and re-establish credibility with its creditors. "To solve our problem we need the support of international funding," acknowledged Mr Wazni. Even Hizbollah, the dominant Shia Islamist political bloc and terrorist-designated paramilitary movement, has signalled it would be open to an IMF package — if Beirut could secure favourable terms. While the government's "constructive" discussions with the IMF team represented "a first positive step", according to Mr Wazni, negotiations ahead could be tough. "There are many differences between our point of view and the IMF's point of view," he said. While the IMF would want sweeping increases to value added tax, according to Mr Wazni, the government would rather restrict rises to luxury goods. "We cannot take measures that will increase the suffering of the population," said Mr Wazni. Toufic Gaspard, a former IMF official and Lebanese economist, said that without an injection of outside capital, Lebanon's situation was "hopeless". Nafez Zouk, an emerging markets strategist at Oxford Economics, said: "Lebanon needs the IMF in order to establish credibility with bondholders. A local programme backed by the IMF would help anchor the negotiations on the basis of which debt relief is to be provided."

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