The Governor's promise: the reserves will not be touched

By Dr. Fadi Khalaf
Secretary General
Association of Banks in Lebanon

Dr. Wassim Manssouri took over the governorship of the Central Bank of Lebanon and found himself facing the needs of the State and its everlasting reliance on the depositors’ funds, which have been confiscated over the years. Dr. Manssouri came forward to assure the Association of Banks that he will not use a single dollar of the reserves, stating, "These are the depositors' funds."

Yes, using the depositors’ funds has always been and continues to be unacceptable, regardless of the excuses and explanations. In this regard, the Association of Banks had previously sent two strongly-worded letters on this matter to the former governor of the Central Bank of Lebanon, Riad Salameh, on April 1, 2021, and April 4, 2022. Additionally, a statement was issued on this matter on July 8, 2021. The solution presented by the governor was to return the funds in Lebanese pounds at a rate of 1500, should the banks insist on claiming their deposits from the Central Bank. It's worth noting that sacrificing the depositors' funds did not prevent the dollar from rising in value. Deposits were squandered in vain, and depleting the reserves proved ineffective in preventing the collapse. The failure was evident.

In front of the State’s persistence on continuing to deplete what remains of the reserves, a question arises: what will the State do if the last dollar of the depositors' funds in the Central Bank of Lebanon runs out? Will the State resort to the argument that necessities allow for exceptions and move to liquidating gold? And what comes after gold? All of this is to avoid implementing the necessary reforms and to ensure that the priority remains on keeping the holes in the basket. Who knows how many favoritisms benefit from these loopholes!!!

Today, Dr. Manssouri emphasizes the importance of enacting laws related to restoring the balance of the financial system and banks’ restructuring, as well as other laws essential for Lebanon's recovery. Without these laws, there can be no genuine reform or revival for Lebanon. Let's rally behind his efforts, hoping to see light at the end of the tunnel in the near future.

Preserving what remains of the depositors' funds at the Central Bank of Lebanon:

Before delving into what international conventions say on this matter, it's worth mentioning that researchers worldwide have never addressed the possibility of using depositors' funds to support the national currency. This hypothesis has never been raised, and none of them have even considered it. This is because central banks depend on their free reserves, which they have accumulated through their previous interventions in the foreign exchange market or through various mechanisms that do not involve the depositors' funds in any way.

When the International Monetary Fund classified the Lebanese situation as unprecedented, it was based on the fact that there has never been a use of depositors' funds in the manner witnessed in Lebanon. In our personal belief, the Lebanese situation will become a new research topic studied in universities and addressed by researchers around the world.

On the other hand, advocating for preserving social security at the expense of depositors contradicts logic. Unless the principle of wealth redistribution, as applied in countries following Marxist philosophy, prevails – which is not the case in a country where public services are absent and the economy relies on individual initiative. So don’t kill individual initiative, as it alone has the potential to relaunch the economic activity.

The State, along with its institutions, has consumed the vast majority of depositors' funds, resulting in equal poverty and hardship among them. We have become a country where the deposits of the poor are taken to give to the people, or perhaps even to the privileged few. Even Karl Marx, if he were to hear of this theory, would stir in his grave. The little that remains in the Central Bank should be exclusively used to repay the small deposits in cooperation with banks, without any debate on the matter and under no pretext, even the pretext of stabilizing the exchange rate.

Maintaining the exchange rate:

Before discussing the drawbacks of using depositors' funds to maintain the exchange rate, it's important to remember that the exchange rate of the dollar has risen from 1500 L.L. to 90000 L.L. (times 60) in the first 42 months of the current crisis. In comparison, during the 1980s, the dollar increased by 11 times in the first 42 months of the monetary crisis, and at that time, the State did not use a single dollar of the depositors' funds. Have the officials surpassed in 42 months the negative financial effects of the war by six times (11 times back then, compared to 60 times currently)?

On the other hand, some find comfort today with the dollar exchange rate being at 90000 L.L., because they witnessed it at 141000 L.L. in March and have come to accept 90000 L.L. in July on the basis that they had to witness the worst to accept the current situation. The latest increase brought up the dollar from 40000 to 141000 and it was natural for it to technically return halfway to digest its increases. We've seen this before after the rise from 1500 to 10000 before it returned to 6000 L.L. Similarly, it did so after rising from 15000 to 35000, only to return to 22000 L.L. The exchange rate market needs a corrective phase after major increases, followed by periods of "digestion" where everyone adapts to the high prices. Therefore, the recent decline would have occurred in any case, even if the Central Bank hadn't intervened. The Central Bank prolonged the corrective period, but at what cost?

How did the Central Bank deal with market techniques?

Under his previous governing body, the Central Bank relied on the technique of confronting the general trend of the exchange rate of the dollar against the local currency for many years. This trend is usually determined by the country's economic indicators. To implement the technique of fighting the general trend, scientifically known as "leaning against the wind" technique, there are conditions that cannot be bypassed, including:

- The use of the "leaning against the wind" technique is limited to facing fluctuations resulting from unexpected and temporary events whose effects are expected to dissipate in a short period.
- Using the "leaning against the wind" technique for extended periods depletes the Central Bank's reserves, thereby weakening its ability to confront market speculators.
- The role of central banks is to focus on addressing sharp fluctuations in the exchange rate around the general trend of the currency, rather than attempting to break the general trend itself, which is defined by the country's economic situation.
- Among the conditions for the success of the "leaning against the wind" technique is that the Central Bank maintains a high level of foreign currency reserves, which contradicts depleting a part of the reserves to fund the State's foreign currency needs.

For more details on this subject, please refer to the article written by the Secretary General in March 2022 entitled "Depletion of Reserves and Interventions of the Central Bank of Lebanon According to International Standards."https://www.abl.org.lb/Library/Assets/Gallery/Documents/KALIMAT%20ADDAD%20MARCH%202022.pdf

It is now time for the State to realize the impossibility of continuing the policy of buying time and using the “leaning against the wind” technique, and easily depleting the remaining depositors' funds. In addition to the harm it is causing, it will certainly not ensure the exchange rate stability as long as the required reforms are not implemented.

In conclusion:

Tampering with the placements of banks at the Central Bank of Lebanon has not been and will not be the solution; in fact, it will worsen the crisis instead of resolving it. Everyone should know that the exchange rate can only reflect the economic reality, and we rely today on the new governor, Dr. Wassim Manssouri, hoping that he will succeed in leading us out of the dark tunnel.

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