مصرف لبنان
BANQUE DU LIBAN

Regulatory - Socioeconomic Renovation in Monetary Policy

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I. Introduction

Your excellencies, ladies and gentleman,

It is such a pleasure to be here to address an esteemed audience on such a contemporary significant topic that encompasses two crucial notions: resilience and prosperity.

As a central banker, the question that I would like to pause when discussing resilience and prosperity is: how can central banks deliver credible commitment to economic prosperity and, at the same time, be "emergency institutions" to innovatively sustain financial resilience?[i]

In order to answer this question, we should develop a deep understanding of the delicate balance that characterizes monetary policy. In my remarks today, I will highlight some macroeconomic facts that foster the need for balance in monetary policy, and then I will briefly dwell on Banque Du Liban's (BDL) dual mandate as a renovation approach to this balance, before concluding with some challenges that face Arab regulatory - socioeconomic renovation in monetary policy.

II. The Macroeconomic Outlook: Need for Balance

A decade after the burst of the global financial crisis, we can clearly sense that it is still severely impacting the global economic landscape in developed, emerging, and developing economies alike. On the global level, the phenomenon of economic secular stagnation is still affecting the real economy, exhausting quantitative easing policies that led to negative interest rates, along heightened uncertainties in the global political economy. All of these factors have exacerbated economic slowdown and socioeconomic disparities. Eventually, what once served as remedial cash flow reserves from emerging markets in the period of the financial crisis is now, more or less, paralyzed.

At the regional level, the political and security turmoil caused by various wars and conflicts, regional unrest caused particularly by the spillover risks from the Syrian crisis, the humanitarian refugee crisis, estimated at 11 million internal and external refugees, of which six million are external[ii], and the drop in oil prices, have all led to severe macroeconomic and socioeconomic-developmental drawbacks. This has been mostly evident in the deteriorating aggregate demand, slowdown in economic growth estimated at 2.6 percent in 2017, transformation of a huge fiscal surplus in 2010 into a deficit of $285 billion in 2016[iii], and deficit in current-account balances for many Arab countries[iv], in addition to the austerity measures of oil-producing countries. In effect, the main economic indicators, namely foreign trade, tourism, investment, and consumption, have been steadily decreasing since 2011.

This global and regional socioeconomic and financial turbulence has emphasized the necessity for stimulating the unconventional role of monetary policy. This role has proven to be inevitably efficient in closing the socioeconomic and fiscal gaps through developing essential tools to support the government in creating the necessary conditions for sustainable growth, providing the potentials to revitalize the labor market, reinforcing social and environmental security, and promoting economic and human development. This role is based on the delicate regulatory - socioeconomic monetary balance: on one hand, the monetary authority must preserve the credibility of its commitment towards the utmost national economic and monetary interests, and abide by the mission assigned by the constitution as a regulatory authority, within applicable laws and regulations. On the other hand, this authority is obligated to participate efficiently in facing and resolving unforeseen economic crises and must also act as necessary to preserve economic security, particularly on the monetary and financial level, as an autonomous authority that has sufficient maneuverability in handling and adapting effectively and efficiently the available resources.[v]

The dilemma that this balance introduces is the tension between the two premise extremities: the first, stresses on the regulatory perspective of the central bank, which is bound by rigid constitutional and systematic monitoring. The second, emphasizes the significance of the central bank's independence and flexibility, as a crucial condition for practicing the very essence of its mission as a monetary authority, i.e. preserving monetary, financial, and economic resilience, particularly in times of crisis. The resolution of this apparent conflict is approached outside the normal scope of economic research and policymaking through dynamic and contested debate among political theorists and constitutional scholars.[vi]

No matter what outcomes or regimes this debate will generate about the nature, acceptability, and inevitability of the monetary "emergency powers"[vii] exercised by central banks, we believe that there are certain financial and socioeconomic standards and pillars that should underline these unconventional policies, and that act as renovators for them. I will highlight these standards through Banque Du Liban's unconventional monetary initiatives and through certain notions that constitute challenges for the Arab monetary policy in this context.

III. BDL's Unconventional Transmission Mechanisms for Socioeconomic Growth and Development

In light of political and socio-economic upheavals in the Arab region and its spillover repercussions on the Lebanese scene, the Lebanese economy has witnessed a relative slowdown in activity, with foreign trade and tourism receipts being adversely affected while investment and consumption having slowly, but steadily, declined. Consequently, BDL has resorted to unconventional financial engineering tools that benefit the economy and society. These tools include the following:

First, *the provision of stimulus packages*. The aim of these packages is to stimulate internal demand and sustain the country's growth and job creation potential. The stimulus packages took the form of exemptions in the required reserve ratio and soft loans extended to Lebanese banks in order to boost lending activity and fuel economic growth. These packages, extending from 2013 through 2017, and amounting to an annual average of $1 billion, proved to be successful through contributing by 50 percent to the real GDP growth.

These included incentives to support housing, education, renewable energy projects, innovative projects, research and development ventures, entrepreneurship, and other productive sectors of the economy.

Second, *launching knowledge economy*. BDL has placed additional focus on targeting the knowledge industry, as being considered a strategic comparative advantage for the Lebanese economy. Lebanon's highly qualified human capital is apt to effectively turn innovative ideas into successful businesses, creating room for new employment opportunities, therefore expanding the country's GDP and ensuring sustainable development. Accordingly, BDL issued Circular 331 in 2013 to encourage Lebanese banks to invest in the equity capital of startups, incubators, accelerators, and other companies working in the knowledge economy. Through innovative scheme we made available around $600 million to support creativity and innovation.

Third, *adopting a multipurpose and multidimensional financial engineering*. Based on the continuous critical economic and financial situation, BDL deemed appropriate to pursue its unconventional monetary initiatives, by adopting an additional multipurpose financial engineering that combines the objectives of preserving monetary and financial stability, maintaining Lebanon's solvency, and boosting local demand and economic activity. The impact of this financial engineering was multidimensional: strengthening BDL's foreign-currency assets, consolidating the capital base of Lebanese banks, increasing liquidity in local currency, improving the public debt profile and the credit rating, improving the balance of payments, and raising the inflation rate to the required targeted level.

IV. Challenges Facing Arab Regulatory - Socioeconomic Monetary Renovation

In accordance with our experience in unconventional monetary policy, we perceive that are several challenges facing required renovation in the Arab regulatory - socioeconomic monetary balance. They can be summarized as follows:

First, *practicing macro-prudential supervision*. In addition to ensuring the resilience of individual financial institutions through more equity capital funding, macro-prudential supervision serves at ensuring the resilience of the system as a whole through implementing two mirror-image functions: to protect the financial system from the destabilizing developments of the economy, and to protect the economy from the excesses of the financial system.[viii]

Second, *actualizing synergy between financial regulation and monetary policy*. As financial regulation and monetary policy were traditionally seen in isolation, the new challenging focus is to analyze them complementarily together, in light of the interrelatedness between financial systemic risks and disruptive implications on output and price stability.[ix]

Third, *popularizing finance through enhancing financial inclusion and financial capability*. Financial inclusion and financial capability should be practiced with a prioritized view of promoting economic and financial wellbeing, as well as sustainable economic growth and financial stability. Hence, serving this purpose, financial inclusion involves the process of promoting affordable, timely, and adequate access to regulated financial products and services, and broadening their responsible use by all segments of the population, through the implementation of tailored existing or innovative approaches, including financial regulation, financial education, and financial consumer protection.[x]

Fourth, *committing to the delicate balance between financial inclusion and financial credit control*. Accordingly, this balance aims at enhancing financial inclusion and its benefits in facilitating consumption and price stability on one hand, and the control of extensive borrowing and the consequent credit risks that threaten social stability on the other. Thus, this necessitates the formulation of a balance between debt financing and capital financing. The formula here implies that financial inclusion should be enhanced with the development of financial control, but without constraining financial innovation.[xi]

Fifth, *addressing monetary renovation through catalytic central banking*. This catalytic role encloses three fronts: supply-side, demand-side, and financial infrastructure.[xii] Moreover, a comprehensive catalytic central banking should be a top-bottom, bottom-up approach that is based on four corner stones: the synergetic financial inclusion strategy applied by the central bank, the enabling stakeholders that include the market forces and the consumers, the compliance and governance frameworks, and the international institutions and organizations.[xiii]

Sixth, *mitigating the costs of compliance and de-risking*. Mitigating the costs of compliance and de-risking serves the goal of regulatory - socioeconomic monetary renovation since it tackles both financial stability and social security. This can be approached through tailoring regulatory decisions that harmonize between the incentives for financial intermediaries, the safeguarding of the interests of consumers, the restrictions of correspondent banks, and thus abiding with compliance requirements.

Seventh, *implementing monetary practices that target sustainable growth and development*. In this context, initiatives should be launched to ensure that the incentives of financial intermediaries are in alignment with the objective of upholding the economic interests in growth, employment, and development of the consumers, economy, and community as a whole.[xiv]

Eighth, *aligning between the sustainability of economic growth and development, and the independence of development*. Promoting genuine sustainability of economic growth and development requires securing the conditions of independent development. Hence, the monetary policy should contribute in providing these conditions, including: a productive economy that curbs rentier trends, knowledge and technology, participative democracy, human capital, accumulating national provisions, regional integration, economic diversification, industrialization, and anti-corruption good governance.[xv]

Ninth, *enhancing the strategic interaction with the fiscal authority*. This strategic interaction is vital for the monetary authority to combine credible commitment with effective crisis management, hence contributing in improving the efficiency of real economy.

Tenth, *applying transparency that endorses accountability*. There should be sufficient transparency to permit accountability for the central bank's stewardship of the regulatory – socioeconomic monetary system and for any legislators' formulation of that system, to ensure optimal democratic legitimacy.[xvi]

V. Conclusion

Briefly set, meeting all these challenges should flow into a holistic vision for formulating a regulatory - socioeconomic renovation in monetary policy. This renovation incorporates promoting economic and financial wellbeing, sustainability of both growth and independent development, and monetary and financial stability.

Thank you.

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