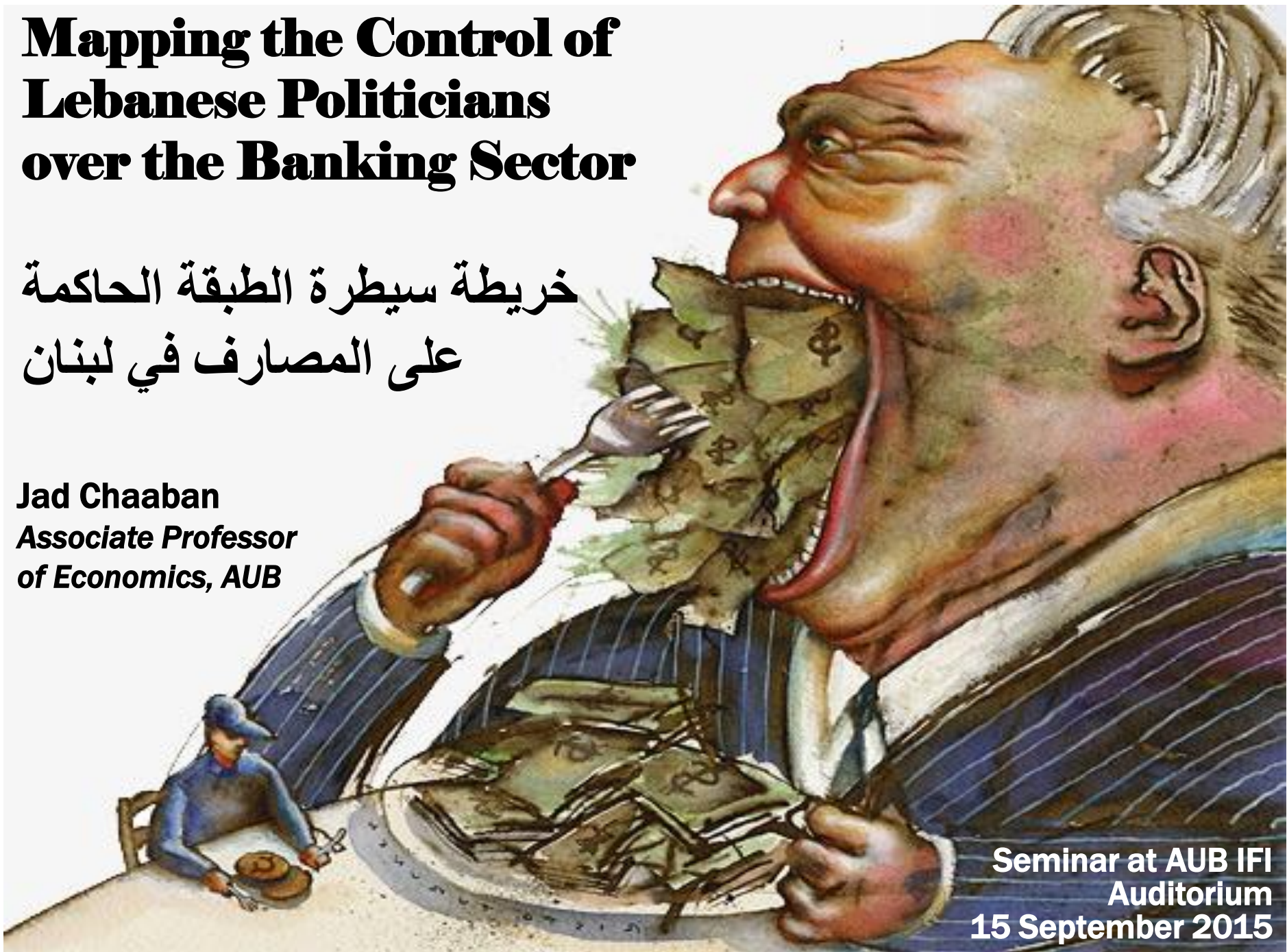


Mapping the Control of Lebanese Politicians over the Banking Sector

خريطة سيطرة الطبقة الحاكمة
على المصارف في لبنان

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Auditorium
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Outline

1. Background and objectives
2. Research Methodology
3. Data Sources
4. Main Findings

Note: *Work in progress*. The project is part of a wider regional initiative entitled “The Political Economy Determinants of Private Sector Dynamism in the Middle East”, coordinated by the Economic Research Forum (ERF). The contents and recommendations do not necessarily reflect the views of the ERF, or any other institution the author is affiliated with.

I would like to thank Antoine Dib for excellent research assistance.

Background and objectives

- **Lebanese banking sector one of the biggest in MENA: Assets US\$ 199 billion in 2013, 440% of Lebanon's GDP**
- **Extraordinary influence on monetary, fiscal, and other government policies**
- **Lebanese banks have been quite close to the country's ruling apparatus, often sustaining clientelistic networks (Moore, 1987) and heavily intervening in monetary and exchange rate policy (Hakim & Andary, 1997, Dibeh, 2002)**
- **Yet empirical evidence on the extent to which Lebanon's banks are dominated by a crony form of capital is non-existent**
- **Two objectives:**
 - **Map the ultimate shareholders of Lebanese commercial banks and identify their linkages with the ruling class**
 - **Analyze the impact of elite capture on the efficiency of the banking sector**

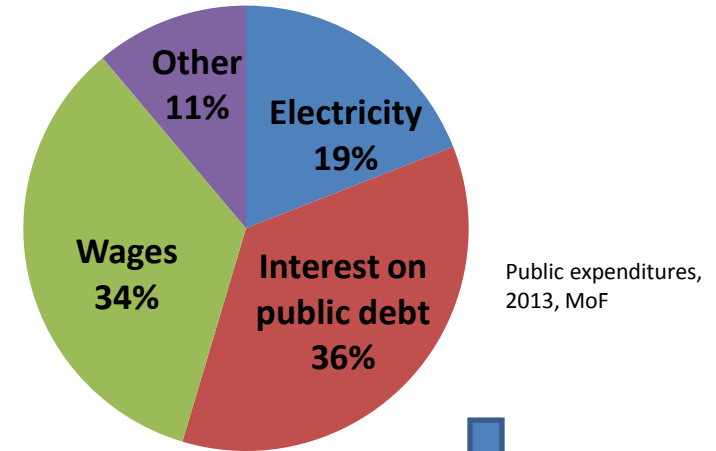
Lower bound estimates of true size of influence!

Position held by banks' representatives

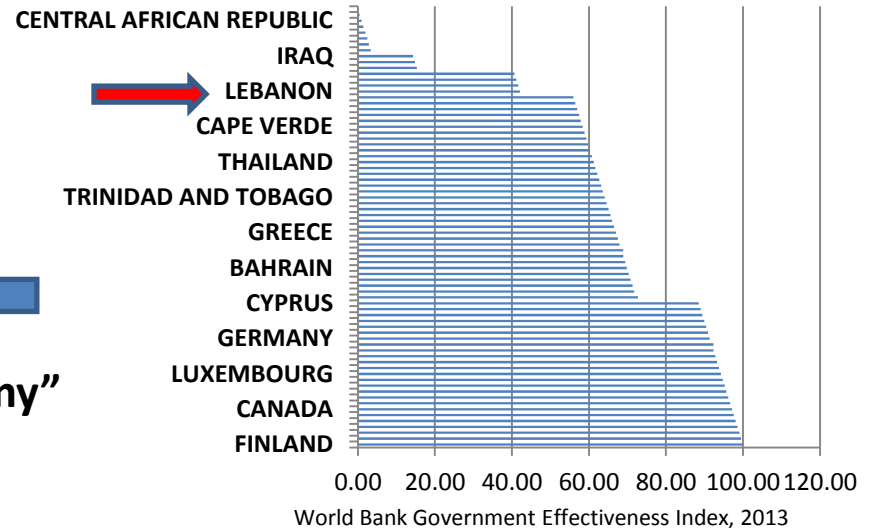
1. "Public services are very bad"



2. Because government budget swallowed by wages and EDL



3. Because politicians are corrupt & inefficient



4. Therefore banks step in to help the economy"

Lebanese banking sector

- 54 commercial banks, of which 20 control 99% of sector assets
- Highly concentrated: Top 15 banks (Alpha Group) control 96%

Bank short name	Year established	Listed on Beirut Stock Exchange	Assets USD billion Dec. 2013	Share in total assets
Bankaudi	1930	Y	41.97	0.21
Blombank	1951	Y	27.99	0.14
Byblosbank	1950	Y	19.04	0.10
Fransabank	1921	N	16.97	0.09
BankBeirut	1963	Y	14.97	0.08
Bankmed	1970	N	13.79	0.07
SGBL	1953	N	12.94	0.07
BLF	1967	N	11.30	0.06
Creditlibanais	1961	N	9.17	0.05
BLCbank	1950	Y	5.14	0.03
BBAC	1956	N	5.11	0.03
IBL	1961	N	4.73	0.02
FirstNational	1996	N	3.55	0.02
Creditbank	1981	N	2.64	0.01
AlMawarid	1980	N	1.70	0.01
MEAB	1991	N	1.68	0.01
Fencia	1959	N	1.52	0.01
LebaneseSwiss	1962	N	1.50	0.01
BEMO	1964	Y	1.48	0.01
ELB	1964	N	1.45	0.01

Concentration ratios	Value
Cr3	45%
Cr5	61%
Cr10	87%
Cr15	96%

Research Methodology

- **Ownership mapping**
 - Drawing up a comprehensive list of each bank's ultimate owners (Morck et al., 2011, Caprio et al. 2007)
 - Ultimate owners are state organs or biological persons, and a threshold of 5% is used to identify controlling shareholders (as per Lebanese Law)
- **Once ultimate owners are identified by backward iteration (examining each corporation's owners), a linkage between these owners and political powers is established**
 - **Five levels of linkages with political elites (scale from highest to lowest):**
 - 5. Direct: Person is currently a member of Parliament or the Government
 - 4. Indirect1: Person was MP/minister/public official
 - 3. Indirect2: Person's family member is a current or former politician
 - 2. Indirect3: Person has close ties to local or foreign political elites
 - 1. Nolink: no linkages with politicians
- **The composition of the banks' Board of Directors is also explored to construct an additional variable for political influence via the bank's management**

Research Methodology

- **Bank-level financial efficiency and performance indicators**
 - Ultimately impacted by the ownership structure
 - Non-performing loans (a measure of favoritism towards unqualified borrowers) and share of treasury bills held (a measure of exposure to sovereign risk)
 - **Other profitability and operational indicators:**
 - **Neti:** Net interest Margin.
 - **ROOA:** Returns on assets.
 - **ROAE:** Returns on equity.
 - **Cost_br:** Cost per average branch in Bil LBP (*Total Non-Interest Expenses/ Number of Branches*).
 - **Staff_av:** Staff expenses per average staff in US\$. (*Personnel Expenses/Number of employees*).
 - **Staff_exp:** Staff expenses to general operating expenses ratio (*Personnel Expenses/ Total Non-Interest Expenses*).
 - **Cost:** Cost to income ratio (*Total Non-Interest Expenses/ (Other Operating Income + Net Interest Revenue)*).
 - **Cost_a:** Cost to average assets ratio (*Total Non-Interest Expense/ Average assets*).
 - **Dividends:** Total amount paid as dividends in Bil LBP.
 - **Equity:** Total equity in Bil LBP.

Data Sources

- **Ownership data:** Bankscope database, ORBIS database, Lebanese Official Commercial Register, Banks' websites
- **Political affiliation:** Government websites, local media
- **Financial data:** Bankscope, Bilanbanques 2014
- **Variables include:**
 - **Assets:** Latest total assets in mil LBP.
 - **Branches:** Number of branches.
 - **Emp:** Number of employees.
 - **Sover:** Sovereign exposure, ratio of *(LB treasury bills LL + Eurobonds + BDL certificates deposits in LL and FC) / deposits*. All of them are converted into LBP before calculating.
 - **Loan_dep:** Loans to deposits ratio.
 - **Loan_bad:** Ratio *(substandard loans + doubtful loans) / gross loan*.

Ownership mapping

- Example of Bank Audi

Shareholder name	Share	Type
Deutsche Bank Trust Company Americas	29%	Foreign bank
FRH Investment Holding SAL	10%	Holding LB
Audi Family	7%	Persons
Sheikha Suad Hamad Al Saleh Al Homaizi	6%	Persons (GCC)
Sheikh Dhiab Bin Zayed Al-Nehayan	5%	Persons (GCC)
Levant Finance 2 Limited	5%	Holding UK
Al Sabbah Family	5%	Persons (GCC)
Executives and Employees	4%	
Investment and Business Holding S.A.L.	3%	
Al Hobayeb Family	3%	
International Finance Corporation I.F.C	3%	
Ali Ghassan El Merhebi Family	2%	
Said El-Khoury Family	2%	
Others	17%	



Mr. Fahd Hariri 100%

Source: Lebanese Official Commercial Register

Sources: Bank Audi and Bankscope

- Example of BankMed

Shareholder name	Share	
Groupmed Holding SAL	100%	Holding LB



Shareholder name	Share
Mr. Saadeddine Hariri	42%
Mr. Ayman Hariri	42%
Mrs. Nazek Hariri	16%

Source: Bankscope

Source: Lebanese Official Commercial Register

Main Findings

Individuals closely linked to political elites control 43% of assets in Lebanon's commercial banking sector

- **18 out of 20 banks have major shareholders linked to political elites**
- **4 out of the top 10 banks have more than 70% of their shares attributed to crony capital**
- **Substantial control over the banks' Board of Directors, including its chairperson (15 out of 20 banks have the chair of the Board linked to politicians)**

Families of current or former politicians control 32% of the sector's assets. 8 families control 29%, with total equity more than 7 billion \$

Family (+link)	Equity in mill. US\$, 2013
Hariri (former PM, current MP)	2,517
Kassar (former minister)	2,382
Sehnaoui (former ministers)	1,380
Raphael (former minister)	724
Assaf (former minister)	211
Habib (former MP)	58
Kheireddine (former minister)	24
Hrawi (son of President)	17
Total	7,313

Source: Author estimates based on BankData and ultimate shareholders identification. Equity refers to consolidated equity in the controlled banks as of Dec. 2013.

Some examples



- Saad Hariri, Former PM, current MP, head of Future Movement
Parliament block : 800 million US\$ equity, direct shareholder of BankMed



- Adnan Kassar, Former Minister of Economy, Former head of Chamber of Commerce
1.2 billion US\$ equity, direct shareholder Fransabank

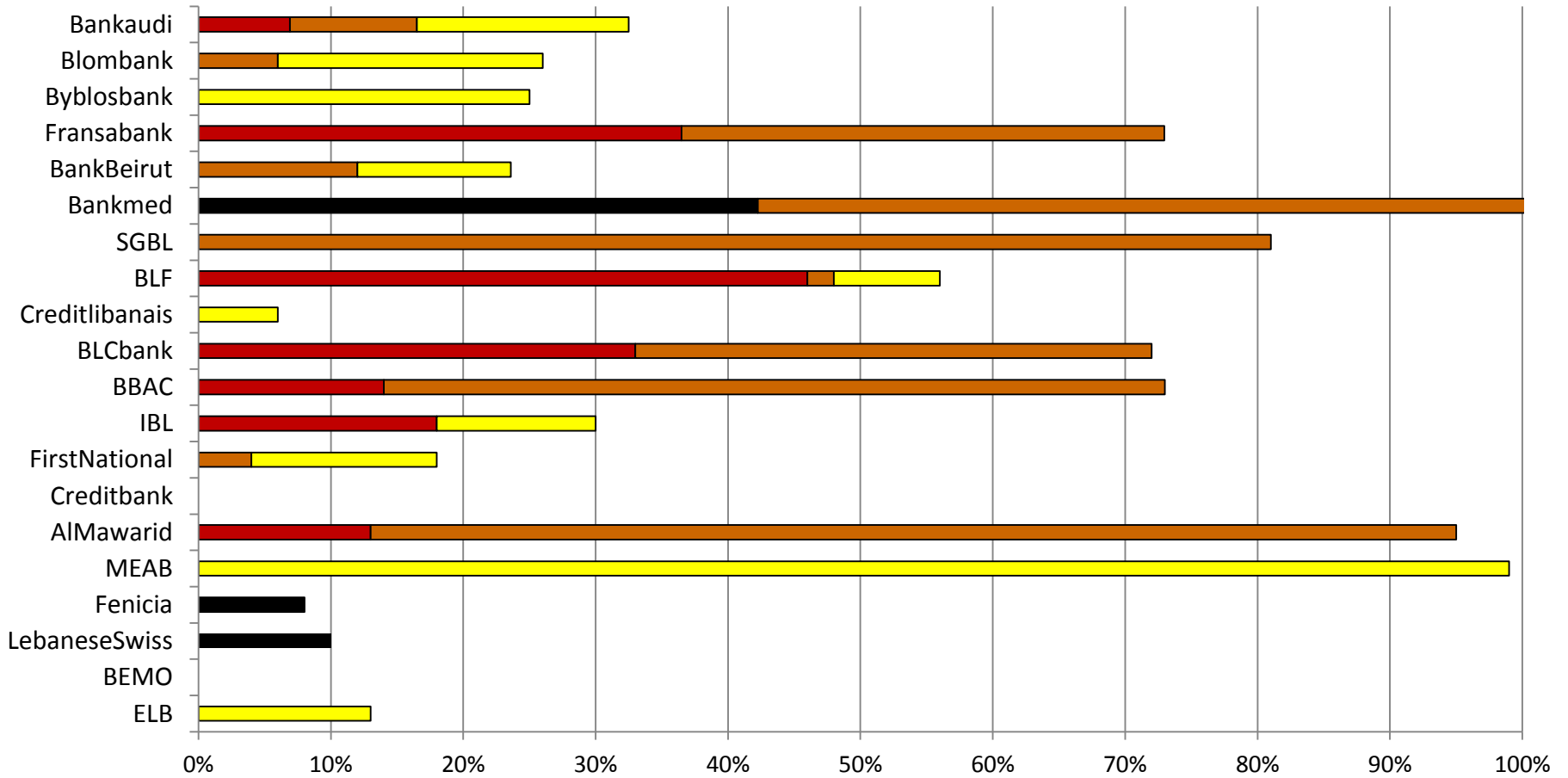


- Maurice Sehnaoui, Former Minister of Economy and Trade, father of Nicolas Sehnaoui (FPM member, former Telecom Minister)
1.4 billion US\$ equity (family), direct control in Societe Generale de Banque au Liban (SGBL)



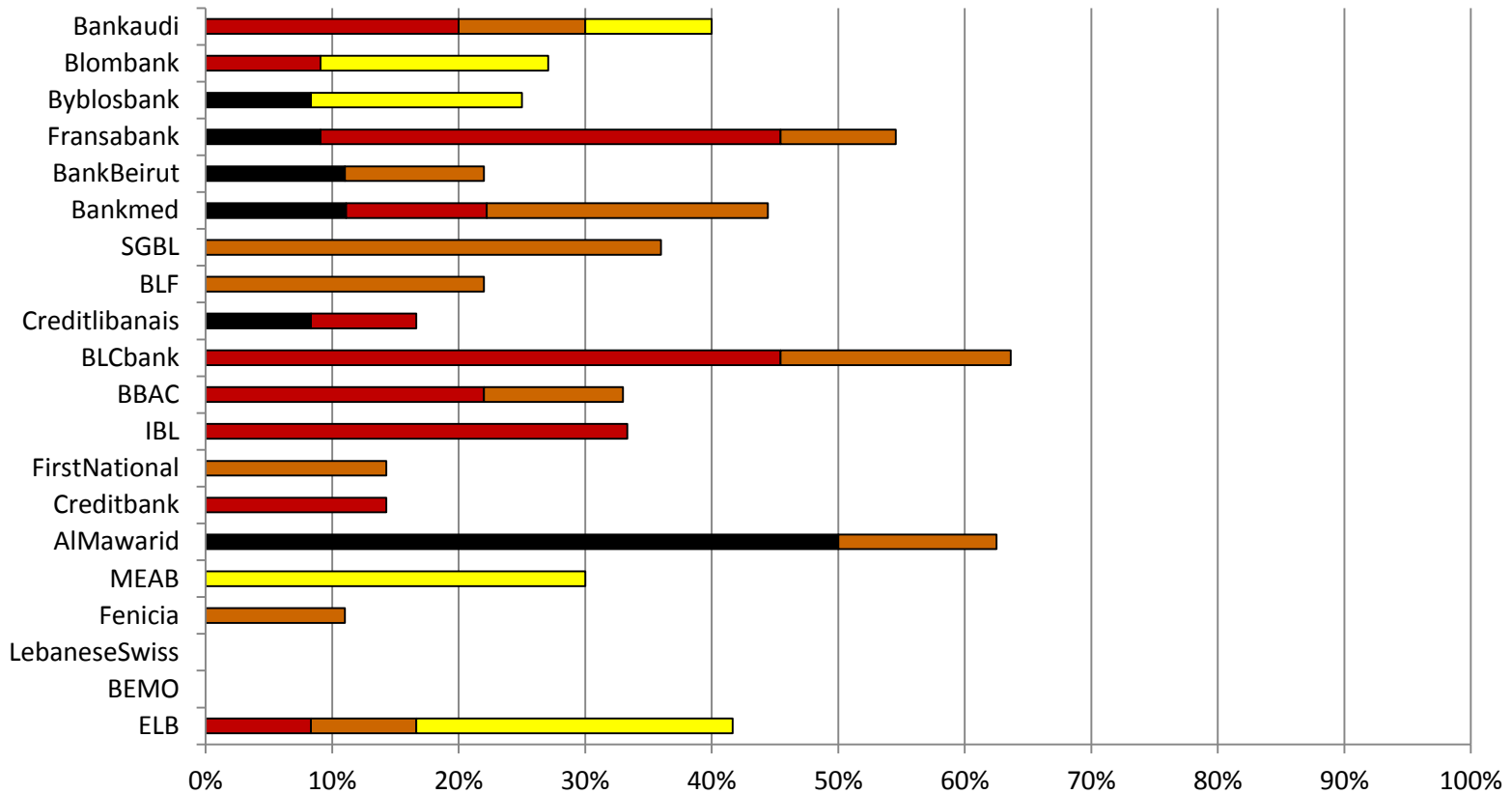
- Farid Raphael, Former Minister of Finance, Telecommunications, Justice, Former head of Association of Banks
Deceased 2014, family equity 700 million US\$, direct control Banque Libano-Francaise BLF

- Control by politically affiliated shareholders



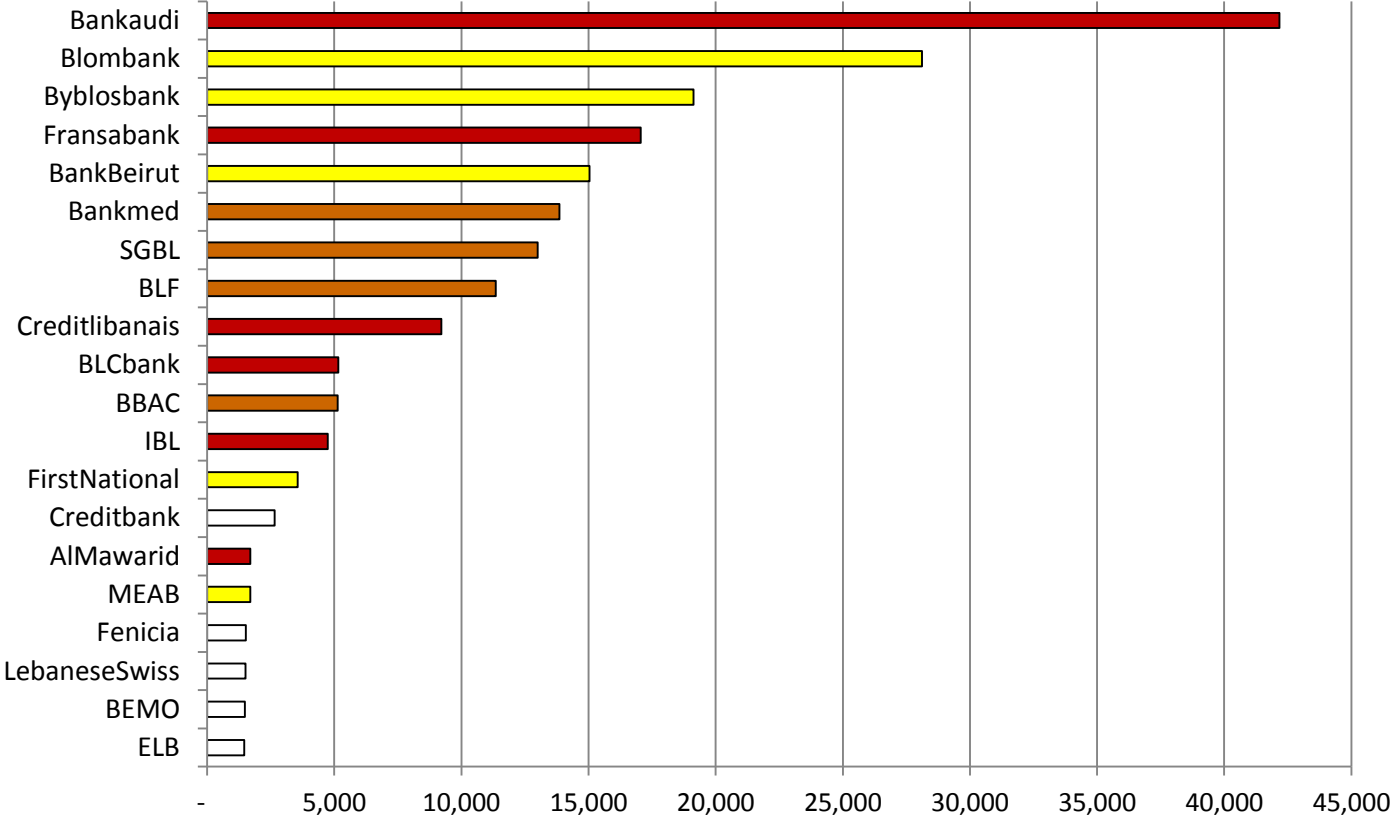
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	3. Indirect2: Person's family member is a current or former politician
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	1. Nolink: no linkages with politicians

- ‘Crony’ control within the Board of Directors



■	5. Direct: Person is currently a member of Parliament or the Government
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- Affiliation of the Chairman of the Board of Directors (by bank assets million US\$)**

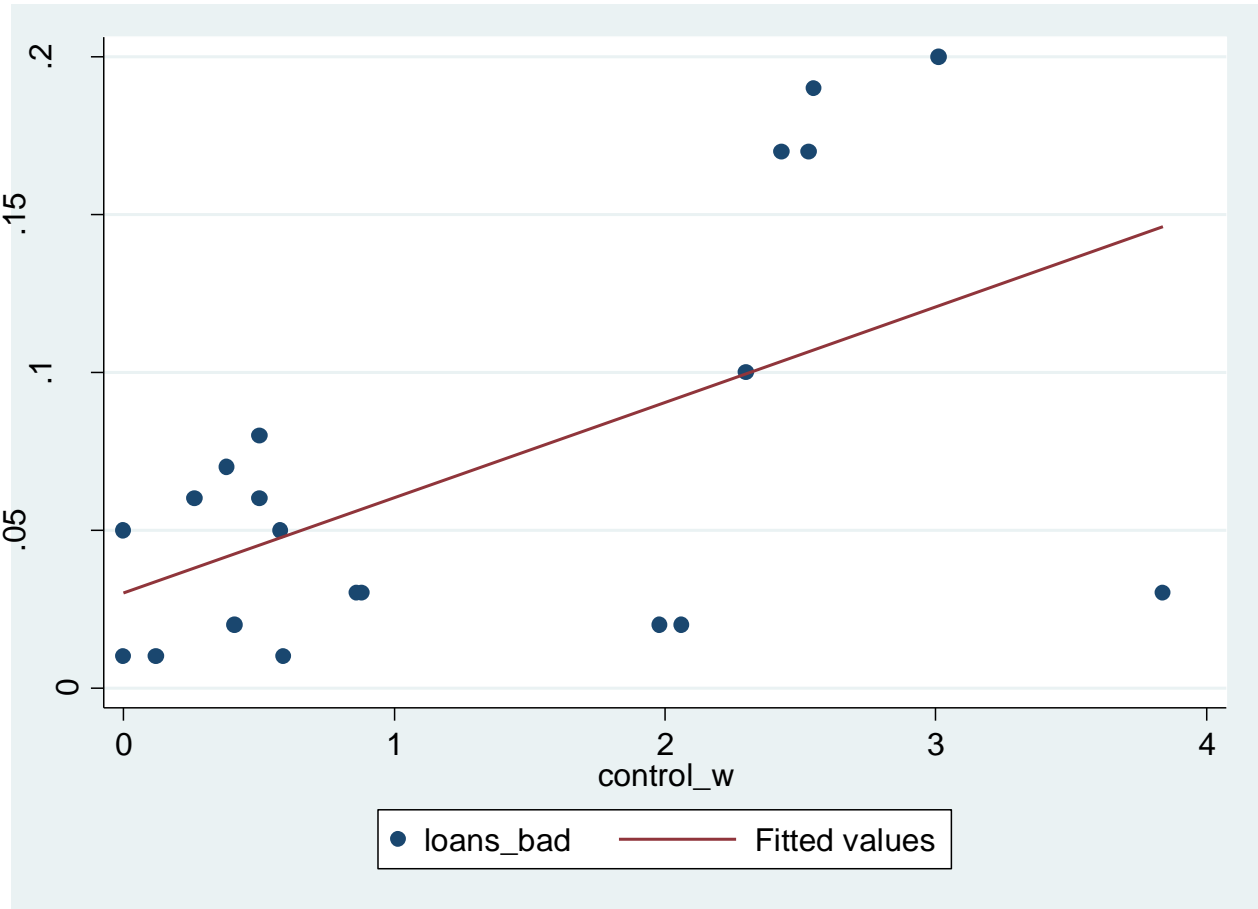


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Main Findings II

- Political control of shares and political control of Boards strongly correlated (expected)
- No evidence of size effects: larger banks not necessarily correlated with more political control
- Political control not correlated with higher sovereign exposure
- Political control not correlated with profitability and banking costs variables
- Strong and significant positive correlation between political control and non-performing loans
 - » Ratio: $(\text{substandard loans} + \text{doubtful loans}) / \text{gross loan}$.
- Similar to Morck (2011): “A more widely held banking system is significantly correlated with fewer nonperforming loans, while more predominantly state-or family-controlled banking systems both correlate with more nonperforming loans”.

- Nonperforming loans increase with the higher prevalence of politically-affiliated shareholders



Control: normalized to a scale between 1-5

Banks (& politicians) earn a lot from public debt service

Estimates of dividend earnings attributable to interest on public debt

Banks	Political Family	Political Party	Years in office	Percentage held of public debt, 2013	Earnings made from public debt while in office m\$
BankMed	Hariri	Future (Hariri)	2006 - today	27%	108
SGBL (+ BLC)	Sehnaoui	Free Patriotic Movement (Aoun)	2004-2005, 2011-2014	47%	20
Al Mawarid	Kheireddine	Democratic Party (Arslan)	2011-2014	31%	5
Fransabank	Kassar	None	2004-2005, 2009-2011	40%	24

Issues going forward

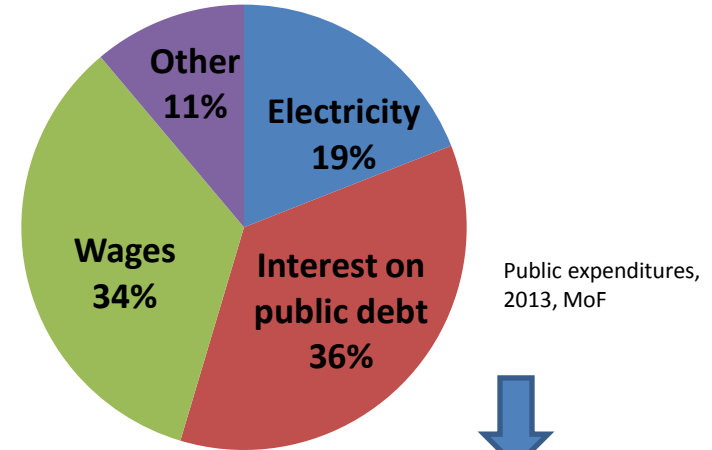
- **Legal and judicial:**
 - Law of illicit enrichment
 - Conflict of interest and abuse of public office
- **Accountability**
 - **Because of “Holdings” law, politicians saved 25 million \$ in taxes in 2013, 5 times the budget of the Ministry of Environment**
- **Efficiency of economic and financial model in Lebanon**
- **More mapping needed of other sectors**

So in reality:

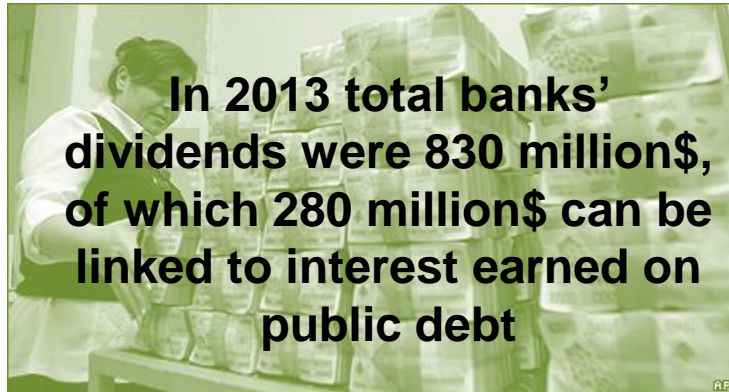
1. Public services are very bad



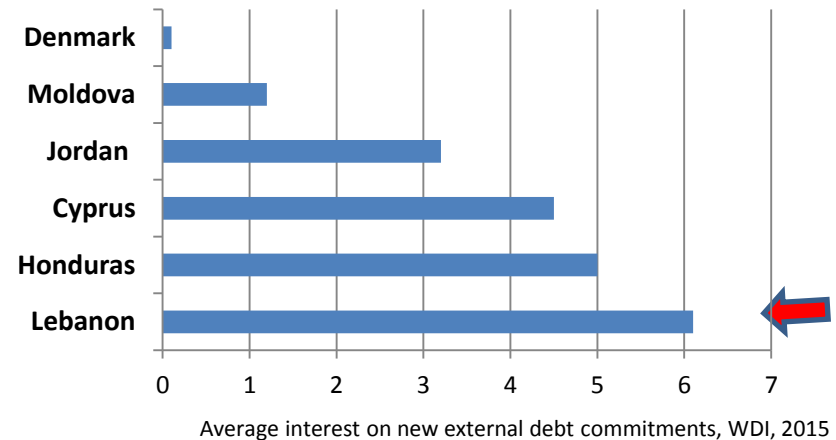
2. Because government budget swallowed by wages and EDL **AND interest on public debt**



3. Because politicians who own 45% of banks are not interested in reducing spending, and keep interest rates on public debt high



4. So that they keep on profiting from our pockets, while keeping public services bad



Thank you

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