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Lebanese Banking Sector Model and Its Implications on Small and Medium Enterprises

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Abstract: This paper studies the specifics and developments of Lebanon's banking sector with special emphasis on the bank loans for the SMEs. The methodology is mainly based on descriptive analysis. The analysis covers the years after the foundation of Lebanese Central Bank and focus on implications on SMEs access to finance. There were found proofs for close relations between enterprises and banks. Far more Lebanese enterprises rely on banks to finance investments and working capital. These relations are the main reason banks to be considered as largely integrated in the Lebanese economy. Collateral-based lending is very well developed in Lebanon. In the same perspective, circulars and loan packages are clarifying this strict relationship. Basel agreements also affect the crediting process. Thus, nearly half of the firms in Lebanon identify the access to finance as a major constraint. There was also found evidence for oligopoly type of the credit market in the country. Together, intensifying competition with digitalization makes banks optimize their branch networks and bank machine coverage. All these points witness in favor of the assumption of a very well developed and modern banking crediting system in Lebanon. The general conclusion is in favor of the implication for very well developed, modern and efficient financial sector of Lebanon which creates favorable conditions for sustainable growth and development of SMEs' credits in the Lebanese economy.

Keywords: Central banks; banks; SMEs; credits, financing policy.

JEL Classification : E58, G21, G32, H81.

1. INTRODUCTION

Banks serve as safe havens for depositors and are significant providers of credit for individuals, small and medium-sized businesses, companies, and governments, according to the literature (Allen *et al.*, 2019; Berger, *et al.*, 2002). Banks also use diversification, derivatives, and other on- and off-balance sheet operations to manage credit, liquidity, interest rate, currency value, flow, and other risks (Berger, *et al.*, 2002). Due to the so-called finance-growth nexus, changes in the commercial banking system and financial system - in general - have been demonstrated to be beneficial to economic growth (Berger, et al., 2002; King and Levine, 1993; Demirgüç-Kunt and Maksimovic, 1998; Levine and Zervos, 1998; Rajan and Zingales, 1998; Demirgüç-Kunt and Maksimovic, 2002; Christopoulos and Tsionas, 2004; Bekaert *et al.*, 2005).

A financial system's core consists of the banking system and the financial market. As a result, the financial system develops in lockstep with the banking system. The evolution of a financial system is difficult to measure since there are so many variables to consider. A well-developed financial system, in any event, has the capacity to support economic growth and development. A well-developed financial system should enable a smooth movement of cash from savers to borrowers or enterprises in need of funds. Excess free money will be sent to the businesses who need it the most. These are the companies that are prepared to borrow money at the highest interest rates. As a result, free surpluses will be effectively allocated to projects with the best rates of return via financial institutions and markets.Different players' behavior in their pursuit for external funding has distinct characteristics. Large corporations can access the financial markets directly by issuing shares or bonds that are traded on these exchanges. These large companies can borrow directly from savers who act as investors at a lower rate than small and medium-sized businesses that do not have access to the stock market to sell shares or bonds. As a result, small and medium-sized businesses must rely on commercial banks or non-bank lending institutions to obtain the funds they require. Small and medium-sized enterprises will have to apply for bank loans, which will force them to use more expensive funds and subject them to stringent screening procedures. They must pass the same strict requirements as commercial banks. Many often, these arbitrary criteria lead to the denial of a project that would otherwise be an excellent fit for financing. Many economists are focusing their study on the challenges that small and medium-sized businesses experience in securing finance because ofall these issues. These challenges are referred to as pecuniary restrictions in the empirical literature on the issue (Rahman, et al., 2017, p.650). This is a commonplace; interest in this issue stems from the importance of SMEs to each country's entire economic landscape; as a result, SMEs make a significant contribution to economic growth and employment creation (Ayyagari, et al., 2007). There are also entire economic sectors

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that are dominated by small and midsize enterprises. As a result, most of these businesses' issues might potentially influence the position of all sectors and even hinder the economy's growth.

The goal of this paper is to examine the specifics and trends of commercial banks' lending to SMEs in Lebanon. The presentation of the banking industry will be critical as a starting point for this. The research goes over the history of the BDL, the main characteristics of the Lebanese banking sector, and the most important decrees issued to commercial banks to establish standards and regulations for SME lending. It is critical to remember that our goal is to examine the bank-SME relationship in terms of financial access. In this regard, the following sections will be included in this paper: The banking industry in Lebanon is analyzed, with the Central Bank of Lebanon (BDL) as the governmental body responsible for commercial banks. The Bank of Lebanon's efforts to assist SMEs in obtaining finance will be presented under the "Banque du Liban's Stimulus Package for SMEs," with remarks from SMEs. Basel accords establish rules and criteria for commercial banks to follow when lending to SMEs. Monthly reports from the International Monetary Fund and the World Bank will be used to provide data on the banking services industry in Lebanon and the growth of the Lebanese stock market.

2. BANKING SECTOR EVOLUTION

2.1. Background on Lebanon's Banks

Prior to 1975, many legislative decrees bolstered the Lebanese banking sector's national and international standing, such as the bank secrecy legislation of 1956, the free conversion law of 1952, and the formation of joint accounts in 1961. These policies were critical in collecting Arab capital and establishing Lebanon as the Arab region's primary financial hub. Furthermore, despite 17 years of civil instability, the banking sector in Lebanon has been able to offer essential financial services with minimal impact. Nonetheless, the financial sector has faced several challenges and roadblocks that have hindered its functioning. For instance, the depreciation of the Lebanese pound from 1988 to 1992, the dollarization of deposits and the resulting depreciation of banks' equity, the decline in human capital and expertise, the withdrawal of foreign banks from the domestic market, and the so-called "problem banks" crisis from 1989 to 1991. (Hakim, et al., 2001). This crisis resulted in the merging of 19 banks, and this trend is expected to continue in the future (Table **1**).

During the years 1992-1998, the banking industry grew faster than the national economy. Total bank deposits were more than double the amount of GDP (estimated at $15 billion in 1999). This shows the country's economic position being severely disrupted. The most significant of these are (a) increased financial activity driven by government debt, which comes at a high cost (high interest rates) and at the expense of less activity in more productive sectors, and (b) banks' improved financial performance and greater returns. During this time, Lebanese banks have worked hard to enhance their skills and operations to reclaim their leadership position in the area. They worked hard to build their financial base, resources, and activities, develop new retail items, invest in new technology, hire qualified employees, and train existing employees. Between 1992 and 1998, these initiatives yielded a 13-fold rise in private money, a 282 percent increase in deposits, and a 302 percent increase in loans (Table **2-3**).

Table 1. Mergers and Acquisitions 1993 – 1999.

Year	Banks Merging	Banks Merged
1993	SGBL (societe Generale)	Globe Bank
1994	Credit Libanais	Phoenician and Capital Trust
1995	BLC (Beirut pour commerce)	Security Bank of Lebanon
1997	Fransabank	Tohme
	Byblos Bank	BLC (Beirut pour commerce)
	Audi Bank	CCMO (Credit Commercial Moyen Orient)
	Inaash Bank	Bank of Lebanon and Pakistan
	SGBL (Societe Generale)	Geagaa
1998	UBL (United Bank Lebanon)	Moghtareb Bank and LITEX
	Bank of Beirut	TransOrient and UniBank
	Al Madina	Foreign Trade
	Fransabank	Universal Bank
	Audi Bank	Orient Credit- Nasr Libano Africain- ADCOM Bank
1999	Orbil	Intercontinental Bank

Source: Lebanese Banker's Association.

Table 2. Main Features of the Banking Sector 1992-1998 (Billions of L.L.).

	1992	1993	1994	1995	1996	1997	1998
Deposit	3.697	4.744	7.844	8.994	13.351	13.936	15.897
Foreign Deposit (USD Millions)	4.555	6.462	7.593	9.330	11.169	16.132	20.031
Total Deposits	12.068	15.801	20.350	23.885	30.685	38.570	46.113
Percentage of Deposit L.L./Total Deposits	30,60	30,00	38,50	37,70	43,50	36,10	34,50
Loans	4.804	6.217	8.169	10.695	13.290	16.022	19.300
Percentage of Loans/ Deposits	39,80	39,30	40,10	44,80	43,30	41,50	41,90
Private Funds	264	444	676	1.146	1.943	2.990	3.620
Total Assets	14.634	18.809	24.285	29.055	37.183	45.633	55.031

Source: Lebanese Banker's Association.

Table 3. Growth of Lebanese Banking Sector 1992- 1998 (Percentage).

	1992/1993	1993/1994	1994/1995	1995/1996	1996/1997	1997/1998	1992/1998
Deposits	28,3	65,3	14,7	48,4	4,4	14,1	330
Foreign deposits	41,9	17,5	22,9	19,7	44,4	24,2	340
Total deposit	20,8	5,9	18,7	33,8	22,6	19,5	282
Loans	29,4	31,4	30,9	24.3	20,6	20,5	302
Private funds	68,2	52,3	69,5	69,5	53,9	21,1	1273
Total assets	28,5	29,1	19,6	28,0	22,7	20,6	276

Source: Lebanese Banker's Association.

In the international capital markets, Lebanese banks have also issued global certificates of deposit (GDRs) and Eurobonds. In June 1998, the total value of these offerings was $1.3 billion. Banks have also launched new savings products and financing schemes, including collaborative lending programs, personal loans (housing, automobile, consumer, *etc.*), leasing, investment packages, and a variety of savings programs. Other unique financing schemes have been established, including First, $270 million in IFC loans, including $100 million for mortgages and the balance for productive sector finance. Second, the European Investment Bank (EIB) contributed 30 million euros to support hotels outside of the city expansion (Table **4**).

Table 4. Foreign Issuing of Lebanese Banks.

As of 30/06/1998	In USD Millions
EuroBonds	210
Certificate Deposits	675
Global Depository Receipt	262
Subordonated Loans	150
Total	1297
Euro- Loans	
IFC	270
EIB	35

Source: BDL.

In other words, certain banks have provided confidence loans as part of the inter-Arab trade initiative to promote bilateral commerce. Third, the government has agreed to discharge a portion of its debts to the private sector, amounting to around LBP 1130 billion. It is believed that this money would increase production and provide job possibilities. The government also intends to encourage investment in these fields by providing interest rate subsidies (5%) on industrial loans in Lebanese pounds. A credit insurance agency is being proposed to expand the creditor base for small and medium enterprises. The banks' payment system has also been enhanced by the Central Bank's assistance for the construction of ATM networks and the establishment of a compensation chamber for commercial papers (in addition to clearing checks in Lebanese pounds and foreign currencies).Third, the installation of an updated information system that makes it easier to collect public money (Treasury funds, telephone, power, and automobile maintenance bills- Table **5**).

Table 5. Structure of Lebanese Banking Sector.

	Units- In 1992	Units- In 1998
Operating Banks	73	77
Employees	14075	14922
Financial Institutions	7	21
Representative Offices	11	11

Branches	512	685
ATM	0	205

Source: Lebanese Banker's Association.

The banking sector, which accounts for 9% of GDP, continues to play an important role in the economy, financing 45 percent of overall demand and 50 percent of imports on average, while deposits account for 90% of gross domestic savings. With the current economic crisis, the Lebanese banking industry has shown to be one of the few bright spots. Banks are run on a very cautious basis, with loans accounting for just 35% of total assets, since the industry is closely supervised by the Central Bank, which maintains stringent risk management and control ratios (Association of Banks in Lebanon, 2021). Foreign exchange positions, for example, are prohibited, political loans are prohibited, credits are closely monitored and categorized, and linked party transactions are limited and subject to accurate and timely disclosure. All Lebanese banks have followed international accounting standards since 1998. While this climate has allowed the big players to expand their market share, the banking industry has seen a decline in relative terms since 1999, owing to a reduction in private and public demand as well as a narrowing of net interest margins. The pace of mergers and acquisitions has risen in this setting. Let us first describe the history of BDL foundations, major features, and circulars to better comprehend and clarify some difficulties, keeping in mind the impact on SMEs credits at each stage.

2.2. BDL Foundation

The Lebanese financial sector was distinguished by the presence of international bank branches after World War I and under the French mandate. These international institutions focused on funding Lebanon's overseas commerce, leaving domestic financing to local banks with little capital and operating areas that were limited to the region where they were formed. They mostly dealt with short-term bill of exchange discounts, loans and advances secured against products or in the form of current accounts, and foreign exchange trading. They take deposits as well. Local banks, on the other hand, were largely reliant on obtaining higher-interest-rate deposits. However, a large portion of the money was held in overseas banks. Local banks also performed foreign exchange operations and provided advances in the form of current accounts and the discounting of local bills of exchange. There were also discounting houses, which specialized in discounting and re-discounting commercial invoices that had been rejected by banks. Despite this, they relied on their own capital to finance their enterprises, unlike local commercial banks. Furthermore, a significant number of moneylenders were widely available, offering high-interest commercial, agricultural, and consumer loans (Safieddine, 2020).

The Lebanese banking system prospered from the time of Lebanon's independence in 1943 through the formation of the Banque du Liban in 1964 (known as BDL). The large disparity between foreign and domestic Lebanese banks reduced, as the former no longer monopolized Lebanon's external funding, contributed to domestic financing, and became competitive for local deposits. The Ministry of Finance divided banks operating in Lebanon into three categories prior to the establishment of the Banque du Liban: licensed banks whose guarantees were authorized by the Lebanese government, unlicensed banks whose guarantees were not approved, and discount houses. In 1963, Lebanon decided to create a central bank after the agreement of May 29, 1937, regarding the right of issuing the Lebanese pound came to an end. Legislative Decree No. 13513 on August 1, 1963, created the Code of Money and Credit. It establishes the Banque du Liban as a public legal body with the authority to issue the national currency. The banking system was neither regulated nor supervised until 1964, when the BDL began publishing an official list of banks operating in Lebanon on a yearly basis in accordance with the Code of Money and Credit (in January). Banks were willing to follow the Commercial Code, which governed commercial activities, except for the 1956 bank secrecy law. The implementation of the Code of Money and Credit, as well as the establishment of the BDL, which was granted the responsibility to supervise and monitor the banking system to maintain its stability, were the first steps toward creating regulation, supervision, and control (Banque du Liban, 2019).

2.3. BDL and Basel Agreements

Basel agreements established the regulatory framework of international banking from 1988 to 2017, developing with every new financial and economic backdrop. It is important to grasp the background of this regulatory environment to properly comprehend the most recent implementations, regulations, and emphasis points. What are the Basel Conventions? In 1974, Herstatt Bank, a German bank that specialized in foreign currency, caused significant losses in the financial sector. This instance was the tipping point that prompted the banking regulator to act (Goodhart, 2011). The governor of the Bank of England, Peter Cooke, advocated bringing together the governors of the G10 central banks. (France, Belgium, Canada, Italy, Japan, Luxembourg, Germany, Netherlands, Switzerland, Spain, Sweden, United Kingdom, and United States) in Basel, Switzerland, to address the present banking situation. The Committee on Banking Regulations and Supervisory Practices, later known as the Basel Committee on Banking Supervision, was formed (BCBS). Basel I has been implemented in more than a hundred nations. Lebanon was one of the nations that partially embraced Basel I.

BSBC's goal was to create additional Basel agreements, such as Basel I, Basel II, Basel II.5, and most recently Basel III, to clarify duties between bank branches, subsidiaries, and parent departments. All banking institutions should be monitored, according to the committee: It specifies the local supervisory authority's and subsidiaries' (host) regulatory authorities' proper integrated supervision of a bank. The main goal was to focus on an effective capital adequacy structure now that the foundations of foreign business through banks had been established. They wanted the bank to have enough capital to avoid going bankrupt, giving consumers and companies confidence in the banking sector's stability.The Basel Committees present their work through various types of documents over time, whether within one Basel framework or between frameworks: Consultative, Final, Frequently Asked Questions (FAQ), Report, Newsletters, Working papers,

Quantitative Impact Studies (QIS), and comments received from banks around the world. To clarify policies and procedures, newsletters and Working papers are published on a regular basis. The major source of transition between consultation papers and approved standards is bank comments. Finally, the QIS is held on a semi-regular basis to track the impact of changes in various banks under various regulatory and situational conditions (Penikas, 2014).

The need for a major reform in the regulatory structure was evident even before the credit crisis began. The terrible financial crisis of 2007-2009 underscored the need for this. Specifically, Basel II required modifications to the market risk capital calculation. As a result, Basel II.5 was born. The Basel II.5 framework included three changes: the computation of a stressed VaR (Value-at-Risk) for market risk capital requirements, a new incremental risk charge, and a risk measure for credit-correlated instruments. When all three steps are taken together, the needed market capital charge skyrockets. According to Basic Decision No. 9302 published by the Lebanese central bank on 4/1/2006 and associated to the implementation of the International Basel II Accord on Capital Adequacy, Lebanese banks were adopting Basel Agreement norms and regulations.

The Basel Committee recognized the need to develop a new regulatory framework after the catastrophic financial crisis of 2007-2009. This new rule is divided into six sections, according to Hull's book (Hull, 2012): capital definition and requirements, capital conservation buffers, countercyclical buffers, leverage ratio, liquidity risk, and counterparty credit risk. We will go through the latter two components in more depth because they have an impact on how banks finance SMEs.

2.3.1. Liquidity Risk

Banks' focus on having enough capital has resulted in a huge inconsistency: capital may be accessible and sufficient, but liquidity may be an issue. The subprime mortgage crisis highlighted this point: Banks were unable to meet their obligations owing to a lack of cash. Basel III included two liquidity ratios to ensure that a bank's liquidity profile is robust enough: the Net Stable Funding Ratio (NSFR) and the Liquidity Coverage Ratio (LCR). The LCR stands for short-term coverage (30 days), whereas the NSFR is for long-term liquidity management (one year). Commercial Lebanese Bank is consequently subjected to credit limitations. This limit, in turn, must be divided into tiny portfolios to comply with the risk-spreading requirement. After choosing the best and most successful applications, the outcome will be visible on the restricted quantity of credits available to SMEs.

2.3.2. Counterparty Credit Risk

Another key learning from the subprime crisis is that there are significant gaps in counterparty credit risk, particularly when dealing with non-cleared securities. As a result, Basel III modified a new model for computing the counterparty capital charge to account for a more granular approach to the hedging tactics that may be employed to encourage banks to margin their trades. Due to the unpredictability of market variables and counterparty credit spreads, another enhancement was the addition of an extra capital charge for the credit value adjustment (CVA).

2.4. Main Characteristics of Lebanese Banking Sector

In terms of protecting foreign money and revenue, the Lebanese banking system includes several features that contribute to Beirut's (the capital city's) reputation as a regional financial hub. Here are some of its major characteristics, as well as some of the consequences for depositors and creditors (BDL, 2019).

2.4.1. Capital Mobility and a Free Exchange Service

The Lebanese pound is fully convertible and may be exchanged for any other currency. Furthermore, the free movement of money and wealth within and beyond the Lebanese economy is unrestricted. It is a favorable location for domestic and foreign businesses to establish themselves in Lebanon, where they may easily conduct business.

2.4.2. Banking Secrecy Act

The Banking Secrecy Law, enacted on September 3, 1956, subjected all banks incorporated in Lebanon, as well as international bank branches, to "professional secrecy". All bank managers and workers who are involved in the bank's activities are prohibited from disclosing what they know about their clients' names, property, or assets to any other parties, whether private people or governmental authorities, whether administrative, military, or judicial. This information is only disclosed with the explicit agreement of the client or his beneficiaries, in the event of bankruptcy, or in the event of a legal crisis. Furthermore, to preserve banks' assets, the legislation permits banks to communicate information about their clients' debit accounts under the pretext of banking confidentiality. It is also an important factor in attracting both depositors and creditors.

2.4.3. Zone of Free Banking

Under the Income Tax Law (Legislative Decree No. 144/59 and its modifications), the following items are subject to a 5% income tax: 1) Interest, earnings, and receipts from all credit accounts, including savings accounts, created in Lebanon's banks, apart from government and diplomatic missions accounts 2) Earnings and interest on deposits 3) Interest earned from Lebanese Treasury bonds and banks' certificates of deposit.

On April 1, 1975, Decree No. 29 established a free banking zone by allowing the Lebanese government to exempt non-residents' deposits and foreign currency liabilities from: interest taxation, the needed reserves imposed by the Banque du Liban in accordance with article 76 of the Code of Money and Credit, and the deposit guarantee premium applied on bank deposits to the National Deposit Guarantee Institution's profit. It is also a distinguishing feature of the Lebanese banking industry, attracting investors and Lebanese businesspeople residing abroad to invest in their home country, where they will be free from certain taxes.

2.4.4. Measures to Prevent Money Laundering

Lebanon recognizes the need of combating money laundering, particularly because the bank secrecy rule can be exploited to facilitate such illicit transactions. As a result, and in accordance with the bank secrecy law, the Association of Banks in Lebanon (ABL) has developed a due care agreement, which member banks have signed. This agreement is intended to combat money laundering operations. It is a plus for both local and international depositors/borrowers since they are working with financial institutions that are authorized, well-regulated, and do not threaten dangerous penalties at any time.

2.4.5. Efficient CDR Unit

The Risk Center (Centrale Des Risques- CDR) is an information center that serves as a mediator between banks and financial institutions, allowing them to share information permitted by the Money and Credit Code on their clients' credit. Banks and financial institutions will be able to use this module to: Conduct searches on current CDR customer positions - Run queries and examine the results in order to update the proprietary computer system in the following areas: 1- collecting new customer identification information (with papers attached); 2- updating current CDR customer information (with documents attached); 3- Submit a monthly CDR position report and get feedback files from the Central Bank containing data for the whole banking industry. The business users' operational activities will be guided by two primary process flows available in the internal CDR system:1- Daily process flows for processing ID client information, acquiring and/or updating the CDR number to be used in monthly reporting, and enquiring about the customers' risks; 2- Monthly process flow for reporting customer exposures within the banking industry. Finally, the CDR unit organizes and systemizes the connection between banks, referred to as lenders, and people or businesses seeking loans, referred to as borrowers. Once a commercial bank A makes a credit declaration to the central bank, another commercial bank B can utilize the CDR unit as a data source to obtain information about this client's situation, his commitment to debt settlement, and whether he is eligible for additional credit. Credit risk will be decreased as a result, and the crediting process will be selective and well-organized, with no loan duplication or unethical crediting activity (Jrad, 2023).

2.4.5.1. CDR Main Circular

According to the Basic Decision No. 7705 dated 10/26/2000 related to Central interest system for banking risks, based on the Code of Money and Credit, especially Articles 147 and 179 thereof, based on the provisions of Article 3 of the Law implemented by Decree No. 5439 of September 20, 1982, and based on the decision of the Central Council taken in its session held on 10/25/2000,"Central Bank Risk Regulation System" shall be put into practice. Besides, any person who violates the provisions of this resolution and the system attached to it shall be subject to penalties.

All banks and financial institutions duly registered are legally participates in the central interest of banking risks established. Each subscriber (commercial bank) must submit at the beginning of each month, report that includes a statement of the credits granted to its customers in the Lebanese currency and the equivalent In the Lebanese currency, the credits granted in foreign currencies and the amount of use of each of them at the end of the previous month in one of the ways built in the permit form.Financial leasing companies operating in Lebanon must declare to the Central Authority any updating in CDR cards in case of change in the information related to the customer. This is in accordance with the banking risks of the facilities it grants to its customers. For this purpose, applicants are asked to sign a form allowing banks to investigate their credit status.

3. BDL BETWEEN ITS PREROGATIVES AND GOVERNMENT COORDINATION

3.1. BDL as a Double Operator

BDL is a legally recognized public corporation with complete financial and administrative autonomy. It is not subject to the same administrative and managerial regulations and controls as the government. The state owns the whole capital of the country. The BDL is given the exclusive authority to issue the national currency by law. According to the official site of Central bank of Lebanon, BDL is tasked with the broad objective of preserving the national currency to guarantee the framework for continued social and economic progress, as stated in article 70 of the Code of Money and Credit. The following objectives are included in this mission: maintaining monetary and economic stability- developing money and financial markets- maintaining the soundness of the banking sector- development and regulation of money transfer operations, including electronic transfers- developing and regulating payment methods and instruments- development and regulation of clearing and settlement operations for various financial and payment instruments, as well as marketable bonds. BDL is given the legal authority to carry out its objective for this reason (BDL, 2019).

By modifying discount rates, intervening in the open market, and setting loan limits for banks and financial institutions, the BDL manages bank liquidity. It controls bank credit in terms of amount and forms of credit by imposing credit ceilings, directing credits to certain objectives or sectors, and establishing credit conditions and rules in general. It establishes reserve requirements on assets and/or loans established by BDL, as well as penalties if reserve requirements are not met. The BDL may consider TB investment as part of the reserve requirements. The BDL issues licenses to banks, financial institutions, brokerage firms, money dealers, foreign banks, leasing businesses, and mutual funds that want to set up shop in Lebanon. These institutions are regulated and supervised by the Banking Control Commission. The BDL, in consultation with the Association of Banks, produces circulars and resolutions governing bank-customer relations.

As previously stated, BDL distributes circulars to commercial banks to control their operations. Circulars discussing the loan relationship between commercial banks and Lebanese SMEs are worth highlighting. It is the central topic of our research. In the next part, we will go through a few of the

circulars that we chose from a stack because of their importance in credit relationship regulation Bank-SMEs.

3.2. BDL Circulars pertaining to SMEs Regulations

In this part, we shall show various circulars published by the BDL addressing commercial bank loans extended to SMEs. These principles aid in the formation of the connection between borrowers and lenders.

3.2.1. Basic Decision No 10185: Credit Risk Mitigation Techniques (Basic Circular No 121 to Banks)

In line with Basic Circular No. 121 and its revisions pertaining to the implementation of the Basel II Capital Accord, the Decision of the Central Council of the Banque du Liban, released on June 24, 2009, rules to control bank lending procedures. Some key themes were emphasizing the stringent requirements put on borrowers, whether individuals or corporations, when they request bank credits to support their enterprises. Here are a few examples:

Under Pillar 1 of the Basel II Accord, institutions that utilize the standardized approach for evaluating credit risk are permitted to adopt the following credit risk reduction techniques: 1- Acceptable financial collateral; 2- Netting transactions between assets and liabilities on the balance sheet; 3- The Banking Supervision Commission will clarify in detail eligible collateral provided by counterparties and credit spillovers. Furthermore, banks must mitigate the risks associated with the use of one or more of the aforementioned approaches, as well as adopt suitable processes and internal controls to manage these risks (BDL, 2009).

Credit protection is not acceptable as a credit risk reduction strategy if there is a positive link between the borrowing client's risk profile and the risks connected with the credit protection used, according to this circular (e.g., a guarantee, bond, or credit derivative, where the borrowing company submits shares of its capital to the bank as financial collateral for its debt). Banks are still permitted to utilize real estate collateral to minimize credit risk. This only applies to debt designated as non-performing loans under BDL standards. After determining that part, the portion covered by real estate collateral is scaled by a 50 percent ratio based on 50 percent of the market value of the real estate collateral obtained (land, commercial or residential building). Net non-performing loans completely covered by non-Basel II compliant collateral are scaled at a 100 percent ratio after subtracting provisions that must be less than 15% of the entire loan amount.

3.2.2. Basic Decision No 9794: Distribution of Main Credit Portfolios (Basic Circular No 115 to Banks)

The circular also indicates the central bank's concern regarding commercial banks' well-being while lending to SMEs. The BDL's policies are centered on restricting the quantity of loans made, raising collateral, dividing risk by establishing credit limits, and ultimately defining the processes to be followed with hazardous clients or customers who have not paid their bills. These circulars are then carried out by commercial banks in the form of stringent terms incorporated into loan contracts signed by clients (BDL, 2007). Here are some essential aspects from Circular No. 115 to assist understand what we're talking about:

Banks in Lebanon must separate their loans and credits into three portfolios: Retail Portfolio- Small and medium-sized businesses Portfolio that includes: Loans made available to liberal professions (such as doctors, engineers and lawyers in purpose to finance their professional activities) and loans to firms or corporations (general partnerships, limited partnerships, joint ventures, corporations, holding companies, limited stock partnerships, limited liability companies, or offshore entities) having annual sales of less than $5 million- Corporate Portfolio consists of: Loans to enterprises or companies having yearly sales above the equivalent of USD 5 million (general partnerships, limited partnerships, joint ventures, corporations including holding companies, limited partnerships with shares, limited liability companies, or offshore entities) as well as loans made to insurance firms (whatever is their turnover).

The Regulatory Retail Portfolio, which includes both the Retail Portfolio and the Small and Medium Entities Portfolio, must then fulfill the following requirements cumulatively in order to compute credit risks using the Standardized Approach: The loan must be accepted in both the Retail and Small and Medium Enterprises Portfolios- The regulatory retail portfolio should be eligible by a certain degree of accumulation, such that the total of retail loans and loans to small and medium-sized entities granted to a single natural or legal person or group, as specified in the BDL's policy measures, does not surpass 0.2% of the total legislative retail portfolio, such that any debts above 0.2 percent of the entire portfolio are removed, and the ratio of each debt to the new total is recalculated, in order to have a suitably dispersed regulated retail portfolio free of any debt exceeding 0.2 percent of the debts constituting that portfolio- Before taking into account any accepted guarantees or sureties, the total facilities (on and off balance sheet) given to a single natural or moral person or an associated group shall not exceed the equivalent of USD 750,000. The cap is applied to the overall balance of facilities given to the whole group in the case of several institutions or affiliates of a small group- Loans must not be made specifically to a person or a small or medium-sized business to fund the acquisition of listed or unlisted securities (such as bonds, shares, etc.).

Furthermore, for the purposes of applying the terms of this judgment, the debtor is regarded to be in default in any of the following instances, within one of the previously stated portfolios: If it looks that the debtor has become incapable of handling any of his obligations to the bank, even if the bank does not use its legal right to acquire, liquidate, or execute the guarantees, sureties, or undertakings presented by the debtor when obtaining the loan in order to pursue the customer- If the debtor has not settled his/her/its liabilities to the bank for more than 90 days. In addition to the foregoing, an overdraft borrower is deemed in default if 90 days have passed after exceeding the facility limit obtained under the original overdraft account agreement or the fully recorded updated overdraft account agreement. This also applies to credit accounts that become debit accounts by mistake and are not returned after 90 days.

3.2.3. Basic Decision No. 8779: Related to Microloans (Basic Circular No. 93 to Banks)

It is necessary to define two words to make this judgment. First, a micro-loan is described as a loan given by a financial institution to individuals or small businesses with less than four employees in order to assist them in developing and implementing their own production initiatives (manufacturing, agribusiness, handicraft) or service, tourism, or trading, or to assist them in improving their living or housing circumstances, provided the loan does not exceed thirty million Lebanese pounds or its equivalent in foreign currency, and is returned within six years. Second, microcredit institutions are social or non-governmental groups that work with banks, subject to the Banque du Liban's permission, for these banks to provide microcredits directly and under their own responsibility, satisfying the requirements outlined in the preceding paragraph. Other organizations may be considered microcredit institutions by the BDL Central Council if their regulations enable them to carry out operations comparable to those of a civic or non-governmental organization. As a result, according to Circular No. 93, issuing micro-loans/microcredits is subject to several criteria and bureaucratic hurdles (BDL, 2004). The following is a sample of the content:

Banks may grant microcredit from their own resources, subject to the formulation of due diligence actions, with the approval, guarantee, or surety of microcredit organizations or funds on deposit in the banks, supplied that these institutions approve the bank to offer microcredit to the borrower. Any microcredit institution's total approvals, sureties, and guarantees must not exceed fifteen billion Lebanese pounds (or its equivalent in international money).

Concerned banks must submit a request to the Central Bank with the following papers in order to be allowed to deal with microloans/microcredits: The relevant authorities' notice of the concerned civic or non-governmental organization's establishment- certificate from the competent authorities indicating the members of the governing body as well as the authorized signatories of the linked civilian or non-governmental organization-Certified copy of the concerned civic or non-governmental organization's Articles of Association or regulations- Any further document considered essential by Banque du Liban, including a study detailing the quantity of loans already issued, as allocated by amounts throughout regions and economic sectors.

Furthermore, before issuing loans, financial companies must get written permission from the borrower to assess the borrower's risk exposure. Banks and financial institutions must transmit financial statements and loan progress information to the Central Office of Credit Risk on CD at the beginning of each month. BDL also issued a tailored loan package for SMEs in connection with these circulars. Lebanon has also joined the International Monetary Fund and the World Bank. These developments have ramifications for small business finance. Each of these consequences is clarified in turn in the next section.

3.2.4. Banque du Liban's SME Stimulus Package

In recent years, the Banque du Liban (BDL) has concentrated on promoting the economy through private sector investments. As a result, it has offered low-cost incentives to the private sector through banks in order to encourage investment in key economic areas like tourism, agriculture, manufacturing, information technology, the environment, housing, and education. The major goal of these initiatives is to provide new job possibilities for Lebanese youth while also stimulating the economy by providing required funds for small and medium-sized businesses. The economic downturn in Lebanon, which is mostly owing to the region's unpredictable political and security conditions, spurred Banque du Liban to launch a new program aimed at encouraging private lending and, as a result, economic growth. The BDL published relevant circulars in early 2013, allowing it to introduce a total of 2,210 billion Lebanese pounds in soft loans to commercial banks. These were intended to encourage low-interest loans in the aforementioned areas, as well as research and development, entrepreneurship, new knowledge and innovation initiatives, and renewable energy. This program was a resounding success. It was renewed in 2014 with a total amount of LBP 1,400 billion, in addition to the LBP 2,210 billion in outstanding funds. The BDL continued to stimulate the economy in 2015 by adopting a third stimulus package of LBP 1,500 billion, in addition to the amended funding from 2014. In 2016, the economy received a fourth stimulus package worth LBP 1,500 billion. The following are some of the SMEs that have benefited from the current BDL stimulus package (Table **6**):

Table 6. Stimulus Package for SMEs

Loans	Conditions	Comments/ Examples
SME Loans to: produce information technology (IT) equipment- create technology programs- provide associated services. As well as to initiatives in tourism, agriculture, industry, and handicrafts	Eligible for a government rate subsidy if they fulfill those criteria: →Loan of at least LBP 50 million, or its equivalent in US dollars or Euros, must be fully invested in Lebanon to fund a new project or finish an existing one. →Loan's term must be between 5 and 7 years,15% of principal payable within first two years. →Total amount of subsidized loans cannot exceed LBP 15 billion. →Interest (before taking into account the 4.5% government subsidy): *Interest rate on two-year Treasury notes + 1.075% shall not be exceeded for LBP loans. *For foreign currency loans, the three-month Libor or Euribor rate + 7.075% shall not be exceeded.	LBP loan example (based on current two-year TB yields): →2-year TB+1.075% =5.84%+1.075% (Interest before subsidy) 6.915% →6.915% - 4.5% = 2.415% (Interest after subsidy)

Loans guaranteed by Kafalat S.A.L. benefiting from government subsidies to SMEs	→Companies operating in industrial, agricultural, tourism, handicrafts, and high technology sectors →Kafalat S.A.L. establishes the terms →Before calculating the government subsidies, all interest and commissions should not exceed 40% of the one-year Treasury bill yield + 3.3 percent.	→(40%*1-year TBs) + 3.3% = (40%*5.35%) + 3.3% = 5.44% (before subsidy) →5.44%-4.5%=0.94% (Interest after subsidy)
Individuals and small companies with four or less employees are given loans in LBP	→Consent of microcredit institutions in order to assist them start or develop their own initiatives in the sectors of manufacturing, services, tourism, or commerce →Loan amount is limited to LBP 20 million. →Repayment duration is limited to five years.	Fields require long duration to create returns due to limited loan amount and a short settlement term.
LBP loans used to fund new projects or extend current ones (not benefiting from previous government subsidies)	→Not available for personal use, real estate, or land projects →Not used to refinance current projects, purchase stocks, repay debts →Total loan amount is not more than LBP 22.5 billion →Borrower is given 6-month to 4-year grace period for repayment. →Loan's principal payback duration, excluding the grace period, is not more than fifteen years. →All interest should not exceed 40% + 3.3% of the return on one-year Treasury notes	Based on current 1-year TB returns, here's an example: Maximum interest = 40% * 1-year TBs + 3.3%= 40% * 5.35 %+ 3.3% = 2.14%+ 3.3%= 5.44%
After 1/1/2015, LBP loans to fund working capital for projects supported by publicly subsidized loans	→Loan term is limited to two years, including 1-year grace period. →Loan's value does not exceed 10% of the value of a comparable loan that receives a government subsidy or is issued under the same terms as in the previous example. →All interest and charges should not exceed 40% + 3.3% of the return on one-year Treasury notes	Based on recent one-year TB results, example: Maximum interest = 40% * 1-year TBs + 3.3% = 40% * 5.35%+3.3% = 2.14% + 3.3% = 5.44%
Loans to productive sectors in LBP under the "Guarantee of Small Enterprises" program	→A government subsidy is not available for Loan. →Loan amount is limited to LBP 75 million →Loan's term is limited to 7 years, including a one-year grace period →Kafalat S.A.L. guarantee does not apply to this loan →Loan is not a micro loan, as previously stated →Total amount of interest should not exceed 6%	→Such as loans guaranteed by the Economic and Social Fund for Development →Constraints that hinder SMEs freely investing
SME loans in LBP to fund new initiatives in sphere of knowledge and innovation	→Loan amount is limited to LBP 300 million →Borrower is given a one-to-three-year grace period to repay the loan as of the distribution date →Loan principle to be repaid within 7 years, excluding grace period →Interest and commission combined should not be more than 0.75%	Limited field: only innovation
LBP loans used to fund R&D projects/ productive sector	→Borrower is given a two- to four-year grace period to repay the loan as of the distribution date →Loan principle must be repaid within 10 years →Total amount of interest should not be more than 0.75%	Limited field: R&D

Source: www.bdl.gov.lb- (Author's collection).

4. LEBANESE FINANCIAL SECTOR FROM SMES' PERSPECTIVE

The financial sector is made up of businesses and institutions that provide financial services to both commercial and retail clients. This industry includes a diverse variety of businesses such as banks and investment firms. This section emphasizes the importance of banks in the Lebanese financial system. We shall provide four components to achieve this goal: The weight of banks and their rising services, as seen in section 4.1. The trend of bank loan products in the Lebanese business market will be seen in section 4.2. Then, the credit relationship will be shown in 4.3. based on IMF descriptive data. Finally, in section 4.4, we will demonstrate

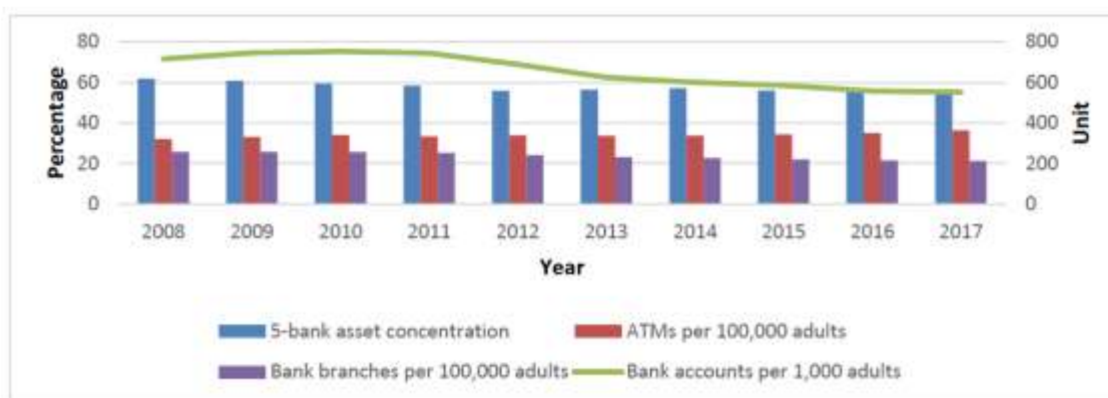

Fig. (1). Bank services accessibility and concentration of the credit market in Lebanon.

Source: World Bank, Data Catalog; Enterprise Surveys, What Businesses Experience.

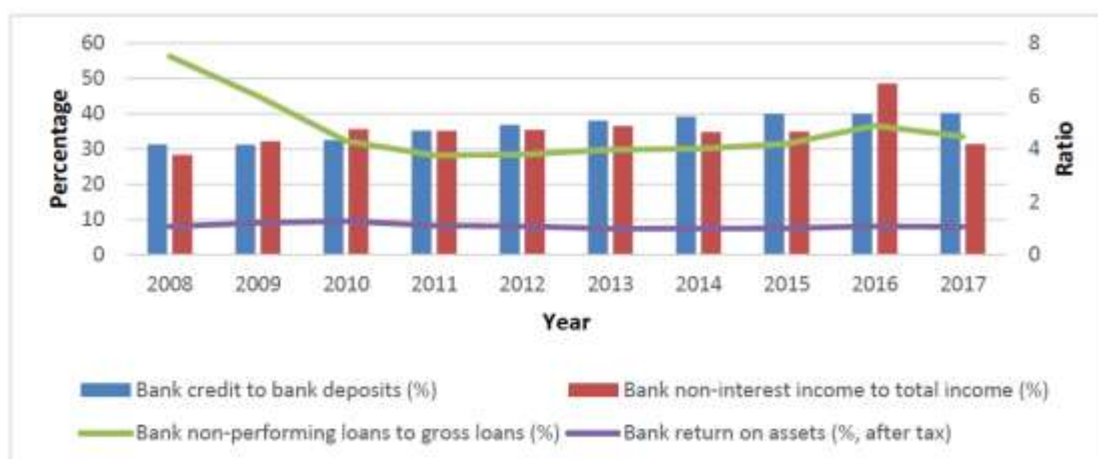

Fig. (2). Specifics of bank crediting process in Lebanon.

Source: World Bank, Data Catalog; Enterprise Surveys, What Businesses Experience

the poor performance of the Lebanese stock market to emphasize again the importance of banks as a distinct component of the financial system.

4.1. Expansion of Lebanon's Banking Service Market

Competition between banks, concentration and distance between the bank and the borrower are recognized as factors that may describe the credit market. The management of banks develops branch networks in order to have maximum coverage in the territory of a country. Efforts and attention are focused primarily on the most populous cities and those with the most affluent citizens. In this way, they aim to reach a maximum number of targeted customers for their services. For this reason, the establishment of a company in a specific city means appropriate access to a concentrated and developed credit market. This is much more valid for an emerging market economy. It is important to note that digitization and installation of ATMs in areas without bank branches exponentially improve the accessibility of banking services for as many people and companies as possible.

Fig. (**1**) highlights some indicators of the accessibility of banking services and the concentration of the banking services market and, in particular, the credit market in Lebanon. The time series could be found on the World Bank's data catalog, which provides periods long enough to cover an economic cycle. Unfortunately, it ends in 2017, a year in the middle of the business cycle, in an upward phase of the Lebanese economy's development. As shown in Figure 1, credit market concentration is measured by the concentration of assets of five banks. These are the commercial banks that hold the largest share of the credit market in a country since business loans are assets for commercial banks. This share varies around 60% in the different years of the period, but a slight downward trend can be observed towards the end of the period. The maximum value of this proxy is estimated in 2008. Thus, the crisis and the slow recovery have created favorable conditions for the sustainable growth of the credit market in Lebanon. The course of growth continued to include more and more new and smaller banks in the market, so that the asset concentration of the five banks decreased slightly at the end of the period. As can be seen, the trend is downward with a slight rate of decline. The reason is that during this period, the population of Lebanon has increased by more than 50%. Thus, a slight increase in the bank branches number is matched by many more inhabitants. As a result, there is a perception that bank branch coverage has deteriorated over this period, which is not the case. The

growing population seems to be covered by ATMs. A sustained upward trend can be observed from the beginning to the end of the period.

Another interesting trend was masked by the number of bank accounts per thousand adults. There is a visible break point in the upward trend in 2011. This was the year when many rebellions began in Arab countries and caused a significant influx of refugees into Lebanon. These new residents often had nothing more than a cell phone and a few bank bills in their pockets. Another cause of this trend could be found in the competitiveness of non-bank payment institutions that successfully compete with the old traditional banks. Nevertheless, the evolution of this variable deserves special attention and a separate study on this topic because the belief in a global conspiracy is not the only reason why people avoid using banking services. What is remarkable for us is the impact of this development on SMEs, which have become an attractive customer category for banks, and their business credit is a product for which commercial banks have created divisions and departments to serve.

4.2. Bank Credit Evolution

The specifics of the bank credit process could be described by some more quantitative indicators. These are estimated on the Lebanon data in 2019 and plotted in Figure 2. Overall, these proxies are specificities of the Lebanese banking system.

Important findings about the trend of bank credits can be monitored in the figure above and here is our interpretation: the ratio of bank credit to bank deposits is positive and appears to have a sustained upward trend over the period. It is typical for periods of crisis and initial recovery that credit exceeds deposits by firms and citizens. The maximum values of this variable were reached in the last three years of the study period. While credits exceed funds for them accumulated as deposits in banking institutions, the return on credit tends to decrease slightly over the period. The economic recovery after 2010 catalyzes the supply of banking services and the granting of credit to businesses. Commercial banks are entering a period of intense competition to attract new customers. They are increasing their market share, but at the cost of lower returns. The return on bank assets - most of which are business loans - declines after 2010. It declines in percentage terms but not in number of currency units. Increased competition is forcing banks to offer loans at lower interest rates. This is prompting banks to look for other ways to earn profits and improve their return on capital and assets. Thus, commercial banks are trying to find ways to generate additional non-interest income through service fees and commissions. This is seen as a modern approach to improving banks' income statements. The same trend is visible in Lebanon. What's more, it is a sustainable trend of increasing non-interest income in the total income of banks, the peaks of which were reached in 2016. Among the most important specifics in a credit market is the number of non-performing loans (Jrad, 2023). In Figure 1.2, non-performing loans were plotted as a share of gross loans. We see a sharp decline in this share. What is more impressive is that the downward trend includes a sharp decrease in the share of non-performing loans during the 2008-2010 crisis periods. This development seems to be peculiar to Lebanon and deserves special attention and why not a separate empirical study.

4.3. IMF/ World Bank and Descriptive Data on Credit Relationship

Lebanon joined the International Monetary Fund and the World Bank on April 22, 1947 (International Bank for Reconstruction and Development- IBRD). Lebanon's Country Partnership Framework, developed by the World Bank Group, focuses on improving access to and quality of services, as well as boosting economic prospects and human capital.It was created after extensive consultations with the government, parliament, business, and civil society. IBRD provides financial solutions and policy assistance to nations to help them decrease poverty and spread the benefits of long-term prosperity to all their citizens.The IMF is required by Article IV of its Articles of Agreement to monitor its members' economic, financial, and exchange rate policies in order to guarantee the smooth operation of the international monetary system. The IMF's assessment of these programs entails a thorough examination of each member country's overall economic position and policy plan, including Lebanon. Once a year, IMF economists visit the member nation to gather and evaluate data as well as interview government and central bank officials. Staff present a report to the IMF Executive Board for discussion upon their return. The information gathered will be published in official publications and utilized as a source of information for studies and research. This is the situation with our next research.

Thus, the descriptive analysis is based on statistical data from the World Bank Databases-Data Catalog and Enterprise Surveys, What Businesses Experience. While the Data Catalog contains time series for some variables, the Enterprise Surveys, What Businesses Experience data were accumulated by interviewing business owners and senior managers between May 2019 and April 2020 (532 surveyed firms) and between April 2013 and September 2014 (561 surveyed firms). The interview's topic discusses financial sides like financial obstacles, access to funds from banks, banking loans relationship, owning banks account, and others many issues that determine credit aspects. It is the reason behind the consideration of those data as a precious source for our study. To verify the diversification of the sample and to underline the specificity of SMEs, figure 3 visualizes the distribution of surveyed companies by size, economic sector, and location for 2019.

As seen, the raw data is collected from firms in all the sectors of the economy – food production, manufacturing, wholesale and retail, and other services. Firms of all sizes have been included in the process of interviewing. Firms with 5-19 employees are defined as small firms. Firms hired between 20 and 99 are defined as medium-sized ones. Those having 100 and more employees are considered large firms. Firms from all the regions of Lebanon have been interviewed for collecting raw data. These regions are Mount Lebanon, Beirut, South Lebanon, Bekaa Valley, North Lebanon, and Nabatieh. These filters are part of the standard approach of compiling raw data that the World Bank applies.The total sample of firms surveyed includes 473 small and medium-sized firms and 59 large firms.

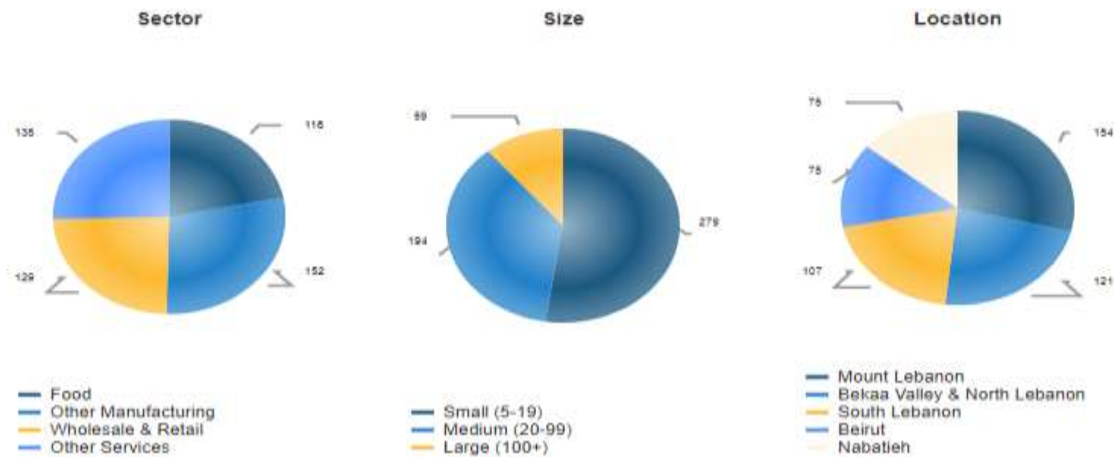

Fig. (3). Size, economic sector, and location of the enterprises interviewed in 2019.
Source: World Bank, Enterprise Surveys, What Businesses Experience.

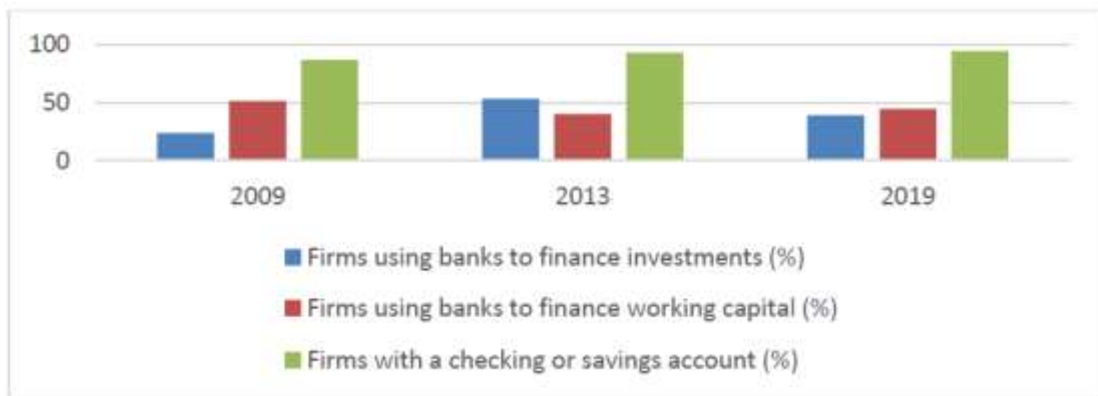

Fig. (4). Functional type of the bank-enterprise relations.
Source: World Bank, Data Catalog; Enterprise Surveys, What Businesses Experience.

An important aspect of bank-firm relationships is their "credit relation". Fig. (**1.4**) presents the indicators that describe those bank-firm intense relations in Lebanon. Over the three years analyzed, the percentage of firms with a bank account varies around 90 percent. An upward trend can also be observed, so that each subsequent year this rate exceeds that of the previous year. Therefore, the trend of increasing payment intermediation is sustainable and is reflected in the improved accessibility of the banks' payment services. Overall, the percentage of businesses with a checking or savings account has the highest values in 2019, which is the last year for which observations have been accumulated. Taking this variable into account, we can deduce that the Lebanese banking sector is well developed. This can be seen in a comparative way. The average value of this percentage for all countries is 88.6%, which is lower than that of Lebanon (94.3%). The percentage of Lebanese firms with a checking or savings account is much higher than the percentage of firms in the entire Middle East and North Africa region. For example, World Bank data shows that 79.6% of the total numbers of businesses in Middle East and North Africa region have a checking or savings account. Therefore, it would not be an overstatement to consider Lebanon as the financial capital of the Middle East (Deutsche Welle, 2021).

Fig. (**4**) also suggests some very interesting implications for the credit relationships of firms and commercial banks over the period of a business cycle. Business cycle theories have great potential to offer satisfactory explanations of developments in financial markets and banks and their relationships with the real economy. The business cycle determines the sectoral policies pursued by public authorities - government and central bank. The central bank sets its monetary policy in full accordance with the business cycle in order to smooth out cyclical fluctuations in the economy. However, monetary policy changes the credit policies of commercial banks. For example, during upturns in the business cycle, central banks raise interest rates to make external funds more expensive in order to avoid accelerating inflation in the economy. This can be seen in Figure 1.4. Firms give up borrowing to finance their working capital in the middle of the year (2013) of the cycle. In contrast, firms were using cheaper funds at the very beginning of the cycle (2009) and at the end of the upward movement of the Lebanese economy. At the same time, firms and banks prefer to use funds to finance long-term investments if they are more expensive. Thus, they borrow more to finance investment in the middle years of the cycle due to the restrictive monetary policy that is expected to reduce the supply of money and credit and thus increase

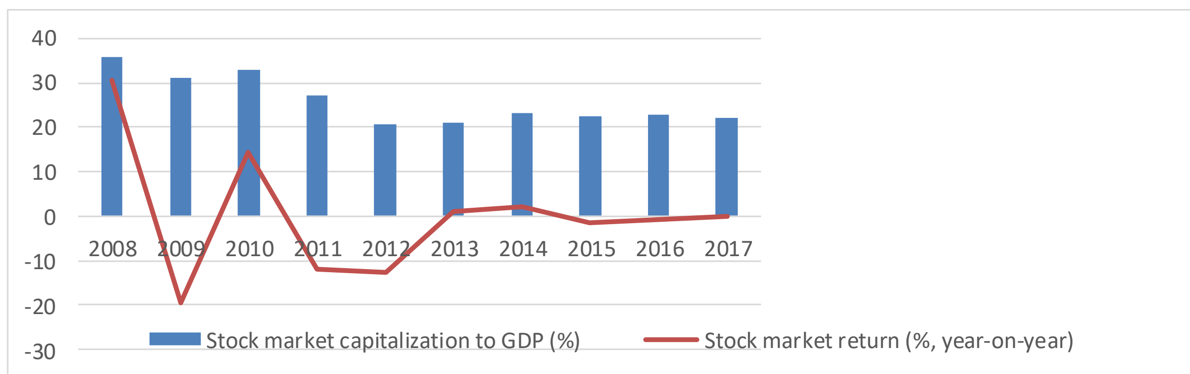

Fig. (5). Lebanese stock market performance.
Source: World Bank, Data Catalog.

the requirements imposed by banks to apply for a bank loan (Kashyap, *et al.,* 1993; Kashyap, et al., 1994; Disyatat, 2008; Aiyar, Sh., *et al.*, 2016). Banks and firms prefer to invest external funds in higher return projects but not in working capital.

International comparisons hide interesting details in the overall picture of the banking system and credit market in Lebanon. Considering the last year with detailed observations, we have the highest percentage of companies using banks to finance investments in Lebanon compared to the average values for all countries in the WB database and the average percentage for the Middle East and North Africa. What is interesting is that there are similar rates of companies using banks to finance investments in all countries (26.5%) and in the MENA region (27.7%). More concretely, 38.9% of Lebanese companies use banks to finance their investments. This figure is impressive and could be seen as evidence in favor of the hypothesis that Lebanese financial and banking systems are well developed. Similar implications could be suggested by the other indicator reported in the WB database - the percentage of firms using banks to finance working capital. As can be seen in Figure 1.4, this indicator has an opposite trend to the first one - firms using banks to finance their investments. There are also similar rates between all countries (30.0%) in the database and the Middle East and North Africa region (27.2%). Lebanese firms again have closer relationships with their banks.

Fig. (**1.4**) mirrored the fact that 44.5 percent of Lebanese firms use banks to finance their working capital. This is much higher than the rates in the other regions we mentioned. Moreover, Lebanese business units rely much more on banks to finance their working capital than in the other regions mentioned. This is evidenced by the proportion of investments financed by banks. While commercial banks finance 14.8% of the working capital of enterprises in all countries and 13.5% in the MENA region, Lebanese banks provide residential enterprises with funds representing 23.8% of their working capital. This close relationship between commercial banks and businesses in Lebanon is the main reason why they are considered "largely integrated in the Lebanese economy" and a cause of the "favorable and sustainable growth and performance" of the banking system in the country (Association of Banks in Lebanon, 2021). Its closest integration into and acceptance by the economy is currently visible in Figure 1.4.

4.4. Insight on the Lebanese Stock Market Development

The last section of this paper is devoted to the development of the Lebanese stock market. It is commonly accepted that the stock market is a place for large companies and banks, but its developments are important and representative of the dynamics of the overall economy. Banks and large companies use the stock market to acquire capital at lower cost. This approach is generally not available and applicable for small and medium-sized firms.

Fig. (**5**) presents the dynamics of the main proxies that have the potential to describe, in general terms, the performance and dynamics of the Lebanese stock market. These proxies are market capitalization and stock market performance. As it is obvious, market capitalization was seriously affected by the global financial and economic crisis that started in 2008. After that year, market capitalization declined on a sustained basis, so the initial economic recovery failed to bring it back to its pre-crisis level. The minimum point of the Lebanese market capitalization was reached in 2012, but no significant recovery took place after that year.

The stock market returns show the impact of the crisis in the best way. There were strong fluctuations that calmed down in 2013 and seem to be smoother after this year. Returns have the best potential to prove the financial crisis. They are the basis for evaluating market efficiency. This might be implied by the figure, but economists estimate the autocorrelations of daily returns to judge the efficiency of a stock market.

The objective of this section is to stress on the absence of any financial source for SMEs other than commercial Banks. That is what control the relationship between those two actors and maximize the oligopoly of the Lebanese banking sector at the financial market.

5. CONCLUSIONS

There were found proofs for close relations between enterprises and banks. Far more Lebanese enterprises rely on banks to finance investments and working capital than the average values for all the countries on the WB database and

the countries of Middle East and North Africa. These relations are the main reason for banks to be considered as largely integrated in the Lebanese economy. Collateral-based lending is well developed condition to get credits in Lebanon. Nearly half of the firms in Lebanon identify the access to finance as a major constraint. There was also found evidence for oligopoly type of the credit market in the country. Together, intensifying competition with digitalization also makes banks optimize their branch networks and bank machine coverage. All these points witness in favor of the assumption for a very well developed and modern banking system and crediting in Lebanon. Making use of the raw data of Lebanese Central Bank foundation, its characteristics and circulars, and the Basel agreement impact, the study presents evidence of the seriousness of the relation Bank-SMEs where SMEs rely on banks to finance their businesses, at the time where banks are extremely caution of lending risks. Lebanon's financial regulatory structure complies with international norms. Therefore, the general conclusion of the paper is in favor of the implication for very well developed, modern and efficient banking sector of Lebanon which creates favorable conditions for sustainable growth and development of Lebanese economy and society.

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