

# Road Maps, Growth and Financial Services

*Dr. Nasser Saidi*

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# Road Maps, Growth and Financial Services: Agenda

- Growth prospects: Global, Middle East & North Africa
- Challenges facing the MENA countries
- Governance & Policies for Reform
- Financial Services & the Insurance Industry: Some Reform Proposals

**Global Growth Prospects: Assessment as of September 8, 2003** (annual percentage real GDP growth rates)

Country or region	Year over year			Q4 to Q4		
	2002	2003	2004	2002	2003	2004
<b>Industrial countries</b>	1¾	1½	3	2½	2	3
United States	2½	2½	4	3	3½	3¾
Japan	¼	1½	2	2½	2	2
Western Europe	1	¾	2	1½	¾	2¼
United Kingdom	2	1¾	2¼	2¼	1½	2½
Euro area	¾	½	1¾	1¼	½	2¼
Germany	¼	0	1½	¾	¼	1¾
France	1¼	¾	1¾	1½	½	2¼
Italy	½	½	1¾	1	½	2¼
<b>Developing and transition countries</b>	4	3¾	5½	4	4	5½
Asia	6½	5½	7			
China	8	7¼	7¾			
India	5½	6	6½			
Others	4¾	3	6			
Latin America	-1½	1	4			
Argentina	-11	5	5			
Brazil	1½	1	4			
Mexico	1	1¼	4½			
Central and Eastern Europe	4¾	4¼	4½			
Middle East	1½	0	3			
Africa	3	2½	3½			
World (WEO weights)	2¾	2½	4¼	3¼	3	4¼

# Global & MENA Economic Prospects

- World economy recovering: 2 ½% first half 2003 to 3 ½% -4% in 2<sup>nd</sup> half
- Recovery led by US rebound: up to 4% in 3<sup>rd</sup> quarter. US for 30% of world GDP
- Upside risks: mutually reinforcing expansion, exceeding expectations
- Downside:
  - Equity markets recovery jeopardized if not justified by economic results
  - World oil prices
  - Declining stimulus from expansionary monetary & fiscal policies
  - Adjustment to decline in US\$ and Current Account deficit

# MENA Prospects

- War & insecurity had negative effects on growth, investment and capital flows
- Negative effects part compensated by higher oil prices
- Expect 0% to ½% growth for 2003, rebound to 3% in 2004

# Economic Costs & Consequences for Arab Countries

- Risk factors:
  - Future course of oil prices
  - Future of OPEC
  - Regional geo-strategic & political instability
  - Reform agendas
- Overall effect: lower growth over 2003-2005 by 1%-2%
- High dependence on remittances and unilateral transfers

# **The MENA Countries face numerous challenges**

- **Political, strategic**
- **Demography and labour force**
- **Macro-economic environment**
- **Governance**
- **Structural reforms**

# Globalisation is a major challenge

- Competition between countries, both macro and micro
  - Investment
  - Human capital
  - Technological innovations
  - Regulatory frameworks
- Limited International Economic Integration
  - Limited trade integration
  - 1.6% of total FDI- \$2,645 million in 2001
  - 3.6% of aggregate Net Resource Flows in 2001
- Challenge of competitiveness regime
  - Intellectual property protection to boost innovation
  - Compliance with international codes, norms and standards
  - New legislation and institutions to enter WTO and to adopt reforms

**OVERALL CHALLENGES  
OF GLOBALISATIONS...**



**... ARE ALSO  
CHALLENGES FOR  
MENA COUNTRIES**



# MENA Governance Issues

- Substantial natural resource wealth has not resulted in prosperity or economic growth
  - The region is ‘wealthy’ in natural resources, but poor in economic performance
- Governance issues along with wars, violence and insecurity have been retarding factors
  - Voice and accountability
  - Political stability: no violence
  - Government effectiveness
  - Regulatory quality
  - Rule of law
  - Control of corruption

# Core Principles for Good Governance

- Evidence from economic growth and financial crises
- Role & importance of good governance
- Evidence on Governance in MENA

# ‘New Institutional Economics’ & “Good Governance”

- Empirical evidence suggests that well performing institutions, enabling legal infrastructure, regulatory regimes and enforcement, “good governance” are major contributors to economic growth & prosperity and democracy
- “Good governance” is required by both government and business in MENA & Lebanon
- Good CG essential in MENA & Lebanon to compensate for *weak overall (i.e. public) governance*

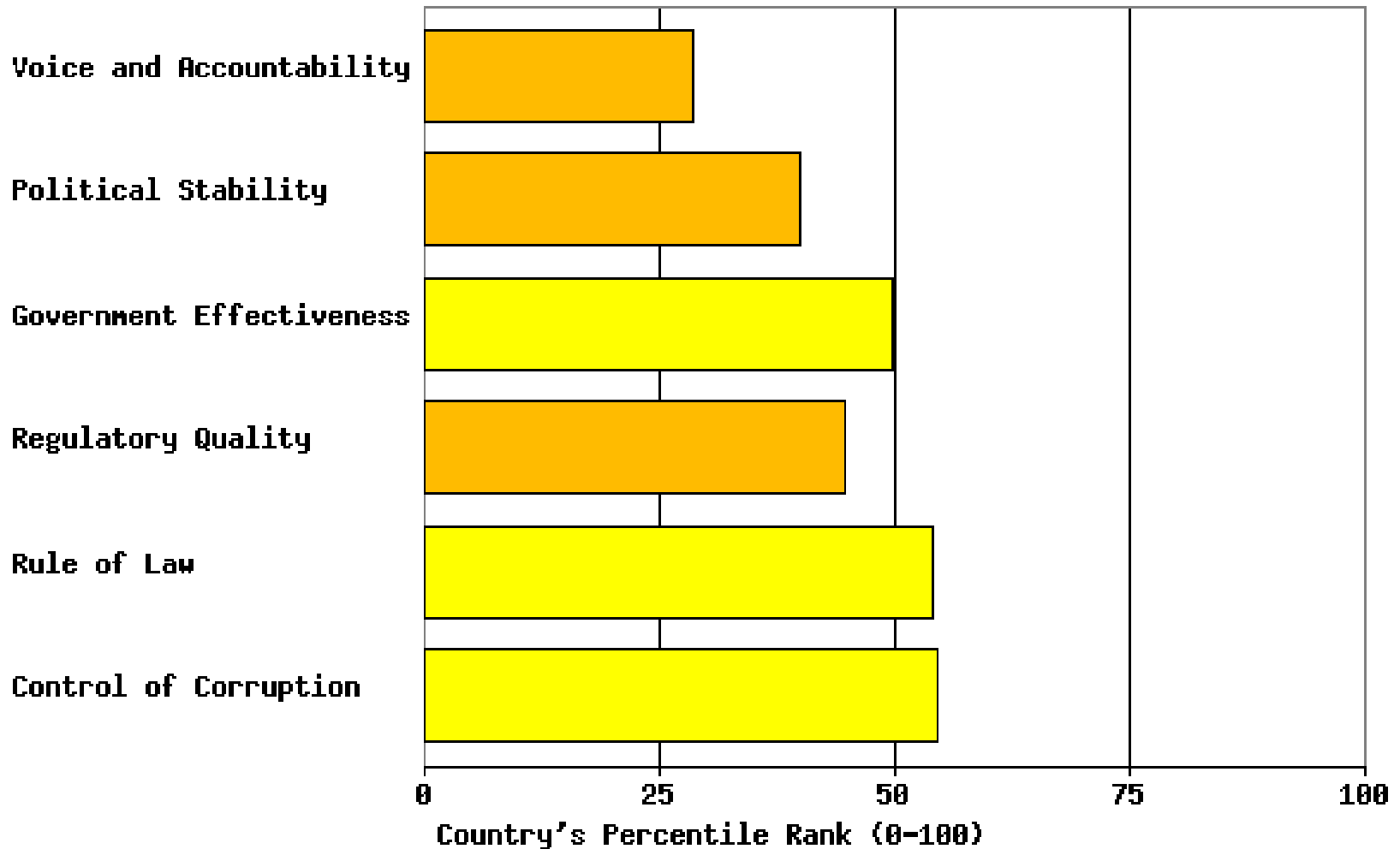
# Dimensions of Good Governance (Source: World Bank)

- Voice and accountability
- Political stability; No violence or conflict
- Government effectiveness
- Regulatory quality
- Rule of law
- Control of corruption



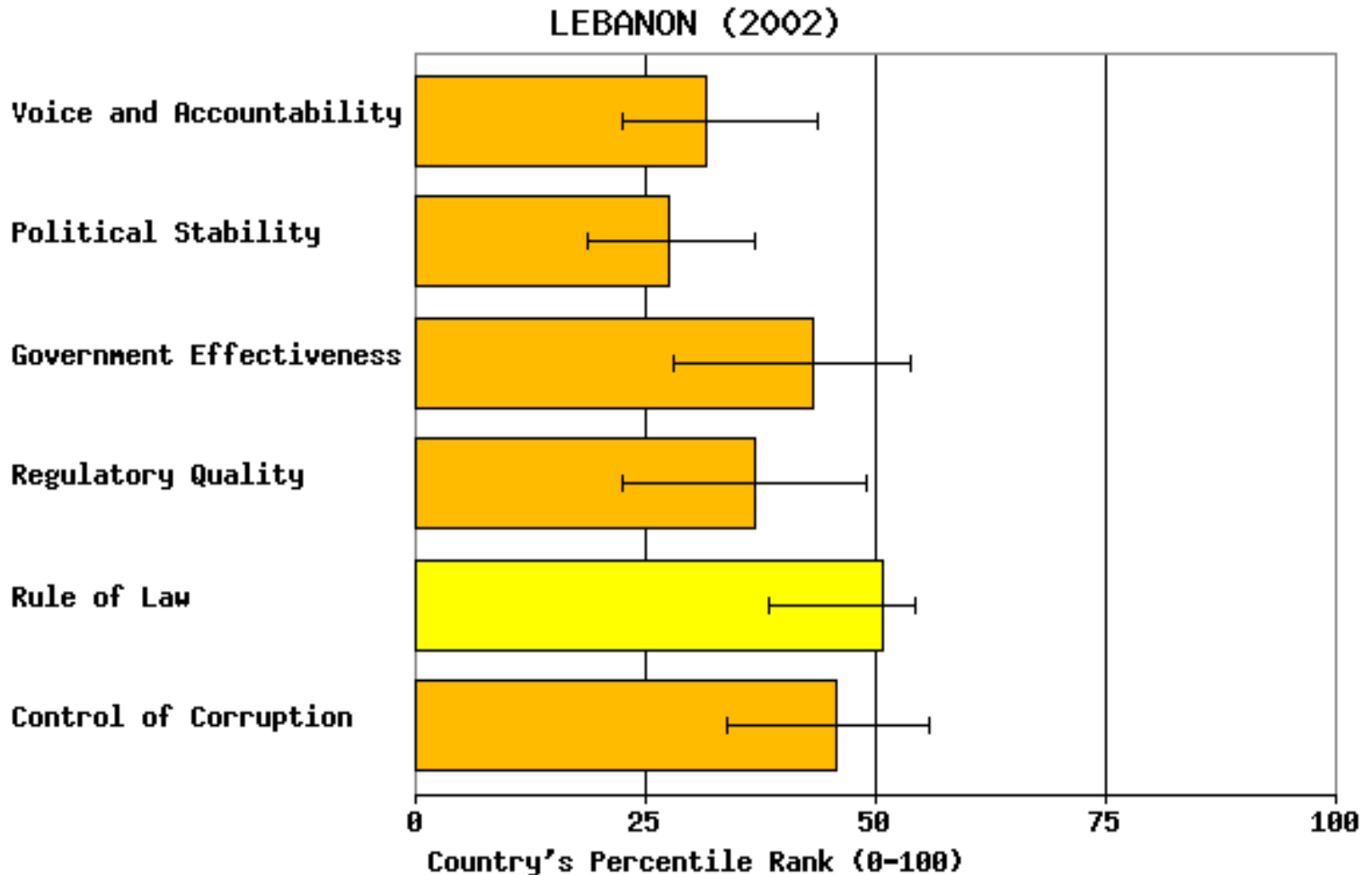
# MENA Governance Indicators

Middle East & North Africa – Regional Average (2002)



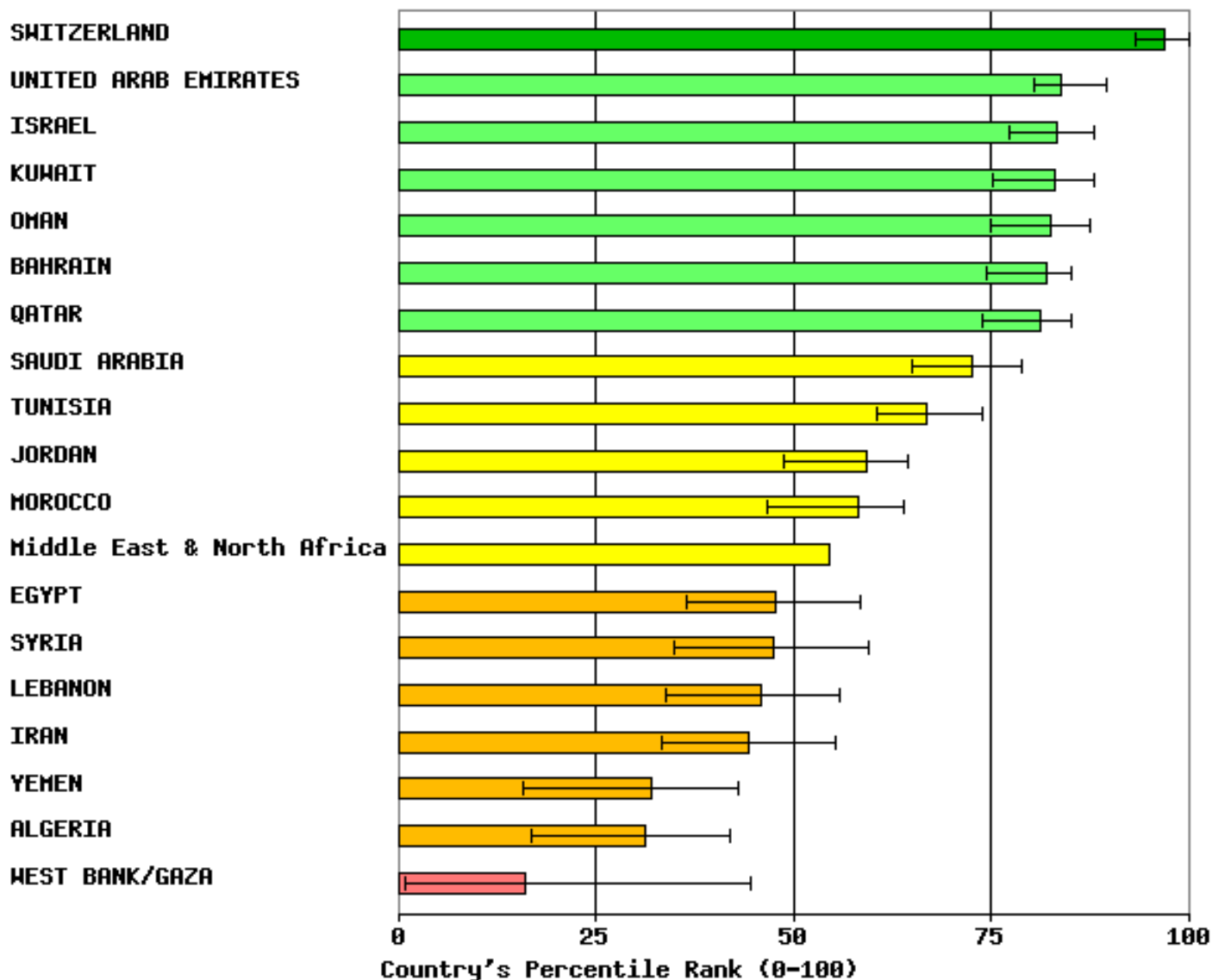
Source: D. Kaufmann, A. Kraay and M. Mastruzzi, 2003: Governance Matters III: Governance Indicators for 1996-2002 (<http://www.worldbank.org/ubi/governance/pubs/govmatters3.html>)

# Lebanon Governance Indicators



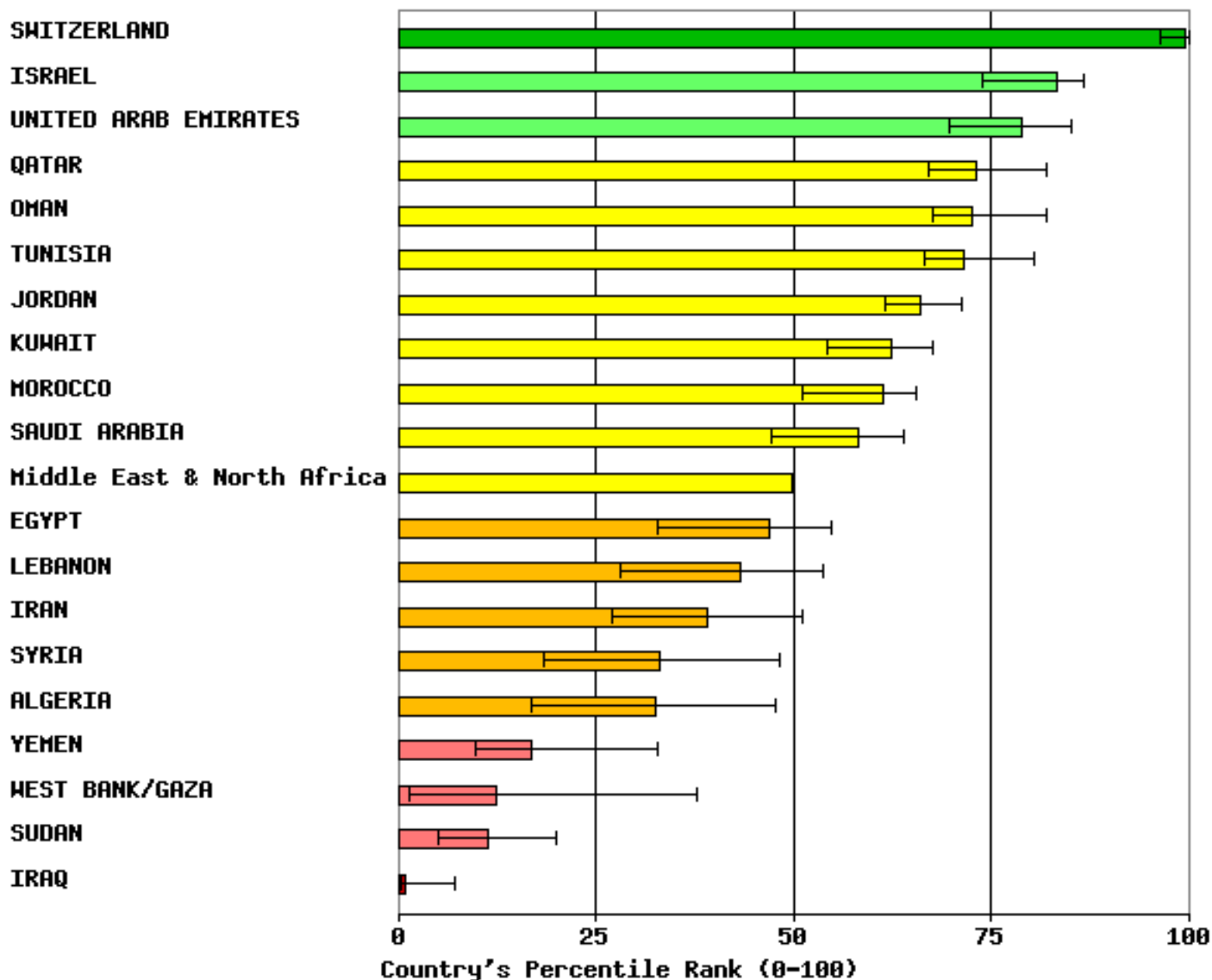
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## Control of Corruption (World, 2002)



Source: D. Kaufmann, A. Kraay and M. Mastruzzi, 2003: Governance Matters III: Governance Indicators for 1996-2002 (<http://www.worldbank.org/ubi/governance/pubs/govmatters3.html>)

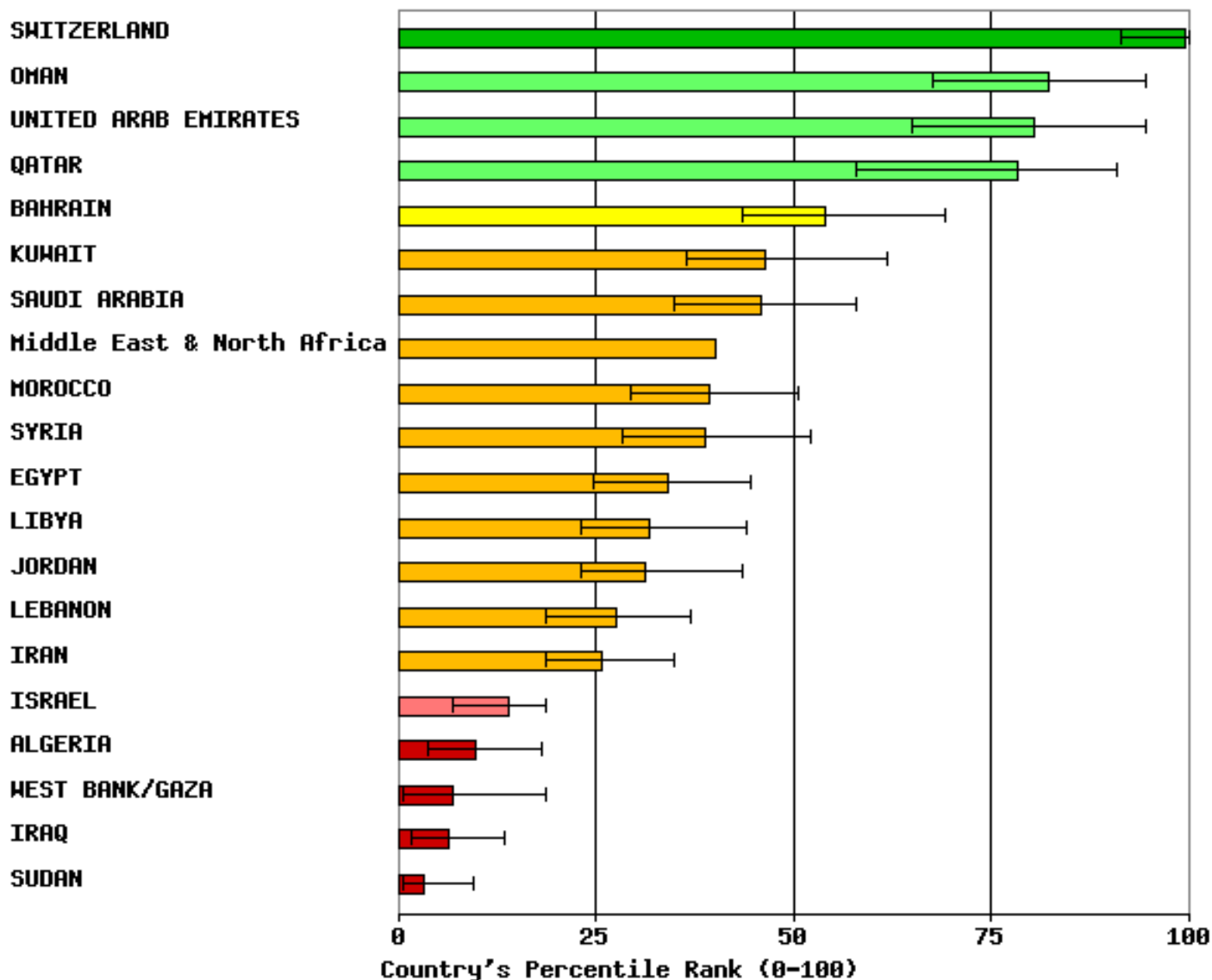
## Government Effectiveness (World, 2002)



Source: D. Kaufmann, A. Kraay and M. Mastruzzi, 2003: Governance Matters III: Governance Indicators for 1996-2002 (<http://www.worldbank.org/ubi/governance/pubs/govmatters3.html>)

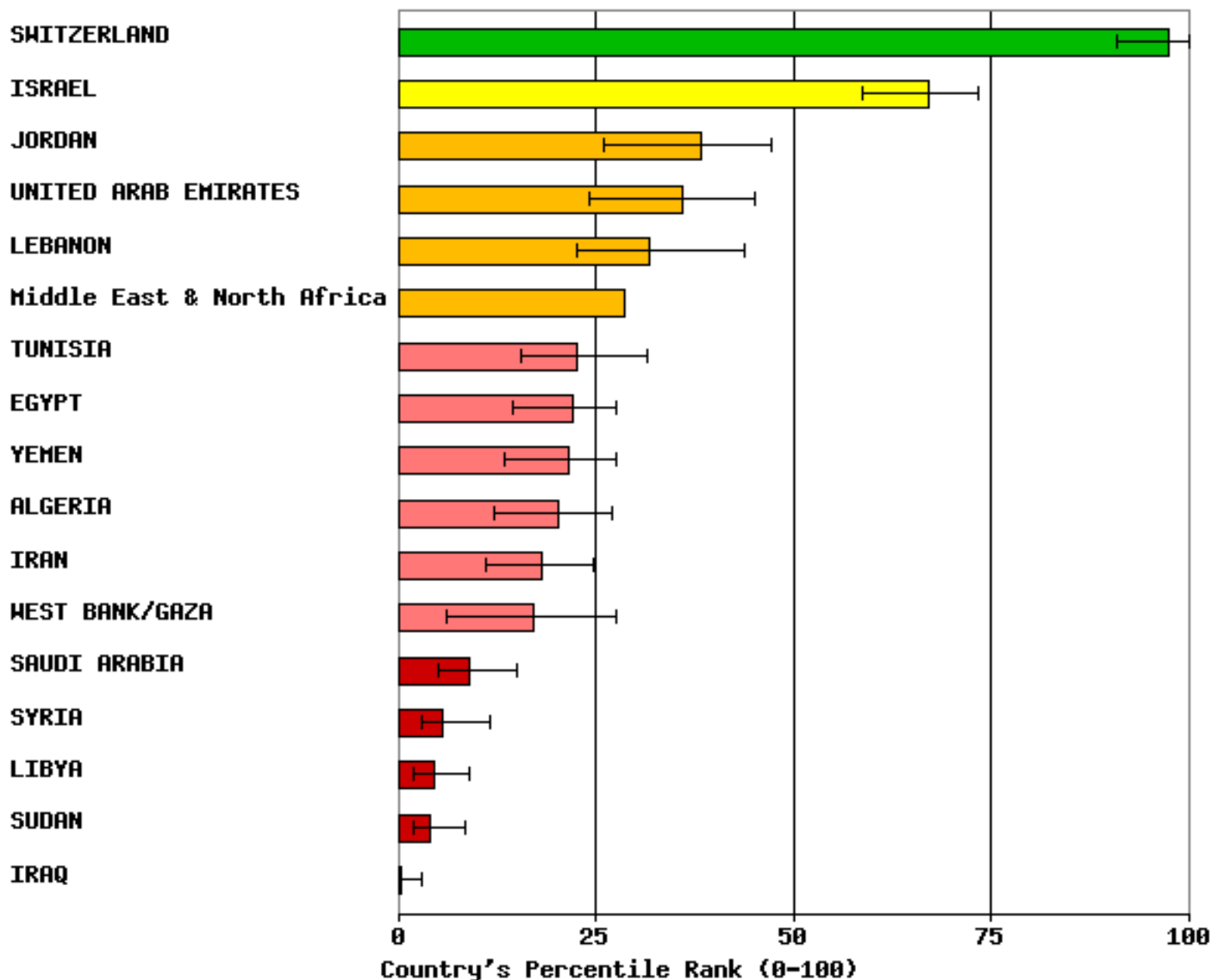


## Political Stability (World, 2002)



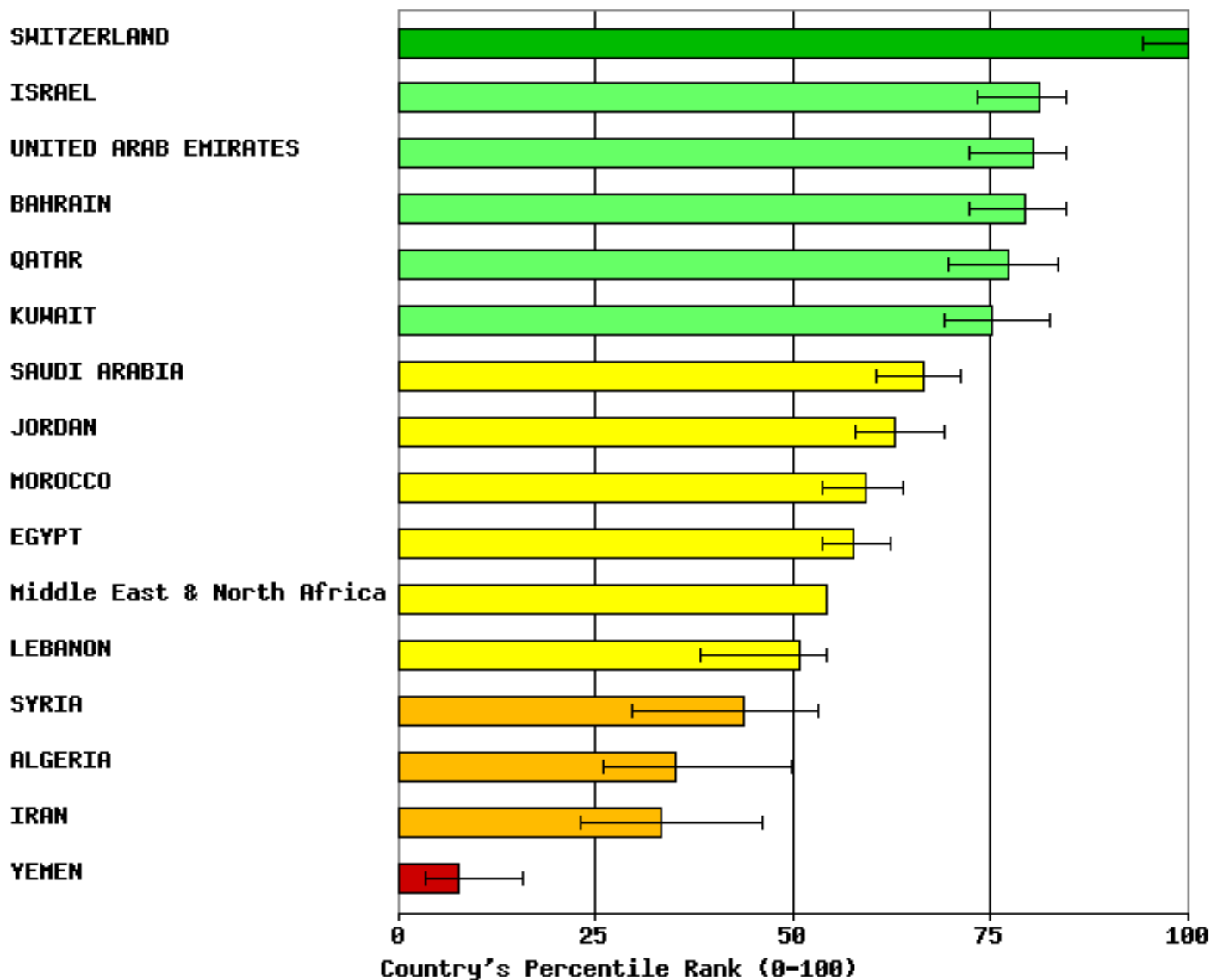
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## Voice and Accountability (World, 2002)



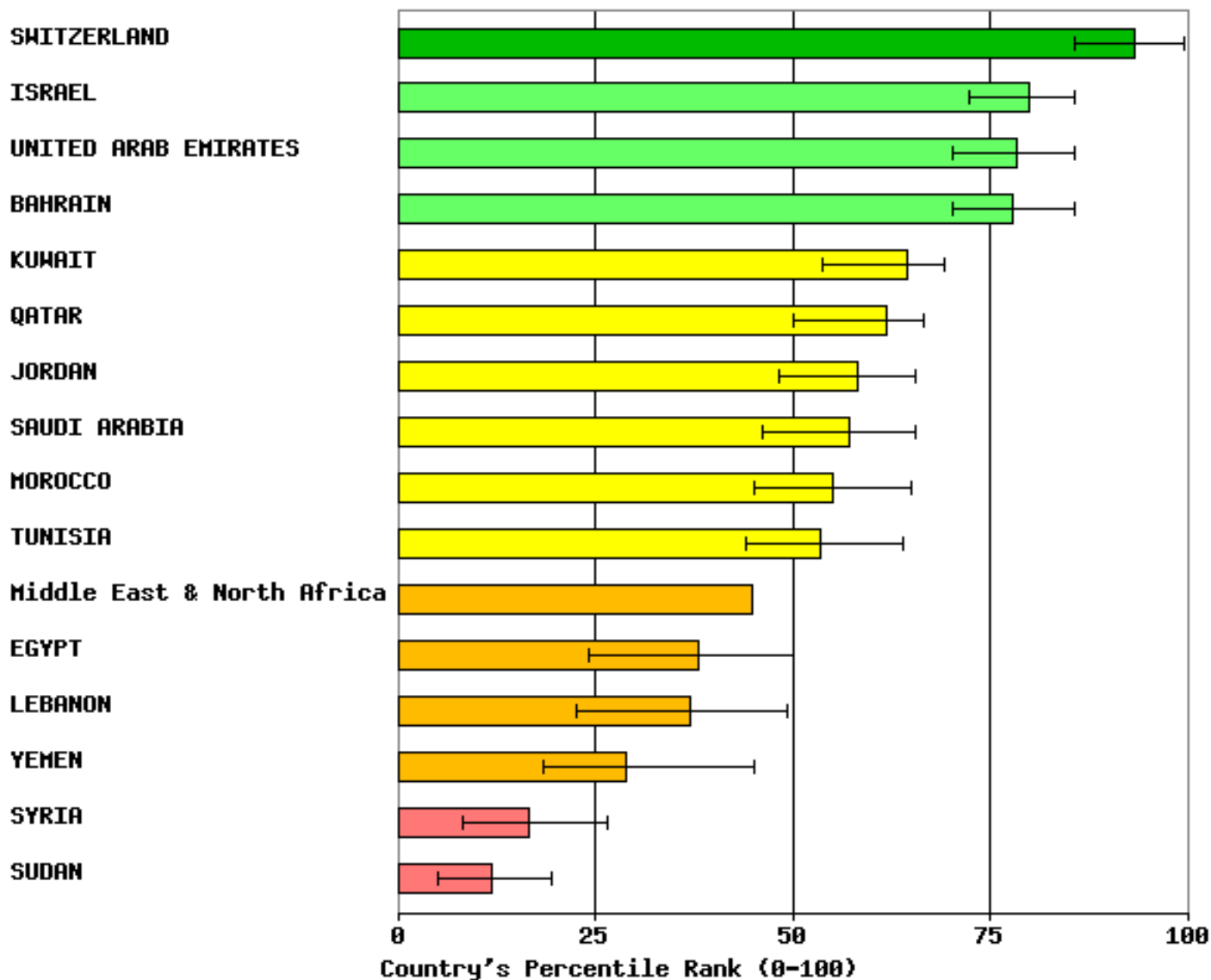
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### Rule of Law (World, 2002)



Source: D. Kaufmann, A. Kraay and M. Mastruzzi, 2003: Governance Matters III: Governance Indicators for 1996-2002 (<http://www.worldbank.org/ubi/governance/pubs/govmatters3.html>)

## Regulatory Quality (World, 2002)



Source: D. Kaufmann, A. Kraay and M. Mastruzzi, 2003: Governance Matters III: Governance Indicators for 1996-2002 (<http://www.worldbank.org/ubi/governance/pubs/govmatters3.html>)

# Changing World of Financial Services

## Three major factors affecting financial services

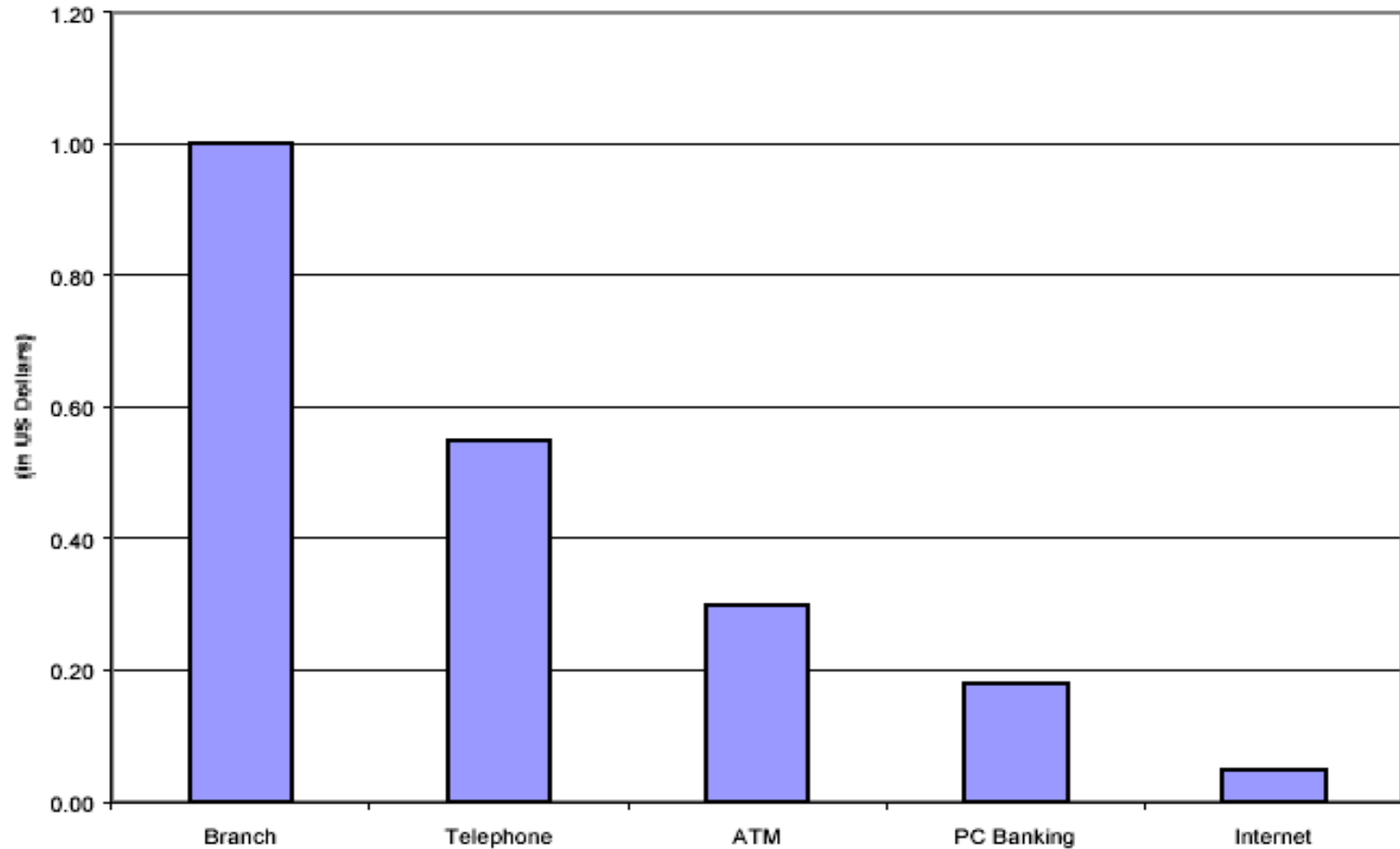
- Globalization: increase in capital flows, cross-border financial services, migration of trading/listing offshore:
  - Leading to increasing economic integration
  - Resulting in greater trade in financial services
  - and in cross border M&A activity
- Deregulation: geographic, markets and products:
  - New entry and increase of foreign presence in many domestic markets
  - Integrated banks offering a broad array of services
- Technological progress in Information & Communications Technology, particularly internet

# Changing World of Financial Services [2]

These factors are:

- Changing industrial structure for financial services (products and markets)
- Reducing costs of producing financial services and providing new delivery channels
- Providing large potential benefits to consumers and business clients, including governments

# Technology Reducing Cost of Financial Services



# Impact on Emerging Markets

- E-finance is growing rapidly in many emerging markets
  - many financial institutions are using best practice e-finance approaches, e.g., best banks in Brazil rival US banks
  - on-line brokerage expanding fast, e.g., in Korea more than 2/3;
  - many new trading systems being introduced; migration of listing and trading offshore rapid in some markets;
  - small markets and lack of institutional setups can allow for rapid progress, e.g., Estonia
  - forms of e-finance vary, e.g., more mobile (cell-phone) solutions in emerging markets
  - demand and institutional factors major constraint to growth



# Implications for Banking & Financial Sector Development

Our countries should leapfrog: not easy, but changes call for

- Revise view of financial sector development
- Role of government & central banks to change: selected leapfrogging to be considered more proactively, and monitoring of increased risk to participants
- Public policy needs to develop preconditions:
  - infrastructure (telecommunications) & **infostructure**
  - law and regulations to enable eBanking and eFinance
  - Security
  - Competition policies
  - From institutional to more functional approach to regulation and supervision

# Changes in Public Policies

- Enabling environment
  - Communications Infrastructure
  - Electronic Security Arrangements
  - Information Infrastructure
  - Legal framework and enforcement Risk related regulations
- Competition policy
- Managing risks
  - Institutions/prudential
  - Consumer/investor protection

# Regulatory Environment

- Credible and transparent regulatory environment
- Regulatory environment must not be perceived to be under control or influence of any particular interest group
- Regulators should be independent from industry and from political parties

# Financial services: Institutional Reforms & Governance

Major Reform Areas:

1. Social Security Reform
2. Develop the Capital Markets
3. Focus on Governance of Banking and Financial Services

# Financial Stability & Soundness Standards

- **Macroeconomic Policy and Data Transparency**
- **Institutional and Market Infrastructure**
- **Financial Regulation and Supervision**

# Macroeconomic Policy and Data Transparency

- Monetary and Financial Policy Transparency
  - Code of Good Practices on Transparency in Monetary and Financial Policies IMF
- Fiscal Transparency
  - Code of Good Practices in Fiscal Transparency IMF
- Data Dissemination
  - General Data Dissemination System IMF
- Data Compilation

# Institutional and Market Infrastructure

- Insolvency & bankruptcy World Bank
- Corporate Governance
  - Principles of Corporate Governance OECD
- Accounting
  - International Accounting Standards (IAS)
- Auditing
  - International Standards on Auditing (ISA)
- Payment and Settlement
  - Core Principles for Systemically Important Payment Systems BIS
  - Recommendations for Securities Settlement Systems CPSS/IOSCO
- Market Integrity
  - Forty Recommendations + 8 Special Recommendations Against Terrorist Financing of the FATF
- Market Functioning

# Financial Regulation and Supervision

## Banking Supervision

- Core Principles for Effective Banking Supervision BCBS
- Securities Regulation
  - Objectives and Principles of Securities Regulation IOSCO
- Insurance Regulation
  - Insurance Core Principles IAIS
- Financial Conglomerate Supervision



# Lebanon's Compliance with Financial Soundness Standards

- *Monetary and financial policy transparency/ Code of Good Practices on Transparency in Monetary and Financial Policies*, with the issuing body being the IMF.
  - Lebanon has achieved substantial progress in this area
- *Fiscal policy transparency/Code of Good Practices in Fiscal Transparency*; the issuing body is the IMF.
  - Lebanon is seeking to implement the Code
- *Data dissemination/ Special Data Dissemination Standard (SDDS)/General Data Dissemination System (GDDS)*, IMF
  - Lebanon has now entered the GDDS and the Central Bank, with assistance from international institutions (IMF, World Bank) is establishing the Lebanese Statistics Portal (LebStat), which will provide a statistics gateway, a single-access point to available economic, social, financial and real sector data

# Lebanon's Compliance with Financial Soundness Standards

- *Insolvency and Bankruptcy Procedures*
  - The World Bank is assisting the Lebanese government in drafting modern insolvency and bankruptcy laws. Principles of bankruptcy are essential for the viability of corporate governance.
- *Principles of Corporate Governance*
  - The standard defined by the OECD awaits formal adoption in Lebanon by relevant institutions such as Chambers of Commerce, business & professional associations
- *Accounting*—International Accounting Standards, issued by the IASB
  - Lebanon recognizes the IAS, but there is no mandatory implementation by business or effective enforcement.
- *Auditing*—International Standards on Auditing, issued by the IFAC
  - Lebanon recognizes the ISA, but there is no compliance mechanism for the auditing and related professions.

# Lebanon's Compliance with Financial Soundness Standards

- *Payment and Settlement*— Core Principles for Systemically Important Payment Systems and the Recommendations for Securities Settlement Systems, issued respectively by the BIS-CPSS and the BIS-IOSCO
  - Lebanon has, with the assistance of the IMF, modernized its payments media and systems, bringing them into compliance with BIS Core Principles and related recommendations
- *Market integrity*—40 Recommendations of the Financial Action Task Force (FATF) and 8 Special Recommendations Against Terrorist Financing, issued by the FATF.
  - Lebanon has issued and enforces a modern Anti-Money Laundering Law (No. 318, April, 2001)

# Lebanon's Compliance with Financial Soundness Standards

## *Banking supervision*

- Lebanon is at the forefront among emerging economies in the application of the Core Principles for Effective Banking Supervision issued by the BIS and related measures, such as the creation credit and audit committees, general audit, and independent surveillance reporting that are directly accountable to the board of directors. It has a well-managed, professional and independent Banking Control Commission.

# Lebanon's Compliance with Financial Soundness Standards

- *Securities regulation*—the standard is the implementation of the Objectives and Principles of Securities Regulation, issued by the IOSCO.
  - Lebanon cannot effectively enforce principles and regulations in this key area, until the government establishes an independent capital market authority with the relevant mandate
- *Insurance supervision*— Insurance Core Principles (ICP), issued by the IAIS
  - An independent Insurance Control Commission has been established as a result of passage of a Law (in 1999) leading to extensive reform of the insurance industry in Lebanon.
  - However, policy measures have yet to be taken to implement the ICP.

# Recommendations & Proposals I

- Change attitudes: highlight high value of effective, transparent & accountable public & corporate governance
- CG practices matter more in Lebanon due to weak overall governance, protection of minority shareholder rights, legal & judicial systems
- Standardize Accounting and Auditing Practices

# Recommendations & Proposals II

- Families/Entrepreneurs should contribute to development & well-functioning of financial markets
- Reforms:
  - Amend Laws to protect investors and minority shareholders
  - Introduce separation between Board and Management
  - Modernize & Reform Insolvency & Bankruptcy Law
  - Introduce a comprehensive Capital Markets Law
- Appoint a Commission to develop set of Core Principles for Good Corporate Governance

# Core Issues for the Future

- Complete legal infrastructure:
  - Enact draft “Organization of Capital Markets Law”
  - Enact Draft “Securitization Law”
  - Enact Draft “Mutual Funds Law”
- Set-up independent regulatory body: *Capital Markets Authority* to create a better regulatory environment
- Create a more complete financial market structure: develop active secondary capital markets
- Develop *Securities Law* to include Options & Derivatives and Securities Lending



# Draft “Capital Markets Law”: main provisions

- Organizes the capital markets
- Independent Capital Markets Authority
- Independent, private, capital markets operators
- Central Depository
- Guarantee Fund for Investors
- Administrative Procedures
- Special Court for Capital Markets

# Core Issues: Social Security, Pensions System & Privatization

- **Social Security Reform & Pension System**
  - Pillar I : A Publicly administered defined benefit basic retirement benefit to all workers funded through the social security tax.
  - Pillar II: A Publicly administered defined contribution retirement benefit based on contribution by workers to their own individual accounts.
  - Pillar III: Privately run retirement supplementary schemes.
- **Develop the Capital Markets to allow Initial Public Offering (IPO) of Privatization Issues**

# Insurance Sector Reforms

- Facilitate Mergers & Acquisitions and consolidate insurance sector
  - Allow cross-border M&A
- Privatize the Insurance sector in MENA and prepare for GATS
- Reform SocSec
- Build on Insurance Reform Law (1999)
- Expand scope of Financial Intermediation Law (1999) to encompass Insurance Brokers
  - Introduce licensing process
- Set-up *Centralized Insurance Reporting* similar to the Centrale des Risques

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***Thank you***

**Q & A**