

RIAD TOUFIC SALAME

Governor of the Lebanese Central Bank

The central banks are, in fact, looked at or entrusted to keep the confidence in the economy, so that the economy can grow and credit can flow. The task of the central banks has been more difficult because of external developments to the traditional scenery that they used to work on. One of these is the development of the financial markets. These markets have been creating their own dynamics. They are completely detached from economic realities and they have, by themselves, created their own world that makes it difficult for central banks to pre-empt crises with the traditional tools that were used. There is the appearance of hedge funds, which have great potential, the possibility of short sales without any restriction, and the development of black boxes that trade only on mathematical formulae without any human intervention and control sizable amounts. You can remember when there was one mistake in one programme in New York; the stock market fell 10%, without any explanation. Later, we knew the cause. We have experienced, in Lebanon, such phenomena, where we see, sometimes, our bonds being shorted. We do not understand the reason. Then, we understand that there is a mathematical formula linking various markets and countries that dictated such a position. All of this has an impact. It has an impact on stability. It has an impact on the capital inflows and outflows and it has an impact on confidence that is more damaging for the economy than two other mentioned sources. We have also seen actions by the rating agencies that have aggravated certain crises previously. Sometimes, their movements are unexpectedly deep and unexpectedly strong, whereby they can bring down, without any recourse, a country, a product, or an institution from investment grade almost to a failure grade. These operations are not really being followed or controlled by anyone. I know that the European Union has passed laws, now, to try to instil some order in the activities of rating agencies. During the sub-prime crisis in 2008, these instruments that were investment grade went to a default grade, suddenly. We have seen the same approach in certain European countries or, if we go back in history, in certain Asian countries.

Today, one of the responses to neutralise the effect of rating agencies is to maintain the stature and the respectability of the Central Bank, so that it can counteract or neutralise the reactions that might be created by these ratings agencies. It is very difficult and only a few central banks in the world have been able to keep such a position that would allow them to neutralise the effects of rating agencies.

On the other hand, Monsieur Trichet has talked about the 2008 crisis. However, today, the response to avoid another crisis is not yet convincing to the markets. We have seen this in the fact that the existing liquidity for lending is huge, but the demand for that liquidity is not important. That is costly, in terms of growth and in terms of creating employment. To serve stability and growth, I think that one should, on one side, regulate the rating agencies. Also, one should create controls on other players in the market that are, today, working outside any regulation, such as the hedge funds. There should be a separation between the investment banks and the commercial banks, to protect savings and to, once again, create confidence in the banking industry. As you know, people sometimes buy bonds with negative yields, instead of keeping their money deposited at the bank. One should also put the supervision agencies under the umbrella of the Central Bank, so that there is someone looking at the entire system and so agencies that have not been talking to each other will, at least, report to one authority that can pre-empt a systemic crisis. Perhaps, one should think about creating a specialised agency to control the hedge funds and the differently structured products.