IS GOOD GOVERNANCE, AN OXYMORON?

THE LEBANESE MULTIFACETED PREDICAMENT

1)INTRODUCTION

Whenever significant adversity erupts somewhere on the planet, governance bears a considerable if not the whole responsibility. Be it local or global, economic, financial, social, or even environmental, in the private or public sector. What is it about this phenomenon that makes it so difficult to subdue? For the sake of our analysis, we bring forth hereafter one of the most salient and timely cases from around the world; the multifaceted Lebanese predicament. The present paper strives to examine this flagrant governance deficiency case in light of the management theory and the international norms and best practices. The work addresses both the public and corporate governance through the conduct of Lebanon's central bank (BDL) as well as the majority of the nation's commercial banks since the early nineties to date.

2) THE PROBLEM

The country is currently facing the most challenging economic, financial, and social crisis since its independence in 1943. The Lebanese pound lost to date more than sixty percent of its value against U.S.Dollar in the parallel market. Food prices have shot up as a result. Unemployment soared, the economy is almost coming to a halt exacerbated further by the corona pandemic. Imports of goods and even critical medical stuff has plummeted. Foreign currency in the dollarized economy is becoming very scarce. Banks have effected a de facto capital controls choking the economy even further. As a result, the Lebanese diaspora has reduced transferring their vital remittances, thus more aggravating the crisis. Foreign inflows, mostly from the Gulf states, have sharply dwindled in the last few years. The situation has reached a point where the government of Lebanon (GOL) suspended in March 2020 for the first time the payment of its sovereign debt.[1]

Conversely, that same government has responded with a Financial Recovery Plan (FRP) targeting an international financial relief package against long-awaited structural reforms. These include rebalancing the government's budget by improving tax collection, recuperation of stolen assets, reforming the tax system, improving the spending efficiency, and enhancing the financial management and the essential services/utilities in the public sector. The FRP also comprises restructuring the spiraling public debt and fighting corruption. The long-standing anchor of the Lebanese pound to the US dollar appears to be coming to a gradual end. Also, the plan aims to fairly restructure the financial system, including the central bank and the commercial banks. Besides, the FRP has specified aggregated losses of LBP177 trillion in the BdL balance sheet, and LBP64 trillion direct aggregated losses in the commercial banks' balance sheets.[2]

Furthermore, the international banker's analysis attributes the crisis to many factors, the most poignant of which is the monetary policy since the nineties:

> Several factors have led to Lebanon's current quagmire, but few have been more impactful than the country's rather bemusing monetary policy over the last decade. During this time, the central bank, Banque du Liban, liberally hiked its interest rate for depositors to fund the government's spiralling debt problem, as well as to pay for its substantial volume of imports, and to draw in dollars to help maintain the Lebanese pound's 22-year-old peg to the US currency. Many have called the central bank's behaviour during this time as being akin to running a Ponzi scheme. Banks' incoming

[1] "Starved of Dollars and Drowning in Debt, Lebanon's Economy Sinks Fast," *Reuters*, March 12, 2020, https://www.reuters.com/article/us-lebanon-crisis-economy-insight-idUSKBN20Z1FC.

[2] "The Lebanese Government Financial Recovery Plan," April 30, 2020, 1–2.

> customer dollars were lent to the central bank at attractively high rates, and in return, they purchased government debt, all the while making consistent profits on such transactions. It is not surprising, then, that deposits placed with the central bank between 2017 and August 2019 swelled by a whopping 70 percent. The dividends paid out by banks, moreover, went to shareholders, of whom many were politicians and who were thus incentivized to continue with the scheme.[3]

Indeed, inadequate policies and malfeasance will come to an end eventually.

Nevertheless, signs of the escalating stress on the Lebanese pound and the commercial banks have been apparent many years back. One crucial sign is the central bank's (CB) dwindling foreign exchange reserves despite his constant borrowing from commercial banks at incrementally high-interest rates. Another significant sign is the unprecedented steady deficit, as of 2011, in the balance of payment. This is not to mention the chronic government budget deficit.[4]

On the other hand, Carnegie Middle East Center expectedly attributes the country's affliction to governance and the political system: "The economic crisis is, at its core, a governance crisis emanating from a dysfunctional sectarian system that hindered rational policymaking and permitted a culture of corruption and waste. The country, led by the public sector, lived beyond its means. Decades of pursuing this model left the economy with high debt and a bloated banking sector.[5]

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[3] International banker, "What Is Behind Lebanon's Deepening Financial Crisis?," International Banker, February 10, 2020, https://internationalbanker.com/finance/what-is-behind-lebanons-deepening-financial-crisis/.

[4] "Lebanon: Anatomy of a Currency Crisis," *Middle East Transparent* (blog), November 23, 2019, https://middleeasttransparent.com/en/lebanon-anatomy-of-a-currency-crisis/.

[5] Firas Abi Nassif et al., "*Lebanon's Economic Crisis: A Ten Point Action Plan for Avoiding a Lost Decade*," Carnegie Middle East Center, accessed May 6, 2020, https://carnegie-mec.org/2020/01/06/lebanon-s-economic-crisis-ten-point-action-plan-for-avoiding-lost-decade-pub-80704.

3)<u>BACKGROUND</u>

The word “governance” came from the Latin verb “gubernare,” or more originally from the Greek word “kubernaein,” which means “to steer.” Basing on its etymology, governance refers to the manner of steering or governing, or of directing and controlling, a group of people or a state.[6] Merriam Webster dictionary attributes the first use of this word to the 15th century in the following defined meaning: “the act or process of governing or overseeing the control and direction of something (such as a country or an organization).”[7] The Unesco’s International Bureau of Education provides a more contemporary, comprehensive, and specific description:

> Governance has been defined to refer to structures and processes that are designed to ensure accountability, transparency, responsiveness, rule of law, stability, equity and inclusiveness, empowerment, and broad-based participation. Governance also represents the norms, values and rules of the game through which public affairs are managed in a manner that is transparent, participatory, inclusive and responsive. Governance, therefore, can be subtle and may not be readily observable. In a broad sense, governance is about the culture and institutional environment in which citizens and stakeholders interact among themselves and participate in public affairs. It is more than the organs of the government.[8]

Hence, governance has to do with more than just the conventional institutional frameworks and methods. It has to do with a society's culture and values, among others.

On the other hand, the World Bank (WB) Worldwide Governance Indicators (WGI) project provides a somehow different definition of governance that is more focused on governments rather than the wider general scope. It holds: “Governance consists of the

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[6] “What Is Governance?,” *Law, Politics, and Philosophy* (blog), August 21, 2014, https://tamayaosbc.wordpress.com/2014/08/21/what-is-governance/.

[7] “Definition of Governance,” accessed May 4, 2020, https://www.merriam-webster.com/dictionary/governance.

[8] “Concept of Governance,” International Bureau of Education, May 26, 2015, http://www.ibe.unesco.org/en/geqaf/technical-notes/concept-governance.

traditions and institutions by which authority in a country is exercised. This includes the process by which governments are selected, monitored and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them."[9] Else, the UN chronicle attributes the vigorous emergence of the term "good governance" to the collapse of the Berlin wall and to the 1990s fall of South Africa's apartheid regime. The late UN secretary-general kofi Annan delineated: "Good governance is perhaps the single most important factor in eradicating poverty and promoting development."[10] Moreover, the World Bank specifies governance in the public sector and Anticorruption as the development preferences of utmost significance.[11] Today, many types of governance exist. The ones most relevant to our study are corporate governance concerned with running organizations, public sector governance, and international financial and economic governance.

4) THE STRATEGIC PLANNING ANGLE

Translating governance practice, strategic planning is a fundamental function in every organization that is mainly the responsibility of top management. It consists of determining the organization's goals, analyzing its environment, scrutinizing its resources, specifying the activities necessary to drive the firm towards achievement of its goals, and lastly, executing these activities and supervising progression. The defined goals usually

[9] "WGI 2019 Interactive > Home," accessed May 2, 2020, http://info.worldbank.org/governance/wgi/.

[10] "Global and National Leadership in Good Governance | UN Chronicle," accessed May 5, 2020, https://unchronicle.un.org/article/global-and-national-leadership-good-governance.

[11] "Overview," Text/HTML, World Bank, accessed May 3, 2020, https://www.worldbank.org/en/topic/governance/overview.

guide the evaluation of the environment and the resources. Moreover, goals will have to be specific and able to be measured. Besides, it is fundamental to properly examine the environment, including the economy, markets, competition, the physical environment, and regulatory and social medium. Carefully analyzing every one of these sides is essential because menaces, as well as opportunities, can emanate. It is common practice in the majority of organizations to review strategic planning every year or two. That is because the environment is in continuous change resulting in a change in risks and opportunities.[12] The evaluation of the resources should define whether they are appropriate to confront the threats and to benefit from the opportunities. On the other hand, strategic planners usually consider alternative planning scenarios. These might rely on sluggish, average, and rapid economic growth. Another possibility is to establish a resource assessment on favorable, unfavorable, and best estimate of revenues or share of the market. The simulation of different scenarios enables the planner to acquire a more realistic view of the effects of every alternative.[13]

Worth mention the notion of "Strategic improvising," and the essentiality of proactive and continuous monitoring of the business environment to discern relevant trends and patterns as early as possible. That is particularly vital since the environment is the backbone of strategy. Moreover, the business environment might change faster than expected to make the strategy wrong or futile. Hence, the need to take also the short term aspect into account while formulating the long term strategy, and to revise it accordingly

[12] Tom Gorman, *Complete Idiot's Guide to MBA Basics*, 3rd ed. (USA: Penduin Group, 2011), 355–58.

[13] Gorman, 367.

regularly.[14] On the same subject, Steven Silbiger confirms: “Strategy is dynamic. Executives must review their strategy continuously to ensure that it reflects the changes in the business environment, the company, and its goals.”[15] Moreover, management devising contingency plans is essential in any organizational frame.[16]

In terms of Banque Du Liban’s (BDL), article 70 of the Code of Money and Credit specifies its core mission and goals as, among others, preserving monetary and economic stability, as well as ensuring the health of the banking sector, and the development of money and financial markets.[17] The strategy or policy adopted by BDL to achieve those goals was based primarily on pegging the currency to the US dollar. Then, defending it by accumulating foreign currency reserves from remittances, foreign direct investments, and a usually positive balance of payment. Whenever needed BDL hiked interest rates to attract foreign deposits. All of that, while servicing GOL's persistent and sizeable budget deficit with a swelling public debt.

However, the environment has changed since 2011. According to the International Labor Organization (ILO), the Syrian war erupted, imposing negative implications on the Lebanese economy and the labor market. Growth of the economy lingered, private investments slumped, the deficit of trade widened, and the two most significant sectors of real estate and tourism have plummeted.[18]

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[14] Kathleen Allen and Peter Economy, *Complete MBA for Dummies* (Indiana, USA: Wiley Publishing, Inc., 2008), 76.

[15] Steven Silbiger, *The Ten-Day MBA*, 3rd ed. (HarperCollins, 2009), 363.

[16] Gorman, *Complete Idiot’s Guide to MBA Basics*, 16.

[17] “Code of Money and Credit.Pdf,” 12, accessed May 11, 2020, http://www.databank.com.lb/docs/Code%20of%20Money%20and%20Credit.pdf.

[18] “Wcms_240130.Pdf,” accessed May 26, 2020, http://www.ilo.org/wcmsp5/groups/public/@arabstates/@ro-beirut/documents/genericdocument/wcms_240130.pdf.

On the other hand, it is well known that the governing political class typically is responsible for directing the economy of a nation. Unfortunately, no proper accountability exists in that republic's governance system, making the long-coveted reforms a far fetched goal. However, remittances from the nostalgic Lebanese diaspora and a spree of generous international financial assistance as of the 1990s, allowed the system to hobble further unreformed. Two indicative samples of this costly governance ineptitude are the chronic disastrous failure to resolve the electricity sector problem and the more recent protracted lack of transparency and effectiveness in confronting the present-day adversity.

Furthermore, a significant change in the international environment extended to Lebanon a precious opportunity that the country, unfortunately, wasted again. The country perceived as a safe refuge received billions of dollars in the wake of the 2008 international financial upheaval. These could have been used to remedy the electricity sector, expand the economy, boost the export manufacture, and get rid of the risky, costly, and unsustainable currency peg. Moreover, this latter has weakened the competitiveness of Lebanese goods and services due to its unrealistically vigorous exchange rate. Consequently, export industry growth has been hampered. Besides, the influx of funds has been squandered on extravagant import consuming, sterile real estate ventures, and profuse expenditure by the government.[19] An expected consequence when ill and unchecked economic policies prevail.

In continuation, the Lebanese center for policy studies (lcps) prominently elaborates on the poor governance of the CB:

> The responsibility also lies with BdL's decision-makers for their mismanagement of the country's monetary policy, their lack of transparency and data availability, and their

[19] "Lebanon's Financial Crisis: Where Did the Money Go?," accessed May 27, 2020, http://lcps-lebanon.org/agendaArticle.php?id=158.

> willingness to oversee the hollowing out of the Lebanese economy by refusing to publicly raise the alarm bells about the excessive costs of maintaining the exchange rate peg. The "financial engineering" operations over the last five years were simply an attempt to kick the can down the road at tremendous cost. BdL offered exorbitant interest rates on new dollar deposits, even though it had very little dollar earnings itself and, therefore, incurring huge losses on these deposits. The interest paid on dollar deposits was thus paid by attracting new dollar deposits at even higher interest rates, resulting in an explosion in the size and scale of the problem. This was carried out with little transparency to the Lebanese people.[20]

Catastrophic strategic planning and risk management blunder that engendered the loss of a great opportunity to smoothly and inexpensively move away from the policy of pegging the currency when the environment was favorable. Such a move could have driven the country into a whole different path.

5) GOVERNANCE AND DECISION MAKING

a) The rational view

At the heart of management and governance in general, lies the decision making process. Grave implications and brilliant ones could ensue depending on how carefully studied and analyzed decisions are. Rigor, logic, and rationality are essential in this matter. The management theory extends several models of decision making. The prominent rational decision-making process calls initially for recognizing that a decision is needed.[21] Hence, a stimulus is required. In the case of BDL, the stimulus to review the monetary policy decision of pegging the local currency to the US dollar could have been triggered by the eruption of the enduring Syrian conflict in 2011 that has stifled the routes of hard currency generating Lebanese export to the important markets of the gulf. The massive

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[20] "Lebanon's Financial Crisis."

[21] Ricky Griffin, *Fundamentals of Management*, 4th ed. (Boston - New York: Houghton Mifflin Company, 2006), 117.

flow of Syrian refugees into the country could have contributed to the decision as well. The suffocation of the economy as a result, for years onward, also could have stimulated such a decision. Not to mention the eventualities of dwindling foreign reserves as part of a mandatory risk assessment exercise that accounts for all the potential threats. These could be for example, reduced remittances, fainting foreign direct investments, the evident perpetual government unrestrained fiscal behavior, the tremendous deficit in the trade balance and current account, or the overall unsound governance practices.

i) ***An economics spotlight***

Over and above, the economics theory does not appear to support the pegging policy if specific criteria are not fulfilled. Limitations to what nations can do with their currencies do exist. Silbiger delineates: "A concept called the impossible trilogy says a government can have only two of the following three options: Independent monetary policy, Fixed exchange rates, Absence of capital controls."[22] The concept was first brought forward in the 1960s by economists Robert Mundell and Marcus Fleming, who independently described the relationships among exchange rates, capital flows, and monetary policy. Coincidently, Maurice Obstfeld, the researcher who introduced the Mundell-Fleming model as a "trilemma" in a 1997 paper, was appointed Economic Counsellor and Director of Research at the International Monetary Fund (IMF) in 2015.[23] The Economist magazine in 2016 classified the monetary trilemma among the six greatest notions that describe the world's functioning. Feenstra and Taylor, two of the most prominent researchers in the field of international economics, delineate the monetary

[22] Silbiger, *The Ten-Day MBA*, 317.

[23] "Maurice Obstfeld -- Biographical Information," accessed May 18, 2020, https://www.imf.org/external/np/bio/eng/mo.htm.

trilemma as “one of the most important ideas in international macroeconomics.”[24] With all of the above, it is inconceivable to justify defying this proven concept with reasonable arguments! It becomes similar to challenging the law of gravity, which shall eventually prevail. Indeed, Lebanon’s governance sustained the trilemma for more than two decades before the great lightning struck.

In continuation of the rational model’ decision-making process, the step of evaluating each one of the alternatives after identifying them, draws attention with its practical and vital three stages: Feasibility, satisfactoriness, and consequences.[25] Had the long term consequences of BDL’ pegging decision been properly evaluated and weighed against its feasibility and satisfactoriness, it is very likely the situation could have been much different. Moreover, even after the extended implementation of the pegging decision, the theory of rational decision making calls for following up to assess the effectiveness of the decision and its outcomes. Should the decision prove to be not achieving its goals, the management theory calls for choosing from other alternatives.[26]

b) The behavioral angle

A bitter yet an unsurprising fact of life is that decisions are rarely made based on rationality and logic. That is why decisions’ success is not very dominant. For instance, in the US, it is estimated that firms resort to rational decision-making techniques less than twenty percent of the time, according to some specialists. However, even rationality and

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[24] William J. Rieber, “A Model To Explain The Monetary Trilemma Using Tools From Principles of Macroeconomics,” *Journal of Economics and Economic Education Research*, January 4, 2018, https://www.abacademies.org/articles/a-model-to-explain-the-monetary-trilemma-using-tools-from-principles-of-macroeconomics-6814.html.

[25] Griffin, *Fundamentals of Management*, 118.

[26] Griffin, 120–21.

logic do not fully guarantee success. At times, it occurs that decisions taken without consideration to logic and rationality may prove effective. The behavioral aspect of decision-making theory may provide further explanations in this regard.[27]

ii) ***The bounded rationality***

Herbert Simon, Nobel prize in economics laureate, was among the first to discern in the 1950s that decisions are not always made with rationality and logic. His prominent administrative model and bounded rationality concepts explain not how decisions should be made but rather how they are made. The model contends that: “managers (1) have incomplete and imperfect information, (2) are constrained by bounded rationality, and (3) tend to “satisfice” when making decisions. Bounded rationality suggests that decision-makers are limited by their values and unconscious reflexes, skills, and habits. They are also limited by less-than-complete information and knowledge."[28]

Projecting the above framework to our decision-makers in the case of BDL and the commercial banks, one notes that ample information about the economy was available. Also, satisficing is not likely to be the driver for the fixed currency and high-interest rates monetary policy view its obvious high risk and negative implications. Moreover, the decision-makers, in this case, are generally qualified and competent people who have a proven and successful track record over the years. Therefore, most probably, it is not a question of skills, habits or conscious reflexes. What remains in doubt in this model are the decision-makers’ values.

[27] Griffin, 121.

[28] Griffin, 121.

iii) ***Other possible influences***

So many other effects can interfere in the decision making process. Political forces are one effective factor, and coalitions are particularly a pertinent component here. Griffin holds: "A coalition is an informal alliance of individuals or groups formed to achieve a common goal. This common goal is often a preferred decision alternative."[29] A possible application to our case referred to above by the "International Banker" journalist, identifies the likelihood of a coalition between both parties in question and the politicians holding positions in the government and the parliament, while at the same time being major shareholders at commercial banks. Such a fatal eventuality calls for local and international laws and regulations to break, impede, and deter such destructive collusion.

Another relevant phenomenon to our analysis is the "escalation of commitment," which translates the issue of adhering to a position even after it proves erroneous. BDL's decision to hold to the peg could bear the traces of this element. Griffin fittingly argues: "Decision-makers must walk a fine line. On the one hand, they must guard against sticking too long with an incorrect decision. To do so can bring about a financial decline. On the other hand, managers should not bail out of a seemingly incorrect decision too soon."[30]

One more behavioral factor that solicits attention is the risk propensity of the decision-maker. How much is he willing to venture when making a decision. Is he the type that is very prudent and conservative, adopting the rational model? In this case, the decision-maker is prone to averting errors, and rarely takes decisions resulting in havoc. Conversely, the other type of decision-makers are very daring, and their appetite for risk is

[29] Griffin, 123.

[30] Griffin, 125.

elevated. Intuition and promptness characterize their decisions. Often, huge stakes are involved in their bets. However, their decisions' potential for realizing great achievements is more than their peers who are risk-averse. Reciprocally, they risk affording bigger casualties. The organization's culture is a major constituent in embracing the various extents of risk tendency.[31] Projecting the above to our case favors the high-risk propensity type of decision-makers, though the general organizational culture in both BDL and commercial banks is known to be generally conservative.

iv) ***the role of ethics***

A prime influence on decision making stems from personal ethics. These simply represent the individual's own ideology about what is correct and what is not. Robert Prentice, who teaches business law at the University of Texas, candidly gathers that ethics training is not enough for scholars. Teaching ethical behavior should start in the first place before the university: "Research shows that it is very difficult to teach ethical values to undergraduates . . . If they didn't get a sense of right and wrong from their families or their faith, it's unlikely a business school professor can instill one."[32]

On the other hand, the management theory places ethical practices among the fundamental six business principles that govern a manager's work. The theory corroborates that managers and mostly senior ones must engage only in completely ethical pursuits. A reason of that requirement is managers are entrusted with the interests of their stakeholders, including shareholders, customers, employees, and community.[33] Therefore, the stakes

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31 Griffin, 125.

32 Griffin, 46.

33 Gorman, *Complete Idiot's Guide to MBA Basics*, 13.

become even higher if they are charged with the fate of a whole nation. A second reason is that managers are most favorably placed to make use of their position for self-enrichment at the expense of their stakeholders. A third reason is that managers set the standard for all others across their organization or the country in our case. Managing the risks that an organization faces while conducting business is the last reason. This risk management function is critical to avoid the destruction of the company. An organization whose officers do not behave ethically is prone to high and needless risks. Deserve mentions that integrity lies at the core of every business dealing or responsibility, simply because its absence brings devastation to organizations, so what about nations.[34]

Further, the largest economy in the world, the US', faced a strong wave of corporate business scandals around 2002, and another one even more grave with the subprime mortgage banking industry crisis of 2007-8. This latter bears some similarity with the stalemate Lebanon is facing nowadays. The 2007-8 upheaval was attributed to reckless mortgage loaning by the banks to financially unsound borrowers and trading those pledges within the international financial establishment. Back then, many banks went bankrupt. Also, governments had to interfere and to bail out part of the international banking system to prevent a global economic crisis. However, according to Tom Gorman, the main responsibility for what happened lies on the lenders: "While borrowers, regulators, and bond rating agencies also behaved badly, lenders are responsible for their lending policies. The parties which originated those mortgages did so without proper documentation and without caring whether the borrowers could repay the loans."[35] Some of the Lebanese

[34] Gorman, 13.

[35] Gorman, 13.

commercial banks did almost the same. They have accepted to lend a financially unsound borrower, the GOL, beyond all prudence limits, thus risking people's deposits. Worth noting that Lebanese commercial banks generally exhibited very conservative lending exercise with the private sector, contrary to their unrestrained behavior with regards to government lending from depositors' savings. The same applies to BDL, who back then, conservatively prevented the banks from dealing with the subprime derivatives.

The Lebanese Center for Policy Studies (lcps) eminently concurs on holding some banks, executives, and shareholders responsible, at least ethically:

> The responsibility also lies with certain bank executives and shareholders who made tremendous profits from the unsustainable financial and economic system at the expense of depositors and taxpayers. The banks attracted depositor dollars by offering exorbitant interest rates and depositing such funds with BdL, without disclosing to customers the risks involved. At the same time, banks and their executives made outsized profits. They were in a position to blow the whistle, but most of them did not. Today, the same banks are attempting to make-up their losses at the expense of depositors by convincing customers to freeze their deposits or to subordinate their position by converting their dollar deposits into bank capital (which almost certainly has no value and is, in any case, subordinate to deposits in the event of an insolvency).[36]

It is amazing what the lack of ethics at high governance levels can do to organizations and nations, especially when combined with greed. Worth noting also that lcps did not spare from responsibility any individual holding a post of power or influence who chose to keep quiet although he could have raised the red flag on corrupt practices, bad management, as well as the untenable manner in which the financial and economic affairs of the country were conducted.

In the same vein, theory indicates that relativism is one philosophical frame used to justify unethical solutions and why ethics are, most of the time, ignored in decision making. It is being

[36] "Lebanon's Financial Crisis."

taught in business schools for students to guard against it in their business life. Silbiger argues: “The proponents of relativism hold that we can't decide on matters of right and wrong, or good and evil. Things are rarely black or white. There are so many shades of gray. Relativism proposes that ethics are “relative” to the personal, social, and cultural circumstances in which one finds oneself.”[37]

On the other hand, stakeholder analysis is a practical framework for aiding executives to deal with ethical resolutions. Interestingly, It involves listing all potentially affected parties, then assessing “Harms and Benefits”, and “Rights and Responsibilities.” An analysis is performed in the end to reach the best possible ethical decision with the least negative implications.[38]

Concluding on this part, one notices there is a strong case for relativism in our Lebanese condition. Moreover, stakeholder analysis does not appear to be a common practice in decision making there.

v) ***Social responsibility***

Proponents of social responsibility of organizations and businesses stipulate that the criteria for judging a business's success are not just financial gains. Businesses have to conduct activities within the confines of ethics, the law, the respect for the environment, and in a community-conscious manner. Besides having profit as their main mission, businesses have a social mission. They are expected to set the right tone within their organizations as well as their societies. They are also supposed to act as “a change agent for the betterment of society.”[39]

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[37] Silbiger, *The Ten-Day MBA*, 63.

[38] Silbiger, 65.

[39] Allen and Economy, *Complete MBA for Dummies*, 25.

Furthermore, another crucial view emphasizes the fiduciary responsibilities of corporate officers towards all their stakeholders, including their community, and society.[40] Specifically, the board of directors under sound corporate governance, has many critical functions. Gorman confirms that the board is entrusted, among others, with the interests of the owners, and the oversight of senior management whom he advises on policy issues. Nevertheless, the board is also entrusted with the interests of the community and society as a whole. Directors in general, and more specifically outside directors, are supposed to counsel and forewarn management on the communal and public implications of some policies and resolutions.[41]

Considering the above given for our case, one can qualify the run for excessive profits that have characterized the dealings as a non-socially responsible behavior. Besides being unethical, it did not take into account the interests of the community and the whole nation, nor did it engender any betterment for society. On the contrary, it has brought tremendous harm. Moreover, the boards of directors of these banks seem to fail in fulfilling their main corporate governance duties towards their communities and society. Yet, the other astonishing fact is that such behavior is still considered legal.

6) THE PULP OF HUMAN MOTIVES

While the theories explaining human needs are usually utilized for business purposes, to probe new markets and business opportunities, we shall exceptionally apply them to examine some behaviors in our case. Maslow's hierarchy of needs and Clayton Alderfer's version of Maslow's hierarchy called “ERG theory” both concur on the human

[40] Silbiger, *The Ten-Day MBA*, 62.

[41] Gorman, *Complete Idiot’s Guide to MBA Basics*, 41.

inclination to emphasize on esteem, self-actualization, and growth among others. However, the way this could be achieved is another matter. Two Harvard Business School professors, Paul Lawrence and Nitin Nohria have authored a book named: *Driven: How Human Nature Shapes Our Choices.* They argue that all human beings have four Core Human Drives that deeply affect their decisions and have a profound influence on their behavior. These are the drives to Acquire, Bond, Learn, and Defend.[42]

Based on the above input, one expectedly deduces that greed and the drive to acquire could apply where extravagant profits have been realized. In the same context, one can ascribe today's surge in malignant business demeanor to competitiveness and the hunt for gains. However, since the dawn of humanity, roguery and greediness have subsisted. Nevertheless, although the larger part of persons doing business is truthful, executives particularly, are expected to conduct themselves only ethically.[43] Besides, the urge for esteem and self-realization through further political ambitions might also explain the sustained commitment to the peg. This latter used to be perceived by citizens as a glorious achievement that has entitled them to a high living standard.[44]

7)THE ROLE OF RISK MANAGEMENT

Risk management (RM) has grown in significance in today's business world because of the mounting frequency and gravity of risks as well as the interconnection between the various businesses and industries, not to mention the links with the public

[42] Josh Kaufman, *Personal MBA*, Master the Art of Business (New York, U.S.A.: Portfolio / Penguin, 2012), 41–42.

[43] Gorman, *Complete Idiot's Guide to MBA Basics*, 12–13.

[44] "Lebanon's Central Bank Governor: Saviour or Scapegoat?," The National, accessed May 20, 2020, https://www.thenational.ae/business/economy/lebanon-s-central-bank-governor-saviour-or-scapegoat-1.1011283.

sector. RM is usually exercised via first determining the risks faced by organizations, evaluating their magnitude and probability of occurrence, acquiring the proper risk-management apparatus with the expertise necessary to effect them, then spreading a risk-management culture so that everyone senses its responsibility.

In corporate settings, RM is mainly the charge of general management' senior officers. It falls under the board of directors' corporate governance responsibilities. Management effects RM based on direction from the board. Comprehension of the various kinds of risks the firm faces is mandatory for proper RM. The main types of risks encountered by firms usually are: financial, currency (or foreign exchange), credit, security, property, regulatory, legal, IT, country (or political), and reputational risk.

The global financial crisis of the late 2000s which caused the foundering of banks obliged the majority of executives and board members to give more emphasis to RM. Besides, financial fraudulence events similar to the Bernie Madoff scandal, as well as tighter regulative examination and the menace of terrorism have exacerbated management's sensibility to risks.[45]

Furthermore, an exemplary model of RM in financial institutions is that of the IMF. It adopts a comprehensive RM framework that involves procedures to alleviate conventional financial risks as well as strategic and operational risks. For instance, major constituents of their financial risk mitigation system include:

> Lending policies (program design and monitoring, conditionality and phasing, access limits and the exceptional access framework), investment guidelines, internal control structures, financial reporting, audit systems, and the IMF's preferred creditor status. The IMF also uses precautionary balances to absorb the impact of risks once they crystallize. Besides, the IMF conducts safeguards assessments of central banks to ensure that their governance, control systems, auditing, financial reporting, legal structures, and autonomy are adequate to maintain the integrity of operations and minimize the risk of

[45] Gorman, *Complete Idiot's Guide to MBA Basics*, 375–76.

> any misuse of IMF resources…the IMF faces a range of financial risks in fulfilling its mandate, relating to credit, liquidity, income, and market risks, and has developed a multilayer financial risk mitigation framework.[46]

Should the Lebanese commercial banks as well as BDL adopt and abide by such a rigorous risk management setting, they, among others, would not have extended further credit to a no creditworthy client, and Lebanon would possibly have averted the current swamp. Moreover, they would not have incurred such huge losses that could lead some banks to bankruptcy and would entail the loss of trust, not to mention a bad reputation. Downgrading by the international rating agencies is another worthy negative implication that reflects gravely on the banks as well as the whole economy. The regulation and the legal framework bear significant amendment and reform.

Also, the IMF has a risk management maturity assessment program to evaluate the effectiveness of risk management practices at central banks:

> Effective risk management at central banks is best enabled by a sound framework embedded throughout the organization that supports the design and execution of risk management activities. To evaluate the risk management practices at a central bank, the Safeguards Assessments Division of the IMF's Finance Department developed a tool that facilitates stocktaking of elements that are present and categorizes the function based on its maturity. Tailored recommendations are then provided to the central bank which provide a roadmap to advance the risk management function.[47]

View the long-standing relation between BDL and IMF; it is legitimate to investigate whether such a program was ever conducted with BDL, and what were the outcomes. Moreover, IMF organizes beneficial specialized courses such as the course named Sovereign Liability And Risk Management Principles And Practices (SLRM),

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[46] International Monetary Fund Finance Dept, *6. Financial Risk Management*, *IMF Financial Operations 2018* (INTERNATIONAL MONETARY FUND), accessed May 22, 2020, https://www.elibrary.imf.org/view/IMF071/24764-9781484330876/24764-9781484330876/ch06.xml?redirect=true.

[47] "Risk Management Maturity Assessment at Central Banks," IMF, accessed May 22, 2020, https://www.imf.org/en/Publications/WP/Issues/2019/12/27/Risk-Management-Maturity-Assessment-at-Central-Banks-48860.

targeted mainly to: "Mid-level to senior debt managers, central bankers, and related officials with policy and operational responsibilities relating to monitoring and managing sovereign liabilities, debt, and the development and functioning of domestic debt markets."[48]

Based on the above, should a proper risk assessment and management function been rigourously implemented at both BDL and the relevant commercial banks, the decision of fixing the currency may have been most probably amended. Also, the decision to further lend the faltering GOL might have been revisited.

8) FINANCIAL AUDIT

Moreover, a question is raised about the audit opinions extended about the fairness of the financial statements in the external audit reports. Notable here is the fact that no trace of BDL's audited financial statements, including the profit and loss statements nor audit reports, can be found on its website. Some research indicates that BDL did not publish income statement (profit and loss) since 2002. Although, as in any democracy, all public enterprises are required by law to publish financial statements.[49] This undoubtedly poses at least an accountability and transparency question as well as the quality of independent oversight if good governance is to be exercised. The general public is one of the main stakeholders of a central bank (CB). This public is driven by the necessity to ensure proper management of public resources, including taxes.[50] Moreover, most central banks in well-

[48] "Sovereign Liability And Risk Management Principles And Practices," IMF, accessed May 22, 2020, https://www.imf.org/en/Capacity-Development/Training/ICDTC/Courses/SLRM.

[49] "Lebanon," November 23, 2019.

[50] *"External Audit Arrangements at Central Banks,"* IMF, 8, accessed May 15, 2020, https://www.imf.org/en/Publications/WP/Issues/2018/09/11/External-Audit-Arrangements-at-Central-Banks-46210.

governed countries publicize their annual audited financial statements. The Federal Reserve in the US publishes even the signed independent audit report and the management's report on Internal Control over financial reporting.[51] Profit and loss statements usually are explicitly announced and commented regularly at the beginning of each year, as is the case with the European Central Bank (ECB).[52]

In the same vein, the findings of a 2018 IMF working paper that surveyed CB websites of 170 countries confirm a notable improvement in exercising financial translucence pursuits. 83 percent of CBs publish their audited financial statements, and with recently enhanced timeliness. Moreover, 64 percent of the audit reports made known use International Standards on Auditing (ISA). Not surprisingly, 70 percent of CBs are audited by firms with international association. More importantly, espousal of modernistic audit oversight via audit committees is becoming further pervasive.[53] Noteworthy is the fact that Audit Arrangements at the 60 CBs subject to IMF Safeguards Monitoring indicate an average external auditor rotation period of 3.86 years. Further, 141 CB out of the 170 had published audit opinions as of September 30, 2017.[54] The worth indication that no rotation of BDL's auditors has been effected since the late 1990s. The same two international audit firms have been incessantly in service, which raises valid questions in many directions.[55]

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[51] *"Federal Reserve Board - Federal Reserve System Audited Annual Financial Statements,"* Board of Governors of the Federal Reserve System, accessed May 15, 2020, https://www.federalreserve.gov/aboutthefed/audited-annual-financial-statements.htm.

[52] European Central Bank, *"Financial Statements of the ECB for 2019,"* European Central Bank, accessed May 15, 2020, https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200220~6e608d569d.en.html.

[53] *"External Audit Arrangements at Central Banks,"* 5.

[54] "External Audit Arrangements at Central Banks," 33-35.

[55] "Salameh: Foreign Currency Reserves at $20.9 Billion - Georgi Azar," An-Nahar, April 29, 2020, https://en.annahar.com/article/1177315-salemeh-foreign-currency-reserves-stand-at-228-billion.

Furthermore, the IMF working paper expectedly asserts that independent external audit upholds CB financial accountability. The document clearly relates the IMF's policy in this regard based on IMF's "Code of Good Practices on Transparency in Monetary and Financial Policies." The code clearly establishes the eligible CBs' transparency exercises as follows: "4.2 The central bank should publicly disclose audited financial statements of its operations on a preannounced schedule. 4.2.1 The financial statements should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements."[56] The least one could note is that BDL is not compliant with the IMF's "Code of Good Practices on Transparency in Monetary and Financial Policies."

On the other hand, and since nowadays, the government of Lebanon has requested financial assistance from the IMF, it is worth to mention the terms of IMF's Safeguards Assessments (SA). These apply to all member states who shall need to make use of IMF resources. The SA's main objective is to make sure that the system of reporting and monitoring of a CB can handle resources as well as IMF funding. To enhance financial safeguards, the assessments emphasize on CB governance and underline the significance of independent oversight, transparency, and accountability. Further, according to the IMF, SA inside CBs should comprise five main fields of control and governance abridged as ELRIC: "(i) the External audit mechanism; (ii) the Legal structure and independence; (iii) the financial Reporting framework; (iv) the Internal audit mechanism; and (v) the internal

[56] "External Audit Arrangements at Central Banks," 7–8.

Controls system."[57] It remains to be seen what would be the outcome of IMF's Safeguard Assessment for BDL, if any.

9) IGO'S POSITION

Worth mention in the same context that the IMF's position few years back was much more accommodating towards BDL, qualifying the financial engineering it performed as "unconventional financial operation." On December 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Lebanon. It holds:

> In the context of Lebanon's fixed exchange rate regime, foreign exchange inflows slowed in the first half of 2016, resulting in a drop in official international reserves. In response, during May–October the Banque du Liban (BdL) engaged in an unconventional financial operation which, among other objectives, helped boost reserves to above 2015 levels. At the same time, the operation also created sizable excess Lebanese pound liquidity and increased commercial banks' exposure to the sovereign.[58]

While such a position briefly highlights the pros and cons of this financial engineering, it comes short of the pressing need to prevent further damage and indebtedness of the country. The executive board assessment went further to approve keeping the monetary policy of pegging or fixing the exchange rate and praised BDL's foreign currency reserves. However, the directors underlined that these operations do not constitute a lasting solution to the country's financial requirements. They also timidly

[57] "Safeguards Assessments Completed to Date," accessed May 15, 2020, https://www.imf.org/external/np/tre/safegrds/complete/index.aspx.

[58] "Lebanon: IMF Executive Board Concludes Article IV Consultation," IMF, accessed May 13, 2020, https://www.imf.org/en/News/Articles/2017/01/24/PR1720-Lebanon-IMF-Executive-Board-Concludes-Article-IV-Consultation.

signaled the weakness in BDL's balance sheet advising towards a remedying medium-term strategy.[59]

On the other hand, the World Bank has been following closely since long with the Lebanese authorities. It has in turn extended good advice and financial support. His Systematic Country Diagnostic engendered starking but expected findings about an obsolete type of governance: “Lebanon’s Systematic Country Diagnostic (SCD) identified elite capture, hidden behind the veil of confessionalism and confessional governance, as one of two overarching constraints for the country’s economic development.”[60]

On the part of commercial banks, the impact is heavily felt on the balance sheet soundness and the quality of assets. An alarming 71 percent of bank's assets are credited to the public sector, 58 percent of which are to the central bank which is normally supposed to lend money to the banks, not the opposite. Such an unhealthy situation implies a weak financial state and dwindling liquidity levels, not to mention the huge slump in advances to the private sector, and the resulting slowdown of the economic vigor.[61]

Another devastating “good governance breach” occurred when the banks shifted their prime correspondent banks’ foreign US Dollar purse to loan the central bank with favorable terms. Representing one of the most dangerous results of BDL’s “unconventional financial operation,” such a feat weakened the commercial banks' financial position, exposing them further to the degenerating public finances.[62] All of these

[59] “Lebanon.”

[60] “World Bank: Lebanon Is in the Midst of Economic, Financial and Social Hardship, Situation Could Get Worse,” World Bank, accessed May 14, 2020, https://www.worldbank.org/en/news/press-release/2019/11/06/world-bank-lebanon-is-in-the-midst-of-economic-financial-and-social-hardship-situation-could-get-worse.

[61] “Lebanon,” November 23, 2019.

[62] “Lebanon.”

extremely harmful governance behaviors and much more occurred. However, we are concerned here at least with those at the level of BDL and the commercial banks and not with the local political institutions and their potentially harmful influence.

Worth mention that the a.m. detrimental governance practices passed under the close oversight and scrutiny of authoritative global intergovernmental bodies, such as the IMF, the World Bank,[63] EU[64], and the UN[65] Also, two of the "Big Four" international accounting firms have been auditing BDL and the majority of the commercial banks in the country for more than two decades. Putting aside the political aspect and local causes of the current crisis which are evident. One wonders about the role, effectiveness and value of the international governance bodies in such circumstances where poor local governance practices and the consequent drive of a whole nation towards the cliff have been obvious, gradual, firm and prolonged since years.

10) THE INTERNATIONAL SPHERE

c) Public governance

The World Bank has initiated an ambitious project to establish tangible governance indicators for nations based on specific criteria: "The Worldwide Governance Indicators (WGI) project reports aggregate and individual governance indicators for over 200 countries and territories over the period 1996–2018, for six dimensions of governance:

[63] "World Bank."

[64] "EU Support for Lebanon: If Not Now, When?," ECFR, accessed May 14, 2020, https://www.ecfr.eu/article/commentary_eu_support_for_lebanon_if_not_now_when.

[65] "UN Backs Lebanon in Economic Crisis, Call for Global Help - The New York Times," accessed May 14, 2020, https://www.nytimes.com/aponline/2020/05/04/world/middleeast/ap-un-virus-outbreak-lebanon.html.

Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption."[66] Not surprisingly, the Middle East and North Africa region score way behind the high-income OECD and North American regions in all six dimensions. Zooming in to Lebanon, the scores are conceivably low for the first four dimensions but even more alarmingly lower for the last two.

On the other hand, public governance improvement efforts in the OECD countries gained impetus after the late 2000s global economic and financial crises. Pursuing business the common way is not an option anymore. The formulation of the ability of governments to anticipate, prohibit, and react to complex and constantly changing defiances has become a necessity. Impairments in the governance systems that require reinforcement are the elements that have been recognized as responsible for the plight. Moreover, the findings emphasized the essentiality of managing the long-range effects of the reactions to the crises. Worth mention are four governance matters that were recognized to have a significant effect in the upheavals. These are evidence-based policymaking, integrity in the public sector, co-ordination of policies and programs across levels of government and fiscal sustainability. The Regulatory Impact Analysis (RIA) is one instrument of significant assistance to governments. It can be utilized to found policy decisions on the available body of facts or information and to evaluate the effects and implications these decisions may bring about. Moreover, settings such as the Integrity Framework are gaining further

[66] "WGI 2019 Interactive > Home."

attention with the expanding role of governments in the economy via, for instance, their growing investment actions.[67]

d) Corporate governance

On corporate governance in the EU, the CFA institute that is a global association of investment professionals concerned with setting standards for professional excellence, concluded its report on the subject with elaborate action memoranda. These are aimed generally towards those in charge of policymaking and to market players who are engaged in formulating and exercising good governance. Of particular interest also are civil society groups concerned with governance which have been addressed as well. One of the main report's conclusions emphasizes that good governance requires more than laws and directives: "Better corporate governance, similar to better political governance, cannot be achieved by regulation alone. It also depends on an understanding among participants of their appropriate roles, rights, and responsibilities."[68] Further, the great importance of corporate governance is splendidly highlighted by James Wolfensohn, former head of the World Bank: "The governance of the corporation is now as important in the world economy as the government of countries." The report goes further to borrow from political governance, the precious notion that "the price of liberty is eternal vigilance." The CFA institute corroborates that this notion similarly applies to corporate governance being a continuous operation rather than an end product. [69]

[67] OECD, "Current and Future Public Governance Challenges," in *government at a Glance 2009*, by OECD, Government at a Glance (OECD, 2009), 20-22, https://doi.org/10.1787/9789264061651-4-en.

[68] "Corporate Governance Policy In The European Union," August 2016, 2.

[69] "Corporate Governance Policy In The European Union," 47.

Finally, it is of the essence to invoke some conclusions of the US Financial Crisis Inquiry Commission Report[70] initiated in the wake of the 2008 financial crisis. These conclusions might apply to our Lebanese case. The report attributes the crisis to many factors: A pervasive debacle of the financial regulatory and supervisory setting, considerable failures of corporate governance and risk management at several key financial establishments, as well as a blend of extravagant borrowing, perilous investments, and transparency shortfalls. In addition, the report signals the lack of government readiness and its incompatible reaction, as well as a systemic failure in accountability and ethics.

11) CONCLUSION

Fostering good governance is a multi-pronged endeavor. At the personal level, it can receive a strong boost from building clear and deeply entrenched ethical values in the individual's early years of childhood. What's right and what's wrong need not be ambiguous. Be it within the family or through the teachings of faith; without lessening the significance of school education and the overall civil society's culture on the national scale. In the public and corporate realms, good governance can be exercised and enhanced via the conscientious, diligent, and strict application of the relevant managerial functions. These span among others, from constantly vigilant strategic planning to rational and ethical decision-making, to stringent risk assessment and management practices. Under the rule of law, accountability, transparency, responsiveness and inclusiveness proved to be among the main determinants. Effective regulation and legislation is of no less importance. Flaws in nearly all of these areas appear to pervade in the case under study. Hence, a wide scale

[70] "Get the Report : Financial Crisis Inquiry Commission," accessed June 5, 2020, http://fcic.law.stanford.edu/report.

remedying response is called upon from the relevant authorities and organizations to say the least. For instance, legislative bodies need to enact laws for instauring, motivating, and enforcing good governance, prevention and deterrence of corrupt and socially irresponsible practices, accountability, transparency, and responsiveness among others. Promoting the highest standards of ethics, integrity, in the early years of education proves vital for fostering a suitable environment for good governance. A code of ethics is mandatory for the public and private sectors as well as a code of ethics for citizens and the whole nation to raise a new generation of families where right and wrong is not simply a point of view. Furthermore, we reiterate a focal point: "Better corporate governance, similar to better political governance, cannot be achieved by regulation alone. It also depends on an understanding among participants of their appropriate roles, rights, and responsibilities."[71]

On the other hand, considerable efforts need exertion from the part of the concerned IGOs to devise appropriate ways of incentivizing good governance and proactively assisting and guiding nations and sectors in need, to avoid future disastrous economic, financial, and social perils. Be it through treaties, financial or trading incentives, or any other smart policy instrument. The regular soft guidance role is proving to be insufficient. Besides the responsibility of the local political class, system, and the people; the current crisis of Lebanon is a striking example of the failure of the international governance framework to prevent such a drastic implosion of the fiscal, monetary, and banking system of a whole nation.

[71] "Corporate Governance Policy In The European Union," 2.

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