

**Information Memorandum**

**Submission of an Expression of Interest  
To Set Up a Subsidiary Bank in Libya**

**Central Bank of Libya  
February 15, 2010**

## I. EXECUTIVE SUMMARY

### **Economic environment**

The Socialist People's Libyan Arab Jamahiriya Libyan (Libya) has been implementing a comprehensive reform program driven by the Government's decision to move away from an ownership role in the economy to that of a prudent regulator. The entire economy is undergoing a restructuring, underpinned by widespread public support. The reform program—supported by technical assistance from international institutions and private consulting firms—aims at diversifying the economy away from oil and promoting the role of the private sector. Reflecting the shift in economic policies, a private investment boom is underway and the private sector's share in the economy is growing at a rapid pace.

Libya's integration into the global economy took a further step forward in 2009 when both Standard & Poor's and Fitch gave it an investment grade rating A-/stable/A-2 and BBB+/stable, respectively.

### **Economic development**

Prudent macro-economic and foreign exchange reserve management has shielded the economy from the recent global financial market turmoil. Since 2005, non-oil real economic growth has been strong and both the fiscal and current accounts balances have registered large surpluses. Non-oil growth continues to be broad based, benefiting from heightened foreign investor interest in the banking, services, infrastructure, and tourism sectors. Inflation remains under control and net external assets of Libya reached \$138 billion at end-2009.

### **Banking sector**

The last three years have witnessed a major transformation of Libya's banking infrastructure with privatizations, mergers, initial public offerings and opening of foreign banks. Out of the 16 commercial banks currently licensed in the country, 6 have strategic foreign partners. The entire banking system will be in private hands by 2011. A new central bank of Libya (CBL) structure has been finalized, it will strengthen the monetary policy framework and banking supervision; and establish a functional-based organizational structure. The many complex aspects of a national payments system are being put in place and a credit bureau started operations in April 2009.

### **The period ahead**

Economic growth is expected to remain very strong over the medium-term driven by public, and private domestic and foreign investment. Both the budget and current account balances are expected to remain in surplus. All sectors of the economy are experiencing strong growth and most investments that are taking place in Libya have a public/private partnership. Many of the strategic private partners are international companies. All investments are made with a commercial objective and upon completion all projects will be managed by private companies. Demand for banking services is expected to increase significantly.

## II. ECONOMIC ENVIRONEMENT

### 1. Macroeconomic context

Since 2002 Libya has been experiencing strong economic growth and large fiscal and external current account surpluses. The strong economic growth has been achieved in an environment of low inflation and stable macroeconomic conditions. Growth has been particularly strong in the construction and service sectors. On-going privatization in most sectors is increasing public participation in the country's economic boom.

In the last 3 years, Libya has signed about 70 trade agreements related to double taxation, investor protection and promotion of trade. Libya is preparing for accession to the WTO and is negotiating a partnership agreement with the EU. The government remains focused on improving the domestic business environment to foster private sector development and attract foreign investment. A set of laws is under preparation, including: (i) customs law; (ii) a new law on FDI that unifies the three existing laws; (iii) a land registry law; and (iv) a new labor law. A new tax law which was passed recently will lower the maximum corporate income tax to 15% from 40%. All these laws aim to develop standards that are in line with international best practices.

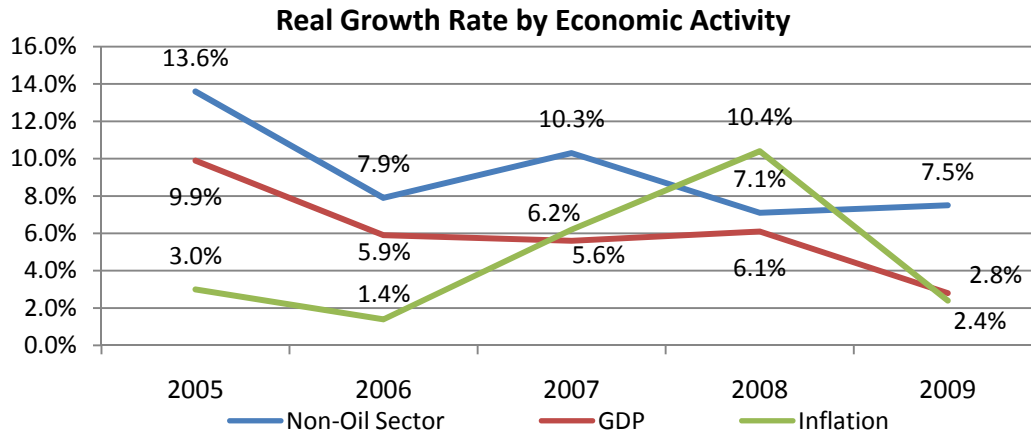
The government and the private sector are working in partnership to develop a world-class infrastructure. In 2009, the state agencies in charge of promoting local and foreign investment and for the privatization of state-owned enterprises were merged to create the Privatization and Investment Board (PIB). PIB offers a one-stop shop to private foreign and domestic investors, that centralizes all necessary public departments, incorporating branches of the labor, customs, and tax departments. In 2009, 47 projects were implemented by the private (domestic and foreign) sector, reaching LD2bn (\$1.63 billion). Total projects that are under development and received approval are 532 and valued at LD49.2bn (\$40 billion), 67% from foreign investors.

In addition, the Economic and Social Development Fund (ESDF) which was established in 2006 to support the poorest families in the country, is pairing international and local businesses, enabling them to carry out strategic projects, now numbering 74 in operations. Thus far LD14bn (\$11.4bn) has been allocated by the government to the fund and some significant investments have been made.

### 2. Key economic indicators

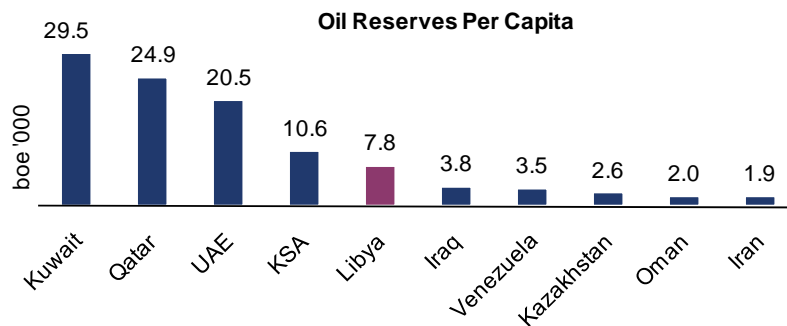
Since 2005 Libya's macroeconomic performance has been impressive. Non-oil real GDP growth averaged above 9% annually, driven by strong public, and private domestic and foreign investments. Despite strong economic growth, inflation remained under control and averaged about 4.5% annually since 2005. Major gains were registered in the trade and service sectors as a result of the liberalization of external trade and the marked resumption of foreign tourism.

### The non-oil sector has been the key economic driver since 2005



The prospects for continued growth in oil and gas production are supported by foreign and domestic investment. In 2010, oil production is expected to rebound to 1.84m bbl/day and oil and gas investment will almost double to LD2.2bn reflecting the enormous potential of the sector. Libya enjoys Africa's second largest oil and gas reserves and ranks in the world's top five on a per capita basis. Based on current production, reserves will last for more than 70 years. With most of Libya's territory still untapped, there is a high potential for more oil and gas discoveries as evidenced by the six oil and gas field finds made in 2009 by international oil companies. International partners continue to have a very strong interest in the oil and gas sector.

### Reserves will offer prosperity for years to come



Implementation of fiscal policy has been in line with the economy's absorptive capacity. Also, long-term fiscal sustainability considerations are factored in the design of fiscal policy. Budget surpluses have been achieved every year since 2000 and the government has accumulated significant amounts of foreign assets. Going forward, to avoid fluctuations in public investment, the development budget has been prepared in a medium-term framework (2010-12). Oil price fluctuations will not impact the implementation of fiscal policy over the medium-term. All priority projects will be funded. This is

achievable because of the government's substantial assets, including an oil stabilization account at the CBL amounting to \$21.2bn as well as about \$65 billion in external assets held with the Libyan Investment Authority.

**Consolidated Fiscal Operations**  
**In millions of Libyan Dinars**

	2005	2006	2007	2008
<b>Total Revenues</b>	<b>37,413</b>	<b>47,089</b>	<b>53,136</b>	<b>69,389</b>
Oil	34,764	43,566	48,639	61,037
Non Oil 1/	2,650	3,523	4,497	8,352
<b>Total expenditure</b>				
Administrative Budget	<b>8,206</b>	<b>8,540</b>	<b>11,891</b>	<b>15,308</b>
Development Budget	<b>8,335</b>	<b>11,039</b>	<b>18,993</b>	<b>28,807</b>
Extra budgetary expenditure	<b>2,788</b>	<b>1,285</b>	-	-
<b>Overall Surplus</b>	<b>18,084</b>	<b>26,225</b>	<b>22,252</b>	<b>25,274</b>

The favorable developments in Libya's oil sector have contributed to a significant improvement in the external current account surplus which averaged about 40 percent of GDP annually since 2005. Hydrocarbon export earnings reached about \$62 billion in 2008. Reflecting higher capital expenditures, imports have been increasing. Overall, total external assets of Libya surpassed \$135 billion at end-2009.

**Balance of Payments**  
**In millions of US dollars**

	2004	2005	2006	2007	2008
<b>I - Current Account</b>	<b>4,580</b>	<b>16,474</b>	<b>26,697</b>	<b>28,452</b>	<b>36,203</b>
Trade balance	8,599	19,484	27,314	29,212	40,858
Exports (Fob)	17,334	31,801	40,341	46,879	62,820
Imports (Fob)	8,735	12,318	13,027	17,667	21,963
<b>II - Capital and Financial Account</b>	<b>(309)</b>	<b>433</b>	<b>(4,978)</b>	<b>(9,564)</b>	<b>(21,335)</b>
<b>III-Overall Balance</b>	<b>4,638</b>	<b>17,040</b>	<b>17,674</b>	<b>16,606</b>	<b>15,149</b>

The Libyan Stock Market enjoyed buoyant activity in 2009. The market started with five listed stocks that has more than doubled. It currently has a market capitalization that exceeds the LD1bn. There are 40 companies in the pipeline for public offerings over 2010-11. A new stock exchange law will facilitate registration, accelerate dispute resolution and probably increase foreign participation.

Considerable progress has been made in liberalizing and opening the economy, including implementing a comprehensive privatization program of state enterprises, simplifying procedures for business application, removing customs duties, liberalizing most prices, removing restrictions on external trade, and allowing foreign investment in key sectors. The reform process will be broadened and accelerated in the period ahead. The government is committed to these reforms.

### **III. BANKING SECTOR OVERVIEW**

#### **1. Background**

Libya's process of transformation has been underpinned by a program of institutional reform that has had as its core the development and restructuring of the banking sector. Since 2005, with the passage of the banking law, the CBL has been implementing a gradual liberalization process of the entire banking system with the aim to restructure and modernize the commercial banks. An important component of the CBL's strategy has been to open the Libyan market gradually for foreign banks and develop the Libyan banking sector and improve its competitiveness regionally and internationally.

#### **2. Role of the Central Bank**

The CBL started its operations in April 1956, replacing the Libyan Currency Committee that was established in 1951. In 2005, a new banking law broadened the mandate of the CBL and assigned it the following responsibilities: (i) currency issuance; (ii) monetary policy; (iii) financial stability; (iv) reserve management; and (v) supervision of the foreign exchange market. In addition, the CBL has been entrusted to advise the government on macroeconomic policies. The CBL is managed by a board of directors with a broad authority to achieve the above objectives and responsibilities.

A comprehensive program is under way to modernize the central bank, upgrade the monetary policy framework, and establish a functional-based organizational structure. Banking supervision is being enhanced through improving regulations in line with international standards; and strengthening bank reporting and both on-site and off-site supervisory procedures.

#### **3. Reform of the Banking System**

Two public banks, Sahara and Wahda, are now partly privatized with foreign partners, BNP Paribas and Arab Bank respectively holding 19% stakes and management contracts. Both banks have the option to raise their stakes to 51% within 3-5 years if the reform measures and benchmarks agreed on with the CBL at the time of sale are met. The two largest commercial banks, which are still owned by the CBL, Gumhouria bank (which is the result of the merger of the old Gumhouria Bank and Al-Ummah Bank) and National Commercial Bank (NCB), are now listed (15%) on the domestic stock market. As for the community banks, they merged and formed the National Banking Corporation (NBC). There are nine small private banks among the current list of 16 commercial banks.

The First Gulf Libyan bank with share holding divided equally between the First Gulf bank of Abu Dhabi and the ESDF, started operations in November 2008. The Libyan Qatar bank which is owned equally between the Libyan Foreign bank and a Qatari holding company, will start operation in March 2010. And, in 2009, two private banks, Aman and Al Motahad, sold a 40% stake to Banco Espirito

and Ahli United Bank, respectively. In addition, there are 19 foreign banks' representative offices in Libya.

The CBL has a medium-term privatization strategy to gradually phase-out its holdings of the three commercial banks (Gumhouria, NCB, and NBC). The entire banking system will be in private hands by 2011.

#### 4. **Other measures to strengthen the financial system**

**The anti-money laundering law (AML)**, passed in 2005, established two supervisory bodies, a Financial Intelligence Unit (FIU) and a national committee for combating money laundering. The main role of the FIU is to investigate all suspicious transactions as reported by commercial banks and make recommendations to the CBL governor. The FIU is also responsible for exchanging information and cooperating with its foreign counterparts on anti-money laundering cases. Whereas, the role of the national committee for combating money laundering is to recommend policies and procedures on all issues related to AML.

**The credit bureau**, known as the Libyan Credit Information Center (LCIC), started operations in April 2009. In the first stage, the LCIC focused on the commercial side, just corporate and small and medium enterprises (SMEs). Work to include information on consumers will start in 2010. Banks use of the LCIC has been increasing. All banks have been invited to join the LCIC and the expectation is that all of them would have joined by end March/April 2010.

**Considerable progress has been made in putting together the many complex aspects of the payment system.** In 2008, the CBL went live with a Real Time Gross Settlement System, and the automated clearing house (ACH) and automated check processing (ACP) are in operation now.

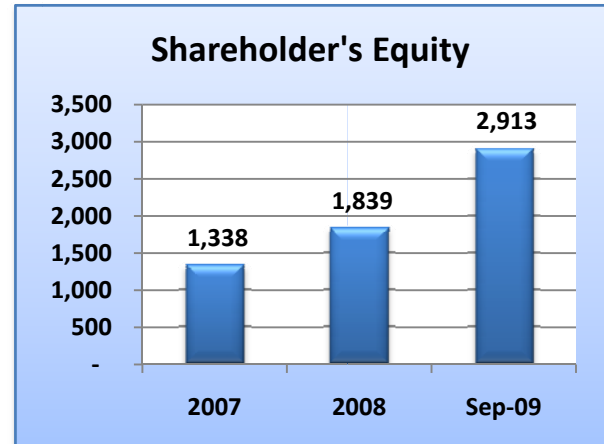
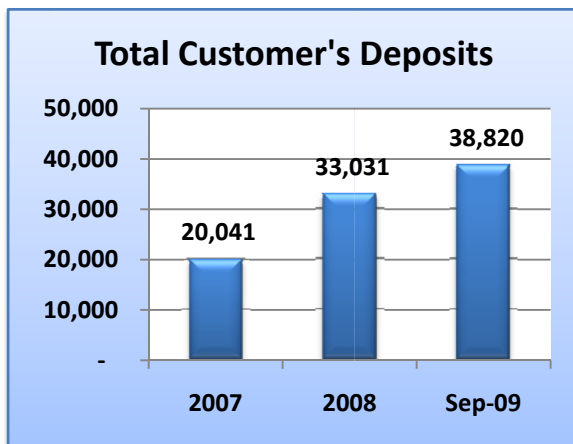
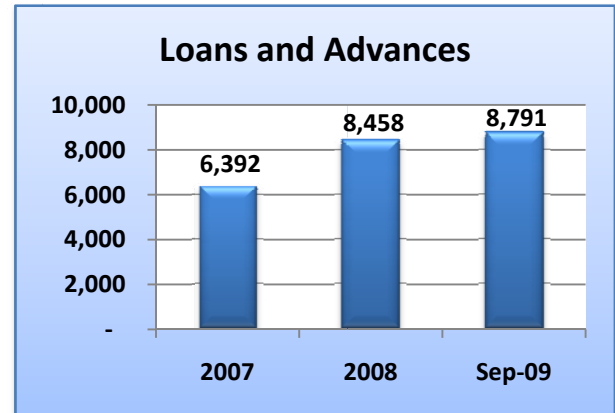
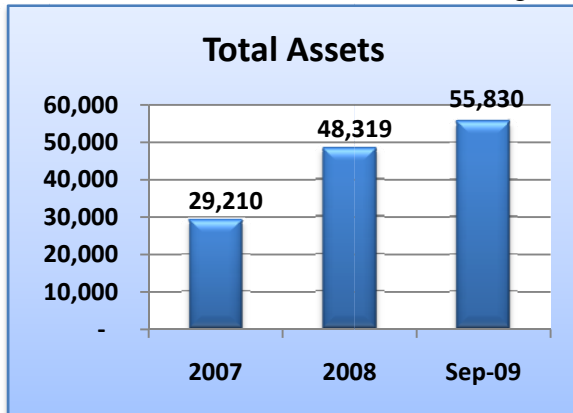
**A deposit insurance fund** has been set up, funded by the commercial banks, to protect deposits up to LD100,000. However, the level of protection declines gradually after the first LD 10,000.

**Interest rates** on both deposits and lending are completely market determined. Banks are free to set rates as they see fit.

#### 5. **Developments in the Libyan Banking Sector**

Since 2007, the Libyan banking sector has achieved extraordinary growth, deposits almost doubled. This increase was accompanied by an increase in the equity of banks which grew by about 58% in the first nine months of 2009. The ratio of NPLs to total loans has declined to 18.6 percent at end September 2009 and the level of provisions was approximately 80% of total NPLs at end September 2009.

Figures in LYD millions



	2007	2008	Sep-09
Loans / Deposits	31.8%	25.6%	22.6%
Liquid Assets / Total Assets	72.6%	77.3%	78.8%
Equity / Total Assets	4.5%	3.8%	5.2%
Capital Adequacy Ratio	-	10.1%	15.6%
Return On Assets <sup>1</sup>	1.1%	2.0%	1.6%
Return On Equity <sup>1</sup>	25.1%	39.9%	28.2%
Non-Performing Loans / Total Loans	26.6%	22.8%	18.6%
Provisions / Non-Performing Loans	65.2%	71.0%	79.9%

<sup>1</sup> Measured on the basis of Earnings Before Taxes

## 6. **Regulatory environment**

The CBL continues to strengthen the regulatory environment and has adopted a more risk-focused approach to banking regulation and supervision. To that end, the measures below were introduced:

### **Capital Adequacy Ratio**

- Banks are required to comply with Basel 1 requirements. Their capital adequacy ratio (Tier 1 and Tier 2 capital) should be at least 8%.

### **Leverage Ratio**

- Over and above the capital adequacy ratio, banks should keep a maximum leverage ratio, determined as the ratio of deposits to equity, not to exceed 30.

### **Credit Risk Limits**

- Credit to Deposit Ratio, the total credit portfolio should not exceed 70% of the deposit base;
- Credit Concentration, total loans to one customer or group of related customers (after taking into consideration eligible collateral) should not exceed 20% of the bank's tier 1 capital; and
- Placements with foreign banks should satisfy the following criteria: (i) foreign banks should be rated A- or better; (ii) deposits at each foreign bank abroad should not exceed 70% of Tier 1 Capital; and (iii) total accounts and placements deposited in all foreign banks outside Libya should not exceed 200% of Tier 1 Capital.

### **Liquidity Ratio**

- Banks are required to keep a minimum liquidity ratio of 25%, defined as total liquid assets over total deposits and other liabilities.

### **Required Reserves at CBL**

- Banks are required to maintain minimum reserves at CBL equal to 20% of total deposits and other liabilities;

Besides the above limits, there are also several other regulatory ratios that the CBL will be introducing in the period ahead, in line with international standards and best practices.

**Banking Opportunities**

The restructuring of the Libyan economy, the increased role of the private domestic and foreign investors, and the large public development budget planned over the medium-term are providing banks with excellent opportunities to expand their business in Libya.