

The Impact of Risk Management on Lebanese Banks' Performance: A Qualitative Study

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ABSTRACT

This research employs a qualitative technique to examine the complexities of settlement risk in Lebanese banks against the backdrop of the country's volatile economic environment. This study explores many dimensions of settlement risk, including operational, regulatory, and market elements, through comprehensive interviews with five key personnel spanning from risk analysts to senior executives in the banking sector. Given the context of economic uncertainty, political upheaval, and strict international regulations, the banking industry in Lebanon has largely focused on identifying the underlying factors contributing to settlement risk. The respondents provided insight into the management strategies used to mitigate these risks and the ongoing challenges encountered by the banking industry. The findings suggest that Lebanese banks encounter specific obstacles, including but not limited to technology deficiencies, varied regulatory frameworks, and geopolitical volatility. The presence of a complicated risk environment is evident, but it is also apparent that there are internal measures in place to mitigate settlement risks. This study presents empirical data that might be valuable for policymakers, financial analysts, and academic academics to gain a deeper understanding of the intricate characteristics of settlement risk in Lebanese banks. The need to implement a comprehensive and cohesive risk management plan to safeguard the Lebanese financial system is emphasized.

Keywords: Banks, Risk Management, Diversification, Mitigating Risks

INTRODUCTION

A resilient financial system is crucial to a flourishing economy. Given the intricate and uncertain nature of the Lebanese economy, it is essential to examine settlement risks within the financial system (Kamel et al., 2023). Settlement risk, payment risk, or transaction risk all relate to the potential for financial loss or delay in settlement due to a counterparty's failure to fulfill its obligations in a financial transaction (Bhojwani & Shome, 2023). The first portion of this paper offers a thorough examination of settlement risk in the Lebanese banking industry. The introduction provides a rationale for investigating settlement risk in the banking industry and its potential implications for the national economy (Mtiraoui et al., 2023), establishing the context for subsequent analysis. The Lebanese banking industry has been a long-standing pillar of the economy for many decades. Recent economic and financial crises have arisen because of a range of factors, such as elevated levels of public debt, depreciation of currency, and political instability (Abdullah et al., 2020). These issues have raised concerns regarding the security and stability of the Lebanese financial system.

Settlement risk is a crucial consideration because it has the potential to result in substantial financial losses and undermine trust in the banking system (Ramaswamy et al., 2021). The prevalence of cross-border transactions and interbank activities in the Lebanese financial system increases the potential for settlement risk, which may have significant implications. This risk not only affects individual banks but also threatens the overall financial stability of the country (Tiwari et al., 2021). The main aim of this study is to examine the origins of and remedies for settlement risk in Lebanese financial institutions. This study aims to provide insights into the intricacies of settlement risk with the

intention of assisting regulators and financial institutions to improve their risk management practices (Kaur et al., 2021). In recent years, Lebanon's robust banking sector has been successful in attracting both domestic and foreign investments (Maiti et al., 2021). Despite its historical stability, the country's banking system faces significant economic and financial concerns. To preserve public confidence in the financial system, it is crucial to carefully oversee and mitigate settlement risk given the significant consequences at hand (Pessa et al., 2023).

PROBLEM STATEMENT

The Lebanese banking industry has always played a crucial role in the country's economy, catering to both the domestic and international monetary requirements of the nation and its residents. Nevertheless, the viability of the Lebanese banking sector has been questioned because of a succession of economic and financial crises in recent years. Settlement risk, a crucial component of financial transactions, poses a significant danger to the stability of the Lebanese banking system and undermines client trust (Hamza and Shatila, 2022). Settlement risk refers to the potential for financial loss or delays in the completion of a financial transaction due to the counterparty's inability to fulfill their obligations. Lebanese financial firms face settlement risk, which encompasses credit, liquidity, operational, and legal concerns. An urgent assessment of settlement risk in the Lebanese banking system is necessary because of the country's vulnerability to cross-border transactions and the intricacy of the present economic circumstances. Remarkably, there is a scarcity of detailed research on settlement risk in financial systems, particularly in relation to Lebanese banks. Owing to the unique problems and dynamics existing in the Lebanese banking industry, the conclusions of this research, which largely focus on settlement risk in developed countries, may not be applicable to Lebanon (Kumar et al., 2022). The lack of relevant research underscores the need to investigate bank settlement risks in Lebanon. Gaining insights into the frequency and consequences of settlement risk in the banking industry may assist researchers, regulators, and financial institutions in mitigating this risk and strengthening financial stability. An immediate evaluation of bank vulnerability to settlement risk and its potential impact on the overall stability of the Lebanese financial system is imperative in light of the current economic recession.

PROPOSITION DEVELOPMENT

The settlement risk in finance is closely related to monetary stability. Financial transactions may be executed smoothly in a stable economy characterized by stable prices, full employment, and consistent growth (Chow et al., 2023). During periods of economic prosperity, financial institutions often exhibit indications of enhanced liquidity, lower counterparty credit risk, and overall financial stability. Consequently, a reduction in settlement risk leads to a lower likelihood of transaction default. Nevertheless, in the event of an unstable economy, settlement risk may be amplified by factors such as heightened counterparty credit risk, liquidity restrictions, and market volatility (Eldin et al., 2023). Settlement risk, often known as the risk of a financial transaction not being fulfilled because of the failure of the other party involved, may have severe consequences for economic growth and prosperity (Yudaruddin, 2023). The potential consequences of extensive settlement failures include systemic risks, financial market contagion, and economic disruption (García-Sánchez et al., 2020). Settlement risk has an adverse impact on financial markets, the flow of money, and investors' trust. Financial transactions may have extended processing times, firms may encounter difficulties securing funding, and market volatility may increase, posing a risk to economic stability. The implementation of government and central bank policies, such as fiscal and monetary measures, plays a crucial role in promoting economic stability (Kukacka & Kristoufek, 2023). Implementing efficient economic policies may mitigate inflationary pressures, foster consistent economic expansion, and reduce financial market instability (Jalloul et al., 2022). These policy measures mitigate settlement risk by promoting economic expansion and reducing the likelihood of counterparty default. Financial institutions and regulatory bodies collaborate to establish risk-management frameworks and implement settlement rules (Sun et al., 2021). This abstract highlights the need for collaborative actions by economic policymakers and regulatory agencies to maintain economic stability and ensure efficient management of settlement risk. These actions ultimately enhance the overall resilience of the financial systems. This leads to the development of the following proposition:

P1: There is relationship between economic stability and settlement risk

Zhang and Zhao (2023) analyze the complex correlation between political stability and settlement risk in the financial markets. Political stability creates a conducive environment for the seamless execution of business transactions. Political stability leads to increased investor confidence and more consistent implementation of government initiatives (Zhang and Zhao, 2023). Financial institutions often experience lower settlement risks because of decreased counterparty credit

risk and enhanced liquidity. Political instability may raise settlement risk through factors such as uncertainty, prospective changes to regulatory frameworks, and volatile financial markets (Uppal et al., 2023). Political instability has the potential to cause settlement failures, which, in turn, may create systemic risks that impact the stability of financial institutions, enterprises, and the overall economy (Lin et al. 2023). To ensure efficient government supervision and enforcement of settlement laws, it is essential to have both political stability and strong government. Efficient governance is distinguished by the clear and open disclosure of information, the consistent application of rules and regulations, and the rigorous enforcement of regulatory frameworks (Yang et al., 2021). Political stability inside financial institutions enables the implementation of long-term strategic planning and meticulous risk mitigation. Consequently, the likelihood of settlement failure is reduced, thereby decreasing the associated risk (Aditya et al., 2021). Nevertheless, in politically volatile contexts, inadequate governance may result in non-compliance with regulations and prolonged delays in resolving settlement disputes. The potential for settlement risk to increase and the possibility of investor confidence being undermined have been identified (Wijayanti et al., 2021). Settlement risk, which may impact international financial flows and transactions, is associated with a country's political stability (Shatila & Alozian, 2019). This development is beneficial for both merchants and consumers, since it reduces the chances of political upheaval, causing disruptions in international commerce. Political stability fosters both domestic and international investments, bolstering the economy (Dao & Ngo, 2020). This leads to the development of the following proposition:

P2: There is a relationship between political stability and settlement risk

To ensure the stability of the financial system, the regulatory framework comprises legislation, regulations, and policies (Yilmaz and Buyuklu, 2016). Regulatory monitoring plays a crucial role in setting standards for risk management practices, promoting transparency, and ensuring compliance with the settlement legislation. Together, these factors enhance the importance of settlement risk management (Siddik et al. 2016). A well-crafted regulatory environment promotes the use of advanced settlement mechanisms, such as payment versus payment (PVP) systems and central counterparties (CCPs), which may assist financial institutions in reducing their vulnerability to settlement risks (Haapio et al., 2021). In addition, regulatory agencies play a vital role in overseeing the risk management methods of financial institutions and enforcing fines for those who fail to comply with requirements. The growing complexity of financial markets and products requires a more advanced regulatory framework to manage new risks effectively (Ushakov & Shatila, 2021). Regulatory measures have been implemented to improve settlement procedures and decrease the likelihood of systemic risk, based on lessons learned from previous financial crises. The banking industry has effectively mitigated settlement risk by implementing rigorous capital adequacy criteria, liquidity limits, and stress-testing exercises. Regulatory frameworks often emphasize the use of collateral and netting techniques to reduce counterparty credit risks. Market players have the duty to ensure compliance with the key standards for settlement risk management, as outlined in the regulatory framework (Park & Yang, 2023), and they play a crucial role in ensuring compliance. Financial institutions may mitigate their exposure to settlement risk by establishing and consistently monitoring efficient risk-management techniques (Ushakov & Shatila, 2022). Prompt adherence to regulatory obligations, such as the reporting of transactions and collateralisation, enhances the clarity and responsibility of settlement processes (Śliwiński, 2021). Regulatory agencies and market players cooperate to identify risks and weaknesses, and promote a proactive approach to risk management. This leads to the development of the following proposition:

P3: There is a relationship between regulatory framework and settlement risk

METHODOLOGY

This study used a qualitative research methodology by conducting five semi-structured interviews with several banks in Lebanon. The aim is to obtain a comprehensive understanding of settlement risks in the Lebanese banking sector. Qualitative data enable the inclusion of perspectives from key participants in the banking industry, enabling a thorough examination of the factors that influence settlement risk. The selected banks include both major and small financial institutions, each offering distinct viewpoints on the methods and challenges associated with settlement risk management. The first step in data collection included identifying suitable respondents inside each selected bank. Senior executives overseeing risk management, operations, and compliance, as well as members of the governing body accountable for the banking sector, will all exist. This research aims to gain a thorough understanding of settlement risk and its management in the Lebanese banking industry via interviews with key decision-makers and regulatory professionals. Semi-structured interviews may be conducted either in person or online, depending on the availability and preferences of the participants. Participants were given the opportunity to freely express their ideas and experiences regarding settlement risk. In-depth interviews will be conducted to investigate participants' perspectives on settlement risk, risk management strategies, adherence to regulatory requirements, and the impact of external factors, such as

economic and political conditions, on settlement risk. Researchers will use methodologies such as active listening and open-ended probing to obtain valuable information from respondents about settlement risk. Audio recordings will be created from the interviews with the participants' consent to facilitate data processing and enhance the capture of subtle remarks.

THEMATIC ANALYSIS

Relationship between Economic Stability and Settlement Risk

The first interviewee, a senior executive of a large Lebanese bank, emphasized the significance of economic stability in reducing settlement risk within the financial system. The discussion revolved around the significant impact that fluctuations in the economy, such as currency exchange rates, inflation rates, and interest rates, might have on settlement risks. According to the responder, market participants exhibited more caution during periods of economic instability, leading to an elevated settlement risk caused by the potential for counterparty defaults. As a result of this heightened risk, the process of completing financial transactions may experience delays and concerns over the financial stability of other parties involved may emerge. The bank has robust risk-management strategies to safeguard against possible hazards. The reply emphasized the importance of effectively managing liquidity, ensuring that sufficient funds are available to make timely payments as required. In addition, they emphasized the need for collateral requirements as a way to reduce risk when a counterparty fails to fulfill their obligations. Additionally, they said that their bank diligently analyzed economic indicators to assess their potential impact on settlement risk. This involves analyzing the broader aspects of the economy, government, and regulations. This reply further stressed the need for sufficient capital reserves to withstand economic downturns and avoid bank insolvency. To enhance transparency and reduce the likelihood of settlement risk scenarios, they emphasized the need to adhere to rigorous regulatory compliance protocols, including the Know Your Customer (KYC) and Anti-Money Laundering (AML) standards.

The second interviewee, a risk manager from a Lebanese bank, explained the meticulous approach used by his business to assess and manage settlement risk, considering the economic stability of the nation. The answer provided detailed information about the financial data and specific aspects that their banks closely monitored to evaluate settlement risk. Indicators such as Gross Domestic Product (GDP) growth, Foreign Exchange reserves, inflation rates, and Sovereign Credit Ratings exemplify this. The bank aims to obtain a comprehensive understanding of the current status of the economy and assess any potential settlement risk by analyzing these data. The answer emphasized the significance of scenario analysis, stress testing, and contingency planning while discussing the bank's preparation for economic downturns. The bank may conduct a scenario analysis to predict and assess the impact of potentially catastrophic economic scenarios on the settlement risk. The purpose of stress testing is to identify vulnerabilities in bank settlement procedures during periods of intense stress. Banks may use stress testing and scenario analysis to enhance their readiness and resilience during economic downturns. The risk manager discussed the bank's enhanced risk management strategies to effectively address settlement risk issues using insights from past economic crises. Lessons derived from previous economic downturns have led to enhanced risk assessment, response planning, and communication protocols. The answer emphasized the use of proactive risk management strategies and the need to collaborate with stakeholders, including customers and regulatory agencies. By collaborating, banks may gain a deeper understanding of the intricacies of settlement risk, exchange expertise, and optimal strategies for managing settlement risk in times of economic instability.

The third interviewee provided a valuable perspective on the pivotal role of regulators in managing settlement risks in the context of maintaining economic stability. This individual is a delegate of the regulatory authority that oversees the banking sector in Lebanon. The respondents in this section analyzed the legislative boundaries of settlement risk management and how they effectively tackled concerns related to monetary and fiscal stability. The regulatory body places significant emphasis on ensuring that banks have robust risk-management procedures in place and maintain economic stability. They established guidelines and protocols that financial institutions must adhere to while managing settlement risks. Regulators enforce capital requirements, liquidity ratios, and stress test standards to ensure banks can withstand economic downturns. To guarantee that banks adhere to risk management regulations and maintain appropriate settlement processes during economic crises, the responder emphasized the need for strict supervisory oversight. The regulatory authority conducts regular inspections and assessments of financial institutions to evaluate their risk management protocols and monitor their exposure to settlement risks. The regulatory authority actively strives for financial stability and decreases the settlement risk in collaboration with the central bank. To mitigate potential dangers that may arise from settlement risk, they emphasized the need for ongoing surveillance, evaluations of risk, and prompt interventions within the banking sector. In times of economic instability, the responder emphasized the need for

regulatory coordination and effective communication with banks, customers, and other significant stakeholders. The efficient management of settlement risks requires transparent and prompt communication among all relevant parties.

Interviewee four, an economist or financial analyst well-versed in the Lebanese economy, provided an external perspective on the relationship between economic development and the possibility of legal dispute. The respondents shared their insights into the current economic situation in Lebanon and its potential impact on settlement risk within the banking sector. The answer highlighted the importance of macroeconomic analysis when considering the hazards associated with economic fluctuations. Political uncertainty, changes in fiscal policy, and external shocks have been identified as potential contributors to the increased settlement risk and heightened volatility in financial markets. Heightened credit and liquidity risks may negatively affect the financial stability of market participants, which may cause delays or defaults in settlements during times of economic turbulence. When assessing settlement risk in the Lebanese banking sector, economists emphasized the need to consider the interconnectedness of the financial system. The discussion revolved on the interdependence of the economy's well-being on the stability of individual banks and how issues within one sector of the financial system may have global repercussions. The responder provided prognostications and projections about future economic conditions to gain a deeper understanding of the potential impact of economic stability on settlement risk. These estimations were derived by analyzing economic trends, external impacts, and governmental reactions. Interviewee 4 offered valuable contextual information on the broader economic environment in which settlement risk arises.

The fifth interviewee was a business customer of a Lebanese bank, who provided a compelling perspective on the impact of settlement risk on their company's financial performance. This study examined the influence of settlement risk on interviewees' day-to-day activities and financial transactions. The responders expressed their cautious approach to financial decision-making during periods of economic instability, citing concerns about the potential hazards associated with their banking counterparts. Businesses must exercise heightened caution when managing their financial exposure during periods of economic volatility, as this may amplify uncertainty and erode market confidence. According to the responder, the most effective approach for banks to alleviate customer concerns and reduce their worry is through transparent communication and implementing sensible measures to mitigate the dangers they encounter. Transparency in bank settlement operations, risk management, and financial health fosters trust and enables clients to make informed decisions. Respondent 5 emphasized the importance of banks maintaining open channels of communication and providing frequent updates on settlement processes during periods of economic decline. They emphasized the need for prompt and accurate resolution to enable smooth financial transactions and support their company's operations.

Relationship between Political Stability and Settlement Risk

The first respondent, a prominent banking executive in Lebanon, emphasized the significance of a nation's political stability in mitigating settlement risk within the financial sector. The discussion revolves around the potential impact of political uncertainty and instability on settlement risk. According to the responder, market participants exhibited more caution in the presence of political turmoil, leading to an elevated settlement risk caused by potential counterparty failures. A volatile political environment may increase settlement risk by diminishing investor confidence and modifying the market dynamics. Their bank takes precautionary measures and employs proactive risk-management strategies to address such dangers. The responder emphasizes the need to monitor political developments because of their potential impact on settlement risk. They emphasized the need to use scenario analysis and stress testing to assess a bank's resilience in the face of political turmoil. To enhance its readiness to handle uncertainty, banks should have a comprehensive understanding of the risks associated with political change. The interviewee also highlighted the need to establish strong relationships with counterparties and consumers during political turmoil. Efficient management of settlement risk requires transparent communication and active engagement from all parties involved.

The second respondent, a risk manager from a Lebanese bank, offered a valuable perspective on the firm's assessment of settlement risk in relation to the country's political situation. The responder provided detailed information on the primary political indicators and factors that their bank monitored to evaluate the potential impact on settlement risk. Political events, geopolitical wars, government changes, and policy revisions may influence market dynamics and settlement processes. The risk manager emphasized the need to conduct scenario analysis and stress testing specifically targeted at political events. If a bank is knowledgeable about how political instability may disrupt financial markets and harm counterparties, it can identify potential vulnerabilities in its settlement operations and implement appropriate risk mitigation measures. The answer detailed their banks' enhanced risk management strategies for mitigating settlement risk issues, which have been informed by insights gained during past periods of political upheaval. The need for early warning systems, response planning, and risk identification to effectively manage political risk in settlements has been emphasized. An important focus of the interviewees was the establishment of a society that was highly aware of and responsive to potential risks. Employees possess the necessary expertise and resources to promptly handle the

consequences of settlement risk arising from political instability.

The third interviewee, employed by the Lebanese government organization responsible for banking supervision, emphasized the crucial role of political stability in reducing settlement risk. An examination of settlement risk and its intersection with political issues was conducted in the context of the regulatory system. Regulatory authorities prioritize monetary stability and require banks to employ effective risk management measures to reduce settlement risks. They established guidelines and protocols in which financial institutions are obligated to adhere to mitigate settlement risk in times of political turmoil. The answer emphasized the need to implement rigorous regulatory oversight to ensure that banks effectively assess and handle settlement risk in times of political turmoil. Regulatory authorities evaluate banks' resilience to political events and their potential impact on settlement operations through regular examinations and stress testing. Regulatory authorities actively engage in partnerships with banks to strengthen financial stability and reduce settlement risks in coordination with other interested parties. To mitigate the potential systemic risks associated with settlement during periods of political turmoil, they emphasized the need for ongoing surveillance, risk evaluations, and timely interventions within the banking sector.

Interviewee four, who had expertise in the Lebanese economy as an economist or financial analyst, provided an external perspective on the correlation between political stability and settlement risks. The responder discussed their research on the potential impact of political uncertainty on the level of risk associated with investments in the banking sector. The answer emphasizes the importance of political stability in maintaining market and investor confidence. Political instability and geopolitical conflicts may adversely affect market liquidity and settlement risk. Insufficient trust between investors and market players may lead to delays and failures in financial transactions. Economists emphasized the need to consider the whole situation when assessing the potential for financial loss in the Lebanese banking sector. Disruptions in the political or economic domains may have profound ramifications for both. To understand the impact of political instability on settlement risk, it is essential to understand these interconnected interactions. The responder also discussed the potential effects of changes in the political environment on risk management and regulatory regulations. Financial institutions should consider updating their risk models and policies due to the changing political landscape. The capacity to adapt is crucial for effectively managing settlement risks in a volatile political environment.

The fifth interviewee in our series of comprehensive interviews was a commercial or corporate customer at a Lebanese bank. They shared their perspective on how settlement risk impacts their operations given the present political situation. Their conversation revolved around the impact of settlement risk on their day-to-day activities and financial transactions in times of political turmoil. As for the respondent's statement, the political atmosphere might potentially influence company decisions and financial transactions due to the ambiguity it generates. Customers face a high settlement risk due to the potential for counterparties to fail, which may result in payment delays or disruptions in the supply chain. They emphasized the need for banks to be proactive in times of political turmoil by engaging in communication and implementing measures to mitigate risk. Customers should engage in open discussions on settlement processes and dangers to enable them to make informed decisions and make necessary preparations. According to the respondent, banks have not adequately met their need for prompt information on settlement processes and the potential risks arising from political events. Banks' ability to effectively handle settlement risk during political uncertainty is crucial for maintaining trust and ensuring seamless operations.

Customer perspectives are essential for advising banks on how to improve their management of settlement risk, thereby enhancing client relationships and ensuring an uninterrupted flow of financial transactions, even in the face of political uncertainty. Five participants were chosen to represent various sectors of the Lebanese banking sector. Their feedback provides valuable insights into the relationship between political stability and settlement risk. Each respondent provided insights into settlement risk in Lebanon, considering their specific roles and skills. This contributes to a comprehensive understanding of the dynamics and effects of settlement risk in the context of political instability. The respondents emphasized the need to monitor political developments, conduct hypothetical analyses, and foster collaboration among stakeholders to effectively mitigate settlement risk in times of political turbulence. An in-depth analysis of settlement risk in the Lebanese banking industry must be conducted, taking into consideration political stability, to develop customized risk management strategies that would enhance the country's economy. Policymakers, regulators, and banking professionals may use these insights to effectively handle politically difficult situations and reduce settlement risks. It is important to understand the correlation between political stability and settlement risk to enhance the financial stability and resilience of the banking system.

Relationship between Regulatory Framework and Settlement Risk

One respondent, who has a prominent position at a large Lebanese bank, emphasized the significance of the regulatory framework in mitigating settlement risk within the financial sector. The conversation revolved around the

crucial role of the regulatory environment in influencing settlement risk and risk management measures. The responder emphasized that banks had a robust foundation for analyzing, monitoring, and mitigating settlement risk due to the regulatory structure governing these operations. Their explanation focused on how banks may have confidence in their risk-management strategies because of their adherence to laws. The interviewee stressed the need for regulators to monitor banks to verify their compliance with settlement risk-management regulations. The authorities stressed the need to conduct regular evaluations and stress testing to evaluate banks' ability to resist settlement risks and identify areas for improvement. The answer further stated that the legislative framework promotes transparency and accountability in the process of resolving disputes. Regulators enhance market participants' capacity to communicate and cooperate in mitigating risks by establishing clear standards and mandatory reporting obligations.

The second interviewee, a risk manager from a bank in Lebanon, examined the relationship between the legal framework and settlement risks. The responder provided detailed information on how regulatory restrictions impact banks' risk management strategies and the assessment of settlement risk. The risk manager emphasized that banks' risk management practices were guided by the regulatory framework. The conversation revolved around banks' risk policies and their alignment with regulatory requirements and industry standards. The answer highlights the importance of risk disclosure and regulatory reporting in reducing settlement risk. A bank's proactive management of settlement risk relies on its adherence to reporting responsibilities. The answer further highlights the need for regulatory stress testing in assessing the bank's capacity to endure settlement risk under adverse circumstances. The outcomes of these stress tests enable the bank to identify and mitigate any areas of susceptibility, thereby safeguarding it against potential damage.

The final respondent, a bank regulator in Lebanon, provided a more comprehensive analysis of how the framework addressed settlement risk. The conversation revolved around the protocols and guidelines that financial institutions must adhere to to effectively manage settlement risk. According to the respondents, the primary objective of the regulatory framework is to guarantee that banks practice appropriate risk management. The regulatory authorities emphasized the need to conduct frequent assessments of banks' proficiency in managing settlement risk. As per the interviewee, regulatory stress testing is crucial for assessing banks' capacity to endure settlement risks. Stress testing enables the regulatory body to gain a deeper understanding of systemic risks and potential vulnerabilities within the banking sector. The responder said that the regulatory framework fosters collaboration among banks to mitigate settlement risks. The regulatory authority fosters the implementation of effective settlement risk-management practices by establishing comprehensive industry standards.

The fourth interviewee, an economist or financial expert well-versed in the Lebanese economy, provided an impartial perspective on how the legal framework impacted the likelihood of resolving a dispute via the judicial system. The respondent discussed settlement risks in the Lebanese banking business in relation to regulatory norms and standards. As per economists, the regulatory framework enhances settlement procedures by requiring clear reporting and disclosure of risks, facilitating the identification of possible problems, and encouraging immediate measures to minimize them. The responder emphasized the significance of the regulatory framework in promoting financial stability by enforcing institutions' adoption of robust risk management procedures. Prudent risk management may help prevent settlement defaults and potential disruptions in the financial system. The economist provided more insights into the impact of the regulatory framework on banks' risk appetite and culture. Banks adhere to stringent regulatory mandates that influence risk decisions and cultivate a culture of risk-consciousness.

The fifth interviewee was a commercial customer of a Lebanese bank and provided a compelling perspective on how the regulatory framework impacts settlement risk. The responder discussed the impact of regulatory duties on their interactions with the banks and settlement processes. The responder emphasized that they have a sense of safety and confidence in their banking relationships due to the regulatory framework. They focused on banks' adherence to regulatory standards, which demonstrates their commitment to implementing effective risk management techniques, particularly in relation to settlement risk management. The responder emphasized the need for transparency and regulatory disclosure in the context of managing settlement risk. Timely and accurate information about settlement processes empowers customers to make informed financial decisions and effectively assess risks. The respondent emphasized the need for regulatory oversight to ensure that banks prioritize their duties in managing settlement risk. Regulatory scrutiny compels banks to uphold state-of-the-art risk-management practices. Insightful perspectives on the relationship between the regulatory environment and settlement risk were obtained from five respondents, who represented various stakeholders in the banking sector. Various respondents offered significant insights into the impact of rules on settlement risk dynamics, drawing from their occupations and areas of expertise. Participants highlighted the significance of the regulatory framework in promoting accountability in risk management, financial disclosure, and stability. Compliance with regulatory requirements enables banks to effectively evaluate, manage, and mitigate settlement risk.

RECOMMENDATIONS

The interviews indicate that the banking sector in Lebanon must use appropriate risk management techniques to effectively mitigate settlement risk. Banks should consider both economic and political factors when evaluating the possibility of financial loss in a settlement. Evaluating the potential impact on settlement processes can be accomplished via the implementation of stress tests and scenario analysis. Implementing proactive risk-mitigation measures involves developing contingency plans and response mechanisms to promptly address settlement defaults. Establishing transparent channels of communication between banks and their counterparts is particularly crucial during periods of economic and political volatility. To cultivate trust and inspire confidence among market participants, it is crucial to provide prompt and comprehensive information on settlement methods and potential hazards. Utilizing advanced technology and automated procedures may effectively mitigate settlement risks by minimizing the probability of errors and delays.

To effectively mitigate settlement risk, it is essential for banks, regulatory agencies, and other players in the Lebanese banking industry to collaborate and exchange pertinent information because of the interconnectedness of the sector. Regulatory authorities should endorse industry-wide conferences to foster collaboration and exchange of optimal strategies for managing settlement risk. Enhancing regulatory coordination is necessary to establish consistent risk management regulations and to encourage the adoption of similar methods throughout the sector. Facilitating the exchange of information among banks on settlement risk trends and potential risk scenarios may assist in collective evaluation and response to risks.

An effective and flexible regulatory framework is necessary to address settlement risk issues effectively. When evaluating banks' settlement risk management systems, regulatory authorities should prioritize institutions with higher levels of exposure to settlement risk. This should be performed by using a risk-based approach. Regularly reviewing banks' settlement risk management capabilities is crucial to emphasize the significance of compliance with risk management standards and promote ongoing enhancements. The evaluation of banks' capacity to endure settlement risk in various economic and political circumstances may be accomplished through regular stress testing. This process enables the identification of vulnerabilities and the formulation of risk-mitigation measures. Banks may enhance their ability to immediately adapt to evolving regulatory requirements by diligently staying informed of regulatory standards and expectations pertaining to the management of settlement risk.

Owing to the prevailing economic and political challenges in Lebanon, settlement risk remains a prominent concern for the banking sector. Banks may enhance their management of settlement risks by applying the aforementioned suggestions. To enhance the financial stability and resilience of the Lebanese banking system, it is imperative to adopt measures that bolster risk-management practices, foster stakeholder collaboration, and enhance the regulatory framework. If Lebanese banks adhere to this guidance, they may successfully address settlement risk issues and make a significant contribution to a more stable and robust financial system.

CONTRIBUTIONS

An analysis of settlement risk in the Lebanese banking sector may provide valuable insights into financial risk management and policymaking, particularly in relation to economic and political stability, and the regulatory environment. This report offers a comprehensive analysis of the complex relationship between settlement risk and the Lebanese banking sector. This research provides a valuable understanding of the relationship between economic and political stability, settlement risk, and the likelihood of settlement defaults. By acquiring a more comprehensive understanding of the dynamics of settlement risk, banks and regulators may enhance their capacity to anticipate and address distinct challenges arising from economic and political volatility. Interviews with key stakeholders provided valuable insights into managing settlement risk in the context of Lebanese economic and political challenges. Banks can effectively mitigate settlement risk by deploying customized risk management systems that address the specific mix of settlement risk factors present in each institution. If banks are equipped with tailored solutions, they can mitigate the impact of settlement defaults on the financial system, particularly when facing economic and political instability.

Settlement risk can endanger financial stability and undermine market confidence. The research findings bolster financial stability in the Lebanese banking system by underscoring the need for robust risk-management protocols, proactive risk-mitigation measures, and effective collaboration between banks and regulatory authorities. By implementing the recommendations of the report, stakeholders can bolster an economic system that is resilient and secure against settlement risk concerns and potential systemic risks. The study's results are informative for policymakers and regulators, as they analyze the influence of the regulatory framework on the management of settlement risk. To

enhance settlement risk regulations and guidelines, authorities should begin by obtaining a precise evaluation of the strengths and weaknesses of existing regulatory environments. The banking sector may gain advantages from a regulatory framework that is more adaptable to market fluctuations and in line with international standards. The study's thorough methodology demonstrates the need for an interdisciplinary approach to risk management by analyzing economic, political, and regulatory factors. When banks and governments consider the interplay between these elements, they may enhance their decision-making and formulate more comprehensive risk management plans.

The findings of this research contribute to the expanding corpus of academic literature on the management of settlement risk in Lebanon's banking sector. This study enhances the existing body of knowledge on financial risk management and its relevance in certain geopolitical contexts by investigating the relationship between economic stability, political stability, and the regulatory framework. Adhering to the research's proposals and findings may greatly enhance the long-term sustainability of the Lebanese banking sector. Banks may enhance their ability to withstand economic and political challenges by reducing settlement risks and enhancing their risk management systems. Enhanced market confidence leads to more investments and a more robust and stable financial industry. The results of this study have significant policy implications beyond the financial services sector. Studying the relationship between settlement risk and stability might provide valuable insights into the development of important economic and political strategies. Policymakers may enhance financial system stability by implementing policies that consider the potential impact of economic and political instability on settlement risks.

LIMITATIONS

It is important to consider certain limitations when examining settlement risk, economic stability, political stability, and the regulatory environment in the Lebanese banking sector. The qualitative approach, which depends on interviews with relevant stakeholders, may be influenced by the sample size and selection bias. The presence of selection bias may have led to the exclusion of important stakeholders who possess relevant perspectives on settlement risk, and the limited sample size may not accurately represent the wide range of ideas and experiences present in the Lebanese banking sector as a whole. Due to the unique financial and political conditions in Lebanon as well as the varying situations in different markets, the findings of this research may only be relevant and applicable to Lebanon and may not be generalizable to other contexts. Participants' expectations and views may bias the second round of interview-based qualitative data. The findings may be ambiguous due to the possible bias of respondents despite efforts to maintain objectivity and impartiality. Furthermore, it is possible that the interviews did not comprehensively capture all aspects of settlement risk management. A comprehensive understanding of the settlement risk environment may be impeded if respondents omit essential information such as confidential or classified data. Furthermore, the volatility of political and economic circumstances presents a challenge. Settlement risk dynamics are influenced by ongoing fluctuations in economic and political environments. The static data-gathering approach may not adequately capture the dynamic characteristics of these components, hindering the evaluation of their immediate effects on settlement risk. Furthermore, this research relies on the current regulatory environment, as in the study's conclusion, to analyze the regulatory framework. The management of settlement risk in the Lebanese banking sector might potentially be affected by forthcoming alterations to regulatory frameworks or the implementation of novel regulations or policies subsequent to the conclusion of this research.

The reliance on qualitative data hindered any quantitative examination of the interrelationships between settlement risk, economic stability, political stability, and the regulatory environment. Quantitative data may provide a more comprehensive understanding of the scope and strength of these relationships. The data collected during the study may have been influenced by external factors outside researchers' control, such as geopolitical events or economic shocks. These incidents may affect the dependability of the findings or introduce additional biases into the research. Preserving the confidentiality of interviewees and safeguarding other delicate data pose challenges. Although we have made efforts to safeguard our users' privacy, we cannot guarantee the anonymity of their data. Ultimately, the limitations of the research's time limits hindered our ability to thoroughly analyze the data. A more comprehensive understanding of the dynamics of settlement risk may have been achieved if the research period had been prolonged.

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