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Goldman asks what if Lebanon is forced to restructure debt

Goldman Sachs Group Inc. still sees an imminent debt restructuring in Lebanon as unlikely but is already turning its attention to how much investors could recover as one of the most indebted countries teeters on the brink of financial crisis. Under the U.S. bank's base scenario, foreign investors would recover 35 cents on the dollar, Farouk Soussa, an economist at Goldman Sachs, said in a report. He added, however, that any debt overhaul would put the country's banks first, meaning "the actual recovery value" would be significantly different to contain damage. Local lenders are among the biggest holders of Lebanon's sovereign debt.Political turmoil and sluggish economic growth are prompting questions on how long Lebanon can avoid a financial meltdown that would further destabilize an area rattled by war in Syria and tension between Israel and Hezbollah.Lebanon's sovereign debt risk surged 280 basis points over the past year to 800, making it the world's third-worst performing among credit default swaps tracked by Bloomberg. "In the continued absence of significant improvements in the political, economic and financial prospects of the country, the possibility of a financial crisis and sovereign default is growing," Soussa said.In his report, Soussa said the country is unlikely to make its debt sustainable through fiscal adjustment because that would require a sharp decline in interest rates or substantial economic growth.While possible, both "are largely outside the control of policymakers, and are highly dependent on regional economic and political developments," he wrote.Starting in 2016, commercial lenders have been encouraged to draw new deposits and park their liquid foreign assets at the Central Bank. The "symbiotic" relationship between authorities and banks complicates the math of easing one of the world's biggest debt burdens, Soussa said in the report dated Jan. 4."Any possible restructuring is likely to be designed in such a way as to minimize the fallout for the local banks," he said.While Lebanon has long teetered on the brink of a full-blown crisis, it's never defaulted despite the 15-year Civil War, numerous flare-ups with Israel and a devastating war next door in Syria that cost its economy an estimated $18 billion.Its financial system probably has enough foreign-currency liquidity to fund deficits "for the next couple of years, all else equal," Soussa added.Foreign investors, however, aren't discounting the possibility this time may be different. Caretaker Finance Minister Ali Hasan Khalil admitted as much last month when he warned "the crisis today has started to transform into a financial crisis from an economic crisis."Goldman Sachs puts the exposure of local lenders to the government's local debt and Eurobonds at some 55 trillion Lebanese pounds ($36.5 billion), almost double the capital base of the whole banking system.