# COMMERCIAL BANKING IN LEBANON

by

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## ABSTRACT

The Lebanese commercial banking system is composed of two types of institutions. On the one hand, there are the branches of foreign banks in Lebanon, on the other, there are the local commercial banks. It is the latter group of banks that is the subject of this work.

The history of these local banks does not go back to more than a decade. In fact they have assumed their importance only after independance in 1943. Within such a short period, a banking system will not have had the time and the means to acquire the professional experience and technical proficiency needed, especially in the absence of a developed money market and efficient government control and guidance. Within this framework an attempt is made to give the reader a general description and analysis of the commercial banking system.

Since world war I, and up to the end of the second world war, the rudimentary banking system in Lebanon had changed little. The basic picture was one of a few branches of foreign banks utilizing small amounts of capital of their parent organization mainly to finance short-term and seasonal credit to stronger local merchants and land owners of the country. Local banks on the other hand were small private enterprises or partnerships which had very limited capital

at their disposal and could not rely to any significant degree on deposits as source of funds.

Since the end of world war II, and due to late internal and external causes, banking activities in Lebanon expanded in a spectacular fashion. But only slight structural changes took place in the banking system. The number of foreign banks increased and the volume of their business multiplied. Local banks organized by Lebanese individuals or groups entered the field in a more professional fashion. This expansion was naturally induced by growing foreign trade and economic activity in the post-war period and particularly after 1956. But in spite of this expansion, however, there still exist some basic defects in the banking system of Lebanon.

One of the most important of these defects is the absence of banking legislation and a banking code that has for its purpose the control of banks activities in a way to protect depositors, and to safeguard the solvency and liquidity of the system.

Another major defect is the nonexistance of a central bank. Such a bank in Lebanon will organize the commercial banking system on a wholesome basis. In order to establish this aim, the central bank should be flexible in its operations and dealings with the commercial banks and help the promotion of further development in both commercial banking as well as in the money market.

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CHAPTER I

## THE MONETARY SYSTEM AND MONETARY EVENTS OF LEBANON

### I. The Monetary System up to the End of World War II

Modern history of the Lebanese money started in 1920 when the French authorities created for the first time a Syrian-Lebanese paper currency.[1]

Before the end of World War I, the Anglo-French army occupied Syria and with it brought the Egyptian paper currency which it was using during the time of its invasion. The Egyptian pound remained in circulation until the French Administration took over from the British at the end of 1919. In order to alliviate the burden of buying Egyptian pounds, the French Government abrogated the declaration decreasing the Egyptian pound legal tender and established by Arrete No. 129 of April 2, 1920 a new Syrian-Lebanese paper currency.

The new Syrian-Lebanese currency was linked completely to the French Franc. The new currency became the Lebanese pound which was made equivalent to 20 French

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1. Syria, of which modern Lebanon is the Western part, was part of the Ottoman Empire since the beginning of the 16th century.

Francs and was freely redeemable in French Francs by cheque on Paris. The right to issue the Syrian-Lebanese pound was conferred on the Banque de Syrie, a private French bank, in accordance with the agreement signed between it and the French Minister of Finance and approved by the French Minister of Foreign affairs in April 1919.

The new currency was at first exchangeable for the Egyptian pound which was in circulation in the occupied territory. To facilitate the withdrawal of Egyptian currency from circulation, the French Treasury charged the B.S.L. and the offices of the French Army in Lebanon and Syria to exchange Lebanese-Syrian notes for Egyptian notes. This free conversion of Egyptian money into the new Lebanese-Syrian pound continued until January 1, 1921 when the Lebanese-Syrian currency was made the sole legal tender. In October 1923 negotiations were opened with the government of the Great Lebanon, the Syrian Federation and Jabal el-Druz to recognize the Syrian-Lebanese currency and confirm the status of the Banque de Syrie et du Liban. A convention between the B.S.L. on the one hand, and the said Governments on the other was signed on January 23, 1924.[1] According to this convention the franc exchange standard was sanctioned and the B.S.L. received the exclusive privilege of issuing notes of unlimited legal tender for a period of fifteen

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1. See Appendix I.

years beginning April 1, 1924.

The advantages to the French Government of the new monetary system (as described in Appendix I) are obvious. The French Administration could easily get from the Banque de Syrie the money it needed for its expenditure in Syria against corresponding credit in francs at the French Treasury, or against bons de la Defense Nationale. The credit in francs acted as a cash reserve enabling the bank to redeem its notes in checks on Paris; while the bons served to make up the remainder of the cover, at the same time forming a lucrative investment. With the above reserve the new currency, in effect, constituted a loan by the people of Syria to the French Government, made possible by the legal tender quality given to the paper. The part of the notes, covered by the bons, represented a time loan; while its portion, covered by the franc credit, represented a demand loan. To the extent that the new paper could be circulated, to the extent that the French Government could defray its expenditure in Syria through its own credit. Consequently, the financial burden on the French Treasury was lightened. On the other hand the Egyptian money received directly in exchange for Syrian notes could be used by the French Government in settlement of Foreign claims"[1]

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1. Himadel S.B. Monetary and banking System of Syria. Beirut 1935. p. 66.

Before the introduction of the new currency the French Government was a buyer of Egyptian money for its expenditure in Syria and Lebanon. The demand of Egyptian money, or indirectly of British exchange, influenced adversely the rate of exchange of the franc. When the expenses of the French Government in Syria began to be defrayed in paper money representing francs, Egyptian currency was no longer needed. Besides, the Egyptian money withdrawn from Syria and Lebanon by the French Treasury through the Bank were presented to the National Bank of Egypt for payment in London exchange. Thus the benefit to the French Treasury due to the circulation of the new Syrian-Lebanese currency was two-fold. In the first place it lessened the demand for foreign exchange for the Government expenditure in Syria and Lebanon and second it increased the supply of French credit abroad.

From the time it was introduced in May, 1920 until the end of 1926, the Syrian-Lebanese currency, following the changes in the value of the franc suffered considerable fluctuation and depreciations. From table one below the rate of the American dollar ranged between 54.7 Syrian-Lebanese piasters for the month of April, 1922 and 207.8 Syrian-Lebanese piasters for the month of July, 1926. This caused holders to suffer inconvenience and loss.

The effects of depreciation were more pronounced in Lebanon,

TABLE I

DOLLAR EXCHANGE RATES MAY 1920 TO DEC. 1927

(monthly average - Syrian Piasters per Dollar)

| Month | 1920 | 1921 | 1922 | 1923 | 1924 | 1925 | 1926 | 1927 |
|---|---|---|---|---|---|---|---|---|
| Jan. | | 60.0 | 61.6 | 73.4 | 105.0 | 92.7 | 132.5 | 126.3 |
| Feb. | | 70.8 | 56.0 | 81.5 | 112.1 | 94.5 | 135.7 | 127.6 |
| Mar. | | 71.4 | 55.6 | 79.5 | 108.7 | 96.6 | 138.6 | 128.1 |
| Apr. | | 54.7 | 55.5 | 82.2 | 82.2 | 96.0 | 147.7 | 127.8 |
| May | 72.9 | 59.7 | 55.3 | 75.2 | 86.0 | 95.5 | 157.6 | 127.6 |
| June | 62.9 | 61.7 | 75.5 | 79.0 | 95.4 | 104.3 | 167.2 | 127.6 |
| July | 61.7 | 62.9 | 60.6 | 84.5 | 97.0 | 106.4 | 202.8 | 127.6 |
| Aug. | 69.5 | 69.6 | 63.0 | 88.5 | 92.0 | 106.8 | 179.6 | 127.6 |
| Sept. | 74.0 | 68.7 | 64.9 | 86.9 | 93.7 | 106.1 | 173.4 | 127.5 |
| Oct. | 77.0 | 68.9 | 67.8 | 83.8 | 95.4 | 112.7 | 170.9 | 127.3 |
| Nov. | 83.3 | 68.7 | 72.7 | 89.9 | 94.8 | 126.3 | 147.2 | 127.3 |
| Dec. | 86.2 | 65.0 | 69.5 | 95.3 | 92.4 | 133.4 | 127.5 | 126.9 |

Source: Himadeh, op.cit., p. 78

particularly in the coastal cities where Lebanese-Syrian bank notes were the principal currency. The interior was less affected as the new currency was very little used there.

After August 1926, the rate of the Lebanese-Syrian pound following the franc, began to advance reaching 127.5 Lebanese Syrian piasters to the American dollar in December 1926, the month during which the pegging of the French franc started. It continued around this figure until June 25, 1928 where the franc was stabilized at 65.5 milligrams of gold. From June 25, 1928 to September 26, 1936 Lebanon had in effect a gold exchange standard. The Lebanese-Syrian pound was exchangeable into 20 francs, which in turn were exchangeable into gold at the rate of 65.5 milligrams to one franc. With the departure of France from the gold standard on September 1936, the monetary standard of Lebanon reverted to the Franc exchange which had been the standard from April 2, 1920 to July 25, 1926.

In spite of the evils that befell Lebanon and Syria from the franc depreciation before 1928, the French High Commission brought considerable pressure on the Syrian and Lebanese Governments to renew the 1924 convention between them and the "Banque de Syrie et du Grand Liban" which was to terminate on March 31, 1939. Before the termination of this convention (1924) separate negotiations were made for its renewal between each of the Government of Syria and the Government of Lebanon and the Bank. These negotiations led to the signing of a new convention on May 29, 1937 between the Lebanese Government and the bank for a period of 25 years beginning April 1, 1939. A similar convention between the Syrian Government and the Bank was signed on March 25, 1938. But while the Lebanese Parliament ratified the convention it was not even presented to the Syrian Parliament because it was expected that the majority of its numbers would refuse to ratify it.

Not long after the signing of the 1937 convention World War II broke out and consequently a number of changes in the above agreement and in the operation of the B.S.L. took place. These changes were necessitated by war conditions and were supposed to be temporary. One of the important changes related to the composition of the note cover took place on September 4, 1939. By decree No. L.R./208, the High Commissioner authorized the B.S.L. to increase the proportion of commercial papers in the reserve to 25 percent and the proportion of the amount of commercial papers together with the optional deposit at the French Treasury to 35 percent. He also authorized the Bank to place in the currency reserve the whole or part of all loans made to the states of Syria and Lebanon or loans guaranteed by these states and bonds issued by public institutions and guaranteed by these states.

But by far the most important of these changes was that decreed by Arrete No. L.R./152 according to which the High Commissioner charged the B.S.L. with the responsibility of giving permits for the export of capital, and required the bank to establish a bureau of exchange as "Office des Changes" which was to operate for the account of the Mandatory Power and under its responsibility. All exchange operations were to be centralized in the "Office". With few exceptions all possessors of foreign exchange and foreign securities were required to sell these possessions to the office. Shortly afterwards the control of the "Office" passed from the hands of the Vichy authorities which represented the French Government that sided the Germans during World War II, to the Free French Deligation. This control remained in the hands of the Free French Deligation up to 1944 when it was transferred to the Governments of Syria and Lebanon.

Through the control of the "Office des Changes" the French were able to lay their hands on all foreign exchange in Syria and Lebanon. The Vichy authorities secured the foreign exchange by paying for it in Syrian-Lebanese currency advanced to the B.S.L. against deposits of French Francs at the French Treasury and French Government bonds at the Bank of France.

In June 1941 the invasion of Syria and Lebanon by the Allied forces started. In November 12, 1941 i.e. three months after the occupation of Syria and Lebanon by the Allied Armies, the Deligate General, General Catroux issued an arrete No. F L/38 concerning the office de changes. According to this arrete the Office was made an independent office working for the account of the Free French Deligation and on its responsibility. The administration of the "Office" was entrusted to the B.S.L. The purchase price of the pound sterling was fixed at 883.125 Syrian-Lebanese piasters, and the purchase price of other foreign currencies were to be fixed according to this equivalent in sterling in the London market.

The bank was authorized to substitute the whole or a part of the loans in Syrian-Lebanese currency advanced by the bank to the Office des Changes for certain elements in the reserve for subsequent issues in the currency. The elements substituted are;

a) The obligatory deposit in francs at the French Treasury in Paris amounting to 25 to 26 percent of the note circulation.

b) Bonds issued by the French Government or secured by it maturing within a period not exceeding five years provided that not less than 25 percent of the amount of these bonds mature within a period of two years.

c) The optional demand deposit in francs at the French Treasury the amount of which should not exceed 6 percent of the amount of notes in circulation.

The foregoing arrete made the office des changes the property of the French Deligation. It also made the loans advanced by the B.S.L. in Lebanese-Syrian currency, in order to enable the office to buy foreign exchange eligible to constitute a part of the note circulation reserve. In other words the foreign exchange held by the Office des Changes was made the property of the Deligation General and it also made the loans advanced by the bank to the Deligation General occupy in the note circulation reserve the place of the sterling and dollar exchange. The purchase of foreign exchange in this way was thus financed by the Lebanese people through the B.S.L.

On January 13, 1944 an "Aide Memoire" exposing the question of a new Franco-British agreement was handed to the government of Lebanon. The "Aide Memoire" pointed out that the Franco-British authorities decided that it was essential to create a block of the franc and of the monies attached to it. With this view a Franco-British agreement was drawn and the "Memoire" pointed out that the needs of the war necessitated the signing of the agreement without delay. The Memoire then demanded the consent of the Lebanese Government to the incorporation of the Lebanese-Syrian pound in the franc block.

After studying the Memoire, the Syrian and the Lebanese Government insisted on the transfer of the office des changes to their common ownership and on the independent status of the Lebanese-Syrian currency. The demands of the two governments were of no avail, and under the British and French authorities pressure the two governments signed an accord to the measures that concern them in the Franco-British financial agreement on January 25, 1944. Some promises however were made by the French which were embodied in a letter sent by General Catroux to each of the Presidents of Syria and Lebanon.[1]

## II. The 1948 Franco Lebanese Monetary Agreement

The "Aide Memoire" mentioned above fixed the value of the sterling pound at 200 francs per pound. On December 1945 the French franc was devalued from 200 to 480 francs

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1. The contents of the letter and the promises are given in appendix II.

to the pound sterling and the rate of the Lebanese pound was raised from 22.65 to 54.35 francs. (Table II below shows the successive franc devaluations from 1920 up to September 1949).

TABLE II

SUCCESSIVE FRANC DEVALUATION

"The franc is the monetary unit of the french. It weighs 0.32258 gr. of gold to the title of 900/1000".

1920 to June 1928

F.F. 1 = 0.32258gr. of gold

25th June 1928 F.F. 1 = 0.0635 gr. of gold

1st. October 1936 "elastic" franc

F.F. 1 varying between 0.043 and 0.049 gr. of gold

21st. July 1937 F.F. 1 = 0.043 gr. of gold

12th. November 1938 F.F. 1 = 0.0275 gr. of gold

29th. February 1940 F.F. 1 = 0.02334 gr. of gold

| At the Liberation of France | 26th December 1945 |
|---|---|
| £1 = FF 200 | £1 = FF 480 |
| $1 = FF 49.62 | $1 = FF 119 |
| LL1 = FF 22.65 | LL1 = FF 54.35 |

| 26th January 1948 | 17th October 1948 |
|---|---|
| £1 = FF 864 | £1 = FF 1061 |
| $1 = FF 214 to 313 | $1 = FF 264 |
| LL1 = FF 120.30 | LL1 = FF 120.30 |

| 27th April 1949 | 19th Sept. 1949 |
| --- | --- |
| £1 = FF 1097 | £1 = FF 980 |
| $1 = FF 270 to 330 | $1 = FF 350 |
| LL1 = FF 124.10 | LL1 = FF 159.70 |

Source ??

The French Government however, notified the Lebanese Government that though it was responsible for making good loss in the value of francs in the cover of currency and deposits with the bank of issue due to the devaluation, it will not be responsible for losses that may arise due to further devaluations. The Government of Lebanon insisted that the guarantee of losses should continue to be interpreted in the light of the promises of General Catroux and insisted that the guarantee of future losses should be constant.

On March 15, 1946 the French authorities notified the Lebanese Government that they were unable to continue the free conversion of the Lebanese-Syrian currency into sterling. The real reason for discontinuing free conversion of the Syrian-Lebanese currency into the sterling exchange was the great desire for the conversion on the part of Lebanon and Syria. Such a conversion was doubtless not in the interest of France since the French authorities desired to keep for France the largest possible amount of such exchange.

The insistance of the Government of Syria and Lebanon for a larger appropriations of "hard currencies" for their import trade needs, and their insistence that the French Government was responsible for maintaining at all times the counter-value in sterling of the francs in the cover of the currency and bank deposits, led the French Government to invite them for negotiations to settle this question together. Negotiations were opened in Paris between the delegates of the Syrian and Lebanese Governments and the delegates of the French Government in the first of September 1947. These negotiations continued for about five months. The final project agreement was presented to the Governments of Syria and Lebanon on January 24, 1948 with an ultimatum that refusal to sign the agreement would release the French Government from its obligations towards the country refusing to sign.

The main provisions of the agreement relating to monetary questions are:

1. The French Government promises to maintain for ten years the countervalue in pounds sterling of the francs in currency cover (16 milliard francs) but not of the deposits with the B.S.L.

2. The French Government promises to grant some European currencies in exchange for half of 7 milliard francs (the francs in the cover of bank deposits) during the first two years, and to allow use of the remaining half in purchase of goods from France and its dominions during the first five years.

3. The French Government promised to allow use of

half of the francs in the currency cover in purchase of goods from France and its dominions in the second five years.

4. Agreement to cancel the protocol of April 19, 1944 regulating the exchange control during the first three months of the financial agreement, and to replace it by a new protocol designed to ensure cooperation in financial relations between Syria and Lebanon and France and its dominions.

5. The Syrian and Lebanese Governments respect the concessions to and agreements with the French companies operating in Syria and Lebanon which include the concession to the Banque de Syrie et du Liban.

6. Renewal of the agreement, with or without modifications, at the end of the ten years term, with a full or a partial guarantee of losses from future devaluations of the franc.

The reasons given by the Lebanese Government for accepting the agreement were first that it could not bear the loss that would result on the currency cover from devaluation of the franc on January 24, 1948, and second the Lebanese Government was not willing to devaluate its currency.

A number of objections are raised against the agreement the chief ones that relate to the monetary part of it are;

1. Appendix 4 of the agreement provided for the extension of the 1939 convention with respect to the B.S.L. having the sole right of issuing currency notes redeemable

in francs. The agreement therefore does not ensure the attainmment of an independent currency.

The agreement does not permit monetary independence even after the expiration of the term of the agreement since article 7 refers to similar agreements to be signed at the end of ten years;

2. The agreement contains in article 20 a recognition by the two countries of French Control over the "Office des Changes."

3. The agreement does away with the right of Lebanon to the guarantee of maintaining the countervalue in sterling of the monetary cover in francs in respect of 7 milliard francs that are in the cover of Bank deposits.

4. The amount of European currencies which the French Government promises to give to Lebanon in exchange for francs during the ten years comes only to about half what was appropriated to it in dollars and sterling in 1946. Moreover, the French Government reserves the right to grant this amount in the European currencies it chooses.

The injustice of the above promise becomes apparent when it is remembered that most of the francs in the monetary cover would have been sterling had it not been for the fact that the French authorities used to take the sterling exchange and put francs in the cover of currency and bank deposits.

5. Article 16 of the agreement distinguished between the right of France and that of Lebanon in transfer of funds

resulting from invisible trade. Transfers from Lebanon to France and its dominions may be approved whereas transfers from France and its dominions to Lebanon can be made only subject to conditions laid down by the French Exchange Control. If these restrictions were against Lebanon, Lebanon according to article 16 of the agreement can not retaliate.

6. Appendix 4 of the agreement respects all conventions with and concessions to the French companies in Lebanon which were made or granted during and under the influence of the French Mandate. Of these conventions and concessions are the concessions to the B.S.L. for a period of 25 years beginning April 1939, and the guarantee against losses of all lines of the D.H.P. (Damascus Homs et Prolongements).

Against the above objections two advantages may be cited; First, the French Government provides a reimbursement of the loss on franc in the currency cover though not also on the francs in the cover of Bank deposits resulting from the last devaluation of the franc. Second, the agreement settles all financial questions resulting from the liquidation of the Mandate which have been left outstanding.

As stated above the Lebanese Government based its decision to sign the agreement on the evidence of a loss (estimated at 70 million Lebanese pounds) which it might have to sustain if it refused to sign.

## III. The 1949 Monetary Law

Following the Monetary agreement with France, Lebanon promulgated a law on May 24, 1949 regulating note issue and the composition of note cover. The main provisions of this law are first that the monetary unit is the Lebanese pound divided into 100 piasters issued by the institute of issue the B.S.L. Another provision provided that notes in circulation are to be covered in full; 50 percent in gold and foreign exchange and 50 percent in Government loans and securities, securities of institutions accepted by the state and commercial bills.

The exact proportion of each element in the note cover according to these percentages is to be determined by a council of ministers. Thus Decree No. K/15/05 of May 1949 stipulated that:

1. Gold and foreign exchange reserves are to be recorded at the official price of the Lebanese pound as accepted by the International Monetary Fund (405.512 mgms. of pure gold to the Lebanese pound). If gold or foreign exchange are bought or sold below the official price, the change in the total value becomes obligatory deposit when positive. If the change is negative it is compensated by a Government guarantee for the debting balance.

Gold reserves should amount to 10 percent of note circulation by the end of 1950, 20 percent by the end of 1951 and 30 percent by the end of 1952. These proportions though not obligatory in case the monetary conditions of the country proves that their fulfillment is difficult. The proportion of the foreign exchange in the reserve of notes cover will be determined jointly by representatives of the Government and the B.S.L., the latter in its capacity as the manager of the "Office des Changes". These reserves should include the guaranteed francs of the cover of the Lebanese pound and other foreign exchange and government bonds. Profits from Government bonds and I.B.R.D. (International Bank of Reconstruction and Development) securities transactions are part of note cover losses will be supported by the B.S.L.

2. The other half of the note cover may be composed of a) Government bonds and advances guaranteed by the Government and b) Commercial bills not exceeding 15 percent of note circulation maturing within 90 days and bearing three signatures.

To such a country as small as Lebanon a 50 percent proportion of gold in the note cover is not a high ratio. The 1949 monetary law however sets up a minimum which may be exceeded. Thus the actual gold ratio in the cover was increased to 95 percent by 1955 (see table III below). Yet no matter how high the ratio is to a country like Lebanon which depends basically on its foreign trade, stability of the currency counts more than gold ratio in the note cover.

The monetary law also provides for the maintenance of the official parity rate of the Lebanese pound at 405.512 mgms. of pure gold for the Lebanese pound. This parity is over valued and accordingly the official rate of the dollar as declared by the International Monetary Fund is (LL 2.19 for the dollar) is insignificant. The law also provides that gold coins may be issued by the Treasury. Should such an issue be made at the official rate of the Lebanese pound there would be a rush to buy these coins since their market value would be much higher. This provision however has a political significance more than a monetary one since the right to issue gold coins is considered a symbol of Sovereignty and so such an issue of gold coins is not likely to be made.

Another limitation of monetary significance to the law is that it limits the amount of trade bills in the note reserve to 15 percent only. Such a limitation may be a handicap when an increase in the supply of money is desired to combat a temporary recession.

## IV. Composition of the Note Cover

The above section discussed the legal provisions for the note cover in accordance with the 1949 monetary agreement. Table III below shows the actual composition of note cover as of the end of the year. From this table the analysis of the changes are:

TABLE III

COMPOSITION OF THE NOTE COVER
(in LL 000,000)

| End of | Gold | % | Foreign Exchange | % | Total | % Govert. oblige | Note cir |
|---|---|---|---|---|---|---|---|
| 1948 | 5 | 2 | 123 | 67 | 129 | 31 | 185 |
| 1949 | 42 | 25 | 38 | 23 | 81 | 52 | 168 |
| 1950 | 70 | 36 | 26 | 14 | 98 | 50 | 196 |
| 1951 | 93 | 45 | 13 | 6 | 105 | 49 | 208 |
| 1952 | 109 | 55 | - | - | 109 | 45 | 200 |
| 1953 | 127 | 62 | 6 | 3 | 133 | 35 | 205 |
| 1954 | 219 | 90 | - | - | 219 | 10 | 242 |
| 1955 | 253 | 95 | - | - | 253 | 5 | 266 |
| 1956 | 264 | 79 | - | - | 264 | 21 | 333 |
| 1957 | 309 | 87 | - | - | 309 | 13 | 356 |
| 1958 | | | | | | | |
| Jan. | 309 | 87 | - | - | 309 | 13 | 356 |
| Feb. | 309 | 87 | - | - | 309 | 13 | 356 |
| March | 309 | 87 | - | - | 309 | 13 | 356 |
| Apr. | 309 | 86 | - | - | 309 | 14 | 357 |
| May | 309 | 81 | - | - | 309 | 19 | 379 |
| June | 309 | 75 | - | - | 309 | 24 | 407 |
| July | 309 | 73 | - | - | 309 | 27 | 424 |

Source: Bulletin Statistique Trimestriel

Figures for 1958 onwards privately secured from Ministry of National Economy.

1. At the present gold constitutes the largest item in the cover. It has been continuously increasing both absolutely and relatively since 1948. In 1948 it constituted only 2 percent of the cover by 1955 the proportion rose to 95 percent. The figures for 1956 are exceptional owing to the effect of the Suez crisis that took place late in November of that year. Because of the crisis, notes in circulation were increased from LL 282 millions at the end of June 1956 to LL 333 millions at the end of December the same year thus decreasing the gold reserve ratio to 79 percent. This ratio however began to be adjusted soon after the crisis was over. As shown by the figures for 1957 gold reserves increased to LL 309 millions making gold 87 percent of the cover though notes in circulation increased by LL 23 millions. In April 1958, at the beginning of the present (June 1958) political crisis notes in circulation increased by LL 67 millions within three months, that is up to June 1958. This increase was covered only partly by an increase in the Government obligation in the cover thus decreasing the gold reserve from 67 to 73 percent i.e. a decrease of 6 percent in three months.

The value of the gold is given at cost price and not at market price. The difference between the two is debited to a compensatory account. The value of the gold at the official price of the Lebanese pound of 405.512 mgms. of pure gold was LL. 162,175,200 at the end of December 31, 1955.[1]

2. While gold has steadily increased, foreign exchange in the cover has decreased. The amount of foreign exchange in the cover decreased from 123 millions at the end of 1948 to nil by 1952. Percentage wise it dropped, from a 97 percent high in January 1948 to zero in December 1952 and continued to be so up to the present.

3. Government obligations constitute the remainder of the assets in the note cover reserves. Government obligations reached a maximum of LL. 105.5 millions in 1950 (50 percent of all the assets in the cover.) The increase in Government obligations in the note cover is usually the result of a shifting of these assets from B.S.L. Banking Department to the issue Department.[1] This kind of transfer is likely to happen when the banking department of the B.S.L. is in need of money. A good example of this feature is expressed by the 1956 figures in the above table. In October 1956 the Suez crisis took place and the banking system as a whole faced a rush on cash by the customers. In order to help the banks the Government increased the notes in circulation from 266 to 338 millions. The gold reserves in the note cover thus decreased relatively from 95 percent

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1. Mikdashi Z., <u>The Monetary System of Lebanon: 1955</u> AUB 1956, M.A. Thesis.

in 1955 to 79 percent in 1956. This decrease in the note cover was balanced by an increase in the Government obligations from 5 percent at the end of 1955 to 21 percent at the end of 1956. These obligations consisted mainly of obligations to the B.S.L. The shift of the B.S.L.'s assets was responsible for the increase in the note circulation from LL. 266 millions to LL. 333 millions.

The Government obligations in the note cover consists of three main elements: "differences in the exchange rates covered by the state, advances for the exchange of Syrian notes and advances to the State or guaranteed by the State. The first item represents the Treasury bonds which were issued to make up for the loss in the franc note cover owing to the sterling devaluation of September 1949.[1] The second item appeared early in 1948 and was liquidated in October 1954. The other elements did not constitute at any time an important portion of the note cover. They consisted of a small interest free advance to the state (LL.250.000),[2] loans to municipalities, to industries and to S.C.A.I.L. Guaranteed by the Government. At the end of 1955, Treasury bonds in the note cover were LL. 12,924,000, while the other government obligations were insignificant (a LL. 250.000 advance to the state and a LL. 3.024 loan guaranteed by the Government)".[3]

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1. Decree No. K/15/05 Article 4.
2. B.S.L. convention of May 29th 1937 Art. 9.
3. Mikdashi, op.cit., p. 36-37.

# CHAPTER II

## DEVELOPMENT OF THE BANKING SYSTEM

The purpose of this chapter is to introduce the banking system of Lebanon and to trace its development up to the present time. This chapter therefore will be more concerned with tracing the historical development of commercial banking institutions than with the analysis of the causes of such development. Such analysis will be the subject matter of the next chapter on "Principal features of the commercial banking system."

The history of the development of the Lebanese banking system is traced through three periods. First the period of the Ottoman rule and up to the end of World War I, second is the period of the French Mandatory regime, and third is the present period which began with the independence of Lebanon.

### I. The Banking System Up to and During World War I

Before the beginning of the 19th Century there were practically no banking institutions in Lebanon. Whatever credit activities, loans and discounts made, were carried out by money lenders. Moreover during the fifteen years before World War I, Lebanon witnessed a marked increase in the number and operations of banking institutions. Not only native banks increased but foreign banks established branches in the main cities and centers of the area.

Foreign banks were branches of well known banking institutions that had the advantage over local banks of having wider connections abroad. Because of this advantage foreign banks were able to take over the larger part of the volume of banking business. They were also supported by their own Governments, which, motivated by political motives for a share in the estate of the "Sick Man", gave them every support to promote their country's trade. The interest of the area was only of incidental consideration.[1] "However, not with-standing the absence of concern for the country's welfare, these banks helped much in financing trade in general and foreign trade in particular."[2] The most important foreign banking companies operating in the Lebanon then were;[3] the Imperial Ottoman bank, Banque de Salonique, the Deutsche Palestine bank, and the Deutsche Orient bank.

Beside these foreign institutions, many private smaller banks and discount homes with local capital operated in the large towns especially Beirut. They did a considerable

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1. Himadeh, op.cit., p. 30
2. Ibid., p. 30
3. Ibid., p. 29-30.

amount of lending and discounting, received time and demand deposits, and carried out some minor exchange business. But very few of them had foreign connections and therefore their business was mostly confined to financing domestic trade. In general, banking business up to World War I was inadequate in relation to the needs of the country. The banks took a very small part in financing industrial undertakings and were extremely conservative in extending credit to merchants. Sale of bonds and securities was an insignificant part of the banks operations because of the prejudice against corporate securities in general and because other forms of investments such as real estate property and mortgage on lands and buildings yielded higher incomes and/or was more in line with the mentality and habits of individual investors.

The effect of the war upon banking was considerable. Institutions belonging to enemy countries and many local banks, fearing confiscation of their assets, endeavored to transfer the greater part of their resources to neutral countries. This was possible because the "Central Exchange Bureau" was not created until August 1917. Banking activities were reduced to minimum as the war and its measures interfered with all sorts of business. Foreign trade slackened greatly on account of the almost complete stoppage of sea transportation and the many exchange restrictions, and internal trade suffered because of many difficulties of land transport and taxation by requisition, which did not stop at articles of military need, but included all kinds of commercial goods. In order to meet the necessities of war, a number of moratoria were declared in order to ensure a safe transition from pre-war to war conditions. Because of the provisions of some of these moratoria the banks were chiefly concerned with liquidating their debts and credits. The extension of credit was considerably limited because of the risks, complications and uncertainties of the abnormal state of war.

"The most important banking transactions, during the war, were those carried on with the Central Powers. These transactions were handled by German and Austrian banks. Their favorable position enabled them to transact all types of business including those forbidden by law. Their main operations however were in financing trade between Turkey on the one hand and its allies and neutral countries on the other. Among the prohibited transactions were the export of gold and the import of foreign money, securities, etc., which were then in demand.[1]

## II. Banking System During the French Mandate

During the French Mandatory Regime commercial banking developed rapidly. The main foreign bank established

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1. Ibid. p. 41 - 42.

during this period was the Banque de Syrie et du Liban. The B.S.L. was established in 1919 with a capital of Fr. Fr. 10 millions and with branches in Beirut and Tripoli. It is a private French corporation which took over in 1919 from the Ottoman bank all its agences and privileges in Syria and Lebanon. It paid for the assets thus acquired in its own shares thus becoming affiliated to the Ottoman Bank.[1] According to the concession, as approved by the French Minister of Foreign Affairs in April 1919, the right of issue was conferred on the B.S.L. This privilege was again confirmed by the 1937 convention which gave the B.S.L. a larger control over the monetary system of Lebanon. As already mentioned in the previous chapter, the Franco-Lebanese Monetary agreement of 1948 stipulated that the Lebanese Government should respect the concessions it granted to French companies among which was the concession granted to the B.S.L.[2]

Besides the B.S.L., other foreign banks were established in Lebanon during the mandate period and these were: The Credit Foncier d'Algerie et de Tunisie, founded in 1880, which established a branch in Beirut in 1921 and another in Tripoli in 1931. The Compagnie Algerienne which established a branch in Beirut in 1931 and another

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1. *Ibid.* p. 137

2. These monetary agreements were mentioned earlier in chapter I and in appendix I.

in Tripoli in 1932. Banco di Rome which established a branch in Beirut in 1919 and another in Tripoli.

Not only did foreign banks increase in Lebanon during this period, but new local banks were also established. Of these local banks Banque Misr-Syrie-Liban (partly Egyptian capital) was established in 1929. Banque Georges Trad and Co., Banque Alexander P. Haddad, Far'oun and Shihab, and Banque Robert Sabbagh and Co.

Since World War I there has been a marked development in commercial banking. Both foreign and native institutions have multiplied rapidly. Foreign banks, whose operations were more or less limited to foreign trade finance, have increasingly undertaken to finance domestic trade.[1] But there was still need for development and advancement in the extent and quality of their banking service. As to native commercial banks, their operations were also not well developed. They generally had a small capital. According to estimates by Professor S.B. Himadeh up to 1935 not more than six banks had a capital over 50,000 Turkish pounds. "Consequently, most of them have become dependent upon a comparatively few business houses; at the same time they were unable to afford skilled management."[2] In many cases a large part of the capital of these

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1. *Ibid.*, p. 127

2. *Ibid.*, p. 175.

banks was tied up in land and building holdings. This practice was resorted to because these banks did not publish financial statements and the public used to judge their strength on the basis of the tangible assets they possessed. "So in order to win the public confidence, it has become a common practice with the native banker to own real estate.

"Such a practice is of course, contrary to conventional commercial banking theory and practice. The banks' capital is an insurance fund against unforeseen losses which are usually severe at times of business crisis. At such a time real estate depreciates considerably, and losses might be so great as to leave the equity buffer at an inadequate figure. The proceeds of the real estate might not be sufficient to cover the losses from the banking business and the banker would be driven to bankruptcy. The liabilities of the bank, being of a fixed money value, should have, as far as possible, the corresponding asset as well as the insurance fund in fixed money value. A part of the capital might be invested in premises, when these are necessary, but the part should be so small as to leave a sufficient insurance fund free from the risk of heavy depreciation."[1]

Another characteristic of the local banks of that period was the unit banking system. Only one bank possessed

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1. Ibid., p. 176.

branches, namely Banque Misr-Syrie-Liban which is only partly financed by native capital. The unit system has the following drawbacks: (a) The limitation of resources; (b) inevitable dependence upon a few business undertakings and (c) the difficulty of securing skilled management. (d) Unit banking also hinders the mobility of capital to those parts of the country when it is most needed. Such a mobility however is afforded by the foreign banks that do have branches in the main towns of the country.

## III. The Present Banking System

The modern banking system of Lebanon assumed its present importance after independence. The independence of Lebanon was proclaimed by the French Authorities in 1941 and confirmed in October 7, 1943. The last French soldier left the country in December 31, 1946. Table IV shows that of the 33 operating commercial banks in Lebanon, both foreign and native, 27 banks were established after independence. Of the remaining 6 banks that existed during the French mandatory regime five are foreign and of those four are French.

The ministry of Finance distinguishes between three types of commercial banking institutions. Accredited banks, non-accredited banks and Banquiers or discount homes. Part II of Table IV shows that all foreign banks are accredited banks. They are branches of foreign banks that are established outside Lebanon. Appendix III shows a detailed description of accredited local banks. Many of these banks however have either foreign interest in them or are affiliates of foreign banks.

TABLE IV

BANKS OPERATING IN LEBANON

(December 31, 1957)

I. Accredited Commercial Banks

| Name | Nation-ality | Estab-lished (Date) | Authorized Cap. in LL Mill. |
|---|---|---|---|
| A. LOCAL BANKS | | | |
| 1. Banque Misr-Liban | Lebanese | 4.6.1929 | 3 |
| 2. Banque Tohmé | " | 28.10.1942 | 1 |
| 3. Eastern Commercial Bank | " | 21. 3.1955 | 1 |
| 4. Societe Bancaire du Liban (Zelkha) | " | 4. 9.1946 | 1 |
| 5. Banque Libanaise pour le Commerce | " | 10.11.1949 | 5 |
| 6. Banque Sabbagh (Banque d'Indochine) | " | 20. 6.1950 | 2 |
| 7. Banque G. Trad (Credit Lyonnais) | " | 10. 3.1951 | 1 |
| 8. Banque du Liban et d'outr Mer | " | 8. 5.1951 | 5 |
| 9. Federal Bank of Lebanon | " | 25.10.1951 | 7 |
| 10. Intra Bank | " | 17.11.1951 | 12 |
| 11. Bank Saradar | " | 20. 7.1956 | 1 |
| 12. Banque Al-Ahli | " | 7.11.1952 | 10 |
| 13. Banque Belgo Libanaise | " | 13. 8.1953 | 5 |
| 14. Banque de Beyrouth des Pays Arabes | " | 14.3.1956 | 2 |
| B. FOREIGN BANKS | | | |
| 15. Banque de Syrie et du Liban | French | 2. 1.1919 | FF300 |
| 16. Credit Foncier d'Algerie et de Tunisie | " | 1921 | FF765 |
| 17. Banque Nationale pour le Commerce et l'Industrie | " | 1. 6.1927 | FF500 |

| Name | Nationality | Established (Date) | Authorized Cap. in LL. Mill. |
|---|---|---|---|
| 18. Compagnie Algerienne | French | 15. 1.1931 | FF 1,500 |
| 19. Banco di Roma | Italian | 12. 3.1936 | IL 1,000 |
| 20. Arab Bank | Jordanian | 31. 1.1944 | JD 3,5 |
| 21. The British Bank of the Middle East | British | 15.10.1946 | Ь 1 |
| 22. Rafidain Bank | Iraqi | 1. 6.1948 | ID 1 |
| 23. The Saudi National Commercial Bank | Saudi Arabian | 6.1952 | LL 1 |
| 24. Banque du Caire | Egyptian | 9.1953 | LE 0.5 |
| 25. Nederlandsche Handel Maa ttachappij | Deutch | 15. 6.1954 | DF 75,03 |
| 26. The Chase Manhattan Bank | USA | 8.1955 | $ 150 |
| 27. First National City Bank of N.Y. | " | 10.1955 | $ 200 |
| 28. Bank of America | " | | |
| 29. The Eastern Bank Ltd. | British | 30. 4.1956 | Ь 7 |

II. NON ACCREDITED COMMERCIAL BANKS

| | | | |
|---|---|---|---|
| 30. Banque Albert Homsy | Syrian | 1895 | LS 2 |
| 31. Beirut Bank | Lebanese | 9.11.1936 | LL 6.5 |
| 32. Banque Chartouni | " | 1.1951 | LL 2 |
| 33. Commercial Bank | " | 18. 3.1954 | LL .200 |

III. NON-COMMERCIAL BANKS

| | | | |
|---|---|---|---|
| 34. Compagnie Mediteraneenne de geston et de Placement | French | 17. 5.1919 | FF 6 |
| 35. Monts de Piete Egyptienne | " | 23. 2.1934 | FF 6.4 |
| 36. S.CA.I.L. | Lebanese | 6. 3.1939 | LL 1 |
| 37. B.C.A.I.F. | " | 23.10.1954 | LL 5 |
| 38. Bank Beirut Al Riyad | " | 12. 3.1958 | LL 25 |

Of the 37 operating banks listed in table IV, 33 are commercial and 4 are non-commercial banks. As shown by the same table, the aggregate capital of commercial banks is by far greater than that of non-commercial banks. The predominance of commercial banking in both number and the total capital employed clearly proves that commercial credit is the main form of credit available in Lebanon. The type of operations of commercial banks will be discussed in chapter IV.

## CHAPTER III

## PRINCIPAL FEATURES OF THE COMMERCIAL BANKING SYSTEM

In the preceding chapter a general description of the history of the commercial banking system and its development was given. From this description it is evident that the system is predominantly a commercial banking system and that it is a newly developed one. Though the system is a new one and its history does not go back to more than a decade, there are certain features that have evidently expressed themselves. These features though subject to change in the future are the basis upon which future development will be built.

It is the purpose of this chapter to point out these features as they appear in the commercial banking system of Lebanon, and to discuss them critically and compare them, whenever possible, with those of other more advanced system. A summary of those features follows.

### I. Absence of Commercial Banking Legislation and Government Control.

One of the main features of the banking system in Lebanon is the complete absence of commercial banking law or any Governmental supervision of the banks' operations, both foreign and local.

Any group of individuals may establish a bank as a corporation, a partnership or an individual proprioter-ship subject to no other regulation than those of ordinary commercial law with no special requirements as to manage-ment, operations, loan commitments, reserves, investments or annual reports, etc. This absence of legislation has to a large extent encouraged foreign banks to establish branches in Lebanon since this gives them greater liberties in their operations than is available to them in any of the neighbouring Middle Eastern countries.

To increase the freedom and flow of funds in the banking system the Government issued in September 1956 a bank secrecy law.[1] According to this law all banks accounts are made secret even to any Government agency. In its essence this law is an imitation of that of Switzerland. The effect of this law on the operations and deposits of the banking system will be discussed in more detail in the next chapter.

## II. The Rapid Expansion of Commercial Banking

We have seen in the previous chapter that since independence the number of commercial banking institutions has increased considerably. Together with this increase in the number of banking institutions there was a parallel

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1. The text of this law is given in appendix II.

increase in the volume of business of these banks. This increase in the volume of business is due to the following reasons;

1. <u>The Increased Habit in the Use of Cheques</u>

During the Turkish and French regimes the use of the cheque as means of payment, and the acceptance of bank deposits as cash, was very limited. This limitation was partly due to the distrust on the part of the public in banks in general because of the failure of some of them, and partly because the public did not desire to hold bank deposits due to the instability of the value of the currency. As we have seen in the earlier two chapters, the currency during both the Turkish and French regimes has undergone many devaluations.[1] These devaluations have made the public lose its confidence in the currency and resort to hoarding rather than hold bank deposits.

Since independence, Lebanon started to experience stability in the value of its currency. At present, and even during the crisis that the country experienced in the summer of 1958, the value of the Lebanese currency enjoyed considerable stability. This stability in the value of currency which was built up since independence have regained the confidence of the public in the currency and induced it to accept bank deposits as money. Thus the cheque as means

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1. See table II.

of payment is becoming predominant. Businessmen have taken to the habit of depositing their cash daily at banks after the close of the working day. Not only businessmen are using the cheque as a means of payment but people in general are doing that as well. Instead of hoarding their liquid assets, people started to make use of the benefit in the form of interest paid them by banks for their deposits.

2. Economic Development of the Country

Since independence there has been a marked increase in economic activities in Lebanon. This increase is expressed by an increase in the national income of the country derived from the various economic sectors. Table V shows the contribution of each of the economic sectors to national

TABLE V

NATIONAL INCOME FROM SECTORS

(in LL Millions)

| Sector | 1948 | 1949 | 1950 | 1951 | 1952 | 1953 | 1954 |
|---|---|---|---|---|---|---|---|
| Trade | 261 | 278 | 300 | 337 | 333 | 344 | 350 |
| Agriculture | 169 | 159 | 206 | 211 | 216 | 221 | 226 |
| Industry | 134 | 136 | 137 | 135 | 137 | 139 | 141 |
| Service | 91 | 93 | 101 | 103 | 106 | 109 | 113 |
| Real Estate | 91 | 93 | 96 | 97 | 98 | 101 | 104 |
| Government | 63 | 65 | 72 | 64 | 64 | 71 | 73 |
| Transport | 40 | 41 | 44 | 46 | 50 | 62 | 63 |
| Finance & Ins. | 35 | 35 | 40 | 43 | 46 | 50 | 56 |
| Construction | 35 | 32 | 42 | 35 | 40 | 40 | 41 |
| TOTAL | 919 | 932 | 1038 | 1071 | 1090 | 1137 | 1167 |

Source: Badre A., National Income of Lebanon. Monographs 1 to 7, Beirut, July 1954.

income over a period of 7 years from 1948 to 1954. Trade, Agriculture, Industry and the Service Sectors account for the main part of the national income, the share of each of these sectors in total national income as shown by table V has been increasing over the 7 years' period. In general the growth in the sectors mentioned is due not only to internal economic development, but is to a certain extent also due to the prosperity of the oil producing neighbouring countries.

Situated in a junction point between Europe and the countries of Asia and the Middle East, Lebanon has been a commercial bridge between the two continents, since early history. Trade has been the main occupation of the people of Lebanon especially those who inhabited the large towns on the coast. Besides its geographic position, the country is gifted with a good climate and with beautiful mountains which make it an attractive summer resort to many people of the neighbouring countries. These natural resources have increased in importance over the past few years, when the oil deposits of the neighbouring countries were discovered. Not only did some of the people of these newly enriched countries find Lebanon a beautiful country to resort to during the uncomfortable seasons of the year in their own countries, but they also found it the most suitable port for the export of their products including crude oil. The port of Beirut with its modern facilities was also the port of import for the neighbouring countries.

With tourism and trade, the prosperity of these oil producing countries, found its way into Lebanon. But besides tourism and trade Lebanon benefited from the prosperity of its neighbouring countries in the form of capital deposited in its banks and in the form of purchase of real estate. The purchase of real estate with capital from outside is to some extent made by Lebanese emigrants to oil prosperous or other foreign countries. These emigrants having made some savings return to their home country and invest their savings in real estate.

The prosperity of the neighbouring oil rich countries have thus influenced the growth in the trade, service, industry, real estate, transport, construction, and finance and insurance sectors. The growth in these sectors, whether due to internal development or to the recent increased expenditures of oil prosperous neighbouring countries, had certainly increased the volume of business of the banking system since independence.

### 3. Absence of Restrictions

To a large extent both economic development and the increased expenditures of neighbouring oil prosperous countries are due to the absence of Government restrictions in Lebanon. Trade, especially transit trade, is considerably encouraged by the fact that Lebanon is a free exchange country. The absence of Government control of exchange encourages the flow of capital and in turn encourages trade.

TABLE VI

FOREIGN TRADES OF LEBANON

in LL MILLIONS

| Year | Transit | Re-export | Export | Import |
|---|---|---|---|---|
| 1952 | 1,038 | 19.3 | 77.5 | 250.7 |
| 1953 | 1,063 | 12.2 | 87.5 | 361.5 |
| 1954 | 1,034 | 13.8 | 105.6 | 484.1 |
| 1955 | 1,191 | 16.2 | 120.5 | 526.9 |

Source: Bulletin Statistique Trimestriel

Table VI shows the increase in foreign trade movement. During the period between 1952 to 1955 imports have increased by 110 percent, exports by 55 percent and transit trade (including oil) by 15 percent. Such an increase brings with it of course an increase in the volume of business of commercial banks.

4. Political Stability

To a depositor security and stability, especially political stability, are the two main criteria by which he judges whether or not to deposit his funds in the banks of any country. To a certain extent Lebanon has provided such security. The Lebanese Government has followed a stable political policy that made the country politically the most stable in the Arab Middle East.

This stability encouraged the inflow of foreign capital to the country and made Beirut a money market that benefited whenever, due to political instabilities of the neighbouring Arab states, foreign capital flew out of them. Such a flow was evident after the Suez crisis of 1956. Due to the political situation, foreign enterprises left Syria and Egypt and established their headquarters in Beirut, From Beirut these enterprises supervised their branches all over the Middle East. But the recent (summer 1958) crisis has certainly weakened confidence in this political stability. The extent of the effect of this crisis on future development of the banking system is difficult to assess at the present owing to many uncertainties the most important of which is the political settlement of the crisis.

In order to increase the confidence of foreign concerns the Government passed in September 1956 the bank secrecy law. This law aimed at attracting foreign deposits into the Lebanese banking system. How far this aim was accomplished will be discussed below.

The aforementioned factors have helped to increase bank deposits and advances and to facilitate trade transactions, thereby increasing the volume of business for commercial banks. Such an increase in the volume of business is reflected in the volume of deposits and advances as shown by table VII.

TABLE VII

BANKS DEPOSITS AND ADVANCES

(in LL. Millions)

| End of | Fixed Dep. | Demand Dep. | Total | Adv. & Disc. |
|---|---|---|---|---|
| 1939 | 0.9 | 26.5 | 27.5 | 9.6 |
| 1940 | 0.8 | 39.7 | 40.4 | 8.1 |
| 1941 | 0.7 | 30.3 | 31.0 | 12.1 |
| 1942 | 1.6 | 85.7 | 87.0 | 15.1 |
| 1943 | 1.5 | 164.9 | 166.4 | 17.8 |
| 1944 | 1.6 | 178.4 | 179.9 | 31.1 |
| 1945 | 1.3 | 225.8 | 227.1 | 69.8 |
| 1946 | 0.9 | 208.8 | 209.7 | 67.4 |
| 1947 | 1.5 | 205.4 | 208.9 | 106.4 |
| 1948 | 4.5 | 194.3 | 198.8 | 223.0 |
| 1949 | 4.8 | 175.8 | 180.6 | 272.3 |
| 1950 | 5.3 | 209.7 | 215.2 | 280.2 |
| 1951 | 6.2 | 253.1 | 259.3 | 318.3 |
| 1952 | 11.8 | 301.5 | 313.2 | 336.1 |
| 1953 | 19.1 | 324.4 | 343.4 | 337.1 |
| 1954 | 26.7 | 362.1 | 388.7 | 401.9 |
| 1955 | 39.3 | 443.9 | 483.3 | 494.6 |
| 1956 | 42.4 | 440.3 | 482.6 | 564.0 |
| 1957 | 50.4 | 551.1 | 601.5 | 636.7 |
| 1958 | | | | |
| Jan. | 53.5 | 560.1 | 613.6 | 637.8 |
| Feb. | 56.9 | 591.7 | 648.6 | 657.6 |
| Mar. | 55.1 | 605.1 | 660.2 | 659.1 |
| Apr. | 56.8 | 591.9 | 648.8 | 669.6 |
| May | 60.5 | 537.7 | 598.1 | 667.7 |
| June | 56.7 | 501.7 | 558.4 | 713.7 |

Source: Bulletin Statistique Trimestriel
Privately secured from Statistics Department, Ministry of National Economy, Beirut.

Table VII shows that within a period of 19 years, from the end of 1939 to end of March 1958, total deposits have increased 24 and a half times i.e. from LL 27 millions to LL. 660 millions. Advances on the other hand have increased by about 71 times during the same period. This increase in the volume of deposits and advances as shown by the same table has been constant. With the exception of the two years 1948 and 1949, total deposits have been constantly increasing. After 1949 the volume of deposits continued its previous rising trend at an increasing rate. This increase was again haulted in 1956 when the Suez crisis took place. But it is interesting to note that the direct effect of the Suez crisis did not decrease total deposits below the volume of the previous year i.e. 1955. Though the crisis took place in October 1956, at the end of December of the same year, deposits were still about the same as those of 1955. The year 1957, however, registered a marked increase in the volume of deposits. Total deposits increased up to LL. 601 millions i.e. an increase of LL. 119 millions within a period of one year. This increase may be explained as being the effect of two favourable causes. These were the passing of the bank secrecy law in October 1956, and the inflow of capital from the outside into Lebanon, especially from Syria and Egypt following the Suez crisis. What effect did each of these factors have on this increase is difficult to assess but it is noted that the trend is a rising one in the first place and therefore may be not much is due to either.

Again the increasing trend in the volume of deposits was hindered in April 1958 after reaching a maximum of LL. 660 millions in the previous month. This fall continued until June 1958 when deposits reached LL. 558 millions i.e. a decrease of LL. 102 millions within three months. This fall is due to the present (summer 1958) political crisis. At the present (Sept. 1958) the crisis is being solved but the effect of its solution on the volume of deposits remains to be seen.

The relation between advances and discounts on the one hand and total deposits on the other as shown by table VII above is a close one. It was not possible to find out from data available what part of total deposits is primary and what part is derivative deposits. As will be shown later in chapter IV, banks in Lebanon discount commercial papers and either credit the proceeds to the accounts of their customers or pay there proceeds in cash on discounting such papers. How much is deposited thus forming derivative deposits and how much is paid in cash is also a ratio that is not possible to obtain. However a personal estimate based on experience yet may not be very representative and mentioned only with reservation is that such derivative deposits may amount to about 10 to 15 percent of total advances and discounts. On the basis of this estimate the volume of primary deposits will be less than the figures given in table VII above, let alone interbank deposits and other derivative deposits.

At this point it is important to note (as will be shown in chapter IV below) that Lebanese banks in general do not distinguish between time or fixed deposits and demand deposits. This is because time and fixed deposits are handled as demand deposits by these banks. Because of this relaxation in the treatment of these two types of deposits whenever deposits are referred to in this work they are taken to mean the total of both. Thus it is total deposits that are taken for comparison with money supply in table VIII below and not demand deposits alone as the case should be.

TABLE VIII

DEPOSITS AND VOLUME OF MONEY SUPPLY IN LEBANON

| End of | Total Dep. | Notes in Ciro. | Total Money Supply | % Dep. of total money Supply |
|---|---|---|---|---|
| 1948 | 199 | 185 | 384 | 52 |
| 1949 | 181 | 165 | 349 | 52 |
| 1950 | 215 | 196 | 411 | 52 |
| 1951 | 259 | 208 | 467 | 56 |
| 1952 | 313 | 200 | 513 | 61 |
| 1953 | 343 | 205 | 548 | 63 |
| 1954 | 389 | 242 | 631 | 61 |
| 1955 | 483 | 266 | 749 | 64 |
| 1956 | 463 | 333 | 796 | 58 |
| 1957 | 602 | 356 | 958 | 62 |
| 1958 | | | | |
| Jan. | 614 | 356 | 970 | 63 |
| Feb. | 649 | 356 | 1005 | 65 |

| | | | | |
|---|---|---|---|---|
| March | 660 | 356 | 1016 | 65 |
| April | 649 | 379 | 1028 | 62 |
| May | 598 | 407 | 1005 | 60 |
| June | 588 | 424 | 1012 | 58 |

Source: Derived from table III and table VII

As shown by the above table total deposits in comparison to total money supply have increased from a minimum of 52% in 1948-50 to a maximum of 65% in February and March 1958. This ratio varied, as shown by the above table, due to the effects of political events that took place during the period. These events had their effects on both the volume of deposits and the volume of currency in circulation.[1] However, an important limitation to the significance of these ratios is the velocity of circulation of both deposits and currency in circulation. In the US the ratio between deposits and currency has varied from 77% to 87% during the period between 1900 and 1930, and from 87% back to 77% between 1930-1950.[2] The velocity of circulation of currency has ranged from 13 to 20 times during the period from 1940-1949 which it ranged from 25-29 times in the 1920's and 1930's.[3]

## III. Predominance of Foreign Banks

Of the 33 commercial banks operating in Lebanon

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1. See table III & VII.
2. Woodworth G.W., The Monetary & Banking System, McGraw Hill Co. 1950, p.192.
3. Ibid., p. 194.

as listed in table IV of chapter II, 16 are of foreign nationality. These are branches of large banking institutions of foreign origin. In general the purpose of these branches is to facilitate trade between Lebanon and the countries they represent, and, by making use of the free exchange facilities in Lebanon, they help their home offices clear their transactions through them.

At the end of the mandatory regime there were only five foreign banks operating in Lebanon of which four were French and the fifth Italian. The increase in the number of foreign banking institutions is due to the increased interest of foreign countries in this part of the world. A good example is the recent increase in the number of US bank over the last three years. The advantages foreign banks have over local banks may be summerized as follows;

1. Foreign banks can always depend upon their head offices to supply them with liquid cash through any of its near branches. This is of special importance in times of crisis when extra cash is needed to meet the public's rush for cash. With this assurance of ready cash at any time these foreign banks can afford to maintain minimum cash balance and so invest their resources with more liberty than local banks do. Local banks on the other hand should always be ready to supply themselves with their needs for cash on their own at any time without resort to any outside means of help.

2. Close to the above advantage is that of geographic diversification. By diversification in this connection is meant the establishment of a branch banking system. If we consider for example the Bank of America which has branches practically all over the world, no matter in how many countries trade cycles are at their descending phase, there will still be other countries not hit by the crisis and in which the bank has branches. Should the crisis be one that has the characteristic of being exported, by the time its effect on the importing country is felt it might be about over in the exporting country. Thus the branches of the same bank will be able to cooperate and distribute their funds not only to benefit themselves but also to help the country as well, not with standing the fact that some of the branches will bear the serious effects in the country in which the crisis occurs.

3. Being branches of foreign banks well known all-over the world for their long experience in the banking business gives foreign banks a competitive advantage over local banks for attracting deposits. In general a depositor prefers to deposit his savings in a bank that is safe. To him safety means more than profitability. Thus depending on the name of their head offices they attract deposits more. An exhibit of their head office balance sheet with figures beyond the ordinary use of the common people in Lebanon is in itself a goodwill that is already existing

and need not be built up as is the case with local banks.

4. A last advantage foreign banks have over local ones is that they can always employ well trained and experienced management which is characterized by not being itself the owner of the bank as is the general case with most of the local banks. In other words management of foreign banks is there because it is best suited to be there and not because it owns the bank. Foreign banks can afford to employ such efficient management because it can attract it by payment of good salaries. The employment of such specialized, well trained, and experienced management is lacking in most of the local banks. This advantage however is usually the result of bigness rather than the fact that the bank is foreign. It is a criteria to the advantage of any big establishment over the small one that it can afford the means for the employment of highly specialized staff.

So far the advantages of branch banking in general have been discussed with little mention to the advantages of foreign banks in Lebanon over the Lebanese local banks. We should attempt to discuss the effect of the operation of the 16 foreign banks operating in Lebanon on the operations of the local banks.

The fact that foreign banks form a serious competitive element to the local banks is unquestionable. They compete not only by offering attractive remuneration, but by the goodwill which their head offices have built up all over the world. The fact that they have this goodwill which the local banks do not have, has made the latter appeal to the depositor by granting him a larger remuneration on his deposits. This is expressed by the fact that interest rates granted by most of the local banks on deposits, especially time deposits and saving accounts, is in general higher than that granted by foreign banks. (For further discussion see chapter IV).

On the other hand, a businessman with a good credit standing and whose signature on a commercial paper renders it a first class note finds it often cheaper to get loans from foreign banks at a cheaper rate of discount or at a lower interest rate on an overdraft. Such businessmen often do not resort to local banks for borrowing. In such cases the local banks find themselves faced with the problem of extending loans to some customers whose credit standing is not yet clearly established and with not much information about them. Although this means that a larger risk is to be undertaken on the part of some of local banks, there is no doubt that there is an advantage to them by helping these newly established concerns. By giving such concerns financial help the bank helps them to grow. When they grow and stand on their own they change their status from debtor customers of the bank and become depositors.

The risk in such instances is that such concerns may fail due to bad entrepreneurship. The local banks do not have the means or the adequate experience to judge whom to help and whom not to out of the growing concerns that need their financial help.

Another effect of the operation of foreign banks is a result of the dealings in foreign exchange where the foreign banks act as the suppliers and the native banks as demanders of foreign exchange and in some cases vice versa. In general local banks need foreign exchange to finance commercial and exchange transactions in foreign currency. Such transactions are made at the request of importers and individuals in Lebanon. The main forms of these transactions are the letter of credit and the cheque in foreign exchange sold in Lebanon and cashed abroad.[1] The foreign exchange needed for this purpose is secured by means of the local banks maintaining current accounts with foreign correspondents abroad and on which they draw either by cheque, letter, cable, or any other means; this account in some cases may be overdrawn according to the individual agreement between the local bank and its foreign correspondent. These drawings are covered by remittances in the form of bankers cheques in foreign currency which the local

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1. These operations are explained more fully in chapter IV.

bank buys from the market at the free exchange rate. Such remittances however are often not enough to meet the withdrawals made by the local banks and here comes the part of the foreign banks in Lebanon as suppliers of such exchange.

The local bank in need of foreign exchange may buy its needs of such exchange from the foreign bank who transfers it to the credit of its account with its correspondent. To the foreign bank the transaction is a mere book entry where it credits its head office account for the foreign currency transferred and debits the local bank. The ultimate effect is that liquid capital is imported into Lebanon to the extent that the local banks are debtors to foreign banks.

Foreign banks on the other hand buy foreign exchange when there is excess exchange in the hands of local banks. In such cases foreign banks act in the opposite direction explained above and transfer balances to their head offices.

IV . <u>The Expansion of Local Commercial Banks</u>

In chapter II we have seen that some of the banks established as Societe Anonyme Libanaise are affiliates to foreign banks. Of the 15 banks registered as Lebanese 6, or 40 percent, are affiliated to foreign banks. These affiliates are pointed out by a foot-note to table IX below.[1] In the present section we shall discuss branch banking in local banks including those that have such foreign interest in them. In other words, in the definition of a local bank we shall follow the legal status of the bank.

The advantages foreign banks have, as branches of their head offices, over local banks have been discussed above. These are advantages of any branch banking system whether foreign or local. But it is a feature of the local Lebanese banks that they do not form a branch banking system in the sense foreign banks established in Lebanon do. Some of the local banks do have branches but these branches are limited mostly to Lebanon and Syria and a few are in the other neighbouring Arab countries. Table IX shows that of the 15 local banks operating in Lebanon eleven have no branches. Of the remaining four banks one i.e. Banque du Liban et d'Outre Mer, has only one branch besides its head office and the remaining three namely Banque Misr-Liban (partly local), Federal bank of Lebanon and Intra Bank each has nine branches. As to the location of these branches table IX shows that of the 41 branches which belong to the system both in and outside Lebanon, 25 or 62 percent are located in Lebanon, 8 or 20 percent in Syria and the remaining 8 are with the exception of one

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1. For details see appendix III.

TABLE IX

BRANCHES DISTRIBUTION OF

LEBANESE COMMERCIAL BANKS

| Bank | Total Branches | Distribution of branches | | | |
|---|---|---|---|---|---|
| | | Lebanon | Syria | Iraq | Others |
| Banque Misr-Liban* | 9 | 4 | 5 | | |
| Banque Tohme | 1 | 1 | | | |
| Eastern Commercial Bank | 1 | 1 | | | |
| Societe Bancaire du Liban (Zelkha)* | 1 | 1 | | | |
| Banque Libanese pour le Commerce | 1 | 1 | | | |
| Banque Sabbagh* | 1 | 1 | | | |
| Banque Trad (Credit Lyonnais)* | 1 | 1 | | | |
| Banque du Liban et d'Outre Mer | 2 | 1 | | | 1 |
| Federal Bank of Lebanon | 9 | 5 | | 4 | |
| Intra Bank | 10 | 4 | 3 | 1 | 2 |
| Banque Saradar | 1 | 1 | | | |
| Banque Al-Ahli | 1 | 1 | | | |
| Banque Belgo-Libanaise* | 1 | 1 | | | |
| La Banque de Beyrouth et des Pays Arabs | 1 | 1 | | | |
| Banque Beyrouth Al Ryad | 1 | 1 | | | |
| | 41 | 25 | 8 | 5 | 3 |

Source: Annual reports of the banks mentioned
* Affiliates of foreign banks.

in other Arab states. This exception is the very recently (June 1958) established affiliate to the Intra Bank in Geneve named Intra Bank Geneve.

From the above it is clear that the system is not a branch banking system. This feature may be explained by the fact that the system is a new one. Having limited experience, management is not adequately equipped to undergo expansion into a branch system. Of the three banks with the largest number of branches, the first, namely bank Misr-Liban, ia as noted an affiliate of a foreign establishment and thus can rely for expansion on its mother company. The other two, namely the Federal Bank of Lebanon and Intra Bank, have the largest capital invested among all the other local banks (see table IV chapter II). Experience, and resources are major factors for the development of a branch system.

The general trend however is towards establishing branches outside Lebanon. This feature is a recent one. Of the 15 branches belonging to Lebanese established banks, 12 were established during the last six years. At this rate the content of table IX is likely to be radically changed with the passage of time. This tendency towards branch banking started when the local banks established branches other than their main Beirut branch. The facilities created because of such branches encouraged them to establish other branches in the main towns of Lebanon.

## V. Inter Bank Relations

The Lebanese banking system is characterized by individualism. Each bank works towards complete independence of the other banks whether local or foreign. To some extent, this is due to the absence of a central bank, A central bank being impartial and having the welfare of the economy as its aim, fosters cooperation between the individual banks of the system. In Lebanon the B.S.L. performs some of the functions of a central bank, but it is a private foreign institution that competes with the other commercial banks and therefore is distrusted.

There were attempts however for cooperation between Lebanese bankers. An attempt to form an association of Lebanese bankers was made in 1954 by Banque Libanaise pour le Commerce, The Federal Bank of Lebanon and Intra Bank. The directors of these three banks met but their attempt failed when Intra Bank withdrew. While the attempt of the native banks failed some foreign banks reached an agreement in January 1956 to form a banker's association. This association is looked upon with suspicion by the local bankers. Another reason for the absence of inter Bank relation is the fact that the system is a highly competitive one. As mentioned earlier, competition among the banks is keen, and it is expressed mainly in the rate of interest granted on deposits. Whatever the form ~~the~~ competition takes, it is not expected that it would produce a cooperative spirit between the competing institutions. As to the relation of the local banks with the B.S.L., the fact that this bank acts as the Government agent and has some of the functions of a central bank puts it in a special favored poaition.

A sign of cooperation was amde in 1953 when, upon the direction of the Government authorities concerned, the Central des Risques was established under the supervision of the B.S.L. and the membership of the banks. According to this establishment all member banks are required to submit to the B.S.L. monthly returns about the loan facilities available to each customer, and the extent the customer has made use thereof. The B.S.L. consolidates these returns into a single one and informs the member banks about the extent to which indebted customers have made use of the credit facilities available to them. Accordingly any customer who contracts for loans from more than one bank is thus discovered and misrepresentation in this respect is prevented. Such an indirect exchange of information between the banks through the B.S.L. is of great importance to the individual banks. But it is obvious that it gives the B.S.L. an advantage over the other banks.

## CHAPTER IV

## COMMERCIAL BANKS OPERATIONS

The purpose of this chapter is to examine the operations of commercial banks in Lebanon. These operations will first be explained and then illustrated in terms of their effect on the banks statements.

It should be noted at this point that of the 29 accredited commercial banks in Lebanon 15 are branches of foreign banks. The statements of these fifteen banks are incorporated with those of their head offices , as there is no banking law which requires them to issue separate statements for their branches in Lebanon. The figures shown in this chapter are taken from the statements of the remaining fourteen local banks.

### I. Sources of Funds

#### 1. Proprietorship

The contribution of the owners is represented on a bank balance sheet by capital stock, capital surplus, undistributed or retained profits and equity reserves. From the stand point of depositors, the function of the owners equity is to provide a buffer of safty in the event of losses sustained by the bank. There is a conflict of interest between shareholders and depositors. The former, wanting liberal earnings and dividends, try to serve this purpose by a low ratio of proprietorship equity to deposits. Depositors on the other hand seek a high degree of safety thus desire a large ownership interest. Table X below extracted from a condensed balance sheet of eight commercial banks given in appendix V shows that this ratio has varied over the last four years decreasing from 15 to 9 percent between 1954 and 1957.

TABLE X

TOTAL PROPRIETORSHIP IN RELATION TO TOTAL ASSETS OF 8 COM. BANKS.

(figures in LL 000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Capital (paid up) | 29404 | 37425 | 42500 | 46979 |
| Legal Reserves | 364 | 538 | 829 | 953 |
| Special Reserves | 1585 | 1949 | 3732 | 4153 |
| Retained Savings | 24 | 205 | 102 | 81 |
| Other Reserves | | | 258 | 393 |
| Total Proprietorship Equity | 31377 | 40117 | 47421 | 52559 |
| Total Assets | 205836 | 335738 | 460623 | 590627 |
| % Total Equity of Total Assets | 15 | 12 | 10 | 9 |

This decrease means that depositors are becoming less secured since proprietorship equity is decreasing in relation to their deposits. The decrease in this ratio has taken place though the capital accounts as shown above have increased by 60 percent in 1957 over that for 1954. This increase however was more than offset by the increase in the volume of deposits.

2. Deposits

By far the most important source of a banks funds is the deposits of customers. These deposits consist primarily of chequing accounts and time or fixed deposits. The latter type of deposits are of two classifications: Fixed deposits accounts and saving accounts.

In opening a fixed deposit account the depositor agrees not to draw the amount deposited or any part thereof before a certain due date or before giving notice as agreed beforehand. The interest rate is also agreed upon and mentioned in the contract. The rate depends upon the amount of the deposit, the length of the period of time it will remain with the bank and the bank itself. In Lebanon interest rates on time deposits ranges between 3 and 4.5 percent. The interest proceeds are credited to the account on or after the due date of the period of deposit . If that period is not renewed, interest ceases as from the maturity date and the deposit becomes payable on demand without any interest.

The advantage of this kind of deposit to the banker is that it is fixed for a certain period of time and accordingly he can better plan the use of the funds thus available. To the creditor customer the advantage is a higher rate of interest than on current account as a return for keeping his account illiquid until the expiration of the deposit agreement.

The time depositor is not given a cheque book as in the case of a current account depositor because he is not allowed to draw on his account before maturity. This provision however is often not strictly applied in some of the local Lebanese banks. In a number of instances some of these banks allow some withdrawals on fixed deposits before their maturity date and they go as far as issuing cheque books for fixed depositors thus treating them as current creditors. This they do in order to attract time deposits and in order to encourage time depositors to renew their contracts.

Saving accounts are designed to attract bank deposits by encouraging savings. Regulations applying to savings at one of the local banks are:

1. Only one saving account will be opened for a given name.

2. The bank will deliver to every depositor a non-transferable saving booklet in which are recorded all deposits, interests and withdrawals. Each entry will be authenticated by the signature of two authorized officials of the bank.

3. Deposits below LL 5 are not accepted and a saving account should never exceed the sum of LL 10,000.[1]

4. Withdrawals under LL 25 may be made at any time. Withdrawals exceeding this limit will have to be notified at least seven days before the actual withdrawal will be allowed.

5. Interest is calculated on the lowest balance of each month every six months and the amount is credited to the customers account.

Though the types of deposits in Lebanon vary as shown above, the rate of interest granted on each type does not vary correspondingly as is expected. That is the rate of interest on deposit accounts are expected to be in general higher than that on current accounts. In Lebanon this is not necessarily the case. Some of the local banks give high interest rates with little consideration to the type of deposit. As we have seen above some of these banks do not impose the fixed deposit agreements in respect of restricting withdrawals and issue cheque books for deposit accounts. Such a treatment eliminates the distinction between fixed and current deposits, and means that a higher interest rate is paid by these banks on current accounts.

The above discussion of the types of deposits

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1. This provision is no longer significant because of the Bank secrecy law.

applies to all currencies with no distinction. A depositor may have an account opened according to the above terms in any currency besides the local Lebanese one. The interest rate given on foreign currency accounts however may be influenced by the interest rate on deposits in the country of that currency.

Table XI compares the volume of deposits in LL and in foreign currencies over a period of three years. According to the director of the statistics department in the ministry of National Economy, the ministry has not decided yet whether or not to release the data concerning the volume of deposits in foreign currency. The content of table XI in that respect however is taken from the B.S.L. auditors' report to the general assembly.

Table XI shows that foreign currency time deposits have increased by 2.5 times compared to a corresponding increase of 1.5 times for local currency time deposits over the same period of three years. Total volume of deposits in foreign currency is about 20 percent of that of deposits in Lebanese currency. It would have been interesting to study the effect of the bank secrecy law of 1956 mentioned earlier on the inflow of foreign capital into Lebanon in the form of foreign currency bank deposits, but unfortunately no such data is available since 1956.

In developed banking system deposit items are usually

TABLE XI

DEPOSITS IN FOREIGN & LEBANESE

CURRENCIES

(in LL Millions)

| end of | F/C Dem. Dep. | LL Dem. Dep.[1] | F/C Time Dep. | LL Time Dep.[1] | Total Dep. | Total LL Dep[1] |
|---|---|---|---|---|---|---|
| 1954 | 47.5 | 362.0 | 6.6 | 26.7 | 54.1 | 388.7 |
| 1955 | 58.5 | 443.9 | 12.6 | 39.3 | 71.1 | 483.2 |
| 1956 | 65.7 | 440.2 | 16.3 | 42.4 | 82.0 | 482.6 |

Source: 1. Bulletin statistique trimestriel
2. B.S.L. General Assembly, Report of the auditors June 1957, p. 25.

between 8 and 16 times larger than proprietorship.[1] Table XII below gives this ratio for eight Lebanese commercial banks over a period of four years.

TABLE XII

PROPRIETORSHIP AND TOTAL DEPOSIT RATIO

FOR 8 LEBANESE COMMERCIAL BANKS

(Figures in LL 000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Demand Deposits | 96386 | 135049 | 187793 | 268359 |
| Time Deposits | 20358 | 44306 | 48535 | 53149 |
| Total Deposits | 116744 | 179355 | 236328 | 321508 |
| Total Proprietorship | 31377 | 40117 | 47421 | 52559 |
| Ratio Total Dep. to Total Proprietorship | 3.7 | 4.5 | 5.0 | 6.1 |

1. Woodworth, op.cit., p. 85

Though these ratios are very small in comparison to those given for developed banking system, it is noted that they have been increasing considerably. This also agrees with what table X above shows about the relation between total assets and proprietorship. From that table we saw that the relation between total assets and proprietorship is decreasing. This decrease is partly explained by what table XII above shows about the increase in deposits in relation to proprietorship. Though in 1957 the ratio compares very favorably with that for developed systems (6.1 - 8&16) it is much higher than that for 1954. This is explained by the fact that deposits are increasing at a much higher rate than the increase in proprietorship a sign of development in the banking system.

3. Re-discounting

Up to the time of the suez crisis in October 1956 the B.S.L. did not rediscount bills for commercial banks; it rather accepted bills for security against which it gave advances to these banks

Such advances were made by the B.S.L. against first class trade bills endorsed to it by the commercial bank sending them. Against the value of such bills the commercial bank is allowed to draw funds from the B.S.L. up to a maximum amount of 75 percent of the value of those bills. On these drawings the commercial banks were charged an interest rate of 4.5 percent. This was not a rediscount activity but rather one according to which, the B.S.L. treats the commercial banks as customers depositing bills for security with it against which they are allowed to draw funds, and on which they are charged an interest rate in the same way a debtor customer is charged.

In 1956, owing to the suez crisis, the rush for cash by the public affected many banks especially those of Egyptian and foreign origin. To help the banks meet this rush for cash the government interfered by making the B.S.L. discount trade bills for commercial banks employing for the purpose the government free reserves deposited with the B.S.L. The bills thus discounted had to be first class trade bills written for an amount not less than LL 200.

The amount of total papers discounted by a commercial bank is also limited to a certain maximum and the rate of discount is fixed at 3 percent.

The difference between the two types of dealings in bills between the B.S.L. and commercial banks mentioned above is that while according to the first no actual discount of bills was made and bills were kept as security against "loans" to commercial banks with the purpose of financing trade, the latter involves actual discounting at a fixed rate with the same aim of financing commercial transactions.

The role of commercial banks according to the above discussion is that of a middle man between discount houses and the B.S.L. which acts as a last resort. They prefer to rediscount bills already endorsed by the discount houses thus relieving themselves from the risk of default. When discount houses are refused short term credit facilities by bankers, they have no lender of last resort and so have to support the shock of a drain in the liquidity of the market. Discount houses found themselves in such a position early in 1953 when the B.S.L. called back its loans and commercial banks followed suit. The effect was that many traders had stocks on hand with no liquid cash and in order to pay their debts to commercial banks resorted to forced sales of their goods with considerable losses, while others were declared insolvent and bankrupt. During that period the number of protested bills quadrupled as shown by table XIII. The value of protested bills rose from LL 367,000 in July 1953 to LL 1,208,000 in September of the dame year, and to LL 1,052,000 in October 1953, but then fell sharply to LL 432,000 in November 1953, partly because the government advised bankers and especially the B.S.L. to lebralize credit to traders to overcome their illiquidity.

## CHAPTER XIII

### PROTESTED BILLS IN BEIRUT

( in LL 1000)

| Month | 1953 | | 1955 | | 1956 | |
|---|---|---|---|---|---|---|
| | No. | VALUE | No. | VALUE | No. | VALUE |
| Jan. | 142 | 220 | 183 | 470 | 250 | 384 |
| Feb. | 87 | 189 | 145 | 220 | 171 | 347 |
| Mar. | 116 | 132 | 194 | 269 | 210 | 567 |
| Apr. | 117 | 216 | 133 | 126 | 231 | 291 |
| May | 144 | 387 | 144 | 161 | 247 | 305 |
| June | 194 | 455 | 140 | 152 | 231 | 184 |
| July | 205 | 367 | 231 | 426 | 264 | 317 |
| Aug. | 443 | 722 | 248 | 302 | 293 | 411 |
| Sept. | 487 | 1208 | 226 | 379 | 203 | 470 |
| Oct. | 477 | 1052 | 260 | 413 | 363 | 546 |
| Nov. | 286 | 432 | 191 | 295 | 366 | 452 |
| Dec. | 347 | 658 | 227 | 305 | 548 | 655 |

Source: Bulletin Statistique Trimestriel.

Under the present conditions, commercial banks are able to rediscount trade bills at the B.S.L. at the rate of 3 percent, can always accept to discount trade bills produced by the discount houses. These discount houses are thus relieved from their responsibility of supporting the shock of a drain on liquidity such as that of 1953. This is proved by the figures for 1956 in the above table. In September 1956 the suez crisis started and many traders found themselves unable to settle the bills due against them. But the B.S.L., upon instructions of the Government, started to rediscount bills for the commercial banks. Being able to rediscount at the B.S.L., the commercial banks arranged with the discount houses to renew or extend the maturity of the bills discounted and rediscount them with the B.S.L. rather than insist on payment and in many cases accepting default. Thus the protested bills during the suez crisis, both in number and value, did not reach the size of that of the July-September crisis of 1953.

II. Uses of Funds

1. Loans and Advances

Commercial banks are typically fitted to advance commercial loans and discounts. In Europe and the US such a demand for loans and advances has decreased considerably. In these countries , commercial banks' funds have found new outlets such as investment in securities.

Such a use of funds in Lebanon is very limited. This limitation is due partly to the fact that there are other more profitable means for the use of loanable bank funds, and partly because the investment market is not yet developed to allow such a use of funds.

In Lebanon loans and advances are in general the main outlets for bank funds. Commercial banks dealings in ~~through~~ advances and discounts have increased by about 62 times between the end of 1939 and May 1958, that is, from a total of LL 9.6 millions to LL 687.7 millions. As shown by table VII of chapter III, between 1939 and 1947 advances and discounts were increasing at an accelerating rate, but they have not risen above or reached the level of the volume of total deposits. After 1947, advances and discounts exceeded the volume of total deposits.

The purpose of these loans and advances is mainly to finance foreign and local trade. Other forms of credit, however, do exist, but the volume of these credits is relatively small. Of the main forms of these credits are industrial, real estate, and public utilities and government agencies credits. Informed banking circles in the American Embassy at Beirut estimate loans and advances distribution among the economic sectors and compares them for 1954 and 1957 as follows:

TABLE XIV

DISTRIBUTION OF ADVANCES AND DISCOUNTS

IN LEBANON

(in Percentages)

| Sector | 1954 | 1957 |
|---|---|---|
| Trade | 60 | 40 |
| Land & Buildings | 20 | 35 |
| Advances to Public Utilities Government Agencies and Municipalities | 20 | 25 |
| Total | 100 | 100 |

Source: American Embassy Report No. 447.

These estimates are produced here because of the absence of official figures and under strict reservation. According to these estimates and comparisons, the largest share in the advances and discounts goes to trade. But between 1954 and 1957, the share of trade in the volume of advances and discounts has decreased by 33 percent. On the other hand credit, for land and buildings increased by 75 percent; and advances to public utilities, government agencies and municipalities have also increased by 25 percent over the same period. This means that commercial banks are increasing their extention of credit for the lands and buildings sector as an outlet for their loanable funds probably because it is more secure and profitable, and because demand for trade loans has become almost saturated. This financing of the building boom has produced speculation in lands on the part of some banks. Advances to industry are not given seperatly, but it is assumed that they are included in the estimate for the advances for trade. However as mentioned above these are only estimates that are presented with strict reservation.

In general commercial banks do not find the means for acquiring the proper information they need about debtor applicants. So they tend to accept more to advance loans that are backed by a mortgage on tangible assets. This may explain why in the estimate given above advances for lands and buildings purpose and for government agencies have increased. The former kind of advances is secured by mortgage on actual property up to a part of its market value and the latter is secured by the Government. Commercial and industrial credit on the other hand is backed by the credit standing of the debtor only. In some cases trade advances are secured by mortgage on actual goods, the value of such a security depends on the nature of the goods mortgaged. In case these goods are of very specialized nature, or in case they are perishable goods, they may not realize even part of the advance made against them.

The form loans take are the overdraft and discounts. These forms will be discussed in the following section seperately.

## A. The Overdraft System

The overdraft account or current debtor accounts, as it is called by some banks, is a form of current account. It is an account opened upon agreement between the bank and a certain customer according to which that customer is allowed to overdraw his account up to a certain maximum. This maximum limit allowed is the line of credit of that customer as set by the bank. This limit is set by the banker on the basis of the credit standing as determined in accordance with the information and after investigation of the recommendations he has about the customer.

Such an agreement is usually reached by both parties in which there may or may not be a third party as guarantor of the debtor customer. At the same time, this agreement sets the rights and obligations of both parties in details. Some of the main provisions of such an agreement are summarized and shown in appendix IV.

A customer however may have more than one line of credit. He may have two or more different lines of credit in two or more banks. In such cases the total lines of credit this customer will have with all banks constitutes his credit standing. The central de risques (discussed earlier in chapter III), helps to give the information about this total line of credit, and to what extent such a customer has made use of the credit facilities available to him.

B. Bills Discounted

Bills of exchange are of two types. A bill may be an inland bill i.e. local, or foreign bill. An inland bill is one which is a) drawn and payable in the country i.e. Lebanon, and b) drawn within Lebanon upon a person resident therein. Any other bill is a foreign bill.

In this section inland bills are to be discussed.

Foreign bills of exchange will be handled in the following section under operations of the Foreign Department.

Commercial papers in Lebanon arise from two main types of transactions. First, there are trade bills which are used to finance short term commercial transactions, and, second, there are bills which finance consumer credit. Trade bills are those that arise out of trade transactions between merchants. They are usually drawn by one trader on another in settlement of a trade transaction between them. Such bills are drawn for a maximum duration of 90 days. These bills are widely accepted by commercial banks for discount. The other kind of bills is used to finance consumer's credit. This kind of credit is new in Lebanon and until recently its use was very limited. However, the financing of such consumers' credit by bills is increasing at present due to the increase in the sale of consumer's durable goods on the instalment basis. In general the duration of such bills ranges between one and eighteen months.

Such promissory notes are drawn for small amounts that on the average range between LL 25 and LL 150. They are drawn by the consumer's durable goods retailer on his customers whose credit standing is unknown to the retailer and is costly to investigate. The retailer however has a lien on the goods he sells until he covers the whole amount of the sale, and in case of default, he can always reacquire his goods. Commercial banks therefore are not interested in discounting such notes unless they are endorsed by somebody whose credit standing is known to them.

As in the case of overdrafts, a line of credit is also established by the banker for discounting bills. These bills are discounted with the commercial banks not on the basis of the credit standing of the drawee but on that of the drawer. So a businessman with a good credit standing discounts his bills directly at the commercial banks. Discount houses are thus left to deal with second class bills.

There are in Beirut about thirty discount houses whose exclusive function is to discount or purchase bills offered in the market. There are also a number of brokers acting as intermediaries between traders and these discount houses. These houses get their loanable funds mainly from their capital, time deposits usually placed by relatives and friends and on which they pay an interest rate of about 6 percent per annum, and by rediscounting their bills with the commercial banks at a rate which varies between 7 and 8.5 percent.[7]

With the endorsement of the discount house on the bills, these bills become first class ones and are thus accepted by the banks. The discount house usually keeps a current account with the commercial bank it deals with and on which it is allowed a certain line of credit. The proceeds of any bill it rediscounts with the bank are credited to that account and any defaulted bills are automatically debited to it. The function of a discount house therefore is to make good bills which are not accepted by commercial banks, endorses them, and rediscount them with the banks. Such bills are not accepted by the banks because they are drawn for small amounts and on people whose credit standing is difficult to assess.

2. Investments

The distinction between loans and investments is rather an arbitrary one since any advance of funds may be labled as a loan or as an investment. In developed banking systems investment items on the statements of banks include bonds of all types and stocks in so far as banks are permitted to hold them and government securities.

Such a restriction on the natures and composition of the investment account does not exist in Lebanon because of the absence of control and the non-existence of commercial bank law. Thus investments held by banks in Lebanon are found to be kept not for secondary reserve purposes but rather as investments in immovable properties such as real estate and sites which are thought to give more prestige and is in public confidence for the banks.

Table XV blow compares these investments items, to total proprietorship for the eight banks considered.

Table XV

Relationship between Investments and Proprietorship
(in LL 000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Premises & Sites | 2062 | 2629 | 6033 | 7937 |
| Other Investment | 2150 | 6141 | 7893 | 11413 |
| Total Investment | 4212 | 8770 | 13926 | 19350 |
| Total Proprietorship Equity | 31377 | 40117 | 47421 | 52559 |
| %total Inv. is of total Proprietorship Equity. | 13 | 22 | 30 | 37 |

However, before commenting on these figures it is important to note that this table is not representative of all the banks considered since one of the component balance sheets, namely that of Intra Bank, distorts the picture and misrepresents the ratios for the other remaining seven banks. Excluding the figures for Intra Bank (which will be commented on later) the new figures are shown in Table XVI below.

Table XVI

Relationship between Investments and Proprietorship for 7 Local Banks

(in LL 000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Premises & Sites | 1272 | 2629 | 2929 | 2908 |
| Other Investment | 446 | 2884 | 4206 | 3157 |
| Total Investment | 1718 | 5513 | 7135 | 6065 |
| Total Propr. Equity | 23792 | 31101 | 37766 | 41768 |
| % Total Inv. is of total Propr. Equity | 7 | 18 | 19 | 15 |

The ratios shown by the above table are undoubtedly high if we consider that investment is mainly in immovable property. The purpose of an investment portfolio is to permit adjustment of the cash balance with changing business conditions. Investment portfolio of banks increases when business declines so that instead of keeping idle assets banks invest in earning assets as securities. In good business, booms investment portfolio decreases i.e. banks sell their investments and lend more money. In the case of Lebanese banks this is not the case since investments as mentioned before are mainly in immovable property. Such assets, though held in the ratio shown above, are not the type of assets that a commercial bank should hold. In periods of crisis the realizable value of such assets may fall much below their book value, let alone the question of their marketability. Such an investment portfolio therefore is by no means of the secondary reserves type.

3. Primary or Cash Reserves:

The necessity of maintaining an adequate supply of primary reserves is the principal limitation upon expanding the proportion of earning assets. For Lebanese banks, the items which make up this fund are cash in vault and demand deposits maintained with correspondent banks, local and foreign. Because of the fact that banks must be ready to meet demands for cash at a moments notice, they cannot afford to sacrifice liquidity for the sake of income. In normal times and in developed banking systems cash reserves are kept between 6 and 12 percent of total deposits depending on the time and place of the individual bank.

Table XVII below shows this ratio for the 8 selected Lebanese banks. As shown by this table, the ratio varied

Table XVII

Cash Reserve Ratio to Total Deposits

(in LL. 000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Total Cash | 40204 | 52587 | 88251 | 113513 |
| Total Deposits | 116744 | 179355 | 236328 | 321508 |
| % Ratio of Cash to total deposits | 35 | 30 | 34 | 35 |

between 30 and 35 percent. Compared to that kept by commercial banks in developed banking systems this is a high ratio. This is because in Lebanon, as mentioned above, banks do not have a secondary reserve portfolio because of the underdevelopment of the securities market. Thus they keep all their reserves in the form of cash or, more often, in the form of demand deposits at other banks, mostly foreign banks abroad.

But it should be noted that the above figures are end-of-the-year balances and therefore are not quite representative since banks usually take the habit of window dressing their statements.

Compared to total assets, table XVIII below shows that on the average the cash balance is about 19 per cent of total assets for the period of the four years presented.

Table XVIII

Ratio of Cash to Total Assets

(in LL.000)

| | 1954 | 1955 | 1956 | 1957 |
|---|---|---|---|---|
| Cash | 40204 | 52587 | 88251 | 113513 |
| Total Assets | 205836 | 335738 | 460623 | 590627 |
| % total cash of assets | 19 | 16 | 19 | 19 |

This is of course a high ratio which affects profitability of the banks concerned since it means that 19 percent of total assets is in the form of cash and inter bank deposits.

Here again it should be pointed out that this cash item is taken as of the end of the year, that is the figures shown on year-end statements and therefore are not quite representative. Besides, demand deposits with other banks which constitute a considerable part or even the larger part of the cash balance do earn interest although the rate may not be quite high.

## III. Other Operations

The operations of the foreign department are a major part of the main activities of commercial banks in Lebanon. Such operations consist mainly of letters of credit and of dealings in foreign exchange. The letter of credit is a form of a foreign bill of exchange mentioned earlier. In Lebanon it is the main instrument of financing foreign trade, which is greatly facilitated by the existence of a free exchange market. In the following section the letter of credit and foreign exchange dealings are discussed.

### 1. The Letter of Credit

The basic principle behind the letter of credit is that a bank is requested by its custome• to lend its obligations to pay to sellers of goods stated sums of money against delivery of stipulated documents usually representing title to goods. In most cases the form of a letter of credit is irrevocable. Because of its irrevocability it is important that the terms and conditions be simple and easily understood. These conditions imply that the exporter receives the value of his goods upon parting with his title to them. In other words, foreign trade carried out by means of letters of credit are made on the basis of cash on delivery. Such a kind of dealing has increased after world War II because of the general economic and political instability in the world.

The most important document of a commercial letter of credit is the bill of lading. Together with this important document the letter specifies the other documents the importer wishes to get hold of as required by the Lebanese customs regulations.

On opening a letter of credit for a customer, banks in Lebanon usually require the customer to pay in cash a part of the amount of the credit. This part varies between 15 per cent and 50 percent, and may rise to 100 percent in uncertain times such as those of the Suez crisis. This amount deposited on account of the letter of credit depends, among other things, on the credit standing of the customer, the nature of the commodity, the general economic and political situation, and the competition between the banks. A customer with a good credit standing may not be asked to pay a deposit on account. On the other hand, a customer with a weak credit standing and a very specialized commodity may be required to pay a 100 percent deposit. In times of political crisis and uncertainties no matter what the credit standing of the customer is a bank may insist on a 100 percent deposit. In ordinary times, competition between the banks tends to reduce this deposit to a minimum.

Having accepted to open the credit to a customer the bank instructs its foreign correspondent to pay the exporter the amount against the specified documents. The correspondent bank pays the amount, receives the documents and charges the Lebanese bank for the amount paid plus charges and commissions. The length of time that passes between the time the correspondent charges the Lebanese bank account and the time the customer pays the amount varies. On that time, the customer is charged interest on the amount at the current market rate.

The benefits to the local bank from this activity come from:

a) The use of the money deposited as margin by the customer from the time the credit is opened to the time payment is made. No interest is allowed to the depositing customer.

b) The interest charged the customer on the net amount of the credit from the time it is paid abroad by the correspondent bank to the time it is finally settled. This rate is at present the current interest rate which is 9 percent.

c) Commissions charged the customer for the service. This commission varies between 1/8 of 1 per cent to 1 percent depending upon the amount of the credit and the credit standing of the customer.

d) Profits from the rate of foreign exchange.

If we consider the fact that for the 8 banks whose consolidated statement is presented in appendix IV, total outstanding credits at the end of 1957 amounted to LL. 143,188,000, the significance of the deposit made as margin, the commission, and the interest charged is no doubt an important income to the bank.

B. Foreign Exchange

Lebanon is a free exchange country and foreign exchange transactions are profitable to many Lebanese commercial banks. These foreign exchange transactions are carried out by the following activities:

a) Purchase and sale of foreign exchange in the forms of currency and cheques for personal uses.

b) Transfers by individuals and companies.

c) Sale of exchange for foreign trade purposes.

The purchase and sale of foreign banknotes is not very common in commercial banks. This activity is more in the line of business of money brokers and exchange dealers. The main form of exchange dealings by banks is in cheques and in the purchase and sale of foreign bank balances abroad and at home. The purchase and sale of cheques in foreign currency is made directly with the customers. Banks buy bankers cheques drawn in foreign currency and remit those cheques to their correspondents abroad. When collection is made the proceeds are credited to the Lebanese bank account with that correspondent for the amount collected.

On the other hand, Lebanese banks offer to supply cheques drawn in foreign currencies when customers want to make payment in foreign exchange for individuals or business concerns abroad. They draw on their accounts with their foreign correspondents by cheques and sell those cheques to the customers at the current exchange rate. When the correspondent drawn on pays the amount of the cheque he charges its amount to the Lebanese bank account with it. On such operations the Lebanese bank charges a commission usually about 1 per 1000. Besides this commission, the bank makes some profit on the difference between the selling and buying price of the foreign exchange. Between these two prices there is usually a spread. That spread however is greater in times of instability and uncertainty because in such times the value of the Lebanese currency varies greatly and suddenly thus increasing the risk of dealing in foreign exchange. In normal times, this spread decreases because of competition between the banks.

Besides the above activities some of the Lebanese commercial banks deal in futures on the exchange market.

This they do for two reasons. First, they may predict their future needs for foreign exchange for their every day transactions and operations. To secure such needs they may buy at the present for the future. The second reason for such operations is made by some of the banks for speculation purposes. Of course such operations are not in line with sound banking practice and should proper Government control on the assets of commercial banks exist such investment will certainly be forbidden. In a perfect market such operations help to stabilize the exchange rate of foreign currency. Such stabilization is because of the already partly determined future demand and supply of foreign exchange. But the Beirut money market is by no means a perfect one.

The other two forms of dealings in foreign exchange mentioned earlier, i.e., foreign trade and ordinary transfers, are of the nature of ordinary banking operations. The benefits derived by the banks thereon arise from commissions charged and any other similar charges for service rendered.

Another operation of commercial banks in Lebanon is the keeping of trust accounts for customers. This operation is a service rendered by the bank to the customer. Both parties agree that the bank will look after certain possessions that belong to the customer in return for a certain commission for the service. The bank remits a periodical statement to the owner customer of the services rendered and of income derived, if any.

A third operation of commercial banks is the issuance of guarantee on behalf of customers. In dealing with one another, especially when dealing with Government agencies, contractors and traders are sometimes asked to produce a written bank guarantee for a certain sum of money for a certain period of time. The purpose behind such a guarantee and the insistence on its being issued by a bank is that the interested party will have a bank whose credit is more secured to sue in case of default. To issue such a guarantee therefore means that the bank is lending its name to the person on whose behalf the guarantee is issued. For the lending of its name the bank charges the customer a commission fee which varies according to the risk involved and the amount of the guarantee.

In most cases the bank insists on a margin to be deposited with it by the customer before it issues its guarantee. The margin the customer is asked to deposit with the bank is a percentage of the value of the guarantee, and it depends upon the rating by the bank of the customer and his credit standing, and on the risk involved in guaranteeing him. This risk of course varies with the variation in the terms of the contract or the purpose of the guarantee. Such a margin is from the viewpoint of the bank a deposit which ensures its interest. Besides, this margin becomes a part of the deposits of the bank which it may use up to the time of the expiration of the guarantee, at which time the margin is refunded and the obligation of the bank expires.

CHAPTER V

## COMMERCIAL BANKING OPERATIONS II

In the previous chapter a general description of commercial banks operations was presented. The purpose of this chapter is to go a step further and to discuss the cases of two specific banks. The choice of these two specific banks for discussion was made not without purpose.

The first case is that of Intra bank and the choice was made because of the particular reason concerning the investment policy of this bank. The second case is that of the Eastern Commercial bank which was declared illiquid early in 1959. The study of these two cases will be based on the banks' statements as published by these two banks. A limitation to this study however is the absence of detailed profit and loss statements which makes the study limited to balance sheet items. The profit and loss statements published by all banks gives the gross income and match it with total expenses, the balance being the profit of the period. Incomes from interest, discounts, commissions on exchange transactions, and other incomes are not given seperately, a fact which renders income analysis and the profitability of each banking operation undeterminable.

In the previous chapter, when the relation between investments and proprietorship equity for eight banks was discussed, The figures for Intra bank were first included and later excluded (see table XV and XVI of chapter IV). The effect of the figures of this bank on the results was considerable and the reader was promised a seperate discussion for the figures of Intra Bank. Table XIX below is a comparative balance sheet of the Intra Bank for four years 1955 to 1958. It should be pointed out that of those four years two, namely 1956 and 1958, were not normal because of the 1956 suez crisis and the general five months strike of 1958.

Table XIX

COMPERATIVE BALANCE SHEET

INTRA BANK 1955 - 58

(in LL 000)

| ASSETS | 1955 | 1956 | 1957 | 1958 | LIABILITIES | 1955 | 1956 | 1957 | 1958 |
|---|---|---|---|---|---|---|---|---|---|
| Cash. | 8292 | 16356 | 25137 | 25779 | Paid up Capital | 8415 | 8500 | 9336 | 10100 |
| Investments. | 3257 | 3687 | 5916 | 5991 | Legal Reserve. | 566 | 897 | 1062 | 1710 |
| Premises & real Estate. | 786 | 3104 | 5029 | 6783 | Capital Reserve. | | | | 508 |
| Purchace of real Estate (on a/c). | | | 2340 | 4255 | Other Reserves. | 116 | 258 | 393 | |
| Furnitures. | 342 | 324 | 610 | 824 | Earned Surplus | 508 | 547 | 834 | 608 |
| Loans & Adv. | 16312 | 17548 | 20401 | 33123 | Time & Fixed Dep. | 12627 | 17785 | 25876 | 37267 |
| Bills Discounted. | 8768 | 9637 | 11722 | 15562 | Demand Dep. | 16054 | 22094 | 33971 | 44412 |
| Other A/C | 675 | 676 | 1169 | 551 | Other A/C | 46 | 1250 | 852 | 1262 |
| Customers Liab. under Credits. | 8490 | 16326 | 28717 | 33108 | Liability on Credits | 8490 | 16327 | 28717 | 33108 |
| | 46823 | 67658 | 101041 | 128975 | | 46823 | 67658 | 101041 | 128975 |

From the above balance sheet figures the following ratios of investment to total proprietorship are derived:

TABLE XX

(in LL 000)

| | 1955 | 1954 6 | 1957 | 1958 |
|---|---|---|---|---|
| Real Estate & Premises | 786 | 3104 | 5029 | 6783 |
| Payment on Account of Purchase of Real Estate | - | - | 2340 | 4255 |
| Total Investment in Real Estate | 786 | 3104 | 7369 | 11038 |
| Total Proprietorship | 9097 | 10057 | 10791 | 12216 |
| Ratio of Investment in Real Estate to Proprietorship | 9% | 31% | 70% | 90% |
| Other Investment | 3257 | 3687 | 5916 | 5991 |
| Total Investment | 4043 | 6791 | 13285 | 17029 |
| Ratio of Total Investment to Proprietorship | 35% | 68% | 123% | 140% |

The above table shows that through the four year period 1955-58 the ratio of total investment in real estate to total proprietorship has increased by ten times i.e. from 9 to 90% . When other investments are included, this ratio rises from 85 to 140 percent. This rise in the ratio is primarily due to the increase in the investment in real estate, other investments more or less holding the same ratio. The increase in investment in real estate is due to two reasons. First, the construction of the new Intra Bank building over the years 1957 and 1958, and, second, the purchase by instalments of the Lazarieh building, payment of which started during 1957. This latter investment is the origin of the item shown on the bank's statement as payment on account of purchase of real estate.

The policy of investing heavily in real estate rather than in other assets, such as receivables, is defended by the management of the bank on the grounds that it is more profitable and safer. In seeking investment, the ultimate purpose is income. Should the bank invest in loans and advances, or in discounting bills, the interest or discount earned thereon will not exceed the market rate which for safe loans and safe commercial papers is about seven percent. Allowing a margine for bad and doubtful debts, and for defaulted bills and income tax the rate will even fall lower. On the other hand, the management of Intra Bank claims that the net rate of earning on real estate investment in the form of rent is much higher. It amounts to about than 15 percent, even after allowing for depreciation and proper maintenance.

Furthermore, management says that these properties are at the present appreciating in value; market value being at present above cost. Management is also convinced that the present marketability of these estates and their conversion in to liquid cash is at present easier than converting other assets such as loans and advances to liquid cash.

These are the arguments of management in defending the policy of investing in real estate. The marketability question is difficult to judge with no consideration of the political and economic stability of the country. It is when there is no stability that liquidity is needed for the purpose of meeting the demand of the public for liquid cash. At the same time, it is when there is no stability that the price of real estate drops and their marketability becomes more difficult because of the people's preference for liquid cash.

Besides this question of policy, these ratios are in themselves obviously high. From the depositor customer view point it is unquestionably not safe to deposit his money at a bank which shows on its statement an investments figure equal to 140 percent of the total proprietors equity. especially when investment in real estate alone amounts to 90 percent of such equity. These ratios simply mean that the bank is using the public's money for its banking business as well as to cover part of its investment in immovable properties which by themselves amount to about the owners equity. The purpose of capital as a reserve at which the depositors look upon as a cushion in case of need is thus defeated since the owner's contribution is tied up in real estate property whose liquidity depends upon times and circumstances, both of precarious nature and unpredictable.

The bank's policy of investing more in real estate rather than in loans and advances is also revealed when comparing total advances to total deposits as shown by table XXI below. The ratio between deposits and advances, as shown

Table XXI

INTRA BANK RATIO

BETWEEN DEPOSITS AND ADVANCES

| | 1955 | 1956 | 1957 | 1958 |
|---|---|---|---|---|
| Loans and Advances | 16213 | 17548 | 20401 | 33123 |
| Discounts | 8768 | 9637 | 11722 | 15562 |
| Total Advances | 24981 | 27185 | 32123 | 48685 |
| Time Deposits | 12627 | 17785 | 25876 | 37267 |
| Demand Deposits | 16054 | 22094 | 33971 | 44412 |
| Total Deposits | 28671 | 39879 | 59847 | 81679 |
| Percent Total Advances of Total Deposits | 80 | 69 | 54 | 51 |

above, has been constantly decreasing over the four years period. This decrease corresponds with the policy of the bank as shown earlier and as expressed by table **XX** above. But if these ratios are considered separately, they cannot be considered safe especially if we keep in mind the fact that investment in real estate alone amounted to 90 percent of proprietorship in 1958, and total investments amounted to 140 percent of proprietorship in the same year.

The second case to be discussed in this chapter is that of the Eastern Commercial Bank. The Eastern Commercial Bank is a local Lebanese bank established in 1955 as a Societe Annonym with a capital of LL 1,000,000 shared between two partners. Early in 1959 this bank was declared insolvent and the following balance sheets were drawn up by the bank to show its condition.

| Assets | | Liabilities | |
|---|---|---|---|
| Cash | 1,882 | Capital | 1,500,000 |
| Uncleared Effects | 1,210 | Reserve for Bad Debts | 92,767 |
| Bills Discounted | 484,000 | Reserve for Indemnity | 46,365 |
| Advances on Foods | 47,241 | Bills Payable | 132,750 |
| Commercial Accounts debtors | 662,659 | Taxes Payable | 1,330 |
| Secondary Debtors | 145,233 | Telephones | 700 |
| Foreign Currency Advances | 607,500 | Secondary Creditors | 18,584 |
| Banks | 2,081 | Taxes & Revenue Stamps | 2,000 |
| Lands and Buildings | 26,943 | Banks | 16,983 |
| Mortgage | 39,871 | Current A/C | 516,030 |
| Furnitures | 54,966 | Savings | 42,289 |
| Preliminery Expenses | 13,200 | Deposits Fixed | 314,039 |
| Advances to Lawyers | 224 | Foreign Currency Current A/C | 88,500 |
| Goodwill | 500,000 | | |
| Deficit | 187,147 | | |
| | 2,774,337 | | 2,774,337 |

According to this statement the deficit shown is LL 187,147. The Goodwill as shown above has been capitalized making the capital LL 1,500,000. However a committee was formed representing three other banks prepared the following statement to represent the actual position of the bank.

| | | | | |
|---|---|---|---|---|
| Lands & Building | 26,943 | | Current Accounts | 518,030 |
| Furnitures | 20,000 | | Savings | 20,000 |
| Mortgage | 39,871 | 86,814 | Deposits | 374,039 |
| Cash | | 1,882 | Foreign Currency Deposits | 88,500 |
| Uncleared Effects | | 1,210 | Banks | 16,983 |
| Banks | | 2,081 | Bills Payable | 132,750 |
| Recoverable Assets | | | Secondary Creditors | 22,614 |
| Promissory Notes | | 60,000 | | |
| Commercial Bills | | 32,000 | | 1,135,205 |
| Bills Protested | | 60,000 | Reserve for Indemnity | 46,365 |
| Advances on Foods | | 7,000 | | |
| Commercial Debts | | 113,300 | Reserve for Bad Debts | 92,767 |
| Advances in Foreign Currency | | 10,000 | | |
| | | 374,287 | | |
| Deficit | | 900,050 | | |
| | | 1,274,337 | | 1,274,337 |

The above statement shows that the realizable value of the assets of the bank to be only 14 percent of what the bank showed on its statement. According to this statement, and the evaluations made by those who drew it, the deficit becomes LL 900,050. The origin of this deficit comes mainly from the following items. See page 99.

The origin of this deficit was studied by the committee formed; and the investigations of loans, advances,

| | Book Value | Realizeable Value | Deficit |
|---|---|---|---|
| Bills Discounted | 484,000 | 152,000 | 332,000 |
| Current Debtors | 607,500 | 113,300 | 494,200 |
| Advances on Foods | 47,241 | 7,000 | 40,241 |
| Secondary Debtors | 145,233 | | 145,233 |
| Foreign Currency Advances | 607,500 | 10,000 | 597,500 |
| Furniture | 54,966 | 20,000 | 34,966 |
| Preliminary Exp. | 13,200 | | 13,200 |

and discounts revealed that one of the co-owners of the bank, whose capital contribution was LL 600,000, has withdrawn from the bank an amount, in Lebanese and foreign currencies, of LL 1,200,000 i.e. twice his contribution to the capital. Comparing this amount to total advances made by the bank, as shown below, reveals that about 70 percent of the bank's assets

| | |
|---|---|
| Bills Discounted | 484,000 |
| Current Debtors | 607,500 |
| Secondary Debtors | 145,239 |
| Foreign Currency Debtors | 607,500 |
| Total Advances | 1,844,239 |

in the form of advances and receivables was owed by one of the owners. Investing in loans to one individual to this extent has assured the insolvency of the bank. The assets of this individual are not illiquid although they have a market value of about LL 1,400,000.

This is a perfect case where government control and supervision, if existent could have saved the bank's insolvency.

CHAPTER VI

## COMMERCIAL BANKING IN LEBANON

## EVALUATION AND SUGGESTED REFORM

This chapter is intended to give an evaluation of the banking system of Lebanon in the light of the analysis and discription given in the previous chapters. Recommendations that follow from this analysis and description are made in a summary form. Some of these recommendations have already been suggested in one form or another in the earlier chapters.

Since the first world war, and up to the end of the second world war, the rudimentary banking system in Lebanon had changed little. The basic picture was one of a few branches of foreign banks utilizing small amounts of capital of their parent organization mainly to finance foreign trade of Lebanon, and, to a degree, to advance short-term and seasonal credit to the stronger local merchants and landowners of the country. At the head of this small list of foreign banks was the Banque de Syrie et du Liban, which handled the greater part of the banking business and which had the largest number of branches. Lebanese foreign trade was also largely financed by branches of the foreign banks in Beirut.

Domestic savings and deposits entrusted to banks were negligible in volume until the profits of the war period, together with the strict exchange and import control, led to their considerable expansion (see table I chapter I). Business activity during the war and post-war periods spread among the business population the habit of utilizing banking services and of effecting payment in the form of bank cheques. Nevertheless, banks remained all-purpose institutions, lacking in specialization and serving all sectors of the economy. Foreign banks did not deal in long term investment. Investment in agricultural or industrial expansion was almost absent. This is partly explained by the smallness and backwardness of industry at that time; and by the uncertainty of title, the administrative cost, and the big risk associated with agricultural lending. Mortgage credit was small in volume because of the relatively heavy burden of the high rate of interest in this sector, and the low building activity in Lebanon until the end of the war. In contrast, short-term commercial credit was developed. The relative safety and high profitability of such short-term credit are obvious. In addition, the well-established relations of branches of foreign banks with banks abroad made them particularly well-equipped to finance foreign trade of the country.

Local banks on the other hand were small private enterprises or partnerships which had very limited capital at their disposal, and could not rely to any significant degree on deposits as a source of funds. They tended to specialize in discounting bills to domestic traders or accept mortgages on real estate, gold, or jewelry. These local banks relied on their intimate personal knowledge of the borrower in undertaking their business.

Since the end of the war, and due to both internal and external causes, banking activities in Lebanon expanded in a spectacular fashion. But only slight structural changes took place in the banking system. The number and capital of foreign banks increased and the volume of their business multiplied. Local banks organized by Lebanese individuals or groups entered the field in a more professional fashion. This expansion was naturally induced by the growing foreign trade and economic activity in the post-war period and particularly after 1956. This growth which generated the expansion was not purely Lebanese. To a considerable extent, the prosperity and development of the neighbouring oil producing Arab countries, and the oil royalties therefrom, also responsible for a large share of this expansion in the business of the Lebanese banking system.

In spite of this expansion, however, there still exist some basic defects in the banking system of Lebanon.

These defects may be summerized as follows:

1. The limited amount of capital invested.

2. Local banks are mostly individually owned.

3. Some of the local banks invest a large part of their capital in real estate property, thus reducing their current ratio and consequently the amount of credit they would otherwise be able to extend.

4. The absence of banking legislation to protect depositors and to safeguard the solvency and liquidity of some banks.

5. The lack of government control.

6. The absence of a central bank.

The absence of banking legislation and government control of bank activities have to some extent helped to attract foreign capital. But they certainly had adverse effects on the safety and liquidity of the banks themselves. The seriousness of such effects may outweigh the advantages derived from the attraction of foreign capital. Because of keen competition and the profit motive, banks tend to acquire assets excessively, and to undertake transactions which involve a high degree of risk. Such investments and transactions should be supervised by the government. Supervision should also include the information reported on the banks statements. Banks' statements appear once at the close of the business year. These statements, though certified by an auditor, are by no means representative of actual conditions. It is true that the auditor certifies that such statements are made on the basis of accepted accounting principles, but that does not mean that they are representative of the actual conditions of the issuing bank. In other words, the auditor certifies the account correctness of the statement but not the banking principles that underly the statements. Such an act should be assigned to specialized controllers representing a special government agency for control.

Another defect in the Lebanese banking system is the absence of a central bank. Some of the functions of a central bank are being performed by the B.S.L. But the B.S.L. is by no means a central bank, and the objections raised against it are:-

1. In its capacity as the bank of the government and its financial agent, with the privilege of note issue, the B.S.L. is in a position to compete unfairly with the other commercial banks. This favored position of the B.S.L. makes possible an addition to its liquid resources by having recourse to the Issue Department. With the Issue Department at its disposal, it can shift some of the assets of its Banking Department to the Issue Department against additional note issue. Such ready liquidity enables the B.S.L. to compete with other commercial banks at a great advantage.

2. The policy of the B.S.L. is motivated by the interest of its shareholders and not by the public interest. In matters that have to do with monetary policy, profitability

had so far in this respect. Besides, as in the case of any government agency, state administration of a central bank may prove unsatisfactory, and therefore of inefficient performance. A suggestion was made with respect to operating a central bank in Lebanon. This suggestion says that such a new bank should not be governed or controlled by the government or the Ministry of Finance, but rather by the various banks in Lebanon (as is the case in the USA), or by capable and efficient officials appointed by the government without any bias.

The functions and operations of a central bank, the advantages of its existances, and the means by which these functions and operations control and regulate the money market may be found in any text or chapter about central banking and will therefore not be presented.

Central banking business however is not a rigid one. It can be applied differently in different countries to achieve the differentneeds of each country. During the past ten years the Lebanese economy has become increasingly monetized. Should a central bank in Lebanon be established, such a tendency will no doubt be advanced. The flexebility in the operations of a Lebanese central bank should be applied to help the promotion of further development in the money market. The existance of such a developed market will help the central bank to use the tools at its disposal and to apply central banking techneques for fighting inflation and deflation. A central bank and a developed banking system are essential for the development of a money market. In turn the existance of a central bank is necessary in order to have a developed money market. In other words a central bank and a money market have to co-exist in any developed banking system.

Another important aim[1] of a central bank in Lebanon should be the organization of the commercial banking system on a wholesome basis. Commercial banking is very much related to the well being of the monetary system. In the first place, upon the organization of the commercial banks depends the sucess of their use as means at the disposal of the central bank to carry out its monetary policy. In the second place, demand deposits constitute the larger part of currency in circulation, the other part being actual banknotes. With the existance of a well organized and controlled commercial banking system, the function of the central bank as the executor of the monetary policy of the state is very much facilitated. At the present no such function exists by any agency, government or otherwise. Interbank relations are by no means of a co-operative nature. Any form of cooperation that exist, such as the central de Risques or the clearing functions of the B.S.L., are successful because they are useful to the bank

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1. Himadeh S.B., Necessity of Establishing a Central Bank in Syria and Lebanon, Al-Abhath, (V. 4 Beirut Dec. 1951) p.373.

rather than because of any other reason. The B.S.L., though performs some of the functions of a central bank, is in its capacity as a foreign competitive commercial bank suspected by most banks. This suspicion does not by any means help to foster a sound cooperative inter-bank relations.

Another major reform that should be established is the setting of a commercial banking code. This code should provide for the submission of periodic returns and statements by individual banks to the public authorities. The purpose behind such returns should be to expose the actual position of the bank submitting these returns.

At present the only returns submitted to public authorities by banks are those of deposits and advances. Their purpose is strictly statistical; and the information given by them is not enough to make possible critical analysis. Besides the statistical value of the information given by these suggested returns, they should be technically studied and analyzed and ratios extracted from them to make possible passing judgement on their liquidity, solvency, and saftey.

The analyses and observations to be made about those returns and their interpretation should of course be entrusted to well-trained and experienced staff with a good foundation in the theory of commercial banking. In the light of these interpretations, the public authorities represented by such expert staff should be allowed to interfere and direct the commercial bank which diverts from the standards set up by the code.

This interferance should not be made with the purpose of limiting the bank's activities or putting difficulties in their way, but primarily to defend the interest of the public.

As thing exist, local Lebanese commercial banks undertake the banking business primarily for profit. Such a motive is only natural for any kind of business, including commercial banking. But this motive should not dominate to the extent of guiding banks to divert from strict commercial banking practices and enter such fields as commerce, trade in real estate, or share in the capital of business concerns, commercial or industrial. In one instance (discussed in chapter V) the bank was declared illiquid because it extended loans and advances to finance one of its co-owners who had diversified interests. Such actions should be regulated and their control should be an important aim of the commercial banking code suggested.

When public intervension in the banking business is implemented in the way suggested commercial banks will then be forced to adhere to strict banking business. In order to maximize their profits, which is their primary motive, they will have to employ better trained and more skilled officials. As things stand in most local banks, management and policy making officials are owners of the banks. In other words, management is there because it owns the business and not because it can run it most efficiently. In many cases, the owners managers know little about banking business and they rely mainly on their past experience in running their banks.

# APPENDIX I

## THE FRANC EXCHANGE STANDARD

According to the 1924 convention, the bank was authorized to carry on the operation allowed in its statute. It was to function as the official bank of the state under French mandate and accordingly it was renamed "Banque de Syrie et du Grand Liban". The note issue cover was to be equal in value to the total of notes in circulation and was to be made up as follows:

1. Gold coins or bullion or foreign government securities payable in gold. The bank, however, was under no obligation to keep any definite proportion of the reserves in this form. In fact only a small amount of gold about 3 percent of notes in circulation was usually kept.

2. a) Foreign bills of exchange bearing at least two signatures acceptable to the bank. These bills should have a maximum duration of 90 days and drawn in foreign currency on foreign or local markets.

b) Local bills of exchange bearing at least three signatures acceptable to the bank, with a maximum duration of 90 days, and drawn in Syrian-Lebanese currency.

The total value of the foreign and domestic bills was not to exceed 7 percent of the notes in circulation nor should they exceed in value the sum of one million pounds.

3. An obligatory deposit designated as "A" account in the Central Public Treasury at Paris, equal to, but not exceeding one third of the total circulation and bearing an interest rate of 1.5 percent. If the bank desires, it could also have a demand deposit at the Central Public Treasury at Paris designated as "B" account bearing an interest rate not less than that allowed by the Treasury on demand deposits of individuals.

The total value of commercial bills and the balance of "B" account was not to exceed 22 percent of the notes in circulation.

4. French Government securities or securities guaranteed by it payable within a period not exceeding two years and deposited at the bank of France.

## APPENDIX II

### GENERAL CATREAUX PROMISES

Mr. President

"I have the honour to confirm to you that following the approbation given by the Lebanese Government to the stipulations of the Franco-British financial agreement interesting the Lebanon, the French Committee of National Liberation has decided to take certain measures to the advantage of this state:

1. The Caise Central of the French Committee of National Liberation will revalorize the present deposits in Francs of the Syrio-Lebanese exchange office.

2. The French Committee of National Liberation will guarantee the institution of issue of Syria and of the Lebanon against losses which might result from the maintenance of francs presently in France in the cover of issue.

3. The French Committee of National Liberation undertakes to restore to the institution of issue a quantity of gold corresponding in weight and in fineness to the quantity of gold which constituted in June 1941 a part of the cover of the Lebanese and Syrian money.

4. In the eventuality of the rate of exchange between the French francs and the pound sterling, which will be fixed at 200 francs for a pound sterling by the new Franco-British

financial agreement, being again modified, the French Committee of National Liberation undertakes to do whatever necessary to maintain constantly the countervalue in pounds sterling of the holdings in France of the B.S.L., including those carried as cover for the note circulation in the Lebanon & Syria.

"By Vertue of this undertaking the French Committee of National Liberation, in the hypothesis of a new devaluation of the French franc as regards the pound sterling, will make good the holdings in francs in question in such a way that the countervalue in pounds sterling, calculated on the basis of the rate of 200 francs.

"Further more to comply with the wish expressed by your Excellency, I am happy to inform you that the French authorities are prepared to adjust with the Lebanese authorities the following questions:

a) The arrangement of certain stipulations concerning the institution of issue and in particular those of a nature to give to the Government an effective control over the maximum of the issues.

b) The Exchange Office, with a view to transforming it into an autonomous public service of the state, the administration of which will be confined to the Institution of issue under conditions to be determined subsequently between the state and institution of issue.

c) The exchange control which, in view of the special conditions resulting from the state of war, will be assured by a Committee including represntatives of the French Central Committee and the states.

These three questions will be treated in a way to take into consideration the legimate interests of the state s and of their nationals.

"Please accept, Mr. President, the assurance of my high consideration.

Damascus, January 25, 1944
Signed: CATREAUX.

## APPENDIX III

### BANQUE AL-AHLI

A Societe anonyme Libanaise established in 1952 under decree No. 327 of November 7, 1952 and 2712 of October 5, 1953. Initial capital LL 2 millions is increased to LL 5 millions and under decree No. 12182 of May 18, 1956 increased to 10 millions. Its capital is divided into 20,000 shares of LL 500 each. Its head office is in Beirut and it has branches in Beirut, Damascus and Aleppo.

### BANQUE BELGO-LIBANAISE

A Societe Anonyme Libanaise established in 1953 under decree No. 2496 of August 13, 1953 with an initial capital of LL. 2 millions increased to LL. 5 millions by decree No. 12017 of April 25, 1956, devided into 5,000 shares of LL. 1000 each. Its head office is in Beirut and is affiliated to the Banque de la Societe Generale de Belgique, Brussels.

### BANQUE LIBANAISE POUR LE COMMERCE

A S.A.L. established in 1949 by decree No. 326 of November 10, 1949 with an initial capital of LL. 1.5 millions increased to LL. 5 millions by decree No. 9325 of August 28, 1952 devided into 100,000 shares of LL. 50 each. Its head office is in Beirut and it has branches in Beirut, Tripoli, (Lebanon), Damascus (Syria) and Cairo (Egypt).

EASTERN COMMERCIAL BANK

Originally established as a partnership and by decree No. 6774 of March 21, 1955 was reorganized as a Societe Anonyme Libaise with a capital of LL. 1 million devided into 10,000 shares of LL 100 each. Its head office and only branch are in Beirut.

FEDERAL BANK OF LEBANON

A Societe Anonyme Libanaise established in 1951 by decree No. 6343 of October 25, 1951 with a capital of LL. 7 millions devidied into 28,000 shares of LL. 250 each. It has its head office and branches in Beirut and Ras Beirut and agencies in Bourj Hamoud - Beirut and Aly Lebanon and one Branch in Baghdad (Iraq).

INTRA BANK

Originally a partnership reorganized and established as a Societe Anonyme by decree No. 6647 of November 17, 1951 with an initial capital of LL. 6,4 millions increased to LL. 12 millions by decree No. 2711 of October 5, 1953 devided into 24,000 shares of LL. 500 each. Its head office is in Beirut, and has branches in Beirut, Ras Beirut, Beirut International Airport and Tripoli (Lebanon) Damascus, Latakia, and Aleppo, (Syria), Baghdad (Iraq) and Amman (Jordan).

BANQUE MISR-SYRIE-LIBAN

A Societe Anonyme established in 1929 by decree No. 5131 of June 4, 1929 with an initial capital of LL. 1 million increased to LL 3 millions by decree No. 6443 of November 10, 1951 devided into 60,000 shares of LL. 50 each. Its head office is in Beirut and has branches in Beirut, Tripoli and Saida (Lebanon), Damascus, Homs, Hama, Aleppo, Latakia (Syria).

BANQUE SABBAGH

A Societe Anonyme established in 1950 by decree No. 2150 of June 20, 1950 with a capital of LL. 2 millions devided into 10,000 shares of LL. 200 each. Banque de l'Indochine and Banca Commerciale Italiana have each acquired a part of the capital share of this bank. It has its head office in Beirut.

BANQUE SARADAR

Originally a private company established in 1948 and reorganized and established a Societe Anonyme in 1956 by decree No. 12784 of July 20, 1956 with a capital of LL. 1 million divided into 20,000 shares of LL. 50 each. It has its head office and branch in Beirut.

BANQUE TOHME

A Societe Anonyme established in 1942 by decree No. 1421 of October 28, 1942 with a capital of LL. 1 million divided into 20,000 shares of LL. 50 each. It has its head office and branch in Beirut.

BANQUE G. TRAD (CREDIT LYONNAIS)

A Societe Anonyme established in 1951 by decree No.4366 of March 10, 1951 with a capital of LL. 1 million divided into 2,000 shares of LL. 500 each. The Credit Lyonnais acquired part of the share capital of this bank. I has one branch in Beirut.

SOCIETE BANCAIRE DU LIBAN (ZELKHA)

Originally established in Baghdad in 1899 with a branch established in Beirut in 1927. This branch was established a Societe Anonyme in 1942 by decreeNo. 1657 of December 3,1942 with an initial capital of LL. 500,000 increased to LL. 1 million in 1946 by decree No. 5838 of September 4, 1946. Its capital is divided into 20,000 shares of LL. 50 each.

# APPENDIX IV

## SOME MAIN PROVISIONS OF AN OVER-DRAFT AGREEMENT

1. The nature of the currency in which the overdraft is allowed.

2. The maximum amount of overdraft allowed is to be set by the lending banker according to what he considers reasonable and according to his estimates of what the customer worths to be allowed to overdraw his account.

3. The agreed per annum interest rate to be charged the customer, and a statement to the effect that the interest is to be calculated at the end of every month on the end of day balance. The amount of interest thus calculated is to be added to the debt at the end of every month.

4. The date of the expiration of the agreement and a statement to the effect that on that date all debts, interest thereon, commissions and charges will fall due. The bank however has at any time the right to put an end to the agreement or change its expiration date by simply notifying the debtor by means of a registered letter ten days from which time the debtor agrees to settle all debts be own the bank.

5. The debtor may draw on his overdraft account by cheque, transfer, or against receipt.

6. In case the debtor holds any other credit account with the bank or any of its branches, the bank has the right to transfer at any time such balances to the account overdrawn

to settle the debt. In case these other accounts were in foreign currency other than that of the account overdrawn, the bank may use the free exchange rate of the day to effect the transfer.

7. All Commercial papers submitted by the debtor to the bank whether these are discounted papers or securities of any kind remains in the custody of the lending bank as additional security for the settlement of the debt. The banker may present the papers for collection on the expense of the debtor. But he is not responsible to take legal action for the collection should the need arise.

8. The bank is to submit to the debtor a statement of account every fixed period as requested by the customer. Such a statement becomes binding if within a period of fifteen days the customer presents no objection thereto.

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