

FOREIGN EXCHANGE MARKET IN BEIRUT

NABIL ADIB MUHAMMAD

Submitted in partial fulfillment of the requirements
of the degree of Master of Business Administration
in the Business Administration Department of the
American University of Beirut, Beirut - Lebanon, 1962.

FOREIGN EXCHANGE MARKET

N. MUHAMMAD

ACKNOWLEDGEMENT

The topic of this thesis was suggested to me by Dr. Harry Guenther, the Chairman of the Business Administration Department, under whose supervision and direction this thesis was written. I am greatly indebted to him for the guidance, advice and constructive criticism which he so generously extended to me during the preparation of this thesis. I am also indebted to Dr. Salim Hoss, whose un-failing willingness to consult with me are greatly appreciated. I would like to make special mention of the assistance provided to me by Mr. Anis Habiby, Foreign Exchange Manager, Intra Bank, Beirut. Recognition and thanks go to Miss Mary Hissen for the patience and the carefulness in typing this thesis. In fine, I would like to mention the fact that I accept full responsibility for all errors of fact and for all conclusions based upon the analysis and interpretation of factual material contained in this study.

ABSTRACT

The foreign trade sector is undoubtedly the important sector in the Lebanese Economy. The economic activity of the nation is mainly directed towards this sector. To realize foreign trade transactions, a country should deal in foreign exchange as a form of remittance and receipt. Besides this, an important contributor to the foreign trade sector is the foreign exchange operations as a separate activity. The existence of a free foreign exchange market in Beirut is a primary factor in activating Lebanese foreign trade. Moreover, the Beirut foreign exchange market plays an important role not only as far as Lebanon is concerned, but regarding the other Mid-Eastern countries as well. This thesis is directed mainly to discuss the institutions that comprise the Beirut foreign exchange market as well as the foreign exchange operations undertaken in the market. The study will show too the existing relationships and operations between the Beirut market and other world centres.

The study is divided into two main parts. The first part is a theoretical introduction to the subject under study. It aims at acquainting the reader to the condition in which the Beirut market is operating, and the development of foreign exchange in the Lebanese economy.

Moreover, the first part of this study introduces to the reader the terminology used in the foreign exchange market in general. This aims to help the reader to follow the discussion on foreign exchange operations on the Beirut market which will

follow in the second part of the thesis.

The second part of the thesis is a field study of the foreign exchange market and operations in Beirut. The study covers all the different operations transacted on the Beirut market together with a description of the institutions that participate in the market, stressing mainly the importance of the exchange dealers and commercial banks.

The study's value lies less in reaching conclusion than in unveiling a series of questions to scholars interested in the subject. In doing this the study will be opening new horizons for other studies to follow.

TABLE OF CONTENTS

<u>CHAPTER</u>		<u>PAGE</u>
	ACKNOWLEDGEMENT	IV
	ABSTRACT	V
ONE	INTRODUCTION	1
TWO	THE LEBANESE ECONOMY - Salient Features	8
	A. Agriculture	
	B. Industry	
	C. Construction	
	D. TRANSPORT and communication	
	E. Services	
	F. Government	
	G. Currency and monetary policy	
	H. Trade	
	K. Balance of payments	
THREE	WHAT IS FOREIGN EXCHANGE	35
	A. Introduction	
	B. Theory on Foreign Exchange	
	C. What brings foreign exchange into existence ?	
	D. How are foreign exchange rates determined ?	
	E. Foreign exchange market.	
	F. Foreign Exchange instruments	
	G. Foreign Exchange operations	
FOUR	THE HISTORY AND DEVELOPMENT OF FOREIGN EXCHANGE IN LEBANON	56
	A. Pre-Control period	
	B. Beginning of control period 1939	

- C. Exchange control regulations 1944
- D. Separation of exchange system of Syria and Lebanon
- E. The 1948 agreement with France
- F. Official recognition of foreign exchange market
- G. Free market era

FIVE THE BEIRUT FOREIGN EXCHANGE MARKET PART I 67

- A. Introduction
- B. Exchange dealers
 - 1. Introduction
 - 2. Banknotes operations
 - 3. Bills of exchange operations
 - 4. Handpayment operations

SIX THE BEIRUT FOREIGN EXCHANGE MARKET PART II 92

- A. Commercial Banks
 - 1. Introduction
 - 2. Foreign Exchange dealings
 - 3. Functions of the foreign exchange manager
 - 4. Role of the U.S. dollar in the market
 - 5. How the exchange rate is born ?
 - 6. Foreign exchange policies
 - 7. Forward exchange operations
 - 8. The brokers
 - 9. Exchange market sanction
 - 10. Role of Banque de Syrie et du Liban in the foreign exchange market.

SEVEN	FUTURE OF THE FOREIGN EXCHANGE MARKET	116
	A. Summary	
	B. Conclusion	
	1. Future of the market through the analysis of Lebanon's balance of payments	
	2. Banking system and the foreign exchange market	
	3. The introduction of the telex	
	4. The Forex Club	
BIBLIOGRAPHY		135
Appendix A	Foreign Exchange terminology	139
Appendix B	Currencies of the world	142
Appendix C	Exchange regulations in the Sterling Area and French franc area	148
Appendix D	Banks in Lebanon	152

LIST OF TABLES

<u>TABLE NUMBER</u>		<u>PAGE</u>
11	Classification of land in Lebanon	11
2	Badre's estimate of national economic	12
3	Number of vehicles	11
4	Budget for years 1950 and 1960	24
5	Note in Circulation	27
6	Note cover	27
7	Money and Credit in Lebanon	29
8	Lebanese Arab Trade	34
9	Balance of payment 1951 - 1959	127

LIST OF EXHIBITS

<u>EXHIBIT NUMBER</u>		<u>PAGE</u>
1	Personal Letter of Credit	98
2	Swap contract	108

CHAPTER I

I N T R O D U C T I O N

KNOWLEDGE IS THE ONLY
INSTRUMENT OF PRODUCTION
THAT IS NOT SUBJECT TO
DIMINISHING RETURNS

J.M. CLARK

Entree en Matiere could be considered one of the difficult tasks that face any author when starting to write about any subject. This is merely because ideas rush to pass through the bottleneck, the opening sentence. But the introductory chapter of any study is its mirror and should always reflect discipline and precision in thinking and presentation.

The study of foreign exchange is the study of the means of settling the indebtedness or debts between nations which arise principally from international trade, and the fluctuations in the price of the various forms of remittance used to settle these debts. This study aims to scrutinize and describe the activities of the different institutions dealing in the Beirut Foreign Exchange Market. This thesis is significant because of the lack of similar studies on the subject and the lack of understanding of institutional aspects of foreign exchange in Lebanon, even in academic and other professional fields. It is also significant as a guide to the study of the set-up of the Lebanese economy in general because of the outstanding role played by the banking system and the foreign sector in the Lebanese economy. Both these sectors are cause and effect as far as the foreign exchange market is con-

cerned. This fact will be exhibited as the reader proceeds in reviewing the study.

The study depended mainly on field research and primary sources. The writer, in his capacity as a member in the exchange market was able to make all necessary contacts to obtain information, and, in addition he has had wide personal experience in this respect. The collection of data was either through personal interviews or telephonic contacts, the main means of communication in the market. Moreover, the first part of the study depended mainly on secondary sources in books, reviews, and unpublished studies and research.

The paucity of statistics on the volume of foreign exchange transactions carried out through Beirut, renders the best estimate of volume a mere guess, which made any such effort a waste of time and effort if not a misleading guide to the reader; and as it has been said, there are three kinds of lies; lies, damned lies and statistics

Accordingly, a significant limitation to the study was the lack of statistical data. The lack of previous studies on the subject handicapped the research and made this paper a pioneering work. Moreover, organized bodies in the market which could have provided compiled information do not exist.

Following this introductory chapter, the study will discuss throughout Chapter II in a brief and condensed form the main features of the Lebanese economy to acquaint the reader with the country in which the Beirut exchange market is located. Besides the geographic

characteristics of the country, the Lebanese economy will be discussed sector by sector, stressing wherever needed the improvements that were realized in recent years as well as points that are directly related to the study. This chapter will be noted too for the number of tables that it contains exhibiting the various phases of activity in Lebanon in the last decade.

Chapter III aims mainly to acquaint the reader with foreign exchange in general. The reader will become familiar with the terminology in the foreign exchange market. Moreover, the various foreign exchange operations are introduced. This chapter will discuss the theory of foreign exchange and how foreign exchange comes into existence. Furthermore, it will discuss how the foreign exchange rates are determined and the rates fluctuations. The chapter will spot-light the set-up of the foreign exchange market and different instruments used during its daily business. Reading through this chapter the reader will be able to follow the study on the Beirut market.

In Chapter IV the study will review the different stages through which the foreign exchange market in Lebanon had to pass during the last twentyfive years or so. The survey starts just before the Second World War and discusses the various rules and regulations set-up by the authorities to restrict the foreign exchange market and the development of the market until all the regulations were released one after the other, up until 1952 when the Beirut foreign exchange market became, de facto and de jure, free. The study will give some attention to the condition prevailing when Syria and Lebanon were considered one monetary area

using LLS. as its currency, and how this unity came to end when each country followed a different monetary policy in its dealings with the ex-mandatory power, France. The termination of the economic unity between the two countries in 1950 is also discussed.

The foreign exchange market in Beirut is discussed in two separate chapters. Chapter V discussed the exchange dealers in the market and Chapter VI discusses the commercial banks. These two institutions together with the brokers form the Beirut foreign exchange market. Chapter V, starts by defining the exchange dealers to differentiate between them and commercial banks. This is because there are several organizations in the Beirut market which carry the name and official charter of banks but only work in their capacity as exchange dealers. This chapter discusses too the mode of work exchange dealers follow, the role of the U.S. Dollar in the market, explaining why the Beirut market is known as a dollar market. The media of communications in the market are also discussed here. At this juncture the role of the broker is explained showing his work in the market. The rest of the chapter is divided into three parts according to three main classifications of operations, the exchange dealer undertakes. These are namely foreign notes and coins operations, bills of exchange operations and handpayments operations. Under every classification the forces of supply and demand are scrutinized. An elaborate review of the currencies transacted under every classification is also discussed. All the necessary examples to clarify the different transactions are presented, although when discussing the third classification examples were not elaborate due to the secrecy that encloses such operations.

In Chapter VI, the study of the market centers around the role of the commercial banks in the foreign exchange market. The banks participate in the market in two aspects, the banking activities that result in foreign exchange, and the foreign exchange operations. The Beirut banks exchange operations are of two types: those that are similar in nature and, most of the time, in magnitude, to the exchange dealers' operations; and those operations that are the sole characteristic of the banks in foreign exchange dealing on the Beirut market. The latter can be best illustrated by the forward exchange operations, namely swaps. A great deal of attention is also given to the role and functions of the foreign exchange manager in the commercial bank. A thorough discussion is devoted to the daily routine of the manager and how he undertakes his obligations. Accordingly, the study shows how he calculates the rates of exchange and at this point the role of the dollar in the Beirut market is explained. Then the study discusses the foreign exchange policies of banks and the reasons behind such policies as well as the dealings that result from following one policy or another and how attitudes of banks change as their foreign exchange balances change in magnitude and composition. In this chapter too the role and functions of brokers is discussed, but this time it pertains to their role in dealing between banks as well as between banks and merchants or exchange dealers. The study shows as well the marginal commission brokers earn on transactions they complete. The latter part of the chapter is devoted to the discussion of the role of the Banque de Syrie et du Liban in the foreign exchange market. In this

respect the Banque de Syrie et du Liban is shown in its capacity as a central bank and representative of the government and/or the Stabilization Fund in market operations to stabilize the exchange rate of the Lebanese pound. The last chapter in this thesis includes two parts. The first part summarizes the study undertaken in this thesis. The second part is a review of the future of the foreign exchange market in Beirut; sketching out the trends prevailing in the market at present.

Several appendices follow to familiarize the reader with some technical terminology pertaining to the foreign exchange market. Therefore, Appendix "A" presents some foreign exchange clauses, and terms, Appendix "B" contains the names and denomination of the world currencies, Appendix "C" contains the exchange restrictions in two major areas, the French Franc Area and the Sterling Area and Appendix "D" contains the names of banks in Lebanon. Such appendices contain material that could not be contained in the text of the thesis but still of interest and of importance to the student of foreign exchange.

If the writer appears guilty of over-emphasis and repetition here and there he prays forgiveness. In a desire to impress certain facts clearly in the minds of his readers, there may appear a certain measure of over-emphasis to some readers but it is confined to points of vital importance that are only given their due consideration. Where the present tense is employed in describing exchange practices or economic conditions, an effort has been made to reflect the situation as it existed during the

first half of the year 1962.

The author has not cited a reference for every one of the many factual statements made in this thesis. This is because the information has been gathered from unpublished sources and mainly interviews with businessmen in the field, who prefer to remain anonymous. To these men I extend my deep gratitude.

CHAPTER II

THE ECONOMY OF LEBANON: SALIENT FEATURES

NORMALLY THE ECONOMIC
ORDER IS A FUNCTION OF
THE SOCIAL ORDER IN WHICH
IT IS CONTAINED.

KARL POLYANI

Lebanon is an Arab Republic situated on the crossroads of 3 continents which made of the country commercial outlet of the Middle East. This geographic position plays a great role in molding the economic features of the country.

Lebanon has an area of about 10,380 square kilometers and an estimated population of 1,700,000.¹ This brings the density of population per kilometer to a figure of 160 persons per square kilometer.

About one third of the population are concentrated in the capital city of Beirut. "Considering the density of the population its standard of living, the paucity of natural resources, and limited development possibilities, the country must be regarded as over-populated".² Nonetheless, Lebanon enjoys a significantly higher standard of living than almost all its Middle East neighbours. The country enjoys diverse climatic conditions, and is divided into four regions. First are the coastal plains which have Mediterranean

1. No census has been taken since 1932. Political reasons prevent such a census from being undertaken (I.F.S. estimated Lebanese population to be 1,646,000 in 1961, I.F.S. Vol.XIV No.10 Oct. 1961)

2. IBRD, Report on the Economy of the Lebanon, No.E45 WASHINGTON D.C. 1948, revised June 8, 1949 p.3. (TYPESCRIPT).

climate and agricultural production. Second, there are the Lebanon Mountains which are characterized by snowy winters and heavy rainfall. This region enjoys a wide range of altitude and cultivation. Third is the Beqa'a region, a plateau which supplies the country's major agricultural production. Fourth is the second mountain range (ANTE LEBANON) which forms the geographical eastern boundary with Syria. This area is largely barren.

The country is endowed with scarce water resources. The only river worth serious consideration for its potentialities in producing hydro-electric power³, is the Litani River in the Southern Lebanon. The proven mineral resources of the country are of no significance.⁴

The last but on no ground the least feature of the Lebanon is its natural beauty. As it will be shown on the following pages this feature is responsible for the generation of a major sector in the national income of Lebanon.

MAIN SECTORS OF THE ECONOMY

AGRICULTURE

At present only 25% of the total area is under cultivation (3880 km²) although some studies show that if irrigation works are carried out this area can be raised to 50% of the total area. A wide variety of crops are being cultivated because of the aforementioned topography and of the climatic conditions to which it gives rise. Thus, tropical fruits such as bananas and sugar-cane

3. A dam is being under construction to regulate irrigation and produce electric power.

4. The search for petroleum proved to be a failure.

are grown along the coast, whereas a wide range of fruits of the temperate zone, mainly apples, are grown on the mountain slopes while cereals, grapes and vegetables are grown in the inland valleys, e.g. the Beqa'a.

The agricultural land of Lebanon is parcelled out into a large number of very small holdings and a small number of relatively larger areas.⁵ Most of the farmers own the land they cultivate. Thus the case of the agricultural labourers which forms a major problem in the other Middle Eastern countries is almost negligible in Lebanon. These labourers only form 10% of the total farming population.⁶ This is significant for the social set-up of the country and is to be kept in mind when studying the per capita income of the country.

Agriculture contributes LL.219 million to the National Income while it contributes about 50% of exports, mostly fruits.⁷ Meanwhile, the importation of agricultural products is considerable. This is simply because the country's agricultural production does not cope with the increasing population.

Lebanon at the same time, is developing export surpluses in fruits and vegetables and it is believed that fruit growing is one of the most promising development projects in Lebanese agriculture.

5. U.N. Dept. of Economic and Social Affairs, Land Reform and Defects in Agrarian Structure as Obstacle to Economic Development, (Sales No.195/11 B.3, New York 1957) p.154.

6. Conference on Agricultural Credit, Report on Agricultural Credit in Lebanon, Beirut Oct. 1953 p.5

7. See Table 21.

TABLE I
Classification of Land in Lebanon

<u>TYPE OF LAND</u>	<u>THOUSAND HECTARS</u>
Cultivated Area	273
Irrigated	98
Rain-Fall	225
Cultivable but uncultivated	115
Forest	74
Rocky and Waste Areas	556
Other	19
	1037

Source: Conference on Agricultural Credit. Report on Agricultural Credit in Lebanon. Beirut 1953.

TABLE 3

Lebanon: Number of vehicles as at December, 60 - December, 1961

	<u>Dec. 1960</u>	<u>Dec. 1961</u>
Private Automobiles	43975	53475
Taxis	3200	3200
Autobus	1361	1519
Trucks	6836	7651
Motorcycles	4450	5005

Source: Lebanese Government: Bulletin statistique trimestriel, March, 1961 and March 1962.

TABLE 2

LEBANON : BADRE'S ESTIMATE OF NATIONAL INCOME

1950 - 1958

(in million of L.L.)

	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>
TRADE	300	337	333	344	368	407	410	469	365
AGRICULTURE	206	211	216	221	226	223	231	238	219
OWNERSHIP OF BLDGS	96	97	98	101	112	116	130	139	155
INDUSTRY	141	147	155	161	166	175	183	189	181
SERVICE	100	103	106	122	134	165	160	168	104
CONSTRCTIONS	43	35	48	47	60	60	50	41	38
GOVERNMENT	72	64	64	71	73	83	95	108	113
TRANSPORTATION	44	46	45	50	60	75	78	80	57
FINANCE	40	46	50	51	57	70	80	91	93
	<u>1042</u>	<u>1086</u>	<u>1115</u>	<u>1168</u>	<u>1256</u>	<u>1375</u>	<u>1417</u>	<u>1503</u>	<u>1325</u>

SOURCE: Albert Y. Badre as reported in the United Nations, Year Book of National Accounts Statistics, 1958 - 1959
 and in the Food and Agriculture Organization, Mediterranean Development Project, Lebanon, Rome, 1959
 p. 11-13 Unpublished dissertation, The Roles of Central Banking in Lebanon, By courtesy of Prof. Salim Hoss.

The existence of a number of bilateral trade agreements illustrate the interest of the Lebanese government in opening new markets for Lebanon's fruits and vegetables.

INDUSTRY

Judging from the 1958 figures, Lebanese industry contributes about 14% to the National Income, amounting to LL.181 million.⁸

Before the First World War, Lebanese industry was composed of weak and poor handicrafts. The severe competition of the industrial goods signaled the dying away of the handicrafts industry. By 1952 substantial investments were being attracted by new industries such as the textile, cement, soap, tanning and food industries.

It was not until the Second World War that industry received a stimulating impetus under extraordinary conditions and unlimited demand. The windfall profits of that period were reinvested into the industry. The Middle East Supply Centre contributed to the initiation of industrial progress during that period. Once peace was regained demand declined and a slack started in 1946 resulting in idle capacity in most of the existing firms. Industry had to reorient itself to the new conditions. The loss of Palestine in 1948⁹ and the breakdown of the economic union with Syria put Lebanese industry into a tight position. But the prosperity that started in the early fifties in the oil countries of the Arab Gulf and in Saudi Arabia compensated for the loss and later led to

8. See Table 2.

9. A market and a competitor at the same time.

the prosperity that industry is enjoying at present.

The circles interested in development of the Lebanese economy have industry as their main concern in their discussions. A wide variety of viewpoints have been introduced as plans to solve the problems of Lebanese industry.

Some observers believe that Lebanese industry will not gain from a protective policy. This is because the foreign imported goods and the Lebanese products do not share a common market. "The opposition of trade to industry lies in the former's fear that protection might reach such a height as to strangle trading opportunities and dry up trading gains without in the end necessarily guaranteeing a viable industry. The official policy has so far been a dual one of reducing tariffs on machinery and industrial raw material, and providing a reasonable degree of tariff protection against manufactured goods the like of which are produced in Lebanon".¹⁰ The aim of this policy is the progressive coexistence of industry and trade. A policy of a fair extent of industrial expansion without destroying the country's lucrative internal as well as transit and triangular trade.

Two recent developments have occurred which will go some distance in helping industrial expansion. These are the establishment in 1953 of the Industrial Institute for the purpose of research, analysis, study of standards and similar operations purporting to be of assistance to industry, and the establishment

10. Sayigh, Yusif, A., Economic Development of Lebanon
(Johns Hopkins University October, 1955 (Mimeograph))
p.22.

in 1954 of the Agricultural Industrial and Real Estate Credit Bank to furnish these sectors with the medium and long term credit which they cannot obtain from the existing commercial banks.

The vast majority of the industrial establishments are of small-size.¹¹ The total number of these establishments is 1861 engaging 35013 persons. Moreover, the 1955 industrial census estimated cash receipts to be LL.399,503,000 while the value added was calculated to be LL.154,879,000.¹²

One can sum up the industrial sector to classify it under the following industries:-

1. Mining and quarrying
2. Foodstuffs and beverages
3. Textiles
4. Foot-wear and wearing apparel
5. Furniture, fixtures and wood manufactures
6. Printing and publishing
7. Chemicals and chemical products
8. Products of petroleum and oil
9. Metal and machinery manufacturing
10. Non metallic minerals production.

CONSTRUCTION

It is a characteristic of Lebanon, as of underdeveloped countries generally, that a large part of new investments goes into construction. People view buildings as a safe long-lasting form in

11. These were 1129 individual proprietorships, 659 general partnerships, 28 limited partnerships, 38 corporation and seven other forms of ownership.

12. Badre, Albert and Asad Y. Nasr, National Income of Lebanon, Income arising in the Industrial Sector (Beirut May 1953), (Typescript).

which to invest savings. Moreover, a large part of the capital coming from abroad is being invested in construction. In 1958 about 3% of national income arose in the construction sector, i.e. 38 millions,¹³ but it had an importance beyond this proportion for a number of reasons.

1. It represented over one fourth of the annual net investment in Lebanon.
2. It is the sector in which wages absorb the highest proportion of income in any sector of the economy. It is one of the most mechanized activities as well as one in which wages are high owing to the skills, the physical strain and the risks involved.
3. Most of the materials needed are produced locally except elaborate sanitary fittings, fancy tiles and iron beams.¹⁴

At present it is a leading sector in the boom. If activity slackens in the construction business in the coming future, it will place economic prosperity under severe strain.

TRANSPORT AND COMMUNICATION

This sector of the economy reflects the importance Lebanon is giving to the promotion of services. Transport and communication accounted for LL.57 million of the national income in 1958.¹⁵ With the exception of railways, the means of communication are rather modern and efficient. The country being small and distances short, railways are not being given serious interest. The lines in the

13. See Table 2.

14. Sayigh op.cit. p.26

15. UN Statistical year book 1960. Also refer to Table 2 where one can notice that this sector contributed LL.80 million during 1957.

country were either built by the British Army during the Second World War or during the French Mandate. The Beirut port, already full with activity, has been drawing and handling a steadily increasing tonnage in recent years. The average number of ships cleared during 1961 was over three hundred a month and an average of 400,000 tons of goods were handled.¹⁶ It is worthy to note at this juncture that the opening of Latakia Port and Akaba Port in Syria and Jordan respectively did contribute to diminish the transit activity through Beirut port.

Beirut International Airport which is a first class aerodrome is another factor in promotion of the services sector by stimulating tourism. Air traffic has been increasing steadily during the past few years.

The number of automobiles have been steadily increasing in Lebanon which makes it necessary to give special attention to roads and highways. Several highways were built in the country through cooperation of the Government and U.S. Point Four Mission.

The telegraphic service, a concession of Radio Orient, is adequate and efficient. The telephone service is not at it should be. It is not expanding with the growth of the country. Only in 1954 did Lebanon install its automatic exchange in Beirut. Since then some improvements have been added.

SERVICES

This sector involves the largest number of non-Lebanese

16. Lebanese Government, Bulletin statistique trimestriel Beirut, March 1962

17. Sayigh op.cit. p.40

thousands of whom come for education and hospitalization or vacationing and tourism.¹⁷ These contribute substantially to the country's foreign exchange earnings. The services contribute to cover the deficit in the balance of payments that results due to the deficiency in the trade account. Lebanon, giving considerable weight to tourism and travel, is keen to keep travel, foreign exchange and importation restrictions to a minimum. In fact, in case of estimate the government has gone as far as to subsidize partly or wholly the travel expenses of visitors coming from Arab countries. To promote this sector the Government encouraged the establishment of the Casio du Liban, a magnificent entertainment center boasted to compete with Casino Monte de Carlo. Hotels are being given encouragements to improve their service. New hotels construction has been encouraged too.

THE GOVERNMENT

This sector comprises the central government, the municipalities, and the autonomus administrations or departments (such as the telephone services, the national lottery, and the commissariat of tourism). The income arising from this sector, which was about LL.113 million in 1958¹⁸, is virtually all salaries and other employee emoluments. Table 4 shows the growth in government expenditure.

The ordinary budget of Lebanon is usually balanced or nearly so, with revenue exceeding expenditures when inbalance exists. This

17. Sayigh op.cit. p.40

18. UN Statistical year book 1960 and refer to Table 2.

is partly an adoption of good individual budgeting to state budgeting, partly an honest desire to build-up sizeable reserves of annual surpluses, from which to finance development projects and to meet emergencies, partly as a safeguard against a low level of tax collection, so that there may be enough revenue to match the expenditures committed,¹⁹ and partly a failure of the Government to be aggressive and decisive, Table 4 clearly shows the major sources of revenue, the highest income arising from customs duties. The tax machinery is inefficient in Lebanon and two years ago a project was submitted to the Chamber of Deputies demanding the cancellation of income tax as the expenses incurred are not justified by the tax collected. Objections on theoretical grounds have been levelled at the iniquitable distribution of tax burdens, due to the predominance of indirect taxes.²⁰ In the absence of a thorough

19. Sayigh, op.cit. p.24

20. It must be noted that most of the indirect taxes are levied on such commodities as table salt, sugar, tobacco, alcoholic drinks and combustibles. These commodities do not have close substitutes and their demand is therefore expected to be inelastic in the relevant range of prices. Because such taxes tend to raise considerably the prices of the products taxed, and thus weaken their competitive position vis-a-vis foreign products, they are usually followed by high import duties designed to protect the domestic industry thus taxed.

Badre, Albert and Asad Y. Nasr, National Income of Lebanon, Income Arising in the Government Sector (Beirut: Economic Research center of A.U.B. November, 1953) (Typescript) p.25.

Also see Himadeh, Raja S., The Financial System of Lebanon (Beirut: Khayat's Bookshop, 1961) Chapter VI on Indirect Taxes.

examination of this issue, it would seem that the following opinion on indirect taxation is quite sound. Such methods of taxation have for an immature government obvious and compelling advantages. They require much simpler government machinery and are easier to collect than does the income tax which calls for more satisfactory tax morality than seems to prevail in many underdeveloped countries such as Lebanon.²¹

The civil service is heavily centered in Beirut. Centralization is high, in part owing to the smallness of the country and the practicability of focusing authority in one place, and in part because it is not thought very efficient and administratively reassuring to delegate and diffuse authority. As a result, the wheels of government move heavily and slowly and at times, inefficiently.²²

LEBANESE CURRENCY AND MONETARY POLICY

The Lebanese currency is a paper inconvertible currency, whose unit is the Lebanese pound (LL) divided into 100 piasters. In terms of gold, its par value is 0.405512 grams of fine gold per currency unit and its par value in terms of US. Dollar is 2.19148.²³ This was established in July 29, 1947.²⁴ The life cycle of the Lebanese pound can be divided into five phases.

21. Albert, Badre, op.cit. Monograph No.5 p.24

22. Sayigh, op.cit. p.42

23. IMF, Schedule of Par Values 13th issue; (Washington, DC, 1960) p.3

24. Ibid, p.3

1920 - 1926

During this period the French Franc fluctuated widely. This resulted in similar fluctuations in Lebanon-Syrian Pound (LLS) as shown in Table 5. This is because the LLS. was covered by the French franc.

U.S. Dollar	was	54.7	PLS.	on	April,	1922
"	"	"	202.8	"	July,	1925
"	"	"	127.5	"	August,	1926

This naturally had severe effects on the economic conditions of the country. To lessen the evils of fluctuation, measures were taken to permit the use of foreign money as the standard of deferred payment for all contracts of over 5 days term.

1926 - 1936

The French franc was de facto stabilized in September, 1926 but actually de jure not before 1928. It was established at 0.0635 grams of gold 900/1000 fineness or at about 1/50 of its value in 1920. This conditions of stability lasted for ten years.

1936 - 1941

During this period the French franc left the gold standard to depreciate and with it went the LLS. On February 29, 1940 the franc was quoted at 0.02334 grams of gold or in other words 8% of its value in 1920.

1941 - 1948

The fourth period 1941 - 1948. During the period of World War II, Lebanon and Syria were occupied by the British and Free French Troops. The LLS. left the franc exchange standard. The Franco-Lebanon-Syrian Agreement of February 9, 1944 sanctioned this

step and guaranteed the franc assets of the LLS. in terms of Sterling. During this period Lebanon was part of the Sterling Area.

1948 to Present

The milestone of the fifth period in the life cycle of the Lebanese pound is the Franco-Lebanese Monetary Agreement of 1948. It is of significance to point out here that during the twentyfive years 1920-45, the franc fell in value by more than 97.5% to the extent that on July, 1945, the French franc was devalued for FF.176 to FF.200 per Sterling pound. The Lebano-Syrian pound's value became 1 to FF.22.65 and on December of the same year the franc was devalued again to FF.480 per Sterling pound and Lebano Syrian pound became 1 to FF.54.35.

THE 1948 Agreement

This monetary agreement between France and Lebanon established the monetary condition between the two countries as follows:-

1. A ten year Sterling exchange guarantee for balances in the note cover only, (these were 67.30% of the total franc assets) but these balances had to be blocked until 1953 after which date they were to be released in annual instalments.
2. Capital transfers from Lebanon to the French Monetary Union were to be free from any restrictions. Transfers in the opposite direction were subject to French exchange control.
3. Settlement of all transactions between Lebanon and French Union were to be made in French franc or Lebanese pound.
4. Trade facilities were provided.

5. The exchange control office of April, 1944 was to be replaced by mutual agreement so as to promote the good functioning of financial relations between Lebanon and the French Union.

The Lebanese pound is issued by the Banque de Syrie et du Liban which has a concession ending in 1964. It acts as a central bank but at the same time handles ordinary commercial credit operations. By the end of 1948 official holdings consisted of \$.1.7 million worth of gold and \$.72.4 million worth of French francs and French securities. Since then however, the composition of the holdings has changed considerable. Although the law requires no more than 30% of gold in the cover the proportion now is 92%.²⁵ Objections were raised against this high proportion of gold cover because of the rigidities in currency issue and credit expansion which cause deflationary pressures. These arguments are outside the scope of the paper for the time being.²⁶

The financial institutions in the country have had an unbalanced growth, with commercial credit banking well-developed and quite adequate but with agricultural, industrial and real estate credit banking very much short of the needs. Saving institutions too, are virtually non-existent. This is both a reflection of the trade lines in the economy and a cause of it. The two partly explain and partly complement each other. The distribution of banking institutions is also very uneven, with

25. Bulletin Statistique Trimestriel March 1962.
op.cit.

26. Refer to Tables 5 and 6.

TABLE 4
BUDGET FOR YEARS 1950 AND 1960¹⁾
(IN MILLIONS L.L.)

<u>ITEM</u>	<u>1950</u>	<u>1960</u>
Expenditures	90.05	222.24
EDUCATION	9.76	30.84
HEALTH	4.58	10.56
DEFENCE	17.99	47.44
PUBLIC WORKS	15.48	37.85
OTHERS	42.24	95.55
RECEIPTS	105.31	222.24
INCOME TAX	11.31	22.00
Tax on Buildings	3.75	10.00
Automobile tax	1.25	3.60
Registration duties	8.24	22.67
Other indirect taxes	34.48	39.38
Other receipts	12.75	47.06
Custom duties	33.53	77.58

SOURCE: UNITED NATIONS STATISTICAL YEAR BOOK, 1960

¹⁾ The fiscal year in Lebanon coincide with the calendar year.

a heavy clustering in Beirut and only a bare minimum in a few other towns, and none in the other urban and rural centres.

In 1962, Beirut had 70 Banks of which 52 were domestic, 6 non Lebanese Arab and 12 foreign non Arab including the commercial section of Banque de Syrie et du Liban. Included among the national banks are 21 "banks" mainly dealing in foreign exchange, besides discounting bills at high interest.

TRADE

The most distinctive feature of the Lebanese economy is the preponderance of the trade sector over the other sectors. "The channelling for centuries, of an important part of Middle East commercial and financial operations through Lebanon created an experienced class of merchants, entrepreneurs and bankers.²⁷ In more recent years, with excellent contacts abroad, a fluency in foreign languages and trading techniques, a keenness for opportunities both in supply and in demand markets, and an accommodating brisk financial market, Lebanese merchants have handled large quantities of goods, their own and other countries', both in two-party and in triangular trade.²⁸ The income arising in the trade sector in 1950²⁹ is as follows:-

Import Trade	40%
Entrepot	5 %
Transit Trade	20%

27. IBRD., The Economic situation and Credit worthiness of Lebanon, (Washington; D.C. AS2, 1952)(Typescript) p.4.

28. Sayigh, op.cit. p.27.

29. The only available and reliable figures were those reached by the staff of the Economic Research Institute of A.U.B. in 1950.

Export Trade 3 %
International Trade 32%

The first three items which account for 65% of the total, represent goods of foreign origin, which goes far to explain the often-expressed anxiety that the country has an excessive dependence on foreign supplies, the freedom of seas, and on the market of those countries for which transit and entrepot goods are destined.

Lebanese trade relations with the Arab countries is of significant importance. Lebanon imports between one-fourth and one-third of its total imports from the Arab countries and its exports to those same countries represents an even higher proportion, almost one-half of total exports. The Arab countries are such important clients of Lebanon that keeping its volume of trade with them is a powerful stabilizing factor for the economy. With annual income from oil in the oil-producing region running well beyond the half-a-billion dollar mark, the role of Lebanon as a trade and middleman to the Saudi Arabian, Kuwaiti, Bahreini, and Qatari markets can become increasingly useful and lucrative. ³⁰

Trade relation with non-Arab countries are also receiving increased attention. Several bilateral trade treaties have so far been entered into, some with western European countries, others with countries of the Eastern block. Agreements with European countries

30. Sayigh, op.cit. p.31

TABLE 5
LEBANON: NOTE IN CIRCULATION
AS AT DECEMBER, 1960 (LL. MILLION)

	<u>Dec. 1960</u>	<u>Dec. 1961</u>
NOTE IN CIRCULATION	437	443.419
BANK NOTE	431	437.000
SILVER COINS	2.20	2.291
METAL COINS	2.970	3.092
	1.040	1.036
INDEX (1939 = 100)	1925	1952

Source: Lebanese Government - Bulletin Statistique Trimestriel
March, 1961 and March, 1962

TABLE 6
LEBANON: NOTE COVER
AS AT DECEMBER, 1960 - DECEMBER, 1961 (LL. MILLION)

	<u>Dec. 1960</u>		<u>Dec. 1961</u>	
Gold	399	92%	399	91%
Foreign Exchange	-	-	-	-
Others	32	8%	38	9 %
Total	431	100%	437	100%

Source: Lebanese Government - Bulletin Statistique Trimestriel,
March, 1961 and March, 1962

are bilateral in form "more in the nature of an advertising medium which indicates to the other party what commodities are available for sale and what commodities are needed, than binding bilateral trade compacts."³¹

In a country which greatly depends on income from foreign trade and where (due to administrative laxity) it may not be easy to carry out a strict control of foreign trade operations (especially where a separation between imports for local consumption and imports which are eventually exported is involved), there is a more or less natural reluctance to introduce strict foreign trade restrictions. The liberalization of foreign trade paralleled the development in the relaxation of exchange controls. This freedom of trade has been very instrumental in establishing the country's position as the main entrepot trade and tourist centre in the Middle East.

The great majority of tariffs in Lebanon are specially imposed for revenue purposes and not for protecting local productions. These categories of tariffs may be indentified.

1. Maximum tariff usually applied to imports from certain non-members of U.N. and which is normally equivalent to about twice the ordinary tariff.
2. Ordinary tariff which normally applied to imports from U.N. members as well as from certain privileged non-member countries.
3. Preferential tariff which applies to imports from countries which have signed with Lebanese trade ~~agreements~~ to this effect.
agreements

31. Economic Research Institute, Business Legislation in Lebanon, Beirut 1956 p.60

TABLE 7

LEBANON: MONEY AND CREDIT IN BANKS
AS AT DECEMBER, 1960 - DECEMBER, 1961 (THOUSAND L.L.)

<u>ITEM</u>	<u>Dec. 1960</u>	<u>Dec. 1961</u>
DEPOSITS		
Deposits in Leb. pounds	1,068,778	1,220,222
a. Time deposits	113,386	138,443
b. Current accounts	955,392	1,081,779
DEPOSITS IN FOREIGN EXCHANGE	376,301	459,629
a. Time deposits	53,690	72,030
b. Current accounts	322,611	387,599
Total Deposits	1,445,079	1,679,851
ADVANCES		
Advances in L.L.	763,570	842,640
Advances in F. exchange	147,675	146,352
Total Advances	911,245	988,992
BILLS DISCOUNTED IN L.L.	232,885	265,106
BILLS DISCOUNTED IN F. EXCHANGE	11,578	15,101
Total Bills Discounted	244,463	280,207

Source: Lebanese Government Bulletin Statistique Trimestriel 4th quarter
1960 - 4th quarter 1961.

The ordinary tariff is the most important. It usually consists of an ad-valorem duty of 25% and calculated on the basis of official rates of exchange which are only about 2/3 of free rates actually paid by the importer.

The Free Zone was started by the French Authorities in the thirties. It never attracted considerable business due to the strong economic competition of Haifa, until Haifa was closed down to Arab countries after the outbreak of hostilities. Development of the Free Zone is attributed also to the recent development in the Arab countries, whether through oil riches or agricultural progress. The Beirut Free Zone is the entrepot centre of the Middle East, where transit trade entrepassage,³² commodity arbitrage and switch operations are made.

THE BALANCE OF PAYMENTS

The Lebanese balance of payments and indeed the whole economy has shown considerable resilience during the last fifteen years, riding out two or three crises without grave consequence. The Allied Armies expenditure in Lebanon and Syria dropped suddenly in 1946-47, and yet the balance of payments of the Syrian Lebanese area, estimated to have shown a surplus before the war under the mandatory regime, recovered very rapidly from that blow. In 1950 when the Syrian Lebanese customs union terminated and traditional outlets for Lebanese exports of goods and services, as well as convenient sources of basic commodities seemed to be imperiled, yet the surplus in the Lebanese balance of payment increased thereafter. A third crisis that may be mentioned here is the civil commotion of

32. Entrepassage is either done on Lebanese territory or more often in the Free Zone, where goods, mainly agricultural, undergo a transformation process.

1958. This crisis did paralyse the country's economic life for six months or so. Still the country's economy could regain its strength and vitality soon after normal conditions were established.

For an evaluation of the Lebanese balance of payments it should be admitted from the start that the balance of payments is in a fairly satisfactory shape despite the heavy annual deficits that are recorded in the trade balances. These surpluses nonetheless do not fore-shadow the many weaknesses in the balance of payments.

The first weakness is the heavy dependence on sources of revenue which are highly precarious and unstable, such as services rendered to foreigners.

- a. exchange transactions
- b. triangular trade operations
- c. transit trade
- d. tourism and estivage
- e. grants and remittances

Many of such services are the result of disparities in exchange control regulations of the various countries and are thus unstable sources of revenue. It may be sufficient for only a mild international crises, or for even a local crisis which results in a more strict application of exchange in any one of the countries where Lebanon's tourists, ~~dancers~~ or emigrants are located, in order that capital in-flow from such sources may be appreciably reduced.³³

33. It is interesting to note at this juncture that the foreign exchange market may benefit from such exchange restrictions as will be shown later in this study.

The second weakness is the dependence on capital movements, "hot" in nature, which very frequently remain in Lebanon for refuge in the form of current accounts in the local markets pending its ultimate withdrawal for investment in other more politically stable countries (namely to U.S.A, and Switzerland). If kept in the country as a current account, it can be withdrawn from the country with insufficient notice, to the possible detriment of the country's bank liquidity. But if on the other hand, they are invested in outlets such as real estate, they are not beneficial to Lebanon's economic growth.

The third weakness is the recent reduction in the country's revenue from gold transit. This is because of new restrictions executed by India and China, and because of the sale by the Union of South Africa of large quantities of gold on the free markets of the world.

Mentioning the points of weakness in the balance of payments does not under any condition dwarf the signs of strength in the balance. As a matter of fact, Lebanese balance of payments is quite healthy.

The first sign of strength is the increase in export trade due to developments in agriculture and to the conclusion of bilateral trade agreements.

The second sign is the stability of revenue from tourism, international tourism coming through the Beirut International Airport.

Lebanon is adopting the functions of a commercial intermediary in lieu of its previous functions as exchange intermediary. This is

due to the continuous growth in economic development of the area.³⁴

The third point is the appreciation of the Lebanese currency from LL.3.73 per one US dollar in 1951 to LL.3.01 per US dollar in 1961 and the rise in gold cover of currency to some 95% from 20% in 1950. This appreciation of the Lebanese currency, which is immediately due to the favourable balance of payments position of the country and which may thus be considered as a sign of strength of the balance of payments has in turn reacted to give more strength to that position by materially contributing to the growth of the nation's capital.

34. For further reference please see Table 7.

TABLE 8
LEBANON: LEBANESE ARAB TRADE
(IN THOUSAND L.L.)

	1956		1957		1958		1959	
	IMPORT	EXPORT	IMPORT	EXPORT	IMPORT	EXPORT	IMPORT	EXPORT
SYRIA	111078	18998	92158	20909	3451	21324	4693	23212
JORDAN	8770	8862	8774	11725	23964	10609	11346	13086
IRAQ	23476	5278	24795	13349	49322	6654	51039	10760
PALESTINE	282	944	318	927	1015	392	1075	560
S. ARABIA	36416	19071	39770	23498	32883	16027	17109	21104
EGYPT	10253	6283	12777	12295	8731	2545	12125	3053
TOTAL	190275	59436	177592	80703	119366	57551	97387	71775
ARAB COUNTRIES								
TOTAL	606403	160447	666035	178068	548975	126757	687080	163637
ALL COUNTRIES								
PERCENTAGE	31.3	37.03	26.6	44.7	20.9	45.3	44.02	43.2
LEBANO-ARAB								
TRADE								

Source: Lebanese Government, Customs Higher Council Report, Beirut 1960

Data compiled by the author

CHAPTER III

WHAT IS FOREIGN EXCHANGE

TO KNOW THAT WE KNOW
WHAT WE KNOW, AND THAT
WE DO NOT KNOW WHAT WE
DO NOT KNOW, THAT IS
TRUE KNOWLEDGE.

CONFUCIUS.

The international exchange of goods and services naturally involves payments by the nationals of one country to another. In primitive countries such payments were made by means of barter. As international trade has grown wide and diverse, and financial obligations between countries had to be expressed in terms accepted by all parties; a common denominator had to come into existence, a means by which the currency, or medium of exchange, of one country is expressed in terms of the currency of the other country.

Foreign exchange may be defined as that section of economic science which deals with the means and methods by which rights to wealth expressed in one country's currency are converted into rights to wealth in terms of another country's currency. It involves the investigation of the method by which the currency of one country is exchanged for that of another, the causes which render such exchanges necessary, the forms which exchanges may take, and the ratios or equivalent values at which such exchanges are effected. Accordingly the rate of exchange is the price of one currency in terms of another or, in other words, the number of units of another currency. To reach such a rate one should begin

with a starting-point. The obvious method of arriving at such point, or the ratio of value of the standard units of two countries is to compare their respective gold values, whether an actual or theoretical amount of pure gold which each contains. This is called Mint Par of Exchange.³⁵ The great inflation of the currencies of nearly all the belligerent nations which took place during and just after World War I led to the almost total abandonment of any attempt to retain a gold backing or even a gold basis for such currencies.

Consequently, in the absence of limits set by the gold standard the rates of exchange started fluctuating widely, and the need for a new basis of comparison of currency values became apparent. Professor Gustav Cassel, of Stockholm³⁶ at length advanced the theory that, under normal conditions, people do not buy a currency for the sake of owning it, but because the possession of it enables them to satisfy some want to better advantage than if they carry some other currency. This led to the evolution

35. Mint Par of Exchange may be defined thus; where two countries use the same metal as the basis of their currencies, the Mint Par of Exchange between them is the number of units of the one currency which should legally contain the same amount of pure metal as does, legally, a given number of units of the other currency.

The expression "Foreign Exchange" is also popularly used to denote a foreign currency. Again "Foreign Exchange" is used, particularly by the Press, to describe the ratios, or rates of exchange, at which currencies exchange for one another.

36. Cassel, Gustav, Money and Foreign Exchange After 1914 (London: Constable and Co. Ltd. 1922)pp.138 - 140.

of the Purchasing Power Parity Theory of exchange.³⁷

While the value of the unit of one currency in terms of units of the other will vary over short periods, or at any particular time, in accordance with fluctuations in the market conditions of supply and demand, yet, in the long run, that value will be determined by the relative command over goods, services, and securities of similar status, i.e. purchasing power, which each unit of currency possesses in its own country.³⁸

Earlier Theories on the Exchange

The first theory of exchange of a scientific character was probably that given by Ricardo in the chapter on foreign trade in his work Principles of Political Economy. The subject which interests him, however, is not directly the exchanges but the distribution of the precious metals in the case of free commercial intercourse between nations and the different value of money dependent thereupon in the different countries. By the value of money, therefore, he means the purchasing power of gold (or silver) against commodities. At an earlier stage in the history of the community, says Ricardo, when every country's products are much alike, the value of money in the various countries is principally regulated by their distance from the mines from which the precious metals are derived but at a more advanced stage, when different nations win the advan-

37. The purchasing power parity between any two countries is that amount of the currency of one country which endows the holder with the same amount of purchasing power, i.e. command over goods and services, as would a stated amount of the currency of the other country.

38. Evitt, H.E. A Manual of Foreign Exchange (London: Sir Isaac Pitman & Sons Ltd. 1950)pp.65-70.

tage in particular manufactures, the value of the precious metals, mainly comes to be regulated by pre-eminence in these manufactures. According to Stuart Mill the price level in any country is determined by that country's ability to buy its imports, and particularly the precious metals, at a low value. He points out that a deviation of the exchange rate from par effects international trade in a direction which must counteract the deviation, and thus represents a corrective to it. A paper currency is regarded even by Mill merely as a depreciated metal standard. The actual exchange rate in the case of such a depreciated currency is the result of two factors: The "real" rate, which follows the alternations in the balance of payment, and the "nominal" rate, which is determined by the amount of the depreciation of the currency below its metal parity. Goschen, in his work The Theory of the Foreign Exchanges largely adopts the same point of view as his contemporary Mill. In case of currencies maintained at their metal parity, the exchange rate is determined, according to Goschen by the balance of payment i.e. by the supply of and demand for (exchange) bills. But the balance of payment is itself affected by the granting of credit, which in its turn is necessarily affected by the interest rates. The study of the effect of money interest upon the immediate balance of payment, and thereby upon the exchanges, seems to represent Goschen's most important contribution to the solution of the exchange problem.

What Brings Foreign Exchange into Existence

It was mentioned earlier that foreign exchange is the medium through which international payments are settled. Among the trans-

actions leading to international trade intercourse are:-

1. Foreign trade in goods and drafts for settlement of these transactions.
2. Foreign securities transactions.
3. Foreign capital lending
4. Credit facilities to foreign banks.
5. Interest and dividends on foreign capital.
6. Freight and insurance to foreign naval and aviation companies
7. Emigrants remittances.
8. Tourism, and related services.

It is obvious that the above-mentioned transactions result in both the inflow and outflow of foreign exchange according to demand for them in any one country, provided the absence of any controls.³⁹ With these transactions taking place every day, a rate is reached for the different currencies in the market. This means that exchange rates fluctuate. They rise and fall according to the transactions undertaken pertaining to their respective countries. Consequently, we can say the exchange rate to a country for a currency falls when:-

1. There are high exports of goods to foreign country.
2. National securities are sold to foreigners.
3. The bank rate rises at home.

39. Any interference on the part of the government with the freedom of the market for the exchange of one country's money for that of another. The aims usually are:-

1. To influence the balance of indebtedness in foreign trade and thus to influence the rates quoted for foreign bills.

4. Interest rates are lower at foreign depositing points.

On the other hand we may say the exchange rate for a currency rises when:-

1. There are high imports of goods from foreign sources.
2. Foreign securities are purchased locally
3. Payment of interest on securities held abroad
4. Bank rate falls at home
5. Interest rates are high or rising at foreign depositing points.

Yet, it is worthy of nothing here, that there is more than one influence acting in opposite directions at the same time, which creates a rate at a certain time.

/ The normal consequence of thinking is to ask what effects has the foreign exchange fluctuations on the balance of payments of any country and accordingly upon its economy. From the days of Ricardo as mentioned earlier in the chapter, exchange rates have provided economists with interesting problems for the application of their theoretical tools. The problem was how to distinguish short-term forces from fundamental changes in the demand for, and the supply of, foreign exchange so that the market rate could be supported at an "equilibrium"⁴⁰ level. There have been

-
2. To depress unnecessary imports
 3. To restrain exports of essential goods
 4. To stop evil effects resulting sometimes from unrestrained speculations on foreign exchange

40. A criterion of equilibrium rate is a rate which could be maintained without a net loss of foreign exchange reserves over a period of time sufficient to allow for seasonal and short-term cyclical variations in the balance of payments and which would not adversely affect employment and income level.

always contradicting points of view on the subject of "exchange rate management." Some writers were for the preservation of "equilibrium" in foreign exchange rates for the prosperity of the national economy, Others like Alfred Hansi had a new approach to this subject. In an article published recently⁴¹ HANSI said that there are for every national economy three "CORNERSTONES" of economic policy namely the price-level, the exchange rate and equilibrium in the balance of payments.

"Since dynamics of economic progress entail continuous changes in structure and in values, it is never possible to hold more than two of these three cornerstones immovably fast. Cornerstone No.3, balance of payment equilibrium, is at most times "indispensable". It is the means of integrating every national economy into the world economy. If there is one of the three cornerstones, that is indispensable, it follows that of the other two cornerstones-the price-level and the exchange rate-never more than one can be held fast or subordinated to the objectives of autonomous economic policy, while the other is subject to the influences of foreign trade and payments and changes therein. Autonomous anti-cyclical economic policy and stability of exchange rates cannot be tolerated without endangering the integration of the world economy. Exchange rates must not be treated as taboo. A policy of rigid exchange rates is not any more possible. Whenever needed for the benefit of national and international economies

41. Hansi, Alfred The Monetary Utopias of our Times
(Berlin: Berliner Bank, September, 1961)

changes in exchange rate should be undertaken."

Moreover, there are still other subsidiary policies pertaining to the exchange rate: the multiple exchange rate where the use of different rates for different categories of merchandise and services transactions are held; the discriminatory cross-rates, a system in which the exchange rates applicable to different currencies do not conform to the effective rates between the foreign currencies themselves.

How are Foreign Exchange Rates Determined ?

The price of one currency in terms of others depends upon the demand for that currency and the supply of it. Let us first determine precisely what we mean by the demand for and the supply of currency. By the demand for a certain currency, we mean that the relation which links the amounts of this currency that would be demanded at each possible price to these prices.

By the demand for currency e.g. pound sterling (in terms of dollars) for instance, we mean the whole table in which we set out that at, say \$2.80 X pounds would be taken, @ \$2.82, y pounds would be sought, @ 2.84, z pounds would be wanted and so on. The "demand for the pound" then, expressed the same kind of relation between pounds and dollars as between wheat and dollars. Now does the amount of sterling that those in other countries seek to acquire vary inversely with the price of sterling, expressed in other currencies, when other things are equal? Though this may be in the affirmative it is not at all certain. The elasticity of the demand for a particular type of foreign exchange depends not only upon the kinds of goods and services which enter into a

country's export list but also upon whether that country is easily able to build up its exports at the expense of other exporters. Thus if a country's currency becomes cheaper to foreign buyers, the sale of its products could be expected to increase by a large amount, if the country in question sells in competition with many others which do not reduce the price of their currencies in third markets. Summing-up, in some cases the amount demanded would be very responsive to changes in the price of this currency, and in others only slightly responsive.

FOREIGN EXCHANGE MARKET

A market may be defined as the coming together of buyers and sellers. Therefore, it involves all the mechanism necessary to facilitate their intercourse. The foreign exchange market includes, besides the commercial and industrial organizations which buy or sell drafts, all middlemen of whatever class who engage in the trade. The middlemen may be divided roughly into three classes:-

1. Bankers which do a regular foreign exchange business, buying bills from those who have them to sell, and selling them their own drafts on foreign correspondents to persons desiring to remit;
2. Exchange dealers who buy bills and resell them to banks;
3. Independent brokers who make commissions by bringing buyers and sellers together.

There is no meeting place, but because of the modern techniques in communications, spot purchase and sale is rendered possible.⁴²

42. More details on market transactions will follow in Chapter Six.

Moreover, with so many brokers⁴³ bent on executing the orders with which they have been entrusted and with so many dealers keenly watching for every possibility to buy at one price and sell at another, the chance for continued simultaneous differences in quoted prices is reduced to practically nothing.

The first duty of the exchange dealer⁴⁴ at the beginning of the day, is, therefore, to study carefully the telegram received from his correspondents abroad giving the closing rates ruling in other centres at the end of the of the previous day. From there he attempts to form an opinion as to the rates likely

43. A main feature of the foreign exchange market is the broker. The exchange broker is not, strictly speaking a "member" of the exchange market. The broker does not deal but merely provides the dealers with a channel through which their operations can be carried out. His capital is more of a reputation for ability and integrity than a large cash backing, since he is not concerned with the payment of or for the amounts of foreign currency passing between the dealers. It is a profession calling for a clean head, a high code of honour and unlimited energy, together with at times a thick skin. They must make no deals for their own account. They must not take any profit in the rate at which a deal is arranged by them, but must rely for their remuneration on the standard scale of brokerage. A broker assumes no legal responsibility and cannot be bound or forced by any dealer to conclude business at the rate quoted by the broker. Nor can a broker compel a dealer to stand by a price at which the dealer may have stated that he was prepared to buy or sell. Owing to the keenness of competition brokers specialize in certain currencies. A broker is not supposed to disclose the names of either party to the other where business is proposed until the deal has been finally concluded.

44. The exchange dealer's room is largely filled by telephones and calculating machines to facilitate all operations.

to rule on the opening of business. Soon after he receives his "position sheet"⁴⁵ from the account department. The brokers also endeavour to use their judgement as to the probable trend of rates though without the same data as the dealers possess and make their opening rates accordingly. The broker then commences to ring his clients, the banks, and to endeavour to secure firm orders to buy and sell so that he can quote a firm two-way price. The activity during the day depends on the prevalence of local buyers and sellers as well as foreign demand.

FOREIGN EXCHANGE INSTRUMENTS

Foreign exchange instruments are the different means and tools used by banks and exchange dealers to execute their orders to their foreign correspondents. An exchange dealer may not merely use any means he chooses haphazardly. This is because every tool in foreign exchange has a different price. The price of each tool depends on the spread of time from the day the transaction is concluded to the day the buyer's account is credited with his foreign correspondent. This date is important in foreign exchange, and is known as the value date.⁴⁶

Telegraphic Transfers (T.T.) A T.T. is an order for the payment of money sent by cable. As no signature in writing, which could be compared with a specimen signature of the sender, can be included in the telegraphed instructions, a system of private codes by means

45. For further information see Chapter Six.

46. The date on which a payment-over of funds or an entry to an account becomes actually effective and/or subject to interest payment-over, of the respective currency in each centre and takes place on the same day, so that no gain or loss of interest accrues to either party. Such payments are said to be "valeur compensee".

of which the genuineness of the instructions can be tested and authenticated.⁴⁷

By arrangement, as funds are paid out in the foreign centre usually on the same day that payment is made in the home centre in local currency, there is no gain or loss of interest. T.T. forms the safest and quickest mode of transfer of funds. The price of T.T. may be considered the basic rate of exchange between the two countries concerned as at any given moment. L.T. is a deferred cable which is paid on the following day.

Mail Transfer (M.T) M.T. is an order to pay sent by letter from principal to agent. It may be an order for actual payment of cash to a third party, or for a credit to be passed to the account of the payee in the books of the agent. A current account between the signer and the addressee is necessary and such transfers perform all the functions of a cheque in effecting a transfer of funds but are not negotiable or transferable and need no stamps, and eliminate the risk of a cheque or draft coming into wrong hands. There is loss of interest by the purchasers. This difference in interest value is made up by an allowance in the price at which the instrument is sold, i.e. it is cheaper than the T.T.

47. A Test word is usually the first word in the text of a cable. It is written in Arabic numerals. It is formed by adding up numbers for the date of despatch (date, day and month) the amount of money in question. The currency and the fixed number of the test key in question. When the cable is received, the same numbers are added. If the addition coincide with the test word in the cable, the telegram is genuine. There are various forms in which the test word is formed, the way each bank desire to keep with its correspondents.

Guaranteed Mail Transfers (G.M.T.) In order to eliminate any unexpected gains or losses of interest because of irregularities in mail and to render dates of payment independent of the possible availability of a mail carrying vessel, the practice has grown up of dealing in a special type of transfer known as a G.M.T. This instrument is sold with an undertaking by the seller that the funds in question shall be paid over in the foreign centre on a fixed date, irrespective of the arrival of any mail and the title arises from the fact that the date of payment is so fixed "guaranteed". The payment order is given good value under any condition of delay.

Bill of Exchange. A bill of exchange is an unconditional order in writing addressed by one person to another, signed by the person giving it requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person or to bearer.⁴⁸

Clean Drafts.⁴⁹ A clean draft is a draft unaccompanied by documents and is, as a rule, drawn in accordance with previous arrangements for the financing of merchandise or for outstanding amounts owed by the drawee to the drawer.

Documentary Draft. A documentary draft is a draft to which the shipping documents required by the terms of the sales contract are attached.

48. Richardson, Dudley, A simple guide to Negotiable Instruments and the Bills of Exchange acts (London: Butterworth & Co., 1948) pp. 37-41

49. A draft is a written order from one person or bank to another requiring the payment of a stated amount of money.

Sight Drafts. A sight draft is a demand draft payable upon presentation to the drawee. The basic object of the sight draft is to relieve the exporter from the credit risk of an account receivable.

Time Drafts. A time draft is a draft which calls for payment at a certain number of days or months after sight.

Stock Cheque. A stock cheque is the term applied to a cheque or sight draft drawn on another centre in respect of a sale of stock and having the stock or share certificates attached to the cheque. The selling firm may not be prepared to part with the stock or shares except against payment in cash while the buyer is not prepared to pay over his cash except against delivery of the security or the seller may be unable to finance the operation himself and needs temporary accommodation. In such cases the buyer may instruct his bank to honour the cheque drawn on it by the seller for a stated amount, if certain specified securities accompany the cheque and are found to be in order.

Letters of Credit. These are issued by foreign connections of the bank in terms of a foreign currency. These are carried by foreign travellers and tourists to draw the equivalent of all or part of the letter of credit to meet their expenses or disbursements in this country. The holder signs a form of receipt or sight draft on the foreign issuer for the amount of foreign currency which he wishes to convert. The dealer purchases this as if it were a cheque in foreign currency and allows in his buying rate for the cost of service rendered by his bank in making the encashment, as well as for the loss of interest through making the payments at once, but only receiving credit in the foreign currency

on the arrival of the instrument in the foreign center, and the cost of stamps.

Traveller's Cheques. Travellers Cheques are a means by which foreign travellers safeguard their money while travelling. These cheques are issued by banking institutions in different denominations and several currencies. Each cheque should be signed when purchased and countersigned when sold. The cheque is not accepted for remittance by the issuing institution unless the two signatures are similar when compared.

FOREIGN EXCHANGE OPERATIONS⁵⁰

After reviewing the different instruments of foreign exchange we shall discuss below the various operations undertaken by the exchange dealers and banks.

FORWARD EXCHANGE

A forward exchange is an operation in exchange whereby a rate is fixed at once for a purchase and sale of one currency for another which is to be completed at some future date. Under such an operation the exchange of one currency for another is arranged, for a stipulated date at a rate of exchange fixed immediately and no matter what the current rate of exchange may be at the date of the actual exchange of currencies. The exchange is carried through at the rate fixed when the contract was entered into. A person who wishes to invest funds for a short period can eliminate any risk of

50. This section is based mainly on Evitt, A Manual of Foreign Exchange. op.cit. pp.253-265

loss through fluctuations in rates of exchange by effecting a forward sale of the foreign exchange currency which he is buying as "Spot" for the purpose of the investment, so that when his investment matures, he has already fixed the rate of re-conversion into his own currency.

51

HOW FORWARD RATES ARE CALCULATED ?

These rates are obtained by a seller deducting from the rate at which he is willing to sell T.T. the margin he requires in his favour for selling forward, and by a buyer deducting from his buying rate for T.T. the margin he is willing to give away for buying forward. Dealings in the market could probably be effected at rates between these two extremes, so that a bank dealer could undo an operation carried out with a customer at a small profit to himself, if he sold to or bought from the customer at these extremes of prices and covered himself at some intermediate rate in the market.

The relation of any forward rate to the spot rate for the same currency depends, first on the relative rates of interest obtainable on similar classes of securities in the two centres, and secondly, on the relation between the demand for and supply of forward currency in the world's markets. The interest factor is the basic factor in arriving at a forward margin. If the rate of discount

51. A bank in New York may wish to invest funds in three months, London bills for the sake of a higher rate of interest to be obtained in London than in New York. To buy such a bill it must first buy Sterling and if it does not "cover exchange" it may lose all the profit from the higher interest rate and even lose when it wishes to reconvert the Sterling into dollar. Thus if it makes a purchase of Sterling it must sell forward against dollar when bill matures.

in Paris for three months' prime bank bills is 2% per annum, while similar paper in London can be purchased at a rate of discount of 3% per annum there will be a flow of funds from Paris to London of such floating balances as are normally used in this type of investment, to take advantage of the higher yield shown by London bills. As long as exchange movements in the value of French franc in terms of Sterling are confined to within comparatively narrow limits, a certain proportion of transfers of such funds will be carried out "uncovered" as regards the exchange; that is, the French investor will run the risk of being able to buy back as many francs per pound, while he wishes to repatriate his funds, as it cost him when he originally purchased the Sterling in order to buy Sterling bills. This leads to a certain demand for spot Sterling, as has already been explained, with a consequent rise in the value of the pound in terms of French francs. In other cases and under less stable conditions French investors will make a transfer of funds only if they can secure their exchange for eventual re-conversion into French francs of the Sterling they purchase; that is they insist on covering their spot purchase of Sterling by a forward sale of Sterling for a date approximating the estimated maturity of the Sterling investment. This means that there will be a general tendency in the world's exchange markets for operators to be asked to buy French francs on the spot against a resale of the franc for a future date, both against Sterling. As a result spot franc will be offered and forward francs wanted, giving a tendency for the forward franc to be dearer than the spot, i.e. forward franc will tend to go to a premium over spot, as against Sterling. A dealer, wishing

to give more francs to buy his spot Sterling then, he will receive a premium for his forward resale of the Sterling against francs. Consequently, a certain loss is incurred in selling spot and buying forward francs, and this loss must be set against interest profit which will occur by moving funds from Paris to London; but operators will give away only a part of their gross interest profit, in the form of a premium on the forward currency, and the premium thus set up will never therefore, under normal conditions represent a percentage cost equal to the percentage gained in interest, but will remain at a lower level. The extent to which the premium on the forward currency will under such conditions, approach a percentage equal to the percentage margin of interest depends on the volume of funds in the low interest center available for transfer to the high interest center and the consequent pressure of the demand to buy spot and sell forward currency in the latter center. Force of competition, between investors, should the volume of available funds be large or the interest margin of gold be considerable, will cause the net difference between the percentage gain in interest and the percentage loss in the forward margin to become so narrow as to represent a minimum margin of net profit. While the relative interest rates in two centres is the basis of calculation of the forward margin in the exchange between them under stable conditions, this basis ceases to exert any influence as soon as the conditions become abnormal. The margin between the spot and forward rates for any currency will be at a premium on spot when the rate of interest at home is higher than that ruling in the foreign centre, and will be at a discount over spot

when interest rates in the foreign centre are higher than those ruling here for similar classes of securities, but the percentage per annum equivalent of the forward margin will fall short of the full percentage per annum difference in the rates of interest.

OPTION FORWARD

Option forward is a contract under which one contracting party cannot state definitely at the time of entering into the contract on what exact date he will be able to complete the contract and he, therefore, obtains the consent of the other party that the contract may be completed on any date between two specified dates or during a stated period, at the option of the party to whom such option is granted. The giver of the option must obviously protect himself under such circumstances by taking the view that the contract may be completed on the worst possible day from his point of view, and must quote a price accordingly.

SWAPS

Operations consisting of a simultaneous sale or purchase of spot currency accompanied by a purchase or sale, respectively, of the same currency for forward delivery. They are "swaps" or "double deals" as the spot currency is "swapped" against the forward. This is the type of operation carried out by a short-term investor in order to secure himself against loss in exchange during the period of investment. The rate of re-conversion of the foreign funds into home currency is thus secured and the investor can calculate his profits on the basis of interest and capital appreciation, if any, of his investment. The pur-

chase of the spot foreign currency gives the investor immediate funds in the foreign centre of which he can dispose as he pleases.⁵²

SWAP AND DEPOSIT

If a bank needs Sterling for a certain period of time, it will make an offer to another bank to sell it dollars on the spot, against Sterling and to buy it back forward again against Sterling, at a margin to be agreed upon; at the same time this said bank will offer to take the dollar on deposit with itself at a stated rate of interest so as to offer the other bank employment for the dollar which it will obtain if it carries out the swap.

SWAP INVESTMENT. This implies that the purchase spot rate of foreign currency and sale forward are at a set rate and date. The foreign currency funds are then invested at best until the contract matures.

JOINT ACCOUNT INVESTMENT

Two correspondent banks usually join in such a venture.⁵³ We may see that certain securities can be purchased cheaply at the time, securities which can probably be sold, later, at a substantial profit. But Bank A has use for all the funds under its own immediate control and does not wish to invest any of these funds in such securities.

Bank A suggests to his correspondent, Bank E, that both can go into this investment on joint account, securing the means through the use of exchange. Bank A. then draws on Bank E a draft maturing

52. For further reference, please see Chapter Six.

53. For our purpose Bank A and Bank E.

in say 90 days after sight which is sold in New York with the proceeds the securities are purchased and held for 70 days or perhaps a shorter period. They are then sold, presumably at a profit and remittance is made to Bank E. The draft on Bank E was purchased in New York sent to London, and sold in the London discount market. By the time the purchaser presents it to Bank E, for payment Bank A has remitted. Neither bank has sacrificed the use of its own funds.

ARBITRAGE TRANSACTIONS

A slight change in the exchange rate between two distant markets may be quite sufficient to start the arbitrageur at one point selling or buying some related currency at some entirely different point. The amounts dealt in by the banks, it must be remembered, are very large, so that the smallest of rate fluctuations run into money.

CHAPTER IV
THE HISTORY & DEVELOPMENT OF THE FOREIGN EXCHANGE
IN LEBANON

THE HISTORY OF THE WORLD
IS THE RECORD OF MAN IN
QUEST OF HIS DAILY BREAD
AND BUTTER.

H.W. VAN LOON

The development of the foreign exchange market in Beirut can be dated back to early this century. It started mainly with dealings in gold and silver coins in circulation at that time. Turkey, like the other belligerent nations in W.W.I had to resort to several extraordinary measures to meet the exigencies of war. One of these measures was the introduction of government paper money to replace the Turkish gold and silver coins in circulation. Accordingly as from the First World War, notes in circulation of different countries started to increase on the exchange market. Besides this, there have always been emigrants' remittances to their dependents in Lebanon and these were a source of supply to the market. The native bankers at that time used to send these drafts to London and New York to the credit of their accounts there. Bankers used to draw on these accounts when their clients demanded checks for settling their foreign indebtedness.⁵⁴ There was no restriction on exchange operations up until the Second World War. But the mandatory authorities found it necessary to introduce exchange

54. For further reference see Himadeh B., Economic Organization of Syria (Beirut 1935)

control with the outbreak of World War II. The step was nationalized by the importance of such control to secure the victory to the Allies. On December 3, 1939 a series of "Arretes" were issued regulating exchange operations in general, including foreign trade.

The regulations provided for limiting exchange transactions to authorized banks, mainly Banque de Syrie et du Liban.⁵⁵ This included all operations dealing with sale, grant, transfer or receipt of means of payment expressed in other than LLS.⁵⁶ Although facilities were granted to transact with the French Franc Area, it was limited to banks of issue in the respective countries. Supervision and control were left in the hands of the "OFFICE DES CHANGES" the exchange office newly created and attached to the Banque de Syrie et du Liban. The office was to acquire all foreign exchange receipts required to be sold to the authorities and to license foreign exchange payments.

Banks were supposed to present daily records of the foreign exchange transactions they had carried out and to sell daily to the exchange office any foreign currencies received. Exchange dealers were required, subject to the request of the "Office des Changes", to report transactions carried out on behalf of non-residents of the French Franc Area.

Similarly, capital movements were prohibited without prior

55. To be referred to later as B.S.L.

56. Lebanese Syrian Pound.

permission of the "Office des Changes". This included the purchase of foreign assets in the French Franc Zone belonging to non-residents. Furthermore, all non-residents accounts in LLS, or French Francs were to be closed as from 2.12.1939. As for the actual export of capital funds from Lebanon, residents of the Franc area were forbidden to take out of the two countries any means of payment or other movable assets, whatsoever, except by special permission of the exchange office. Non-Residents were given facilities as far as taking with them movable assets or means of payment equivalent to that which they could prove they had brought in with them upon entry. On the other hand, the import of capital funds of all kinds by residents as well as by non-residents into Lebanon was kept free from restrictions.

Foreign trade was regulated as well. The import of foreign goods was prohibited, although exceptions were granted.⁵⁷ Imports of essential goods were given priority after obtaining a license from the Department of Economic Affairs. According to this license the exchange office used to provide the necessary foreign funds. The export of goods required a prior export license from the Department of Economic Affairs. Furthermore, exports paid for, either wholly or in part, with foreign currency were subject to a guarantee signed by the exporter to sell to the exchange office his foreign currency receipts within a specified period.

57. Arrete No.337 of December 3, 1939 permitted the free import of goods from the French Franc Area.

As for exchange receipts from invisibles such as services rendered to foreigners or incomes accruing in foreign exchange to holders of foreign assets, these were required to be repatriated and sold to the exchange office within two months of their receipt.

During 1940, the regulations of 1939 were modified. It happened that in January and June two series of arretes were issued which changed nothing in substance although they introduced alterations in form. Mostly the arretes aimed at closing the loopholes in the previous regulations, which appeared through practical experience during the first few months. The arrete number 152 of June 12, 1940 is worth discussion at this point. It differentiated between what it referred to as the "A" currencies and the "B" currencies. The former list contained Holland and Dutch East Indies, Luxembourg, Portugal, Switzerland and U.S.A. The latter list included currencies of all other countries outside the French Franc Zone. Moreover, "D" securities which were officially quoted in Argentina, Bolivia, Canada, Holland, Luxembourg, Portugal, Switzerland, Tangier and U.S.A. were to be strictly controlled as these formed means for international payments at the time. In fact the important innovation introduced in this period was the permission to all residents to transact in all foreign currencies, except the "A" and Sterling Area currencies, against the same foreign currencies which transactions were centralized previously in the exchange office. Thus a restricted foreign exchange market was introduced, and control was extended beyond authorized

banks as all exchange dealers were to submit their reports to the foreign exchange control authorities.

On June 8, 1941 the Allied forces entered Syria and Lebanon and on July 15, the armistice was proclaimed between the Allies and the French Vichy Forces. The significance of this event at this juncture is the relaxation of the economic blockade and the inclusion of Lebanon and Syria into the Sterling Area. An official rate for Sterling was established at LLS.8.83125. The rate of other foreign currencies was determined on the basis of this parity according to the prevailing rates in London.

FOREIGN EXCHANGE MARKET

"The most important statutory change as far as exchange operations were concerned was the permission granted to the exchange office to sell, upon request, without limitation any requirement for justification, all kinds of Sterling Area currencies to residents of Lebanon and Syria. Currency thus bought could be transferred to London or to any other centre within the Sterling Area or could be used to buy goods and services from within the Sterling Countries. This privilege was not officially extended to residents of Lebanon and Syria until May 30, 1943, though large sums were transferred by residents of the two countries into the Sterling Area before that date."⁵⁸

By 1943, formal independence of Syria and Lebanon was established. Both countries were striving to take the administration of their countries into their own hands. Upon the suggestion of the

58. Saba, Elias S., The Foreign Exchange Systems of Lebanon and Syria 1939-1957. (Beirut: The American University of Beirut, 1961) p.43

French authorities and with legislative decrees issued in Syria and Lebanon, the exchange office was transferred into a Lebanon-Syrian public department, managed by the Banque de Syrie et du Liban^{issue} department.

Exchange control regulations were all assembled in the form of a comprehensive system promulgated by Lebanese decree No.2025 of 11.10.1944. Few main changes were introduced. Henceforth, the French Franc was considered a foreign currency. Residents travelling to any country not within the French Franc Area or the Sterling Area were not permitted to carry with them any currency.⁵⁹

As for capital transfers, countries were divided into three groups:-

1. Lebanon and Syria; no restrictions on capital transfers.
2. French Franc and Sterling Area; residents could transfer capital to them without any restrictions, but the transfer of banknotes was prohibited.
3. The rest of the world; residents were not allowed to transfer capital to those countries except by special permission from the exchange office.

On March 13, the French authorities revoked their earlier promise to maintain the complete convertability of the Lebanon-Syrian Pound into pounds Sterling.⁶⁰ Three main reasons were given in explanation of this action.⁶¹ The Franco-British Financial Agreement of

59. The Anglo-French-Lebanon-Syrian Financial Agreement of 25.1.1944 maintained this convertability.

60. Ibid, Saba p.56-57

61. Deficit was in 1946 about LLS.100 million.

February 8, 1944 had expired, and had not been renewed or replaced with the result that France itself was not quite sure about the availability of Sterling in the future. It aimed at restricting the flight of local capital funds seeking security abroad, and limiting the deficiency in the balance of payments of the two countries.⁶² It was also believed that the British authorities concerned might have wished to suspend convertability into Sterling Britain being anxious not to increase further, and unnecessarily her already considerable Sterling balances due to the foreign countries.

The year 1948 may be considered as a milestone in the economic history of Syria and Lebanon. The exchange systems of the two countries were separated, and a free exchange market was legally established in both countries and for the first time since the regulations were established in 1939. This took place in several steps.

Lebanon signed an agreement with France in 1948 to settle all monetary conflicts between them. Syria on the other hand did not sign a similar agreement which made France block the Syrian Franc balances. This had an immediate effect on the relation between Syrian and Lebanese pounds. The latter were sold at a premium in relation to the former,⁶³ although they had the same official par value. The centralization of the free exchange market in Beirut meant that most of the important exchange dealings of Syria were carried out through the Beirut market.⁶⁴

62. Deficit was in 1946 about LLS.100 million

63. 3½ - 4 points in 1948, 21 points in 1962.

64. Syria used the Beirut port to ship and receive most of its exports and imports before the economic

France decided to stop selling foreign exchange to Lebanon. Accordingly a law was passed September 7, 1948 establishing a new general exchange control in the Ministry of Finance composed of an Exchange office and a Control Department.

This step was in fact a turning point in freeing Lebanon's foreign exchange policy from French influence, and came as a result of France's decision to stop her financial help (by selling hard currencies) to Lebanon.⁶⁵

The new exchange controls introduced in November of the same year were an official recognition⁶⁶ of the existing and busy foreign exchange market.⁶⁷ Decree No.13532 divided foreign currencies for the purpose of exchange control regulations into two types; those the prices of which were quoted by the general exchange control (i.e. specified currencies), and which included Belgian francs,

separation of 1950.

65. Saba, Ibid, p.105

66. Its magnitude could be judged from the fact that in 1946 the value imports as recorded by customs statistics was about LLS,267 million while foreign exchange granted by the "Office des changes" was only LLS,138 million. In fact it is estimated that during 1944-46 around 40-50% of Syro-Lebanese imports were financed by the foreign exchange obtained from the black market. In the following two years the percentage rose to around 65%.

Makdisi, Samir Post-War Lebanese Foreign Trade and Economic Development (Beirut A.U.B. 1959) p.14

67. It is interesting to note that Decree No.13532 of November 5, 1948 which recognized the black market included in its preamble the following statement: "And as it is adviseable that the present laxity permitted in enforcing exchange regulations should be defined.....".

Canadian dollars, Egyptian pounds, French francs, Iraqi dinars, Sterling pounds, Swiss francs, and U.S. dollars;⁶⁸ and those which were not quoted by the general exchange control, which included all the rest. All transactions in the latter currencies were freed from any interference whatsoever by the general exchange control and a free market for them was officially re-organized.

Furthermore, transactions in coins and banknotes of all kinds were also freed from all restrictions, and could be carried out without any control whatsoever; thus a completely uncontrolled market was recognized both for transactions in coins and banknotes of all kinds, and for transactions in all foreign currencies not quoted by the general exchange control.⁶⁹ Any exchange dealer who asked for a licence was given one freely. This practice had the effect of widening the extent of the free exchange market. When these new regulations were introduced, there came to be a multiple exchange rate system. There were recognized at the time four different buying rates and two selling rates.

The buying rates were the following:⁷⁰

1. The official rate applying to sales of French francs
2. A fluctuating free market rate, applicable to all sales of non-specified currencies and to the sales of coins and banknotes of all currencies.
3. A mixed rate (a) at which were sold all exchange receipts in

68. These were considered the most necessary currencies for the purpose of meeting Lebanon's international payments.

69. Ibid, Saba p.105

70. Ibid, Saba page 110-11

specified currencies other than French francs. This was a composite rate, 10% calculated at the official rate,⁷¹ and the balance at the fluctuating free market rate.

4. A mixed rate (b), applying to exchange imports of concessionary companies in specified currencies other than French francs. Again, this was a composite rate, 80% calculated at the official rate and 20% at the fluctuating free market rate. The two selling rates were the following:-
 - a. The official rate, applicable to governmental payments in all foreign currencies and to private payments in French francs.
 - b. A fluctuating free market rate, applicable to all other payments.

The years 1948 to 1952 were the period which the remaining regulations and controls for foreign exchange were liquidated in Lebanon.

Accordingly the various laws still in action were annulled one after the other. The first was on September 26, 1949 where the surrender requirement concerning foreign exchange repatriated to Lebanon was altered. In December 8, of the same year a law was issued declaring that export proceeds in foreign exchange need no longer be repatriated but could be retained abroad.

On 1949, Lebanon suspended the convertibility of its currency into French francs at official prices, following the French franc and

71. 71. These were the 10% to be handed on to the exchange office by importers of specified currencies according to exchange regulations.

Sterling pound devaluation in that year.

Moreover, on November 7, 1950 non-residents were permitted to open and maintain free accounts without prior authorization. It is of significance to note too that during the summer touristic seasons of 1950 and 1951 special foreign exchange facilities were granted to tourists with aim of encouraging tourism. During the first half of 1952, the exchange system was steadily liberalized until, on May 24, the last exchange restriction was annulled.

The (a) and (b) mixed rates mentioned earlier were abolished as well as the surrender percentages of 10% and 80% respectively, and the mixed rates.

Since 1952 there have been no new laws or decrees dealing with the exchange market and on the buying side, only the free market rate is prevailing. On the selling side the official rate applies only to governmental payments, insignificant in comparison with total exchange transactions.

CHAPTER V

FOREIGN EXCHANGE MARKET IN BEIRUT I

EXCHANGE DEALERS

THE ALMIGHTY DOLLAR,
THAT GREAT OBJECT OF
UNIVERSAL DEVOTION.

WASHINGTON IRVING

The Foreign Exchange Market

Markets are people with money to spend and the desire to spend it. When we speak of a market we speak of place, time and institutions that make out this concept. In general, marketing is the economic process by means of which goods and services are exchanged and their values determined in terms of money price. The term "process" implies activity, coordinated groups of activities, in fact having a definite purpose, the purpose being to move goods from points of production to points of ultimate use, not simply in a physical sense but in such a way as to facilitate the maximum satisfaction of consumers' wants. The time notion of the market enters into the practical thinking of all businessmen in their buying and selling operations. Kind of goods, quantity, and price are largely determined in the present; delivery and payment are in the future. A market structure is the formal organization of the functional activity of a marketing institution. Institutions become recognizable only as they take different structural forms.

The foreign exchange market enjoys the same features, in general, as other commodities market. In this case the good is foreign exchange, the price is the market rate that rules between

exchange dealers as members of the market. It consists of offerings by dealers who wish to sell at one price and bids by dealers who wish to buy at another price. The saying that prevails in the market is:

Low rates are for us,

High rates are against us.

Structurally, the foreign exchange market is divided into three groups: the exchange dealers, the brokers, and the foreign exchange departments of commercial banks. For convenience, a chapter of this study will be dedicated to exchange dealers and another to commercial banks. This will enable us to examine the characteristics of each more carefully. Although the exchange brokers are effective members in the market, still they are of lesser importance and accordingly will be treated with as necessary in each of the following two chapters.

Exchange dealers⁷²

To begin with, one should try to define what is meant by exchange dealers. In some cases they carry the name of a bank, although they do not undertake any banking transactions except foreign exchange. They are "Banquiers" who deal mainly in foreign exchange bills, banknotes of foreign currencies and gold. They transact transfers to foreign countries as well, but through their agents. Usually their capital is not less than LL.50,000.- together with some credit facilities in several banks.

The number of exchange dealers in Beirut is approximately 150. The majority are of an Armenian origin, with smaller numbers of native Jews, and native Christians. There are a few Moslem dealers⁷³, most of whom are not Lebanese but rather Syrians.⁷⁴

Most exchange dealers open their shops along two narrow streets in Beirut where they form a market place for foreign exchange. This place is known as Souk Soursoq. Other exchange dealers are distributed in the different quarters of the city, especially in tourist centres (e.g. hotels).

72. The arabic word used in Beirut is "SARRAF"

73. It is interesting to note at this juncture that the number has nothing to do with the capacity. The most outstanding exchange dealer in Beirut is an Iraqi Moslem.

74. Those left Syria to work in Beirut because of exchange restrictions in their home country.

A main principle in the business is that foreign exchange is a perishable commodity. Accordingly, exchange dealers start their business day with a certain sum of Lebanese pounds and end their day with the same in Lebanese pounds plus or minus profit or loss. Usually the exchange dealer prefers not to keep an inventory of foreign currency for the following day. This is simply because the exchange rate may change to his disadvantage. Consequently, at the end of the business day each exchange dealer is sure that his safe carries only Lebanese pounds together with some small quantities of foreign currencies. Nevertheless, some of the big exchange dealers have foreign balances with banks in Beirut and at the world's financial centres (London, New York, Geneva, etc.)

At some periods, foreign exchange is quoted against the dollar instead of against the Lebanese pound. This is because the dollar rate against Lebanese pounds starts fluctuating violently which makes the Lebanese pound an inadequate measure of value, for the other currencies.⁷⁵ Beirut is a "dollar market"⁷⁶ That is, the dollar rate is the foundation for the rates of the other foreign currencies. To simplify matters, let us illustrate this in the following example.

If the rate for the dollar T.T. is LL.3.00 in Beirut
and " " " " Sterling Pound
T.T. is \$2.80 in London
The rate for the Sterling will be LL.8.40 in Beirut
 $L.L.3.00 \times 2.80 = 8.40$

75. Fluctuation of exchange rate for the dollar will be discussed further in Chapter 6.

76. See Chapter 6.

and so every currency quoted against the dollar will be multiplied by the rate of dollar against the Lebanese pound to know the rate to be quoted for that currency.⁷⁷

But why should other currencies be quoted against the dollar under abnormal conditions on the Beirut market ? This will be the theme of the following discussion.

Beirut is the pool of foreign exchange in the Middle East. To quote a price for any transaction, a common medium should be accepted by all parties. Undoubtedly, the dollar is the currency most fit, for its international acceptance. Therefore, if an exchange dealer has an external order to buy Kuwaiti dinars for example, the rate quoted is usually on the dollar (say \$.2.77). If the dollar is fluctuating violently against the Lebanese pound it is not safe to pay in Lebanese pounds because this may result in a loss. The safest behavior to follow is to quote the Kuwaiti dinar against \$ (say \$.2.75) to guarantee a profit margin.⁷⁸

Moreover, there is another fact why foreign currencies at times are quoted against the dollar. It is because the Lebanese pound becomes a rare commodity. Exchange dealers will find it more adequate and cheaper to buy their needs, in dollars than to exchange dollars into Lebanese pounds to settle their transactions.⁷⁹

77. A further discussion of how the rates are born every morning will follow in chapter 6.

78. If the dollar rate is LL.301 at the beginning of the business day, the buying quotation will be $3.01 \times 2.77 = \text{LL.}8.3377$. If the \$ rate rises to LL.3.01½ the KD. will become LL.83515. This means the exchange dealer will be incurring a loss of L.P.1.38.

79. This point will be discussed further in Chapter 6.

There are two media of communication in the exchange market, namely the telephone and the broker.

A minimum of two telephone lines are under the use of every exchange dealer. He has to be in constant contact with the market. Rates of exchange change continuously during the day. The exchange dealer has to be in contact with the market minute by minute so as to follow the rate and therefore, buy and sell accordingly.⁸⁰

Consequently, the exchange dealer spends most of his day calling and receiving calls.

The other medium of contact in the exchange market is the broker. The number of brokers in the Beirut market is around 100 persons. As described in Chapter Three, their capital is their personal qualifications of honesty, vital energy and thick skin. They keep in constant contact with the different exchange dealers and with the commercial banks. Early in the day they start forming an idea about the rate for certain currencies.⁸¹ Once a broker is given an "order" to buy a certain amount of his speciality, he starts contacting the various dealers until his order is covered. As the transaction is being operated on, the rate may change if the dealers feel that the demand is active for that specific currency, and the rate rises. The capable broker can cover all his order at the rate quoted for his customer when the

80. As it is not possible for exchange dealers to follow-up the rate. The usually keep a margin of security between buying and selling rates for unexpected fluctuations.

81.-Each broker is specialized in a certain currency. Accordingly he knows the sellers and purchasers of that currency and how to deal with each order he received.

latter gave him the order.

Each exchange dealer is also known to be specialized in a certain currency. This does not imply that he does not deal in the other currencies, but rather that he has a comparative advantage in that currency. This is usually because he has the appropriate connections for both supply and demand of that currency and he is familiar with the different means and methods of trading in it. This being the case, the dealer specialized in a certain currency is always ready to buy and sell this currency at a competitive rate and his quotation weighs heavily in determining the rate for the day.⁸²

TYPES OF EXCHANGE OPERATIONS

Besides gold, one can classify three main exchange operations on the Beirut market. There are:-

- a. Banknotes operations
- b. Bills of exchange operations
- c. Unofficial transfers operations

On the following pages each of the above-mentioned operations will be discussed separately. Reference will be made in each case to currencies that are dealt with; and specifically under what conditions and terms these dealings are executed.

BANKNOTES OPERATIONS

Practically speaking there is no currency whose banknotes

^{be}
82 That part will/referred to when discussing how the rate is born.

and not available on the Beirut foreign exchange market. Such being the case, one finds currencies of controlled market countries as well as those of free market countries. Banknotes of free market countries are usually quoted at a rate very close to the T.T. rate. On the other hand banknotes of controlled markets are quoted at a large discount below an official transfer rate.⁸³ One of the chief sources of supply of banknotes to Beirut is tourists coming to Lebanon from their home land for estivage and tourism in Lebanon. These exchange their national currency for Lebanese pounds to meet their expenditures. There are also Lebanese tourists coming back from abroad carrying with them banknotes belonging to the countries they have visited. Another source of foreign banknotes is international tourists. These are the travellers who stop-over in Beirut in transit.

A second source of foreign banknotes to Beirut is emigrants' remittances to their families in Lebanon. These emigrants either send cash with a traveller coming to Lebanon or carry it themselves when returning home on leave. A good amount of Kuwaiti Dinars, South American Currencies, Gulf Rupees,⁸⁴ West African Francs,⁸⁵ U.S.Dollars and Saudi Riyals, enter the country this way.

83. Cheap currency markets are usually found in free market countries. The main centers besides Beirut are New York, Tangiers, Hong Kong, Kuwait, Bangkok, Amsterdam and Zurich.

84. Indian Rupee issued for use in the Gulf Area.

85. Currency in circulation in French African colonies.

A third source for foreign banknotes is the Gulf Area tourists. Although their attitudes are undergoing great changes, the dwellers of that area still do not care to carry with them as a store of value other than banknotes. Nationals of these areas are the main source of Gulf Rupees, Kuwaiti Dinars, and Saudi Riyals, banknotes on the market.

A fourth source is the flight of capital in the form of smuggled banknotes. When restrictions are introduced on transfer of capital and when bills of exchange are not available or are not easily accepted for negotiation on the world markets, banknote smuggling becomes one of the remaining means for capital flight.

In recent years, capital flight was a main source of supply for Egyptian Pounds,⁸⁶ Turkish Pounds, Iraqi Dinars,⁸⁷ Pakistani Rupees, Irani Riyals, Indian Rupees, Ghana Pounds,⁸⁸ Spanish Pesetas,⁸⁹

86. In 1948, when the hostilities in Palestine started, Jews living in Egypt started to transfer their capital. The second rush for capital flight was 1951-1952 due to Canal Zone troubles with British troops and which culminated on January 26, 1952 when Cairo was burned. The third rush was after the tripartite aggression in 1956 which was followed by the nationalization of British and French property. The fourth rush was that of 1961 when socialist measures were put into execution.

87. Since 1958 when the coup d'etat succeeded in Iraq, capitalists and ex-regime men found out that it was more advisable for them to flee with their wealth.

88. Ghana, after independence, followed a controlled economy policy aiming at a socialistic state. This policy did not agree with the plans of the foreign emigrants who accordingly decided to leave the country with their wealth.

89. Foreigners investing in Spain try to transfer a good part of their capital and profits every now and then.

Syrian Pounds,⁹⁰ West African Francs,⁹¹ and some of the South American Currencies.⁹²

A fifth source for foreign banknotes is the smuggling of goods. When there are restrictions on importation of consumer goods, or certain commodities are forbidden from entry, smuggling is a normal means to break through such restrictions. Payments for such goods is by means of banknotes of the home country.⁹³ Egypt (U.A.R.) is an active field for such operations. The main commodities smuggled to Egypt are the intoxicating drugs such as opium and hashish. Also valuable consumer goods are smuggled from Lybia to Egypt through the desert. Smugglers are paid in Egyptian banknotes.⁹⁴ Watches smuggled to Turkey and East European countries⁹⁵ goods smuggled from Kuwait to Iraq, opiom smuggled to Iran from Turkey, goods smuggled from Lebanon to Syria, and Jordan and gold smuggled to India from the Gulf Area are all paid for in banknotes.⁹⁶

90. Since 1949 because of the political unrest that characterized Syria for the last decade.

91. As the former French colonies started gaining their independence.

92. Notable flight of capital is a characteristic of countries with unstable political conditions.

93. Countries which put restrictions on imports usually lack foreign exchange and have controlled economies.

94. As from January, 1962 all Egyptian banknotes were repatriated and accordingly Egypt is not anymore officially responsible for Egyptian notes outside its borders. This is significant because Egypt can now change its currency into new banknotes without any responsibility, on the international scene. This no doubt freezed the smuggling operations in banknotes for the time being.

95. This is a main reason why there are so many watch dealers in the city of Beirut.

96. These operations declined considerably due to the restrictions that were put into force in India. This affected Beirut market considerably as gold was bought from Beirut and Indian Rupees exchanged in Beirut again for dollars.

Other sources of supply of banknotes are numerous, but the main source is the amounts brought in by merchants from neighbouring Arab countries who buy their goods from the Lebanese market. Others, especially the Syrians, buy their needs of foreign exchange by selling Syrian banknotes on the market.

After reviewing the sources of supply, one has to complete the picture by relating the sources of demand that utilize this supply of foreign banknotes. A general remark that the Lebanese exchange dealers ship to all foreign exchange centres in the world foreign notes whether be it Middle Eastern currencies or that of other countries.

Particular cases can be named in this respect. The Egyptian pound had once a busy traffic between Beirut and Zurich. Dollar banknotes of small denominations are still being shipped to Liberia,⁹⁷ East European currencies to Switzerland, Egyptian Pounds⁹⁸, Kuwaiti Dinars,⁹⁹ and Iraqi Dinars to Kuwait, and Gulf Rupees to the Gulf Area. Exchange dealers usually repatriate the excess banknotes of any currency if the regulations of the respective country permit such an action.¹⁰⁰

Tourists are a major source of demand for banknotes. Beirut

97. It is cheaper to buy dollar banknotes from Beirut than to import from U.S.A. by the debit of the banks account in New York; because of the charges incurred.

98. Before January, 1962

99. Kuwaiti Dinar, when repatriated, can be changed to Sterling Area account in London as will be shown in the following pages.

100. All such transactions are sold against T.T. to London or New York and sometimes Geneva and against New York and London drafts. .

being the gateway to the East, helps to sell a good amount of foreign notes to international tourists over and above national tourists.¹⁰¹

Students studying in Egypt formed always potential demand for Egyptian pounds to cover their scholastic expenses.¹⁰²

Moreover, the Egyptian pound note was always accepted for payment for certain goods imported from Egypt such as motion-picture films, books, magazines and newspapers.¹⁰³ The Syrian pound was always used by Lebanese merchants to buy Syrian goods.

The Jordan dinar is accepted by fruit and vegetable merchants selling their goods on the Lebanese market.

Employees returning home exchange their savings into their home currency if the terms are to their advantage.

The Dollar banknote is on internal demand at times for a very interesting reason. It is demanded by travel agents when the difference between the rate for the dollar as set by IATA is much higher than the rate prevailing on the market.

101. Countries whose banknotes on the market are much cheaper, than the official exchange rate in the home country are always in demand by tourists. Tourists returning home and buying respective banknotes in exchange of what remained with them of Lebanese pounds and foreign currency is also a source of demand in itself.

102. After January, 1962 the Egyptian pound was repatriated to the credit of Egyptian banknote Non-resident account acceptable for payments to cover certain goods imported from Egypt and tourism. It was officially quoted at \$.1.65 per pound banknote.

103. That was the case with the Egyptian pound. It is still the case with the Jordan Dinar. Sterling banknotes are on demand by British nationals abroad to send home in form of savings or transfers to families. This is because if they send these amounts by bank official transfers they incur tax on earning. But in this way the Government cannot trace their incomes.

The agents sell air tickets for Lebanese pounds, claim that they sold these for dollars. They buy dollar banknote from the market and claim for this Lebanese pounds at the IATA rate (e.g. IATA rate was LL.3.18 for the \$ when it was sold for LL.3.04, LL.3.06 when it was LL.2.99. As from 1st of March, 1962 IATA rate was lowered to LL.3.00).

The livestock trade is a source of demand for banknotes. The Lebanese merchants buying livestock from Turkey transfer officially a certain sum in dollars. On this transfer the merchant receive an export permit for a certain amount of livestock measured by weight, at a set price per kilo. When the Lebanese merchants start buying from Turkish side, they pay a lower price per kilo, as they buy per head and not by weight. This permits them to buy more than the officially transferred money would indicate. Accordingly, these merchants smuggle dollar notes and Turkish pound notes to pay for the livestock bought in excess due to price differences. 104

Iraqi dinars are used to pay for livestock which is smuggled from Iraq to Syria.

BILLS OF EXCHANGE OPERATIONS

This classification includes all the drafts, personal cheques, bankers' cheques, travelers' cheques and similar sight and time drafts. It is worthy to note here that only a limited

104. Turks accept the dollar banknote to sell it in the black market where it is smuggled out again in the form of capital flight from Turkey.

number of foreign exchanges have bills circulating in the Beirut Market. These are the bills pertaining to hard currencies of international acceptance, namely , Dollar, Sterling , Swiss franc, Belgian franc, French franc and Deutsche mark. Syrian and Jordanian drafts are also available on the market.

Contrary to the banknotes, bills of exchange need not come from their home country but are issued all the world over. Before starting to discuss the market for the exchange bills, the writer would like to emphasize another time the position of Beirut market as the pool for foreign exchange in the area. As foreign banknotes pour into Beirut so do bills of exchange. As a matter of fact, exchange dealers in the neighbouring Arab countries sell their portfolio of bills of exchange in Beirut against their home country's currency.

The tourists to Beirut are the main source of travellers' cheques and letters of credit. These are mainly in dollars and Sterling pound transferable. Some are in Deutsche mark¹⁰⁵ and Swiss francs too. A good amount of the travellers' cheques are sold by exchange dealers from the neighbouring countries. Several international banking institutions issue these cheques.¹⁰⁶ Some are issued by travel companies¹⁰⁷. Besides, several Arab banks issue travellers' cheques too¹⁰⁸, in dollars and Sterling.

105. West German Currency

106. Most famous among them are Bank of America, Midland Bank, Barclays Bank.

107. American Express Co. and Thomas Cook and Sons.

108. Namely, Arab Bank, Rafidain Bank, National Bank of Lybia.

Emigrant remittances to their families in Lebanon form alone a major source for foreign currency to the country. Emigrant remittances are usually banker's cheques, either New York drafts or London drafts. The latter is of two types, External Accounts and Resident Accounts.¹⁰⁹ (Known too as Transferable and Area drafts respectively).

109. After 1931, the concept of a "Sterling Area" began to emerge. It is difficult to define because its content is constantly changing and may continue to do so. Prior to 1939 one could name three leading features of the "Sterling Area" as then established.

- a. Its members tended to hold "Sterling balances" for whole or part of their central monetary reserve.
- b. They tended to have their foreign trade invoiced in Sterling. (These two characteristics were by no means confined to members of the Sterling Area nor did they come into existence only in 1931.)
- c. The Sterling Area group tended to keep their currencies fairly stable in relation to Sterling rather than to the dollar.

The larger Sterling Area, as it tended to establish itself after 1931, included, as well as the British Commonwealth and Empire (except Canada), Norway, Sweden, Denmark, Portugal, Japan and the Argentine with Greece and Turkey coming in at a later date. With the outbreak of the Second World War, the Sterling Area was consolidated, but with narrower limits. Most of the circumambient countries fell away and the Sterling Area was mainly confined to the British Commonwealth and Empire with one or two additions such as Egypt and Iraq. It enjoyed special facilities for the internal movement of funds. Its central feature was the "dollar pool". The net dollar takings were turned in by the whole area to the Bank of England and its dollar requirements financed from their central pool. To the extent that there was a net dollar contribution by the outer area, its Sterling balances rose in proportion. Exchange controls took the place of the free foreign exchange market, and "Special account" were established with foreign countries normally on a bilateral basis, by which net deficits on current payments took the form of an accumulation of Sterling balances. (By the end of the War, 1946, externally held Sterling balances had

The New York drafts are usually sent from the Americas, the London drafts are sent from Africa and the Gulf Sheikhdoms.

Although Lebanon is not a country scheduled in the Sterling Area now ¹¹⁰ (refer to chapter 4) still such cheques are negotiated on the market. To begin with, the reason that the emigrants send Sterling Area cheques to their families is because they cannot obtain exchange control permit to transfer these amounts. ¹¹¹ The rate quoted for the Sterling area cheques is usually one to five

risen from £.476 million to £.3700.- million of which latter £.2417.- million were held in the Sterling Area and £.1284.- million outside it). Moreover, the features of the postwar system must be mentioned.

I. Exchange Control has been maintained. Its main object is to prevent capital movements out of the country.

II. Within the general system, American holders of Sterling have had a priveleged position. For them free convertibility obtains.

III. Outer Sterling Area is also in a relatively privilaged position, since the British Authorities are always willing to meet, by provision of gold or dollars any deficit arising between the outer Sterling Area and the dollar area or any other country, requiring gold payments.

IV. Outside the Sterling Area there is a system of bilateral agreements which in many cases carry on the "special accounts" system of war time. Under these Sterling may be used only for the purchase of Sterling Area goods. (For further reference please see Appendix C.)

NB. Compiled from Harrod, Roy F. The Pound Sterling (Princeton: Princeton University 1952).

110. In addition to the United Kingdom, the Sterling Area comprised Burma, Ceylon, Cyprus, Ghana, Iceland, India, the Irish Republic, the Hashimite Kingdom of Jordan, Lybia, the Federation of Malaya, New Zealand, Nigeria, Pakistan, the Federation of Rhodesia and Nyosaland, the State of Singapore and the Union of South Africa, together with all British Colonies Protectorates, Protected States and Trust Territories.

111. It is reported that an important source of supply of resident Sterling is Kuwait, a Sterling areaterritory

Lebanese piasters below the rate quoted for Sterling transferable drafts.

The Syrian and Jordanian drafts are usually personal cheques on banks in Syria and Jordan or sight drafts on merchants and mercantile establishments. These are paid in cover of merchandise bought from Lebanon or for services, and students' expenses. Still more a handsome amount of these cheques are in the form of capital flight from the mother country.

Another bill of exchange of a dual character is the French Franc, namely the internal account and the Lebanese account. The former is an account for the resident of France and those countries in the Franc area.¹¹²

with no exchange control laws. Sterling is acquired by smuggling gold into Bombay and converting the rupees proceeds into Sterling, selling this in New York for dollars which are used to purchase more gold from South Africa or elsewhere.

112. The French Franc Area comprises 1. the territory of the French Republic, i.e. continental France, Corsica the Departments of Algeria, Oasis and Saoura, the Overseas Department (Guadeloupe, Martinique, Guiana and Re'union), the Overseas Territories except French Somaliland (Comoro Islands, St. Pierre and Miquelon, New Caledonia, Wallis and Futuna Islands, and French Polynesia). 2. the Condominium of the New Hebrides and 3. the Republic of Cameroon, the Central African Republic, the Republic of Chad, the Republic of the Congo (Brazzavill), the Republic of Dahomey, the Gabon Republic, the Republic of Guinea, the Republic of the Ivory Coast, the Malagasy Republic, the Republic of Mali, Republic of the Niger, the Republic of Senegal, the Republic of Togo the Tunisia and the Republic of the Upper Volta.

Payments for invisibles related to trade are permitted freely when the basic trade transaction has been approved. The exchange allowance for French Residents for tourist travel abroad is NF.1500 a calendar year. Outward Transfer of capital by residents requires approval.
I.M.F. Annual Report on Exchange Restrictions, 1961

French citizens or residents of the Franc area still draw personal cheques on their internal accounts to cover their expenses in Lebanon. Moreover, Lebanese emigrants to French West Africa intending to transfer their capital to Lebanon usually transfer their accounts first to France where their African franc is exchanged for French francs. The following step is that they draw cheques on their account in France which they negotiate on the Beirut market for Lebanese pounds. The quotation for internal account is around one Lebanese piaster per N.F.F. below the rate quoted for external accounts.¹¹³

Now the demand for the bills of exchange has generally the same end, namely to be credited to the balances of the purchasers in London and New York. These balances are used to cover trade transactions of goods and services.¹¹⁴ Undoubtedly, Sterling Area drafts are not credited in London to accounts of Lebanese residents as it is contrary to the British laws. This is done in several ways.¹¹⁵ Accounts are kept in the name of British residents who

113. For further reference please see appendix "C"

114. This will be discussed further in Chapter 6 on Commercial Banks.

115. New York is the most important for this type of unofficial transactions known as "cheap currency". Sterling, because of its general use in international trade, is the most widely traded currency in unofficial markets for inconvertible currencies. The weekly turnover of inconvertible Sterling in the New York market has been variously estimated at from £.500,000 to £.2000000 during 1951-1952. The actual volume of transactions varies with conditions of demand and supply. When certain countries have large amounts of inconvertible sterling which they are anxious to exchange for dollars, the dollar price, of course, will fall. As the spread between American account sterling and inconvertible or cheap Sterling widens, it becomes profitable for American importers to cover their imports from the United Kingdom or Sterling Area countries, by purchasing cheap Sterling.

NB. compiled from Mikesell, R.F. Foreign Exchange in Post-War World, (New York: The Twentieth Century Fund, 1954).

have been dead for years. Exchange dealers in Lebanon open fictitious offices in Sterling Area countries such as Kuwait or Jordan. These offices open Sterling resident account under their name. The Beirut office credits the account with drafts it purchases and sells transfers in the name of the Kuwaiti office as if orders are coming from the Kuwait office. The Sterling Area balances are used for three main purposes:

1. As transfers to residents of Sterling Area countries;
2. Sold against dollars on the London foreign exchange market;
3. Import of goods from the Sterling Area countries. It is cheaper for a Lebanese merchant to import tea for instance from Ceylon through Sterling resident account. The order is made in the name of the Amman office for instance. Goods are shipped to Beirut Port-Zone-Franche, in transit. Once the goods arrive there the Lebanese merchant acting on behalf of Amman Branch disposes of the goods.¹¹⁶

What applies to Sterling area applies to French franc internal account but on a limited scale because of the nature of the franc area trade. The Jordan and Syrian drafts are smuggled through the borders to be cashed and credited to the accounts of the Lebanese exchange dealers and opened by their agents in the respective countries. These accounts are used to pay Jordan and Syrian exchange

116. It is estimated that Bank of England lost Dollars 100 million on wool sales from Australia to U.S.A. during one year. Cheap Sterling is also used extensively to pay for services including transportation, insurance and tourism. Such transactions may be financed with little risk, since the British exchange authorities are less able to check payments not related to commodity sales.

Ibid, p.199.

dealers who smuggle dollar and Sterling drafts to sell on the Beirut Market.

There are some other foreign drafts on the market, but they are not dealt with on a large scale.

UNOFFICIAL TRANSFER OPERATIONS (HAND-PAYMENTS)

The operations to be discussed below are usually encompassed by the high walls of secrecy. These operations are done between countries with controlled economies and those with free economies and open markets. The aim is to evade the prevailing laws and regulations pertaining to movements of private capital and consumers' goods. In this respect, the writer would like to state clearly and bluntly that he does not claim to be an authority on these transactions, yet he will not fail to write down every word he believes will clarify and explain such operations.

A main fact about these unofficial transfers is the ever changing nature in the methods in which they are executed. This is because of two reasons: one, to evade the watching eyes of the exchange control men in the respective countries; two, the changing regulations that are issued every now and then to stop the stream of capital flight or similar unofficial transfers, in the concerned countries.

Comparatively, speaking, Lebanon is the most stable country in the area. Moreover, it is supporting an open market which facilitate the entry and exit of capital. Consequently, whenever social, political or economic conditions are altered in any country to the disadvantage of a class or group, the concerned individuals start

to seek refuge for their capital outside their countries. The existence of exchange controls hinders these movements. This being the case, these individuals have to depend on unofficial transfers. The Beirut market is supplied through several methods.

The most familiar method used in unofficial transfers is the following:- The individual wishing to transfer meets the agent in his home town, pays the amount on the agreement to receive the equivalent in Beirut in the same currency less a commission of around ten percent. The transfer is delivered, against a word given to the transferer, who leaves to Beirut, by the agent according to previous agreement with the exchange dealer in Beirut.

This method is used for the transfer from Egypt. The transferer receives, in Beirut, Egyptian Pounds which he exchanges for Lebanese pounds or dollars according to his needs. This applies too in case of Syrian transfers; Iraqi transfers, Jordanian transfers and Pakistani transfers.

Another method fits a person residing in Beirut and who has an account in another country. This person draws a cheque on his personal account drawn to self and endorsed in blank. He gives this cheque to the exchange dealer in Beirut. The exchange dealer sends it to his agent in the respective country where it is collected. The exchange dealer is informed of the collection and pays to the drawer either in the same currency or its equivalent. This applies too, to the countries mentioned above.

Another method is that the exchange dealer gives the transferer an address to which he goes and pays the money without receiving

a receipt. Later that amount is delivered less the agreed commission. It is important to note here that the commission varies considerably according to the risk taken, the country under question, and forces of supply and demand. This method is used too in the above mentioned countries.

The transferrer is sometimes given a code word or sign by the agent to the exchange dealer in Beirut to pay a certain sum of money¹¹⁷. The more interesting means under this method is to use one pound lebanese banknotes. The notes are each cut into two parts. Both parts carry the same serial numbers. The transferrer who is residing in Beirut takes a half and sends it home to a relative or representative and the exchange dealer takes the other part and sends it to his agent in the respective country. Once the agent receives it, he calls on the given address and presents his half. Upon identifying the serial numbers the representative pay the agreed amount to the agent who informs the exchange dealer in Beirut to pay. These are the methods used here between Beirut and the neighbouring countries to transfer capital from these countries to Beirut.¹¹⁸ In case the capital to be transferred is in Africa or South America, for instance, the arrangement is slightly different. This is because Switzerland plays the role of the intermediary in the transaction.

117. e.g. Deliver three tons of rice = pay three thousand pounds. My baby has now four teeth = Pay forty thousand dinars.

118. The Cairo daily newspaper "Al-Ihram" reported that the exchange control authorities there arrested a gang while executing a similar operation-the pound in halves was used as the secret sign. Al-Ihram Friday, April 6, 1962 year 88, N.2.

These transactions are not only done in case of capital transfers but they can as well be made to pay for smuggled goods. It takes the form of triangular transaction.

Goods are smuggled from Kuwait to Baghdad to evade customs duties or because these goods are forbidden to enter Iraq (e.g. luxury goods). A transfer is made to Beirut, hand payment. The agent in Beirut exchanges the Iraqi Dinars for Kuwaiti Dinars where this amount is either credited to the account of the Kuwaiti merchant in the Lebanese banks or the sum of money is sent to Kuwait.

In most cases the payment for smuggled goods are made in banknotes because of mistrust. 119

We already discussed the supply of unofficial transfers to Beirut. The second part of our task is to discuss the demand in Beirut for these transfers. That is, how the Lebanese exchange dealers are compensated for the payment they make in Beirut.

The main demand for hand-payment is caused by the cheap rate quoted for it. In countries where banknotes are not repatriated hand-payments are a cheap transfer of capital. Moreover, the demand may be due to payments to cover goods imported from the country in question. Still more when the Egyptian banknotes were forbidden to enter Egypt, and as it is the condition after January,

119. In case of capital transfers the trust is there. This is because it is the permanent business of the agents and exchange dealers, while merchants need not depend on that type of business; it is not their line.

1962 the hand payment are cheap transfer of money into Egypt.

Hand payments are on demand too by foreigners residing temporarily in controlled economy countries. These usually receive payments from their home country in hard currency. If exchanged in the country of residence they are paid according to the official rate, while if they transfer the same payment to Beirut instead of receiving them in Turkey for example, they can exchange the hard currency into Lebanese pounds and buy for these hand-payment in Turkey.¹²⁰ Moreover, in the case of Turkey, hand-payments are used to pay for livestock as mentioned earlier in this chapter Airlines. companies cover their expenses through hand-payments. They as well transfer their receipts in the same way. But this is only possible in countries whose exchange control system is weak, and inefficient e.g. Iran.

At this juncture it is of importance to note that persons who make most use of hand-payments are the foreign diplomats. To begin with they have access to transferable accounts or drafts. They sell these on the Beirut market and buy with the proceeds hand-payments in their country of residence; the difference between the price in Beirut and that in the Sudan or Pakistan, for instance, is worth the trouble.¹²¹

120. One U.S. dollar is exchanged for 9 Turkish lira while one can get 13 to 14 Turkish liras for one U.S. Dollar on the Beirut market.

121. The difference amounts to about 30% of the original value of the Pakistani Rupees.

The above was a general summary of the activities of exchange dealers. In the following chapter the activities of the commercial banks in the exchange market will be discussed. No doubt that there exist links between the activities of both parties and consequently the writer will continuously refer in Chapter VI to the material in this chapter.

In the following chapter the rest of the picture of the foreign exchange market will be sketched out. These two chapters will be the basis for the evaluation which will follow.

CHAPTER VI

FOREIGN EXCHANGE MARKET IN BEIRUT II

COMMERCIAL BANKS

A CREDITOR IS WORSE THAN
A MASTER. FOR A MASTER
OWNS ONLY YOUR PERSON. A
CREDITOR OWNS YOUR DIGNITY
AND CAN BELABOUR THAT.

VICTOR HUGO

Banking is a prosperous business in Beirut. The number of banks has doubled in the last decade. Although foreign exchange is not usually the major business of a commercial bank in general, it is being given great attention by the Beirut bankers. This is attributed to three main factors: the first is the large profits obtained from foreign exchange transactions, the second is the large balance in foreign exchange carried by the Lebanese banks,¹²² and the third is the fact that most of the national banks started as offices dealing only in foreign exchange.

Commercial banks and exchange dealers share some features in their dealings in foreign exchange, although some operations are exclusive characteristics of the banks. We find banks purchasing foreign coins and notes, cheques, drafts and other types of exchange bills. Banks also sell foreign coins and notes, but never does the bank act in the capacity of the exchange dealer and resell the actual drafts which it purchases. Consequently the discussion will focus in this chapter, on the foreign exchange dealings that banks undertake,

122. See Chapter II, on banks.

referring only whenever necessary to transactions that exchange dealers share with commercial banks.¹²³

FOREIGN EXCHANGE DEALINGS

The bank has two main sources of foreign exchange for its foreign exchange dealings. The first is the actual foreign exchange operations undertaken by the foreign exchange department in the bank and the other is the foreign exchange that results from the usual banking transaction in the other departments of the bank.

It is more feasible for our purpose to start by discussing the second source of foreign exchange in banks. Almost all banking activities of the Beirut banks result with foreign exchange. This is because the main role of the commercial banks in Lebanon is to finance trade which in Lebanon happens to be primarily foreign trade. The banking activity nearest to the foreign sector is that of the issuance of letters of credit,¹²⁴ and similar tools to facilitate the import and export of goods to the Lebanon and the triangular trade transactions. Lebanon is a net importing country of goods and a large amount of the foreign exchange balances is used for this purpose. The exports of the country yield a small proportion

123. It is of importance to point out here that some business organizations which carry the statute of a bank are only working in the capacity of exchange dealers. This is one of the defects that results from the lack of a banking law in Lebanon.

124. There are several types of credits namely, confirmed, credit, unconfirmed credit, documentary credit, clean credit, and revolving credit. The confirmed credit is the simplest form of the bank credit in which the importer arranges for his bank to accept drafts drawn on itself by the exporter. The exporter is called the "beneficiary" under the credit, and, on presenting the

of foreign exchange. Most credits opened in Beirut are against payment and therefore no drafts or exchange bills result from this activity. On the other hand, a rather large amount of goods are imported against documents for collection as well as time drafts. These are only sent to customers with good credit standing and strong and old relations with the foreign exporters. Under this the collecting bank assumes no responsibility but rather acts on behalf of the foreign bank or exporter. The bank only remits the value of the documents. When letters of credit are involved the opening bank (i.e. Lebanese) is debited by its foreign correspondent when the latter pays the value of the documents to the beneficiary. Usually, the Lebanese client¹²⁵ pays interest from the day

documents to his own banker as evidence of his right to draw; he is able to sell drafts on the bank granting credit at the best available market rates. Unconfirmed credit should be carefully distinguished from the confirmed credit. In the latter case, there is an unequivocal undertaking on the part of the bank to accept bills drawn under the credit, provided that they conform to the conditions laid down therein. In the case of an unconfirmed credit, there is no such definite undertaking; if bills are drawn on him the banker may or may not accept them. Where a documentary credit is granted, the banker does not undertake to accept bills, but to negotiate them. The credit is opened by the importer in favour of the exporter, and the bank granting it undertakes to make advances to the exporter against drafts which he draws on the importer. Clean credit is unsupported by documents, and is granted to an importer whose credit is high. The banker negotiates the bills, but does not accept them. As for the revolving credit, the beneficiary of a credit does not necessarily exhaust it by a single shipment; where a credit is granted for a series of transactions, it is after provided that bills up to a certain amount may be drawn, and on those being honoured the credit is automatically renewed for the drawing of further bills.

125. Known as the principle.

the documents are mailed by the foreign correspondent bank¹²⁶ until the client terminates the credit.

When the Lebanese banks act in their capacity as foreign correspondents, they pay to the Lebanese exporters the counter-value of the documents in Lebanese pounds and are credited with the value in foreign exchange by the issuing bank. Through the above mentioned transactions the documentary credits department contribute to the foreign balances of their respective banks.

Cheques and drafts which are accepted for negotiation on the market are sent for collection to the foreign centers. Some foreign exchange bills are discounted in the Lebanese banks. Usually, these bills belong to Lebanese firms and are drawn on foreign firms against Lebanese goods and services.

Lebanese investors speculate and invest in foreign stock markets.¹²⁷ The yields and capital profits of these stocks and shares are a source of foreign exchange to the balances of the banks, in their capacities as trustees on behalf of their customers.

The largest share contributed to the foreign exchange balances of the banks is through the accounts opened by Lebanese nationals and foreigners in foreign currencies. Most of these accounts represent capital transferred from areas with unstable economic and political conditions. Part of these accounts are in the form of hot capital but the rest, which is a handsome amount, is in the form of deposits which earn interest of three

126. Usually correspondent banks mail documents on the same day they pay their value to the beneficiary.

127. New York stock market, London stock Market and Paris stock market.

percent on the average. Some of these accounts pertain to emigrants who remit part of their monthly savings to Beirut, to the credit of their accounts.

Banks may carry current accounts in foreign notes in favour of their clients. But hardly any bank would keep in its vaults foreign notes and coins, whether its own or balance of customers above a certain minimum, which is usually low. This behaviour is justified by the fact that banknotes in general and foreign notes in particular are a source of loss to the bank because they have no yields. Accordingly foreign notes and coins are sold to exchange dealers or repatriated whenever they accumulate. Banks act as clearing houses for international debts. They buy rights to wealth in term of other currencies, from those who have them to sell and sell rights to wealth in term of other currencies to those who wish to buy them. The usual form of those rights to wealth has already been described. Banks sell rights to wealth in more than one form. Banks draw cheques on foreign centers against their balances there. They transfer by airmail upon request of their clients to pay for services rendered or goods imported from abroad. Banks also sell telegraphic transfers to be paid immediately in foreign centers in cover of operations of high value and urgent nature. Foreign~~exchange~~ departments in foreign banks also render services to citizens of the country. They sell travellers' cheques to persons journeying abroad. ¹²⁸ They also issue personal letters of credit for the same purpose. ¹²⁹

128. No Lebanese bank issues traveller's cheques. These cheques are issued by American and British Banks and sold to Lebanese banks for meagre commission.

129. See Exhibit One.

FUNCTIONS OF THE FOREIGN EXCHANGE MANAGER

The exchange manager usually has a long busy day. The business day starts early in the morning when the manager starts receiving cables from the bank's branches or correspondents in the foreign centers, each cable indicating the closing rates ruling in other centres at the end of the previous day and prevailing trends on the market.

Over and above these cables the manager receives the COMTEL Reuter, a bulletin issued daily by the Arab News Agency,¹³⁰ in Beirut. The agency receives quotations from the main foreign exchange centers of the world.¹³¹ This process of information collecting is a necessity for the manager before establishing his rates and his plan for the day. Once all this information¹³² is available the rates can be born. It is important to point out here that almost all the main banks of Beirut receive the same tools and means of information which helps to produce homogeneous quotations for the different currencies.

THE ROLE OF THE U.S. DOLLAR IN THE MARKET

The U.S. dollar is the currency whose rate against the Lebanese pound determines the rates for the other foreign currencies

130. This Agency is an affiliate of Reuter's News Agency.

131. The bulletin reports rates in Zurich, London, New York, Paris and Milan.

132. There are also two other bulletins which supply information to the market; the Bourse de Beyrouth bulletin of foreign exchange rates and gold coins prices on the Beirut market, and the "Commerce du Levant" bulletin which is a publication of some twenty pages quoting various information about the foreign exchange market in Beirut, the stock exchange market, the commodity and stock exchange market and precious materials market in London, New York and Paris.

EXHIBIT ONE

PERSONAL LETTER OF CREDIT

Ref. NB/2/5

May 15, 1962

The Manager,
The Chase Manhattan Bank,
41, rue Cambon,
Paris.

Dear Sir,

Our good customer Mr....., the bearer of our letter will be calling on you during his stay in France. Any courtesy extended to him will be greatly appreciated.

Furthermore, we shall be glad if you would kindly accept his drawings on us up to a total sum of NF.3225.- (THREETHOUSAND TWOHUNDRED TWENTYFIVE NEW FRENCH FRANCS ONLY), debiting our account with any amounts drawn under advice.

Every drawing under this credit should bear reference to it and all payments made under it are to be endorsed thereon.

Thanking you for your kind cooperation, we remain,

Yours faithfully,
For A.B.C. BANK

in Beirut's foreign exchange market. No doubt the importance of the U.S. Dollar is not only realized in Beirut but in other foreign centres as well, but the significant fact is that the other foreign centres have their own home currencies on international demand which is not the case with the Lebanese pound.¹³³

Accordingly, as the U.S. Dollar is accepted internationally and in Beirut is interchangeable for the Lebanese pound, and as the dollar is quoted in all foreign centres, it is but normal for the Beirut market to accept it as the base to quote other foreign currencies. The dollar is the thermometer or measure that the Beirut market uses to check its position with the other foreign centers. Therefore, if the Beirut market quotes a rate for the dollar against the Lebanese pound, it could value the other currencies, and consequently quote their rate to the Lebanese pound.

HOW THE EXCHANGE RATE IS BORN

With the U.S. Dollar rate known to him, the exchange manager starts preparing his exchange rate bulletin. The exchange manager can choose the rates of any foreign center where the dollar is usually quoted and calculate the rate for the other currencies. It has become the practice and tradition in Beirut's market to accept the rates quoted in London as the base for the calculation, but at the same time not neglecting the other foreign centres especially

133. The Lebanese pounds is not quoted in the international market, as it is the case for the Sterling pound the Swiss franc etc. For such currencies one finds their rates in all centers fluctuate similarly.

when calculating the rate for the home currency of these centres.
The following illustration will show how these rates are calculated.

London Foreign Exchange Market closing rates

U.S. Dollar to £.	\$2.8150
Switch (Area) to £.	\$2.8130
Swiss Franc	SF.12.25
French Franc	NF.12.80
Deutsche Mark	DM.11.25
Dutch Florin	D.Fl.10.17
Swedish Kronor	S.Kr.14.50
Danish Kroner	D.Kr.19.40
Italian Lire	It.L.1749.75

etc. (These are medium rates)

The closing rate for the dollar on the Beirut market was LL.3.0010. Therefore, the calculation will follow thus:-

$$\text{£. } 2.8150 \times 3.0010 = \text{LL.8.4478}$$

$$\text{£(area) } 2.8130 \times 3.0010 = \text{LL.8.4328}$$

But when calculating the other rates quoted on the London market, one stops multiplying and starts dividing. That is dividing the Sterling rate against the LL. by the Deutsche Mark (for example) rate against the Sterling, because there is no other relationship between the Lebanese pound and these other currencies other than this medium.

The rate for the D.M. is	$\frac{8.4478}{11.25}$	= LL.0.7509
The rate for the D.Fr.	$\frac{8.4478}{10.17}$	= LL.0.8306
The rate for the S.Kr.	$\frac{8.4478}{14.50}$	= LL.0.5826
The rate for the D.Kr.	$\frac{8.4478}{19.40}$	= LL.0.4353
The rate for the LIT	$\frac{8.4478}{1749.75}$	= LL.4.828 per 1000 units

Now the rate for the French franc and the Swiss franc, can be calculated differently.¹³⁴ That is to say they may be calculated as quoted in their home center.

e.g. The rate for the U.S. Dollar in Zurich is SF.4.34 and accordingly. The rate in Beirut for SF. would be: $\frac{30010}{4.34} = \text{LL.0.6914}$

e.g. The rate for the U.S. dollar in Paris is N.F. would be $\frac{30010}{4.90} = \text{LL.0.6124}$

The Mid-Eastern currencies, are treated differently. There are two major sections into which these currencies can be classified: independent currencies¹³⁵, and Sterling Area currencies. Both classifications are affected by two main factors, the law of supply and demand and the rate quoted for the currency against the dollar in their home country. A currency like the Egyptian pound is mainly dependent on the law of supply and demand, while a currency like the Kuwaiti dinar, a Sterling Area currency, is determined by more than one factor including its relation to the Sterling Area, as the dinar is a satellite of the Sterling pound and, therefore, its rate against the dollar is usually close to that of the Sterling pound; the rate of the U.S. dollar in Kuwait, and the demand for the Kuwaiti dinar in Beirut.

The Gulf rupee rate is calculated according to the relation of the Rupee to the Sterling pound. There are about 13.33 Rupee in Sterling pound and as the Gulf Sheikhdoms are part of the Sterling

134. The same way apply to the Italian Lire except that although the Milan market is important it is not completely free, government intervension is always there to maintain a certain level for the rates.

135. Independent currencies are those currencies which stand alone forming their own area inside the borders of their countries.

Area, the rate is calculated by dividing the quotation for Sterling Area by 13.33 thus $\frac{8.4328}{13.33} = \text{LL.0.6326}$

The rate is quoted according to the interplay of the forces of supply and demand.

After preparing his bulletin, the exchange manager (or his assistant) contacts the market to compare the rates before typing the bulletin for distribution to the different departments concerned. Calls are made to other banks to check for two rates, the Dollar and the Sterling pound.¹³⁶ Other calls are made to exchange dealers to check with them the rate for the foreign notes and coins because they are in closer contact with this commodity, as it is their business. After the exchange rates bulletin is typed and distributed, calls by the exchange manager, continue. He keeps himself in continuous contact with the market. Almost all banks follow the same technique.

FOREIGN EXCHANGE POLICIES

In order to keep in exact touch with the state of his accounts in other centers, the exchange manager keeps a "position sheet" or book which is started each morning with the approximate total credit balance or overdraft in each foreign centre (most banks maintain accounts with several banks in each principal foreign centre) as agreed at the closing of the previous day by the accounts department. As he transacts each operation of purchase or sale, the exchange manager will either debit or credit the amount of currencies to the balance in the relative centre, making a note at the side of the class of instrument dealt in.

136. Because if those two rates are agreed upon the rest will simply follow as explained.

He can thus see at a glance whether he is becoming overbought or oversold and effect adjusting operations accordingly. The exchange manager endeavours to carry out his operations in such a manner as will show a reasonable profit for his bank by buying at one rate and selling at another. It is by no means essential that he should cover a purchases or sale of one class of instrument by the sale or purchase of another instrument of the same type, and in fact, much of the bank's profit is derived from covering one class of transaction by means of a different class of transaction. For instance, he may cover a purchase of "cheque" by a sale of T.T. or a purchase of long bill by a sale of forward T.T. depending upon the funds which he may have available at home and in the foreign centre and the rates of interest which he can obtain.

The policy followed by the exchange manager varies from bank to bank. The degrees of the variation depends on the abundance and scarcity of foreign exchange balances of the concerned bank. This policy is not definite and determinate for any bank. Rather the policy is drawn according to the changes in the composition of the bank's deposits of Lebanese pounds and foreign exchange.

If a bank has a large proportion of deposits in foreign exchange it may be short of Lebanese pounds. Its reserves are in foreign exchange. Such a bank usually tries to keep its "position" covered in regards to its CFC accounts (customers foreign currency). This precautionary action is to avoid risking a "run on position". Damage could result when the exchange rate changes to the disfavour of the bank. A bank in such a condition would always be a seller

of foreign exchange to obtain Lebanese pounds. These sales could either be spot or forward contracts while on the other side there is the bank which has scarcity in its foreign exchange balance with abundance in Lebanese balances. Such a bank would be a purchaser of foreign exchange, whether against spot or forward operations, until his needs are satisfied.

The branches of foreign banks have a more peculiar situation. Due to the confidence of the public in the bank, it has a large proportion of its deposits in Lebanese pounds. But these branches are limited by their central offices to arrange facilities for their Lebanese customers. Under such conditions these banks would stand as purchasers of foreign exchange against their Lebanese pounds deposits. They also offer sales operations on the Beirut market whenever their "position" permits.

The type of operations undertaken by the banks on the Beirut market could be classified in three attitudes; speculation, investment, and "go home with a square book" attitude. This last attitude is mainly the characteristic of smaller and the more conservative banks. The exchange manager in these banks, is expected to set off, within narrow limits the totals of his purchases and sales of any currency each day, and is not allowed to leave any substantial amount of currency "uncovered". In other words he must not show either an unduly heavy over-bought or over-sold position at the end of the business day. Moreover, he will not carry a "position". He will not touch the foreign balances of his customers unless a very safe and profitable opportunity arises. Such a bank cannot be considered an active member of the market but rather a passive member. It will not undertake foreign exchange operations as such for the sole sake of earning a profit from exchange, but

exchange operation for that bank is an auxiliary activity to the other activities of the bank. The foreign exchange department will only be rendering a routine service to the customers and concerned departments of the bank.

Therefore, the active part undertaken in the market is that of investors and "speculators". Branches of foreign banks play an important role in the investment of foreign exchange. Local banks may deposit Sterling balance for interest with these branch banks.¹³⁷ These banks (usually American) invest these Sterling balances in Japan.¹³⁸ Other banks are not familiar with the Japanese money market to invest their Sterling balances there.

Lebanese banks may also carry these balances with British banks in London where the bank rate is high. Some banks buy for their account in London, treasury bills or war bonds which give a fair yield coupled with a safe investment liable to speculative rise. A more elaborate method of investment is carried on by banks with efficient exchange managers and strong connections in London. These banks sell spot in London part of their Sterling balances, say £.100,000.- against U.S. Dollars. At the same time they purchase forward Sterling against U.S. Dollars for, say a three months period. In Beirut they swap the dollar against Lebanese pounds for the same period of three months. When the two forward contracts

137. Interest may reach up to 5% or some ½ percent below the bank rate in England.

138. The interest paid on Sterling balances in Japan runs as high as 9% usually.

mature they receive the dollar in Beirut transfer it to New York for account of the party that will deliver the Sterling in London and the cycle is complete. Such transactions will benefit the banks in two ways first, the interest they receive on the forward contract in London and second the investment of the Lebanese pounds in Beirut. Before discussing the forward exchange transactions in Beirut, we have to examine what happens to the dollars that are swapped in Beirut for Lebanese pounds. If the other party is a branch of an American Bank it usually invests the dollars through its head office in New York. This dollar may even be used to purchase Sterling for investment in London in long bills maturing in the period of three months; in this case the Sterling is sold against dollars. According to this arrangement the bank will benefit from both the interest on the long bill and the interest on the forward contract. The dollar was at one time invested in Syria where it was used to finance foreign trade before exchange controls were installed. Banks used to give loans to Syrian exporters of grain and cotton to help them comply with their international trade obligations.

FORWARD EXCHANGE OPERATIONS

If we neglect, for the time being the transactions that happen outside the Beirut market by the Beirut banks, we find that the swap is the main if not the only forward exchange operation on the market. As it has been mentioned in Chapter 3, swaps are operations consisting of a simultaneous sale or purchase

of spot currency accompanied by a purchase or sale, respectively of the same currency for forward delivery.¹³⁹

Swaps are widely used on the Beirut market. The main aim is to exchange a currency, a bank does not need for the time being, for a currency it needs for one project or the other. But as the bank does not own the foreign currency or cannot sell foreign exchange for fear of loss due to changes in the exchange rate, it swaps this foreign currency against Lebanese pounds. The majority of the swap contracts are made against dollar.¹⁴⁰

The cause that lead banks to enter into swaps contracts are various. The bank may need to cover a dollar "position" it "ran" at some earlier date. The bank may be out of Lebanese pounds. Therefore, it swaps its dollar deposits for the sake of liquidity, in Lebanese pounds. Swaps are also used as safeguards against fluctuations in the exchange rate. The two parties utilize the funds for their purposes up until the contract matures. When returning to their original positions their exchange balances are still the same, as no loss or profit on exchange accrued.

Swap contracts are charged with interest according to the forces of supply and demand of either currency and for swap contracts. The interest ranges between 1/8 to 1/4 per cent per month, which is

139. See Exhibit Two

140. Swaps are made too for any other currency. Foreign notes swaps are familiar too, especially Syrian pound.

EXHIBIT TWO

SWAP CONTRACT

Ref. NB/2/7

18th January, 1962

The Manager,
XYZ Bank,
Beirut.

Dear Sir,

This is to refer to our telephone conversation of to-day and to confirm that we have sold you the sum of \$.200,000.- (TWOHUNDRED THOUSAND U.S. DOLLARS ONLY), at the rate of 300, which amount we have remitted by cable to your account with Messrs. The Chase Manhattan Bank, New York, value to-day.

It will be greatly appreciated if you kindly credit our Lebanese Pounds Account with Messrs. Banque de Syrie et du Liban Beirut with the sum of LL.600,000.- (SIXHUNDRED THOUSAND LEBANESE POUNDS ONLY), in settlement.

We also confirm that we have bought from you the sum of \$.200,000.- (TWOHUNDRED THOUSAND U.S. DOLLARS ONLY), at the rate of 300, to be delivered to us on 18th March, 1962.

Yours faithfully,
For A.B.C. BANK

usually added to the rate used as the base for the swap contract on maturity. If the dollar is abundant, the bank offering the dollar against Lebanese pounds pays interest while if the dollar is scarce the bank demanding the dollar against the Lebanese pounds pays the interest. At times when forces of the market are equal or rather cancelling each other, the swap contract is made at par.

When the contract is signed, the bank offering the dollar transfers by cable the agreed amount to the account of the second party in New York, as desired. The second party offering the Lebanese pounds credits the account of the first party with Banque de Syrie et du Liban on the same day.

Accordingly, both banks are credited on the same day to preserve value date. In case the swap contract is for foreign notes, the physical exchange of currencies takes place on the spot. When the contract matures and no party is wishing to renew the contract the second party credits by cable the dollar account of the first party in New York while the latter credits the Lebanese account of the second party with Banque de Syrie et du Liban, Beirut plus or minus the interest charge (if any). If both parties agree to renew the contract and there are interest charges involved, the debtor pays the creditor the charges of the matured contract and start a new contract tied on the old base rate, already agreed upon. Otherwise, if the swap contract is at par, this question does not arise.

Another forward exchange activity is undertaken by the Beirut commercial banks outside the Beirut market. This type of transaction is undertaken under the speculative attitude we mentioned earlier. The transaction is a contract under which the purchaser agrees to take up sight exchange at a future date at a predetermined price. When the bank becomes liable under the contract to take up the exchange, it sells an equivalent amount at the current sight rate; the difference between the contract rate and the actual rate will constitute the profit or loss on the operation. The Beirut banks usually enter such operations on the London market where specialized houses in such operation are always able to transact such contracts. The Beirut bank will make a profit if the exchange has moved against the Sterling and a loss if it has moved in favour of it. The principle is identical if the Bank sells exchange (dollars in the case of Lebanese banks) for future delivery. The purchaser then becomes obliged under his contract to pay (in Sterling) for the sight exchange at the future date, and the Beirut bank is under an obligation to deliver dollars on that day. The dollar must be bought at the rate then ruling, and if that rate has become favourable to the Sterling, the bank will gain; otherwise it will lose. 141.

-
141. The following examples will illustrate the operations mentioned above. In the first case :
- | | |
|--------------------------------|-------------------------------------|
| Purchase forward exchange | |
| \$.200,000.- | at \$.2.79 a £ |
| Sell spot exchange on maturity | |
| \$.200,000.- | at \$.2.78 a £ |
| Profit realized | |
| 2.79 - 2.78 | = \$.0.01 |
| | = \$.2,000.- |
| | or a loss if the spot rate was 2.80 |

THE BROKERS

Brokers were discussed in the previous chapter, as was their role in terminating transaction among exchange dealers. Brokers also terminate transactions among commercial banks as well as between exchange dealers and commercial banks. Moreover, the brokers are the contact between merchants and commercial firms and the exchange market.¹⁴² Their income is derived from a commission they receive on the transaction they undertake. Usually their commission is paid by the party that asked for their service. The commission ranges between LL 0;0005 and LL. 0.0007 per unit of foreign currency. They may as well receive an equivalent amount from the second party if their bid is attractive, or if they can bargain on their bid for earning the commission. Brokers are now losing business as telephonic communications are steadily improving. Moreover, the increasing number of exchange dealers and commercial banks is accentuating competition. This is leading to narrower and narrower margins, which directly effect the percentage commission paid to brokers and the number of transactions they undertake.

EXCHANGE MARKET SANCTION

The "name" of the seller of any exchange instrument is of the first importance to the buyer. Even between the big banks themselves, each has a "limit" to the total obligation.

In the second case
sell forward exchange
\$.200,000.- at \$.2.79 a £
Purchase spot exchange on maturity
\$.200,000.- at \$.2.80 a £
profit realized
2.80 - 2.79 = 0.01 = \$.2,000.-
or a loss if the spot rate was 2.78

142. Brokers in Beirut are not similar to the brokers in European or American centres. they have no offices

of the other which may be allowed to remain outstanding at any one time and, as the grade of the other party descends, so the amount of the "limit" on that name decreases. In the case of cheques, demand drafts, and similar exchange bills, the operation of purchase is similar to the discounting of a bill, and while attention is paid to the standing of the drawee or payee, even more is devoted to the standing of the customer from whom the articles are being purchased. With the exception of encashment under personal letters of credit for which the purchasing bank must assume responsibility, and so must take every precaution against fraud when effecting such payments, banks will purchase exchange instruments only with recourse to the seller and only from regular customers. In order to make the responsibility of the customer clear and to relieve the bank from liability in respect of any acts of its agents or of any expenses incurred in connection with instruments purchased, it has been customary to take from the customer a general form of authority for collection or negotiation of foreign bills. The customer agrees that any such operation shall be at his entire risk and responsibility and that in addition to any rights which the bank may acquire as holder of any such articles, the bank shall have the right to debit the customer's account immediately with the value

and no employees or assistants. They work on an individual basis and their incomes are limited.

of any such articles which may be unpaid, together with any charges which may have been incurred. The written form of this agreement has been neglected on the market. Instead this behaviour has become part of the traditions and customs that prevail on the market and govern its daily routine proceedings.

ROLE OF BANQUE DE SYRIE ET DU LIBAN IN THE FOREIGN EXCHANGE MARKET

One of the functions that Banque de Syrie et du Liban undertakes which usually characterise central banks is its interference on behalf of the Lebanese Government in the foreign exchange market.

The general purpose of the interference is to mitigate undue fluctuations in the exchange rate of the Lebanese pound. Its first interference after the abolition of exchange regulations in 1948, was in the year 1953, on behalf of the Exchange Stabilization Fund.¹⁴³ During the fall of 1953, many merchants became insolvent and then bankrupt as a result of their inability to liquidate their stocks of piled goods, most of which were bought at relatively high exchange rates. The Fund "which feared that further appreciation might impair the country's competitive position" and which was concerned with the rise in the number of bankruptcies, got into the exchange market and bought dollars whenever its rate fell below LL. 3.20. It used government

143. By decree Number 8 - October, 1946 this Fund was established to be managed by a board formed of :
Minister of Finance, Director General of Finance,
Controller General of Exchange, Director of the Issue
Dept. (B.S.L.), Official delegated by the Minister of
Finance. The Fund's assets are \$.0.50 million only
but it has access to Government deposits.

deposits to purchase dollars. These dollars were put in the note cover against an increase in fiduciary issue. Additional issues were remitted to replenish government accounts. As economic conditions improved the fund represented by the Banque de Syrie et du Liban allowed the dollar to drop, interfering only every now and then so as to slow down the depreciation of the dollar against the Lebanese pound.

Two factors are responsible for the Banque de Syrie et du Liban's reluctance in interfering in the market. The first is the good economic conditions in the country and the second is the inflow of foreign exchange into the country, which made it difficult for the fund to interfere and stabilize the dollar rate. ¹⁴⁴

Early in 1961, Banque de Syrie et du Liban tried to keep the rate for the dollar above LL. 3.05 as long as possible. Later, in the last quarter of 1961 and first quarter 1962, the Banque de Syrie et du Liban was trying to keep the dollar from falling below LL. 3.00. At this juncture it is interesting to note that commercial banks speculate on the intervention of Banque de Syrie et du Liban. Let us suppose that the dollar rate reached LL. 3.00 (selling rate). ¹⁴⁵ The Banque de Syrie et du Liban exchange manager would start calling the different banks and offer to buy 50,000 to \$. 100,000.- per bid, according to the "name" of the bank. When the banks realize this they start buying at the market rate and accordingly the price will rise.

144. The different implications on this matter will be discussed still more in Chapter VII.

145. Buying rate in this case would be LL. 2.99875 for T.T.

The rise will range from LL. 0.0025 to LL. 0.0075 or even to one Lebanese piaster. In other words the buying and selling rates are above LL. 3.00. The speculation of the banks is to buy when the Banque de Syrie et du Liban enters the market and sell when the rates seems to reach its maximum (i.e. LL. 3.0075 for instance). The sale to realize profits will normally lead the rate to fall again.

The danger which hinders this speculation from being a safe investment is that at times the Banque de Syrie et du Liban does not interfere and the rate cannot rise and starts to fall as the "bears" offer the dollar on the market. ¹⁴⁶

In the following chapter the impact of the foreign exchange market on the economy will be discussed. The Banque de Syrie et du Liban as the agent of the Government will be studied still further, because even in a free economy the role of the Governmental institutions and policies is of utmost importance for the national welfare.

146. Prices that are established under the influence of speculation result from the cooperation of two parties, the bulls and the bears, each of the two parties is always equal to the other in potential strength and in the extent to its commitments. Each has an equal responsibility for the determination of prices. The price is determined at that level at which the two parties counter balance each other. The fluctuations of the foreign exchange rate are not determined solely by bears selling but just as much by bulls buying.

CHAPTER VII

FUTURE OF THE FOREIGN EXCHANGE MARKET IN BEIRUT

I NEVER THINK OF THE
FUTURE. IT COMES SOON
ENOUGH.

ALBERT EINSTEIN

SUMMARY

Before starting to discuss the future of the foreign exchange market in Beirut, it is of importance and relevance to exhibit in brief the material contained in this thesis.

Although industry and agriculture progressed in Lebanon in recent years, the trade sector still is the dominating sector in the economy. It is that sector which determine the rate of activity in the other sectors. Profits incurred in this sector are the main source of funds financing new investments in industry and agriculture. The banking system is the cornerstone of the commercial activity, as indicated by the specialization of the system; commercial credit is the system's main activity. Another activity of the banking system is the foreign exchange operations. The banking system in Lebanon is handicapped by two main factors; the lack of a central bank, and the absence of a banking law that regulates the banking activities in the country.

The construction boom in the last decade was one of the main factors responsible for the prosperity the country enjoyed since then. In the last year or two, this boom started to slacken as the first class apartment buildings increased far beyond demand which had some depressive effects on the economy in general.

The services sector, a sector which caters mainly to foreigners visiting Lebanon, is, beside, trade a characteristic of the Lebanese economy. The attention given to transport and communication reflects on the progress in the services sector. The encouragement of tourism is but one manifestation of the importance attended to this sector.

It has been noted that the government participation in the national income has been increasing year after year. Projects undertaken by the public sector of the economy are a "must" for the development and growth of the Lebanese economy. The fiscal policy of the government has been that of a budgetary surplus, and as a result accumulated some 500 million pounds.

The Lebanese pound is over 90% covered by gold. Money in circulation doubled in ten years. Although the pound was tied to the French franc before independence and for few years after that, Lebanon had to leave the franc due to the constant fluctuation in value of the latter, as well as the depreciation the franc had to undergo following the depreciation of the Sterling pound. Before this, the Lebanese pound passed four stages of its life cycle, starting as the Lebanese Syrian pound which was introduced to replace the Egyptian pound after the mandate was declared on Syria and Lebanon. The 1948 agreement stated the monetary relationships between Lebanon and France after independence. The Banque de Syrie et du Liban in 1939 renewed its contract to remain as the bank of issue until 1964.

Lebanese trade relations are mainly with the Arab World. It is estimated that around one half of Lebanese total exports go to Arab Countries and one quarter of Lebanese imports come from them. This makes the Lebanese economy sensitive to any instability in this area. Besides, Lebanon fills, the role of the middleman between the Arab countries and the World, especially these Arab countries with weak trade relations with the Western World. The freedom of trade has been very instrumental in establishing the country's position as the main entrepot trade and tourist centre in the Middle East.

A general review of the balances of payments shows its weak and its strong points. One general remark can be said at this juncture, that because of the set-up of the Lebanese economy, it is a good conductor of economic fluctuations in the World. No doubt importation of depression is usually much faster than importation of prosperity, a challenge the Lebanese economy has always to face.

What is foreign exchange ? This was the question raised and answered in Chapter III. A review of foreign exchange early theories together with the different definitions given on the subject are discussed there. Accordingly foreign exchange may be defined as that section of economic science which deals with the means and methods by which rights to wealth expressed in one country's currency are converted into rights to wealth in terms of another country's currency. Transactions leading to the exchange of wealth between countries are consequently what brings the foreign exchange into existence. With these transactions taking place every day a

rate is reached for the different currencies in the market. Under flexible exchange rates freely determined in open markets, the first impact of any tendency towards a surplus or deficit in the balances of payments is on the exchange rate. If a country has an incipient surplus of receipts over payments and excess demand for its currency, the exchange rate will tend to rise. If it has an incipient deficit, the exchange rate will tend to fall.

The foreign exchange market may be divided roughly into three groupings; banks, exchange dealers, and brokers. Through the intercourse among these groups, a rate is born for the different exchanges. Through the modern techniques in communications, the major foreign currencies' rates are similar because of the constant ~~contact~~ between the dealers in the different centers. Dealers on the foreign exchange market use different forms of instruments for purchase and sale of foreign exchange on market. Dealings on such a market are not in physical matter but rather an exchange of rights to wealth. These instruments are used to facilitate the foreign exchange operations. Foreign exchange is not only transacted on spot but also on future. How the forward rates are calculated is of importance in this respect because this rate changes at a certain calculated margin from the spot rate. The factors that determine this margin are several such as the difference between the short loan rate in the home country and that in the foreign country, the political factors in the two centres, the market organization and condition of competition and the stability of the monetary standards

Once the reader becomes familiar with the terminology of

foreign exchange, he can proceed to the following chapters.

The foreign exchange market developed in Lebanon since early this century. It has been always a free market up until 1939, where, due to the Second World War, the mandatory authorities found it necessary to introduce exchange controls. These controls lasted until after the war when Lebanon obtained its independence. The national government started to ease the controls as it was clear to the monetary authorities that the black market was significant and beyond control. By 1952 the last official control measure was removed. The foreign exchange market has been free since then.

The exchange dealers are a significant element in the foreign exchange market of Beirut. Their activities can be divided into three main operations; banknotes operations, bills of exchange operations and handpayments operations. The supply of foreign notes to the Beirut market comes from tourists coming to Lebanon, emigrants' remittances to their families, capital flight in the form of banknotes, and for payment of smuggled goods.

Foreign notes are demanded by tourists, shipped to Geneva, and demanded by smugglers of luxury goods and sheep through the borders of the neighbouring countries.

Contrary to the foreign notes, bills of exchange need not come from their home country but are issued all the world over. The Beirut foreign exchange market act as the pool for foreign exchange in the area. Tourists, emigrants' remittances and foreign trade are the main sources of bills of exchange. These bills are sent to the respective world centers where they are

credited to the accounts of exchange dealers and banks at these centres. Unofficial transfers operations are done between countries with controlled economies and those with free economies and open markets. The aim of these transfers is to evade the prevailing laws and regulations pertaining to movements of private capital. A main fact about these unofficial transfers is the ever-changing nature in the methods in which they are executed. Demand on these transfers is usually motivated by their cheap prices compared to official transfers to the concerned countries. The activity in this field is significant and the profit yield is high and tempting.

The commercial banks have two main sources of foreign exchange for its foreign exchange dealings. The first is the actual foreign exchange operations undertaken by the foreign exchange department in the bank and the other is the foreign exchange that results from the usual banking transactions in the other departments of the bank. The largest share contributed to the foreign exchange balances of the banks is through the accounts opened by Lebanese nationals and foreigners in foreign currencies. The U.S. Dollar is the currency whose rate against the Lebanese pound determines the rates for the other foreign currencies in Beirut's foreign exchange market. The U.S. Dollar is accepted internationally and in Beirut is interchangeable for the Lebanese pound, and as the dollar is quoted in all foreign centres, The Beirut market accepts it as the basis to quote other foreign currencies. According to the rate quoted for the U.S. Dollar, the rates for other currencies are calculated.

Foreign exchange policies followed by banks differ. The degrees of variation depends on the amount of foreign balances in

the concerned banks. If a bank has its reserves in foreign exchange, such a bank would usually be seller of foreign exchange to obtain its needs of Lebanese pounds. The type of operations undertaken by the banks on the Beirut market would be classified in three attitudes: speculation, investment and "go home with a square book" attitude. This last attitude is mainly the characteristic of smaller and the more conservative banks. Branches of foreign banks play an important role in the investments of foreign exchange. These banks invest their Sterling balances in Japan. Other banks with strong connections in London invest their balances there. Swaps are the main forward exchange operation on the Beirut market. Speculative transactions are operated by some banks on the London market. The Banque de Syrie et du Liban has a significant role in the Beirut foreign exchange market. In its role as the representative of the government's Stabilization Fund, it interferes in the market to prevent the U.S. Dollar rate from fluctuating widely.

CONCLUSION

The considerable increase during the past few years in Lebanese transit and ordinary trade, in employment in the banking business, in the number of foreign companies operating in Lebanon and the employment herewith and in the number of foreign travellers and amount of transit, is undoubtedly due largely to the free commercial and exchange policies which the country has followed. In most instances, contribution of the free market cannot be isolated from the contribution of other factors which prohibit the availability of data to measure such a contribution, of the free exchange market

to the national income is, in the form of exchange commission (or profits) earned on foreign exchange transactions. This is introduced as a separate item in the balance of payment (See Table 9).

If one scrutinize the other items as shown on the balance of payments one should perceive in general the movement of the foreign exchange on the Beirut market.

Undoubtedly the trade account is the handicap of Lebanon's balance of payments. It has always shown a deficit. A large volume of the domestic consumption is dependent on imported goods. The home production is not producing enough to cover home demand and of course only exporting very little to help cover that gap which results from the almost unrestricted imports (refer to Chapter II). Such a deficit in the balance of trade has been and undoubtedly will remain a source of demand on the foreign exchange holdings of the country. This will continue unless some measure would be undertaken to narrow this gap. This being the case, the merchants solely depend on the free market to obtain their needs of foreign exchange to finance their imports. Entrepot transactions are an active factor in the export sector, as well as a source of supply for foreign exchange.

The gold traffic through Beirut has slackened in recent years. Gold coming to Beirut was for exportation to the Arabian Gulf area and the Far East (India and China). Gold is bought against U.S. dollars. Consequently, the weak gold traffic did indirectly affect the foreign exchange operations and activities.

Nonetheless, there still is gold traffic, and specifically *tola* which is used as a means for hoarding wealth in the gulf area.

As it has been mentioned earlier in the study the services sector in the Lebanese economy is a significant sector in terms of income it provides the country and particularly in terms of foreign exchange. Tourism is one of the economic activities the Lebanese authorities care most to encourage and propagate. *Estivage* is the main activity for tourism in the country. Nationals from the neighbouring Arab countries as well as the wealthy Gulf area oil sheikhs are a source of a strong flow of foreign exchange. This sector is gaining importance as time passes and as the entertainment business and complementary organizations mature. Moreover, the internal political stability is undoubtedly a major factor in encouraging tourism. Moreover, the Lebanese spend a large amount on foreign travel, although only around one quarter the amount that is spent by tourists in the country, but this is a source of demand on foreign exchange.

The growth in transit trade between Arab countries will undoubtedly affect the transport business in Lebanon. The agreement signed between the Arab countries to facilitate transit trade in 1960, is a corner-stone in this respect. The transport activity yields large amounts of money in foreign currencies either in the form of freight payment or in purchasing imported goods from Lebanon.¹⁴⁷ This is besides transport by air where Lebanon has one of the leading Arab Airlines companies, together with a major air-freight company and two smaller airline companies. All these make of air transport a significant source of supply to the

147. The agreement did not contribute much since it was signed, due to the political instability in the Arab World since then.

foreign exchange stock in two ways; one is through the sale of passengers' tickets and freight expenses; the other is travel facility for tourists to visit the country.

Although, the writer cannot confirm the figures given in Table 9 for profits on exchange operations and especially that figure given for 1959, these are an indication on the growth of the exchange market and the high profits earned, from such operations. It is interesting to remark here that the profit margin in the early fifties was larger than it is to-day. The profit margin is narrowing year after year mainly from severe competition as a result of the increase in number of banks and exchange dealers, as well as the large increase in foreign exchange balances in the country. In the early fifties, the market was limited and confined to a few organizations. Moreover, the Sterling accounts were diversified and there always have been differences in the rates of the various accounts which made it a profitable business to buy from one account (low rate) and sell to the other (high rate) while collecting the difference as profit.

Nonetheless, one can notice in Table 9 that profits are on a rising trend. This is because of the increase in number of operations on the market, which minimized the influence of the falling profit margin. The growth in the exchange market will undoubtedly increase foreign exchange profits.

The foreign exchange that results from the expenditure of foreign companies, mainly comes from oil companies that maintain

their offices in Beirut. Because of its free economy, Lebanon became the choice for foreign companies working in the Arab World. These companies establish their head offices in Beirut where they deposit their liquid assets because of the facilities in transfer of money in and out of the country.

Looking at the position of Lebanon in the context of the Arab world one can see that Lebanon enjoys a unique condition. It enjoys a liberal economic policy, stable political conditions and world communications facilities which makes it ideal for foreign entrepreneurs to establish head offices in Beirut. This is besides the favourable weather and the availability of efficient, well-trained local staff to man clerical posts in these foreign companies.

Donations are of two types; foreign aid to the Lebanese Government and emigrants' remittances to their families in Lebanon. While the former depends mainly upon the foreign policy of Lebanon the latter depends mainly on the economic conditions prevailing in the second homeland. Emigrants' remittances are an important source of income for the Lebanon. It is partly responsible for the surplus in Lebanon's balance of payments and is a main source of supply of foreign exchange to the country. Reviewing an item such as this we can realize how the Lebanese economy is sensitive to the international conditions and its dependence on the outside world for its internal prosperity and economic growth.

One last remark on the balance of payment pertains to the IBRD loan to Lebanon. This is as well an important source of foreign exchange, namely, U.S. dollars. This loan is being used

TABLE 9
LEBANON : BALANCE OF PAYMENTS 1951 - 1959

(IN MILLIONS OF L.L.)

	1951	1952	1953	1954	1955	1956	1957	1958	1959
Goods & Services	- 191	- 206	-191	- 177	- 235	- 248	-334	- 295	- 240
Merchandise									
Total credit (a)	832	809	702	814	1120	1190	1414	1414	...
Exports	159	149	162	169	202	236	246	117	152
Total Debit (b)	-1124	-1121	-987	-1159	-1584	-1665	-1943	...	...
Imports	-464	-473	-458	-527	-684	-730	-798	-673	-762
Nonmonetary Gold	24	-3	-17	-20	-5	-8	-3	-7	-9
Foreign Travel Credit	35	48	58	114	131	126	82	62	87
Debit	-12	-24	-30	-19	-25	-25	-16	-22	-25
Transport & Insurance									
Investment Income									
Credit	16	16	17	18	18	21	22	49	55
Debit	-12	-9	-10	-10	-9	..	..	..	..
Gov't Credit (c)	15	27	31	32	36	43	50	47	79
Debit (c)	-2	-13	-2	-2	-3	-4	-5	-4	-4
Misc. Credit	35	35	43	52	69	71	57	98	145
Profit on Exchange operations	11	12	15	22	33	33	39	..	85
Foreign Companies expenditure	24	23	28	30	36	38	18	..	60
Donations	73	99	105	128	144	..	..	165	108
Private (d)	65	83	87	97	102	..	..	...	98
Official(e)	8	16	18	31	42	37	31	...	10
Total current transaction	-118	-107	-86	-49	-91	..	..	-130	-132
Capital & Monetary Gold	-4	-6	-29	-77	-41	..	..	-39	-15
Gov't Contractual payments	-8	-4	-4	-12	-	-	-	-	-
IBRD Loan Drawing	-	-	-	-	-	-	1	7	12
Foreign Exchange official Assets	20	6	-29	24	1	7	9	18	-
Others	8	7	17	3	-7	-2	7	18	6
Monetary Gold	-24	415	-13	-92	-35	-11	-45	-4	-33
Errors & Omissions	122	113	115	126	132	..	..	91	147

a- Commodity exports, tourist and entrepot trade.

b- Commodity imports transit and entrepot trade.

c- Royalties from foreign concessionaries, diplomatic and consular expenditure in Lebanon, UNRWA expenditures and other minor items.

d- Personal donations to charitable and cultural institutions and emigrants' remittances.

e- Foreign Aid.

Source: International Monetary Fund, Balance of Payments year book, 1956-57, Washington D.C. 1959 years 1958 and 1959, data were adopted from unpublished estimates of the U.S.A. Embassy in Beirut, Lebanon

to finance the Litani Dam project. Lebanon can still draw on its account with IBRD for the coming few years on the balance of the loan. It would appear that the trend in the balance of payment will remain in favour of Lebanon. If economic conditions remain constant, the flow of foreign exchange will remain abundant.

Still, what is important is activity in the exchange market. This is important for two reasons; the profit earned from exchange operations and the position of the exchange rate, because the constant flow of foreign exchange into the market may together with other favourable conditions lead the exchange rate of the Lebanese pound to rise against the dollar.

To discuss the future of the foreign exchange market in Beirut, one should examine some inherent factors in the market, the factors that were responsible for the growth of the market to where it stands now.

The insurance of the growth and the prosperity of the banking system in Lebanon is a major issue when discussing the future of the exchange market. One should bear in mind that the flow of capital into Lebanon is due to the trust of the foreign capital in the banking system of Lebanon.¹⁴⁸ This being the case the foreign exchange market's prosperity depends on the prosperity, perpetuation and the vitality of the banking system. Moreover, for the foreign exchange market to grow it has to depend on the growth in the banking system not only because banks are the main institutions in the foreign exchange market organization but also because they are the initiators of both purchase and sale and thus activity in the market.

148. The Secrecy Law of banks is a stimulant too.

The facilities rendered by the banking system to business men are major factors in encouraging and activating the foreign trade sector in the economy, which is the main client of the foreign exchange market. The soundness of the banking system is again a main factor in releasing significant foreign trade operations. All this does not minimize the important role played by the banking system as the main line of contact between Beirut and the foreign centres of the world on which an open market such as Beirut's market largely depends. However, one dare not say that banks are the only link with the outside world because general merchants and wholesalers have strong contacts as well as the big exchange dealers who have representative offices or agents, in the foreign centres. But banks, through their correspondents the world, over and through their own branches in foreign centres, can play a more effective role in activating the foreign exchange market in Beirut. Banks are undertaking triangular operations between Beirut and foreign centres as well as arbitrage operation in the foreign centres. It is only the big known banks who are undertaking forward exchange operations on the world markets. The monopolistic position of banks in such spheres is possible for the simple reason that they are accepted as sound customers by the foreign centres. Brokers in London, for instance, will not accept to deal with a Beirut exchange dealer or a local bank on a forward exchange contract when this latter is unknown to them whether in his means or morality. The issuance of a banking law for Lebanon is the first concern of academic, Governmental and commercial circles. Together with a strong and efficient central bank, the banking system

can guarantee its perpetuation and growth. The banking law could provide for a minimum requirement of capital that will clear the banking system of its weak members, whether through total elimination or merger with stronger institutions as well as limiting entry and therefore, lessening competition. Moreover, the existence of a central bank is a factor of assurance for the banking system in periods of crisis and need. The author is inclined to believe that such a project should be treated as urgent by the concerned official authorities.

As has been mentioned earlier in this chapter, the profit margin on exchange operations is narrowing. This necessitates multiplication of operations undertaken on the market to run the exchange business on a profitable basis. In other words the market has to widen in scope to sustain a larger number of operations. The Beirut market has a wide fame as a world center for foreign operations and Beirut needs to grow to fill the role open for it. This is possible by introducing to the market new and modern tools of foreign exchange operations particularly forward exchange. The majority of the exchanger operations transacted in Beirut are spot operations. Excluding swaps, forward exchange is absent from the market, for as it was mentioned before forward exchange operations by lebanese banks are undertaken at foreign centres. The forward exchange has not yet been introduced to the market. One rarely finds merchants who purchase forward exchange to cover their payments due on their imported goods, or banks covering the credits they open with their foreign correspondents. Very few banks even seek swap operations. Undoubtedly, the market can expand remarkably in this respect.

There is still a technological factor that is missing in the Beirut market, namely the TELEX¹⁴⁹. A system for Lebanon was inaugurated on April, 1962. It is expected to gain widespread use during the coming year. Through this system the Beirut market will be in close contact with foreign centres. Changes in the markets of Zurich and London, for instance, could be instantly received on the private telex of each bank. For the time being, the information is either received on telephone calls with representative agents in foreign centres or through Comtel-Reuter bulletin which only gives the opening and closing rates.

The opening rates are received around 12 a.m. Beirut mean time and closing rates by the following morning. Accordingly one can say that the Beirut market has only two hours¹⁵⁰ in the morning to operate on correct international foreign exchange rates. Theoretically speaking, the market should stop operations until it receives the opening rates from the foreign centres. On these grounds, the Beirut market transacts during the main part of the day ignorant of the changes on the world markets. This could be presented as a reason why the Beirut market transacts operations on wider margin between purchase and sale than other centres. It is believed now, that as the telex system is introduced to the country, exchange operations on the Beirut market could be transacted on a sounder and healthier basis as Beirut will be on con-

149. A teletype printer which is a device for printing messages at a point remote from the transmitting machine.

150. This is the difference in time between Beirut and London means time. This difference drops to one hour during the summer due to the change in timing to summer hours.

tinuous contact with other world centres.

Early in the year 1961 an effort was made on behalf of some banks to have the foreign exchange managers of the different banks dealing on the market to meet so as to get acquainted with each other. The aim was to initiate close ~~ties~~ amongst the banks to persuade these banks to lead one and the same policy in their foreign exchange dealings. During these meetings the decision was taken to fix purchase and sale rates to the U.S. dollar and Sterling pound operations covering a certain margin. Two banks were appointed to fix the rate every morning and distribute it among the banks by telephone. The system did not last more than a week or two due to the continuous negligence of the fixed rates. The goal of that agreement was to lessen competition and increase the margin of profit for the participating banks.

During April, 1962, another effort was made to revive the old project and bring it to life again.¹⁵¹ This time the initiative

-
151. An unofficial organization was formed under the name of Forex Club with an executive committee of seven member banks. The aims of the Forex Club were stated to be:-
- a. To coordinate the work and create an atmosphere of intimacy between the exchange managers of the banks.
 - b. To communicate the buying and selling rates of the main foreign currencies dealt with between the banks and their customers. The member banks should observe the maximum buying rates and the minimum selling rates pegged daily.
 - c. To observe and insure the execution of the agreement.
 - d. To accept suggestions of member banks and prepare these suggestions for discussion in the general assembly.

seemed different. Although it was the increasing of the profit margins and the lessening of severe competitions that dominated the discussion in the first meeting of exchange managers, the real reason was different. Up to the completion of this study the conferees came to agree to peg the rates daily for the U.S. dollar the Sterling pound and New French franc. Three banks were appointed for this job. This rate ties the banks for operations below U.S. \$.25,000.- £10,000.- NFF.50,000.- The agreement included too that the margin between purchase and sale would be LL.0.0050 for the U.S. dollar LL.0.0150 for the sterling pound and LL.0.0020 for the New French franc.

The writer cannot predict how far the experiment will continue to operate but possibilities for its success balance probabilities for its failure. This is because as from the beginning of 1962 the exchange market activity was slow and accordingly profits meager, which makes banks enthusiastic to a system that would increase their profit margin. Moreover, such a system would decrease severe competition amongst banks on smaller operations in which clients make use of the severe competition between banks to obtain favourable rates, which will not be possible under such a system. But most important of all, if executed effectively, is the decision reached by the conferees to boycott any bank which breaks the rate pegged for the day.

Nonetheless, it is still possible for a bank to break the pegged rates without the possible knowledge of other banks through special arrangements; although such behaviour need not be reverted

to as the banks will feel safe that their customers cannot obtain a better rate from their competitors. There remains the exchange dealers who are not part of the agreement. They can still sell cheques as well as telegraphic transfers on competitive rates; but these will not compete with banks for the simple reason that exchange operations in banks are tied with other banking facilities which will force the client to accept the rates produced by his banker.

Going back to the beginning of this discussion the author is inclined to think and believe that the aim behind reviving the old system is to stabilize the exchange rate for the Lebanese pound. The Banque de Syrie et du Liban had been entering the market on behalf of the Stabilization Fund for a long time to prevent the Lebanese pound from rising above LL.3.00 for the dollar but soon after the rate returned back to LL.3.00 and started to slip below it. Now it is believed that if the competition is frozen among banks the rate for the dollar can be maintained around LL.3.00 (i.e. LL.2.9975 buying LL.3.0025 selling). This situation could be strengthened then by interference by Banque de Syrie et du Liban to keep the rate from falling for transactions between the banks for amounts above \$.25,000.- This is all that can be said for the time being on this matter, the rest remaining for the future to tell.

Bibliography

BOOKS

- Allen W.R. and Clark L. Allen, Foreign Trade and Finance, New York, The Macmillan Co. 1959.
- American Economic Association, Reading in the Theory of International Trade, Philadelphia, The Blakiston Co., 1949.
- American Economic Association, Reading in the Theory of International Trade, London, George Allen and Urwin Ltd., 1958.
- Badre, Albert and Asad Y. Nasr, National Income of Lebanon, Income Arising in the Industrial Sector, Beirut, May 1953.
- _____, National Income of Lebanon, Income Arising in the Services Sector, Beirut, July 1953.
- _____, National Income of Lebanon, Income Arising in the Government Sector, Beirut, Nov. 1953.
- Badre, Albert and Staff of Economic Research Institute at A.U.B., National Income of Lebanon, Income Arising in Real Estate Sector, Beirut, July 1954.
- Beyen, J.W. Money in a Maelstrom, New York, The MacMillan Co. 1949.
- Bradford, Frederick, Money and Banking, New York, Longmans Green and Co. 1949.
- Cassel, Gustav, Money and Foreign Exchange After 1914, London, Constable and Co. Ltd., 1922.
- Dupriez, Leon H. et al, Money, Trade and Economic Growth, New York, The MacMillan Co. 1951.
- Einzig, Paul, The Exchange Clearing System, London, MacMillan and Co. 1935.
- _____, International Gold Movements, London, MacMillan & Co.Ltd. 1929.

- Evitt, H.E., Exchange and Trade Control in Theory and Practice, London, Sir Isaac Pitman and Sons, Ltd., 1958.
- _____, A Manual of Foreign Exchange, London, Sir Isaac Pitman and Sons, Ltd., 1950.
- Fei, Edward and Paul Klat, The Balance of Payments of Lebanon 1951 and 1952, Beirut, Dar el Kitab, 1954.
- Flux A.W., The Foreign Exchanges, London, Ps. King and Sons Ltd. 1924.
- Gillett Bros Discount Co. Ltd., The Bill on London, London, Chapman and Hall, 1952.
- Hall, N.F., The Exchange Equalization Account, Macmillan and Co. Ltd., 1935.
- Hansi, Alfred, The Monetary Utopias of our time, Berlin, Berliner Bank, 1961.
- Harris, S.E., Exchange Depreciation, Cambridge, Harvard University Press, 1936.
- Harrod Ray F., The Pound Sterling, Princeton, Princeton University Press, 1952.
- Higgins, Benjamin, Economic Development, New York, W.W. Norton and Co. Inc. 1959.
- Himadeh, Raja S., The Fiscal Systems of Lebanon, Beirut, Khayat's 1961.
- International Monetary Fund, Schedule of Par Values, Thirtieth issue, Washington, 1960.
- International Monetary Fund, Twelfth Annual Report Exchange Restrictions, Washington, 1961.
- Katz, Samuel, Two Approaches to the Exchange Rate Problem; The United Kingdom and Canada, Princeton, Princeton University Press, 1956.
- Klopstock, Fred, The International Status of the Dollar, Princeton, Princeton University Press, 1957.

- MacDougall, Donald, The World Dollar Problem, London, MacMillan and Co. Ltd, 1957.
- Mikesell, Raymond F., Foreign Exchange in the Postwar World
New York, The Twentieth Century Fund, 1954.
- Richardson, Dudley, Negotiable Instruments and the Bills of Exchange Acts, London, 1948.
- Rosenthal, Moriss, Techniques of International Trade, New York McGraw-Hill Co. 1950.
- Saba, Elias S., The Foreign Exchange Systems of Lebanon and Syria 1939-1957, Beirut, American University of Beirut, 1961.
- Sen, S.N. Central Banking in Underdeveloped Money Markets, Calcutta, Bookland Private Ltd., 1956.
- Tarishis, Lorie, Introduction to International Trade & Finance
New York, John Wiley and Sons Inc., 1955.
- Taylor, E. Miles & C.L. Lawton, Banking, Currency and Foreign Exchange, London, Textbook Ltd, 1928.
- Thomas, Rollin G. Our Modern Banking and Monetary System, New York Prentice Hall Inc., 1952.
- Triffin, Robert, Gold and the Dollar Crisis, New Haven, Yale University Press, 1961.
- United Nations, Department of Economic Affairs, The Foreign Exchange Position of the Devasted Countries, Lake Success, 1947.
- _____, The International Flow of Private Capital 1946-1952,
New York, 1954.
- _____, Instability in Export Markets of Underdeveloped Countries,
New York, 1952.
- _____, U.N. Conciliation Commission for Palestine, Final Report of the United Nations Economic Survey Mission for the Middle East, Lake Success, 1949.

Von Mises, Ludwig, The Theory of Money and Credit, New Haven,
Yale University Press, 1953.

UNPUBLISHED MATERIAL:

Lebanon, Ministry of Economy, Bulletin Statistique Trimestriel
1960 - 1961.

Makdisi, Samir, A.K., Postwar Lebanese Foreign Trade and Economic
Development, AUB, M.A. Thesis, 1955.

Mikdashi Z., The Monetary System of Lebanon, AUB, M.A. Thesis, 1956.

Saba, E.S. Requirements and Desirability of a Convertible Lebanese
Currency, AUB, M.A. Thesis 1956.

Salem, Khalil I., Foreign Exchange Practices in the Economy of
Lebanon, AUB, M.A. Thesis 1955.

Sanbar K.W., The Lebanese Economy with Special Reference to the
Impact on it of existing Development Progress, AUB, M.A.
Thesis, 1955.

Sayigh, Yusif, Economic Development of Lebanon, Its Prospects and
Problems, Johns Hopkins University, October, 1955.

Appendix A

Foreign Exchange Terminology

This appendix contains terms and clauses in use in the foreign exchange business and which were either not mentioned in the thesis or were not given elaborate explanation.

Exchange Clause : Exchange clause is a clause included in the wording of a bill which fixes the method of arriving at the rate of exchange at which the drawee may pay the bill.

Exchange as Per Endorsement : The effect of this clause is to enable the bank to whom the drawer sells the bill to fix the rate of exchange at which the draft will become payable in terms of foreign currency. The bill is therefore treated as a bill for that amount of foreign currency.

Payable without Loss in Exchange: This clause also has the effect of insuring that the drawer in the country of export shall receive the full foreign exchange amount of the bill under discount but only after deduction of all collection charges and the cost of foreign stamps. The conversion rate is not fixed but negotiated between the collecting bank and the drawee.

Payable by Approved Banker's Cheque on London for full face value:

This clause implies that the bill is to be paid by a cheque drawn on London in Sterling. No exchange rate is involved in such a case.

The Interest Clause: "Payable at the bank's current rate of exchange for a demand draft on London, together with interest at seven percent per annum from date here of until approximate date of arrival of return remittance in London plus all collection charges".

This implies that the drawee will pay interest on the period from the date the bill was mailed by the bank until it is collected. The rate of exchange is fixed according to the rate of the day, for drafts on London.

Payable at the Bank's Current rate of Exchange for a Demand draft on London:

This clause is significant as a Sterling draft could be drawn on any world center, including Beirut. In such case drafts drawn on other centers than London usually have a lower rate of exchange. This is because of value lost between the time for a draft to be collected from any world center and remitted to the beneficiary's account in London.

Foreign Domicile Bill:

These are bills drawn on and accepted by banks, companies or individuals abroad. The holder of a foreign domicile bill may obtain an advance

against it from his bankers if he hands it to them for collection but he cannot rely on being able to sell it to a discount house.

Documentary Bill :

This is drawn to cover an actual movement of goods from the seller to the buyer, and the relative documents are attached to the bill when it is drawn. The bill before and after it is accepted is negotiable. The seller of the goods can sell it for immediate cash to his local bankers. The seller is thus paid for his goods when they are despatched. The buyer for his part does not have to pay until the bill, having been duly accepted matures and this will usually be after the goods have reached their destination and have been re-sold.

The Long Rate:

This is also known as the forward rate. it is based upon the sight rate, rising and falling in agreement with it, and the amount of its deviation depends on the rate of discount ruling in the country upon which the bill is drawn, and on the state of credit prevailing there.

Appendix BCURRENCIES OF THE WORLD

<u>COUNTRY</u>	<u>CURRENCY</u>	<u>UNIT</u>
Aden	Shilling	100 cents
Afghanistan	Afghani	100 puls
Albania	Lek	100 qintars
Algeria	Nouveau Franc	100 centimes
Andorra	Peseta	100 centimos
Angola	Escudo	100 centavos
Antigua	Dollar	100 cents
Argentina	Pesos	100 centavos
Aruba	Guilder (Florin)	100 cents
Australia	Pound	20 shillings
Austria	Schilling	100 groschen
Azores Islands	Escudo	100 centavos
Bahrain Islands	Indian Rupee	100 nays paisa
Balearic Islands	Peseta	100 centimos
Barbados	Dollar	100 cents
Basutoland	Pound	20 shillings
Bechuanaland	Pound	20 shillings
Belgian Congo	Franc	100 centimes
Belgium	Franc	100 centimes
Bermuda	Pound	20 shillings
Bolivia	Boliviano	100 centavos
Brazil	Cruzeiro	100 centavos
British Guiana	Dollar	100 cents
British Honduras	Dollar	100 cents
British North Borneo	Dollar	100 cents
British Somaliland	Shilling	100 cents
Brunei	Dollar	100 cents
Bulgaria	Lev	100 stotinki
Burma	Kyat	100 pyas
Cambodia	Riel	100 sen
Cameroons	Pound	20 shillings
Cameroon	Franc	100 centimes
Canada	Dollar	100 cents
Canary Islands	Pesseta	100 centimos

Cape Verde Islands	Escudo	100 centavos
Central African Republic	Franc	100 centimes
Ceylon	Rupee	100 cents
Chad	Franc	100 centimes
Chile	Escudo	100 condors
China	Jen-Min-Piao	100 fen
Colombia	Peso	100 centavos
Comoro Islands	Franc	100 centimes
Congo	Franc	100 centimes
Costa Rica	Colon	100 centimos
Cuba	Peso	100 centavos
Curacao (Netherlands Antilles)	Guilder	100 cents
Cyprus	Pound	1000 mils
Czechoslovakia	Crown	100 heller
Dahomey	Franc	100 centimes
Denmark	Krone	100 ore
Dominica	Dollar	100 cents
Dominican Republic	Peso	100 centavos
Dubai (Trucial States)	Rupee	100 naya paisa
Equador	Sucre	100 centavos
Egypt	Pound	100 piasters
El Salvador	Colon	100 centavos
England	Pound	20 shillings
Ethiopia	Dollar	100 cents
Faroe Islands	Krone	100 ore
Federation of Rhodesia & Nysaland	Pound	20 shillings
Fiji	Pound	20 shillings
Finland	Markka	100 pennis
Formosa	Dollar	100 cents
France	Nouveau Franc	100 centimes
French Guiana	Franc	100 centimes
French Somaliland	Franc	100 centimes
Gabon	Franc	100 centimes
Gambia	Pound	20 shillings
Germany (Western)	Deutsche Mark	100 pfennige
Germany (Eastern)	Deutsche Mark	100 pfennige
Ghana	Pound	20 shillings
Gibraltar	Pound	20 shillings
Grand Cayman Island	Pound	20 shillings

Greece	Drachma	100 lepta
Grenada	Dollar	100 cents
Guadeloupe	Franc	100 centimes
Guam	U.S. Dollar	100 cents
Guatemala	Quetzal	100 centavos
Guinea	Franc	100 centimes
Haiti	Gourde	100 centimes
Hashemite Kingdom of the Jordan	Dinar	1000 fils
Honduras	Lempira	100 centavos
Hong Kong	Dollar	100 cents
Hungary	Forint	100 filler
Iceland	Krona	100 aurar
Ifni	Peseta	100 centimes
India	Rupee	100 naya paisa
Indonesia	Rupiah	100 cents
Iran	Rial	100 dinars
Iraq	Dinar	1000 fils
Ireland (Northern)	Pound	20 shillings
Ireland (Republic)	Pound	20 shillings
Israel	Pound	100 agorot
Italy	Lira	100 centesimi
Ivory coast	Franc	100 centimes
Jamaica	Pound	20 shillings
Japan	Yen	100 sen
Jordan	Dinar	1000 fils
Kenya	Shilling	100 cents
Korea (Republic)	Hwan	100 chon
Kuwait	Dinar	1000 fils paiss
Laos	Kip	100 at
Lebanon	Pound	100 piasters
Liberia	U.S. Dollar	100 cents
Libya	Pound	100 piasters
Liechtenstein	Franc	100 centimes
Luxemburg	Franc	100 centimes
Macao (Macao)	Pataca	100 avos
Madeira Islands	Escudo	100 centavos
Malagasy Republic	Franc	100 centimes
Malaya	Dollar	100 cents
Malta	Pound	20 shillings

Marie Galente	Franc	100 centimes
Martinique	Nouveau Franc	100 centimes
Mauritania	Franc	100 centimes
Mauritius	Rupee	100 cents
Mexico	Peso	100 centavos
Monaco	Nouveau Franc	100 centimes
Montserrat (Leeward Islands)	Dollar	100 cents
Morocco	Dirham	100 moroccan franc
Mozambique	Escudo	100 centavos
Nepal	Rupee	100 pice
Netherlands	Guilder	100 cents
New Caledonia	Franc	100 centimes
New Guinea	Pound	20 shillings
New Hebrides	Franc	100 centimes
New Zealand	Pound	20 shillings
Nicaragua	Cordoba	100 centavos
Niger	Franc	100 centimes
Nigeria	Pound	20 shillings
Norway	Krone	100 ore
Okinawa	U.S. Dollar	100 cents
Oman	Rupee	100 naya paisa
Pakistan	Rupee	166 annas
Panama	Balboa	100 cents
Papua	Pound	20 shillings
Paraguay	Guarani	100 centimos
Peru	Sol	100 centavos
Philippines	Peso	100 centavos
Poland	Zloty	100 groszy
Portugal	Escudo	100 centavos
Portuguese East Africa	Escudo	100 centavos
Portuguese Guinea	Escudo	100 centavos
Portuguese India	Escudo	100 centavos
Principe Island	Escudo	100 centavos
Puerto Rico	U.S. Dollar	100 cents
Reunion Island	Franc	100 centimes
Roumania	Leu	100 bani
Ruanda-Urandi	Franc	100 centimes
Ryukyu Islands	U.S. Dollars	100 cents
St. Kitts	Dollar	100 cents
St. Lucia	Dollar	100 cents

Saint Pierre-Miquelon	Franc	100 centimes
St. Vincent	Dollar	100 cents
Samao, Wesern	Pound	20 shillings
Sao Thome Island	Escudo	100 centavos
Sarawak	Dollar	100 cents
Saudi Arabia	Riyal	22 gurshe
Scotland	Pound	20 shillings
Senegal	Franc	100 centimes
Sicily	Lira	100 centesimi
Sierra Leone	Pound	20 shillings
Singapore	Pound	20 shillings
Solomon Islands	Pound	20 shillings
Somalia	Somalo	100 centesimi
South West Africa	Pound	20 shillings
Spain	Peseta	100 centimos
Vahamas	Pound	20 shillings
Spanish Sahara	Peseta	100 centimos
Sudan	Pound	100 piaster
Sudanese Republic	Franc	100 centimes
Surinam	Guilder	100 cents
Swaziland	Pound	20 shillings
Sweden	Krona	100 ore
Switzerland	Franc	100 centimes
Syria	Pound	100 piasters
Tahiti	Franc	100 centimes
Taiwan	Dollar	100 cents
Tanganyika	Shilling	100 cents
Thailand	Baht	100 satang
Timor, Portuguese	Escudo	100 centavos
Tobago	Dollar	100 cents
Togoland	Franc	100 centimes
Trinidad	Dollar	100 cents
Tunisia	Dinar	100 dirham
Turkey	Lira	100 piasters
Uganda	Shilling	100 cents
Union of South Africa	Pound	20 shillings
Union of Soviet Socialist	Roubles	100 kopecks
Upper Volta	Franc	100 centimes

Uruguay	Peso	100 centimos
Venezuela	Bolivar	100 centimos
Viet-Nam	Piaster	100 cents
Virgin Island	U.S. Dollar	100 cents
Yugoslavia	Dinar	100 paras
Zanzibar	Shilling	100 cents

Appendix C
UNITED KINGDOM

Although what is mentioned below is the exchange regulations in the United Kingdom it represents the policy followed in all the Sterling Area countries in this respect.

EXCHANGE RATE SYSTEM

Market rates for spot exchange transactions in U.S. dollars are maintained between official limits of US.\$2.82 buying, and US.\$2.78 selling. Forward premiums and discounts are left to the interplay of market forces. Authorised banks are allowed to engage in spot and forward exchange transactions in any currencies.

EXCHANGE CONTROL TERRITORY

Exchange control is not imposed on transactions with other parts of the Sterling Area.

ADMINISTRATION OF CONTROL

Exchange control in the United Kingdom is administered by the Bank of England on behalf of the U.K.

PRESCRIPTION OF CURRENCY

Payments from countries in the Sterling Area may be received in any Sterling Area currency; payments from countries outside the Sterling Area must be received in sterling from an External Account or in any specified currency; alternatively, any other foreign currency that is freely exchangeable for sterling may be accepted. Payments to countries in the Sterling Area may be made in any Sterling Area currency; payments to countries outside the Sterling Area may be made by crediting sterling to an External Account or in any foreign currency.

NONRESIDENT ACCOUNTS

The sterling accounts of persons, etc., resident in other parts of the Sterling Area are treated as those of residents of the United Kingdom. Thus, for transfers within the Sterling Area no U.K.

exchange control permission is required; but for payments to other countries by residents of any territory of the Sterling Area, the U.K. authorised banks are required to ensure that the payment has the approval of the exchange control authority of the territory concerned.

External Accounts: With the exception of Blocked Accounts (see below) the sterling accounts of nonresidents, i.e., those resident outside the Sterling Area, are designated External Accounts. Balances on External Accounts are available for payments to residents of the Sterling Area, for transfers to other External Accounts, and for purchases of any foreign currency or gold.

Blocked Accounts: These accounts are applicable to residents of all countries outside the Sterling Area except Denmark, Norway, and Sweden (residents of these three countries may transfer all their sterling assets to their respective countries). The purpose of Blocked Accounts is to receive funds that are not placed at the free disposal of non-residents, e.g., capital proceeds. Such funds may be used to purchase on a recognized stock exchange in the United Kingdom securities that are payable in a Sterling Area currency, cannot be redeemed under any contractual provision within five years from the date of acquisition, and are not optionally payable in dollars; the income from such securities, and the proceeds at maturity of any that are redeemable, may be remitted to the country of the holder. Transfers between Blocked Accounts are permitted freely, and Blocked Account sterling is negotiable, mainly against U.S. dollars, in free markets abroad.

IMPORTS AND IMPORT PAYMENTS

Imports of practically all goods are permitted freely, under an Open General License, from all sources other than Japan and the "Eastern Area".

Permission to import either under the Open General License or by some other form of license carries with it an entitlement to obtain foreign exchange to pay for the import. Exchange control forms are not required for payments to residents of the Sterling Area, or for payments to other countries for imports not exceeding £500.

PAYMENTS FOR INVISIBLES

Payments for invisibles to residents of the Sterling Area may be made freely. Payments to countries outside the Sterling Area require exchange licenses, but these are granted freely, subject to the presentation of supporting evidence. The completion of an exchange control form is not required for payments not exceeding £250.

An allowance of up to £250 in foreign exchange is made available automatically to travelers, who may obtain additional funds upon authorization by the Bank of England. Not more than £50 in British banknotes may be taken out of the United Kingdom, except by persons traveling directly to the Irish Republic or the Channel Islands. Authorized banks may export sterling notes to nonresidents against payment in sterling from an External Account or any foreign currency.

EXPORTS AND EXPORT PROCEEDS

Exports to countries outside the Sterling Area are permitted without specific exchange control approval, provided the proceeds are received in conformity with the prescription of currency regulations. Exchange receipts in specified currencies must be offered to an authorized bank.

PROCEEDS FROM INVISIBLES

Exchange receipts from invisibles in specified currencies must be surrendered.

CAPITAL

Transfers of resident capital to countries outside the Sterling Area require approval, which normally is granted for commercial

investment that promises to employ Sterling Area skills or techniques or to assist Sterling Area exports or the production of raw materials. Permission may be obtained to invest foreign currency capital receipts in marketable securities expressed in foreign currency, but any such receipts in a specified currency which have not been invested within six months must be sold to an authorized Bank.

Foreign exchange or permission to credit sterling to an External Account is granted freely for repayments abroad due to a nonresident in respect of matured capital obligations; otherwise, the proceeds of nonresident-owned capital may be credited only to Blocked Accounts.

Nonresidents may buy sterling securities on a recognized stock exchange in the United Kingdom against payment from an External Account or, if the securities cannot be redeemed under any contractual provision within five years from the date of purchase and are not optionally payable in dollars, with sterling from a Blocked Account.

Nonresidents may purchase officially quoted non-sterling securities with sterling from an External Account. Such securities may not be resold on a stock exchange in the United Kingdom but may be exported.

BANKNOTES

The authorized banks may buy and sell foreign notes and coins at market rates of exchange. They may buy foreign notes and coins from residents without limit. In transactions with nonresidents abroad, they may buy and sell foreign notes and coins against External Account sterling, against sterling notes to be exported or that have been imported, or against any other foreign currency in notes or any other form. The authorized banks may also purchase foreign notes and coins from nonresidents visiting the United Kingdom, against payment in sterling in cash or to the credit of an External Account.

FRANCE

Although what is mentioned below is the exchange regulations in France, it represents the policy followed in all the French Franc Area countries in this respect.

EXCHANGE RATE SYSTEM

The par value is New Francs 4.93706 = US. \$ 1. Market rates for spot exchange transactions in U.S. Dollars are maintained between official limits of NF4.90 buying and NF 4,9740 selling per US. \$1. Forward transactions take place at rates freely determined by supply and demand. Authorized banks in continental France are permitted to deal spot or forward in the Paris exchange market in all currencies.

Most payment agreements concluded by France provide for settlements between the French Franc Area as a whole and the other country concerned. Payments from France to other parts of the French Franc Area, except Guinea, are free of restrictions.

ADMINISTRATION OF CONTROL

The Bank of France is concerned with the issue of licenses for transactions of a financial nature for France. Other countries of the Franc Area have their own central banks to run their exchange control system, except that all central banks follow the same policy.

PRESCRIPTION OF CURRENCY

For prescription of currency purposes, countries outside the French Franc Area are divided into two groups: the bilateral group and the area of convertibility (all other countries).

Settlement with countries in the area of convertibility may be made in any of the currencies of those countries, or through Foreign Accounts in Convertible Francs (see section on Non-Resident Accounts below). Payments to countries in the bilateral group are

made by crediting a Foreign Account in Bilateral Francs related to the country concerned. Payments from bilateral group may be received to the debit of a Foreign Account in Bilateral Francs related to the country concerned, or by the same methods as those prescribed for receipts from the area of convertibility. Settlements with countries in the bilateral group may also be made in their respective currencies if the regulations of the other country permit this, as in the case of Czechoslovakia, Settlements with Hungary, Laos, and Viet-Nam are subject to special regulations.

NON-RESIDENT ACCOUNTS

Foreign Accounts in Convertible Francs are not related to a specific country, while Foreign Accounts in Bilateral Francs are designated according to the country of the account holder. A non-resident account in francs may be opened by an authorized bank for a non-resident foreigner or for a French national who has been residing abroad for at least four years. Non-Resident accounts established under certain bilateral agreements may be opened only with the approval of the Bank of France. Non-Resident accounts in francs may not show a debit balance unless specifically permitted.

Foreign Accounts in Convertible Francs may be credited freely with francs obtained from sales of currencies of countries in the area of convertibility, in the exchange market or through a French authorized bank in an exchange market abroad; with transfers from other Foreign Accounts in Convertible Francs; and with French francs obtained from the sale of foreign banknotes. They may be debited freely for purchases in the exchange market of any foreign currency negotiated in that market; for transfers to the credit of another Foreign Account in Convertible or Bilateral Francs; and for payments in the French Franc Area.

Foreign Accounts in Bilateral Francs may be credited freely with proceeds from sales in the exchange market of currencies of countries in the area of convertibility; and with transfers from a Foreign Account in Convertible Francs or from a Foreign Account in Bilateral Francs of the same nationality as the account to be credited. They may be debited freely for transfers to a Foreign Account in Bilateral Francs of the same nationality, and for payments in the French Franc Area, provided that the person on whose behalf such payment is made resides in the country to which the account to be debited is related and the creditor is a person residing in the French Franc Area, or that the amount withdrawn is used to cover expenses in France of a person residing in the same country as that of the account debited.

PAYMENTS FOR INVISIBLES

Payments for invisibles related to trade are permitted freely when the basic trade transaction has been approved. However, foreign exchange is not granted to exporters and importers for insurance abroad of risks concerning persons, property, or liability in France, which may be insured only in France with French insurance companies or foreign companies authorized to conduct insurance business in France. Income accruing to non-residents in the form of profits, dividends and royalties is remittable, subject to supervision. Exchange up to NF.400 monthly for each beneficiary is granted for family maintenance abroad. Appropriate foreign exchange is granted for the remittance of banking commissions, patent fees, royalties, and specified categories of taxes. Transfers on account of membership fees, subscriptions, donations, and emigrants' funds are also permitted.

The exchange allowance for French residents for tourist travel abroad is NF.1,500 a calendar year. Residents, may freely make arrangements through licensed travel agencies operating in France,

or purchase credit cards in France, for their travelling expenses abroad, without limitation and independently of any exchange allocation.

Travellers, may take with them out of France banknotes or coins up to NF.250 in metropolitan francs.

EXPORTS AND EXPORT PROCEEDS

Export proceeds must be collected within 180 days from the arrival of the goods at their destination and in the manner set forth in the regulations.

Foreign exchange proceeds that are not used to make authorized payments abroad must be surrendered within a month from the date of their receipt.

PROCEEDS FROM INVISIBLES

Residents are obliged to collect, and to surrender within a month from the date of receipt, amounts due from non-residents in respect of services and of income exceeding NF.500 from foreign securities.

Travellers, may bring in any amount of banknotes or coins, (except gold coins), in metropolitan francs, CFA francs, or CFP francs.

CAPITAL

Most of outward transfers of capital by residents require approval. Residents of foreign nationality may dispose freely of their assets abroad. Residents of French nationality are permitted to reinvest such assets either in quoted securities in accordance with a general authorization or in other investments under individual license.

The export of French securities held in France is permitted if they are at the free disposal of a resident of the area convertibility.

BANKNOTES

Authorized banks are permitted to buy foreign banknotes freely from any person against payment in French francs and, in accordance with a general or individual license, to sell foreign banknotes to residents going abroad against payment in French francs.

Appendix D

BANKS IN LEBANON, 1962

LEBANESE BANKS

- / Bank of Lebanon and the Middle East.
- / Banque Al Ahli,
Azar National Bank
- / Banque de Beyrouth et des Pays Arabes.
- / Banque Beyrouth Riyad.
- / Banque Cabbabe.
- / Banque Chartouni.
- / Banque Commercial.
Banque Commercial Libanais.
Banque Comptoir d'Avance Commerciale.
- / Banque de Credit Agricole, Industriel et Foncier.
- / Banque de Credit National.
- / Eastern Commercial Bank.
- / Banque d'Epargne et de Credit Foncier.
- / Federal Bank of Lebanon.
Banque Haddad.
- / Intra Bank.
Banque Kairouz Freres.
Banque Karam.
- / Banque Lati J. et Fils.
- / Bank of Lebanon and the Middle East.
- / Banque du Liban et d'Outre-Mer.
- / Banque Libanaise pour le Commerce.
Banque Majdalany M. et Cie.
- / Banque Naayem.
- / Banque Pharaon et Chiha.

- Banque Sabbagh R. et Cie.
- / Banque Sabbagh S.A.L. (Banque d'Indo-Chine)
- / Banque Saradar.
- / Banque Shoucair, Sami.
- / Banque Tohme.
- / Banque Trad, G. (Credit Lyonnais)
- / Banque de l'Union Nationale.
- / Sinno Bank.
- Banque des Activites Economiques.
- / The Arab Real Estate Bank.
- / Banque Libano-Bresilienne.
- / Development Bank.
- Lebanese Saving Bank.
- / Middle East Banking Co.
- Banque Audi (Sons of Wadie Audi).
- La Banque d'Affairs.
- The Lebanon Savings and Loan Bank.
- / Banque de l'Economie Arabe.
- / Banque de l'Industrie et du Travail.
- Banque Joseph Geagea.
- / Banque Beyrouth pour le Commerce.
- / Societe Bancaire du Liban.
- / Credit Libanais.
- / Banque Fonciere Libanaise.

ARAB NON-LEBANESE BANKS

- Arab Bank.
- Banque du Caire.
- Jordan National Bank.
- Banque Homsy.

/ Banque Misr Liban.

Bank of Rafidain.

FOREIGN NON-ARAB BANKS

/ Eastern Bank Ltd.,

/ Bank of America.

/ Banco di Roma.

/ Banque Belgo Libanaise.

/ British Bank of the Middle East.

/ Banque Compagnie Algerienne de Credit et de Banque.

/ Banque de Credit Foncier d'Algerie et de Tunisie.

/ First National City Bank of New York.

/ Banque Nationale pour le Commerce et l'Industrie (Afrique)

/ Banque de Syrie et du Liban.

/ Chase Manhattan Bank.

/ Lombard Bank Lebanon.