

THE ORGANISATIONAL STRUCTURES OF BEIRUT STOCK EXCHANGE AND OTHER ARAB EXCHANGES

Since 1996, the Beirut Stock Exchange (BSE) has been trying, with no great success to regain its former status among the regional stock markets. If it is rightful to claim that the present economic context lies far from encouraging market development, we must say that the gap in our Stock Exchange cannot only be attributed neither to the prevailing economic stagnation nor to the lack of confidence of the public opinion.

Other, even more intrinsic problems, reside in the organisational structure of the Beirut Stock Exchange. Such problems are considered to be the source of this lack of confidence and impede any possible rebound of the Lebanese market.

Since its creation in July 3, 1920, the BSE has been, the aim of multiple regulations. Nowadays, the two main enactments that govern the Beirut Stock Exchange are the following:

- executive order 120 of September 16, 1983 (modified by executive order 30 of March 23, 1985 and by act 418 of May 15, 1995).
- order 7667 of December 16, 1995 which has published the by-laws of the Beirut Stock Exchange pursuant to article 20 under executive order 120.

These two enactments constitute today the quintessence of the Lebanese financial markets substantive law and regulate, among others, the organisational structure of the Beirut Stock Exchange.

The present organisational structure of the BSE

Legal status

Neither executive order 120 nor order 7667 determine the legal status of the BSE as an administrative body, despite its heterogeneous composition which creates some doubts about the issue. A contentious matter which has opposed Merrill Lynch with a group of financial intermediaries to the BSE gave the *Conseil d'Etat* (the highest administrative jurisdiction in Lebanon) the opportunity to erase the uncertainty. The BSE was considered as being a “public authority empowered to issue regulations ” (Decree 60/94 of November 9, 1994)

The BSE Committee

By virtue of article 40 under order 7667, the BSE counts as members all the Lebanese joint stock companies having a capital which exceeds the amount of LBP 30 million (around 20.000 USD). It is managed by a committee, appointed by order in cabinet and made up of 10 members:

- A chairman, chosen from among experts and specialists.
- A representative of the Ministry of Finance, appointed Vice-Chairman.
- Two representatives of the banks operating in Lebanon.
- Two representatives of the financial intermediaries.
- Two representatives of Lebanese listed companies.
- A representative of Lebanese joint stock companies that are members of the Beirut Stock Exchange.
- A Lebanese or foreign expert.

The representation of banks in the BSE Committee is unfortunate if not unfounded because of the conflict of interests existing between the banking activity from one side and the stock exchange activity from the other.

In fact, both activities pursue almost the same goal; attracting public saving and redirecting it to the investment needs. Thus, it is absolutely absurd to involve the competitor banking sector in the management of the financial markets.

Prerogatives of the BSE Committee

Article 13 under executive order 120 entrusts the Committee with the same prerogatives given by the Lebanese Code of Commerce to the board of directors of a joint stock company in addition to the following prerogatives provided for by articles 21 and 22 under order 7667:

- manage, regulate and develop markets
- protect the investors interests
- control the activities of listed companies
- insure information of issuers and investors
- propose draft laws.

With these prerogatives, the BSE Committee becomes simultaneously the Exchange manager and the market regulator (even if the regulation authority is shared with the Ministry of Finance, represented by the Government Commissioner before the BSE and the *Banque du Liban*, the Lebanese central bank which controls the professionals of the market).

However, the order 120 of September 16, 1983 provided the creation of a “Council of Financial Markets”, with the mission of “assuring the good functioning of the Stock Exchange and its Committee”. In other words, the executive order of 1983, in its initial format provided the separation between the Exchange management and the market regulatory roles. Unfortunately, and for unveiled reasons, the articles referring to the creation of the “ Council of Financial Markets” have been revealed by the executive order 30 of March 30, 1985.

This anomaly due to the gathering of management and regulatory tasks in the core of the same entity seems to be detrimental to the development of the Lebanese financial market.

The importance of separating between the Exchange management and the regulating authority

The functioning of a regulated financial market requires the implementation of two main tasks:

Primo, establishing the general conditions of the organization and the functioning of the market, mainly those pertaining to the admission of members, the admission of the financial instruments for negotiations, the organization of the transactions, the publication of information and the creation of stock indexes serving as reference to futures contracts.

Secundo, regulating and supervising the activity of the market, in a way that assures a transparency for the transactions and protects the public saving.

Since their first appearance in the 17th century, the Stock Exchanges have been structured in two different types:

The liberal English type which used to empower the intervening parties on the market, gathered in clubs, the organization of the stock exchange, independently from public authorities. And the French system, in which, the public authorities held the monopoly of organizing the financial markets.

Nowadays, the main capital markets elect to a uniform organization, in the virtue of which the Exchange manager (most likely, a private corporation) controls the functioning and the organization of the market, under the supervision of a public regulatory agency.

The advantages of this architecture are obvious. It reinforces the market transparency and widely opens the market to institutional investors, especially when the control is performed by an independent administrative authority with undisputed credibility. As for handing the market management to the private sector, it certainly develops the market activity by increasing the number of issuers and diversifying the financial instruments. Moreover, corporatisation brings in new technologies such as stock trading on electronic communication network, provides a level playing field, thereby encouraging competition and facilitates mergers with other Exchanges reinforcing the market capitalisation.

In France, for example the separation was achieved only a few years ago with the modernization of financial markets activities act of July 2nd,1996 (commonly known as the MAF act). Hence, the SBF-Bourse de Paris (a private corporation, that has become Euronext since September 2000 after the merger of the Exchanges of Paris, Brussels and Amsterdam) has become the managing agent of the first and second markets as well as the European Depositary Receipt (EDR) market. Other private companies, such as the *Société du Nouveau Marché (SNM)*, *Monep SA* or *Matif SA* are the respective managers of the new market, the options market and the futures market. The *Commission des Opérations de Bourse* and the *Conseil des Marchés Financiers* , two autonomous administrative authorities, are the main watchdogs of the French capital markets.

The organisational structure of Arab capital markets

Following the global trend, the Arab financial markets have been subject to radical organizational reforms, for the past decade.

Jordan

A total separation was established between the market managing body and the regulatory authority.

In 1997, the Jordan Securities Commission, an autonomous administrative authority was created with the task of supervising the activity of the market.

And since March 1999, the Amman Stock Exchange, a non-profit making association counting as members all the financial intermediaries operating on the market is the Exchange manager.

Egypt

A recent act of 1992 governing the financial markets provided the possibility of Stock Exchange corporatisation. The supervising authority remained within the competence of the Financial Market General Commission which is an autonomous administrative authority.

United Arab Emirates

Only since 1999, a Securities Commission has been created by virtue of a federal law. The same law also regulated the required administrative conditions for the creation of regional regulated markets.

Tunisia

In 1994, a legislative reform created the *Conseil des Marchés Financiers*, an autonomous administrative authority implementing the role of a regulatory authority. Whereas the Exchange managing body was handed to a joint-stock company counting as shareholders all the intermediaries authorized to join the *Bourse des Valeurs Mobilières de Tunis* (BVMT).

Morocco

Since July 1994, the market manager is the *Société de la Bourse des Valeurs de Casablanca*, a joint-stock company of private ownership. Whereas the control authority is within the competence of the *Conseil Déontologique des Valeurs Mobilières* (CDVM), a public legal entity having a financial autonomy.

Oman

Surprisingly, among all Gulf Exchanges, Oman has the best organizational structure. The capital markets act of January 15 1999 splitted the old Muscat Securities Market into three different entities; the Capital Market Authority, an independent administrative authority acting as a regulator, the Muscat Securities Market, a semi-governmental body, managing the Exchange and the Muscat Depository and Securities Registration Company as a central depository.

All the previous Arab Exchanges have aligned their organisational structure to the international standard of financial markets organisation and thus, separated between management and regulating activities.

Unfortunately, other Arab Exchanges did not follow the international trend and still have archaic organisational structures

Saudi Arabia

Although having the largest market capitalization among the Arab Exchanges (around 60 billion USD) the Saudi Arabian Stock Market remains managed and controlled by the same administrative body which is the Saudi Arabian Monetary Agency, the Saudi central bank.

Bahrain

Since its recent creation in 1987, the Bahrain Stock Exchange is a public agency acting as a managing body and as a regulatory authority at the same time.

Kuwait

The Kuwait Stock Market, an autonomous financial institution of public ownership handles both management and regulatory functions.

Palestine

The Exchange organisation and the regulating authority are within the competence of the Palestine Stock Exchange, which is a private company! Without any doubt, this is the most outrageous structure.

Conclusion

At the end of this comparative review of the Arab financial markets, we realize that despite being one of the first Exchanges established in the Middle East, the Beirut Stock Exchange is far from following the global trend in terms of organisational structure. The actual status quo will always be an impediment to the market development.

In order to get out of this situation, we recommend the following:

- a total separation between the market organisation and the regulating authority
- the creation of an autonomous administrative authority totally independent of other financial authorities aiming at protecting public saving, informing investors and looking after the good functioning of the markets.

- the split of the market into several sub-markets (first, second, options, futures...)
- the corporatisation of the markets.

Only the implementation of such a reform will attract foreign institutional investors whose presence is necessary for any development, and thus, allow the Beirut Stock Exchange and other Arab Exchanges to have their place among emerging capital markets.