FINANCIAL NATION-BUILDING IN IRAQ 1920–32

GEOFF BURROWS
PHILLIP E. COBBIN
Department of Accounting & Business Information Systems
The University of Melbourne

June 2010

Address for Correspondence:
Associate-Professor Geoff Burrows,
Principal Fellow,
Department of Accounting and Business Information Systems,
University of Melbourne, Parkville, Victoria, 3010, Australia
FAX: 61-3-9349-2397;
Telephone: 61-3-83442162
e-mail: ghb@unimelb.edu.au

Acknowledgments: The authors thank Peter Symes, Ian McDonald, Robert Dixon, Marianne Pitts and participants at the Accounting, Business and Financial History Conference, Cardiff, September 2007, for providing helpful comments, and Wayland Young (2nd Baron Kennet) for permitting access to his family’s papers.
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Abstract

The post-2003 turmoil in Iraq is a reminder that the former Mesopotamia emerged as a fledgling state only after World War I in difficult circumstances. This process, occurring under British hegemony, was complicated by existing and proposed financial obligations and involved the creation of viable financial systems and a new national currency. Financial aspects of state-creation are under-researched in the accounting and finance literature but have importance because of the challenging processes involved and the danger of failure. Iraq’s early financial history provides an additional perspective to its current problems and a useful resource for the investigation of state-creation processes more generally.

Key words: public-sector budgeting, currency boards, Iraq,
Introduction:

State (re)creations post-1900 have taken a variety of forms. Most numerous have been the various de-colonisation processes through which former colonies, dependencies or satellites separated from hitherto controlling powers, developments often hastened by powerful nationalist movements and weakening imperial controls and capabilities. Occasionally, multiple steps have been involved, a conspicuous example being the former Czechoslovakia, freed from Soviet control in the ‘velvet revolution’ of 1989, which then separated into its Czech and Slovak components in the ‘velvet divorce’ of 1993. More generally, wars have been a major factor in state creations. The final break-up of the Ottoman Empire after World War 1 gave rise to several new states in the near-East, while in Europe it facilitated the re-emergence of Poland which had been divided between Russia, Austria-Hungary and Prussia in the late eighteenth century. Similarly, World War 2 hastened the decline of British hegemony in the Indian sub-continent and much of Africa (but also enabled the USSR to occupy a swathe of formerly independent nations in central and eastern Europe). More recent state-creations accompanied the disintegration of the former Yugoslavia.

Whatever their origins, state-creations invariably involve major financial and economic discontinuities. Tyro states have to develop their own financial systems and introduce new currencies. If state-failure is to be avoided, transitions to financial independence must be handled as efficiently and effectively as possible, conditions difficult to achieve when, as frequently occurs, armed conflict and/or political chaos are present. Yet despite their importance, accounting and financial aspects of state-creation remain under-explored in the relevant specialist literatures, including their historical arms. Coffman and Wingfield’s (1983) index of the previous decade’s contents of the Accounting Historians Journal (AHJ) shows no relevant entries while the subsequent contents of AHJ and its newer accounting-history consorts, Accounting Business and Financial History and Accounting History, confirm this continuing gap in accounting’s historiography.

The broader political-economy literature similarly lacks comprehensive accounts of how fledgling nations have dealt with immediate budgetary pressures. Even such an obvious source as Post-Communist Economies (formerly Communist Economies & Economic Transformation), has emphasised economic-liberalisation, privatisation, exchange-rate and microeconomic-policy issues rather than budgetary-stabilisation problems. While currency matters have fared somewhat better in this literature, witness Lainela’s (1993) and Wyzan’s (1993) accounts of the introduction of new currencies in, respectively, the Baltic States and Macedonia, probably the best source of information consists of unpublished presentations by International Monetary Fund (IMF) staff at various international forums, usually by those who have been on the front line of the body’s international financial-support operations. Examples are Valdivieso’s (2000) overview of macroeconomic conditions in East Timor one year after independence, and Lonnberg’s (2001, 2003) analyses of
attempts to restore or transform East Timor’s, Kosovo’s and Afghanistan’s financial systems. However, even these accounts provide only partial budgetary data and cover only relatively short initial periods in what are obviously longer-term processes.

To help fill this gap in the accounting-history literature we examine the financial history of Iraq during 1920–32. The recent turmoil in the country highlights the fact that the former Mesopotamia emerged as a sovereign nation only as a result of the disintegration of the Ottoman empire during and after World War 1. State creation in this case was undertaken under British hegemony, albeit under League of Nations auspices, and involved attempts to create a viable financial system together with the introduction of a national currency. A complicating factor was that Iraq, almost from its inception, was encumbered by Ottoman-era financial obligations and a military agreement negotiated with its contemporary occupier, the UK. Inevitably, the financial aspects of state-creation proved problematic, necessitating the despatch of British financial missions to Iraq in 1925 and 1930. These missions are particularly well documented. The first was the subject of a report (Young-Vernon, 1925) to the British Parliament and details of the second are contained in Special Report by His Majesty’s Government in the United Kingdom of Great Britain and Northern Ireland to the Council of the League of Nations on the Progress of Iraq During the Period 1920-1931 (Report to League of Nations). In addition a range of other documents and records relate to these missions, including the private papers of E. Hilton Young, a key participant on both occasions.

Against this background, our particular focus is on three matters:

- The objectives of these missions and the factors which led to their despatch;
- The taxation, budgetary and currency measures prescribed.
- The success or failure of individual measures.

To this end the next section of the paper deals with the 1925 mission, providing background information about the creation of Iraq, events leading to the initiation of the mission, the revenue and expenditure measures suggested, and the degree to which these measures were implemented and were successful in the years immediately following. Then follows a similar analysis for the 1930 mission, augmented by an examination of the creation of an Iraqi national currency. In the penultimate section, Britain’s overall financial stewardship of Iraq is reviewed using criteria developed more recently by the IMF. The final section summarises the main findings and provides suggestions for further research.
The 1925 mission:

Background

From Report to the League of Nations (1931), Longrigg (1953) and Macmillan (2003), the following chronology of key political and economic developments can be constructed for Iraq:

- Britain occupying ‘Mesopotamia’, the former Ottoman administrative provinces of Baghdad, Basra and Mosul, through the gradual expulsion of the Ottomans by Anglo-Indian forces during 1914–18.
- The introduction of the Indian rupee (backed by sterling) as an interim national currency.
- The Principal Allied Powers conferring a mandate for Iraq upon Great Britain in April 1920.
- Widespread rebellions against British occupation in mid-1920, with order gradually restored partly through the use of the new medium of air power.
- The creation of a Council of Ministers—effectively an Iraqi Government—in November 1920, with each minister ‘aided’ by a British advisor.
- The transformation of Iraq’s constitutional status to that of kingdom through the enthronement of King Faisal, a member of the Arabian Hashemite dynasty, as the country’s monarch on 23 August 1921, following agreement by the Iraqi cabinet and the endorsement of a national referendum.\(^1\)
- Major economic and financial problems in Britain in the early 1920s, partly caused by the ‘stickiness’ of World War 1 expenditure, prompting the appointment of the Geddes Committee whose subsequent report (Geddes Report, 1922) recommended \textit{inter alia} major retrenchments in the armed forces and the transfer of its overseas defence responsibilities (and expenditure) as far as possible, to locals.\(^2\)
- Formalisation of the British mandate by the League of Nations in October 1922.\(^3\)

However, while Iraq’s constitutional developments and mandated status were suggestive of statehood it is questionable whether there was the necessary substance in the sense of Iraqis possessing the required political cohesion and feeling of national identity. Longrigg and Stokes (1958: 90), doubtless drawing on the former’s experience in the Iraqi administration during 1923–30, observed that:

There were the deep divisions within Iraqi society (urban-tribal, Kurd-Arab, Sunni-Shia) and the widely various stages of evolution reached by different elements in the population, from cultured intelligentsia to the mass illiteracy of tribesman … There was an uncompromising
national character, uncorrected by previous experience in public life, and by its extreme individualism ill-adapted for the workings of any real democracy, yet intolerant of other forms of government.

Significant Christian, Jewish, Turkoman and Assyrian minorities also existed. A complementary perspective is that of Macmillan (2003: 397) who averred that

In 1919 there was no Iraqi people; history, religion, geography pulled the people apart, not together. Basra looked south, towards India and the Gulf; Baghdad had strong links with Persia [Iran]; and Mosul had closer ties with Syria.

Other than the introduction of the Indian rupee in the early years of the new state the Ottoman taxation and budgetary-control systems were retained. By 1924, these inherited systems, overseen by the new Anglo-Iraqi administration, had turned earlier budget deficits into a healthy surplus as shown by Table 1 which also illustrates the dependence on land and farm taxation, and customs and excise duties, which together accounted for almost 75 per cent of total revenue in this triennium:

**Table 1 goes here**

However, by 1925, this improving financial position was about to deteriorate due to the conjunction of two events which appeared likely to generate unsustainable deficits:

- The conclusion of a military agreement between Britain and Iraq in March 1924, described by Young-Vernon (1925: 4) as obliging Iraq within four years to ‘accept full responsibility for the maintenance of internal order and for the defence of Iraq from external aggression’. The latter provision reflected ongoing incursions by Turkey in the north of the country and Britain’s desire to curtail its own military expenditure and progressively withdraw its forces from Iraq.
- The final arbitration in April 1925 (of which Britain had advanced warning) of the financial provisions of the Treaty of Lausanne under which the public-debt burden of the former Ottoman Empire was allocated between Turkey and the detached onetime Ottoman states. Iraq’s share of this debt, almost 6 per cent of the total, was likely to be well in excess of £2m, with repayments spread over at least two decades.

The estimated repayments during the first seven years of this arrangement are shown in Table 2:
Thereafter, the payments would gradually reduce but continue into the 1940s.

So serious was the expected impact of these new charges on Iraq’s projected financial position that the British High Commissioner, Sir H.R.C. Dobbs (1925), advised London on 25 February 1925 that Iraq was proposing to breach its Lausanne Treaty obligations by refusing to pay the Ottoman debt instalment then due on the grounds that ‘payment would entail the suspension of the payment of salaries and bring the machinery of administration to a standstill’.

**Mission initiation**

Against this background, on 3 March 1925, the Secretary of State for the Colonies, the Rt Hon. L.S. (Leo) Amery, appointed the two-man team of E. Hilton Young, MP, and civil servant, Roland V. Vernon, whose terms of reference, cited in the subsequent Young-Vernon Report (1925: 3), were:

> To enquire and report to His Majesty’s Government and to the Iraq Government what steps should be taken to ensure that it shall be possible to balance the Iraq Budget during the treaty period and afterwards, having regard to the requirements of the country for defence and security, administration and development, the provisions of the Financial Agreement and the obligations in respect of the Ottoman Public Debt imposed by the Treaty of Lausanne.

The duo comprising the financial mission represented Westminster’s political and bureaucratic arms. Biographical sources, particularly Young’s son, Wayland Young (1971) and Hall (2006), reveal that Young (1879–1960) was the youngest son of a baronet, whose family had long been prominent in the navy and administration, but with forebears that included one of the Baring brothers. After taking a ‘first’ in natural sciences at Cambridge, he was briefly a barrister before switching to financial journalism, initially as deputy editor of the *Economist*, then city editor of the *Morning Post*. An early participant in Bloomsbury gatherings, he was a friend of economists Maynard Keynes, Ralph Hawtrey, and Gerald Shove, and suitor (unsuccessful) to Virginia Stephen (later Woolf). During service in the RNVR during 1914–18, he became Liberal MP for Norwich, published the first edition of his *System of National Finance*, and was severely wounded in the Zeebrugge raid, causing the amputation of his right arm. In Lloyd George’s coalition government during 1922-3, he was Financial Secretary to the Treasury—junior minister to the Chancellor of the Exchequer—in which capacity he liaised with the Geddes Committee which advised on the restoration of the UK’s finances. At the time of the Iraq mission he was a backbencher following the advent of Bonar Law’s Conservative government in October 1922, the year in which he had married Kathleen (Lady) Scott, widow of the
Antarctic explorer, Captain R.F. Scott. Young’s letters to his wife provide additional source material about the mission, enriching the formal reports and records.

Party-political cronynism can have played no part in Amery, a Tory, appointing Young, a Liberal, to the Iraq mission. In the Lloyd George coalition, Amery, as First Lord of the Admiralty, had opposed the retrenchments that the Geddes Committee, with which Young was associated, had proposed for the navy. However, the two did have experiences in common which must have engendered mutual respect: both had been journalists pre-war and each had been on active service throughout the war. Whatever the depth of their personal relationship—Wayland Young (2005) recalled Amery being an occasional visitor to the family home during the 1930s—Iraq would form an enduring link between the two men.

While Vernon’s (c.1878–1942) *Who’s Who* entry indicates a family background more modest than Young’s, his Oxford ‘first’ was a prelude to an impressive civil-service career. At the Colonial Office his early postings included stints in the West Indies, South Africa, Australia (as private secretary to Governor-General, Lord Denman, during 1911–13) and the New Hebrides. Transferring to Treasury in 1914, he held a senior financial post in the Ministry of Munitions during World War 1. Returning to the Colonial Office post-war, his assignments increasingly centred on the near-east, including membership of the British team at the Treaty of Lausanne negotiations in 1922.

Baghdad was not the most accessible of locations in the mid-1920s. Young (1925) described how the pair left London on 6 March 1925, travelled by ferry and train to Marseilles thence by the S.S. *Macedonia* to Port Said, from where their nine-man party was conveyed overland, completing the 550-mile desert crossing from Damascus to Baghdad in 36 hours in a modern ‘caravan’ of four open-top Buicks.

**Revenue and expenditure estimates and recommendations**

The task Young and Vernon confronted is illustrated by data shown in Table 3, showing revised estimates for 1924–5 (of which eight months had already elapsed) and proposed expenditure for 1925–6, the latter incorporating (i) the Iraqi Ministry of Defence’s estimate of the expenditure required to fulfil the Military Agreement, and (ii) the first repayment of the Ottoman public-debt liability (which also included the belated payment of the previous year’s obligation) as estimated by Young and Vernon:

*Table 3 goes here*
Commencing their investigations into how to reduce this forecast 1925–6 deficit to a more-sustainable figure, Young-Vernon (1925: 3) articulated the conflict between the desirable and the possible. They recognised that Iraq

lacks much of the apparatus essential for a developed State … As an independent State it has to support an administration which is necessarily far more expensive than its former one, with all the institutions of self-government, and those higher standards in the discharge of State service which are inevitably required of a progressive Government … Under these circumstances, the present scale of expenditure … is not more in general than the country requires. It may be more than is possible … but it is not more than is desirable.

This dilemma was particularly acute in relation to public works for which Young-Vernon (1925: 39) observed that in countries such as Iraq, often an ‘investment is an excellent one. It would give a good return in better services and more economical administration. But in the present state … funds cannot be spared from revenue for the investment. Nor in the present state … can the funds be borrowed’.

Against this background, during their six weeks in the country, with Iraq’s auditor-general, Mr J. Parlby acting as secretary to their mission, Young and Vernon undertook a ‘Geddes Axe’-type review of public expenditure and revenue. The revised budget prepared by the pair, with the initially-proposed Iraqi budget included for comparison, is shown in Table 4.

**Table 4 goes here**

On the revenue side, data availability and administrative complexities prevented the imposition of an income tax. Consequently, some £223,000 of the total £290,000 recommended increase was to come from customs and excise duties, seen by Young-Vernon (1925: 15–16) as having the advantage that ‘the machinery for their collection is simple and efficient’. Land and agricultural taxes which Young-Vernon (1925: 10) recognised ‘is a matter which enters closely into the whole social structure of the country, which affects tribal organisation and the position of the sheikhs, and which cannot be dissociated from general questions of policy in internal affairs’, were seen as more problematic, capable of enhancing revenue in the future with better collection systems and land-tenure information, but offering little immediate prospect of higher revenue. The balance of the increased revenue was to come from selling a limited area of government land, the imposition of new turnover-taxes on the professions and corporations, together with the introduction of an income tax on all salaries exceeding £20 per month.
In their recommended £546,000 cuts in non-defence expenditure, only health services escaped the Young-Vernon axe. Government administration, education, police and posts and telegraphs, were all to be reduced by small cuts, most of which related to the workforce. However, small reductions in monetary terms often implied large-scale retrenchments. For example, to save £45,000 annually in the lower echelons of ministries and departments considered by Young-Vernon (1925: 27) to be ‘extravagantly’ staffed with ‘menials’, ‘messengers’ and ‘armed messengers’, would involve the abolition of approximately 1,000 positions. With more-major expenditures on irrigation and other public works, economies were achieved principally by postponing construction programs and retrenching staff that would otherwise have been required for their implementation. In the longer term a suggested (Young-Vernon, 1925: 26–7) review of salary levels could lead to additional savings given the falling cost-of-living.

Defence spending was also to be spectacularly downsized in proportionate terms, with Young-Vernon (1925: 47) averring that their recommended expenditure of £1,005,000, almost 25 per cent less than the original Iraqi proposal, would still enable the nation to meet its obligations under the military agreement. Conscription was also suggested by Young-Vernon (1925: 28) as a possible economy strategy in this connection.

Although the overall effect of these recommendations reduced the 1925–6 budget deficit from £1,432,000 to a more sustainable £367,000 the latter figure was still huge relative to total revenue and expenditure. The implication, as Young-Vernon (1925: 7–8) observed, was that either a part of the Ottoman debt-charge must be left unpaid (perhaps to be funded by agreement with the Ottoman Debt Council); or the [contemplated] military programme … must be substantially reduced … It might perhaps be said that there is a third possibility, to make further wholesale reductions in the services performed by the State. In our opinion this is a possibility which should be dismissed from practical consideration. The reductions which we recommend appear to us to be the utmost that can be effected if the Government is to continue to discharge its essential functions.

While they considered it outside their remit to determine how the military-spending/debt-repayment choice should be resolved, their discussion implied that the former was virtually sacrosanct and that there were prospects for renegotiating the latter. They also saw that, providing military spending was not increased, the budgetary situation would gradually ease due to eventual reductions in the annual Ottoman debt repayments, and the prospect of higher revenues as collection systems improved.
**Currency**

Separate from the budgetary position was currency which, despite some Iraqi objections, remained the Indian rupee. According to Symes, et al. (2001), the Iraqi Minister of Justice in 1922 had proposed that the nation replace the rupee with its own currency. This proposal was rebuffed by the British, who subsequently ignored stipulations in the new Iraqi constitution in 1924 relating to a national currency and issuing authority. On this matter, Young-Vernon (1925, p.25) declared that

> The establishment of a national Bank of Issue would be premature. That being so, the only sort of national currency which it would be prudent to contemplate would be an Iraqi rupee supplied in effect by the Indian Government, or an Iraqi sterling-rupee supplied in effect by the British Government. Either must be costly and might be inconvenient. The change to either of such currencies from the Indian rupee would, from the point of view of the gratification of national sentiment, be rather nominal that real. There is therefore in our opinion nothing to be gained at present by such a change, to set against the great disadvantage of unsettling the population in a manner in which so much depends on habit and on the confidence which is born of habit.

The Young-Vernon report (1925: 57) was signed ‘Baghdad, 25th April 1925’, indicating that the pair had drafted their report before departing for London where they arrived on 8 May. Amery tabled the report in parliament the following month.

**Aftermath**

As to the follow-up to the Young-Vernon mission, a contemporary observer, Longrigg (1953: 164), later summarised the position thus: ‘A large part of its suggestions, especially as regards new taxation and reorganisation, was not adopted. The Iraq Government was destined, indeed, to remain solvent but impecunious for years to come’. This was despite Vernon returning to Baghdad in late 1925, where he remained, according to Longrigg (1953), as adviser to the Ministry of Finance until 1928.

Similarly, Britain’s later Report to League of Nations (1931: 97) commented in relation to the Young-Vernon report that:

> Reasons of local policy prevented a large part of their proposals from being carried out, in particular, their suggestions for increased taxation. Nevertheless, the year 1925–26 resulted in a surplus of … [£503,000] for 1925–26, and the following years brought a surplus of … [£226,000].
Further insights into the success of the Young-Vernon mission, and the general progress of Iraq, can be obtained from Table 5 which shows actual revenue and expenditure for the six years following the mission, with 1924–5 (shown in italics) included for purposes of comparison:

Table 5 goes here

On the revenue side, the key features are:

- The ongoing dependence on customs and excise duties and agricultural taxes which, collectively, continued to provide approximately 75 per cent of total revenue throughout this period. However, within these categories it appears that Young-Vernon were unduly pessimistic about the immediate prospects of increased land and agricultural taxes which jumped by over 20 per cent in 1925–6 and remained mostly at this elevated level until the slump of 1929–30. In contrast, higher customs duties took longer to implement but ultimately increased by 10 per cent between 1924–5 and 1928–9.

- The introduction of income tax in 1927, described in Report to League of Nations (1931: 89) as being based ‘on the British law’ and initially levied at the rate of 3.63 per cent on all non-farm and non-property incomes (which were already subject to taxation) above 4,000 rupees (approximately £298). The Report indicates that although this tax raised only 1 per cent of total revenue in 1929–30, it was regarded as controversial and would undoubtedly become more so with a projected increase to 9 per cent for 1931.

- Although Iraq’s potential as an oil producer had, according to Mejcher (1976), long shaped Britain’s attitude to Mesopotamia/Iraq, significant production commenced only in 1927, and total production in 1929 was only 800,000 barrels. Oil royalties were minute at this stage and Iraq did not receive major oil revenues until the 1950s.

On the expenditure side, the noteworthy elements are

- The dominance of expenditure on the defence and police forces, which collectively always exceeded 31 per cent of total expenditure, and, with the large increase in defence expenditure following the implementation of the military agreement, increased to over 40 percent. However, in the four years following the Young-Vernon report, defence spending averaged less than 5 per cent above the £1,005,000 level they had recommended.

- The gratifying increases in education and health expenditures, respectively of 36 and 105 per cent during this period.
Negligible initial spending on capital works, consistent with the earlier Young-Vernon strictures on this point, but with some expenditure from 1927–8.

The absence of any repayment of Ottoman Debt obligations which had been expected to total almost £1.9 million during this period.

Overall, the aggregate net surplus for 1921–30 was £1.53 million. The Report to League of Nations (1931: 92) recorded that this amount, together with other ‘floating balances’ held by the Iraqi government, was used to:

- Extinguish Iraq’s share of the Ottoman Public Debt liabilities, £1.43 million;
- Invest in loans for railway development and reconstruction, £0.34 million.

In elaborating on the Ottoman Debt repayments, the Report to League of Nations (1931: 127) explained that

In 1927 the Minister of Finance in consultation with the British Government took the responsibility of purchasing, in the market [using Iraq’s financial reserves], Ottoman Debt securities with a view to handing them over in settlement of Iraq’s liability. These operations were finally concluded at a cost of £1,228,000 sterling. The cash value of the bonds and coupons which could not be bought and certain other liabilities which could not be extinguished by the delivery of bonds and coupons was found to be about £383,000. The Debt Council has agreed to this sum being paid in seven equal yearly instalments of about £63,000 each, including interest, of which four remain to be paid at the end of the period under review.

Files CO 732/28/18 and T 161/247 in the UK National Archives contain details of the negotiations during 1927 leading to these on-market purchases and annual payments. Modelled on an earlier scheme used by Italy to discharge its Ottoman debt obligations incurred in connection with the takeover of Tripoli, merchant banker N.M. Rothschild & Co, acting for the Crown Agents, purchased on-market heavily-discounted Ottoman securities which were then handed to the Debt Council in settlement of the majority of the debt. The outstanding balance was to be paid in cash in seven annual instalments (although Britain had initially requested a 20-year repayment period).

Although they proposed no specific remedies, Young-Vernon (1925: 24) identified Iraq’s international trade and payments as a matter of concern with net imports of goods exceeding net
exports by almost £3.5m in 1924–5, with this deficit only partly covered by expenditure by imperial forces in Iraq—an ‘invisible’ export—of approximately £2m, the balance being covered by the export of currency and drawing on ‘whatever cash or credit … [Iraq] has abroad’.

Despite the Young-Vernon opposition to a separate Iraq currency, according to Symes et al (2001) in 1926 Britain

proposed a Currency Board based in London as an authority that could issue a distinctly Iraqi currency. However, this proposal was roundly rejected by the Iraqi authorities because it would not be based in Iraq. In … 1927, Iraq resolved to establish a National Bank, but debate over the basis on which the currency would be issued caused the idea to founder.

While these developments were occurring, Young’s own eminence was increasing. Although he remained a backbencher, it was as a Conservative MP after he switched parties in 1926 over what he (Young, 1926) considered Lloyd George’s ‘socialistic’ farm-acquisition policies and pro-miner sympathies during the 1926 General Strike. Knighted in 1927, he became editor-in-chief of the Financial News, rival to the Financial Times for daily finance and business coverage. A director of the Southern Railways, English Electric, and Hudsons Bay companies, he had also chaired several parliamentary enquiries, and commissions, including the 1925–6 Royal Commission on Indian Currency and Finance (at which his friend Maynard Keynes was a key witness) and the 1927–8 East African Commission on Closer Union.

The 1930 mission:

Background

The Report to League of Nations (1931: 97) provides the following background to the second mission undertaken by Young:

In 1930–31, the preparation of the [Iraqi] budget again caused the Minister for Finance much anxiety. An economic crisis, due chiefly to the fall in the value of agricultural produce, had seriously affected the revenues of the country. At the request of the Iraqi Government, Sir Hilton Young paid his second visit to Iraq and in June, 1930, made recommendations with a view to balancing the budget. He was careful to emphasize that his recommendations were based on the assumption that the economic difficulties … were only temporary, and that if they continued it would be necessary to review the position again and make further economies. The crisis, however, continued and it soon became evident that the estimates of
revenue, though reduced by Sir Hilton Young, were still much too high, and that further drastic steps had to be taken.

This Iraqi requested represented a huge vote of confidence in Young and doubtless reflected the favourable impression he had made on King Faisal and his government during the 1925 mission. Although budgetary problems were one cause of the 1930 mission, another important factor was an Iraqi rethink towards the concept of a London-based currency board. Symes et al (2001) recorded that in 1930 the ‘government of Iraq invited Britain to reopen discussions of an Iraq currency based on the 1926 proposal’. The upshot was a ‘proposal to create the Iraq Currency Board’ which was approved by the Iraqi Cabinet on 17 March 1930 and presented to Young when he arrived in Baghdad on 15 May 1930, for a visit which lasted almost two months.4

Evidence that currency matters had primacy on this mission is Young’s (1930a) claim, in a letter to his wife written while travelling by sea from Marseilles to Ismailia, that he had been

Thinking out Iraq’s currency problem from the bottom in words of one syllable … The currency problem is perfectly simple, the substitution of a new Iraqi currency based on sterling exchange … The only problems involved are practical, not theoretical. For example, it must be a matter of practical difficulty in a country without statistics to judge how much currency here is in circulation, and so how much of new currency to provide.

Similarly, Young (1930b) in an early letter from Baghdad stated that he had “arranged with the P.M. [prime minister, Nuri al Said] to advise on 1. Currency, 2. Budget, 3. The slump, 4. Loans, in that order.” Young claimed to have made a

good beginning … The currency business is fairly plain sailing… the budget position is not really a panicking matter … The other two matters are rather fudge. There is not much to be done in Iraq to cure the world slump. Loans must await the conclusion of the treaty that the H/C [high commissioner] and Hubert are negotiating, and the settlement of a new oil concession.’

A week later, Young (1930c) wrote that he had told Nuri that Iraq needed two financial advisers, ‘a good man regularly in Baghdad and a consultant in London at a retaining fee (I contemplate £1,000 p.a.) and a special arrangement if he was needed in Baghdad’. He advised his wife that Nuri ‘is considering the idea and asked at once “would you be able to be the consultant?”’ The H.C. [high
commissioner] asked the same. Obviously it would be a good thing for them’. It would have been a good thing for him too!

Young’s £1,000 annual consultancy was short-lived. When he returned to London in mid-July 1930, it was after, according to Symes et al. (2001), amending the Iraqi proposals which were presented to the Iraqi parliament that October, and passed into law on 19 April 1931, ‘after a few minor modifications’. The first report of the Iraq Currency Board in March 1933 (p.2) in connection with the introduction of a national currency, recorded that Young ‘proposed a scheme for a new currency linked to sterling and managed by an independent Currency Board. The Government approved this scheme’. Subsequently, Lainela (1993, p.430) described the currency-board concept as an arrangement whereby the introduction of the currency is the responsibility of … a monetary authority separate from the central bank or the central bank’s other activities … the domestic currency in circulation is fully backed by foreign exchange and the amount of currency in circulation can only change according to changes in the foreign exchange reserves.

Hanke (2002) dated the origin of the currency-board idea to Britain in the early 1800s, citing the British colony of Mauritius in 1849 as the first application of the concept. Hanke (2002) also viewed currency boards as alternatives to central banks and outlined 20 points of difference between the two types of institution. Most of these differences relate to the highly circumscribed role of currency boards—basically concerned only with managing national currencies—compared with the much broader economic and regulatory roles of central banks.

As outlined in Iraq Currency Board (1933: 2), the major features of the Iraqi scheme were:

- The basic currency unit was the Iraqi dinar, ‘to be equal in value to the pound sterling’.
- Dinars were to replace rupees which were to be converted at the prevailing exchange rate with sterling.
- The Currency Board was to invest in the securities of States whose currencies were convertible into gold.
- Currency Board assets were to provide coverage of 100 per cent of currency issued.

The Iraq Currency Board (1933) also detailed the structure of the five-man board to which Young was appointed chairman on 11 June 1931. Two members were to be nominated by the Iraqi government; two members would be nominated on rotation by the three major foreign banks operating in Iraq (the
Eastern Bank, the Ottoman Bank and the Imperial Bank of Persia); the final member would be nominated ‘on the invitation of the Government of Iraq by the Governor of the Bank of England or by the Finance committee of the League of Nations’. One of Young’s early tasks as chairman was to oversee the design of Iraq’s new currency notes. Symes et al. (2001) reported that the notes were printed in England and issued in six denominations ranging from ¼ to 100 dinars, and signed by Young and two other members of the board. In his case, Young had to sign with his ‘wrong’ left hand, using the half-uncial script he had learned after losing his right arm to wounds sustained at Zeebrugge.

The Iraq Currency Board (1933: 3) reported that the exchange of Indian for Iraqi currency occurred during April-June 1932, with the rupees being repatriated to India and the sterling equivalent being received by the Board. Currency-board accounts when currency redemptions occur are complicated creatures with, in addition to balance sheets and profit and loss accounts, separate accounts inter alia for costs of notes and coins manufactured, issues and redemptions, and currency reserve funds. Perhaps most informative is the Board’s inaugural ‘statement of estimated general position’, based largely on the ‘mark-to-market’ concept, shown as Figure 1:

Figure 1 goes here

Consistent with the strictures of Lainela (1993) and Hanke (2002) about the operations of currency boards, all the Iraq Currency Board’s investments in 1933 were in sterling-denominated British Government or British colonial loans.

As regards the Iraq Currency Board’s seminal figures, Young’s first stint as chairman was curtailed in January 1932 when he was appointed Minister for Health in Ramsay McDonald’s ‘national’ government. He was replaced as chairman by his former patron, Leo Amery, who maintained this position until May 1940 when he resigned after being appointed Secretary of State for India. In the meantime, Young, who had been elevated to the peerage as Baron Kennet following his retirement from politics in June 1935, had become a major figure in the city, holding multiple directorships as well as chairing the Capital Issues Committee which regulated all significant corporate capital-raisings in the UK. He was also a ready-made replacement for Amery as chairman of the Currency Board whom he followed in that capacity in May 1940, serving until 30 June 1949 when the Board ceased operations upon responsibility for the note issue being transferred to the National Bank of Iraq.

As Lord Kennet, Young’s second stint chairing the Iraq Currency Board, in which capacity he signed all new issues of banknotes from 1942, gave rise to a unique phenomenon. In the style of the peerage, he signed simply as ‘Kennet’. In his first brief stint chairing the Board he had signed as ‘E.
Hilton Young’, giving him as Symes (2003) observed a ‘strangely unique position as a signatory of world banknotes. He is the only man to have signed the banknotes of an issuing authority with two different names’.

**Stewardship evaluated:**

Lonnberg (2003: 9) detailed how the Monetary and Financial Systems Department of the IMF in the 1990s developed a five-element transition strategy in relation to the minimal financial, regulatory, and information-systems structures required to ensure the financial viability of nations in post-conflict situations. These elements or criteria comprise:

- Credible means of payment and capabilities for external payments;
- Reasonably stable prices, calling for convincingly firm monetary control;
- Efficient utilisation of foreign aid and foreign exchange resources;
- Efficient mobilisation and allocation of savings (credit); and
- Effective financial services to execute the government budget (means to collect revenue, make payments, finance deficits, etc.).

Qualifications to the use of these criteria are that they were fashioned in an era of more-complex financial systems and institutions than existed when the 1925 and 1930 Iraqi financial missions occurred. In this latter period, currency rather than credit transfers was the predominant medium of payment; exchange rates were fixed; non-government agencies played little role in economic development and multilateral institutions such as the IMF and World Bank lay in the post-Bretton Woods future.

Regarding the first IMF criterion of capability to transact external payments, while Iraq’s balance of trade on invisible items had been reduced only marginally from £3.5m in 1924–5 to £3.1m in 1929–30, the nation’s overall external imbalance, a matter of concern in 1925, had been largely overcome due primarily to increased ‘invisible’ exports—disbursements by foreign governments, businesses and individuals in Iraq—according to Report to League of Nations (1931: 214). However, it is not clear whether this was due to changes arising from the 1925 Young-Vernon mission, although improvements in financial stability arising from the mission may have indirectly encouraged foreign investments and visits.

Although no price-indices for Iraq’s mandatory period can be located, overall it was a time of deflation due to both external and internal factors. The Report to League of Nations (1931: 129) referred to post-1921 reductions in agricultural prices and falls in the cost of living, together with a
policy of reducing public-sector salaries to levels affordable in times of budget stringency. Public servants’ incomes were reduced marginally in 1926 and by between 5 and 8 per cent from November 1930, with those on higher salaries suffering the greatest reductions. Thus price stability probably occurred independently of British policies. However, placing the nation’s currency under the control of an independent currency board—a device described by Lainela (1993: 430) as ‘the most simple, credible and pressure-resistant way to introduce a national currency in underdeveloped monetary conditions’—doubtless facilitated price stability. Although delaying the introduction of an Iraqi currency until 1932 clearly offended Iraq nationalist sentiments, in defence of Young-Vernon (1925) it can be said that the objection to introducing a national currency in the mid-1920s, when the Iraqi administration was still new and facing potentially serious budgetary deficits, was soundly based. That, post-1931, an independent Iraq retained Young’s five-member currency board until 1949 implies that domestic and international confidence in the currency was enhanced by this arrangement.

In relation to mobilisation and allocation of savings, the IMF doubtless envisaged capital accumulation in both private and public sectors to enable investment in business and public-infrastructure assets. Judgment is difficult on this point because of Iraq’s obligation to contribute to past investments made by the Ottoman Empire. However, it seems that Britain did act expeditiously to extinguish this liability at minimum cost to Iraq. In contrast, the military agreement with Britain, clearly was to Britain’s benefit: the Report to League of Nations (1930: 47–8) disclosed that the British garrison in Iraq was reduced from 33 infantry battalions in March 1921 to 1 battalion in October 1928, with large reductions also in RAF squadrons and Armoured Car companies. Arguably, some of the large increases in Iraqi defence expenditure shown in Table 5 could have been avoided and diverted to public services and infrastructure if Britain had retained a larger presence. However, given that the mandatory period was intended to prepare for full independence and that it was incumbent on Iraq to develop its own defence capabilities, it likely that Iraqi defence expenditure would have been higher had the nation enjoyed total autonomy in relation to defence.

Regarding the effectiveness of budgetary systems for revenue and expenditure, it appears that Britain inherited reasonably workable systems from the Ottomans which it was slowly upgrading, largely by increasing indirect-tax collections and expanding the tax base to incorporate income taxes. Given the various geographical, social, ethnic and security constraints facing Iraqi administrations, Britain deserves praise rather than blame for the real progress made with enhancing the effectiveness of the Iraqi financial administration.

**Conclusion:**
The creation of a new nation together with an associated national currency and financial system is a rare, but not unique, event. It is instructive to examine how these processes occurred in Iraq and the
degree to which they were successful. Iraq’s experience indicates that they never occur in a vacuum, and inevitably, are affected by encumbrances arising from either (i) past associations, or (ii) obligations incurred or imposed as a result of the nation-creation process itself. Given these constraints and judged by criteria developed by the IMF to deal with more-modern settings, Britain deserves praise for the post-1924–5 improvements it brought about in Iraq’s budgetary position and for the introduction of the national currency.

How these processes evolved in Iraq provides a useful benchmark to assess progress in other nations that have been (re)created in modern times. The most obvious examples are, in Eastern Europe and Central Asia, the post-1990 liberated member-states of the former Soviet bloc and the Balkan states which emerged from the disintegration of Yugoslavia. In the Southern Hemisphere, the emergence of East Timor as an independent entity in 1999 provides another example. For these tyro nation-states, new financial systems and currencies had to be created. Perhaps the closest contemporary parallel to Iraq is Poland which had ceased to exist as an independent political entity in the late eighteenth century and only re-emerged after World War 1. The parallels between Iraq and Poland are strengthened by the role that Britain played in Poland’s reconstruction, which involved a financial mission—albeit unofficial—by E. Hilton Young (1924) on Britain’s behalf in 1923. More recent descriptions of the introduction of new currencies in Estonia, Latvia and Lithuania (Lainela, 1993) and Macedonia (Wyzan, 1993) provide resources for comparative studies of this process in Iraq. Equally apposite would be a comparison between the introductions of the new Iraqi dinar in 2004 and its predecessor in 1932.6
ABBREVIATION

Abbreviation: KP – Kennet Papers, Cambridge University Library, Manuscripts Collection.


Committee on National Expenditure (1922): First Interim Report (Cmd 1581); Second Interim Report (Cmd 1582); Third Interim Report (Cmd 1589); Parliamentary Papers (Commons), 1922 Session 1, Vol. 9: 1–456 (Geddes Report).

Dobbs to Amery, 25/2/1925, National Archives, T161/247.


Young, E.H (1925) to Young, K, 14/3/25 (KP 107/2).

Young, E.H (1926) to Lord Asquith and Oxford, 19/2/26 (KP 78/5a).

Young, E.H. (1930a) to Young, K., 13/5/30 (KP 107/3).

Young, E.H. (1930b) to Young, K., 20/5/30 (KP 107/3).

Young, E.H. (1930c) to Young, K., 27/5/30 (KP 107/3).


Young, W. (2005), interview, 17/10/05.
Table 1: Iraq, revenue and expenditure 1921–4 (£’000 equivalents)

<table>
<thead>
<tr>
<th></th>
<th>1921–2</th>
<th>1922–3</th>
<th>1923–4</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land, crop and livestock taxation</td>
<td>1,313</td>
<td>1,045</td>
<td>1,078</td>
</tr>
<tr>
<td>Customs and excise duties</td>
<td>1,502</td>
<td>1,532</td>
<td>1,766</td>
</tr>
<tr>
<td>Post and telegraph receipts</td>
<td>405</td>
<td>210</td>
<td>247</td>
</tr>
<tr>
<td>Other revenues</td>
<td>712</td>
<td>751</td>
<td>693</td>
</tr>
<tr>
<td><strong>Total revenue</strong></td>
<td>3,932</td>
<td>3,538</td>
<td>3,784</td>
</tr>
<tr>
<td><strong>Total expenditure</strong></td>
<td>4,260</td>
<td>3,568</td>
<td>3,113</td>
</tr>
<tr>
<td><strong>Surplus (deficit)</strong></td>
<td>(328)</td>
<td>(30)</td>
<td>671</td>
</tr>
</tbody>
</table>

Sources: Young-Vernon Report (1925: A2); Report to League of Nations (1931: 95–6)
Table 2: Estimated Ottoman debt repayments 1924–31 (£‘000 equivalents)

<table>
<thead>
<tr>
<th>Year</th>
<th>Repayment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1924–5</td>
<td>173</td>
</tr>
<tr>
<td>1925–6</td>
<td>425</td>
</tr>
<tr>
<td>1926–7</td>
<td>370</td>
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<tr>
<td>1927–8</td>
<td>351</td>
</tr>
<tr>
<td>1928–9</td>
<td>272</td>
</tr>
<tr>
<td>1929–30</td>
<td>272</td>
</tr>
<tr>
<td>1930–1</td>
<td>271</td>
</tr>
</tbody>
</table>

Source: Young-Vernon Report (1925: 49)
Table 3: Iraq, budget data 1924–6 (£’000 equivalents)

<table>
<thead>
<tr>
<th></th>
<th>1924–5 (revised estimates)</th>
<th>1925–6 (proposed)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td>3,873</td>
<td>3,605</td>
</tr>
<tr>
<td><strong>Expenditure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-defence</td>
<td>2,674</td>
<td>3,113</td>
</tr>
<tr>
<td>Defence</td>
<td>752</td>
<td>1,326</td>
</tr>
<tr>
<td>Ottoman debt</td>
<td>—</td>
<td>598</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>3,426</td>
<td>5,037</td>
</tr>
<tr>
<td>Surplus (deficit)</td>
<td>447</td>
<td>(1,432)</td>
</tr>
</tbody>
</table>

*Source:* Young-Vernon Report, pp. 3, 47, 51
<table>
<thead>
<tr>
<th></th>
<th>1925–6</th>
<th>1925–6</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(Initial Iraqi proposals)</td>
<td>(Young-Vernon recommendations)</td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td>3,605</td>
<td>3,895</td>
</tr>
<tr>
<td><strong>Expenditure</strong>:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-defence</td>
<td>3,113</td>
<td>2,659</td>
</tr>
<tr>
<td>Defence</td>
<td>1,326</td>
<td>1,005</td>
</tr>
<tr>
<td>Ottoman debt</td>
<td>598</td>
<td>598</td>
</tr>
<tr>
<td><strong>Total expenditure</strong></td>
<td>5,037</td>
<td>4,262</td>
</tr>
<tr>
<td><strong>Surplus (deficit)</strong></td>
<td>(1,432)</td>
<td>(367)</td>
</tr>
</tbody>
</table>

*Source: Young-Vernon Report (1925: 3, 47, 51)*
Table 5: Iraq, revenue and expenditure 1923–30 (£’000 equivalents)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land, crop and livestock taxation</td>
<td>1,096</td>
<td>1,323</td>
<td>1,256</td>
<td>1,333</td>
<td>1,353</td>
<td>1,183</td>
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<tr>
<td>Customs and excise duties</td>
<td>1,829</td>
<td>1,861</td>
<td>1,852</td>
<td>1,972</td>
<td>2,014</td>
<td>2,010</td>
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<tr>
<td>Post and telegraph receipts</td>
<td>244</td>
<td>223</td>
<td>203</td>
<td>203</td>
<td>201</td>
<td>201</td>
</tr>
<tr>
<td>Income tax</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>13</td>
<td>28</td>
<td>43</td>
</tr>
<tr>
<td>Oil royalties</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>8</td>
<td>12</td>
<td>14</td>
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<tr>
<td>Other revenues</td>
<td>759</td>
<td>920</td>
<td>912</td>
<td>873</td>
<td>819</td>
<td>829</td>
</tr>
<tr>
<td><strong>Total revenue</strong></td>
<td>3,928</td>
<td>4,327</td>
<td>4,223</td>
<td>4,402</td>
<td>4,427</td>
<td>4,280</td>
</tr>
</tbody>
</table>

<p>| | | | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Expenditure</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Defence</td>
<td>653</td>
<td>1,058</td>
<td>1,012</td>
<td>1,096</td>
<td>1,046</td>
<td>897</td>
</tr>
<tr>
<td>Police</td>
<td>525</td>
<td>571</td>
<td>595</td>
<td>575</td>
<td>621</td>
<td>603</td>
</tr>
<tr>
<td>Health services</td>
<td>144</td>
<td>145</td>
<td>171</td>
<td>179</td>
<td>191</td>
<td>211</td>
</tr>
<tr>
<td>Ministry of Education</td>
<td>165</td>
<td>175</td>
<td>201</td>
<td>204</td>
<td>238</td>
<td>277</td>
</tr>
<tr>
<td>Capital works</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>124</td>
<td>96</td>
<td>93</td>
</tr>
<tr>
<td>Other expenditure</td>
<td>1,975</td>
<td>1,875</td>
<td>2,018</td>
<td>2,067</td>
<td>2,269</td>
<td>2,214</td>
</tr>
<tr>
<td><strong>Total expenditure</strong></td>
<td>3,462</td>
<td>3,824</td>
<td>3,997</td>
<td>4,245</td>
<td>4,461</td>
<td>4,295</td>
</tr>
<tr>
<td>Surplus (deficit)</td>
<td>466</td>
<td>503</td>
<td>226</td>
<td>157</td>
<td>(34)</td>
<td>(15)</td>
</tr>
</tbody>
</table>

Sources: Report to League of Nations (1931: 90–6)
**Figure 1:** Iraq Currency Board, Statement of Estimated General Position as at 31st March 1933

<table>
<thead>
<tr>
<th>Currency in circulation:</th>
<th>Investments at mean market price</th>
<th>Source: Iraq Currency Board (1933)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Notes</td>
<td>£2,005,150</td>
<td>£2,130,527</td>
</tr>
<tr>
<td>Coins</td>
<td>Dividends accrued on investments quoted ex-dividend</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cash at bankers and in hand</td>
<td>19,512</td>
</tr>
<tr>
<td></td>
<td>Estimated value of silver in coin in stock and in circulation, less 10% to cover cost of realisation</td>
<td></td>
</tr>
<tr>
<td>Balance</td>
<td>243,035</td>
<td>54,696</td>
</tr>
<tr>
<td></td>
<td>2,248,165</td>
<td>116,177</td>
</tr>
<tr>
<td></td>
<td>72,727</td>
<td>2,320,912</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>£2,320,912</td>
<td>£2,320,912</td>
</tr>
</tbody>
</table>
Endnotes

1 Here and elsewhere the modern English spellings of names such as Faisal, Shia and Iraq are used.
2 Strictly speaking, the Geddes Report consisted of three interim reports but no final report.
3 The status of the mandate was particularly contentious, with the League of Nations regarding the UK as the mandatory power, but this position never being formerly accepted by Iraq which regarded its relations with the UK as governed by Treaty. See Report to League of Nations (1931).
4 Rather than the overland Buick ‘caravan’ of 1925, this time according to Young (1930a) transport from Ismailia in Egypt to Baghdad, was by two-engine ‘Victoria’ aeroplane, which made a forced landing en route at Gaza when a burst oil pipe caused the pilot to shut down one engine. Accompanying him, but on a separate mission, was the former Foreign Secretary, Lord Robert Cecil, who was to offer political advice on a treaty and oil concessions being negotiated.
5 This was also the year in which Britain’s League of Nations Mandate concluded with Iraq joining the League as an independent nation.
6 As reported by the Governor of the Bank of England, Mervyn King (2004), between the first Gulf War in 1991 and the assumption of control by the Coalition Provisional Authority in July 2003, Iraq virtually functioned as two states: the south controlled by Sadam Hussein and the north as a defacto Kurdish protectorate. Most of the country’s extant British-printed (from Swiss-made plates) high-denomination dinar notes were located in the northern zone, and continued to circulate there, in effect becoming the currency of the north, albeit with no formal institutional backing (but in the expectation of same). In the south, the Saddam regime was forced to print its own dinar notes, which, compared to the northern ‘Swiss’ dinars, rapidly depreciated in value against the US dollar. Ultimately, both dinars were exchanged for a ‘new’ Iraqi dinar during late 2003 and early 2004, at a conversion rate of 150 ‘Saddam’ dinars to 1 ‘Swiss’ dinar.