

Syria

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- ◆ The first year or so of the new president's rule has been ambiguous: on the surface there is little tangible achievement, though in fact the groundwork has been laid for important change. The old regime dominated by the military and security apparatus survives, as witnessed by the arrest of some opposition figures in the summer of 2001.
- ◆ The country's socialist legislation has begun to be modified, though practical implementation of the needed economic reform remains hesitant due to the need to take account of internal opposition. This has come in particular from elements of the ruling Baath Party, many of who are entrenched in the state's bureaucracy.
- ◆ For the first time in decades, a role for the opposition in calling for change is beginning to emerge in a new political landscape characterized by a greater number of participants, especially from the private sector. Political culture in its widest sense is evolving to become more open and inclusive of previously marginal groups, but the manner of the decision-making processes remains the same, with the old regime's dominant elite still in control.
- ◆ The Syrian economy in the year 2000 improved somewhat over 1999, with growth at around 1.5%, having contracted at the same rate in the previous year. However, economic growth was half the rate of rise in population, and GDP per capita fell to about US-\$1,000. Merchandise exports rose to US-\$4.7 billion (from US-\$3.8 billion in 1999) but this was mainly due to higher oil prices, while imports rose very slightly to US-\$3.6 billion. The ratio of investment to GDP fell in 2000 to 17.6 %, continuing the negative trend that has prevailed since the mid-1990s.
- ◆ In light of these and other negative indicators, the need has been recognized for a sustainable process of national development to replace the country's untenable current economic model. Yet, for the time being, basic state and administrative practice shaping conditions for the economy remain unchanged. However, the medium-term prospects for change and growth may be brighter.

The beginning of change

Into his second year in power, Syrian President Bashar al-Assad and like-minded allies in the regime, as well as many among the public at large, have recognized **the need for a sustainable process of national development to replace the country's untenable current economic model.** Yet, for the time being, basic state and administrative practice shaping conditions for the economy remain unchanged as a precarious balance is maintained between reformists on the one hand, and elements of the military, of the ruling Baath Party, and of the security services on the other who are warier of change.

Social stability is assured by traditional structures of family, clan, and sect, under a strong central government. At the same time, various steps towards reform have begun, against opposition elements in both state and society.

These are numerous and can hinder development, but new patterns of technology, education, and social behaviour are becoming stronger, and will eventually replace many traditional values. Thus, **though in the short run very little has actually changed, various medium-term development trends are encouraging.** Under a moderately optimistic scenario, much future investment in Syria could be profitable, given that it is practically a virgin market for many types of infrastructure, as well as capital and consumer goods. However, before this happens, serious new financial, administrative, and physical infrastructure must be put in place. In addition, the quality of the workforce must be enhanced through training and rehabilitation. This will require solidifying the presence of modernizing forces and reforms, while maintaining stable political and social conditions.

Stability still comes first ...

The first year or so of the new president's rule has been ambiguous: on the surface there is little tangible achievement, though in fact the groundwork has been laid for important change. The old regime dominated by the military and security apparatus survives, as witnessed by the arrest of some opposition figures in the summer of 2001. At the same time, however, the state's priorities have begun to shift, as have those of parts of the population.

The private sector (which has expanded in recent years and resumed working in many

parts of the economy) and to some extent the intelligentsia have become more active in a livelier public discourse, with the aim of creating a fairer and more efficient system. Though profound media reform remains distant, the press's margin of freedom today is greater than at any other time in the past four decades.

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count of internal opposition. This has come in particular from elements of the ruling Baath Party, many of who are entrenched in the state's bureaucracy.

The president has yet to appoint his own cabinet. Though talk of new administrative arrangements has continued for the past year, the president has entrusted his reforms to what is essentially a caretaker government not up to the job of carrying out a serious program of change. There

has been no cohesion among cabinet ministers, with different ministries tending to go their own way in policy decisions. An example has been the clash between the Minister of Planning 'Isam Za'eem and some of his colleagues. He stated in a recent report that by next year there would be 600,000 people jobless in Syria, with extremely low average productivity of those employed. (Partly because of his forthrightness, Za'eem has consolidated his position in the regime and may even be promoted in any new cabinet.)

... but change has started

For the first time in decades, a role for the opposition in calling for change is beginning to emerge in a new political landscape characterized by a greater number of participants, especially from the private sector. Political culture in its widest sense is evolving to become more open and inclusive of previously marginal groups, but the manner of the decision-making processes remains the same, with the old regime's dominant elite still in control.

The flexibility of the system in the face of new challenges is being tested, while tolerance of the old levels of corruption appears to have been reduced. Openness towards the outside world has evolved rapidly towards better relations with neighbours as well as the European Union, and the general position of the regime is to strengthen these links. The role of the military and security apparatus remains very important, but that of civilians (reformists and others alike) is becoming more significant.

The economy has yet to feel the impact of these developments in political conditions, though the international and regional contexts are begin-

ning to appear more favourable to business. **The overall structure of the economy and of economic policies remains unchanged. However, there have been changes in the exchange rate regime, which has been partially liberalized. Tariffs are also lower and investment rules have been relaxed, but these and other barriers to business are still formidable. The state's foreign economic policy has seen considerable change in the direction of openness towards neighbouring countries, as well as extra-regional contacts.**

At the same time, the legal system remains cumbersome, administrative efficiency is poor, and the role of non-democratic political directives from the top in shaping economic and social processes means that the country is as authoritarian as it ever was under the old regime.

Though there is considerable resistance by people in state industries that will be affected by competition and other adaptations to a market economy, large groups of the Syrian population are amenable to change and have the cul-

tural flexibility to begin the process of adaptation. **However, for the time being Syria's limited experiment with liberalization has been slowed amid heightened regional tensions stemming from the Palestinian uprising that began in September 2000 and the sub-**

sequent election of Israeli Prime Minister Ariel Sharon. Members of the Old Guard within the regime justify the suppression of dissent on national security grounds, and have even accused some liberal reformers of collaborating with Israel.

The State begins to move in the right direction ...

Under the new president, the government has adopted a policy of reducing political pressure as an alternative to complete openness or the sudden development of widespread democracy so as to avoid the social tension and political confusion to which this could lead. In this context, agents of civil and political society have become vocal, not least these 99 intellectuals who demanded an end to the state of emergency in an open letter to the president two months after his accession to office. Damascus MP Riad Sayf's Movement for Social Peace advocates an end to one-party rule, abolishing state socialism, and restoring Syria's pre-1958 democratic republic. Sayf has antagonized the authorities by making public documents that implicate senior state officials in illegal deals conducted with cellular phone contracts in Syria. He also announced his collaboration with a group of political activists in forming the Syrian Human Rights Committee, a body aimed at shedding light on abuse, punishing those guilty of committing it, and ensuring that such injustices are not repeated.

In a continued relaxation on political conduct, the Syrian government has started reissuing identity cards and passports to ex-detainees and political activists. All of them had their civilian rights terminated either while in prison or while

under around-the-clock surveillance for suspicious political conduct. Other indicators of good will are the relaxation on previously banned written material, which is finding its way into homes, bookshops, and newsstands. Articles on the restoration of civil rights, along with those calling for the end of one-party rule in Syria, are allowed to pass freely, and so are other published materials on opponents of the regime. Much political material long considered taboo can be bought in public, and so can the works of previously blacklisted authors and political activists. **The state has not yet allowed most of the parties outside the ruling National Patriotic Front (NPF) to be re-activated, though it has permitted the relaunch of the Syrian Social Nationalist Party. Under a new party law, which is expected to take effect by the end of this year, parties not affiliated with the NPF – on either end of the political spectrum – will be permitted to operate so long as they do not threaten Syria's unity and security.** Coinciding with this will be a decree allowing the new parties to establish their own publications and authorizing private sector newspapers to function. The president last year allowed NPF parties to set up their own papers, and several communist and socialist publications have appeared since then. Both publication law and party law are expected to coin-

cide with the expected Cabinet dissolution before the beginning of 2002. Another positive step is the laissez-passer given to previously banished figures, while the former editor-in-chief of the state-run daily *ath-Thawra*, who was sacked in May 2001 for promoting the views of dissidents, was appointed advisor to Premier three months later.

Syria will develop toward pluralistic, democratic competition on the legislative level, but the state will still maintain basic control of the military and everything else the security establishment considers essential. The next legislative elections are due in 2002, though they may not be completely competitive. The regime has opted for a gradual development of the system in place. On the other hand, it would also be difficult to cut back the measure of free and pluralistic debate that has emerged, to totally ignore popular expectations connected to the end of a 30-year period of one-man-rule, or to reintroduce the fear that has all but vanished.

The president enjoys the support of most of the liberal forces because they expect that he will improve political conditions and allow for a gradual opening of the system. Others (including some in the military, in the ruling Baath Party, and in the security services) want to slow down this process, being uneasy about the reformist tendencies of the new generation, but they also know that they cannot stem the tide of change. For them, the president provides a measure of continuity of a basically authoritarian system, which, even with a modicum of legal security, a largely independent judiciary, and a lively and open political debate, including a real voice for opposition forces without, will not provide any real chance for a change of power through the

ballot box. Following this model will involve the ruling party's transformation to a more modern type of corporatist regime party that would also have slots for private businesspeople.

In parallel, and on the economic level, the state is considering a series of important measure that would go some way to dismantling the socialist system that has been in place for the past four decades. These include

- **the application by state firms of business principles in operations**
- **administrative and financial autonomy for state enterprises**
- **subjecting the industrial public sector to the provisions of commercial law with respect to pricing, employment, and wages**
- **applying market mechanisms with respect to competition, profits, quality and prices**
- **permitting state enterprises to resort to domestic or foreign management companies**
- **limiting state enterprises' relationship with the Ministry of Finance to issues of taxes and profits**
- **designating the Ministry of Industry as the only supervisory authority over the public industrial sector.**

This will give public sector companies more autonomy and insulate public sector enterprises from central government interference, while reorganizing state enterprises along the lines of joint stock and holding companies. With respect to the private sector, major reforms in the regulatory environment are also being proposed, though opposition to such steps remains strong.

All of these measures can be seen as necessary steps in a process of economic reform. However, they have not really been adopted

or applied yet, and even when this happens, they might still eventually fall short of creating a proper investment climate.

... while steps against corruption remain timid

For that to occur, other issues have to be dealt with, especially corruption. An intention to fight corruption was a main facet of the image the new president built in the years before his accession, and the theme was also part of his inaugural speech in July 2000. Some action has been taken in this regard (including a crackdown led by the president's brother Maher in July 2001 on smuggling in coastal areas) but **it is still true that to be successful in business in Syria, connections are needed to a senior figure in the army or government. Powerful private-state mafias are still closely linked to the public sector economy, which still makes it possible for government officials and others to directly interfere with anything from employment to contracts.**

The regime will not try to rid the system of corruption or at least seriously fight it. That will be done mainly with respect to the petty corruption of civil servants, policemen, customs officials and judges. Fighting such widespread corruption is certainly a demand of the general public, as well as of most of the business sector; and it is a necessity, if foreign and expatriate investors are to be attracted. The regime will also try to curb some grand corruption at the level of government officials, the military, or big business, without actually trying to eradicate it. Otherwise, the campaign would have to touch some of the president's aides as well as members of his family.

The Lebanese factor is important ...

With internal obstacles to change in Syria, external factors may come more prominently into play to promote development of the economy. At the same time, weaknesses in the domestic economy have been instrumental in spurring moves towards stronger regional and international ties. On the economic front as well as in other areas, Syria has made measurable progress in opening itself to outside influences and establishing ties to its neighbours. One of these is **the very strong link between Syria and Lebanon, formalized in the 1991 treaty between**

them and the stationing in Lebanon of tens of thousands of Syrian troops. Other manifestations of this phenomenon include the presence in Lebanon of several hundred thousand Syrian labourers, and the considerable volume of trade between the two countries, making Lebanon one of Syria's major markets.

On another level, a strong influence is exerted by the Beirut press and other Lebanese media on Syria. Previously, all Lebanese papers

would make it to newsstands in Damascus at noon, after going through a thorough check for anti-regime material. However, during the past year even *an-Nahar*, which remains officially banned in Syria, has started to reach homes via subscription, with no postal censorship; and unlike other opposition material on the Internet, the *an-Nahar* site can be accessed with no state proxy. The same applies to all Internet sites and material sympathetic to former Lebanese Army commander, General Michel Aoun. Previously, *an-Nahar* could not officially enter Syria at all. Now, articles written in it and other publications by prominent Lebanese figures get photocopied and make it into and through Syria by e-mail, fax, or hand.

On the business level, Lebanese investors are becoming increasingly active in Syria, and are in particular the most likely to be approved as the first non-Syrians to enter the banking sector. The new private banks will allow Syrians to bring back funds they have moved to Lebanon and other countries for lack of an adequate banking system at home. Syrians account for about six billion dollars of deposits in Lebanese banks alone, and some of those funds

are bound to find their way back to Syria. Furthermore, the law calls for the creation of bank secrecy laws similar to those in Lebanon. Non-Arab banks – working with or without Syrian émigrés – are eyeing the potentially lucrative Syrian market, but their chances of penetrating it quickly and profitably may be less than that of Lebanese institutions.

The role of Lebanon is vital in this respect. Lebanese business representatives have become quite assertive, defining what is needed to make Syria an interesting place for them to invest and work. Lebanese business is thus in effect lobbying for Syrian economic reform. The entry of the expatriate private sector and Lebanese expertise into banking and other areas is sought by the regime in order to cope with the demands of finance as well as to train those who are employed in state-owned banks. However, the role of the Lebanese will also be important in other sectors of the Syrian economy, as for example Lebanon's Mikati group has become in the telecom business of the Debanné family in agriculture. At the same time, Beirut-based expatriate Syrians will play a role in this process.

... with other regional links also significant ...

Apart from Lebanon, Syria is looking to increase its economic links with others in the region. Syrian links with various neighbouring states are thus improving as the country's emergence from isolation continues. Within its drive for better economic relations with other countries in the region, and also for important political reasons, Syria has recently opened up its trade with **Iraq**. Most notably, it has signed a

free trade agreement with Baghdad amid hopes that trade between the two countries would double from last year's level of \$500 million to \$1 billion by the end of 2001. Syria insists this can be accomplished within the limitations of UN sanctions, a consideration underscored by the visit this year of US Secretary of State Colin Powell to the country. The shoring up of trade and infrastructure ties is evidence of détente

with Baghdad. This is illustrated by the refurbishment of the Iraqi-Syrian oil pipeline, with plans for a new one also on the cards, evidence of the importance of shipments of Iraqi petroleum to Syria.

Another major regional infrastructure project that has progressed this year is the Wihdeh dam to be built between Syria and **Jordan**. The project had been on the drawing board for decades but had to await detente between Syria and Jordan to move forward. Meanwhile, water is being pumped from Syria to Jordan to meet shortages in Jordanian supplies, even though the Syrians also have problems in this regard. Political differences had kept the two economies relatively distant in the 1980s and for most of the 1990s. However, with a new leadership in Amman in 1999 and in Damascus in 2000, a rapprochement came about at various levels, including the economic.

The links between Syria and any one neighbouring Arab state on the one hand, and third parties, especially Arab, on the other, can be delicate. Thus, any further Jordanian-Syrian rapprochement for example cannot come at the expense of the Lebanese or the Iraqis. This means that in the longer term, the best framework for co-operation between Jordan and Syria will be a multi-lateral one that includes other Arab states; meanwhile, the interests of third parties, especially other Arab countries, must be kept in mind by Syrian officials. This is especially true of relations with Saudi Arabia, which must not be jeopardized by links to Baghdad. The Syrians must remain on good terms, for strategic and economic reasons, with the Saudis, not least of which is that **Saudi Arabia** is and will remain a major market for Syrian

exports. Meanwhile, links with **Kuwait**, closely associated with Saudi Arabia, have improved, as the Kuwaitis offered Syria a \$320 million loan shortly after the Syrian president's recent visit to the emirate. Earlier, Gulfinvest, a Kuwaiti investment company, said that it would launch the first Syrian investment trust.

In other forms of co-operation between Syria and regional players, an **Egyptian joint venture** and a Lebanese firm have been granted a joint, fifteen-year license to develop a mobile telephone network. In addition, economic relations with **Iran** have become more important, as well as various forms of co-operation with **Turkey**. Syria recently signed a five-year co-operation agreement with the latter for development of technical, commercial and economic cooperation in the agricultural field. At the same time, a joint committee of Syrian and Turkish businessmen was established, and relations between the two are expected to develop further in the short-run, with Turkey remaining both a major importer of Syrian goods, as well as one of the most important exporting countries to Syria.

The inauguration of a regional power grid, with Syria at its center, has been a very important development on the regional economic level. Syria recently took this big step toward economic co-operation with its neighbours by completing a 360-km, 400-kv power line linking its electricity grid with that of Jordan. The line represents an extension of an existing electricity link between Egypt and Jordan, which was completed in 1999. The next phases of the project will link Syria's network with Turkey's by the end of this year, and with Lebanon's grid in 2002, with an Iraqi link to be completed in 2003. **Syria is the crucial link in a regional power grid that may eventually extend to**

Europe via Turkey and to the Maghreb via Egypt. The unified power grid will add reliability to the power system. The regional grid scheme provides for a 20% production reserve to cover emergencies.

The regional electricity plans follow a separate announcement of **a regional gas pipeline**. Syria has also been participating in plans for regional gas pipeline schemes though these have not yet born fruit. One project involves building a pipeline to carry natural gas from Egypt via Jordan to Syria and Lebanon. There are doubts about the viability of the project, as the sub region's demand for imported gas may not be large enough to justify the cost of the pipeline.

Relations with the Palestinians have also improved as the Aqsa Intifada approaches the end of its first year. However, the stalemate in the peace process with Israel postpones serious consideration of the important economic implications of peace. On the one hand, some Syrians

see that peace involves economic opportunities, not least an increased investors' interest in the region. Some members of these have even begun to speak of an expected peace dividend – a concept that was conspicuously absent from the lexicon of Syria's public discourse before the year 2000. On the other hand, they also see that peace will expose the country to new forms of economic competition.

Peace, as is also understood in Syria today, will not only be a political or military peace, but will go along with new patterns of regional competition, particularly in the economic field. Israel, for the first time, will be a direct economic competitor of most Arab states, Syria included. Here, it is particularly the ability to co-operate with Arabs or Europeans that will influence Syria's chances of development and growth, especially in fields such as trade, industrial investment, and tourism.

... as are international relations, especially with the EU

Syria is also looking for economic ties beyond its immediate neighbours, with Damascus seeking observer status at the WTO as a prelude to the launch of accession negotiations. However, there is no guarantee that these will be quick or easy. There is limited serious external pressure on Damascus for change, as Syria is not under IMF tutelage nor is it seriously involved with the World Bank (despite some reports that relations with the latter should expand in the short-term).

Nevertheless, some incentives for Damascus to change its foreign economic policy have increased, however. **The EU is urging Syria to**

accept support in the context of the Barcelona Process, which the Syrians entered upon its launch in 1995 without yet concluding an association agreement. A recent visit to Damascus by European Commission president Romano Prodi helped to compress the timetable for negotiating a free trade agreement with the EU. By contrast, the US has not fully mended fences with Syria since the troubled 1980s – the brevity of Secretary of State Colin Powell's stopover in Damascus a few months ago serving as a reminder of still cool relations – and may not do so before the Syrians settle their differences with Israel.

At the same time, Damascus suspects the EU of wanting to dictate democratic reforms to Syria, which is vehemently denied by the European side. On the economic front, Syria has accused the EU of agricultural protectionism, and of wanting to push it to speed up economic reforms without taking into account the social and fiscal consequences. The official press in Damascus often relays opinions saying European competition will have a negative effect on Syrian industry. The association will give the EU preferential access to the still very closed Syrian market and should lead to a free trade zone, in a maximum of 12 years from the accord coming into force. Syria can hope that by linking itself economically to Europe that it will see an increase in foreign investment.

Despite differences across the negotiating table, a tour of Europe by the president and a further round of talks between the EU and Syria have resulted in closer ties, eventually leading to a trade association agreement. However, **Syria is not making full use of the funds it already receives from the EU (about 200 million euros since 1999). Just one of the ten EU projects planned for Syria in the past few years, ranging from culture to banking reform, has been completed, and only a tiny fraction of the loans made available to Syria by the European Investment Bank since 1999 has been used.** The latest EU aid came this year for the execution of an integrated coastal management program, extended to the Syrian and Lebanese governments jointly. Another EU program aims to support the telecom sector, including the technological and managerial modernization of the Syrian state telecommunications agency. A third recent scheme, within the EU's MEDA Democracy Program and not in the eco-

conomic sphere, finances a project to increase the capacity building in mobilization, communication and leadership skills for NGOs in Syria. Other EU projects are also being implemented.

At the same time, EU countries remain major trading partners of Syria, especially Italy and Spain (which currently take 27% and 7% of the annual value of Syria's exports respectively), as well as Germany, and the UK (respectively supplying 7% and 6% of Syrian imports). However, a problem that has arisen recently with Syrian cotton yarn exports to EU markets threatens to disrupt these links. As a result, the European Commission has established a control system on Syrian cotton yarn exports to EU countries, which have increased from less than a thousand tons annually in 1996 to over 30 thousand last year. The commission stated that the control system does not mean restrictions on Syrian cotton yarn exports to European markets, but the setting up of a prior export license system, (to be accorded five days after its request) which would not impede trade between the two sides. The Syrian government for its part stated its readiness to hear EU complaints on this matter, denying the European charge of the existence of subsidies on Syrian cotton exports.

Nevertheless, economic relations with EU countries will continue to expand in the short-run. This is especially true of Germany, which has just extended a major multipurpose loan to Syria for the protection and preservation of environment, to fight unemployment and poverty, as well as for educational projects. This is part of the agreement signed last year on the consolidation of debts owed to Germany by Syria (mainly old obligations related to the GDR) following

Chancellor Schroeder's visit to Damascus. That cleared the way for the resumption of normal economic relations between the two countries, which are expected to strengthen in the short-term. (At the same time, Syria's overall foreign debt remains seriously high, at over \$22 billion, including \$12 billion to former Soviet bloc countries.)

Aside from the European factor, if there was no domestic pressure for reform under the previous regime, things have changed in the past year. It is noticeable that with the change at the top, the Syrian business community has also begun to make its own demands heard more.

A major stumbling block to Syria's integration into the global economy could be Damascus's lack of rapport with the US. So far the US has not moved concertedly to staunch the flow of oil across Syrian territory, or to punish Syria for helping Baghdad circumvent UN Security Council program regulations to get Iraqi oil on the market. Another issue worrying the West in general and the US in particular is respect for intellectual property, so the signing by the president this year of Syria's first copyright law is yet another signal that Damascus is prepared to pay greater heed to international business norms. However, much more needs to be done to bring Syria into line with global economic practices and rules.

The financial sector is crucial

One of the key missing elements in Syria's business environment remains the lack of a modern financial system. The decision to reform the banking sector and to allow the establishment of private banks has been one of the most significant developments so far of the era of the new Syrian president. In June 2000 Syrian Prime Minister Mustafa Miro spoke of the necessity of developing the country's banking sector, describing the matter as one that was urgent and could not be delayed. He added that this must take place side by side with improving the efficiency of the banking sector and developing Syria's central bank, yet over a year later a great deal remains to be done in this regard. Foreign banks were allowed in Syria's Free Zones last year, and the Baath party leadership endorsed a draft banking law in December 2000. (Muhammad al-Hussein member of the ruling Baath leadership, who is also the chairman of its Economic Bureau, publicly confirmed that

these and other steps towards economic modernization are a top priority for the country.) The new law was signed by the president in April of this year, yet the pace of banking reform remains slow.

The opening up of the sector is a crucial step to encourage foreign and expatriate investment, increase the number of development projects, and stimulate economic growth. The reform program drawn up for the Syrian financial sector also included a plan to improve the role of the Central Bank of Syria in directing financial and monetary policy, to create a stock exchange, and to amend foreign exchange laws for the Syrian pound so as to reflect free market rates.

Financial sector reforms are of particular importance, and there is an urgent need to establish a strong supervisory structure at the central bank in conjunction with strict, transparent conditions for licensing new pri-

vate banks, and restructuring existing public sector banks, in conjunction with reforming state owned enterprises. Implementation of the banking law is awaiting the issuance of administrative guidelines by the Central Bank. A modern banking system is non-existent in Syria. The development of such a framework is necessary for a renewal of economic growth and investment. Without a modern, well-regulated financial system, it will be difficult to mobilize local and foreign investment, or to lure back some of the money held by Syrian expatriates abroad. If the government succeeds in attracting some of these funds as investments, the economic impact on Syria would be profound. The new banks will help allow Syrians to bring back assets they have moved out of the country or failed to repatriate, estimated at over \$60 billion. Much of this wealth is held in the West, as well as in Lebanon and the GCC countries for lack of an adequate banking system at home.

However, the banking boom in Syria may be some way off, since several months after the passage of the relevant law, the regulations required for commercial banking are still – unusually for such a legal measure – lacking. This is in addition to the absence of many practical steps that need to be taken before a modern efficient banking system can start to function. One of these is that the Central Bank of Syria needs to undergo reform before international financial institutions and other investors will be interested in entering the Syrian market. On the positive side, the central bank is training young personnel in modern banking and finance methods, with these and other changes being made in co-ordination with the Syrian private sector as well as non-Syrian trainers (including ones from other Arab countries such as Bahrain.)

Establishing private banks represents a major departure from state ideology, which until recently considered banking to be the monopoly of the public sector. The banking law allows Syrian individuals and institutions to establish 100% privately owned banks, and banks in collaboration with the public sector, in which case the latter would hold 25% of shares. The law also allows Arab and non-Arab individuals and institutions to establish banks, but only in association with the Syrian private or public sector, and provided that foreign ownership does not exceed 49% the bank's capital. Also bank capital should not be less than \$30 million and the new banks will be subject to a flat tax of 25% on profits. However, these conditions may not be attractive enough for larger or more international banking organizations, so the expectation is for smaller entities, possibly Lebanese, to be initial entrants to this market as they have done in the free zones. Syria is expecting its decision to allow foreign banks operate in free trade zones for the first time to spur investment there. Syria has six free trade zones, which it is planning to expand in order to service the local market and also transit trade. The largest expansion would be in the port city of Latakia where a new free trade zone is planned.

Draft legislation for establishing a stock market is also on the cards, but it has been the subject of a heated debate that centers on two main issues. The first is whether Syria is ready for a stock market in the absence of company financial disclosure regulations and agreed international accounting and audit standards, and of local technical capability to supervise the market effectively and transparently. The second issue is who should own and operate the bourse: the Union of the Chambers of Commerce, as

the draft law stipulates, or another entity, consisting perhaps of banks or stockbrokers or both. Other important draft legislation under discus-

sion is the new Money and Credit law, which sets bank supervision.

Hydrocarbons will remain important

Until the country has a proper business climate and investment begin to flow in, Syria will remain dependent on Arab aid as well as on traditional exports. Of these, hydrocarbons are the most important. Oil has been a mainstay of the Syrian economy since the late 1980s, and will continue to be so for at least another decade. The growth in the oil sector in 2000 was 44% compared to 1999.

Syrian oil reserves will last for approximately 12 years if production remains at its current levels and no new exploitable discoveries are made. On the other hand, the Syrian Ministry of Petroleum has said recently that the country's oil resources could last until 2020, 10 years longer than previous reports had claimed. **Based on Syria's current production rate of 600,000 barrels per day – 320,000 of which are shipped to the West - the ministry projected that oil reserves would run dry in about two decades. Foreign investment outside the oil sector has been virtually non-existent due to the lack of access to private debt financing.** Oil accounts for up to 60% of the country's export earnings and more than one-third of GDP. The government has, after some delay, begun to move on oil, modifying terms of its production sharing agreements to bring them into line with international standards. Syria is also placing emphasis on exploiting its natural gas reserves. Syria remains highly dependent on oil for 40-50% of the state budget. Syria could become a

net oil importer again (which it last was in 1987) within the next decade or so, not only because major oil fields are likely to be depleted. Even if new oil finds were to be made, domestic consumption, accounting for 50% of Syria's production, is increasing.

The Syrian economy will also continue to realize increased revenue from illicit Iraqi crude oil exports to Syria. The past few months have seen the reopening of a pipeline between the two countries, with Iraqi crude being pumped through and sold to Syria at a discount. Damascus and Baghdad also plan to build a new oil pipeline, as the old one linking Iraq with Syria is corroding and no longer economical. The planned capacity of the new pipeline is around 1.4m b/d. It would be built in two stages: the first inside Syria up to the Iraqi border, and the second in Iraq. Financing is expected to come from some of the country's newly established banks.

At the same time, gas is starting to become more important for the Syrian economy. **In 1998, Syria discovered a reserve of natural gas that amounted to 600 billion cubic meters, expected to last well beyond 2020. The find prompted the government to invest heavily in a \$400 million extraction plant, administered by the American company Conoco, in the Dayr al-Zour district along the Euphrates.** The plant is expected to satisfy Syria's gas needs, of which the country imports 40% at a cost of \$50 million per year. The new project

will generate annual revenue of \$180 million. Lebanon has already benefited from the Syrian discovery, having since 1999 received 3 million cubic meters of gas per day for electricity production. Turkey is also a beneficiary, with Damascus having this year signed a treaty with Ankara that also allows Syria to direct gas to Europe through Turkey. In four years, the Syrian Ministry of Petroleum will take over the operation. Syria was producing 13 million cubic meters of gas per day before the Dayr al-Zour project was launched. Production is now expected to rise to 25 million cubic meters per day.

In general, gas will continue to become more important in the Syrian economy. The government is working to convert its power sector from oil to gas fired generation to free more petroleum for export. The generating plant in the coastal city of Banyas would be transformed into a natural gas refinery. Kuwait will provide both financial and technical assistance to help develop the recent discovery of natural gas. Kuwaiti experts on the extraction, manufacturing, and marketing of the gas are helping to export the country's gas reserves to Lebanon, Turkey, and Cyprus.

Powerful social change continues

In addition to major economic and political developments taking place in Syria, important social pressures for change are continuing to build up. Quantitatively, **demographic growth is still close to 3% annually. The result is enormous pressure on schools and universities, and an annual 200,000-250,000 new jobseekers.** (Current estimates about new entrants onto the job market are conservative in that they do not consider any increase in female participation.)

Syria's population of over 16 million is extremely young, with almost 45% under the age of 15, which puts enormous pressure on various aspects of the system. Even within the Baath party, younger members are less ideological than the Old Guard, and the president feels a strong commitment to his own generation, as well as Syria's youth and their expectations in general.

Qualitatively, technical modernization, not least the spread of computer technology, wide-ranging access to the Internet and mobile

phones, has continued to change society, through the education system and otherwise. Increased openness, especially towards Lebanon and Europe, has also encouraged further social change at many levels. The young president, with his high level of education, experience of life in the West, and exposure to and interest in various aspects of technology, has played and will continue to play a role in this process. (His wife, Asma, also has these attributes, and her role should also become important in this respect, even indirectly).

One major social problem in Syria, especially for the younger generation, is unemployment. Joblessness among younger people (age 15-30) is generally estimated to be not below 25%. There is increasing informal joblessness i.e. unregistered unemployment interrupted by occasional marginal jobs. This problem is exacerbated by lack of data: except for employment in the government sector, reliable statistics do not exist in this field.

The Syrian government is likely to follow an expansive course for the year ahead at least, rather than the austerity policies of the last decade. Plans are being implemented to fight unemployment by extending soft loans to graduates who wish to set up their own small or medium enterprises. However, even these schemes and government plans for the public sector to employ some 65,000 newcomers in 2001 will not be sufficient to cope with growing unemployment, particularly among younger people.

That less overt poverty is visible in Syria than some other Arab states seems to be due to a deep-rooted system of private social security associations that care for the poor even outside the extended family. There is the threat of decreasing standards of living and human development, and of increasing poverty. No reliable statistics exist on these issues, but spending on education has been on the decrease during the second half of the 1990s, both in relation to GDP and to the budget. At the same time, it is evident that the number of poor has been on the increase and income differentials have widened since the mid-eighties at least. This influences the levels of public health and education, and it can threaten social stability. Such a situation adds urgency to the need for concentrating on social issues in order to meet at least some of the demands and expectations of society.

The education system has seriously deteriorated, and cannot be improved by piecemeal or conventional reform. Recent efforts to promote edu-

cation have thus included reform that would have been more difficult under the old regime. For example, **basic and university education have recently been opened to the private sector, allowing establishment of branches of Arab and foreign schools and universities in Syria. As a result, the first private secondary school in Syria since 1963 to obtain a license, the Choueifat International School of Damascus is opening this year.** The school curriculum, chosen by an independent committee approved by the Syrian Ministry of Education will be carried out in English and Arabic, with French being taught intensely. The Choueifat school is Lebanese-based, yet another example of the influence that Lebanon is exerting on Syria.

Europe continues to play a powerful social and cultural role in Syria, despite the important spread of American influence. However, a major difference between the two is that US aid and technical co-operation is still virtually non-existent in Syria, while European programs expand. For example, during the visit of French Foreign Minister Devrine to Damascus in April, a Memorandum of Understanding was signed between Syria and France for among other things, cultural cooperation for the years 2001-2003. A scientific cooperation agreement was also signed between Le Havre and Damascus Universities, involving among other things a closer association between the two institutes' Departments of French.

Conclusion: Internal change interacts with external opening

Syria is faced with serious external and internal economic challenges. These include the need to open up to the region and the rest of the world while trying to avoid the pitfalls of globalization and hasty structural change, and at the same time cope with crises stemming from the Arab-Israeli conflict as well as other problems in the Middle East.

After several decades of central control of the economy and self-imposed isolation, Syria is coming out of its shell. At the same time, infrastructure and other links with neighbouring states are being strengthened, as Syria's emergence from isolation continues.

In a positive step, although difficult to implement, high-ranking Syrian officials have recently promised that loss-making state companies would be restructured and forced to adopt more market-orientated policies, hopefully making them more attractive to potential investors further in the future. However, before this happens, a serious new financial, administrative, and physical infrastructure must be put in place. This will require solidifying the presence of modernizing forces and reforms, while maintaining stable political and social conditions.

Despite these and other pieces of unfinished business, it is becoming increasingly apparent in Syria that the dynamic of internal economic reforms interacting with an opening up to the outside world is unstoppable. At the same time, it remains to be seen whether political reform will keep pace with changes in the economy, or whether the country will follow the model espoused by some emerging

economies of liberalizing business while maintaining a strong security apparatus and one-party rule. The latter will involve a tricky balancing act. Whether an ambitious program can be accomplished quickly against a background of regional turmoil is questionable.

What is no longer in doubt is the need for reform; its pace and style, however, have yet to be determined. **Reform has accelerated in the past year, but still slow, hesitant, and ad hoc. The government has declared economic reform, but there is still no conceptual framework for it and no comprehensive program. Syria does not have a privatization policy. However, de facto privatization has been pursued over the last few years in certain sectors such as infrastructure.** Once the exclusive preserve of the state, they have now opened by various means to private sector participation. Privatization in the sense of selling public assets is not a priority at this stage, and not before a clear regulatory framework is in place. At the same time, draft legislation aims to reform state enterprises to make them more autonomous and free of central government interference.

Syria has promising investment opportunities in practically all sectors of the economy and an entrepreneurial class that was constrained in the past but is now preparing itself to assume a leading business role once an enabling regulatory environment is put in place. There is strong government interest in promoting greater downstream investment in the agricultural sector, in particular food pro-

cessing and textile manufacturing. Outside investors have been welcomed in certain sectors, notably telecom and tourism.

The change at the top has reset political priorities in a way that critics had often demanded. The new power-holders concentrate on the domestic scene, and they attach a higher priority to economic policies. It is also accepted that new jobs and modern, export-oriented industries have to be based largely on foreign and expatriate investment. This, however, requires a proper investment climate, including legal security as well as a workforce of higher quality.

There is more harmony today between the private sector and government, and the regime is likely to further increase the room for private-sector activities rather quickly. At the same time, the government will seek to maintain external rent flows, including aid, mainly from Gulf sources, as well as profits from Iraqi oil pumped through Syria.

Syria's economy is currently in transition. Putting in place the necessary infrastructure for the development of a market economy has become a priority since the country's new president came to power. A year or so of accelerated but erratic liberalization has brought encouragement to private business but also sown confusion. Syrian reform and its homegrown structural change still face major hurdles, but a pattern has emerged of external opening interacting with domestic liberalization, though without the pressure from Bretton Woods institutions or bilateral donors. However, with oil prices higher and the agricultural sector recovering, along with the reform about to shake up the banking industry, Syria could soon be on the path to higher economic growth.

The author

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