

BTI 2010 | Syria Country Report

Status Index	1-10	3.88	# 108 of 128	
Democracy	1-10	3.23	# 115 of 128	↗
Market Economy	1-10	4.54	# 94 of 128	➔
Management Index	1-10	2.77	# 117 of 128	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	20.5	HDI	0.74	GDP p.c.	\$	4276
Pop. growth	% p.a.	3.5	HDI rank of 182	107	Gini Index		-
Life expectancy	years	74	UN Education Index	0.77	Poverty ²	%	-
Urban population	%	53.9	Gender equality ¹	0.42	Aid per capita	\$	3.8

Sources: UNDP, Human Development Report 2009 | The World Bank, World Development Indicators 2009.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

Executive Summary

The Syrian state and economy are currently stable despite ethnic tensions, external pressures and the inherited economic order's long-term weakness. Under Bashar al-Asad, Syria remains an authoritarian regime with a state-dominated economy. In recent years, however, power has shifted from party apparatchiki to reforming technocrats around the president who are trying to implement a limited transition to a market economy without sacrificing stability. The dwindling of Syria's oil resources, which provide over half of government revenues, has driven the political leadership to deepen marketization. This process has thus far included adhering to liberal international trade agreements, opening private banks, adopting new more investor-friendly laws and attempting to broaden the tax base. The result has been a combination of crony capitalism and Dubai-like tertiary inward investment, but not industrial renewal. While a certain amount of political decompression continues in Syria, political pluralization remains rudimentary. The growth of crony capitalism is a major hindrance to democratization.

Bashar al-Asad's vision of Western-style modernization was initially matched by an attempted rapprochement with the West, notably the decision to join the Euro-Mediterranean partnership. This partnership was expected to encourage new investment and overcome resistance to change from Syria's vested interests. International developments, however, deflected Syria from proceeding in this new direction. The failure of the Syrian-Israeli peace process triggered Syria's 2001 opening to Iraq under Saddam Hussein and its opposition to the U.S. invasion. This diplomatic alignment, in turn, sparked a struggle over Lebanon. The fallout from the assassination of former Lebanese Prime Minister Rafiq Hariri precipitated Syria's withdrawal from Lebanon. It also blocked Syria's accession into the Euro-Mediterranean partnership. Syria then shifted its foreign policy toward support for Hezbollah and Hamas and alignment with Iran. U.S. attempts to isolate Syria slowed down its economic opening while efforts aimed at regime change froze political decompression. The failure of Israel to destroy Hezbollah in 2006 and the

latter's blockage of U.S. efforts to turn Lebanon into an anti-Syrian bastion showed that Syria could not be isolated. The Obama administration's recognition of Syria's regional importance together with Turkey's sponsorship of indirect Syria-Israel pre-negotiations appear to have restored conditions more favorable to economic and political transition in Syria. The global financial crisis, however, will likely have a counter-effect.

History and Characteristics of Transformation

The constraints on a liberal transformation in Syria are rooted in its recent formation as a modern state. The post-independence rise of radical nationalism among the middle class and peasantry destabilized the semi-liberal oligarchic regime, deterred investment and paved the way for the Ba'thist coup of 1963. This initiated a period of revolution from above, in which nationalization of big business and land reform demolished the class power of the old oligarchy and gave the Ba'th state control of the economy. This was followed by a period of intense struggle between the regime and the opposition. During this time, factional struggles within the regime played a role in precipitating the 1967 war, in which the more radical faction was discredited. In 1970, Hafiz al-Asad rose to power by consolidated his regime and concentrated authority in his so-called presidential monarchy. Al-Asad created stability by achieving balance between the army, the Ba'th party, a largely Alawi-staffed security apparatus, and a new state-dependent private bourgeoisie. The latter was appeased through limited economic liberalization. Over time, a combination of repression, institution building, patronage, and foreign policy legitimacy defined al-Asad's Syria.

Al-Asad's regime had a built-in resistance to liberalization. As an ideological party rooted in plebeian strata, the regime institutionalized populism. The public sector, the main source of public revenue, could not readily be replaced by taxation of a private sector deft at tax evasion. Regime legitimacy was contingent on an informal social contract under which citizens surrendered liberal political rights in return for state provision of subsidized food, jobs and farm support prices. The regime's reliance on a system of patronage dispensed to core supporters means that the state's withdrawal from the economy would put its stability at risk. Sustained liberalization would require the state to permit the creation of an entrepreneurial bourgeoisie, which, being willing to invest, could provide a viable alternative to the public sector. This seems unlikely to happen as the old bourgeoisie was politically opposed to the regime and newer elements are largely commercial or rent-seeking. Syria's industrialists are weak, and foreign partners absent. In the absence of investor confidence, Syria's capital was largely exported. In order to reverse this trend, the historic gap between the state and the bourgeoisie must be bridged, the rule of law must be upheld, and the on-going conflicts in Syria's regional environment must be resolved or ameliorated.

Syria's inability to maintain its statist development has forced the regime to embark on several waves of *infatih* (opening) and economic liberalization. This trajectory, however, failed to acquire momentum because rent windfalls in the form of oil revenues and Arab aid periodically relieved economic pressures. While Syria's first *infatih* during the 1970s largely recycled oil rent, the second late-1980s opening witnessed the state's acceptance of the private sector as a partner. The result was that the private sector's share in production, investment, foreign trade, employment and GDP had by the 1990s exceeded that of the public sector. In 1991, a law providing incentives for inward investment further opened the economy. Economic liberalization generated a so-called military-mercantile complex, which was formed around a new upper class. This class was deepened as the sons of the state elite went into business, producing an amalgamation, through intermarriage and business partnerships, between the largely Sunni bourgeoisie and the Alawi-dominated state elite.

Initially, the state pursued a policy of balance between the new bourgeoisie and its initial plebeian constituencies by charting a middle course between populist statism and a thorough turn to market capitalism. This allowed a new politically connected rent-seeking class to emerge, which exploited state-granted import monopolies and contracts. In a more open and transparent market, these monopolies and contracts would have been threatened by competition. After Bashar al-Asad's rise, the Ba'th party started to lose power to a new bourgeoisie and a group of liberalizing technocrats. This new class pushed measures to liberalize Syria's economy and to prioritize the needs of investors over the regime's former plebeian constituency. Syria now finds itself amid a period of crony capitalism as it makes its transition to a market economy of sorts. This transition has been accompanied by limited political liberalization but not rule of law or democratization. Thus, in the first years of Bashar's rule he encouraged greater freedom of expression, unleashing the so-called Damascus Spring; however, when opposition forces crossed "red-lines" including attacks on the legacy of Hafiz and the corrupt practices of incumbent elites, they were repressed. Syria claims to want to follow the Chinese model of economic growth first, democracy postponed. However, the influx of investment by Gulf capital into the tertiary sector and the continuing rudimentary capacity for industrial exports suggest that Syria is, instead, slipping into the Dubai model.

Transformation Status

I. Democracy

1 | Stateness

The state enjoys an effective monopoly on the use of force over its territory. Its political infrastructure penetrates the rural periphery. However, sporadic outbreaks of inter-group violence and terrorism, such as the car bomb attack in late September 2008 when 17 people were killed near the Shi'ite Saydah Zeinab shrine outside Damascus or the killing of Syrian General Muhammad Suleiman on 1 August 2008, highlight a certain enervation in the formidable capacity of Syria's security forces.

Monopoly on the use of force

Syria was long considered an artificial state. It enjoyed limited loyalty from its people, many of whom saw Syria as the bastion of the pan-Arab cause. Syrian politicians, thus, legitimized themselves by advocating a pan-Arab mission and Syria's sovereignty was even sacrificed in the 1958 union with Egypt in the name of pan-Arab unity. After thirty years of Ba'thist state-building, however, a Syrian identity has been constructed (albeit Arab in content) and the boundaries of the contemporary state are accepted as the normal framework of politics. All citizens are accorded formal equality, although Syria's dominant Arab identity assumes the Arabization of minorities such as the Kurds. Arabic alone is the official language. Moreover, sectarian affiliations are manipulated in the political process, with the minority Alawis often seen to benefit from favoritism.

State identity

Syria is a secular state, although provisions requiring the president to be a Muslim and designating Islamic law as a main source of legislation circumscribe the equal status of all religions. Though 90% of Syria's population is Muslim, significant religious and ethnic minorities exist. These minorities enjoy greater protections than in most other Middle East states by virtue of the Ba'th's character as, in some ways, a regime of minorities. Personal status matters remain largely governed by rules specific to the various faiths. This gives minorities considerable autonomy in such matters.

No interference of religious dogmas

Both the size and the degree of social penetration of Syria's government administration are impressive. The party and bureaucracy penetrate every village, factory and school. Nevertheless, the administrative staff lacks competence and the

Basic administration

administration as a whole functions ineffectively. The administrative apparatus is subservient to regime interests and at the same time it is frequently colonized from below by local, kin or other special interests.

2 | Political Participation

Formal competitive elections exist but play a negligible role in determining the ruling elite. The constitution grants sweeping powers to the president, whose ultimate strength derives from support by the armed and security forces. Presidential elections are referenda in which the voters endorse the single candidate who is officially chosen by the elite of the official ruling Ba'th Party; in the only instance of succession, they endorsed the deceased president's nomination of his son Bashar as his successor. A referendum approved a second seven-year term for the president in 2007. The composition of parliament is manipulated by the regime. Two-thirds of seats are reserved for candidates of the National Progressive Front (NPF), a coalition of the Ba'th and small pro-regime parties, with one half of the total number of seats going to the Ba'th Party. Independent candidates, mostly from the cities, vie for the remaining one-third of parliamentary seats. These candidates, however, are thoroughly screened by security agencies and thus become an instrument used by the regime for co-opting elements outside of the regime's state- and rural-centered power base.

Free and fair elections

President Hafiz al-Asad consolidated power in Syria after decades of instability. After his death, several competing centers of power shared governance, notably the presidency, held by Hafiz's son, Bashar, the regional command of the Ba'th party, the commanders of the armed forces and security apparatus, and the council of ministers. By 2005, Bashar al-Asad had established the presidency as the unchallenged center of authority in the regime. Power has shifted from party apparatchiki to a new group of Western-educated reforming technocrats in the presidency and cabinet. Informal power centers, such as the extended Asad and Makhoul families, wield great influence. While the government (council of ministers) is formally accountable to an elected parliament, in reality it answers to the president, the Ba'th Party and informally to mukhabarat (security police) barons.

Effective power to govern

During the Damascus Spring immediately after Bashar's accession, the government briefly tolerated a civil society movement, which met in semi-private spaces throughout the country and demanded democratization. Since then, overtly politicized assembly, including public demonstrations, have not been tolerated, although restrictions on fairly private assemblies to debate public issues within red lines have eased. The public's fear of the security police, whose powers have been reined in, has been much reduced.

Association / assembly rights

The scope of public expression has somewhat widened with more critical opinions expressed in the pro-government press. Opposition-mounted petitions that question

Freedom of expression

the current order, especially in the aftermath of Saddam Hussein's regime collapse, meet with repression. The government initially allowed private newspapers. After clashes with the government, however, the main one, Al-Domari, was shut down. Other private publications survived, including the political weekly magazine Abyad wa Aswad (White & Black) and the economic monthly Al-Iqtisad (The Economy). Both run critical, reform-oriented articles.

3 | Rule of Law

With the legislature and the judiciary dominated by the regime, there is no conventional separation of powers. This is true both in a constitutional and in a practical sense. The presidency generates the reform legislation, which the parliament routinely approves. Parliament is mainly a consultative body and cannot influence the formation of the government. This function is shared between the president and party politburo. The parliament merely responds to government legislation, normally approving it. The main roles of the deputies are to act as brokers between power holders and their constituents and as channels for rent-seeking.

Separation of powers

The judiciary is politicized by Ba'th party appointments and suffers from corruption and interminable delays in litigation. As such, it elicits little public confidence and is, rather, a major obstacle to the rule of law. It does not protect civil liberties or property rights. Redress of grievances typically rests on access to informal clientele connections. Though it has not been attempted, reform and independence of the judiciary is widely recognized as essential to Bashar's reform project.

Independent judiciary

Periodic campaigns against corruption have targeted some of the most corrupt figures only when they fall out of political favor. Others, however, enjoy impunity. It remains practically impossible to sue the government or regime representatives, a situation that contributes to deterring foreign and less well-connected domestic investors.

Prosecution of office abuse

A state of emergency, under which civil rights can be suspended, has existed since 1963, despite recent demands from the intelligentsia for its lifting. Since the 1990s, repression has been eased in various respects. A large number of political detainees, who in some cases had been held for decades without being charged with any crime, were released. Exiles could return to Syria under certain conditions. Torture has been generally less used. Human rights organizations, though illegal, are handled delicately in comparison with the past. Petitions signed by thousands of intellectuals calling for an end to the emergency law indicate that the barrier of fear has probably been permanently broken. Even as the regime releases some political prisoners, it continues to arrest other high profile opponents. Citizens who refrain from political opposition enjoy many everyday freedoms and personal security.

Civil rights

4 | Stability of Democratic Institutions

Though Syria's institutions incorporate significant constituencies and have contributed to the stabilization of the state, they are not liberal-democratic. The smooth June 2000 presidential succession engineered by the state establishment, in spite of the regime's seeming dependence on the personality of the deceased top leader, was evidence of the elite's shared stake in regime stability, and also that Syria's state structures were, to a degree, institutionalized. This was further demonstrated by the president's subsequent consolidation of power over intra-regime opposition through legal means (such as official retirements) and without violence or instability.

Performance of democratic institutions

The generation of Syria's political elite that assumed power in the 1970s had no commitment to Western style democracy. They argued that they had built an alternative popular democracy in which the ruling party acted as a channel of upward political mobility from the villages and created or co-opted syndical associations representative of various sectors of society. Under Bashar al-Asad, a new generation of elites is more receptive to the need for some political liberalization. Democratization, on the other hand, is a distant and low priority. Liberal Ba'thists argue that the Ba'thi political system is capable of initiating economic reform and that, as this advances, political liberalization will be widened.

Commitment to democratic institutions

5 | Political and Social Integration

The Ba'th party's status as the official governing party remains enshrined in the constitution despite hopes that this would be ended by a new party law suggested by the Ba'th party in 2005. The Ba'th, bridging urban-rural gaps and incorporating a cross-sectarian alliance, remains a major instrument of integration in Syria even if its capacity has declined as patronage has come to replace ideology as its main cement and as it has been increasingly marginalized by the presidency and government. The small parties in the National Progressive Front incorporate historically declining segments of non-Ba'thist political activists. Parts of the urban bourgeoisie, especially in Damascus, but much less so in other cities, are incorporated through clientele networks or parliament and business associations. The Islamist-minded traditional urban petit bourgeoisie has no formal representation. Without significant party pluralization, which would permit legalization of the Muslim Brotherhood and Kurdish parties, major political currents remain excluded from the government and in opposition to the regime.

Party system

Interest representation and aggregation outside parliament, and other regime-dominated syndical organizations such as the official trade unions, are only possible via clientele networks. However, these organizations have had some measure of

Interest groups

success in lobbying for their constituents. Most notably, the peasant union has succeeded in obtaining higher crop prices and, more recently, in protecting the rights of tenants in agrarian reforms. In general, however, these organizations are instruments of regime control rather than channels of pressure from below. They appear increasingly ineffective in defending the interests of their members in the face of attacks on populist laws and welfare rights, which have accompanied economic liberalization.

Syrians, since the rise of Hafiz al-Asad, have surrendered political liberties in return for stability. The vast majority of the generation socialized under Hafiz al-Asad's rule was not exposed to any democratic practices. Outright paternalistic and authoritarian procedures guide Syria's political culture, whether the issue in focus relates to families, schools, the workplace or public affairs. Consultation is as far as the regime will bend. Demand for democratization is concentrated among a small group of middle class intellectuals and a minority of the private bourgeoisie. The democracy movement, such as it was, could not break the regime's hold on the masses and thus failed to mobilize broad support. While some democracy activists initially welcomed the collapse of Saddam Hussein's regime as an occasion to demand political reform in Syria, the subsequent chaos in Iraq enabled the regime to legitimize authoritarian order. Similarly, the continuing struggle over Palestine and the Golan Heights legitimizes the persistence of a national security state.

Consent to
democratic norms

Non-political cooperatives, charities and the pooling of resources by extended families are well-developed in Syria. The Ba'th by no means atomized society, even if they did succeed in de-politicizing it. Economic pressures reinforce vertical divides in society, with individuals falling back on their families, wider kin groups and religious charities. The Bashar regime, seeking to revive civil society voluntarism, has encouraged officially aligned NGOs, such as the Syrian Young Entrepreneurs, rural development groups and women's charities.

Associational
activities

II. Market Economy

6 | Level of Socioeconomic Development

Socioeconomic inequality has steadily increased, with gaps widening primarily between haves and have-nots, but also between the wage earners in the private and public sectors. The failure of official salaries to keep up with inflation impoverished the salaried middle class during the 1980s. Since 2000, several salary increases have brought wages to a level comparable to other countries in the region. Public sector

Socioeconomic
barriers

salaries, however, are still between 40% and 45% lower than those in the private sector. Although they enjoy better job security and retirement schemes, public sector workers normally must work multiple jobs to make ends meet. The 1990s economic liberalization enriched a new business class, but their failure to invest in significant job-creating enterprises combined with the regime's attempt to create a favorable investment climate severely limited trickle-down effects. Fifty-six percent of people in poverty work in agriculture and construction. Agriculture has enjoyed support prices, and subsidization of basic consumption commodities such as bread provides a safety net of sorts. In 2008, however, the government raised the prices of various petrol products, effectively cancelling the subsidies for benzene and scaling them back for heating oil. Deteriorating public education and health services and the negative impact of public sector shrinkage on female labor participation work against social inclusion and equality. A 2005 UNDP study found that 30% of Syrians live below the official poverty line. Unemployment is estimated at close to 18%. Syria's earlier socioeconomic reforms, however, produced growth and resulting in rising scores on the Human Development Index (HDI), improving from 0.580 in 1980 to 0.634 in 1990, 0.665 in 1995 and 0.691 in 2000. Despite this progress, Syria still ranked 105th out of 179 countries in the updated 2008 edition with an HDI value of 0.736. Life expectancy is about 70 years and the literacy rate is 76%.

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	24474.7	28202.7	33406.6	40548.7
Growth of GDP	%	5.8	4.5	5.1	4.2
Inflation (CPI)	%	4.4	7.2	10.0	3.9
Unemployment	%	-	-	-	8.4
Foreign direct investment	% of GDP	1.1	1.8	1.8	-
Export growth	%	23.9	-1.5	40.8	2.5
Import growth	%	40.2	26.0	0.2	8.4
Current account balance	\$ mn.	591.5	299.0	919.8	-
Public debt	\$ mn.	-	-	-	-
External debt	\$ mn.	-	-	-	-
Total debt service	% of GNI	-	-	-	-

		2004	2005	2006	2007
Cash surplus or deficit	% of GDP	-	-	-	-
Tax Revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	15.7	13.9	12.8	10.8
Public expnd. on edu.	% of GDP	-	-	-	-
Public expnd. on health	% of GDP	2.2	2.1	1.9	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	5.6	5.1	4.4	4.1

Sources: The World Bank, World Development Indicators 2009 | UNESCO Institute for Statistics | International Labour Organization, Key Indicators of the Labour Market Database | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security.

7 | Organization of the Market and Competition

Since 2000, the regime has attempted a systematic transition to a market economy. The role of the state in the economy, however, remains substantial. The public sector has remained the main source of public revenue and acts as the country's principle economic stimulator via its investment budget. The three key productive sectors of the economy, agriculture, energy and industry, continue to be state-dominated. Agriculture, which is partly state subsidized and controlled, directly generates 30% of GDP and almost half of Syria's export earnings. The declining hydrocarbon sector makes up the other half of Syria's exports and around one-fifth of GDP. The public sector share of GDP has consistently fallen proportional to the private sector; whereas the public sector constituted 50-60% of industrial GDP in the 1970s, its share declined to less than 40% as private industries boomed in the 1990s. Because the public sector also supplies contracts and intermediate goods at low cost to the private sector, their relation is symbiotic, not adversarial. The private sector has rapidly boomed in such tertiary sectors as trade, housing, construction and tourism. A large informal underground economy also operates. Institutional reforms aiming at strengthening competition, good governance, property rights and the rule of law have been initiated, but their implementation has been uneven and incremental. Under the 2006 Index of Economic Freedom, Syria was still rated 145 out of 157 countries; but reflective of Syria's incremental deepening of marketization, its ranking jumped to 91 in 2008. In 2004, the State Planning Commission announced that Syria will adopt the principles of a market economy by 2010.

Market-based
competition

Although formal anti-monopoly legislation has been passed, the president has refrained from directly challenging crony capitalists in his own family. He seems ready to tolerate the creation of a dominant business class from within the regime in the hope that he can then use international economic agreements to force the members of this class to become competitive capitalists. In the meantime, the predatory practices of crony capitalists, including the monopolization of rent opportunities, state contracts and privatization by means of intimidation and extortion, remain major disincentives to the private investment. In turn, this lack of private investment jeopardizes Syria's overall reform project.

Anti-monopoly
policy

Since 1963, Syria's economy has been primarily inward looking, with production aimed at the domestic market. The 1986 foreign exchange crisis led to prioritization of industrial exports, which, however, declined with the loss of soft Eastern bloc markets after 1990. Syria then reoriented its predominantly oil-based trade toward the European Union. Since 2000, Syria has undertaken a process to liberalize its restrictive foreign trade regime in order, primarily, to become a member of the Euro-Mediterranean Association Agreement (until today, the agreement, not least due to Dutch and British opposition, has not been concluded). To comply with the Euro-Mediterranean Association's requirement that Syria open its economy completely within 12 years, the Syrian government reduced the number of prohibited goods, streamlined, customs procedures, and simplified and lowered import duties (by 2006 the maximum tariff rate had fallen from 255 to 65% and the average rate from 20 to 14.5%). Syria signed free trade agreements with several countries, including Turkey, which has become a major trading partner. Syria also joined the Greater Arab Free Trade Area, which foreign investors, sometimes in joint ventures with Syrian businessmen, used to export goods to the Arab world. Liberalized imports have, however, hurt small private businesses and are likely to threaten the already non-competitive public sector.

Liberalization of
foreign trade

The exclusively state-owned banking system failed to perform its function of mobilizing savings and channeling it into investment. Subsidized credit went chiefly to agriculture and public sector industry where loans often could not be recovered; a top priority of reformers is now to reform these banks and end their losses. Small and medium-sized private enterprises received a minute fraction of state bank credit. Unlicensed currency exchange dealers finance 80% of private sector imports. In 2004, as a centerpiece of its marketization strategy, the government legalized private banks and insurance companies. Islamic banks were founded to mobilize savings that hitherto remained outside of the formal banking sector. Foreign exchange bureaus were legalized. By 2007, 10 private banks were mobilizing business deposits and had increased private sector access to credit; however, their limited experience making informed lending decisions made credit expansion risky. In the end, private banks lent out only 17% of their total deposits. They may have been more effective in exporting capital or facilitating trade

Banking system

operations than in funding Syrian investment. To oversee the new banking sector, the government established a regulatory framework under the authority of the Central Monitoring Committee, which, although dominated by ministers, is somewhat insulated from politics. Poor accounting, however, impairs its ability to provide adequate supervision. The idea of a stock market initially faced ideological opposition from the Ba'th party, but, indicative of the new climate of opinion, a stock market law passed parliament and a Securities and Financial Markets Authority was established to implement it.

8 | Currency and Price Stability

Rising international prices for Syria's oil exports from mid-1999 helped maintain financial stability. Inflation remained subdued up to 2005 when the influx of Iraqis increased the cost of housing and food and reductions of subsidies on fuel and cement set off a domino effect in production and transportation costs. As a result, the consumer price inflation rate rose to more than 7% in 2005. The Syrian lira has remained stable. The 14 separate exchange rates of the 1980s were reduced to a handful. Foreign exchange liberalization ended a requirement that a portion of export earnings of foreign exchange be sold to the central bank at official rates while private sector importers of raw material and intermediate goods were given access to the official foreign exchange market. In 2003, an old law criminalizing foreign currency exchanges other than with government banks was revoked.

Anti-inflation /
forex policy

Macroeconomic stability has been maintained albeit with some fluctuations. In the 1970s, the regime pursued a policy of inflationary financing of economic development with deleterious consequences for price stability. This policy was countered by a highly deflationary policy in the 1980s. From the second half of the 1990s, Keynesian counter cyclical expansionary policies were given priority over previous budgetary discipline. In 2003, the non-oil budget deficit reached 18% of GDP. Domestic public debt was kept at relatively moderate levels. After substantial balance of payments surpluses in the early 2000s (\$2.2 billion in 2002), the decline of oil revenues, a decrease in remittances by expatriate Syrian workers in Lebanon and trade liberalization led to deficits of \$1.6 billion in 2004 and \$2.3 billion in 2008. Foreign debt remains manageable. Syria eschewed borrowing from Western lenders and the IMF and negotiated debt settlements with East European countries and Russia entailing up to 90% forgiveness. Debt as a percentage of GDP, around 20% into the 1990s, began to increase by 2005 from \$4 billion to \$6.5 billion. However, net foreign assets stood at \$18 billion in 2004. Thus, in the short term, Syria is largely living within its means.

Macrostability

9 | Private Property

The constitution allows for public, private, cooperative and mixed sectors. The days of outright nationalization or sequestration of property are long gone. Under Bashar, property rights have been legally consolidated by laws on commercial arbitration, foreign direct investment, and the protection of commercial and industrial ownership, as well as those against monopolies and establishing a corporation code. The 2005 legislative decree abolishing economic security courts, which had been in operation since 1977, removed one of the main threats to property rights. The other principle threats stem from the predatory practices of regime-connected crony capitalists. Investors have a right of appeal local court decisions to the Arab Investment Court or other international jurisdictions.

Property rights

Syria has a large, if fragmented, private sector that accounts for more than 60% of GDP. Since the 1990s, private companies have been permitted in virtually all fields, although they still require non-transparent official approval. Capital can be repatriated. Foreign banks can wholly finance projects. Labor laws have been relaxed. The regime is adamant that the public industrial sector will not be privatized, at least not until the private sector is robust enough to absorb job seekers and those who would be displaced. In 2002, the private sector employed 296,000 people out of an estimated 4.8 million employed. As an alternative to total privatization, the regime is experimenting with contracting the management of public sector firms to private firms.

Private enterprise

10 | Welfare Regime

Basic health care exists for the majority of the population. State education is free. Declines in government spending, however, have lessened the efficacy of these services. Prices of certain basic foods, notably bread, remain fixed. A Syrian agency for combating unemployment was set up to provide credit to small businesses or development projects. Government's wage and employment policies in recent years have been aimed at correcting the erosion in wages during the early 1990s. In the medium term, the erosion of the state's fiscal position from the depletion of oil revenues calls in question the ability of the regime to supplement the market economy with social safety nets.

Social safety nets

The social leveling carried out by the Ba'athist so-called revolution from above resulted in a significant redistribution of agrarian property, more widespread education, increases in public employment for the lower social strata and the establishment of welfare entitlements, including labor rights and subsidized food. The middle class benefited from rent control and public housing. While the revolution broke down formerly rigid class divisions, which led to substantial social

Equal opportunity

mobility, a new set of inequalities crystallized around access to state resources. These resources were unequally distributed according to political (and to a degree sectarian) affiliation. This growth of corruption allowed state elites to enrich themselves while, as inflation mounted, the publicly-employed middle class found their livelihoods under attack. The standard of living in the villages, however, has risen substantially over the decades. The erosion of public health care owing to decreases in funding has pushed those able to pay towards private medical care administered both inside and outside the country. Similarly, state education is complemented with private lessons; the wealthier prefer foreign universities to local ones and recently four private universities have been opened for the children of the elite. Those unable to pay suffer in terms of health, life expectancy and formal education.

11 | Economic Performance

The World Bank categorizes Syria as a middle-income country with a per capita of around \$1,200. Syria has experienced boom and bust for three decades parallel with fluctuations in oil prices and crop weather. By the mid-1980s, as the exhausted public sector became loss-making and capital flight far exceeded miniscule FDI, Syria's labor and firm productivity levels and savings rate plummeted. In the half decade (1990-95) following Syria's receipt of rent for its stand in the Gulf war and the influx of investment stimulated by its 1991 liberalization of investment laws, the economy grew 7% per year and GDP per capita increased 4.3% annually. When these inflows were exhausted, in part because of the lack of follow-up economic liberalization measures, economic growth fell to an average of 1.25% per year from 1999 to 2003. During this time, petroleum revenues, worker remittances and informal transfers to families from the holdings of Syrians abroad largely propped up the economy and allowed the government to sustain savings (26% GDP) and investment (22%) at a reasonable level. Average growth of GDP was 3% between 2000 and 2006. From 2004 onwards, growth recovered, reaching 5.1% in 2006 and 6.2% in 2007, benefiting from private exports, investment due to excess liquidity in the Gulf region, the implementation of GAFTA and Syria's overall improved business climate. Since the 1980s, however, GDP per capita (PPP in current U.S. dollars) has stagnated as average economic growth has barely kept up with population growth. These official rates may understate real economic levels since they exclude or undercount the enormous informal and hidden economy.

Output strength

12 | Sustainability

Environmental considerations have been largely absent from economic planning. The expansion of population and agriculture has led to soil and water deterioration. Syria also faces water shortages. The government has formed a new environment agency, which indicates some growth in environmental consciousness.

Environmental policy

Syria ranks 87th out of 88 countries in technological sophistication of exports and 75th out of 88 in industrial competitiveness. R&D spending accounts for 2% of GDP. Government funds for education have been declining. By 2007, however, eight private universities had joined the four main public universities and enroll a total of 380,000 students.

Education policy /
R&D

Transformation Management

I. Level of Difficulty

Syria suffers from no insurmountable structural liabilities and in many ways has a balanced distribution of resources. The main constraints are a function of policy dead-ends. Syria suffers from the exhaustion of its public sector and unemployment in an economy that cannot create the requisite number of jobs. In addition, the current decline and looming exhaustion of Syria's oil revenues, which in lieu of an adequate tax base have funded investment and rewarded regime insiders, pose a threat to the population's basic economic security. There is a chance that oil reserves might be exhausted before economic reforms have been able to generate new sources of growth and state income. The influx of Iraqi refugees has boosted domestic demand and increased pressure on already-constrained public services and housing.

Structural
constraints

Formal civil society is controlled by the regime through a network of syndical organizations under regime leadership. At the same time, an informal civil society comprised of neighborhood, friendship and patronage networks is strong. The regime sharply restrains the development of more formal and autonomous civil society organizations. Civil society is faced with very restrictive and arbitrary legal provisions.

Civil society
traditions

On the one hand, Syria's diverse society makes it potentially vulnerable to communal strife. On the other hand, a shared Syrian identity, a long history of tolerance and the cross-sectarian coalition incorporated into the regime have, since the Islamic uprisings of the late 1970s and early 1980s, contained and eased communal cleavages. There remains little trust across these social divides and intermarriage remains the exception. At the top of the social pyramid, however, partnerships between Alawi political insiders and Sunni or Christian business people have eased the sharp cleavages of the 1960s. Sunni Kurdish riots in the northwest Kurdish areas, an Alawi-Ismaili clash in the regime's northwest heartland and clashes between Druze and Bedouin populations in the south suggest communal tensions, though contained, have revived to an extent.

Conflict intensity

II. Management Performance

14 | Steering Capability

Over the long term, the regime has displayed a high level of consistency in pursuit of goals that centered on regime survival and the struggle with Israel. Economic management, however, has long been a second priority. Beginning in the 1980s, the regime has proven able to steer incremental liberalization, which has allowed it to tap increased resources and to foster new private sector constituencies without conceding political power or wholly abandoning its initial popular constituents. After Bashar as-Asad's accession to power, the government's previous piecemeal reform became systematic. Ba'thist ideology no longer governed economic policy, though Bashar's project can still be understood as modernizing authoritarianism. Initially, the reforming president had to share policy-making with other power centers, such as the Ba'th party, which were less convinced of the need for change and which could veto his initiatives. Over time, the presidency became a center of reform initiatives and Bashar was able to appoint Western educated reformist technocrats to key economic ministries, such as foreign trade, industry, telecommunications and higher education, though he at first proved unable to protect some of his protégés when they challenged vested interests. Within three years of succession, a renovation of the political elite with a turnover of 60% in top offices had transferred power to a new generation. Bashar consolidated his power at the 2005 Ba'th party congress and in 2007 was inaugurated for a second seven-year term as president of Syria. Those who feared in 2000 that he was not suited for the job appear to have been proved wrong.

Prioritization

A multitude of laws have been promulgated to create the framework for a market economy, but many have gone wholly or partially unimplemented. The elimination of the main opposing centers of power did not eliminate either the inertia and hostility of the bureaucracy that must carry out the reform or the vested and corrupt interests that pervert it for their own ends. Productivity by the overstuffed and under-qualified politically appointed bureaucracy is very low. Budgeting is not transparent. A weakness in data impedes the ability to monitor the impact of reforms and the capability of conducting macroeconomic management. According to the president, the major constraint on reform implementation is the absence of efficient, trained cadres with technical expertise. He has therefore given priority to educational reform and to recruiting a critical mass of qualified people into his administration. International advisors are leading reforms in the financial

Implementation

administration and judiciary, crucial sectors for economic management and the rule of law. The Ba’th party is supposed to withdraw from day-to-day interference in state administration and economic matters.

The leadership has displayed considerable capacity to adapt to constant environmental pressures. Syria is reforming on its own initiative, aware that long-term threats – demographic growth, the decline of the oil economy – make the current economic system unsustainable. The regime lacks an elaborate blueprint to substitute for Ba’thism yet has been loath to wholly embrace neoliberalism. In this context, reform proceeds by trial and error. The president sees reform as a gradual process, acutely aware of the risks of going too fast and thereby provoking enemies, making mistakes and risking stability.

Policy learning

15 | Resource Efficiency

Syria does not effectively employ its resources and as a result there is much waste. The regime, however, is attempting to improve its administrative capabilities. A main test of this (and of its ability to make the transition from dependence on oil-funded state-dominated development) is its ability to develop a tax base. Continued access to rent incomes made tax extraction a low priority, and Syria’s 10% tax-to-GDP ratio was extremely low. Businesses mostly evade taxes, placing the burden on the public sector and state employees. To address this problem, income tax rates for the highest earners were slashed and penalties for evasion increased. Tax exemptions offered under investment law No. 10 of 1991 were ended, but the top corporate tax rate was reduced from 65 to 35%. Though collection rates have improved, Syria’s weak administrative capacity, corruption and opaque and false accounting practices in business continue to obstruct the widening of the tax base.

Efficient use of assets

The State Planning Commission’s development plan sets targets and measures, but bureaucratic rivalries at the top obstruct policy coordination. In addition, contradictions from the addition of a multitude of new laws to those already on the books impede implementation.

Policy coordination

Corruption is systemic in Syria. Although Bashar embarked on an anti-corruption campaign in the waning years of his father’s presidency, corruption has not lessened. Indeed, given the absence of accountability to a strong president and the increasing overlap of the state and private sectors, it may have increased. At least the outright theft of public firms, like what happened in Eastern Europe, has been avoided. Bashar has made no direct assault on the new class of crony capitalists whose corrupt stranglehold on the economy deters productive investment.

Anti-corruption policy

16 | Consensus-Building

There is a consensus that private capital investment is the only solution to the exhaustion of Syria's statist economy. According to the 2005 Ba'th Party conference, however, this transition is to take place within a "social market" economy, a vague formula that allows for considerable disagreement over pace, extent and details, particularly with regard to sensitive matters, such as subsidies and the reform of public enterprises. Moreover, public support for the transition to a market economy is contingent on containment of its socially deleterious effects. The state's legitimacy rests on its ability to provide economic security and ensure basic welfare. The Chinese model, a dual track approach in which the existing state-dominated system is maintained while the market is introduced alongside it, has been adopted by most groups as a way of avoiding social disruption.

Consensus on goals

The main obstacle to democratization in Syria is the inability to arrange a pact between reformers in the regime and moderates in the opposition. The minority Alawi elites that dominate the regime will not risk democratization as long as they believe sectarian voting (as in Iraq) would drive them from power and opposition forces would seek revenge. The so-called Damascus Spring failed because the opposition played into the hands of regime hard-liners by crossing red-lines and threatening national unity with sectarian conflict. The reformers denounced the "path of the late leader Hafiz al-Asad," were seen as ready to collaborate with foreign forces, and openly attacked the corruption of powerful elite insiders. More radical elements of the opposition framed the conflict in such zero-sum terms. Bashar, relying on the organizational base of the regime, could not repudiate his father's heritage. Syria does have, relatively speaking, a secular consensus and an educated population, but despite this the regime considers a concerted move toward democratization to be premature. Before democratization can take place, according to the regime, the transition to the market economy must have produced results and security threats, much enhanced by Western pressures on Syria, need to be relieved. Even the reformers do not seek democratization since many liberal reforms would be blocked if the masses were empowered by the vote. The opposition is deeply divided along secular-religious, inside-outside, hardline-moderate lines. Moderate members of the opposition among intellectuals and businessmen want gradual political reform but have very limited constituencies. The Muslim Brotherhood has the best potential to mobilize mass support but is mistrusted by many for the violence of the rebellion it led in the 1980s. Since the Muslim Brotherhood was brutally repressed, its supporters jailed and its leaders exiled, Syria has appeared relatively immune to the power of political Islam. The exiled Brotherhood has moderated its ideology, calling for democracy in concert with the secular opposition; the regime still fears its violence and popular sectarian appeal. While individual Muslim brothers have been allowed back from exile or out of prison, the

Anti-democratic
veto actors

organization remains outlawed. The regime has allowed a non-political Sufi-liberal Islamic establishment to set up charities and educational foundations. The regime hopes this establishment can offer an alternative to political Islam. The fact that Islamic piety is spreading, however, means that this establishment could in fact help mobilize political Islam.

Bashar's style is not to wield power in a ruthless way but to govern by consensus. His consolidation of power narrowed the innermost power base of the regime, excluding Sunni old guard elites such as the former vice president and some intelligence barons. On the other hand, Bashar promoted members of a new younger generation, who were personally loyal to him, and co-opted other groups from the private sector. The regime's capacity for repression and co-optation is sufficient to contain centrifugal forces.

Cleavage /
conflict
management

Bashar has sought to encourage volunteerism. Over twenty NGOs have been recently formed, many of them charities that include on their advisory boards one or two members with clear government connections. New think tanks and associations such as the Syrian-European business center and the Syrian Young Entrepreneurs Association have assumed a role in debating development policy.

Civil society
participation

The main problems with regard to reconciliation involve Islamists and Kurds. In 2004, Syria experienced major unrest in the Kurdish populated areas of eastern Syria. This unrest was, in part, encouraged by the autonomy enjoyed by Iraqi Kurds and followed the fraying of the regime's alliances with Iraq's Kurdish parties, which had long enabled it to demobilize Syrian Kurds. The major source of Kurdish disaffection has been the denial of citizenship rights to some 100,000 Kurds who were settled in Syria under the French mandate. Although the security forces repressed the disturbances, jailing many Kurds, the president is widely thought to have mitigated the severity of the regime's response and has promised to consider Kurdish grievances – arguably an improvement on previous silence on the matter. Democratization cannot proceed without reconciliation between the regime and the Muslim Brotherhood. Although small steps have been taken in this direction, the regime does not feel the need to proceed further.

Reconciliation

17 | International Cooperation

Syria is often seen as unwilling, on nationalist grounds, to embrace international advice as a total package and instead to tailor policies to fit its own national interests in the face of a homogenizing globalization. Nevertheless, Syria is now more open to cooperation over internal reform than at any time since 1963. Bashar embraced first the Euro-Mediterranean Partnership and then the Union of the Mediterranean in order to reduce domestic opposition to reform. The European Union has funded institutions and advisory missions that have helped generate the technical capacity to enable reform to advance. Technical negotiations over the EU-

Effective use of
support

Syria Euro-Mediterranean Association Agreement were concluded in fall 2004, but this agreement has not been ratified yet.

Syria seeks good relations with the West but has been unwilling to submit to Western efforts to make this contingent on its abandonment of an Arab nationalist role. This role has brought it into conflict with the United States over Syria's opposition of the invasion of Iraq and its support for Palestinian militants. These actions led to U.S. economic sanctions, under the so-called Syria Accountability Act, designed to isolate the country. Syrian relations with the European Union soured over Syria's purported role in the assassination of former Lebanese Prime Minister Rafiq Hariri. This led the European Union to put Syrian membership in the Euro-Mediterranean Partnership (EMP) on hold. The president's domestic legitimacy has been enhanced by his stand against what Syrians see as Western imperialism and double standards that favor Israel. The climate for domestic reform has also been damaged by U.S. efforts to make Syria a pariah state. In response, Syria has systematically diversified its economic and political ties toward Russia and Asia. Damascus points to the contribution it can make to regional security if its legitimate interests are recognized. Its keenness to normalize relations can be seen in its continued desire to join the EMP and its involvement in Turkish-sponsored indirect peace talks with Israel. By 2009, most Western states had come to realize it is better to engage with than isolate Syria.

Credibility

Regional cooperation and Syria's regional relations have been caught up in a broad struggle for the Middle East between the United States and its so-called "moderate" allies and "nationalist" forces including the Syrian-Iranian alliance and radical trans-state actors such as Hezbollah and Hamas. The main battlegrounds are Iraq, Palestine and Lebanon. In Lebanon, Syria was blamed for the assassination of former Prime Minister Rafiq Hariri, a client of both France and Saudi Arabia. The assassination cost Syria its good relations with these important powers and mobilized Lebanese and international pressure to compel Syria's withdrawal from Lebanon. The international inquiry into the Hariri murder remains a sword hanging over Bashar al-Asad's head. In the struggle for Lebanon, the Sunni-Christian March 14 coalition backed by Saudi Arabia, the United States and France formed against a Hezbollah-led counter-coalition backed by Syria and Iran. In 2008, Hezbollah fighters turned the tables on a challenge by the pro-U.S.-Saudi Arabia governing coalition by sweeping into government fiefdoms in West Beirut and transforming the balance of power on the ground. This action broke the deadlock between the two sides and paved the way for a Qatar-brokered election of a new neutral Christian president, army chief Michel Suleiman. A national unity government was formed in which the Shi'i opposition had a veto, ensuring that all major decisions would be taken by consensus. This essentially restored the practice of consociational democracy against the attempt of the U.S.-backed government to use its temporary majority to challenge Shi'i and Syrian interests in the country.

Regional
cooperation

Syria also suffered an Israel air attack approved by the United States on what some charged was a nuclear facility. At the same time, it was engaged in exploratory peace talks with Israel under Turkish auspices, another move that obstructed Washington's plans to isolate it. The terms of a Syrian-Israel peace settlement – return of the full Golan in exchange for normalization of relations – was established in the 1990s Syria-Israeli negotiations, but peace was frustrated by Israel's unwillingness to fully return to the 1967 lines. Negotiations have since been complicated by Israel's conditioning of a deal on Syria cutting its relations with Iran, Hezbollah and Hamas.

Events in Lebanon precipitated a realization by some in the West that Syria could not readily be isolated and that it can be a force for stability if its interests are recognized and for instability if they are not. The first immediate payoff for Syria was the high-profile invitation by France to President Bashar al-Asad to attend the Paris European-Mediterranean summit. The United States under President Barack Obama now hopes to use the promise of a return of the Golan Heights to break Syria's alliance with Iran.

Turkish-Syrian relations have turned on the issues of Euphrates water and the Kurds. Under Hafiz, Syria tried to use support for the Kurdish PKK to pressure Turkey to concede it a greater share of water controlled by new Turkish upstream dams. Turkey's military threats brought Syria to abandon this strategy and thereafter relations warmed. The empowerment of Kurds in Iraq after the U.S.-Iraq wars of 1991 and 2003 gradually drew Turkey and Syria together over the shared threat of Kurdish separatism.

Strategic Outlook

Syria's main challenge is to adopt reforms that will stimulate the investment and growth needed to cope with dwindling oil revenues and burgeoning unemployment. Buffered by accumulated foreign reserves and buoyed by inward investment accompanying the oil boom, reformers proceeded cautiously but consistently toward marketization of the economy. They should and will continue this. There is no guarantee, however, that the reform agenda itself will translate into higher (foreign) investment, growth and employment. The aim of attracting \$34 billion in investments in the period from 2006 to 2010 is highly optimistic, considering present investment levels, political uncertainties in the Middle East and the wider domestic political and institutional setting. More substantial economic liberalization, in particular reforms of the public sector and further deregulation, would challenge present crony capitalist arrangements and could result in social unrest. Syria appears to have survived the effort of the United States to make it a pariah state. Re-engagement with the West is clearly essential to the success of domestic reform. Mending relations with Egypt and Saudi Arabia should be a top priority. The regime missed the opportunity to capitalize on the nationalist legitimacy it won by standing against the United States and Israel to broaden its base by co-opting the loyal opposition. With the collapse of oil prices and inward investment owing to the global financial crisis and the draw down in oil revenues and foreign reserves, Syria faces hard times. Now that external threats are lessening, broadening inclusion in the ruling coalition would be less risky. Political and institutional reform would enhance the legitimacy of the regime. Likewise, an independent judiciary able to ensure security of contract and property would greatly enhance prospects for investment. Party pluralization and greater political competition would widen inclusion and could coexist with stability if Syria adopted measures similar to Turkey's National Security Council. Such reforms would likely be greatly facilitated if a peace agreement were reached with Israel, which would accelerate inward investment and economic reforms and allow for a gradual reduction of the bloated national security apparatus. If (and only if) accompanied by a parallel settlement of the Palestinian issue, peace would endow the regime with a legitimacy windfall that it could invest in political liberalization and even democratization.