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CHANGE WITHIN STABILITY:
THE POLITICS OF FINANCIAL SECTOR REFORM IN SYRIA

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I. Introduction

Syria opened the Damascus Securities Exchange (DSE) for business on March 11, 2009, in the midst of a global economic depression and to much international media attention.¹ No mere window dressing, the DSE is a manifestation of a broader trend of financial liberalization begun in 2001 after Bashar al-Assad took power. In 2001, the regime officially legalized private banking and, three years later, the first three private banks opened. In 2002, the regime established the Credit and Monetary Council, a theoretically independent body responsible for creating and implementing monetary policy. In 2005, private Islamic banks were legalized and the Syrian Stocks and Financial Markets Authority was created to oversee the Damascus Securities Exchange, which opened four years later. In addition to these laws, a series of legislative decrees established International Accounting Standards (IAS) as official practice for public and private banking systems, anti-money laundering standards, and established bank secrecy laws for private bank account holders.

This recent sequence of reforms has been heralded as a step towards a newly dynamic and diversified Syrian economy. But the market-oriented scope of these reforms seems to be a substantive break with Syria's recent economic history. The wave of drastic nationalizations in the late 1950s and early 1960s, and the subsequent rise of Ba'athism, set Syria on a course towards a state-directed economy. Subsequent decades of consolidation

¹ For example, see: Reed Rafael, "Syria launches stock exchange," *Los Angeles Times*, March 11, 2009; "Syrian stock exchange set for launch," *BBC News*, March 10, 2009.

of the state's control over the economy entrenched a system hostile to Syria's traditional private sector. Thus, reading the regime's recent economic initiatives as straightforward liberalization fails to take into account the institutional legacy of state intervention in the Syrian economy.

In many respects, the regulations and legislation governing private sector finance in Syria are consistent with liberal economic doctrine, and geared towards the development of a robust domestic financial sector. For example, the legalization of private banks and private currency exchange has given the private sector a larger role in generating new capital and directing investment. However, other regulations seemed designed to impede these same activities, ceilings on foreign ownership and a tax system that remains hostile to foreign investors. The cumulative effect of Syria's contradictory financial reforms is a regulatory structure that presents an incoherent economic logic.

But why is the regime implementing these reforms now? The space in which banking, currency trading and investment can take place is delineated and constrained by an overriding political calculation that governs the regime's relationship with society. One particularly persuasive conceptualization of the relationship between regime and society in Syria paints it as a "tacit pact" between unequal parties, with the regime (the stronger party) responsible for securing material well-being for society (the weaker party). The regime can provide material inducements by providing opportunities for citizens to make money and/or insuring levels of national economic growth that allow for the continued provision of state welfare programs such as high public sector employment and subsidies for fuel and food. At the same time, the regime wields a constant threat of exclusion from

those material benefits in the case of political noncompliance.² Specifically, the state crafts regulations that allow for quasi-legal punishments of economic behavior in order to punish unacceptable political behavior. Balancing the tacit pact is necessary for regime survival. Thus, rather than following prescribed economic doctrine, the timing and scope of financial reform in Syria are determined by the political necessities of the tacit pact.

So what is the future of financial and economic liberalization in Syria? To what extent might these reforms be undermining or augmenting the political stability of the regime? Interestingly, structural economic shifts have both constrained the regime's ability to exert itself as well as created new pathways for the regime to maintain its hold on power. Consequently, the future of economic liberalization in Syria will differ widely from the kind of economic liberalization that international financial institutions might recommend. As Syria continues to manage economic reform strictly in terms of the political payoffs, the regime's future will remain stable, and the prospect of subsequent political liberalization low.

II. Structural Economic Shifts and Regime Responses

A. Factors Undermining the Old Tacit Pact

Observers of Syrian economic reform have prioritized a number of reasons for Syria's new economic direction, some rooted in international events and others in changing domestic conditions. Most prominent in discussions of the shifting international economic

² Annette Büchs, "The Resilience of Authoritarian Rule in Syria under Hafez and Bashar Al-Asad," *GIGA Working Paper No. 97*, German Institute of Global and Area Studies, March 2009: p. 8. Available at: http://www.giga-hamburg.de/dl/download.php?d=/content/publikationen/pdf/wp97_buechs.pdf. Büchs bases her conception of the "tacit pact" on Nazih Ayubi's "tacit political pact."

climate is the assassination of Rafiq Hariri and Syria's subsequent withdrawal from Lebanon, Syria's main financial hub prior to 2005. Although three private banks were already operating in Syria when the Syrian army withdrew from Lebanon in 2005, much of Syria's private and commercial banking deposits were still held in Beirut. After the Hariri assassination and the subsequent popular movement in Lebanon pushing for Syrian withdrawal from Lebanese territory, the Syrian regime was under intense international scrutiny. Given the depth of financial transactions conducted in Lebanon that were compromised after 2005, the regime realized a more robust domestic financial sector would prevent such an economic disruption in the event of future shifts in the political winds.³

A second explanation is that anti-money laundering sanctions placed on Syria's Commercial Bank by the United States in 2006 drove Syria to develop alternative financial institutions in order to maintain access to the international financial system. In 2004, the U.S. Treasury Department, using its authority under the USA Patriot Act, labeled the Commercial Bank of Syria a "primary money laundering concern" and invoked sanctions.⁴ These sanctions, as one U.S. diplomat argued, created the impetus for Syrian financial liberalization.⁵ Prior to the sanctions, the Commercial Bank of Syria acted as the largest holder of deposits as well as foreign exchange reserves (a function normally reserved for independent central banks). Under American sanctions, however, currency exchange was

³ Zeina Karam, "Syrian economy opens-will its politics follow?" *Associated Press*, September 8, 2008; Andrew Tabler, "The High Road to Damascus: Engage Syria's Private Sector," *Stanley Foundation*, Policy Analysis Brief, August 2007; Interview with U.S. diplomat, Damascus, Syria, March 19, 2009; Interview with private bank executive, Damascus, Syria, March 23, 2009.

⁴ US Treasury Department, "Treasury Designates Commercial Bank of Syria as Financial Institution of Primary Money Laundering Concern," May 11, 2004. <http://www.treas.gov/press/releases/js1538.htm>.

⁵ Interview with U.S. diplomat, Damascus, March 19, 2009.

essentially halted, as any transactions by the Commercial Bank of Syria were isolated from most of the international banking system. In order to maneuver around the sanctions and allow for business to continue as usual, the Syrian regime loosened its regulatory hold on private banking.

Finally, others point to the worldwide balance-of-payments crisis in the late 1980s that drove the Ba`ath party to agree in principle to allow private sector access to banking, making further financial reform at some point inevitable.⁶ In the mid-1980s, the price of oil collapsed and states—like Syria—that relied on oil revenue to fund their budgets faced severe deficits. Moreover, Syria’s budget had also benefited from foreign aid flows from larger, richer oil producing states as well as remittances from Syrian laborers working in those oil-producing states. After the price of oil collapsed, however, aid flows and remittances temporarily dried up, further exacerbating Syria’s budget crisis. The ensuing economic crisis pushed the Syrian regime to construct alternative sources of economic growth that could make up for the lost oil revenues, foreign aid and remittances, including the first intimations of a more liberalized economy.⁷ Specifically, the regime passed laws requiring state-owned companies to generate their own currency reserves (in effect, requiring them to enter and compete in the private sector) and allowing Syrian firms greater flexibility to import certain raw materials.⁸ Although, owing to substantial new discoveries, Syrian oil production skyrocketed throughout the 1990s and alternatives to

⁶ David Lesch, “Is Syria Ready for Peace?: Obstacles to Integration in the Global Economy,” *Middle East Policy* 6 (3): February 1999.

⁷ Bassam Haddad, *The Economic Price of Regime Security: Mistrust, State-Business Networks and Economic Stagnation in Syria, 1986-2000*, Unpublished Ph.D. dissertation, Georgetown University, 2002, p. 391.

⁸ *Ibid.*

rent income were no longer deemed politically necessary, the initial policy shifts undertaken in the late 1980s certainly set the tone for future economic liberalization in Syria.⁹

Changing domestic economic factors were also instrumental to the enactment of specific liberal financial policies. In recent years, oil production has dwindled to pre-1990 levels with few new oilfields being developed and, in 2007, Syria became a net importer of oil for the first time in 30 years.¹⁰ Syria also signed the Greater Arab Free Trade Agreement and a free trade agreement with Turkey, which has reduced customs revenues.¹¹ Taxes have been, at best, an irregular source of state revenue, and the budget boasts a growing deficit, as it remains burdened by large food and oil subsidies as well as massive public sector employment. Collectively, these factors impede the regime's ability to provide the material gains that ensure political acquiescence.

B. Creating a New Tacit Pact

The growing deficit and stagnating economy have potentially severe political ramifications for the regime. The political sensitivity of the situation is exemplified by the regime's hesitance to talk about the extent of the deficit. Moreover, the growing poverty rate in Syria is a largely hushed issue as well. As the regime phases out its untenable social welfare provisions in order to balance the budget, an alternate and accessible source of revenue is required in order for the tacit pact to remain whole. The development of a revenue-generating financial sector has the potential to reduce the weight on state coffers

⁹ International Monetary Fund, "Syrian Arab Republic: 2008 Article IV Consultation," IMF Country Report No. 09/55, February 2009.

¹⁰ Jay Solomon, "Syria to Open its Economy to Foreign Investors," *Wall Street Journal*, May 15, 2009.

¹¹ Bernd Lucke, "Fiscal Impact of Trade Liberalization: The Case of Syria," *Proceedings of the 75th International Conference on Policy Modeling*, Brussels: 2001.

and, as such, it represents a recalibration of the regime's survival tactics rather than a fundamental strategic shift.

In order to ensure its survival, as described above, the regime seeks to maintain its tacit pact with society by generating material inducements for political buy-in and maintaining implicit threats of exclusion. In pursuit of these two goals, the regime employs multiple, though not necessarily contradictory, strategies. The way in which the regime prioritizes one strategy over another at any given time explains the specific regulatory reforms enacted.

As far as the first goal—generating material inducements—the regime utilizes three strategies: first, maintaining material payoffs for constituencies already incorporated, via the public sector, into the regime's tacit pact; second, allowing access to a private financial sector in order for society to generate new sources of material growth; and third, generating revenue to service the budget deficit. On the other hand, in order to maintain implicit threats of exclusion from material benefits, the regime employs three different strategies: first, cooptation of monetary policy; second, regulatory ambiguity; and third, maintaining ceilings on foreign ownership. The negotiation of all of these priorities yields an economically incoherent, yet politically logical regulatory structure.

III. Financial Sector Reforms as Material Inducements

The structural economic shifts that undermined the old tacit pact in Syria directly challenged the regime's ability to deliver material inducements, thereby providing

incentives to allow for a more dynamic and deregulated private financial sector.

Specifically, the regime sought to maintain the material rewards for established, politically loyal constituencies, provide new sources of capital from outside of state coffers to Syrian economic actors, and generate new sources of national revenue to balance the budget.

In transitioning to a new tacit pact, the regime sought to retain the support of already loyal constituencies. The public-private clientelist networks that made up the regime's previous tacit pact distributed substantial material benefits in large part through public sector channels. Leaving former cronies to fend for themselves in the new private sector would be costly for the regime as their formerly state-guaranteed privileges would be subject to less-friendly market forces.¹² As a result, public banks continue to dominate the banking sector as public banking assets still represent 80% of total banking assets in Syria.¹³ Further, in 2001, the Regional Command of the Ba'ath party reaffirmed Syria's commitment to the public sector and took privatization firmly off of the table.¹⁴ In interviews, Syrians involved in the financial sector called privatization a "dirty word" and further, not an apt description of the current changes.¹⁵

In addition to maintaining support to already-loyal constituencies, shifting economic conditions have required the regime to provide new sources of capital for Syrian businesses and consumers in order to boost the flagging economy. In 2001, Bashar al-

¹² For a full discussion of the formation and perpetuation of public-private economic networks, see Haddad (fn 7).

¹³ Central Bank of Syria, "Monetary and Banking Statistics," March 2009.

¹⁴ Anna Galdo, "Policies for Business in the Mediterranean Countries: The Syrian Arab Republic," Centre for Administrative Innovation in the Euro-Mediterranean Region, 2006: p. 10. Available at: <http://unpan1.un.org/intradoc/groups/public/documents/caimed/unpan018700.pdf>.

¹⁵ Interview with private sector manager, Damascus, Syria, March 21, 2009; Interview with financial consultant, Damascus, Syria, March 22, 2009.

Assad signed Law 8, allowing for the opening of private banks. The first private banks opened in 2004 and since then, six more have opened for business. The initial public offerings for all private banks were oversubscribed--Bank Audi's IPO, for instance, was oversubscribed to the tune of 1000%--suggesting a wide and consistent demand for banking services.

Moreover, the overall amount of credit made available to the private sector has increased since 2004, and in that same time private banks have increased their overall share of total credit over public sector banks.¹⁶ A senior bank executive in Damascus noted that the first three banks to open—Banque BEMO, Bank of Syria and Overseas, and the International Bank for Trade and Finance—all turned a profit within their first year, which was a notable feat. The success of private banks has gone so far as to prompt a competitive response on the part of public sector banks in order to try and maintain market share. The same bank executive noted that state banks have begun offering absurd products--such as car loans with no interest attached—as a reactionary attempt at competing for retail banking business.¹⁷

In addition to private banking, the Syrian regime went forward with the creation of a stock exchange in the hope of creating another mechanism to invigorate private sector growth. In exchange for public ownership, companies could access deeper and broader pools of capital, and citizens could earn dividends by investing their savings, most of which they have tended to keep in cash holdings stored in their homes. Opened on March 11, 2009, the Damascus Stock Exchange began with 6 listed companies and promising

¹⁶ Interview with international financial institution economist, Washington DC, May 7, 2009.

¹⁷ Interview with private bank executive, Damascus, March 22, 2009.

indicators of investor interest.¹⁸ Up to 20 companies could be trading publicly on the DSE by the end of 2009 and it is expected that the initial limits placed on intra-day trading will be lifted to accommodate the increased volume.¹⁹ To the same end, the legalization of private currency exchange, and unification of exchange rates increased levels of accessible finance for Syrian traders.

Finally, the potentially most salient strategy of the regime's financial liberalization program—providing new revenue in order to pay down the deficit—is served by a push to establish uniformity and transparency in accounting practices by adhering to International Accounting Standards (IAS).²⁰ Establishing credible documentation practices paves the way for more regular tax collection and budget projections. Additionally, adhering to IAS standards increases foreign investor confidence in the transparency of the tax regime, presumably leading to increased foreign investment flows. Before the wave of liberalizing regulations that began in 2000, the official corporate tax rate in Syria approached 60%.²¹ However, the excessively high rate combined with inconsistent and politically motivated enforcement prompted equally excessive rates of tax evasion and ad hoc book-keeping. As a result, total tax revenue collected was always far lower than official regime projections. The introduction of a lower tax rate has so far yielded more consistent revenue flows into state coffers, according to analysts.²²

¹⁸ See: "Syrian stock exchange set for launch"

¹⁹ Dominic Dudley, "Syriatel to list on Damascus exchange," *Middle East Economic Digest*, March 13, 2009; "Freeing the market's bonds," *Zawya*, April 2009. Available at <http://www.zawya.com/printstory.cfm?storyid=ZAWYA20090415120130&l=120100090415>.

²⁰ International Monetary Fund, pp. 16-17.

²¹ Interview with private bank executive, Damascus, Syria, March 19, 2009.

²² Ibid.; Interview with private bank executive, Damascus, Syria, March 22, 2009.

IV. Financial Sector Reforms: Maintaining Threats of Exclusion

Whereas a prosperous domestic financial sector is a crucial component of the regime's new tacit pact with society, it is also politically necessary that the regime maintains the final say on who can profit from that sector. Economic networks operating independently of government oversight could challenge the tacit pact, threatening regime stability. Thus, the regulatory structure has been crafted to serve the regime's second goal of maintaining a political monopoly over the private financial sector. By constantly wielding the threat of exclusion from the benefits of economic liberalization, the regime can enforce widespread political compliance, despite the economic incoherence of such a goal.

The regime is pursuing its political monopoly through three regulatory strategies. First, the regime has co-opted monetary policy, so that autonomous manipulation of the financial sector is not possible. Second, the regime employs ambiguous language in financial regulations so that it maintains the final say in enforcing those regulations. Finally, the regime requires that any private banks operating in Syria are majority-owned by Syrian investors, in order to guarantee the regime's authority over actors in the private financial sector.

The regime's first goal of maintaining final authority over monetary policy is achieved in part through its exchange rate regime. In 2006, Syria pegged its currency, the pound, to the International Monetary Fund's Special Drawing Right (SDR) unit.²³ By moving from

²³ "Syria to peg currency to SDR," *Khaleej Times*, October 31, 2006. Available at: http://www.menafn.com/qn_news_story_s.asp?storyid=1093131858; The SDR "is an international reserve

an exchange rate regime in which the Syrian pound was strictly pegged to the US dollar (meaning that Syria directly imported US monetary policy) to a regime in which the Syrian pound was pegged to an index of currencies, Syria gave itself wider latitude to set its own monetary policy.²⁴ Control over domestic interest rates, specifically, opened the door to political rather than purely market-oriented national economic policies.²⁵ While economically inefficient, the strategy allows the regime to maintain widespread political compliance.

How exactly, though, do Syria's indirect monetary tools and its control over domestic interest rates give the regime the ability to enforce political compliance? By controlling interest rates, the regime has increased control over the national price index. Low interest rates increase borrowing levels, increasing the amount of money circulating in the economy and, therefore, reducing the value of salaries and personal savings. High interest rates conversely mean that less money circulates in the economy and salaries and personal savings maintain, or in deflationary circumstances, lose their values.

The regime seeks the middle ground in which salaries and personal savings neither lose nor gain value in order to give Syrian citizens stable expectations of their respective

asset, created by the IMF in 1969 to supplement the existing official reserves of member countries. SDRs are allocated to member countries in proportion to their IMF quotas. The SDR also serves as the unit of account of the IMF and some other international organizations. Its value is based on a basket of key international currencies.” International Monetary Fund, “Special Drawing Rights,” February 2009. Available at: <http://www.imf.org/external/np/exr/facts/sdr.htm>

²⁴ A pegged exchange rate regime requires the pegging country to directly import the monetary policy of the country whose currency is the reserve currency. In other words, countries that peg their currencies have no autonomous monetary policies. On the other hand, a country that allows the value of its currency to be determined by fluctuations in the international currency markets (floating exchange rate regimes) retain full monetary policy independence. A third possible exchange rate regime is for a country to peg its currency to an indexed value of a discrete collection of currencies (a basket-peg regime). Under a basket-peg regime, the pegging country retains only indirect monetary tools.

²⁵ Interview with international financial institution economist, Washington, DC, April 29, 2009.

purchasing powers. This is especially important given that the purchasing power of a large portion of the population is supplied by the state. By maintaining stable purchasing power expectations, the regime can prevent widespread economic dissatisfaction, and thus maintain widespread political compliance. Currently a range of interest rates are issued by the Ministry of Finance and private banks are required to comply. Although some private bankers suggested that the regime might be considering the liberalization of interest rates, the decision to control them is politically motivated and therefore unlikely to happen in the near future.²⁶

The absence of primary or secondary markets in which banks can invest their excess capital liquidity²⁷ is another way in which the regime restricts the private sector from influencing monetary policy. Treasury bills or certificates of deposit could absorb some of the banks' excess liquidity and allow them to increase their profit margins beyond what they earn in interest payments. There is talk of an inter-bank bond market, and treasury bills have already been tested by the regime, but the development of such liquidity markets will ultimately be determined by their political utility to the regime.²⁸ Until then, private banks have few options for the productive use of their excess deposits that are not tied up in loans. Banks are currently required by law to deposit a portion of their total assets in a non-interest bearing Central Bank account.²⁹ In their quarterly analysis of the Syrian

²⁶ Interview with private bank executive, Damascus, March 19, 2009; Interview with private bank executive, Damascus, March 22, 2009.

²⁷ The amount of cash on hand that exceeds reserve requirements

²⁸ Treasury bills are thought to be a likely development as they not only absorb excess capital liquidity and provide investment opportunities for banks, they also serve the political goal of providing revenue to finance the budget.

²⁹ See "Licensing and Registration Procedures of Banks Established According to Law No. 28 for the Year 2001," available at: <http://www.banquecentrale.gov.sy/eg-laws/Licensing%20and%20Registration%20Procedures%20for%20law%2028.htm>

economy, Bank Audi analysts reported that deposits are driving the growth of the banking sector, rather than investment revenue.³⁰

Third, the Central Bank's lack of regulatory independence means that all monetary decisions must pass through the regime's political organs. Specifically, the Ministry of Finance oversees public sector banks—including the Central Bank—along with the other sectoral banks (Agricultural Bank, Industrial Bank, etc.). In fact, it was actually the Commercial Bank of Syria that was the de facto central bank until the 2006 U.S. sanctions paralyzed its activities. Roughly two-thirds of Syria's foreign exchange reserves are still held at the Commercial Bank, rather than at the Central Bank.³¹ The Credit and Monetary Council, the board of high-ranking government officials that is intended to function like the U.S. Federal Reserve Board, was only created in 2002 and has not yet established itself as an independent institution.

In addition to keeping the monetary policy reins tightly in its own hands, the regime employs regulatory ambiguity as another, more subtle, strategy to ensure that only the politically compliant are able to profit in Syria. Writing about the regulation of private business in Syria, Bassam Haddad notes that “most new economy-related legislation and decrees in Syria do not cancel previous legislation, leaving no legal shield for inadvertent ‘transgressors’ operating on the basis of the new law.”³² By keeping both old and new

³⁰ According to Bank Audi's most recent analysis of the Syrian banking sector, deposits account for 60% of the sector's assets. Bank Audi, “Syria Economic Report,” August 2008: p. 7. Available at: www.banqueaudi.com/geteconomy/syria/SyriaEconomicReport.pdf

³¹ Interview with private bank executive, Damascus, March 22, 2009; Interview with international financial institution economist, May 7, 2009.

³² Haddad, p. 111.

laws on the books, the regime is able to pick and choose the kind of enforcement it metes out at the time of its choosing.

Contradictions and ambiguities in new financial legislation have been characterized as “partially orchestrated” by the regime.³³ Interestingly, such confusion is perceived to be directed by mid-level bureaucrats rather than the regime's senior leadership. Mid-level bureaucrats can extract potentially lucrative side payments from private sector actors in exchange for preferential governmental treatment. Thus, the regime streamlines the language of regulation at the risk of undermining a source of indirect material inducements.

Finally, the regime requires majority-Syrian ownership of private banks as a third strategy of retaining threats of exclusion. Current regulations forbid a foreign partner from having a majority stake in a bank (the foreign ownership ceiling is set at 49%) -- preventing international banks from establishing a presence in Syria. Although international banks are seen as the next step toward further developing the banking sector, the foreign ownership ceiling ensures that all current banking ventures fall squarely under the control of the regime.³⁴

V. The Future of Economic Reform in Syria

³³ Interview with private bank executive, Damascus, March 22, 2009.

³⁴ Bank Audi, p. 8.

The regime in Syria not only uses economic liberalization to generate economic growth but also to construct new points of leverage with which it can have the final say over the content and direction of economic change. However, international financial institutions have latched on to the opening in the Syrian economy and are currently lobbying for deeper engagement and further reform. Their recommendations, nevertheless, fail to take into account the regime's political logic, which will dictate the future of the Syrian financial sector. Given the regime's political framework laid out in this paper, what is the likely fate of these recommendations?

First, the International Monetary Fund has recommended that the traditional dominance of state banks be broken in favor of a stronger private banking sector.³⁵ Relinquishing the dominance of state banks would involve, however, relinquishing several sources of material inducements for the regime, and, therefore, is unlikely to happen as part of a concerted policy. First, state banks are a source of essentially no-cost loans for state enterprises as well as well-connected members of the state bourgeoisie and the private sector would not offer the same privileged access to capital.³⁶ Likewise, for lower classes, the strictures of private loans for material goods purchases is prohibitively higher than via state banks -- for instance, a car loan can require a down payment of more than half the value of the car. Additionally, as with other sectors of the economy run by the state, public banks employ more workers than are necessary for efficient functioning of the banks. Removing substantial numbers of these employees from the state payroll would exclude them from the material inducements sustaining their political compliance.

³⁵ International Monetary Fund, p. 8.

³⁶ Again, see Haddad.

Although the regime is unlikely to privatize state banks in the near future, their dominance may be an unintended casualty of the reform impetus. One economist interviewed mentioned that once private banks begin claiming market share, public banks that are unable to compete inevitably became irrelevant.³⁷ Evidence suggests that the public sector banks are definitely feeling competition already from the burgeoning private sector.

A second recommendation from the IMF is that the Central Bank should have autonomous authority over indirect monetary tools.³⁸ A Central Bank operating outside of the purview of the Ministry of Finance, and with access to a wider range of monetary tools would have the ability to regulate the financial sector in a manner more consistent with accepted economic doctrine. This situation would, however, remove the regime's ability to co-opt monetary policy in order to serve its political goals. Thus, the regime is likely to retain regulatory oversight over the Central Bank.

At the same time, the gradual development of certain indirect monetary tools such as primary and secondary capital markets, may actually come to fruition.³⁹ Tools such as treasury bills can maintain the regime's political survival by providing alternate sources of state revenue. Additionally, treasury bills or Central Bank certificates of deposit (CDs) would provide venues for excess liquidity in the private banking sector, allowing for the expansion of private finance.

³⁷ Interview with private bank executive, Damascus, March 22, 2009; Interview with international financial institution economist, Washington DC, May 7, 2009.

³⁸ International Monetary Fund, p. 8.

³⁹ Interview with private bank executive, Damascus, March 22, 2009.

Finally, the IMF has recommended that Syria should guarantee a more transparent regulatory regime.⁴⁰ Yet, as mentioned earlier, such irregular regulatory enforcement is the product of mid-level bureaucrats who stand to personally benefit from wielding threats of enforcement in exchange for side payments from private sector actors. These clientelist networks have long guaranteed the broader political compliance of both state bureaucrats and their private sector affiliates. Dismantling these networks would remove the material incentives for political acquiescence among members of the networks. Therefore the regime is unlikely to seriously pursue a more transparent regulatory regime.

The regime currently has little incentive to alter the pace of reform in Syria. Absent any new structural shifts, both economic and political liberalization will continue to occur on the regime's terms. However, international factors on the horizon—such as detente with the United States, trade agreements with Europe, or deeper engagement with international financial institutions—have the potential to create new structural realities

The effects of the global financial crisis are perhaps the most immediate forces that could upset the balance in Syria. In November 2008, the Minister of Finance Mohamed al-Hussein initially issued a statement that the crisis would “affect most countries, but in different proportions,” and therefore would have a negative impact on Syria’s budget.⁴¹ However, subsequent statements from the government insisted that Syria’s isolation from international banking had largely sheltered the economy from any serious effects.

⁴⁰ International Monetary Fund, p. 8.

⁴¹ Sahil Nagpal, “Syrian Finance Minister: Global financial crisis will affect budget,” *TopNews*, November 18, 2008. Available at: <http://www.topnews.in/syrian-finance-minister-global-financial-crisis-will-affect-budget-290536>.

However, despite Syria's isolation from the global financial system, it has felt the impact of the crisis indirectly. In February 2009, Deputy Prime Minister for Economic Affairs Abdullah Dardari acknowledged in an interview that the Syrian economy's dependence on foreign trade for revenue meant that, "its vulnerability to external factors is very large."⁴² In addition, the most significant effect of the crisis on Syria has been the loss of potential foreign investment, as countries that were more integrated into US and European credit markets have scaled back any new investment plans.

This rollback of already meager foreign investment comes at a critical point in Syria's attempt to reconfigure the tacit pact that keeps the ruling regime in power. Financially, the regime needs capital flows from both domestic and foreign sources in order to offset the growing budget deficit and threatened access to liberalized banking services. Politically, it is also troublesome, as the regime has long denied that the 2006 US sanctions were hurting the economy because of Syria's continued ability to continue to attract investment.⁴³ The global financial crisis thus poses a challenge to the regime's strategy of circumscribed economic liberalization. The regime's ability to re-calibrate its tacit pact with society to accommodate the structural shifts presented by the crisis will determine the extent to which these, and other, international factors are able to force a new logic of reform in Syria.

⁴² Julian Weinberg, "Credit crunch afterthoughts," *Forward Magazine*, April 2009. Available at: <http://www.fw-magazine.com/content/credit-crunch-afterthoughts>.

⁴³ Ehsani2 and Joshua Landis, "Is Syria setting a Price Tag on a US Brokered Peace with Israel?," *Syria Comment*, February 6, 2009. Available at: <http://joshualandis.com/blog/?p=2106>.