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Syrian Arab Republic: 2008 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for the Syrian Arab Republic

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2008 Article IV consultation with the Syrian Arab Republic, the following documents have been released and are included in this package:

- The staff report for the 2008 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on October 30, 2008 with the officials of the Syrian Arab Republic on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on December 19, 2008. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A staff statement of January 9, 2009, updating information on recent developments.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its January 9, 2009 discussion of the staff report that concluded the Article IV consultation.

- A statement by the Executive Director for the Syrian Arab Republic.

The document listed below has been or will be separately released.

Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

SYRIAN ARAB REPUBLIC

Staff Report for the 2008 Article IV Consultation

Prepared by the Staff Representatives for the 2008 Consultation
with the Syrian Arab Republic

Approved by Adam Bennett and David Marston

December 19, 2008

- Discussions for the 2008 Article IV consultation were held in Damascus during October 15–30, 2008. The staff team comprised Messrs. Sakr (Head), Dridi, Sumlinski, El-Said, and Ms. Farahbaksh (all MCD), Mr. Geadah (MCM), and Mr. El Daher (World Bank). Ms. Abdelati (OED) attended the meetings, and Mr. Bennett (MCD) joined the policy discussions.

- The mission team met with Deputy Prime Minister Dardari, Minister of Finance Al-Hussein, Minister of Tourism Al-Kalaa, Central Bank Governor Mayaleh, and representatives of financial institutions and nongovernment organizations.

- The Executive Board concluded the 2007 Consultation on July 31, 2007. The staff report and PIN are available on:
http://www.imf.org/external/pubs/cat/longres.cfm?sk=21272.0

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EXECUTIVE SUMMARY

Background

- **The economic recovery that started in 2004 continued in 2007**, with non-oil GDP growth in excess of 5 percent. This has been aided by progress in implementing reforms and higher regional demand for Syrian non-oil exports. Oil output, however, remained on a downward trend. The fiscal and external deficits widened slightly to still-sustainable levels, and the level of official net foreign assets remained comfortable.

- **The impact of adverse global and regional developments currently underway on the Syrian economy are expected to be relatively moderate** in the short term. The effects are likely to be through weakening FDI, remittances, and demand for Syrian exports from the Gulf region.

- **The medium-term outlook is expected to improve** as the global and regional economies begin to recover, with non-oil growth accelerating to about 6.5 percent by 2013. The fiscal and external and current account deficits are projected to stabilize at about 3 and 4 percent, respectively. This positive outlook is contingent on perseverance in advancing fiscal and structural reforms and an improvement in global conditions over the medium term.

Key policy issues and recommendations

- **Further fiscal consolidation is necessary.** It is essential to further reduce petroleum subsidies, advance the preparatory work to launch the VAT in 2010, and continue to restrain public expenditure, while encouraging public-private partnership agreements, with adequate safeguards, for investment in infrastructure.

- **The 2008 FSAP identified financial sector reform priorities in the period ahead.** These include the need to audit and restructure state banks; build up regulatory and supervisory capacity and strengthen enforcement of regulations; and enhance the monetary policy framework by modernizing the central bank and developing indirect monetary policy instruments.

- **The switch of the de jure peg from the dollar to the SDR is appropriate for Syria.** A gradual increase in exchange rate flexibility would be beneficial, but would need to be preceded by the development of indirect monetary policy tools.

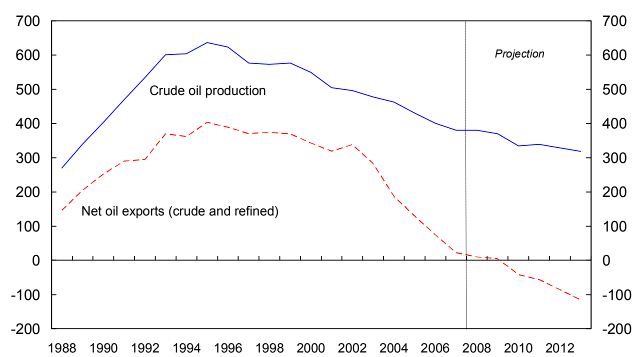
- **Efforts to transition toward a market-based economy should continue.** Enhancing the business environment by modernizing and streamlining the regulatory framework, and further liberalizing trade would help enhance medium-term growth prospects.

I. Background and Recent Developments

1. **Global political and economic ties have been strengthened in recent years.** Relations with the EU have improved recently following the establishment of diplomatic relations with Lebanon. Subsequently, France, which currently chairs the EU, issued positive signals regarding the ratification of the association agreement with Syria. However, the large number of Iraqi refugees in Syria continues to pose economic and social challenges. While their presence has contributed to growth, the refugees have put a strain on public expenditures for petroleum and food subsidies, education, health, and utilities. As the refugees run down their savings, they may seek work and add pressure to the labor market.

2. **Syria's overall macroeconomic performance has remained strong.** Non-oil GDP growth is estimated to have been about 6 percent in 2007 despite unfavorable weather conditions affecting agriculture. Virtually all other non-oil sectors continued to grow strongly. However, overall growth registered only about 4 percent due to declining oil production. These developments continued through 2008. Preliminary data indicate a rate of non-oil growth similar to 2007, despite a further decline in agricultural output, as construction and services maintained their rapid expansion. Overall growth is expected to be about 5 percent. Inflation accelerated in 2008 to 17–20 percent by mid-2008, up from a reported 5 percent in 2007. It is, however, expected to decline in the fourth quarter of 2008, in line with international food prices, and is projected to average about 15 percent for the year.

Figure 1. Syrian Arab Republic: Oil Production and Net Oil Exports ('000 barrels/day)



Sources: Syrian authorities; and Fund staff estimates and projections.

3. **While the overall fiscal deficit increased to about 3.5 percent of GDP in 2007, the non-oil deficit improved slightly.** Oil revenue decreased by about 2 percent of GDP. Non-oil receipts also declined, partly reflecting the reduction in customs tariffs. Current and capital outlays were reduced by about one percent of GDP in total. This was achieved despite the pressure on budgetary expenditure arising from the large number of Iraqi refugees.

4. **The fiscal deficit is expected to stabilize in 2008 mainly as a result of the reduction in fuel subsidies.** The authorities launched a program to phase out petroleum subsidies in May 2008. Gasoline and diesel prices were increased by 33 and 240 percent, respectively. To mitigate the impact of the diesel price increase, the authorities issued coupons to all Syrian households that would allow them to purchase diesel up to 1,000 liters

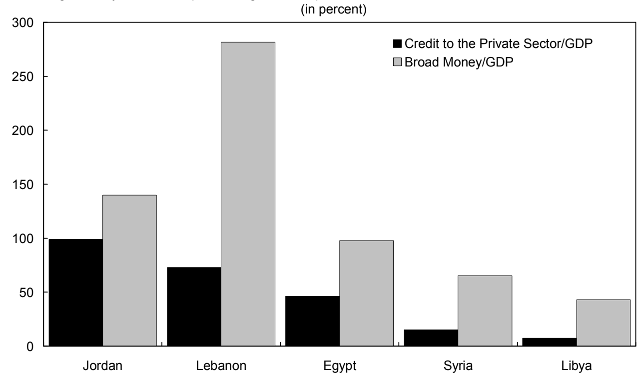
per household at 9 SYP/liter.[1] The price of fuel oil, which is used by large industrial establishments and power plants, was raised by 33 percent in December, 2008. These price increases and overall expenditure restraint led to a further small narrowing of the non-oil deficit despite the continued decline in customs revenue resulting from the full year effect of the 2007 reduction in tariffs.

5. **The external current account deficit is expected to widen to about 4 percent of GDP in 2008,** from 3.3 percent in 2007. The net oil balance (after subtracting the share of foreign partners) turned negative due to declining output and rising domestic consumption. However, non-oil exports, tourism, and remittances grew rapidly as a result of strong regional demand and the relaxation of foreign exchange controls. Net official foreign assets have been stable at about $17 billion (10 months of imports). The real effective exchange rate of the Syrian pound appreciated by 4 percent in 2007, and about 9 percent in the first three quarters of 2008 due to the combined effect of rising inflation and the pound's nominal appreciation against the dollar.

6. **Broad money has been growing in line with nominal GDP.** This growth mainly reflected domestic credit expansion. Credit to public enterprises grew by about 40 percent in 2007 and by 60 percent in the first half of 2008 (y-o-y), reflecting the rising financing needs of enterprises providing fuel and other subsidies. Growth of credit to the private sector was about 20 percent in 2007 and is expected to register 25 percent in 2008. Interest rates remained low, and became largely negative in real terms with the rise in inflation in 2008.

7. **Financial intermediation continues to be low** by regional standards. Credit to the private sector has been at about 15 percent of GDP since 2005. Broad money to GDP ratio stood at about 65 percent at end-2007.

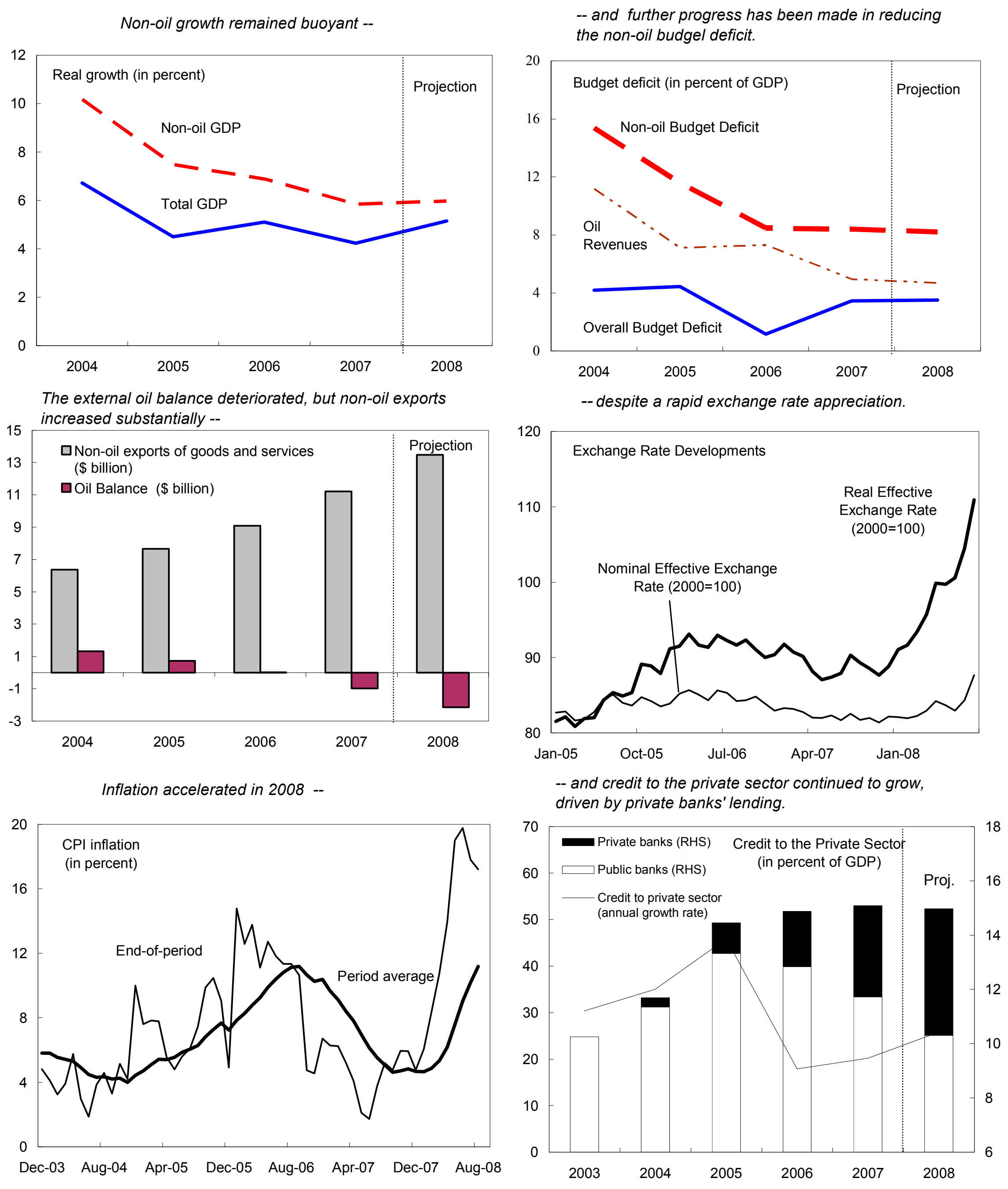
Figure 2. Syrian Arab Republic: Regional Comparative Indicators for Financial Intermediation, 2007 (in percent)



Sources: IFS; and Fund staff estimates.

[1] These coupons covered about 4.4 million tons, roughly the amount of local production of diesel. However, the cost of oil subsidy increased due to the sharp rise in international prices during the first eight months of 2008.

Figure 3. Syrian Arab Republic: Macroeconomic Developments

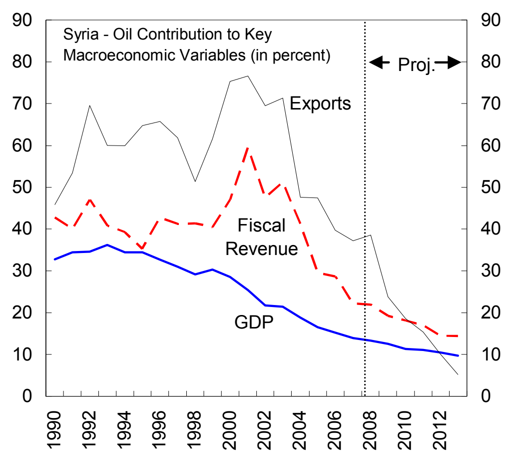


Sources: Syrian authorities; and Fund staff calculations and projections.

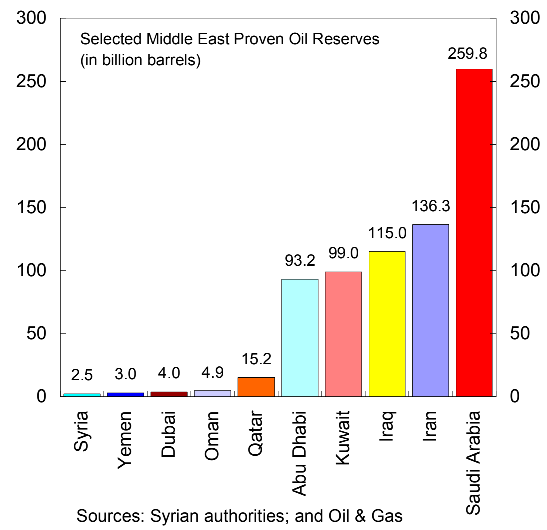
Box 1. The Rise and Fall of Oil in the Syrian Economy

Substantial oil discoveries were made in Syria during 1970–1990s. Oil production increased from about 250 thousand barrels per day (bpd) in the mid 1980s to almost 650 thousand bpd in 1995. As a result, oil's contribution to GDP, fiscal revenue, and exports, reached 34, 35, and 65 percent, respectively, in that year.

However, Syria has less oil reserves than most of the regional oil exporters. As of October 2008, Syria's proven oil reserves of 2.5 billion barrels were equivalent to about half of Oman's reserves and less than 3 percent of Kuwait's reserves.



Sources: Syrian authorities; and staff estimates and projections.



Sources: Syrian authorities; and Oil & Gas Journal, Jan.1, 2007.

Since 1995, Syria's oil production has been on a downward trend and domestic energy consumption has been increasing. Consequently, Syria became a net oil importer again starting in 2007. In that year, the "overall oil balance," which is the net oil trade balance minus payments made to the foreign oil companies, showed a deficit of 2.4 percent of GDP.

In an attempt to reverse these trends, the authorities have stepped up their efforts since the early 2000s to increase exploration in Syria. Successive bidding rounds were launched on over 20 blocks in the country. The arrival in the last four years of a large number of independent oil companies has helped slow down the decline in production. However, the authorities expect production to continue declining in the coming years, bottoming out at about 300,000 bpd by 2025 and remaining constant thereafter. At these production levels, current recoverable reserves would be depleted by 2030.

8. **Private banks are well capitalized.** Their overall capital adequacy ratio was reported at about 13 percent in mid-2008, compared to the Central Bank of Syria's (CBS) minimum requirement of 12 percent. Nonperforming loans (NPLs) are reported at about 5 percent of total loans for all banks at end-2007. Data on public banks loan classification remain weak, hindering a meaningful calculation of their capital adequacy or NPLs ratios (Box 2).

Box 2. Key Findings and Recommendations of the 2008 FSAP

The financial system is still dominated by state banks, which hold 80 percent of bank assets. Private banks have grown rapidly since having been first licensed in 2004. Licensing of private insurance companies started in 2005. A stock market will be opened in 2009. The payment and settlement system needs strengthening.

The CBS lacks effective monetary policy tools and independence. There are no bills to conduct open market operations and no standing facilities. Furthermore, the CBS does not have full control over international reserves, a substantial part of which is held by the Commercial Bank of Syria (CBoS).

A basic supervisory and regulatory framework is in place, but enforcement needs strengthening. The CBS should enhance supervision of public banks.

The assessment of the soundness of the banking system is hampered by serious data deficiencies in public banks. Private banks and the CBoS are well-capitalized, but profitability is generally low. Public banks' financial statements are not audited according to international standards.

Risks for public banks could arise from possibly weak balance sheets and low capitalization, poor underlying profitability, and outdated business practices. **For private banks**, risks could result from their recent rapid growth, entry into new untested business lines, and high loan concentration in bank portfolios.

The key FSAP recommendations are: (i) accelerate CBS modernization and reform, including by enhancing its research capacity, strengthening financial sector risk management, developing the debt market, and transferring the official foreign exchange reserves held by the CBoS to the CBS; (ii) develop systemic liquidity management by creating money and foreign exchange instruments and markets; (iii) build up adequate regulatory and supervisory capacity; and (iv) conduct a comprehensive diagnostic audit for state banks, produce reliable financial soundness indicators for these banks, and restructure them.

II. Policy Discussions

9. **The policy discussions focused on**: (i) fiscal policies and reforms needed to compensate for the decline in oil revenue; (ii) monetary and exchange rate policy; and (iii) structural reforms aimed at enhancing the medium-term growth outlook, with emphasis on the financial sector.

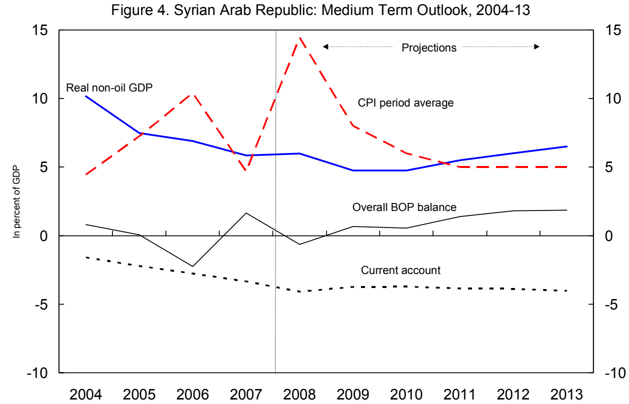
A. Outlook and Risks

10. **The near-term growth outlook is expected to be only mildly influenced by the current adverse global conditions.** The worsening of international financial conditions does not appear to have affected Syria's financial sector, given its limited integration with the global system and with CBS regulations strictly limiting banks' foreign exposure. However, Syria is likely to be indirectly affected by a regional slowdown resulting from global financial linkages with other countries in the region, notably with the Gulf; FDI, worker

remittances, and demand for Syrian exports from these countries may decline.[2] Non-oil growth is therefore projected to slow down by about one percentage point (to around 5 percent) over the next two years.[3] The external current account is expected to narrow slightly as the decline in oil prices should reduce the cost of net petroleum imports. The fiscal deficit is projected to narrow due to the reduction in fuel subsidies.

11. **The medium-term outlook is expected to improve as the global and regional economies begin to recover.** Non-oil GDP could accelerate gradually to 6.5 percent by 2013. The external current account deficit is projected to stabilize at about 4 percent of GDP, and the fiscal deficit at about 3 percent. However, this outlook is subject to considerable downside risks should Syria's fiscal and structural reforms efforts weaken, the severe weather conditions affecting agriculture continue, or the regional slowdown deepens.

Figure 4. Syrian Arab Republic: Medium Term Outlook, 2004-13



Sources: Authorities; and Fund staff estimates and projections.

B. Fiscal Policy

12. **The authorities aim to continue to improve the non-oil fiscal balance,** in order to adjust to the reduction in oil output. To this end, they are determined to fully eliminate the fuel subsidies by 2010. It has not been decided yet whether distribution of fuel coupons would continue in the coming years. The authorities are aware that a secondary market has developed for illegal trading in these coupons. They are, therefore, giving consideration to moving to a form of targeted cash transfers. The authorities also intend to continue to restrain both current and capital outlays. To this end, preliminary information on the 2009 budget indicate a small reduction in expenditure in real terms.

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[2] The impact of adverse regional conditions on Syria is expected to be relatively mild due to the fact that inflows from the region had not grown in line with the rise in oil prices and remain at a low base. For example, workers' remittances into Syria grew since 2005 by an annual average of less than 3 percent. FDI and tourism inflows are projected at about $2 billion and $3.5 billion, respectively in 2008. These levels are below the potential of Syria, which remains a relatively less costly destination for FDI and tourism by regional and global standards.

[3] This non-oil growth projection reflects a stronger slowdown in most sectors, other than agriculture, in response to the weakening in the global outlook. On the other hand, agricultural output, which constitutes around 25 percent of non-oil GDP, is projected to steadily rebound from the estimated cumulative reduction of about 15 percent over the past two years.

13. **Good progress is being made in the preparatory work for the VAT.** However, the introduction of the VAT, which was initially planned for 2009, has been delayed until January 2010. This was partly to avoid contributing to inflationary pressures in view of the ongoing phasing out of fuel subsidies. The authorities are also keen to complete sufficient preparatory work to ensure the readiness of tax administration and the public for the introduction of the VAT.

14. **The authorities are aware of the need to improve public expenditure monitoring and management.** At present local authorities report their expenditures on a frequent basis to the Central Accounting Authority, while the ministry of finance receives such information with a considerable lag. Large quasi-fiscal operations, in particular to finance fuel and other subsidies, are conducted through the banking system. The authorities agree that these operations should be reduced. However, they felt that simply bringing them on-budget could perversely soften their financing constraint. The ministry of finance believed that streamlining these operations should be addressed in the context of an overall reform strategy to reduce their size and modernize the subsidies system.

C. Monetary Policy and Financial Sector Reform

15. **There is excess liquidity in the banking system, and real interest rates have become largely negative.**[4] The negative real interest rate, in the authorities' view, is due to the temporary high inflation rates. They also pointed out that the exchange rate peg limits the scope for a significant differential between the interest rate on the pound and rates on major currencies. In the meantime, the CBS increased the reserves requirement ratio from 5 percent to 10 percent in October, 2008, which would help mop up part of the excess liquidity.[5]

16. **The authorities intend to continue their effort to enhance the monetary policy framework.** There are currently no indirect monetary policy instruments or standing facilities. The CBS has recently held two trial auctions of treasury bills. Full fledged issues of the bills are expected in 2009. If this plan gets delayed, the CBS would consider issuing its own certificates of deposit. The authorities indicated that the transfer of international reserves from the CBoS to CBS, in line with the FSAP recommendation, is expected to be completed in 2009. The CBS has also embarked on a technical cooperation program with the Fund to modernize its structure and enhance the payments system, with a view to improving its ability to conduct monetary policy.

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[4] Interest rates on deposits are subject to rules effectively imposing a 5-11 percent band. There are indications that depositors are seeking better returns in the informal credit market, which is illegal and not regulated.

[5] Since required reserves are not remunerated, their increase is likely to lead to a widening of the spread between the deposit and lending rates.

17. **The CBS sees strengthening bank supervision as a priority.** In particular, off-site surveillance techniques and methodologies to calculate capital adequacy measures are being improved. Furthermore, efforts are underway to enhance the supervision of state banks. These banks have started producing some key FSIs and reporting them to the CBS. In addition, the free-zone banks will be brought under CBS supervision in 2009.

18. **Efforts are underway to enhance the framework for anti-money laundering and combating the financing of terrorism (AML/CFT).** A high level financial intelligence unit has been created, assessment criteria have been tightened, and the scope of AML/CFT has been extended to cover foreign currency changers, insurance companies, and brokerage houses.

D. External Sector Issues

19. **The de jure exchange rate peg was switched from the dollar to the SDR** in August 2007.[6] De facto, the pound has been trading within a narrow band against the SDR and appreciated against the dollar by about 7 percent (as of end-September 2008). Econometric estimates, which are not reliable because of data and methodological shortcomings, suggest that the real exchange rate of the pound may be moderately overvalued relative to its medium-term equilibrium level (Box 3).

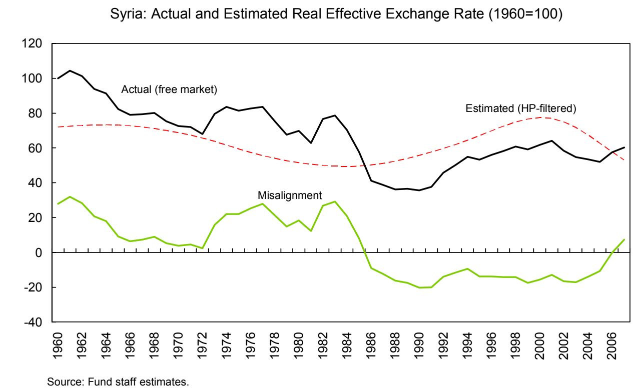
20. **The authorities expressed their intention to remove the remaining foreign exchange restrictions and multiple currency practices. They allowed the use of credit cards to pay for foreign transactions starting in June 2008.** They hoped to be in a position to accept the obligations under Article VIII in the near future. To this end, they are considering requesting a Fund TA mission to conduct a comprehensive review of the exchange system.

21. **The authorities view the current exchange rate arrangement as appropriate under current circumstances.** They believe that preconditions to widen their policy options with regard to the choice of the exchange regime could be in place gradually over the medium term, with the development of indirect monetary policy instruments and a liquidity management framework.

[6] Significant progress toward exchange rate unification was made on January 1, 2007, with the abolition of the "budget" rate.

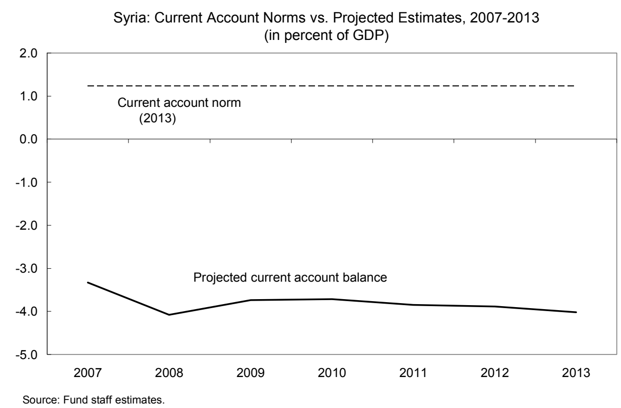
Box 3. Exchange Rate Assessment

Econometric estimates suggest that the pound may be moderately overvalued in real effective terms. However, these estimates, which utilized CGER methodologies,[1] are not reliable due to serious data and methodological shortcomings. Syrian balance of payments statistics need major improvement, and the data used by staff are in many cases only estimates. The results are also very sensitive to the model specification used in the regressions.



The equilibrium real exchange rate (ERER) methodology points to an overvaluation in the pound by about 14 percent. This methodology utilizes a vector error correction model to estimate the ERER using as the determining variables oil income, net foreign assets, openness to trade, government expenditure, and relative productivity.

The macroeconomic balance approach (MB) also indicates an overvaluation of the pound by about 12 percent. Based on a panel regression for oil- exporting countries, the equilibrium current account norm for Syria would be a surplus of about 1 percent of GDP. This compares with a projected deficit for Syria of about 4 percent of GDP. The set of determining variables in this approach include the fiscal balance, population growth, NFA, oil balance, and per capita income.



The external sustainability (ES) approach provides inconclusive results. These results range from an undervaluation of 14 percent to an overvaluation of about 3.5 percent, depending on the assumptions used. The outcome depends on whether the objective is to keep constant the annuity from oil wealth in real terms, in real terms per capita, or as a percent of GDP.

1/ "Methodology for CGER Exchange Rate Assessment," IMF, November 2006 (www.imf.org/external/np/pp/eng/2006/110806.pdf)

E. Structural Reforms and Other Issues

22. **The authorities have been making progress in structural reform.** In particular, advances have been made in trade liberalization by substantially reducing the tariff schedule. The export of strategic agricultural products, however, remains subject to government approval. Trade liberalization has also continued in the context of bilateral and regional trade agreements. The authorities' future reform agenda includes the streamlining of agricultural

subsidies, introduction of a one-stop shop for company registration, incorporation of the Syrian Telecommunication company, and creation of an independent regulatory body. Notwithstanding these reforms, there is considerable scope to improve the business environment, as indicated by the high cost of "doing business."[7] Areas identified for improvement included modernizing the tax system, reducing bureaucratic discretion, and further enhancing the legal framework.

23. **The authorities issued two decrees in 2008 to combat under-invoicing of imports.** The first decree allows the customs department to purchase imported goods at invoice prices. The decision to buy the goods would be made by the Director General of the Customs Department. The authorities hope that the existence of this decree will be sufficient to deter underinvoicing, without customs actually having to intervene in this manner. The second decree requires importers to open letters of credit through domestic banks. The implementation of this latter decree is still on hold due to objections from the business community.

24. **Serious shortcoming in economic and financial statistics continue to hamper effective surveillance.** Efforts are ongoing to improve the data situation, in the areas of national accounts, balance of payments, and fiscal statistics. The timelines and quality of data would also benefit from enhanced coordination between government agencies.

III. Staff Appraisal

25. **Syria's economic performance has been strong.** Non-oil growth remained robust despite the adverse impact of the severe drought on agriculture. The recent acceleration in inflation was largely due to temporary increases in food and fuel prices. Inflation started to decline in the second half of 2008. The fiscal and external current deficits has worsened only moderately over the past two years despite the significant deterioration in the net oil balance. This was made by the restraint on public expenditure, ongoing fuel subsidies reform, and strong performance of non-oil exports, remittances, and tourism receipts.

26. **The impact of the adverse global and regional developments currently underway on the Syrian economy are expected to be relatively mild in the short term.** The effects are likely be manifested through weakening FDI, remittances, and demand for Syrian exports from the Gulf region. The medium-term outlook is then expected to improve as the global and regional economies begin to recover. This generally positive outlook is contingent on perseverance in advancing fiscal and structural reforms and a gradual recovery in agriculture and in the global economy over the next two years.

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[7] Syria ranked 137 (out of 145) in the World Bank's 2009 *Doing Business Report.*

27. **The non-oil deficit needs to be further reduced.** It would be essential to consolidate the nascent gains in turning around Syria's fiscal outlook. This is crucial for preserving fiscal sustainability, and is appropriate given the relatively mild impact of the global slowdown on Syria's growth outlook. Achieving this goal will require continued restraint on current expenditures, notably wages and subsidies, and the prioritization of investment projects by focusing on infrastructure. It will also be important to continue to encourage private sector participation in these projects, including through private-public partnership agreements, with adequate safeguards.

28. **The steps taken to reduce fuel subsidies have helped improve Syria's fiscal outlook.** Staff encourages the authorities to maintain this progress, with a view to eliminating these subsidies by 2010, while developing a well-targeted compensation scheme to mitigate the impact on the poor.

29. **There is an urgent need to further enhance public expenditure management.** Priority should be given to improving the monitoring of expenditures at the regional level. Establishing a single treasury account would help achieve this objective. It is also important to reduce extra budgetary and quasi-fiscal operations that are conducted by public enterprises and financed by the banking system. These operations should be brought on budget, and the consolidated budget deficit should be primarily financed by treasury bills, the interest on which should be market determined.

30. **Staff commends the authorities for the progress made in the preparatory work for the VAT.** Introducing the VAT by the new target date of 2010 would be important to help offset the impact of the declining oil revenue on the budget. To ensure the success of the VAT, staff encourages the authorities to (i) adopt a single rate with few exemptions; (ii) put in place an adequate tax procedure code and information technology system; and (iii) ensure that the existing large and medium taxpayer offices—which will administer the VAT — report directly to the central Syrian Tax Commission. It is also important to advance other tax reforms, particularly to simplify the income tax regime and the rationalize excises.

31. **The commitment to maintain a cautious monetary policy stance is welcome.** In this connection, public banks should be instructed to strictly limit directed lending. At the same time, it is important to develop indirect monetary policy instruments and further liberalize interest rates. If plans to launch market-based treasury bills are delayed, the CBS should seek to issue its own certificates of deposit. Consideration should also be given to establishing standing facilities at the CBS. Enhancing the CBS independence and giving it control over all official international reserves would strengthen its ability to formulate and implement monetary policy.

32. **The authorities' early response to the 2008 FSAP recommendations is commendable.** The CBS has already started to address the existing shortcomings identified in the FSAP, including by efforts to improve the supervision of state banks. Staff encourages

the CBS to continue its efforts in this regard. In particular, compliance with prudential regulations by public banks needs to be enforced. All banks should be subject to annual audits by independent firms, and provide timely information to the CBS, including financial soundness indicators. In addition, priority should be given to restructuring state banks and to ensuring that they operate on a commercial basis.

33. **The switch of the pound's peg to the SDR is appropriate for the Syrian economy.** This arrangement provides a credible monetary anchor, while allowing some flexibility in the pound's exchange rate vis-à-vis major currencies. Econometric estimates suggest that the pound may be moderately overvalued in real effective terms. These estimates are, however, unreliable due to severe data and methodological shortcomings. The staff recommends maintaining the current level of the nominal exchange rate in the present context, as this appears to be in line with market forces and consistent with the CBS' policy of containing inflation. For the medium term, the mission encourages the authorities to prepare the ground for allowing a gradual move toward greater exchange rate flexibility. Increased flexibility would help maintain stability over the medium term, given the prospective depletion of oil reserves. It would also facilitate a gradual increase in monetary policy independence. This would have to be preceded by a switch to market-based monetary management and the development of expertise in foreign exchange operations.

34. **The progress made in transition to a market economy is welcome, but the remaining structural reform agenda is substantial.** Accelerating structural reform is crucial to minimize the impact of the global slowdown on Syria's growth prospects, particularly in view of the need to persevere with fiscal consolidation. In this connection, staff encourages the authorities to continue to liberalize foreign trade. Staff believe that the authorities should reconsider the recent decisions requiring importers to open letters of credit through local banks and to allow the customs department to buy imports at invoice prices. It is not clear that this is the most effective way to improve accurate invoicing of goods for customs. Reducing the cost of doing business will also be crucial to further encourage private investment, promote exports, and create jobs.

35. **Syria continues to maintain exchange restrictions under Article XIV, Section 2 (Appendix I)**. It also maintains exchange measures subject to approval under Article VIII (Appendix I). The staff does not recommend approval for their retention. The staff therefore advises the authorities to eliminate remaining restrictions and multiple currency practices, and stands ready to conduct a comprehensive review of the exchange system upon the authorities' request.

36. **Staff urges the authorities to improve data quality and provision** to facilitate better analysis of developments and guide policy formulation.

37. **It is proposed that the next Article IV consultation take place on the standard 12-month cycle.**

Table 1. Syrian Arab Republic: Selected Economic Indicators, 2004–09

	2004	2005	2006	Prel. 2007	Proj. 2008	Proj. 2009
	(Change in percent, unless otherwise indicated)					
National income and prices						
Real GDP	6.7	4.5	5.1	4.2	5.2	3.9
Oil	-6.1	-8.6	-7.1	-5.0	-0.1	-2.6
Non-oil	10.2	7.5	6.9	5.8	6.0	4.7
Nominal GDP (LS billions)	1,263	1,491	1,709	2,025	2,567	2,477
Of which: Non-oil	986	1,134	1,305	1,558	1,886	2,131
Nominal GDP ($ billions)	25.0	28.6	33.5	40.6	55.2	50.7
Crude oil production ('000 barrels/day)	462	431	400	380	380	370
GDP deflator	10.9	12.9	9.1	13.7	20.6	-7.2
Oil export price ($ per barrel)	33.5	48.1	57.6	65.3	90.0	48.9
CPI period average	4.4	7.2	10.4	4.7	14.5	8.0
Total population (millions)	18.8	19.3	20.4	20.8	21.3	21.8
Of which: Iraqi Immigrants (millions)	0.8	0.9	1.5	1.5	1.5	1.5
	(In percent of GDP, unless otherwise indicated)					
Government finances						
Revenue	27.2	24.0	25.5	22.3	21.4	21.8
Oil-related revenue	11.2	7.1	7.3	4.9	4.7	4.2
Non-oil revenue	16.1	16.9	18.2	17.3	16.7	17.6
Expenditure	31.4	28.5	26.6	25.7	24.9	25.0
Current expenditure	19.0	18.1	16.3	16.1	15.4	15.5
Development expenditure	12.4	10.4	10.3	9.6	9.5	9.5
Overall balance	-4.2	-4.5	-1.2	-3.4	-3.5	-3.1
Non-oil budget balance	-15.4	-11.6	-8.5	-8.4	-8.2	-7.3
	(Changes in percent of initial stock of money)					
Broad money	11.1	11.5	9.4	9.8	19.0	13.0
Net foreign assets	5.4	0.7	-2.3	-2.0	3.7	2.2
Net domestic assets	5.8	10.8	11.7	11.9	15.3	10.8
Credit to government	2.8	6.1	0.3	-3.1	-0.7	3.5
Credit to public enterprises	0.5	1.7	3.4	7.6	9.2	3.1
Credit to private sector	4.3	6.9	3.5	4.3	6.0	4.4
Credit to private sector (change in percent)	35.0	45.9	17.9	20.2	25.8	18.0
Credit to private sector (in percent of GDP)	11.7	14.5	14.9	15.1	15.0	18.3
	(In billions of U.S. dollars, unless otherwise indicated)					
Balance of payments						
Current account balance	-0.4	-0.6	-0.9	-1.4	-2.3	-1.9
(in percent of GDP)	-1.6	-2.2	-2.8	-3.3	-4.1	-3.7
Overall oil balance 1/	1.3	0.7	0.0	-1.0	-2.1	-1.3
(in percent of GDP)	5.3	2.1	0.0	-2.4	-2.6	-2.7
Non-oil exports of goods and services	6.4	7.7	9.1	11.2	13.5	14.2
(change in percent)	99.2	20.4	18.6	23.5	20.2	5.1
Non-oil imports of goods and services	-9.3	-10.4	-11.9	-13.8	-15.6	-16.7
(change in percent)	20.8	12.5	13.9	16.2	13.2	7.0
Overall balance	0.2	0.0	-0.8	0.7	-0.4	0.3
Official net foreign assets	17.6	17.6	16.8	17.5	17.1	17.5
(in months of imports of GNFS)	20.2	16.4	13.7	11.6	9.4	10.5
Weighted average nominal exchange rate LS/$ 2/	50.5	52.2	51.0	49.9	46.5	…
Real effective exchange rate (in percent, + appreciation) 3/	0.0	1.7	10.7	4.9	9.0	…

Sources: Syrian authorities; and Fund staff estimates and projections.

1/ Oil trade balance less profit of foreign oil companies.

2/ Trade-weighted average of official and parallel market rates before 2007. For 2008 data are for July.

3/ For 2008 data are for the first three quarters.

Table 2a. Syrian Arab Republic: Summary of Fiscal Operations, 2004–09 1/
(In percent of GDP)

	2004	2005	2006	Budget 2007	Prel. 2007	Budget 2008	2008	Proj. 2009
Revenue	27.2	24.0	25.5	24.9	22.3	15.9	21.4	21.8
Oil	11.2	7.1	7.3	11.7	4.9	3.5	4.7	4.2
Non-oil	15.9	16.8	18.2	13.2	17.3	12.4	16.7	17.6
Tax	11.5	10.7	11.6	7.4	10.8	8.3	10.3	11.2
Income and profits	4.7	4.0	3.8	3.3	3.5	3.2	3.5	3.6
International trade	2.5	2.1	1.9	0.9	1.5	1.0	1.1	1.2
Other indirect taxes	4.4	4.7	5.9	3.1	5.8	4.2	5.7	6.4
Non-tax	4.4	6.0	6.5	5.8	6.5	4.0	6.4	6.4
Public enterprises surpluses	3.8	5.1	6.0	5.1	6.2	3.6	6.0	6.0
Other	0.7	1.1	0.5	0.8	0.4	0.5	0.4	0.4
Expenditure	31.4	28.5	26.6	28.2	25.7	22.2	24.9	25.0
Current expenditure	19.0	18.1	16.3	15.5	16.1	13.2	15.4	15.5
Defense	5.9	5.3	4.1	3.5	3.5	2.9	3.5	3.5
Wages and salaries	5.5	5.3	5.5	5.0	4.9	4.4	4.8	4.6
Goods and services	1.5	1.4	1.3	1.2	1.2	1.0	1.1	1.3
Interest payments	0.9	1.2	1.0	0.9	0.9	0.6	0.6	0.6
Subsidies	2.4	2.3	2.3	2.2	2.6	1.9	2.3	2.5
Transfers	2.8	2.7	2.1	2.8	3.0	2.3	3.0	3.0
Pensions & Social Assistance	1.1	1.1	1.1	1.1	1.0	1.0	1.0	1.0
Transfers to Public Enterprises	1.7	1.6	1.0	1.7	2.0	1.3	2.0	2.0
Development expenditure	12.4	10.4	10.3	12.7	9.6	9.0	9.5	9.5
Overall balance	-4.2	-4.5	-1.2	-3.3	-3.4	-6.3	-3.5	-3.1
Of which: Non-oil balance	-15.4	-11.6	-8.5	-15.0	-8.4	-9.8	-8.2	-7.3
Identified Financing	3.7	5.4	3.6	-0.3	2.3	-0.3	3.5	3.1
External	0.1	0.2	-0.7	-0.3	-0.5	-0.3	0.9	0.8
Domestic bank financing	2.8	4.6	4.8	...	2.8	...	2.5	2.2
Unidentified Financing	0.5	-0.9	-2.5	...	1.1	...	0.0	0.0
Memorandum items:								
Government debt 2/	82.7	35.9	36.0	...	28.9	...	22.0	23.6
Domestic	9.4	12.6	16.8	...	14.4	...	11.7	11.5
External 2/	73.3	23.4	19.2	...	14.5	...	10.4	12.1

Sources: Ministry of Finance; and staff estimates and projections.

1/ Central government budget and Price Stabilization Fund (PSF).
2/ Most of the decline in 2005 is due to the restructuring of the old Soviet era debt in late 2004 to early 2005.

Table 2b. Syrian Arab Republic: Summary of Fiscal Operations, 2004–09 1/
(In billions of Syrian pounds)

	2004	2005	2006	Budget 2007	Prel. 2007	Budget 2008	Proj. 2008	Proj. 2009
Revenue	343.9	358.0	435.3	504.2	450.7	408.4	549.2	540.3
Oil	141.2	106.2	124.7	236.2	100.2	90.3	120.7	104.0
Non-oil	201.3	250.1	310.2	267.5	350.0	317.5	428.0	435.6
Tax	145.4	160.3	198.6	149.7	217.9	214.1	264.1	277.5
Income and profit	59.1	59.3	65.0	67.4	70.8	81.2	89.8	88.9
International trade	31.3	30.7	32.9	18.9	29.6	25.9	27.1	30.2
Other indirect taxes	55.0	70.3	100.7	63.4	117.5	107.1	147.1	158.4
Non-tax	55.9	89.9	111.6	117.8	132.0	103.4	163.9	158.1
Public enterprise surpluses	48.0	75.9	103.1	102.3	124.6	91.2	155.1	149.6
Other	9.3	15.8	8.9	16.1	7.5	12.8	9.5	9.2
Expenditure	396.9	424.5	455.2	571.4	520.5	568.9	639.3	618.0
Current expenditure	240.3	270.1	278.7	313.4	325.7	338.9	395.4	382.7
Defense	74.7	78.7	69.4	70.3	70.3	74.4	89.3	86.2
Wages and salaries	69.5	78.3	94.6	100.7	99.3	114.2	123.4	113.1
Goods and services	19.3	21.5	22.5	23.5	24.3	26.4	29.4	33.3
Interest payments	11.0	17.4	17.9	18.1	18.1	16.5	16.5	15.1
Subsidies	29.8	33.6	38.5	44.4	52.1	47.8	58.8	61.5
PSF expenditure	27.0	29.6	33.9	33.7	30.4	36.8	36.8	40.8
Other subsidies	2.8	4.0	4.6	10.7	21.8	11.0	22.1	20.6
Transfers	36.0	40.5	35.8	56.5	61.6	59.7	78.0	73.6
Pensions & social assistance	14.4	16.3	19.0	22.8	21.3	25.9	26.8	24.3
Transfers to Public Enterprises	21.6	24.3	16.8	33.8	40.3	33.8	51.1	49.3
Development expenditure	156.6	154.4	176.5	258.0	194.8	230.0	243.9	235.3
Overall balance	-53.0	-66.4	-19.9	-67.2	-69.8	-160.5	-90.1	-77.7
Of which: Non-oil balance	-194.1	-172.6	-144.6	-303.4	-170.0	-250.8	-210.8	-181.7
Identified Financing	47.0	79.8	62.3	-5.5	47.4	-6.6	90.1	77.7
External	1.3	3.2	-12.6	-5.5	-10.3	-6.6	22.5	19.4
Domestic financing	35.3	68.5	82.9	...	57.7	...	63.1	54.4
Unidentified Financing	6.0	-13.4	-42.4	...	22.4	...	0.0	0.0
Memorandum items:								
Government debt 2/	1,044.5	535.9	615.1	...	585.1	...	565.8	584.8
Domestic	118.9	187.3	287.2	...	291.2	...	299.3	285.5
External 2/	925.6	348.6	327.9	...	293.9	...	266.6	299.4

Sources: Ministry of Finance; Central Bank of Syria; and Fund staff estimates and projections.

1/ Central government budget and Price Stabilization Fund (PSF).

2/ Most of the increase in 2005 is due to the restructuring of the old Soviet era debt in late 2004 to early 2005.

Table 3. Syrian Arab Republic: Monetary Survey, 2004–09

	2004	2005	2006	Prel. 2007	Proj. 2008	Proj. 2009
	(In billions of Syrian pounds)					
Foreign assets (net)	750	757	731	707	894	973
Central bank	136	144	148	190	382	408
Commercial banks	614	613	583	517	511	565
Domestic assets (net)	238	345	473	616	681	807
Domestic credit	410	555	635	740	931	1,104
Claims on public sector	263	340	381	434	547	650
Central government (net)	80	141	144	106	97	152
Public enterprises	182	199	237	328	449	499
Claims on private sector	148	215	254	305	384	453
Other items (net)	-172	-211	-161	-123	-250	-297
Broad money	988	1,101	1,205	1,323	1,575	1,780
Money	602	688	687	732	916	904
Currency outside banks	333	385	399	422	503	568
Demand deposits	269	304	288	309	413	336
Quasi-money	386	413	517	592	659	875
	(12-month change in percent)					
Broad money	11.1	11.5	9.4	9.8	19.0	13.0
Money	11.2	14.4	-0.1	6.4	25.2	-1.3
Quasi-money	11.1	7.0	25.2	14.4	11.4	32.8
Net claims on government	45.1	75.5	2.3	-26.1	-8.3	55.8
Claims on public enterprises	2.7	9.2	18.8	38.5	37.0	11.0
Claims on private sector	35.0	45.9	17.9	20.2	25.8	18.0
	(Change in percent of the initial stock of broad money)					
Net foreign assets 1/	5.4	0.7	-2.3	-2.0	3.7	2.2
Domestic assets (net)	5.8	10.8	11.7	11.9	15.3	10.8
Domestic credit	7.6	14.7	7.2	8.7	14.5	11.0
Central government (net)	2.8	6.1	0.3	-3.1	-0.7	3.5
Public enterprises (net)	0.5	1.7	3.4	7.6	9.2	3.1
Private sector	4.3	6.9	3.5	4.3	6.0	4.4
Other items (net)	-1.9	-3.9	4.5	3.2	0.9	-0.1

Sources: Central Bank of Syria; and Fund staff estimates and projections.
1/ For 2008 includes valuation effects.

Table 4. Syrian Arab Republic: Balance of Payments, 2004–13
(In millions of U.S. dollars; unless otherwise indicated)

			Est.	Prel.	Proj.					
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Current account balance	-396	-632	-923	-1,352	-2,254	-1,895	-2,019	-2,271	-2,471	-2,762
(In percent of GDP)	*-1.6*	*-2.2*	*-2.8*	*-3.3*	*-4.1*	*-3.7*	*-3.7*	*-3.8*	*-3.9*	*-4.0*
Goods	-878	-1,270	-1,693	-2,825	-3,061	-3,403	-3,533	-4,001	-4,518	-5,169
Exports, f.o.b.	7,155	9,035	10,224	11,713	14,597	12,251	13,668	15,629	17,619	20,008
Oil	3,406	4,286	4,062	4,355	5,630	2,914	2,539	2,404	1,770	1,035
Nonoil	3,749	4,749	6,162	7,358	8,967	9,338	11,129	13,225	15,849	18,973
Imports, f.o.b.	-8,033	-10,305	-11,917	-14,538	-17,657	-15,654	-17,201	-19,630	-22,137	-25,178
Oil	-1,156	-2,473	-2,884	-4,250	-6,283	-3,424	-4,110	-4,473	-4,688	-4,858
Nonoil	-6,877	-7,832	-9,033	-10,288	-11,375	-12,230	-13,091	-15,157	-17,449	-20,319
Services	228	327	93	366	286	360	519	807	1,092	1,364
Receipts	2,613	2,912	2,924	3,861	4,518	4,831	5,214	5,715	6,364	7,093
Travel and tourism	1,800	1,944	2,025	2,883	3,460	3,736	4,035	4,439	4,971	5,568
Freight and insurance	198	219	217	226	275	287	342	406	487	583
Government services	270	350	275	300	312	322	334	347	361	376
Other services	345	398	407	452	470	486	503	523	544	567
Payments	-2,385	-2,585	-2,831	-3,495	-4,232	-4,471	-4,695	-4,908	-5,272	-5,730
Income	-729	-975	-935	-689	-1,104	-359	-396	-446	-413	-368
Credit	385	395	428	594	649	713	785	863	950	1,045
Debit	-1,114	-1,370	-1,363	-1,283	-1,753	-1,072	-1,181	-1,309	-1,363	-1,412
Oil companies' profits	-931	-1,200	-1,165	-1,085	-1,494	-807	-881	-983	-1,005	-1,018
Transfers	984	1,286	1,612	1,796	1,624	1,506	1,390	1,369	1,369	1,411
Workers' remittances	689	761	610	831	839	881	925	1,064	1,224	1,346
Capital and financial account balance	288	669	-586	1,019	1,899	2,238	2,315	3,100	3,627	4,032
Capital account (migrants' transfers)	18	18	18	118	50	20	20	20	20	20
Direct investment	427	776	875	1,143	2,116	2,211	2,288	3,073	3,600	4,005
Long-term government debt	27	64	-252	-206	-158	398	327	389	495	520
Other	-185	-189	-1,227	-36	-108	-391	-320	-382	-488	-514
Errors and omissions	310	-19	756	1,004	0	0	0	0	0	0
Overall balance	202	18	-753	671	-355	343	296	829	1,156	1,269
Financing	-202	-18	753	-671	355	-343	-296	-829	-1,156	-1,269
Convertible	-9	-479	754	-643	355	-413	-296	-829	-1,156	-1,269
Central Bank	-271	-1,200	-539	-2,143	177	-207	-148	-415	-578	-635
Commercial Bank of Syria	263	721	1,293	1,500	177	-207	-148	-415	-578	-635
Nonconvertible (Central Bank)	-193	461	-1	-27	0	70	0	0	0	0
Memorandum items:										
NFA of the Central Bank and CBoS	17,567	17,585	16,831	17,474	17,119	17,533	17,829	18,658	19,814	21,084
(In months of imports of GNFS)	20.2	16.4	13.7	11.6	9.4	10.5	9.8	9.1	8.7	8.2
Oil balance (in percent of GDP) 1/	5.3	2.1	0.0	-2.4	-2.6	-2.7	-4.7	-5.2	-6.2	-7.5

Sources: Central Bank of Syria; and staff estimates and projections.
1/ Oil trade balance less profits of foreign companies.

Table 5. Syrian Arab Republic: Medium-Term Macroeconomic Framework, 2004–13

				Prel.	Proj.					
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
	(Change in percent, unless otherwise indicated)									
National income and prices										
Real GDP	6.7	4.5	5.1	4.2	5.2	3.9	3.3	5.3	5.2	5.7
Oil	-6.1	-8.6	-7.1	-5.0	-0.1	-2.6	-9.5	1.2	-2.9	-3.0
Non-oil	10.2	7.5	6.9	5.8	6.0	4.7	4.7	5.5	6.0	6.5
Nominal GDP (LS billions)	1,263	1,491	1,709	2,025	2,567	2,477	2,739	3,037	3,338	3,682
Of which: Non-oil	986	1,134	1,305	1,558	1,886	2,131	2,366	2,622	2,918	3,262
Nominal GDP ($ billions)	25.0	28.6	33.5	40.6	55.2	50.7	54.4	59.1	63.6	68.8
Crude oil production ('000 barrels/day)	462	431	400	380	380	370	335	339	329	319
Oil export price ($ per barrel)	33.5	48.1	57.6	65.3	90.0	48.9	58.6	64.4	67.8	70.1
CPI period average	4.4	7.2	10.4	4.7	14.5	8.0	6.0	5.0	5.0	5.0
Government finances 1/	(In percent of GDP, unless otherwise indicated)									
Revenue	27.2	24.0	25.5	22.3	21.4	21.8	21.5	21.2	20.7	20.8
Oil-related revenue	11.2	7.1	7.3	4.9	4.7	4.2	3.9	3.6	3.0	3.0
Non-oil revenue	16.1	16.9	18.2	17.3	16.7	17.6	17.6	17.6	17.7	17.8
Expenditure	31.4	28.5	26.6	25.7	24.9	25.0	23.9	23.9	23.8	23.8
Current expenditure	19.0	18.1	16.3	16.1	15.4	15.5	15.4	15.4	15.3	15.3
Development expenditure	12.4	10.4	10.3	9.6	9.5	9.5	8.5	8.5	8.5	8.5
Overall balance	-4.2	-4.5	-1.2	-3.4	-3.5	-3.1	-2.4	-2.6	-3.1	-3.0
Non-oil budget balance	-15.4	-11.6	-8.5	-8.4	-8.2	-7.3	-6.3	-6.2	-6.1	-6.0
Gross public debt 2/	82.7	35.9	36.0	28.9	22.0	23.6	23.6	23.5	24.8	25.8
Domestic	9.4	12.6	16.8	14.4	11.7	11.5	11.7	11.9	13.2	14.2
External 2/	73.3	23.4	19.2	14.5	10.4	12.1	11.9	11.7	11.7	11.6
Saving/investment balances										
Consumption	78.8	79.8	79.8	81.4	78.1	76.6	77.6	76.0	75.3	75.0
Public	13.8	12.8	11.6	10.2	10.0	10.0	9.9	8.1	8.1	8.1
Private	65.0	67.1	68.2	71.2	68.0	66.6	67.7	67.9	67.2	66.9
Gross capital formation	23.8	23.5	25.0	24.6	27.0	29.3	27.9	29.4	30.1	30.4
Public	11.2	11.1	11.1	10.4	10.2	10.2	9.1	9.1	9.1	9.1
Private	12.6	12.3	13.8	14.3	16.8	19.1	18.8	20.2	20.9	21.3
Gross savings	22.2	21.3	22.2	21.3	22.9	25.7	24.2	25.6	26.2	26.5
Saving/investment gap	-1.6	-2.2	-2.8	-3.3	-4.1	-3.7	-3.7	-3.8	-3.9	-4.0

Sources: Syrian authorities; and Fund staff estimates and projections.

1/ Including the Price Stabilization Fund and a broad coverage of public enterprises.
2/ The sharp decline in 2005 is due to the rescheduling of the old soviet debt that took place in early 2005.

Table 6. Syrian Arab Republic: Financial Soundness Indicators of the Banking Sector, 2006-08 1/

	2006			2007			June-08		
	Consolidated	Public	Private	Consolidated	Public	Private	Consolidated	Public	Private
Capital Adequacy									
Regulatory capital to risk-weighted assets	...	...	...	...	...	16.4	...	...	12.9
Regulatory tier I capital to risk-weighted assets	...	...	...	...	...	16.4	...	...	12.9
Capital to assets	7.0	7.0	6.9	6.5	6.5	6.4	...	3.5	8.0
Asset Composition and Quality									
Sectoral distribution of loans to total loans									
Agriculture	16.7	18.0	0.1	15.7	17.4	0.1	12.7	14.4	0.6
Mining, Manufacturing, and Utilities	8.1	6.8	24.9	8.0	4.0	16.3	5.5	3.4	19.5
Building and Construction	14.4	15.4	2.4	13.9	15.6	4.3	13.7	15.3	3.2
Wholesale and Retail Trade	41.3	41.4	40.1	41.7	47.7	44.3	53.8	55.6	41.2
Other Activities	19.5	18.5	32.4	20.7	15.3	35.1	14.3	11.3	35.5
Non-performing loans to total loans	4.7	5.0	1.0	5.3	5.9	1.0	…	…	0.9
Specific provisions to gross non performing loans	61.0	61.3	41.7	23.7	22.0	92.0	…	…	67.1
Non performing loans net of provisions to Tier I capital	6.3	6.8	1.5	14.4	16.1	0.3	20.0	24.3	1.2
Large exposures to Tier I capital	...	...	...	53.2	44.2	127.1			
Specific provisions to gross loans	2.9	3.1	0.4	1.3	1.3	0.9	1.2	1.3	0.6
Profitability									
Return on average assets (ROAA)	2.0	2.3	0.3	2.4	2.8	0.5	0.8	86.3	32.9
Return on average equity (ROAE)	19.6	21.2	3.9	23.9	26.1	7.7	17.2	20.1	455.4
Net interest margin to gross income	41.8	40.1	85.9	77.3	77.2	78.2	86.3	86.8	83.2
Non-interest income to gross income	22.7	22.7	22.7	22.7	22.8	21.8	14.2	13.2	20.1
Non-interest expenses to gross income	36.4	35.3	63.7	18.3	13.9	56.2	10.5	5.4	41.1
Non-interest expenses to average assets	1.8	1.9	0.9	0.6	0.5	1.1	0.1	0.1	0.5
Liquidity									
Liquid assets to total assets	59.6	57.7	73.4	44.1	38.9	70.1	19.8	17.0	39.9
Liquid assets to short term liabilities	102.2	103.7	95.0	59.6	54.1	82.6	59.6	63.4	50.3
FX- loans to total loans	1.5	0.8	10.2	2.5	1.5	9.7	2.6	1.0	12.6
FX- deposits to total deposits	19.3	11.8	54.0	20.4	12.0	49.4	19.6	11.4	41.4
FX- liabilities to total liabilities	37.7	35.8	50.8	47.9	47.4	50.0	31.9	30.7	40.2
Deposits to assets	57.2	53.7	80.8	57.0	52.9	77.5	60.7	55.5	81.4
Loans to deposits	61.0	69.2	23.5	62.0	70.3	33.6	86.6	75.7	35.0
FX- loans to FX-deposits	4.6	4.8	4.4	7.6	8.8	6.6	5.7	6.5	5.4
Sensitivity to Market Risk									
Net open FX position (overall) as percent of Tier I capital	225.0	241.3	64.8	138.1	145.0	80.7	10.9	0.1	57.5

Source: Central Bank of Syria.

1/ Financial Soundess Indicators need to be interpreted with caution due to persisting deficiencies in banks' implementation of International Financial Reporting Standards, their audit practices, and reporting standards.

Table 7. Syrian Arab Republic: Structure of the Financial System, 2007–08

	Dec-07				Jun-08			
	Number	Total assets (in billions)	In % of total	In % of GDP	Number	Total assets (in billions)	In % of total	In % of GDP
Banks	22	1,593	100	79	22	1,634	100	64
Public Sector Banks	6	1,299	82	64	6	1,298	79	51
Commercial	1	842	53	42	1	830	51	32
Specialized	5	457	29	23	5	468	29	18
Domestic Private Banks	9	290	18	14	9	331	20	13
Islamic Banks	2	19	1	1	2	34	2	1
Free Economic Zone Bank	7	4	0	0	7	5	0	0
Insurance Companies	…	…	…	…	…	…	…	…
Total Financial System	22	1593	100	79	22	1634	100	64

Sources: Authorities; and staff calculations.

INTERNATIONAL MONETARY FUND

SYRIAN ARAB REPUBLIC

Staff Report for the 2008 Article IV Consultation—Informational Annex

Prepared by The Middle East and Central Asia Department
(in consultation with other departments)

December 19, 2008

Contents Page

Appendix I. Syrian Arab Republic: Relations with the Fund

(As of October 31, 2008)

I. Membership Status: Joined April 10, 1947; Article XIV

II. General Resources Account:	**SDR Million**	**Percent of Quota**
Quota[8]	293.60	100.00
Fund holdings of currency	293.60	100.00
Reserve position in Fund	0.01	0.00

III. SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	36.56	100.00
Holdings	36.57	100.03

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements: None

VI. Projected Obligations to Fund: (SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2008	2009	2010	2011	2012
Charges/Interest	0.00	0.00	0.00	0.00	0.00
Total	0.00	0.00	0.00	0.00	0.00

VII. Exchange Rate Arrangement

The Central Bank of Syria issues on a daily basis quotations for the buying and selling exchange rates for the Syrian pound against major currencies. The official budget exchange rate, which was applied to all public sector transactions, was pegged to the U.S. dollar until end-December 2006. Since the abolition of the official “budget” rate on January 1, 2007 and its unification with the private sector exchange rate, the central bank has been managing the value of the currency vis-à-vis the U.S. dollar within a tight trading range. The authorities switched the reference currency from the U.S. dollar to the SDR in August 2007. The *de facto* exchange rate arrangement is classified as a peg to a basket.

[8] Under the Eleventh General Review.

VIII. Article IV Consultations

Syria is on an annual consultation cycle. The last Article IV consultation was held in April/May 2007 and was completed by the Board on July 31, 2007 (CR/07/288).

IX. Article XIV and Article VIII Restrictions

Syria continues to maintain, under Article XIV, restrictions on payments and transfers for current international transactions, including administrative allocation of foreign exchange. Syria also maintains exchange measures that are subject to Fund approval under Article VIII: (i) prohibition against purchases by private parties of foreign exchange from the banking system for some current international transactions; (ii) a multiple currency practice resulting from divergences of more than 2 percent between the official exchange rate and officially recognized market exchange rates; (iii) a non-interest-bearing advance import deposit requirement of 75–100 percent for public sector imports; and (iv) an exchange restriction arising from the net debt under inoperative bilateral payments arrangements with the Islamic Republic of Iran, and Sri Lanka.

The Executive Board adopted decision No. 13958 (07/67) at the Board meeting on July 31, 2007:

38. The Fund takes this decision relating to the Syrian Arab Republic's exchange measures subject to Article VIII, Sections 2(a) and 3, and in concluding the 2006 Article XIV consultation with the Syrian Arab Republic, in light of the 2006 Article IV consultation with the Syrian Arab Republic conducted under Decision No. 5392-(77/63), adopted April 29, 1977, as amended (Surveillance over Exchange Rate Policies).

39. The Syrian Arab Republic maintains restrictions on the making of payments and transfers for current international transactions in accordance with Article XIV, Section 2, as described in CR/06/294. In addition, as described in CR/06/294, the Syrian Arab Republic maintains exchange measures subject to approval under Article VIII. The Fund encourages the Syrian Arab Republic to eliminate the restrictions maintained under Article XIV, Section 2 as soon as its balance of payments position permits, and to eliminate the measures that are subject to approval under Article VIII as soon as possible. (CR/07/288).

X. Technical Assistance

Department	Topic	Date
METAC	Central Bank Accounting	Ongoing
FAD	Tax administration	July 2008
STA	Multi-Sector Statistics (National Accounts, Fiscal, Monetary, and Balance of Payments)	December 2007
MCM	Strategic Planning at the Central Bank of Syria and New Central Bank Law	November 2006
FAD	Public Financial Management	February 2006
METAC	Revenue Administration	Ongoing
METAC	Consumer Price Index	Ongoing
MFD	Long-Term Advisors on Central Bank Accounting, Reserves Management, and Monetary Policy Issues	Ongoing
MFD	Foreign Exchange Market Development, Unification and Exchange Regime	January 2006
LEG/MFD	AML/CFT outreach training	December 2005
MFD	Long-Term Advisor on Securities Market	September 2005
MFD	Centralization of Official Foreign Reserves and Associated Accounting, Reserves and Public Debt Management Issues	September 2005
METAC	National Accounts	Ongoing
	Bank Regulation and Supervision	Ongoing
MFD	Re-organization of the Central Bank of Syria	May 2005
FAD	Revenue Administration	March 2005
LEG/MFD	AML/CFT legal drafting	Feb/March 2005
STA	Multi-Sector Statistics (National Accounts, Fiscal, Monetary, and Balance of Payments)	June 2004
FAD	Value-Added Tax	July 2004
MAE	Two Long-Term Advisors on Bank Regulation and Supervision	2002–04
MAE	Two-Day Workshop on On-Site Banking Supervision	July 2002
MAE	Workshop on Off-Site Banking Supervision	March 2002

ANNEX II. SYRIAN ARAB REPUBLIC: RELATIONS WITH THE WORLD BANK GROUP[9]

(End-August 2008)

Syria joined the World Bank in 1947. Between 1963 and 1974, IDA approved four credits for Syria totaling $48.6 million. Following Syria's graduation from IDA in 1974, IBRD approved 15 loans during the period 1974-86. In 1986 Syria ceased debt service payments to the Bank, which prompted a suspension of Bank disbursements. Following several rounds of negotiations with the Bank, by July 1, 2002, Syria settled all its overdue service payments to IBRD and IDA, thereby reinstating the country's eligibility for disbursement.

There is currently no World Bank Country Assistance Strategy (CAS) for Syria. A Memorandum of Understanding (MoU) covering the period 2005-07 provided the framework for the Bank's program of advisory and analytical (AAA) services. The MoU allowed the Bank to support reforms in areas of economic growth and transition, along with human development and social protection. Activities have included, among others: (i) advise on restructuring public banks and establishing a government securities market; (ii) FIAS support provided in reviewing the recently adopted Investment Law; and (iii) analytical work on energy subsidies and advise on drafting a Basic Finance Law and improving public financial management.

The Syrian authorities have expressed interest in World Bank Group technical and advisory services in three areas: (i) economic growth and transition support; (ii) human development and social protection; and (iii) improving the environment for sustainable development. Based on preliminary discussions with the Syrian authorities, Bank assistance would take the form of analytical and advisory services focusing on the following themes:

- *Economic Growth and Transition Support.* Trade reform; fiscal sustainability; price liberalization; sources of non-oil growth; private sector development and business environment.

- *Human Development and Social Protection*. Enhancing policymaking and implementation capacity in social protection; support to avian influenza preparedness; reform options for social insurance; and education sector strategy.

[9] World Bank TA mission focusing on trade, fiscal issues, and the development of a SAM for Syria will overlap with the 2008 Article IV Consultation mission, facilitating Bank-Fund coordination.

- *Sustainable Development*. Electricity sector strategy; agriculture sector reform; solid waste technical assistance; water and wastewater technical assistance; and transport sector technical assistance.

IFC has been active in Syria since 1999 when the Board approved the corporation's first investment in the country—a $1 million equity stake in a manufacturer of drip irrigation systems. Since that time, IFC has made two other investments, including an equity position in the first private sector bank in Syria and a loan to a chemicals company. The total held portfolio is $20 million. IFC has also conducted technical assistance work, including studies of aspects of the financial sector.

ANNEX III. SYRIAN ARAB REPUBLIC: STATISTICAL ISSUES

1. Data provision has serious shortcomings that significantly hamper surveillance. The weak statistical infrastructure has been unable to cope with the acceleration of structural reforms, and the inherent difficulties in recording the flows of people, goods, and money to and from Iraq have added to this challenge. The staff's assessment of economic developments and policies is constrained by these circumstances. In the context of Article IV missions, the authorities have expressed an intention to improve the statistical system. With the assistance of the 2007 multisector statistics mission, Syria began participating in the General Data Dissemination System (GDDS) in December 2007, and the plans for improving the statistical system are posted on the Fund's Dissemination Standards Bulletin Board.

A. Real Sector Statistics

2. Annual national accounts by expenditure data are reported for publication in the *International Financial Statistics (IFS)* with about 2-years lag. In addition, significant weaknesses remain in the source data and statistical techniques for national accounts statistics.

3. A STA-resident statistics advisor has been in place since July 2008 to help implement the recommendations of the December 2007 STA multisector mission in the area of national accounts. During the past two years, METAC has also provided technical assistance for improving data sources and methods for the compilation of national accounts statistics in accordance with the *System of National Accounts, 1993* (*1993 SNA*). Guidance has also being provided for using existing data for improving gross domestic product (GDP) estimates at current and constant prices and for the appropriate treatment in the national accounts of implicit subsidies to some public enterprises. The Central Bureau of Statistics (CBStat) made a steady progress for implementing recommendations made by the technical assistance missions. Economic surveys covering private sector enterprises had been conducted for years 2004–06. The central purpose of these surveys was to serve as main data source for improving national accounts statistics in accordance with the *1993 SNA*; however, the results are yet to be fully processed and validated.

B. Government Finance Statistics

4. Government finance statistics (GFS) suffer from major deficiencies with respect to definitions, coverage, classification, methodology, accuracy, reliability, and timeliness that generate severe inconsistencies with monetary and balance of payments statistics. Fiscal statistics are not provided for publication in the *IFS*. The multisector mission of June 2004 found that compilation is adversely affected by cumbersome institutional arrangements, inadequate resources, and unresolved methodological problems. The methodology used for compilation does not follow either *GFSM 2001* or *GFSM 1986*. While budget data are available with very long lags (two years for final budget accounts), financing data are not available. There is no dissemination of GFS data, and even access to key data sources by GFS compilers within the Ministry of Finance (MOF), such as the breakdown of debt service into interest and amortization, is problematic. This contributes to discrepancies in external financing as reported in the budget and the balance of payments statistics.

5. The largest, most persistent and volatile discrepancies, are between the financing requirements of the budget, as reported by the MOF, and government financing as reported by the Central Bank of Syria (CBS). The lack of a common and regularly updated coverage of the government sector between the MOF and the CBS, misclassification of public enterprises investment expenditure, as well as timing and valuation issues, are mainly responsible for those discrepancies.

6. Other discrepancies between fiscal and monetary accounts relate to the unorthodox treatment by the CBS of some transactions with government, such as the parallel rise of government deposits and claims on government in the CBS balance sheet, which is likely due to government withdrawals being counted as credit and never netted out against deposits, and profits transferred to government treated as permanent claim on the government.

7. To address the methodological issues, the June 2004 multisector mission developed a preliminary bridge table that maps the budgetary source data codes to the GFSM 2001 classification codes, and conducted a seminar to clarify various aspects of the GFSM 2001 methodology to the MOF officials. To help the Directorate of Planning and Statistics (DPS) implement a proper sectorization scheme, the mission provided an updated institutional table showing the current coverage of government and public enterprises—the investment expenditure of public enterprises is included in government's capital expenditure—for circulation to all relevant agencies. Moreover, the mission formulated a detailed work plan centered around the provision of adequate resources and training for the DPS to fulfill its tasks. The work plan calls for the DPS to access core source data necessary for compilation—initially on a cash basis—of annual GFS data according to the *GFSM 2001*, and for the resumption of data reporting to STA for publication in *GFSY* and *IFS*, together with improved reporting, in terms of coverage and classification, to the IMF's Middle East and Central Asia Department (MCD). The mission also recommended improvement in the timeliness of annual data, including data on financing, and a start on the compilation of sub-annual data.

C. Monetary and Financial Statistics

8. Monetary statistics suffer from major deficiencies which hamper the staff's ability to conduct meaningful analysis of monetary developments. Monthly monetary statistics are reported for publication in the *IFS* with about 10-month lags, falling short of recommended dissemination practices under the GDDS of 3-month lags. Progress has been made in addressing some issues identified by the multisector statistics mission in June 2004, namely including in the monetary survey the private banks, the Savings Bank, and banks/bank branches operating in the Free Zones. Although the format of monetary statistics is largely consistent with the structure of the *MFSM*-recommended sectoral surveys, there are deficiencies in the source data arising from, inter alia, (i) the use of different exchange rates at the CBS and at the other banks for valuing their foreign-currency positions; (ii) financial positions are not valued at market prices or market-price equivalents; (iii) a number of accounting procedures for the maintenance of public sector accounts cause distortions in the measurement of gross positions; and (iv) there are disparities between the institutional coverage of public sector in monetary statistics and the government finance statistics.

9. A technical assistance mission during November–December 2008 worked with the authorities on developing data reporting based on the Standardized Report Forms (SRFs), which reflect the *MFSM*-recommended compilation principles. The mission's work was underpinned by detailed data recently provided by the authorities.

D. External Sector Statistics

10. Balance of payments statistics are compiled by the CBS on a provisional basis. Trade data are compiled monthly by the Customs Department and reported quarterly by the CBStat in local currency units with a six-month lag. The BOP is presented in *BPM5* format, but its compilation method is not entirely consistent with the *BPM5* methodology.

11. In February 2006, a STA assessment mission assessed the status of the work program as a basis for developing a METAC technical assistance program on external sector statistics. In December 2007, STA conducted a multisector statistics mission in collaboration with METAC and follow-up METAC missions took place in January and July 2008.

12. In September 2008, a STA inspection visit followed up on the recommendations of the 2007 multisector mission and METAC's work program and discussed the reporting and publication of data on international liquidity for *IFS*, which has been an outstanding issue for over three years.

13. Regarding the balance of payments, the mission found that the CBS had made progress in improving source statistics through surveys and International Transactions Reporting System (ITRS), by adopting appropriate classifications, and improving consistency with other data sets. The CBS's new organizational structure is designed to include a balance of payments division

of five staff (currently two staff are assigned to BOP work but plans are in place to fully staff the division).

14. The October 2008 STA balance of payments statistics mission worked to provide advice on international reserves, trade data, and the treatment of Iraqi immigrants was provided, to the extent possible. Data for 2007 were adjusted where needed and the mission assisted the CBS staff to compile January-July 2008 balance of payments in *BPM5* format.

15. Despite recent progress, further efforts are needed to improve the accuracy of the BOP data to meet data needs for surveillance purposes, in particular; (i) continue **data collection initiatives** (ITRS and surveys) that have been developed with a view to strengthening source data, and ensuring coverage of free zones, (ii) improve the undercoverage of **imports**, (iii) examine the scope of **transfers**, including the treatment of inflows related to Iraqi immigrants, (iv) review the coverage of **reserves** , and (iv) improve the coverage of **financial account data of the private sector** (bank and nonbank).

16. The authorities have made some progress in the compilation of international merchandise trade statistics. The Customs Department has adopted Automated System for Customs Data (ASYCUDA) as its operating system and is presently implementing it and a Statistical Committee on Foreign Trade Statistics has been formed to assist with trade methodology. However, significant weaknesses remain in the source data and statistical techniques for foreign trade statistics.

SYRIAN ARAB REPUBLIC: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

As of November 20, 2008

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of publication[7]
Exchange Rates	Nov. 19, 2008	Nov. 20, 2008	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Feb. 2006	Mar. 2006	M	Q	M
Reserve/Base Money	Dec. 2007	Aug. 2008	M	Q	M
Broad Money	Dec. 2007	Oct. 2008	M	Q	M
Central Bank Balance Sheet	Dec. 2007	Aug. 2008	M	Q	M
Consolidated Balance Sheet of the Banking System	Dec.2007	Oct. 2008	M	Q	M
Interest Rates[2]	Sep. 2008	Oct. 2008	M	Q	M
Consumer Price Index	Sep. 2008	Oct. 2008	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2007	Oct. 2008	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	2007	Oct. 2008	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2007	Oct. 2008	A	A	A
External Current Account Balance	2007	Oct. 2008	A	A	A
Exports and Imports of Goods and Services	Jun. 2008	Oct. 2008	Q	Q	Q
GDP/GNP	2007	Oct. 2008	A	A	A
Gross External Debt	2007	Oct. 2008	A	A	A
International Investment Position[6]	NA	NA	NA	NA	NA

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); Weekly (W); Monthly (M); Bi-monthly (B); Quarterly (Q); Annually (A); Irregular (I); Not available (NA).

Statement by the IMF Staff Representative
January 9, 2009

1. The following information has become available since the staff report was issued. It does not change the thrust of the staff appraisal.

2. On December 1, 2008, the authorities increased the domestic price of fuel oil by 46 percent, which is a larger increase than the initially anticipated 33 percent. The additional revenue from this larger increase is equivalent to about 0.85 percent of GDP. The lower WEO oil price projection of January 6, 2009 would also have a positive impact on the fiscal deficit equivalent to about 0.25 percent of GDP due to the smaller cost of the negative external net oil balance.

3. Additional information on the 2009 budget law has also become available. Staff has not had a chance to discuss the details with the authorities. However, in view of the new aggregate information, staff has revised the projections for wage and development expenditures upwards by about 0.7 and 0.6 percent of GDP, respectively.

4. Taking into account the net impact of the above factors, the revised fiscal deficit projection for 2009 would be about 3.3 percent of GDP, slightly above the initial projection of 3.1 percent. This revision does not change staff's assessment, but further highlights the need to restrain expenditure and further advance other fiscal reform efforts, particularly those aimed at fully eliminating oil subsidies and introducing the value added tax by 2010.

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Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

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Washington, D. C. 20431 USA

IMF Executive Board Concludes 2008 Article IV Consultation with the Syrian Arab Republic

On January 9, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Syrian Arab Republic.[1]

Background

Syria's overall macroeconomic performance has been strong. Non-oil real GDP is estimated to have been about 6 percent in 2007, despite unfavorable weather conditions affecting agriculture. Virtually all other non-oil sectors continued to grow strongly. Oil output, however, remained on a downward trend. As a result, overall growth registered only about 4 percent. Preliminary data for 2008 indicate a rate of non-oil growth similar to 2007, despite a further decline in agricultural output, as construction and services maintained their rapid expansion. Overall growth is expected to be about 5 percent in 2008. Inflation accelerated to 17-20 percent by mid-2008, up from a reported 5 percent in 2007. However, it started to decline in the fourth quarter of 2008 in line with international food prices, and is projected to average about 15 percent for the year.

While the overall fiscal deficit increased to about 3.5 percent of GDP in 2007, the non-oil deficit improved slightly. Oil revenue decreased by about 2 percent of GDP. Non-oil receipts also declined, partly reflecting the reduction in customs tariffs. Current and capital outlays were reduced by about 1 percent of GDP in total.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

The fiscal deficit is expected to stabilize in 2008, mainly as a result of the reduction in fuel subsidies. The authorities launched a program to phase out these subsidies in May 2008 by increasing the prices of gasoline and diesel. These price increases and an overall expenditure restraint led to a further small narrowing of the non-oil deficit, despite the continued decline in customs revenue resulting from the full year effect of the 2007 reduction in tariffs.

The external current account deficit is expected to widen to about 4 percent of GDP in 2008, from 3.3 percent in 2007. The net oil balance (after subtracting the share of foreign partners) turned negative due to declining output and rising domestic consumption. However, non-oil exports, tourism, and remittances grew rapidly as a result of strong regional demand and the relaxation of foreign exchange controls. Net official foreign assets have been stable at about $17 billion (10 months of imports). The real effective exchange rate of the Syrian pound appreciated by 4 percent in 2007, and about 9 percent in the first three quarters of 2008 due to the combined effect of rising inflation and the pound's nominal appreciation against the dollar.

Broad money has been growing in line with nominal GDP. This growth mainly reflected domestic credit expansion. Credit to public enterprises grew by about 40 percent in 2007 and by 60 percent in the first half of 2008 (y-o-y), reflecting the rising financing needs of enterprises providing fuel and other subsidies. Growth of credit to the private sector was about 20 percent in 2007 and is expected to register 25 percent in 2008. Interest rates remained low, and became largely negative in real terms with the rise in inflation in 2008.

The impact of adverse global and regional developments currently underway on the Syrian economy are expected to be relatively mild in the short term. The effects are likely to be through weakening FDI, remittances, and demand for Syrian exports from the Gulf region. The medium-term outlook is then expected to improve as the global and regional economies begin to recover. The fiscal and current account deficits are expected to stabilize as a result of the fiscal reforms currently in the pipeline and a resumption in the strong growth of exports of goods and services. This generally positive outlook is contingent on perseverance in advancing fiscal and structural reforms and a gradual global recovery over the next two years.

Significant progress has been made on the structural front over the last two years, but the reform agenda remains substantial. Important progress toward exchange rate unification has been achieved; a dynamic private banking sector is growing; the investment regime is being liberalized; and trade liberalization has also continued.

Executive Board Assessment

Executive Directors welcomed Syria’s strong macroeconomic performance in recent years, as manifested in the rapid non-oil GDP growth, comfortable level of foreign reserves, and low and declining government debt. This performance reflected both robust regional demand and the authorities’ reform efforts to shift toward a more market-based economy.

At the same time, Directors observed that oil production and exports are declining, and Syria has already become a net oil importer. Inflation has declined in recent months as a result of falling international food and fuel prices, but remains high. Directors also noted the downside risks to growth arising from the current adverse global and regional developments—although many Directors considered these risks to be relatively mild because of Syria’s still limited integration into the international financial system and the significant potential for raising foreign direct investment and tourism exports. Directors were encouraged by the authorities’ efforts to address these challenges, and urged steadfast implementation of fiscal and structural reforms to support economic growth and diversification.

Directors encouraged the authorities to continue to reduce the non-oil fiscal deficit through mobilization of non-oil revenue, restraint on current expenditure—notably wages and subsidies—and prioritization of investment projects. They underscored the importance of the authorities’ adherence to plans to introduce the value added tax by the new target date of 2010, and supported the adoption of a single rate with limited exemptions. They commended the steps taken to reduce fuel subsidies, and encouraged the authorities to eliminate such subsidies by 2010 as planned—while developing a well-targeted compensation scheme to mitigate the impact on the poor.

Directors emphasized the importance of strengthening public expenditure management, including by reforming the budget process, improving the monitoring of expenditures at the regional level, establishing a single treasury account, and reducing extra-budgetary and quasi-fiscal operations through the banking system and bringing them on budget. They welcomed the authorities’ intention to issue treasury bills in 2009, observing that this will also help develop the domestic capital market and strengthen the conduct of monetary policy.

Directors welcomed the authorities’ commitment to maintain a cautious monetary policy stance. They urged the authorities to strictly limit directed lending by public banks, develop indirect monetary policy instruments, further liberalize interest rates, and modernize the role and responsibilities of the central bank.

Directors welcomed the 2008 FSAP finding that banks are well-capitalized and liquid, while noting the vulnerabilities in state-owned banks. They noted that enhancing the availability of reliable financial sector indicators would facilitate a more precise assessment and monitoring of the banking sector. They commended the authorities’ quick response to the FSAP recommendations, and encouraged them to continue their efforts in this regard. Directors stressed that bank supervision should be strengthened, and that all banks should be subject to annual independent audits and should provide timely information to the central bank. They urged the authorities to give priority to restructuring and commercializing the operations of state-owned banks. Directors noted the authority's efforts to enhance the framework for combating money laundering and terrorism financing, and encouraged further work in this area.

Directors agreed that the Syrian pound's peg to the SDR remains appropriate, as it provides a strong monetary anchor while allowing some flexibility in the pound's rate vis-à-vis major currencies. While acknowledging available estimates of the real effective exchange rate that show moderate over-valuation, Directors noted that these estimates are not reliable. Accordingly, Directors did not recommend any change in the exchange rate level in the present context. Directors encouraged the authorities to prepare the ground for a gradual move toward greater exchange rate flexibility over the medium term. They called on the authorities to remove the existing exchange restrictions and multiple currency practice.

Directors emphasized that vigorous implementation of the authorities' substantial structural reform agenda will be crucial to accelerate the shift to a more market-oriented and non-oil-based economy. They commended the reduction in import duties, and encouraged the authorities to continue to liberalize foreign trade and to improve the business environment.

Directors underscored that shortcomings in Syria's economic and financial statistics continue to hamper effective Fund surveillance and national policy formulation. They urged the authorities to improve the quality and timeliness of economic data.

Syrian Arab Republic: Selected Economic Indicators, 2004–08

	2004	2005	2006	Prel. 2007	Proj 2008
	(Change in percent, unless otherwise indicated)				
National income and prices					
Real GDP	6.7	4.5	5.1	4.2	5.2
Oil	-6.1	-8.6	-7.1	-5.0	-0.1
Non-oil	10.2	7.5	6.9	5.8	6.0
Nominal GDP (LS billions)	1,263	1,491	1,709	2,025	2,567
Of which: Non-oil	986	1,134	1,305	1,558	1,886
Nominal GDP ($ billions)	25.0	28.6	33.5	40.6	55.2
Crude oil production (‘000 barrels/day)	462	431	400	380	380
GDP deflator	10.9	12.9	9.1	13.7	20.6
Oil export rice ($ per barrel)	33.5	48.1	57.6	65.3	90.0
CPI period average	4.4	7.2	10.4	4.7	14.5
Total population (millions)	18.8	19.3	20.4	20.8	21.3
Of which: Iraqi Immigrants (millions)	0.8	0.9	1.5	1.5	1.5
	(In percent of GDP, unless otherwise indicated)				
Government finances					
Revenue	27.2	24.0	25.5	22.3	21.4
Oil- related revenue	11.2	7.1	7.3	4.9	4.7
Non-oil revenue	16.1	16.9	18.2	17.3	16.7
Expenditure	31.4	28.5	26.6	25.7	24.9
Current expenditure	19.0	18.1	16.3	16.1	15.4
Development expenditure	12.4	10.4	10.3	9.6	9.5
Overall balance	-4.2	-4.5	-1.2	-3.4	-3.5
Non-oil budget balance	-15.4	-11.6	-8.5	-8.4	-8.2
	(Changes in percent of initial stock of money)				
Broad money	11.1	11.5	9.4	9.8	19.0
Net foreign assets	5.4	0.7	-2.3	-2.0	3.7
Net domestic assets	5.8	10.8	11.7	11.9	15.3
Credit to government	2.8	6.1	0.3	-3.1	-0.7
Credit to public enterprises	0.5	1.7	3.4	7.6	9.2
Credit to private sector	4.3	6.9	3.5	4.3	6.0
Credit to private sector (change in percent)	35.0	45.9	17.9	20.2	25.8
Credit to private sector (in percent of GDP)	11.7	14.5	14.9	15.1	15.0
	(In billions of U.S. dollars, unless otherwise indicated)				
Balance of payments					
Current account balance	-0.4	-0.6	-0.9	-1.4	-2.3
(in percent of GDP)	-1.6	-2.2	-2.8	-3.3	-4.1
Overall oil balance 1/	1.3	0.7	0.0	-1.0	-2.1
(in percent of GDP)	5.3	2.1	0.0	-2.4	-2.6
Non-oil exports of goods and services	6.4	7.7	9.1	11.2	13.5
(change in percent)	99.2	20.4	18.6	23.5	20.2
Non-oil imports of goods and services	-9.3	-10.4	-11.9	-13.8	-15.6
(change in percent)	20.8	12.5	13.9	16.2	13.2
Overall balance	0.2	0.0	-0.8	0.7	-0.4
Official net foreign assets	17.6	17.6	16.8	17.5	17.1
(in months of imports of GNFS)	20.2	16.4	13.7	11.6	9.4
Weighted average nominal exchange rate LS/$2/	50.5	52.2	51.0	49.9	46.5
Real effective exchange rate (in percent, + appreciation) 3/	0.0	1.7	10.7	4.9	9.0

Sources: Syrian authorities, and Fund staff estimates and projections.
1/ Oil trade balance less profit of foreign oil companies.
2/ Trade-weighted average of official and parallel market rates before 2007. For 2008 data are for July.
3/ For 2008 data are for the first three quarters.

Statement by A. Shakour Shaalan, Executive Director for Syrian Arab Republic
January 9, 2009

1. The Syrian economy has enjoyed buoyant growth since it embarked on a liberalization program aimed at unleashing the economy's growth potential and integrating into the world economy. Non-oil growth has averaged 7 percent from 2004-2008, and is expected to pick up after a temporary slowdown in 2009. The Syrian authorities are firmly committed to their reform program that aims to lay the foundation for sustainable higher growth. Their 5-year development plan (2006-2010) targets medium-term growth of 7 percent from 2010 as the economy's productive capacity is unleashed. The plan aims at maintaining macroeconomic stability, continued deregulation, and furthering global integration to attract private investment, as well as a wide range of structural reforms to ensure good economic governance and growth with equity.

Near-term outlook and impact of global turmoil

2. The economy has been relatively sheltered from the global financial turmoil partly owing to strict regulations on banks' foreign exposures. Nevertheless, growth is expected to moderate somewhat in the period immediately ahead as the global and regional slowdown may temper the growth rate of non-oil exports and remittance receipts. However, the potential adverse impact is limited because these flows have been growing at a modest rate from a low base and hence are less likely to face declining demand than had they grown in line with the rise in oil prices. Moreover, there is considerable scope for growth in FDI and tourism receipts, both of which are at low levels relative to Syria's comparative cost advantage. Declining oil import prices will also assist in strengthening the external position.

3. Oil has been an important contributor to growth, fiscal revenue, and foreign exchange receipts. At its peak in 2001-2004, oil contributed to over 70 percent of exports and about 50 percent of fiscal revenue. However, current oil production has fallen short of domestic needs on account of rapidly growing domestic consumption demand, turning Syria back into a net oil importer in 2007. Without any further discoveries, production levels would gradually decline and reserves would be depleted by 2030. Although exploration activity has recently picked up with ongoing bidding on additional blocks that could lead to future discoveries, the authorities' plans are based on building the economic foundations for non-oil sustainable growth.

Fiscal policy and reforms

4. Fiscal outcomes have out-performed earlier expectations with the overall fiscal deficit in 2006 and 2007, at 1.2 and 3.3 percent of GDP, respectively. More notably, the balance excluding oil revenue has improved by 7 percentage points of GDP between 2004 and 2007. This favorable outcome was achieved through underspending of both the current and capital outlays despite budgetary pressures stemming from the large number of Iraqi refugees. Meanwhile, non-oil revenue collections had been strengthened primarily through increased

indirect taxes and public enterprise surpluses, which helped offset the impact of tariff liberalization. Based on preliminary indications, the overall fiscal out-turn will remain stable in 2008 and current expenditures will decline further as a share of GDP. Significant fuel price adjustments in May 2008 helped curtail fuel subsidies and reduced fuel imports. While these necessitated a 25 percent public sector wage increases to compensate for rising fuel prices and help retain its skilled civil service, the public wage bill has been kept under control and is declining as a share of GDP. Public debt is low and has fallen further to 22 percent of GDP by end-2008.

5. Fiscal policy remains constrained in 2009 to consolidate recent gains. The new budget extends the authorities' efforts to prepare for the decline in oil revenue, and as such, it is expected to deliver an additional 1 percentage point reduction in the non-oil fiscal balance by constraining current and capital outlays. They are considering targeted cash transfers and further fuel price adjustments, if needed, consistent with their plan to eliminate subsidies by 2010. The authorities view the VAT as a key source of revenue to offset dwindling oil revenues and are keen to ensure that the necessary preconditions are in place for its successful launch, including improved billing practices. Reform of customs administration is proceeding under an EU project while The Fund's METAC is helping to modernize budget processes including through the introduction of a medium-term expenditure framework. The ongoing implementation of an integrated information technology system is an important step toward improved expenditure management through a single treasury account.

Monetary and exchange rate policies

6. Monetary policy has been cautious and the Central Bank of Syria (CBS) has actively pursued institutional and monetary system reforms. Important progress has been achieved in the two key reform priorities, namely developing market-based monetary management instruments and strengthening banking sector regulation and supervision. Treasury bills were issued in two successful pilot auctions in July 2008 and regular Treasury bill auctions are set to be launched in 2009. At the same time, the CBS is considering issuance of its own certificates of deposits to mop up excess liquidity should Treasury bill auctions be delayed. Discussions have commenced on the transfer of state foreign exchange assets held by the Commercial Bank of Syria to the CBS and this process is due to be completed in 2009. A liquidity framework is being developed and the central bank is undertaking reforms to modernize its operations, expand its research capacity, and strengthen financial sector risk management.

7. The authorities view favorably their experience with the peg to the SDR which has served as a credible monetary anchor. Strong export growth and buoyant international reserves attest to the maintenance of competitiveness and reaffirm the appropriateness of the current regime. Liberalization of foreign exchange trading has solidified market confidence and brought about exchange rate stability, which in turn has helped curb inflationary pressures.

The banking sector

8. The banking system is well capitalized and well provisioned and banking supervision is being strengthened to improve resilience to shocks. Private banks have been licensed since 2004 and their share of total banking assets is nearly 20 percent. The authorities welcomed the assessment and recommendations provided by the FSAP team and have moved swiftly to adopt many of its recommendations. In particular, state banks are improving their reporting and preparing restructuring plans that outline their reform priorities. Off-site and on-site supervision have been strengthened and the entry of private and foreign banks has increased incentives to improve state banks' cost control and profitability.

9. The Syrian authorities value the analysis and advice of the Fund and appreciate the constructive spirit of the discussions. On their behalf, I wish to thank the staff team for their well-appreciated work.