

Syria's Economy: Prospects for Peace, Aid, and Market Reform

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Brief Analysis

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In many ways, Syria's economy is not very different from that of other countries in the region. Oil is important, accounting for 60 percent of exports. Agriculture is more important than might be expected on the basis of natural endowment: it contributes about 20 percent of the gross domestic product (GDP) and about 30 percent of employment. Industry remains very much state led, even when not state owned. The private sector is subject to comprehensive regulations, and foreign trade is less than might be expected for an economy Syria's size. On the other hand, there is a fair amount of labor moving from Syria to neighboring countries. Syria has a young population, so the labor force is growing; young people entering the labor force have a much better education than did the previous generation and therefore seek better jobs and better opportunities.

In the 1990s, Syria improved its economic policies regarding macroeconomic fundamentals, that is, the basic budgetary and monetary policies. The environment for the private sector has also improved, especially regarding foreign trade. These improvements, however, slowed down in the latter part of the decade. The liberalization of the late 1980s and early 1990s had a positive impact on growth, while the 1990s saw slower growth and less diversification of the economy away from a heavy dependence on oil.

While the World Bank was engaged rather actively in Syria in the 1970s and 1980s, Syria accumulated arrears with the institution, which has prevented Bank involvement in recent years. Finally in 1997, an agreement to resolve the arrears was concluded; payment has begun, and a full clearing of the arrears is expected in 2002. During the interim period, the Bank has resumed engagement with Syria on a limited basis, essentially in support of institutional development as well as environmental and sectoral issues, and most recently the International Finance Corporation has prepared a project with the private sector in Syria.

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Following Syrian president Hafiz al-Asad's ascent to power in 1970, basic socialist policies were modified slightly to give a somewhat wider scope to private enterprise. The most important change was that foreign oil companies were invited to explore and develop Syria's oil potential. The 1970s were years of prosperity, largely due to the effects of

oil. While Syrian oil production was small by Middle Eastern standards, it had a significant impact on the Syrian economy, especially after oil prices rose in 1973-74 and again in 1979-80.

After the early 1980s, the overall trend in oil prices was strongly downward, and for Syria as well as other oil-dependent countries, low oil prices generally spell trouble. Between 1982 and 1989, there was a steep decline in GDP per capita as well as in living standards. Numerous reports noted the widening gap between the few rich and the many poor--a trend that was aided and abetted by corruption on a wide scale. The late 1980s were particularly miserable. One safety valve for Syria has been its occupation of Lebanon; about 10 percent of the Syrian labor force hold jobs there, where wages are about double those in Syria.

But again, rescue primarily came from an exogenous force, not from fundamental changes in Syrian economic policies. As a reward for joining the anti-Saddam coalition in 1990, Syria received some \$4 to 5 billion. This aid provided a strong stimulus to the economy during the first half of the 1990s, but since the mid-1990s, the fundamental problems have reasserted themselves, mainly stemming from the socialist measures of the 1960s. The 1990s were a difficult time for Syria's economy, even though U.S. estimates during that time show a steep decline in Syrian arms imports as well as in overall military expenditures. This goes contrary to the widely held belief that Syria's economic problems are seriously aggravated by onerous military expenditures.

Of all Israel's neighbors, Syria has been most virulent in its expressed hatred of Israel. So why the current negotiations? Economic factors may be important: peace may bring aid, the wiping out of debts, and more investment. But Syria has no intention of entering into major economic deals with Israel; Syrian leaders do not think they can compete with Israel in the free market. Nor does the Syrian leadership intend to make fundamental economic changes; the opponents of change are firmly entrenched, and they are the main beneficiaries of the existing system.

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Syria's growth record has been particularly poor, not only in comparison with Israel, which did exceptionally well in the last two decades but also in comparison with its Arab neighbors. For instance, twenty years ago, Egypt's GNP per capita was only 35 percent that of Syria; today, Egypt's GNP per capita has surpassed that of Syria. It would seem that Asad does not seem particularly concerned about Syria's economic decline. That raises the question of what impact foreign aid has on Asad's decision making.

In the 1970s, Syria got a lot of aid from various sources. After the disengagement agreement with Israel in 1974, the United States re-started its aid program; in 1980-81, the U.S. aid allocation for Syria was \$228 million. When this aid began, it was hoped that Asad would go the same route as President Anwar Sadat of Egypt--on both foreign policy and economic reform--and the prospects indeed seemed promising. Instead, Syria went the opposite way. It stopped making economic reforms and instead ran up significant arrears on its debt payments to European countries and the World Bank. Even more seriously, Syria became a designated terrorism-sponsoring country, and congressional opposition forced an end in aid to Syria for this reason. Syria's stance on the Middle East process also hardened with the 1978 formation of the "rejectionist front" of countries repudiating Egypt's peace with Israel. In other words, as economic aid made Syria stronger, Asad's response was to get tougher. That pattern continued into the late 1970s. After the Arab states pledged at the 1978 Baghdad summit to provide Syria with \$1.8 billion in aid each year, and the Soviet Union promised arms aid, Asad announced a drive toward "strategic parity," that is, a military buildup until Syria achieved arms parity with Israel.

So overall, the experience of aid to Syria is not encouraging. At present, Syria gets approximately \$200 million a year in aid, roughly one-third each from Arab sources, international organizations, and Japan. European Union (EU) and EU countries' aid for Syria has been held up by unpaid arrears, mostly for the \$1.5 billion lent by the former East

Germany to pay for weapons. Syria takes the position that since East Germany no longer exists, Syria should not have to repay this debt. Damascus takes the same position regarding its debt to the former Soviet Union, now evaluated at about \$15 billion.

In the event of a peace treaty between Syria and Israel, Syria might get more aid. Russia, which has offered to settle the debt for a payment of only \$2 billion, might agree to even less. Germany might also agree to generous debt relief, freeing up the tentative allocations of funding worth some \$700 million, set aside for Syria in the past by EU institutions. Mobilizing aid for Syria, however, will be hampered by Asad's lack of interest in the issues on the development community's agenda. The goals for which international institutions and the United States Agency for International Development (USAID) want to provide funds--better governance, more transparency, rule of law, promotion of democracy, and the empowerment of the poor--are not issues likely to be welcomed by Asad. There are also problems with the very basic elements essential for making economic development assistance work. In fact, Syria still has economic policies that aid agencies say are antithetical to growth: the exchange rate is unrealistic, nearly all goods are subject to price controls, interest rates are well below inflation, and the government budget is opaque. Despite the progress that has been made in liberalizing foreign trade, in general it will be difficult to argue that on development grounds, Syria is deserving of more aid.

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