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COMMENTARY

No. 51 Wednesday, 20 June 2012

Syrian Authorities to Print Currency with Hopes of Alleviating Liquidity Woes

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The Syrian authorities have recently printed a new batch of Syrian currency in Moscow in order to pump liquidity back into the markets, which have recently been suffering from a liquidity shortage. Thus, there are now two editions of currency in the markets: the original old one, which is still widely in circulation, and the new one being tested by the government, perhaps in a bid to replace the original currency. It is widely known that sovereign states are entitled to print as much currency as they want as long as the new currency is supported by enough foreign currency, gold, etc.

This especially applies to small countries like Syria, whose currency lacks commercial convertibility. The United States, European countries and Japan, for example, do not worry about their currencies, and much less about how much they print because those currencies can be converted into other hard currencies, or traded. Moreover, these currencies can be used as reference currencies for international contracts and financial transactions. None of these conditions apply to the Syrian Lira, which has lost nearly half of its real value over the past year. This has affected the prevailing inflation levels and prompted many to get rid of the Lira and convert it to foreign currencies that are more stable.

In this context, the question is: what has prompted the authorities to make such a move? Clearly, there is a liquidity shortage in terms of the revenue that the state is collecting from taxes, fees and service charges. The government is busy grappling with issues relating to security, and is no longer capable of collecting taxes or electricity and water bills. As a result, economic activity has witnessed a downturn and a drop in tourism revenues has reduced government revenues to a minimum – one local observer estimated that it has dropped by more than 50 percent. What's more, citizens are reluctant to pay their bills because of the difficult living conditions. Add to this the fact that the central state is no longer capable of exercising its control over some areas witnessing armed conflicts. Tax collection in some areas is no longer being channelled to the state treasury, but instead to new regional centres of power, by force.

This decline in revenue is taking place as more pressure is being placed on the government to increase its expenditure and preserve stability. However, the scarcity of liquidity has imposed undesired alternatives on the government, such as printing new quantities of paper currency, thereby depreciating the value of the Lira. Nonetheless, the lira has kept its balance with the banks so far able to meet the demand for foreign currency. How did this happen?

The monetary policy is reportedly out of the hands of the Central Bank of Syria because traditional tools are no longer able to rise to the challenge. There is a security cell working with monetary experts, which is depriving commercial banks of the freedom to deal with the demand for foreign currencies. Now, banks operating in Syria are forced to meet the foreign currency demand through security delegates who are working in the main banks in order to defend the Lira. For its part, the Central Bank is pumping up the rest of its foreign currency reserves to close the loopholes in the markets.

Now the question is: how long will this policy be sustained? Increasing the money supply by printing new currency infers that Syria will enter a spiral of inflation, rising prices and an unprecedented loss of confidence in the currency. In this context, we cannot forget the experience of former Iraqi President Saddam Hussein, who resorted to printing new paper currencies in the middle of the siege, thereby creating two editions in the market: the original Swiss edition and the Saddam edition. In the end, both editions collapsed despite the enormous cash reserves that Iraq had at the time. Collapse then was attributed to the lack of hope that things were headed toward a solution.

In the Syrian case, sources of foreign currency are sharply dropping, and official transfers of foreign currency are in decline. What's more, the amounts being transferred to Syria through Iran and Iraq, Syria's major trade partners, are not clear. However, it is obvious that the central government's ability to manage its monetary policy, fiscal policy and tax collection is sharply waning.

The printing of additional banknotes at a time when foreign currency revenues are decreasing indicates that Syrian authorities are beginning to lose control of their currency and their fiscal policies. It points to a level of precariousness in the authorities' economic policies, and that they are running out of alternatives to reassure the Syrian public. The impending wave of inflation, which will result from the decision to print more currency, means that a new phase of economic deterioration lies ahead for Syria.

Ultimately, economic distress has begun imposing options that the government has long sought to avoid. However, the effects of the deteriorating security situation and increasing international pressure are starting to adversely influence important sectors. In the short run, printing money perceived by authorities as the easiest way to manage the deteriorating situation, but only temporarily. The challenge of defending and protecting the currency remains the most difficult one, failing to do so will reveal the defects of the banking and financial system. The concerns plaguing the public psyche are justified, especially since the situation is not heading toward any political settlement that can in turn help restore economic stability.

Note: **This article was originally published in Arabic in *Al-Hayat* and in English in *Carnegie Middle East Center.***
Web link: http://www.carnegie-mec.org/publications/?fa=48579&lang=en

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