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## Country Report

# Syria

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"0 or 0.0" means nil or negligible; "n/a" means not available; "-" means not applicable

# Syria

## Forecast

### Highlights

#### Outlook for 2014-18

- 2 [Political stability](#)
- 4 [Election watch](#)
- 4 [International relations](#)
- 5 [Policy trends](#)
- 5 [Fiscal policy](#)
- 6 [Monetary policy](#)
- 6 [International assumptions](#)
- 7 [Economic growth](#)
- 7 [Inflation](#)
- 8 [Exchange rates](#)
- 8 [External sector](#)
- 8 [Forecast summary](#)

#### Data and charts

- 9 [Annual data and forecast](#)
- 10 [Quarterly data](#)
- 11 [Monthly data](#)
- 12 [Annual trends charts](#)
- 13 [Monthly trends charts](#)
- 14 [Comparative economic indicators](#)

#### Summary

- 14 [Basic data](#)
- 16 [Political structure](#)

## Recent analysis

### Politics

- 18 [Forecast updates](#)
- 18 [Analysis](#)

### Economy

- 24 [Forecast updates](#)
- [Analysis](#)

# Highlights

Editor: **Robert Powell**

Forecast Closing Date: **August 6, 2014**

## Outlook for 2014-18

- Although the government's diplomatic position has been assisted by the sweeping gains of the extreme jihadi Islamic State (IS) in Iraq, in reality IS's rise is only likely to accelerate Syria's fragmentation during the forecast period.
- The position of external backers will contribute to the continuation of the conflict, with Iran unlikely to cease its financial backing for the Assad regime and the Gulf Arab states funnelling cash and arms to the Sunni opposition.
- The failure of the opposition to make inroads into regime territory and the stabilisation of the front lines will provide the government with an opportunity to attempt an economic development drive in areas under its control.
- With the civil war expected to persist throughout the forecast period, the government will scale back subsidies further and rely on UN aid agencies. However, this will be insufficient to prevent repeated fiscal deficits in 2014-18.
- We forecast that the economy will bottom out by end-2014 as the economy and business gradually adjust to the realities of the military stalemate. However, even by 2018 real GDP will still be one-third smaller than in 2010.
- Having reached 89.6% in 2013, inflation will ease to an average of 25.5% in 2014-15, aided by a helpful base effect. However, persistent shortages and the continued weakening of the pound will keep inflation elevated thereafter.

## Review

- On July 16th the president, Bashar al-Assad, was sworn in for a third seven-year term. In his speech, he stuck with his tactic of portraying his opponents as terrorists, adding that many of those fighting the regime had been "misled".
- The cabinet has announced that its main focus will now be to launch the reconstruction of the economy. It appears that the model for the programme will be the Solidere redevelopment of Beirut after the Lebanese civil war.
- The State Planning Commission reports that the economy is growing again, based on projected increases in consumer spending, trade and investment.
- The UN Security Council passed a resolution on July 14th authorising UN humanitarian agencies to send aid convoys over the Syrian border and across conflict lines without securing prior approval from the government.
- In late July the Syrian army and the National Defence Force retook a major natural gas installation east of Homs from the IS. However, they suffered heavy losses in the process.
- A natural gas project being undertaken by Russia's Stroytransgaz for the state-owned Syrian Gas Company is scheduled to come on stream in August, according to the oil minister, Suleiman al-Abbas.

## Outlook for 2014-18

### Political stability

Syria's civil war, which we expect to persist over the entire forecast period, has descended into something resembling a free-for-all, with multiple, overlapping conflicts punctuated by periodic, localised gains and reversals. In keeping with this, the regime's military offensive of recent months has petered out, in part reflecting

the growing strength of the extreme jihadi Islamic State (IS; formerly the Islamic State of Iraq and al-Sham), which previously had largely avoided direct confrontation with the Syrian army. Unusually, the rise of IS has seemingly placed the regime on the same side as the US—as well as Iran and the Iraqi government; seeking to capitalise on this, the regime launched air strikes on IS targets on the Iraqi border in late June. Although the clashes between IS and the government might be good news for the fragmented opposition—which has itself been locked in battle with IS for months—the rise of the group will further undermine the rebels' cohesiveness. Overall, with the government seemingly incapable of sustaining a broad offensive to re-impose control over the whole country, the rise of IS is only likely to accelerate Syria's fragmentation during the forecast period, with no one side able to gain an outright victory.

Instead, we envisage that the military stalemate will solidify into a de facto partition of the country, with the regime of the president, Bashar al-Assad hunkered down in a corridor running between the capital, Damascus, and the Alawi areas in the north-west (viewed as the regime's heartland). Elsewhere, the country will be divided into "fiefdoms", held by a shifting combination of opposition forces representing the Free Syrian Army (FSA; a largely secular force ostensibly tied to the politically oriented Syrian National Coalition, or SNC), Islamist groups of various hues, including IS, and Kurdish parties. The position of external backers will contribute to the continuation of the conflict, with Iran in particular committed to buttressing the Assad regime, while Saudi Arabia is stepping up the funnelling of arms and cash to the predominantly Sunni opposition.

Meanwhile, IS will seek to sustain its position from a combination of discounted oil sales from seized fields (including the Omar field, captured in July), donations from private backers in the Gulf and taxes imposed in areas under its control in Syria and Iraq. However, IS's brutal and intolerant methods will prompt a backlash from locals, as was recently witnessed when it was driven out of three Syrian villages by tribal fighters, and eventually an international crackdown on trade in IS-sourced oil may well be imposed. As a result, we expect IS to struggle to make significant gains far beyond its strongholds in eastern Syria.

With the humanitarian catastrophe worsening (more than 150,000 people have been killed since the war began, with 2.6m having fled the country and another 7m internally displaced), diplomatic efforts to end the conflict will periodically be stepped up. These included the hastily drawn-up chemical disarmament proposal—under which Syria sent its final stock of chemical weapons for destruction in June—and two recent rounds of negotiations, overseen by the US and Russia, in Geneva (Switzerland). However, the talks made no progress on the major issues, and the rupture in ties between the US and Russia probably precludes another similar joint diplomatic drive. We therefore continue to expect all sides to pursue a military resolution to the war, despite the stalemate on the ground.

The regime, for its part, will be able to rely on financial and military support from Iran, Russia and a Lebanese Shia group, Hizbullah, although the Syrian army—weakened by defections and heavy losses—is insufficiently strong to successfully regain, let alone subdue, the half of the country now outside regime control (a factor that helps to explain the government's heavy reliance on Hizbullah troops). The opposition, meanwhile, has become beset by internal fissures. Besides political machinations within the SNC itself (which elected a new, Saudi-backed leader, Hadi al-Bahra, in July), the rebels remain divided between more secular, grass-roots groupings and the increasingly confident (and well-financed) Islamist factions. The Islamists themselves are divided between the Salafi (puritanical Sunni) Islamic Front, backed by Saudi Arabia, and two al-Qaida offshoots, al-Nusra and IS. Adding to the fragmented picture, the Kurdish Democratic Union Party has continued to pursue the creation of its own semi-autonomous region in the north-east of Syria.

Amid this deteriorating picture, towns (and, potentially, entire regions) will become in effect self-governing—a major stumbling block in reuniting the country once peace is restored. Although not our central scenario, in the event that the regime

does fall during the forecast period (perhaps as part of a withdrawal of support from Iran, in the wake of a "grand bargain" between that country and the US), any post-Assad government would struggle to assert itself, with the current ethnic and sectarian tensions only likely to re-emerge as the post-war government seeks to build a new state edifice.

## Election watch

Mr Assad comfortably won the presidential election on June 3rd, winning 88.7% of the vote on a highly dubious official turnout of 73.5%. However, in reality, both of his opponents had minimal name recognition and were from the regime-tolerated opposition. Combined with the lack of a transparent election process and a boycott by the SNC, this meant that the election was a walkover for Mr Assad (who will not face "re-election" for another seven years). Nonetheless, it will do nothing to affect the course of the war, with the opposition—and much of the international community—continuing to reject his legitimacy.

## International relations

The Syrian government will continue to rely heavily on Russia and China to provide it with diplomatic cover, while portraying itself as a bulwark against terrorism in an attempt to court Western opinion (a task arguably made simpler by the rise of IS). The drive to buttress its image via the UN-overseen chemical-weapons disarmament process has, however, largely fallen into the background, reflecting not only the lack of appetite within the US (and the EU) for a humanitarian intervention in Syria, but also the more immediate distraction emanating from IS's sudden advance. As a result, the prospect of one-off US air strikes (possibly involving drones), designed to counter the jihadi threat, has increased substantially. Such an outcome in turn lowers the chances of US attacks on the Syrian regime, which has stepped up attacks on IS. However, a rapprochement between the two countries will not occur; indeed, in June the US president, Barack Obama, requested US\$500m from Congress to train and equip "appropriately vetted" Syrian opposition groups.

Elsewhere, the approach of the Arab states will remain divided, with Qatar and—in particular—Saudi Arabia continuing to supply weaponry to the opposition. However, Iraq, which has been indirectly meeting a significant proportion of Syria's crude oil needs for some time, will prove friendlier to the Syrian regime, encouraged by recent Syrian air strikes on IS targets. Meanwhile, the involvement of Iran-backed Hezbollah has spread the conflict beyond Syria's borders, with, most notably, the Iranian embassy in Beirut being bombed in November 2013 in a reprisal attack. Similarly, Israel has launched periodic attacks on Syrian targets, including air strikes in June against several Syrian army sites in retaliation for the death of a teenager killed in the Golan Heights by a mortar launched from Syria.

## Policy trends

The failure of the opposition to make inroads into regime territory and the relative stabilisation of the front lines will provide the Assad government with an opportunity to attempt an economic development drive in areas under its control. The government appears to be basing its plans on the redevelopment of downtown Beirut after the Lebanese civil war; local holding companies will be set up to undertake reconstruction, with owners of property rights given shares in relation to the value of their assets. In an early signal of private-sector support, there was a strong turnout of prominent Syrian businesspeople at a reconstruction seminar hosted in Beirut in June.

However, major progress will be stymied by the fallout from the country's civil war, including the government's loss of oil income. With this in mind, the regime will seek external financial support from Iran (including a US\$7bn credit line) and, to a lesser extent, Russia and Iraq to enable its reconstruction plans. However, doubts remain over Iran's ability to continue to buttress the regime, given the weak state of the Islamic Republic's economy. As a result, a sustained and major reconstruction programme will have to await the end of the war. This would entail, among other things, ramping up capital spending, attracting international oil operators back to the country and seeking considerable donor support.

## Fiscal policy

The government's fiscal policy will be focused on military spending and wages, although some increase in the capital budget is possible in the face of its reconstruction aims. No revenue projections have been issued in recent budgets, but we expect state receipts to remain far below 2011 levels, reflecting the fact that Syria is no longer exporting oil (which generated around 25% of total revenue before the war). Exacerbating the situation, customs receipts will remain depressed. The only main revenue source to have been sustained is the state's income from Syria's two mobile-phone companies, which, despite damage to the telecommunications infrastructure, has actually risen in 2014.

Although we expect the civil war to persist throughout the forecast period, the deficit should narrow in 2014<sup>18</sup>. The hardening of the front lines in the war will allow the resumption of some business activity in areas under regime control, in turn providing the government with a chance to boost tax and customs revenue, and high inflation will bring down the deficit as a proportion of nominal GDP. On the expenditure side, further reductions in subsidies will be implemented (an increase in prices of foodstuffs, water and electricity was announced in July), reflecting the burden of fuel imports and the weakening local currency. The impact of this will be abated, however, by the ramping-up of food and healthcare aid from UN agencies, which will provide an important supplement to the government's activities, especially as UN agencies distribute these goods and services through state channels. In spite of this, the shallowness of the banking sector and a paucity of bilateral support will probably see the government turning to the Central Bank of Syria to monetise the deficit.

## Monetary policy

Domestic unrest has prompted occasional runs on the Syrian pound, causing the Central Bank to bring back restrictions on foreign-currency transactions. In August 2013, for example, a decree was issued banning the use of foreign currency or precious metals for commercial transactions within Syria. These measures, together with the near-term lifting of the threat of US military intervention, prompted a stabilisation of the black-market and official rates in the second half of last year. However, the continuation of the war will periodically exert downward pressure on the pound (the black-market rate lurched downward again in April), prompting the Central Bank to introduce further capital-control measures.

## International assumptions

	2013	2014	2015	2016	2017	2018
<b>Economic growth (%)</b>						
US GDP	1.9	1.7	3.2	2.5	2.4	2.6
OECD GDP	1.3	1.9	2.6	2.4	2.4	2.5
World GDP	2.0	2.5	3.0	2.9	2.9	3.0
World trade	2.7	4.4	5.0	5.3	5.4	5.5
<b>Inflation indicators (% unless otherwise indicated)</b>						
US CPI	1.5	1.8	2.2	2.3	2.3	2.5
OECD CPI	1.6	2.1	2.2	2.3	2.2	2.1
Manufactures (measured in US\$)	-3.1	0.0	0.9	1.8	1.9	1.6
Oil (Brent; US\$/b)	108.9	108.3	105.1	103.8	97.5	93.0
Non-oil commodities (measured in US\$)	-6.8	-3.1	0.0	0.9	3.0	2.9
<b>Financial variables</b>						
US\$ 3-month commercial paper rate (av; %)	0.1	0.1	0.4	1.4	2.4	2.9
US\$:€ (av)	1.33	1.35	1.30	1.28	1.27	1.26
¥:US\$ (av)	97.60	102.03	102.24	102.00	101.00	100.00



## Economic growth

Syria's economic performance will continue to be hampered by the impact of the civil war. Damage to the economy has been broad-based, with rural incomes (and thus private consumption) hit by drought and poor harvests, oil production depressed by sanctions and damage to fields, and domestic demand dampened by the continued exodus of Syrian refugees to neighbouring countries. Although the country's two refineries are operating at over 50% capacity and natural gas output has remained relatively resilient (indeed, a natural gas project being undertaken by Russia's Stroytransgaz for the state-owned Syrian Gas Company is scheduled to come on stream in August, according to the oil minister, Suleiman al-Abbas), the rebels have increasingly targeted gas pipelines, and the refineries' access to spare parts and specialised materials will be hindered by new US sanctions imposed in May.

Amid the worsening violence, we estimate that real GDP contracted by around 19% in 2013. Economic activity will be restrained as long as the war continues, with most of Syria's oilfields set to remain off stream (although small quantities of refined fuel will be trucked into Turkey from rebel-held areas). Investment will remain stagnant amid the violence and the departure of around 3m refugees will depress domestic demand.

However, we forecast that the economy will bottom out before the end of 2014, as business gradually adjusts to the realities of the military stalemate. (This view is in keeping with that of the State Planning Commission, which reported in July that real GDP is now starting to grow after three years of contraction.) Among other things, there has been a significant move of population from Homs and Aleppo to the coastal region—including industrialists and merchants, who have set up operations in an expanded industrial zone outside Tartous. As a result, the economy should stabilise, growing by around 2-3% annually in 2014–18. However, this will still leave it almost one-third smaller at the end of the forecast period than it was in 2010.

### Economic growth

%	2013 <sup>a</sup>	2014 <sup>b</sup>	2015 <sup>b</sup>	2016 <sup>b</sup>	2017 <sup>b</sup>	2018 <sup>b</sup>
GDP	-18.7	1.8	2.4	2.5	2.6	3.0
Private consumption	-18.0	2.3	3.0	3.2	3.2	3.4
Government consumption	-8.0	2.0	2.2	2.0	2.1	2.3
Gross fixed investment	-20.0	0.3	1.2	2.0	2.7	3.5
Exports of goods & services	-46.5	1.8	1.9	3.1	3.4	3.8
Imports of goods & services	-26.0	2.2	3.0	3.9	4.4	4.5
Domestic demand	-16.5	1.9	2.5	2.8	2.9	3.2
Agriculture	-13.0	2.0	2.5	2.5	2.6	3.0
Industry	-20.6	1.0	1.4	1.5	1.8	2.2
Services	-21.0	2.1	2.4	2.6	2.9	3.1

<sup>a</sup> Economist Intelligence Unit estimates. <sup>b</sup> Economist Intelligence Unit forecasts.

## Inflation

Although inflation slowed markedly in the final months of 2013, on the back of a dip in food costs and improved currency stability, it still averaged 89.6% last year. Even with a helpful base effect, we forecast that further subsidy cuts will keep inflation relatively high, at an average of 34.8% and 16.2% in 2014 and 2015 respectively. With localised shortages set to persist as the war continues, the Syrian pound continuing to weaken and the government monetising its deficits, we expect that inflation will subsequently rise again, reaching 17.6% in 2018.

## Exchange rates

The Syrian pound will continue to decline against the US dollar and other major currencies in 2014–18, owing to the collapse in export revenue, sanctions and a resultant shortage of foreign exchange. The gap between the official and black-market exchange rates started to widen in late March, prompting the Central Bank to authorise renewed sales of foreign exchange to banks and money changers in order to close the gap. However, we judge that Syria's foreign reserves are close to being exhausted. Similarly, we expect the country's weak trade fundamentals to reassert themselves, ensuring further depreciation of the currency and, as the forecast period progresses, a widening of the gap between the official and black-market rates. As a result, we expect the official rate to weaken from S£140.8:US\$1 at end-2013 to an average of S£311.4:US\$1 in 2018.

## External sector

We expect the current-account deficit to remain exceptionally wide, on the back of a continued curtailment of oil exports (oil sales by IS are not included in our calculations) and the more general depressing impact of the war on Syrian businesses. Persistent wide trade deficits, averaging 15% of GDP in 2014–18, will partly be offset by strong current transfers inflows, largely reflecting rising aid levels and remittances from Syria's growing diaspora. However, non-merchandise exports will remain depressed, with tourism, previously Syria's second-largest source of foreign exchange, unsurprisingly remaining almost non-existent. Overall, we expect the current-account deficit to average 7.3% of GDP in 2014–18, with the shortfalls financed primarily by Iranian and Russian credit.

## Forecast summary

### Forecast summary

(% unless otherwise indicated)

	2013 <sup>a</sup>	2014 <sup>b</sup>	2015 <sup>b</sup>	2016 <sup>b</sup>	2017 <sup>b</sup>	2018 <sup>b</sup>
Real GDP growth	-18.7	1.8	2.4	2.5	2.6	3.0
Oil production ('000 b/d)	28.0	15.3	16.0	30.0	57.5	75.0
Gross agricultural production growth	-13.0	2.0	2.5	2.5	2.6	3.0
Consumer price inflation (av)	89.6 <sup>c</sup>	34.8	16.2	16.4	17.0	17.6
Government balance (% of GDP)	-6.8	-4.6	-3.6	-2.9	-2.2	-1.6
Exports of goods fob (US\$ bn)	1.9	2.0	2.1	2.3	2.4	2.6
Imports of goods fob (US\$ bn)	7.6	7.7	8.1	8.5	8.8	9.2
Current-account balance (US\$ bn)	-5.2	-4.6	-4.6	-4.6	-4.4	-4.4
Current-account balance (% of GDP)	-8.3	-7.3	-7.3	-7.5	-7.4	-7.1
External debt (year-end; US\$ bn)	9.2	10.7	12.2	13.4	14.3	15.0
Exchange rate S£:US\$ (av)	108.4 <sup>c</sup>	150.0	178.7	217.5	265.4	311.4
Exchange rate S£:US\$ (end-period)	140.8 <sup>c</sup>	157.6	194.1	236.7	282.9	331.6
Exchange rate S£:¥100 (av)	111.1 <sup>c</sup>	147.0	174.8	213.2	262.8	311.4
Exchange rate S£:€ (av)	144.0 <sup>c</sup>	202.9	231.5	278.3	337.1	392.3

<sup>a</sup> Economist Intelligence Unit estimates. <sup>b</sup> Economist Intelligence Unit forecasts. <sup>c</sup> Actual.

# Data and charts

## Annual data and forecast

	2009 <sup>a</sup>	2010 <sup>a</sup>	2011 <sup>b</sup>	2012 <sup>b</sup>	2013 <sup>b</sup>	2014 <sup>c</sup>	2015 <sup>c</sup>
<b>GDP</b>							
Nominal GDP (US\$ m)	53,967	60,185	52,588	65,973	63,059	62,619	62,431
Nominal GDP (£ bn)	2,521	2,792	2,544	4,248	6,837	9,391	11,160
Real GDP growth (%)	6.0	3.2	-3.4	-18.9	-18.7	1.8	2.4
<b>Expenditure on GDP (% real change)</b>							
Private consumption	4.6	7.6	-3.0	-16.7	-18.0	2.3	3.0
Government consumption	17.3	10.8	7.2	-6.0	-8.0	2.0	2.2
Gross fixed investment	11.5	13.6	-2.5	-27.0	-20.0	0.3	1.2
Exports of goods & services	-19.0	11.2	-12.0	-48.1	-46.5	1.8	1.9
Imports of goods & services	-23.0	15.1	-3.2	-35.0	-26.0	2.2	3.0
<b>Origin of GDP (% real change)</b>							
Agriculture	12.8	-9.6	0.0	-21.0	-13.0	2.0	2.5
Industry	3.7	7.8	-3.3	-32.8	-20.6	1.0	1.4
Services	5.4	5.6	-5.0	-12.0	-21.0	2.1	2.4
<b>Population and income</b>							
Population (m)	21.0	21.5	21.8 <sup>a</sup>	21.4	20.1	19.9	20.0
GDP per head (US\$ at PPP)	4,860 <sup>b</sup>	4,958 <sup>b</sup>	4,823	4,053	3,557	3,713	3,856
Recorded unemployment (av; %)	8.1	8.6	14.9 <sup>a</sup>	25.0	35.0	33.0	30.0
<b>Fiscal indicators (% of GDP)</b>							
Central government revenue	21.5	23.5 <sup>b</sup>	21.9	11.9	4.6	4.3	4.6
Central government expenditure	24.4	24.9 <sup>b</sup>	34.0	19.1	11.4	8.9	8.1
Central government balance	-2.9	-1.4 <sup>b</sup>	-12.1	-7.1	-6.8	-4.6	-3.6
Net public debt	23.9 <sup>b</sup>	22.7 <sup>b</sup>	37.4	32.0	31.4	32.0	34.5
<b>Prices and financial indicators</b>							
Exchange rate S£:US\$ (end-period)	45.70	46.76	55.89 <sup>a</sup>	77.27 <sup>a</sup>	140.81 <sup>a</sup>	157.64	194.10
Consumer prices (av; % change)	2.9	4.4	4.8 <sup>a</sup>	95.4 <sup>a</sup>	89.6 <sup>a</sup>	34.8	16.2
Stock of money M1 (% change)	9.2	17.6	15.0	6.0	-12.5	3.0	8.4
Stock of money M2 (% change)	8.6	13.5	5.4	-2.6	-14.6	3.1	6.4
Lending interest rate (av; %)	10.0	10.0	10.5	11.7	10.5	10.0	10.5
<b>Current account (US\$ m)</b>							
Trade balance	-3,064	-3,663	-7,310	-6,935	-5,612	-5,652	-5,932
Goods: exports fob	10,884	12,273	10,288	3,876	1,939	2,031	2,137
Goods: imports fob	-13,948	-15,936	-17,598	-10,811	-7,552	-7,683	-8,069
Services balance	2,079	3,860	429	32	-456	-301	-124
Income balance	-1,107	-1,514	-1,682	-872	-501	-440	-430
Current transfers balance	1,062	950	837	1,035	1,364	1,792	1,898
Current-account balance	-1,030	-367	-7,726	-6,740	-5,205	-4,601	-4,588
<b>External debt (US\$ m)</b>							
Debt stock	7,323 <sup>b</sup>	7,442 <sup>b</sup>	8,327	8,107	9,245	10,699	12,180
Debt service paid	162 <sup>b</sup>	160 <sup>b</sup>	152	119	102	73	81
Principal repayments	110 <sup>b</sup>	108 <sup>b</sup>	102	91	78	45	46
Interest	51 <sup>b</sup>	52 <sup>b</sup>	50	27	24	28	35
<b>International reserves (US\$ m)</b>							
Total international reserves	17,436	19,519	14,443	4,793	1,895	1,799	1,674

<sup>a</sup> Actual. <sup>b</sup> Economist Intelligence Unit estimates. <sup>c</sup> Economist Intelligence Unit forecasts.

Sources: Central Bank of Syria; IMF, International Financial Statistics; World Bank, Global Development Finance.

## Quarterly data

	2012				2013			
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr
<b>Prices</b>								
Consumer prices (2005=100)	127.0	135.6	146.0	164.3	195.2	235.6	319.3	335.9
Consumer prices (% change, year on year)	22.5	33.4	41.3	48.8	53.7	73.8	118.8	104.5
<b>Financial indicators</b>								
Exchange rate S£:US\$ (av)	58.2	62.6	65.8	71.0	81.1	96.9	116.4	139.3
M1 (end-period; S£ bn)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M1 (% change, year on year)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (end-period; S£ bn)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (% change, year on year)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Sectoral trends</b>								
Crude oil production (m barrels/day)	0.17	0.16	0.16	0.16	0.04	0.04	0.03	0.02
Crude oil production (% change, year on year)	-54.7	-56.8	-50.0	-27.3	-76.7	-75.0	-81.3	-87.5
<b>Foreign trade (US\$ m)<sup>a</sup></b>								
Exports fob	2,785	3,510	3,219	2,620	2,218	2,873	2,574	2,158
Imports cif	4,730	5,135	4,345	4,353	3,546	4,065	4,219	4,824
Trade balance	-1,945	-1,626	-1,126	-1,734	-1,328	-1,192	-1,645	-2,667

<sup>a</sup> IMF, Direction of Trade Statistics estimates.

Sources: Central Bank of Syria; International Energy Agency, Oil Market Report; IMF, International Financial Statistics, Direction of Trade Statistics.

## Monthly data

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
<b>Exchange rate S£:US\$ (av)</b>												
2011	46.9	46.9	46.9	47.5	47.5	47.5	47.5	47.5	48.5	49.4	50.0	54.7
2012	56.4	58.5	59.6	61.0	63.2	63.7	64.4	65.9	67.0	68.5	70.2	74.3
2013	78.8	80.4	84.1	139.7	98.3	100.1	104.5	111.8	132.9	137.5	139.7	140.8
<b>M1 (% change, year on year)</b>												
2011	13.9	13.1	15.9	15.5	12.4	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2012	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>M2 (% change, year on year)</b>												
2011	12.2	11.5	10.5	8.9	8.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2012	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Consumer prices (av; % change, year on year)</b>												
2011	-24.6	-26.7	-27.7	2.9	3.0	4.0	5.5	3.9	3.4	3.2	5.8	11.0
2012	15.7	21.3	30.8	31.5	32.5	93.5	93.5	98.3	110.6	113.1	112.6	120.7
2013	116.7	115.4	123.6	129.3	138.9	92.1	114.0	121.3	121.1	117.3	107.8	88.2
<b>Deposit rate (av; %)</b>												
2011	6.0	6.0	6.0	6.0	7.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2012	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Lending rate (av; %)</b>												
2011	10.0	10.0	10.0	10.0	10.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2012	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
<b>Total exports fob (US\$ m)</b>												
2011	1,328	1,092	1,434	1,460	1,960	1,529	1,681	1,418	1,478	1,060	827	724
2012	1,078	712	994	973	1,597	940	1,056	1,013	1,151	1,023	850	747
2013	825	586	807	807	1,300	766	859	776	938	832	707	619
<b>Total imports cif (US\$ m)</b>												
2011	1,997	1,939	2,602	2,339	2,042	2,102	2,260	2,374	2,389	2,048	2,098	2,307
2012	1,533	1,378	1,818	1,683	1,791	1,661	1,362	1,342	1,640	1,321	1,415	1,617
2013	1,037	1,042	1,466	1,436	1,328	1,301	1,115	1,420	1,684	1,360	1,611	1,854
<b>Trade balance fob-cif (US\$ m)</b>												
2011	-669.2	-847.3	-1167.8	-879.3	-82.3	-573.3	-579.1	-956.4	-911.3	-987.8	-1270.5	-1582.9
2012	-454.8	-666.8	-823.8	-710.2	-194.4	-721.1	-306.7	-329.5	-489.4	-298.3	-565.5	-870.0
2013	-211.9	-456.8	-659.2	-629.3	-28.7	-534.2	-255.6	-643.6	-745.8	-528.0	-904.4	-1234.2

Sources: Central Bank of Syria; IMF, International Financial Statistics, Direction of Trade Statistics; Haver Analytics.

# Annual trends charts

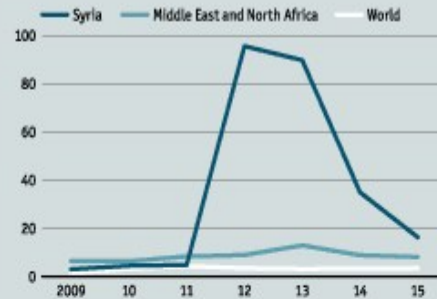
## Annual trends charts

**Real GDP growth**  
(% change)



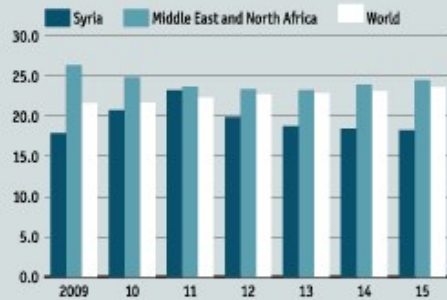
Source: The Economist Intelligence Unit.

**Consumer price inflation**  
(av; %)



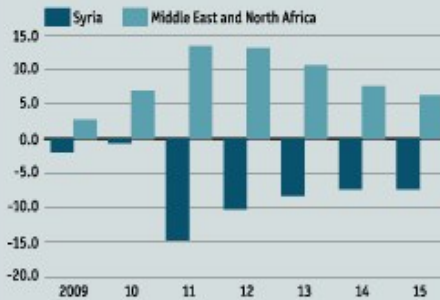
Source: The Economist Intelligence Unit.

**Gross fixed investment**  
(% of GDP)



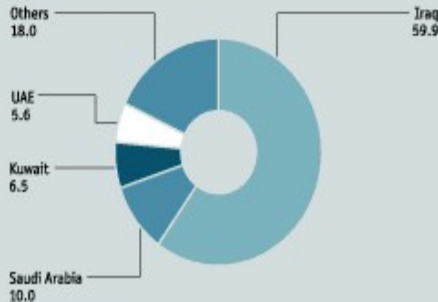
Source: The Economist Intelligence Unit.

**Current-account balance**  
(% of GDP)



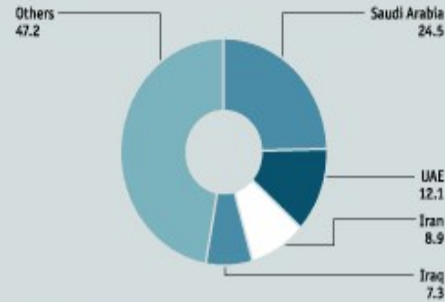
Source: The Economist Intelligence Unit.

**Destination of exports, 2013**  
(% of total)



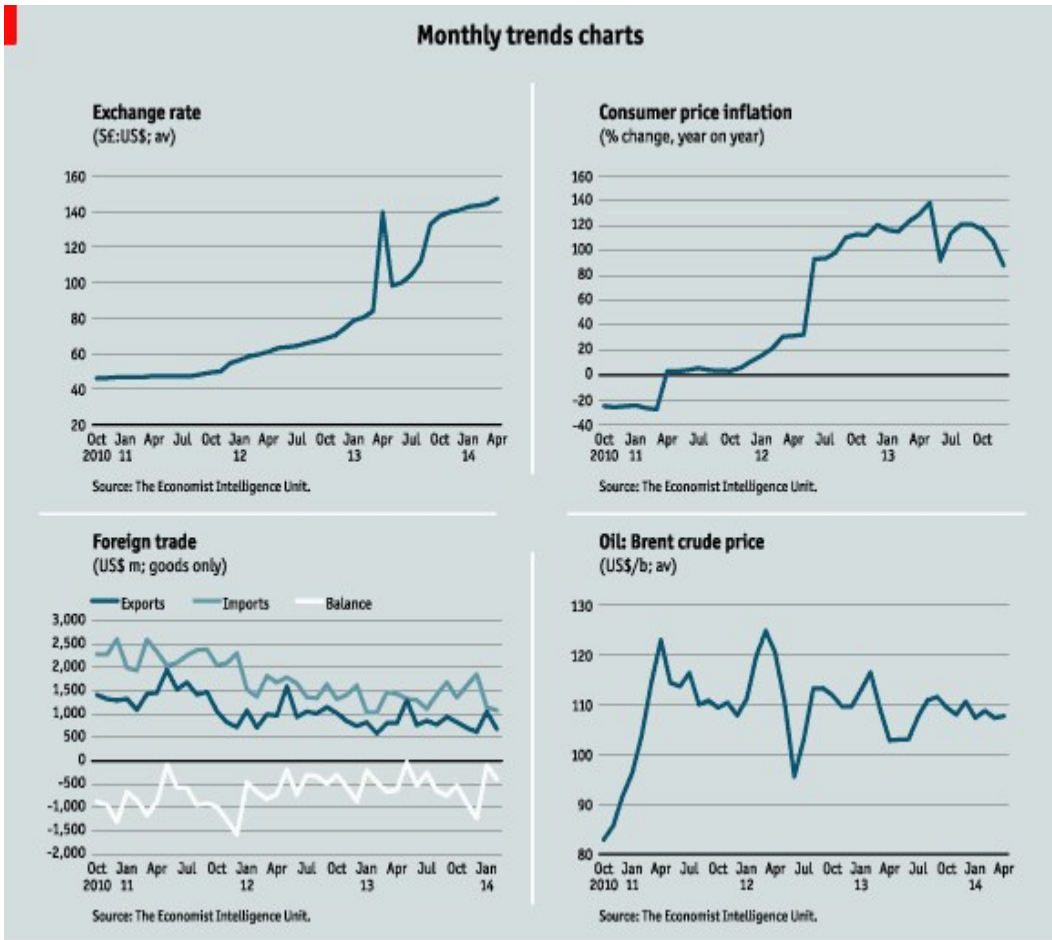
Source: IMF, IFS Annual.

**Origin of imports, 2013**  
(% of total)

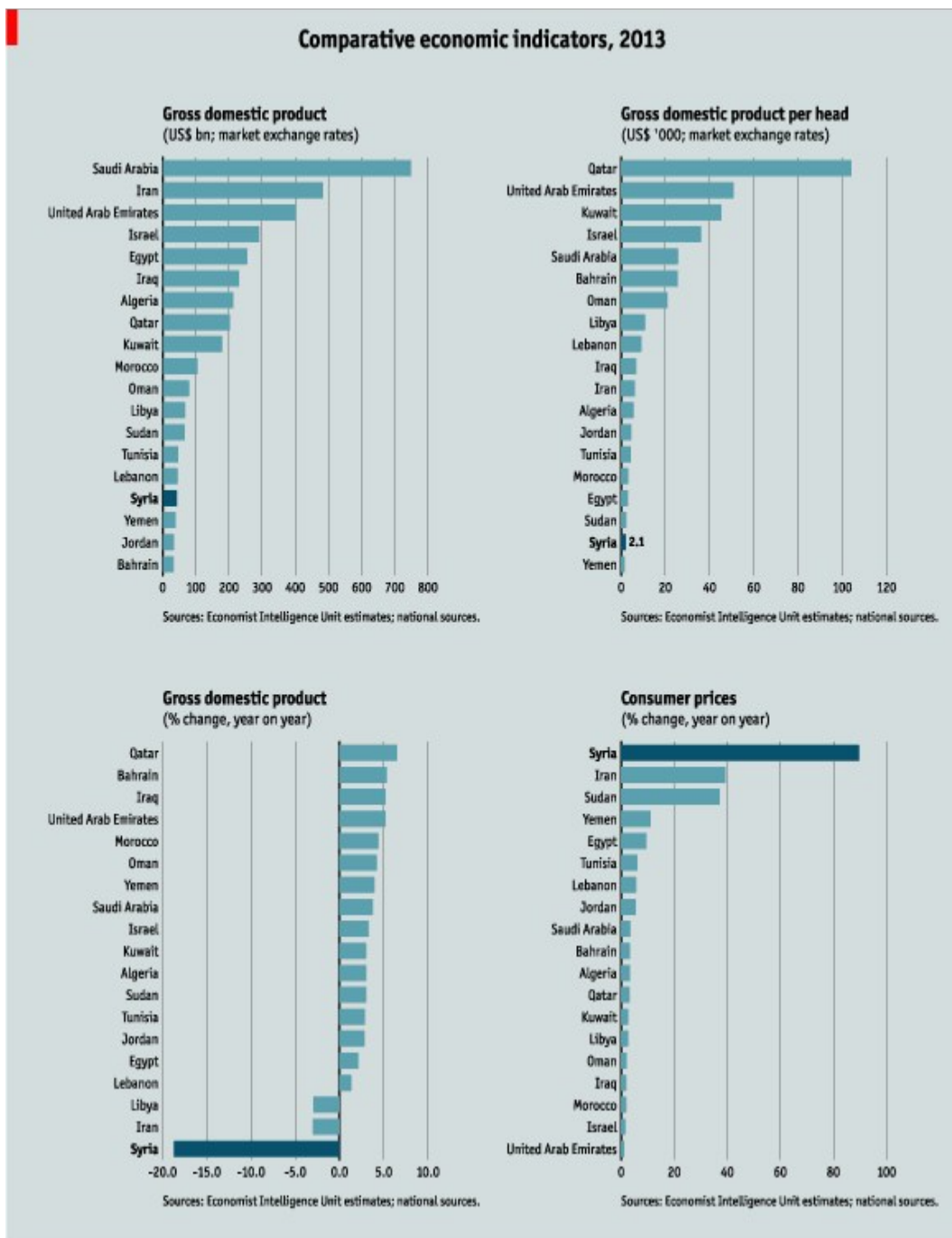


Source: IMF, IFS Annual.

# Monthly trends charts



# Comparative economic indicators



## Basic data

### Land area

185,180 sq km

### Population

22.9m (2010 estimate)

### Main provinces



Population in millions, 2010

Damascus (capital) area: 4.48

Aleppo: 4.74

Homs: 1.76

Hama: 1.59

Hassakah: 1.47

Idlib: 1.46

## Climate

Subtropical on coast, arid in the centre, cold winters in the highlands

## Weather in Damascus

Hottest month, August, 18-37°C (average daily minimum and maximum); coldest month, January, 2-12°C; driest month, August, zero average rainfall; wettest month, January, 43 mm average rainfall

## Languages

Arabic, French, some English

## Religion

Sunni Muslim (72%); Alawi Muslim (14%); Christian (12%); Shia Muslim and Druze minorities

## Measures

Metric system

## Currency

Syrian pound (S£) = 100 piastres

## Time

GMT plus two hours

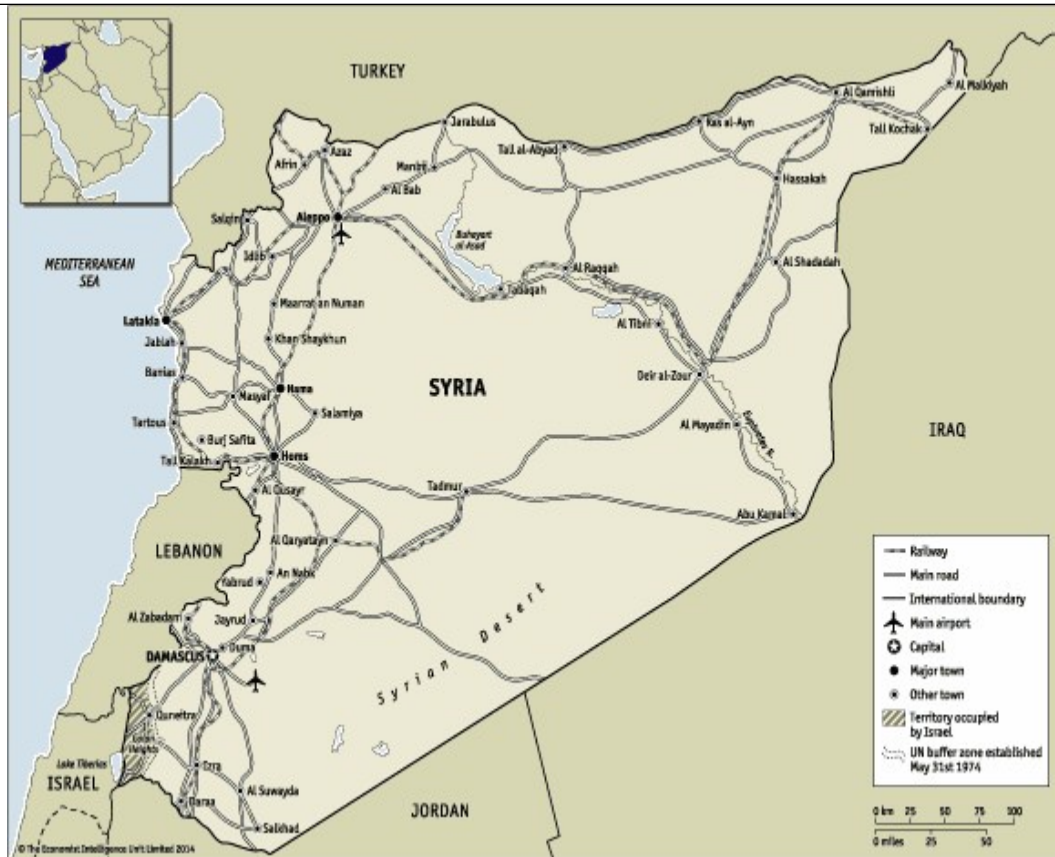
## Fiscal year

January 1st-December 31st

## Public holidays

The dates of Islamic holidays are based on the lunar calendar and are therefore approximate. Mawlid al-Nabi (the birthday of the Prophet, January 13th 2014); Eid al-Fitr (July 28th); Eid al-Adha (Feast of the Sacrifice, October 4th); Islamic New Year (October 25th)

New Year's Day (January 1st); Revolution Day (March 8th); Mother's Day (March 21st); Easter (March 31st); Orthodox Easter (May 5th); Independence Day (April 17th); Labour Day (May 1st); Martyrs' Day (May 6th); October Liberation War Day (October 6th); Christmas Day (December 25th)



## Political structure

### Official name

Syrian Arab Republic

### Form of state

Republic

### Legal system

Based on the constitution of 1973

### Legislature

250-member Majlis al-Shaab (People's Assembly) directly elected for a four-year term

### Electoral system

Universal adult suffrage

### National elections

Next legislative and presidential elections due in 2016 and 2012 respectively

### Head of state

President, elected for a seven-year term. The president appoints the vice-president, the prime minister and the Council of Ministers. Bashar al-Assad, the current president, is also the commander-in-chief of the armed forces and the secretary-general of the Baath party

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## Executive

The prime minister heads the Council of Ministers, a large number of whom are drawn from the ruling Baath party and its partners

## Main political parties

The ruling National Progressive Front includes the Arab Socialist Baath Party; Arab Socialist Party; Arab Socialist Unionist Party; Communist parties; Syrian Arab Socialist Union Party; Unionist Socialist Democratic Party; Union Socialist Party

## Key ministers

Prime minister: Wael Nader al-Halqi

Deputy prime minister & defence: Fahad Jassim al-Frej

Deputy prime minister & foreign affairs: Walid al-Muallim

Deputy prime minister & local government: Omar Ibrahim Ghalawanji

Deputy prime minister & economic affairs: Vacant

Awqaf (Islamic endowments): Mohammed Abdel-Sattar al-Sayed

Communications & technology: Imad Abdel-Ghani Sabbouni

Culture: Lubana Mashouh

Economy & foreign trade: Mohammed Zafar Mahbak

Education: Hazwan Alos

Electricity: Imad Mohammed Deeb Khamis

Environment (minister of state): Nazira Sarkis

Finance: Mohammed al-Jleilati

Health: Said Abdel-Salam Nayef

Higher education: Malek Ali

Housing & construction: Safwan al-Assaf

Industry: Adnan Salakho

Information: Omar Zuabi

Interior: Mohammed Ibrahim al-Shaar

Internal trade & consumer protection: Samir Ezzat Qadri Amin

Irrigation: Bassam Hanna

Justice: Najim Hamad al-Ahmed

Labour & social affairs: Jasem Zakariya

Petroleum & mineral resources: Suleiman al-Abbas

Presidential affairs: Mansour Azzam

Tourism: Bishr Yazigi

Transport: Mohammed Ibrahim al-Said

## Central Bank governor

Adib al-Mayaleh

## Head of State Planning Commission

Amer Lufti

# Recent analysis

Generated on August 20th 2014

The following articles have been written in response to events occurring since our most recent forecast was released, and indicate how we expect these events to affect our next forecast.

## Politics

### Forecast updates

**August 11, 2014: International relations**

#### **US's air campaign unlikely to spread to Syria**

##### **Event**

The commencement of US air strikes against Islamic State (IS) targets in northern Iraq has raised the possibility of the US conducting similar such attacks against the extreme jihadi group in Syria.

##### **Analysis**

On August 7th the US president, Barack Obama, announced that the US Air Force would begin launching air strikes against IS targets. Since that time, the US has launched five rounds of strikes, using both manned and unmanned aircraft, against a range of IS artillery and heavy equipment being used to attack embattled members of the Yazidi minority currently taking refuge on Mount Sinjar in north-western Iraq.

However, given the fluid movement of IS personnel and equipment between Syria and Iraq (where the group has set up its own, self-styled caliphate), there would be a military logic in widening the scope of US air attacks to IS targets on the Syrian side of the border. This logic would be reinforced by the IS's major victory on August 7th against government forces in Syria's Raqqqa province, in which it captured a base and substantial amounts of heavy military equipment (including tanks). There is now a possibility that this seized materiel will be pressed into service in Iraq.

However, in his reasoning for the US's intervention, Mr Obama appeared to provide several justifications that would rule out widening the attacks into Syria. In particular, he cited the threat to US interests in the Iraqi Kurdistan region—where a number of US personnel, and a US consulate, are based. In contrast, no such US representation exists in Syria, and thus there is no imminent threat from the IS in that theatre. Equally, the president specifically cited the threat of "genocide" against the Yazidis in Iraq for his actions—a situation not currently being replicated in Syria, although the IS has periodically committed atrocities against Christians in Syria.

As a result, the hard-pressed and less extreme Syrian opposition and the Syrian government—both of which are locked in battle against the IS—can probably only expect to benefit indirectly from US intervention, with both sides hoping that the damage wrought on the group in Iraq will in turn weaken its position in Syria.

##### **Impact on the forecast**

We have for some time highlighted the possibility of US air strikes against jihadi targets in Syria, but have not made it our central forecast. Despite the US's intervention in Iraq, we will not adjust our forecast for the time being.

## Analysis

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August 8, 2014

## Fighting on multiple fronts

The dramatic gains made over the past two months by the Islamic State (IS), an extreme jihadist group that started to make its mark in early 2013, have transformed the conflict in Syria. The group, which rebranded itself from the Islamic State of Iraq and al-Sham (ISIS) after seizing control of large swaths of territory on both sides of the Iraqi-Syrian border, is now looking to extend its domain. This has put it in conflict with most of the other actors in the Syrian arena, including the regime, Kurdish groups, Sunni tribal militias and the numerous factions of the non-jihadist opposition.

Despite facing a large array of opponents, IS has been strikingly successful in seizing and holding new territory. It has effectively deployed a twin tactic of terrorising its enemies and co-opting the local population in areas that it has conquered. Little is known about the group's leadership structure, other than that it includes a mixture of al-Qaeda-affiliated former rebels against US forces in Iraq and some former military and intelligence figures from the regime of Saddam Hussein. The group's operations appear to have been well-planned, and it has achieved a high degree of financial self-sufficiency through oil trading, taxation and extortion.

### Group's successes lure foreign fighters

Its military capabilities have been enhanced through its seizure of huge caches of weapons from the Iraqi and Syrian armies, and its subsequent successes have allowed it to lure a stream of jihadist volunteers, including both foreign fighters and other Islamist groups within Syria. As well as attracting fighters, it has also been able to tap into a large pool of finance managed by Islamist fundraisers in the Gulf—in particular Kuwait (an operation highlighted by a recent US Treasury Department designation of three individuals in the Gulf Arab state as financiers of terrorism).

The main battle fronts involving IS are the following:

- **Raqqa:** IS moved into this northern town on the Euphrates in April 2013, displacing other rebel groups that had seized several districts from the forces of the Assad regime. It became IS's main base after the group was pushed back from the Aleppo region by other rebel forces. The regime remained in control of bases on the outskirts of the town and made little effort to confront IS, either on the ground or through air attacks. In the past two months IS has gone on the offensive against this residual regime presence. In July it overran the base of Division 17, and on August 7th IS declared that it had captured the base of Brigade 93 in the northern part of Raqqa province. It is not clear whether IS has complete control of these bases, but the group has posted pictures and videos indicating that it has secured large hauls of weaponry from them. Regime forces are said to have fallen back to the Tabqa military base, near the main dam on the Euphrates.
- **Deir al-Zor:** The Euphrates valley town and much of the oil-producing area between it and the border with Iraq fell largely under the control of the rival jihadist Jabhat al-Nusra (JN) in 2013, with the regime holding on to parts of the town and the air base outside. In the past two months JN has left the region, under pressure from IS but without major confrontations. IS has also expelled regime forces from the town, and is reported to have gained control of at least parts of the air base. IS has sought to impose its order on the oil production and trading operations in the province. However, it has encountered opposition from tribal groups in several villages around Deir al-Zor, as well as in the border town of Albu-Kamal.
- **Hasakeh:** The north-eastern province of Syria has been under the shared control of Kurdish political groups and the Assad regime for most of the past three years. IS has sought to make inroads into the province, which contains valuable farmland and oilfields, but has met stiff resistance from the

main Kurdish force in the region, the YPG, a Syrian offshoot of the Turkey-based Kurdish Workers Party (PKK). The assaults have intensified, and in July IS scored a major breakthrough when it captured the base of the Syrian army's Regiment 121, outside Hasakeh city. The YPG has since been reinforced with units from the PKK, with the apparent approval of the Turkish government. Syrian Kurdish groups, among whom the Democratic Union Party (PYD) is the dominant player, have long complained that Turkey has been helping IS as part of its long-term strategy of curbing the PKK, but the kidnapping of Turkish diplomats by the IS in Iraq in June will have eased Kurdish concerns about Turkey's intentions. The YPG and the PYD are also now working more closely with the Iraqi Kurdistan Regional Government (KRG), as their mutual fear of IS has overridden their political differences.

- **Aleppo:** IS forces are pressing to regain control of parts of Aleppo province, in particular border crossings into Turkey, that they lost during the campaign against them by non-jihadi rebel groups earlier this year. Thus far, IS gains have been less significant in this area than on other fronts.
- **Homs-Palmyra:** During July IS forces struck out to the west of Deir al-Zor and seized control of the al-Shaer gasfield between Homs and Palmyra, killing a large number of regime forces and civilian staff. The Syrian army eventually succeeded in recapturing the facility.
- **Damascus suburbs:** Efforts by IS to establish a presence around the capital have been rebuffed by the main anti-regime groups active in these areas.

## Tensions between Jabhat al-Nusra and other rebels increase

The IS advances through the Euphrates valley have had an impact on relations between JN and the non-jihadi groups operating elsewhere in the country under several guises, including the Syrian Revolutionary Forces (SRF), the Islamic Front (IF) and the Free Syrian Army (FSA). Having been deprived of the revenue accruing from control of oilfields around Deir al-Zor, JN has sought to compensate through trying to take over the revenue-generating operations of these other groups, including smuggling routes, local taxation and extortion from farmers and businesses. JN had already made inroads into Idleb province in the north-west and into the southern areas of Deraa and Quneitra, but until recently it had avoided confrontation with the other groups. Intra-rebel tensions are now rising, however, and there have been several violent clashes. In early August a JN commander in Idleb was killed in a car bomb explosion, assumed to have been the work of rival groups. In Deraa, 18 opposition groups formed a new front to combat JN's plans to place the area under an Islamic emirate to be governed by JN sharia courts, practicing Islamic law.

Simultaneously, despite long-standing tensions between IS and JN, which both have their roots in the former al-Qaida in Iraq, the two groups are reported to have been operating in harness in some parts of western Syria, including Qalamoun, along the border with Lebanon. Both IS and JN have been engaging with Syrian regime forces and with fighters of Lebanon's Hizbullah, a military and political group allied with Iran. The recent clashes around Aarsal, a Lebanese town housing thousands of Syrian refugees, have stemmed from a spillover of operations from Qalamoun into Lebanese territory. JN withdrew from Aarsal earlier this week, but IS has been slower to depart the area.

## Strength of Islamic State is a concern for the regime

The gains made by IS have been a setback for the Syrian regime. The president, Bashar al-Assad, had been looking to kick off his third term by making further inroads against rebel forces, having regained control of Homs earlier this year. However, his forces have taken heavy casualties in the IS offensives of recent weeks, and the return to their home country of Iraqi Shia militias, following the IS

push towards Baghdad, has removed an important ally from the regime ranks.

The regime had been poised to gain control of Aleppo, but it has been unable to build on gains it made in the northern part of the city before the IS onslaught elsewhere in the country. Rebel forces have also recorded some advances in Hama province, between Homs and Aleppo, as well as in some outlying areas of Damascus. The regime, meanwhile, continues to cause heavy damage and civilian casualties through barrel-bomb attacks on rebel-held areas.

IS is managing to maintain the momentum of its campaign to spread its dominion as far as possible, largely as a result of the weapons and resources it has been able to plunder as it has overrun Iraqi and Syrian army bases and oilfields. The Assad regime appears to have been taken aback by the ruthlessness and effectiveness of the IS assaults on its bases in the north-east of the country. IS had previously served the regime's purpose by weakening the main rebel forces, but now it appears to pose a serious threat to the regime itself.

Ultimately IS could overreach itself and find itself facing too many enemies. However, for the time being it is still very much on the offensive.

## August 14, 2014

### Combating the Islamic State

**The extraordinary rise of the extremist jihadi Islamic State (IS) has left the world's governments scrambling to devise ways to counter the group. This has manifested itself most dramatically in Iraq, where a new, less divisive prime minister, Haider al-Abadi, has been appointed, and the US has launched a series of air strikes against IS positions. Yet defeating and dismantling the group, which now controls an area proximate in size to the kingdom of Jordan, will almost certainly prove a long-term undertaking, given both its near unassailable position in Syria and its control of over half a dozen oilfields.**

However, at least in northern Iraq, its position is more vulnerable than is commonly assumed, with the group in serious danger of overreaching. Its tactics in Iraq thus far can probably be best categorized as conquer and plunder, with the movement focused on: recruiting personnel (often by freeing its prisoners from jails); seizing weaponry (as it spectacularly succeeded in doing after its capture of Mosul, when it amassed huge quantities of Iraqi army equipment); and, most recently, capturing and redistributing government food supplies, as evidenced by its recent seizure of some 40,000-50,000 tonnes of wheat from government silos in Nineveh province. Yet such a tactic naturally relies on maintaining the group's forward momentum, as well as, to an extent, the group's aura of invincibility after repeated astonishing military successes in the field against Iraqi and Kurdish forces.

### Momentum shifting against IS in Iraq

Yet all this could move into reverse if the IS's advance in Iraq is halted. Thus far the group has successfully plucked the low-hanging fruit: it moved into fellow Sunni Arab areas, where resentment against the government of Iraq's contentious former prime minister, Nouri al-Maliki, was strongest, and exploited the obvious lack of motivation and discipline within Iraq's armed forces. However, both the political and military momentum has now shifted in four key areas.

- **A motivated and capable opponent.** Although the peshmeraga (armed Kurdish fighters) have suffered a series of surprising reverses, it retook two towns, Makhmour and Gweir, from IS on August 10th and is now benefiting from a veritable flood of donated military supplies (including new ammunition and French equipment).
- **Western military intervention.** The IS's heavy equipment—including the tanks and artillery seized from the Iraqi army—is hugely vulnerable to US air power out on the Nineveh plains. Although thus far these air strikes have

been piecemeal, we expect the US to step up its air-delivered bomb and missile strikes once a new government of national unity is formed in Baghdad (albeit the US administration will almost certainly shy away from putting boots on the ground).

- **A plausible, national unity government.** A new, less sectarian (and less Shia) government would provide an alternative political route for those within IS territory, or on the front lines. Mr Maliki had alienated Iraq's Sunni Arab population to such an extent that it accepted (albeit perhaps not fully welcomed) the return of the jihadis less than seven years after bloodily evicting them. The nomination of Mr Abadi, although not universally welcomed among all Iraqi Sunni groups, has for the most part been positively received, including by puritanically Sunni Saudi Arabia.
- **International unity over the issue.** The backing given by all major external players to the new premiership of Mr Abandi—including Saudi Arabia, Qatar, Iran, and the US—should ensure that no major party will seek to undermine the transition (in the way that Iran did in Iraq after 2003).

## Momentum behind IS in Syria

In contrast, however, the position of the IS in Syria looks almost impregnable. It is worth noting that the Islamic State of Iraq and al-Sham (now renamed the IS) was rebuilt in Syria, from the ashes of al-Qaida in Iraq. Unlike Iraq, the IS's Sunni strain of Islam overlaps more closely with Syria—over 60% of Syria is Sunni Arab, compared with just 20% in Iraq. Admittedly, prior to its civil war, Syria was viewed as a relatively secular place, under successive Assad regimes; however, three and a half years of war and 170,000 dead has undoubtedly unleashed increased religious extremism.

On the back of this, a plethora of Sunni Islamist groups has formed across Syria, most of whom are currently rivals of IS, but may be persuaded to shift into its camp. For example, al-Qaida-affiliated Jabhat al-Nusra co-operated with IS in the attack on the Lebanese town of Arsal on August 2nd, and there is speculation that, as IS advances on Syria's second city, Aleppo, the Salafi-oriented Ahrar al-Sham, which reportedly has more boots on the ground than IS (up to 20,000, compared with 10,000-15,000, respectively), is considering throwing in its lot with IS.

More importantly, however, arguably none of the four key political and security elements moving against IS in Iraq are being repeated in Syria.

- **A motivated and capable opponent.** In this regard, the Syrian regime certainly counts, but its focus is split by the multiplicity of opponents confronting it (including up to 1,000 rebel groups). Equally, until recently, the Syrian government had avoided confronting IS, as the group had previously served its purpose of both weakening and dividing the main rebel forces, and helped reinforce the narrative that the regime's opponents are terrorist extremists. On the other side, several of the various rebel groups are certainly motivated to take on IS, but lack the necessary weaponry—indeed, the Saudi-backed Syria Revolutionaries Front reportedly suffered a heavy defeat in Akhtar in August 13th.
- **Western military intervention.** After President Barack Obama's abortive effort in August/September 2013 to launch air strikes against the Syrian regime to punish it for using chemical weapons, any sort of US military intervention in Syria is unlikely for the time being. This impression was reinforced by his speech on August 7th announcing the US's intervention in Iraq: first, he said it was to defend US interests in the Iraqi Kurdistan region—where a number of US personnel, and a US consulate, are based—and he cited the threat of "genocide" against Iraq's Yazidis. Neither situation applies in Syria.
- **A plausible, national unity government.** Although the Syrian president, Bashar al-Assad, might point to his thumping victory in the (highly dubious) presidential election in June, the mass uprising against his regime



demonstrates the widespread loathing that his rule engenders. Meanwhile, the opposition political coalition, the Syrian National Coalition, has become at best peripheral and in many ways irrelevant to the ongoing war on the ground.

- **International unity over the issue.** In contrast to Iraq, the major external actors are divided over the best way to approach Syria's civil war. On the hand, Iran, Lebanon's Shia political/guerrilla group, Hizbullah, and Russia backs the Assad regime; on the other, the Saudis, Qatar, the US and EU back the rebels (and not necessarily the same ones). As a result, the key international players tend to focus on countering the influence of each other, rather than unifying against IS.

## Halting the sale of "blood oil" will be key

Arguably, the best way to counter the IS in Syria would be to undermine its economic underpinnings: notably its oil. Currently, the Paris-based International Energy Agency (IEA) reports that the group has seven fields under its control, largely based in the Euphrates, while the Iraq Oil Report estimates that IS is earning as much as US\$1m a day from its Iraqi oilfields alone (via smuggling routes through Turkey and Iran). Although the UN Security Council condemned the purchase of the IS's oil in a vote in late July, a much more co-ordinated crackdown on the trade of what might be called "blood oil" is necessary to stem the flow. Seeking to build a firmer foundation for its rule, the IS has an energetic hearts-and-minds programme in the areas it currently rules (with a focus especially on children), but its efforts would probably not add up to much without the cash behind them. Of course, it could revert to other, more violent options to cow the population, but such methods can only go so far: as al-Qaida in Iraq (AQI), which was roundly defeated by a combination of US forces and, in particular, armed Iraqi Sunni tribal groups, would attest.

Yet, even if IS's oil trade is curtailed, two crucial drivers necessary to undermine the group's grip are lacking in Syria. First, there is no obvious security (and financial) alternative to the IS—a key component of AQI's defeat was the controversial US surge, which reassured locals taking up arms against al-Qaida that the US was not about to abandon them. The IS's ideology may not be especially popular—they were recently kicked out of three villages near the Syria-Iraq border—but any would-be anti-IS fighter will desire outside reassurance before confronting such a fearsome organisation. Second, and as a corollary, Syria remains a fertile location for the IS's conquer and plunder approach. Even if its oil funds are cut off, IS could divert its pillage policy to the south, against the Syrian army and all the way to Damascus. Although the Assad regime could rely on Iran's full backing and Russian equipment, it is not clear that the Syrian government would be able to stem the IS tide. If the US is horrified at the prospect of IS rampaging through northern Iraq, it would explore a whole new level of anxiety should the group end up pressing up against the borders of its two closest political allies in the Middle East, Jordan and, above all, Israel.

# Economy

## Forecast updates

August 11, 2014: Fiscal policy outlook

### MTN aims for 20-year licence

#### Event

South Africa's MTN has told its shareholders that it is negotiating with the Syrian government about converting its current revenue-sharing mobile-phone operating contract into a 20-year licence agreement.

#### Analysis

The company said that it will finance the licence out of dividends that it has earned in Syria over the past four years, but which it has been unable to repatriate owing to the restrictions on foreign-exchange transfers out of the country.

The conversion of the two build-own-operate contracts into licences had been envisaged in 2010, when the government invited bids for a third licence. However, the process was aborted after the uprising against the regime of the president, Bashar al-Assad, in March 2011. The other operator is Syriatel, which is controlled by Rami Makhlouf, a maternal cousin of Mr Assad.

According to the UK-based *Financial Times*, MTN has indicated that the licence fee would be between S£18bn (US\$120m) and S£25bn (US\$168m), roughly equivalent to one year of the government's current share, which is set at 50% of gross revenue. The company said that it had about US\$250m of accrued earnings blocked inside the country, and that it would use the balance of these funds, after the licence payment, for fresh capital expenditure.

MTN Syria announced total earnings of S£26.4bn in the first half of 2014, of which it paid S£12.4bn to the government. It made a net profit of S£2bn, compared with S£900m in January-June 2013. Clearly it has decided that its continued healthy profits justify the maintenance of its presence in war-torn Syria. Earlier this year the company revealed that its biggest challenge was to safeguard its equipment in the face of the continued violence, which has resulted in 47% of its installations being out of action.

MTN owns 72% of its Syrian affiliate, which it acquired in 2007 as part of its takeover of Lebanon-based Investcom. The venture started operations in 2001, and has about 5.7m subscribers. MTN also has a 49% stake in a mobile-phone company in Iran, where it has also had problems repatriating profits because of sanctions.

#### Impact on the forecast

MTN's announcement reinforces our forecast that the only main fiscal revenue source likely to be sustained is the state's share of the income of Syria's two mobile-phone companies.

## August 13, 2014: External sector

### Iran accounts for almost half of Syria's imports

#### Event

The Assad regime's reliance on continued economic support from Iran has been highlighted by recently issued trade statistics showing that the Islamic Republic accounted for almost half of Syria's imports in the period between January 1st and July 20th 2014.

#### Analysis

*Al Watan*, a Damascus-based newspaper, cited figures from the General Foreign Trade Organisation (GFTO) showing that, during this period, Iran supplied goods worth S£252.5bn (US\$1.7bn), out of a total of S£547.5bn from the top ten suppliers to Syria. A significant portion of the imports from Iran is thought to consist of crude oil, which is processed through the Baniyas refinery on the Mediterranean coast. Iran also supplies electrical equipment, flour, medicines and processed foods. Imports from Iran are mainly financed through lines of credit provided by state-owned banks in Iran. These include a US\$1bn facility for nonoil imports, of which at least half must be sourced from Iran, and separate facilities covering crude oil supplies from Iran and other sources. The Syrian government has recently indicated that it wishes to conclude fresh credit line agreements, as most of the previous facilities have been used up.

Ukraine and Lebanon came in second and third place, respectively, in the ranking of exporters to Syria. Supplies from Ukraine are likely to consist mainly of wheat and refined petroleum products. Petroleum products are also likely to account for a significant portion of imports from Lebanon.

#### Syria's main trading partners, Jan 1st-Jul 20th 2014

(S£ bn)

Imports from		Exports to	
Iran	252.5	Saudi Arabia	16.7
Ukraine	52.3	Lebanon	10.0
Lebanon	51.8	Jordan	7.7
Egypt	48.7	Iraq	5.3
China	34.1	Egypt	4.8
Turkey	30.8	Turkey	3.3
UAE	21.6	UAE	2.9
Jordan	19.9	Bulgaria	2.5
India	19.3	Qatar	2.4
Argentina	16.5	Ukraine	2.3
<b>Total</b>	<b>547.5</b>	<b>Total</b>	<b>57.9</b>

Sources: General Foreign Trade Organisation; Al Watan.

Exports to Syria's top ten markets amounted to only S£57.9bn (US\$390m) in the period covered by the GFTO data. The leading market was Saudi Arabia, followed by Lebanon, Jordan and Iraq. Syria's exports in 2013 and in the first part of 2014 have been dominated by phosphates, mainly involving sales from stocks rather than from ongoing production.

#### Impact on the forecast

Both sets of numbers look relatively low (we forecast imports of US\$7.7bn this year, and exports of US\$2bn), and, of course, they cover only the top ten markets. As a result, we are unlikely to incorporate these numbers into our forecasts, in the absence of supporting data.

