Why economic liberalism is not sufficient to change the Arab world and why politics is crucial. Lessons from Algeria and Syria

By

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Abstract

This paper assesses the role of politics in the failures of Syria and Algeria to change their economy. Indeed, the tremendous amount of reforms that had concerned Syria’s and Algeria’s financial system gave the impression that both countries were living a liberalization process. The recent upheavals confirm that this was an illusion. This article will examine why the adoption of economic liberalism, notably under the impulse of international institutions, had been a failure. The article will particularly focus on the financial and monetary architectures that have been preserved in order to maintain the control of financial flows. One interesting result is that the manifested economic liberalism has even strengthened the political power of the Syrian and Algerian authorities because it created new rent-seeking opportunities which had been used by the politics to recruit new elites that are now fighting to preserve the status quo in Algeria and Syria.

1. Introduction

In the 1990’s, in line with the literature on transition economies Algeria and Syria had chosen to respect the constraints imposed by the international institutions. For instance, Algeria was then seen as a bon élève of the IMF following its conservative monetary policy and in the huge cut of Algeria’s budgetary policy. The challenge was to abandon the old Arab socialism in these countries to succeed the transition towards capitalism. One major reference of the literature in the success of transition is Kornai (see Kornai, 1984, 2000).
Kornai (2000) proposes a conceptual framework from which one can evaluate the success of a transition from socialism to capitalism. The model of the socialist system shares the following specific common characteristics (Kornai, 2000, p. 29):

“1. Undivided power of the Marxist-Leninist party

2. Dominant position of state and quasi-state ownership

3. Preponderance of bureaucratic coordination

4. Soft budget constraint; weak responsiveness to prices, plan bargaining and quantity drive

5. Chronic shortage economy, sellers’ market, labor shortage and unemployment on the job.”

In opposition to that model, capitalism involves:

1. Political power friendly to private property and the market,

2. Dominant position of private property

3. Preponderance of market coordination

4. Hard budget constraint; strong responsiveness to prices

5. No chronic shortage, buyers’ market, chronic unemployment, fluctuations in the business cycle

In Kornai’s view, these criteria are seen as representative of both models and not as loyal reproduction of the reality.
According to Kornai, transition from socialism to capitalism succeeds when systemic changes occur. Indeed, Kornai draws a distinction between systemic changes that correspond to changes affecting the working of the system and even could disrupt its evolution and non-systemic change which relates to events that would not affect the system. For instance, in Kornai’s view, devaluation of a currency is a non-systemic change whereas the introduction of a currency convertibility is a systemic change. The five elements constituting the five former attributes have been selected because Kornai interprets them as elements that could be at the source of systemic changes.

Another important condition for success if that firms or more generally organizations should pass the standard survival test. In other words, if organizations/firms make losses, they should die. This is the spirit involved by the concept of a soft budget constraint (SBC) introduced first by Kornai when he examined the impact of market reforms in Hungary (Kornai, 1980). State-owned enterprises were not allowed to fail. They were always bailed out with financial subsidies. Firms could count on surviving even after chronic losses, and this expectation has an impact on their (inefficient) behaviour. Since Kornai’s first observations, the contention that softness of the budget constraint was a major cause of failures of socialist economies to promote economic development has received a favourable reception.

In Kornai’s framework, the most important element that could explain the success of a transition from socialism to capitalism is the political factor:

“These arguments imply that while the interaction of political power, property and the modes of coordination are all important in movements between capitalism and socialism or
back again, the political dimension plays the primary role.” (Kornai, 2000, p. 33, italics are mine)

What interests us particularly in this paper is that the political dimension in Kornai (2000) should not be understood as a reference to democracy since “democracy is not a necessary condition for capitalism to function” (Kornai, 2000, p. 29). What counts is that the political power creates market-incentives and either supports free enterprise or at least does not restrain too much private property and freedom of contract between individuals. Then, democracy is not a condition for a successful transition. Rather, it is capitalism which is a necessary condition of democracy (Kornai, 2000, p. 35). This paper will show that this assertion is highly questionable and that politics counts above all for the change to succeed. In particular, politics should not be understood in a narrow sense as a system that promotes private incentives in the political sphere. One major lessons of the Arab spring is that it illustrates how the introduction of capitalism was biased by the political sphere. One can even goes further and defends that the introduction of capitalism under the pressures of international institutions has led to the creation of new rents in the private sector that has either strengthen the power of installed authoritarian governments or created new mafias that have invested in the private sector. Both cases involve the same observation: economic liberalisation in Arab socialist countries, under the pressure of international institutions and following the inspiration of the political economy of reforms, has strengthened the power of political forces whose aim is to preserve the status quo. These political forces are now using their power to impede economic and political change in the Arab world. Section 2 will characterize Algeria and Syria as a socialist economy. Section 3 will present the main reforms that have launched the liberalization process. Section 4 will propose arguments that help to explain the failures of economic liberalism in Syria and Algeria. Section 5 will conclude.
2. Arab Socialism and financial controls

It is interesting to notice that Syria presents many similarities with Algeria as regards its financial organisation inherited from the past of these two Arab countries. Al-Ahmar (2007) insists on the French influence on the Syrian business legislation. It is worth noting that Syria and Algeria both chosen the path of socialist planning which led to a specific organisation of their financial systems. Figure 1 represents this intimate inter-connection between the political authorities, public bank and public firms.

Fig. 1 Representation of Arab Socialist Systems (Algeria, Syria)

If we apply Kornai’s framework to Algeria and Syria, it becomes clear that the economic system they adopted after independence can be characterized as pertaining to the socialist world for the following reasons related to Kornai’s five main building blocks.

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1 For Algeria, see Zouache and Ilmane (2009)
Firstly, from the political side, the political power has been centralized in the hands of a political party, the Front de Libération Nationale (FLN) in Algeria and the Socialist Arab Baath Party which “is the first movement in the Arab homeland which gives Arab unity its sound revolutionary meaning, connects the nationalist with the socialist struggle, and represents the Arab nation's will and aspirations for a future that will bind the Arab nation with its glorious past and will enable it to carry out its role in achieving victory for the cause of freedom of all the peoples” (Preamble, Syria’s Constitution, 1973).

Secondly, the development strategy chosen involved a control by the state of the economy or even more: it the duty of the state to intervene directly in the development of the country. Algeria opted in 1962 for a development strategy based on industrialization of the country since it had always been a political objective in Algeria. For instance, the 1976 National Act clearly identifies an industrial development strategy for Algeria: to support the industrial sectors, especially the chemical, steel and hydrocarbon industries, which are supposed to have external effects on other sectors, either agricultural or industrial, and to try to reduce the mass unemployment inherited from the colonial period. This development strategy had been financed with the oil rent that allowed a dramatic increase of investment in capital in the years following the independence of Algeria. The average investment rate was equal to 28.3 % between 1970 and 1973 and even rose to 40.4 % between 1973 and 1978, reaching a peak of 47.8 % in 1978 when it was one of the highest rates of investment in the world (World Bank, 2003, p. 12). In that perspective, Algeria embarked in the 1960s on an import-substitution strategy that led to the rapid development of a public manufacturing sector. From independence to the 1990s, the economy was under the control of state enterprises. About
1300 local public enterprises and 400 national companies accounted for about 80% of value added and 75% of employment in the manufacturing sector in 1993 (IMF, 1998, p. 17). Moreover, public sector employment at the end of 1991 accounted for 70% of industry, more than half of construction and 30% of services (ibid.).

This development strategy involved that public companies have always constituted the foundations of Algeria’s and Syria’s economic development.

Thirdly, after independence, Algeria and Syria quickly adopted a bureaucratic coordination through planning. This system was the result of an ideological choice that considered that planning was more efficient than market coordination for developing the ‘national economy’. This Soviet-type planning was formulated in physical terms. The fundamental principles that governed the financing of planned investments were the following:

• The centralisation of internal and external financial resources at the level of the Treasury, including central bank advances.

• Those financial resources were to be used to finance long term planned investment via the banking system;

• Otherwise, investments would be financed by medium-term credits that were automatically re-discountable at the central bank;

It must be noted that, given the planning mechanism, it was not obvious that there was an Algerian and a Syrian banking system as such. Once the plan was formulated and approved in physical terms, it was necessary to add the financial part.
In this system, the Treasury was at the heart of the political and economical controls. The role of the Treasury was to centralise long-term external and internal resources which were then distributed by the public banks among the public enterprises in charge of planned investments. The second step was to call on the public banks to take charge of medium-term investments in the form of credits that were both legally and effectively re-discountable by the central bank. Banks also financed the working of public enterprises insofar as short-term credits were freely re-discountable by the central bank. One consequence of this system was that the Central Banks had no autonomy as lenders of last resort. There was no real hierarchy between the commercial banks and the Central Banks so that the banking system constituted a one level system. The aim of this financial and banking system is to control the realisation of planned investments by the banks. This kind of economic and political system has a direct influence on the way monetary policies are conducted and the power central banks can ask for. Both are constrained by the political power, either the government or the Army.

In Syria, the Legislative Decree n° 87 dated 28/3/1953 presents the central bank as an independent public institution under the control of the government and within the general directions issued by the Council of Ministers, and exercised on behalf of the state concession issuing banknotes and cash management of the Fund. The central bank began its operations on the 1st of August 1956. The central bank managed the Office of Foreign Exchange. After the revolution of March 1963, legislative decree n° 37 of 2 May 1963 nationalised all banks operating in Syria. The 1953 decree ceased to be into operation. The central bank turned into mere storage of foreign currencies, domestic liquidity at the disposal of the government altogether and fill unload at other times. Finally, the central bank played the role of government financial agent.
Indeed, Syria’s monetary policy was in the hand of the government. Since 1963, the aim of monetary policy has been to stabilize prices and to achieve the goals of economic development and social stability. Since that date, monetary policy was designed primarily to achieve a balanced public budget. No monetary or financial markets had been designed. The only instrument used was the interest rates, an instrument fixed by the authorities. As in the case of exchange rates, there were multiple interest rates each affected to a certain purpose.

Interest rates remained stable in Syria for a long time. The basic economic reasoning was the following: to maintain stable and low interest rates so that it would encourage domestic investment and thus national production. Moreover, stable and low interest rates would lead to stable and low prices so that people with limited income could live under a certain standard (and would not be motivated to riot). However, in the eighties, because of high inflation, the real interest rates became negative until mid-1990s. High inflation in 2005 and 2006 also led to negative interest rate.

It should be noted that the Bank of Syria was also dependent on the planning system as regards its exchange rate policy. Now, Syria offers an incredible history of exchange-rate regimes (cf. table 1). This history shows that the exchange rate was clearly a political instrument. Fourthly, Algeria and Syria benefited from a soft budget constraint that can be explained by the rent furnished by the natural resources, mainly oil and gaz. Fifthly, Algeria and Syria have been clearly chronic shortage economies with labour shortage and unemployment on the job. The labour market was extremely rigid.
<table>
<thead>
<tr>
<th>Change of Exchange-Rates</th>
<th>Main change</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Before 1961</td>
<td>- Two exchange rates: official rate and free market rate</td>
<td>- Official rate set by the Exchange office and applied to the proceeds of major exports + the payment for most imports + few services</td>
</tr>
<tr>
<td>February 1961</td>
<td>- Free market rate abolished</td>
<td>- + Exchange-rate controls</td>
</tr>
<tr>
<td>July 1962</td>
<td>- The free market rate is reintroduced</td>
<td></td>
</tr>
<tr>
<td>May 1963</td>
<td>The legal free market rate is abolished</td>
<td></td>
</tr>
<tr>
<td>January 1964</td>
<td>The legal free market is set in a parallel market by the Commercial Bank of Syria in consultation with the central bank (the parallel market rate)</td>
<td></td>
</tr>
<tr>
<td>July 1973</td>
<td>The parallel and the official market rates are unified</td>
<td></td>
</tr>
<tr>
<td>April 1981</td>
<td>The parallel market rate is re-established</td>
<td></td>
</tr>
<tr>
<td>May 1982</td>
<td>A tourist rate is created</td>
<td></td>
</tr>
<tr>
<td>September 1985</td>
<td>A fourth selling rate is introduced</td>
<td>Applicable only to medical and travel expenses by Syrian nationals abroad</td>
</tr>
<tr>
<td>August 1986</td>
<td>A new “promotion rate” is created. The selling rate is thus abolished.</td>
<td>Applied to private remittances, travel abroad for tourism and medical treatment, imports of printed materials.</td>
</tr>
<tr>
<td>October 1986</td>
<td>Two specific rates introduced</td>
<td>For payment for airline tickets by non residents and for transfers of profits by airline companies</td>
</tr>
<tr>
<td>January 1988</td>
<td>The parallel and tourist rates are abolished</td>
<td></td>
</tr>
<tr>
<td>1989</td>
<td>Two new depreciated rates are created</td>
<td>An export promotion rate and a neighbouring countries’ rate</td>
</tr>
<tr>
<td>January 2007</td>
<td>The commercial and budget rates have been unified</td>
<td>Most restrictions on current transactions abolished</td>
</tr>
</tbody>
</table>

Table 1. Syrian “original” exchange-rate regimes since independence

*source: Hasan M and J. Dridi, 2008*
3. Economic reforms and liberalisation in Algeria and Syria

In both countries, rising unemployment and the decline of oil revenues on which state expenditures had long relied, following the decline in oil prices in the 1980s, created an urgent need for reforms. In both cases, this need involved a transition from socialism to capitalism. For instance, in Syria, the Ba’ath party, in a meeting in 2005, recommended a program of economic transition:

“Issuing the social market economy according to a gradual movement that protects the society, stressing the importance of the state’s role in the economy according to modern models, and re-qualifying the public sector in the strategic sectors, and strengthening the participation of the private sector in economic activities.” (Abboud, 2009, p. 3).

In Algeria, the Hamrouche government (1988-1991) promulgated a series of laws centered on the liberalisation of prices and the end of subsidies, the end of state monopolies on trade (imports), the liberalisation of the labour market with the adoption of the principle of labour flexibility. Two ordinances, 95/22 of the 26th of August 1995 and 95/25 of the 25th September 1995, organised the privatisation policy. But the most important reform was the law on money and credit of the 10th of April 1990, which, further to giving an institutional framework to the liberalisation of the banking and financial system, cut the state monopoly on foreign trade.

3.1 In Algeria

Algeria suffered from a series of political troubles from 1988 to 1998, which certain observers described as a civil war. These events followed years of economic downturn which the country experienced in the eighties after the oil price slump that caused a deterioration of
Algeria’s deficits and public debt. The Algerian authorities were then unable to continue sustaining the manufacturing public sector. Consequently, as was the case in many transition economies, by the 1980s, Algerian public enterprises were incurring major losses that caused a rise in industrial unemployment. From 1988, following the political troubles, Algeria launched a series of reforms that were understood as a signal that the country decided to abandon the old “socialist” system and to adopt the principles of market-oriented economies. These reforms affected both the political and the economic sphere.

*On the political reforms*

End of the “parti unique” + relative freedom of press + free mobility of journalists.

*On the economic reforms*

The reforms concerned the whole of the economic sphere.

Firstly, the financial architecture of Algeria has dramatically changed from 1990. The transition process in the financial sphere was first legitimised through the 1990 law relative to money and credit (LMC) which was inspired by French monetary and financial arrangements. There is a general agreement that the LMC was a decisive step on the path of economic reforms that Algeria took at the end of the 1980s. First, the LMC cancelled the legal domination of public enterprises over public banks by suppressing (a) the obligation for a public enterprise to keep its accounts at a single bank, and (b) the automatic granting of credits to public enterprises by public banks. Furthermore, the granting of credit had to follow prudential rules, notably on the division of risks and the provision of funding. Second, the LMC increased the autonomy of the central bank relatively to the Treasury. More specifically, from 1990 to 2003, the Bank of Algeria benefited from a legal framework – the 90–10 law
relative to money and credit (LMC) promulgated on 14 April 1990 – which improved its legal independence compared to the socialist era, but the Bank did not enjoy a de facto independence, in particular because of the political context and the supervision of the IMF. Since 2003, the new ordinance led to a decrease of the legal independence of the Bank of Algeria. However, in practice, with the relaxation of the institutional constraints, the de facto independence increased.

Secondly, the LMC increased the autonomy of the central bank relatively to the Treasury. From the 1965 complementary finance law that suppressed the limitation of central bank advances to the Treasury, the budget deficit had been systematically monetized. At the end of 1989, the debt of the Treasury with regard to the central bank was equal to 110 billion dinars. At this date, the overall debt of the Treasury vis-à-vis the banking system represented 50 per cent of the internal public debt.

The LMC put an end to this situation through the following articles:

• Article 213 obliged the Treasury to repay its debt to the central bank over a period of fifteen years and according to a convention between both institutions.

• Article 78 restricted the impact of the annual public budget since it put an upper limit on central bank advances to the Treasury equal to 10 per cent of the ordinary fiscal revenues of the current fiscal year and set a maximum duration of 240 days. The whole of the advances has to be paid back before the end of the fiscal year.

• Article 77 put an upper limit on the amount of public assets that the central bank could hold in its portfolio to 20 per cent of the ordinary fiscal revenues of the current fiscal year.
• Article 80 obliged the central bank to keep in its National Girobank account (CCP) an amount of resources equivalent to its annual expected needs.

• Finally, article 93 established mandatory reserves which allowed the central bank to regulate banks’ liquid assets so that the compulsory subscription of Treasury bonds by the banks no longer had any raison d’être.

Thirdly, Algeria tried to promote market incentives and the rise of private firms. Algeria adopted at the end of the 1980's a market-oriented economy that provided a favourable context for the emergence of new entrepreneurs. In 2001, a national agency for the development of investment (ANDI) was created. The 01-18 law was promulgated in the same year to support entrepreneurship in small and medium enterprises.

Fourthly, the labour market has been reformed through three laws in 1990, 1994 and 1997 (Ruppert, 1999). The aim of the reforms was to make the labour market more flexible and to facilitate layoffs in order to reduce mass unemployment. In particular, the Algerian authorities adopted a new retrenchment system in order to reduce the number of redundant workers in the public sector. (Ruppert, 1999). Thus, firing conditions had been softened. The Algerian political authorities have committed to not intervene in wages bargaining. Union liberty has been increased and strikes have been allowed. These laws gave the liberty to private firms to fire their employees. Administrative constraints that were imposed on layoffs are suppressed. Collective bargaining between unions and firms is promoted to take the place of the government in the determination of labour conditions, including wages and firing.
3.2. In Syria

Since the beginning of Bashar al-Assad’s presidential mandate in 2000, it has been considered by the Syrian authorities that the financial and banking sectors should be the engine of reform and economic development. Reforming financial institutions would raise the efficiency of the Syrian economy and its competitiveness. In order to increase the volume of public and private investments - both national and foreign - the Syrian authorities, in their economic plan for the period 2005-2010, aimed the development of the monetary sector and the achievement of “full” independence of the Central Bank of Syria. Different institutional reforms had occurred (laws, decrees) so that Syria’s financial organisation changed. In particular, since 2001, Syrian’s Council of Money and Credit now manages monetary policies.

Considering that the creation of an integrated banking system needs a wide variety of financial institutions, a number of laws and legislation governing the development of such institutions had been adopted. From the viewpoint of monetary policy, in accordance with the new competences of the Council of Money and Credit, a number of measures has been adopted. For instance, a monetary market has been created which allows transactions between banks on the one hand and between banks and the central bank on the other hand, transactions either in Syrian Lira or in foreign currencies. Furthermore, banking rates have been partially liberalised with a margin of 4% on interest rates set by the Council of Money and Credit. Syria experienced in the 2000s a series of reforms that apparently changed the monetary and financial environment. Main reforms are synthesised in table 2.
Table 2. Change in Syrian monetary and financial legislations

<table>
<thead>
<tr>
<th>Main laws/decrees</th>
<th>Main contribution(s)</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Law n° 28 – April 2001</td>
<td>- Private Banks allowed</td>
<td>- Every private banks should be hold in majority by Syrians citizens - Minimum capital: 30 billion dollars</td>
</tr>
<tr>
<td>Law n° 29 - 2001</td>
<td>- Banking secret is warranted</td>
<td></td>
</tr>
<tr>
<td>Law n° 35 - 2005</td>
<td>- Islamic Banks allowed</td>
<td>- Minimum capital: 100 billion dollars</td>
</tr>
<tr>
<td>Law n° 23 - 2002</td>
<td>- Creation of the Council of Money and Credit (CMC) - The Central Bank of Syria (CBS) controls public and private banks.</td>
<td>- The CMC defines monetary policy - The CBS depends on the Treasury</td>
</tr>
<tr>
<td>Decree 43 - 2005</td>
<td>- Private Insurance Companies are allowed</td>
<td></td>
</tr>
<tr>
<td>Law 22 - 2005</td>
<td>- Gives the conditions under which Damas Stock Exchange would be created</td>
<td>- Opening of Damas Stock exchange expected in 2009</td>
</tr>
<tr>
<td>Law n° 24 - 2006</td>
<td>- Exchange operations on foreign money with non-banking actors are allowed</td>
<td>- Bureau de change, specialised society</td>
</tr>
</tbody>
</table>

Concerning the banking system, table 3 presents main banking actors in Syria. These legislations had supposedly contributed to the enrichment of Syria’s monetary and financial environments. The principle of competition between private and public banks is now accepted. Islamic banks have also recently been introduced. Actually, there are in Syria six public banks competing with private banks in addition to the Islamic banks that have recently been licensed. Many licences are still under study, either at the level of exchange companies and banking offices. In terms of the insurance industry, a number of insurance institutions were expected to be licensed.
<table>
<thead>
<tr>
<th>Table 3. Banking Actors in Syria</th>
</tr>
</thead>
</table>
| **1. Public Banks** | - Commercial Bank of Syria (later monopolist)  
- Industrial Bank  
- Savings Bank  
- Land Bank  
- Agricultural Bank  
- Popular Bank |
| **2. Private Banks** | - Banque Saudi Fransi  
- Jordan’s Housing Bank for Trade and Finance  
- Saudi Arabia’s Banque  
- Bank Audi  
- Lebanon’s Banque Européenne pour le Moyen-Orient  
- Syria Gulf Bank  
- Bank of Syria and Overseas  
- Arab Bank Syria  
- Fransabank  
- Byblos Bank Syria |
| **3. Islamic Banks** | - Syria International Islamic Bank  
- Cham Bank |
| **4. Others** | Micro-Finance banks created in 2009 (Agha Khan Foundation) |

4. Economic liberalism vs political change?

4.1. When one accepts Kornai's criteria or why economics is important
The first argument relates to the monetary and financial reforms. Finally, these reforms have not revealed systemic. When they were systemic, the political power has decided to amend some of them.

In Algeria

For instance, the changes made to the LMC in 2001, then its abrogation and finally its replacement in 2003 have considerably reduced the legal independence of the Bank of Algeria for two main reasons.

The first reason is related to article 13 of ordinance 01-01 dated 27–12–2001 which cancelled the arrangements made in article 22 of the LMC relative to the mandates of the governor and of the vice-governors. Article 10 of the same ordinance added to the seven members of the Council of Money and Credit three new external members, turning the managers of the Bank of Algeria into a minority. Those members were two professors in economics and the general secretary of the Association of Banks and Financial Companies (ABEF). Here, it is important to remember that Algerian banks are mainly public banks under the control of the Minister of Finance.

The second reason derives from the 03-11 ordinance, especially article 46, according to which ‘the Bank of Algeria is also authorised to consent exceptionally to the Treasury an advance exclusively aimed at the active management of the external public debt’. Clearly, this clause allowed the financing of the budget deficit. It is true that this possibility has not been used so far because of the budget surplus resulting from the favourable oil context. But the intention was clear. In the 2004 finance law, a line ‘advances to the Bank of Algeria’ had been added to the resources from the revenue regulation fund (FRR) which had been created following the rise in the oil price.
In the same vein, the commitment of Algeria to privatize different financial institutions had come to an end – thanks to the financial crisis. Indeed, the privatization projects of several banks - Crédit Populaire d’Algérie (CPA), Banque de Développement Local (BDL), Banque Algérienne de Développement Rural (BADR) and financial institutions – Compagnie Algérienne d’assurance et de reassurance - had been abandoned.

The second argument is that the reserve funds that had been created by the Algerian authorities have softened the budget constraint of Algeria. This fund had been designed to reduce the public debt and to protect public expenditures from fluctuations in the budget surplus due to unpredictable variations in the oil price. The 2006 finance law made the situation official. It allowed the financing of the Treasury deficit up to a limit of 740 billion dinars (10 billion US dollars). That means that if the resources from the FRR are insufficient, there remains the possibility of ‘printing money’. What is revealing is that, even if the financial resources of the FRR are largely positive, and, despite its good financial situation (a surplus of 3244 billion dinars at the end of 2006), the Treasury called in the second half of 2006 for exceptional advances from the Bank of Algeria aimed at the reimbursement in advance of the re-scheduled debt (Bank of Algeria, 2007). In other words, a part of Algeria’s external debt has been transformed into internal debt.

In this perspective, the change of fiscal policy of the recent financial crisis – and especially the 2009 complementary fiscal law – appears as a prolongation of a radical attempt from the Algeria authorities to soften the budget constraint as it was the case in the first years after independence.
The third argument is that even if the Algeria authorities have reformed the exchange-rate regime, the dinar is not fully convertible. Then, this partial convertibility involves that the reforms on the exchange-rate regime were not systemic.

The exchange rate regime was also brought within the control of the IMF. Under the structural adjustment programme, Algeria’s exchange rate regime became in 1996 a managed float with no pre-announced path for the exchange rate. This floating exchange rate regime was established in several steps. From September 1994 to December 1995, the managed float regime was implemented through fixing sessions between the Bank of Algeria and the commercial banks. At the end of 1995, the Council of Money and Credit initiated an inter-bank foreign exchange market that was established in 1996. But this market has never really functioned, since forward transactions have not been made feasible. Accordingly, the Algerian dinar turned out to be a partially convertible currency: it is not fully convertible but it is commercially convertible, which means that any locally registered enterprise can import goods and pay by debit of its Algerian dinar account without prior approval from the Bank of Algeria. For payments of services, prior approval from the central bank is needed. This partial convertibility of the Algerian dinar enables the Bank of Algeria to monitor all international financial operations carried out by public and private banking institutions.

The fourth argument is that a private sphere has not emerged yet. In particular, Algeria has not benefited from the rise of a new class of entrepreneurs. An econometric study based on a survey gathering 256 small firms located in seven Algerian regions (wilayates) and representing eight industrial sectors, reveals that the institutional heritage remains crucial: the
“new entrepreneurs” are not so new since they often come from the old socialist public sector (Belarbi and Zouache, 2010).

The fifth argument refers to the working of the labour market. Again, the reforms conducted by the Algerian authorities has not produced a systemic change. In certain cases, the political power has blocked the impact of these reforms. The main result is that workers have been displaced from the public sector to the informal sector. According to the Algerian national bureau, the share of informal employment in total employment increased from 39 % in 1997 to 49.1 % in 2005 (ONS, 1997 and 2005). Furthermore, the political authorities have maintained its bargaining power in the labour market. The main union, Union Générale des Travailleurs (UGTA) collaborates closely with the successive governments whereas independent unions are not considered as legitimized partners. In the private sector, less than 5 % of workers are unionized.

In Syria

We particularly examine whether the changes in legislation led to a greater independence of the central bank of Syria. To our knowledge, this issue has not been grasped in the recent literature. Even Gisolo (2009) who examined the legal independence of a sample of MENA central banks excluded from his basic analysis Syria.

Let us first look at decree n°87 which defines the founding functions and tasks of the Central Bank of Syria:
- Issuing the national currency. The Issuing of the currency Syrian is a privilege of the state attributed exclusively to the Central Bank of Syria on behalf to meet the needs of the development of national economy. The Central Bank of Syria is thus the only financial institution capable of managing the entire monetary circulation in material terms.

- The central bank is the “bank for banks”. The central bank is the lender of last resort for banks. Consequently, the central bank of Syria can monitor the implementation of the policy credit and assess how it fits with the requirements of the national economy.

- The central bank issues the national bonds of different terms and carries out exchange and payment processes. The central bank also contributes to the negotiation of international agreements of payments and foreign exchange operations.

- The central bank obliges the banks to have a certain level of compulsory reserves in the forms of bonds issued guaranteed by the State.

- The central bank under the provisions of the basic monetary system, functions as the financial agent of the Syrian State.

- The Central Bank of Syria supervises the public and private banks operating in Syria.

We note that this decree does not provide many details but is in line with the philosophy of most of the laws of that period, that is the generality and the numerous potential interpretations, so that the government keeps a great monetary power.
Concerning the financial institutions, the main change concerns the creation of the Council of Money and Credit (CMC). What is interesting to notice is that, despite this change, Syria’s new financial system seems still close to the old socialist functioning. Let us presents two arguments.

Firstly, when we look at the members of this council and analyse their mission, one should be careful with the extent to which these reforms had really changed Syrian’s financial systems. Indeed, the members of this council are:

- The president of the council is the governor the central bank of Syria;
- The first deputy governor of the central bank of Syria is the vice-president of the CMC;
- The second deputy governor;
- The deputy minister of the Ministry Economy and Trade;
- The deputy minister of Exchequer;
- The deputy minister of the Ministry of Agricultural Reform;
- The deputy minister of the Ministry of Industry;
- The head of the state planning council;
- Three members experts in money and credit.

Eight members are government officials and have the rank of deputy minister. It should be noted that banks are not represented in the CMC. In addition, the Finance Minister has the
right within seven days to stop the implementation of the resolution if it considered contrary to the interests of the state:  

“The decisions taken at the Monetary and Credit Council have to be presented to the Minister of Economy and Foreign Trade. The Minister can suspend the implementation of any decision he deems it is contrary to the interests of the state for up to seven days to get re-introduced resolution to the Council and in the event of continuing divergence of views is incumbent on the Minister of Economy and Foreign Trade presents to the Cabinet for a decision quickly”

Secondly, the missions of the CMC reveals that it is at the service of the government. Indeed, the CMC warrantee the coordination between banking and financial institutions in order to reach the objectives defined by the authorities. The CMC stabilises the parity of the Syrian pound and guarantees its convertibility Moreover, the CMC organises and develops monetary and financial markets for the needs of national economy. In other words, the CMC is in charge of the monetary Policy of the “Syrian Arab Republic” as it is defined by the Syrian State.

4.2. The crucial role of politics

The main argument is that the economic reforms imposed from international constraints had not been efficient and had even strengthened the power of authorities, either in Algeria or in Syria.

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2 Article No. 8 of the law of money n° 23 of Syria in 2002.
In Algeria

“dropping oil prices and high repression costs brought Algeria close to bankruptcy and the Algerian government had little choice but to embark on an IMF structural adjustment program in order to reschedule the foreign debt and receive international credits. Yet, the selective way in which market reforms were implemented – for instance, liberalizing trade but keeping the state’s heavy hand on the bank and credit system – favoured the emergence of private sector elites with close ties into the public administration and the security apparatus, in some cases they emerged from the latter.” (Werenfels, 2009, pp. 182-183)

Despite the pressure of international institutions and the intent expressed by the Algerian authorities, economic liberalisation has caused a reproduction of the former authoritarian system for the following reasons (see Werenfels, 2002, 2009).

Firstly, the appearance of new actors, such as the “Islamist” leader from the Front Islamique du Salut (FIS), caused an increase in the number of actors belonging to the political elite. The maintenance of the political system combined with the appearance of these new actors involved the necessity to distribute new rents to these actors that have accepted to enter into the political game in a “legitimate” way, that is the actors that elites with vested interests in the statues quo. Thus, and secondly, market reforms, and here particularly trade liberalisation brought new rent-seeking opportunities directly dependent on the import sector. Indeed, the majority of goods and services consumed in Algeria are goods and services imported. Consequently, liberalisation created a new business elite that emerged both from the military bureaucratic apparatus (Werenfels, 2009, p. 182) and from the new “islamist” elite that have accepted to play the rule of the Algerian authoritarian game. The political participation of “Islamists” in the Algerian government began in 1992 when the authorities decided to
integrate some of the Islamists opponents in the political regime, in order to isolate the FIS. In 1996, the Islamists, now gathered in a new political party (MSP) accepted participating in the government with two ministers, and since then they have always been present in the government. In 1999 they even participated to the presidential coalition with the National Liberation Front (FLN), the National democratic assembling (RND), and the (MN). In 2004 the coalition was renewed without (MN), and it still exists until now.

Finally, the political openness ended with the end of constraints, especially because of the rise in oil prices. The recent change of the constitution – giving the right to the president to be re-elected until his death- marks the end of the political process of democratization and the success of the reproduction of the Algerian authoritarian system. This change has been made possible by an improvement of the economic situation in Algeria, that is an increase of the oil rent but also the creation of new rents, thanks to the liberalisation process.

**In Syria**

Despite differences between both countries, the impact of liberalisation has produced similar effects: the appearance of new rent-seeking opportunities distributed both to the former military/ba’ath actors and to the new military and economic elites. One can even conclude that abandonment of the socialist planning strategy and the adoption of market reforms had strengthened the authoritarian regime:
“By 2005, he [Bashar-al-Asad] had consolidated his power without resort to violence, purges or repression and largely through legal and institutional means.” (Hinnebusch, 2009, p. 2-3)

What was these “institutional means”? Firstly, like in the case of Algeria, the challenge was to integrate new actors in the political game. But, instead of integrating the “Islamists”, the Syrian authorities chose to recruit technocrats in order to renovate the administration of the regime: “He [Bashar-al-Asad] also engineered, within three years of succession, a renovation of the political elite, with a turnover of 60% in top offices, thereby transferring power to a new generation. His priorities were reflected in those he recruited to ministerial office, most of whom could be characterized as technocrats with Western advanced degrees in economics and engineering and favouring integration into the world economy.” (Hinnebusch, 2009, p. 2)

Secondly, like in the case of Algeria, economic liberalisation created new rents in the private sector. Schmidt (2009) gives a perfect illustration of this phenomenon in the case of the mobile industry:

“Syria was one of the last countries to introduce mobile phone services. In the year 2000 the government licensed two private companies to supply the services: Syriatel and ‘94’. Syriatel was owned by the Egyptian company Orascom (25 per cent) and by Rami Makhlouf (75 per cent) who happens to be the cousin of the Syrian President. Orascom provided the management. The license with the government was a build-own-transfer (BOT) contract for fifteen years. The other mobile-phone company, ‘94’, was owned by the then Lebanese Minister of Communication, Mekati, and by Rami Makhlouf. There is no competition on prices, as these are set by the state agency, the Syrian Telecommunication Establishment.
Competition between the two companies is restricted to marketing, customer service and signal coverage. The operation is hugely profitable.” (Schmidt, 2009, p. 30).

Schmidt (2009, p. 41) concludes that the economic liberalization process in Syria has resulted in “a zero-growth, un-dynamic, rent-seeking, and inequitable economy, which is more dependent on oil-revenue than ever.”

5. Conclusion

An implementation of Kornai’s grid (2000) to the cases of Algeria and Syria led us to two main results. Firstly, the reforms have not caused systemic change in the economic system. In particular, the financial architecture in Algeria and Syria (central bank, banking and financial system) is still under-developed and fiscal policies are used to soften the budget constraints. Secondly, the political power has not accepted to sustain systemic changes. Consequently, the selective economic liberalisation that Algeria and Syria have chosen to adopt from the beginning of the 1990s has not led to democratization dynamics. On the contrary, the economic neoliberalism accepted by the authorities had made more complex and more difficult political changes since new actors appeared on the scene. Now these new actors have adopted a rent-seeking behaviour and thus defend the status quo. One lesson we can learn from this study is that changing legislation is not a sufficient condition for transforming the institutional environment. A political change is needed.
Indeed, the tremendous amount of reforms that had concerned Syria’s financial system gave the impression that Syria took a new path towards the adoption of a market economy. But this was not the case. Syria did not really break with her past for at least two reasons. Firstly, Syria’s banking system still presents the picture of a system in line with the socialist principles where the economy is organised around a closed relationship between public banks, public firms and the government. Secondly, Syria’s authorities still have a direct control both over the new institutions created, as the Council of Money and Credit, or former institutions as the central bank.

In the same perspective, in the 2000’s, Algeria changed completely its economic policies, especially its fiscal policy. This change led to two successive fiscal waves, followed by a third one estimated to 150 billions US dollars. These programme revivals were not, by essence, in contradiction with the literature on transition economies since they primarily aimed the renovation of Algerian infrastructures. But, recently, a complementary fiscal law (2009) points out a new ambition: to protect the national economy. This new orientation questions Algeria’s economic strategy. Is Algeria coming back to its old socialist system? Is it a break caused by the financial crisis? This paper shows that the complementary fiscal law is only one event among many others that testify to what extent the selective economic liberalism adopted by the Algerian authorities was an illusion that hided the political will: to maintain a status quo.

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