Syria: Decoupling the Dollar

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Syria has taken another step towards unpegging its currency from the US dollar, a move initiated in August last year, and now expected to come into force in September.

On August 15, Prime Minister Muhammad Naji Al Otari signed the formal decree authorising the linking of the Syrian pound to a mixed basket of currencies, rather than the long-standing tie up with the dollar.

"The prime minister signed the official decree today, and the new basket will be completely adopted within a month,"reported Adib Mayaleh, Syria's Central Bank governor. "The currency will be linked to the International Monetary Fund's (IMF) special drawing rights (SDR), which represent a basket of currencies including the dollar, euro, yen and the UK pound."

Initially, the decoupling with the dollar had been planned for the first half of this year, but the Central Bank announced in June more groundwork needed to be laid.

Under the new scheme, the dollar will account for 44% of the total, with the euro representing a further 34%, and the British pound and yen 11%.

The shift was in part prompted by Washington imposing trade and financial sanctions on Damascus back in 2004, and confirmed in May last year following a ban on the Commercial Bank of Syria from dealing in US currency over allegations that it had links to illegal activity. Most analysts see the move to adopt the IMF's SDR basket as making sound economic sense.

According to a report on the Syrian economy released by Bank Audi Saradar in early August, the decision to break with the dollar peg is a positive sign that the Central Bank is doing all it can to combat inflation.

"The decision to peg the pound to the IMF's currency is actually a favourable move, in line with the country's trade portfolio," the report said. "Within this environment, Syria is witnessing an improvement in its global risk positioning."

Mayaleh said Syria had no plans to change its policy of maintaining a stable exchange rate but wanted to achieve a better balance through adopting a more diversified basket.

"The switch to a basket of currencies will help us deal better with volatility in the international currency market," he said. "We took this decision for purely financial reasons. Europe is a major trading partner and the euro constitutes a major part of our reserves."

According to Abdallah Dardari, Syria's deputy prime minister for economic affairs, severing the link with the dollar would help "reduce the impact of dollar exchange rate fluctuations with other currencies which will give more stability to the Syrian pound," he said on August 8.

With the fall in value of the US dollar, the Syrian pound lost around 10% of its value last year, adding to the costs of imports, especially from Europe. In June, the Central Bank estimated that decoupling the Syrian pound from the dollar would take two percentage points off the country's inflation rate, which hit 10% in 2006, in part a reflection on the weaker local currency.

Though the new currency peg has yet to come into force, Syria has already moved to distance itself from the dollar, now pricing its main export - oil - in euros. It has also diversified its foreign currency reserves, previously all in dollars, to include a spread that takes in dollars, euros, sterling and Swiss francs, with the greenback representing around half the total of $20bn currently held.

Ending the long standing link between the currencies of the two countries is allowing Syria to leverage itself a better exchange rate while at the same time reducing Washington's leverage on Damascus.