SYRIA AND THE MEDITERRANEAN PARTNERSHIP

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Foreword

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The two studies in this publication on Syria's EU Association Agreement depart from fairly divergent assumptions about the long-term consequences of economic liberalization under EU auspices but tend to converge on the conclusion that, at least in the short run, the agreement's likely costs outweighed its benefits. It gives only marginally better access to Europe's protected agricultural market. Syrian industrial goods already have such access but Syrian exports to Europe are mostly crude oil anyway; however, Syria's increasing non-oil trade with other markets will face discrimination. On the other hand, the agreement exposes Syria to de-industrialization and its agriculture to European competition. It cripples the state as a generator of backward and forward linkages by forcing public sector procurement open to European companies. It will produce unemployment and trade deficits. The agreement is more disadvantageous to Syria than the agreements signed by other Arab countries with the EU; in particular, Syria's agricultural and public procurement markets would be forced open in a way these other states did not face while adjustment funding is substantially lower.

Why should such an inequitable deal have been negotiated? The deal calls in question the idea of the EU as a benign actor for whom the developmental interests of LDCs are a priority. As Dostal shows, the Partnership Agreements have become an instrument for imposing the neo-liberalism that favors the core onto the periphery states. But what explains Syria's readiness to accept it? If this agreement was sought as a political shield against US hostility, it proved irrelevant. If Syria's negotiators were outmanoeuvred, it makes a contrast to Syria's reputation for tenacious bargaining under Hafiz. If the agreement was seen by the reformers as a weapon against entrenched statist interests or to credibly "lock-in" reforms, or to evade responsibility, by pointing to its legally binding character, for the social consequences of reforms, it contrasts with the Hafiz period when austerity was imposed without a major sacrifice of national autonomy. If Syria's reformers uncritically swallowed neo-liberal ideology, even as it is going out of fashion elsewhere, the episode shows the costs of authoritarian governance even in the hands of reforming technocrats. Syria was lucky that the EU declined to ratify the agreement.

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The European Union and Economic Reform in Syria

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Introduction

This paper analyses the Association Agreement of the European Union (EU) with the Syrian Arab Republic, an element of the EU's 'European Neighbourhood Policy' (ENP), which was 'initialled' by EU and Syrian negotiators in 2004 but has so far not been ratified. The discussion falls into five substantial sections followed by a conclusion.

The first section outlines how the Association Agreements of the EU with Mediterranean non-EU states contribute to a new neoliberal policy of global competitiveness which is based on the transformation of the political economy of the state – that is, of its role in the economy. Syria is put forward as a critical case with which to analyse such shifts in statehood. The second section examines how the EU and other international organisations put forward demands for changes in developing countries' political economy in particular, the EU demands that developing countries agree to the opening of their domestic markets and to large-scale trade liberalisation, irrespective of their stage of socio-economic development. This push for trade liberalisation has been part of the EU's 'grand vision' for a set of ten Mediterranean partner countries (including Syria). It was originally supposed to contribute to the creation of a Euro-Mediterranean free trade zone by 2010 (European Commission 1994). While this goal is unlikely to be realised by the original deadline, it nevertheless provided the starting point for a degree of 'regulatory convergence' (Müller-Jentsch 2005) between the EU and Mediterranean countries that has been informed by orthodox neoliberal economic doctrine. This concept has been put forward jointly by the EU, the international financial institutions and the World Trade Organisation (WTO). Section three proceeds to analyse the draft of the EU-Syrian Association Agreement in detail and demonstrates that the provisions place high demands on Syria. In particular, the Agreement links political and economic issues and contains substantial points that did not feature in the other nine Euro-Mediterranean Agreements. The fourth section sketches the history of Syrian economic policy-making and some of the main socio-economic challenges facing the country. The fifth section outlines the course of Syrian economic reform under the Presidency of Bashar al-Asad since 2000. It is suggested that the Syrian government has made substantial efforts to follow an agenda of global competitiveness but that the structure of Syrian trade, which relies heavily on declining oil rents, places question marks against the project of full-scale liberalisation of the Syrian economy. In particular, domestic demands for social protection from the results of the liberalisation process are not addressed in current policy-making.

In conclusion, the paper argues that the EU will have to negotiate the tension between a simple transmission of the 'Washington consensus'[i] as regards the liberalisation of global trade and its own foreign policy objectives in the region. Thus, EU member states must decide whether to assume the position of transmission belt for a neoliberal agenda as put forward by the Bretton Woods institutions or, alternatively, whether they would be prepared to offer resources and long-term commitment to contribute to political re-regulation and stabilisation of Syria and the larger Middle East region.

Defining the politics of global competitiveness

The concern with global competitiveness is a core element of today's neoliberal capitalism. The political project of neoliberalism emerged in the 1970s, became dominant in Anglo-American countries in the early 1980s and in the member states of the then European Community (EC) in the late 1980s (the EC was transformed into the European Union (EU) in 1992). It turned into the global framework of reference after the dissolution of the state-socialist systems in Eastern Europe and the Soviet Union.

In brief, neoliberal capitalism is based on a combination of at least seven core features that, taken together, enforce the subordination of social relations to market discipline: (1) deregulation of the labour market and cuts in social and employment standards; (2) privatisation of the public sector; (3) removal of barriers to trade such as non-tariff barriers (a process which tends to reinforce rather than remove existing trade asymmetries which favour the advanced OECD countries); (4)

deregulation of financial markets and increased global capital mobility; (5) increased commodification of the sphere of education and social reproduction; (6) full commodification of agriculture and elimination of remnants of subsistence farming; and, last but not least, (7) permanent discursive pressure to limit state agency and social reforms in favour of accepting market outcomes. In sum, the supporters of the neoliberal transition hold that market agency, rather than societal self-organisation and regulatory intervention, provides for the best possible coordination of competing interests in society, thereby increasing overall welfare.

At the same time, most neoliberals have moved beyond the simple anti-statism of their classical liberal predecessors. They now acknowledge that the interests of capital demand both the selective 'rolling back' and 'rolling out' of state agency. What is required is on the one hand a 'competitive state', moving away from direct service provision and towards an indirect and 'enabling' function, that serves rather than limits the scope of private capital to dominate society. Thus, what is 'rolled back' is the state's function as promoter of social welfare: the role of organised labour and of social democratic reformism declines while the state shifts policy to facilitate the dominance of capital at the cost of neglecting the demands of other groups. What is 'rolled out', on the other hand, is the state's function as a supplier of the infrastructure of accumulation and of complementary education systems. The process is no longer dominated by earlier quasi-Keynesian policies that were largely based on public sector bureaucracies and increases in overall public spending. Instead, neoliberal policy facilitates private investment into or direct takeover of core functions of the traditional public sector. Thus, public spending now needs to be vindicated and rhetorically framed as facilitating competitiveness rather than social integration. Overall, it is appropriate to suggest that neoliberal statehood depends more on coercion and less on hegemonic incorporation of the popular classes and their interests.

A crucial source of neoliberalism's strength is its global scope. It is based on the assumption that *all* countries need to follow a set of standard policies. Whilst starting at different points, low and mid-income countries and OECD countries must all engage in structural reform to open their markets, facilitate the transformation of the state to serve private capital more effectively, downsize the public sector and open it to competition, shift the burden of social spending towards 'active' measures meant to develop a more competitive workforce and accept that states can no longer provide solidaristic protection against market forces. Advocates of neoliberalism pursue a strategy of presenting such polices as based on international convergence which is driven by 'model countries' and 'best practice'. It is suggested that 'policy learning' would be facilitated by the copying of models. However, this one-size-fits-all approach is misguided: it ignores national path dependency and the limited regulatory capabilities of developing countries thereby resulting in inappropriate policy choices (Casey and Dostal 2008). What is on offer, in fact, is a global competitive hierarchy based on winners and losers. In other words, joining the liberal open market system certainly does not offer any guarantees against failure. But not to join means to be a certain loser as all outsiders must fall further behind the rate of economic growth and degree of 'competitiveness' of the advanced OECD countries.

In the neoliberal order, the strong and the weak return to their 'natural' position in the global hierarchy, i.e. a global division of labour in which the economies of the periphery serve the needs of the core. If economically weak developing countries want to maintain any prospect of future prosperity, they need to accommodate to this natural order. Their demands for recognition must be based on niche strategies – the pursuit of competitive advantage in tightly limited areas of economic specialization (Gereffi 2008). Moreover, they must accept trade rules that are put in place by the OECD countries, thereby abandoning 'unreasonable' economic nationalism. Next, they need to dismantle existing industrial policies and protection of domestic markets from external competition as they limit the attractiveness for foreign direct investment, which is seen as the most crucial indicator of emerging 'competitiveness'.

In sum, the less developed countries are asked to follow the neoliberal policies that have been introduced in Europe and North America since the 1980s. However, they arrive at this juncture from a different point of origin because state legitimacy, especially in the Middle East region, and in Syria in particular, has been based on a social contract in which states were obliged to provide for the basic economic needs of citizens. For example, Syrian developmental policies during the period of import-substituting industrialization in the 1970s included the construction of a modest national welfare state.[ii] Moreover, in developing countries the impact of neoliberal restructuring is potentially more severe. In particular, many groups live close to the poverty line and the middle class is less isolated from the threat of social decline.

Thus, many sections of society are likely to see a deterioration in their social status as a breach of an implicit contract between their social interests and state agency. In more general terms, the imposition of neoliberalism in developing countries also fails to recognize that practically all successful industrializing countries apart, from the UK as the first developer, have protected their infant industries behind tariff walls. Moreover the role of the state has continued to expand in the later stages of development. In sum, the neoliberal programme for developing countries ignores the historical track record and proclaims that past experience is no longer valid.

Moving on to the question of how the neoliberal 'model' of capitalism is disseminated, the connection between domestic and supranational politics has been stressed (Dostal 2004; Harvey 2006). In particular, coordinating institutions such as the IMF, World Bank, OECD and WTO act as agents of neoliberal restructuring. Their supranational character helps to insulate them from domestic pressures and interests as long as the dominant member countries support their normative political stance. Their role is to subject both business and labour to the disciplines of capitalist competitiveness. They do so by combining their own supranational authority with the authority of national states. Both sides influence each other, in particular the major OECD countries remain the dominant actors within supranational institutions in 'deciding on their functioning, structure and conditions of entry, and sustaining them financially' (Özkırımlı 2005: 134). Thus, when OECD governments become objects of supranational regulatory intervention, this is to a large extent of their own making and carefully controlled. Developing countries experience this intervention differently: supranational institutions offer advice with little scope for tailoring it to the needs of the individual state. Indeed, the stability of the neoliberal normative framework depends on its apparent universality. The neoliberal transformation of domestic capitalism requires the acceptance of 'objective' external pressures that enforce adaptation in order to prosper in economic competition with other countries. It has been pointed out that:

> the political economy of global competitiveness is *simultaneously* systemic and state-centered…. It is for that reason both that the state is central, and that the logic must operate at a global level if it is to be effective at the national level (Cammack 2006: 4-5, emphasis in the original).

What is new here is that the member states of the EU and other OECD countries accept not only responsibility for their own domestic neoliberal reform but insist that all states have to join and that the project is now genuinely global in scale. In institutional terms, the less developed countries are asked to join existing and new supranational institutions such as the recently founded 'International Competition Network' to 'lock in' domestic market liberalisation and to force an opening of their economies for competitive pressures deriving from the advanced countries.

In this context, the politics of trade liberalisation is of particular strategic importance because it puts sustained pressure on developing countries to engage in business-oriented domestic reform. By adapting to external pressures, governing elites in developing countries are empowered to develop their own 'competitiveness', often at the cost of abandoning existing social agreements with their domestic political power base. Domestic economic liberalisation therefore is facilitated because political decision-making has been predetermined by norms and values that derive from the advanced countries as represented by supranational organisations, international financial institutions and regional free trade areas such as the EU and NAFTA. The next section analyses the EU's efforts in the Euro-Mediterranean partnership (EMP) (since 1995) and the European Neighbourhood policy (ENP) (since 2003) to facilitate the transition of neighbouring North African and Arab countries towards market liberalisation and increased adaptation and integration with the EU's neoliberal model.

The EU and its neighbours: the uneven and combined spread of market and trade liberalisation

The capitalist world economy is dominated by three major economic blocs (EU, NAFTA and Japan/South-East Asia) that have been built around regional free trade agreements and increasingly deep economic and trade integration between the three blocs (Dicken 2007: 106-36). In the 1980s, European debates focused on the question of whether the EC should put forward an industrial policy using the common external tariff of the EC to protect industrial producers in a similar way as had been done earlier in the case of EC agriculture. However, this scenario lost out against the alternative of increasing openness between the main trading blocs thereby allowing deeper integration between different economic blocs (Sandholtz and Zysman 1989).

At present, the debate seems to favour a global orientation although the regular conflict over issues of trade liberalisation between the major blocs in venues such as the WTO suggests that this strategic decision might again be challenged at some future point. The strength of neoliberal ideas within supranational organisations and in EU institutions is based on the dominance of factions of capital that believe that a transnational and global orientation will deliver them economic gain and that the costs of adaptation will be worth paying to sustain regional competitiveness in the global system. The EU has therefore shifted from a potential venue of re-regulation of the pressures of globalisation towards the role of embracing and diffusing the imperatives of neoliberal restructuring (Bieler 2006: ch. 2).

These shifts at the European level have moved in parallel with attempts to deliver liberalised trade relations at the global level. In this context, the transition from the General Agreement on Trades and Tariffs (GATT), which had governed global trade since 1947, to the World Trade Organisation in 1995 was significant as was the more recent effort to create an integrated system of global economic governance based on a network of World Bank, IMF and WTO. Nevertheless, these developments must not be understood as a historical breakthrough of trade liberalisation in comparison with earlier periods. In his seminal study of GATT and WTO, Wilkinson has argued that:

> the WTO is not about free trade; nor has it, or the GATT, ever been…. It is about facilitating and entrenching in international law political bargains that enable the economic agents of participating governments to pursue opportunities in some markets while protecting others (2006: 17).

The same author stresses that global trade relationships are based on asymmetry, which favours the advanced OECD countries in focusing on industrial and service liberalisation and the protection of intellectual property rights. In particular, international agencies such as the ‘World Intellectual Property Association’, which cooperates with the WTO, aim to enforce OECD countries’ technological rents deriving from intellectual property. What this policy fails to appreciate is that today’s OECD countries historically have all ignored intellectual property rights at one point or another in the past. In fact, the ability to copy the most successful technologies of their time was of crucial importance in helping them to speed up their own economic development (Wade 2003; Naylor 2007).

On the other hand, the primary, agricultural and textile producing countries have had little influence on the agenda of trade negotiations since various barriers such as quantitative restrictions and the protection of OECD agricultural producers from competition have historically limited their access to OECD markets. According to Wilkinson, the result has been the emergence of a set of international and regional organisations that is ‘organised into a multi-layered system of economic governance that further locks in the [trade] asymmetries in the WTO’s legal framework’ (2006: 99). The current Doha Development Round of global trade negotiations is set to continue this pattern as OECD countries will gain more from further liberalisation of trade in services, protection of intellectual property and in non-agricultural market access than developing countries will gain from a moderate liberalisation in market access for agriculture (*ibid.*: 139).

From the point of view of its advocates, the major advantage of a politics of trade liberalisation is the modular nature of the strategy. It allows for the emergence of a shared normative framework over time but accepts that progress will be negotiated incrementally and that the most powerful countries will continue to exercise their veto power in the process (Hudson 2003: ch. 9). Nevertheless, the scope of economic reform and trade liberalisation is wide-ranging:

> The ultimate objective is the removal of a wide spectrum of non-tariff barriers that obstruct economic transactions and resource flows across borders…. The focus [is] on a tailor-made type of “regulatory convergence”…. What is primarily needed are decisive domestic reforms that enhance productivity, improve the general business climate, and remove non-tariff barriers (Müller-Jentsch 2005: 79).

In this context, the EU’s Mediterranean policies such as the EMP and ENP form part of a larger strategy of opening up developing countries for the agenda of global competitiveness:

> While it [the EMP/ENP] formulates a “grand vision” for the region, it can be implemented incrementally and at multiple speeds…. [D]eeper integration may be tackled at different policy levels (national reforms, regional integration, multilateral liberal-

ization) and in a wide range of policy areas (individual sectors and themes)… While the long-term goal is clear, there are many ways of getting there (ibid.).

Thus, the EMP/ENP policies serve a broad variety of purposes, ranging from the geopolitical to the economic. At first glance, they might appear to compete with parallel geopolitical initiatives for the region implemented by the United States. Nevertheless, they also often share US concerns and positions as will be demonstrated later on in the case study of the relationship between the EU and Syria.

Observers of the history of the relationship between the EC/EU and Mediterranean countries have pointed to a 'high birth rate' and 'high death rate' of European political initiatives in the region (Aliboni 2001). Table 1 below outlines the seven major initiatives between 1972 and the present and briefly sketches the policy content of each initiative.

Table 1: Major EC/EU policy initiatives towards Mediterranean countries since 1972

Year	*Title of policy initiative*	*Policy content*
1972	Global Mediterranean Policy (GMP)	Bilateral economic cooperation agreements and economic and financial aid in the form of bilateral financial protocols
1973	Euro-Arab Dialogue	Promotion of economic and cultural ties
1990	Renovated Mediterranean Policy (RMP)	Continuation of GMP, increased aid, additional emphasis on human rights
1992	Euro-Maghreb Partnership	Shift from development co-operation to political dialogue
1995	Euro-Mediterranean Partnership (EMP) 'Barcelona process'	Establishment of a free-trade area by 2010, bilateral Euro-Mediterranean Association Agreements
2003	European Neighbourhood Policy (ENP)	'European Neighbourhood Action Plans', focus on political dialogue and economic reform, trade liberalisation, energy, security, human rights through 'European Neighbourhood and Partnership Instruments'
2008	Mediterranean Union	Announced to give new élan to the Barcelona process, focusing on new development projects and led by a new dual Directorship consisting of one representative each from EU and Mediterranean countries appointed for two years

Sources: Aliboni 2001; Baracani 2005; European Neighbourhood and Partnership Instrument (ENPI) 2007, Le Monde 2008.

The first generation of policies in the 1970s was based on cooperation agreements that granted Mediterranean countries preferential access to European markets for some of their agricultural products. The current second generation policy of signing individual 'Association Agreements' between the EU and the MENA (Middle East and North African) countries emerged in reaction to developments that were largely external. In particular, the completion of the EC's Common European Market programme in 1992 and the setting-up of the EU in the same year was followed by the process of EU Eastern enlargement. This process granted EU membership to Central and East European countries and two Mediterranean states (Malta and Cyprus) in 2004 and 2007, respectively. The new EU member states now qualify for preferential treatment under the rules of the EU's Common Agricultural Policy. Subsequently, many MENA agricultural exports to the EU faced increased competition as a result of this enlargement.

To some extent the Barcelona process after 1995 – a second generation EU Mediterranean policy – served to balance the commitment of the EU to Eastern enlargement with the requirement to engage with the MENA countries. The Barcelona process linked differentiated access to the EU market with differentiated convergence: rising degrees of convergence could be rewarded with closer association deals and financial assistance. This situation was made more complicated by the re-launch of the Barcelona process as European Neighbourhood Policy in 2003 and most recently, the launch of the 'Mediterranean Union' in March 2008. Under these, EU neighbours are divided into prospective candidates for membership and the MENA countries which will not gain admission but might qualify for the establishment of a new tier of institutions for which the term 'European Partnership Area' has been suggested (Bechev and Nicolaidis 2008: 3).[iii]

The EU's current policy towards MENA countries focuses on the signing of bilateral economic Association Agreements with each Mediterranean partner country. These Agreements commit the EU and MENA countries to the incremental abolition of tariffs and the mutual granting of full market access, subject to certain qualifications, after a transition period. The explicit goal is the economic integration of the MENA countries with the EU and the world economy in a dual process. On the one hand, the MENA countries are encouraged to gain privileged access to the EU regional trade bloc and must open their own markets to goods originating in the EU. On the other hand, signing the Agreement with the EU commits MENA countries to the existing global trade regime to whose rules and regulations on trade in goods, services and protection of intellectual property rights the bilateral Agreements refer frequently.[iv] Thus, both regimes mutually reinforce each other and the EU works in this context as the agent of the global trade regime.

Returning to the situation in the mid-1990s, MENA states reacted to the globalization of neo-liberalism by advancing domestic and regional liberal economic reforms. At the domestic level, new regulatory rules were adopted to restructure the banking and financial sector and to advance tax and customs systems in tune with policies of trade liberalisation. At the regional level, MENA states started to engage each other in regional South-South free trade agreements, such as the Greater Arab Free Trade Area (GAFTA) and the Mediterranean Arab Free Trade Agreement (MAFTA).[v] The former was formally agreed in 1997 under the auspices of the Arab League and came into existence on 1 January 2005. The latter is the outcome of the parallel Agadir process which led to the establishment of the MAFTA in 2004 (United Nations 2001: v-vi; Wippel 2005).

The potential for this MENA regionalism to mitigate the effects of the core-periphery structure of the neo-liberal global economy remains, however, uncertain. First, earlier initiatives for regional trade liberalisation in the MENA countries since the 1970s collapsed. Second, the MENA countries tend to produce similar commodities and all suffer from a narrow industrial base. This limits their potential for regionally integrated production chains and mutual South-South trade. Third, all major MENA countries share in common the view that the EU provides the main market for their exports. This might work to limit the potential of the MENA countries to extract meaningful trade concessions from the EU, thereby making EU-MENA trade liberalisation even more asymmetrical.[vi] This feature has been reinforced by the EU's decision to negotiate Association Agreements individually with each Mediterranean and Arab country rather than to take account of regional initiatives such as GAFTA and MAFTA. Fourth, the MENA countries have different regional interests and geopolitical concerns. Trade between MENA countries is limited in comparison with each country's trade with the EU but MENA countries often have privileged relationships with regions beyond the scope of the EU and of GAFTA and MAFTA. And both regional free trade agreements are linked to the global level through frequent reference to WTO regulations in their documents.

Lastly, it must be observed that political commitment to the large-scale liberalisation of access of EU and OECD countries to MENA markets has not yet been tested. The potential of increased EU exports to trigger deterioration in Arab state budgets and local labour markets is only beginning to become visible (Wippel 2005: 7). There is agreement in the literature that the elimination of tariffs and barriers for EU industrial goods (and possibly services) will threaten MENA small and medium-sized businesses. Moreover, large-scale liberalisation of trade in agriculture would trigger increased migration from the countryside and social dislocation in rural areas (Asseburg 2005: 4). In sum, the liberalisation of trade at both the regional and global level is likely to remain contested.

The case of the EU-Syria Association Agreement

In this section, the Syrian Arab Republic is selected as a case study in order to examine the encounter of the neoliberal model with a relative outsider in the capitalist world economy. Syria has represented pan-Arab nationalist aspirations for more than three decades; it has focused its resources on constructing a national security state to balance its regional opponent Israel and has historically been largely self-sufficient in core economic fields such as agricultural production and energy supplies. The analysis of Syria, governed for more than four decades by the Arab Socialist Baath Party, is therefore a critical case to examine the universal strength or otherwise of neoliberal globalisation.

Since the Barcelona process in 1995, the EU has signed bilateral agreements with all MENA partner countries except Syria and all but one of the Agreements subsequently have been fully ratified. The negotiation process between the EU and Syria started in 1998 as the last of all bilateral deliberations. An agreement was first approved on a technical level in December 2003 and then 'initialled' by the chief negotiators in October 2004 (Directorate General for Trade 2003; EuropaWorld 2004). In June 2005, the Head of the European parliament delegation to Syria declared that signing could be expected before the 10th anniversary of the Barcelona process in November of the same year (Business Newsletter 2005).

However, no ratification has been forthcoming and the Agreement has subsequently become a permanent political bargaining chip between the EU and Syria. Disagreement has focused at various points since 2004 on the Lebanon crisis and the 2006 Israeli military campaign, demands for Syrian withdrawal from Lebanon, the issue of proliferation of weapons of mass destruction as regards Syria's chemically armed missile force, human rights and other issues (Hinnebusch 2005: 9). However, what has been decisive for the blocking of the Agreement was a change in French policy after the murder of the former Lebanese Prime Minister Hariri on 14 February 2004. Some observers have also pointed to additional economic factors in explaining the shift in the French position, notably failed negotiations between Syria and France about oil and trade deals in October 2004 (Crisis Group 2005: 26). Yet the Hariri case marked a clear turning point towards a degree of realignment between the US and the EU on the Syrian issue – regardless of Syria's subsequent withdrawal from Lebanon and continuing Syrian steps towards liberal economic reform. In particular, both the US and EU supported the international inquiry into the Hariri murder and European discourse has subsequently stressed that the outcome of the inquiry is 'a *decisive* factor in the signing and ratification of the association agreement' (Committee on Foreign Affairs 2006, emphasis added).[vii]

Moreover, since 2004, the European side has put forward long lists of demands to the Syrian representatives that mix political and economic issues. What is crucial is that the EU has insisted that Syrian economic concessions will not result in a turning down of the EU's additional political demands. On the Syrian government's side, this European posture – especially once Syria had met the first part of UN Resolution 1559 to withdraw from Lebanon only to be pushed on the second part of the Resolution which requires Syria to cooperate in the disarmament of the Hezbollah militia – has been met with increasing scepticism. A European diplomat is quoted saying that 'Syrians have come to think that it's a game and ask what the next condition will be' (Wieland 2006: 153). In the spring of 2005, the Syrian side started to feel that concessions only resulted in additional demands and that the negotiations failed to deliver. However, both sides continue to refer regularly to the need to sign the Agreement when the time is right, and the Syrian government has started to implement many of the economic commitments entailed in the Agreement. Syria has received some assistance in modernizing its domestic economic governance from Germany, thereby creating pilot projects for more large-scale cooperation at a future point. Most important, the French government invited the Syrian government to attend the founding conference of the Mediterranean Union on 13 July 2008 in Paris. According to French President Sarkozy, the Association Agreement should re-enter the agenda and should be ratified at some as yet unspecified point (Seale 2008).

In comparison to the political bargaining process, the actual content of the Agreement itself has received less attention. Yet the agreement deserves analysis as its content, if enacted, would lead to a fundamental change in the way in which the Syrian economic system actually works. The 2004 draft Agreement between the EU and Syria contains 77 pages and 433 pages of Annexes and Protocols. Its general focus is on the gradual abolition of tariffs between Syria and the EU over a 12-year period and the progressive establishment of a free-trade area.[viii] The Agreement's economic provisions on customs duties, right of establishment for companies, rules on competition, the settling of disputes in bilateral trade and the opening up of Syrian government procurement for EU exports are more wide-ranging than is the case in the other Agreements (Zorob 2007a: 20-3, 2008: 9-10). Moreover, it contains political provisions not usually found in bilateral trade agreements such as the issue of proliferation of weapons of mass destruction and cooperation on counter-terrorism.[ix]

The key provision is that 'Syria will liberalise its imports regime for Community products so that all tariffs are reduced to zero by the end of the twelve year transition period after entry into force of the Agreement' (European Commission 2004a: 3). Each side to the Agreement must also grant companies of the other side treatment no less favourable than that accorded to domestic companies (Article 43).[x] Syria must be prepared to open 'almost all sectors for [EU] investment' (*ibid.*: 3) and must allow companies originating in the Community to move their capital freely in and out of Syria (Article 62). Furthermore, Syria must engage in 'appropriate economic restructuring' and offer an 'appropriate framework for political dialogue' to allow for the 'progressive liberalisation of trade in goods, services and capital' (*ibid.*: 13 and Article 1). This commitment includes the incremental abolition of customs duties and, more urgently, abolition of 'all import and export prohibitions…upon entry into force of this [Association] Agreement' (Article 23). The introduction of new customs duties or non-tariff barriers is forbidden (Article 9 and 10). Furthermore, Syria must commit to adjust 'State monopolies of a commercial character' and public enterprises to abolish by the end of the fifth year after signing of the Agreement any discrimination in government procurement between EU and Syrian national companies (Article 65 and 66). It must also enforce the protection of intellectual property rights 'in accordance with the highest international standards', which includes the rules of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) (Article 72).

These core provisions are qualified on a number of counts. To begin with, any political obligation for consultation during the reform process is limited to 'consultation mechanisms between administrations and the business community' and is required to 'meet the needs of the trading community' (Article 39). In particular, the Agreement aims to create an environment favourable to the development of private enterprise and a stable environment for investment (Article 98). The Agreement also includes some general statements about social co-operation and improvement of living conditions (Article 110). Yet it does not commit to social dialogue or consultation with trade unions or civil society.

As far as the crucial question of protection of Syrian companies from EU competition is concerned, the Agreement limits any scope for protective measures. The Syrian authorities are granted the power to increase or reintroduce customs duties during the transition period to protect 'infant industries' or sectors whose restructuring produces major social problems (Article 15).[xi] However, this right is heavily qualified in terms of scope and duration. It covers only 20 per cent of the total yearly average value of imports of industrial goods originating from the EU and cannot exceed the duration of five years. All details must be mutually agreed between the EU and Syria in the 'Association Committee', the bilateral EU-Syrian body provided for in the Agreement to manage the association process. Moreover, Syria must offer 'a timetable for the elimination of the customs duties introduced under this Article…. The Association Committee may decide on a different timetable' (*ibid.*). In sum, the ability of Syria to put forward unilateral protective measures is severely limited in scope and might be subject to sanctions under the provisions of the Agreement.

Another potentially important section of the Agreement concerns those economic sectors that are excluded from the scope of Article 43 on non-discrimination between EU and Syrian companies. This article, already referred to above, grants EU, Syrian and third country companies 'Most Favoured Nation' status and allows nondiscriminatory access to each market. Crucially, the application of this paragraph excludes those Syrian economic sectors that are subject to Syrian government monopoly (the list of these sectors in Annex IV of the draft Agreement is left blank). Furthermore, some other economic activities that are not subject to government monopoly still qualify for various degrees of protection from the scope of Article 43. This list of economic activities, also to be found in Annex IV of the draft Agreement, is fairly extensive and covers telecommunications, domestic banking and education services, amongst others. However, the stipulated limits on EU and foreign capital are in most cases rather modest. They mostly concern a guaranteed share of 25 per cent for Syrian investment capital and ownership. The sector of telecommunications is singled out for a more rapid opening to competition during a transitional period of only six years from entry into force of the Agreement.[xii] Other potentially important provisions concern banks whose ownership is subject to a minimum of 51 per cent Syrian ownership and some provisions governing nationality requirements of employees in the education sector. Overall, the Agreement puts much higher demands on the Syrian side than is the case for all other Mediterranean states that have already signed their respective Agreements with the EU.

The political-economy context of the EU-Syrian Association Agreement.

The Association agreement has to be understood in the wider context of Syria's development strategies and dilemmas. Observers of Syria have generally stressed the dominance of geopolitical concerns in policy-making by the country's leadership. The economic base of the regime was in comparative terms less important than the positioning of Syria in the regional system by building up the Syrian national security state in order to balance Israel. After 1970, Syria pursued a policy of external reliance on the Soviet Union that was supplemented by a strategic security partnership with Iran after the Iranian revolution of 1979. After 1991, Syria lost its Soviet backing but re-established a new political relationship with Putin's Russia, especially after Russia agreed a cancellation of Syria's bilateral debt in 2005. In addition, the last stage of Saddam Hussein's rule in Iraq was characterised by a tactical rapprochement between the two countries and Syria was able to rely for some years on oil deliveries from Iraq which helped to free some of Syria's own oil production for export. Meanwhile, Syria attempted to improve the bilateral relationship with the United States, especially after its support of US action against neighbouring Iraq after the latter's occupation of Kuwait, but this did not fully bear fruit, and collapsed after the Clinton Administration's failure to deliver on the Middle East 'peace process'. Since 2003, the US strategy of blocking Syria's aspiration to join the WTO and using sanctions to isolate the country's business community has slowed Syria's economic reform efforts.

After the transition of power from Hafiz al-Asad to Bashar al-Asad, following the former's death in office on 10 June 2000, major shifts in economic policy were avoided. From 2003 onwards, however, the economic reform programme turned towards liberalisation. In particular, the Syrian leadership started to focus on pursuing the option of an Association Agreement with the EU as a matter of urgency. At this time, this signalled a genuine shift in the government's strategy for geopolitical reasons. In particular, it was held to counter the US strategy of isolating Syria in the region after the 2003 occupation of Iraq. The gravity of the threat from the US might also explain why the Syrian government offered to include services in the list of sectors to be liberalised as a way to speed up the signing of the Agreement (Haddad 2005: 17). As it turned out, the EU was not willing to go forward with the Agreement at that point.

Since then, Syria has sought to increase its economic and strategic ties with Russia, Iran and China (Hinnebusch 2005: 11). However, Syria's strategic alliance with Iran lacks the crucial economic dimension. Although it is emerging as a regional power, Iran is nevertheless economically not strong enough to act as anchor of economic reform in Syria. Iranian offers to support the construction of new oil refineries in Syria lack plausibility as Iran itself suffers from a major shortfall in domestic refinery capacity (Spiegel 2007). Syria has also made efforts to attract new foreign direct investment from the GCC states and Turkey. Turkish businesses in Syria have been able to produce for export within the GAFTA regional trade agreement, thereby encouraging South-South integration. The states of the Gulf Cooperation Council have invested in large projects in Syria owing to the sharp rise in their revenue from the current second oil boom (Hertog 2007). One can expect that Syrian 'venue shopping', i.e. the attempt to negotiate with external powers to facilitate domestic economic development, will continue to form part of the country's strategy for the foreseeable future, especially as opportunities appear to improve again from the low point in 2004 due to the current failure of US policy-making in the region. Yet these options do not serve as a full-scale alternative to economic liberalization. On the contrary, at least the relationship with Arab investors might be dependent on further economic liberalization, as does the EU option.

Moving from the geopolitical to the domestic level, it must be stressed that the Syrian government originally relied for its political support on a coalition, which consisted of popular constituencies such as small and medium peasants, unionised workers, public sector employees and the civil and military state institutions. On the other hand, until 1970, the rule of the Bath party largely excluded the old bourgeoisie from access to the state. Thus, a potential ‘triple alliance’ (Hinnebusch 1997) of state, domestic and international capital did not emerge. The stability of the system relied on rents from the oil sector emerging after 1973, which allowed in turn for the build-up of a public sector that served to stabilise the ruling social coalition (Seale 1995: 317-8, 451-3). It also allowed for the establishment of some features of a welfare state based on free access to education and health care and subsidised staple foods. In the mid-1980s, major trade and budget imbalances emerged and the Syrian government engaged in some limited liberalisation (*infitah*) which cut public spending and included a new investment law (Law No. 10 of 1991) to encourage foreign and expatriate investors and the richer Arab states to invest in the Syrian economy.[xiii] However, the law was subsequently not backed up by a more comprehensive reform programme and Nabil Sukkar, a liberal opinion leader within the Syrian elite, described the 1990s as a ‘lost decade’ (Perthes 2004: 28; Syria Today 2005).

The Syrian economy suffers from at least three major problems which have put sustained pressure on the regime to undertake reform. First, economic rents from oil are declining and it is expected that Syria will become a net-importer of oil around 2012. This questions the sustainability of the Syrian welfare state and the very economic foundation of the public sector and of state-owned enterprises. Second, Syrian demographic development is characterised by rapid population growth and a very low average age of population – the so-called ‘youth bulge’ – which increases demands for employment at a time of decreasing economic rents from oil, thereby no longer allowing for expansion of public sector employment. Third, external political support for Syria has declined and the strategic security partnership with Iran has so far only a limited economic dimension. According to one observer, these features appear to constitute a 'textbook example of the nexus of demographic expansion and poor macroeconomic performance' (Leverett 2005: 34). Another analyst suggests that it is only a matter of time until the Syrian government will be forced by structural constraints to shift its social support base away from the public sector and agricultural interests and towards an alliance with private and international capital (Haddad 2005). Such a development would enable the realisation of Hinnebusch's 'triple alliance' and would point to the Syrian government's acceptance of the global competitiveness agenda. How likely is this development to come about under the leadership of President Bashar al-Asad?

In order to analyse the degree of change in economic policy-making under Bashar al-Asad, one first needs to summarise some facts about the Syrian economy he inherited. The basic point is that the Syrian economy has been a mixed economy with state control and state monopolies in some strategic sectors such as electricity, water, telecommunications and, most importantly, oil and gas (Sukkar 2006: 5). Moreover, the public sector includes some other strategic sectors such as cement production, sugar refining, fertilizers and a dominant position in insurance and banking (World Bank 2005b: vii). The state also subsidises inputs in agriculture and purchases domestic agricultural crops at above world market prices. This is an important policy as the agricultural sector – a core constituency of the social coalition led by the Baath party – still constitutes 21 per cent of overall employment while industry makes up 26 per cent and services account for 52 per cent (DG Trade 2007). In addition, the state subsidizes water, electricity and fuel and exercises exclusive control of the procurement and sale of cotton and wheat while state-owned enterprises enjoy different levels of subsidy and protection (DG Economic and Financial Affairs 2005: 132). Another important public sector instrument is state-controlled credit provision and loans to the private sector have until recently remained a small fraction of overall lending (European Commission 2007c: 10).[xiv]

The Syrian public sector's share of GDP has nevertheless declined since the 1980s and the private sector now accounts for an estimated 65 per cent of GDP and employs almost 75 per cent of the civilian workforce (IMF 2005: 15; Perthes 2004: 28-31).[xv] The public and private sectors coexist in a balance that is conditional on the ability of the state to procure sufficient resources from the oil and gas sector to sustain public sector employment. Conversely, the Syrian state's revenue from taxing the private sector is low and it is estimated that only half of private income is reported for tax purposes. Moreover, the non-oil tax revenue is only slightly above 10 per cent of GDP which is low by regional standards (World Bank 2005b: viii; IMF 2006a: 31; European Commission 2007c: 9). The state employs 300,000 workers in state-owned enterprises and 900,000 civil servants (*ibid.*).[xvi] In regional terms, the former figure is fairly low and represents 7 per cent of all employees while the civil service, accounting for 21 per cent, is an employer of last employment of resort with low productivity and low wages thereby limiting open unemployment (Sukkar 2006: 3-4).

In the period of increasing oil rents after 1973, the Syrian state expanded the public sector and state enterprises through a policy of obligatory recruitment of all graduates from advanced schools and universities. This policy was attractive for graduates as employment in the public sector offered a life-long job guarantee and some health, housing and pension benefits not obtainable in the private sector. In 2003, 75 per cent of the total active population with a higher education degree was employed in the public sector. According to two Syrian statistical sources, the 2003 Labour Force Survey and the 2003 Household Income and Expenditure Survey, the public sector accounted for 24 per cent of the total civil labour force while the formal private sector provided 35 per cent and the informal private sector 37 of overall employment although the second survey suggested higher figures for the formal private sector and lower figures for the informal one (European Training Foundation 2006: 23-5; El Laithy and Abu-Ismail 2005: 48).[xvii]

The dynamics of the Syrian labour market are driven by the past build-up of the public sector and complimentary social policies that favour lifelong employment. The Syrian welfare state provides some measure of social protection in the event of death, illness, disability, work injury and old age but does not offer health insurance or unemployment benefits. Existing legislation also provides full job security for public sector workers and near job security for workers in the formal private sector (Sukkar 2006: 2). Due to this emphasis on employment security, Syrian unemployment is heavily concentrated in the cohort of young people between 15 and 24 years who struggle to enter the labour market and make up 80 per cent of the unemployed (European Training Foundation 2006: 6; Sukkar 2006: 46). The demographic pressures on the labour market are set to continue as 40 per cent of the Syrian population are below the age of 15 (DG Economic and Financial Affairs 2005: 132).

As far as employment is concerned, the Syrian labour market provides a surprisingly high degree of wage compression: wage differentials between people with different levels of educational attainment are narrow and official statistics hold that university graduates earn only twice as much as illiterate workers (European Training Foundation 2006: 36). Nevertheless, the significance of this finding is limited as large numbers of workers in the public and private sector hold more than one job and the actual wage differentials might be much higher once this factor is taken into account. Moreover, since educational attainment is used by public and private sector employers to select employees, the informal sector is in practice often the only employment option for poor and illiterate workers (El Laithy and Abu-Ismail 2005: 2, 49). In summary, the implementation of neo-liberal policies in Syria under an EU partnership agreement implies a radical transformation in current socio-economic practices.

Syria's Turn to the Market and the Association Agreement:

To understand, Syria's current moves toward economic liberalization and the partnership agreement, one needs to analyse how the domestic and international planes interact in the Syrian debate.

From the domestic point of view, the Syrian government historically had no preference for liberalisation measures as its social support base was dependent on the state sector. Nevertheless, the projected decline in Syrian oil revenue may leave 'no long-term solution except a sustained take-off of private investment which depends on Syria's conformity to the standards of the global market' (Hinnebusch 2003: 196). This holds true even if 'opportunities and benefits of change remain uncertain, the risks are high and short-term alternatives exist' (*ibid*.).

There is large-scale debate in Syria on the issue of economic liberalisation. Advocates of liberal reform have demanded a full-scale strategic shift of the state in favour of a newly emerging class of Syrian entrepreneurs. According to Nabil Sukkar, 'the best policy for Syria would be to encourage the emergence of a genuine new private-enterprise sector. This means that the government should let entrepreneurs, whether Syrian or foreign … invest, produce, buy and sell, and thus create a genuine market-based economy' (quoted in Leverett 2005: 73). On the other hand, the Head of the Syrian Planning

Commission has warned against policy decisions that question the employment guarantee for older workers stating that 'my only red line is that we cannot layoff anyone' (Raddawi 2007). Not all sections of business, notably those dependent on state patronage, are fully supportive of the new course. Yet there is a clear overall shift in favour of the advocates of liberal reform, especially in the period after 2004 and in contrast to earlier waves of economic reform in the 1980s and 1990s, the Syrian government shows a higher degree of commitment and the severity of reform measures is more pronounced. Indeed, Syrian domestic liberal reform measures – independent from the issue of the Association Agreement – have become so comprehensive that a cascade of change appears to have started. Crucially, groups linked to the government have become associated with new private business projects while the voices of Syrian labor are largely absent from the official debate. This points to a change in the social support base of the regime.

Table 2 below outlines some of the reform measures that have been adopted and have been implemented to various degrees under the Presidency of Bashar al-Assad. These measures can be divided into those that favour economic liberalisation, those that are in effect countervailing measures and those that work to delay the economic reform process. Overall, the liberalisation measures are very substantial and, even if implementation remains limited, suggest that the government has committed to a liberal economic reform programme that is without precedent in the history of modern Syria.

To begin with, most core measures such as the decrease in customs duties, simplified corporate taxation and the unification of the exchange rate of the Syrian lira, which is now set at market rate and pegged to a currency basket of Dollar, Euro and Yen, aim to facilitate trade liberalisation. These core measures will have a major influence on trade patterns between Syria and its trading partners and will pose a challenge to the state's steering of the economy in sectors in which increased competition might threaten domestic suppliers. The strong impact of the measures is clear to see. For example the cut in Syrian import taxes for cars has resulted in a 60 per cent increase in the number of registered private cars since 2003 (Syria Today 2007a). Some other measures such as the opening of banking and insurance for private competition has also had a major impact, although the low level of available credit for the private sector is still held to constitute a problem which limits the growth potential of private companies (European Commission 2007c: 10). However, the most recent data points towards a strong rise in the share of private banks' lending to the private sector (IMF 2007a: 5, 2007b: 34).

By contrast, it appears appropriate to describe the government's countervailing measures as side payments without major strategic significance. The three main measures of wage increases for the public sector, additional public sector job creation and the reintroduction of industrial quotas to protect domestic suppliers all buy time but do not challenge the underlying trend of liberalisation. Moreover, the setting-up of new industrial projects backed by Syria's allies such as the Syrian-Iranian car manufacturing plants or new oil refineries have not yet taken off and their future significance for the Syrian economy is still unclear.[xviii]

More important and most likely to challenge the political commitment towards further liberalisation of the economy are gaps and delays in other policy areas that would have to be filled to sustain major economic restructuring of the public sector. On the one hand, the introduction of new layers of formal social security such as compensation for job losses and retraining has not featured highly. On the other hand, cuts in existing state subsidies for basic goods, especially the petroleum price subsidy, have proceeded slowly (IMF 2006a: 20-3). The need to abolish such general subsidies has been stressed by the international financial institutions like the IMF and the assumption of future Syrian energy shortages is crucial for Syrian reformers in order to present the reform process as the only available choice. What the IMF downplays, however, is that the subsidies form a crucial part of Syrian household income. Some of the assumptions about poor targeting of subsidies, such as the claim that the richest groups 'cream off' most of them, appear overstated and are not based on convincing data. Moreover, their phasing out has not been complemented by a broader shift to a means-tested system of social expenditure, as the Syrian state might not be ready to shift towards such an administratively more complex system.

Table 2: Selected Syrian economic reform measures between 2000 and 2008

Liberal Economic Reform Measures	**Countervailing Measures**	**Delayed Measures**
(1) Decrease in customs duties (maximum rate reduced from 255 per cent to 65 per cent, cuts in the list of prohibited goods) (2) Simplified corporate tax system with reduced rates (3) Unification of the exchange rate of the Syrian Lira (4) Private banking allowed (5) Insurance sector opened for private companies (6) Monopoly of import agencies eliminated (7) Syria has joined GAFTA, has signed Free Trade Agreements with Arab states and Turkey and has applied for WTO membership since 2001 (8) Preparation for the build-up of regulatory agencies (Syrian Securities and Exchange Commission) and for the opening of Damascus-based stock market (9) Introduction of free/special economic zones and of a Syrian Investment Agency (10) Some cuts in domestic energy subsidies (diesel oil) and phasing in of value-added tax (11) New Company Law (Law No. 3 of 2008) and new Anti-Trust Law (Law No. 7 of 2008) issued (12) Licensing of private transport companies and large-scale private investment in tourism sector (13) German technical support for Syrian State Planning Commission and Central Bank	(1) Reintroduction of industrial quotas set by the Ministry of Industry to protect domestic suppliers (2) Setting-up of new industrial projects backed up by political alliances, e.g. two Syrian-Iranian car manufacturing plants and new oil refineries backed by Iran, Venezuela, Russia and China (3) Successive real wage increases for civil servants and creation of additional employment in the public sector	(1) Privatization of state-owned enterprises not discussed (2) Measures to promote exports weak (3) Introduction of retraining measures for the unemployed announced but not enacted (4) Number of investment vehicles still low (apart from real estate)

Sources: DG Economic and Financial Affairs 2005; IMF 2006c: 37-8, 2007a; Landis 2008; Syria Today 2007a, 2007b, 2007c, 2008a; 2008b; Zorob 2007.

In practical terms, these gaps in policy-making might slow down reform at some future point, especially once interested groups become more aware of how they will be affected. In particular, recent legislation granting public enterprises financial autonomy (Law 54 of 1^{st} October 2006), which would start to be implemented with the 2008 budget, might trigger a rise in open unemployment that the authorities would have to address with complimentary social policies. So far, delays pose questions about the ability of the state to sustain the restructuring of the public sector.

Moving on to the issue of liberalisation of trade, one first needs to analyse existing Syrian trade patterns before moving on to the question of how trade liberalisation will affect the Syrian economy. The most striking feature in Syria's economic dealings with the EU is the absolute dominance of energy exports (crude oil) in comparison with all other economic sectors. In 2007, Syrian energy exports to the EU 27 were worth 2908 million Euros while the second and third major export items, agricultural products and textiles and clothing, amounted to 145 million Euros and 118 million Euros respectively (DG Trade 2008). Overall, Syria's export to and import from EU countries has declined between 2000 and 2006 (the Syrian export share to the EU 25 declined from 68 per cent of all exports to 32 per cent while Syrian imports from the EU declined from 33 per cent to 21 per cent of all imports) (DG Trade 2007, see also European Commission 2007d: 63-4).[xix] The structure of Syrian exports to other regions and countries differs from the case of the EU and from the single focus on energy. For example, the export of Syrian non-energy commodities to neighbouring GAFTA countries changes the overall profile of exports to a certain extent. Nevertheless, the overall picture is not encouraging if one focuses on the strategic role of the declining energy sector for the viability of the Syrian economy (IMF 2006c: 23). It also poses the question of how far Syrian industry is actually in a position to take advantage of any increased access to the European market under the association agreement. Moreover, looking at the Syrian trade patterns, one can detect that the Syrian government has to some extent succeeded in diversifying its trade away from reliance on the EU (compare table 3 below).[xx] In particular, Syria has expanded its imports from China and increased its exports to neighbouring Iraq and some GAFTA countries. Nevertheless, the EU remains overall a major economic partner and the Association Agreement therefore also remains a major item on the agenda of Syrian trade diplomacy.

Table 3: Syria's main import and export partners (2006)

Import partner	Volume of trade (€m)	% of total imports	Export partner	Volume of trade (€m)	% of total exports
1 EU	3,186	21.0	**1 EU**	3,136	32.3
2 Saudi Arabia	1,847	12.2	**2 Iraq**	2,661	27.4
3 China	1,184	7.8	**3 Lebanon**	920	9.5
4 Egypt	927	6.1	**4 Egypt**	513	5.3
5 UAE	908	6.0	**5 Saudi Arabia**	462	4.8
6 Ukraine	725	4.8	**6 Kuwait**	290	3.0
7 Iran	670	4.4	**7 UAE**	250	2.6
8 Lebanon	592	3.9	**8 Algeria**	222	2.3
9 Iraq	549	3.6	**9 Jordan**	203	2.1
10 Turkey	528	3.5	**10 Libya**	189	1.9
11 Russia	527	3.5	**11 USA**	166	1.7
18 USA	196	1.3	**12 Turkey**	135	1.4

Source: DG Trade 2007.

Moving from the domestic to the international plane, a comparison of the EU's discourse on Syria with the one sustained by the international financial institutions demonstrates that they share a great deal in common. At present, the IMF is suggesting various transition policies to the Syrian government to deal with the decline in oil revenue, such as the phasing out of general petroleum subsidies and the phasing in of a value-added tax (IMF 2007a).[xxi] However, the IMF's core interest is the restructuring of the Syrian financial sector in order to prepare the country for a second phase of liberalisation in which the Syrian state would no longer hold the capacity to subsidise the public sector with soft loans. This would question the work of the quasi-governmental agricultural procurement agencies and would also trigger large-scale restructuring of the public banking sector (IMF 2006a: 34, IMF 2006b: 20). In particular, the IMF demands that the Central Bank of Syria should be given a clear mandate 'as the core institution of a market economy' and should be granted autonomy in focusing on the primary objective to maintain price stability (IMF 2007a: 10-11). Furthermore, the IMF applauds the Association Agreement and holds in particular that it will 'contribute to making progress towards observance of WTO rules and disciplines' (IMF 2006c: 4). As for the EU, the Agreement with Syria constitutes a textbook case of the bilateral enforcement of WTO rules. The Agreement focuses on 'reciprocity' and 'no distortion' principles. One-way trade preferences and legitimate scope for protection are no longer accepted as guiding principles for trade between countries at different stages of economic development.

Conclusions: the prospects and consequences of a the EU association agreement

The case of the EU's Association Agreement with Syria is unique in a number of ways. Syria differs from other Arab countries due to its long-term track record of economic self-sufficiency based on oil rents and autarchy in agriculture. Nor is the neo-liberal transition of the Syrian economy a foregone conclusion. Syria continues to 'venue shop' for access to economic resources and options outside of the neo-liberal West. While the internal debate in Syria about the Agreement indicates that the liberal reformers retain the upper hand, the use of the slogan of 'social market economy' suggests that the Syrian government remains committed to a degree of domestic compromise on socio-economic issues.

Nor are the costs and benefits of the Association agreement for Syria undisputed. The agreement has been framed by neo-liberal economic theory originating from the World Bank and applied to Syria is a more uncompromising way than to other EU partner countries. It has been suggested that the opening of the Syrian economy might result over time in increased Syrian competitiveness and more rapid economic development. This scenario could create a Syrian 'triple alliance' of state, domestic and international capital, thereby providing an external anchor of domestic reform. On the other hand, Syrian domestic interests would have to accept that their role is cast as that of rather weak associates. Moreover, the current draft of the agreement would initially expand the options of EU companies whilst leaving Syrian producers exposed to superior competition. According to the Agreement, Syria must eliminate quotas and prohibitions on imports, reduce tariffs to zero after a twelve year transition period, cooperate in the enforcement of competition rules, agree to open many sectors of its public procurement, grant national treatment to other party's goods and some services and apply the highest international standards of intellectual property protection. These measures, taken together, benefit EU companies most (Zorob 2006b: ch. 5, 2007a: 20-3). If enacted, they would result in unbalanced trade flows, Syrian trade deficits and, in the longer run, Syrian external indebtedness.

The Agreement is designed to serve a double purpose: it assists global trade liberalisation, being linked with WTO rules, while also supporting the EU's regional project of establishing a set of friendly, and dependent, neighbouring Mediterranean states. The asymmetries of global trade patterns will not be challenged by the EU's attitude to South-South integration which does not support partially closed regional integration that would establish privileged relationships amongst southern states and allow them to retain sovereignty over the agenda and timetable of trade policies. However, the most basic weakness of all the partnership agreements is that they allow for a socially and sectorally disintegrated economic structure in the partner countries. They also fail to offer any strategy regarding capacity building of the Mediterranean states to deal with full-scale liberalization. If they unleash instability in MENA countries, they may be self-defeating. In summary, the Syrian case of economic liberalisation under severe structural constraints not merely tests the capacity of Syrian policy-makers but also highlights the limited contribution of the EU to stability and economic development in what remains the most difficult geopolitical region in the world.

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[i] The 'Washington consensus', jointly driven by the International Monetary Fund (IMF), World Bank and WTO, focuses on a standard set of liberal economic policies (see Jones 2006: 228-9). Recent economic debates suggest, however, that there is no longer a Washington consensus. For example, some former and current opinion leaders associated with the World Bank have publicly stated their disagreement with elements of the above framework. Yet these more recent changes in the debate, sometimes referred to as 'post-Washington consensus' (Knio 2008), are not reflected in the EU's policy advice for Syria.

[ii] In spite of emerging basic state welfare in Syria in the 1970s, many Syrian workers were still forced to leave poor regions of Syria to become migrant workers in richer neighbouring Lebanon or other economically more

advanced countries. Here, they entered a highly deregulated transnational labour market which appears in hindsight to be an early laboratory of neoliberal capitalism (Chalcraft 2007).

[iii] It is too early to judge if the Mediterranean Union can qualify as a new EU partnership policy or whether it is merely a rhetorical relaunch as part of the new French President's diplomatic offensive. Tthe original French proposal pointed towards privileged access for all Mediterranean states, irresponsive of EU membership, to the new policy. This model of a new Mediterranean 'club' has been abandoned after Franco-German consultations which restored an EU policy open to all 27 EU member states. The current proposal leaves a new Secretariat (a body of two leaders, one from the EU and one from the group of Mediterranean partner countries) as the single institutional innovation of the Mediterranean Union.

[iv] The Agreements are less far reaching as far as the liberalisation of trade in services is concerned. Most Agreements simply confirm existing commitments under the GATS regime. These do currently not apply to Syria and Lebanon who are not members of the WTO and of GATS.

[v] The term MAFTA has not become established in common usage. Instead, most subsequent sources refer to it as 'Agadir Agreement'. The main feature of the Agreement is that the four signatories use the EU's rules of origin allowing them to cumulate inputs from each of the four states in their exports for the purpose of accessing the EU's preferential tariff.

[vi] This feature is referred to in the literature as the 'hub-and-spokes' structure in EU-MENA economic relations (Nsouli 2006). This suggests that the EU market (the 'hub') gains access to the markets of all MENA countries (the 'spokes') through separate trade agreements. Meanwhile, 'the spokes only gain access to the hub market which becomes increasingly competitive as new spokes are added ... investors prefer to invest in the hub market rather than its spokes because it ensures them access to a much larger market' (van den Hoven 2004: 221; Zorob 2006b: 142-3).

[vii] The tenth interim report of the UN International Independent Investigation Commission into the murder of Hariri and others notes that 'cooperation provided by the Syrian authorities [for the Commission's mission] continues to be generally satisfactory' (United Nations 2008: 8). The same report does not provide new information about the outcome of the inquiry.

[viii] The 1977 EC-Syria Cooperation Agreement already grants Syria duty-free entry for all industrial goods.

[ix] As has been dryly noted, to 'include the WMD clause might be politically necessary and justifiable. For the Syrian-European AA to function as an effective commitment mechanism for economic reform, however, its definition as an essential element and the potential it provides for both parties to use it as an 'exit option' seems inappropriate' (Zorob 2008: 10).

[x] The first section of the document contains an 'Explanatory Memorandum' followed by the text of the Agreement. In the former case, reference is given to page numbers and in the latter case to the Agreement's relevant article.

[xi] The second line in Article 15 of the draft Agreement appears to wrongly refer to Article 12 rather than Article 14 as the logical coherence of the document would suggest.

[xii] At present, the Syrian mobile phone market is shared between two companies, Syriatel and Investcom. Both companies have close links to the Syrian government. In the event of future market access for competitors, these businesses might suffer losses. The main shareholder of Syriatel was reported to consider selling his shares to the Turkish mobile phone company Turkcell. The negotiations did attract the close scrutiny of the US government which placed pressure on American shareholders in Turkcell and threatened the company's management that they would not be allowed in future to enter the US. The negotiations have subsequently been abandoned (Turkish Financial News 2008).

[xiii] On the official Syrian Arab News Agency website, the Syrian government holds claim to 15 million Syrian expatriates, who are already providing significant remittance transfers and who are seen as an important constituency to support domestic economic reform and development.

[xiv] However, Syria's new private banks have started to make significant inroads in capturing a large share of credit provision to the private sector (IMF 2007b: 9, 24).

[xv] The relative strength of public and private sector crucially depends on the statistical distinction between GDP and non-oil GDP. If the former is used, the public sector contributes according to IMF data 40 per cent while the latter reduces this to only 23 per cent (2005). Most recent data suggests that the public sector share of GDP has fallen below 20 per cent (IMF 2007a).

[xvi] The term MAFTA has not become established in common usage. Instead, most subsequent sources refer to it as 'Agadir Agreement'. The main feature of the Agreement is that the four signatories use the EU's rules of origin allowing them to cumulate inputs from each of the four states in their exports for the purpose of accessing the EU's preferential tariff.

[xvii] It is generally acknowledged by Syrian and foreign observers that Syrian statistical figures do not follow international standards and might be misleading. This is due to weak data gathering but also to objective problems such as how to adequately measure seasonal employment in agriculture for the purposes of defining employment status. Moreover, official Syrian unemployment figures assume unrealistically low female participation rates in the labour market.

[xviii] For example, the Syrian-Iranian car manufacturing plants (SIAMCO and SIVECO) have so far failed to have a major impact. The former, announced as a major step in Syrian-Iranian economic cooperation, is projected to employ only 330 workers and to assemble 10,000 car kits of Iranian origin annually at some future point. The demand of SIAMCO management to receive special tax treatment to facilitate competition with imported cars is therefore likely to carry little weight for the time being and only 2,700 cars had been sold until February 2008 (Syria Today 2007a, Champress 2008). The second plant, SIVECO, it has been announced will be a larger project.

[xix] Some of the sources give different figures which might be due to different methods of data gathering. In particular, as of yet unofficial figures of the Central Bureau of Statistics on Syrian exports in 2006, reported on the blog joshualandis.com (2007), hold that exports to Iraq might be much lower than suggested in the EU statistics that are reproduced in table 3 below.

[xx] The latest available Syrian import and export figures (Central Bureau of Statistics 2005) differ from the EU figures to some extent. In particular, they underline the major significance of two EU member states, Italy and France, which together absorb 33 per cent out of 45 per cent of all Syrian exports towards the EU. The Syrian import figures suggest that Italy and Germany are the two major EU exporters but non-EU states such as Ukraine and Russia are comparatively more important.

[xxi] In this context, the IMF puts forward at least one unorthodox suggestion in holding that the progressivity of Syrian income tax could be enhanced (IMF 2007a: 9).

2
Trade Liberalization and Adjustment via Regional Integration: The Syrian-European Association Agreement

ANJA ZORUB

Introduction[xxii]

The liberalization of trade and the change to an outward-oriented strategy of development is one of the most sensitive issues of economic reform in developing countries. Regional integration and in particular an agreement with a large country or block 'in the North' may allow a developing country not only to credibly lock-in and/or catalyze trade reforms but may also contribute to promoting exports and investment. In addition, agreements of regional integration (RIAs) can deliver an instrument to overcome political-economic constraints on liberalization and adjustment. As the last of all Mediterranean Partner Countries (MPCs), Syria initialed an Association Agreement (AA) with the EU in October 2004. More than three years have elapsed and this most comprehensive of all agreements agreed upon between the EU and its Mediterranean Partners is still pending formal signature. European diplomats keep repeating the political 'prerequisites' which must be fulfilled for the European Council to finally approve the Syrian-European AA. Abdallah Dardari, on the other hand, the 'spearhead' of economic reform in Syria and signatory of the draft agreement in Brussels in 2004, seems recently to have considered dropping the agreement altogether. In 2006 he was quoted for the first time as saying that the liberalization measures implemented in recent years would have gone beyond those anchored in the AA. At least it would need to be renegotiated. What are the reasons behind this shift in perception? Do reforms implemented in recent years really make this agreement dispensable? What were and/or still are its potential benefits? What are the risks and challenges to be expected from the AA? These are the issues this paper wants to shed some light on. To do so, it will take a closer look at what has been achieved as regards trade liberalization in

Syria compared to the situation when the AA was negotiated and finally agreed upon. In addition, the paper will evaluate selected potential effects of the agreement taking into account the conditions currently prevailing in Syria.

The structure of the paper will be as follows. After a short theoretical introduction section two describes the basic characteristics and constraints of the Syrian process of economic reform focusing on the foreign trade system at the beginning of the 2000s and outlines the structure and main content of the Syrian-European Association Agreement. Section three investigates the stimuli which the AA could offer for liberalization and adjustment and the challenges its implementation is expected to create for the Syrian economy. The potential effects to be evaluated in this paper, using economic theory of trade and integration as a framework of analysis, include the static effects of trade creation, trade diversion and loss of tariff revenues in addition to the effect of securing and enhancing market access.

The Political Economy of Trade Reform and the Syrian – European AA

Trade Reform and its Political-economic Constraints

The liberalization of trade and the change to an outward-oriented strategy of development is generally regarded as one of the major elements of structural adjustment.[xxiii] According to standard economic theory and in particular its neo-liberal approaches, the target of trade reform and liberalization is to enhance efficiency and improve the national economy's growth potential.[xxiv] At the same time, trade liberalization is one of the most sensitive issues of economic reform in developing countries as the theory and empirical evidence on the political economy of transformation suggest. Political-economic constraints to trade reform are among the most important reasons why trade liberalization is in most cases implemented on a gradual basis and not according to the so-called "shock-approach" favored by neoliberal economists. They seem to play a particularly strong role in systems where the transfer and maintenance of power is not determined by political elections. In authoritarian systems in which several family clans dominate political as well as economic life, the definition of a long-term growth strategy to improve public welfare is most probably not the leading motive driving economic decision-making. Assuming that politically relevant protagonists act rationally in order to maximize their own benefit as laid out in the theories of New Political Economics or Public Choice, and as part of it the theory of interest groups, the ruling elite is primarily interested in political 'survival.' Accordingly, it is important for the government to consider the impact of trade reform on the interests of different groups of the society on which it relied in the past or is going to rely on in the future. Among those who are generally regarded as reform opponents are the domestic industry engaged in import-substituting production, the import business, the public organs enforcing administration of import substitution, state-owned enterprises (SOEs) and the trade unions. These groups are expected to lose access to rents which are generated by protecting the domestic market and by strictly controlling foreign trade. Moreover, public officials could be counted among the potential reform losers. They risk being deprived of at least some of their personal privileges and fortunes derived from any stake they have in business or from being closely related to those people who do. Against this background it is questionable if the government and/or the ruling elite or more generally those trying to push through reform in a specific country are willing and able to go for comprehensive trade reform. In case they are willing to do so, they need to acquire the approval for their plan from a sufficient number of the politically relevant interest groups. Such an endeavor most probably requires making compromises as regards magnitude, choice and speed of reform measures. Alternatively they could try to substitute some of the groups previously belonging to their 'supporting coalition' and thus opposing liberalization with new groups set to benefit from opening the domestic market to international competition. Such an approach, however, might prove even more risky (see, for instance, Nienhaus 2000). Guaranteeing continuity of trade reform against the interests of its opponents, and thus ensuring its sustainability and credibility, requires the government and/or the ruling elite to prevent those interests being fully exerted. To achieve this end, the government should, as recommended by the literature on trade reform, embark on a critical and comprehensive first phase of liberalization measures as a way to signal its readiness to reform to both domestic interest groups and external actors. At the same time it should announce a schedule of further steps. In addition, those measures could be accompanied by the establishment of an independent reform unit as a means of shielding decision makers from pressure exerted by different interest groups (see Bender 1995; for a more elaborate discussion of trade reform and its political-economic constraints see Zorob 2007: pp. 58-64). Finally, from a longer-term perspective, reforms may be promoted and 'locked in' if the government agrees a programme of structural adjustment (SAP) with the IMF and World Bank or 'ties its hands' by becoming a member of the World Trade Organization (WTO). Alternatively, it could reach a trade agreement with a large block 'in the North' like the EU (see, for example, Galal and Hoekman 1997). The latter could also contribute to promoting exports and investment by granting domestic suppliers improved access to the partner's market via reciprocal elimination or reduction of tariff and other barriers to trade. At the same time and in a similar way as cooperation with the IMF in implementing a SAP such a treaty offers the government opportunities to blame the external actor or partner for the economic hardships to be expected from opening the domestic market.

Characteristics and Constraints of the Syrian Process of Economic Reform at the Beginning of the 2000s

Like many other countries in the MENA region, Syria experienced two phases of economic reform between the end of the 1960s and the beginning of the 1990s. The scope and sector coverage of measures conducted during the first period or *infitah* between 1970-1977/78 and the following second phase starting in 1984/85 and lasting until 1991 remained relatively limited when compared to regional neighbors. Whereas the latter in most cases opted for cooperation with the IMF and the World Bank to implement structural adjustment programmes, Syria refused external intervention.

The process of economic reform restarted already shortly before Bashar al-Assad came to power following his fathers' death in June 2000 albeit still hesitantly and generally retaining the gradual and selective approach of the previous reform phases. Reforms accomplished until 2003/04 have included most notably steps to unify exchange rates, to devalue the Syrian currency and to partly, however hesitantly, liberalize foreign trade. The possession of foreign exchange was legalized and the rule of financing the import of specific goods from foreign exchange earned through exports was abolished. In addition, the government eliminated the monopoly of import agencies and gradually lifted provisions prohibiting or limiting imports on a product-by-product basis. Customs duties were decreased for selected goods, mainly raw materials. Moreover, Syria signed bilateral free trade agreements with several Arab countries and Turkey. It became a member of the "Greater Arab Free Trade Area (GAFTA)," which began operating fully, at least officially, in 2005. In 2001, the Syrian administration applied for membership in the World Trade Organization (WTO) albeit without success. Other reforms concentrated primarily on banking and insurance. Private banking was allowed in Syria for the first time since its nationalisation in the 1960s. In the field of investment, Investment Law No. 10 was amended and a new law on investment in the free zones was passed. In addition, Syria joined the Multilateral Investment Guarantee Agency. As regards fiscal policy a new personal and corporate income tax law lowered tax rates to a substantial degree. This law was accompanied by another law against tax evasion (for more details see Zorob 2005).

Despite several trade reforms, the Syrian foreign trade system in 2003/04 when the draft Syrian-European AA was finally agreed upon had still to be classified as being severely restrictive. Tariffs on imports into Syria remained high with the maximum rate including a unified surcharge on imports being as high as 235% in the 2001 tariff schedule. In addition to duties sharply escalating with stages of processing, the use of non-tariff barriers was still pervasive. In 2004, the import of more than one third of all goods according to the 8-digit level of the Harmonized System (HS) was completely prohibited, whereas other goods were allowed to be imported only by producers, selected industrial branches and/or the public enterprises (Zorob 2006b: 150). Other non-tariff barriers included import quotas, import licensing requirements and costly customs clearing procedures. The Syrian authorities also delayed the elimination of goods exempted from the scheme of tariff reductions allowed for in the provisions of the GAFTA Executive Program. The exemptions originally had to be ended in September 2002. Whereas other countries like Jordan or Lebanon reportedly lifted the exemptions as scheduled, Syria maintained them. Measures of export promotion, finally, were also described as still being weak at that date. Export prohibitions, export licenses and prior approvals for most goods to be exported had been abolished. Syrian fee zones, however, did not prove to be very successful in developing and enhancing Syrian exports (see IMF 2006b: 48; Owen 2005).

All in all, economic reforms gained in scope and sector coverage in the first years of the 2000s as compared to previous reform periods. Nevertheless, the gradual and selective approach was generally retained. In addition, several new laws proved difficult to implement and 'hot issues' like privatization of SOEs were kept off the official agenda of reform. Also reforms of the foreign trade regime remained piecemeal. They were not at any rate sufficient to form a 'critical and comprehensive first phase of measures' signaling 'a clear brake with the past' as recommended in the literature. In general, and despite that the transformation to a market economy seemed to be accepted as the principal target, the government was lacking a clear definition of this target and a strategy of how to achieve it. A first comprehensive reform programme was drafted and widely discussed in Syrian newspapers. It was however never approved by the Syrian government. Accordingly, liberalization measures were still implemented on a rather ad hoc basis (for more details see Zorob 2005).

As a result of this piecemeal and inefficient approach to liberalization and adjustment, Syrian companies at that time were still enjoying a high degree of protection and thus had little incentives to switch from import-substitution to export-oriented production (see also Aita 2005). This strong anti-export bias was best reflected in the very low level of export development and international integration of the Syrian economy even compared to most of its regional neighbors. As illustrated in Table 1, Syrian exports per capita were considerably smaller in volume in comparison to countries like Jordan or Tunisia. In addition, most of Syria's exported goods were primary goods, in particular oil, accounting for 89 percent of total Syrian exports. Only 11 percent of Syrian exports were made up of manufactured goods and only one percent represented high-technology goods. In the other Arab Mediterranean Partner Countries (MPCs) except Algeria the share of manufactured goods in total exports ranged between 31 percent in Egypt and 81 percent in Tunisia. Lack of export development, in turn, coincided with low levels of foreign and domestic private investment as well as low growth of the Syrian economy in general at the end of the 1990s and the first years of the 2000s. Against this background a report on the Syrian economy commissioned by the Syrian State Planning

Commission (SPC) and published in 2005 declared this period as "lost years" for the Syrian economy (see SPC 2005).

The outlook for a substantial widening and deepening of the process of economic reform, and accompanying trade liberalization and export promotion, were rather bleak at the time the agreement with the EU was negotiated. One of the most important reform constraints seemed to be and still remains today domestic opposition to liberalization. Those who would inevitably lose from trade liberalization are domestic industries producing for the local market, import businesses, the public administration and the SOEs. Other groups or agents with 'vested interests' in maintaining the system as it is include public sector managers, the security services or those in the private sector whose success in business depends in large part on a 'privileged relationship' to public sector companies and/or the administration. Even members of the government or, in other words, those who are responsible for the design and implementation of economic reforms may be afraid to forgo personal privileges and fortunes by opening up the Syrian market to foreign competition.

Table 1: Trade Orientation in Arab Mediterranean Partner Countries, 2004

	Trade[1] / GDP	Exports per capita	Primary goods / Exports (2003)	Manufactured goods / Exports (2003)	High-technology goods / Exports (2003)
	in %	in U.S.-$	in %	in %	in %
Algeria	59.6	997	98	2	2
Egypt	26.0	106	63	31	(.)
Jordan	104.9	720	31	69	2
Lebanon	51.2	499	31	68	2
Morocco	54.7	327	31	69	11
Syria	46.7	265	89	11	1
Tunisia	79.6	978	19	81	4

1Trade in goods. Source: Zorob (2007), p. , Table 3.

Besides domestic opposition, other constraints included the lack of an external actor with whom the Syrian administration could work to push through reform. A programme or an agreement with an external actor like the IMF offers the opportunity of assistance to finance reforms as well as social measures to cushion the inescapable negative effects of trade reform on labour and income. However, relations to the IMF and World Bank besides many of Western donor countries on the bilateral level, for example Germany, at this time only started to be restored. Finally, due to its international isolation and reportedly "stiff resistance" from the US, Syria's accession to the WTO was blocked and US resistance would have ruled out also any agreement on a SAP if the Syrian administration had wished to apply for such a programme. Finally, to complete the picture on the situation at the time the agreement with the EU was drafted, three further factors impeding the Syrian process of economic reform must be added. These factors comprised on the one hand of a general lack of domestic capacities for design and implementation of reforms. On the other hand and connected to this a 'reform team' in the administration able and prepared to push for further reforms seemed not to exist. In addition, Syria was and is still lacking an effective and sufficient social security system needed to mitigate the negative effects of liberalization.

All these obstacles and constraints on economic reform characterised the situation in which the Syrian-European AA was negotiated and finally agreed upon. Although observers agree that it was from the beginning a political choice for the Syrians to join the Barcelona process, the opportunities which an agreement like the AA could offer for catalyzing and credibly lock-in reform may have been an additional motivation, at least for the allegedly small circle of those in the political elite supporting economic opening. With this agreement the latter would have an instrument at hand with which they could justify unpopular reforms vis-à-vis reform opponents and the population at large. Besides the opportunity to lock-in reform, this agreement could contribute to the potential for growth and development through the channels of trade, investment and transfers of technology. Nevertheless, negotiations on the AA entered a critical stage only after the Americans invaded neighboring Iraq confronting the Syrian leadership with the threat of being the next potential target. To escape this fate and to find a strong international partner also in the face of further economic sanctions to be imposed by the US administration, the Syrian negotiators seem to have been prepared to accept not only far-reaching economic provisions but also several purely political elements demanded by the EU. Finally, the

Syrian negotiators faced the same problem as all other MPCs and developing countries in general: the blatant asymmetry of relations or fundamental lack of bargaining power when a small country such as Syria tries to negotiate a treaty with a strong and developed partner or large block like the EU.

A first draft of the agreement was reached in December 2003 but was blocked for the by Great Britain, Germany and the Netherlands requesting a tightening of the treaty's clause on Weapons of Mass Destruction (WMD). As Raymond Hinnebusch (2005) has argued, the Syrian-European AA was delayed by EU member countries "acting on behalf of Washington's agenda." After a months-long tug-of-war about the exact wording of this clause, the agreement was finally initialed in October 2004 only to be put on hold again. Among the political 'prerequisites' which must be fulfilled for the AA to get the approval by the European Council are, among others, an adequate cooperation of the Syrian government with the international tribunal to investigate the killing of the former Lebanese prime minister al-Hariri and the restoration of full diplomatic relations with the neighboring country[1]

Despite the failure to finalize the agreement, economic reforms in general and measures to streamline and liberalize the Syrian foreign trade regime nevertheless accelerated considerably. The Baath Party Regional Congress of June 2005 recommended the transition of the Syrian system into a social market economy. Moreover, in May 2006 the Syrian president signed into law the Tenth Five Year Plan (10th FYP) which is based on a completely different logic and methodology than former Syrian development plans and is viewed by many as a comprehensive programme for liberalization and adjustment of the Syrian economy.

Against this background some Syrian and international experts argue that with the year 2004 the process of economic reform in Syria entered a new phase, the phase of "neoliberal economic development". According to Samir Aita's (2008; see also Aita 2006) interpretation, those behind this new orientation were the members of what he calls the Syrian "power system." This "power system" which controls the most powerful bodies within the regime like the presidency, the presidential guard and the intelligence apparatus would have to be distinguished as a separate interest group from the "state". The power system follows its own logic of production and reproduction and should be regarded as the prime decision maker in the Syrian system whereas the state as a group of institutions, among them the government, only execute policies. Moreover, Aita maintains that "foreign threats" provoked the power system's decision to push through first the swift drafting of the agreement with the EU and second, after its signature was put on hold, the widening and deepening of trade reforms after 2004. In earlier periods political instability and international pressure has in contrast been used as an excuse for postponing economic reforms.

This coincided roughly with two other developments or rather changes in behavior of those in charge of economic policy in Syria. First, the Syrian administration apparently started to ask for or at least to accept international aid in the form of technical assistance and economic policy advice. One of the most striking examples for this was most probably the process of drawing up the 10^{th} FYP in which the Syrian administration, in particular the SPC, received support from UNDP, ESCWA, the German GTZ and the EU. Besides policy advice and consultancy, technical assistance is channeled into restructuring of ministries and other public institutions including capacity building to make the staff of these organs capable of devising and implementing economic reforms (Zorob 2006a). Second, the Syrian government seems, as Samir Seifan (2008) expressed it, to have "replaced" critical public debate of its programme of economic reform with the 10^{th} FYP. This does not mean that the discussion on reforms, economic policy and the economic situation in general so lively at the beginning of the decade after Bashar al-Asad came to power has stopped. The lecture series in the framework of the "Economic Tuesday Symposium" for example are ongoing and economic issues are well covered in several newly established economic and political journals and even in the government controlled newspapers. However and again using the words of Samir Seifan, the government decided in 2005 to check the reform dialogue "within the official limits."

Main Structure and Contents of the Syrian-European AA

Table 2 shows the general structure of the draft agreement and emphasizes those titles and chapters (italicized and shaded lines) in which the Syrian-European AA contains broader and/or deeper provisions than the AAs concluded with the other MPCs. In general the agreement consists of provisions for each of the three "baskets" of the European-Mediterranean Partnership (EMP) as agreed to by the EU and its Mediterranean Partners at the Barcelona conference in November 1995 (see European Commission 1996). Objectives and measures of the first basket or *Political and Security Partnership* on the bilateral track between Syria and the EU are covered in the provisions of Title I. They provide for a framework to conduct a regular political dialogue on issues of mutual interest and for cooperation in different areas. In defining 'essential elements' of the treaty the Syrian-European Partnership Agreement goes clearly beyond the provisions contained in the agreements with the other MPCs. In addition to the respect for the principles of democracy and human rights and in line with the Council Decision of 17 November 2003, the Agreement contains as an essential element cooperation to counter the proliferation of WMD and their means of delivery through full compliance with existing obligations under disarmament and non-proliferation treaties and agreements. The Agreements' provisions on cooperation in the framework of the *Partnership in Social, Cultural and Human Affairs* or third basket are also more elaborate and contain more commitments and fields of cooperation as compared to the agreements with the other MPCs. The different areas of cooperation extend from culture and social development to justice, with special focus on the independence of the judiciary, the prevention and control of illegal immigration and the fight against organized crime and terrorism.

Table 2: General Structure of the Draft EU-Syria Partnership Agreement

Article 2	**Respect for the Democratic Principles and Fundamental Human Rights**
Title 1	**Political Dialogue and Cooperation**
	° Article 3: Regular Political Dialogue
	° Article 4+5: Weapons of Mass Destruction
Title II	**Free Movement of Goods**
	° Chapter 1: Elimination of Customs Duties
	° Chapter 2: Common Provisions
	° Chapter 3: Customs and Related Matters
Title III	**Right of Establishment and Services**
	° Chapter 1: Right of Establishment
	° Chapter 2: Cross-Border Supply of Services

	° Chapter 3: General Provisions
Title IV	**Payments, Capital Movements and Other Economic Matters**
	° Chapter 1: Payments and Capital Movements
	° Chapter 2: Competition
	° Chapter 3: Government Procurement
	° Chapter 4: Other Economic Matters
Title V	***Dispute Settlement***
Title VI	**Economic Co-operation**
Title VII	**Co-operation in Social and Cultural Matters**
	° Chapter 1: Social Dialogue
	° Chapter 2: Social Co-operation Actions
	° Chapter 3: Cultural Co-operation
Title VIII	**Co-operation in the Fields of Justice, Migration, and the Fight against Organised Crime**
Title IX	***Co-operation on Counter-Terrorism***
Title X	**Financial Co-operation**
Title XI	**Institutional, General and Final Provisions**

Source: Own compilation based on European Commission (2004c):

The economic provisions are not only much broader in scope and depth than the provisions included in the AAs with the other MPCs. In some aspects they even resemble those anchored in the EU's 'most advanced' bilateral FTAs with Chile and Mexico which are however far more advanced with respect to their economic development and relative standing compared to the industrialized countries than is Syria. The basic element of the *Economic and Financial Partnership* or second basket is the gradual establishment of a free trade area (FTA) between Syria and the EU. With respect to Syrian exports of industrial products to the EU, the duty- and quantitative restrictions-free access *already granted* under the Cooperation Agreement signed by the Parties in 1977 is reconfirmed. Now, however, under the EMP, the establishment of the FTA first of all implies the complete opening-up of the *Syrian* market for European industrial goods. The measures which have to be implemented by the Syrian administration immediately after the treaty has come into force, consist of the elimination of all import or export restrictions on trade between Syria and the EU, including prohibitions, quotas and import or export licensing requirements. Customs duties and other surcharges applicable to the import of industrial products into Syria will be reduced in a linear manner to zero according to different schedules over a transitional period of 12 years starting from the date on which the agreement enters into force. Reciprocal trade in agricultural products, processed agricultural products and fisheries between the EU and Syria shall be liberalized progressively. Syria, however, committed to a far-ranging opening of its agricultural market (for more details see Section 3.1). In addition, trade between Syria and the EU will be bound by the principles set out in the WTO Agreement on the Application of Sanitary and Phytosanitary (SPS) measures as well as the WTO Agreement on Technical Barriers to Trade. As regards standards, the Parties agreed to take steps to encourage the use of EU standards and technical regulations in Syria and Syria committed itself to comprehensively reform and modernize customs procedures in line with EU and international standards.

With respect to investment, Syria grants European investors national or MFN treatment (whichever is better) for right of establishment and operations in Syria. The branches excluded from the general right of establishment include primarily the production of goods and services which were reserved for government monopolies at the time of negotiating the agreement such as wholesale trade in wheat and cotton. In other sectors like wholesale trade, transport or construction a minimum Syrian ownership is required which in most cases is set at 25 percent. Furthermore, within a year of the treaty coming into force Syria committed itself to put forward a schedule for opening the telecommunications industry within six years at the most. Besides the right of establishment the parties undertake to allow, except in cases of serious balance-of-payments difficulties, all payments for current transactions to be made in a freely convertible currency and shall ensure the free movement of capital relating to FDI as well as free liquidation and repatriation of capital and profits. As regards competition rules, Syria committed itself to taking into consideration the EU rules when formulating its own law. Moreover, and in contrast to the agreements concluded with the other MPCs, the parties will cooperate on the enforcement of competition rules. As far as government procurement is concerned, and again contrary to the other MPCs, the parties agreed to open procurement activities and to grant national treatment to the other party's goods, services and suppliers for a list of entities annexed to the agreement. This means, for example, that the Syrian Ministry of

Irrigation, which is included in the list on Syria's government procurement annexed to the AA, is not allowed to discriminate in favor of local Syrian suppliers against European competitors by way of specific rules, procedures or practices of procurement. The effective opening of procurement markets will be reviewed regularly. With respect to intellectual, industrial and commercial property rights, the partners committed themselves to granting and ensuring their protection in accordance with the highest international standards including the principles set by the WTO-Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). For this purpose Syria agreed to accede to a number of multilateral conventions according to a specific calendar. Finally, the trade and trade-related provisions of the treaty will be applied by both partners in advance pending its entry into force by means of an interim agreement.

Incentives for Trade Liberalisation and Adjustment in the AA

Opening-Up the Syrian Market: Trade Creation, Trade Diversion and Tariff Revenue Losses

In the following sections the analysis of the Syrian-European AA will concentrate primarily on two major effects or group of effects of free trade and integration: on the one hand the static effects of trade creation, trade diversion and tariff revenue losses and on the other hand the effect of securing and enhancing market access. By doing so it will investigate the direct and indirect incentives or stimuli the AA is offering for trade liberalization and adjustment and compare it to what has been achieved in trade reform in recent years. In addition, the expected impact of these effects will be evaluated illustrating the challenges the implementation of the AA will probably create for the Syrian economy.

As noted above, the establishment of the FTA with the EU first of all implies the complete opening-up of the Syrian market for European industrial goods. Except for cars, all duties above 50% will be brought down to 50% at the entry into force and be abolished in twelve years. Tariff rates for cars at 255% (145%) shall be reduced to 150%

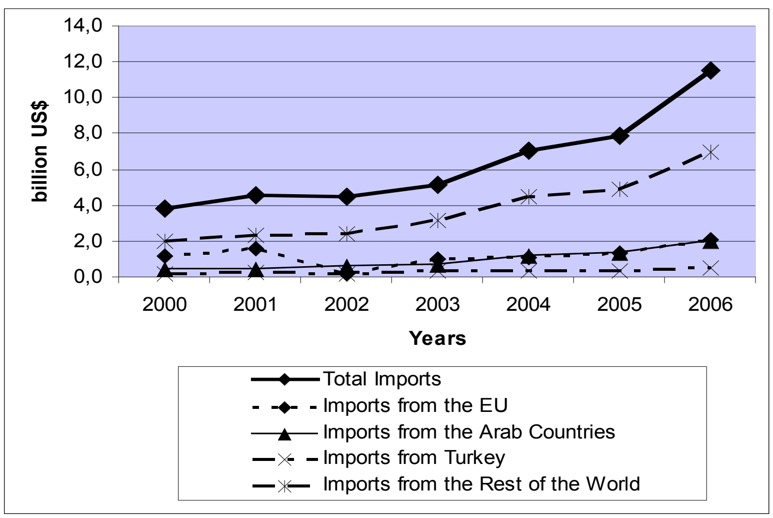
(65%) in the first three years and then be gradually reduced to zero during the rest of the transition period. Similar to industrial goods, customs duties applicable to the import of agricultural products into Syria will be dismantled to zero in a linear manner within 12 years according to different schedules. Annual tariff quotas at zero duty have been established for the EU's export of several sorts of oranges, mandarins and fresh apples. Wholesale services for 'strategic products' like wheat, tobacco and cotton which are to date under government monopoly will not be opened to foreign competition. Duties on imports of selected fisheries and a large number of processed agricultural products into Syria will be reduced to zero according to different schedules in a linear manner latest until the end of the twelve years transitions period as well. Quotas at reduced MFN-duties have been set for EU-exports of mineral water, soft drinks, spirits, cigarettes and tobacco.

Despite the many measures of trade liberalization enacted since the initialization of the AA in 2004, the above outlined provisions would translate into a major further opening of the Syrian market. Nevertheless, the tariff reductions implemented on the unilateral level and elimination of import prohibitions anticipate some of the measures integrated in the AA. Maximum tariff rates have already been reduced to 50 percent or 60 percent respectively with the latter rate only applying to selected goods of HS 87, i.e. the category of vehicles and parts thereof. The number of rates has declined to eleven ranging between 1-60 % excluding a surcharge which however applies only to a part of goods and amounts to 1 percent or 15 percent depending on the product concerned (see Syrian Customs 2008). In addition, many import prohibitions have been eliminated in recent years and in particular during the second half of the last and this year. Officials from the Ministry of Economy and Foreign Trade announced in the Syrian media that the new negative list published at the end of April this year mainly contains goods which are still prohibited from importation to Syria because of religious, health, security or environmental reasons (see for example Ma'la 2008). The new negative list covers only seven pages of goods according to the 4-digit HS-level reduced from initially 63 pages in 2006. A closer look at the new list however shows that around 30 percent of agricultural goods (HS 1-24) and 10 % of industrial products according to the 4-digit HS-level are still banned from importation and/or can only be imported by public entities or selected branches of the economy. As regards agricultural produce, many fresh and chilled fruits and vegetables are among the goods still prohibited from importation. It should be mentioned in this context however that agriculture is protected by tariff and other barriers in almost every country on this earth and in particular in the industrialized world! Besides tariff reductions and lifting of import prohibitions, the first steps for a streamlining of customs procedures have been taken. Accordingly, the Syrian-European AA offers on the one hand the possibility to anchoring the measures enacted in recent years on the unilateral level by a binding legal agreement. On the other hand, additional reforms or a deepened opening of the Syrian market could be catalyzed by the provisions of the AA.

But what are the effects to be expected from the AA as regards trade creation, trade diversion and loss of tariff revenues.?[2] In general, the expected positive effects of regional integration on trade, investment and growth cannot be determined *a priori.* Nevertheless, it is possible to establish a set of different criteria or preconditions which should be met by a 'successful' free trade or regional integration agreement. Of crucial importance is the degree of openness of the agreement, the existence of mechanisms for enforcing the agreement's provisions in addition to purely political preconditions like a peaceful environment. Another criterion applies to the form and content of an RIA and its degree of "deepness." Because the probability of positive effects increases with the decline of barriers to transactions and the costs to overcome them, an RIA will be the more beneficial the more it contributes to eliminate restrictions 'behind the border' in addition to the reduction of transaction costs caused by 'border' barriers such as customs duties (for more details on the theoretical background and the 'preconditions' developed in the literature see, among others, Borrmann 1997; Schiff and Winters 2003; Zorob 2006b).

Albeit the nominal average tariff has declined from more than 20 percent at the time when the AA was negotiated to 14.5 percent now, tariff protection remains substantial in Syria with maximum rates at 60 percent and rates escalating with the stage of processing. In addition, there are still goods banned from importation and a host of other non-tariff barriers in place. Therefore the introduction of free trade with the EU promises substantial effects of trade creation. EU exports to Syria would likely expand, particularly in those branches where production is currently protected by high tariffs and other trade barriers and where the Syrian economy does not enjoy comparative advantages; this means that many of Syria's import-substituting and especially capital-intensive industries in the public sector may come under strong pressure. As regards agricultural products, the still numerous import prohibitions, in many cases high tariffs and the maintenance of competitive production structures of Syria and the EU particularly in typical temperate zone products such as bovine meat, dairy products, vegetable oils, corn and wheat promise substantial efficiency effects. The process of adjustment might however be distorted to a substantial degree because both parties are subsidizing for example production of cereals and the prohibition of subsidies is not stipulated as target in the AA.

Figure 1: Syrian Imports, 2000-2006



Source: *Author's compilation based on data extracted from* UN Comtrade Database.

The impact of recent trade reforms on the probability of the AA to generate trade-diverting effects seem to be rather ambiguous. Whereas the elimination of import bans aggravates the risk of trade diversion, tariff reductions are diminishing it. Preference margins for European suppliers and therefore the potential for trade diversion should be low in such product categories and branches where customs duties have been reduced to no more than one or three percent which is according to the new Syrian tariff schedule the case for most of raw materials and other inputs of production as well as capital goods. In trade in most goods for final consumption, however, the risk of trade diversion, i.e. switching with the dismantling of tariffs on imports sourced in the EU from more cost-efficient (for example Chinese suppliers) to less cost-efficient European suppliers thereby forgoing tariff revenues, remains substantial because tariffs are still high with maximum rates as high as 50 or 60 percent. In addition, only a relatively small part of Syrian imports is currently originating in the EU. Whereas imports in general soared in recent years as illustrated in *Figure 1,* imports from the EU more or less stagnated with its value in 2006 being only slightly higher than that in 2001. As a result, the share of imports from Europe in total Syrian imports dropped from some 35 percent in 2001 to below 20 % in 2006 (see *Table3*).

When imports from the Arab countries and Turkey are added with whom Syria has signed and started to implement free trade agreements**,** the share of trade that would be included within free trade zones were the AA to be implemented, jumps to 40 percent. Since these partners together are currently the most important sources for Syrian imports of mineral and chemical products (HS 25-26, 28-38) and tariffs in these product categories are generally low, the risk of trade diversion should also be low. There is, however, a high risk of trade diversion in most categories of other manufactured goods as well as agricultural produce where imports in large part originate in the "rest of the world" category. This is also the case for the category of machines and vehicles (HS 84-89) which traditionally contributed a large part to Syrian imports from the EU, but in which Syrian importers have increasingly switched in recent years to suppliers from other regions of the world and in particular Asian countries. In addition, this kind of import coming from the EU comprises a large proportion of the equipment for Syrian industry for which customs duties are generally rather low in contrast, for example, to cars and other vehicles for private use which are mostly delivered by Asian suppliers. Since many of these goods are still subject to high tariffs, there is a substantial risk of trade diverting effects associated with the discriminatory dismantling of trade barriers with the

HS	Product Group	EU	Arab Countries	Turkey	Rest of the World	Total
as a share of total imports (in percent)						
1 bis 24	Agricultural Goods	1.7	2.8	0.6	8.5	13.6
27	Mineral Fuels	7.2	2.6	1.0	16.7	27.5
25-38	Mineral and Chemical Products	1.7	3.1	0.6	2.8	8.2
39-49	Plastics, Paper, Hides, Wood and Articles Thereof	1.2	4.0	0.3	4.8	10.3
50-67	Textiles, Footwear	0.5	0.3	0.4	3.0	4.2
68-83	Other Manufactures	1.3	3.2	0.6	8.3	13.4
84-89	Machines, Elect. Equipment, Vehicles	4.6	1.3	0.6	14.9	21.4
90-97	Optical, Musical Instruments, Furniture, Toys	0.3	0.1	0.0	1.0	1.4
Total		18.5	17.4	4.1	60.0	100.0

Table 3 Sources of Syrian Imports according to Major Product Groups, 2006

Source: *Author's calculations based on* UN Comtrade Statistics Database.

EU. To contain this risk as much as possible there seems to be no other way but to further reduce customs duties at the unilateral level.

There are, however, substantial efficiency and welfare enhancing effects to be expected from the implementation of trade facilitation measures anchored in the AA. Measures of this kind could lead to a reduction of transaction costs not only in trade with the EU, but also in trade with third countries. This would probably induce further trade creating effects besides saving costs which could contribute to compensating for the loss of tariff revenues in the state budget. Since the Syrian administration, however, seems more or less lacking not only the institutional capacities and technical expertise but also the financial means required to implement measures like streamlining and modernization of customs procedures or harmonization of standards, the EU should be prepared to back this process with generous financial and technical assistance probably in cooperation with other donors. The MEDA-funded Quality & Standards programme which aims at supporting the Syrian administration to develop the national capacities for formulation of technical rules and control of their implementation, finally started implementation in spring this year after years of delays. Additional efficiency gains are expected to be generated by the liberalization of trade-related and other services anchored in the AA. Streamlining of customs procedures and the liberalization of services seem on the other hand to be the only opportunities which the AA offers for Syrian manufacturers to reduce production costs since tariffs on most raw materials and other inputs of production are already relatively low. In this context it should be repeated that dismantling trade barriers with the EU will put strong pressure not only on the current account but also on Syrian firms in industry, agriculture and services. It must be expected that many domestic suppliers will be forced out of the market generating potentially high losses in the short to medium term in income and employment. Theoretically, the resources set free by liberalization will move to other, more competitive branches and sectors benefiting from the new division of labor between the partners to a FTA. The problem is, however, that chances for a reallocation of resources might not be ready available in a country like Syria. At least such a process will take time and depends crucially on the agreement's contribution to improve market access of Syrian products to the EU.

To minimize the negative effects on production, income and employment to be expected as a result of trade liberalization with the EU, the Syrian administration could take steps to help Syrian firms to better prepare themselves for EU competition through a programme of 'mise-à-niveau' in advance of the agreement's implementation. In February 2007 a pilot programme called 'Industrial Modernization and Upgrading Programme for the Syrian Arab Republic' sponsored by the *United Nations Industrial Development Organization (UNIDO)* and the Italian government started to be implemented which however seems not directly connected to the AA. This small programme would of course need to be substantially enlarged for which the EU also might provide additional funding. According to the revised National Indicative Programme (NIP) 2008-2010 for Syria, the EU has scheduled a programme for start of implementation in 2010 to support the modernization of state-owned industrial enterprises and their corporatization (see European Commission 2008). Moreover, the Syrian administration should take measures to cope with income and employment losses through the establishment of social safety nets for affected income groups which are currently lacking or are at least insufficient (see, for instance, IMF 2006b). Finally, and in case there is a possibility for renegotiating the AA, one could think about prolonging the transition period of introducing free trade with the EU to gain more time for restructuring local enterprises. It may be noted here that Egypt succeeded in retaining a longer period of transition for specific industrial goods going beyond the 12-years period agreed to with Syria and the other MPCs.

Complementary measures such as social safety nets require substantial financial means which most probably must be provided to a large extent by the Syrian government. The liberalisation of trade with the EU, however, will generate losses in government revenues. These losses nevertheless should be manageable. First, tax revenues from international trade as shown in *Table 4* are traditionally low, especially if compared to other MPCs, amounting to around 2 percent of GDP and 7-9 percent of budget revenues in the period 2001-2006. Second, there are several alternatives at hand to develop the domestic tax base including the introduction of a VAT which is planned according to recent announcements for 2009.

Table 4: Revenues from Tariffs and Other Taxes on International Trade in the

Syrian Budget, 2001-2006

	2001	2002	2003	2004	2005	2006*
Revenues (tariffs and other taxes on foreign trade) (LS billion)	20.4	25.3	28.8	31.3	30.7	30.6
As a Share of Total Budget Revenues (in percent)	6.7	8.6	9.0	9.1	8.6	7.8
As a Share of Tax Revenues (in percent)	22.1	21.8	24.5	21.5	19.1	15.4
As a Share of GDP (in percent)	2.0	2.2	2.6	2.5	2.1	1.7

Preliminary estimates.* ***Source:* *Partly author's calculations based on data extracted from IMF (2006, 2007): Article IV Consultation – Staff Report.*

More problematic is the general state of the government budget with a rising deficit despite steady cut backs in investment expenditures in recent years as a result of declining oil export revenues and rising costs of government subsidies. A budget deficit amounting to 5.7 percent in 2006 and the prospect of oil export revenues soon depleting completely will not leave much room to finance additional measures like a programme for industrial restructuring or the establishment of social safety nets.

Promoting Exports and Diversification: Aid and Market Access

Securing and enhancing market access is generally regarded as one of the most important dynamic effects of regional integration.[xxv] Better access for Syrian goods to the market of the EU could vitally contribute to support Syrian manufacturers switching from import-substituting to export-oriented sectors in the framework of an overall outward-oriented strategy of development. Benefits for Syria's manufacturing sector could include market enlargement, the impulse to improve efficiency from competition, and greater incentives for inward investment, with technology transfer. Resources set free by the opening of the domestic market to European competition could be reallocated to those branches and sectors with export potential destined to the European market.

In general, however, the new RIAs concluded since the beginning of the 1990s aim for the most part at *reconfirming* the market access provisions achieved under former trade arrangements (i.e. 'historical' preferences) and this is so for Syria. Syria had been granted duty-free access to the European market for its industrial goods in the framework of the 1977 cooperation agreement. The benefit to Syria of reconfirming these 'historical' preferences via the AA is however severely constrained first of all by the continuous erosion of these preferences in recent years caused by different factors including the EU's reduction of customs duties in the multilateral framework, the abolishment of textile quotas for the Syrian competitors on the European market, the EU enlargement and finally the large number of free trade and cooperation agreements the Union has signed with other third states.

The agreement can be seen as gaining Syria 'insurance' against the possibility that the Northern partner arbitrarily resorts to new and non-conventional measures to protect their markets from foreign competition (through, for example, the exclusion of antidumping provisions in the treaty). The Syrian-European AA, however, in a similar manner as all the treaties with the MPCs, allows for antidumping, safeguards and countervailing measures. This risks severely limiting the 'insurance effect' of the AA and future exports to the EU especially in those branches and sectors where Syrian manufacturers enjoy comparative advantages such as the textiles and foodstuffs industries. To make things worse, the provisions for antidumping, safeguards and countervailing measures in the AA as such do not only offer large scope for discretion but in addition are not covered by the dispute settlement mechanism established by the AA. Until now however, Syrian exports were not targeted by EU antidumping or countervailing measures but the EU initiated in 2001 for the first time in its relations with Syria surveillance measures for cotton yarn imports originating in Syria (see European Commission 2004a; Zorob 2006b).

Table 5: Volume and Structure of Syrian Exports to the EU

	2000	2001	2002	2003	2004	2005	2006
Exports to the EU* (US$ million)	3,050	3,382	3,943	3,271	2,897	4,080	4,384
EU Share in Syrian Exports (in percent)	65.8	70.0	60.3	57.1	53.8	63.2	43.1
Share of Crude Oil in Exports to the EU* (in percent)	92.6	93.5	93.4	91.5	91.9	92.6	84.6
Non-Oil Exports to the EU (US$ million)	226	221	260	279	235	302	677
EU Share in Syrian Non-Oil Exports (in percent)	20.6	19.4	14.3	17.0	13.5	14.5	11.8
Agricultural Exports to the EU (SITC 0, 1, 2 and 4 excluding 27, 28) (US$ million)	81	66	96	108	81	138	230
EU Share in Syrian Agricultural Exports (in percent)	13.0	12.5	8.9	11.1	8.2	12.7	10.8

2000-2003 = EU (15); 2004-2006 = EU (25).* ***Source:* *Own calculations based on United Nations:* UN Comtrade Statistics Database.

The benefits of the agreement are also qualified by the fact that at present, most of Syrian exports to the EU are still made up of crude oil while its non-oil exports are increasingly directed to other markets. Oil exports account for more than 90 percent of exports to the EU in the period 2000-2006 as illustrated in *Table 5*. Even in 2006, when the share of Syrian oil exports to the world in total exports dropped below 45 percent, the share of crude oil in exports to the EU remained as high as 85 percent. The volume of Syrian non-oil exports to the EU more than doubled in the period 2000-2006. Since non-oil exports to the world, however, have risen nearly sixfold in the same period, the EU share in Syrian non-oil exports decreased steadily from more than 20 percent in 2000 to only 12 % in 2006 despite the EU's enlargement in 2004. Around one third of the non-oil exports destined for the EU market are made up of agricultural goods. They account for only a small share in total Syrian agricultural exports, hovering around 8-13 percent in the period 2000-2006. In foodstuffs and beverages this share is even lower. In contrast, countries like Morocco or Tunisia are delivering more than half of their total agricultural exports to the EU.

Whereas in the case of industrial products, the low competitiveness of Syrian goods on the European market could well be responsible for their poor export performance, the access of Syrian agricultural exports to the EU remains until today heavily restricted. The reasons for this are the general high protection of the European agricultural market as a result of the Union's Common Agricultural Policy (CAP) and the low level of concessions granted to Syria for agricultural exports in the framework of the 1977 cooperation agreement. The product coverage of the concessions amounted to only some 16 percent of total agricultural exports to the EU in the period 2001-2003 compared to 67 percent in the case of Morocco and 72 percent in the case of Tunisia reflecting that the other MPCs had been granted substantially more preferences in their former agreements with the EU (Grethe / Nolte / Tangermann 2005: 306). Therefore, a significant extension of agricultural concessions in the framework of the AA ranked from the beginning as one of the most important claims from the Syrian side.

With respect to agricultural goods, the AA offers, theoretically, an improvement in market access. As measured by the amount of products, Syria would get the most concessions for agricultural produce among all MPCs. According to the 8-digit level of the Combined Nomenclature (CN), tariff reductions without any restrictions are granted for 376 goods compared to 46 goods in the agreement with Morocco and 61 goods in the AA with Tunisia. It should be mentioned, however, that on the one hand the agricultural protocols with Morocco and Tunisia have been renegotiated and extended already (Grethe / Tangermann 1999: 17; Grethe / Nolte / Tangermann 2005: 300). Lebanon was granted duty-free access for all its agricultural exports to the EU except a list of goods (of course the most competitive Lebanese agricultural goods on foreign markets) for which quotas have been established. On the other hand, only for a part of the above-mentioned agricultural goods will customs duties be abolished completely. Moreover, for most of those agricultural products which the Syrian administration defined as ‘strategic’ and in which it enjoys comparative advantages on the international level, such as potatoes, fresh tomatoes, oranges, fresh apples and olive oil, annual tariff quotas (TRQs) at zero or preferential duty are in most cases limited to certain calendar periods and on above-quota exports of these goods full or reduced MFN duties will apply. Customs duties on most fisheries originating in Syria will be abolished immediately or in the second year of entry into force of the Agreement. For selected processed agricultural products TRQs at zero duty are granted, whereas for others ad valorem duties will be abolished while maintaining specific duties on the agricultural component. For those processed agricultural products not listed in Protocol 5 no customs duties or quantitative restrictions will apply in the future (see Zorob 2006b; Hindi 2004). During the third year after entry into force of the Agreement, the Parties shall review the situation in order to determine further steps for liberalization.

It is hoped in Syria that the enlargement of agricultural concessions will promote agricultural exports to the EU and thus production and employment besides attracting substantial foreign and domestic investment to this sector. In addition, increasing agricultural exports could contribute to contain a rising deficit in the trade and current account balances expected to result from trade liberalization with the EU. These expectations were initially based on the fact that there are many agricultural products (for example different sorts of fruits and vegetables besides olive oil and sheep) in which Syria enjoys a comparative advantage on the international level, produces high surpluses and at the same time are not or only in small quantities exported to the EU. These conditions seem, however, to have changed to some extent in recent years. According to Syrian experts, the Iraqi market currently absorbs much of the excess production in agricultural goods besides a higher demand for foodstuffs on the local market generated by the estimated 1.5 million Iraqi refugees living in Syria. In spring this year export controls for selected products like tomato were even introduced to hold in check spiraling price increases on the local market. Moreover, to make effective use of the above mentioned concessions, enhance agricultural exports to the EU in a substantial magnitude and attract investment, Syrian farmers must work hard to fulfill other conditions required for a successful access to the European markets as regards, among others, standards and quality. As many authors specializing on Euro-Med agricultural trade have emphasized, concessions are a necessary but not sufficient condition for entering the European market (see, for instance, García-Alvarez-Coque 2001, 2002). Finally, Syria 'bought' its new concessions, and in contrast to the other MPCs, with an extensive opening of its own agricultural market despite warnings expressed in several reports compiled by experts in agricultural trade (see García-Alvarez-Coque 2001). Accordingly, one might expect more jobs and income in Syrian agriculture to be lost than created with implementation of the AA. Syrian experts however do not expect Syrian consumers to substitute traditional local produce in particular as regards fruits and vegetables with goods coming from the EU.

Besides the above mentioned erosion of historical preferences, restrictive technical barriers to trade like EU standards and quality controls, complex rules of origin and the EU's right to resort to measures of contingent protection could seriously impede the AA's effect in securing and enhancing Syrian market access. Differences in definitions of product and processing standards between Syria and the EU and connected to this the requirement of complex and time-consuming conformity assessment and certification procedures are threatening to increase transactions costs in exports trade with the EU. Manufacturers in the foodstuffs, textile and pharmaceutical industries in Syria and other countries of the region are complaining about high costs associated with the process of complying with European standards and specifications and/or about lacking adequate and high-standard domestic capacities for conformity assessment.

Among the most constraining factors hampering exports as well as imports in Syria are traditionally cumbersome and time- and cost-consuming customs procedures together with red tape (see, for instance, Zarrouk 2003). As outlined in section 2.3, Syria committed itself to comprehensively reform and modernise customs procedures in line with EU and international standards which should make it possible to reduce transaction costs for exports as well as for imported inputs and thus to enhance competitiveness of Syrian exports to the EU besides generating positive spillover effects to trade with other partners. However, those reforms will take time to materialise and like harmonisation of standards will require additional funds and expertise.

Finally, the impact of the complex and restrictive rules of origin (RO) in particular in finished goods and in those industries like textiles and apparel on Syrian exports' market access to the EU as well as indirectly on Syria's ability to attract FDI are at best ambiguous.[xxvi] In the worst case they will seriously hamper it by increasing trade transaction costs in trade with the EU to the extent that the duty-free access granted to Syrian industrial goods is fully eroded. In many cases the reorganization of production processes to comply with rules of origin requirements and the costly obligation to prove origin might urge manufacturers to accept paying customs duties. In addition, cumulating inputs originating in the EU, for example, might deprive Syrian exports of competitiveness where they substitute for cheaper inputs coming from other, for example Asian or (non-MPC-) Arab countries. For being allowed to cumulate inputs from other members of the Paneuromediterranean System in addition to the EU, Syria is required to conclude FTAs with all of them comprising the same rules of origin protocol. Accordingly, in the current situation Syrian manufacturers would only be allowed to cumulate inputs originating in Turkey as local content for exports to the EU. This is because Syria neither belongs to the *Agadir Agreement* or *Mediterranean Arab Free Trade Area (MAFTA)* nor did it conclude FTAs with the remaining non-Arab members of the System such as the EFTA countries.

Finally, restrictive RO are in general among the major factors supporting the establishment of a so-called hub-and-spokes system and its risk of diverting investment from the spokes to the hub. Potential investors who want to sell predominantly on the market of the large country or in this case the EU are induced to locate there because by doing so they are not obliged to comply with rules of origin. The risk of hub-and-spokes effects can be mitigated by free trade and if possible deeper integration among the spokes. For this reason it is extremely important for Syria to conclude FTAs with the other partners of the Pan-Euro-Med System; in particular it needs to foster integration with its Southern partners via a potential widening and deepening of GAFTA to improve its capability to attract market-seeking FDI and thereby to become a sub-regional hub reaching out for neighboring and Gulf countries besides serving as a major spot for transit trade. Given that GAFTA does not confer the right of cumulation of origin in the framework of the Pan-Euro-Med System, Syria should also accede to the

Agadir Agreement to be able to benefit from the right of cumulation. Finally, in order to urge the EU to simplify rules of origin in the AA, the Syrian administration seems to have no other option than to work together with the other MPCs and probably rest of members of the Pan-Euro-Med System and approach the EU as a group.

On the other hand, however, Syrian suppliers might benefit from the Pan-Euro-Med RO in those branches where the Syrian industry maintains fully integrated production chains like for example in cotton textiles and apparel. In addition, the Pan-Euro-Med System of Cumulation is expected to deliver substantial incentives for Syrian industry to develop production and exports of intermediate goods to the other members of the System and connected to this attracting FDI into those branches.

Positive effects of market-access will only materialize in the long term and only if the Syrian administration is prepared to implement the necessary reforms. In this process, however, the EU could and should become a major partner providing the Syrian administration with generous financial and technical assistance. As illustrated in *Table 6,* the amounts committed or allocated to Syria in the framework of the *MEDA programme*, the former principal financial instrument of the EU for the implementation of the EMP, and its successor the *European Neighbourhood Instrument (ENPI),* are substantially lower than the amounts provided for most of the other Arab MPCs.

Table 6: Assistance in the Framework of MEDA and ENPI (€ million)

	Algeria	Egypt	Jordan	Lebanon	Morocco	Syria	Tunisia	WBG	Regional
MEDA I 1995-1999 Commitments	164	685	257	182	644	107	431	106	211
MEDA II 2000-2006 Commitments	307	596	314	127	907	207	472	397**	688
ENPI 2007-2010 Allocations	220	558	265	187	654	130	300	632	343***
A* MEDA I (€)	1.07	2.15	10.28	10.41	4.49	1.32	8.99	7.05	0.26
A* MEDA II (€)	1.43	1.33	8.97	5.18	4.52	1.84	7.02		0.61

*A = Average per year per inhabitant.** 2000-2004 only***Regional Programme - South

Source: European Commission (2007a): ENPI – Funding 2007 – 2013; European Commission (2007b): ENPI Regional Strategy Paper 2007 – 2013 and Regional Indicative Programme 2007 – 2010.

This is in particular the case with regard to the per capita ratios shown in the last two rows of the table. If actual payments are assessed, the picture becomes even worse. Of the amounts committed in the framework of MEDA I only one third have been actually disbursed. However, loans provided by the EIB to Syria have increased considerably in recent years and in particular since the *Facility for Euro-Mediterranean Investment and Partnership (FEMIP)* started its operations. Although the EU has provided little assistance to the MPCs as a group relative to the magnitude of reform and liberalization that these countries have committed themselves to within the framework of the AAs, it has to be noted, that the Syrian administration itself has to take some of the responsibility for the limited amounts committed and disbursed. Counted among the major factors responsible for the small amount of assistance offered to Syria are problems like low absorption capacity or lack of experience of the Syrian administration to coordinate development cooperation (Zorob, 2006b; European Commission, 2007c).

To be realistic, one can hardly expect the EU to back up the Syrian economy with the same amount of massive financial assistance the US government has offered Mexico in the 1990s to help it to escape a major balance of payments crisis. Nor can one expect EU assistance to compensate for the high short-term adjustment costs which the Syrian economy certainly will have to face as a result of opening-up its market. This is not to deny, however, that on the one hand EU assistance can be expected to be expanded considerably after the AA is signed and started implementation. On the other hand EU support mainly in form of technical assistance provided to Syria in recent years apparently generated some positive effects in restructuring ministries and developing local capacity.

The National Indicative Programme (NIP) for 2007-2010 mentions support for political and administrative, economic and social reform as priorities for action with a special focus on capacity building in all areas (see European Commission 2007c). Assistance to be offered in the framework of the current NIP will cover a Trade Enhancement Programme offering policy advice and capacity building for trade facilitation and trade promotion and a Business Environment Simplification Programme with the general target to support the removal of the most stringent regulatory and administrative barriers to doing business in Syria. Both programmes were approved in late 2007 but the signature of their financing agreements seems to be still pending (Syria Report 2007). In addition, the EU plans to provide assistance for the modernization of Syrian industrial SOEs and their corporatization

(Industrial Upgrading and Restructuring Programme) as well as to support the Syrian government in developing and implementing social protection programmes (Social Protection Programme). EU-funded assistance programmes like the Trade Enhancement Programme or the Quality & Standards Programme should help add substance to those issues which are only defined in broad terms in the AA's provisions such as harmonization of standards and accordingly to improve market access of Syrian exports to the EU in the longer run. In addition, programmes to assist the establishment of social protection systems and the upgrading of the Syrian industry may provide adequate first steps in assisting Syria to mitigate to some extent and to come to terms with the negative effects to be expected from opening-up the Syrian market to European competition. EU assistance however needs not only to be significantly expanded in its magnitude.

In sum the analysis outlined in the previous sections showed that measures of trade and accompanying reforms in other fields of the economy enacted in the years since the initialization of the Syrian-European Association Agreement do not make this agreement redundant. Rather, these measures and their impact on the economy in the form of increased competition on the Syrian market and related efficiency effects should improve the conditions for entering the agreement. Nevertheless, there is still a long way to go for Syrian decision makers to foster Syria's integration into the world economy via promotion of exports and foreign direct investment. Accordingly, there are still many provisions in the agreement with the EU which would catalyze a widening and deepening of trade and associated reforms. In addition, the treaty with the EU offers an opportunity for the Syrian government to credibly "lock-in" the measures of trade reform enacted in recent years by a legally binding agreement.

This is not to say, however, that the agreement will not be harmful for at least parts of the Syrian economy particularly in the short to medium term. Given the currently still low level of global competitiveness of the Syrian economy in general, opening up to the EU will confront the Syrian economy with potentially high losses in income and employment as many local firms may not withstand European competition. In addition, because of remaining relatively high customs duties, there is a substantial risk of trade diversion robbing the Syrian government of tariff revenue losses without delivering efficiency effects or benefiting Syrian consumers. The reciprocal liberalization of services and opening of public procurement will certainly benefit European companies the most. Opportunities for improving market access of Syrian exports on the other hand and with them major incentives supporting the shift from import-substituting to export-oriented production will only emerge in the longer run.

Against this background, one may ask if it's worth the price for Syria to sign the new agreement. Alternatively, the Syrian government could prefer to stick to the older cooperation agreement which most probably will remain in place in case the AA will not be signed. This means, however, that Syria won't benefit from a potential expansion of EU financial and technical assistance and improvement of market access conditions in the longer term besides other expected dynamic effects of the agreement like locking-in reform, stimulating investment and increasing competition (for a detailed analysis of these effects see another work of the author: Zorob 2006b). In addition, those who want to foster and deepen trade liberalization in Syria would forgo the opportunity to make use of the AA as an instrument to overcome opposition to liberalization. As noted above and despite an acceleration of trade reforms in recent years there are still many tariff and in particular non-tariff barriers in place the elimination of which will most probably challenge a host of vested interests.

With or without the AA the Syrian economy is in an urgent need of restructuring and to access new sources for growth and development apart from oil. Despite all its loopholes and potential negative effects the Syrian-European AA might serve as an instrument to support the Syrian economy in this way. However, to promote alternative sources of growth, to make the agreement with the EU a success and to limit short-term adjustment costs the Syrian government has no other option but to implement a whole variety of complementary reforms. In addition, the EU could do its part and improve the conditions of the agreement via, for example, an extension of the transition period in opening the Syrian market beyond the 12 years fixed in the AA, a further expansion of agricultural concessions and substantially enlarged financial and technical assistance. However, a future renegotiation of the Syrian-European Association Agreement is from the author's point of view rather unlikely.

Conclusion

Regional integration and in particular an agreement with a large country or block 'in the North' like the EU may offer a developing country like Syria to catalyze and lock in trade reforms besides contributing to the promotion of exports and investment and thus adjustment of the economy in the longer run. Moreover, it can deliver an instrument to overcome political-economic constraints on liberalization. To achieve this role and effectively support the developing member's export-oriented development, it is crucial that an RIA does not only provide for the opening-up of the domestic market to competition of the partners' goods and services. In addition, it should also secure and enhance the developing country's access to the market of the developed member and provide technical and financial assistance.

In 2003/04 the Syrian foreign trade system had still to be classified as being severely restrictive. In addition, the process of reform faced formidable constraints among them most importantly domestic opposition to liberalization. Confronted with the EU's unwillingness to proceed with the AA, Syrian decision makers opted for a widening and deepening of trade reforms on a unilateral basis. Signing the AA will confront the Syrian economy with potentially high losses in income and employment, a substantial risk of trade diversion and loss of tariff revenues while improving market access for Syrian exports only in a longer-term perspective. Notwithstanding this, if the Syrian-European AA were to come into force, it would still contribute to catalyze a widening and deepening of trade and associated reforms and give Syria the opportunity to benefit from positive dynamic effects of integration such as stimulating investment, promoting transfers of technology and enhancing efficiency.

[xxii] I am indebted to Michael Dostal for valuable comments on the first draft of this paper presented at the *Conference on Economic Reform in Syria,* University of St. Andrews, as well as to the conference organizer Professor Raymond Hinnebusch for his critical review and excellent guidance.

[xxiii] It should be noted in this context however that the underlying positive nexus between trade and economic growth remains an issue of debate (for this discussion see, for instance, World Bank 2005).

[xxiv] Measures aimed at liberalising foreign trade encompass the conversion and/or elimination of non-tariff barriers to customs duties, simplification of

and/or reduction of tariffs and the unification of exchange rates. However, openness to trade is by itself not sufficient for growth. Therefore, trade liberalization should be combined with a strategy of export promotion or diversification, enhancing the range of goods exported in addition to increasing the share of higher value-added industrial goods in a country's exports. Typical export promotion measures comprise of elimination or reduction of export taxes, the removal of licences, establishment of free-trade zones, the provision of export subsidies and the duty-free sourcing of inputs by introducing schemes of duty-drawback (see, for instance, Abdallah 1997, Bender 1995).

[xxv] Dynamic or long-term effects of integration are generally regarded as being of much higher importance than purely static effects of free trade and in particular for developing countries participating in a North-South RIA. Important *dynamic* include *scale* and *competition* effects. Market enlargement as a result of removing trade barriers between the members of a FTA or CU *enhances competition* on the members' domestic markets breaking up monopolistic market structures and forcing firms to improve efficiency. In addition, a larger regional market offers opportunities for exploiting *economies of scale, scope* as well as dynamic economies or learning effects. A further advantage of market enlargement is seen in its potential effect on *stimulating investment* and, in particular, foreign direct investment (FDI) with its expected positive impact on capital accumulation and transfer of technology. *Technological* or *knowledge spillovers* spurred by increased investment and trade on the basis of regional integration in turn may deliver a mechanism to improve prospects of long-term growth. The effect of *securing and enhancing market access* and the effect of *locking-in reform* are often referred to as the main 'non-traditional' effects of regional integration. Both are characterized by their specific relevance for North-South agreements. Additional 'political effects' comprise of the expected impact *of regional integration on consolidation of peace and security, strengthening of political influence* and *enhancing bargaining power*. RIAs can also serve as a platform for *regional project cooperation* as well as *technical and financial cooperation* (for a more detailed discussion see, for instance, Baldwin / Venables 1995; Fernandez / Portes 1998; Kennes 2000; Schiff / Winters 2003).

[xxvi] Rules of origin are designed to identify the 'economic nationality' of a good. Although rules of origin are indispensable for the implementation of free trade between two or more countries on a regional level, they are increasingly regarded as NTBs with far-reaching impact on market access. In the Syrian-European AA the rules of origin form part of a separate protocol. This protocol defines for each product at six-digit HS level one or several different conditions which have to be fulfilled for a 'substantial transformation' based on which the product is granted 'origin status'. Accordingly, the rules of origin in the AA are regarded by many as being restrictive. To mitigate the restrictiveness of the rules of origin in the agreements between the EU and the MPCs, the *Paneuromediterranean System of Cumulation of Origin* was introduced in 2005. Based on this producers in the MPCs are allowed to cumulate inputs originating in other member countries of the *System* as 'local content'. Cumulation however is limited to 'partial' (as opposed to 'full') cumulation. Members of the

Paneuromediterranean System of Cumulation are currently the EU member states, MPCs, EFTA countries and EU accession candidates.

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