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# TARGETING INFLATION AND ITS APPLICABILITY TO SYRIAN ECONOMY

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**Abstract**

*Inflation targeting consider as an instrument of financial policy instrument, that target to handling Inflation through announcement accurate, explicit, and determined target for attainment low price level stability.*

*Therefore, Inflation targeting method requirements are:*

- ✓ *Independence of the Central Bank.*
- ✓ *Having a Sole Target.*
- ✓ *Effectiveness of Monetary Policy.*

*Inflation targeting method depend basically on Independence of the Central Bank, because this independency is guarantee for government. There are deferent degrees for independency, start from monetary policy instruments to their targets.*

*Many development countries concentrate their monetary policies on Inflation targeting method as instrument to handling Inflation through announcement accurate, explicit, and determined inflation target to decline prices and they succeed, but the basic channel for this success is the dominance on savers and investors expectations, were they trust to Central Bank policy. If the Central Bank can convincing public with its credibility and his commitment to handling inflation it can inquiry it easily.*

*In this research, we are studding the definition of Inflation targeting, and its requirements, and conditions, and The Situation of Monetary Policy in Syria through:*

- ✓ *Absence of Independence Monetary Institutions and Policy*
- ✓ *Freeze of Basic Monetary System Rules*
- ✓ *Fixed of Interest Rates.*
- ✓ *Absence and Ineffective Monetary Policy Instruments.*

***Keywords:*** *Inflation targeting, Monetary policy, Financial policy, Central Bank, Independency.*

***JEL Codes:*** *B41, B55*

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## 1. INTRODUCTION

In order to achieve economic stability and fight inflation, the central bank should be entrusted with the responsibility of controlling the economic growth rates, and in proportion to the real growth rates of production, i.e. maintaining a low inflation rate. targeting inflation is an instrument of monetary policy aimed at combating inflation by proclaiming a clear and precise public objective to achieve a stable and low price level. Thus, the targeting inflation method cannot be effectively applied without the following prerequisites:

- ✓ Independence of the Central Bank.
- ✓ Set a single goal.
- ✓ Establish a stable and predictable relationship between monetary policy instruments and inflation.

In this research we have studied the method of targeting inflation by studying the concept of this method and the requirements of its application, its advantages and disadvantages, in addition to studying the reality of monetary policy in Syria.

### Research Importance

The importance of targeting inflation stems from the fact that in today's world it is one of the most important tools of monetary policy in dealing with inflation, because achieving low inflation is one of the most important objectives of monetary authorities to be achieved in the long run.

### Research Goal

The research aims to:

- ✓ Studying targeting inflation as a tool of monetary policy that is increasingly used by most developed and developing countries, especially with the beginning of the 1990s.
- ✓ Focus on the importance of the independence of the Central Bank.
- ✓ focus on the advantages of using the method of targeting inflation in monetary policy.
- ✓ the possibility of using the method of targeting inflation to achieve economic stability.
- ✓ The role of targeting inflation in determining the predictable relationship between monetary policy instruments and inflation.

### Search Method

The research is based on the descriptive analytical method to describe targeting inflation and its applicability to the Syrian economy, through:

Definition of targeting inflation, and its advantages and disadvantages and requirements. Focus on the independence of the Central Bank and the monetary authorities in Syria.

## 2. THE CONCEPT OF TARGETING INFLATION

New Zealand is the first country and founder of the targeting inflation method, and officially applied in 1990, followed by Canada in 1991, the United Kingdom in 1992, Australia and Sweden in 1993, Finland and Spain adopted this method (before accession to the European Union), and then adopted many Developing countries this method. The European Central Bank (ECB) has set a clear targeting inflation as well as price stability as a central objective.

Targeting inflation consider the prices stability is the goal, and setting of a specific and public target for inflation and the timeframe for achieving this, and then eliminating and addressing any deviations from this target.

Inflation is sometimes determining as a target (as a specific point), and sometimes determine as a numeric domain, i.e. for example, it determine the rate of inflation between (2% -3%) as an inflation target. But most often the purpose of inflation is to measure consumer price inflation.

The target point or the average of the target is generally set at about 2%, and the target range is often determined between (2-3%) (Donald T. Brash, 2002: 95). The determine of the inflation target varies according to the economic system of each country. In New Zealand, the first country to implement this method, the targeting inflation has been set by the Minister of Finance, and the Governor of the Central Bank is within the range (0–3%) (Donald T. Brash, 2002: 96). In Canada, the goal was set by an agreement between the central bank and the bank's financial authorities (Donald T. Brash, 2002: 96), this agreement set price stability as the basis for monetary policy, as well as many other countries that followed this approach, and achieved successes during the short period of its life, which gave the central bank more flexibility in dealing with Monetary policy (e.g. Turkey).

### 2.1. Definition of Targeting Inflation

There are many definitions of this method, some of which we can cite in this context. Mishkin and Savastano are known, targeting inflation is a public declaration of a specific numerical target for inflation, a commitment to price stability as a fundamental political objective, or the use of this method as a comprehensive strategy, based on high levels of transparency and responsibility (Stefan Gerlach, 2002: 782).

Laurence sees inflation as a clear target for inflation, while promoting price stability and a high level of employment. Other policy elements include increased transparency and credibility (Laurence H. Meyer, 2002: 147).

Marianne Nessen sees the inflation target as targeting the central bank to stabilize the inflation rate over a given period of time by setting a digital inflation target that is sought through increased transparency, responsibility and credibility of the central bank (Marianne Nessen, 2002: 313).

Klaus Schmidt defines the targeting inflation as, setting a specific inflation target and relying on the central bank to reduce inflation by increasing the degree of credibility and transparency in its work and achieving monetary policy development in order to enhance the inflation target and achieve a low inflation rate and stable (Klaus Schmidt, 2002: 125).

Donald Brash defines inflation as, a tool of monetary policy characterized by public and official announcement of a specific quantitative target, or a specific target area of inflation for a given period of time, and the clear recognition that low inflation is the primary objective of all monetary policies in the long run. Moreover, the central bank's position is enhanced by transparency and responsibility in achieving these goals (Donald T. Brash, 2002: 99).

As for David Dodge, he believes that targeting inflation is the method that aims to set the goal of inflation, by raising the degree of confidence, credibility, transparency, understanding of monetary policy and focusing on achieving price stability (David Dodge, 2002: 113).

Peter and Douglas argues that targeting inflation is not only a way to reduce current inflation but also to monitor price stability in a post-recession economy (Peter Isard, & Douglas Laxton, 1999: 115).

In general, the policy of targeting inflation is for the Central Bank to chart the future path of inflation and establish the rate of inflation that the government deems appropriate and appropriate for the economy and direct its monetary instruments for this purpose. How successful this goal is depending on how well the central bank is able to adjust monetary policy when there is any deviation between target inflation and real inflation (Monetary Policy in the Arab Countries, 1996: 54).

The targeting inflation is an official announcement by the monetary authorities of a specific numerical target or scope of inflation for a certain period of time, by raising the degree of credibility, transparency and responsibility of the Central Bank in the performance of its work.

Key elements can be identified from previous definitions of targeting inflation:

**First,** declare a specific and clear target or scope of a specific target for a certain period of time.

**Second:** The independence of the Central Bank and its creation of an environment conducive to price stability, which is the main objective in the long run.

**Third:** The Central Bank has strong means to achieve inflation expectations, using some indicators and variables that contain information about the future of inflation.

**Fourth:** The Central Bank has a vision for the future work of the procedures in the development of instruments and use based on the assessment of inflationary pressures, and the extent of the use of inflation forecasts.

From the above, we find that the targeting inflation requires the monetary authorities to possess technical and legal capabilities to subdue inflation, and have the ability to fully influence the rate of inflation.

### 2.2. The Basic Principles of the Targeting Inflation Method:

The success of this method and the achievement of its objectives are based on three basic principles:

#### 2.2.1. Transparency

This method is characterized by the adoption of a high degree of transparency, that is, transparency in the work of the Central Bank, through the issuance of regular periodic reports explaining its policy to the public.

But what is the role of transparency in monetary policy in general, and in targeting inflation in particular? The transparency of the Central Bank's work in determining the objectives, and the means available to achieve these goals, whether related to the interest rate, exchange rate or employment, or the change of the Monetary Policy Council or the change of portfolios or any other of its basic policies for the continued success of the work of the Bank.

Therefore, transparency drives the private sector to rely on the reports issued by the Central Bank. The increased degree of transparency allows the private sector to respond to the central bank's expectations of expected inflation, and to trust the bank's policies on the employment target significantly, which gives the bank a good reputation and confidence in him, especially through the response of the private sector to inflation expectations.

In addition, the public prefers more transparency, but the bank prefers less transparency in its work, in order to pursue its business and objectives and achieve them at the lowest cost while maintaining its reputation and status (Giorgio Valenti, 2004: 530).

According to Fauost & Svensson, the transparency of the central bank's work allows the public to understand monetary policy, increase the degree of confidence in the central bank to pursue and announce the objectives of monetary policy, and thus improve the credibility of its objectives taking into account the following three elements, which increase the effectiveness of monetary policy (Lars E.O.Svensson, 1999: 631):

- ✓ Declaring the objectives of monetary policy to the public.
- ✓ The independence of the Central Bank in the selection of the necessary tools to follow up the achievement of these objectives.
- ✓ The responsibility of the Central Bank to the public in achieving these monetary policy objectives.

Under the targeting inflation policy, the central bank's reports on inflation expectations, including information, assumptions, instruments and provisions for their construction, allow the public to monitor, scrutinize and examine the conditions for achieving the inflation target. Under the targeting inflation, the central bank issues periodic inflation reports or monetary policy reports.

There are three banks that adopt this approach, namely, the US Federal Reserve, the Bank of England, and the Swedish Central Bank (Lars E.O.Svensson, 1999: 631). These banks issue periodic reports and charts on the expectations of the conditions of achieving the inflation target, in order to enable observers from outside the bank to monitor and audit the tools and means to achieve the target. Where the Bank of England issues reports on the bank's monetary policy board meetings, including election reports.

These reports provide exceptional opportunities for the public to monitor the quality and appreciation of the information and discussions presented during Monetary Policy Council (MPC) meetings and discussions (Giorgio Valenti, 2004:532). In general, a high degree of transparency allows the public to monitor monetary policy performance and enable it to achieve its objectives in an optimal manner, through the support it receives from the public.

### 2.2.2. Accountability

The targeting inflation method raises the level of responsibility for monetary policy-makers by increasing the above-mentioned degree of transparency. It is quite clear that any failure to achieve the inflation target, and as a result of any error by the Central Bank, or any breach or error in forecasting or decision-making, the Central Bank alone bears the consequences.

### 2.2.3. Credibility

One of the most important elements in the application of the targeting inflation method and its achievement for its purposes is to build credibility and strengthen it through decisions and laws adopted, and credibility directly affects inflation expectations. The credibility of monetary policy positively affects the objective of inflation and, consequently, inflation expectations. The higher the credibility, the more likely the inflation expectations are to be achieved, and thus the actual inflation. Thus, the role of inflation targets is measured and valued by the credibility of the system.

### 2.3. Advantages and Disadvantages of the Targeting Inflation

The targeting inflation method has been applied by many developed and developing countries in recent years, because this method includes many advantages, especially in its contribution to achieving price stability, and achieve a balanced and stable relationship between monetary policy instruments and inflation target. This is in addition to some disadvantages.

### 2.3.1. Advantages of the Target Inflation Method

- ✓ This approach enables monetary authorities to achieve and maintain a low and balanced inflation rate, which in turn leads to significant benefits for economic growth, and the central bank's clear mandate and independence to use its instruments drives it to correct and achieve a low inflation rate. The imbalance and wage imbalance between wages and prices is always present, and thus increasing the degree of transparency, responsibility, independence and focus of the central bank on a clear inflation target may be used as an optimal means of balancing wages and prices.

- ✓ Target inflation enables the central bank to strengthen its credibility at work by providing clear and periodic price reports, which in turn help to confirm the central bank's commitment to reducing inflation in the public eye by announcing a specific quantitative target or target area.

- ✓ The commitment of the Central Bank to achieve the goal of inflation creates the conditions and conditions (i.e. the environment) to achieve its credibility to the inflation expectations predicted by the Central Bank, which increases the interaction and participation of market forces with the bank and confidence in the bank and hence these expectations.

- ✓ The application of the targeted inflation method positively contributes to optimal periodic adjustments in the economy, as it leaves room for maneuver and work, and monetary policy, thus enabling the Central Bank to gain flexibility in dealing with aggregate demand and supply shocks.

- ✓ The target inflation method is specific and unique because it does not need to be replicated directly after the final target is set. On the other hand, monetary policy needs frequent and periodic adjustments, especially in achieving a balanced relationship between monetary growth and price stability (C.H.Lim, 1998: 98).

According to the above advantages, the targeting inflation method has become more credible compared to other methods, because it makes monetary policy more transparent and defined responsibility, and contribute to providing and improving a stable investment environment, in addition to achieving a safe, stable and encouraging environment for investors (Chares Nolan, 2001: 357).

**2.3.2. Disadvantages of the Inflation Target**

- ✓ There is no real guarantee that the Central Bank will succeed in using its discretion and independence to formulate and determine an appropriate monetary policy, as opposed to the monetary target and target exchange rate. That is, it is not easy to apply the inflation target.

- ✓ The nature of the outlook for the targeting inflation method requires taking into account the possibilities of contradiction between changes in monetary policy and its effects on inflation. In addition, the nature of the outlook for the targeted inflation method introduces uncertainty in the political decision-making processes, as it allows the central bank more freedom regarding exchange rate policies or targeted monetary expansion. This freedom may allow political decision-makers to take excessive expansionist policies.

- ✓ Despite the solid and strong structure of the targeting inflation method and its provision for the best periodical regulation of the economy, this advantage may lead to non-inflation. Because developing countries, in particular, face this problem when inflation falls from high to low levels. In this case, the prospects for achieving inflation forecasts are low, in addition to instability in output (Jonsson, 1999: 166).

- ✓ Compared to the exchange rate or monetary policy, it is very difficult to monitor inflation, and monetary policy instruments show deficiencies in their ability to achieve the determined inflation target. Initial inflation reductions resulting from the use of targeted inflation may result in higher output costs in the short term if private sector confidence is not earned, confidence in the application of this method is restored, and the credibility of the central bank's work.

- ✓ Targeting inflation requires considerable exchange rate flexibility, which in turn may lead to financial imbalance (financial instability) (Fernando Alexander, 2002: 548).

**2.4. Requirements of the Target Inflation Method.**

There are three basic requirements for applying the targeting inflation (Lars E.O.Svensson, 1999: 633):

- ✓ The independence of the monetary authority (Central Bank).
- ✓ Unity of the target, i.e. the absence of other basic objectives (such as wages, employment level, exchange rate, etc.), which may contradict the goal of reducing inflation.
- ✓ Achieve a balanced, stable, and predictable relationship between monetary policy instruments and inflation.

**2.4.1. Independence of the Central Bank**

The basic requirement for applying the targeting inflation is to give the central bank autonomy to use, adapt, and adjust monetary policy instruments freely to achieve the inflation target. i.e. the independence in the use of its instruments freely, in a way that allows him more diligence and freedom of initiative in dealing with monetary policy.

There should be no political pressure on the central bank to increase the rate of economic growth, especially if it is disproportionate to the achievement of the inflation target, especially if it is in conditions that are not conducive to achieving the inflation target (Monetary Policy in the Arab Countries, 1996: 75). The weight of public sector borrowing in public finance must be low, and borrowing must be direct from the central bank (G. Debelle, 1997: 33).

The independence of the central bank depends not only on the legal aspect, but also on many other regulatory factors, such as formal arrangements between banks and the government, the capacity of the research center of the bank, the personality of key individuals in the bank and the stability of the government. However, because of the difficulty of identifying such features objectively, previous studies have developed indicators of the independence of the central bank, often based on legal independence. The adoption of indicators only on the legal side involved two problems:

**First:** laws are incomplete, because they cannot clearly define the limits of authority between the central bank and political authorities under emergency situations. These resulting gaps can be filled by the bank's tradition at best, and by a policy of tough power at worst.

**Second:** even when the law is quite clear, practice may deviate from it.

Legal independence, of course, is the basis for effective independence, but it is also important for other reasons:

- ✓ It refers to the degree of autonomy that legislators are intended to give to the Central Bank.
- ✓ In practice, all current attempts depend on distinguishing the independence of the Central Bank and focusing on the legal qualities of independence.
- ✓ The independence of the Central Bank does not mean full independence, but independence and freedom in the use of monetary policy tools, which allows to give him more freedom in the implementation of his options in dealing with monetary policy and fundamentally not to apply the Central Bank's funding to the state budget.

- ✓ The central banks in the industrialized countries aim to stabilize economic activity at the highest possible level of employment where there is no unemployment or inflation (Ziad Salim Ramadan, 1996: 177).

In the area of the relationship between the level of inflation and the independence of the central bank, there is a hypothesis that central banks focus more on achieving price stability, because monetary policy is usually the result of a compromise between the central bank and the executive authorities, and that a more independent central bank will have an effective impact on policy Cash, and thus reduce inflation (Helge Berger, 2004: 588).

The legal independence variable gives the Central Bank the right and the clear mandate to pursue price stability at the expense of other objectives. It is well established that high inflation weakens the independence of the central bank and therefore the independence of the central bank and the stability of prices reinforce each other.

Thus, measures of independence include indicators of institutional independence, such as appointment procedures, as well as measures of the relative importance of achieving price stability for the Central Bank in legal and practical terms. Studies show that the difference between de jure and de facto independence in developing countries is vast compared to developed industrial countries. Because the central banks in most developing countries are not discriminated against independently, and the political authorities in these countries are controlled by the central bank, monetary and fiscal policy. Thus, an important step in the independence of the Central Bank is to create and establish respect for the Government's administration and law of the Central Bank (Bilin Neyapti, 2004: 23).

**2.4.2. Unifying Target**

The second requirement for adopting the inflation target is the absence of other changing targets, such as wages, employment level, exchange rate, etc.

Because these monetary policy objectives may conflict with the aim of targeting inflation (price stability). In other words, there should be a single objective to be pursued is the specific inflation target, in which the target inflation method is applied.

For example, when a country chooses a fixed exchange rate regime, it will not be able to achieve the inflation target and the exchange rate target at the same time, because, in particular, with free movement of capital, the exchange rate target follows monetary policy, which leads to deviation from Targeting inflation rate.

On the other hand, the adoption or targeting of more than one target may lead to weak credibility of the application of the target inflation method, in addition to that there may be a contradiction between the objectives set.

In any case, other economic goals can be achieved as long as they fit in with the inflation target. For example, under a flexible exchange rate regime, the nominal exchange rate target may correspond and coexist with the defined inflation target, but this consensus may produce an uncertain and undesirable outcome, since it is impossible for policy to correctly and clearly explain priorities to the public before it has credibility before those contradictions occurred.

Under these circumstances, the public makes their own opinions about the work of the policy, convinced that the policy does not give clear estimates of its work, and therefore does not produce correct results, therefore, the safest and surest way to avoid these problems, is not to focus on more than one variable, but Just focus on the targeting inflation aim as the main target (M.A.Savastano, and S.Sharma, 1997: 130).

### 2.4.3. Effectiveness of Monetary Policy

The third requirement for the application of the targeting inflation method is a stable and balanced relationship between the results of inflation and monetary policy instruments, where Jonson believes that to apply the targeting inflation method, the monetary authorities must be able to synthesize and adapt the mechanisms and predictions of the rate of inflation in the economy to be reasonable, monetary authorities must have a way to make monetary policy instruments effective in influencing macroeconomic variables (G.Jonsson, 1999: 124).

In addition, there must be sufficient development in cash and capital markets to interact between the use of these instruments, because by relying entirely on monetary policy instruments to achieve the inflation target, this may lead to weak bank positions, or may lead to the inability of the bank to achieve the inflation target. In addition, there may be some deviations from the inflation target resulting from monetary policy or Inflationary pressures that appears as a result of a defect or crisis in the banking sector (G.Debelle, 1999: 35).

### 2.5. Conditions to be Met to Apply the Method of Targeting Inflation:

Adopting the targeting inflation requires several basic conditions (Helge Berger, 2004: 591):

- ✓ **The degree of independence of the monetary authority:** There is no monetary authority that enjoys complete absolute independence from the government influences from the axioms, but the monetary authority should be free to choose the tools by which it can control the rate of inflation.

- ✓ **The monetary authority shall be liberated from the control of the financial authority:** In other words, government borrowing from the Central Bank shall be low or zero. The existence of fiscal control weakens the effectiveness of monetary policy, where the central bank is required to provide the government with the financial resources it needs at low interest rates. Dependence on the Currency minting fee is the most common indicator of financial control over central banks. The annual income of developing countries from Currency minting fee ranges between (1.4-3%) of the GDP, according to each country, while the annual revenues of developed countries from Currency minting fee in the past 10 years averages less than 1% of GDP (Arab Monetary Fund, 1970-2000: 269).

- ✓ **Development and expansion of financial markets:** to be able to absorb domestic savings and public debt securities.

- ✓ **Revenue Availability:** There is sufficient revenue for the government to rely on its own resources for funding.

- ✓ **readiness, desire and capacity:** enjoyed by the monetary authorities to focus on one goal, which is the stability of prices and give it priority on other objectives of monetary policy, such as wages and the level of employment and the exchange rate ...... etc.

## 3. THE REALITY OF MONETARY POLICY IN SYRIA

Since the 1990s, monetary policy in Syria has certain characteristics, the most important of which are:

1. **Inflation of money in circulation and absence of monetary policy and independent monetary institutions**

The cash in circulation and demand deposits increased significantly, and the main reasons for this enormous increase were the increasing indebtedness of the state to cover deficits of the public budget and deficits of subsidies that do not appear in the budget allocations and the deficits of specialized companies to buy the main agricultural crops and to finance these recent deficits. The banking system is then the government cover by issuing bonds to be placed in cash coverage, and supply deficits are specifically added to the government frozen debt (Irfan Al-Azma, 2000: 4).

On the other hand, monetary policies in Syria over the past years have been ineffective in influencing both the growth of the cash in circulation and the size and type of lending.

The low cost of borrowing from the state from the banks has contributed to its continuation in its expansionary financial policies. The state owes the central bank only a 1% interest (including the bank’s commission), for treasury bonds (of a period of 15 years) that are placed in coverage, and without interest for overdraft (Hisham Metwally, 1994: 19). This constitutes direct financial support provided by the central bank of the state, which prevents it from thinking seriously about financing its deficit through real savings in the economy (Hisham Metwally, 1994: 19).

The absence of monetary policy has contributed to the fragmentation of monetary management matters among the institutions established by the basic monetary system and the new bodies established after the establishment of central planning.

**2. Freezing the provisions of the basic cash system:**

The application of the basic monetary system continued until the issuance of Legislative Decree No. 147 of 1967, which authorized the Economic Committee of the Council of Ministers to study the policy of prices, credit, and savings, and interest rates, and submit the necessary recommendations about it to the Cabinet. The decree was considered a type of suspended solution, which maintains the provisions of the basic monetary system in place but is not fully implemented (Irfan Al-Azma, 2000: 9).

Economic Committee became the place of the Monetary and Credit Council, which has exercised its powers and submitted its proposals to the Economic Committee, through the Ministry of Economy. The role of the Monetary and Credit Board began to gradually diminish until its work ceased since 1984. The Economic Committee became the monetary authority on the surface, but without the functions of this authority (Irfan Al-Azma, 2000: 5).

In the absence of the role of the Monetary and Credit Council, the role of the central bank has not exceeded the work of the treasurer of the state and the last lender of the banking system, and the result has been an absence and lack of clarity in determine the objectives and tools of monetary policy, and a severe deficiency in the work of these tools, at a time when the Economic Committee could not The permanent role is to play the full role of monetary authority.

Therefore, it can be said that the independence of the monetary authority has been greatly eroded and monetary policy has been practiced practically by the monetary authority represented by the Economic Committee and the Minister of Economy and Foreign Trade, and the role of the central bank was limited to suggestion and implementation. In addition, the Governor of the Central Bank of Syria, by virtue of Legislative Decree / 87 / of 1953, was appointed by decree for a period of five years, renewable repeatedly, and his service may not be terminated except in violation of the law or the bank’s regulations or a grave sin in the bank’s administration. As for the subsequent laws issued after the socialist transfer, his appointment was not limited to the duration and his removal is linked to the desire of the Council of Ministers, as is the case with other general managers of public institutions.

The bottom line is: Central banks are public institutions and their independence is not absolute independence but rather relative to ensure the freedom necessary to take what it deems appropriate from objective measures to achieve the goals entrusted to them by law. Economists across the world have unanimously agreed that the independence of central banks gives monetary policy greater credibility and effectiveness.

**3. Fixed Interest Rates:**

A tracker of interest rate developments notes that these rates have only changed three times over the past three decades. This is due to the adoption by Syria of the policy of central planning since 1963 (Muhammad Ayman Ezzat Al-Midani, 1995: 20), which made the effect of the policy of adjusting interest rates on the volume of investments, or on inflationary or deflationary conditions, diminishing or significantly reducing their impact.

**4. The absence and ineffectiveness of monetary policy tools:**

Ineffective monetary policy tools include:

**4.1. Inefficiency of the interest rate:** The Monetary and Credit Council has set interest rates for re-discounting and loans after the Central Bank has started its work there has been no noticeable change in these rates since 1967.

Thus, these rates reflect the levels of the period in which they appeared and continued, and interest rates ranged between 2-5.75%, depending on the nature of the process and the production sector and the bank requesting the process, and special reductions are granted for priority operations, and it is noted that all these rates except for a few years, are less From the rate of inflation, that is, it has a negative real value, and does not reflect the actual cost of credit, it represents an implicit support to banks, which partly explains the increased dependence on financing from the central bank, as one of the main sources of specialized bank resources. The policy of maintaining benefits and keeping them low for long periods has had several negative effects, the most important of which are:

- ✓ Turning interest into interest of negative value, as a result of increasing inflation rates at huge rates over the interest rates set by the Central Bank.
- ✓ Encouraging borrowing from banks, especially by the government and economic public sector bodies that have found this borrowing a way to solve their financial problems in an easy way, **instead of their efforts to rationalize expenditures, control expenditures, and pay attention to increasing productivity.**
- ✓ Encouraging banks to borrow from the central bank to finance their operations instead of working to increase deposits (due to the low discount rate in the central bank and its inconsistency with the credit interests of other banks).
- ✓ The low percentage of savings deposits in the money supply.
- ✓ The inability of interest to play a role in reducing consumption (by absorbing excess cash and transferring it to savings and then to investment).
- ✓ Facilitating escape from the local currency to foreign currencies, as a result of the significant decrease in the value of the Syrian pound and the dollar from one dollar is equal to 46 Syrian pounds in 2010 to more than one dollar is equal to 900 Syrian pounds in 2019.
- ✓ Facilitating the tendency to invest in in-kind assets such as real estate and durable consumer goods.

**4.2. Absence of open market operations:** The basic monetary system allowed the monetary authority to undertake the creation and development of the monetary and financial market, and made it one of the first tasks and goals for the Monetary and Credit Council, but once the council began taking executive measures to establish this market, the process stopped in its infancy this is due to the government adopting the central planning method in the administration of advance and credit. The work of the Central Bank was limited to financing the general budget, overdraft, and issuing long-term, non-negotiable public bonds, and no attempt was made to place these bonds on public subscription.

**4.3. The stability of the ratios of the statutory cash reserve:** The Monetary and Credit Council has determined the rates of the legal cash reserve for each bank and its assets from current or short term deposits less than one month, at 15%. Then determine the distribution of ratios among the various bodies as follows (Muhammad Salih Jum`a, 2000: 125):

%5.0 cash in the bank.

%2.5 reserve deposits with the Central Bank of Syria.

%7.5 employed in public debt Bonds.

The Board also specified 15% of commercial bank deposits for a term ranging from 1 to 12 months, as ready-made funds in the bank's fund. These ratios have remained stable for a long time. This means that the statutory cash reserve policy cannot be used to address the existing economic and monetary conditions, i.e. the reserve ratio is always disabled.

**5. The dependence of the Central Bank of Syria on the government and reducing its role:**

The government's adherence to the policy of central planning and economic intervention, and the limited work of the State Planning Authority to collect annual plans for banks in terms of the size of deposits, loans, etc., made the monetary authority represented by the Monetary and Credit Council completely absent, and dealing with the central bank like other public sector institutions has become tasks Government treasurer, generating public revenues, spending public expenditures, and covering the public budget deficit, which mainly determines the amount of the money supply, which is a major reason for expansionary monetary policy, which causes inflation and high prices, which reflects indebtedness The government from the central bank.

Thus the dependency of the central bank on the government appears, which is at the same time one of the most important factors causing high inflation rates in Syria, which reduced the importance of the central bank's role in managing money and credit and making its role marginal and ineffective in light of the existing economic conditions.

**6. Low level of banking performance:**

**6.1. Governmental banks:** Governmental banks in Syria suffer from a number of administrative, technical, legal, and other difficulties that together lead to a decrease in the level of banking performance, the most important of which are:

- ✓ The Central Bank and specialized banks are subject to the decisions of the Economic Committee, which is a government committee that plans to meet the government's desires and financial position, while the Central Bank, through its oversight of monetary policy, sees otherwise.
- ✓ The multiplicity of banking supervision and control bodies such as the Economic Committee, the Higher Planning Council, the Supreme Agricultural Council, and the Higher Tourist Council, among others, which leads to multiple implementation procedures.
- ✓ Contradiction between laws, such as Law 24, which prohibits possession and trade in Foreign currency, and Investment Law No. 10, which permits foreign investment and the possession of hard currencies.

- ✓ Workers in banks are subject to the unified law of workers in the government, whereas workers in banks are not considered workers, and a special law should be allocated to them, because they are called in economic literature (moneymen and banks).

- ✓ The banking development and modernization plan is linked to the state's economic plan, while banks must be given independence when developing their business mechanism, equipment, and technologies used to keep pace with new conditions and changes.

In front of this reality and in addition to the multiplicity of control bodies, the central bank and other banks are no longer able to perform any kind of banking supervision, or to supervise the banking system, which is owned by the state and works with its guarantee, which negatively affected the safety of banking conditions, and greatly increased the debt problem Troubled.

It has increased the decline and low level of banking performance, the limited tasks assigned to the banking system by the government, excessive bureaucracy, the absence of incentive among workers, as well as the weak level of their performance, and the determination of interest rates on deposits, loans and commission rates on banking services with administrative decisions that lack flexibility and far From the reality, all of this was reflected in the declining levels of performance in the banking system, and this was reflected in an increasing failure to attract national savings, and a greater failure in providing various banking services to its applicants.

**6.2. Private Banks:** The case of private banks is no less difficult than that of government banks, especially their suffering from the procedures and teachings of the Central Bank and government decisions, which contribute greatly to restricting their work in the field of credit, including the complexity of credit granting procedures, and reducing the duration of bad loan reserves, has resulted This is until most private banks have stopped receiving deposits from clients, due to the lack of investment imposition and the lending of deposited funds.

## 4. RESULTS

Through the study, we reached a set of some results:

**1. The absence of monetary policy in Syria and the ambiguity of its features:** There is no relative independence of the monetary authorities in Syria that enables them to use monetary policy tools effectively, just as the central bank limited its role to providing loans to the state and specialized banks, issuing currency, and participating in Syria's foreign currency reserves, In addition, banks can:

- ✓ That the central bank bypasses it to the Ministry of Economy and Finance in order to obtain loans and advances.

- ✓ Re-discounting its bonds with the Central Bank, bypassing the specified credit limits.

**2. The banking system in Syria**

The current banking system was established in Syria to serve the central planning economy that Syria moved to in the early 1960s. This system was characterized mainly by state ownership of banks and by banking specialization on a sectoral basis, and was characterized by the scaling of the role of both the central bank and monetary policy in line with the central planning system. Financing for the public sector and short-term financing for the trade sector dominated the financing structure, as we noted.

In recent years, in conjunction with the steps for economic reform, the government has taken steps towards banking reform, some of which are "reform" and others are "open". But these steps were slow and dispersed, and were not part of a comprehensive program to reform the Syrian economy or a prior program to reform the banking sector.

The steps of the "reform" banking centered in the field of automation, training and qualification, raising the ceilings of lending and expanding the areas of lending, while the steps of "openness" were to allow the establishment of private banks and the revival of the Monetary and Credit Council, in preparation for the activation of both monetary policy and banking supervision, and the reducing of restrictions on dealing in foreign currencies, In addition to the steps that led to the establishment of a stock market.

But these procedures were not enough and the banking system in Syria is still unable to play the role of financial intermediation effectively and is still far from the developed banking systems in the region. One cannot help but notice that Syria is still in dialogue with itself between "reform" and "openness" in relation to its banking sector, while other Arab countries have overlooked this dialogue for years, and Arab banks have diversified in their products and services, and established investment and business banks, It has moved towards comprehensive financial services, including investment banking, finance, and e-commerce, and towards the provision of financial and banking services based on developed technology such as credit cards, phone banking (WAP), computer banking, and ATM service.

**3. Banking supervision**

The Central Bank of Syria is currently work through the government's commission with the banks (which regains its position now after it had distributed its position during the past years between each of the ministries of economy and finance, the Central Agency for Financial Supervision and the Central Authority for Supervision and Inspection), to set performance standards and criteria of solvency and liquidity for banks, Public and private, according to the new Basic Monetary Law, and enhance the expertise of bank observers. But the central bank must prepare as well and from now adopt the financial stability criteria set by Basel II in relation to the liquidity and solvency of banks, and in terms of classifying bank assets according to their quality, and it must also educate public and private banks to prepare for the application of these standards.

It is worth noting that the process of banking supervision becomes more difficult whenever the liberalization policies are liberalized and banks are allowed to borrow from abroad, and they are allowed to provide some of their foreign exchange loans and to introduce banking products in foreign currencies and other procedures of globalizing the banking system. It remains necessary for the banking supervision process to be strict and independent and not subject to interference by the authority.

**5. The rigidity of fiscal policy in Syria and its inflexibility:**

This is due to its lack of speed and flexibility to change the rates of taxes and fees, and to reduce or increase public spending and change its structure, mainly due to the following reasons:

- ✓ Weak financial expertise in Syria, lack of rehabilitation and increased efficiency.
- ✓ The lack of integration and coordination between the Ministry of Finance and other ministries. The low level of tax deductions shows that it depends on loans or cash issuance as a continuous way to finance the deficit in the state's general budget without searching for new financial means.
- ✓ The large tax exemptions that were given to companies and projects under the Investment Law No. 10 of 1991 and Decree No. 10 of 1986 for agricultural companies.

- ✓ Tax evasion for most merchants and industrialists and not declaring the actual profits they earn.

## 5. RECOMMENDATIONS AND PROPOSALS

To apply the targeting inflation method in Syria, an independent monetary authority is necessary and a targeted monetary policy is established, directing credit towards priority sectors on the one hand, and controlling aggregate demand and inflation in the economy on the other hand, this requires the following:

- ✓ Unifying the bases and principles of monetary policy and subjecting them to a unified authority as stipulated in Decree 87 of 1953 (the Basic Monetary Law), and this requires the revival of the Monetary and Credit Board or the formation of a new monetary authority that supervises, monitors and directs monetary and banking procedures.

- ✓ The central bank is considered the supreme monetary authority that determines based on the studies and research carried out by it, the volume of cash, the interest rate, and the national credit plan, in addition to that, banking activities must be controlled from deposit and credit based on the need of the national economy and not the banks 'need and its profits, because Granting independence to the Central Bank of Syria is necessary:

  - ➢ Because monetary authority implementing the decisions of the Monetary and Credit Council in order to keep abreast of developments in the current economic conditions to take its real role by stabilizing the national currency and ensuring the freedom to transfer it to other currencies, and to be able to prepare and draw a monetary and credit policy compatible with the needs of development and economic growth. And the use of monetary policy tools to achieve the rate of stable growth in the monetary base through monitoring the real growth rate during the year and adjusting the growth estimates for the rest of the year in a manner consistent with what may happen from developments and monitoring the rate of inflation during the year and thus adjusting the rate of stable growth in the monetary base and adjusting it continuously under the Changes in the possibilities for real growth and inflation.

  - ➢ Because granting independence means that he has technical and legal capabilities that enable him to subdue inflation, and possess the ability to influence and fully control inflation.

  - ➢ Granting independence means that he has great flexibility in applying monetary policy.

- ✓ Developing the mechanism of the banking system, and this requires canceling the banking specialization that may lead to the freezing of funds in one bank and its shortage in another bank, in addition to granting benefits and rewards to workers with the aim of making good use of the funds and not disrupting them.

- ✓ Adopting a monetary policy that links real GDP growth and the rate of money supply growth through restrictions and controls on local credit to various sectors.

- ✓ Attention to the policy of legal reserve, and give it more importance, because it is considered the most economic means affecting the money supply and control the volume of credit at a time when the open market process is absent.

- ✓ To start liberalizing the interest rate based on the state of the economy and the current state of inflation, with the aim of reaching the real cost of capital rather than the administrative cost that may lead to undesirable effects in the economy.

- ✓ Applying an effective discount rate policy and not allowing the credit limits set for banks to be exceeded and the need to adjust discount rates to reflect the true cost of credit.

- ✓ Liberalization of exchange rates and disposal of administrative prices that previously led to the creation of structural distortions in the branches of the national economy. The export dollar has contributed to raising the national cost of the industry and reducing its ability to compete in the international market. However, it is used to encourage exports. How do we encourage exports from an angle and raise the cost through this encouragement on the other hand?

- ✓ Increasing government support and interest in the financial market, which occupies an important and vital position in modern economic systems, so that it collects national savings and directs them towards investments that serve the national economy, and works to encourage and attract Arab and foreign investments to finance investments in Syria. The financial market can absorb the excess liquidity from the hands of the public and transfer it to the productive areas, thus reducing the volume of inflationary pressures resulting from the high spending rates. And you can avoid financing the budget deficit by issuing cash through excess liquidity in excess at the hands of individuals, institutions and companies, and thus the result is lower inflation rates and encourage and develop savings and increase them.

- ✓ Providing a wide information base for macro and micro economic performance.

- ✓ Developing banking competencies capable of evaluating projects and managing banking risks.

- ✓ Establishing effective banking supervision and restricting the role of supervision to banks to the Monetary and Credit Council, and exercising this role through the government commission at banks, as stipulated in the Basic Monetary Law.

- ✓ Establishing developed research center in the central bank to conduct monetary, financial and economic studies and research that are an important material for decision-making in the field of cash and money, and to move away from personal estimates when making monetary decisions, because most central banks in the world prepare macroeconomic reports on the state of the economy, and adopt It is based on his decisions and uses them during negotiations with foreign banks.

The current circumstances require the establishment of a monetary authority with sufficient independence and able to make decisions regarding the efficient allocation of resources, control of credit, the regulation of the banking system, and the development of the financial market in accordance with the prevailing economic situations and conditions in Syria in order to be able to control monetary policy and increase its efficiency and thus Adopting the target inflation method.

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