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Economic Update

Slow and steady

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In March, the long-anticipated Damascus Stock Exchange (DSE) was launched and now, some six months into trading, the DSE has 11 companies listed, with three more currently undertaking initial public offerings.

While the volume of trading has been relatively slow to start out, the very launching of an exchange is a crucial step for the country, as Syria looks to transition from a centrally planned economic model to a "social-market" economy. Rateb Shallah, chairman of the DSE, told OBG that, "Syria was without an exchange for a very long time due to the socialist mindset, which viewed stock markets as a western invention favouring big business, making a select few rich at the expense of others. But, with nearly every developed country in the world boasting a capital markets exchange, the government came to realise that they can provide a valuable service."

Given the state of the global economy, which saw markets around the world plummet just before the launch of the DSE, the Syrian authorities are determined to impose regulations that restrict speculation and "hot money" from entering the market.

Mohamad Al Jleilati, CEO of the DSE, told OBG, "The global crisis has made us realise the importance of not rushing into things. We are doing our best to minimise the gap between the real and financial economy."

Among the raft of new regulations are prohibitions and restrictions on trading and prerequisites for investing. Investors are prohibited from selling and buying the same stock in the same day, for example, and share prices cannot fluctuate more than 2% in a single session. Similarly, non-Syrian nationals are only permitted to invest in the exchange if they have a local bank account.

Many have indicated that while they understand the need to be cautious given the current climate, they are concerned that over-burdensome limitations are preventing trading activity from reaching desired volumes.

Of the 11 listed companies, seven are either banks or insurance companies. According to Omar Ghraoui, the COO of Bemo Saudi Fransi Finance, one of six brokerage firms to receive a licence in Syria so far, "For the time being, the exchange will remain dominated by financial service companies, as not many others are able to meet the imposed minimum capital and disclosure requirements. We are lobbying the authorities to ease the requirements as the exchange needs more listings."

With Syria only recently opening private sector participation to many activities that were previously nationalised and dominated by state-owned companies, much of the private economy to date has been dominated by family trading groups. In order to reduce tax burdens and increase their competitive edge, many of these companies have a long history of undisclosed earnings.

It is hoped that among the many ancillary effects of the new exchange is an increased adoption of international reporting standards by those same family trading groups, particularly as they look for ways to raise capital. This will improve the economy's overall transparency and encourage corporate governance, as well as increase government tax revenues.

As further encouragement to entice Syria's major privately owned family groups to list, Al Jleilati explained to OBG that, "Companies who restructure to have more than 51% of their ownership held by multiple shareholders will be taxed at 14% compared to historical rates that sometimes reached as high as 65%. Companies will also be forced to recalculate their past incomes, with the government granting immunity on all reporting discrepancies by imposing a flat back-tax of 1%, which we see as a very fair compromise."

Despite the incentives provided, many companies are still reluctant to report their earnings, according to Sofian Haikal, the director of brokerage firm Cham Capital. "Family companies lack trust in the authorities and many are afraid to be the first guinea pigs in reporting their taxable incomes. That said, I am optimistic of the eventual transition from family to public business, as it only needs a few successful examples to gain collective popularity," he told OBG.

Investors also face difficulties in measuring the intangible assets earned by these companies, such as brand equity, and there is reluctance on the part of investors to sell-off shares. According to research produced by Bemo Finance, share prices have risen 57% over the past four months. As a result of this upward trend, combined with a perception that due to the 2% daily fluctuation cap most listed companies are currently undervalued, many investors are holding onto their stocks.

According to Ghraoui, "The wealthier Syrians have been investing abroad and understand how new exchanges work. But many of our clients who are new to trading are complaining that they cannot buy shares. We would like to see the price cap of 2% be raised to five or 10 in order to allow stocks to reach their full value." But according to Shallah, the low volumes are indicative of the types of investors active on the DSE. "Most investors are looking to create a sustained income over a long period of time and are not after short-term gain. The 2% cap is temporary and will be raised as the volume of listed companies goes up."

Overall, while more robust trading activity has yet to materialise and the number of listings is expected to take a few years to reach critical mass, Syria has laid the foundations for what could prove to be a valuable contributor to the nation's GDP.

According to Mohamad Al Imady, chairman of the Syrian Commission on Financial Markets & Securities, which serves as the market's regulator, "No one thought Syria could do it. Today we have 11 listed companies and by the end of 2010 we plan to have 40."