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Syria to End Dollar Peg, 2nd Arab Country in 2 Weeks (Update3)

By Zainab Fattah and Matthew Brown

June 4 (Bloomberg) -- Syria became the second Middle Eastern nation in two weeks to say it will dump its currency's peg to the dollar to curb rising import costs and inflation.

The country will link the Syrian pound to a broader range of currencies starting in the middle of July, central bank Governor Adib Mayaleh said.

"The decision is final," he said in a phone interview from Abu Dhabi. "This will help stabilize the Syrian pound and bring down inflation."

The shift away from the dollar among Middle East countries is a sign of the waning attraction of the currency for central banks around the world. The dollar made up 64.7 percent of global foreign-exchange reserves in the fourth quarter, down from 65.8 percent in the prior three months, International Monetary Fund data show. The euro's share was 25.8 percent, the highest since its 1999 debut.

Syria is broadening its peg after the country's currency was dragged lower against the euro by a 10 percent slide in the dollar last year, pushing up the cost of imports from Europe. Kuwait switched to a basket of currencies on May 20 because of gains in consumer prices, which are also accelerating in the United Arab Emirates and Qatar.

"The weaker dollar is fueling inflation," said Dorothee Gasser, an analyst at ING Bank in London. "We see the U.A.E. as the next possible shifter."

Who's Next?

The U.A.E. dirham slid 0.01 percent to 3.6727 against the dollar today, the Qatari riyal gained 0.01 percent to 3.6392, and the Saudi riyal was little changed at 3.7504. The Syrian pound was unchanged, according to data compiled by Bloomberg.

Syria will tie its currency to so-called special drawing rights, certificates issued by the IMF that represent a basket of currencies including the dollar, euro, yen and U.K. pound.

Mayaleh said today that the pace of price gains in Syria may slow to 8 percent this year, from 10 percent in 2006, because of the decision.

U.A.E. Prime Minister Sheikh Mohammed bin Rashid al-Maktoum said on May 22 that the country would keep its link to the dollar, even after inflation quickened to 10.1 percent in 2006, from 7.8 percent the year before.

"Inflation is a risk for all these countries and allowing their currencies to appreciate versus the dollar is one way to address that," Jon Harrison, an analyst at Dresdner Kleinwort Group Ltd., said in London.

'We're Technocrats'

Qatar's consumer price index leapt 14.8 percent from a year earlier in the first

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quarter of this year, from 12.8 percent in the prior three months.

Rising costs in the U.A.E. and Qatar are ``a clear call for currency revaluation," Serhan Cevik, a London-based economist at Morgan Stanley, said in an e-mailed research note last week.

Syria, under fire from the U.S. for alleged support for terrorism, said in July last year it planned to dump the dollar peg by the end of 2006 to reflect closer trade ties with Europe.

The Central Bank of Syria had converted half its currency reserves to euros, Mayaleh said last July. The reserves, including gold, totaled \$4.1 billion at the end of 2005, according to the U.S. Central Intelligence Agency.

Mayaleh said today the switch in the peg would contribute to investment growth and ``there's no political reason" for ending the dollar link. ``We're technocrats," he said. Reuters earlier today cited Mayaleh as saying that previous plans to end the dollar peg had been held up.

The IMF based the valuation of SDRs as of Jan. 1, 2006, on a weighting of 44 percent for U.S. dollars, 34 percent for euros and 11 percent each for the yen and U.K. pound.

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