Will crashing oil prices mean the collapse of Iraq's economy? No. Will the Iraqi economy (and people) suffer? Yes, a great deal…

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Introduction

Since the crash in Iraqi oil prices from US$61.0 (per barrel) at the end of January 2020 to US$20.7 by mid-April 2020, a crisis compounded by the spread of COVID-19 virus, political vacuum, failed ethno-sectarian polity, to mention but a few, the country has been grappling with quasi-existentialist questions?

> **First**, can/should Iraq as a country and an economy continue to be so massively crude oil-export-dependent?
> **Second**, can/should Iraq continue to have no real control of its economy, given that oil prices/production is overwhelmingly determined by OPEC + and others, operating in the oil global market, rather than *sovereign* Iraqi decision makers?
> **Third**, is the current oil prices crisis an existentialist reminder that the economy *must* be diversified from this point in time onwards in favour of other productive sectors by engaging the private sector in a significant way/scale, which has been undermined for over nearly 60 years now?
> **Fourth**, given the failed post-2003 (ethno-sectarian) political system, which has severely undermined the 'state of Iraq' in favour of self-serving plutocratic political class, what form of political system should Iraq have instead? What sort of polity would genuinely represent Iraqi people, listen to, and act upon professional independent economic advice, and initiate economic development for current and future generations?

As insinuated above, Iraq, of course, needs to address multiple major, well-recognised, challenges facing it at present: COVID-19 virus; filling the vacuum left by a resigned prime minister and his cabinet; regaining sovereignty as an independent country; reducing unemployment; stopping widespread violence against women, and applying the rule of law against those advocating marginalising women's position in society, economics and politics, alleviating poverty for a third of its population, etc. etc. To this add open interference by other countries in decision-making processes at all levels, undermining *sovereignty* and the livelihood of millions of Iraqis.

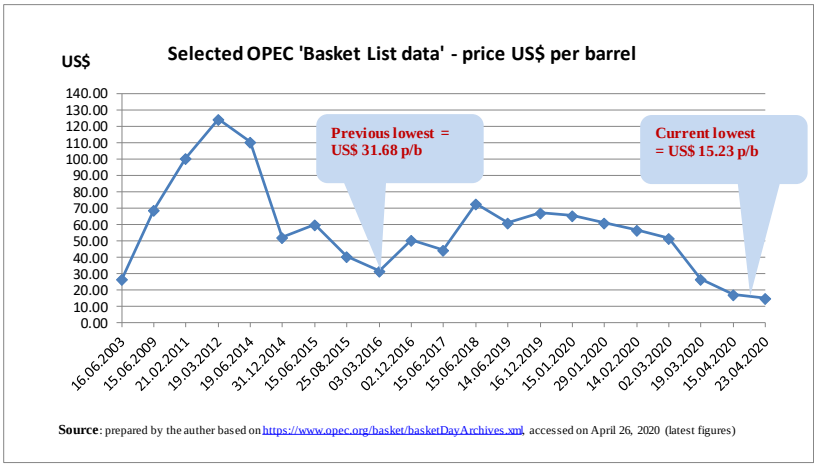
This note, however, focuses, albeit briefly, on the first three questions. Whilst the fourth question is critical in addressing the first three questions, it is outside the scope of this note, and more the province of specialist political scientists and professional politicians.

The current economic situation in Iraq – question # 1

To repeat, here are some of the well-known facts/indicators:

1. During 2019, Iraq's average exports of crude oil amounted to 3.53 mb/d (million barrel per day), with an average US$ 61.0 p/b (per barrel), with total revenue of US$ 78.53 billion (https://oil.gov.iq/index.php?name=Pages&op=page&pid=77);
2. Various scenarios for 2020's oil production and revenues in Iraq have been predicted. [i] In this note, Iraq is predicted to export 1.431 bn barrels in 2020 (average 3.98 mb/d), at an average US31.9/barrel, yielding a revenue of US 45.69 bn [ii];
3. The predicted oil revenue for 2020 is around 58.2 percent of the 2019 - a decline of 41.8 percent. The implications for the Iraqi economy (i.e. GDP) and the 2020 'federal budget' are simply dire;
4. Based on a *ceteris paribus* assumption, i.e. if all the components of 2019 Iraq GDP remain constant, except for the crude oil sector, oil revenue of US$ 45.69 bn in 2020, would imply a contribution to GDP at US$ 55.92 billion, a decline in the order of US$ 40.16bn on 2019. Not all the oil produced is exported;
5. On this basis, **2020 GDP** at *current prices* would be around **US$ 180.1 bn**, a decline by **18.2** percent on 2019 due to the recent oil prices crash [iii];
6. This implies a drop in **per capital GDP** from US$ 6,754 in 2019 to US$ 4,398 in 2020, a massive *decline by 35.0 percent*. As per capita income is not evenly distributed, the poorer sections of the society will suffer most; [iv]

7. A scenario based on *ceteris paribus* basis, however, is unlikely to be realised. Other sectors in the economy, e.g. agriculture, might increase contribution to GPD, especially given the issues COVID-19 poses in relation to imports, and the need for self-reliance, security, etc.
8. Speculating, the decline in 2020 GDP might be anything between 10 to 15 percent on 2019;
9. The above observations illustrate the severe impacts of the volatility of oil price changes (Figure below) in a rentier economy like Iraq's, where oil comprises over 60.0 percent of GDP, at 2007 constant prices (http://cosit.gov.iq/documents/national_accounts/... 202019.pdf, Table 5);
10. This also means, as many commentators have already noted, significant borrowing from domestic and foreign sources, rescheduling current debt (e.g. IMF's) loan, deferring payment (e.g. Kuwait's 'Gulf War' reparations), etc. And, that is on top of the massive anticipated deficit-financing (estimated at around US$40 bn) in the yet un-approved 2020 'federal budget' to pay for, *inter alia*, public sector salaries/pensions bill estimated at around US$ 45bn [v]. All in all, it is a 'terrible mess'!;
11. This is also a self-inflicted deep wound; oil prices are determined by political and economic decisions (i.e. manipulating supply within OPEC) etc. Decisions that are effectively outside the control of Iraqi decision-makers; be they politicians, ministers or economic advisors; Iraq is not a price maker. The severity of the recent collapse in oil prices is depicted in the Figure below;



Source: prepared by the auther based on https://www.opec.org/basket/basketDayArchives.xml, accessed on April 26, 2020 (latest figures)

12. An important implication of the above observations is that in additions to other huge challenges Iraq faces (as noted in Q4 above), a swift and credible economic policy response is ***imperative***. The Iraqi ethno-sectarian political class at the helm of the state and government has, arguably, deliberately ignored the economy (except for maximising oil revenues) so that this class can maximise their share of the booties;
13. Advice delivered to government from some of the brightest academic and professional Iraqi economists has been deliberately (and in some cases callously) ignored, to the detriment of the well-being of the overwhelming of the Iraqi people;
14. It is difficult to see how the calamity the Iraqi economy finds itself in can be ignored. This calamity is far deeper than the 2014-2016 economic crises. Not even the current political class can. Strong political will that transcends ethno-sectarianism is needed, and serious actions need to be taken to mitigate the multiple negative impacts of the current present (in Q1 of 2020) crises in the country; and
15. Arguably, Iraq needs to move away from the loose, *ad hoc*, disjointed, patchy, politically-driven 'economic' policies, to set out a serious economic programme that (yes you have read this correctly) diversifies the economy, using oil proceeds to improve the well-being of all Iraqis, principally by rejuvenating the role of the private sector in the economy, with the state playing an enabling role (no this is not the writing of an admirer of F. Hayek, d.1992). Government's role remains critical in initiating economic development, of which the ultimate aim is to improve the well-being of people.

The *imperative* of multiple policy actions, immediately…now!

For a long time now, even before the 2003 regime change in Iraq, numerous contributions have been made by prominent Iraq economists, politicians and the general public, inviting the political class to initiate *economic development* in the country. The aim being to avert (and/or mitigate) potential crises caused by over-dependence of the Iraqi economy on oil revenues, and for public and private sectors to work together to achieve this.

Instead of heeding credible advice, the political classes have been in persistent denial, notes Ahmed B. Ali [vi], "social justice is a moral and practical process, just as is the elimination of corruption, (but the political class) are abandoning *economic development* in a pretence that they are interested in justice, integrity (*nazaha*), or even replacing it by 'sustainable human development' or 'international development goals'; lamenting the environment and calling for green investment and solar energy in Iraq!...They diffidently note *economic development*, avoiding the case for industrialisation, the economic calculus for growth and its requirements." Ali (*ibid*) draws our attention to the high rate of population growth (2.7 percent pa) in Iraq, which even if it (optimistically) declines to 2.0 percent pa, would be problematic in the future (2050) should the country's GDP continue its current path of heavy dependence on oil revenues. This fact alone Ali argues, makes it imperative that change must take place towards initiating economic development proper, so as to avoid an otherwise likely scenario where future generation would still experience the misery of backwardness and poverty.

In his recent 'Power of oil wealth…' contribution, Sabri Z. al-Saadi concludes that "It is not economically efficient, or socially just, let alone politically wise to continue applying the current fiscal and monetary macroeconomic policies as well as foreign trade policy. These (post-2003) policies have led to distribution of oil wealth in the interest of expanding both public and private consumption via financing expanding imports, and haemorrhaging foreign reserves realised through increased crude oil exports. These policies have also contributed to a slide into the 'trap' of increasing the public and foreign debt, and (importantly) avoided government investments in projects to diversify the economy, financed by oil revenue." [vii] Al-Saadi goes on to say "In Iraq, deteriorating political and security circumstances, as well as failure of governments and controlling political parties in tackling the consequences of endemic and acute structural economic crisis, has been in part due to political mockery of using oil wealth, deploying it for corruptive purposes, undermining the efficiency of the executive, legislative and judicial institutions (across the whole country). This situation dictates a constant reminder of the importance of maintaining public ownership of oil wealth" (*ibid*).

The present writer has elsewhere [viii] emphasised the ***imperative*** of immediate action to restructure the Iraqi economy (GDP), using oil revenues in the interest of Iraq, and its economic sectors (investing significantly especially in agriculture, manufacturing, physical and social infrastructure). It is plainly obvious that this is the surest way to reduce high unemployment and poverty through building a constructive working relation between the public and private sectors. The rejuvenation of the private sector in Iraq is vital for this to happen; this author believes that the creation of competitive markets must be at the centre of nation-economy-building in Iraq going forward.

Control over economic decision-making, based on a realistic vision and an economic strategy - question # 2

History shows that for such imperative actions to be successful, they must be implemented efficiently and effectively by a sovereign state and professional and impartial institutions.

As is widely reported in the media, the Iraqi state and government are considerably influenced by outside forces - be they regional or international – dictating strategic and tactical political and economic decisions at all levels, in diametrically opposite directions. This effectively dilutes Iraq's sovereignty, as demonstrated by both the October 2019 youth uprising and also the recent attempts to appoint a new prime minister.

For Iraq to succeed in rejuvenating its economy, this situation must change, sooner.

To note the obvious, economic development needs political stability, clear realistic vision for the future supported by clear socio-economic strategic policies that can be translated into economic development *calculus*.

That is to say, economic development means getting into the nuts and bolts of population and labour force projections, changing the structure of GDP, calculate volume/value of necessary domestic and foreign trade (how much oil should be produced, exported and processed domestically), study how the forces of supply and demand determine prices in Iraq (and its regions), study very closely the sectoral inter- and intra-commodity exchanges over time (supply chains/I-O tables, F-B linkages etc.), linking universities with industry to manage entry into the labour market, promote R&D in the digital age, etc. etc. all based on robust, verifiable, calculus of the development.

In summary, economic development is about improving the well-being of Iraqis through, *inter alia*, accumulating productive (and nominal) capital, expanding the absorptive capacity of the economy, and improving human capital. It is also about diminishing poverty and significantly increasing the participation of women in the labour market, in society generally and in political life. Such *calculus* is, in theory, easily accessible.

Iraqi history clearly shows that conflicts, wars, nationalist ideology and ethno-sectarian polity ***do not*** deliver economic development. **Peace does**.

The imperative of diversifying GDP, and creating a sovereign fund to mitigate potential future crises - question # 3

It is beyond reasonable doubt now that the current oil crisis poses an existentialist reminder that the economy *must* be diversified from this point in time (April/May 2020) onwards in favour of other productive sectors. Iraq's experience over the past 100 years clearly shows that this should be done by engaging the private sector in a significant way/scale.

Over the last five years a number of failed (*ad hoc* and *incremental*) initiatives have been undertaken; but it is difficult to detect material progress. Here are some examples:

1. Between mid-2014 and early 2016, one of the largest oil price declines since WWII occurred. The 70.0 percent price crash (from US$120 to below US$40 per barrel) was the longest lasting since the supply-driven collapse of 1986 (*cf.* blogs.worldbank.org/...oil-price-plunge-2014-2016-...eight-charts). At that time there was an urgent need for greater sectoral diversification for Iraq (indeed for oil exporters, generally). Alas, such a price (and revenue) crash did not spur any significant policy response, given subdued long-term prospects for oil prices at that point; defeating ISIS was (in many ways quite rightly) a priority for the Iraqi government, apparently to the exclusion of major economic initiatives.
2. Following the expulsion of ISIS from Mosul (and other areas in Iraq) in 2016, the government sought to draw a plan to rebuild the city and repatriate displaced citizens. Iraq pleaded to raise US$ 100.0 bn in a conference organised in Kuwait (February 2018). Hoping to obtain US$ 88.9 bn, the pledges for US$ 30 bn only were made [ix], but as of today, no transparent account of what happened post-conference has been made public by the Iraqi government.
3. The 'Iraq - 2030 Vision: Prosperous Economy' (July 2017) contains numerical targets for private sector contribution to GDP – at 57%. This is difficult to comprehend, as a 'vision' is actually a statement of intent, not of specific targets given the timescale covered.
4. The '2018-22 National Development Plan' document does not seem to aim at changing the current economic structure in a marked way. Agriculture, manufacturing and oil were projected to contribute 2.2 , 1.1, and 57.0 percent respectively to GDP in 2022 (presumably at 2007 constant prices - the document does not say – see: mop.gov.iq/en/static/uploads/8/…pdf , p.56, Table 7, in English, accessed on 29 April 2020). So, no change planned re: the dominance of oil in the economy.
5. The Ministry of Planning's 2019 report 'The Future We Aspire – Iraq's Vision for Sustainable Development – 2030' sets out to achieve 'social market economy' (p.31), increase contribution of agriculture and industry in GDP to 10 and 15 percent respectively, decrease oil's to 35 percent (p.33). On the investment (Gross Fixed Capital Formation) front, the 'Vision' aims to increase foreign investment to 17 percent (up from zero) and domestic private sector investment to 50 percent, up from 17 percent in 2018 (https://mop.gov.iq/..... 202030.pdf). No calculus of sustainable development is offered in the document, and no historical evidence is provided as to how successful Iraqi government has been in the past in inducing private investment. Indeed, as successive World Bank reports on doing business in Iraq have demonstrated, government has effectively suppressed

domestic private investment in productive sectors (See e.g. http://documents.worldbank.org ... Doing-Business…2020- Iraq).

6. In a 2019 move, government established a 'Ministerial Council for Economics' headed (collectively) by seven ministers, including the minister of planning. The Council is tasked with proposing the bases for economic and fiscal policy for Iraq. It is also tasked with setting out effective implementation mechanisms of these policies. However, in his late-April 2020 study of the work of this Council, professor Hassan L. Kathim notes that whilst the Council has so far conducted eight working sessions, its work is difficult to evaluate as the Council does not have a website, nor PR means so that the public can detect their decisions, actions, policies, etc. (http://iraqieconomists.net/ar/2020/04/28/...). In sum, it is not clear how effective or transparent the Council has been in conducting economic policy.
7. And, last but not least, the 'ministerial programme' of the prime minister-designate, Mustafa al-Kathimi, was leaked to the media on April 29. Chapter three (of eight) sets out the "State's vision for the economy and investment." It proposes, *inter alia*, setting up a 'Higher Council for Construction and Investment' homing in on social infrastructure, initiate 'made in Iraq' project, to stimulate domestic industry; a comprehensive programme for employing youth, and support social welfare network. None of which is new. On the political front, the programme intends to maintain ethnic and sectarian representation in government, and in the case of the military, the political/religious militias will maintain a place as part of the army! If al-Kathimi becomes prime minister, only time will tell whether he will succeed in taking Iraq towards initiating economic development and establish functional democracy.

For now, it is safe to assume that the mishandling of the Iraqi economy by the ethno-sectarian political class, over the past 17 years has elevated *distrust* in local and central governments, indeed the state, sowing seeds of uncertain political future in the near-term.

Concluding remarks

On April 9, Jamal Kochar, a member of the Iraqi Parliament was reported to have suggested that oil exports "would guarantee only half of the wages budget." Perhaps more strikingly, he added that "without reforms and strong and effective remedy of the Iraqi economy dossier, it will never be possible to ensure the needs of the country even if the price of a barrel of oil rises to US$100." [x]

This statement perhaps sums up neatly the poor state of the Iraqi economy at present.

Iraq's economy will not collapse; given the large extent of predicted decline in GDP (18.1 percent) and per capita GDP in 2020 (35 percent), the less well-off Iraqis will suffer a great deal, in the near-term to start with.

Iraq has come through many crises in the past deeply wounded mentally and physically , its people, for example, have withstood the vagaries of the 'Great War', WWII, the despotic regimes, the 1980s and 1990s wars, the economic sanctions, and post-2003 ethno-sectarian polity that is tearing the social fabric of the country apart.

The suffering of Iraqi people, alas, *would be much less* had the economic structure of Iraq been diversified towards the productive sectors of the economy other than oil, and if Iraq had accumulated a significant sovereign fund.

It is now up to the Iraqis to turn this calamity into an opportunity, learn from the lessons of history, and move forward with strong will and determination to initiate economic development. A determined leadership, with strong will is needed; a leader with the craft of securing a more prosperous Iraq for future generations!

End Notes

The writer is grateful to Misbah Kamal for editorial comments on a previous version.

[i] See for example, Al-Musawi, Nabil J. (April 2020) *Quick fixes to confront the financial crisis in Iraq* (posted at: http://iraqieconomists.net/ar/, accessed on April 20, 2020);
Al-Bani, Mahdi (April 2020) *Economic boost bazooka* (posted at http://iraqieconomists.net, accessed on April 20, 2020); and FitchRatings (April, 2020) Fitch Revises Outlook on Iraq to Negative; Affirms at 'B-'

(https://www.fitchratings.com/research/sovereigns/fitch-revises-outlook-on-iraq-to-negative-affirms-at-b-16-04-2020, accessed on 22 April 2020).

[ii] These predictions are based on a number of assumptions, including:

1. The government will provide monetary and fiscal stimulus to the economy, providing liquidity, which may not necessarily be sufficient to support the productive sectors, but supply is likely to be hit hard;
2. Trade will be rationalised to protect foreign reserves (at CBI);
3. Domestic and foreign debts will be rescheduled and or deferred;
4. Wages, salaries and pensions will be supported to an extent, so effective demand will decline but not totally collapse;
5. The effects (and costs to the economy) of COVID-19 will diminish, but not disappear;
6. Average daily crude oil exports throughout 2020will be 3.975 mb/d (Table below); and last but not least
7. Average price per barrel will be US$31.93 throughout 2020, picking up in the second half, to average US30.00 (Table below).

2020 All IRAQ	Exports - barrel per day (actual and predicted)	Price: US$ per barrel (actual and predicted)	Total revenue US$
1	2	3	4
Daily exports for Jan + Feb 2020 i	4,500,000	41.27	11,247,000,000
Daily exports for March + April 2020 ii	4,000,000	35.50	8,520,000,000
Daily exports for May + June iii	3,600,000	25.00	5,400,000,000
Daily exports for July to Dec. 2020 iv	3,800,000	30.00	20,520,000,000
Annual (2020) average exports per day (15,900,000 / 4)	3,975,000	31.93	45,687,000,000
Notes: i Actual figures based on Ministry of Oil website -https://oil.gov.iq/index.php?name=Pages&op=page&pid=77			
ii Figures in col. # 2 are based on actuals and take into account comments made by the minister of oil (Mr T. Ghathban) suggesting difficulties selling oil in March 2020 (especially to India) - https://oil.gov.iq/index.php?name=News&file=article&sid=2574			
iii Figures in col. # 2 are based on 22.8 percent reduction in production, as agreed by OPEC - (*ibid*)			
iv Figures in col. # 2 are based on 18.0 percent reduction in production, as agreed by OPEC (*ibid*).			
The figure of US$ 31.93 (col. # 3) is not a weighted average; it is based on dividing total predicted annual revenue by barrels sold.			
The figure of US$ 45.687 bn predicted revenue for 2020 (col. 4) is 58.2 percent of the 2019 revenue of US$ 78.527.			
All figures are approximate.			

[ii] This is close, though the assumptions may be different, to the results of a scenario provided by Professor Hassan L. Kathim, who predicts GDP to decline by 17.0 percent, in case where oil prices in the second half of 2020 might rise to US$40. See Hassan L. Kathim (April 2020) *The Iraqi economy in the time of Covid-19 - the impact of three crises on 2020 GDP* (2nd in a series, posted at http://iraqieconomists.net/ar/2020/03/28/, accessed on 27 April 2020).

[iii] This is **close**, though the assumptions may be different, to the results of one of three scenarios provided by Professor **Hassan L. Kathim,** who in one of his scenarios predicts GDP in 2020 to decline by **17 percent**, in case where oil prices in the second half of 2020 might rise to US$40. The other scenarios predict **29 and 35 percent fall in 2020 GDP**. See Hassan L. Kathim (April 2020) *The Iraqi economy in the time of COVID-19 - the impact of three crises on 2020 GDP* (2nd in a series, posted at http://iraqieconomists.net/ar/2020/03/28/, accessed on 27 April 2020).

[iv] Population estimates for 2019 (at 39,124,000) and 2020 (at 40,150,000) are provided by the Central Statistical Organisation (http://cosit.gov.iq/ar/2013-01-31-08-43-38)

[v] *cf*. Al-Musawi, Nabil J. (*op cit* – p.5).

[vi] See Ahmed B. Ali (Feb. 2020) *Challenges of economic development and the narrative of demonstrative political intentions* (تحديات التنمية الأقتصادية وخطاب الدافع السياسي والأستعراضي
http://www.ahewar.org/debat/show.art.asp?aid=666406, accessed on 23 Feb. 2020).

[vii] al-Saadi, S. Zier (2020) *The power of oil wealth and the Iraqi economic system – duality of central planning and competitive market mechanisms* (al-Mustaqbal al-Arabi, March 2020, No. 493: 75-97 Centre of Arab Unity Studies, Beirut, Lebanon. (https://caus.org.lb).

[viii] Hirmis, A. K. (Dec. 2019) *Private sector investment in Iraq – what strategy for the next prime minister* (posted at: http://www.iraq-businessnews.com/2019/12/13/private-sector-investment-what-strategy-for-the-next-pm/)

[ix] See for example, https://www.nytimes.com/2018/02/14/world/middleeast/iraq-kuwait-donor-conference.html and, https://www.theatlantic.com/international/archive/2018/02/iraq-conference/553325/.

[x] See https://www.iraqicp.com/index.php/sections/news/34672-2020-04-09-13-14-27.

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