

## **Iraq's PM meets the President of the United States... What outcome...for the Iraqi economy?**

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### **Introduction**

This Thursday, August 20th, the “*President Donald J. Trump will welcome Prime Minister Mustafa Al-Kadhimi of the Republic of Iraq to the White House ...As close partners, the United States and Iraq will look to expand (their) relations across a range of issues, including security, energy, health care, and economic cooperation.*”<sup>1</sup>

The question is: what does each side expect, indeed wish, the outcome of the talks and negotiations should be?

Here, some aspects of the potential for ‘economic cooperation’ between Iraq and the U.S., in the near/medium term are covered.

### **A likely U.S. perspective**

Contextualising the US perspective, one could speculate that its strategic interests in Iraq, and the Middle East generally, can no longer be secured by exchanging oil for political support and the export of arms. The last 100 years have shown that this is not a sustainable position, and it must change. Stability in Iraq, though, is critical for securing US’s strategic interests. Having invested enormous human, financial and political capital in Iraq, the US would encourage the establishment of a diversified, “free-market”, economy based on increased employment in productive sectors (thus alleviating poverty), good governance and rule of law. The US could help in tackling pervasive corruption (a major economic cost and hazard to doing business in Iraq) in part by deploying advanced technology.

More specifically, The US recognizes the existentialist economic challenges facing Iraq in light of these *three crises*: the post-2003 disastrous economic policies that nurtured widespread corruption, increased the economic power of (Iran-backed) influential personnel within/without the state apparatus and the (armed and well-financed) Hashd militias; the COVID-19 pandemic; and, finally, the severe decline in oil prices, in March/April of this year.

The US also recognizes that Iraq should enact fundamental economic reforms, which, from a US view point should consider:

1. The 2008 Strategic Framework Agreement (SFA) with Iraq. The fourth point in the Preamble emphasizes “the building of a *diversified and advanced economy* that ensures the integration of Iraq into the international community.” This is echoed in Section V of the SFA. Section V (point no. 7) which goes further to say “Facilitate the flow of direct investment into Iraq to contribute to the reconstruction and development of its economy.” The US would assert that the 2008 SFA is a reasonable and rational vehicle to do so, providing there is a strong *political will*, and public acknowledgement of the constructive part both parties *should* play, without which democracy in Iraq will not take root in the long-run;

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<sup>1</sup> (<https://www.whitehouse.gov/briefings-statements/statement-press-secretary...-iraq/>. The Press Statement was issued on August 7th).

In their June 2020 meeting, the respective teams preparing for the visit jointly stated that “The two countries reaffirmed the principles agreed upon by the two sides in the Strategic Framework Agreement (SFA), as well as the principles in the exchange of diplomatic notes and the letters of the Republic of Iraq to the United Nations Security Council...The United States reaffirmed its respect for Iraq’s sovereignty, territorial integrity, and relevant decisions of the Iraqi legislative and executive authorities.” (see: <https://www.state.gov/joint-statement-on-the-u-s-iraq-strategic-dialogue/> This was released on June 11, 2020).

2. Making use of US economic advisors to work directly with the Government of Iraq to help advance international support for Iraq's reform efforts, including from the international financial institutions. They know that Iraq may not concur on all parts of this point; there is already a wealth of research by economic experts pointing to what needs to be done to initiate economic development in Iraq. The time now is for action – i.e. policy implementation, and soon. Iraq might argue that this (al-Kadhimi's) government needs to demonstrate its worth for the people of Iraq, given the planned general elections in June 2021;
3. The enactment of 'firm plans for fundamental economic reforms' soon; the enactment of these plans by parliament is a pre-requisite for US involvement in investment projects in Iraq. Arguably, Iraq must soon create the conditions for foreign investment to take place on a wider scale, and reverse the recent decline of FDIs in Iraq, as the 2019 UNCTAD report indicated. The conditions for doing business in Iraq must change soon, and become favourable - these, as the 2020 World Bank's 'Doing Business in Iraq' report shows, are diverse. To pick one example, the US side might point to the weakness of the banking system, let alone its near-impossible conditions for extending credit to potential investors. These huge problems facing investment in Iraq are also well-known to, and appreciated by, the Minister of Finance, Ali Alawi, and senior civil servants, including those working at the PM Office; and,
4. Petrochemicals and electricity might be priority investment fields from a US perspective, as they might be able to make a swift impact on the domestic market, though this would require dealing with reported corruption within this sector including in the areas of illegal connections to the grid, and contracts awarded for distribution/transmission of electricity. This means that Iraq would need to swiftly deal with the 'deep state' that engenders corruption in this and other sectors of the economy.

Finally, the US side might argue that its support must not be one-sided. It *must be reciprocated* by effecting tangible changes in the economy and political system, amongst other things. Otherwise 'the potential for investment projects involving world-class U.S. firms in the energy and other sectors' might not proceed.

To survive, it is imperative for any economic/political relationship to be based on some common ground – in this case, a real commitment for change to initiate *economic development* in Iraq must be demonstrated by Iraq and the U.S. So what would Iraq's government hope to get out of the negotiations?

## **A likely Iraqi perspective**

The Iraqi Prime Minister, Mustafa al-Kadhimi, and the team accompanying him are fully aware of the challenges they face: be they political, economic, social or environmental.

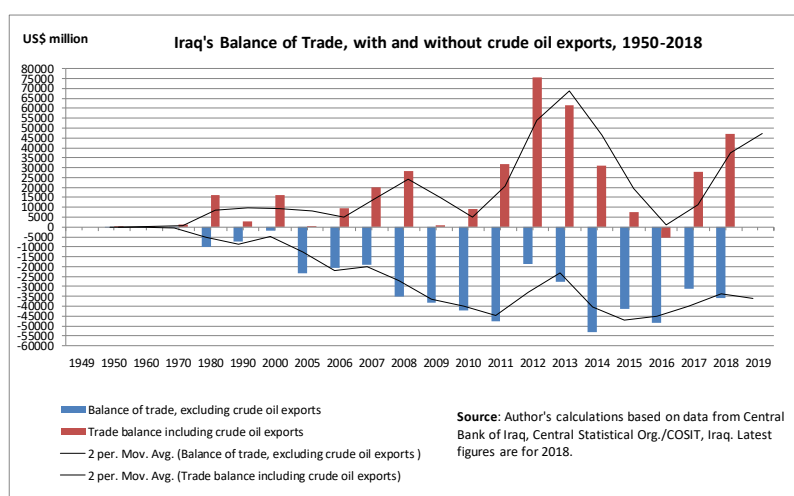
Soon after being appointed, al-Kadhimi set out his 'Government Programme' on May 6th, in which Article 3.1 states that in the *short term*, the government intends to handle the ramifications of the oil price crises by rationalizing public expenditure and stemming unnecessary expenditure. It also intends to develop the tax and tariff collection system. (see: <https://www.pmo.iq/press2020/6-5-202002.htm>). The Programme goes on to say (in Article 3.2) that a 'Development and Investment Board' would be established, this will provide a comprehensive plan for investment in infrastructure etc. al-Kadhimi's team might also point out that since his government is fully aware of the weaknesses of the banking system, the CBI (Central Bank of Iraq) has been asked to handle this problem within a specific timescale! Finally, the Programme also points out that a comprehensive reform of the administrative system will be undertaken, youth employment in the private sector will be encouraged, etc.

More recently, on August 3rd, al-Kadhimi has pointed out that a 'White Paper' is being prepared dealing with the wider economic issues. His Finance Minister, Ali Alawi, had in several occasions indicated the government's awareness of the problems and promised that

these will be dealt with appropriately! (see: <https://www.france24.com/en/20200622-without-urgent-reform-iraq-economy-will-face-irreparable-shocks-minister-to-afp>).

So the Iraqi side has a number of aspirational objectives to cover in their talks with the American side. They will, however, be well advised to be open about the long term problems Iraq's economy has been suffering from (what is called 'structural problems' to do with the GDP's composition). They should declare their vision/solutions which they might have in mind and the extent to which they think the U.S. side could, in the long-run, assist in transforming/diversifying the economy.

1. One such chronic problem that the Iraq economy has been afflicted with is the historically acute negative balance of trade (when excluding the export of crude oil), as shown in the Figure below.



2. Although inextricably linked to various (structural) aspects of the Iraqi economy, especially the recurrent deficits in the 'Federal Budget', the government might be well advised to bring this issue in the talks with the U.S. This provides a glaring example why it is *imperative* for Iraq to diversify its economy and why it will need U.S. assistance deploying the 2008 SFA, though the SFA itself might itself need to be reviewed, to be more specific in the capital investment field.
3. The Iraqi delegation might be candid enough to go as far as admitting that the recurring budget deficit is not entirely due to excessive reliance on oil exports, it is perhaps mainly because Iraq hardly exports anything else of high-value-added that other countries might have a comparative disadvantage in and would otherwise import goods/services from Iraq.
4. Now that it has been acknowledged by many experts that both the high rate of increase of Iraq's population and the likely decline in oil prices as it becomes less in demand as an energy source, in the coming few decades, al-Kadhimi's wisdom (or perhaps his survival instinct) might lead him to believe that this is a strategic priority for Iraq, and that if the U.S. is genuine in its desire to assist Iraq, this is where the emphasis should be – rectify the balance of trade (excluding oil) over the next 20-30 years, driven by the private sector with an enabling public sector.

Would al-Kadhimi opt for this direction of travel, and, if he did, will he adjust his thought process to make this *the* major strategic economic objective for Iraq?

## The Joint-Statement

It is anticipated that the 'joint Statement' it issues will be drafted in the most diplomatic, courteous, and respectful manner. It is likely to postulate the existence of good relations between the U.S. and Iraq, with the former offering support and assisting to the Iraqi people

to achieve their aspirations in establishing democracy, rule of law, good governance, and alleviating poverty, amongst other things (to be said in the Statement). It will probably acknowledge that the coming months will be critical in deciding the short-to-medium-term events in Iraq, given the depth of the resentment to al-Kadhimi's government in some quarters whose interest are seen to be seriously threatened.

The Joint Statement doubtless will touch on the security partnership, the anticipated elections in June 2021, humanitarian aid, the significant progress made towards eliminating the ISIS threat, over the coming months, etc.

The two sides will reaffirm the 'importance of the strategic relationship and their determination to take appropriate steps to enhance it in the interest of both countries and to achieve security, stability, and prosperity in the region.'

The time-honored dictum, though, will ring loud – that a combination of polity and economics that serves the people will thrive, and so will the country that upholds it. The polity and economics that does not serve the people will soon perish. The long history of Iraq, since early Mesopotamia, provides witness to the truthfulness of this dictum.

Both the current Iraqi and U.S. governments have now a new opportunity to choose one path or the other. We should find out soon!

**\* Amer K. Hirmis, August 17, 2020**

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