

1 Managing costs for Iraq's Reconstruction and 2 Recovery

3 4 5 ABSTRACT 6

Aims: To analyze the current situation in Iraq in terms of government expenditure, allotment of funds to different sectors and cooperation with international organizations.

Study design:

Place and Duration of Study:

Methodology: The patterns for managing costs during the past years were determined in order to assess the efficiency of the new government, estimated budget and development plans, as well as the results of the past involvement of international organizations in the stabilization of the Middle East scene.

Results: The limited credibility of the government of Iraq has its roots in years of poor governance, inconsistent regulations, corruption and security issues, in spite of the numerous foreign investments; the aforementioned problems have been causing structural weakness and extensive damage to the economy as a whole and thus, the international institutions has to intervene actively and set strict standards for proceeding in the reconstruction of Iraq as a high-potential country.

Conclusion: Relying on significant achievements in the global fight against terrorism and in high hopes of the declaration of the Middle East as a peace zone, Iraq will be able to fully recover over an extended period of time with the aid of international authorities, by developing its non-oil industries, properly managing investments and shrinking costs.

7
8 *Keywords: reconstruction, investments, expenditure, development*

9 1. INTRODUCTION

10 In the actual global context, the lack of political and administrative leadership, the ethnic and
11 religious division and the rapidly growing level of corruption of impromptu regimes have
12 created an unprecedented opportunity for destabilizing economies, political pluralism and
13 dominance of terrorist groups. This destructive mix has been posing a threat to the well-
14 being of the overall society for a prolonged period of time, affecting mainly the countries in
15 the Middle East and Northern Africa. The current crisis in Iraq represents a tangible example
16 in this regard, reflecting the consequences of the unresolved civil war in Syria, the tension
17 between Saudi Arabia and Iran religious beliefs, all of them being bordering countries of Iraq.

18 Despite the continuous efforts, large amounts of money invested and complex projects of
19 managing costs and resources incurred by the Western countries, the extended Middle East
20 is far from achieving peace and balance. Hence, Iraq is now facing a new episode of this
21 tragic process of regional destructuration, jeopardizing the lives of its citizens and
22 sabotaging the recovery and reconstruction project of a systemic, sustainable and mutually
23 beneficial relationship with the Western civilization. Notwithstanding, forging alliances and
24 properly managing the foreign investments and government spending in order to secure and
25 pave the country road to development is a matter of the utmost importance.

26 The structural weakness of Iraq's economy has allowed the Islamic State of Iraq and Levant
27 to control almost one third of its territory, causing the displacement of millions of people and

the death of thousands civilians due to the alarming frequency of armed conflicts the escalating number of violent manifestations. The massive flow of refugees and armed groups inside and outside Iraq has also stretched the private sector to an extremely damaging degree, while jeopardizing the progress of non-oil economic activities. Being highly dependent of government spending and therefore on oil revenues, all the other industrial sectors, accounting for 46% of the economy, have been suffering utter devastation due to the disruption in trade, depraved infrastructure and lack of capital as a result of the decline in oil prices. Further on, the demographic pressure, obstructed access to electricity and increasingly high unemployment rate have weakened the business environment, already strained by the ongoing security issues.

Likewise, the Kurdistan region requires special attention and separate funding due to its delicate situation and the high influx of Syrian refugees, increasing the region's population with 28% in the background of a doubled rate of poverty. Even though the government of Iraq has shown responsiveness in aiding the displaced population, the adversely affected resources available at the moment are not sufficient for overcoming this humanitarian crisis.

2. METHODOLOGY

The Iraqi government expenditure patterns and its reconstruction and recovery plans for the future years must be thoroughly analyzed in order to assess their chances of success, respectively failure, as well as the consequences reverberating on the international economic scene as a result of their implementation. The New Development Plan and the Iraq Development Management Systems set ambitious standards for the evolution of Iraq as a state, in terms of attracting investments and covering the budget deficit.

However, the results of the involvement of international institutions must also be determined in order to estimate the future necessary funding for stabilizing the situation in the Middle East. Currently, Iraq is a member of the United Nations and its affiliated agencies, the International Monetary Fund, the International Labor Organization and the World Health Organization, collaborating with all of them for preserving world peace and security and promoting human rights. Additionally, Iraq belongs to diverse pan-Arab organizations such as the Arab League.

2.1. Government expenditure patterns

The Iraqi government expenditure from previous years has contributed to establishing a pattern into how the country sets its priorities, manages the costs and allocates funds. Per contra, the actions undergone in this regard have diminished the credibility of the management of Iraq on the international scene.

In 2013, the average expenditure totaled more than \$118 billion, an increased value compared to the previous year, which further exceeds 70% of the Iraqi gross domestic product. The prioritized sectors for receiving significant funding were the Energy sector, accounting for 21%, Security and Defense, standing up to 14% and Social Services, amounting to 13% of total budget investment expenditure. Being one of the major oil producers, Iraq used to allocate a high percentage of the investment expenditure in the oil field, strategy which allowed the government of Iraq to cover its operating expenditure in the past. Nonetheless, the considerable reliance on oil has made its budget vulnerable to oil shocks and the recent destabilization of the market prices has put pressure on the authorities to go through complementary budgeting and delay investment projects implementation. Notwithstanding, the oil industry alone proved itself to be unable to cover the existing budget deficit. For improving Iraq financial resilience and reserves, the Arab

74 country was forced diminish its dependence from the oil Iraq needs, by attempting to
75 increase non-oil revenues.

76 Further on, the government expenditure has skyrocketed in the following year, almost 70%
77 of the public budget being allocated for public payroll, food and energy sector, besides
78 financing the armed forces struggle to combat the Islamic State of Iraq and Levant and train
79 the volunteers in this regard. The refugee crisis has also stretched the budget limits in spite
80 of the billions of dollars invested, together with the mismanagement and corruption of a
81 fragile public financial system. Unfortunately, the budget assumption have not matched the
82 tragic reality of both lower than planned oil production and descending oil prices, posing the
83 risk of rampant inflation and currency weakening.

84 Comparing 2013 and 2014 in terms of budget expenditure, the energy sector, security and
85 defense have remained among the priorities of the government of Iraq. An increase in the
86 available budget in 2014 permitted sizeable investments to be directed to the social services
87 advancements. The crisis situation in the Kurdistan region was not neglected, receiving a
88 higher amount of money in order to ameliorate the pressing problem. The Iraq budget
89 expenditure for the aforementioned years and the main fields receiving considerable
90 financing are depicted in Figure 1.

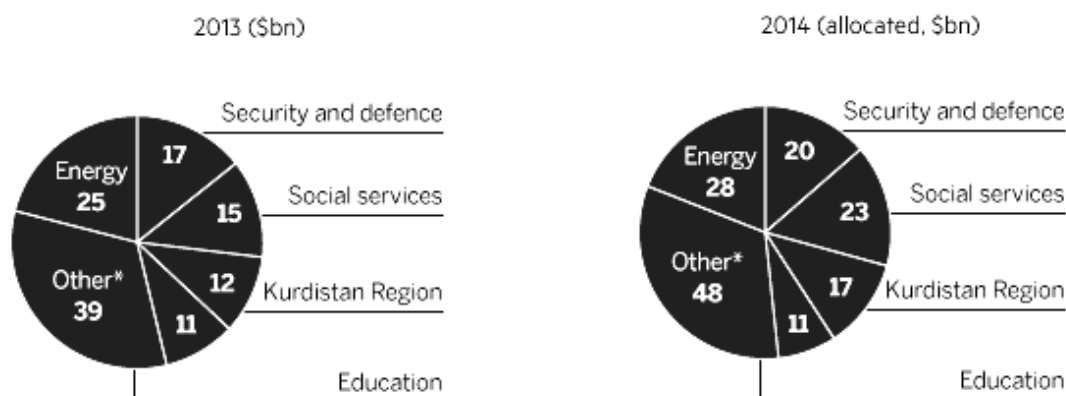


Figure 1 - Iraq Budget Expenditure for 2013 and 2014

91 * Other expenses include local and central administration, health, environment, water,
92 sewage and sanitation, agriculture, culture and youth, transport and communications,
93 construction and housing, debts.

94 Even though the government has struggled to allocate proper funding to the most
95 demanding sectors, the lack of administrative capacity has deterred potential helpers, whose
96 unwillingness to continue funding Iraq's cause in the absence of an approved budget has put
97 the Arab country in a sensitive position towards the international stage. As a result, after the
98 instauration of a new government at the end of 2014, the Iraqi parliament approved the 2015
99 budget of \$105 billion, supported by the lawmakers in the context of an unprecedented
100 crisis. Severe austerity measures were also implemented at the same time, since the
101 accessible funds in 2015 are estimated to be limited, thus causing a considerable deficit in
102 the budget, which stands for 11% of the gross domestic product.

103 The past ratios of government expenditure to gross domestic product as well as future
104 estimations are depicted in the Figure 2. Aware of the lack of budget execution rate to
105 administer performance at governmental level, the government of Iraq has now the
106 opportunity to strategically rationalize its expenditures in a variety of manners such as
107 diminishing the number of subsidies and increasing speed and ease of movement in public
108 employment.

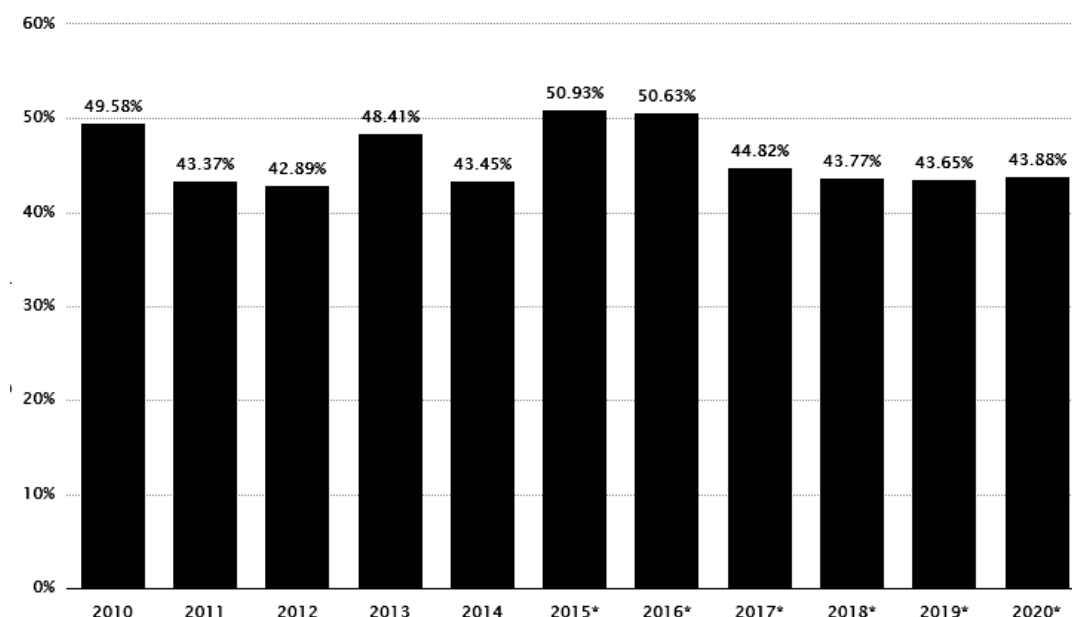


Figure 2 - Ratio of government expenditure to Gross Domestic Product

110 2.2. Reconstruction through thorough planning

111 Throughout time, the investments made following the Arab Spring directed to Iraq, taking
112 into consideration the military and diplomatic costs, have raised to more than \$800 billion, as
113 declared by the Congressional Budget Office of the United States of America. Nonetheless,
114 decades of wars, dictatorships and corruption have left their mark upon the Iraqi society and
115 despite the coherent strategies of international bodies for recovering the Middle East, the
116 majority of the funds received are pumped into the army. Security and defense of the
117 citizens remains a priority on the government's agenda, as the streets of the major cities
118 from Iraq are still cowed by deadly bombings, along with the health sector stabilization, more
119 than a quarter of the country's population living below the poverty line and the lack of reliable
120 electricity and clean water being intolerable.

121 Yet, the urgent need for taking radical action has been already assessed starting with 2013,
122 when the Iraq's new National Investment Plan proposed by the Ministry of Planning was
123 ratified by the Council of Ministers. This shift plan, extending until 2017, has the United
124 States of America playing an important advisory role on Iraqi business and investment
125 policies. Moreover, it has its roots in a prior national plan and aims to overcome the previous
126 inefficiencies encountered and acknowledged.

127 Gas and oil production have still remained one of the best assets of Iraq for decades, but the
128 damage of the other industrial sectors, i.e. electricity sector, has rendered the infrastructure
129 obsolete, directly damaging the economy through an excruciatingly high level of

130 unemployment. However, it would be advisable for a country in Iraq's position to lower its
131 dependence on oil and widen its range of production sectors for strengthening the national
132 economy. Furthermore, it is worth tackling the issue of the cooperation between the public
133 and the private sector if the recovery of Iraq's economy is in question.

134 Ultimately, with the purpose of monitoring the progress of the National Development Plan,
135 the government of Iraq has launched few years ago a bilingual publicly accessible web-
136 based application, formerly known as the Iraq Development Management System. It is
137 designed specially to monitor the ongoing progress of donor-funded projects, while ensuring
138 accountability and transparency. As far as the United Nations are concerned, the Iraq
139 Development Management System represented a milestone in the introduction of a far-
140 reaching reform of the public sector by allowing the monitorization of capital investment
141 projects and avoiding the misuse of public funds.

142 Devoting as high as \$357 billion solely on rebuilding the infrastructure, the ambitious new
143 National Investment Plan of Iraq still struggles with aligning its interests with the political
144 system, although a base of cooperation and continuous feedback with the international
145 institutions and foreign investors has already been established. Therefore, the main focus
146 areas of this comprehensive plan encompass the following:

147 **2.2.1 Living conditions**

148 Despite the continuous efforts of the whole community, there is a stark contrast between the
149 huge potential of Iraq as a country having plenty of natural and human resources and the
150 actual sorrowful situation caused by the lack of quality of life and development. Statistically,
151 the Quality of life index is incredibly low, namely below 35, while the Pollution index has
152 been skyrocketing in the past years, reaching 96.63. Regarding the overall level of prices,
153 the Consumer price index is low compared it its desirable normal value, alike the Purchasing
154 power index, which barely reaches 61.

155 Since more than 1.45 million citizens having to deal with and protect themselves from
156 violence, armed conflicts and persecution on a regular basis, are displaced and obliged by
157 the circumstances to flee and settle in churches, roadsides and camps, housing is among
158 the first milestones to be achieved on the National Investment Plan agenda. The
159 construction of one million housing units is targeted until the end of the project, with
160 emphasis on the rural areas and strategic urban planning. However, the demand for housing
161 is estimated to be twice as high and therefore a shortage will arise, but given the need for
162 structured management of civilian and military costs, it is expected that the level of crime
163 and terrorist attacks will be reduced until 2017.

164 **2.2.2. Oil and gas**

165 Even though Iraq's gradual reconstruction should allow the country to extend among new
166 production areas, Iraq finds itself among the world's largest oil exporters and its potential
167 must be not be wasted. Nonetheless, the regulation should be adapted to the new planned
168 levels of production, since at this moment there are discrepancies in the selling prices, the
169 quantity exported and the amount of money received in exchange. The crash in oil prices
170 has affected dramatically the earnings of Iraq and widened the budget shortfall.

171 However, according to the National Investment Plan, besides targeted production level, the
172 objectives for the oil and gas industry set standards for both export and warehousing, as
173 depicted in the Table 1.

Table 1 - Planned levels in the Oil and Gas Sector

	Actual level	Planned level (2017)
Crude oil production	3.2 million barrels/day	9.5 million barrels/day
Exports of crude oil	2.6 million barrels/day	6 million barrels/day
Capacity of crude oil warehousing	10.987 million barrels	30.057 million barrels
Liquefied natural gas production	880 metric tons	2.600 metric tons

174

175 **2.2.3. Ports**

176 The strategic location as a bridge between Europe and Asia allows Iraq to further develop its
 177 import and export capabilities and become a major hub in the area. Although there are
 178 several port cities with potential to improve, the southern port Al Faw is the main one, having
 179 deep water access and already handling large amounts of shipments due to the recent
 180 exemption of taxes and customs clearance of foreign companies, established by the
 181 government of Iraq. In this regard, Al Faw port container capacity will increase to 3 million
 182 tons/year and the general cargo capacity to 10 million tons/year by 2018 in order to ensure
 183 the availability of supplies and promote international trade.

184 **2.2.4. Power**

185 The raising demand for electricity has been challenging Iraq's power generation capacity
 186 throughout time and until now the output of the electricity sector was not able to cover the
 187 basic needs of Iraqi citizens. The average shortage was of 4.000 megawatts, arose due to
 188 the economic instability and increase in consumer purchases of electronics.

189 Bearing in mind that the electricity is subsidized in Iraq, the plan envisions to rehabilitate
 190 successfully the national grid by increasing production up to 25,000 megawatts per year and
 191 minimizing disruptions. If this performance is to be achieved by 2017, the output will exceed
 192 the estimated demand. Furthermore, the power consumption for each habitant will increase
 193 with 1,900 kilowatts per year in 2017.

194 **2.2.5. Water**

195 A couple of decades ago, more than 75% of Iraqi households had access to clean water, but
 196 the following years of war together with the limited environmental awareness have
 197 jeopardized the whole water resources management system. Currently supplying with water
 198 the majority of Iraq's surface, the Tigris and the Euphrates rivers are still vulnerable to water
 199 diversions and various other risks. Hence, the government aims provide the Iraqi population
 200 with safe drinking water supplies by authorizing the construction of new dams as well as the
 201 rehabilitation of the existing ones, which will increase the water reserve capacity by 22 billion
 202 square meters and water reclamation by 6.25 billion square meters in the next years.

203 **2. RESULTS AND DISCUSSIONS**

204

205 The efforts undergone by the government of Iraq for diminishing the impact of the constant
 206 terrorist attacks and persecution, which have been straining the country resources along with

the instability of the oil market, have proved themselves to be necessary, but not sufficient for stabilizing the Arab country as a whole. Thorough planning and strategic allocation of the existing resources and foreign aid, the situation in Southern Iraq has improved, while the Northern region of the country still struggles to combat the damages of the phenomenon to be assessed as a humanitarian tragedy.

The aforementioned Iraq National Development Plan aims to rehabilitate the infrastructure and private sector assets by managing costs and allocating funds to each sector and industry in order to be able to provide decent living condition to all the citizens, while cooperating with other countries for eradicating the Islamic State insurgency through military funds administered by the army. However, the unfortunate current situation depicting millions of internally displaced people and constantly high crime rates has attracted the involvement of international bodies. The United Nations charter puts special emphasis on the responsibility to protect and following this pattern, several international bodies, institutions and non-governmental organizations have mobilized for fighting against the repression of Iraqi citizens, human rights violations and overall regional instability.

Military interventions have always been a sensitive subject in the United Nations sessions in spite of the expansion of the Islamic State as a de facto state. Expressing the concern about the production and illicit trade of weapons of mass destruction, the Security Council of the United Nations has focused on enforcing foreign policy commitments and international treaties. Initially, trade sanctions and arms and related materials (i.e. military ammunition, weapons) embargoes were imposed on Iraq, but following the chaos resulted by the inability of the government to protect the civilians, the resolution of the Security Council has exempted supplies to the Iraqi government and the multinational forces, but not for end-users in Iraq, by regulating the process of applying for licenses.

Moving further to single countries efforts, the United States of America have been involved actively for more than 10 years in rebuilding the war-torn Iraq. 60\$ billion in American taxpayer funds were invested by the P5 country, together with troops for keeping the situation under control, and the Arab country is still unstable, longing for the actual results of the foreign funds expended, which have left Iraq highly indebted. Furthermore, given the Western nations skepticism regarding military intervention in the Middle East, the latter countries, i.e. United Kingdom of Northern Ireland and Great Britain, Germany, have dramatically increased the intensive training of Kurdish forces in Iraq.

3.1. The importance of international financial aid

Due to the precarious condition of the market, affected by the recent crash in oil prices, the Iraq's consistent attempts of managing government expenditure were not able to attain their objectives. The lack of funds for both reconstruction and recovery of industrial sectors and security and defense purposes have put Iraq in the convenient position of receiving financial aid from international institutions. The World Bank Group, having as main purposes to end extreme poverty and boost shared prosperity, and the International Monetary Fund, aiming to foster global growth and macroeconomic stability, are two of the main bodies that agreed to help Iraq's efforts to tackle the economic impact of terrorism, high unemployment rates, refugee crisis and poverty.

Firstly, the International Monetary Fund reports outline that Iraq economy has contracted 2.1% of the available funds in 2014 on the ground of the increased level of violence, but the recovery of the investment in the current year has been rather shallow, being expected to reach only to 0.5%. On the account of the overall pressure of conflict-related spending, unexpectedly low oil revenues and decline of foreign assets, the budget deficit has raised

tremendously, with more than 10%. Addressing these urgent challenges, the International Monetary Fund is prepared to allot as much as \$833 million as financial assistance to Iraq in the case of an emergency triggered by the Islamic State insurrection. The Rapid Financing Instrument was designed to provide prompt assistance to all member countries facing an urgent balance of payments need and the Iraqi authorities are currently negotiating with the International Monetary Fund officials for implementing the program. So far, a staff-level agreement has been attained, which will be further subject to the International Monetary Fund management approval, but whose successful implementation is reckoned to bring substantial improvements to Iraq's current situation.

Secondly, the World Bank has also been analyzing the urge of Iraq for more financial resources in order to avert the current crisis and address the need of its citizens on the long-term. Genuinely, the World Bank had managed and administered numerous investment operations in Iraq in the past, accounting for \$588 million and including a loan from the International Bank for Reconstruction and Development, two credits from the International Development Association and other grants offered by the Japan Social Development Fund and the Extractive Industries Transparency Initiative. Regardless of the prior efforts and given the current underdeveloped infrastructure and alarming unemployment rates, the World Bank currently administers the Iraq Trust Fund, which has seventeen donors such as the European Union, Japan and the United States of America, working together through the Iraq Partnership Forum and succeeding to raise almost \$500 million. Additionally, special emphasis is put on the close cooperation and consultation of the World Bank with third parties (i.e. Swedish International Development Agency, Agence Francaise de Developpement, Islamic Development Bank) over a variety of subject matters affecting Iraq, encompassing management reform, augmentation of the private sector, transport through lending operations and service delivery.

In addition, qualified member institutions of the World Bank Group have shown their support and solidarity for the Middle East, in particular for Iraq, through a series of assistance activities and supplementary funds. Therefore, in the past 5 years, the investments of the International Finance Corporation have reached \$654 million, assigned to different problematic issues, such as managing freight in major Iraqi ports, building facilities for processing household waste and produce refuse-derived fuel and developments of agribusiness. On the other hand, the investments of the Multilateral Investment Guarantee Agency, standing at \$11.8 million, have targeted the improvement of sewer services, rehabilitation of water networks and pipes as well as the construction and restoration of schools; the health sector, which has suffered extensive damages in the past years, benefited from a new comprehensive emergency system, rehabilitated emergency units and special training of staff.

4. CONCLUSION

Considering all of the above, the government of Iraq envisages ambitious tax measures together with a strict expenditure control and investment prioritization through the New Development Plan and responsiveness for international cooperation. Nonetheless, the best case scenario of the present tragedy destabilizing the whole region cannot be achieved without foreign intervention and international surveillance.

An integrated and sustainable economy capable of providing decent living conditions will remain only an ideal without a reform tackling the fiscal status, trade regulations, social inclusion and poverty. International institutions such as the International Monetary Fund and the World Bank have shown their willingness to contribute in this regard to Iraq's reconstruction and recovery for the common goal of overall shared prosperity. The previous

303 involvement of international organization in the controversial situation from Iraq has proved
 304 to be extremely beneficial, but a more active implication and a wider pool of significant
 305 resources are demanded in order to surpass the consequences of decades of corruption,
 306 mismanagement and hostilities. Hereof, Iraq must guarantee a high degree of compliance
 307 and commitment to the ongoing strategic plans and the established priorities, as well as
 308 openness to future projects aiming to stabilize the country as a whole.

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