

Part IV

Economic Prosperity in Kurdistan

Chapter 12

Economic Diversification and Reconstruction

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Based on consultations between KRG ministries, international agencies, and development professionals, in 2013, the KRG announced a regional strategic development vision titled “Kurdistan Region of Iraq 2020: A Vision for the Future.” Overall, the strategic vision aimed at putting people first, building the region’s infrastructure, creating an economically prosperous region, and making the government work for the people, rather than vice versa.¹ Despite many great achievements, the economic and humanitarian crises affected the implementation of this vision and led to slow-down, sometimes even freeze, of these activities.

Following the Syrian conflict in 2012, the KRG implemented an open-door policy for Syrian refugees to enter the KRI as a haven of safety and protection. Despite there being a large number of internally displaced persons (IDPs), the KRI is now hosting more than 240,000 Syrian refugees inside and outside camps in three governorates: Erbil, Sulaimania, and Duhok. Around 62 percent of these Syrian refugees, which equals to 150,000 individuals, are living in urban and rural locations. The rest are living inside nine camps (Darashakran, Kawergosk, Qushtapa, Domiz-1, Domiz-2, Gawilan, Akre, Basirma and Arbat). In the Middle East, five countries—Iraq, Jordan, Lebanon, Turkey and Egypt—are currently hosting Syrian refugees. Close to 97 percent of all Syrian refugees that entered Iraq are living in the KRI.²

In June 2014, when the Islamic State in Iraq and Al-Sham (ISIS) captured Mosul (the second-largest city in Iraq), a huge wave of IDPs fled from the horrors of this terrorist group towards the KRI. This created a humanitarian crisis, falling on the shoulders of the KRG. The Kurdistan Region is a region within Iraq, and thus the IDPs should be under the responsibility and the protection of the government of Iraq (GoI). How-

¹ Ministry of Planning, KRG. *Kurdistan Region of Iraq 2020: A Vision for the Future*. 2013.

² UNHCR. *Syria Refugee Regional Response*. July 31, 2017. Accessed August 10, 2017. <http://data.unhcr.org/syrianrefugees/country.php?id=103>

ever, Baghdad has shown that the Iraqi government does not care about these IDPs.

The Office of the United Nations High Commissioner for Refugees (UNHR) has estimated that because of the inflow of refugees and IDPs, the population in urban areas throughout the KRI has increased by around 25–26 percent, and the population of the Erbil, Duhok and Sulaimania governorates' by around 15 percent.^{3,4,5} Moreover, the displaced population in some places like the Shaqlawa, Khabat, Bahrka districts in Erbil, the Sumel, Shekhan and Bardarash districts in Duhok, and the Kifri district in Sulaimania equals half of the host community. In addition to the IDPs and Syrian refugees, religious minorities like Yezidis and Christians are living side-by-side the Iraqi and Syrian sectarian communities (Sunni Arabs and Kurds) in peace and harmony.

By definition, IDPs and refugees are different from each other. Nonetheless, they all require the same services from the government (of the host community). Essentially, refugees have a legal framework as mentioned in the Geneva Convention of 1949, but IDPs' responsibility is the state itself, as clearly illustrated in many UN general assembly resolutions, as well as contributions from UN agencies. Taking care of IDPs requires several steps. During their first year of displacement, IDPs need food, WASH (Water, Sanitation and Hygiene) and shelter. In their second year, these IDPs need health service facilities and they need to have their children enrolled in educational programs. In the last step, the IDPs are seeking job opportunities.

As there was no entity in place to deal with the humanitarian crisis, the Council of Ministers of the KRG quickly put in place a High Committee for Humanitarian Needs Assessment, the first step in countering the humanitarian shock that hit the region. In direct cooperation with the UN and with the participation of NGOs, the KRG succeeded to prepare an Immediate Response Plan (IRP) for the duration of September 15–November 15, 2014, and the second phase of this plan, which was called

³ UNHCR. Displacement as Challenge and Opportunity, Urban Profile: Refugees, Internally Displaced Persons and Host Community, Erbil Governorate. 2016, p. 11.

⁴ UNHCR. Displacement as Challenge and Opportunity, Urban Profile: Refugees, Internally Displaced Persons and Host Community, Duhok Governorate. Erbil: Karwan Printing. 2016, p. 5-6.

⁵ UNHCR. Displacement as Challenge and Opportunity, Urban Profile: Refugees, Internally Displaced Persons and Host Community, Sulyamaniyah Governorate and Garmian Administration. 2016, p. 15.

Fiscal Austerity and the Iraqi Budget Share

Out of the 16.6 billion dollars of the KRG budget share of 2014, Baghdad only transferred 1.9 billion dollars (or 11.4 percent). In December 2014, after negotiations took place between the KRG delegation and the central government in Baghdad, an agreement was signed. According to this budget sharing agreement, KRG should handover 550,000 bpd from KRI and Kirkuk fields to Iraq's State Oil Marketing Organization (SOMO) for the purpose of receiving 17% of the federal budget. However, in 2015, Baghdad transferred only 300 million dollars (out of the agreed 1 billion dollars) per month on average for the first six months. In June 2015, following a decisive decision among KRI political leaders, the KRG averred that its oil should be exported independently to Turkey's Ceyhan harbor through a pipeline it shares with Turkey, and without handing it over to SOMO. Aside from the aforementioned amount in 2014 and 2015, there has been no extra transferred money from Baghdad so far. There are also other aspects of the federal budget law, which deals with Peshmerga forces in the Kurdistan Region. Between 2007-2015, all federal budget laws released by the House of Representatives of Iraq have stated that Baghdad should transfer 9.5 billion dollars to the KRG for payroll, armament, and military equipment for Peshmerga forces. Unfortunately, this never took place.

To address the fiscal shock, the KRG introduced short-term austerity measures. This included 42 decrees issued by the KRG Council of Ministers regarding fiscal consolidation, accountability, social reforms and structural reforms. By implementing these reforms, the KRG saved more than 1.7 billion dollars from its original expenditures.⁹

KRG are also deprived from grants and loans of the International Monetary Fund (IMF), World Bank Group and other international organizations. On July 7, 2016, the IMF executive board approved a 5.34 billion dollars-worth Stand-By Arrangement (SBA) for Iraq.¹⁰ It seemed a good idea to financially rebalance Iraq following the several internal and external shocks. However, Iraq did not distribute this money equally among all Iraqis. Unfortunately, the KRI did not receive anything of this SBA. On

⁹ World Bank Group. *KRG Economic Reform Implementation Progress*. 2017. p. ix.

¹⁰ IMF. "IMF Executive Board Approves 5.34 billion dollars-worth Stand-By Arrangement for Iraq." IMF, July 7, 2016. Accessed July 20, 2017. <https://www.imf.org/en/News/Articles/2016/07/07/19/55/PR16321-Iraq-IMF-Executive-Board-Approves-US5-34-billion-Stand-By-Arrangement>.

May 22, 2003, the United Nations Security Council issued Resolution 1483 for the establishment of a Development Fund for Iraq (DFI).¹¹ aiming to collect Iraqi oil revenues. Iraq had to pay back the debts acquired by Saddam Hussein's regime, including a Kuwaiti Compensation Fund, Paris Club, and other debts. The KRI, as part of Iraq, also contributed to paying back these debts. The KRG budget share will be calculated after sovereign expenses (clearing debt is part of this) and governance expenses within the Iraqi budget law. The new debts for Iraq, which do not apply for Kurdistan Region, will be part of general Iraqi debts that Kurdistan Region should contribute to pay back this money in the future.

Moreover, the sharp fall in global oil prices also affected the Kurdistan Region negatively, as its economy is dependent on oil production and exportation. In June 2015, when the KRG began to export oil independently, the oil price was around 60 dollars per barrel. The price declined drastically in January-February 2016 and reached around 30 dollars per barrel,¹² which in turn overwhelmingly affected the entire fiscal and macro-economic realm.

The goal of these reforms was for the KRG to diversify its economy away from its reliance on oil. The focus was on three sectors: agriculture, tourism, and trade. Agriculture is one of the most important sectors that contribute to national income and employment generation. The World Bank has suggested an economic reform roadmap¹³ with policies on agriculture and trade, support for farmers, and a regulatory framework. In addition, it is necessary for the KRG to invest more in water supply, a sanitation system, and irrigation to increase efficiency and recover costs as well. Meanwhile, the tourism sector is gaining more revenues, and also leads to more job opportunity, developing the region, extending relationships with other countries and introducing the Region's culture to those who visit. Regarding trade and industry, the World Bank is said to start a program to assist the KRG Ministry of Trade and Industry to implement some of these projects to grow this sector effectively, especially projects for improving trademarks, intellectual property, industrial zones, State-Owned Enterprises (SOEs) and related issues.

¹¹ Security Council, UN. *UN Security Council: Resolution 1483 (2003)*. 2003. Accessed July 20, 2017. <https://www.iaea.org/sites/default/files/unsc1483.pdf>.

¹² Macrotrends. "Crude Oil Prices- 70 Year Historical Chart". Macrotrends. NA. Accessed July 20, 2017. <http://www.macrotrends.net/1369/crude-oil-price-history-chart>.

¹³ World Bank Group. *Kurdistan Region of Iraq: Reforming the Economy for Shared Prosperity and Protecting the Vulnerable*. 2016.

Due to the large public sector, private sector development should also be subject to focus. In 2014, 53 percent of the total labor force was under the public-sector umbrella.¹⁴ This fact alone shows that the KRG should take further steps towards establishing a vibrant private sector. The largest problem is the mismatch between available skills and private sector needs. The KRG can provide services such as training, seminars and opening new faculties in universities in order to fill these gaps in the future.

According to a joint report prepared and published by the KRG and the World Bank Group titled “Assessing the Economic and Social Impact of the Syrian Conflict and ISIS” in 2015, the stabilization cost for the KRG in regards to IDPs and Syrian refugees equals 1.4 billion dollars for the baseline scenario (IDPs number 1,003,300 individuals and Syrian refugees number 225,000 individuals), 1.8 billion dollars for the low-case scenario (250,000 more IDPs and 30,000 more refugees) and 2.5 billion dollars for the high-case scenario (500,000 more IDPs and 100,000 more refugees). The study analyzed both the macroeconomic and sectoral approaches. The stabilization assessment covers two main pillars: human development and infrastructure. The first pillar includes health, education, food security and agriculture, poverty and shelter sectors. The second pillar is comprised of electricity, transport, solid waste management, and water sectors.

Preliminary estimates show that these crises have direct impacts on all types of investment. Despite declining foreign direct investment (FDI), the vast majority of investment projects in this region were hit hard by the economic crises. These infrastructure projects, which reach 4,000 projects, are no longer funded by the KRG due to the fiscal deficit. The process of non-funding led to high debts towards contractors and investors. This, in turn, led to lost jobs at the same time when poverty was increasing amongst the people of the Kurdistan Region. According to the latest data from the Kurdistan Region Statistics Office (KRSO) the poverty rate had risen to 14 percent from 3.8 percent before the humanitarian crises.

To counter the economic crisis in this part of the world, many steps have been taken. The reforms were announced by the Kurdistan Region Presidency (KRP) on February 10, 2016. This laid the first stone to begin implementing steps gradually, which cut a long way towards a stable financial status. Joint efforts between the KRG Ministry of Planning, the World

¹⁴ World Bank Group. *Kurdistan Region of Iraq: Reforming the Economy for Shared Prosperity and Protecting the Vulnerable*. 2016. p. 7.

Bank and the United Nations (UN) resulted in the launching of an economic reform roadmap on May 30, 2016. The plan focused on fiscal consolidation, structural reforms to strengthen private sector sustainability and inclusiveness, mitigation on the impacts and social sector reforms, accountability, and judicial oversight.¹⁵ Moreover, this roadmap was scheduled for an implementation period of three years. It is also important to mention many other projects produced under the implementation process, including the new procurement regulation Social Protection Strategic Framework (SPSF), Funding Facility for Economic Roadmap (FFER), oil revenue via external audit companies (conducted by Deloitte, and Ernest and Young), biometric system for KRG's payroll, electricity reform plan, Technical and Vocational Education and Training (TVET), among others.

In the light of the reform plan KRG announced, Public-Private Partnerships (PPPs) also play an important role for the new public procurements regulation. PPP refers to a contractual arrangement between two parties, government and private sector so as to provide public assets, public services and infrastructure.

Conclusion

The inflow of IDPs and refugees, the unanticipated budget cuts by Baghdad, Peshmerga fighting against the most dangerous terrorist group in the world, and a global drop in oil prices persuaded the KRG to borrow 1.5 billion dollars from International Oil Companies (IOCs) and another 1.5 billion dollars from internal private sector companies. The KRG began to cut wages and salaries in January 2016, but at the same time, the government promised to pay back unpaid wage bills of public employees.¹⁶

By improving its budgetary process through economic diversification while also carrying out austerity measures, the KRG can once again grow its economy. This can be achieved through implementing the KRG Vision 2020 roadmap and suggestions proposed by the World Bank Group. The KRI is rich in natural resources, has many agricultural lands, consists of a young population, is along an important trade route, and offers a secure environment. If the Kurdistan Region finally gains its long-deserved right to self-determination, the new state could easily overcome the current fiscal issues. Furthermore, independence would allow it to sell oil at the

¹⁵ Ibid.

¹⁶ Ibid., p. 3.

global oil price, issue a new currency, control its monetary policy, issue bonds and trade on international markets, receive loans from international agencies, and accept more from donor countries for its care of IDPs and refugees. KRI's right to independence has been long overdue; it is time, now more than ever, for the KRI to become an independent state.