



IMPACT OF HIGH INCOME FROM “DICTATOR PETROL” ON THE ECONOMY OF THE REPUBLIC OF IRAQ

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Abstract: According to the late Prof. Alexander Fall, “It all began in Mesopotamia, the cradle of human civilization.”

Oil occupies a strategic place in the resource structure of the world economy. The beginning of the modern oil industry is considered to be 1859, when the American settler, oil explorer and entrepreneur E. L. Drake drilled a well for oil production in the state of Pennsylvania (USA).

In the modern world, it is almost impossible to imagine an economy without oil. Already during the First World War, Henri Béranger, the chief commissioner for supplying France with oil, wrote: “He who controls oil will control the world.”

The purpose of this study is to reveal the role of oil revenues in stimulating economic growth and in raising the standard of living of the population in the Republic of Iraq by outlining the main guidelines for overcoming the crisis in the country and by carrying out successful structural changes and solving the complex political and economic problems.

Keywords: Iraq; petrol; political and economic problems.

Introduction

There is no doubt that the countries of the Ancient East marked an economic rise and cultural flourishing too early. The ancient Eastern country of Iraq is distinguished by a broad and comprehensive interpretation of economic processes and problems in the age of transforming the world. Today, for many reasons, in the region of Mesopotamia, it plays an active role of great importance in the process of the country's development, the production of oil, and the revenue obtained from its sales. Oil has been known to humankind since ancient times, from oil spills on the surface of the earth. Egyptologists agree that ancient Egyptians may have been the first to use oil in embalming, and that they covered their inscriptions with their own bitumen to preserve them better. A stone sarcophagus was discovered from the time of the Second Dynasty (after 3700 AD), sealed with bitumen¹.

The first oil well was discovered in 1859. It was dug by Colonel Drake in the state of Pennsylvania, USA².

¹ Д-р Инж. Хамди ал-Бинби, „Петролът и животът“, изд. „Ал-Маареф“, Кайро, 2000 г. (на арабски език).

² Джустурк, „Близкоизточният петрол е енергийната криза“, 1973 г. (превод на арабски език).

“The most valuable piece of real estate in the world“ – this is how US President Dwight Eisenhower defined the Middle East after World War II³ because of the oil. Thanks to it, the region gained extremely strategic importance. Crude oil resources are mainly concentrated in four countries in the Middle East, namely the Kingdom of Saudi Arabia, Iraq, Iran, and Kuwait, which hold 75% of the region’s oil reserves and about 50% of the world’s⁴.

According to the late Prof. Alexander Fall, “It all began in Mesopotamia, the cradle of human civilization.“ After the discovery of vast oil reserves in 1927, Iraq became the world’s leading oil producer and exporter. In 1932, the country was declared an independent monarchy. In 1958, a republic was established.

The latest report by the Iraqi Finance Minister indicated that the rise in oil prices has led to an increase in the Treasury’s deposits with the Central Bank, which provided the government with flexibility in the event of a drop in the price of oil. It also pointed out that the fall in the value of the Iraqi dinar against the dollar has led to a decrease in demand for the dollar. This was reflected in the increase in foreign reserves at the Central Bank of Iraq, which was expected to reach a record level of \$90 billion by the end of 2022. Furthermore, the report explained that one of the most important results of devaluing the dinar was the narrowing of the difference between the nominal exchange rate and the parallel exchange rate, which removed the profit margin for those who exploited the foreign exchange market at the expense of Iraqis.

On the other hand, the report stated that the government has boosted economic recovery through massive liquidity injections, which has provided an impetus for the non-oil economy to witness an increase of 20% in 2021, compared to a contraction of 8% in 2020, and it was expected to grow by about 25% in 2020–2022.

The IMF report revealed that Iraq’s economic growth rate stood at 9.3% and indicated that this growth was the result of high global demand for crude oil and natural gas.

Iraq is a major exporter of crude oil and OPEC’s second largest crude producer after Saudi Arabia, with an average daily production of 4.6 million barrels, of which roughly 3.3 million barrels are exported under normal conditions, according to the report.

Growth Factors

The Iraqi economy has gone through two cycles that witnessed a sharp reversal in economic growth, with the first being negative in 2020 when the GDP declined to -11%, then moving to a positive level.

Positive growth was estimated at 9.3% in the first influential cycle of oil assets, which was represented by an increase in the amount of Iraqi oil produced by more than one million barrels per day. This contributed to an increase in the rate of oil production to about 4.6 million barrels, in addition to crude oil prices increasing by more than 33% compared to 2019.

The second cycle was represented by the non-oil business cycle “through the growth of extraordinary activity in the sectors of transport, digital economy, housing construction and accompanying strong drivers in reconstruction – especially in the liberated areas, – after which the Central Bank of Iraq adopted a policy of facilitating lending to support the housing sector.“ All of these factors, together with construction and lending for youth initiatives, the industry and agriculture, which totalled nearly \$15 billion, contributed to half of the increase in the growth rate.

Various analysts believe that, in addition to boosting oil prices and export levels, Iraq has benefited from the reset of its debts to Kuwait, which previously deducted 3% of the revenue from the sale of Iraqi oil, contributing to the growth of the economy.

Other economic experts add another factor – the depreciation of the Iraqi dinar against the dollar, which has helped the country secure billions of dollars.

³ Дуайт Айзенхауер е 34-ият президент на САЩ в периода 1953–1961 г., армейски генерал, главнокомандващ съюзническите сили през Втората световна война.

⁴ Ал-акбари, Д. О. Близкият изток: петролът и международните отношения, София, 2006 г.

Sustaining Growth

As for the question of how to sustain this growth, the Prime Minister's financial adviser confirmed that there was a financial surplus estimated at between \$15 billion and \$20 billion, represented by the increase in Central Bank reserves and others related to the rise in oil prices. This required work to invest these funds in the next year's budget legislation, especially since it represented 50% of GDP and since there was an investment aspect that supported the development sector in the country.

According to other analysts, there is a need to restore the public sector to stimulate growth in the private sector, which will contribute to the creation of strategic partnerships with foreign direct investment in untapped sectors, such as transport, tourism, and the shift to smart agriculture, as well as industrial and technological cities. They emphasize the need to shift to investing in quality of life and enabling Iraq to have a digital economic environment.

And the recovery in oil prices increases the state's options and its ability to invest some of these revenues in developing non-oil sectors.

Iraq's revenue from oil exports exceeded \$88 billion in the first nine months of 2022, and it was expected to rise by \$120 billion at the end of the year, allowing the government to cover public spending and invest the surplus.

Unreal Growth

While some are optimistic about the economic growth achieved by Iraq, others see it as unstable, which is confirmed by the existence of three types of economic growth, the first of which is automatic growth that occurs in industrialized countries, and the second one is planned growth which the state strives to achieve.

As for the third type, it is "the transitory growth resulting from the quantitative development of the gross domestic product, which is related to an external variable or related to nature or climate, such as oil prices, as in oil-producing countries, including Iraq." This means that when the price of oil rises, the rate of economic growth rises along with it, as there is a direct relationship between the two.

The growth of the Iraqi economy by more than 9% is not real; it does not reflect a specific model of economic development and is not considered a reflection of the development of non-oil sectors, because it depends on the value of oil and its contribution to the gross domestic product; therefore, this type of growth is not taken into account.

1. Estimate of the Iraqi Economy for 2022

The performance of the Iraqi economy can be assessed by looking at the most prominent positive and negative economic events that occurred in 2022 as follows:

First: it is really quite common to talk about positive economic events in the country, such as:

1. Increased Economic Growth

While economic growth was 2.8% in 2021, it accelerated in the first half of 2022 to a record 10.5%, and the World Bank expected it to reach 8.7% by then. It should be noted that this improvement in growth does not reflect the reality of the Iraqi economy, which is driven by rising oil prices amid the Russo-Ukraine war and the start of recovery from the COVID-19 pandemic, both globally and locally.

2. High Oil Prices

As oil prices have risen and crossed the \$100 barrier on average in 2022, this has had a positive impact on Iraq's oil revenues due to the Russian war against Ukraine and to the sanctions that Russia has been subjected to, in addition to the recovery of global economy from the pandemic and to the OPEC+ alliance, which led to a reduction in production quantities.

3. An Increase in Oil Revenues

The Iraqi Ministry of Oil confirmed the achievement of more than \$115 billion for 2022 according to preliminary statistics, noting that the daily rate of exports amounted to approximately 3.32 million barrels per day, bringing the total exported amounts to more than 1.209 billion barrels for the same year.

Despite the achievement of more than \$75 billion in 2021, knowing that the daily export rate is 3,027 million barrels per day, total exports were brought to 1.102 billion barrels per day according to the Ministry of Oil.

4. An Increase in Foreign Reserves

In 2022, foreign reserves increased to their highest value since 1960 by reaching more than \$99 billion. In 2021, these reserves did not exceed \$60 billion, noting that this increase was due to the oil sector and not to other sectors.

An increase in foreign reserves is one of the positive economic developments due to its importance in preserving the value of the local currency, helping the government meet its obligations arising from foreign debt, and limiting exposure to external shocks, especially in light of the difficulty of borrowing and standing up in an emergency.

5. Unconstitutionality of the Oil and Gas Act

When the Federal Supreme Court ruled Iraq's Kurdistan Region Oil and Gas Act, issued in 2007, the latter was unconstitutional and limited oil and gas management to the federal government.

6. Finalization of the Compensation Issue

Iraq managed to pay \$52.5 billion to compensate individuals, companies and governments that proved they had suffered damages as a result of the 1990 invasion of Kuwait.

In 1991, the Security Council passed Resolution 678, requiring Iraq to pay compensation to Kuwait, taken from the total oil revenues according to certain percentages determined by the two Security Council resolutions.

In 2003, the Security Council established the Iraqi Development Fund (IDF) and required the receipt of oil revenues in an account at the Federal Reserve, the function of which is to deduct a share of a certain percentage to put it in a fund controlled by the Compensation Committee, as well as the transfer of the balance to a Treasury account managed by the Central Bank, and from there to other accounts that Iraq opens and disposes of its balances.

On 22 February 2022, the Security Council adopted Resolution 2621 to liquidate and close the compensation account. In fact, the decision was implemented at the end of the year; the compensation issue was closed, and the oil resource was released from this restriction. Thus, it is no longer necessary to receive oil revenues in a single account, whether at the Federal Reserve or anywhere else.

7. Electrical Connection

The foundation stone was laid for the electricity link between Iraq and Jordan to meet the demand for electricity in view of the continued inability of the local generation. Iraq is estimated to produce and import between 19 000 and 21 000 megawatts of electricity, while actual demand exceeds 30 000 megawatts.

8. Reserved Public Funds

The total public funds were retained by the Anti-Corruption Commission, for which recovery orders were issued. The Commission prevented or stopped them from being spent, based on its procedures; they were actually returned to the public treasury account in the first half of 2022, amounting to more than 1.700 trillion dinars (<https://fcds.com/> February 2023, Euphrates Center for Development and Strategic Studies Report Prepared by: Hamid Abdul Hussein Al-Juburi, Arabic language).

In the second half of 2022, the largest theft was revealed, which was defined as the "theft of the century," – \$2.5 billion, which is equivalent to 3.7 trillion Iraqi dinars according to official data of the ministries of finance and oil in the country. This caused public discontent, which led the government and the relevant authorities to trace the details of this theft. Some of those involved were arrested, and no more than 9% (318 billion dinars) of the amount was recovered. This issue is not yet resolved.

In this regard, the question arises as to the extent to which the government of Mohamed Al-Sudani can recover the remaining amount, which is the largest (91%), especially if the investigations prove the involvement of the parties that support him at the local and regional level.

Through the above representation, it is clear that most of the positive results achieved in 2022 did not originate from or were generated by the Iraqi economy; rather, they were driven by external causes, so these positive results cannot be considered something specific to the Iraqi economy.

Second: negative economic events can be systematized as follows:

- Terrorist-financing hotbed – the world views Iraq as a terrorist and militia-financing hotspot; therefore, the country is not allowed to fully dispose of its money;
- Absence of a national sovereign economic decision due to the absence of a nation state in Iraq;
- Lack of a focus on infrastructure and economic diversification;
- Exacerbation of unemployment, poverty, social problems and lack of skill development;
- High inflation and volatile oil prices;
- Release of the administrative apparatus;
- The lack of clarity in the relations between the centre and the region;
- Expanding the base of the black economy in Iraq;
- Economic crime is increasing;
- Enactment of bad laws, the Normalization Act, the Food Security Act and the Work of Councilors Act, which will strain the budget;
- The lack of a budget for 2022 that shows the income and expenses of the state and the restriction of the law on food security, voted by the Parliament on 8 June 2022, which is also not deprived of legal and financial protection;
- An alarming increase in corruption, especially theft by tax officials, which is the largest since the foundation of the Iraqi state (as mentioned above, \$2.5 billion / 3.7 trillion dinars were stolen);
- Modesty of investment through low levels of investment in the budget, which negatively affected the reality of the Iraqi economy;
- The remarkable increase in real estate prices by three times according to some, not in line with the incomes of social segments for many reasons, including corruption, government loans, population growth, family separation, high prices of construction materials, lack of planning, sanctions (Iran) and regional crises (Lebanon);
- The resignation of the Minister of Finance Abdul Amir Alawi; what he mentioned in his resignation represents a negative sign for the reality and future of the Iraqi economy and public finances;
- Finally, the significant rise in the price of the dollar at the end of 2022 and at the beginning of 2023 from 1.460 to 1.600 dinars per dollar, due to the decrease in window sales of foreign currency for administrative and audit reasons, not for dollar shortage reasons, as foreign reserves are at their best. As we mentioned in the pros, some of the reasons can be listed below:
 - There are two types of dollars: a cash dollar used for travel, education, treatment and other purposes, and a remittance dollar used by merchants, which is either a transfer or a documented credit. Due to the shortage of supply of dollars (traders' dollars), traders resorted to buying dollars in cash, causing the price of the dollar to rise;
 - A conversion error: considering the electronic work platform for dollar transfers at the beginning of the current year (2023) and given the novelty of the experience, many errors occur on the part of banks in transfers, and this requires procedures and time to eliminate them; the novelty of the experience contributed to the decline in sales of the Central Bank and to the recent rise in the exchange rate;
 - Some banks are still not ready to enter the automation system and to receive dollars, so they resort to the parallel market, which means an increase in demand and in the price of the dollar;
 - International control of financial transfers to ensure that dollars are not transferred to people and countries loyal to countries that are subject to sanctions, which has led to the rejection of many transfers, a decrease in sales in dollars, a recourse to the parallel market, an increase in demand and in the dollar price. This was evident by the exclusion of four private foreign exchange banks (Al-Ansari, Middle East, Al-Kabid, Asia).

A rise in the price of the dollar can have a range of effects, most notably:

- inflation rise;
- fear of the investor, especially since the import is in dollars;
- the possibility of the Iraqi economy to go into recession.

To deal with rising dollar exchange rates, the Central Bank has taken a range of measures, including:

- preferential pricing for endorsing letters of credit;
- allowing some banks to sell dollars to the public for travel, medical treatment, education and other purposes;
- limitation of purchase and sale operations exclusively in Iraqi dinars.

In my view, the political system in Iraq has not adopted a clear and definite integrated economic course that achieves growth and prosperity for Iraqis through wise and fair programme, but rather has transformed the country's economy into a "dependent economy" abroad.

In conclusion, bearing in mind the differing opinions expressed by many of the economic analysts, in order to have any hope of positive change, the current government with Prime Minister Mohammed Shia Al-Sudani must adopt an ambitious programme to tackle poverty and unemployment by achieving effective private sector participation and the best investment of oil revenues.

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