

# REPUBLIC OF IRAQ

## Key conditions and challenges

Table 1	2020
Population, million	41.5
GDP, current US\$ billion	166.9
GDP per capita, current US\$	4019.5
Lower middle-income poverty rate (\$3.2) <sup>a</sup>	14.8
Upper middle-income poverty rate (\$5.5) <sup>a</sup>	52.4
National poverty rate <sup>a</sup>	22.5
Gini index <sup>a</sup>	29.5
School enrollment, primary (% gross) <sup>b</sup>	108.7
Life expectancy at birth, years <sup>b</sup>	70.5

Source: WDI, Macro Poverty Outlook, and official data.

Notes:

(a) Most recent value (2012), 2011 PPPs.

(b) Most recent WDI value (2018).

COVID-19 repercussions and oil price volatility are deepening Iraq's economic woes. GDP contracted sharply in 2020 driven by a steep decline in oil production and non-oil output. Twin surpluses turned into large deficits in 2020 putting pressure on public debt and foreign currency reserves. Economic outlook depends on oil market developments and reforms implementation. Key risks relate to deteriorating security situation, delayed vaccination rollout and setbacks in oil markets, with severe consequences on poverty and unemployment.

Oil price volatility and the pandemic have amplified Iraq's economic woes, reversing two years of steady recovery. These twin shocks have deepened existing economic and social fragilities, which further added to public grievances that existed pre-COVID-19. The absence of fiscal space has limited the ability of the Government of Iraq (GoI) to provide a stimulus to an economy highly dependent on oil exports for growth and fiscal revenues. As a result, the country experienced the largest contraction of its economy since 2003.

These crises have also impacted the economic welfare of Iraqi households, adding further pressures on unemployment especially among informal workers and those in self-employment. Unemployment remained more than 10 percentage points higher than the pre-pandemic level. Limited fiscal space has impacted transfers, including the universal Public Distribution System and remittances, where the share of households receiving transfers dropped by more than 8 percentage points. The loss of household income and social assistance has increased vulnerability to food insecurity. COVID-19 has also severely limited child learning as evidenced by the small proportion of students engaged in learning activities during school closure. These impacts coupled with reduced access to market and healthcare services

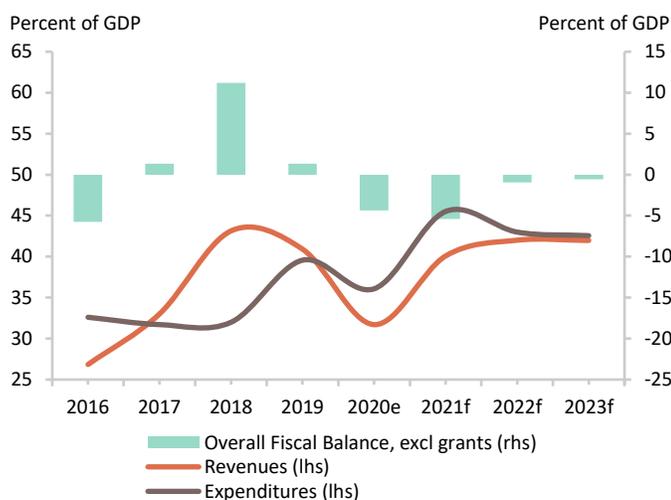
undermine human capital accumulation and economic mobility.

Recognizing the severity of the crisis, the GoI devised a national reform plan (the 'White Paper') that sets out a blueprint of reforms to achieve sustainable medium-term growth. The 2021 budget proposes measures aimed at boosting domestic revenue mobilization and public financial management, as well as announcing an 18.5 percent devaluation of the IQD against the USD. The ultimate success of reforms depends on political will and public support to implement the proposed measures and lead the country out of a long-standing fragility trap. Amid persistently high perception of corruption and weak public service delivery, fiscal consolidation could give rise to social tensions and undermine reform implementation. Other priorities include limiting the spread of COVID-19 and ensuring a quick vaccine rollout to manage the economic fallout from the pandemic.

## Recent developments

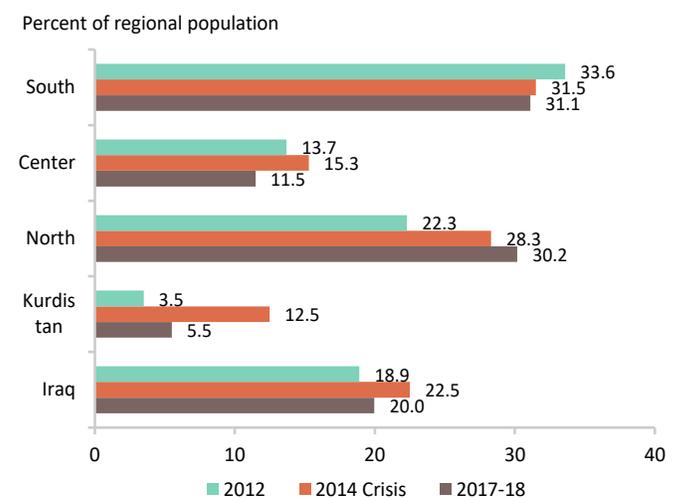
The twin shocks took a heavy toll on Iraq's economy, with GDP (at factor cost) posting a contraction of 10.4 percent in 2020. Growth was weighed down by depressed global oil demand and adherence to OPEC+ production cuts agreement which led to a 17.6 percent contraction in oil GDP. The non-oil economy also underwent a 9 percent contraction as COVID-19 induced lockdown battered domestic demand with religious tourism and services

**FIGURE 1 Republic of Iraq / Fiscal revenue, expenditures, and balance**



Sources: Ministry of Finance; and World Bank staff projections.

**FIGURE 2 Republic of Iraq / Poverty head count rate**



Sources: World Bank staff estimates.

sectors suffering the most. Weak domestic demand and cheaper imported goods kept inflation pressures low with headline and core inflation only edging up to 0.6 and 1.0 percent in 2020, respectively.

Cuts in oil production exerted severe pressures on government finances, with oil revenues—accounting for 92 percent of total revenue in 2019—falling by over 45.1 percent in 2020. The GoI responded through cutting discretionary spending and slashing public investment. To deal with Budget rigidities, especially those linked to the public wage bill and pension, the GoI deferred the regularization of new entrants and contractual workers to 2021 thus accruing wage arrears. Hence, the 1.4 percent of GDP fiscal surplus in 2019 turned into a 4.4 percent of GDP deficit in 2020, raising gross budgetary financing needs to over 6.5 percent of GDP following also a restructuring of domestic debt held by state-owned banks and central bank. This together with the higher value of foreign debt following IQD devaluation also caused central government debt-to-GDP ratio to increase by 21 percentage points to 69.3 percent in 2020.

Lower oil exports led to a worsening of the current account balance, which turned from a surplus in 2019 to a 12.9 percent of GDP deficit in 2020. With net FDI flows at only US\$3.2 billion and limited other foreign borrowing in 2020, CBI

foreign currency reserves fell by almost US\$13.6 billion to cover the gap. This brought reserves coverage to 9.6 months of imports by end-2020 despite a decline in imports.

## Outlook

Iraq's economic outlook hinges on the evolution of COVID-19, global oil markets prospects, and reforms implementation. The economy is forecast to gradually recover on the back of rising oil prices and OPEC+ production quotas. GDP growth is projected to rise to 1.9 percent in 2021 and 6.3 percent on average over the subsequent two years. Delays in vaccine rollout would lead to additional lockdowns, which in turn impact economic activity. Non-oil GDP is forecast to recover in 2021, growing by 5.5 percent before converging to historical potential GDP growth trend in 2022-23.

Economic recovery and mass vaccination will gradually reverse the surge in poverty, projected by 7 to 14 percentage points rise at the national poverty line of IQD110,881 per person per month. The disproportional impact of the shock on the informal sector, dominated by the poor and vulnerable, will worsen inequality. The currency devaluation is estimated

to push inflation to 8.5 percent in 2021 due to limited capacity for import substitution. This will present an additional pressure on households' wellbeing and poverty reduction.

The fiscal stance remains expansionary as the wage bill and pensions are expanded in the 2021 budget law to regularize wage arrears, while reform measures were attenuated in Parliament debate. Higher oil revenues coupled with the devaluation effect are projected to narrow the fiscal deficit to 5.4 percent of GDP in 2021. Financing needs are forecast to remain elevated compared to pre-COVID-19 levels, averaging at US\$13.7 billion/year in the outlook period.

The projected oil recovery will boost exports while devaluation is expected to have an impact on imports. This will also contribute to the current account deficit declining to 4.4 percent of GDP by 2023 and reduce pressures on the central bank's FX reserves. Reforms could help motivate new FDI which could further appease external financing needs.

Sizeable risks cloud the prospects for Iraq's economic recovery over the medium-term. Oil price down cycles, failure to implement fiscal and structural reforms in an election year, delays in vaccine rollout, deteriorating security conditions amidst high regional geopolitical tensions are significant downside risks to the outlook.

**TABLE 2 Republic of Iraq / Macro poverty outlook indicators**

(annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
<b>Real GDP growth, at constant market prices</b>	6.8	2.4	-11.9	1.9	8.4	4.2
Private Consumption	2.3	1.5	-9.0	1.5	8.0	5.6
Government Consumption	17.7	25.2	-10.6	31.5	2.1	1.1
Gross Fixed Capital Investment	-74.2	-16.2	-40.0	5.0	15.0	10.0
Exports, Goods and Services	9.4	2.7	-15.8	1.1	10.3	5.1
Imports, Goods and Services	16.6	28.4	-9.4	15.0	2.0	3.0
<b>Real GDP growth, at constant factor prices</b>	-1.2	4.4	-10.4	1.9	8.4	4.2
Agriculture	12.8	38.8	34.3	14.0	10.0	5.0
Industry	-2.4	3.7	-11.6	2.7	10.2	4.0
Services	0.7	3.7	-12.2	-1.9	3.6	4.5
<b>Inflation (Consumer Price Index)</b>	0.4	-0.2	0.6	8.5	3.8	3.3
<b>Current Account Balance (% of GDP)</b>	10.6	6.1	-12.9	-11.3	-5.6	-4.4
<b>Net Foreign Direct Investment (% of GDP)</b>	2.4	1.5	1.9	1.9	1.9	1.8
<b>Fiscal Balance (% of GDP)</b>	11.9	1.4	-4.4	-5.4	-1.0	-0.6
<b>Debt (% of GDP)</b>	52.4	48.2	69.3	61.1	55.6	52.7
<b>Primary Balance (% of GDP)</b>	13.1	2.6	-3.2	-4.0	0.9	1.7

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.  
Notes: e = estimate. f = forecast.