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ECONOMIC ISSUES IN IRAQ AFTER POST-REGIME CHANGE: INTERNAL POLICY AND EXTERNAL ENGAGEMENT

Key points

Internally

1. To minimise economic disruption following regime change immediate priorities will be food and medical supplies, public finances, and economic institutions. The position in Northern Iraq must not be neglected.
2. If it is politically important to deliver early improvements in economic conditions an expanded food ration looks like the front-runner.
3. There should be an early start on reconstruction/restoration of basic public services. In slightly slower time a new administration will need to develop and work to a comprehensive new domestic economic strategy, with many elements familiar from reform packages elsewhere.

Externally

4. US/coalition forces will have a hands-on economic role early on. For years afterwards the US in particular and the West in general will have great leverage over economic policy.
5. Getting the right flow of external finance to Iraq will be crucial. There are huge competing claims on Iraq's limited foreign exchange earnings: not just reconstruction and development but debt service and compensation payments. External stakeholders – including the US and others prepared to put new money into Iraq – will have to get together to produce a package which reconciles these claims and guarantees Iraq enough funds for reconstruction and development. Creditors and compensation recipients look likely to be squeezed.

Preparation

6. Advance planning for the period immediately after regime change falls to the US. But on all key issues after the initial period – external finance, reconstruction, reform – there will be a need for good information and sound policy analysis from the World Bank and IMF. To avoid lengthy delays later, preparatory work in these institutions should begin as soon as possible.

Scope of the paper

7. This paper, prepared in the FCO, follows on from the papers on post-Saddam issues and on regional consequences already prepared by the FCO's Directorate of Strategy and Innovation. For simplicity it works with one only of the scenarios discussed in the earlier papers: regime change brought about by US-led military action. It focuses on the economic policy issues – for Iraq and the rest of the world – which will then arise. If regime change comes about in another way the economic transition will be different and possibly messier than discussed here, but the big issues will be the same.

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8. It does not look in detail at:

the emergency humanitarian effort which may be the top economic/financial priority immediately after regime change. An internationally funded drive to provide relief supplies, to cope with refugees, and to make emergency repairs to infrastructure and to the oilfields may be required, its scale depending on the amount of new disruption caused by the conflict. This is DFID territory and a big issue in its own right; or

the political, security and institutional context for economic policy making. Economic policymaking and economic development will be vulnerable to any instability which follows regime change. It is assumed that in the early stages following Saddam's removal an externally imposed administration will have to take key economic decisions. But the discussion of medium and longer term policy issues does not prejudice the way in which or the speed at which political and institutional transformation takes place. The form of administration chosen by the UN/coalition victors could make a big difference: a long-term US military administration, for instance, could hope to impose competent expatriate economic leadership relatively rapidly, as in post WW2 Germany and Austria; or

the economic implications for the region.

INTERNAL ECONOMIC POLICY

Economic structure and institutions

9. An incoming administration will inherit a distorted and very badly damaged economy with a number of main and to a large extent separate elements:

- (a) the oil sector: efficiently run under difficult circumstances
- (b) the normal recorded economy, public and private, urban and agricultural: starved of resources, controlled and regulated through reasonably familiar state institutions – Ministries and so on – and mechanisms but with long experience of regime/Ba'ath Party meddling.
- (c) the ration system, an immensely important add-on to the formal economy. Efficiently administered but with again some experience of high level meddling;
- (d) the informal economy in hitherto GoI-controlled Iraq: an unrecorded, unregulated sprawl of trading and services;
- (e) the Northern Iraq economy, with (two sets of) separate institutions and a large NGO presence; and
- (f) the partly secret regime/elite economy, encompassing sanctions evasion and the use of domestic resources and foreign exchange to benefit and protect the elite and to pursue WMD and other aims

10. Economic rejuvenation and sensible policymaking will require that the undesirable parts be stripped out and what remains treated as a unified whole.

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Much of what is required – the purging of undesirable institutions and individuals – is part of the wider political agenda. On the narrowly economic side – in order to minimise disruption and provide the levers for a reformed economic policy – it will be important to preserve the good bits both of essential institutions [the central bank and economic ministries probably still have competent staff below the political appointees] and of necessary evils [notably administration of the ration system – which will be essential in the short term even though it should be eliminated once circumstances permit]. Fairly quick action may be needed to guard against losing competent staff. There will be a need in slower time for new or radically reformed institutions, largely bound up with the management of reconstruction and with the demands of economic reform.

Transition

11. There will be an immediate task of ensuring a smooth economic transition in the early months after regime change. Emergency spending aside, particularly high priority will have to go to preserving food supplies [the ration system having been the backbone of the safety net, the one thing which has prevented mass destitution], in the north as well as the rest of the country, and to effective control of public finances. Both of these are tied in with the future of the oil-for-food arrangements; it will be important to ensure that as these are phased out:

- food supplies for the whole population are maintained. Initially the safest way to do this may well be to keep the existing ration-based distribution system in place, with the main change being to the external procurement arrangements. In parallel it is probably important to give priority (as in postwar Germany under US occupation) to maintaining agricultural production, one sector which has held up tolerably well under sanctions. This means continuing the financial support given (in GoI Iraq) by procurement of domestic production;
- the authorities are able to cope with restored responsibility for substantial flows of foreign exchange [oil earnings have recently been running at an annual rate of \$9-10bn]. Transparent and effective control of public spending by the Ministry of Finance and of exchange arrangements by the central bank – both of whom will have been used to a subservient role under the old regime – will be important

Early economic gains

12. A smooth transition will be a challenge in itself. But to help build popular and regional support for the new administration it may well be necessary to be able to show not just preservation of the economic status quo but some early gains. Depending on the circumstances, emergency humanitarian aid/reconstruction may achieve this objective by itself.

13. If more is needed, the most obvious quick way of doing this would be to provide – through an acceleration of food imports and if possible domestic procurement – a significantly improved food ration, no doubt bolstered with a message about diverting resources from Saddam's extravagances. This would directly benefit every household in the country. Beyond the first 6-12 months

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the focus should turn more to targeting of reconstruction expenditure to achieve political quick wins.

Reconstruction/restoration of basic services

14. Despite heavy investment to benefit the elite, there has been little but emergency investment in most public infrastructure (communications, telecommunications; power; water and sanitation; oil sector; public buildings; state enterprises; public housing) for many years. Public services have suffered in parallel. Even if a new conflict produces little additional damage, the combination of neglect and war damage means that large investments in many areas and spread over many years, are needed if infrastructure and services are to recover even to their pre-1990 condition. Getting this process under way will be essential to economic revival, to the alleviation of humanitarian problems, and to popular support for a new administration.

15. The two big constraints will be finance and implementation capacity. On the former the key will be a workable agreement between external stakeholders which guarantees a reasonable flow of resources to Iraq: see paras 30-31 below. On the latter there will be a need for detailed analysis and planning of the substance, some of which should be set in hand now (see para 35) and also for the establishment of a competent central body within Iraq able to act as the focal point for reconstruction.

Long-term reform strategy

16. Beyond the immediate challenges and in parallel with reconstruction the authorities will have to embark on a long-term process of economic reform designed to create a liberal and dynamic economy. It's easy enough to sketch out what the main elements ought to involve: with some adaptations to the particular circumstances, Iraq needs to adopt a range of measures familiar from many other reforming countries. See Annex 1 for an outline. Decisions on substance are not needed yet, though the World Bank, who are likely to be key interlocutors, need to be galvanised to start thinking about the issues.

Northern Iraq/economic federalism

17. Underpinning all this will need to be a commitment to full and fair integration of Northern Iraq into a federal economic structure.

18. Most obviously this is a question of fairness and institution building on the budgetary side. There will need to be transparent and fair sharing of oil and other budgetary revenues, and a degree of budgetary autonomy for the north underpinned by new budgetary institutions. On the other hand the present situation where Northern Iraq uses a different currency from the rest of the country will have to cease.

19. Northern Iraq's interest will have to be protected in other ways. In the short term its vulnerability to a premature ending of the oil for food arrangements must be recognised, and transitional arrangements acceptable in the North as well as the South agreed. In the longer term central government policies towards agriculture will have to take account of the North's particular dependence on agriculture.

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EXTERNAL ECONOMIC RELATIONS AND WESTERN LEVERAGE

Western leverage: general

20. The US/West will have enormous leverage over every aspect of Iraqi economic policy, not just through forces on the ground but because of Iraq's dependence on external finance and other assistance. In particular:

- US/close allies will not only play the key role in ensuring as smooth an economic transition as possible but - supported by other donors - will be in a very strong position to drive forward reconstruction and the restoration of public services. The funding will be largely external, and a large external input of policy advice and technical assistance may also be required.

This being so, it seems essential for the US/coalition to have clearly formulated ideas on priorities and mechanisms [eg the role for turnkey infrastructure projects to relieve particular bottlenecks]. Funding will be crucial, and can be only be settled in the context of a wider negotiation among stakeholders (paras 30-31).

- Donors/creditors in general are likely to use this leverage to insist on a broadly liberal, private-sector oriented approach to economic policy, within which the Iraqis will be free to determine much of the detail. This should be relatively uncontroversial: it amounts to asking Iraq to follow what is generally accepted as economic best practice. Annex 1 presupposes this.

21. There are dangers in leverage. The US/close allies may use it to favour particular external *commercial* or *economic* interests. Contracts for development of Iraqi oil must be the prime concern, though other lucrative reconstruction-related contracts could well become an issue. So could the financial arrangements for a US-led military occupation, if that was seen to be swallowing large amounts of Iraqi resources. This would be potentially economically damaging: it would mean compromising transparency and competitiveness in tendering in key parts of the economy, jeopardising Iraq's economic interests and setting a bad example to the resurgent private sector. It would also be also potentially divisive, opening the US to accusations of partiality and setting Western countries against one another. We need to think through the extent to which economic requirements be subordinated to political.

Normalisation

22. One of the political prerequisites for economic recovery is normalisation of Iraq's external economic relations. At a legal level this is principally a question of removing the UN sanctions regulations imposing restrictions on trade and financial flows. Given the right sort of regime change the UNSC will be keen to oblige.

23. However removal of sanctions will be bound up with the issue of future arrangements for post-Gulf war compensation. This compensation, administered

through the UNCC (UN Compensation Commission), is at present financed by a prior claim on a percentage of Iraqi oil revenues supervised under the oil-for-food arrangements. It will be necessary to agree on a new *mechanism* for meeting claims once sanctions are lifted and the oil revenues are no longer directly under the UN's control [even though the *rate* at which claims are settled will no doubt become a matter of political bargaining - see below].

24. A second, less contentious constraint on sanctions lift may be the need to ensure a smooth transition from the now well-established distribution plans under which food and other imports are distributed in Iraq. The UN would not want premature abrogation of the arrangements to threaten food supplies.

Oil earnings and external obligations

25. The really difficult external issue to be tackled is the regularisation of Iraq's external financial obligations.

26. The big thing Iraq has in its favour is its oil exports, which even under the straitened conditions of the past few years have been producing gross revenues [handled through the UN] of \$9-15bn pa, or even more when prices were very high. If it had only minor commitments to meet these revenues could form the basis for assured planning.

27. In fact Iraq has actual or potential **obligations** which threaten to swamp the available income from oil: debt service, compensation payments under UNCC arrangements, potential Iranian compensation claims, and even perhaps the costs of a military occupation. See Annex 2 for details.

Grants and loans and the need for co-ordination

28. There is thus a problem. If reconstruction and economic revival are to happen fast enough to make an appreciable difference in a few years, some way has to be found to guarantee sufficient finance for new investment and current spending despite these large commitments and an uncertain flow of oil income. Any figuring on the level of such spending is speculative. Somewhere in the range \$10-20bn pa, excluding oil development, may be a sensible guess (the high point of publicly funded development spending in better times was \$10-12bn per year back in 1980-1).

29. New external assistance will be part of the solution. It may be large-scale: there is talk in the US about a Marshall Plan for Iraq. But it is inconceivable that it could be the whole solution. Donors will not be prepared to put in large sums much of which are immediately used to allow the Iraqis to meet debt and compensation obligations.

30. There therefore needs to be proper co-ordination between external players with a stake in Iraq's economic future. A package needs to emerge which includes

- new bilateral grants or loans [from coalition partners, other Western countries, Gulf countries] and
- multilateral assistance [above all from the World Bank and IMF]

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But as part of the package some nettles will have to be grasped:

- creditors will almost certainly have to recognise the need for exceptional treatment for Iraqi debt – either forgiveness [perhaps with the fig leaf of the new French proposal for MICs] or a rescheduling of interest as well as principal due;
- the disbursement of UNCC compensation will have to be slowed right down;
- if Iran's compensation claim proves serious it will have to be prevailed on to stretch out repayment over many years
- Saudi Arabia and Kuwait will have to acknowledge that their Iran-Iraq era 'loans' will not be repaid

Another possible component of the package – perhaps especially attractive to Russia – could be

- debt for equity swaps

31. There are some very difficult issues here. Initial co-ordination among Western stakeholders ought to start soon, with other major players – Russia, Saudi Arabia and Kuwait – brought into the loop soon. Consulting Iran will be more difficult, partly because of US sensitivities and partly because of the need not to appear to be validating the Iranian compensation claim before it has been formally lodged.

Future investment in Iraq

32. The big prospect for private sector flows to Iraq is investment by international oil companies in upstream oil. Whether the investment comes principally from the Russian, French and other companies with whom the present regime has signed agreements or from others, very large sums could be involved. Industry sources have talked of \$10bn+ over five years, and the present regime of \$20bn+ over a longer period. Signature bonuses apart, the short-term benefit to the balance of payments and to the economy will be limited, since much of the investment will pay for imported equipment and services. The real benefit will come from the additional oil revenues once production expands.

33. The prospects for foreign investment in other sectors will be limited to start with. Expatriate and returning Iraqis may begin to invest in small businesses. If the economic reform programme opens up infrastructure to private investment significant sums might be attracted in due course.

Preparing for change

34. The attached table draws on the foregoing and lists some of the ways in which the UK and others can prepare in advance to support economic development in Iraq.

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35. One particular point is worth stressing. Once regime change occurs there will be a need for good information and sound policy analysis to guide both a whole range of internal policies and the discussions among external stakeholders about finance for Iraq. The institutions best equipped to deliver this - and likely in due course to be major players in Iraq in their own right - are the World Bank and IMF. But neither institution has done any substantive work for many years; if we leave it until regime change has happened to ask them to address the issues there is likely to be a considerable delay before they can produce anything useful. On economic grounds there is a good case for asking senior management in both institutions to put work in hand well in advance of military action: the Bank and Fund could no doubt put together in a matter of months some useful preparatory assessments, even if for obvious reasons they do not work with the present Iraqi authorities. These would at least mean that an incoming new regime, and its friends abroad, would not be flying completely blind on economic matters, and they would set the scene for intensive policy discussions with both institutions following regime change.

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PREPARING FOR CHANGE: POLICY ISSUES FOR THE WEST

issue	external engagement	
	principle	next steps
overarching	better understanding of internal economic position, reconstruction requirements, and economic reform issues	<ul style="list-style-type: none"> • US/UK to commission IBRD and IMF to start preparatory work [no contact with GoI] now, moving to intensive dialogue/assessment post regime change • if this is a non-starter, US/UK to collaborate on analogous work • IBRD, IMF to open Baghdad offices post regime change
economic structure and institutions	<p>economic aspects of federation</p> <p>consult opinion-formers on substance and for talent-spotting</p>	<ul style="list-style-type: none"> • assessment and recommendations based on experience elsewhere • US initiative with expatriates [Future of Iraq Project] underway • scope for parallel initiative with UK-based expatriates?
transition	smooth economic transition, with no avoidable dislocation or erosion of institutional capacity	<ul style="list-style-type: none"> • US should prepare guidelines for military authorities for immediate post-regime change economic management, with focus on food supplies and public finances and on preserving interests of Northern Iraq • IMF study on public finances and macro/exchange policy
early economic gains	to build popular support	<ul style="list-style-type: none"> • assessment of cost and mechanics of expanding food ration, preserving interests of Northern Iraq
reconstruction/restoration of services	<p>preparation for early start</p> <p>conference on strategy</p> <p>external interference: partiality in allocation of contracts/use of budgetary resources</p>	<ul style="list-style-type: none"> • World Bank study on requirements • stakeholder co-ordination on finance [see below] • US should prepare guidelines for early start, covering new institutional arrangements, mechanics • UK could host • potentially sets US against UK need for internal consideration first

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issue	external engagement	
	principle	next steps
long term reform issues	developing a sensible growth-oriented strategy to which new Iraqi administration is committed	<ul style="list-style-type: none"> • IBRD and IMF assessments
sanctions/oil for food	<p>removal of sanctions; transitional arrangements including for oil for food programme</p> <p>satisfactory post-sanctions mechanism for compensation payments</p>	<ul style="list-style-type: none"> • discussions on transitional arrangements with UN Office of the Iraq Programme (OIP) • ?high-level political discussion
external finance: overarching	strategy for reconciling interests of Iraqis and of stakeholders at (a)-(h)	<ul style="list-style-type: none"> • preparatory figuring, initially internal (UK/US) but involving IMF as soon as feasible • co-ordination among stakeholders in advance of decisions on individual elements – scope for early formation of multilateral working groups
external finance: claims on Iraq	<p>(a) commercial creditors to agree on treatment of Iraqi external debt</p> <p>(b) Saudi Arabia and Kuwait to decide whether/how to pursue claims for Iran-Iraq war 'loans' to Iraq</p> <p>(c) UNSC/other stakeholders as appropriate to agree on rate at which compensation claims are paid post regime change</p> <p>(d) Iran to decide whether and how to press claim for Iran-Iraq war compensation</p> <p>(e) promotion of external investment in oil sector</p>	<ul style="list-style-type: none"> • ask Paris Club to produce options paper • assess possibility of debt for [oil] equity swaps – attractive to Russia? • consider relevance of new MIC debt initiative [possible forgiveness] • legal view on status of such claims • sound out Saudi and Kuwaiti governments • ?high-level political discussion
external finance: future investment in Iraq		<ul style="list-style-type: none"> • legal view on prospects of such a claim succeeding? • line to take with Iranians • investigate enforceability of existing Iraqi commitments to Russian and other investors • establish guidelines for future investment [open and transparent tender or political deals] • estimates of likely flows of

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issue	external engagement	
	principle	next steps
external finance: grants and loans	<p>(f) promotion of external investment in infrastructure/other sectors</p> <p>(g) grants/concessional loans from Gulf countries</p> <p>(h) package of new Western and multilateral support to underpin reconstruction and recovery</p>	<p>finance, including up-front payments</p> <ul style="list-style-type: none"> • in due course IMF/IBRD to assess scale of possible flows • sound out Governments in Saudi Arabia and Kuwait [alongside (b)] and in Abu Dhabi and Qatar • in due course ask IMF, IBRD Group, IDB to project scale of their support; consider scope for EU support • plan for donor meeting/Consultative Group asap after regime change
longer term: Iraqi integration in regional/global economy	<p>EU/Iraq co-operation, possibly on EU/Iran model</p> <p>Iraqi co-operation with/possible membership in GCC</p>	<ul style="list-style-type: none"> • put down marker on future EU/Iraq relationship • sound out GCC Governments
oil market	handling a resurgence of Iraqi oil production	<ul style="list-style-type: none"> • cover in multilateral and bilateral [eg UK/Saudi] energy dialogue

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ANNEX 1: DOMESTIC ECONOMIC REFORM

The underlying objective must be to create the conditions for sustainable long-term growth. Key components of the strategy will include the following [not an exhaustive list]:

1. **General issues: good governance and the role of the state:**
 - tackling abuses of power/corruption. The present regime has an appalling record: regime change will provide the opportunity to tackle these issues, which tie in with
 - transparency and accountability in economic decision-making, including the use of budgetary resources;
 - the state should focus on providing the environment in which the private sector can flourish: it should not see itself as the main source of investment or employment decisions
2. **Microeconomic policies** designed to promote economic diversification and a healthy, competitive private sector:
 - (a) general internal and external liberalisation to promote competitive markets. Despite the original Ba'ath stress on extreme economic centralisation, there is something to build on in that the private sector has been given a freer hand under sanctions as the state proved unable to deliver, and in that the informal sector has demonstrated the capacity for small-scale trade and services. Things that need to be done internally include
 - creation of the right regulatory framework and framework of commercial law for private sector activity, backed up by a properly functioning legal system including transparent and fair dispute resolution procedures;
 - open and fair tendering procedures for public contracts – crucial given the role that public spending will play in rebuilding the economy;
 - elimination of state interference in pricing. This is certainly an immediate issue for food and agriculture [see below]; implicit subsidies on petroleum products and utilities are also almost certainly an important issue – as they are in most major oil exporters – which needs to be addressed early on if potentially massive reconstruction investments are not to be misdirected;
 - restriction of the state's role in production/service delivery to public goods and strategic sectors. The oil sector apart, once the abuses of the present elite have been swept away there is not much of a productive state sector in the conventional sense, so privatisation should not be a big issue. The main importance of a new policy stance here will be in facilitating private involvement in reconstruction and delivery of public services. Reconstruction will proceed more quickly, and probably more efficiently, if private capital is welcomed into utilities and infrastructure; delivery of public services will similarly pick up more rapidly – and promote domestic private sector development – if they are contracted out where possible
 - anti-monopoly and other measures to promote competition;

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- liberal labour market rules. Often a contentious issue in other reforming countries, but Iraq may have a chance to get the rules right at the outset
- encouragement of a diversified financial sector. Banking will be the first priority; the obvious short cut to an efficient sector able to play its part in financing development is to open the door to foreign banks. Amman-based Arab Bank, to take the most obvious regional example, could probably hit the ground running. As elsewhere, a market in Government debt could help lay the basis for broader financial market development, as well as providing a conduit for monetary policy

externally there need to be

- liberal trade arrangements with as wide a range of countries as possible, with any protection for special cases transparent and time-limited. This will be important for ensuring competition;
 - a level playing field for foreign investment; and
 - a single exchange rate and a transparent rule-driven exchange regime which leaves no scope for administrative decisions about access to foreign exchange
- (b) policies towards specific sectors which balance strategic and social interests against the demands of efficiency:
- the oil sector will remain fundamental to Iraq's prosperity for the foreseeable future. The authorities may wish to place restrictions on foreign ownership of oil and/or insist on a strategic role for the publicly-owned national oil company [both are the case, for instance, in Saudi Arabia]. But they will need to be sure that these constraints – and the tax regime on oil production – are not so tightly drawn that the exploitation of the oil is hindered by lack of foreign investment. Like other OPEC countries they will need to find a middle way.
- Oil production and export *strategy* within OPEC – not really a reform issue – will of course be of great importance. As Iraq builds up oil production it may well emerge as clearly the second most important player in OPEC after Saudi Arabia, and one – like Saudi Arabia – with a real strategic choice between constrained production/high prices and high production/low prices. Concerting strategy with the Saudis over oil market strategy may become a key part of Iraqi policy;
- agriculture: a major employer, and the main employer in fertile, rain-fed Northern Iraq. In GoI-controlled Iraq agriculture has kept going during sanctions partly as employer of last resort [with people moving back to the land] and partly thanks to support through high procurement prices; but with little recent investment yields have fallen and the sector will probably be vulnerable post regime change. Some state support for agricultural restructuring may – exceptionally – be appropriate; a strategy based on a hard assessment of commercial viability will need to be developed
- (c) a social safety net to protect the weakest. At present the food ration system really merits the safety net description: it provides an otherwise very poor population with just enough to keep going. But it is an

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expensive and indiscriminate way of providing support and hugely distorts the market in foodstuffs. It needs to be phased out and replaced with more efficient and less expensive targeted support, possibly through cash payments to the poorest [the infrastructure of the ration system may make this easier]

- (d) development of human resources through education, training, and support for the return of skilled migrants. Before the Iran-Iraq war Iraq had one of the best-educated and trained populations in the region. Much of this human capital has been lost through the atrophying of the education system and the emigration of skilled and professional workers. After regime change there may well be shortages of skilled labour side by side with large scale unemployment of unskilled workers; it may make sense to provide incentives for the return of well-qualified emigrants

3. **Sound public finances** and a **sustainable balance of payments**:

- (a) proper control and prioritisation of public spending, within a newly established federal budgetary framework. A major early objective will be to consolidate public finances so that presently off-budget activities – to the extent they are not simply wound up following regime change – become fully on-budget;
- (b) diversification of revenues to reduce dependence on oil. For practical purposes, this is for the long term ;
- (c) overall control of the budget to avoid excessive deficits;
- (d) monetary policy, conducted through interest rates initially and in due course through central bank intervention in financial markets rather than administrative control of credit, focused on control of inflation;
- (e) a unified national currency [viz no separate currency in the North] and an exchange rate policy which takes due account of balance of payments requirements.

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ANNEX 2: CLAIMS ON IRAQ'S FOREIGN EXCHANGE EARNINGS

There will be inescapable commitments to:

- continue making compensation payments to post-Gulf war claimants. The figures are enormous. There are \$181 billion of claims still to be processed [on top of a reported over \$25bn of agreed but unpaid claims]. If past experience is anything to go by, the \$181bn could translate into c\$40bn of actual awards to claimants – potentially enough to tie up a quarter of oil revenues for a decade or more if revenue was hypothecated at the same rate as in the past
- service longstanding external debt. The Iraqis themselves acknowledged \$42bn of external debt in 1991, in the aftermath of the Gulf War. This debt is to a mixture of creditors: Western [around 60% of the total, with Japan and France the biggest creditors in this group], Russia [ex-Soviet official: around 20% of the total], and former Soviet bloc and developing country [another 20%]. It has not been serviced at all since the Gulf War, and with accumulated interest may now be worth around twice the original figure. Without some form of debt relief, meeting the annual interest costs alone – no repayment – might now cost Iraq \$5bn pa or more;

in addition to these incontrovertible debts are the amounts (c\$35bn at the time) provided by Saudi Arabia and Kuwait to support Iraq during the Iran-Iraq war. Although Saddam was on record at one point as intending to repay these, the usual Iraqi line is that these were grants not loans. Since they were almost certainly not properly structured commercial loans the Saudis and Kuwaitis may not be able to enforce their claims. The significance probably lies more in their use as a bargaining chip.

On top of this there are potential commitments to

- Iran, by way of compensation for the Iran-Iraq war. The Iranians have recently reaffirmed that this is a live issue (Tehran telno 301). In the past they have claimed \$100bn or more – so potentially this is another huge prior claim on Iraqi resources;
- paying for a military occupation. The potential costs of a war and occupation are already a sensitive issue in Washington. One estimate puts the annual cost of occupation at \$16bn. With no Gulf War-type burdensharing in prospect, the US might be tempted to defray some of its occupation costs from Iraqi resources.

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