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2. Sarah* grateful y you can liaise with FIO/ Baghdad



Alison B
What is D Asquith's
view of this
approach?

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Simon
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adv draft
reply
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11 July 2007

Dear Simon:

IRAQ: PRIME MINISTER'S ECONOMIC INITIATIVE

Nick Banner's letter of 5 July to Stephen Hickey refers. I attach a draft letter for the Prime Minister's signature, setting out a number of options which the Prime Minister may wish to encourage PM Maliki to consider. We judge these are the areas on which, with the support of the UK and other donors, the Iraqis could begin to make progress on economic reform. These areas also accord with the Prime Minister's desire, as stated recently, to take forward work on the economic development of Iraq.

However, there are no silver bullets. Progress on economic development in Iraq is fundamentally dependent on two things: reducing violence and much greater political leadership from the Iraqis. The high level of violence increases the risks to investment, forces skilled labour to migrate; distracts government from effectively managing the economy and promotes corruption and criminal activities. In addition, the Iraqi government needs to recognise that economic management is a key strategic issue and needs sustained and concerted high level political attention. To date this has not happened.

The onus rests with the Government of Iraq. It has the resources to fund much of the necessary investment itself (some \$33 billion in 2007) but lacks the political leadership and technical capacity to do so. The Government of Iraq is consistently failing to spend in its budget. In 2006, the Government of Iraq spent only two-thirds of its total budget, according to the Iraqi Ministry of Finance. Capital spending was particularly poor. For example, despite receiving over 50% of the overall capital budget allocation, the Ministry of Oil only spent 3%.

We are helping – both through our own programmes and by leveraging others, in particular the World Bank. However, in a highly insecure operating environment, where we have increasingly limited access, we need to be realistic about what is possible for international actors, including HMG, to actually deliver.

To that end, DFID is focusing on where it can add most value: providing high-level

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policy advice and technical assistance to help the Iraqi Government effectively manage and spend its own considerable resources to deliver public services. DFID's programme emphasises the importance of Iraqi leadership, and of a genuine demand for assistance

We have made some progress. DFID's Economic Reform Programme has been instrumental in supporting early reforms, including, together with HM Treasury, securing the first IMF programme which has been critical in maintaining macro-economic stability in Iraq. Together with FCO, we have worked hard to get a World Bank presence in Baghdad. We are working closely with the Iraqi Government and World Bank on a variety of issues - fuel subsidy reform, improving macro-economic forecasting, 2007 budget implementation and 2008 budget preparation (including investment budgeting). And, through the Basra Provincial Reconstruction Team, we are enabling Iraqi funds to flow from Baghdad to the provinces. Our work directly supports the Government's implementation of its own reform commitments set out in the International Compact for Iraq.

Against this backdrop, our proposals are based on where we think there is further scope to do more. These are proposals that we judge can be delivered, provided there is the support of both PM Maliki and other senior Iraqi figures. Furthermore, we do not need to be doing everything ourselves. We should continue to try leverage the role of others, in particular the World Bank and the IMF, and increase the efficiency and quality of the very large amount of international assistance already being provided. Finally, we should also avoid over-loading the system. Given the limited capacity of the Iraqi Government, we need to prioritise.

I am copying this letter to Sir Gus O'Donnell, Margaret Aldred (Cabinet Office), Stephen Hickey (FCO), (MOD), (HMT), Dominic Asquith (Baghdad) and Richard Jones (Basra).



Howard Taylor
Principal Private Secretary

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