

## Iraq: Deadlock and demos

Florence Eid-Oakden, Ph.D, Chief Economist  
Charlene Rahall, Senior Analyst  
Leila Lajevardi, Analyst

- Finding a new Iraqi government is at an impasse and will be for the foreseeable future following the former prime minister-designate's resignation on 1 March, hours after he failed to get his Cabinet approved by the parliament.
- We see Iraq stuck in a cycle whereby another appointed prime minister is likely to choose a Cabinet that meets the demands of the political establishment, Iraq's clerics and proxy-power Iran, but not those of the protesters for change.
- Coronavirus (COVID-19) is a major threat to the Iraqi economy, particularly via its impact on the dominant, China-focused oil trade. Saudi Arabia's sudden move to flood oil markets -- sinking the price of oil -- could deal a serious blow to economic growth.

### Political impasse threatens stability

Forming a new government is not in the immediate cards with no agreement in the Council of Representatives (parliament), no prime minister-designate expected to be successful in the near-term, and protests against the old way of doing things continuing.

- Before resigning, Prime Minister-designate Mohammed Tawfiq Allawi tried to create a Cabinet that answered to protesters' demands for the overhaul of the Muhasasa system under which Iraq has been run.
  - A quota system, it divides up power between the major political parties that represent Shi'as, Sunnis and Kurds.
  - There are unwritten rules about how this should happen -- the Kurds tend to get the finance ministry, the Sunnis the defence ministry and the Shi'as the interior ministry.
- Allawi tried to appoint candidates who were not from these political groups and, therefore, not beholden to their interests, a move that was not accepted by the establishment.
  - In the meantime, Adil Abdul-Mahdi, the caretaker PM who would otherwise have resumed the role following Allawi's withdrawal, voluntarily surrendered his responsibilities to his deputies.
  - While this averts a constitutional crisis, it complicates the political situation in Iraq even further.
- Additionally, both the oil and electricity ministers are expected to be replaced, which adds to the instability and raises concerns over reforms in the energy sector
  - It may leave the oil ministry leaderless at a time when the price of crude has tumbled due to the supply glut that has been exacerbated by Saudi Arabia's slashing its selling prices for April.

Table 1 - Iraq Macroeconomic Indicators<sup>1</sup>

	2016	2017	2018	2019	2020f
Real GDP Growth (%)	15.2	-2.5	-0.6	3.4	4.7*
Crude Oil Production (M bpd)	4.6	4.5	4.4	4.6	4.8
Oil GDP Growth (%)	24.6	-3.5	-1.3	1.3	10.0
Non-oil GDP Growth (%)	1.3	-0.6	0.8	5.4	5.0
CPI Inflation (%)	-1.5	0.2	-0.1	2.0	2.0
Fiscal Balance (% of GDP)	-13.9	-1.6	7.9	-4.1	-3.5
C/A Balance (% of GDP)	-8.3	1.8	6.9	-5.2	-4.2
Total Gov't. Gross Debt (% of GDP)	64.2	58.9	49.3	51.4	50.5
Total Gross Extn'l Debt (% of GDP)	38.1	36.0	30.4	32.1	30.9
Gross Official Reserves (Mos. of Imports)	7.8	7.3	8.0	6.8	6.2
Nominal GDP (USD B)	175.2	195.5	224.2	224.1	241.5
Population (Millions)	37.2	38.2	38.4	39.3	39.5

- Iraqi President Barham Salih has begun consultations with representatives from parliament to choose a new candidate for prime minister.
  - He must present a nominee within 15 days of Allawi's 1 March resignation.
- Salih intends to propose intelligence chief Mustafa al-Kadhimi as prime minister, but it is unlikely that he will be accepted or even, perhaps, agree to the idea.
  - When Kadhimi was floated as a potential candidate last year, he declined.
- Protesters are backing Alaa al-Rikaby, a pharmacist who has emerged as a prominent activist from Nasiriya and who has no party affiliation.
- Another outcome could be snap elections which both the protesters and political blocs support. The problem is that electoral redistricting needs to be achieved first.
  - The government has met some of the protesters' demands by approving an electoral law which replaces the voting for lists of candidates via party groups and instead replaces it with voting for individuals.
  - The law, however, does not explain how voting districts will be formed or who will designate them. This would delay the chance of any elections soon. Even if there is agreement, it would take time.
- We expect the protest movement to continue to place pressure on the government.
  - Despite the rapid spread of COVID-19 in Iraq, protesters have maintained a steady presence in Baghdad and other areas, with no sign of scaling back their rallies.
  - More than 500 people have been killed and 30,000 wounded since the protest movement began on 1 October 2019 in Baghdad.

<sup>1</sup> Arabia Monitor; IMF.

\* Subject to downward revision.

## Vulnerable economy: first the virus, now oil

Seventy-nine cases and eight confirmed deaths from COVID-19 (as of 12 March) have not kept Iraqi protesters off the streets. But the virus is a major threat to the Iraqi economy, particularly via its impact on the dominant, China-focused oil trade. Saudi Arabia's sudden move to flood oil markets -- sinking the price of oil -- could deal a serious blow to economic growth.

- Iraq is China's third-leading source of oil (after Saudi Arabia and Russia). With oil revenues making up about 90% of the Iraqi budget, any severe drop in crude exports would be devastating to GDP.
  - Iraq has limited fiscal margin to cope with the impact of lower oil revenue from either the lower price or a virus-related drop in demand.
  - The impact could mean payment delays to international oil companies, and, if the situation worsens, delayed payment of public salaries -- which would be bound to stoke further public anger and increase anti-government protests.
    - It would particularly take a toll on the autonomous (and sometimes separatist) Kurdistan region.
  - Even though Iraq boosted oil sales to China by a third in February, most shipments bound for China are arranged at least a month in advance, meaning any direct impact from COVID-19 on Iraqi oil flows to China would only start to reflect in March data.
  - The Sino-Iraqi oil relationship also involves a deal where Baghdad supplies Beijing with 100 Kb/d of oil in exchange for infrastructure projects to be executed by Chinese firms in the country. We will be analysing the impact as data comes in. But if Chinese demand reduction is short-lived, this could be a major respite for Iraq.
- The government's latest response to coronavirus (on 6 March) included an entry ban on travellers coming from France and Spain, bringing the total number of countries on its entry-ban list to 11.
- Since 8 March, Iraq also halted border trade with Iran and Kuwait to curb the spread of the virus.
- On 1 March, Turkey also closed its only border crossing with Iraq -- the Habur crossing -- endangering the livelihoods of millions of people doing business on both sides of the border. Iraq-Turkey trade would also be severely hit.
  - Those most affected will be Turkey's Kurdish-minority in the southeast, an impoverished, conflict-torn region that borders Iraqi Kurdistan.
  - Habur is Turkey's second-busiest border crossing, and Iraq is Turkey's third-largest buyer of its goods.
  - Total bilateral trade between Iraq and Turkey stood at a 10-year high of USD 12.9B in 2019, with 80% of this being Turkish exports to Iraq.
  - Turkey exports food, textile and construction materials to Iraq, while the country imports oil and petroleum products from its southern neighbour.

Figure 1 – Iraq Oil Exports Mb/d<sup>2</sup>

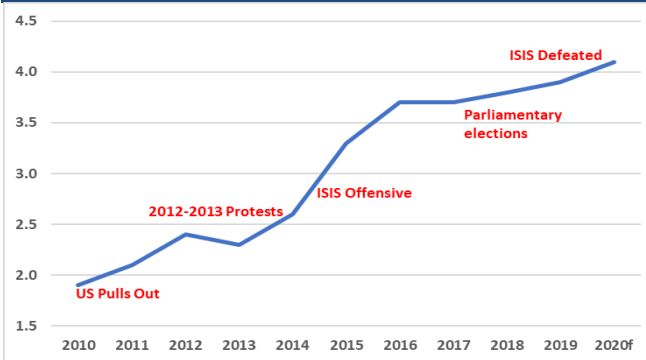
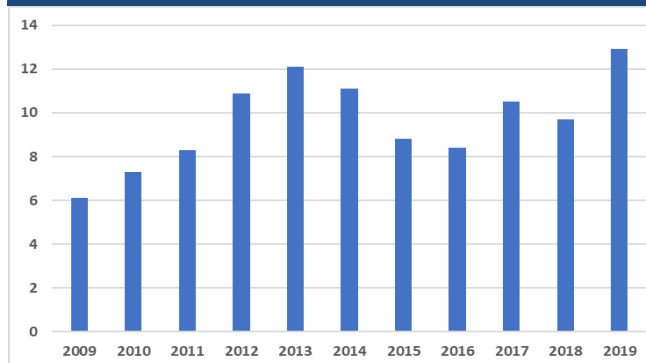


Figure 2 – Iraq-Turkey Trade (USD, B)<sup>3</sup>



The IMF currently expects Iraqi growth to pick up to 4.7% in 2020 from 3.4% in 2019 and a 0.6% contraction in 2018. We believe these figures will now be revised downwards significantly given the political impasse, the impact of coronavirus on trade, and the new, lower oil price.

- Protests have targeted key economic and oil infrastructure, threatening overall economic activity, oil exports and food imports.
  - The longer the government formation process continues, the more damage this would cause to overall economic activity, eventually delaying the progress of major projects.
- Lower oil prices and exports would cause the fiscal and current account balances to remain in a deficit, and international reserves to decline in 2020.
  - Iraq's break-even oil price is around USD 60 a barrel; after Saudi Arabia's move, the global price is in the USD 30 - USD 35 range.
  - However, Iraq can take advantage of the current situation by releasing excess supply into the market.
    - Iraq had about 9 million barrels of crude oil in stock as of December 2019 (less than 3 days' exports).
    - In Qamar Energy's estimate, they could ramp up production from state-operated fields by about 350 Kb/d. Nominal export capacity is about 4.7 Mb/d, but it never operates at these levels. Federal exports were 3.4 Mb/d in February and the peak has been 3.7 Mb/d.

<sup>2</sup> Arabia Monitor; OPEC.

<sup>3</sup> Arabia Monitor; IMF Direction of Trade Statistics.

## Disclaimer

© Arabia Monitor 2020

This is a publication of Arabia Monitor Limited (AM Ltd), and is protected by international copyright laws and is for the subscriber's use only. This publication may not be distributed or reproduced in any form without written permission.

The information contained herein does not constitute an offer or solicitation to sell any security or fund to or by anyone in any jurisdictions, nor should it be regarded as a contractual document. Under no circumstances should the information provided on this publication be considered as investment advice, or as a sufficient basis on which to make investment decisions. The information contained herein has been gathered by AM Ltd from sources deemed reliable as of the date of publication, but no warranty of accuracy or completeness is given. AM Ltd is not responsible for and provides no guarantee with respect to any of the information provided herein or through the use of any hypertext link.

**Arabia Monitor** is an independent research firm specialised in economic and market analysis, and strategy advisory on the Middle East and North African region, which it views as the new emerging market. Arabia Monitor's in-depth, locally informed analysis by Arab, Persian and Chinese speakers has placed it consistently ahead of the curve in identifying new trends within and around the region, and understanding its geopolitics.

**Arabia Advisors** specialises in portfolio strategy and private placements. It works with firms, family offices and government related organisations that are looking to streamline, re-balance or diversify their asset portfolios. Based in the UAE as an off-shore company, Arabia Advisors services a regional and international client base with interest in the Arab countries.

**Arabia Monitor**  
Aston House | Cornwall Avenue | London L3 1LF  
Tel +44 203 239 4518  
[info@arabiamonitor.com](mailto:info@arabiamonitor.com)  
[www.arabiamonitor.com](http://www.arabiamonitor.com)