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IMF Executive Board Approves First Ever Stand-By Arrangement for Iraq

The Executive Board of the International Monetary Fund (IMF) today approved the institution's first-ever Stand-By Arrangement for Iraq, which is designed to support the nation's economic program over the next 15 months. The IMF arrangement, for an amount equivalent to SDR 475.4 million (about US\$685 million), is being treated as precautionary by the Iraqi authorities.

Iraq, a founding member country of the IMF, received its first-ever loan from the Fund in September 2004 through Emergency Post Conflict Assistance ([see Press Release No. 04/206](#)). The initial credit was designed to facilitate Iraq's negotiations with its Paris Club creditors over a debt-restructuring agreement that is now in place, and to support the nation's economic programs through 2005. Approval of the Stand-By Arrangement is a condition for the second stage of debt reduction agreed with Iraq's Paris Club creditors.

Following the Executive Board's discussion of Iraq, Mr. Takatoshi Kato, Deputy Managing Director and Acting Chair, said:

"The Iraqi authorities were successful in promoting macroeconomic stability in 2005, despite the extremely difficult security environment. Economic growth was modest, following the strong rebound recorded in 2004, and inflationary pressures moderated, although prices remained volatile. The Central Bank of Iraq built up reserves and the exchange rate remained stable. The projected fiscal deficit is much lower than expected under the EPCA-supported program, mainly due to higher than projected export prices for crude oil. On the other hand, because of security concerns and capacity constraints, the implementation of structural benchmarks specified in the EPCA-supported program was slower than envisaged.

"The authorities' program for 2006 aims to allocate resources towards the planned expansion of the oil sector, redirect expenditures away from general subsidies towards providing improved public services, and strengthen administrative capacity. The program, which envisages an increase in economic growth, a reduction in inflation, and an increase in net international reserves, maintains a focus on macroeconomic stability, while improving governance and advancing Iraq's transition to a market economy.

"A critical component of the overall strategy is to contain expenditures within revenues and available financing, by prioritizing expenditures, controlling the wage and pensions bill, reducing subsidies on

petroleum products, and expanding the participation of the private sector in the domestic market for petroleum products, while strengthening the social safety net.

“The authorities have recently increased prices of refined petroleum products and will need to press ahead with other structural reforms, including measures to enhance the efficiency and transparency of public financial management and the development of a comprehensive restructuring strategy for the state-owned banks. At the same time, the Central Bank of Iraq aims to establish a modern payments system, implement modern supervisory frameworks, facilitate the proper functioning of foreign exchange and money markets, and conduct a monetary policy geared to ensuring financial stability.

“The medium term outlook for Iraq is favorable, but subject to many risks. A strengthening of the security situation will help the authorities to implement the program. Moreover, Iraq remains vulnerable to shocks, particularly those relating to oil production development and oil export price movements,” Mr. Kato said.

Background and 2006 Program Summary

The Stand-By Arrangement is intended to support Iraq’s economic program for 2006. The authorities’ policies under the Emergency Post Conflict Assistance (EPCA) have succeeded in promoting overall macroeconomic stability despite the extremely difficult security environment. Economic growth in 2005 is estimated at 2.6 percent, following a rebound of almost 50 percent in 2004. Inflationary pressures have moderated in 2005, though prices remain volatile.

Iraq’s projected fiscal deficit in 2005 is much lower than expected under the EPCA-supported program, which is mainly due to higher than projected export prices for crude oil. The Iraqi dinar’s exchange rate has remained stable at about ID 1460-1480 to the U.S. dollar, and the international reserves of the Central Bank of Iraq (CBI) have continued to increase.

Implementation of structural benchmarks specified in the EPCA-supported program was slower than scheduled, and Iraq’s commitment to increase domestic fuel prices of refined petroleum products was not implemented.

For 2006, the authorities aim to strengthen administrative capacity, allocate resources towards the planned expansion of Iraq’s oil sector, and to redirect expenditures away from general subsidies towards providing improved public services. The IMF-supported program envisages an acceleration of economic growth to 10 percent in 2006, and a reduction in the rate of inflation to around 15 percent. Net international reserves of the CBI, which stood at about US\$8.7 billion at the end of September 2005, are expected under the program to increase further in 2006

Iraq’s fiscal stance in the near term will be driven by reconstruction needs, subject to constraints on financing. The primary fiscal deficit in 2006 is projected to be about 8 percent of GDP, following of deficit of nearly 11 percent of GDP in 2005. Over the medium term, and as reconstruction needs subside, the government’s fiscal deficit should gradually decline to zero. To begin the process of appropriate fiscal adjustment and to meet previous commitments to the Fund, the Iraqi authorities have increased domestic prices of all refined petroleum products.

In addition, an audit of the Central Bank of Iraq has reached an advanced stage, which was another pre-condition for the IMF Executive Board’s consideration of the Stand-By Arrangement.

Iraq joined the IMF on December 27, 1945. Its quota is SDR 1.188 billion (about US\$1.71 billion), and its outstanding obligations to the Fund as of November 30, 2005 is SDR297.1 million (about US\$428.12 million).

Table 1. Iraq: Selected Macroeconomic Indicators, 2004–06

(Quota: SDR 1188.4 million)

(Population: 27.1 million)

(Per capita GDP, 2004: US\$ 942)

(Poverty rate: 7 percent; 2004) 1/

| | 2004 | | 2005 | | 2006 |
|--|---|--------|--------|-------|----------|
| | EPCA | Actual | EPCA | Est. | Proj. 2/ |
| Oil and gas sector | | | | | |
| Total exports of oil and gas (in billions of U.S. dollars) | 16.5 | 17.8 | 17.6 | 22.8 | 28.7 |
| Average crude oil export price (in U.S. dollars/barrel) | 30.4 | 31.6 | 26.0 | 43.1 | 46.6 |
| Crude oil production (in millions of barrels/day) | 2.1 | 2.0 | 2.4 | 2.0 | 2.3 |
| | (Annual percentage change) | | | | |
| Output and prices | | | | | |
| Real GDP | 51.7 | 46.5 | 16.7 | 2.6 | 10.4 |
| Consumer price inflation (end-of-period) | 7 | 32 | 15 | 20 | 15 |
| | (In percent of GDP) | | | | |
| Investment and saving | | | | | |
| Gross domestic investment | 34.9 | 26.5 | 44.8 | 29.1 | 29.0 |
| <i>Of which:</i> non-government | 8.5 | 4.3 | 7.4 | 3.5 | 2.4 |
| Gross national savings | 17 | -10.2 | 26.6 | 14.7 | 26.1 |
| <i>Of which:</i> non-government | 33.4 | 28.9 | 16.9 | 0.1 | 8.5 |
| | (In percent of GDP) | | | | |
| Public Finances | | | | | |
| Government revenue (including grants) | 90.6 | 80.0 | 97.7 | 93.6 | 96.2 |
| Oil revenue | 76.7 | 69.6 | 74.6 | 67.8 | 72.9 |
| Expenditure | 133.5 | 120.6 | 125.4 | 104.5 | 105.3 |
| Current | 107.1 | 98.3 | 88.0 | 78.9 | 76.2 |
| Capital | 26.4 | 22.3 | 37.4 | 25.6 | 25.3 |
| Budget balance (including grants) | -42.9 | -40.5 | -27.7 | -10.9 | -9.0 |
| Primary fiscal balance | -41.9 | -39.6 | -27.3 | -10.8 | -8.2 |
| Non-oil primary fiscal balance | -103.7 | -88.4 | -80.5 | -57.1 | -62.8 |
| | (Annual percentage change unless otherwise indicated) | | | | |
| Monetary sector | | | | | |
| Gross central bank foreign exchange assets/base money (in percent) | 68.0 | 94.4 | 75.0 | 98.8 | 99.2 |
| Claims on banks/base money (in percent) | 6.5 | 0.1 | 5.7 | 0.1 | 0.1 |
| Base money | 117.0 | 116.9 | 32.8 | 12.9 | 20.6 |
| Currency issued | 118.4 | 74.9 | 32.8 | 20.7 | 24.2 |
| | (In percent of GDP, unless otherwise indicated) | | | | |
| External sector | | | | | |
| Imports of goods | -102.6 | -76.2 | -104.9 | -73.6 | -67.7 |
| Merchandise trade balance | -24.3 | -7.0 | -32.4 | -4.9 | 1.1 |
| Overall external balance | -4.8 | 6.1 | -14.9 | 4.2 | 4.0 |
| Foreign Direct Investment 3/ | 0.9 | 0.8 | 1.2 | 0.9 | 0.7 |
| Total external debt 4/ | 588.2 | 308.6 | 541.3 | 154.3 | 125.2 |
| Current account (in percent of GDP) | -17.8 | -36.8 | -18.2 | -14.4 | -2.7 |
| Central banks gross reserves (in millions of U.S. dollars) | 5,691 | 7,902 | 8,353 | 9,311 | 11,013 |
| In months of imports of goods and services | 2.6 | 3.2 | 3.7 | 3.1 | 3.6 |
| Memorandum Items | | | | | |
| Nominal GDP (in billions of U.S. dollars) | 21.1 | 25.7 | 24.3 | 33.2 | 41.7 |
| Unemployment rate 1/,5/ | ... | 11 | ... | ... | ... |
| Local currency per U.S. dollar (period average) | 1,500 | 1,460 | 1,500 | ... | ... |

Source: Staff estimates and projections.

1/ Iraq Living conditions survey 2004, UNDP, and ministry of planning and development cooperation. However, the survey notes that 96 percent of households receive food rations.

2/ Tentative projection, based on SBA medium-term framework.

3/ Estimate for 2004.

4/ Data for EPCA are prior to Paris Club agreement of November 21, 2004.

5/ Other estimates range from 28 percent (ministry of planning) to 70 percent (Baghdad University).