



National Development Strategy  
2005-2007  
June 30th 2005



# NATIONAL DEVELOPMENT STRATEGY

2005-2007



JUNE 2005

# Iraq's National Development Strategy

---

## CURRENCY AND EQUIVALENT UNITS (As of April 30, 2005)

Currency Unit= Iraqi Dinar  
US\$1= 1,500 ID

## WEIGHTS AND MEASURES Metric System

## ABBREVIATIONS AND ACRONYMS

Bcf	Billion cubic feet
BCG	Baghdad Coordination Group
CBI	Central Bank of Iraq
CIC	Council for International Coordination
CPA	Coalition Provision Authority
EPCA	Emergency Post Conflict Assistance
GDP	Gross Domestic Product
ICSD	International Center for the Settlement of Disputes
IMF	International Monetary Fund
IRFO	Iraq Reconstruction Forum
IRFFI	Iraq Reconstruction Fund Facility for Iraq
ISRB	Iraqi Strategic Review Board
ITG	Iraqi Transitional Government
IIG	Iraqi Interim Government
ISF	Iraqi Security Forces
NDS	National Development Strategy
MW	Megawatt
MIGA	Multilateral Investment Guarantee Agency
MOF	Ministry of Finance
MOPDC	Ministry of Planning and Development Cooperation
NGOs	Non-governmental Organizations
OPEC	Organization of Petroleum Exporting Countries
OPIC	Overseas Private Insurance Corporation
PDS	Public Distribution System
PER	Public Expenditure Review
SOE	State-owned Enterprise
SWAp	Sector wide approach
SWG	Sector Working Group
TAL	Transitional Administrative Law
Tcf	Trillion Cubic Feet
WTO	World Trade Organization
WB	World Bank
UN	United Nations
UNDG	United Nations Development Group

# Iraq's National Development Strategy

---

## TABLE OF CONTENTS

<b>Foreword</b> .....	<b>vi</b>
Executive Summary .....	viii
<b>I. The Country Context</b> .....	<b>1</b>
The Legacy of the Past .....	1
Recent Achievements .....	2
<b>II. Recent Economic Developments</b> .....	<b>4</b>
Economic Growth .....	4
Inflation and the Exchange Rate .....	5
The External Sector.....	5
Oil Industry .....	5
<b>III. The Medium-Term Fiscal Framework</b> .....	<b>7</b>
Government Revenues .....	7
Government Expenditures .....	8
<b>IV. Strengthening the Foundations of Economic Growth</b> .....	<b>12</b>
A Stable Macroeconomic Environment .....	12
The Oil and Gas Sector .....	15
Structural Transformation of the Economy .....	17
Agriculture .....	18
Tourism.....	22
<b>V. Revitalizing the Private Sector</b> .....	<b>23</b>
Banking and Finance .....	23
Electricity.....	24
Transport and Telecommunications .....	25
Privatization and Restructuring of State-owned Enterprises .....	25
WTO Accession and Trade Liberalization.....	26
Foreign Direct Investment.....	27
<b>VI. Improving the quality of life</b> .....	<b>28</b>
Water and Sanitation .....	28

# Iraq's National Development Strategy

---

Education .....	29
Health .....	29
Housing and Urban Development.....	34
<b>VII. Strengthening Good Governance and Improving Security.....</b>	<b>35</b>
Eradicating Corruption.....	36
Law Enforcement .....	36
Judiciary .....	38
Corrections.....	39
<b>VIII. Implementing the Strategy .....</b>	<b>40</b>
Enhanced Donor Coordination Mechanism .....	40
Improving Iraq's Intra-Government Processes. ....	42
Bringing Both Sides Together .....	45
Intergovernmental Fiscal Framework and the Planning Process.....	46
<b>IX. The Way Forward .....</b>	<b>48</b>
Forecasting .....	48
Monitoring and Evaluation .....	48
<b>X. References .....</b>	<b>49</b>
<b>XI. Annexes .....</b>	<b>51</b>
Annex 1: Indicators for Iraq's Development Goals .....	51
Annex 2: Investment Expenditures by Cluster 2005-2007.....	55
Annex 3: Projects distributed by geographical location (2005-2007) .....	57

# Iraq's National Development Strategy

---

## Text Tables, Figures and Boxes

**Table 1:** Iraq: Key Economic Indicators (2004-2007)

**Table 2:** Iraq: Quarterly Economic Indicators (2003-2004)

**Table 3:** Iraq: National Budget, Investment and Expenditures (2005-2007)

**Table 4:** Quick Guide to the Planning Process

**Figure 1:** Enhanced Donor Coordination Mechanism

**Figure 2:** Simplified Work-Flow Process

**Figure 3:** Sector Programs in the Budgeting Process

**Box 1:** Iraq's Public Distribution System---- Helps the poor but is costly.

**Box 2:** Iraq's National Development Goals—Ambitious but achievable.

**Box 3:** Decentralization----Key Element of the National Development Strategy

# Iraq's National Development Strategy

---

## Foreword

---

“[M]any of the solutions to hunger, disease, poverty and lack of education are well known. What is needed is for efforts to be properly resourced and for services to be distributed more fairly and efficiently. None of this will happen unless every country, rich and poor, assumes its responsibilities....”

**UNDP Human Development Report, 2003**

---

This is the first *National Development Strategy* produced by a democratically elected government of Iraq. It is about creating opportunities for all the people of Iraq to contribute to the reconstruction and development of our great country. It is about ending ignorance, hunger, disease and sectarian conflict. Above all, it is about creating opportunities for job creation so as to raise household incomes, restore people's dignity and move Iraq down the road to prosperity.

This *National Development Strategy* sets out strategic priorities for Iraq's reconstruction and development. It is organized around four key drivers of prosperity that we believe best reflect the multi-faceted and complex challenges confronting us today. In each pillar we identify specific objectives with the aim of fulfilling our fundamental national vision of restoring Iraq to its rightful place in the world community as a prosperous and market oriented regional economic powerhouse.

The multifaceted challenges confronting us require a strategy that delivers actions on two fronts simultaneously. On one hand, we urgently need emergency/humanitarian interventions to provide basic services such as water, electricity, hospitals and schools. On the other hand, we need to start implementing reforms, building institutions and developing the capacities that will support a vibrant market-oriented economy. These interventions need to start immediately but will yield benefits in the medium-term and for generations to come.

This *National Development Strategy* argues that expanding opportunities in Iraq, a country devastated by decades of economic mismanagement, will require both public and private investment. Both forms of investment are critical to prosperity because they are strategic complements. Working together, public and private investment creates powerful synergies that spark economic growth, igniting job creation and raising living standards. Prudent public investment in water, health, electricity, roads, schools and security provides a conducive environment in which private investment can flourish. In turn, private investment creates jobs that generate resources which can be tapped to build better schools, modern infrastructure and guarantee peace and security for all Iraqis

This virtuous cycle has worked in many parts of the world—from the United Arab Emirates in the Middle East to Malaysia and South Korea in the Far East to Mauritius in Africa and, of course, in Europe which was rebuilt after World War II with massive public investments from the Marshall Plan.

We are convinced it will work in Iraq. But we cannot do it alone. As the above quotation points out, we in the Iraqi government have the responsibility of articulating and implementing

## Iraq's National Development Strategy

---

development strategies that are crafted to our local conditions and that benefit all the citizens of Iraq. It is our responsibility to demonstrate a commitment to deepen reforms, eradicate corruption, foster public trust and legitimacy and ensure that the governance of our institutions promotes economic progress and freedom for all.

In turn our development partners have the responsibility to deliver the billions in grants and concessional loans that have been pledged but not yet utilized. For those partners that have not yet made pledges this is the time to act. We need more resources for essential services such as to reconstruct and expand hospitals, water systems and schools. Such humanitarian assistance would best be provided in the form of grants. We also need financial resources for more commercially viable projects, such as a mortgage guarantee company or venture capital funds for small business development. These could be financed by concessional loans.

However, we are keenly aware that simply devoting more money to the challenges confronting Iraq is not enough. We need to work together with all our partners to make sure our internal government processes and our entire development cooperation architecture are effective and coherent. The *National Development Strategy* describes several new mechanisms to illustrate how we have improved on Donor Coordination. It also describes ways in which we are streamlining and simplifying our own internal processes to speed up project preparation and implementation.

For Iraqis, I believe this *National Development Strategy* will come to signify faith in a brighter future, and in our ability to work together as a democratic, multi-ethnic society to achieve betterment for all.

For the international community, I believe this Strategy initiates a fruitful dialogue and marks the beginning of a new era of cooperation. It should be the point of departure for programming international assistance. It establishes an Iraqi policy framework for Iraq that should be supported by international actions, and it delineates the priority areas to which international cooperation should be directed.

Undoubtedly, the stakes are high. Without early and tangible actions to accelerate reconstruction and development, the future of Iraq as a federal democratic country will be seriously jeopardized. At stake are prospects not only for 27 million people to enjoy better, more productive lives, but also long-term peace and security in the region----objectives intimately linked to sustainable prosperity.

**Barham A. Salih**  
**Chairman , Iraqi strategic Review Board**  
**Minister of Planning and Development Cooperation**  
**Republic of Iraq**



# Iraq's National Development Strategy

---

## Executive Summary

---

Iraq's National Development Strategy (NDS) takes as its starting point the fact the country's economy has been grossly mismanaged for 40 years, and its people urgently need an alternative strategy to supplant the failed policies of the previous dictatorial regime. Iraq, once self sufficient in agriculture, with tremendous oil wealth, a vibrant private sector and an educated and skilled population has gone from being one of the most advanced nations in the Middle East to a country with some of the lowest human development indicators in the region.

The democratically elected government of Iraq has articulated a clear vision for the country. The Vision is to:

*“Transform Iraq into a peaceful, unified federal democracy and a prosperous, market oriented regional economic powerhouse that is fully integrated into the global economy”*

This ambitious Vision can only be achieved by a market-oriented economy. One that is open to the world, driven by the ingenuity and creativity of private enterprise, founded on the rule of law, and led by a federal, democratic, transparent and accountable government.

The manifold and complex nature of the problems that confront us have dictated that we undertake to formulate a multi-faceted strategy to overcome the challenges. A few basic guidelines, helpful as they may be, are not sufficient. And macroeconomic policy alone, though it is fundamental, cannot deal with the multitude of sectoral issues that cry out for resolution. Macroeconomic policy sets the overall framework, but policy also has sectoral content, and it must not be forgotten that the economy responds at the micro level. For these reasons, the content of the NDS is very specific, extending to recommendations for reforms in the existing legislative framework and new legislation that would be needed to facilitate the implementation of the policies.

The aim in developing this National Development Strategy has been to weave together macroeconomic and sectoral analyses and proposals into a consistent policy fabric that will bring substantial benefits to all regions in Iraqi society. The orientation is fundamentally pragmatic. It is one of solving problems, everywhere identifying concerns and developing solidly-based remedial courses of action that are sustainable. While no document achieves all its aims, we believe this NDS is unique in its scope and depth, and its policies are strong and sure enough to accelerate reconstruction and make our citizens measurably better off, whilst assuring that our priceless heritage of natural resources has proper stewardship.

The National Development Strategy is intended to serve as the overarching framework for government reconstruction and development policy, as a reference by which civil society can hold government accountable, and as a basis for Donor coordination and harmonization.

It recognizes that a core element for achieving sustainable development is active participation of the population in production activities and creation of wealth, and that this requires securing the involvement of all of Iraq's regions in the implementation of the NDS and in the development process.

# Iraq's National Development Strategy

---

Effective involvement of the regions will be secured through:

1. Abandoning the centralized system of economic management that was the hallmark of the previous regime;
2. Using regional governments to contribute to the formulation, prioritization and implementation of development projects;
3. Distributing investment funds equitably between the regions; based primarily on population size but with consideration of addressing inequities; and
4. Urging donors to adhere to the regional distribution of foreign resources as determined by the national budget.

Regional Development Authorities (RDA's) will be established to spur reconstruction and development at the regional level. The role of the RDA's will be to:

1. Utilize central government departments in the regions for implementing the regional perspective of the NDS;
2. Allocation of investment funds from the central government and donors proportionate to the respective share of the region in the national investment budget;
3. Establish direct relations with donors and international companies in conducting their development activities under the NDS;
4. Become involved in mobilizing internal and external funds to supplement their development effort in their respective region.

The National Development Strategy is established on four major pillars that will govern strategic public actions for reconstruction and development.

1. Strengthening the foundations of economic growth.
2. Revitalizing the private sector.
3. Improving the quality of life.
4. Strengthening good governance and security.

## **Pillar One: Strengthening the Foundations of Economic Growth**

This pillar has three elements;

First, a strong foundation for economic growth and rising prosperity requires maintaining a stable macroeconomic environment. This will require:

1. Maintaining low inflation within the context of sound monetary policy, and expanded monetary policy tools.
2. Maintaining fiscally sound budgets and transparent controls for budget formulation and execution Meeting fiscal targets will be assisted by subsidy adjustments.
3. Strengthening financial management and public expenditure tracking and control.
4. Developing and implementing mechanisms to ensure transparent and full accountability of oil revenues within the national budget process.
5. Concluding debt relief agreements with both Paris Club and non-Paris Club creditors.

## Iraq's National Development Strategy

---

6. Implementing all macroeconomic and structural reforms under the International Monetary Fund's (IMF) Emergency Post Conflict Assistance (EPCA) agreement, including implementing a timely and accurate monetary survey and establishing a single treasury account.
7. Improving the quality, timeliness, and range of financial and economic data produced by government offices for economic planning.
8. Implementing fiscal decentralization and devolution of planning responsibilities to local and regional governments.
9. Increasing domestic resource mobilization by creating conditions conducive to private savings, by strengthening the deposit-taking commercial banking sector with a national payments system.

Second, Iraq has one of the world's largest oil reserves. The oil sector provides more than 60 percent of the country's gross domestic product (GDP) and 95 percent of its hard currency earnings. Given the dominance of oil in the Iraqi economy, it is clear that improving the performance of this sector is key to generating higher rates of economic growth. This will require:

1. Improving the legal and regulatory framework in the oil sector to enable restructuring of the industry.
2. Promoting strategic partnerships between Iraqi and foreign oil and gas companies so as to tap an important source of capital for the expansion and rehabilitation of the industry.
3. Establishing independent national oil and gas companies (both upstream and downstream).
4. Reducing fuel subsidies that distort incentives and encourage wasteful consumption of this precious non-renewable resource.
5. Investing in technical and managerial training to bolster capacity.

Third, a strong foundation for economic growth in an economy with a huge natural resource endowment (oil and gas) requires a diversified economy for the following three reasons. The first reason is that it will protect against the economic phenomenon called the "Dutch Disease". This phenomenon occurs when exploitation of a natural resource, such as oil, deindustrializes a nation's economy. This happens when oil exports cause the value of the local currency to appreciate, which makes manufacturing less competitive, and as a result imports increase and non-resource exports decline.

The second reason is that the oil industry is notoriously volatile. Frequent wide swings in prices make intertemporal planning difficult and can derail Iraq's growth prospects. Transforming the structure of the Iraqi economy to allow for a greater role for agriculture, tourism and industry which experience different cycles from those in the oil sector can cushion the Iraqi economy from oil shocks.

The Tourism industry has huge potential in Iraq. The Holy cities in Iraq are a major destination for hundreds of thousands of pilgrims annually. The ancient ruins of Babylon, the Ziggat of Ur and other "wonders of the world" have tremendous appeal as a destination for tourists. The scenic locations of Bekhma, Sarsink and Doukan in the Kurdistan region have been traditional destinations for domestic tourists and can now be expanded to attract an international clientele.

The third reason for diversification is that unemployment is a major problem in Iraq. Yet the dominant sector of the economy (oil) is capital intensive. Developing the agriculture, industry and tourism sectors which are labor intensive will help create jobs directly through farming, fishing and

# Iraq's National Development Strategy

---

the supply chain associated with delivering agricultural goods to market as well through jobs in agro-industries, hotels and transportation. This will require:

1. Eliminating subsidies that distort market prices and discourage farming.
2. Increasing the productivity of the agricultural sector through investment in new seed varieties , irrigation methods and strengthened market mechanisms.
3. Establishing agricultural demonstration sites throughout Iraq to reinvigorate crop and livestock production, and boost rural job creation.
4. Encouraging programs to revive Iraqi agriculture in areas such as date production, fish farming in the restored Iraqi marshlands, new crop varieties, and the expansion of extension services.
5. Developing the institutional structure to promote industrial sector competitiveness.
6. Promoting small and medium size enterprises through the creation of industrial clusters.

## **Pillar Two: Revitalizing the Private Sector**

Empirical evidence from worldwide experience has shown that a vibrant private sector (and not the public sector) is the engine of growth and job creation. Creating a pro-business investment climate for both domestic and foreign business, for small and large enterprises, for agriculture as well as manufacturing and services is therefore a top priority. This will require:

1. Streamlining and simplifying procedures for doing business in Iraq by establishing an Investment Promotion Agency.
2. Implementing commercial and regulatory reforms to develop a transparent legal and institutional framework to encourage entrepreneurship.
3. Effectively utilizing agreements with the Overseas Private Investment Corporation (OPIC), Multilateral Investment Guarantee Agency (MIGA) and the International Center for Settlement of Disputes (ICSD).
4. Laying the groundwork for eventual privatization of State-owned-enterprises, according to orderly, fair, consistent, and transparent procedures.
5. Promoting private sector-led implementation of local community projects that are executed nationally.
6. Restructuring State-owned banks to encourage consolidation and privatization.
7. Expanding the availability of commercial capital through concessional financing for micro-finance and small and medium enterprises.
8. Completing accession to the World Trade Organization (WTO) and revitalizing regional trading links.
9. Rehabilitating and expanding the air, railway and telecommunications network.
10. Increasing electricity generation and distribution to meet current and projected needs.

## **Pillar Three: Improving the Quality of Life**

Healthy citizens tend to be productive citizens and will be able to take advantage of the opportunities provided in a market-oriented economy. Improving the quality of life of Iraqis is therefore a core pillar of the National Development Strategy. This will require:

# Iraq's National Development Strategy

---

1. Improving access to clean water and sanitation.
2. Improving quality and access to medical care.
3. Increasing affordable housing units through housing finance facilities.
4. Investing in human capital with a focus on adult literacy, vocational training and actions to reduce drop-out rates at the primary level.
5. Enacting a social safety net program for the poor and vulnerable, including reform and monetization of the PDS basket.
6. Accelerating demining actions.

## **Pillar 4: Strengthening Good Governance and Improving Security**

One of the most pressing challenges facing Iraq is nurturing good governance. Corruption---the abuse of public office for private gain--- is arguably the most critical component of governance in a natural resource rich country like Iraq. Corruption has many forms. It extends from “petty” forms of administrative bribery to grander forms of corruption, such as the tendency of elites (individuals, political parties or private companies) to illegally and unethically shape the formulation of laws, policies and regulations. The grand type of corruption (known as *state capture*) requires broader external accountability measures---including asset declaration, transparency surveys, disclosure of parliamentary votes and investigative journalism and citizen oversight. Traditional anti-corruption methods that rely solely on internal bureaucratic structures and new public agencies have often failed because they do not take account of this invisible web of influence.

Other aspects of good governance are also critical for Iraq. Promoting respect for human rights and the rule of law and fostering participatory dialogue are critical in tackling terrorism and driving forward peace-building and nation-building. Access to justice, security and human rights is central to stability in a post-conflict situation. Lack of security has dampened economic activity, encouraged capital flight and caused untold misery and hardship. Strengthening good governance and security will require:

1. Establishing a Leadership Code of Conduct and Ethics requiring, inter alia, declaration of wealth by public officials.
2. Strengthening the Public Integrity Commission and decentralizing its activities to the regions to eradicate corruption.
3. Continuing strengthen the Board of Supreme Audit and decentralizing its activities to the regions to ensure transparency in public financial management.
4. Enhancing corporate ethics and transparency.
5. Implementing the new public procurement regulations for Ministries and public agencies for proper and effective use of State funds.
6. Establishing e-government to modernize governmental business processes.
7. Supporting the Electoral Commission, including voter registration and voter education.
8. Strengthening journalistic professionalism.
9. Supporting civic education initiatives that promote dialogue between communities.
10. Supporting objective public broadcasting (including an independent regulatory structure for license allocation).
11. Increasing representation of women and minorities in both the legislative and executive branches.

## Iraq's National Development Strategy

---

12. Training in respect for human rights for all security services, including the prisons.
13. Enhancing the administration of justice by training judges, lawyers and prosecutors, and providing modern management information systems and equipment.

We consider these four pillars the key drivers of economic performance and prosperity. It is important to note that these four pillars interact. For instance, although improving education is discussed under “quality of life”, it also has implications for all the other three pillars. The distinction between the pillars helps to focus attention on the actions which most directly affect reconstruction and economic development, but the interactions between the pillars need to be borne in mind.

The objectives identified in each of the four pillars are to be achieved by the development of detailed sector plans and investment programs by relevant Ministries. This will require sector-wide programming (where feasible) to translate the key objectives, into strategic actions, outputs and outcomes expected from sector expenditures, and the activities which the expenditures will fund in order to achieve the desired outputs and outcomes.

The National Development Strategy was prepared through an extensive series of consultations that started with the Iraqi Interim Government (IIG) and continued with the Iraqi Transitional Government (ITG). Consultations have drawn together sector experts from various Iraqi Ministries, the private sector and academia. An Inter-Ministerial Committee was established to prepare the first draft, with members from ten Ministries drawing from their official programs as well as from discussions held under the Committee’s auspices. An early draft was submitted to the World Bank (WB) and United Nations Development Group (UNDG) for comment, and was discussed with these two organizations over a series of meetings in Amman, Jordan in early September 2004 to incorporate their comments. Under the IIG, the interim NDS was approved by the Iraqi Strategic Review Board (ISRB) and by the Council of Ministers, as the basis for reconstruction and reform of the Iraqi economy during the next three years.

This consultative process has continued under the ITG. With the support of our development partners a team of economic and legal advisors was brought in to work closely with their counterparts in the Ministry of Finance and Ministry of Planning and Development Cooperation. Consultations were also held with Donors both in Baghdad and with their capitals. The revised strategy was endorsed by the High Economic Committee and the Cabinet. It will be discussed at the Iraqi Reconstruction Fund for Iraq (IRRFI) Donor’s Committee Meeting to be held at the Dead Sea, Jordan on July 18-19, 2005. The National Development Strategy will be endorsed by the National Assembly, which represents the voice of the Iraqi people.

This document is organized according to the four pillars. After an introductory chapter the next four pillars review the state of affairs in each pillar and identifies key objectives. Chapter 6 discusses a new donor co-ordination mechanism and Chapter 7 concludes with an agenda for the way forward.

## I. The Country Context

---

### The Legacy of the Past

There has been an appalling downward trend in almost all human development indicators relative to a baseline of 1980. The recently published Iraqi Living Conditions Survey documents the severe deterioration in the quality of life of the Iraqi family relative to a baseline of 1980, when the previous regime began its tragic effort to gain regional hegemony.

- This is reflected in the unstable and unreliable supply of electricity with more than 3.2 million households experiencing interruptions.
- The high cost and low quality of water with more than 76% of all rural households having problems accessing drinking water.
- The alarming reduction in urban access to safe drinking water from 90% to 60% of the population.
- The decline in the quality of sanitation with more than 1.5 million people suffering from unimproved sewer systems and the high cost and low quality of housing with more than 45% of all households reporting dissatisfaction.

The Survey also documents the precipitous collapse of the health system. This is reflected in the decline in primary health care centers from 1,800 in 1991 to 929 in 2001, of which more than 30% need rehabilitation. Maternal mortality remains above regional averages with more than half of deliveries taking place at home in rural areas. There is an extremely high incidence of respiratory infections in urban areas. Over 200,000 Iraqis have chronic illness due to the war serves to underscore the poor overall conditions of the population.

The Survey shows there is widespread unemployment in Iraq, in particular among young men whose unemployment rate reaches an astonishing 37%. The employment situation is complicated by the fact that Iraq has an estimated 192 State-owned enterprises that together employ 500,000 people. Yet many of these state-owned enterprises are not commercially viable, many having been looted and destroyed during the war. Indeed, most of these enterprises are idle and will not be able to create jobs in the foreseeable future. Supporting these loss-making state-owned enterprises imposes a huge burden on the economy and crowd out opportunities for new private-sector initiatives.

Under the previous regime poor governance practices were common, including widespread nepotism in public appointments and corruption among public servants. The lack of accountability and transparency in managing State resources abetted corruption and increased its corrosive effect on economic progress.

The centrally planned economy, nationalization of the oil sector and the intrusion of the State into economic life distorted the pricing structure, so that prices did not reflect the real value of the products or services. Supply and demand were consequently distorted resulting in allocative inefficiency and waste.

Monetary policy was non-existent. There was total dependence on monetary expansion to finance the deficit in the budget, which led to average inflation of 50% during the 1990s eroding

# Iraq's National Development Strategy

---

the purchasing power for those on fixed incomes, and leading to a depreciation of the Iraqi Dinar from .3125 ID/\$ to 2000 ID/\$.

Iraq's decades long isolation has resulted in a widening of the digital divide, technological stagnation and the use of outmoded production methods in the oil sector in particular. Public institutions used manual outdated administrative systems with poor record keeping and little accountability. To compound these problems critical public sector institutions witnessed serious looting, theft and destruction in the aftermath of the 2003 War.

It is evident from the above grim statistics that the legacy of the previous regime, and regrettably the failure of the international community to ensure that the Oil-for-Food Program was immune from manipulation by the previous regime, has caused immense damage to Iraq.

However, despite the significant security challenges facing Iraq, much progress has been made in several economic, social, and political areas since April 2003. The following represents some of the major achievements over this period.

## **Recent Achievements**

### ***Improved Economic Management***

In the area of fiscal and monetary policy much has been done to restore the capacity and credibility of Iraq's financial institutions. Interest rates were liberalized. The capital base of private banks was increased. Foreign banks were allowed to open branches and to enter into joint ventures with private Iraqi banks. The Central Bank of Iraq (CBI) was made independent. Monetization of government deficit was ceased. An internationally compliant Insurance Law was passed in March 2005 and became effective in June 2005.

Achieving Paris Club debt forgiveness agreement in December 2004 has dramatically improved Iraq's fiscal stance and has introduced fiscal prudence into budgetary processes with a view towards equity and accountability. An auction for Treasury bills was introduced and a more equitable distribution of resources throughout Iraq's governorates was achieved.

Steps towards greater accountability in the use of public resources include improving the fiscal oversight powers and auditing capacity of the Board of Supreme Audit and ministerial inspector general offices, as well as establishing precedents for use of independent external auditors on government accounts. The Commission on Public Integrity has been established, along with Inspectors General in each Ministry, as part of a comprehensive approach to combat corruption.

In the area of market-oriented reforms, several important economic and commercial laws were put in place, including securities, foreign investment, public financial management, public procurement and central banking. Iraq has developed strategies for reducing government price controls and laid the groundwork for privatization. Salaries and pensions of government workers were increased three to ten-fold, from previous levels which were below subsistence level.

To deepen integration with the world economy, Iraq has maintained low custom fees, signed an Emergency Post Conflict Assistance (EPCA) agreement with the International Monetary Fund (IMF), and in December 2004 initiated World Trade Organization (WTO) accession talks.

### ***Reconstruction***

From a slow start in the first year (June 2003 - June 2004) when only 200 reconstruction projects were started, one year later in 2005, more than 2,500 projects valued at \$5.7 billion are underway. More than half of the 2,500 completed projects have a value of \$1.3 billion. Since June 2004 over 2,300 construction projects have started --- employing over 155,000 Iraqi workers.



## Iraq's National Development Strategy

---

Rehabilitation of the oil infrastructure initially led to an increase in the production capacity to 2.8 million bpd, of which 2.1 million was exported. However, oil production has dropped due to sabotage despite the fact that 16 oil projects have been completed. The oil sector has been restructured by combining the three national oil entities into a single national oil company to be run on a commercial basis.

Electrical generation initially increased from 3,500 MW to 5,400 MW, above pre-war levels but significantly below demand. There was a subsequent drop in generation but the average daily load of electricity is comparable to the level in June 2004. Since June 2004 a total of over 2,000 megawatts of power have been added to the grid which is enough to service 5.4 million homes. Over 1, 4400 electrical towers and 8,600 kilometers of transmission lines have been installed.

Telecommunications has vastly improved since 2004 with landlines subscribers rising from 794,198 to 2.8 million in June 2005. Internet subscribers have more than doubled. Cell phone subscribers have jumped from just 488,966 to almost 2.5 million in 2005. Satellite television penetration extends to a majority of the population. Mobile telephone networks are now operating in major urban centers. Eighty water treatment plants have been completed; 90 still in progress. Thirty sewer projects are complete; 10 still in progress.

Health care spending is up more than 30 times its prewar levels. More than 3 million children have received life saving vaccinations. Over 140 health care facilities have been completed and one major hospital is under construction. About 750 nurses have been trained in maternal and child health services and 2,000 primary health care workers also have been trained.

Three thousand schools have been completed since June 2004. Over 860 secondary school master trainers were trained and passed on to training 31,777 secondary school educators nationwide. More than 8.7 million revised math books have been printed.

### *The Democratic Process*

A Transitional Administrative Law (TAL) was adopted to provide for effective government in Iraq until adoption of a Constitution and subsequent elections in December 2005. On June 28, 2004 the Coalition Provisional Authority ceased to exist and the Iraqi Interim Government assumed full sovereignty in Iraq. Moreover this Government fully represents the multi-ethnic, cultural, and religious character of Iraq, with broad participation of groups from across the political spectrum.

Despite early assessments that it would be too dangerous, about 8.5 million Iraqis, 58 percent of those eligible, voted on January 30, 2005. A transitional Government has been formed and a permanent constitution will be written by August 2005. A notable success is the fact that women comprise 31% of the national assembly.

The political process has taken hold as well, with more than 600 community associations in 16 governorates setting the stage for grassroots democracy. More than 19 million people can engage in local policy discourse through 78 district councils, 192 city or sub-district councils and 393 neighborhood councils. Over 2,000 Non-Governmental Organizations (NGOs) have been established.

Gender equality has been firmly established in the law. Iraq has taken on a target of ensuring 25% participation of women in decision making structures—including the National Assembly and the Council of Ministers. Freedom of speech and of the press has been established in the law. All media have been made independent of the state. More than 100 independent newspapers are published.

# Iraq's National Development Strategy

Several new Ministries have been established to reflect important new social groups and concerns: Human Rights, Displacement and Migration, Environment, Civil Affairs and Youth. In addition, Ministers of State for Women's Issues and Provinces have been established. The Ministry of Culture, and in particular its State Board of Antiquities and Heritage, has been restructured and are fully functioning.

## II. Recent Economic Developments

### Economic Growth

Although Iraq's unemployment rate remains astonishingly high at over 30%; the economy has rebounded since 2003 with nominal GDP doubling from roughly \$15 billion in 2003 to \$31.7 billion in 2004 and is expected to reach an estimated \$32.2 billion in 2005.

Real GDP growth in 2005 will be constrained by the expected decline in average oil output over the year. As a result, in 2005 real GDP growth is expected to be in the range of 2%- 4%; much lower than the EPCA target of 17%. This is because in the year to May production stalled at 1.5m bbl/d, and although we expect output to rise in the second half of the year to a projected 2.2m b/d in December, the net effect will be average annual production of 1.5 m bbl/d. However, the growth in non-oil real GDP (which is estimated to account for some 40% of total GDP) will remain relatively strong largely because of continued investment in the country's infrastructure and services, despite the hesitant pace dictated by the security situation.

In 2006 improvements in the security situation should see more aid inflows, helping to generate stronger domestic demand and greater activity in the non-oil sector. In 2006 we forecast that sufficient improvements to the security environment will have taken place to allow a rebound in average annual oil output. The non-oil sector will also pick up more strongly. Overall this should produce real GDP growth of 17% in 2006. Iraq's immediate economic priority is to increase oil output on a sustainable basis from the current level of between 1.5 m-1.8 m bbl/d to the capacity level of some 2.8m bbl/d as quickly as possible. Achieving this will be vital to ensure the stable provision and expansion of basic services. The production target is unlikely to be achieved in 2005, given likely ongoing sabotage in the oil sector and the relatively slow impact of foreign and domestic investment.

	2004	2005	2006	2007
Real GDP growth (% change)	46.5	4	16.8	13.6
Consumer prices (% change)	27	30	12	12
Merchandise exports (US\$ m)	235	452	606	665
Oil Real GDP (% change)	74.2	-1.1	20	14.6
Exchange rate (ID:US\$1)	1,670	1,453	1,450	1,550

Note: Source, Central Bank of Iraq, Ministry of Finance

# Iraq's National Development Strategy

---

## **Inflation and the Exchange Rate**

A slight decline in average inflation in 2005 is expected as the Central Bank demonstrates its commitment to price stability through the use of expanded monetary policy tools. Further dampening inflationary pressures is the expectation that domestic demand will remain relatively subdued as unemployment remains high. Inflation in the year up to May has been running at 30.6%. At current trends, we therefore expect inflation of around 30% in 2005 down from 32 % in 2004.

For most of 2004 the Iraqi diner maintained a broadly stable rate of exchange with the US dollar, and official data up to mid-May 2005 suggest the Iraqi currency averaged ID1, 453: \$1. Given the CBI's commitment to a stable rate, we expect the rate to be little changed in 2005, averaging around ID1, 450: \$1. In mid-May it hit a high of 1,538 ID. In 2006, with improved security and economic activity, the ID is expected to weaken slightly to ID1,550.

## **The External Sector**

In 2005 strong oil prices (reaching a high in the year to June of \$62 per barrel) should yield oil export revenue of \$20.8 billion up from around \$17 billion in 2004. The trade deficit in 2004 was \$1.4 billion with exports of \$17.7 billion. Imports are forecast to grow to \$24.2bn in 2005, while exports should reach \$23 billion, as higher oil prices are slightly offset by lower oil output for the year. This will lead to a trade deficit of US\$1.2bn this year. The services deficit will widen largely in line with import growth. This is expected to result in a widening of the current-account deficit to about \$9bn.

In 2006 a return to growth in oil output will lead to an increase in the total value of exports, to over \$27.2bn. Import spending will rise strongly as greater reconstruction activity (in what could be an improved security environment) stimulates more capital goods imports. Consequently, the trade deficit will widen to about \$7.2bn. Falling UN deductions and a rise in aid-related transfers credits should offset increasing services and income debits, leading to a rise in the non-merchandise surplus to about \$2bn. Overall, these trends should lead to a widening of the current-account deficit to \$4.72bn in 2006, representing 12.1% of GDP.

## **Oil Industry**

The oil industry, which remains the bedrock of the economy, has begun gradually to recover from the toll of years of underinvestment, war-related damage and post-war looting. However, attempts to boost and sustain exports have been held back by persistent and increasingly organized sabotage, targeted mainly at oil export infrastructure, as well as by a lack of investment in new production.

Much of the infrastructure was in a serious state of disrepair before the 2003 conflict. Before the War, production averaged around 2.1m bbl/d over the six years following the government's 1996 acceptance of the terms of the UN Oil-for-Food Program. This made possible the resumption of limited oil exports, allowing some relief for Iraqi's desperate humanitarian situation.

## Iraq's National Development Strategy

Table 2: Iraq: Quarterly Economic Indicators									
	2003				2004				
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	
Sectoral trends									
Crude oil production (m barrels/day)*	2.12	0.2 9	1.05	1.82	2.10	2.07	1.82	1.99	
Crude oil spot prices, Kirkuk-37 (US\$/barrel)	27.6 5	n/a	26.5 5	26.8 1	27.7 1	31.4 9	36.4 7	35.6 9	
Crude oil spot prices, Brent (US\$/barrel)	31.4 9	26. 03	28.3 8	29.4 3	32.0 3	35.3 2	41.5 4	43.8 5	
Foreign trade (US\$ m) <sup>b</sup>									
Exports fob	3,54 3	922	898	2,81 2	3,34 0	3,46 3	2,94 7	n/a	
Imports fob	-850	- 856	- 1,28 0	- 1,88 3	- 1,63 6	- 2,02 7	- 1,75 9	n/a	
Trade balance	2,69 4	67	-382	929	1,70 4	1,43 6	1,18 8	n/a	
Exchange rate <sup>***</sup>									
ID:US\$ (av)	2,30 9	1,6 75	1,83 3	1,92 7	1,43 6	1,45 7	1,46 4	1,46 0	
ID:US\$ (end-period)	2,35 4	1,4 59	2,18 5	1,77 2	1,42 7	1,46 3	1,46 3	1,45 9	
* Estimates. ** DOTS estimates c***Central Bank of Iraq.									
Sources: IEA, Monthly Oil Market Report; Oil Market Intelligence; IMF, Direction of Trade Statistics; Central Bank of Iraq.									

## III. The Medium-Term Fiscal Framework

---

The 2005 national budget underscores the Government's commitment to a sound fiscal framework that supports private sector development for robust economic growth and job creation. The budget priorities include rebuilding and expanding infrastructure, supporting private sector development and restoring national security.

The reconstruction of Iraq and restoration of public services at satisfactory levels requires a massive effort where all segments of society and public administrations at all levels are likely to be involved. In this setting, The Government recognizes that decentralization of powers from the central to sub-national government must play a crucial role.

The main goal of decentralization of intergovernmental fiscal relations is to ensure an equitable regional distribution of the national budget based primarily on population size, but also taking into consideration the need to redress regional inequities. This will require decentralization of intergovernmental fiscal relations to locally elected governments. Various options for reform of intergovernmental fiscal relations are being considered by the National Assembly for inclusion in the new Constitution.

Donors will need to respond to reform of the intergovernmental fiscal framework by working closely with the central and regional governments within an integrated budget process to ensure that national and regional priorities are respected. This is discussed in more detail in Chapter 9 on Donor Co-ordination Mechanism

### **Government Revenues**

Estimated revenues over the next three years is \$83.8 billion (\$23 billion in 2005, \$28.9 billion in 2006 and \$31.8 billion in 2007). Crude oil revenues amount to 90.3% of revenues with taxes and non-tax revenues amounting to 9.7%. (Table 3) Government revenue projections are based on the following assumptions:

### ***Oil Revenues***

Iraqi oil revenues for 2005, 2006 and 2007 are estimated to be about \$20.8 billion, \$26.3 billion and \$29.2 billion respectively. These revenues are based on 2005 crude oil production estimates of 1.5 million, 1.8 million and 2.0 million bbl/d at average prices of \$38, \$40 and \$49 per barrel for 2005-2007 respectively. The Ministry of Oil arrives at the estimates based on the assumption that both Northern and Southern oil fields are operative. Oil exports over the last six months was only 1.4 million bbl/d which is much lower than budgeted. This is because of closure of the Northern pipelines.

Over the past year and a half, oil pipelines and production facilities have encountered deliberate sabotage and vandalism which led to the suspension and/or decrease in the quantity of exports for days and sometimes for over a month. It is important to factor in this risk, as unexpected reductions in the exported oil quantities may offset any higher prices.

# Iraq's National Development Strategy

---

## Taxes, Customs and other Revenues

Despite the reduction in personal income taxes, corporate profits taxes and customs duties, we expect tax revenues to increase slightly from \$620 million in 2005 to \$717 million in 2006 and \$764 million in 2007. Indirect and direct taxes will constitute an average 9.7% of budget revenues over the next three years.

## Government Expenditures

### Salaries and Wages

Employee's wages and pensions account for 19.6 % of the total expenditures for 2005. Aside from a slight increase resulting from the restoration of pension payments to some State personnel dismissed in 2003, these expenditures will remain relatively flat in the following two years.

This limited portion of the budget for salaries and pensions implies that public sector employment will make only a marginal contribution to easing unemployment. However, as reconstruction accelerates and the private sector rebounds we should see a reduction in unemployment. Government expenditures on goods and services account for 17.6 % of the total budget in 2005. These expenditures will be frozen at their current level despite expectation to increase the prices of goods and services purchased by the Government.

### Subsidies

The oil sector is highly distorted by subsidies. Crude is sold to state-owned refineries for 300 Dinars (roughly \$0.20) per barrel. Despite such a low price the refineries and oil distributors experience great losses because of the very low prices of refined products set by the state: roughly \$.01 per liter of regular gasoline and \$.025 per liter of improved gasoline.

As a result of the distorted pricing scheme in the oil sector the government does not collect any revenues from the crude oil for refineries. This foregone revenue amounts to approximately \$5.2 billion annually. Imports of gasoline resulting from the shortage of refinery capacity is projected to cost Iraq \$2.4 billion in 2005. Therefore, the total cost arising from limited refinery capacity is around \$8 billion yearly, more than 40% of the state's total revenue. For this reason, liberalizing fuel prices as called for in the EPCA will be critical for fiscal discipline.

Approximately 47% of electricity production goes to households at subsidized prices. Implicit subsidies for the consumer in the electricity sector are estimated at \$4 billion due to fuel prices charged to generators below opportunity costs, as well as depreciation of equipment which not taken into account in pricing. Water, on the other hand, is provided well below marginal cost. Adjustments need to be made in pricing of electricity and water.

Direct subsidies in the consolidated budget include the Oil-for-Food Program/food basket (now called the Public Distribution System). In 1996, under the UN's Oil-for-Food Program, Iraq's food ration system was expanded to provide the population a basket of basic food items needed to sustain existence. These items included rice, flour, sugar, tea, cooking oil, pulses milk powder and iodized salt. In 2004 about \$5 billion was allocated to the Public Distribution System(PDS). In 2005 \$4 billion was allocated to the PDS.

## Iraq's National Development Strategy

---

Various proposals for reform of the PDS are under consideration. Monetization is one option (see Box 1). Another option is to identify and remove from the food ration system certain segments of the population who are not identified as food insecure. The Food Security Analysis Study along with the National Census, scheduled for October 2005, and the planned creation of a social security number for each citizen thereafter may help provide the data necessary for wider application of this policy. It would then be able to better target food subsidies to the most vulnerable segments of society. This action might save up to 25% of the total costs of the food ration system over the next two years.

Taken together, direct and indirect subsidies consume a major portion of government revenues. Direct subsidies amount to \$10.34 billion in 2005. This is more than 37% of national expenditures. The proportion of direct subsidies in national expenditures will drop to 31% in 2006 and 27% in 2007.

Subsidy reforms will reduce the burden on the national budget and release resources to be used for productive investments in infrastructure and basic service. It is also planned to transform indirect subsidies which do not appear in the public budget and the budgets of some of the government enterprises into direct subsidies, in order to know the amount of these subsidies and their impact and who benefits from them.

### War Reparations

The budget includes war reparations of \$1 billion in 2005, \$1.3 billion in 2006 and \$1.46 billion in 2007. According to a UN Security Council Resolution, war reparations should constitute 5% of the revenues from oil exports. This is a heavy burden on the budget. The Iraqi nation lived under the tyranny and oppression of the previous regime and should not bear the costs that regime imposed on others. However, Iraq is committed to being a responsible member of the community of nations and will pay these obligations as long as required by the international community.

### Investment Expenditures

The national budget recognizes the critical need for capital investments to reconstruct and expand Iraq's infrastructure. Therefore, about \$31 billion has been budgeted for the period 2005-2007. The Investment budget is to be financed both from the Iraqi domestic resources (55.3%) and from grants and preferential long-term loans from Donor countries (44.7%) (see Appendix 2). Capital investment accounts for around 21% of total expenditures in 2005 and remains at this level in 2006 and 2007. This high level of investment in GDP has the potential to spur double digit growth rates if the efficiency of the investment is maintained.

The government is committed to ensuring the equitable distribution of national resources to the regions to redress the inequitable distribution inherited from the previous regime which was heavily biased to the center. This commitment is reflected in the distribution of the capital investment for the period 2005-2007 in which Baghdad takes the lion's share of the investment budget with 16.8%, followed by Kurdistan region with 19.8 % while other regions will collectively receive 34.7% (See Appendix 3)

To support the economic development and reconstruction of the regions the government has allocated \$800 million dollars in the 2005 budget to establish Regional Development Authorities (RDAs) to spearhead economic development at the local level.

## Iraq's National Development Strategy

**Table 3: Iraq; Government Budget, Revenues and Expenditures (2005-2007)**  
**US\$ thousand Millions**

REVENUES	2005	2006	2007	EXPENDITURES	2005	2006	2007
Oil Revenues	20805	26280	29200	Wages and Pensions	5472	6715	6883
				Goods & Services	4922	6273	7528
Taxes	620	717	764	Transfers	10344	9424	8400
				Interest payments	186	272	300
Non-Tax Revenues	1606	1916	1926	War Reparations	1040	1314	1460
				Investment Expenditures	5878	6513	6783
Total Domestic Revenues	23031	28913	31890	Total Domestic Expenditures	27842	30511	31354
External Funds (Grants/Loans)	9000	10000	7000	External Funds (Grants /Loans)	9000	10000	7000
Grand Total Revenues	32091	38913	38890	Grand Total Expenditures	36842	40511	38354
				Deficit/Surplus	-(4772)	-(1598)	536

Source: Ministry of Finance and Ministry of Planning and Development Cooperation

\*Oil revenues estimated from crude oil exports of 1.5, 1.8 and 2.0 m bb/l day at average prices of \$38, \$40 and \$40 per barrel for the years 2005-2007 respectively.

\*\* External Funds are grants and loans from Madrid Pledges of \$33 billion of which \$7 billion was disbursed prior to 2005 and \$26 billion is to be allocated in 2005-2007.



### **Box 1: Iraq's Public Distribution System—helps the poor but is costly.**

The Public Distribution System (PDS) is a universal entitlement scheme under which all 27 million Iraqis receive a food basket each month. It is very effective in reaching the poor but it is very costly. The 2005 budget allocated \$4 billion to the PDS. This is equivalent to \$150 per Iraqi annually. The opportunity cost of the PDS is high. It consumes 21 percent of Government revenue which could be used to scale-up spending on other urgent priorities like infrastructure, health and education. Although the PDS is an effective safety net for the poorest it is inefficient, costing about \$6.30 to transfer just \$1 worth of food to an individual. Furthermore, the PDS is wasteful because it is not targeted at the people who need it most—the poor. The PDS has had perverse effects on agriculture because of its heavy reliance on imports and the artificially low-prices caused by large injections of food into the Iraqi market.

One solution being considered is to replace the PDS with cash payments (monetization) to all households in Iraq. Monetization is intended to increase the efficiency of the delivery of subsidies, reduce distortions in the economy that impede domestic production and improve transparency and accountability of the use of oil revenues. This policy is aligned with the government's strategic objective of building the market structures that promote private business, improves living standards and integrates Iraq into the world economy.

Monetization of the PDS is likely to yield considerable static and dynamic benefits to the Iraq economy compared to the current in-kind distribution system. However, monetization needs to be introduced with care. The complexity of implementing a nation-wide program pertains to the large numbers of recipients involved, setting the amount of Dinars to be given in lieu of the basket right and the political sensitivity of the change-over. Moreover, the monetized system must be a zero-defect system: every Iraqi needs to receive his or her monies on time and must be able to use that money to purchase sufficient food on the market. If even small numbers of people do not receive their monies, or the monies received are considered inadequate, then the transition to the new system is likely to be highly damaging. Secondary, but important concerns include: preventing fraud and the theft of funds; ensuring that the change does not have negative nutritional effects; empowering women; avoiding misuse of oil revenues; and ensuring that the changeover has positive effects on economic development, in particular on agriculture, retailing, wholesaling, transportation, and the financial services (banking) sector.

## IV. Strengthening the Foundations of Economic Growth

---

### A Stable Macroeconomic Environment

Macroeconomic stability is essential to solid economic growth. A sound macroeconomic framework, good microeconomic policy settings and effective financial regulation and supervision policies is the foundation for robust economic growth.

Sound frameworks for fiscal, monetary and financial policy are based on the principles of transparency, responsibility and stability. In practice this means:

- The fiscal framework is designed to achieve sound public finances.
- The monetary policy aims to maintain low inflation over the medium term, while avoiding unnecessary instability in output, interest rates and the exchange rate.
- Financial stability requires a range of policies, including a sound macro- and microeconomic framework. It also requires a capacity for detecting and responding to possible sources of vulnerability.

### Fiscal Policy

An economy's growth potential depends on adequate levels of investment, which in turn require sufficiently high flows of national saving. However, In Iraq private national savings have traditionally been extremely low. The low level of national savings can largely be attributed to the public sector. Excessive and wasteful public consumption and transfer payments (subsidies) have crowded out public investment, and growing public-sector deficits financed by printing money have crowded out private investment and raised inflation. Bringing public-sector finances into better balance is, therefore, a key element of a medium-term growth strategy.

While balancing the budget remains a priority, improving the composition of public expenditure is also critical for delivering durable and high-quality fiscal policy. Empirical evidence suggests that productivity of government expenditure is more important than its size in ensuring sustainable growth and development. It is essential to redirect government expenditures towards uses with the highest social return. Redirecting public expenditure toward growth-enhancing, cost-effective, investment in physical and human capital, and knowledge is a priority in Iraq.

Public expenditure composition can also be improved by enhancing the performance of public enterprises. This not only produces fiscal savings, but also increases efficiency. Some of the largest losses, which are often hidden, occur in the energy sector. A ministerial-level Commission has been established to explore the options for reform of State-owned enterprises in Iraq. While fiscal consolidations can, especially if well-designed, spur growth, they often result in some short-term output and social costs. So a well-designed strategy needs to incorporate targeted social programs to mitigate any adverse impact of economic reform on the poor and the vulnerable.

However, without well-functioning fiscal institutions, even the best designed policy measures may fail. Good fiscal institutions, such as sound, transparent, and efficient budget systems, fiscal responsibility frameworks, and effective revenue administrations, can greatly facilitate adjustment. Fiscal transparency enforces accountability and helps promote broad public

## Iraq's National Development Strategy

---

support for fiscal reforms. Effective implementation of fiscal policy is as important as the design of the policies themselves, and tax policies are no exception. No matter how good in theory, they cannot be successfully implemented without a solid tax administration. On the expenditure side, policy measures need to be supported by an effective budget management system. Such a system is essential for ensuring effective spending control, improving financial management, and achieving cost-effectiveness in service delivery.

### Monetary Policy and Banking

A stable macroeconomic environment requires sound monetary policy. That is often defined as a policy based on a price stability goal, a transparent process for setting the instrument of policy and a flexible exchange rate conducted by an independent central bank. Price stability is critical for growth because it means that entrepreneurs, managers and workers will all receive undistorted price signals from the markets. Decisions are adversely affected when relative price signals are confused by inflation. Investment and saving decisions in particular become distorted, damaging the growth of production and national wealth over the long term. Sound public finances will also contribute to price stability by avoiding undue weight having to be placed on monetary policy as the primary instrument for curtailing inflation.

Banks are at the core of the financial system in Iraq and are intricately linked to monetary policy. Stable macroeconomic conditions are important for a robust banking and financial system. It is not possible to establish and maintain bank soundness unless prices and other nominal variables in the economy are evolving in a relatively stable fashion and economic activity is expanding at a reasonable pace.

The soundness and resiliency of the banking system depend on how effectively banks perform their lending decisions, and on how well they recognize and manage changing risk profiles as the economic circumstances of their borrowers evolve. But banks also perform other important financial functions, such as operating the clearing and payments system and the foreign exchange market. As a result, the banking sector is the main vehicle for transmitting monetary policy actions to market interest rates, the stock of liquidity, and, ultimately, overall economic activity and prices. Because of these diverse functions, a sound banking sector is the single most essential element of a healthy financial system.

How effectively banks perform these functions depends, in turn, on competition in the banking system and the state of the macroeconomy. One major reason why the banking sector in Iraq is not competitive is because of extensive government intervention over the past 40 years.

Strengthening private ownership and competition in Iraq's banking systems to address this vulnerability is a high priority. Responsibility for the internal governance of banks and other financial institutions rests, first and foremost, with their owners, managers, and directors. Owners with their capital at risk have a strong incentive to appoint competent directors and managers and to closely oversee their business. This is why privatization is traditionally seen as a crucial element of banking sector reform in many developing and transition countries. Liberalizing the conditions of entry to make the banking industry "contestable" is another way to increase both private ownership and competition in the banking sector.

### Box 2. Iraq's National Development Goals

Nationally representative living standard surveys have not yet been conducted in Iraq. The last credible Census was conducted in 1957. The lack of reliable data makes it difficult to establish baselines and track progress towards achieving measurable development goals. As an interim measure we use a variety of sources such as the 2004 Iraq Living Conditions Survey (ILCS) as a baseline. Targets are for realization in 2007 (short-term) 2010 (medium term) and 2015 (long-term). The internationally agreed Millennium Development Goals (MDGs) provides the framework for setting Iraq's development goals. (See Appendix for Indicators).

**Goal 1: Eradicate Hunger and Poverty:** In 1990 the average dietary intake in Iraq was 3,300 calories. By 1997 the average dietary intake had sunk by more than 1,000 calories. By 2003 the food ration basket had raised the dietary intake up to 2,000 calories per person per day. However, according to ILCS, in 2004 an estimated 96 percent of Iraqi's receive food rations. This indicates that in the absence of the food ration hunger would be widespread. Unemployment correlates strongly with poverty. Out of a population of 27.1 million, 16.4 million are of working age. Of the working-age population, 6.7 million are in the labor force. Thus, Iraq has a labor force participation rate of only 40 percent. The OECD average is 70 percent.

**Target 1: Reduce by two-thirds the proportion of people living below the poverty line.**

**Target 2: Reduce by two thirds the proportion of people who suffer from hunger.**

**Target 3: Raise the labor force participation rate to 70 percent of the working age population.**

**Goal 2: Achieve Universal Literacy and Lifelong Learning:** Every person will be literate and will possess the knowledge and skills necessary to compete in a global economy and exercise the rights and responsibilities of citizenship. Education levels in a population can be measured by the literacy rate and the rates of highest completed education. According to the ILCS, illiteracy is widespread in Iraq: 39 percent of the rural population is illiterate. Overall 22 percent of the adult population has never attended school. Only 9 percent have secondary school as highest completed education.

**Target 4: Ensure that all boys and girls complete a full course of primary and secondary schooling.**

**Goal 3: Promote Gender Equality and Empower Women:** After improvement in women's position in education in the 1970s there have been dramatic setbacks during the last 20 years. Forty seven percent of women in Iraq are illiterate or partly illiterate. According to the ILCS, the gender gap is highest in the Northern region where the literacy rate is 20 percent lower for women than men. There is significant regional difference in women's education. In Sulamaniya, Dahouk and Al-Muthanna more than 60 percent of women aged 15 years and over have less than an elementary education compared to 32 and 38 percent in Baghdad and Basrah respectively.

**Target 5: Eliminate gender disparity in all levels of education.**

**Goal 4: Reduce child mortality:** Between 1979 and 1989 under-five mortality rates improved from 120 to 60 per 1,000 live births. However, between 1990 and 2001, under-five mortality worsened to 133 (compared to 33 in Jordan and 107 in Yemen). Infant mortality has also worsened dramatically from 40 per 1,000 live births to 107 (compared to 105 in sub-Saharan Africa).

**Target 6: Reduce by two-thirds the under-five mortality rate**

**Goal 5: Reduce maternal mortality:** According to the ILCS, maternal mortality rates in Iraq are extremely high at about 193 per 100,000 live births compared to 41 in Jordan and 25 in Kuwait.

**Target 7: Reduce by two thirds the maternal mortality rate.**

## Iraq's National Development Strategy

---

### Iraq's National Development Goals (continued)

**Goal 6: Achieve universal access to safe water and sanitation:** According to the ILCS, only 54 percent of households have access to a safe and stable supply of water. Improved sanitation has dropped from almost 100 percent to only 67 percent in 2004 (compared to 100 percent in Jordan, 97 percent in Syria and 100 percent in West Bank and Gaza).

**Target 8: Ensure that all people have sustainable access to safe drinking water and improved sanitation**

**Goal 7: Achieve decent shelter for all :** Owning a home is a form of social security and an important asset for a family. According to the ILCS, 76 percent of all dwellings in Iraq are owned by the household inhabiting them. This is particularly true in south and central regions of the country. In the Kurdish region and in Baghdad higher numbers of households rent their dwellings. Overcrowded conditions and dilapidated housing is also prevalent.

**Target 9: Increase to 90 percent the number of households that own their dwellings.**

**Target 10: Reduce by two-thirds the number of people living in slums and overcrowded houses.**

**Goal 8: Eradicate Corruption:** Iraq has a history of massive corruption. The previous regime bankrupted the country through massive embezzlement of public funds for personal palaces and other conspicuous and wasteful consumption at the expense of the average citizen.

**Target 11: Ratify and implement the UN Convention on Anti-Corruption by 2006**

**Target 12: Eliminate *state monopoly* in the economy and other sectors of social life by 2007**

**Target 13: Curtail discretionary power (i.e., the lack of clear administrative rules and regulations) by 2007.**

**Target 14: Increase *accountability* (i.e., poor functioning of watchdog agencies or a lack of such agencies including civil society and media organizations) by 2007.**

### The Oil and Gas Sector

Iraq is estimated to hold 115 billion barrels of proven oil reserves---one of the largest in the world---and possibly much more undiscovered oil in unexplored areas of the country. Iraq is also estimated to contain at least 110 trillion cubic feet of natural gas.

The cost of production is among the lowest in the world because the fields are onshore, very large, and have a relatively simple geological structure. The Ministry of Oil has prepared medium and long term plans to increase the country's oil production capacity to reach or surpass 6 million bbl/d. The target for the year 2007 is 3.5 million bbl/d. Estimated costs to maintain and increase production are in the range of \$4 billion. Iraq's oil sector plan also targets an increase in gas production and invites foreign companies to participate in developing the oil and gas fields in shared production contracts.

Historically, Iraqi production peaked in December 1979 at 3.7 million bbl/d and then in July 1990, just prior to its invasion of Kuwait, at 3.5 million bbl/d. As of May 2005, Iraqi

## Iraq's National Development Strategy

---

production had reached 1.9 million bbl/d. Increasing oil production to pre-war levels is critical if Iraq is to sustain high rates of economic growth.

Throughout the 1990s, Iraq did not have access to the latest state-of-the art oil industry technology (3-Dimensional imaging, seismic, directional drilling, gas injection etc), sufficient spare parts and investment. In the long-run adoption of these new technologies could result in Iraq's oil output increasing by several million barrels per day.

Under optimal conditions, and including routes through both Syria and Saudi Arabia that are now closed or being utilized for other purposes, Iraq's oil exports infrastructure could handle more than 6 million bbl/d (2.8 via the Gulf, 1.65 via Saudi Arabia, 1.6 via Turkey and 300,000 via Jordan and Syria). However Iraq's export facilities were seriously disrupted by the Iran-Iraq War and the 1990/91 Gulf War, the most recent war in March/April 2003 and periodic looting and sabotage since then.

As of May 2005, about 30 companies had signed MOUs (Memoranda of Understanding) with Iraq. They generally cover the training of Iraqi staff, consulting work and reservoir studies. In December 2004, Iraq's State Company for Oil Prospects (SCOP) awarded a 4150 million contract—the first post-Saddam era upstream deal—to Turkey's Avrasya Technology Engineering for development of Khurmala dome. It is expected to increase production at Khurmala dome from 35,000 bbl/d to 100,000 bbl/d. Another large oil field slated for development is Majnoon, discovered in 1975 and containing reserves of 11-30 billion barrels. Future development of Majnoon field ultimately could lead to production of 450,000 bbl/d within two years at a cost of \$4 billion.

In January 2005, a consortium of Shell, BHP, Billiton and Tigris Petroleum signed a deal with Iraq's Oil Ministry to increase output from the 4.5 billion barrel Halfaya field in southern Iraq. Smaller fields with under 2 billion barrels in reserves have also received interest from foreign oil companies. These fields include Nasiriya (ENI, Repsol), Tuba (ONGC, Sonatrach, Pertamina), Ratawi (Shell, Petronas, CanOxy), Gharraf (Mashinimport, Rosneftgasexport), Amara (Petr Vietnam) and Noor (Syria).

Restructuring the oil sector and merging the national oil companies into one conglomerate is already under way. The Ministry of Oil plans to establish open, transparent, and fair policies, practices, and treatments to attract foreign investors. Promoting strategic partnerships between Iraqi and foreign oil and gas companies so as to tap an important source of capital for the expansion and rehabilitation of the industry will be critical. To do this effectively, a strong legal and regulatory framework is needed. However, for the foreseeable future the Government intends to continue to play an active role in this sector through the established national oil company. Limiting private firms, foreign or domestic, to rehabilitation or production.

Another impediment to the sector is the fact that oil products are heavily subsidized. Crude oil is supplied to refineries at a price of 300 ID per barrel (about 21 cents) compared to current spot market benchmark price of more than \$40 per barrel. The quantity supplied to those refineries ranges from 500,000 to 550,000 bpd. According to the price per barrel assumed in the 2005 budget projections, \$26 per barrel, foregone revenues ranges between \$4.7 and \$5.2 billion. Added to this must be the cost of imports (\$2.4 billion) which are sold to the consumer at the price of 20 ID per liter (about 1 cent) while the government imports at market price. Total subsidies are in the range of \$7.1 billion to \$7.6 billion yearly. This is not only a drain on government revenues but also a disincentive to downstream investment. Under the EPCA agreement with the IMF the Government committed to increase domestic prices of refined oil products by January 1, 2005. While this has been delayed due to unavoidable circumstances, the Government remains committed to a gradual increase in domestic prices of oil products as per capita income increases.

## Iraq's National Development Strategy

---

The plan for refinery modernization appears to be to first upgrade the existing refineries by, among other measures, adding more conversion capacity, and then to expand overall capacity. One estimate for this program is \$1 billion for upgrading the three existing refineries and \$2.75 billion for new refinery construction. Alternatively, Iraqi and foreign private sector investment, would be expected to create new refining capacity.

### Natural Gas

Iraq contains 110 trillion cubic feet (Tcf) of proven natural gas reserves. About 70 percent of Iraq's natural gas reserves is associated (i.e. natural gas produced in conjunction with oil) with the rest made up of non-associated gas (20 percent) and dome gas (10%) . In 2002, Iraq produced 83 billion cubic feet (Bcf) of natural gas, down sharply from 215 (BCf) in 1989. Since most of Iraq's natural gas is associated with oil, progress on increasing the country's oil output will directly affect the gas sector as well. To date, most associated gas is simply flared off. Significant volumes of gas are used for power generation and reinjection for enhanced oil recovery efforts. One avenue worth exploring would be investing in capture of natural gas, which is currently flared.

The main sources of Iraqi natural gas are the Kirkuk, Ain Zalah, Butma and Bay Hassan oil fields in northern Iraq, as well as the North and South Rumaila and Zubair fields in the South. The Northern Rumaila gas plant was scheduled to start up in December 2003 and to boost gas utilization by around 500 MMcf/d but has been delayed. In addition, Iraq is considering plans for increasing associated natural gas processing capability in Zubair and West Qurna and to reduce gas flaring which is wasteful and dangerous.

Iraq plans to increase its natural gas output in order to reduce dependence on oil consumption, to use for petrochemicals production and possibly to export. In December 2003 , Iraq, renewed a natural gas supply agreement with Kuwait that dates back to the 1980s, under which Iraq was to supply natural gas to Kuwait via an overland pipeline. In September 2004, Iraq agreed to join the Arab Gas Pipeline Project linking Egypt, Jordan, Syria and Lebanon.

The key objectives in the medium-term for the oil and gas sectors include:

1. Improving the legal and regulatory framework in the oil and gas sectors to enable restructuring of the industry.
2. Promoting strategic partnerships between Iraqi and foreign oil and gas companies, so as to tap an important source of capital for the expansion and rehabilitation of the industry.
3. Establishing independent national oil and gas companies (both upstream and downstream).
4. Reducing fuel subsidies that distort incentives and encourage wasteful consumption of this precious non-renewable natural resource.
5. Investing in technical and managerial training to bolster capacity.

### Structural Transformation of the Economy

#### The Rationale for Diversification

A strong foundation for economic growth in an economy with a huge natural resource endowment (oil and gas) requires a diversified economy for the following three reasons. The first reason is that it will protect against the economic phenomenon called the "Dutch Disease". This

## Iraq's National Development Strategy

---

phenomenon occurs when exploitation of a natural resource such as oil deindustrializes a nation's economy. This happens when oil exports cause the value of the local currency to appreciate, which makes manufacturing less competitive. As a result imports increase and non-resource exports decline. The second reason is that the oil industry is notoriously volatile. Frequent wide swings in prices makes intertemporal planning difficult and can derail Iraq's growth prospects. Transforming the structure of the Iraqi economy to allow for a greater role for agriculture which experiences different cyclical from those in the oil sector can cushion the Iraq economy from oil shocks. The third reason for diversification is that unemployment is a major problem in Iraq. Yet the dominant sector of the economy (oil) is capital intensive. Developing the agriculture and manufacturing sectors which in many instances are labor intensive can help create jobs directly through farming, fishing and the supply chain associated with delivering agricultural goods to market as well through jobs in agro-industries.

The high growth rates achieved during the 1960s and 1970s under import substitution policies were mainly due to the vast oil revenues which enabled the country to sustain this model of development for many years. But the short fall and fluctuations of oil revenues during the following years, and the complete stop of export during the first half of the 1990s, showed the failure of this strategy which became unable to support the increase in labor force and income averages, consequently, the Iraqi economic had faced serious changes due to the high rate of population growth and the deterioration of economy growth and the failure of protected economic activities in public sector to neither offset the decrease in oil revenues nor to promote growth factors. Thus, the development efforts which were achieved during the first stage had almost disappeared following the short fall in oil revenues.

This demonstrates how dangerous it is for an economy to be dependent on a single economic resource. Therefore, there is a consensus that Iraq requires structural transformation of its economy, to diversify its sources of growth. This will require strategies and economic reforms to:

- Move away from dependence on the Oil sector.
- Move towards a private sector led, market-oriented economy.
- Move towards an export promotion strategy.

Realization of these movements requires introducing economic reforms, mainly liberalization of foreign trade and encouraging domestic and foreign investment.

These two factors can play an essential role in diversifying growth sources, which also requires the development and the liberalization of basic services such as transportations, communications, financial and infrastructure services and tourism which is considered as one of the main fields of developing trade. Introducing incentives for private investment, institutional changes and restructuring are also required as important factors in updating and activating the economic capabilities, in both medium and long term periods.

### **Agriculture**

Iraq's agricultural sector represents a small, but vital component of Iraq's economy. However, rapid population growth during the past three decades, the UN Oil-for-Food Program that dumped vast amounts of imported food on the market, coupled with limited arable land and a general stagnation in agricultural productivity, has steadily increased dependence on imports to meet domestic food needs and has made Iraq a major importer of agricultural products.



## Iraq's National Development Strategy

---

By 1980, Iraq was importing about half of its food supply. By 2002, between 80 and 100 % of many basic staples -- wheat, rice, sugar, vegetable oil, and protein meals -- were imported. Iraq is divided into a rain-fed northern winter grain producing zone and a center-south irrigated zone that produces vegetables and fruit, as well as cereal crops. Iraq has a total surface area of 43.7 million hectares of which 34.0 million (78 percent) is not viable for agricultural use under current conditions. Less than 0.4 percent is in forest and woodlands situated along the extreme northern border with Turkey and Iran. The remaining 22 percent (about 9.5 million hectares) are involved in agricultural activities, although almost half of this is very marginal and used only for seasonal grazing of Iraq's livestock population of predominantly goats and sheep. An estimated 340,000 hectares are in tree crops (mostly dates, but also some figs, grapes, and olives). Area cultivated annually to field crops such as cereals, pulses, fruit, and vegetables varies with weather and market conditions, but generally averages 3.5 to 4 million hectares. Between 75 and 85 percent of crop area is generally planted to grains (mostly wheat and barley).

Since the 2003 war the country's agricultural sector remains beset by the legacy of past mismanagement and the lingering effects of a severe drought during 1999-2001. Clearly, Iraq will be dependent on imports to fully meet domestic food demand for several years to come. In the near term, food aid shipments will play a major role in determining the share of Iraq's agricultural imports, and may influence the evolution of future commercial imports.

To appreciate the plight of the Iraqi agricultural sector it is useful to describe the evolution of policies that have devastated the sector. From 1979-1990 the former regime attempted to foster private sector control and investment in Iraq's agriculture. Surging oil revenues were used to acquire Western technology and to lavish extensive government subsidies on the sector. Area and production expanded through the 1980s for cereals, vegetables, and fruit. However, cereal yields stagnated due to poor production practices and limited varieties development. In addition, the Iran-Iraq War diverted labor and other resources away from agriculture. Population growth continued to outpace agricultural production, increasing the importance of trade. Despite governmental efforts at stimulating agricultural production, cereal and poultry imports as a share of domestic consumption nearly doubled to 69 and 48 percent, respectively, during the 1980s. By 1989, Iraq was importing over \$2.5 billion in agricultural commodities annually, including 78 percent of its cereals and nearly 100 percent of its vegetable oils and sugar.

Following the Gulf war, the country was effectively partitioned into two distinct entities -- three northern governorates (Erbil, Dohuk, and Sulaimaniyah) and the remaining fifteen governorates in central and southern Iraq. As a result of the partition, the previous regimes control over agricultural policy was limited to the 15 southern governorates. Following the implementation of U.N. economic sanctions, that government took several steps to increase both production and control of domestic food within its zone of control. These changes included government monopoly control over most grain production and the introduction of a State-managed system of rationing of basic foodstuffs.

Government incentives coupled with rising internal food prices encouraged Iraqi farmers to expand crop area by planting on marginal pastureland and fragile hillsides. Record cropped area was attained in 1992 and again in 1993. However, agricultural productivity suffered for lack of fertilizers, agricultural machinery and the means of spraying planted areas with pesticides. Iraq's irrigation infrastructure fell into disrepair and salinity has spread across much of the irrigated fields of central and southern Iraq. Iraq's poultry and livestock populations were devastated by the loss of rangeland to grain crops and the cut off of imports of feed grains and veterinary medicines needed for routine control of parasites and diseases.

### **Box 3: Decentralization-A Key Element of the National Development Strategy**

Prior to 2003 Iraq was a highly centralized unitary state. After the first Gulf War, the three governorates in Kurdistan began to function autonomously from Baghdad. The Kurdistan region is represented by a Parliament and has elected governors and local councils. There are over 60 municipalities in the Kurdistan region each with elected officials. The Kurdistan region has developed partial controls over local services, although all public employees, including teachers and doctors are appointed by the regional government but paid through the central government.

With the advent of democracy in Iraq, the momentum towards decentralization has picked up around the country. Decentralization is popular because it entails the transfer of legal authority for economic development, service delivery and other public functions from the central government to subnational governments. While there is likely to be some costs in terms of possible efficiency losses due to poor local capacity in the regions, decentralization holds the promise of providing better and more responsive service delivery, greater transparency in the use of public resources and greater resource mobilization than a centralized system.

Currently the 15 governorates outside the Kurdistan region and their associated 251 municipalities operate as “deconcentrated” organs of the central government. Deconcentration is the shifting of power to local branches of the State such as regional administrators or local technical line Ministry agents. Deconcentration is a weak form of decentralization because the “bottom to top” accountability mechanisms from which many benefits are expected are not well established as in democratic forms of decentralization.

Under the current form of deconcentration, municipalities are responsible for some urban functions, such as park services and waste collection, but the major public functions are carried out by local branches of central government line Ministries. Local officials have little influence over these activities.

The design of a decentralized system requires assigning public-sector responsibilities among different types of governments. The design entails four key components: expenditure assignment; revenue assignment; intergovernmental transfers; and subnational borrowing.

On the expenditure side, apart from purely local services such as street paving and feeder roads, virtually all expenditure assignments are controlled from Baghdad. On the revenue side, while there are some local fees, all tax bases (oil revenue, income tax and property rental tax) and collection are centrally determined. Even after the allocation of some revenue raising capacities to governorates they will be unable to finance all their responsibilities. Grants from the central government will continue to be the main mechanism by which subnational governments are funded. Borrowing by regions is currently not practiced, but in a decentralized system must be consistent with national budget.

The National Assembly is currently writing a Constitution that will enshrine the broad principles on which decentralization is to operate, including rights and responsibilities of all levels of government, the description and role of key institutions at central and local levels and the basis on which detailed rules may be established or changed. Several reforms need to be initiated in preparation for decentralization. These include:

- Strengthening the capacity of subnational governments in financial administration, budget execution and project preparation.
- Tax reforms, including preparations for both central and subnational taxes.
- Enhancement of tax administration.
- Strengthening of budget classification and reporting arrangements.

By the mid-1990s severe macroeconomic problems related to the international sanctions led the government to end most support to the sector and instead to implement austerity measures

## Iraq's National Development Strategy

---

that further curtailed agricultural investment. Declining food availability resulted in a significant rise in malnutrition in Iraq, particularly in the center and south of the country.

Clearly, Iraq will be dependent on imports for fully meeting domestic food demand for several years to come. In the long term, after the economy has regained its viability and vibrancy, market forces and international competition will be the driving forces behind Iraq's agricultural trade patterns. Iraq's historical trade and food consumption patterns suggest that food grains such as wheat and rice, feedstuffs including corn, barley, and protein meals, vegetable oil, sugar, meat, and dairy products are all likely to be important imports into Iraq.

The place to start rebuilding Iraq's agricultural sector is with the country's seed supply. Iraqi farmers will need thousands of tons of high quality seed next year, mainly wheat, rice and barley, as well as vegetable seed, root crops, and seeds for replanting degraded pastures.

Iraqi cereal production dropped sharply over the past decade in large part because of inadequate seed production and distribution systems, which led to a degradation of seed quality and productivity. Lack of high yielding seed has greatly reduced farm efficiency and forced thousands of farmers to abandon their fields.

A key challenge will be to cope with salinity problems. Roughly 75 percent of the nation's irrigated land suffers from salinity caused by inappropriate water management practices. Iraq desperately needs to restructure its irrigation management schemes and introduce more salt-tolerant crop varieties from international breeding programs and gene banks.

Iraq lies at the eastern end of the Fertile Crescent, an area of "mega-diversity" of important food crop and pasture species that account for nearly 40 percent of the food crops consumed worldwide. Maintaining that diversity is important not only to Iraq, but to crop improvement programs around the world. Prior to the 2003 War, the Abu Ghraib National Gene Bank contained some 1,400 accessions of different crops. Virtually all of the country's agricultural research centers have been destroyed or severely damaged. Large quantities of genetic materials for crops and livestock animals are feared lost. Even if the Abu Ghraib gene bank survived, it is likely that its holdings were destroyed or looted. Fortunately, ICARDA scientists collected more than 1,000 accessions of Iraq's most important crop varieties and wild species during the 1980s and 90s and have held them in the Center's gene bank for safekeeping. Those materials will play an important role in any future effort to rehabilitate Iraqi agriculture.

Agriculture in Iraq dates back more than 5,000 years, but the damage done over the past two decades will not be easy to undo. What is needed now is information to bring modern agricultural research tools to bear to redeveloping Iraqi agriculture in response to market forces, and begin the job of rehabilitating its land and water resources. A first step would be to reorganize the nation's agricultural institutions into a centralized body that can provide realistic planning and budgeting, and also link up to international agricultural research organizations and the private sector.

There is need for major investments to re-establish a national seed production system and rebuild Iraq's gene bank, agricultural research library and its major research laboratories. Without high quality seed farmers cannot grow food, and without basic facilities agricultural scientists cannot provide the technical support that farmers need to contend things like climate change and water scarcity.

A major effort is needed to educate a new generation of researchers and extension workers. The usefulness of agricultural technology varies from location to location and must be adapted to meet local needs.

Presently, the Government has taken the first steps towards freeing the prices of fertilizers, insecticides, wheat, barley and rice. It has also directed the Ministry of Trade to purchase food

## Iraq's National Development Strategy

---

basket inputs, especially wheat and rice from local farmers at international prices. This is expected to increase agricultural production. The Government has also begun to develop agricultural policies and institutional reform that will provide the basis for food security in the medium-term, including capacity building of the private sector, phasing out subsidies and reshaping water resource management and rehabilitations of agro-industry.

A return to normal weather patterns is critical for domestic cereal production in Iraq. Political stability, improved internal security will also be needed before Iraq's agricultural sector witnesses significant investment and growth. Restoration of the irrigation infrastructure (including a long-term de-salinization program), as well as the grain marketing infrastructure for handling, storing, and distributing agricultural inputs and outputs will be vital. In addition, the development of a viable agricultural research and extension service to develop and disseminate improved varieties and successful production practices are needed to restore agricultural productivity.

The following are the main prioritized actions to be taken in this sector:

- a. Reform of the subsidy regime to eliminate price distortions in agricultural markets.
- b. Restoration of irrigation infrastructure (including a long-term de-salinization program), as well as the grain marketing infrastructure for handling, storing, and distributing agricultural inputs and outputs.
- c. Development of a viable agricultural research and extension service to develop and disseminate improved varieties and successful production practices are needed to restore agricultural productivity.
- d. Increasing production and productivity through providing improved seeds, fertilizers and their scientific exploitation.
- e. Participating effectively in the national plan to revive marshes through the development of animal assets, especially raising buffalo and the development of fish fortune.

### **Tourism**

It is now recognized that tourism has great potential to create and indirectly support job creation in several segments of the economy: airlines; hotels; restaurants; transportation; travel agencies; and telecommunications. Private sector led development of the tourist industry is an important source of foreign exchange revenues in many countries in the Middle East. The tourism industry has also played an important transformational role as a vocal constituency for improvements to airports, immigration and visa procedures, security, road, rail and telecommunication networks.

As the cradle of civilization, Iraq has great potential as a tourist destination. Its Holy cities (Karbala, Najaf, Samawa and Kadumia) are major destinations for hundreds of thousands of pilgrims annually. The ancient ruins of Babylon, the marshes, the Ziggat of Ur and other "wonders of the world" have tremendous appeal as tourist destinations. The scenic locations of Bekhma, Sarsang and Doukan in the North have been traditional destinations for domestic tourists and can now be expanded to attract an international clientele.

The strategy for the tourism sector entails the following:

- a. Establishing active tourist promotion offices in key international capitals.
- b. Streamlining and simplifying visa and immigration procedures.

## Iraq's National Development Strategy

---

- c. Encouraging entry by the international hospitality industry (hotels, car rental agencies, foreign exchange bureaus etc.) into the Iraq market.
- d. Developing marshes and lakes to an appropriate tourism level to attract tourists and visitors.
- e. Developing the infrastructure of religious cities and maintaining the Holy shrines.
- f. Developing tourism education institutes, and developing tourism institutions, building the capacities of people working in the tourism field through specialized training programs, and making use of the experiences of other countries.

### V. Revitalizing the Private Sector

---

The Government is committed to ensuring that the private sector plays a critical role in Iraq's reconstruction and development. For the private sector to flourish security must be established, the rule of law strengthened, and an efficient payments system and a diversified financial sector developed. All quantitative and qualitative restrictions and sanctions which hinder geographical movement among different economic sectors must be removed.

An enabling environment for the private sector requires well-functioning and efficiently-priced infrastructure. An enabling environment for investment is about partnership between governments and the private sector, sharing risks between them to be managed by those best placed to do so. Such a partnership demands good governance, sound policies and capable institutions. Government should implement credible policies and do everything possible to lower business risks and keep it low. Most of all an enabling environment requires public investments in physical and human capital.

#### Banking and Finance

Banking is a critical component of any financial system. Other than the sale of government debt instruments, capital markets are virtually non-existent. The Stock Exchange began operations in July 2004 and has a very small capitalization. State-owned and private insurance companies are very weak.

Iraq's banking system has very rudimentary credit facilities and a weak payments system. There are 24 licensed banks, including 6 public and 18 private commercial and investment banks. In aggregate, the banking sector has only \$2 billion in assets; the banks are marginal in the economy as providers of liquidity. The Central Bank of Iraq supervises the banking sector. However, overall supervision is weak and needs significant improvement in capacity building, organization, technology, and in providing operational manuals, regulations, and a modern legal framework

During the past year, an independent Central Bank Law, a new Security Law and a new Banking Law were adopted. Significant change in the structure of the financial and banking sector is expected to occur during the period covered by the NDS. Foreign banks are now allowed to open branches and to enter into joint ventures with private Iraqi banks. Interest rates have been completely liberalized, new currency notes have been issued and the exchange rate has been stabilized through frequent foreign exchange auctions by the Central Bank. The immediate and medium-term priorities can be identified as follows:

## Iraq's National Development Strategy

---

- a. Restructuring the State-owned banks, including updating technology and providing technical assistance, and capacity building.
- b. Creating an effective operating structure for the Central Bank to provide services and supervision of the banking system.
- c. Upgrading and modernizing the non-cash payments system, including inter-bank clearing and settlement services.
- d. Establishing up to date electronic settlement facilities at the Central Bank and its regional branches.
- e. Addressing the status of State-owned banks and insurance companies to encourage the process of consolidation and privatization.

### Electricity

As of late May 2005, Iraq had around 4,000-5,000 megawatts (MW) of available operable power generating capacity, well below projected 2005 summer demand of 8,000 MW. The shortage of electric generating power in Iraq has been caused by numerous problems, including sabotage, looting, lack of security for workers, disruptions in fuel supplies, difficulty in procuring replacement parts at the aging stations, lack of training for workers and obsolete technology.

It is estimated that restoring and improving Iraq's electric power sector will require about \$12 billion in investment. The Iraq Government has drawn up a list of 200 power projects to start in 2006, at a cost of \$6 billion.

As of early May 2005, work was proceeding on the rehabilitation of the 640 MW Doura Power Plant in Southern Baghdad. Currently the Plant is operating at about half its optimal capacity. In addition to Doura, Iraq's Infrastructure Rehabilitation Program is upgrading eight of Baghdad's power distribution substations. Overall, Baghdad accounts for about 40 % of Iraq's total power load. In March 2005, Halliburton subsidiary KBR announced it had completed work on Al Ameen Substation which is to supply 1, 000 MW of power to Baghdad.

Iraq intends to allow independent power projects on Build-Own-Transfer (BOT) and Build-Own-Operate (BOO) basis. Iraq also intends to reform the electricity tariff system. Traditionally, electricity prices have been kept extremely low. Electricity tariffs were fixed at a level to cover operational costs. However, since March 2003 billing and revenues collection for electricity services has ceased. Ensuring adequate fuel supplies for the power sector has proven to be a major challenge during the last two years.

The medium-term objective for the coming three years is to return the power system to a reliable and efficiently run system, similar to pre-1991, with a generating capacity of about 7,000 MW. This will require additional power generation of about 2,700 MW. In order to achieve the target investment, the rehabilitation and augmentation of current work must continue. The estimated cost to achieve this objective is approximately \$3 billion. The following measures are planned to support this goal:

- a. Reconstruct the electric power network to increase power generation to the levels that guarantee continuous supply to satisfy consumer demand with minimum interruptions.
- b. Update the electric power distribution networks to meet the objective above.
- c. Develop a timetable on short- and long-term bases to qualify and train executives and supervisory staff for the sector to upgrade its efficiency.
- d. A combination of more rational pricing, significant investment, and improved efficiency should eliminate the existing gap between electrical supply and demand. The private sector should be the main source of new investment.

# Iraq's National Development Strategy

---

## Transport and Telecommunications

Iraq's transport system comprises 40,690 kilometers of roads, two international and three major domestic airports, six cargo ports, two oil terminals, and 2,456 kilometers of rail lines. Roads accommodate about 70% of all traffic in Iraq. Existing facilities of telecommunications, post offices, and internet infrastructure are very underdeveloped. The transportation and communication networks in all governorates of Iraq must be expanded and internal, regional and international connections enhanced. The sector needs significant resources and policy changes in order to rise to regional standards. Iraq can "leapfrog" over rivals in this sector by adopting the latest technology and adopting a favorable business environment by establishing proper policy and regulatory frameworks. The following actions are planned:

### *Telecommunications:*

- a. Rebuilding and expanding the existing switching and local access networks and undertake civil works in order to reach fixed line telephone service teledensity of 3.3 million customers by 2007.
- b. Establishing a modern and integrated national long distance backbone network with international connectivity.
- c. Reconstructing the postal system including rehabilitation of post facilities and the existing buildings to bring Iraq in line with other countries in the region.

### *Transport:*

- d. Continue ongoing dredging activities in and around Umm Qasr Port.
- e. Remove wrecks in Shatt-al-Arab and Umm Qasr Ports in the most environmentally sound manner possible.
- f. Develop a master plan to increase efficiency and optimize the institutional arrangement for ports and inland waterways.
- g. Explore the potential for developing a bus rapid transit system and dedicated bus lines.
- h. Rehabilitation of key railway stations and refurbishing rolling stock and maintenance equipment.
- i. Modernize railway training centers in order to maintain the skills of railway staff.
- j. Prepare a railways strategy to assess the merits of restructuring the present system to permit greater private sector participation in the delivery of services.
- k. Develop airports and civil aviation strategy coupled with a master plan, which should include plans for rationalization of facilities and future institutional arrangements, with the possibility of outsourcing airport management to private operators.
- l. Develop programs for the privatization of some activities in the sector, particularly in the field of communications, and land, sea, and air transportation.
- m. Retrain supervisory and operational staff, particularly in the area of previously suspended activities such as aviation and maritime.

## Privatization and Restructuring of State-owned Enterprises

There are an estimated 192 State-owned Enterprises (SOEs) that employ a combined 500,000 Iraqis. This workforce supports a significant portion of the population. Following the end of the War in April 2003, many of these firms suffered severe looting and destruction. Most of the SOEs are currently idle. They can be classified into three categories:

## Iraq's National Development Strategy

---

- Category I: Companies that are a financial burden on the State. These firms should be liquidated or merged into integrated, economically-viable entities.
- Category II: Companies for which additional information is needed to determine whether to liquidate or privatize them.
- Category III: Industrial companies dependent on local raw materials and increasing demand for their products, such as fertilizers, cement, and petrochemicals. Their privatization can be achieved through a new authority linked directly to the Council of Ministers, to which the ownership of such companies will be transferred. The authority should be empowered to pre-qualify, liquidate, sell or enter into partnerships with strategic partners under a comprehensive, transparent reform program over a specific time frame, announced in advance.

The Government has established a Commission under the Council of Ministers to review options for the reform and privatization of SOEs. It is understood that SOE reform must be synchronized with the national reconstruction program, which will draw down the level of unemployment.

An important area for privatization is the manufacturing sector. After a period of rapid expansion in the manufacturing industry sector up to 1980, a long period of stagnation and technological obsolescence started due to protracted wars and sanctions. The result is a small and weak manufacturing sector that contributes no more than ten percent to GDP, but employs no more than 4% of the labor force. The sector depends exclusively on exports of the oil sector to secure its imported technology as well as other required inputs. The sector has suffered from excessive dependence on State investment, inward-looking industrial strategies, and active discouragement of foreign participation. Based on the relatively large and expanding local markets, the country's rich hydrocarbon resources, as well as a variety of other suitable industrial inputs, could be utilized to create a rapid, private sector-led, (and export-oriented) industrial expansion. To facilitate this process the following measures are planned:

- a. Achieving a significant increase in the annual production of industrial enterprises in comparison with 2002.
- b. Closing down SOEs whose physical plant has been damaged where there is no economic advantage from keeping them in operation and facilitating the redistribution of assets to more productive uses elsewhere.
- c. Expanding the activities of geological surveys in northern areas and starting metal exploration activities.
- d. Establishment of industrial zones and complexes for the purpose of industrial integration and the encouragement of joint ventures.
- e. Strengthening standardization and quality assurance services.
- f. Encouraging the establishment of Small and Medium Scale Enterprises (SME) projects and developing appropriate financing mechanism for such projects.
- g. Encouraging the establishment of technical resource networks for women entrepreneurs.

### WTO Accession and Trade Liberalization



## Iraq's National Development Strategy

---

The liberalization of external trade aims to integrate the Iraqi economy into the global economy, remove distortions in prices of commodities and services, increase competitiveness, and enhance the efficiency of the Iraqi economy. This process was initiated immediately after the fall of the previous regime. Restrictions on trade were cancelled and imports were subject to a uniform custom tax of 5%. Food and medicine were exempted.

A national committee already has been established to design a rules-based, transparent and stable foreign trade regime, and domestic regulations and policies which are WTO compatible. The process of joining the WTO and the international commitments arising from it will act as a "lock-in mechanism" and guide for domestic economic reforms. The Committee will also assess the social and economic impact of Iraq's WTO accession and determine remedial measures.

### Foreign Direct Investment

Iraq has a basically sound legal framework for the formation and registration of foreign-, Iraqi-, and jointly-owned companies under the Foreign Investment Law of 19 September 2003. Foreign, legal, and natural persons have the right to be an investor or partner in, or a founder of, companies in Iraq by virtue of Company Law Number 21 of 1997, as amended in 2004. Further objectives in the area of foreign investment include:

- a. Continue to remove all kinds of restrictions on foreign investors and to encourage the flow of foreign direct investment in a manner that ensures the flow of foreign capital, modern technology and management expertise.
- b. Encourage partnerships between foreign and Iraqi investors.
- c. Simplify procedures for foreign investors through a one-stop approach for all procedures related to foreign investors, that would draw together all Iraqi government officials concerned in one place.
- d. Create a specialized authority to provide facilities to investors and offer investment opportunities in the country.
- e. Conclude bilateral and multilateral foreign investment agreements, ratify investment guaranty agreements with the Multilateral Investment Guarantee Agency (MIGA) and effectively utilize the Overseas Private Investment Corporation (OPIC) to catalyze foreign investment
- f. Promote alternative dispute resolution mechanisms to resolve investment disputes.

A "one stop" investment promotion agency will be launched in 2005. This will prove beneficial in facilitating investment and reducing initial costs of setting up and doing business in Iraq. Additionally, the Government is committed to issuing implementing regulations to the Foreign Investment Law, and streamlining the process of licensing new businesses.

## VI. Improving the quality of life

---

### Water and Sanitation

Up to 1991 water and sanitation systems in Iraq were operating efficiently. Safe potable water was accessible to 95% of urban and 75% of rural inhabitants. 218 conventional water treatment plants were operating in the country and 1,191 compact water treatment plants were also in operation. Sanitation services covered 75% of urban communities and 50% of rural ones.

Recent studies show that many water and sewage treatment plants were provided at an “acceptable” level. Of the 177 water treatment plants only 34 were classified as “good.” Sewage collection and treatment service in Baghdad is provided to only 80% of the population and only 9% of urban populations outside of Baghdad, while rural areas in the north of Iraq do not have piped sewage systems.

Sanitation is thus becoming a serious environmental and health problem. Deteriorating sewer pipes are contaminating the potable water network and underground water, further adding to the health and environmental problems. It is estimated that 50% of wastewater generated in Iraq is being discharged into the rivers and waterways. Baghdad contributes as much as 75% of that discharge.

The Government is committed to restoring the standards that existed before 2003 and expanding access in a sustainable way. Emergency activities include water tankering, especially to the southern cities. Water quality monitoring has been established throughout the country. Procurement for water treatment chemicals and garbage collection is being provided. Key objectives over the next three years are:

- a. Provide financial and technical support to water, sewage, and solid waste sectors to achieve pre-2003 levels by the end of this year, including: increasing access to potable water by urban areas by 15% and that of rural areas by 20%; reducing water losses by 10%; raising sanitation coverage by 10% in urban areas; developing city master plans for water and sanitation service in the major cities; building capacity and enhancing management systems.
- b. Rebuild Al Rasafa Plant for potable water in Baghdad and provide safe potable water to the city of Basrah. Provide sewage services to newly built areas in Baghdad and Basrah.
- c. Continue efforts to reconstruct and establish new sanitation plants in urban and rural areas to ensure full coverage of all regions of Iraq, and to reduce inequality between urban and rural areas.
- d. Improve water quality and upgrade the water distribution networks.
- e. Develop short- and long-term plans to train executives and supervisory staff for the water and sewerage projects, and to establish high level training centers for this purpose.
- f. Provide adequate crude water resources for all regions of Iraq.
- g. Maintain and improve the efficiency of existing pumping stations and sewerage networks, while achieving the required environmental standards for processed water prior to pumping to drainage points.
- h. Develop a timetable for the implementation of new projects in all governorates to increase the scope of sewerage service coverage.

## Iraq's National Development Strategy

---

- i. Acquire specialized machinery for cleaning and clearing sewerage networks.
- j. Reconsider the subsidy policies of the sector and develop a timetable for the gradual increase of the prices of drinking water supply, taking into account the pricing differences between the various social categories, regions and consumption.

### Education

The educational system in Iraq was widely regarded as among the best in the Middle East until 1980. Since then lack of resources, politicization of the educational system, and emigration of doctors and teachers have made Iraq's health and educational systems below the standards of all Middle Eastern countries. Illiteracy is widespread with 39 percent of the rural population unable to read or write. Overall 22 percent of the adult population has never attended school. Only nine percent have secondary school as highest completed education. Forty seven percent of women in Iraq are illiterate or partly illiterate. The gender gap is highest in the northern region where the literacy rate is 20 percent lower for women than men. There is significant regional difference in women's education. In Sulamaniya, Dahouk and Al-Muthanna more than 60 percent of women aged 15 years and over have less than an elementary education compared to 32 and 38 percent in Baghdad and Basrah respectively.

To restore the high standards of the 1980s is at the heart of the Governments reconstruction efforts. The private sector will be encouraged to participate and play an important role in provision of education. Private primary and secondary schools may be established and private investment in building professional capacities and upgrading medical technology will be sought. Action is already underway this year to attain this objective. Among other measures, the following are priorities:

- a. Physical rehabilitation and reconstruction of primary and secondary schools.
- b. Ensuring minimal quality standards of teaching and learning through strengthening basic teacher training.
- c. Providing adequate supplies of material, equipment and furniture to schools.
- d. Developing a new curriculum at all levels to prepare students for the twenty first century..
- e. Strengthen links between vocational training, technical education and labor markets.
- f. Encourage life-long professional development of educational staff.

### Health

The health system in Iraq is under acute stress. Iraqi people's health and the Iraqi health system have deteriorated rapidly in the last decade. The health system was considered to be relatively good before the 1990/91 Gulf War – there was wide, equitable access of the population to health care, with secondary and tertiary care in reach of those in need. Since then it has been damaged as a result of wars, sanctions and bad governance. Alongside the deterioration of health services is a mounting burden of disease and malnutrition, made worse by the recent war's damage to an already battered infrastructure, the worsening of food insecurity and a lack of access to clean water, sanitation, power and shelter. The effects of weapons used during the war, including depleted uranium-tipped munitions and cluster-bombs, are further public health concerns.

The overarching objective of the health system in Iraq is to promote health and improve access to quality health care irrespective of ethnic, religious or geographic origin or socioeconomic status. It also aims to improve management of the health sector.

# Iraq's National Development Strategy

---

A clear vision is needed to translate the principle objective of the new health system into concrete policies and strategies. The Ministry of Health established, for this purpose, ten working groups and a steering committee which operated from October 2003 to January 2004. The groups proposed a consolidated vision for the health system in Iraq.

The vision describes a system which is people-centered, giving citizens choice and making them responsible for their own health. Seven core elements are identified: population empowerment; community involvement; integrated health services with emphasis on primary health care; financial risk protection (equity); health provider management autonomy; quality improvement; and human resources development.

While the vision provides the basis for wider and more in-depth discussion on the future shape of the Iraqi health system and requires long-term planning, there is a pressing need to adopt concrete strategies to address the enormous challenges currently facing the health sector.

The following are the immediate needs and strategies:

## **Immediate and short-term strategies**

They include five areas for action:

1. Meeting urgent needs and improving services
2. Strengthening results based management
3. Developing and implementing a 4 year plan for reconstruction
4. Training and capacity building
5. Mobilizing resources

### ***Meeting urgent needs***

These are urgent priorities requiring immediate action. In some of the areas mentioned below, action has already been initiated. It is hoped that these urgent needs will be met by the end of 2005.

- a. Addressing shortages in medicines and urgent supplies.
- b. Upgrading emergency services including obstetric care.
- c. Increasing immunization coverage.
- d. Upgrading blood transfusion services.
- e. Establishing a more efficient information system.
- f. Improving communications.
- g. Improving food safety measures.
- h. Re-organizing the pharmaceutical sector.
- i. Conducting an in-depth review of primary care.
- j. Strengthening disease surveillance system.
- k. Intensifying communicable disease control activities.
- l. Meeting most urgent rehabilitation needs.
- m. Developing a plan for human resources development and attending to urgent organizational and coordination issues .

# Iraq's National Development Strategy

---

## *Strengthening management*

Reconstruction of the health system cannot be achieved without drastic changes in the management of the health sector. There is currently limited capacity in planning, budgeting, finance and management functions of the Ministry of Health. Management practices are often overly bureaucratic and generally outdated. Corruption and financial irregularities are widespread. Action should be initiated immediately in the following areas:

- a. Institutionalizing values such as transparency, accountability, openness, equal opportunity and participation
- b. Strengthening capacity for strategic planning, management, procurement; and modernizing budgeting and finance functions.
- c. Building capacity for managing decentralization and for leadership development.
- d. Changing to evidence-based decision-making, performance appraisal, monitoring and evaluation.
- e. Eradicating corruption.

## *Developing and implementing a four year plan of reconstruction of the health sector*

The Joint United Nations-world Bank Needs Assessment outlines health sector needs and financial requirements. However, careful analysis of available data and experience gained over the last few months has demonstrated the need for a more reliable assessment of needs. The process has already begun and is currently providing a clearer vision of the physical infrastructure of the health sector. A four-year plan is being developed and action has already been initiated in some areas. The plan focuses on:

- Re-visiting reconstruction requirements and prioritizing.
- Developing standards for rehabilitation and new construction.
- Strengthening capacity in project management and implementation.
- Strengthening coordination with partners .

## *Training and capacity building*

Training and capacity building of health professionals and management staff is a top priority. The four areas which require special emphasis are:

- Training and capacity building in management.
- Strengthening capacity in public health and related branches like health planning, economics, financing, and other areas.
- Training in clinical skills.
- Upgrading health professional education (basic, post-graduate, continuing).

# Iraq's National Development Strategy

---

## *Mobilizing resources*

The regular budget of the Ministry of Health can only meet the cost of salaries, operating expenditures, and the medicines bill. There are no reconstruction funds available. Policy makers must recognize that investment in health is a strategic priority for Iraq. It is a prerequisite to long-term sustainable development. The current expenditure on health, as a proportion of GDP, is considerably lower than neighboring countries, like Jordan and Lebanon, and must therefore increase. At the same time, much of our funding requirement for rehabilitating the physical infrastructure of the health sector will depend on donor funding. Thus, our strategy should focus on effective action to mobilize funds at the national, regional, and international levels.

The following represent basic areas of action:

- Raising commitment to the health sector
- Improving information on current status and needs
- Intensifying work with the media
- Strengthening donor partnerships and coordination
- Encouraging partnerships with non-governmental organizations and communities.

While immediate and short-term interventions are vital to meet Iraq's emergency and humanitarian needs, they must not deflect from careful medium to long-term health systems planning.

## **Priorities for the Medium-Term**

### **1. The development of a strong, coherent and integrated public health system**

The rehabilitation of the health sector should be based on the goal of ensuring a strong, coherent and integrated public health system providing primary, secondary and tertiary care. Nevertheless, it is recognized that the State system has deteriorated over the past decade, and that Iraq has undergone a process of 'passive privatization', with a range of private health care providers stepping in to fill the role of government institutions. Where these providers are undertaking competent and safe care, policy-makers should build upon and support this gap-filling operation.

### **2. Health financing**

In light of the need to develop a coherent and equitable public health system for all, financing for Iraq's health system should be based on progressive taxation and government income that is pooled primarily at the national level. The implementation of formal charges at the point of delivery should not be necessary, especially for primary level services. The establishment of complex, fragmented and difficult-to-regulate social health insurance systems should be avoided.

### **3. Supporting and strengthening public sector administration**

A strong public health system should not be equated with a centralized and inefficient state bureaucracy. Plans need to be established to strengthen public management, support the

# Iraq's National Development Strategy

---

development of effective administration systems, and structure appropriate forms of deconcentration to allow more responsive and locally relevant health service delivery.

Reversing the effect of more than 30 years of brutal dictatorship and transforming civil servants and the bureaucratic machinery of government from a command-and-control culture to an open and participatory culture will take concerted efforts, time and resources.

## **Operational issues**

Researchers examining health policy needs in the aftermath of a number of different conflicts have described a number of 'typical' operational responses from donors and have stressed the need for more appropriate interventions. These include the following:

### **Infrastructure Development**

After a war, there are often attempts to re-construct whatever has been destroyed. However, a post-war situation provides an opportunity to review the functions and distribution of health facilities and to rationalize and make more equitable the distribution of the resources that are available. Emphasis should be placed on the rehabilitation of clinics and district hospitals, rather than on the more visible and high profile secondary or tertiary hospitals.

### **Specific disease problems**

The development of vertical programs to tackle specific diseases is a common post-war response, when there is a need to produce rapid results around a set of narrow objectives. (It is also common when there is a lack of donor co-ordination.) While they are sometimes appropriate, vertical programs can divert resources and attention from other equally important Primary Health Care (PHC) services and undermine the development of comprehensive, efficient and integrated PHC programs. A coherent organizational strategy to avoid this trap should be developed by the donor community in conjunction with the Iraqi health administration.

### **Training and human resources**

Health personnel constitute the biggest single budget item of a health system. However, human resource development, (including ministry officials and managers) is often overlooked as a key strategic issue in the post-war situation. A comprehensive human resource strategic plan is a priority and must incorporate:

- The training and skills development of existing health personnel;
- Defining the right mix of health cadres, skills and competencies to address the main public health problems of the country;
- Ensuring equitable human resources distribution;
- Ensuring that health personnel are adequately remunerated and motivated; and
- Promoting the role of women within the public health system at all levels.

# Iraq's National Development Strategy

---

## Medicines

Medicines are typically the second biggest recurrent budget item of a health system. The immediate development of an essential drugs program, which would include an essential drug list and standard treatment guidelines will be important. This will go a long way towards promoting cost-effective and rational treatment; avoiding a black-market in pharmaceuticals; and avoiding the development of antibiotic resistance.

## Promotion of breastfeeding and appropriate food security

It is essential in the post-war reconstruction period that exclusive breastfeeding for the first six months of infant life and partial breastfeeding for a further six months is vigorously promoted and protected. The unscrupulous marketing and promotion of breast-milk substitutes must be monitored and prevented. Any reliance on external food supplies during a post-war situation must be counter-balanced by medium-term strategies to promote household food security, where possible through the consumption of locally available and culturally appropriate foods.

## Housing and Urban Development

Iraq is facing a serious housing shortage which, unless addressed as a matter of urgency, could have a severe negative impact on the overall quality of life and urban development. A consensus has emerged that the solution to Iraq's housing shortage lies in a market-driven system founded on a strong housing finance system which can scale-up housing loans for moderate and low-income families. Creating a viable housing finance system requires new financial agencies such as a Mortgage Guarantee Company. These companies can help alleviate the shortfall in housing units by: generating a greater volume of mortgage lending; lowering down payment requirements; broadening the eligibility for mortgages; and extending mortgage repayment periods. The governments integrated housing and urban development strategy aims to generate sustained investment in housing, promote entrepreneurship and create job opportunities. The strategy will require improvements to the policy, legal and regulatory framework including:

- Reviewing existing land use patterns, zoning regulations, building codes and standards and formulate forward looking land use and development policies for efficient and optimum utilization of land.
- Developing a new strategic Master Plan for Baghdad and all other municipalities utilizing modern technologies and latest city profile data.
- Reviewing existing laws with a view to amending or repealing or promulgating new laws so as to strengthen the legislative framework for housing and urban development.
- Establishing a transparent and fully automated property rights registration system.
- Creating an enabling environment for public and private housing finances institutions to take root.
- Enact a new Mortgage Law to enable all established banks, including the Real Estate Bank, to participate in financing housing projects.
- Evolve appropriate fiscal incentives for resource mobilization and to encourage house lending.



## Iraq's National Development Strategy

---

- Initiate the process of establishing an appropriate regulatory framework to facilitate public and private partnership.
- Develop legal means for cheaper and more stable construction finance such as allowing partly constructed buildings to have standing in law as assets so they may serve as collateral.

### VII. Strengthening Good Governance and Improving Security

---

One of the most pressing challenges facing Iraq is nurturing good governance. Corruption, which is the abuse of public office for private gain, is arguably the most important component of governance in a natural resource rich country like Iraq. Corruption has many forms. It extends from “petty” forms of administrative bribery to grander forms of corruption such as the tendency of elites (individuals, political parties or private companies) to illegally and unethically shape the formulation of state laws, policies and regulations. The grand type of corruption (known as *state capture*) requires broader external accountability measures---including asset declaration, transparency surveys, disclosure of parliamentary votes and investigative journalism and citizen oversight. Traditional anti-corruption methods that rely solely on internal bureaucratic structures and new public agencies have often failed because they do not take account of this invisible web of influence.

Democracy is a cornerstone of good governance. Iraq held its first democratic elections in January 2005 ushering in a new era of democratic freedoms based on respect for human rights and the rule of law. Democracy provides an enabling environment for Iraqi's diverse people to interact in a participatory and transparent manner. Government policies actively promote freedom of speech and public dialogue. To safeguard our democratic freedoms the new Constitution will need to embrace the principles of non discrimination due to race, color, gender, language, religion, political opinion, national or social origin, or wealth.

To emphasize the importance that the Government attaches to the international covenants of human rights and the rule of law, a new Ministry of Human Rights has been established. The Ministry is mandated to develop policies, programs and interventions at the national and community levels in support of human rights.

The second cornerstone of good governance is adherence to the rule of law. The Government is strengthening the rule of law and public order. A high priority in this area is that Iraq must both defeat terrorism and develop a capacity for law enforcement, judicial, and correction systems to establish rule of law and create a secure and prosperous environment for public order.

Integrated policies and procedures within the entire scope of the criminal justice system, including high-level policy coordination and technological systems and procedures of coordination and communication, to maximize effective apprehension, investigation, prosecution, and confinement of offenders with respect for their human rights will be required.

# Iraq's National Development Strategy

---

## **Eradicating Corruption**

Iraq has a history of massive corruption. The previous regime bankrupted the country through massive embezzlement of public funds for personal palaces and other conspicuous and wasteful consumption at the expense of the average citizen. In the new democratic Iraq, it is imperative, that measures be put in place to eradicate corruption in all its manifestations. Iraq has immense oil wealth which leaves it open to the possibility of *state capture*. A form of grand corruption in which business or political elites manipulate the system to win procurement contracts, use favoritism or nepotism to get preferential treatment on jobs, and avoid taxes. The appropriate strategy to deal with such corruption needs to be “voice and incentive driven”. By this we mean using empirically based monitoring tools (e-governance), empowering non-traditional stakeholders, providing checks and balances on public institutions. The strategy will entail

- a. Establishing a Leadership Code of Conduct and Ethics requiring inter alia declaration of wealth by public officials
- b. Strengthening the Public Integrity Commission and decentralize its activities to the regions to eradicate corruption.
- c. Continue strengthening the Board of Supreme Audit and decentralize its activities to the regions to ensure transparency in public financial management.
- d. Enhancing corporate ethics and transparency.
- e. Implementing the new public procurement regulations for Ministries and public agencies for proper and effective use of State funds.
- f. Establishing e-government to increase transparency and modernize governmental business processes.

## **Law Enforcement**

Iraq has become an arena in the war on terrorism. The Iraqi Security Forces (ISF) are newly reconstituted and designed to enforce Iraqi law while providing due process and respect for human rights. Along with institution building, the ISF faces the challenge of combating internal and external terrorist threats infiltrating Iraq. Many tens of thousands of ISF have been trained and equipped to date. These brave forces are deployed nationwide and have reestablished law and order in most provinces and are strengthening control of border areas and the remaining provinces. The ISF conduct their duties under civilian authorities accountable to the public. The Iraqi people and their elected government have the right to know about ISF policies, organizations, financial matters, and operations.

Through their heroic efforts, reconstruction and economic development is progressing. As demonstrated by their success on January 30<sup>th</sup>'s election day, ISF continues to exercise their ability to maintain public order and are steadily improving the lives of Iraqi citizens.

### **Emergency Issues:**

- a. Train, equip, and mentor ISF in technical skills and concepts of enforcement
- b. Build ISF capacity in Management, Fiscal Responsibility, Administration and Leadership
- c. Foster law enforcement Culture of “Protect and Serve”

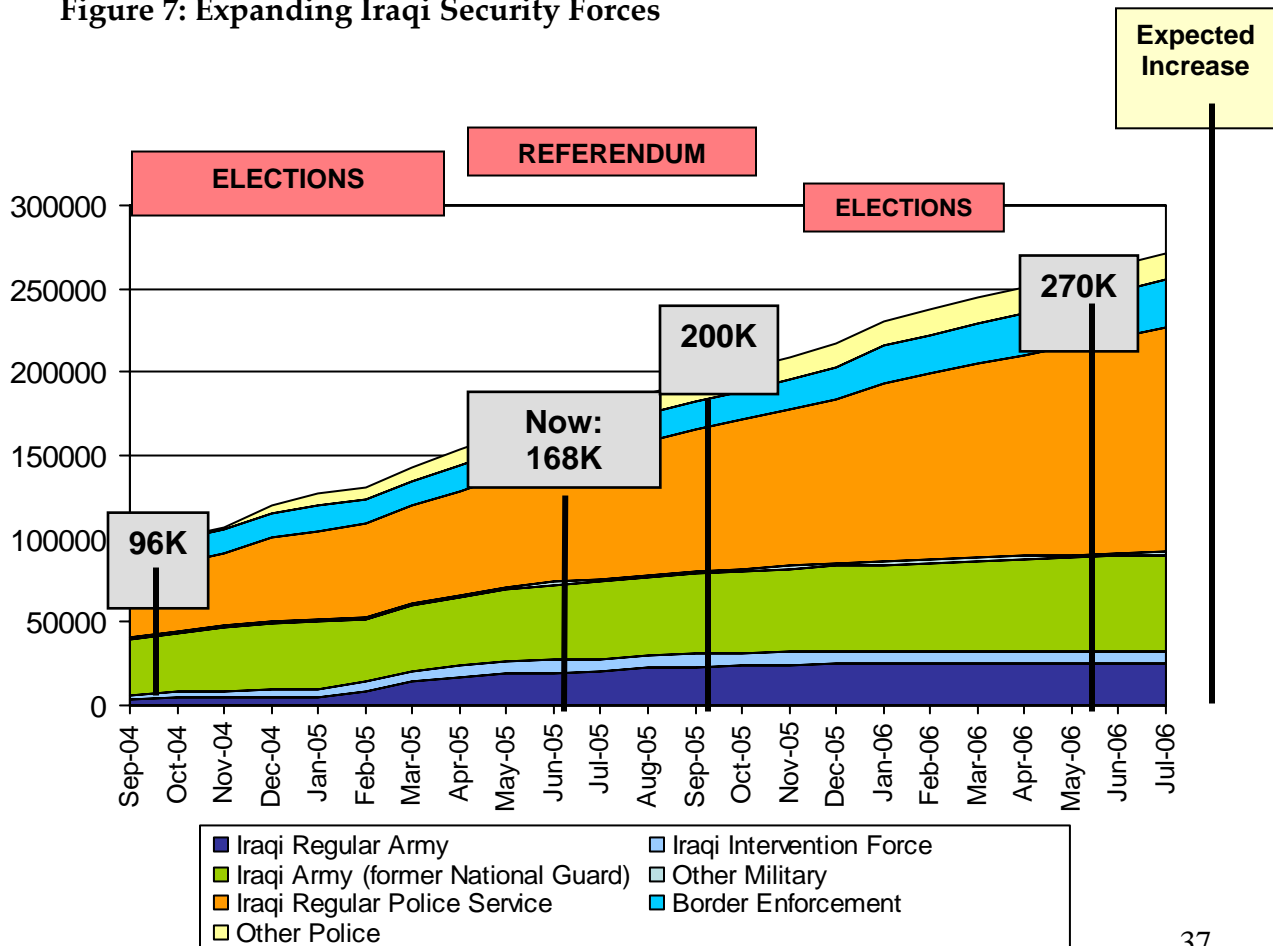
## Iraq's National Development Strategy

- d. Develop centralized administrative and finance management systems
- e. Bolster ISF Station Infrastructure and Operations
- f. Establish policy, procedural and systemic integration and oversight with the corrections system and the judiciary
- g. Develop investigative and forensic capability that respects the rights of those accused
- h. Strengthen control of borders including immigration and customs enforcement
- i. Develop sufficient communication capabilities to engender and enhance provincial public order.

### Specific Immediate Requirements:

- a. Training and equipment for the ISF .
- b. Building senior Iraq law enforcement leadership and command capacities through technical assistance and mentoring in Iraq and internships.
- c. Development of mid-level and first-line supervisory skills through a combined program of Iraq-based training, technical assistance and mentoring.
- d. Implement personnel and payroll management system.
- e. Encourage necessity of close coordination between law enforcement and judicial investigators
- f. Build investigative and forensic capability through training and equipment
- g. Automate case management system

**Figure 7: Expanding Iraqi Security Forces**



# Iraq's National Development Strategy

---

## Judiciary

An independent judiciary provides fair and equitable justice with respect for human rights. Brave and dedicated judges, prosecutors, and staff perform their duties on a daily basis in a challenging security environment. Today, a full-staffed judiciary is conducting both criminal and civil proceeding in all regions of Iraq.

## Emergency Issues -

- a. Build infrastructure for Iraq's court facilities.
- b. Increase court administrative capacity for case management.
- c. Improve security for members of the judiciary and court facilities.
- d. Establish policy, procedural and systemic integration and oversight with the corrections system and the judiciary.
- e. Strengthen the legal profession in support of the judicial process that includes substantive and procedural knowledge, legal research, standards, licensing, higher legal education, and human rights training.

## Specific Immediate Requirements –

Technical assistance and training for the Iraqi High Judicial Council (HJC) to design and implement new policies and procedures including:

- a. Merit-based, transparent procedure for nominating and promoting candidates to fill judicial and prosecutorial positions.
- b. Transparent procedures for investigating allegations of misconduct and incompetence in the judiciary.
- c. Annual budget based upon objectives and technical support.
- d. Mechanisms for interfacing with the executive and legislative branches to provide information on the role of the HJC in a reformed judiciary.
- e. Expanded training programs for judges, judicial investigators, and court staff.
- f. Support court house construction and renovation.
- g. Support and training for legislative drafting.
- h. Support for administrative judiciary training.
- i. Improved transparency and management of the office responsible for ensuring enforcement of judicial decisions.
- j. Improved security for members of the judiciary and court facilities.
- k. Modern computerized case management systems to schedule cases; coordinate attendance of prosecutors, complainants, witnesses, and police; and allow lay persons to view court schedules.
- l. New techniques and technologies in court administration, including docket management, case assignment, collection and analysis of statistics, and training judges and court administrators to use these new systems.

## Iraq's National Development Strategy

---

- m. Support for the Iraqi bar in training lawyers in court administration and case management.
- n. Support for an effective, transparent and equitable public defense system.
- o. Building and strengthening networks of defense attorneys and legal service providers to improve access to justice for the citizenry, especially the traditionally disenfranchised and the poor.

### Corrections

The Iraqi Corrections System should provide safe, secure and humane treatment for the accused while awaiting trial and convicted felons. Iraq is currently building state-of-the-art prison facilities that will meet international standards for correctional confinement. Correction officers have been trained in modern methods to ensure that prisoner human rights are upheld.

### Emergency Issues -

- a. Build capacity of MOJ and management and administration of Prisons with adherence to international standards
- b. Improve prison infrastructure and operations
- c. Train and mentor correction system personnel in relevant international standards and human rights accords
- d. Establish policy, procedural and systemic integration and oversight with law enforcement and the judiciary including
- e. Strengthen system for oversight, accountability, and enforcement of prison personnel and operations
- f. Implement rehabilitation programs to reform and train detainees

### Specific Immediate Requirements –

- a. Training of Iraqi Correction System personnel including human rights and managerial subject matter
- b. Furnish and equip correctional facilities
- c. Training of MOJ personnel in administration and management
- d. Rehabilitation programs to return detainees to society

Iraq is now a democratic country. Law enforcement must adapt to this reality, by using modern policing methods which are human-rights consistent. An independent judiciary serves to guarantee such individual freedoms, while the individual is responsible for abiding by the law. The rule of law is more than obedience to the law. There is the need to reform the Iraqi judicial system by revising the criminal and commercial codes to meet modern standards and to ultimately integrate law enforcement, judiciary, and corrections system.

Further, the Government will not permit unlawful detention and abuses of detainees. The inhumane methods of the previous regime are not acceptable in the new Iraq. Those who violate human rights will be prosecuted for crimes against society.

We recognize our valuable partnership with Coalition Forces, but their role has now changed. It is time for the Iraqi Government to step forward and bear the responsibility of this battle. One thing remains the same. The ISF have earned the respect of the Iraqi people and will do their best

## Iraq's National Development Strategy

---

to maintain the honor that you have shown to our country and its people. It is the ISF mission is to protect all the Iraqi people, no matter their ethnic backgrounds or religious beliefs. The actions of the Government must always be lawful and acceptable to the general public, not just one tribe or political party.

Protecting the Iraqi people against internal and external threats, including terrorism and organized crime is primary commitment of the Iraqi Government. Effective policing and prosecution of criminal activity must follow a transparent rule of law-governed process.

### VIII. Implementing the Strategy

---

#### Enhanced Donor Coordination Mechanism

Implementing the National Development Strategy effectively will require significant resource transfers from our development partners. Improving on donor coordination is essential for the effective use of foreign resources. In this Section we describe a new Donor coordination mechanism that will promote international outreach to a wider range of Donors; get Donors to Baghdad (from capitals via regional hubs if necessary as an interim measure) and ensure continuity and stability during times of transition. The new mechanism is illustrated in Figure 1.

The first step is to move towards a larger more inclusive “Consultative Group” type forum to supplement the more restrictive IRFFI Donor Coordination Meetings. This new group is to be called the Iraq Reconstruction Forum (IRFO) and will meet semi-annually---preferably in conjunction with the semi-annual IRFFI Donor Coordination Meetings. IRFO will be chaired by the Minister of Planning and Development Cooperation (MOPDC) with the World Bank as the supporting Donor. Membership in IRFO will be open to all reconstruction programming and interested donors.

The primary role of IRFO will be to provide an opportunity for high-level representatives from Donor capitals to evaluate progress towards mutually agreed goals, directly with their Iraqi counterparts. The forum will also establish strategic priorities and one of the meetings will fit into the Iraq budget cycle to enable donors to make pledges to cover any financing gaps.

Below IRFO a new body, to be called the Baghdad Coordination Group (BCG), will be established. The purpose of the BCG is to enable Baghdad-based heads of aid agencies to interact with each other and the Minister of Planning and Development Cooperation on a regular basis. The BCG meetings will be linked to Donors in Amman via Video Conference. It is envisaged that this interaction will enable the BCG to quickly translate strategic/program goals into project deliverables, ensure consistency between sectoral and national priorities, and resolve delays in project implementation. The United Nations will serve as the supporting Donor and the Minister of Planning or his Deputy will chair the monthly meetings. The membership of the BCG is open to all Donors.

At the level below the BCG, we will establish Sector Working Groups (SWGs) composed of relevant line Ministries, cross-cutting Ministries, and Donors. The SWG process will facilitate sector discussions between Donors and government. Supporting Donors will have a presence on the ground in Baghdad and be actively providing significant assistance in that sector. Sector discussions in Baghdad currently happen on an ad hoc basis, and vary widely in form, attendance and content. SWGs will be formed after the MOPDC, in consultation with other Ministries and

## Iraq's National Development Strategy

---

Donors has identified priority areas. An illustrative example of SWGs in nine areas is provided in Figure 1. These are

- Oil;
- Transport;
- Health ;
- Water;
- Electricity;
- Rule of Law;
- Education;
- Housing;
- Private Sector Development

The overall objective of the SWGs is to increase the effectiveness and efficiency of aid coordination in support of the attainment of national development and reconstruction objectives through implementation of the national budget. The SWGs provide the framework that enables donors to finalize their support to each sector in consultation with government, stakeholders and ensure consistency with national development goals. SWGs can also play a role by targeting technical assistance to areas which will help accelerate implementation/unblock bottlenecks. They can also play a role in monitoring and evaluating progress at a strategic level (ideally against indicators developed for the sector).

All Donors are welcome to participate in those SWGs which fall within their focus program areas. Each SWG will assist in policy management as well as monitoring implementation of activities as envisaged under the national budget. In particular, SWGs will assist in preparing their respective budgets for each coming fiscal year. The SWGs will provide a forum for general policy dialogue, monitor the overall implementation of the current budget, report regularly on indicators of progress in the sector and elaborate detailed national programs.

Each sector will be chaired by a lead Ministry (e.g. Ministry of Health in the health sector Working Group) and a supporting Donor(s). The supporting Donor(s) will be expected to provide secretarial, analytical and logistic support to the members of the sector. The SWG will meet as often as every week if and when necessary.

To guide the activities of each SWG, Terms of Reference (TOR) will be prepared by the lead Ministry in consultation with the supporting donor and presented to SWGs for further discussion and agreement. The TOR will detail both general and specific responsibilities for SWG members as well as setting clear benchmarks for the preparation and implementation of projects and programs.

Because Donor capacity in Baghdad is currently limited we recognize that it might be not feasible to start all the sector groups at once. Therefore, three or four SWGs will be set up immediately in line with the Government's short term priorities. There are some cross-cutting areas/sectors in which better co-ordination is urgently needed between donors and ministries, in particular energy (including electricity and oil together), rule of law and housing. We believe that it is important to take a phased approach, demonstrate value added and success, and then replicate more widely as we gain experience and as more donors arrive in Baghdad.

We will retain the US-led "Core Group" telephone conference. It has been useful in facilitating the exchange of information between capitals and Baghdad. However, it is proposed that the Chair of the BCG (Minister of Planning and Development Cooperation) co-chair the Core Group with

## Iraq's National Development Strategy

---

the USA. This could become a mechanism for the Iraqi Government to brief Donors, both in Baghdad and capitals, on the deliberations of the Baghdad Working Group and on the thinking of the Iraqi Government without having to arrange a large meeting.

### **Improving Iraq's Intra-Government Processes.**

Much needs to be done on the Iraqi side to streamline internal government processes so as not to cause delays in project implementation. One important problem has been that the legal mechanism for UN and WB project approval is the Iraqi Strategic Review Board (ISRB), chaired by the Minister of Planning and Development Cooperation.

There has been some confusion whether bilateral Donors who are channelling their funds outside the UN and WB trust fund system need to obtain ISRB approval. As a result, some bilateral Donors have not entered into a legally binding MOU with the ISRB. This has resulted in great confusion with some Donors actually operating with no legal framework and implementing projects without the knowledge of MoPDC or the ISRB.

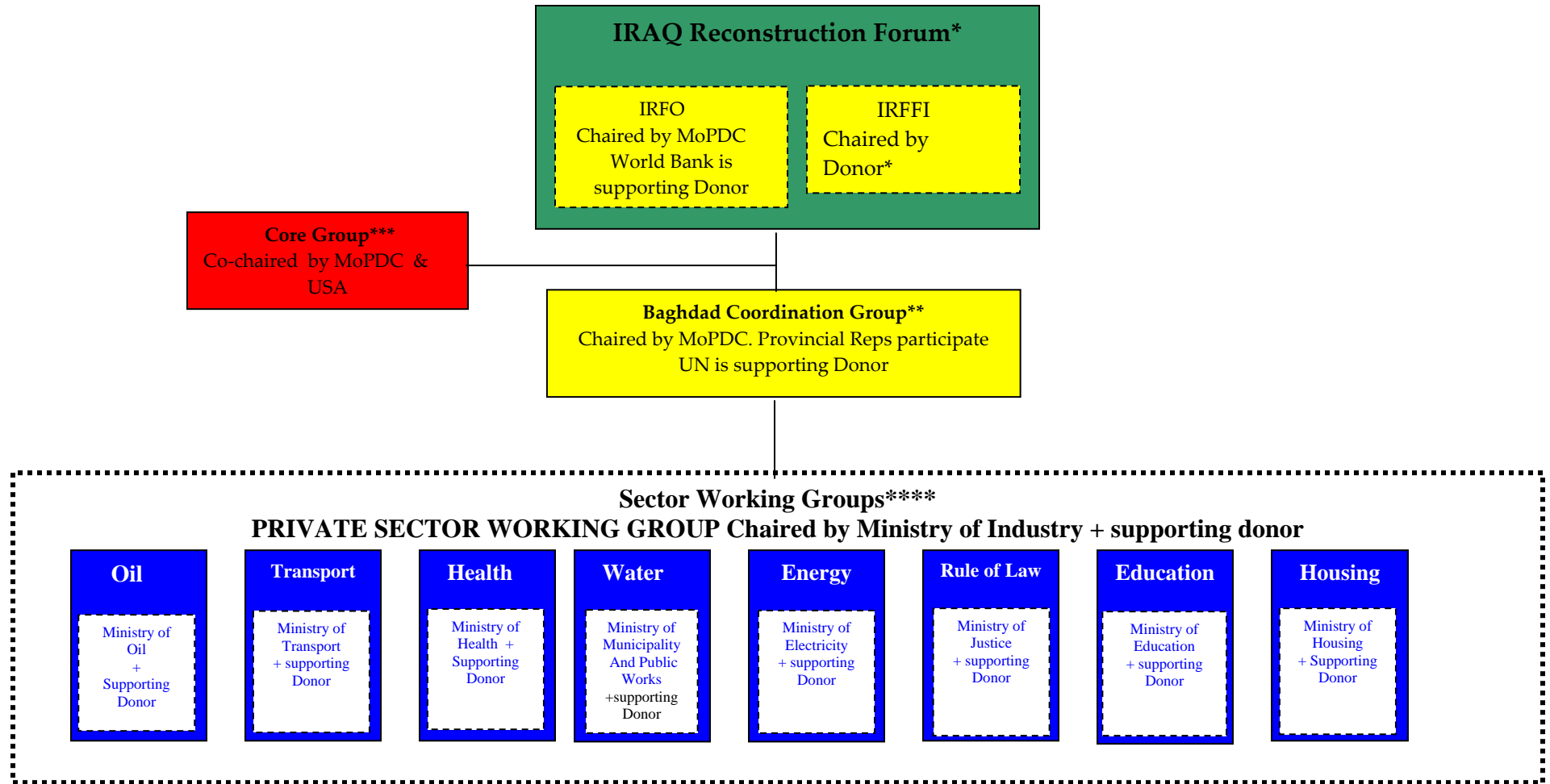
To resolve this legal issue and to facilitate the work-flow process we will retain the Iraqi Strategic Review Board (ISRB) with its current composition, but empower it with a mandate to enter into legally binding agreements with Donors. After approval of the project by the ISRB, each Donor will now need to sign a Memorandum of Understanding co-signed by MoPDC, the Minister of Finance and the respective line Ministry and regional government where appropriate. The MOU will also require the donor to register with the Donor Assistance Database and provide data on a timely basis. The simplified work-flow process is described in Figure 4.

To provide further elaboration of the machinery of government it is useful to focus on the policy setting mechanism. Policy setting within the Iraqi government for the concrete example of the National Development Strategy proceeds as follows, The National Development Strategy is prepared by the Ministry of Planning and Development Cooperation in consultation with line Ministries. The Ministry of Finance works closely with MoPDC because of its key role in determining the medium-term fiscal framework. The draft NDS is discussed by the economic team of the cabinet and presented to the High Economic Council where strategic priorities are discussed in detail and changes and revisions to the draft made. The NDS is then presented to the Council of Ministers. The NDS is an iterative or living document and will constantly be reviewed and updated as priorities shift over time or as new information emerges.



# Iraq's National Development Strategy

**FIGURE 1: ENHANCED DONOR COORDINATION MECHANISM**

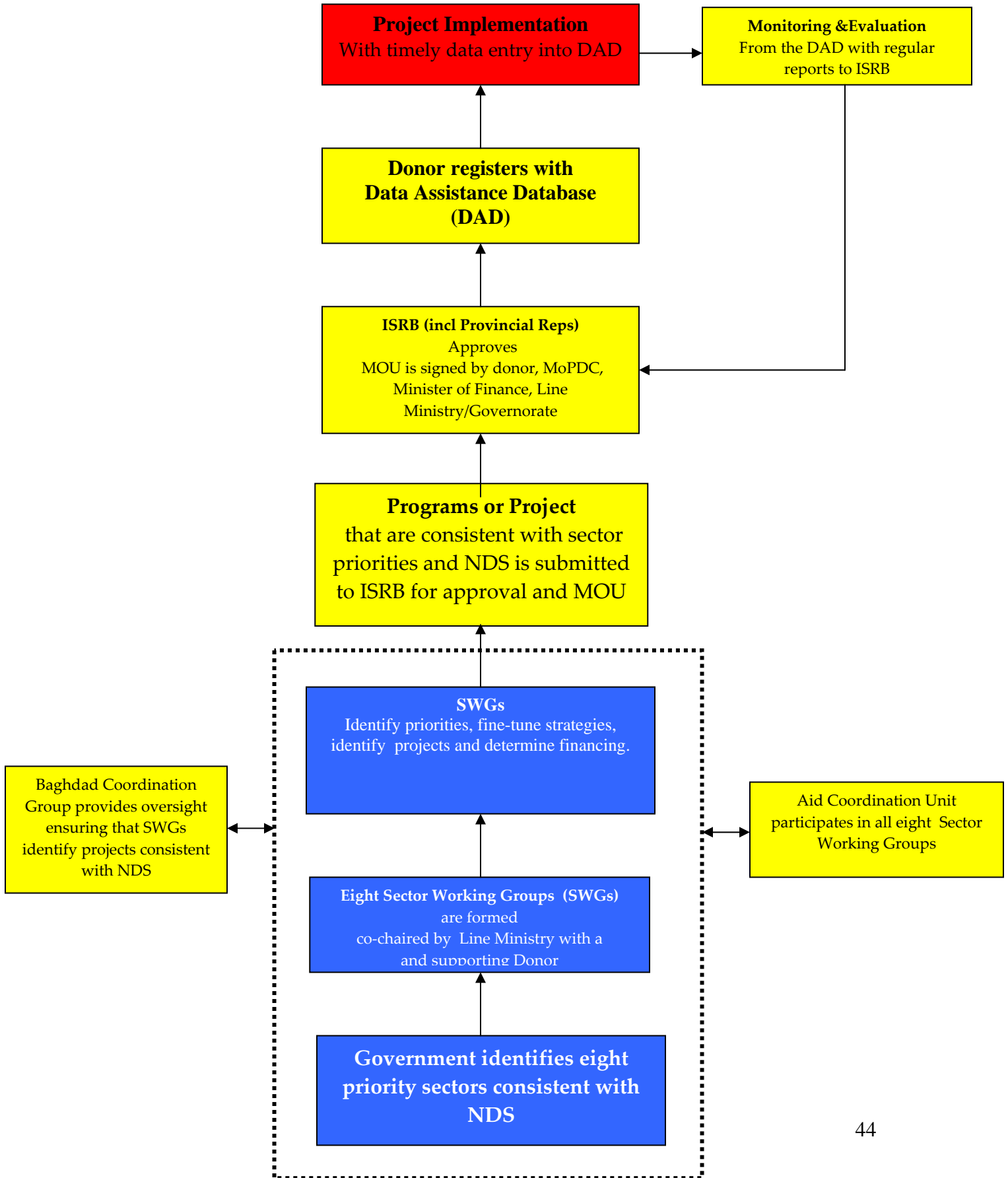


\* Semi-annual meetings of high-level aid representatives from donor capitals and Iraqi Ministers at an international location.

\*\* Monthly meetings of Baghdad-based heads of aid with Minister of Planning and Development Cooperation

\*\*\* Monthly telephone conference with donor capitals, \*\*\*\* Weekly Meeting or as deemed necessary by the group.

## Figure 2: Simplified Project Approval Process



# Iraq's National Development Strategy

---

**Table 4: Quick Guide to the Planning Process**

<b>The NDS:</b>	The national planning framework on which to develop detailed sector strategies.
<b>Sector Planning:</b>	Technical specifications of sector priorities, disciplined by hard budget constraints. Prepared by Sector Working Groups.
<b>Regional Planning:</b>	Implementation plans for sector strategies based on Regional priorities / needs.
<b>National Medium-term Budgets</b>	Annual, rolling 3 year expenditure planning, setting out the medium term expenditure priorities and hard budget constraints against which sector plans can be developed and refined.
<b>Regional Medium-term Budgets</b>	Setting out the medium term expenditure priorities and hard budget constraints against which regional plans can be developed and refined.
<b>Annual Budget &amp; Regional Budgets:</b>	Annual implementation of the 3 year planning framework
<b>Donor; NGO; Private Sector:</b>	Participating and sharing information / ideas in developing sector plans and budgets.
<b>Participatory Processes:</b>	Bottom-up participation of provinces in the planning and monitoring process, as well as providing participatory assessments, and essential feedback on progress towards national development goals.

## Bringing Both Sides Together

Figure 3 (Sector Groups in the Budget Cycle) describes how the new Donor coordination mechanism (i.e., SWGs, BCG and IRFO) fits into the budget cycle. The budget cycle starts with the Ministry of Finance, MoPDC and Ministry of Oil preparing resource projections based on revenues (tax receipts, oil revenues, etc) for the coming year. The division of labor is such that the Ministry of Finance is responsible for the recurrent budget while the Ministry of Planning is responsible for the Capital Investment Budget. The Ministry of Finance and MoPDC then send budget guidelines to line Ministries who in the interim would have been working in their respective SWGs to determine their own priorities and cost them appropriately. During this period of major reconstruction it is expected that sector needs will exceed domestic resources. The role of BCG/IRFO would then be to assist in closing the financing gap after having determined sector

## Iraq's National Development Strategy

---

priorities in close consultation with Iraqi counterparts. A consolidated budget would then be passed including domestic and foreign resources to meet priorities. The Donor Assistance Database will serve as a monitoring tool for Donor resources while the Financial Management Information System (FMIS) will serve as a monitoring tool for domestic resources. Eventually there will be a link between DAD and Government-wide FMIS to ensure full budget integration.

### **Intergovernmental Fiscal Framework and the Planning Process**

There is need to reform the current planning framework because it is a legacy of the central planning system utilized by the previous regime with disastrous results. Decentralization is key to Iraq's vision of transforming itself into prosperous, federal democratic nation. The process of decentralization involves the transfer of responsibilities for identifying local priorities, budgeting, project formulation and implementation to provincial and municipal governments.

A decentralized planning framework would set out the relationship between the NDS and sector plans, between sector plans and province-level plans and between sector plans and the national budget. The link between the NDS, sector plans and the national budget is critical. The NDS provides the overall vision and sets the broad framework for sector plans. The national budget establishes the macroeconomic and fiscal policy framework and identifies the desired outputs and outcomes over the medium-term (typically 3 years).

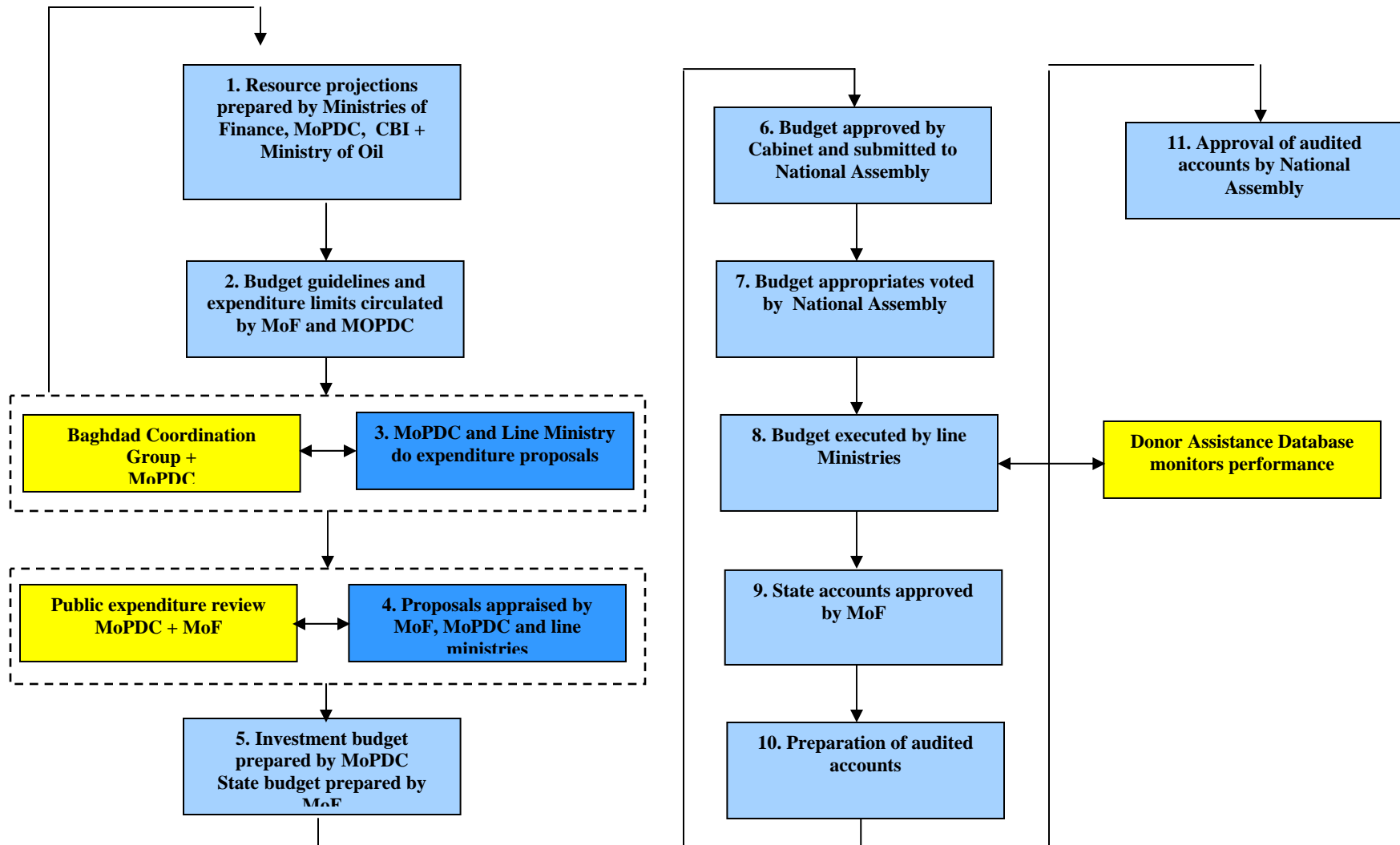
However, sector plans need to be "married" with the national fiscal framework so that they are consistent with resource envelopes. This requires a clear analysis of the link between inputs, outputs and outcomes, in a framework which ensures consistency of sectoral expenditure levels with the overall resource constraint, in order to ensure macroeconomic stability and to maximize the efficiency of public expenditure in attaining predetermined outcomes.

Ultimately, these medium-term objectives need to be consistent with the longer-term objectives defined by the NDS; so the NDS will be used to guide reallocations of expenditures. The sectoral implications of the NDS objectives are reflected in the design of sectoral strategies which should in turn guide the expenditure allocations made each year under the medium-term fiscal framework.

The medium-term fiscal framework should guide all public expenditure including the use of resources committed by Donors. For this reason, a sector-wide approach is preferable wherever feasible. This is an approach under which Government and Donors contribute to a common pool of resources used to achieve the sectoral objectives. The flexibility which this arrangement allows is essential to the efficient use of public expenditures because only in a sector-wide approach can the overall implications of a national program within each sector be considered. Moreover, a sector-wide approach can reduce duplications of effort by different projects and divergences of cost structure between projects and other public activities.

Under such a new framework, sectoral working groups will need to draft sectoral budget framework papers, which then feed into the national budget framework paper which should be coordinated by the Ministry of Finance and Ministry of Planning and Development Cooperation. These papers should give a wide range of input, output and outcome indicators for each sector.

Figure 3: Sector Groups in the Budget Cycle



## **IX. The Way Forward**

Much more needs to be done to streamline Iraq's intra-governmental processes to enable MoPDC and line Ministries to reflect best practices in development management and budget execution. Some elements of a future work agenda are described below.

### **Forecasting**

It is well known that the medium-term fiscal framework prepared by the Ministry of Finance depends on precise (albeit constantly evolving) set of projections for the next three years, yet the overall design of policy by MOPDC needs to take a longer perspective. For this we will need long-term outcome targets, costings of the public expenditures required to achieve these targets, and long-term projections of resource availability. This will necessitate advanced skills in econometrics, statistics, computing and accounting.

### **Monitoring and Evaluation**

For the MOPDC to perform its role effectively it will need to build the foundations of an effective monitoring and evaluation system. Monitoring is critical to the success of the development strategies and needs to be carefully designed for two main reasons. First, it is essential to monitor progress in order to continually inform key stakeholders involved in the process. Encouraging a two-way flow of information between beneficiaries, service providers and policy makers is an essential component of development. In this way, the design and implementation strategies can be continually modified to build on what works, and to avoid repeating mistakes. Second, monitoring helps build accountability. Where targets are set, the Government will expect to account for its successes or failures in achieving them, though it is understood these successes and failures sometimes depend on factors outside Government's control.

Effective monitoring will require several agencies to work closely together. These may include the Macroeconomic Analysis Unit in MOF, the Central Office for Statistics and Information Technology in MOPDC and the Aid Coordination Unit. Two aspects of an effective monitoring system are worth noting.

First, household surveys, labor force surveys, agricultural surveys and industrial censuses will need to be conducted on a timely basis so as to prepare high-quality estimates of trends in employment and human well being. Second, there is a need to develop performance indicators for all sectors. This should be done by sectoral ministries within their Sector Working Groups. Monitoring will be structured at three main levels. First, the monitoring of NDS outcomes. This will focus on progress in reaching Iraq's Development goals including progress in creating jobs, reducing income poverty, improving health, raising educational achievement etc. Most of the information for such outcome monitoring will be drawn from household surveys.

Secondly, the strategy will entail monitoring actions or outputs intended to achieve these outcomes. The intermediate output indicators which have been defined for many sectors will need to be tracked on a regular basis. Data sources will include both sample surveys and data from management information systems.

Thirdly, there will be regular monitoring of the inputs required for actions for development. This is to consist mainly of the tracking of public expenditures on development. Such tracking will include periodic estimates of the benefit incidence of public spending, and of the effectiveness of the sectors in getting funds to institutions which actually deliver public services. In some instances, such monitoring will also involve information on key inputs needed in the sector to deliver its services effectively—teachers and books in education, or drugs supplies in health care facilities. It will also include continued monitoring, and public debate, about the composition of expenditures.

## X. References

**Abrahams, F. and J. Stork**, 2004, “Sideline: Human Rights in Post War Iraq,” Human Rights and Armed Conflict, world Report 2004, [http://hrw.org/wr2k4/6.htm#\\_Toc58744955](http://hrw.org/wr2k4/6.htm#_Toc58744955)

**Ahmad, E.**, ed., 1997, *Financing Decentralized Expenditures, An International comparison of Grants*, Edward Elgar

**Ahmad, E.**, et al., Iraq: Considerations on Intergovernmental Fiscal Relations for the Constituent Assembly, IMF working paper WP/05/69

**Barro, Robert**. 1991 “Economic Growth in a Cross Section of Countries.” *Quarterly Journal of Economics*, 106, 407-433.

**Barro, Robert**. 1996. “Democracy and Growth.” *Journal of Economic Growth* 1(1): 1-27.

**Brown, L and D. Romano**, 2004, “Women in Post –Saddam Iraq: One Step Forward or Two Steps Back?” <http://www.mcgill.ca/icames/events/iraq/Iraq/Montreal>: McGill University, Interuniversity Consortium for Arab and Middle Eastern studies (CAMES) Working paper

**Cukierman, Alex, Steven Webb and Bilin Neypati**. 1994 “Measuring Central Bank Independence and its Effects on Policy Outcomes,” International Center for Economic Growth Occasional Paper No. 58:1-62

**Dollar, David and Lant Pritchett**. *Assessing Aid: What Works, What Doesn't and Why*. 1998. Oxford University Press for the World Bank, Washington DC.

**Deaton, Angus.**, 2001 “Counting the Worlds Poor: Problems and possible solutions” *The World Bank Research Observer* 16(2): 125-147

**FAO & WFP** 2003, Food Supply and Nutrition Assessment mission to Iraq, Rome: Food and Agriculture Organization of the United Nations and World Food Program

**Foote, C.** et al., 2004 Economic Policy and Prospects in Iraq, Federal Reserve Bank of Boston, Boston Massachusetts

**Iraq**, Coalition Provisional Authority, March 2004, *Interim Law of Administration for the State of Iraq*, Baghdad.

**Iraq**, Coalition Provisional Authority, June 2004, *Financial Management Law*, Baghdad

**IMF**, 2004, Iraq: Use of Fund Resources—Request for Emergency Post Conflict Assistance, Washington, D.C. International Monetary Fund

**International Crisis Group**, 2004 Reconstructing Iraq, Amman/Baghdad/Brussels: International Crisis Group

**Iraq Living Conditions Survey 2004 Volumes I an II (2005)** Ministry of Planning and development Cooperation

**Mauro, Paolo.** 1995. Corruption and Growth.” *Quarterly Journal of Economics* 110(3): 681-712.

**Rauch, James and Peter B. Evans** (2002) “Bureaucratic Structure and Economic Performance.” *Journal of Public Economics* 734, 49-71

**Roberts, L** et al., 2004, “Mortality before and after the 2003 Invasion of Iraq: cluster sample survey” *Lancet* 364: 1857-64

**Tanzi, Vito and Hamid Davoodi**, 1997 “Corruption, Public Investment and Growth” IMF Working paper WP/97/139

**UNDP**, 2002 Arab Human Development Report 2002, New York UNDP

**UNESCO**, 2003 Situation Analysis of Education in Iraq, Paris: UNESCO

**WFP**, 2004 Baseline Food Security Analysis in Iraq, Rome World Food Programme

**World Bank**, 2004 a “Millennium Development Goals: About the Goals”  
[www.developmentgoals.or/About\\_the\\_goals.htm](http://www.developmentgoals.or/About_the_goals.htm)

**World Bank**, 2004b, MENA Development Report, Gender and Development in the Middle East and North Africa, Women in the Public Sphere, Washington D.C.: The World Bank



## XI. Annexes

### Annex 1: Indicators for Iraq's Development Goals

**Indicators for Iraq's Development Goals & Expected Achievements for Target Years:  
2007 (short-term) and 2015 (long-term)**

	<b>Indicator</b>	<b>Most Recent Data</b>	<b>Base Year</b>	<b>Expected Achievement by 2007</b>	<b>Target by 2015</b>
1	Proportion of population below \$ 1 (ppp) per day	11.00	2003	8.73	5.5
2	Poverty gap ratio ( incidence x depth of poverty )	Urban / 87.7 Rural / 86.0	1993	56.43 55.34	43.85 43.00
3	Prevalence of underweight children under – five years of age (%)	11.70	2004	9.68	5.85
4	Proportion of population below minimum level of dietary energy consumption (%)	25.0	1997	17.01	12.5
5	Net enrolment ratio in primary education	79.0	2004	84.25	100
6	Proportion of pupils starting grade 1 , who reach grade 5	89.0	2004	91.87	100
7	Literacy rate of (15 – 24 ) year olds	71.0	2004	77.95	100

	<b>Indicator</b>	<b>Most Recent Data</b>	<b>Base Year</b>	<b>Expected Achievement by 2007</b>	<b>Target by 2015</b>
8	Ratios of girls to boys in primary education	85.5	2004	89.23	100
9	Ratios of girls to boys in secondary and tertiary education	70.8	2004	77.79	100
10	Ratios of girls to boys in university education	63.3	2004	71.71	100
11	Ratios of girls to boys in high education	54.0	2004	63.88	100
12	Ratio of literate females to males of ( 15 – 24 ) year – olds	91.4	2004	93.67	100
13	Share of women in wage employment in the non – agriculture activities	16	2004	19	32
14	Proportion of seats held by women in national parliament	25	2004	30	50
15	Under – five mortality rate	131	1999	76	44
16	Infant mortality rate	108	1999	62	36
17	Proportion of 1 year – old children immunized against measles	66.4	2003	76.11	100
18	Maternal mortality ratio	193	2004	132	48
19	Proportion of births attended by skilled health personnel	89.23	2004	92.02	100
20	Condom use rate of the contraceptive prevalence rate	28.85	2004	34.9	57.8
21	Proportion of population in malaria risk areas using effective malaria prevention and treatment measures	18.3 / Prevent 7.4 / Prevent	2000	40.41 15.84	100 100
22	Prevalence associated with malaria	13	2004	7	0

	<b>Indicators</b>	<b>Recent Figures</b>	<b>Base Year</b>	<b>Expected Achievement by 2007</b>	<b>Target by 2015</b>
23	<b>Prevalence and death rates associated with tuberculosis per (100000) peoples</b>	51	2003	25	0
24	<b>Proportion of tuberculosis cases detected and cured under directly observed treatment short course (COTS)</b>	78	2003	84.74	100
25	<b>Proportion of land area covered by forest</b>	4	2003	6	10
26	<b>Carbon dioxide emissions (per capita) and consumption of ozone – depleting CFC,s (odp tons)</b>	3.08 / ton 111.8 / cubic meter	2000	2.23 80.9	1.54 55.9
27	<b>Proportion of population using solid fuels</b>	35	2003	28	18
28	<b>Proportion of population with sustainable access to an improved water source ,urban and rural</b>	54 /SUM 60/ urban 33/ rural	2004	59 65 40	75 80 65
29	<b>Proportion of urban population with access to improved sanitation</b>	72/ urban 70 / rural	2004	76 74	86 85
30	<b>Proportion of households with access to secure tenure (owned or rented</b>	76/ owned 15/ rented	2004	79 22	88 57

	<b>Indicators</b>	<b>Most Recent data</b>	<b>Base Year</b>	<b>Achievement by 2007</b>	<b>Target by 2015</b>
31	<b>Unemployment rate of (15 -24 ) year-olds, by gender and total</b>	43.8 / SUM 46.0/ m 37.2/ f	2004	36.3 38.1 30.8	21.9 23.0 18.6
32	<b>Telephone line and cellular subscribers per (100) population</b>	5.1	2004	6.2	10.2
33	<b>Personal computer in use per (100) population</b>	3.6	2004	4.3	7.2
34	<b>Satellite use per (100) population</b>	32	2004	38.7	64

**Source: Central Office of Statistics and Information Technology, Ministry of Planning and Development Cooperation**

Annex 2: Investment Expenditures by Cluster 2005-2007

Investment Expenditures by Cluster 2005-2007

Seq.	Cluster	External Sources (USD) *	%	Domestic Financing (USD) *	%	Total (USD) *	%
1	Oil and Gas Industry.	1,961,982,155	12.8	9,353,640,000	49.2	11,315,622,155	32.9
2	Education and Health.	1,854,447,697	12.1	436,507,000	2.3	2,290,954,697	6.7
3	Potable Water and Sanitation.	1,894,597,878	12.3	699,595,000	3.7	2,594,192,878	7.5
4	Electricity.	3,143,630,499	20.5	914,580,000	4.8	4,058,210,499	11.8
5	Transport, Telecommunication and Housing.	1,243,629,144	8.1	1,476,737,000	7.8	2,720,366,144	7.9
6	Agriculture, Water Resources and Food Security.	1,264,840,989	8.2	627,318,000	3.3	1,892,158,989	5.5
7	Finance, and Private Sector Development	678,460,564	4.4	998,622,000	5.3	1,677,082,564	4.9

<b>8</b>	<b>Government Institution, Rule of Law, Civil Society and Media.</b>	<b>686,500,446</b>	<b>4.5</b>	<b>350,536,000</b>	<b>1.8</b>	<b>1,037,036,446</b>	<b>3.0</b>
<b>9</b>	<b>Cross - Cutting Themes, Human Rights Gender, Environment and Social Affairs.</b>	<b>116,358,919</b>	<b>0.8</b>	<b>86,888,000</b>	<b>0.5</b>	<b>203,246,919</b>	<b>0.6</b>
<b>10</b>	<b>Kurdistan Region, (Excluding Oil and Electricity).</b>	<b>2,519,784,992</b>	<b>16.4</b>	<b>1,558,940,000</b>	<b>8.2</b>	<b>4,078,724,992</b>	<b>11.9</b>
<b>11</b>	<b>Development of Other Regions</b>	<b>0</b>	<b>0.0</b>	<b>2,500,000,000</b>	<b>13.2</b>	<b>2,500,000,000</b>	<b>7.3</b>
	<b>CLUSTERS (1-11) Grand Total.</b>	<b>15,364,233,282</b>	<b>100</b>	<b>19,003,363,000</b>	<b>100.0</b>	<b>34,367,596,282</b>	<b>100.0</b>

**\* Allocations for Kurdistan Region has been excluded from (1-9 & 11) clusters.**

### Annex 3: Projects distributed by geographical location (2005-2007)

**Projects**  
Distributed According to Geographical Location in Iraq (Funded by Donors and Investment Budget)

(Thousand USD)

Seq.	Governorate	Investment Budget 2005-2007	%	Donations and Loans	%	Total	%
1	Baghdad	1,608,900	16.9	2,842,901	18.5	4,451,801	17.9
2	Al-Basrah	379,224	4.0	2,797,456	18.2	3,176,680	12.8
3	Nineveh	330,775	3.5	1,016,312	6.6	1,347,087	5.4
4	Al-Anbar	226,740	2.4	881,840	5.7	1,108,580	4.5
5	Salah Al-Deen	240,613	2.5	722,882	4.7	963,495	3.9
6	Diala	210,716	2.2	315,283	2.1	525,999	2.1
7	Babylon	165,583	1.7	423,910	2.8	589,493	2.4
8	Al-Tameem	141,433	1.5	251,863	1.6	393,296	1.6
9	Al-Najaf	132,194	1.4	272,947	1.8	405,141	1.6
10	Al-Muthanna	84,547	0.9	310,662	2.0	395,209	1.6

11	Maysan	150,101	1.6	168,366	1.1	318,467	1.3
12	Kerbala	139,327	1.5	1,504,142	9.8	1,643,469	6.6
13	Al-Qadisiya	132,759	1.4	266,425	1.7	399,184	1.6
14	Wasit	160,871	1.7	744,501	4.8	905,372	3.6
15	Thiqar	229,249	2.4	324,958	2.1	554,207	2.2
16	Kurdistan Region	1,891,706	19.8	2,519,785	16.4	4,411,491	17.7
17	Other Regions	3,310,000	34.7	0	0.0	3,310,000	13.3
	<b>Total (Excluding Oil)</b>	<b>9,534,738</b>	<b>100.0</b>	<b>15,364,233</b>	<b>100.0</b>	<b>24,898,971</b>	<b>100.0</b>
	<b>Total With Oil</b>	<b>19,003,363</b>		<b>15,364,233</b>		<b>34,367,596</b>	



