



STATEMENT BY MR. MOHIELDIN, MR. ALHOSANI, AND MR. AL-KOHLANY ON IRAQ

EXECUTIVE BOARD MEETING

MAY 13, 2024





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On behalf of the Iraqi authorities, we extend our sincere appreciation to Mr. Guillaume and his team for the constructive policy discussions during the Article IV mission, and for the insightful Article IV Consultation report.

Iraq has shown commendable progress in overcoming the significant effects of two decades of ongoing conflicts, including the devastating war against ISIS, compounded by the global COVID-19 pandemic and ongoing geopolitical tensions. These challenges, though rooted in the past, persistently influence the structure of the Iraqi economy, necessitating the government to focus on stability and social cohesion. This focus is critical as the authorities pursue a gradual and sustained pace of reforms aimed at maintaining economic stability and addressing the broad needs for growth and reconstruction.

The formation of the new government under Prime Minister Al-Sudani in October 2022 brought an end to a period marked by political stalemates and social unrest, which had previously led to considerable delays in forming the Parliament, selecting the Prime Minister, and passing annual budgets. These delays have led to pent-up demand for public services and delayed legal entitlements, including legally mandated hiring. This has added complexity to current economic challenges and placed significant, unprecedented, and unavoidable pressure on the 2023-2025 budget. Since the establishment of the new government, there has been a demonstrable commitment to advancing economic reforms and enhancing fiscal management, as evidenced by the successful implementation of the first-ever three-year budget and the authorities' successful efforts to normalize the foreign exchange market, which have been key to strengthening the economy, reducing inflationary pressures, and setting the stage for sustainable recovery.

While acknowledging the economic challenges and pressures from successive conflicts and the historical difficulties in passing budgets, the Iraqi government remains steadfast in its commitment to ensuring fiscal and debt sustainability and strengthening the basis for sustainable growth. The request for the Fund's support under the Policy Coordination Instrument underscores the authorities' proactive approach to reform. With Fund support, the authorities aim to implement their homegrown reform program, focusing on increasing non-oil revenues, maintaining sustainable debt levels, and stabilizing the currency. The authorities look forward to constructive engagement with the IMF to discuss and agree on the elements of an ambitious yet realistic PCI, drawing on the guidance offered by the Fund's FCS Strategy.



Fiscal Policy:

The approval of the 2023-2025 budget by the government of Iraq represents a strategic shift towards sustainable fiscal management and multi-year planning, breaking with the past practices hampered by periods of instability. This proactive approach not only addresses immediate needs for spending on public services and infrastructure but also lays the groundwork for addressing long-term economic goals amid fluctuating oil prices. The budget incorporates a conservative oil price estimate of \$70 per barrel, showcasing fiscal prudence against the actual oil price for 2023, and against the higher projected WEO prices for 2024 and 2025, thus highlighting a cautious revenue estimation approach.

The government recognizes the importance of fiscal adjustment to stabilize debt levels over the medium term. The government is rigorously evaluating options to narrow the scope of legally mandated hiring as part of its broader strategy to stabilize the public wage bill through targeted reforms. They have also implemented, effective May 1st, a fuel price increase on premium gasoline. Their efforts to reduce reliance on oil revenues include broadening the non-oil revenue base and enhancing public financial management. Measures underway include reforms in tax policies and the revision of customs tariffs to diversify fiscal sources beyond oil dependency.

Looking ahead, Iraq is committed to enhancing its fiscal framework through the implementation of the Integrated Financial Management System and the Treasury Single Account (TSA), which would significantly improve cash flow management and expenditure transparency, thereby optimizing the allocation and use of financial resources, facilitate more effective budget execution, and reduce the potential for fiscal slippages. Governance improvements are under consideration for extra-budgetary funds to ensure further transparency and accountability. They are also working toward enhancing the efficiency of public investment, especially in infrastructure projects crucial for economic stability and growth.

Monetary Policy and Financial Sector:

The Central Bank of Iraq (CBI) has enacted several measures aimed at stabilizing the national currency and controlling inflation. Notably, in June 2023, the CBI raised its policy interest rate from 4 percent to 7.5 percent and increased reserve requirements from 15 percent to 18 percent. These actions were crucial in curbing the inflationary pressures that peaked earlier in the year and have contributed to a more stable economic environment. Additionally, to address excess liquidity in the market—primarily driven by high government deposits following budget disbursements—the coordination between fiscal and monetary policies has been strengthened. Various liquidity absorption mechanisms, including the issuance of CBI bills and more stringent reserve requirements, have been effectively implemented.

In addition to these monetary policy adjustments, the CBI has also focused on strengthening the structural foundations of Iraq's financial sector. This includes important banking sector reforms



such as requiring the gradual increase of minimum capital requirements for commercial banks from ID 250 billion to ID 400 billion by 2025. This regulatory adjustment is designed to bolster the financial stability of the banking sector by ensuring that banks maintain a stronger capital base. Furthermore, the CBI is actively promoting mergers and acquisitions among smaller banks. This initiative aims to consolidate the banking sector to enhance its efficiency and resilience against economic shocks.

Moreover, in response to the need for more robust anti-money laundering and combating the financing of terrorism controls, Iraq has implemented new compliance measures to improve transparency in cross-border financial transactions. This includes the introduction of an electronic platform that mandates financial beneficiary disclosures, thereby strengthening the integrity of financial flows and aligning with international banking standards.

The modernization of Iraq's banking system, particularly through securing and expanding correspondent banking relationships (CBRs), is crucial for facilitating smoother international trade finance operations. The CBI has been instrumental in assisting local banks in establishing CBRs with major international banks, further integrating Iraq into the global financial system. This not only improves the efficiency of cross-border transactions but also ensures compliance with international banking standards, critical for attracting foreign investment and supporting economic growth.

Efforts to revitalize Iraq's largest state-owned banks (SOBs) are advancing, addressing significant challenges such as undercapitalization and outdated operational frameworks. SOBs are crucial to national financial stability but have struggled due to extensive legacy assets and inefficiencies. The CBI has responded by enhancing their supervisory role and imposing stringent prudential requirements. Furthermore, international experts have been engaged to conduct thorough asset quality reviews, aiming to resolve the legacy issues effectively. Governance reforms are also underway to enhance transparency and accountability in state-owned banks.

Structural reforms:

Structural reforms are pivotal in transforming Iraq's economic framework. The government is deeply committed to promoting a private sector-led development, and economic diversification as fundamental to reducing our oil dependency. Iraq's commitment to structural reforms is underscored by a comprehensive national development plan aimed at revitalizing and diversifying the economy beyond its traditional reliance on oil revenues. Recognizing the private sector as a cornerstone of economic resilience, the government has introduced policies to bolster private enterprise, including efforts to reduce regulatory barriers and improve the ease of doing business. Iraq's development plan outlines strategies for diversifying the economy through support of non-oil sectors such as agriculture, manufacturing, and services.



Aiming to accelerate economic growth and improve public services, the government has been actively prioritizing projects that hold high developmental and service value. They have also successfully completed major strategic projects, including the Grand Al-Faw Port and the Karbala Refinery, and have signed contracts on four major projects in oil, gas, and renewable energy sectors. These projects are crucial for enhancing Iraq's infrastructure and industrial capacity. Meeting Iraq's infrastructure, reconstruction, and adaptation needs are also a priority for the government.

The governance, anti-corruption, and transparency efforts continue to be a major focus for the authorities. They have taken steps to streamline bureaucratic processes and improve public sector management, ensuring that Iraq's governance frameworks are robust and responsive to the needs of its people. The Iraqi government has also made strides in combating financial and administrative corruption, addressing these systemic issues to improve governance and public trust. Significant progress has been made in tracking down and recovering stolen funds, as well as prosecuting the perpetrators of these corruption-related crimes, which are considered critical to restoring integrity within public institutions.

Efforts in alleviating poverty and inequality are being enhanced through targeted social programs aimed at the most vulnerable populations, improving access to education, healthcare, and social services which are essential for reducing poverty levels and improving overall economic equity.

In light of the risks to Iraq's water and food security posed by climate change, the Iraqi government is proactively formulating a comprehensive climate strategy. This strategy aims to mitigate environmental impact and adapt to climate change through measures such as reducing greenhouse gas emissions, adopting modern irrigation techniques, and utilizing renewable energy sources. This includes advancing the adoption of drought and heat-resistant crop varieties and enhancing soil management practices to increase agricultural resilience. Iraq's decarbonization pathway involves a strategic phase-out of liquid fuels in electricity generation and a significant increase in the use of natural gas and renewable energy sources, in alignment with Iraq's commitment to reducing emissions and contributing to meeting the global climate objectives.

Technical Assistance Needs:

The authorities reiterate their utmost appreciation for the Fund's continued technical assistance, which are crucial to the authorities' efforts. Recent and ongoing technical assistance is supporting the efforts of the authorities in the area of strengthening Public Finance Management, tax administration, enhancing monetary policy framework and financial supervision and the area of AML/CFT. The authorities have also requested technical assistance to strengthen areas necessary to support their reforms endeavor, specifically related to further enhancing the tax and customs policy and administration, improving monetary policy transmission and liquidity management, as well as improving the robustness and comprehensiveness of their economic data.