Money and Banking Journal

A semi-annual Journal Issued by Statistics & Research Department

First Issue

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Contents

First Issue

Editorial Staff

Editorial

A new window opens for researchers is represented by the Money and Banking Journal issued by the Statistics and Research Department at the Central Bank of Iraq. The journal represents the vision and approach of the bank in supporting working papers and research activities presented by researchers from various specializations, in addition to its inclusion of the summaries of the most important reports published at this bank. All are presented in Arabic and English to the readers and researchers from all over the world. It is possible to view and browse the journal through the official website of the Central Bank.

The Central Bank of Iraq has committed to support researchers by providing access to its comprehensive library, which is rich in resources on various banking, economic, research, and academic topics. Today we are adding a new tributary to the library that serves as a valuable academic resource for anyone interested in economic affairs.

The topics that the journal will cover through its various sections are of much interest to the bank's senior management. The scientific aspect at the level of analysis and statistics constitutes an essential component of the work of Iraqi banking sector employees due to its role in diagnosing the size of the risks, challenges and difficulties facing the sector and the importance of keeping abreast with the latest financial and banking technological developments in a world that is constantly evolving.

We believe that scientific outputs relying on research methodologies form the basis upon which we rely in building our monetary policy based on ambitious strategies, plans and goals aimed at ensuring stability. Our objective is to increase and spread the banking culture in the country, promote financial inclusion and provide the best banking services to all citizens without exception to drive the wheel of growth and reconstruction in our economy.

In conclusion, we invite everyone to contribute to the journal, which targets all researchers and interested parties and value and appreciate any contributions published in its issues. We also congratulate the Statistics and Research Department on the publication of its first issue, as the important topics it covers will hopefully contribute to the advancement of the monetary and banking sector in line with the reform vision outlined by the Central Bank of Iraq.

Ali Mohsen Al-Alaq
Governor of the Central Bank of Iraq

Features of World Economy Mid- 2024

Dr. Ahmed Ibraihi Ali/ Member of the Board of Directors of the Central Bank of Iraq

The world economy witnessed violent volatility since 2007 when the Subprime mortgage Meltdown escalated to a multinational monetary crisis, which contributed to the most severe recession in decades. As commodity markets were sensitive to economic shocks side by side with unstable expectation, oil prices increased sharply and then collapsed to a quarter of their peaks or less in the second half of 2008. Governments of advanced countries made bold bailouts, and central banks adopted different monetary policies based on quantitative easing to provide sufficient liquidity. As a result of such a policy, central banks' balance sheets were expanded by a variety of assets, including poor liquidity purchases, to raise rates of return, not only in the short term. The inflation rate remained low and policy response was lower than expected. However, assisted by the growth of China and Asia in general (except for Japan-with weak growth), economy resumed the normal course of the situation. Then came the corona virus pandemic that represented another grave setback which seriously threatened the integrity of the public finance system and productive activity. During this period, oil prices fluctuated too, and a wave of inflation emerged with a rapid rise early in 2021, which fell after peaking above (8%) in the United States and Eurozone in 2022. The recovery is expected to continue in 2025, and oil prices will not fall below US$75 per barrel in 2024, based on the hypotheses that shape the near future of the world economy, but they reach close to US$74 in 2025. Inflation is at its desired rates in advanced countries and the world economy is growing at a rate of (3.1%) annually for the next five years. We present a brief follow-up of selected areas on the course of change in the past recent period and tomorrow's outlook.

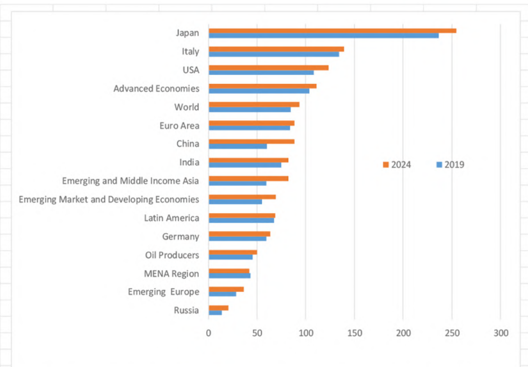
Public Finance:

The world fiscal deficit in 2024 fell to (4.9%) from (5.6%) of GDP of the previous year. In advanced countries, it fell to (2.7%) as the United States is excluded since its deficit remained at (6%) and higher until 2029. Developing and emerging countries remained the same as in 2023. China's deficit increased slightly to exceed (7%) of GDP, as it combined high government spending with large credit coupled with surplus balance of payments. Regarding the group of oil countries, they approached balance with a slight deficit after their surplus in 2022. Inflation, which peaked in 2022, declined to normal rates in 2024 (See the chart below). Given what inflation is representing in the view of advanced countries, its decline helps expand policy options.

We notice that the public debt of governments has increased. Advanced countries with financial depths may find it easy to borrow, backed by central banks at low interest rates. Unless they hit an inflation wave that threatens stability as happened since 2022 when central banks raised the policy rate, which did not decline in the United States until the beginning of April 2024. This means that the monetary policy maintained a relative tightening indicated by central bank's interest rate. Among the results of the large volume of advanced countries' debt is the increasing influence of governments on the functioning of international financial markets and duly the world economy. Public finance was shocked by the corona virus pandemic after the real estate loans crisis, and then by rising inflation related to raw material prices, while policies previously wanted to stimulate inflation through quantitative easing to revive the economy. Public finance worked to cope with these changes as well as monetary policy.

To date, financial policies attempt to return to pre-pandemic situations by bringing expenditure levels closer to revenues, while the government's debt balance is unlikely to be traced back to previous levels. Governments will continue to recycle this debt along with the growing debt of corporations and household sector.

Figure No. (1): General Government Gross Debt % of GDP



Data Source: IMF, Fiscal Monitor, April 2024.

Thus, features of financialization are deepening in the economy of this time, and the relative area of commodity production is shrinking through mechanisms of resource allocation, price formation, income distribution, volatility, business cycle, changes of interest rates, periodic and sudden, changes of market prices of debt instruments and holders' wealth, thus leading to consumption and investment, etc. The accumulation of inflation effects is dependent on raising nominal income towards higher tax rates to keep legislation unadjusted. This phenomenon has a positive effect of reducing the deficit. However, the factors of increased expenditure are strong, including traditional ones related to social justice and the support of the poor, especially in the emerging and developing countries, and others that requires countries' adherence to energy policy requirements to scale the demand for fossil fuels, support research and development in digital technology, address changes of production structure and employment problems of its workforce, and in this context provide financial incentives to increase productivity growth rates. Also, some countries do not avoid increasing military spending either. So, the already mentioned increase in revenue has been confiscated by increased expenditure. As such, the economy is coexisting with a permanent deficit, within limits that make the relative weight of debt endurable. However, the IMF's financial Monitor, April 2024, predicted that the revenue-to-GDP ratio would decrease by less than (1%) until 2029 when the United States and China are excluded, along with an increased interest payments ratio, which is expected as a result of not decreasing the relative weight of debt, thereby enhancing the likelihood of increasing the deficit without reducing it and its implications. It is also expected that governments of several countries will try to stabilize debt-to-GDP ratio but at levels higher than they were before the pandemic. This is what we thought of as a general conclusion that excludes a decrease in the weight of debt.

Undoubtedly, Governments envisage increased spending to raise productivity and growth to expand the tax basis, which is the employment income, profit and consumption and hope to grow tax revenue faster than GDP growth. However, this task requires reforming or changing the institutions of the public finance system and tax administration particularly. The difficulties of reconciling production incentives with social justice and a supportive political environment are also well known. Although it is difficult to meet these elements, practical imperatives will dictate their logic as public finance cannot exceed the scope set by economic potential for a long time.

Low economic growth in the coming years as inflation returns to normal rates, post-crisis rates or low rates, both add obstacles to fiscal sobriety path. Caution against increased deficit is imperative because it weakens the economy's ability to confront new crises. The world economy witnessed two deep crises in a decade, then wars and conflicts intervened in energy supply lines, food, and international financial relations. Each of these crises added burdens to the near and medium future, including indebtedness, postponement of development projects or infrastructure development. With all the preceding factors, IMF's most recent reports expected advanced countries to increase taxes, reduce government spending and restrict government debt, as adopting the point of view that this is in support of economic growth, which is closer to recommending or praising promises with good intentions than to expecting.

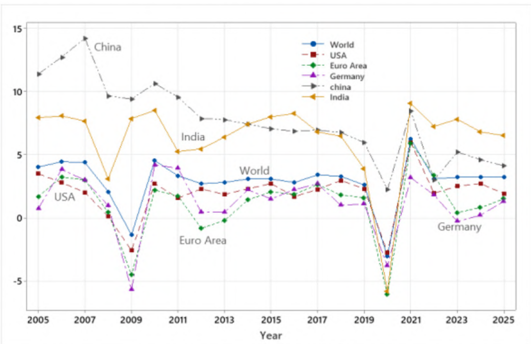
Economic Growth

Economic growth for 2022 and 2023 was not high but lower than that of 2021, while globally it was near or below the post-2005 average. The same happened in China and India, which have been racing China in the growth sphere since 2014. It is expected to become of the highest growth in the coming years. China's resumption of its subsequent high growth, an important lever for the world economy not compensated by India in the foreseeable term, does not preclude considering its large size in industry, external trade and its contribution to the financing of balance-of-payments deficits for other countries, including the United States of America. The most important issue to many followers and stakeholders expressed in the latest IMF World Economic Outlook Report - April

2024, is that the performance of the world economy has eliminated the fears of inflationary stagnation, i.e. the survival of high inflation and dwindling growth, or a sharp recession of economic activity as growth falls. Both had not been achieved, as inflation had fallen rapidly, and growth had maintained a positive rate in the world near the average with inequality among countries and groups.

High total demand spurred by expanding government spending and household consumption helped boost economic growth, accompanied by the improvement of the labor market and the unexpected increase in the labor force's participation in economic activity, and other positive supply-side factors.

Figure No. (2): GDP Growth % Annually

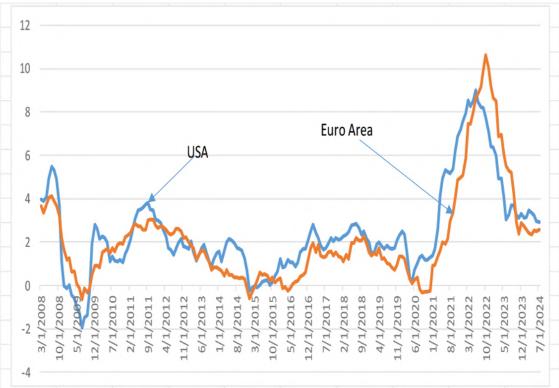


Data Source: WB Data, IMF - WEO, April 2024.

Inflation has fallen and is expected to reach normal rates in advanced countries before the emerging countries, which gives room in the first group for monetary easing but does not see the U.S. Federal Reserve's trend to reduce interest rates soon. Countries' discrepancies in the speed of inflation decline are not excluded, maintaining uneven rates as a reason for changing exchange rates. If interest rates rise, these are among the weak options, and in conjunction with changing exchange rates, the value of invested financial assets falls. Some argue that the continued recovery despite rising interest rates, which were intended to curb inflation, is due in part to the use of accumulated savings by the advanced countries' household sector during the pandemic, as people avoided movement and shopping, a debatable view. Real estate loans and housing markets at low interest rates have for a decade also helped significantly ease the impact of interest rate hikes.

The world economy is expected to grow for 2024 and 2025 by an average of (3.2%), which is estimated for 2023. In advanced countries, (1.7%) and (1.8%) for 2024 and 2025. In China, (4.6%) then (4.1%) down from (5.2%), the question is - has China lost its growth momentum and is still in the category of emerging countries, while the world needs its high growth to offset the decline of commodity production in western countries? To date, China's stay in the middle income trap has been excluded, as has been the case for other developing countries, and the decline in growth explains the problem of the real estate sector, the credit bubble and its expenditure in a cycle from which the economy does not exit quickly, the heavy debt of domestic governments, and perhaps deeper reasons that are for sure related to technology, production system, geographical concentration and the environment.

Figure No. (3): Annual Inflation Rate %



Data Source: FRED.

Annual Expected Inflation %	Japan	USA	Germany	Euro Area
2024	2.2	2.9	2.4	2.4
2025	2.1	2.0	2.0	2.1

Data source: FRED; IMF, WEO - April 2024.

India's growth rate is (6.8%) and (6.5%) for the above mentioned two years, down from (7.8%) in 2023. Growth is below historical rates, and its downward trajectory is observed amid fluctuating and negative shocks. This deficiency can be attributed to the failure to accompany significant technological changes with appropriate growth in productivity. In addition, many of the consequences of the corona virus pandemic remain, as well as the damage of wars on production and investment and their eye-catching risks.

Conflicts, especially where the United States is a party, have worsened international economic relations and spread concern about the future. Disregard bloodshed which has shaken confidence in the international political system, whether we like it or not, ensures stability and prosperity of the world economic cooperation and integration.

Economic growth is the weakest in the eurozone, including Germany, a major economic bloc comparable to both China and the United States. Among the reasons for this performance are energy costs and controls, as well as tight monetary policy and high wage growth, while maintaining workforces that productive enterprises do not need in anticipation of recovery, slow-rising consumer demand and less optimistic consumers than their counterparts in the United States.

Low and middle-income countries' enrolment to advanced and wealthy countries is hampered, and the income gap has widened in the majority. The world fails to reduce the uneven standards of living and the equal utilization of the fruits of civilization. Failure is most evident in the performance of the undoubted duty to the vulnerable and those who have been wronged by fate.

A significant fact that usually disappears behind recipes for ready fiscal and monetary adjustments is the institutional imbalance of the economic system and the deep distortion of the production structure. Political influence and social culture interfere with the revenues of business, profits and distribution of incomes and wealth, all of which, as well as the waste of resources, are distant from the requirements of building and maintaining a solid broad productive base and committing to the tasks of catch-up and economic development.

Finance and Money Markets

Since late 2023, financial markets have been described as optimistic and vibrant; noting the steady decline of inflation towards the levels shown in the figure. Also hoping for monetary ease and lower interest rates. Equity prices rose by (20%) on the global average. These are observations from general market follow-ups that are also optimistic; For example, the US government's 10-year bond yield rose slightly since the end of 2003 and moved below (5%) and did not decline, because the yield was already low. While the Dow Jones stock price index already rose by (19%) between May 2023 and its counterpart from 2024. This is an example of a high yield puzzle for shares compared to other financial investment instruments. Besides, the spread range of sovereign borrowing benefits decreased, hence indicated a reduction of estimated risks, whose margins have been high; the issue that encouraged developing and emerging countries to issue their bonds in advanced countries' markets. Given this optimism, realism requires reminding examples of exaggerated risk away from objectivity without knowledge. The inverse relationship between the sovereign risks and the potential volume of debt must be recalled, including raising sovereign creditworthiness in an assessment conducted by a well-known company, to reduce risks. These include low interest rates on sovereign loans that encourage governments to further borrow to end up with inescapable heavy external indebtedness. Therefore, who ensures that the financial space is more welcoming in the future than at present? This is added to the fact why we believe that export resources are insufficient for these years. Also, tomorrow will overflow the needs of imports and other external payments so that external debt will be paid without creating any hardship for future generations.

The recent International Financial Stability Report, April 2024, praised the solid financial sectors and balance of payments of emerging countries during the period of rising interest rates, as these countries did not form a starting point for instability indeed. The failure of banks in Switzerland and the United States did not spread to other parts of the financial system and the risk of instability declined considerably. It is an experiment that can be built upon to surround flashpoints. Expectations exclude influential declines in financial asset prices, and there is no fear of economic growth in this respect.

The three-month bond yield in the United States was (5.1%) in 2024 and estimated to be (4.1%) in 2025, while it was (3.5%) and (2.6%), respectively, in the eurozone. By observing expected inflation rates, as shown in the chart below, the real rate of return of short-term instruments in the United States and the eurozone is positive, while the first is higher than the second. But Japan's real yield is negative by a large amount using the usual metrics because the interest rate for the two years is zero and then (0.1%). This is evidence of the inconsistency of major countries' economic policies. The nominal yields of the government's bond for 10 years in the United States are (4.1%) then (3.7%), in the eurozone (2.5%) and (2.6%); In Japan (1%) and (1.1%). Real yields remain positive in the United States and the eurozone, while in Japan they are negative by less than its short-term counterpart. As is known, for the same degree of risk, the long-term yield must rise above its short-term counterpart. The yield curve is inverted in the United States, unclear in the eurozone, and typical in Japan, but its real amount is negative.

In today's economy, commercial real estate has become more relevant to the function of banks and financial markets, and its price sensitivity to the interest rate is high and is influenced by the active expectations of demand for credit or refraining it. This relationship has become a cause of instability. Real estate is a loan guarantee, and its price change is a key component of the return compared to the interest rate. This is added to the increased securitization of mortgages and their acquisition by investment banks and other financial institutions. From this entanglement, reports are interested in a (12%) decline in commercial real estate prices during the previous year compared to the global average in terms of the heaviest decline in one year. Countries whose banks have acquired large volumes of mortgages will be affected by falling prices. This decline alone is not enough to trigger a monetary crisis such as the one that began in 2007, because the other parts of the system have sufficient flexibility. Lower prices are not expected to be reflected at the same percentage in a credit failure or decreased prices of traded real estate debt instruments. But this incident alerts to the paramount importance of diversification in protecting enterprises from collapse, as it protects investors from significant losses, though a significant decline in property prices remains a significant risk when met with other negative facts.

In general, the household sector is still able to sustain the debt, and potential credit failure is even described as marginal. The volatility of asset prices has become narrower in scope, hence reflecting market optimism. The correlation between prices in commodity, credit, bond, and equity exchanges remained at typical levels in emerging and advanced countries, hence indicating an acceptable degree of market regularity. Among the most recent recommendations of the International Financial Stability Report to central banks are not to cope with excessive optimism and markets' expectations of the policy price, but rather a gradual transition towards monetary easing. Countries should take sufficient measures to contain debt-related vulnerability. It also advised China to implement robust policies to restore confidence in the real estate sector, which once again underscores the importance of real estate and the increased growing strength of its linkage to credit and financial markets in recent decades. There seems to be a trend imposed by the world experience since the real estate crisis. In recent times, facts have added other reasons to modify working methodologies of banks and monitor systems to pay attention to real estate markets, careful monitoring of real estate credit, conducting tensile, or sensitivity tests to identify risk of credit failure associated with real estate prices. We add that greater caution should be placed on the possibility that banks, and other financial institutions, including investment banks, might be induced into severe real estate speculation that would create a bubble and then cause a wider crisis.

Closing Word:

It is no secret to the reader that the subject is immeasurably broader than the space available for this article. The intention is only to draw attention to the large whole of Iraq's economy within its capabilities and mechanisms. Not only on the part of oil exports and prices, which are identified there, but the ideas and policies that we consider form through dialogue with the realities of the entire world economy.

We have noted the expected growth slightly below the rate, and public finance remains between increased spending pressures and the need to revert to balance conditions. Monetary policy is hesitant between starting easing or hesitation pending adequate identification of stable trends.

The financial and banking markets sector is closer to stability than to turbulence and last, in case of occurrence, it is still on the spot, not affecting the entire system. Positive factors reflected in the constituencies' literature, which help to entrench the system, include high intensity of systematic surveillance and analysis of information, primarily, risk hedging and willingness to encircle and control the imbalance without allowing it to spread. Another issue related to the management of international reserves abroad, where follow-up of central banks' policies and the movement of financial markets understand the seriousness of the task, accuracy of the required follow-up, continuous treatment of information with systematic analysis and the prevention of conflict-related and undeniable political risks. We have also noted the small returns on financial investment other than stocks and these risks are harsh, thus requiring high professional work, and being accustomed to decision after high study, consultation, and transparency.

Monetary Policy and Financial Challenges

Dr. Sameer Fakhri Neamah/Director General of Statistics and Research Department

Introduction:

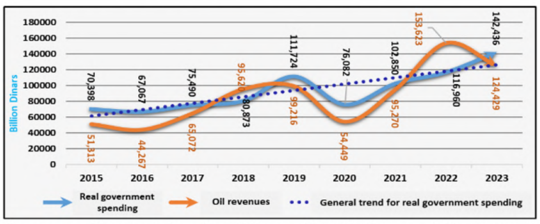
Iraqi economy is considered one of the developing economies that primarily relies on the oil sector for its exports, all views agree that the balance and stability became an exception because the oil sector is the main driver for all other economic sectors with their GDP components, in addition to economic exposure on the outside world due to its reliance on imports. Thus, the breakdown of the productive base due to the low contribution of investment spending to public spending is regarded as one of the most important constraints facing monetary policy and its tools.

As a result of the almost complete reliance on financing public spending from oil revenues and monetary policy dinars, in addition to deducting remittances to cover the financing gap, and by virtue of the independence of the Central Bank, it is tantamount to monetary conditioning to provide financial leverage, which represents a form of financial hegemony, and this represents a refuge for public finance, which has been unable to achieve partial balances in its non-rentier resources through (financial adjustment), if the growth in consumer operational spending, which is linked to the growth of oil revenues is not adjusted towards the redistribution of the rentier effects of the growth of non-oil revenues that is linked to the growth of investment spending through the effect of non-oil output in the interest of adjusting the fiscal deficit itself. Adjusting the exchange rate (devaluation of the currency) is considered the financial effect of monetary policy in unfavorable rentier conditions, causing clear financial dominance over the cash basis. Therefore, the effect on the money supply is considered the greatest restriction that fiscal policy exerted on monetary policy, in addition to several effects that this paper attempts to review.

1. The relationship of public expenditure to oil revenues and the general trend between them:

Usually in countries with a normal situation, government expenditure is financed through tax revenues, but in rentier countries, including Iraq, government expenditures are financed from the local currency at the Central Bank because the government's revenues come from dollar revenues and the link between them is the exchange rate. Therefore, the biggest restriction that monetary policy is exposed to is the pressure on the issued currency channel by restricting oil revenues. In addition, it is more important to finance the budget deficit by deducting remittances through the financing gap, which is approximately twenty-three trillion in the 2023, 2024, and 2025 budgets. This causes pressure in two directions, the first on the general level of prices, expressed in inflation, and the second on the foreign reserves that the central bank possesses to finance the balance of payments deficit by financing imports. From here we would like to say that the process of coordination between the two policies is an absolute necessity.

Figure No. (1): The Relationship Between Public Expenditure and Oil Revenues, and the General Trend Between Them

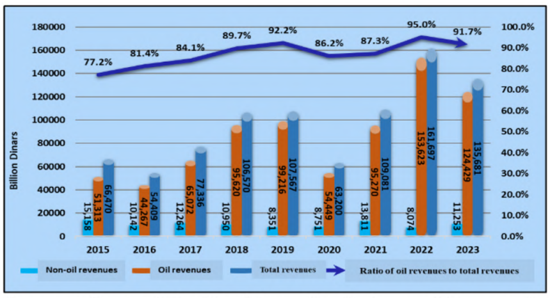


Source: Central bank of Iraq, Statistics and Research Department.

2. The proportion of oil revenues out of total public revenues compared to non-oil revenues:

When monitoring the percentage of oil revenues out of total revenues, it indicates a structural defect in the structure of the economy throughout the previous period, and that the national income is linked to external demand for this unstable resource whose prices are not guaranteed, and even when the contribution percentage decreases, it is not due to the increase in non-oil revenues in total public revenues, but due to the decline in global oil prices. Figure No. (2) shows that relationship which represents a challenge to monetary policy tools with its severity linked to an inverse relationship with the proportion of oil revenues in total revenues, and its impact is clear on the issued currency channel and net foreign reserves.

Figure No. (2): Proportion of Oil Revenues to Total Public Revenue Compared to Non-Oil Revenues



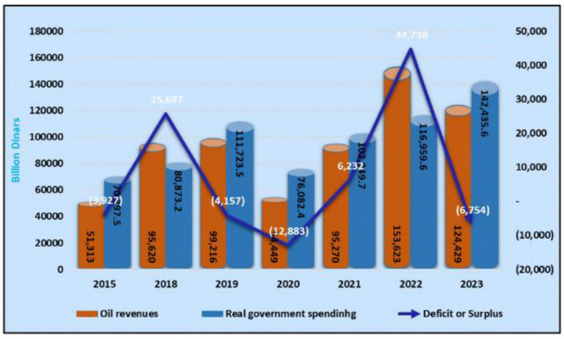
Source: Central Bank of Iraq, Statistics and Research Department.

3. The relationship between operational spending and oil revenues compared to investment spending and its relationship with non-oil revenues:

The growth of consumer operational spending is linked to the growth of oil revenues, which is a fixed cost to the government and inflexible, in contrast to the weak relationship between investment spending and non-oil revenues, and the link between them is the non-oil gross domestic product. The process of investment spending growth is linked to the growth of non-oil output directly affects non-oil revenues, which is a goal for financial and monetary policies.

The process of linking the growth of operational spending to the growth of oil revenues represents an important challenge that is added to the rest of the challenges that monetary policy faces with its tools. Through in-depth studies according to approved scenarios, it is determined that cashed oil revenues must finance government spending at a rate of no less than 70% (that percentage is linked to an inverse relationship with the flexibility of the production system). Otherwise, there will be a deficit in the balance of payments that will be financed by foreign reserves and pressure on the channel of both the exchange rate and the issued currency, so that the effects of this will be reflected in the general level of prices expressed in inflation.

Figure No. (3): The Relationship Between Operational Expenditure and Oil Revenues Compared to Capital Expenditure and Its Relationship to Non-Oil Revenues

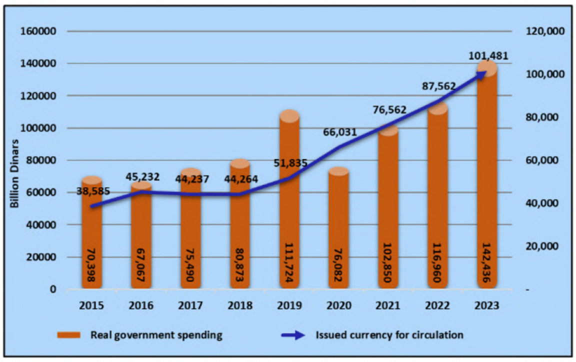


Source: Central Bank of Iraq, Statistics and Research Department.

4. Relationship between government spending and issued currency.

One of the specific and important challenges is the relationship between government spending and the issued currency. The Figure above shows the direction of the relationship between them, as the issued currency curve rises with the increase in government spending in the case of a balanced general budget. Yet, the issued currency curve rises more when a deficit occurs, because of the financing gap being covered by monetary policy through treasury bills. Due to the rentier nature of the economy, there is pressure on the issued currency channel, even if there is a balance in both the government's general budget and the balance of payments. However, the pressure on the issued currency channel is greater when a double deficit occurs, and this deficit is financed through discounted transfers, and the impact of this will be greater on reserves, inflation, and the exchange rate.

Figure No. (4): The Relationship Between Government Spending and Issued Currency

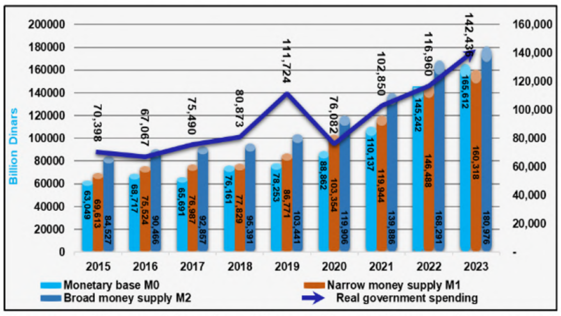


Source: Central Bank of Iraq, Statistics and Research Department.

5. Relationship between government spending and money supply:

One of the important challenges is the link between the movement of the cash basis (M0) and government spending. The link between these relationships is the net credit provided by the central bank to the government as well as the net foreign reserves and the reflection of this relationship on the liabilities side through the issued currency. The effect is more evident when deducting the central bank's transfers on the issued currency channel during a period when revenues are unable to cover actual expenditures. This makes the money supply an internal variable that moves through fiscal policy tools and not monetary policy, and the relationship is clear from the Figure above.

Figure No. (5): The Relationship Between Government Spending and Money Supply

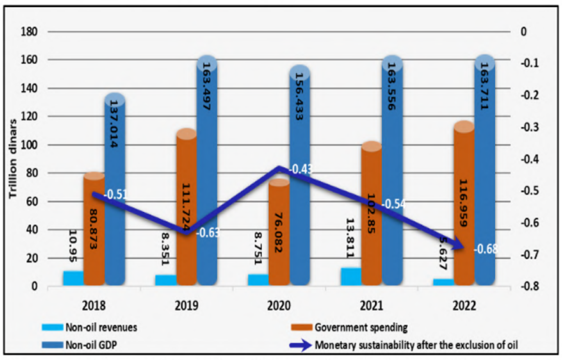


Source: Central bank of Iraq, Statistics and Research Department.

6. Monetary Sustainability through excluding the oil sector.

One of the most important risks that can face Iraqi economy is resulted from the fluctuations of oil prices, due to the low non -oil revenue percentage to the total revenue, compared to oil revenues and their contribution to financing government spending, the financial sustainability cannot be achieved by excluding the oil sector. This is considered one of the most important challenges facing financial and monetary policy makers in developing countries in general, including Iraq. On following up the form above, we can notice that government spending exceeds non - oil revenues because of the rentier characteristic of the Iraqi economy, which negatively affected the non-oil sustainability index that recorded negative values. Therefore, we seek to target this index by controlling operational spending and heading towards investment spending, which will significantly affect the growth of the non-oil GDP, the latter of which will affect non-oil revenues. Also, the failure to achieve financial sustainability by excluding oil sector as a result of the limited non-oil revenues compared to the volume of spending will expose the country to repeated financial crises and then its plunging in public debt unless it takes a serious strategy that includes strengthening non -oil revenues. The most important of these strategies is to rely on manufacturing that targets exporting to ensure exports growth at rates that exceed the growth of imports to achieve the external financial account surplus.

Figure No. (6): Financial Sustainability Excluding the Oil Sector

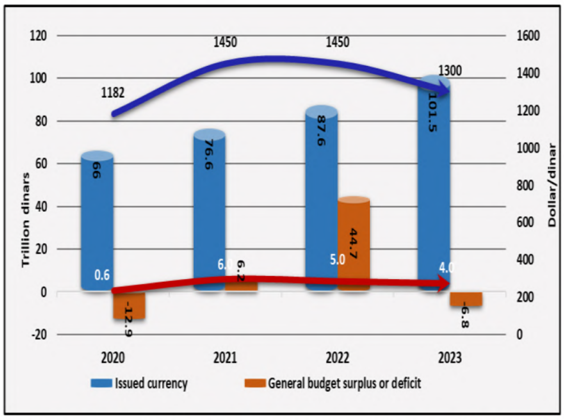


Source: Central Bank of Iraq, Statistics and Research Department.

7. The Relationship between General Budget Deficit and Some Financial Indices:

One of the important relationships that are focused on is the relationship between the impact of government spending and the foreign reserves of the central bank. The link between them is represented by both the oil revenues achieved as a variable linked to fiscal policy and the issued currency channel as a variable linked to monetary policy. The impact of this relationship is reflected in all monetary policy variables, including the exchange rate and inflation. From here, we would like to say that the process of coordination between the two policies is necessary to achieve the real goals of the economy from a comprehensive point of view.

Figure No. (7): The Relationship Between the General Budget Deficit and Some Monetary Indices



Source: Central Bank of Iraq, Statistics and Research Department.

8. Additional challenges for monetary policy:

The accumulated deficit over time indicates the unsustainability of debt, because when external debt grows relative to public debt in comparison to the ratio of internal debt to public debt, it puts pressure on the tools of monetary policy. Today, these proportions of the gross domestic product are not to be underestimated.

Impact of Interest Rate Liberalization on Credit and Deposits Volume in Iraq

Akeel Mohamed Rasheed/ Manager of Monetary and Financial Stability Division

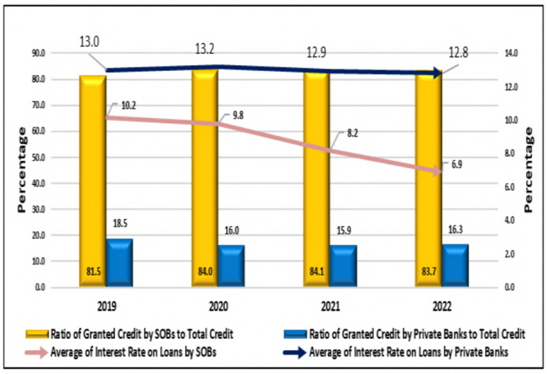
Preface:

The Central Bank of Iraq worked as the monetary authority to liberalize interest rates since 2004, in line with the free economy policy pursued by the Iraqi economy, of which the Central Bank is one of its central pillars. The purpose of interest rate liberalization is to create competition among banks, i.e., leaving interest rates on banks in direct credit, with a margin of interest earned by the bank through the difference between the interest rate of the credit and the debt sides. As interest rates are one of the most important factors affecting banking function by influencing the deposits volume and the credit volume, it, in turn, affect economic activity. The policy rate set by the monetary authority is one of the banks' most important references in determining interest rates within the financial sector. Therefore, this study aims to clear the reflection of the effect of interest rates liberalization on banking performance, and economic activity in general through the following:

First: The Impact of Interest Rate liberalization on Credit:

The granting credit process is considered one of the bank's most important activities, as it relies on the amount of deposits to obtain the required liquidity for the purpose of granting loans. The loan is granted at a certain interest rate. Since the interest rate is liberated in Iraq, a bank is left to determine it according to market requirements. Figure No. (1) shows the volume of credit and deposits of both state-owned banks (SOBs) and private banks, and the interest rate granted by them, noting that the amount of credit granted by SOBs is significantly greater than that granted by private banks, reaching (81.5%) to total granted credit during 2019 at an interest rate of (10.2%), rising to (83.7%) in 2022 with a decrease of interest rate to (6.9%). As for private banks, it is noted that their granted credit to total credit was (18.5%) in 2019, with an average interest rate of (13%), to decline to (16.3%) in 2022 with a slight decrease of interest rate on loans to (12.8%) during the same period. From the foregoing, we note that interest on granted loans from SOBs is lower than interest granted from private banks, meaning that the cost of obtaining funds from SOBs is lower than that of private banks on the one hand. On the other hand, SOBs dominance over salaries inclusion in the financial system is observed because of a pervasive banking culture that shows that SOBs are more confident and widespread. But back to the details of granted interest by banks, for example, the interest rate on loans granted by Erbil Bank was (15%) on both long-term and short-term loans. Similarly, with respect to Babylon Bank, the granted interest rate on loans was (15%) and interest on overdrawn accounts was (16%). The Turkish Agricultural Bank's credit interest rate was (20%) and interest on overdrawn accounts was (25%). As for SOBs, the interest rate on medium-term credit of Al-Rafidain and Al-Rasheed Banks were (7%) and (9%), respectively. This is extremely high if compared to the policy rate of (4%)[1]. Therefore, the process of determining the interest rate is left to the bank without the intervention of monetary authority.

Figure No. (1): Ratio of Granted Credit by SOBs and Private Banks



Source: Central Bank of Iraq, Statistics & Research Department, Annual Bulletin.
- Central Bank of Iraq, The Official Website.

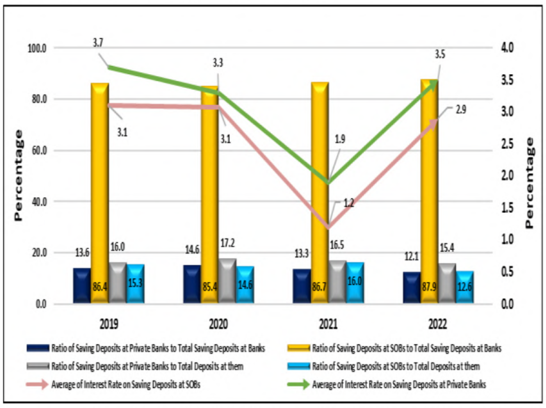
Second: Impact of Interest Rate Liberalization on Deposits:

Deposits are one of the most important sources of liquidity for banks to engage in their various activities, the most important of which is granting credit. Therefore, interest in deposits represents the cost incurred by a bank for the purpose of obtaining funds and is considered one of the most used means to attract the public to deposit funds in that bank. Figure No. (2) illustrates saving deposits at banks. The ratio of SOBs saving deposits to their total deposits

1) Central Bank of Iraq, Interest Rate Table, the official website.

was (15.3%) in 2019 and fell to (12.6%) in 2022. That is, their volume is low relative to total deposits at SOBs, but they represent (87.9%) of total saving deposits with total banks in 2022. Also, their interest rate on saving deposits fell from (3.1%) in 2019 to (2.9%) in 2022, which is lower than the interest rate on private banks' saving deposits. While the ratio of private banks’ saving deposits to their total deposits was (16%) in 2019 and fell to (15.4%) in 2022, which is considered lower than their total deposits, representing (12.1%) of total banks’ saving deposits in 2022. Its interest rate on saving deposits was (3.5%), which is higher than the interest rate granted by SOBs. In other words, although the interest rate granted by private banks is higher, the volume of deposits at them is lower, as private sector deposits at SOBs reached (33.2%) of banks' total deposits in 2022. While private sector deposits at private banks were (9.4%) total deposits during the same period. The recorded interest represents the interest rate of the total banks. However, getting back to banks’ details, it is noticed that some banks had low interest, for example, the Trade Bank of Iraq (TBI) had an interest rate of (1%) on saving deposits in 2022. Also, the Commercial Bank's interest rate was less than the correct one and reached (0.15%) during the same year, while Northern Bank’s interest rate was (1%) in 2022[2].

Figure No. (2): Ratio of Saving Deposits at SOBs and Private Banks



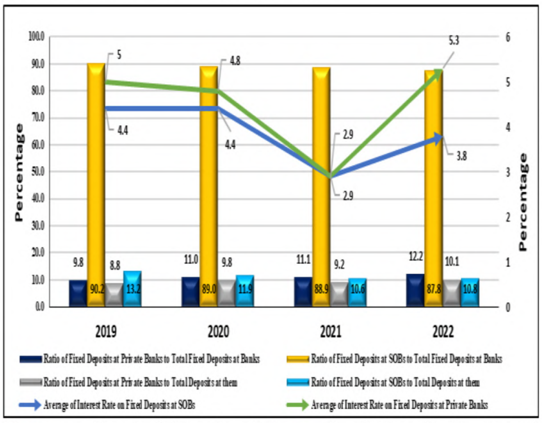
Source: Central Bank of Iraq, Statistics & Research Department, Annual Bulletin.
- Central Bank of Iraq, The Official Website.

Regarding the fixed deposits at SOBs and private banks, they are not much different from saving deposits, as the volume of fixed deposits at SOBs is greater than that at private banks and the interest rate of private banks is higher than that of SOBs. Figure No. (3) shows that the ratio of fixed deposits at SOBs to their total deposits was (13.2%) in 2019 and

2) Central Bank of Iraq, Interest Rate Table, The Official Website.

declined to (10.8%) in 2022, which is low to their total deposits, but constituted a ratio of (87.8%) to total fixed deposits at the banking sector. The interest rate in 2022 was (3.8%), which is low when compared to the 2019 interest rate of (4.4%). As for the fixed deposits at private banks, they were (8.8%) in 2019 to rise to (10.1%) in 2022 constituting (12.2%) compared to total deposits at the banking sector, which is low. Private banks granted an interest rate of (5.3%) on fixed deposits, which is higher than the interest granted by SOBs. The above-mentioned interest rates represent banks' interest rates, but if banks are considered individually, there is a discrepancy in interest rates. For example, ASH Bank granted less than one as interest on deposits of less than two years and (1%) on deposits of more than two years. The 'Economy Bank' granted an interest rate of (10%) deposits of one year and (11%) deposits of more than two years[3].

Figure No. (3): Ratio of Fixed Deposits at SOBs and Private Banks



Source: Central Bank of Iraq, Statistics & Research Department, Annual Bulletin.
- Central Bank of Iraq, The Official Website.

The most important observation is that liberalizing interest rates and leaving their ratio to be determined by the bank did not contribute significantly to attracting deposits, and that the wide variation in granted interest rates reflected bank's policy and orientation within the economy.

Third: Impact of Interest Rate Liberalization on Raising Financial Depth Levels:

Countries seek to achieve greater financial development through increasing financial depth by providing more options of financial services that would increase investment rates and economic growth. One of the most important used indicators to measure financial depth is the ratio of credit provided to

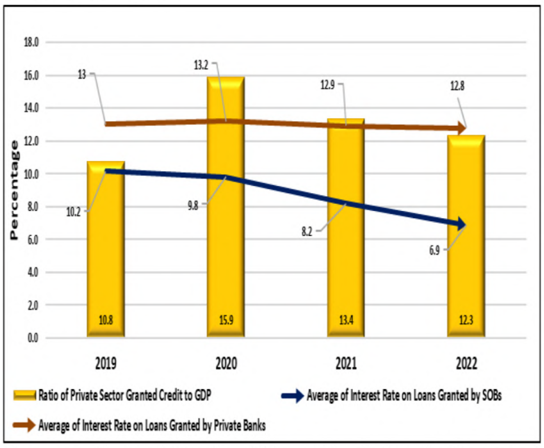
3) Central Bank of Iraq, Interest Rate Table, The Official Website.

the private sector to gross domestic product (GDP), and the private sector's ratio of deposits to GDP. Liberalization of interest rates, when they are productive, increases these ratios because it means expanding financial inclusion on one hand and activating the economy on the other.

1. Ratio of Private Sector's Credit to GDP:

The expansion of this ratio indicates that there is an expansion of banking activity within the real sector, and vice versa. This ratio is often activated in advanced countries because of high activity in the banking sector, with an active private sector working to increase GDP through its various activities. The interest rate is one of the basic determinants of the volume of credit provided to the private sector because it represents the cost of obtaining funds. Figure No. (4) shows that the ratio of credit provided to the private sector to GDP in 2019 was (10.8%), which increased to (12.3%) in 2022, as the ratio is considered low compared to Jordan's as it was (86.5%) in 2022 and (83%) in Kuwait[4]. The interest rate on loans granted by private banks fell very slightly from (13%) in 2019 to (12.8%) in 2022, while it decreased from (10.2%) to (6.9%) for SOBs during the same period. Thus, changes in interest rates did not affect changes in credit volume. In other words, other influences in the financial system affect granted credit volume, perhaps the most important of them is the type of guarantees resulting from following conservative credit policies in terms of consumer credit, or non-turn out of young entrepreneurs and businessmen to projects due to real sector challenges, management routines and work environment.

Figure No. (4): Ratio of Private Sector Granted Credit to GDP and Average Interest Rate



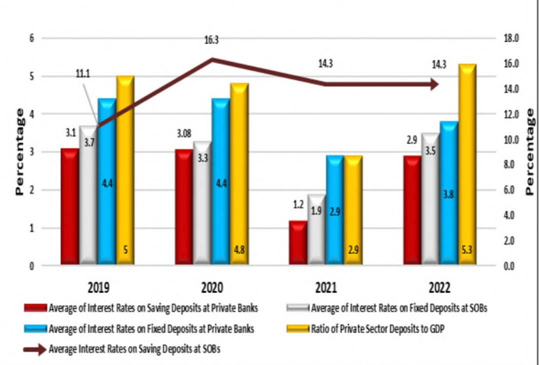
Source: Central Bank of Iraq, Statistics & Research Department, Annual Bulletin.
- Central Bank of Iraq, The Official Website.

4) World Bank: https://data.albankaldawli.org/indicator/FS.AST.PRVT.GD.ZS?view=chart

2. Ratio of Private Sector Deposits to GDP:

This ratio illustrates the public's appetite for banks to deposit funds and reflects banks' ability to grant loans by providing the necessary liquidity. One of the most crucial factors in attracting deposits is the interest rate. Figure No. (5) shows that the ratio of private sector deposits to GDP increased from (11.1%) in 2019 to (14.3%) in 2022. In contrast, the interest rate on SOBs saving deposits fell from (3.1%) to (2.9%) during the same period. As for the private banks, the interest rate on saving deposits fell from (3.7%) to (3.5%) during the same period**.** Also, with respect to the rate of interest on fixed deposits at SOBs, it decreased during the same period. Thus, although the interest rate on deposits had declined, it still rose. This means that the interest rate does not affect the volume of deposits in the private sector. There are other factors that have a greater impact, such as the process of salaries inclusion in the financial system.

Figure No. (5): Ratio of Private Sector Deposits to GDP and Interest Rate



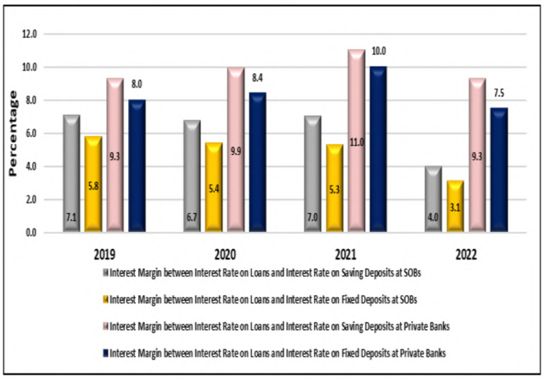
Source: Central Bank of Iraq, Statistics & Research Department, Annual Bulletin.
- Central Bank of Iraq, The Official Website.

It is noted that changes in interest rates did not have a significant impact on the financial depth of both deposits and credit. On the other hand, the monetary authority cannot use the differential interest rate to support a particular sector or direction due to the liberalization of interest rates, which can be used if the interest rate or at least the profit margin of interest is determined**.**

Fourth: Profit Margin of Interest (Spread Factor):

The profit margin of interest is determined by the difference between credit interest and debt interest. Under a liberalized interest rate, the determination of such margin is left to the bank's domestic policy. In general, banks, especially private banks, are profitable institutions. As such, they will maximize their profits by entering quick-profit sectors and will increase the interest profit margin as much as possible. The monetary authority represented by the central bank will lose the advantage of using differential interest rates for some sectors that could have been used to target certain sectors if there was a determined interest margin. Figure No. (6) shows that the interest margin at SOBs is lower than that of private banks, as the interest margin between the interest rates on loans and the interest margin on saving deposits declined from (7.1%) in 2019 to (4%) in 2022 for SOBs. There is also a decline in the interest margin between interest in loans and interest in fixed deposits from (5.8%) to (3.1%) during the same period. Regarding private banks, the interest margin between loans and saving deposits remained constant at (9.3%) during the period (2019-2022), with a slight decrease in interest margin between interest on loans and interest on fixed deposits from (8%) to (7.5%) during the same period. It is worth mentioning that SOBs have the largest share of deposits and loans within the financial system as mentioned above. Public sector deposits and loans are not affected by interest rates. By referring to banks' details, for example, the ratio of interest margin between the interest rate on loans and the interest rate on bank's saving deposits of Trade Bank of Iraq (TBI) reached (4.09%), while it was (2.8%) for Al-Rafidain Bank and (5.1%) for Al-Rasheed Bank during 2022. Yet, it was (20.5%) for the Agricultural Bank of Türkiye, (22.5%) for Al-Warka Bank, (11.8%) for Gulf Bank and (10%) for Erbil Bank during 2022.

Figure No. (6): Interest Margin of SOBs and Private Banks



Source: Prepared by researcher based on 'Interest Rate Table' of Statistics and Research Department.

It is noticed that private banks, despite a higher interest margin than that of SOBs, did not contribute significantly to increasing loans or attracting deposits as SOBs did.

Conclusions:

1. Interest rates are left to banks to be determined.
2. Interest rate liberalization did not contribute significantly to

activating the financial system in terms of both deposits and credit.

3. The ratio of deposits to (GDP) and credit to (GDP) is weak compared to countries in the region.
4. Private banks' interest rates margin is higher than that of SOBs, which is a negative indicator of financial and economic development.
5. The contribution of SOBs is higher than private banks to the volume of credit and deposits within the system because of their acquisition of government funds and the culture of the private sector, which prefers SOBs to private banks.

Recommendations:

As interest rate liberalization is determined by the Central Bank's law to increase competition among banks and determine it based on supply and demand mechanisms, it is necessary to determine the interest margin (spread factor) between the credit and debt rates to a range of (3% - 4%), so that banks can achieve a reasonable return with confirmation of their commitment for the purpose of influencing the volume of credit and deposits and increasing their impact on financial development, taking into account the opinion of the legal Dept. which will give the central bank the advantage of implementing its policy using this tool.

Impact of Raising interest rate in Türkiye on Dollar Exchange rate in Iraq

Prepared by

Hassan Hazem Lafta Researcher
Ruqayya Karim Abbas Researcher
Ayat Muhammad Attia Researcher

Economic relations between Iraq and Türkiye form a fundamental and important pillar of the existing relations between the two countries. These relations encompass numerous aspects and sectors. Moreover, the two neighboring countries enjoy strategic characteristics stemming from their strategic geographic location, as well as shared cultural commonalities.

Economic factors play an important multi-dimensional role in Iraqi-Turkish relations, as there is a mutual need between the two countries. For Iraq, Türkiye constitutes a vital gateway for its commercial imports and the entry of various types of goods and commodities into its markets on one hand, and it is an important outlet for exporting oil through Turkish territory via pipelines that pass through it to reach Turkish ports on the other hand. These relations will be strengthened in the future, especially after the two countries signed the establishment of the development road, the economic artery that will link their economies together.

First: Economic Relations between Türkiye and Arab Countries:

1. **Investments:** Investments in Türkiye witnessed an increase of USD $ (14) billion according to data for 2022, with Türkiye's potential to attract many foreign investors in the coming years, especially after the election period that took place in May 2022, which witnessed foreign investment activity in it, and increased interest of foreign investors in investment projects in Türkiye, which obtained a percentage of (1%) of investments around the world, as it aims to increase this percentage to (1.5%) in the coming years[1].

In addition to the large participation of European and Gulf countries, and the growth with the Gulf region as a positive indicator of investment prospects, especially in the manufacturing sector, across the

1) Türkiye's foreign direct investment expected to break records in 2023https://www.imtilak.net/ar/Türkiye/news/turkiye-investment-break-records-2023

regions of Central and Eastern Europe and the Middle East and North Africa. Türkiye emerged as the largest recipient of industrial investments, as it obtained (21.7%) of investments in the Central and Eastern Europe region and the Middle East and North Africa region over the past decade, in addition to (19.1%) since 2013[2].

The country attracted USD $ (255) billion in international investments over the past 21 years. Türkiye intends to attract more foreign direct investment, by facilitating governmental and legal procedures, according to the medium-term economic program called the "Century of Türkiye" roadmap[3].

As for Arab investments, they are playing a prominent role in the growth of the Turkish economy, as the total Arab direct investments in Türkiye amounted to nearly USD $ (16.6) billion at the end of 2022, representing (8.6%) of the total direct investments in Türkiye during the mentioned period, which amounted to USD $ (192) billion. As for the share of the Arab Gulf states, it was (8.4%). The Gulf states are the third largest source of foreign investment in Türkiye after Britain and the Netherlands, while data from Turkish Ministry of Economy indicate the presence of (1,973) Gulf companies operating in the Turkish market.

In general, Arab investments in Türkiye are concentrated in the fields of real estate, real estate development, finance, banking, textile industry, food, agriculture, animal husbandry and international trade. Türkiye is considered an ideal investment environment for Arab countries, given that it is safe, stable, and close to Arab countries and global markets, which makes companies already established there a bridge of communication between Arab countries and international markets. As for Turkish investments in the Arab region, the volume of direct investments from Türkiye at the end of 2022 amounted to USD $ (2.5) billion[4].

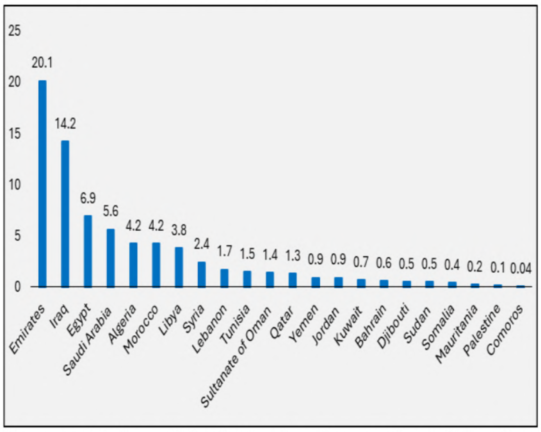
2. **Trade:** According to data from the Turkish Statistical Institute, the volume of trade exchange between Türkiye and Arab countries

2) https://f.invest.gov.tr/en/news/news-from-Türkiye/pages/turkiye-attracts-usd-10.6-billion-in-foreign-direct-investment-in-2023.asp
3) Expectations of breaking records for foreign investments in Türkiye 2023: https://www.imtilak.net/ar/Türkiye/news/turkiye-investment-break-records-2023
4) Report of the Union of Arab Banks, Economic relations between Türkiye and Arab countries and trade exchange (strengthening ties).

amounted to USD $ (72.6) billion at the end of 2023. Turkish exports to the Arab region grew by (1.7%) during 2023, reaching a value of about USD $ (46.4) billion, while imports increased by (21.9%) to reach a value of USD $ (46.6) billion at the end of 2023. On the other hand, the volume of trade exchange between Türkiye and Iraq amounted to USD $ (14.2) billion, which recorded a decline compared to the previous year, as it was in second place after the Emirates, which took first place in terms of trade exchange volume amounting to USD $ (20.1) billion in 2023.

According to the figures of the Turkish Statistical Institute, Iraq topped the list of Arab countries receiving Turkish exports in 2019 with more than USD $ (10.2) billion, and the difference appears vast between it and the country that comes in second place, namely the UAE with about USD $ (3.6) billion, then Egypt USD $ (3.5) billion, followed by Saudi Arabia USD $ (3.2) billion. Also, the volume of trade exchange between Türkiye and Iraq amounted to about USD $ (20) billion in 2020. According to The Turkish Embassy, Iraq is ranked fourth among Türkiye's customers, after Germany, Britain and the United States of America, and this exchange declined to about USD $ (15.2) billion in 2022[5].

Figure No. (1): Volume of Trade Exchange between Türkiye and Arab countries in 2023 (Billion Dollars)



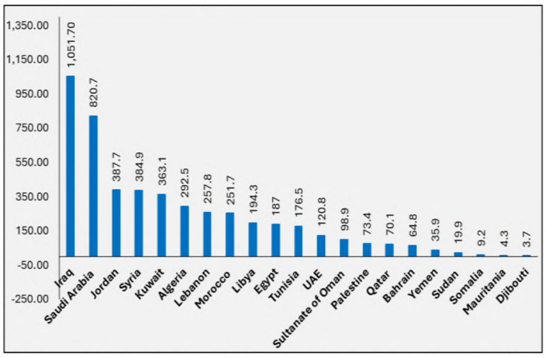
Source: Union of Arab Banks, Research and Studies Department, based on data from the Turkish Statistical Institute.

3. **Tourism:** Tourism between Türkiye and Arab countries is one of the vital sectors that has witnessed remarkable growth in recent years, due to several factors, including cultural and historical convergences, the diversity of tourist destinations in Türkiye that attract Arab tourists, in addition to policies that enhance tourism exchange between Türkiye and Arab countries. According to the Turkish Ministry of Culture and Tourism, the

5) https://www.dw.com/ar

number of Arab tourists who visited Türkiye during the year 2023 alone amounted to about (4.86) million tourists, and they constituted about (9.8%) of the tourists who visited Türkiye, and Iraq ranked first among Arab countries during 2023, with (1051.7) thousand tourists entering Türkiye.

Figure No. (2): Number of Arab Tourists who Visited Türkiye in 2023 by Country (Thousand People)



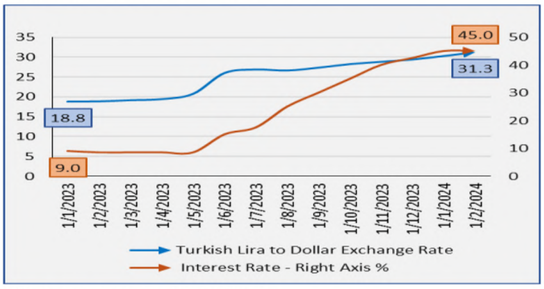
Source: Union of Arab Banks, Research and Studies Department, based on data from the Turkish Statistical Institute.

Second: Recent Economic Events in Türkiye:

In recent years, Türkiye has witnessed a significant increase in inflation rates exceeding (65%) at the beginning of 2023, and in line with the main goal of price stability, the Turkish Central Bank raised the interest rate from (42.5%) to (45%) on 25/1/2024 but kept the interest rate at this rate on 22/2/2024 after eight increases that started from (8.5%) on 25/5/2023. This increase comes as an attempt by the Turkish Central Bank to control the decline in the value of the Turkish lira, which fell from (18.8) liras to the dollar during January 2023 to (31.3) liras to the dollar during February 2024, meaning that it lost (66.5%) of its value in about a year, as shown in Figure No. (3).

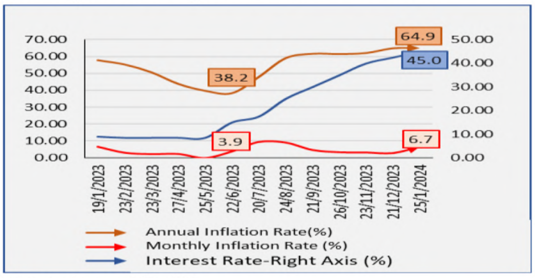
In addition to controlling inflation rates, which rose from (3.9%) monthly and (38.2%) annually in June 2023 to (6.7%) monthly and (64.9%) annually in January 2024, as shown in Figure No. (4).

Figure No. (3): Interest Rate and Exchange Rate of Turkish Lira for the period 1/1/2023-1/2/2024



- Interest rates on the website: https://sa.investing.com/currencies/usd-try-historical-data
- Interest rate changes according to the dates of the meetings of the Central Bank of Türkiye.

Figure No. (4): Interest and Inflation Rate in Türkiye for the period 2023-02/2024



- Interest rate, at the link: https://sa.investing.com/economic-calendar/turkish-one-week-repo-rate-409
- Monthly and annual inflation rate: Turkish Statistical Institute website: https://data.tuik.gov.tr/Bulten/Index?p=Consumer-Price-Index-January-2024-53622&dil=2

The Monetary Policy Committee of the Central Bank of the Republic of Türkiye estimated on 22/2/2024 that the current level of interest rate (45%) will be maintained until there is a significant and sustained decline in the basic trend of monthly inflation and until inflation expectations converge to the expected range. The monetary policy stance will be tightened in case a significant and sustained deterioration in inflation expectations is expected.

The Committee will continue to implement macroprudential policies in a way that preserves the functions of the market mechanism and overall financial stability. The cash transfer mechanism will be supported in the event of unexpected developments in credit growth and deposit interest rates. To support monetary tightening, developments in market liquidity will be closely monitored and sterilization tools will be used effectively whenever necessary. Considering the lagged effects of monetary tightening, the Committee will determine its policy decisions in a way that will create the necessary monetary and financial conditions to ensure reaching the inflation target of (5%) in the medium term[6].

Third: The impact of interest rates and inflation in Türkiye on Iraq:

The Central Bank of Iraq adopted a tight monetary policy, raising its policy rate (interest rate) from (4%) to (7.5%) in June 2023, However, deposit interest rates for one-year dinar deposits did not reach (5%) during November and December 2023, remaining low compared to neighboring countries. To understand the impact of interest rate changes in Türkiye on Iraqi depositors, exchange rate fluctuations must be considered.

Turning to the exchange rate of the US dollar against Iraqi dinar, it recorded (1601) dinars per dollar in November 2023 and decreased to (1523) dinars per dollar in January 2024. This represents an increase in the value of the dinars (4.9%). As for the exchange rate of the dollar versus Turkish lira, it recorded (28.7) lira per dollar and increased to (30.1) lira per dollar. This means, means a decrease of (4.9%) for the same period.

6) https://tcmb.gov.tr/wps/wcm/connect/en/tcmb+en/main+menu/announcements/press+releases/2024/ano2024-09

Considering the higher interest rates on the Turkish lira compared to the Iraqi dinar, this expects to put pressure on the exchange rate in Iraq (causing the US dollar to increase), as Iraqis would increase their deposits in Turkish lira in Turkish banks. However, we observe an increase in the exchange rate of the US dollar against the lira during the specified period, as shown in Table 1, which negates the effect of the return achieved from depositing in Turkish lira. The Turkish lira has depreciated by (66.5%) during the period from 1/1/2023 to 1/2/2024.

On the other hand, there is a significant difference between the interest rates on dollar deposits in Türkiye and Iraq. This could encourage individuals to increase their dollar deposits in Türkiye, thereby putting pressure on the exchange rate in Iraq. While the interest rate on dollar deposits in Iraq is low, it is stable, unlike Türkiye where it has been decreasing alongside the increase in interest rates on the lira. For example, if there is a ($1,000) deposit, the return in Türkiye would be ($90) compared to ($27.3) in Iraq (based on interest rates for December 2023). This example indicates that the interest rates on dollars in Iraq are not encouraging and are a key factor contributing to the pressure on the exchange rate in the parallel market.

Table No. (1): Interest Rate and Dollar Exchange Rate in Iraq and Türkiye during 2023 - January 2024

	Interest rate on deposit in lira up to 1 year (%)	Interest rate on deposit in dinar for a period of one year (%)	Interest rate on deposit in dollars up to 1 year (%) in Türkiye	Interest rate on deposit in dollars for a period of one year (%) in Iraq	Dollar exchange rate to lira in the parallel market	Dollar exchange rate to dinar in the parallel market	Lira exchange rate to dinar
January 2023	34.5	4.99	20.00	2.81	18.77	1613.7	86.0
February	43.5	4.99	20.00	2.83	18.84	1604.8	85.2
March	39.0	5.00	15.00	2.91	19.00	1611.8	84.8
April	39.0	4.92	27.00	2.89	19.35	1598.2	82.6
May	45.0	4.92	20.00	2.89	19.79	1526.9	77.2
June	48.0	4.93	25.00	2.91	23.84	1470.3	61.7
July	45.0	4.93	25.00	2.91	26.50	-	-
August	49.0	4.93	20.00	2.87	26.90	-	-
September	60.0	4.86	8.00	2.81	27.02	-	-
October	60.0	4.86	8.00	2.81	27.90	-	-
November	61.0	4.86	6.75	2.81	28.68	1601	55.8
December	66.0	4.92	9.00	2.73	29.10	1545.6	53.1
January 2024	62.0	-	7.51	-	30.08	1523.2	50.6

- Interest rate on deposit in lira and interest rate on deposit in dollars in Türkiye: https://evds2.tcmb.gov.tr/index.php?/evds/portlet/hIdR20CDwM4%3D/en
- Dollar exchange rate to Turkish lira: https://sa.investing.com/currencies/usd-try-historical-data
- Interest rate on deposit in dinars and the interest rate on depositing dollars in Iraq, the Central Bank of Iraq, the statistical website.
- The dollar exchange rate for the dinar: the Central Bank of Iraq, Statistics and Research Department.
- The lira exchange rate for the dinar = the dollar exchange rate for the dinar\ the dollar exchange rate for the lira.

Fourth: Conclusion:

1. Economic relations between Türkiye and the Arab countries in general and Iraq in particular play a pivotal role in the region, as these relations have a comparative advantage.
2. Despite the Turkish Central Bank raising interest rates at a rapid pace throughout 2023 until January 2024, inflation rates have declined at a slower pace. Interest rates have reached record levels, accompanied by high inflation rates.
3. Real interest rates remain negative as long as the inflation rate is higher, which explains the continued depreciation of the Turkish lira against the dollar.
4. Looking back at previous years, it is found that the monetary policy in Türkiye has tended to raise interest rates by high percentages and in a sudden manner.
5. It is difficult to reach the inflation target of (5%) given the extremely high inflation rate of (64.9%). Reducing inflation to a single-digit level would require keeping interest rates high for an extended period, which is contrary to Türkiye's desire to continue growing its GDP and exports.
6. Despite the very noticeable rise in inflation in Türkiye, Arab countries, especially Gulf region and Iraq, which represent the largest share of Türkiye's relations, maintain low inflation rates. On the other hand, rise in interest rates has put pressure on those countries, especially Iraq, due to the weak financial markets, which are considered an important avenue for investment.

Impact of Government Spending on Issued Currency Channel
(Forecasting Study through 2024)

Prepared by:

Wissam Khalid Saeed
Researcher

Ahmed Jamal Askar
Researcher

Abstract:

The study aims to forecast the issued currency until the end of 2024, as a dependent variable based on the factors affecting it, namely public expenditures, private sector demand for the dollar denominated in dinar (foreign exchange window sales of the Central Bank of Iraq), net foreign reserves, oil and non-oil revenues, with government discounted transfers by this bank, in addition to government bonds) as independent variables, through using the Autoregressive Distributed Lag model (ARDL) in the statistical program (E-views), as the unit root was tested for all variables to ensure the presence of stationarity in the series or not. It was then found that some variables are stable at level I (0), while others are stable at the first difference I (1).

The results showed that the value of the corrected coefficient of determination was equal to (99%), which is an extremely high percentage and indicates that the independent variables explain 99% of the dependent variable. The value of the autocorrelation test (Durbin-Watson) was equal to (1.87), which indicates that there is no autocorrelation between the residuals of the model.

It has been found out that the relationship of the issued currency is direct with each of the government spending, net foreign reserves, oil revenues, and government discounted transfers of CBI. While this relationship was inverse with the private sector's demand for the dollar denominated in dinars (foreign currency window sales), non-oil revenues, and government bonds.

The values of the independent variables were also predicted for the end of 2024 to reach the value of the issued currency for the same year. It was found out that the issued currency will reach approximately (105.8) trillion dinars, with a net increase of approximately (4.5) trillion dinars over 2023, assuming the full implementation of the government

spending program amounting to (198.9) trillion dinars, assuming more than one scenario for global oil prices and measuring the impact of each price on the issued currency through oil revenues starting from (50) dollars per barrel up to (90) dollars, with an increase of (10) dollars for each scenario.

The study has arrived at several conclusions, including full implementation of the government spending program as cited in the public budget for 2023 will lead to an increase in the issued currency by (4.3%) over what it was in 2023, if other factors remain on the same time series pattern. A number of recommendations have been presented, including the necessity of developing a precautionary policy that works to keep the volume of the issued currency within acceptable limits in the economy through direct and indirect instruments, especially after the government's move to implement the total investment and consumption spending program, which requires the availability of a local currency to finance this spending, since it is necessary to finance the largest proportion of this spending by withdrawing the currency from circulation instead of relying on the issuance of new currency.

First: Forecasting the Values of Factors Influencing the Issued Currency:

The purpose of forecasting the issued currency is to estimate its future development based on the previous and current situation, and the factors that influence it. This is achieved by utilizing time series analysis, dependency relationships, and interconnections among various influential factors. Monthly data for all variables has been employed for this purpose.

Building a standard model to estimate the regression equation: A standard model was built to estimate the regression equation for the purpose of predicting the issued currency based on the variables affecting it, as shown in the following regression equation:

Constructing a Standard Model for Regression Equation Estimation:

A standard regression model has been constructed to forecast the issued currency based on the influencing variables, as illustrated in the following regression equation:

$$Y = b_0 + b_1x_1 + b_2x_2 + b_3x_3 + b_4x_4 + b_5x_5 + b_6x_6 + b_7x_7 + e_i \ldots (1)$$

Whereas:

Y: Value of the issued currency

X_1: Value of public expenses

X_2: Private sector's demand for the dollar denominated in dinars (window sales)

X_3: Non-oil revenues

X_4: Net foreign reserves

X_5: Oil revenues

X_6: Discounted Transfers by CBI

X_7: Bonds e_i: random error

Before commencing the time series analysis, stationarity was ensured through the unit root test to determine whether the time series is stationary or not. Subsequently, forecasts were made for the independent variables in 2024, assuming the exchange rate remained stable at (1,300) dinars per dollar and total expenditure as stipulated in the public budget, amounting to (198,910,344) million dinars. Predicting the issued currency for 2024 necessitates the presence of values for the independent variables influencing it as outlined in the equation.

The values of factors affecting the issued currency were forecasted as of 31/12/2024, assuming that the planned government expenditure will reach 198.9 trillion dinars as stated in the 2024 general budget plan. It is expected that the growth rate of oil and non-oil revenues will reach 31.2% at the end of 2024 compared to 2023, while the deficit will increase by 210.3%. It is also expected that the total private sector demand for dollars denominated in dinars from the bank's currency sales window (window sales) will decrease by 2%, and that the net foreign reserves will increase by 2.8% during the same period.

Framework (1)

The forecasts indicate that the growth rate of oil revenues in 2024 will reach 29.3% compared to 2023 and will cover 81% of total government spending in the budget. This percentage suggests that there is no pressure to spend on the issued currency due to the increase in net foreign reserves as a result of the government exchanging its dollar revenues for dinars at the central bank. This gives the bank flexibility to withdraw local currency through the window and finance imports with greater freedom.

After forecasting the independent variables, the issued currency will be forecasted using the (ARDL) model as of the end of 2024 as follows:

a. Lag order selection test using the (HQ, BIC, and AIC) criteria: The optimal number of lags for the study model was determined to be (1,2,2,2,2,2,1,2).

b. Estimation of the (ARDL) model:

The (ARDL) model was estimated after the optimal lags were chosen (1,2,2,2,2,2,1,2). It is noticed from the results that the value of the corrected coefficient of determination was equal to (99%), which is an extremely high percentage, and indicates that the independent variables explain 99% of the dependent variable. Also, the value of the autocorrelation test (Durbin-Watson) was equal to (1.87), which indicates the absence of autocorrelation between the residuals of the model. Concerning the statistics of (F), it was intangible. As such, it indicates the imperceptibility of the model used, because the estimated regression equation was as follows:

$$\hat{Y} = 1728953 + 0.055990x_1 - 0.372907x_2 - 0.127484x_3 + 0.142562x_4 + 0.068181x_5 + 0.217003x_6 - 0.220593x_7$$

Where:

- When the value of government spending increases by (1) million dinars, the issued currency will increase by (0.055990) million dinars. This means that there is a direct relationship between government spending and the issued currency.
- When the private sector's demand for the dollar denominated in dinars increases by (1) million dinars, the issued currency will accordingly decrease by approximately (0.372907) million dinars, which means that there is an inverse relationship between the private sector's demand for the dollar denominated in dinars from the currency selling window and the issued currency.
- When non-oil revenues increase by (1) million dinars, the issued currency will decrease by nearly (-0.127484) million dinars. In other words, there is an inverse relationship between non-oil revenues and the issued currency.
- When net foreign reserves increase by (1) million dinars, the issued currency will increase by (0.142562) million dinars. This means that there is a direct relationship between net foreign reserves and the issued currency.
- When oil revenues increase by (1) million dinars, the issued currency will increase by (0.068181) million

dinars. This means that there is a direct relationship between oil revenues and the issued currency.

- When discounted transfers by the Central Bank increase by (1) million dinars, the issued currency will increase by (0.217003) million dinars, which means that there is a direct relationship between discounted transfers and the issued currency.
- When the government bonds increase by (1) million dinars, the issued currency will decrease by (0.220593) million dinars. In other words, there is an inverse relationship between government bonds and the issued currency.

After verifying the quality of the standard model, the existence of a joint integration relationship between the issued currency and the factors affecting it was tested as in the bounds test.

c. **Bounds test:** In this test, the type of cointegration and the long-term relationship are determined by the (ARDL) Long Run Form and Bounds Test. It is noticed from the test results that the probability value of the (F) statistic was greater than the upper limit I (1), whereas greater than the lower limit I (0) at the level (5%). This indicates the existence of a joint integration relationship overall. Then, the issued currency was predicted based on the parameters of the regression model for 2024 monthly, as shown in table (1).

Table No. (1): Forecast of the issued currency for 2024 monthly (million dinars)

period	Issued currency
01/31/2024	101,323,527 *
02/28/2024	99,237,507
03/31/2024	99,891,600
04/30/2024	100,545,000
05/31/2024	101,199,000
06/30/2024	101,853,000
07/31/2024	102,507,000
08/31/2024	103,160,000
09/30/2024	103,814,000
10/31/2024	104,468,000
11/30/2024	105,122,000
12/31/2024	105,776,000

Source: prepared by researchers based on EViews program outputs.
* Actual values

Based on EViews program outputs, and through the afore-mentioned equation, which explains the variables that affect the issued currency. Accordingly, the issued currency was forecasted until the end of 2024, and it was found out that the issued currency will reach (105.8) billion dinars, with an increase of (4.3) trillion dinars over what it was at the end of 2023 and approaching (101.5) trillion dinars.

Figure No. (1): Oil & non-oil Revenues for (2016-2024) IQD trillion

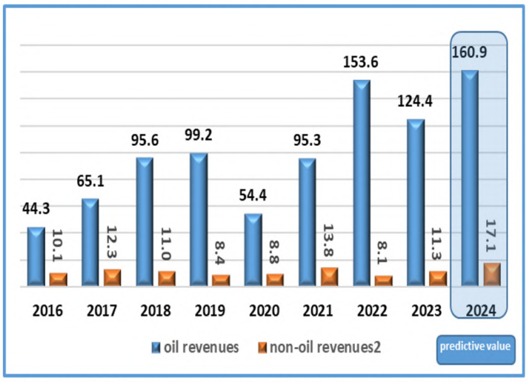


Figure No. (2): Net Foreign Revenues & Demand for Dollars for (2016-2024) IQD trillion

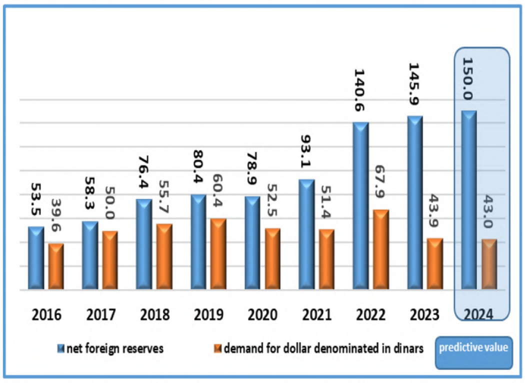


Figure No. (3) Government Expenditure & Issued Currency for (2016-2024) IQD trillion

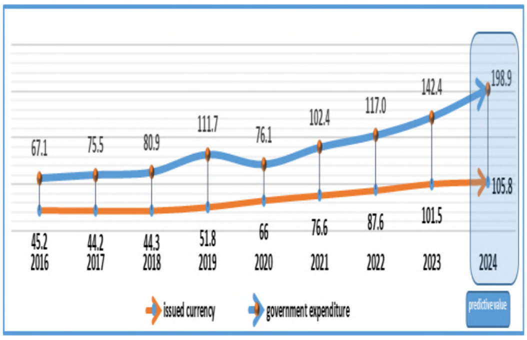


Figure (1) above, based on statistical program forecasts and using time series data from 2016 to 2023, shows that oil revenues will grow by 29.3% in 2024 compared to 2023, while non-oil revenues will grow by 51.3%. Net foreign reserves will increase by 2.8% for the same period. The forecast also showed a decrease in the private sector's demand for dollars denominated in dinars (window sales) by 2.1% compared to 2023 as shown in Figure 2 above for the same period.

Figure 3 above includes a forecast of the value of the issued currency, which may grow by 4.2% to reach 105.8 trillion dinars. With regard to government spending, it was fixed as stated in the general budget at 198.9 trillion dinars, with a growth rate of 39.7% compared to 2023 spending.

Second: Forecasting Net Foreign Reserves and Issued Currency on Oil Prices Changes:

The Iraqi economy is characterized by rentier, with oil revenues serving as its dynamic engine. The impact of oil price fluctuations on the issued currency must be clarified, as this impact is transmitted through net foreign reserves. Therefore, a model was constructed according to the (ARDL) program for the purpose of creating scenarios for oil prices and knowing the extent of their impact on the value of net foreign reserves, and then using these scenarios in the previous model. The values of the predicted net foreign reserves were entered for each scenario instead of the values of net foreign reserves to know the impact of changes in net foreign reserves on the issued currency. Equation (2) explains how to forecast net foreign reserves:

$$Y = b_0 + b_1x_1 + b_2x_2 + e_i \ldots (2)$$

Where:

Y: Net foreign reserves.

X_1: value of crude oil exports.

X_2: total imports.

e_i: random error.

The estimated regression equation was as follows:

$$\hat{Y} = -10785276 + 0.799078x_1 - 0.317626x_2$$

Where:

- When the value of crude oil exports increases by (1) million dinars, net foreign reserves will increase by (0.799078) million dinars.
- When total imports increase by (1) million dinars, net foreign reserves will decrease by (0.317626) million dinars.

Assuming the following:

- The assumed fixed exchange rate for 2024 is (1,300) dinars for (1) dollar.

-The assumed oil price changes according to multiple scenarios (50, 60, 70, 80, 90) dollars.

The following table shows: The impact of the fluctuation in oil prices on net foreign reserves and the extent of the impact of the latter change on the issued currency, assuming other factors remain constant, and as follows:

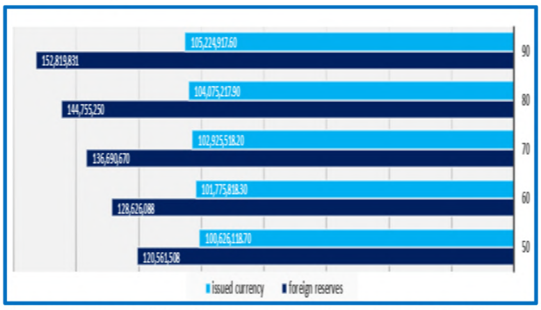
Table No. (2): The impact of oil prices on net foreign reserves and issued currency

issued currency (million dinars)	net foreign reserves (million dinars)	oil price (USD)
100,626,118.7	120,561,508	50
101,775,818.3	128,626,088	60
102,925,518.2	136,690,670	70
104,075,217.9	144,755,250	80
105,224,917.6	152,819,831	90

Source: prepared by researchers based on the outputs of the (EViews) program.

The table above illustrates that if the oil price remains stable at (50) dollars per barrel throughout 2024, it will result in net foreign reserves reaching approximately 120.6 trillion dinars by the end of 2024, according to the variables of equation (2) above. Thus, the issued currency will reach an amount of (100.6) trillion dinars, according to equation (1) above. But if the average oil price reaches (90) dollars per barrel, the net foreign reserves will reach an amount of (152.8) trillion dinars, and the issued currency will be at an amount of (105.2) trillion dinars.

Figure No. (4): Scenario of Import of Oil Price on Net Foreign Reserves and Issued Currency



Source: prepared by the researchers based on table (2).

Conclusion:

1. Public expenditures, oil revenues, net foreign reserves, and transfers affect the issued currency in a direct and significant correlation. Also, the increase in the private sector demand for the dollar denominated in dinars (window sales), non-oil revenues, and bonds lead to a decrease in the issued currency. This means that the effect of these variables is inverse on the issued currency.
2. Full implementation of the government spending program as it is in the public budget for 2023 will lead to an increase in the issued currency by (4.3%) over what it was in 2023, if other factors remain in the same time series pattern.
3. Global oil prices affect the issued currency by influencing net foreign reserves, as it has become clear from the forecasted equation (2). Hence, an increase in oil prices will lead to a rise in net foreign reserves, in addition to the issued currency. If the other factors in equation (1) remain in the same time series pattern.

Recommendations:

1. There is a necessity of drawing up a precautionary policy that works to keep the volume of the issued currency within acceptable economic limits through direct and indirect tools, especially after the government's decision to execute a comprehensive investment and consumption expenditure program, which requires the availability of a local currency to finance this spending. Since it is essential to finance the largest proportion of this spending by withdrawing the currency from circulation instead of relying on the new currency issuance.
2. Adopting a ratio of (70%) or more to cover oil revenues for public expenditures is a crucial factor that maintains financial stability. If the revenue coverage declines below the above ratio, then the pressure on the value of the local currency in the black exchange market will increase, in addition to the pressure on the net foreign reserve. Therefore, it is preferable to rationalize spending at a rate commensurate with the percentage of the decline of revenues.

BRICS and Dollar Dominance

Prepared by: Hasan Hazim Lafta/ Researcher

BRICS Group represents one of the international economic alliances, as a group of countries agreed in 2016 to strengthen economic and trade cooperation among themselves. In 2010, South Africa (the smallest member in terms of economic power and population) joined the group and became known as BRICS. BRICS (Brazil, Russia, India, China, and South Africa countries) agreed at their annual summit in Johannesburg to grant Argentina, Ethiopia, Iran, Kingdom of Saudi Arabia, Egypt, and the United Arab Emirates full membership as of January 1, 2024

BRICS's leaders have expressed a common belief that the international system is subject to domination by western states and institutions and does not serve the interests of developing countries. The joining of six new members now represents the international bloc by 46% of the world's population. Analysts believe that Brazil, South Africa, and India need to balance closeness to China and Russia without excluding the United States, which is a strong trading partner for these three countries. Oil-producing countries such as Saudi Arabia, the United Arab Emirates and Iran would strengthen the bloc's economic influence. As observers warned that Iran's accession could be a threat to the image BRICS as an anti-US bloc.

BRICS Group founded "New Development Bank" in 2015, has a capital of $50 billion to finance development, especially infrastructure, and build broad development partnerships. Egypt participated in the new Development Bank in 2021 with a contribution of about US $1.2 billion and established a BRICS Contingent Reserve Arrangement (equivalent to IMF) with a capital US $100 billion that provides loans, guarantees for development projects, and enters its founding partner.

As for the exclusion of Algeria in BRICS, it was not clear what motives were behind the exclusion decision nor the criteria adopted to include the six countries, especially since some of them are highly indebted, such as Egypt and Argentina, where the ratio of public debt to GDP reached (88.5%) and

(80%) respectively, while Ethiopia reached (46.4%**),** while Algeria recorded (55.6%)[1].

It is clear from this that economic dimensions are not the only criterion for countries to join BRICS, but there are other dimensions that control the acceptance of new members, such as political weight, the extent of the impact of political decisions and geographical location.

Among the most prominent objectives of BRICS stated in their official document (BRICS strategy) are: [2]

1. Achieve inclusive economic growth that eradicates poverty, addresses unemployment, and promotes social integration.
2. Consolidating efforts to ensure higher quality growth by promoting innovative economic development based on advanced technology and skills development.
3. Seeking to increase engagement and cooperation with non-member states in BRICS.

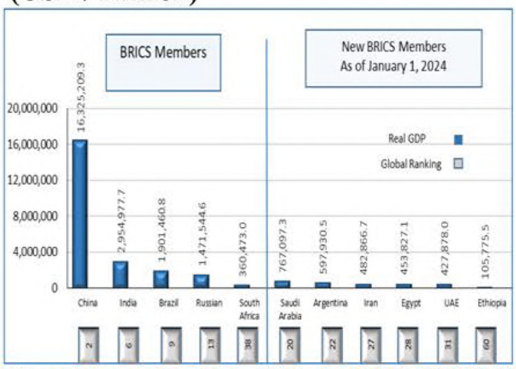
Among the objectives and goals of BRICS is the development of national currency settlements to promote economic growth. This should become one of the areas of partnership for common economic growth.

Here are some of BRICS countries' economic indicators:

First: GDP of BRICS Countries:

Several BRICS countries - China, India, Brazil, and Russia - occupy the world's top fifteen positions in World's First Gross Domestic Product (GDP), making them a global economic power.

Figure No. (1): Real GDP of BRICS Countries and Global Ranking in 2022 (USD$ Million)



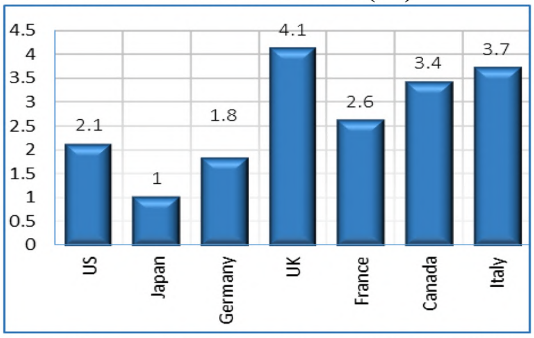
https://data.worldbank.org/indicator/NY.GDP.MKTP.KD?most_recent_value_desc=true

Since its start, BRICS has made comparisons with the Group of Seven (G7)[3] countries based on economic growth and other measures. While the rise of the bloc in recent years has drawn attention to its impact as a geopolitical power, it is noticed that

1) https://www.statista.com
2) https://tvbrics.com/en/news/what-is-brics-and-what-are-the-goals-of-this-alliance/
3) The G7 countries include the United States, Canada, the United Kingdom, Germany, France, Italy, and Japan.

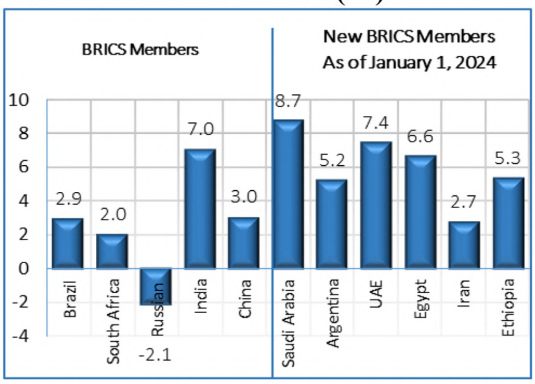
BRICS countries record output growth rates close to the seven countries except India, which recorded a growth rate by (7.0%), while for Russia the output growth rate decreased by (2.1%) after the imposition of international sanctions due to Russia's involvement in Ukraine war, which affected various Russian economic sectors[4].

Figure No. (2): Annual GDP Growth in the Seven Countries in 2022 (%)



https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?most_recent_value_desc=true

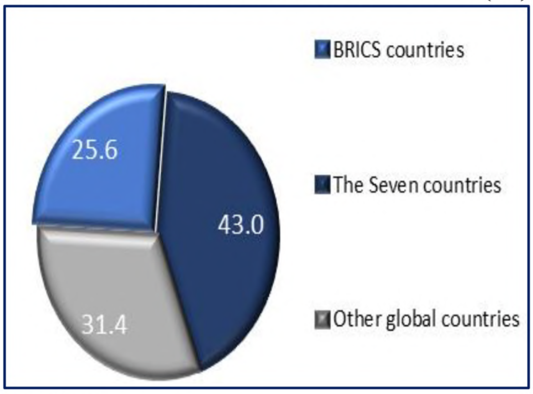
Figure No. (3): Annual GDP Growth OF BRICS Countries in 2022 (%)



https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?most_recent_value_desc=true

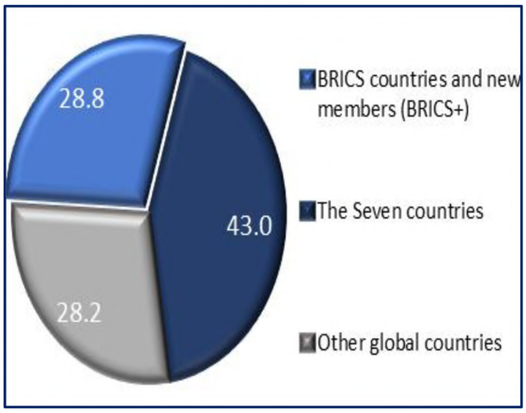
After accession of Ethiopia, Egypt, Iran, the UAE, Saudi Arabia and Argentina, the bloc is heading to increase its contribution to global gross domestic product, as the data shows an increase in the contribution of BRICS to global gross domestic product compared to the seven countries, after the accession of the new members, where the contribution of the BRICS countries increased from (25.6%) to (28.8%) after the accession of the new members compared to (43.0%) for the seven countries in 2022.

Figure No. (4): Contribution of GDP at Fixed Prices of BRICS States in 2022 (%)



Based on: https://data.worldbank.org/indicator/NY.GDP.MKTP.KD?most_recent_value_desc=true

Figure No. (5): Contribution of GDP at Fixed Prices of BRICS States and New Members in 2022 (%)



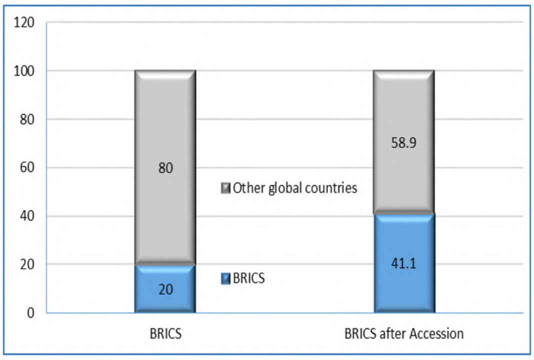
Based on: https://data.worldbank.org/indicator/NY.GDP.MKTP.KD?most_recent_value_desc=true

4) https://www.thenationalnews.com/world/uk-news/2023/08/22/growth-and-dominance-how-do-the-g7-and-brics-match-up/

Second: BRICS Countries and Global Oil Production:

After inviting Iran, Saudi Arabia, and the UAE (OPEC members), this means that the bloc will own a large share of the world's oil production and could therefore be used as an economic or political pressure card. Before the accession of Saudi Arabia, the UAE and Iran, the original BRICS members accounted for about (20%) of global oil production, but the addition of Saudi Arabia, the UAE and Iran raised the group's share to (41.1%) of global crude oil production in 2022.

Figure No. (6): Contribution of BRICS Countries to Global Oil Production before and after Accession of Saudi Arabia, the UAE and Iran in 2022 (%)

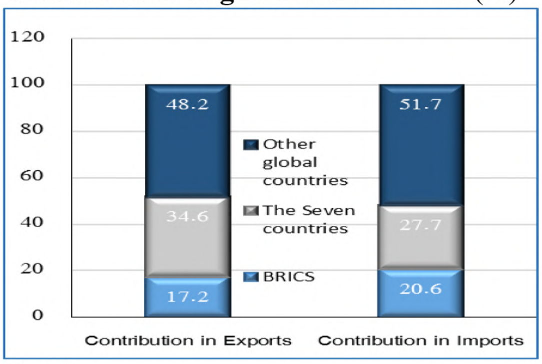


Based on: https://intellinews.com/brics-materials-the-flourishing-intra-brics-oil-trade-289879/

Third: The Volume of BRICS Trade and World Countries:

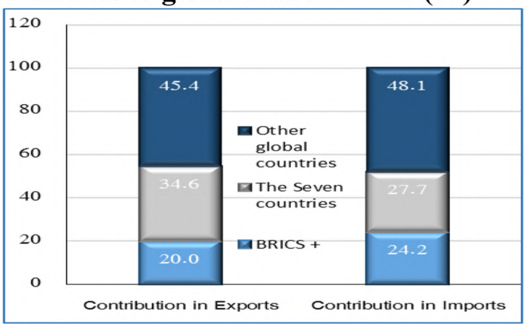
BRICS countries recorded an exports contribution of (17.2%) compared to an imports contribution of (20.6%), but after the accession of the new members (BRICS +), a contribution rate of exports amounted to (20.0%) compared to a contribution rate of imports to (24.2%), while the percentage of the seven countries' contribution of exports amounted to (34.6%) compared to a contribution of imports (27.7%). It is noted that the imports of the BRICS countries before and after the accession of new members were higher than their exports, meaning a deficit in the trade balance, and the deficit ratio increased after the accession of member countries.

Figure No. (7): BRICS countries' contributions to global trade in 2022(%)



Based on: https://data.imf.org/regular.aspx?key=61013712

Figure No. (8): Contribution of BRICS+ countries to global trade in 2022 (%)



Based on: https://data.imf.org/regular.aspx?key=61013712

Fourth: Commercial Transactions between BRICS Countries:

The Chinese yuan has replaced the U.S. dollar as the most traded currency in Russia, a year after the Russian-Ukrainian war, and led to a series of Western sanctions against Moscow.

The Yuan exceeded the dollar in monthly trading volume in February for the first time, and the spread became more pronounced in March, according to data compiled by Bloomberg based on daily transactions reports from the Moscow Stock Exchange.[5]

Brazil and China announced that they had agreed to use their domestic currencies for commercial exchange, rather than using dollar[6].

Argentinian minister of economy, Sergio Massa, announced that his country would officially start paying the value of imports from China in yuan, instead of the US dollar, and said in an official statement that this step would allow to pay the value of imports from this country in yuan, replacing US$ (1.04) billion in April 2023 and US$ (0.790) billion starting from May 2023[7]. A unit of China's state-owned PetroChina and another subsidiary of Abu Dhabi National Oil Company (ADONC) also completed a liquefied Natural Gas deal in **yuan**[8].

Fifth: Dollar Dominance of Foreign Reserves:

According to the international monetary fund's report in April 2023, the dollar's share of foreign exchange reserves globally reached (58.3%), the lowest share in years, and the euro comes in second place after the dollar (20.4%), then the Japanese yen (5.5%), and the Chinese yuan (2.6%)[9].

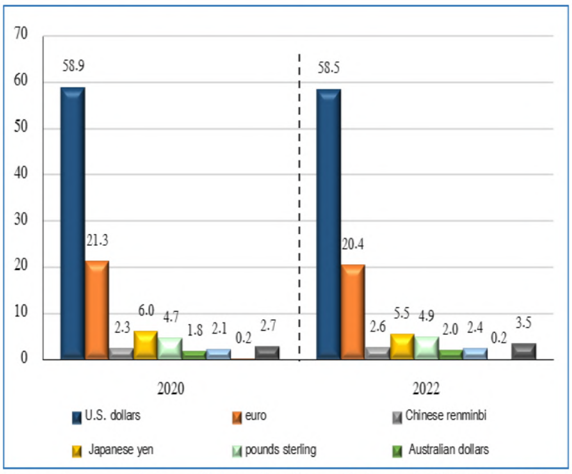
The share of US dollar reserves held by central banks fell to (58.9%)[10] during Q4 2020, its lowest level in 25 years, according to the International

5) https://www.bloomberg.com/news/articles/2023-04-03/china-s-yuan-replaces-dollar-as-most-traded-currency-in-russia#xj4y7vzkg
6) https://www.bbc.com/arabic/world-65150214
7) https://www.trtarabi.com/issues/%D8%A7%D9%84%D8%A3%D8%B1%D8%AC%D9%86%D8%AA%D9%8A%D9%86-%D8%AA%D8%AA%D8%AC%D9%87-%D8%A5%D9%84%D9%89-%D8%A7%D9%84%D9%8A%D9%88%D8%A7%D9%86-%D8%A7%D9%84%D8%B5%D9%8A%D9%86%D9%8A-%D9%87%D9%84-%D8%A8%D8%AF%D8%A3-%D8%A7%D9%84%D8%AF%D9%88%D9%84%D8%A7%D8%B1-%D9%8A%D8%AA%D8%B1%D9%86%D8%AD-13169905
8) https://attaqa.net/2023/08/30/%D9%86%D8%AC%D8%A7%D8%AD-%D8%A3%D9%88%D9%84-%D8%B5%D9%81%D9%82%D8%A9-%D8%BA%D8%A7%D8%B2-%D9%85%D8%B3%D8%A7%D9%84-%D8%AF%D9%88%D9%84%D9%8A%D8%A9-%D8%A8%D8%A7%D9%84%D9%8A%D9%88%D8%A7%D9%86-%D9%88/
9) https://www.aljazeera.net/ebusiness/2023/8/25/%D9%87%D9%84-%D8%AA%D8%B3%D8%AA%D8%AE%D8%AF%D9%85-%D8%A8%D8%B1%D9%8A%D9%83%D8%B3-%D8%A7%D9%84%D9%86%D9%81%D8%B7-%D9%88%D8%B1%D9%82%D8%A9-%D8%B6%D8%BA%D8%B7
10) https://data.imf.org/?sk=e6a5f467-c14b-4aa8-9f6d-5a09ec4e62a4&sid=1408206195757

Monetary Fund's Currency Composition of Official Foreign Exchange Reserves (COFER). Some analysts say this partly reflects the U.S. dollar's declining role in the global economy, in the face of competition from other currencies used by central banks in international transactions. And if Shifts in central bank reserves were large enough, they could affect the currency and bond markets[11].

It is noticed from the Figure that the Chinese renminbi (yuan) increased from (2.3%) in 2020 to (2.6%) in 2022, and other currencies increased from (2.7%) in 2020 to (3.5%) in 2022. On the other hand, the contribution of the US dollar decreased from (58.9%) in 2020 to (58.5%) in 2022. This change came after the Russian-Ukrainian war and the growing reliance on the renminbi (yuan) in commercial exchanges between China and other countries.

Figure No. (9): Currency Composition Ratio of Official Foreign Exchange Reserves 2020-2022 (%)



Based on: https://data.imf.org/?sk=e6a5f467-c14b-4aa8-9f6d-5a09ec4e62a4&sid=1408206195757

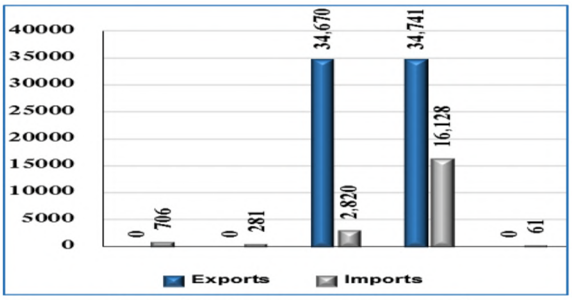
Sixth: Iraq's Accession to BRICS Countries:

Prime Minister Mohammed Shia al-Sudani confirmed that Iraq is ready to join the BRICS group if it receives an invitation from the founding countries. Al-Sudani explained that " Iraq understands the role played by the group and is aware of the conditions and specifications of joining it". He added that he discussed with Russian President Vladimir Putin a wide range of economic issues, including the use of IQD and Russian ruble in commercial transactions between the two countries. The ratio of Iraq imports from BRICS countries is (36.2%) in 2022, while exports to

11) https://www.imf.org/en/Blogs/Articles/2021/05/05/blog-us-dollar-share-of-global-foreign-exchange-reserves-drops-to-25-year-low

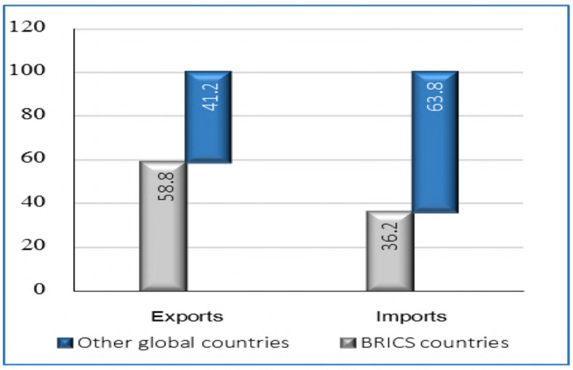
BRICS (58.8%) recorded for the same year, which means that the trade balance is in favor of Iraq with these countries. Iraq imports from China accounted for (29.2%) of total imports in 2022, while Iraq exports to the same country amounted to (29.4%) of total exports for the same year[12], and it is the highest ratio among BRICS countries.

Figure No. (10): Iraq Imports and Exports with BRICS Countries in 2022 (million dollars)



- Source: Central Bank of Iraq/Statistics and Research department/Balance of Payments and Foreign Trade Division.
- Imports are valued based on (CIF).
- Exports include crude oil and petroleum derivatives

Figure No. (11): The ratio of Iraq Imports and Exports with BRICS Countries in 2022 (%)



Based on the data of the Central Bank of Iraq/Statistics and Research Department/Balance of Payments and Foreign Trade Division.
Imports, exports: Central Bank of Iraq, Statistics and Research Department, Annual Economic Report 2022.

12) Iraq imports from China accounted for 80.7% of total Iraq imports from BRICS countries, while Iraq exports to China accounted for 50.1% of total Iraq exports to BRICS countries.

Conclusion:

In the light of BRICS goal of developing national currency settlements to promote economic growth at a time when trade between Russia and China has reached high rates in domestic currencies between two countries, along with the agreement of China and Brazil to abandon the dollar and use their domestic currencies in commercial transactions and the accession of new members, which would increase the proportion of commercial transactions between member countries in domestic currencies, there is great potential to reduce the dominance of the dollar in commercial transactions between member countries.

Increasing abandonment of the dollar and the use of domestic currencies in commercial transactions can reduce its retention for BRICS countries, which eases the severity of sanctions that are usually imposed on some members of BRICS countries, such as freezing funds of these countries. On the one hand, increasing the abandonment of the dollar and using domestic currencies in commercial transactions can reduce the demand of the dollar and thus decline its value, on the other hand.

As for the possibility of Iraq accession success to BRICS countries, it could result in a positive effect on Iraqi economy represented by increasing exports (after increasing oil production). In addition to improving bilateral relations between Iraq and member countries, which results in the possibility of concluding many agreements at all levels, as well as using of currencies other than the dollar in commercial exchange between the countries of the group.

The advantages of joining BRICS countries are highlighted in benefiting from the markets, capabilities and resources of the group countries, as this grouping, which includes the main emerging economies in the world, represents a huge economic market that can absorb large exports from economies, in addition to the investment opportunities offered by this market, and China and India represent major markets for oil imports from Iraq. Therefore, joining this group will open a way for increasing and strengthening the volume of economic cooperation between Iraq and BRICS countries.

Summary of the Economic Report for Third Quarter of 2023

Prepared by: Macroeconomics Division

Introduction:

The global economy witnessed a slow growth during the third quarter of 2023, due to several factors, most notably the ongoing (Russian-Ukrainian) war and the geopolitical tensions. Accordingly, commodity prices were subject to fluctuations, because of the political situations and concentrated production processes.

The following are the most important indices of the domestic economy during the third quarter of 2023 compared to the same quarter of the previous year:

- The gross domestic product (GDP) recorded a decrease of (2.9%) due to the reduction in crude oil production because of Iraq's commitment to OPEC's decisions to reduce production.
- The general inflation rate recorded a rate of (3.6%) for this quarter compared to the same quarter of the previous year, due to the increase in most of its components, due to the global and political circumstances, especially due to the fact the Iraqi economy heavily relies on imports to meet consumption.
- The monetary sector witnessed several developments, as the money supply (M1and M2) increased by (14.8%) and (13.2%) respectively. Foreign reserves recorded an increase of (18.3%) because of the decline in CBI's dollar sales. On the other hand, the activity of Iraqi banks witnessed an increase in deposits balance by (12.6%) resulted from the increase in public expenditures, and as cash credit at the banks increased by (12.2%). Consequently, its ability to create credit for this quarter has increased compared to the same quarter of the previous year.
- The public budget recorded a noticeable decrease during the third quarter of 2023. This decline occurred in the public revenues by (11.9%) because of the decrease in oil revenues, Meanwhile, current expenditures increased by (2.6%), while investment expenditure decreased by (16.5%).
- The volume of trade decreased by (27%) due to the reduction in exports and imports by (24%) and (34%) respectively.

GDP is expected to continue to grow slightly in 2024, supported by the acceleration in government spending, which will mitigate the impact of declining oil output. Given the heavy reliance on oil, the economy is vulnerable to shocks in oil markets. Additionally, the appreciation of the dinar is expected to lead to increased imports and undermine the competitiveness of exports. However, domestic political stability could pave the way for more investments in the economy and boost the potential GDP.

Chapter One: The Real Sector:

First: Gross domestic product:

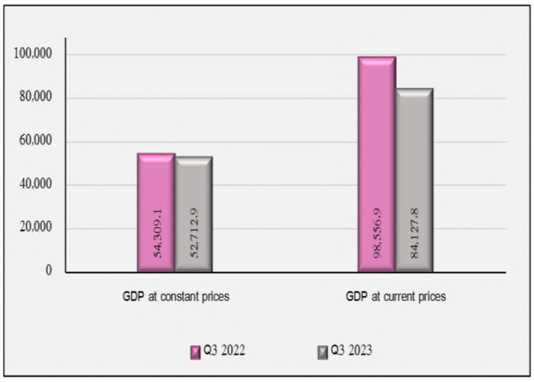
- GDP at constant prices:

The real GDP for the third quarter of 2023 recorded a decrease of (2.9%) to reach (52,712.9) billion dinars compared to (54,309.1) billion dinars for the same quarter of the previous year. This decline is primarily attributed to a 11.5% decrease in crude oil production, resulting from a lower production quota under the OPEC+ agreement.

- GDP at current prices:

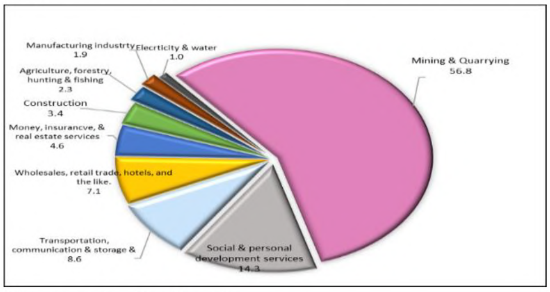
The GDP at current prices for this quarter recorded a significant decrease of (14.6%) to reach (84,127.8) billion dinars compared to (98,556.9) billion dinars for the same quarter of the previous year. This decline comes from the reduction in crude oil prices by (11.1%).

Figure No. (1): GDP at Current Prices & Constant Prices for Q3 of 2022-2023 (billion dinars)



-Sectoral structure of GDP at constant and current prices:

Figure No. (2): Sectoral Structure of GDP

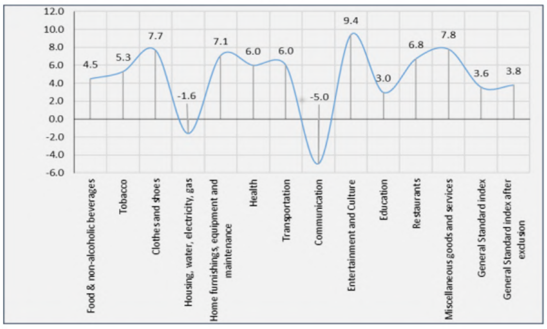


Second: Inflation:

General inflation rate of the consumer price index in Iraq during the third quarter of 2023 recorded a rate of (3.6%) on an annual basis. It reached (122.3) points in the third quarter of 2023 compared to (118.1) points in the same quarter of the previous year. This inflation rate is attributed to the rise in most of its items due to global and political circumstances, especially since the

Iraqi economy heavily relies on imports to cover up the consumption.

Figure No. (3): Inflation Rate According to Main Groups of Consumer Price Index for Q3 2023 (%)

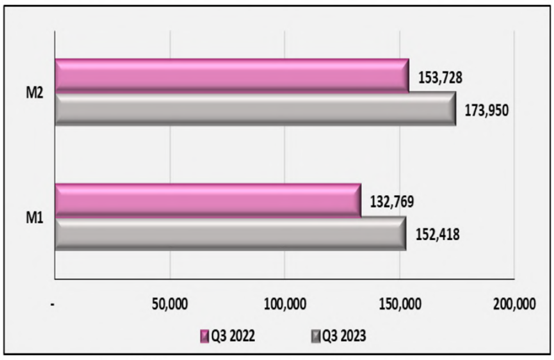


Chapter Two: The Monetary Sector

First: Monetary Indices

The monetary sector witnessed several developments. The money supply (M1) increased by (14.8%). This is attributed to the growth in both current deposits and currency outside banks by (6.5%) and (21.0%) respectively. This was due to the continuation of initiatives and loans provided by CBI and other banks, as well as to the growth of current deposits, which was reflected in the increase of the monetary mass, and the money supply (M2) also increased by (13.2%). This increase was a result of the growth in the narrow money supply (M1) by (14.8%) and other deposits (fixed, savings, postal and insurance) by (1.5%), which constituted (12.4%). Whereas foreign reserves recorded an increase of (18.3%) due to the decrease in the CBI's dollar sales.

Figure No. (4): Money Supply M1 and M2 for Q3 of 2022-2023 (billion dinars)



Second: Monetary Policy Tools

- Foreign Currency selling window

The amount of US dollars sold through CBI's foreign currency selling window in the third quarter of 2023 decreased by (41.5%) to reach (8.3) billion dollars compared to (14.2) billion dollars for the same quarter of the previous year.

This is attributed to the decrease in the CBI's sales of remittances and a (44.7%) increase in foreign reserves, due to the auditing procedures (restrictions imposed on the window). While cash sales decreased (23.1%) compared to the same quarter of the previous year.

- Reserves Requirements

The Reserves Requirements recorded a significant increase of (38.1%) in the third quarter of 2023, reaching (17.4) trillion dinars compared to (12.4) trillion dinars for the same quarter of the previous year. This is due to a (12.6%) increase in the balance of deposits at banks in Iraq for this quarter compared to the same quarter of the previous year.

Chapter Three: The Banking Sector

- Capital Capacity

Total capital of banks in Iraq recorded a (0.7%) increase in the third quarter of 2023, reaching (17.9) trillion dinars compared to (17.8) trillion dinars for the same quarter of the previous year. This is attributed to the CBI's decision to increase bank's capital, so that the capital of private banks would increase by (0.9%), while the capital of stated owned banks remained unchanged in the third quarter of 2023.

- Bank Deposits and Credit

Bank deposits increased by (12.6%) in the third quarter of 2023, reaching (122.4) trillion dinars compared to (108.7) trillion dinars for the same quarter of the previous year. Current deposits increased by (15.7%), due to the increase in public expenses, which were transferred to banks in the form of current deposits, while savings deposits also increased by (3.4%), and fixed deposits by (1.5%). The increase in savings and fixed deposits was due to the increase in the number of banks' accounts during this year, as a result of the facilitation of account opening procedures, in addition to the increase in point-of-sale (POS) devices, whereas the balance of cash credit granted by banks in Iraq at the end of the third quarter of 2023 recorded an increase of (12.2%), reaching (65.1) trillion dinars, compared to (58) trillion dinars in the same quarter of the previous year. This rise is due to the increase in both the balance of credit granted to the private sector and the central government by (22.0%) and (4.4%) respectively, despite the decrease in credit granted to public institutions by (29.4%) compared to the same quarter of 2022.

Figure No. (5): Cash Deposit Balance by type for Q3 of 2022-2023

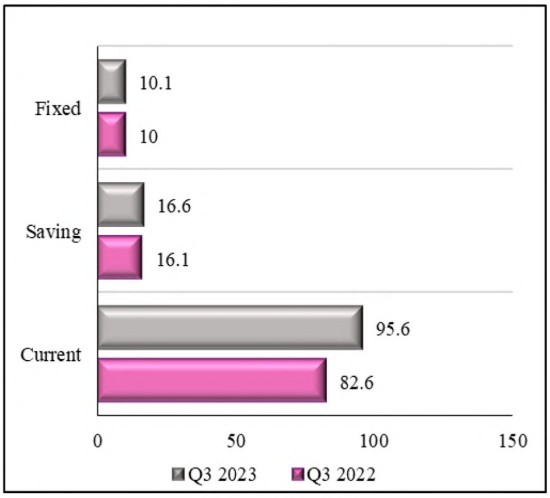
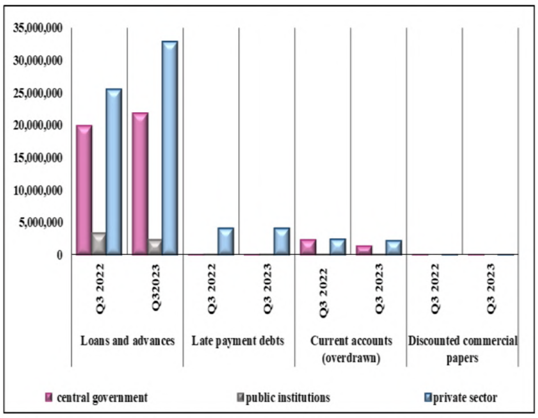


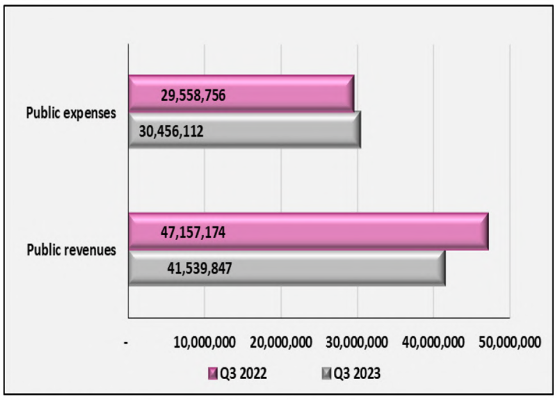
Figure No. (6) Development of Cash Credit Balance by type for Q3 of 2022-2023



Chapter Four: The Financial Sector

The public budget recorded a noticeable decrease during the third quarter of 2023. which was a result of the decrease in public revenues by (11.9%) due to the decline in oil revenues, whereas current expenditures increased by (2.6%) with a decline in investment expenditures by (16.5%).

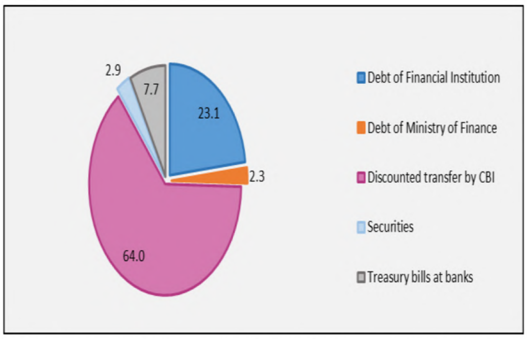
Figure No. (7): Total Public Revenue and Expenditure for Q3 of 2022-2023 (million dinars)



- Domestic public debt:

The domestic public debt balance recorded an increase of (2.3%) in the third quarter of 2023, reaching (68.1) trillion dinars compared to (66.6) trillion dinars for the same quarter of the previous year. This is attributed to (14.8%) increase in the Ministry of Finance's debt item for the third quarter of 2023 compared to the same quarter of the previous year. However, the overall increase was low at (2.3%) due to the Ministry of Finance's repayment and subsequent recovery of funds.

Figure No. (8): The percentage of Domestic Public Debt Contribution for Q3 of 2023 (%)



Chapter Five: The External Sector

Trade Volume:

The volume of foreign trade in Iraq decreased by (27%) in the third quarter of 2023, reaching (35,110.2) million dollars, compared to (48,102) million dollars for the same quarter of 2022. This decrease is attributed to the decline in both exports and imports compared to the same quarter of the previous year by (24%), (33.7%) respectively.

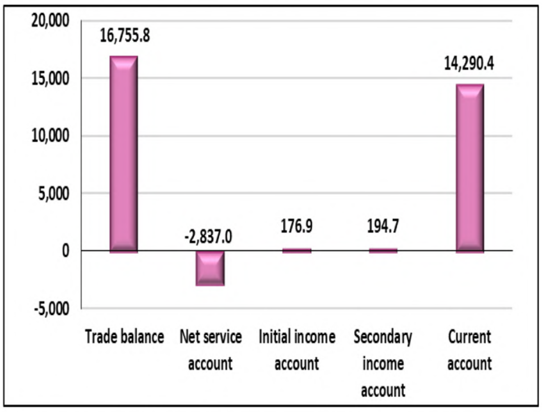
Table No. (1): Trade volume for Q3 of 2022-2023 (million dollars)			
	Growth rate (%)	Q3 2023	Q3 2022
Exports	-24	25,188.9	33,134.7
Imports	-33.7	9,921.3	14,967.3
Trade volume	-27	35,110.2	48,102

- Exports on a (FOB) basis.
- Imports on a (CIF) basis.

- Balance of Payments

The Iraqi balance of payments recorded a surplus of (635.7) million dollars in the third quarter of 2023. This surplus was driven by an increase achieved in the country's foreign exchange reserves, which are managed by CBI. Several factors contributed to the achievement of this surplus, which is explained through the components of the Iraqi balance of payments.

Figure No. (9): Components of the Current Account for Q3 of 2023 (million dollars)



Chapter Six: Payment System

The Iraqi Payments System is defined as a system that connects the CBI with the main branches of banks and the Ministry of Finance to exchange high-value payment orders. The payment system is the modern form of cash circulation, and it is a tool that provides cash payment services through electronic means. It has a positive impact on the capital market, as electronic payments help increase capital accumulation and, consequently, economic growth. Its system also increases the organizational capacity of individuals and institutions and alleviates the cash liquidity crisis. It even eliminates the problem of counterfeit banknotes, as well as protects its users from some significant losses that may be caused by an error of a bank employee. CBI is responsible for educating customers and citizens about adopting the electronic payment system as a fast, secure, and efficient means. This system is a means of establishing a digital economy with technological foundations. As such, it must be monitored by CBI to control monetary policy, in addition to the volume and speed of cash liquidity. The two figures below show the developments in the components of the payment system for Q3 of 2023.

Figure No. (10): Components of the Payment System for Q3 2022 – 2023

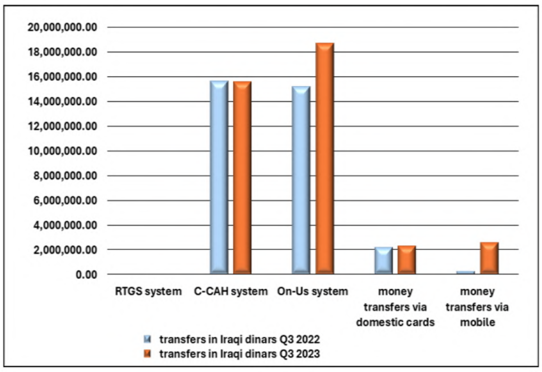
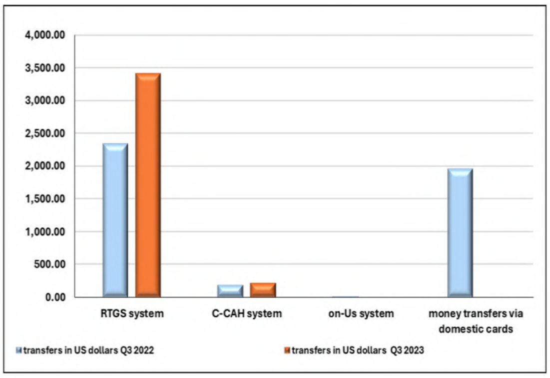


Figure No. (11): Components of the Balance of Payments for Q3 2022-2023



Summary of Early Warning Report for the Fourth Quarter 2023

Prepared by: Monetary and Financial Stability Division

The early warning report for the banking sector is one of the most important direct supervisory tools for this sector, through the indices it contains that can predict the occurrence of imminent and potential crises in general, even if they do not materialize, as well as measure the potential deviations that may affect the banking sector and the variables affecting it.

The report includes three chapters covering most of the indices that affect the work of the monetary authority, as follows:

Chapter One: Analysis of Currency Value Stability Indices

Analyzing the stability of a currency involves monitoring several indices that show unusual pre-crisis behavior when the index exceeds a certain limit. These are considered as "signals" of warning to currency value crisis likelihood during the following 24 months. Among the most important indices that provide an accurate analysis of the fluctuations in the value of national currency are:

First: Adequacy of Net Foreign Reserves Indices

1. Adequacy of Net Foreign Reserves to Issued Currency Index

The ratio of this index expresses the relationship between the value of the net foreign reserves of the central bank and the value of the national currency in the financial system. An increase in the ratio is considered a good sign in the financial and economic system, while a decrease in it indicates the presence of problems that may negatively affect the external value of the currency and the local economy. The coverage ratio of net foreign reserves index for the issued currency recorded a decrease to (144%) in the fourth quarter of 2023 compared to (161%) in the fourth quarter of the previous year. This decrease is attributed to defending the exchange rate because of the government's request for the dinars to finance spending, which in turn led to an increase in the issued currency by (15.9%), which exceeded the growth of net foreign reserves of (3.7%).

2. Net Foreign Reserves Coverage to Total Imports Index:

This index is used to assess the quality of the country's economy and the stability of its financial system. International financial institutions such as the International Monetary Fund (IMF) and the World Bank (WB) are interested in monitoring this index to direct the necessary financial support in case of need. In some countries, the minimum limit of this index ranges from 4 to 5 months. This ratio varies from country to another depending on the country's economic situation. In Iraq, the minimum acceptable limit of this index is 6 months. The period of foreign reserves coverage to total imports for Q4 of 2023 increased to 28 months, up from 27 months for the same quarter of the previous year.

Second: Changes in Interest Rates Averages

Interest rates averages are considered one of the most important factors that affect national and global economies. This report details the changes occurring in the interest rates of :

1.Short-Term Interest Rates on Deposits: It is noticed from the report that interest rates had been maintained for 6 months with a rate of (4.3%) in the fourth quarter of 2022, as well as a decrease in interest rates for one year from (5.1%) to (4.9%). The interest rate on savings deposits also decreased from (3.5%) to (3.2%). Despite these changes in interest rates, they did not significantly affect the volume of deposits.

2.Real Interest Rates: Real interest rate is considered an important index as it takes into account inflationary pressures and their effects on nominal interest rates. The report shows a rise in real interest rate during Q4 2023 to reach (0.17%) compared to the same ratio for Q4 2022, which was (-0.13%).

Third: The Gap Between Black Market Exchange Rate and Official Exchange Rate

It is noticed from the report that the gap between the black-market exchange rate and the official exchange rate reached IQD (273) during the fourth quarter of 2023.

Chapter Two: Analysis of Banks' Performance Indices

The analysis and measurement of the banking sector's performance indices can identify risks to which the banking sector may be exposed. This is done through several indices; the following are the most important indices regarding banks' performance.

1. **Banking Deposits to Broad Money Supply (M2):** This index shows the public's desire to seek banks because of their need for the purpose of obtaining services that attract the public to them. It was found out that the ratio of bank deposits to (M2) decreased during the fourth quarter of 2023 to (47.7%) after it was (51.3%) for the same quarter of 2022.
2. **Types of Deposits at Banks in Iraq:** The report demonstrates that current deposits accounted for the largest percentage of total deposits with banks, as their percentage of total deposits increased to (80.5%) during the fourth quarter of 2023 after it was (79.2%) during the same quarter in 2022, while the percentage of fixed deposits decreased to (7.2%) after it was (7.9%). As for savings deposits, it also decreased from (12.9%) during the fourth quarter of 2022 to (12.2%) for the same quarter of 2023.
3. **Total Cash Credit to Total Deposits:** This Index shows the ability of banks to use the funds obtained from deposits to meet the credit needs of customers, The Central Bank of Iraq set this percentage at (75%) in order to maintain sufficient liquidity in banks to face customer withdrawals and conduct the bank's financial activities. It is noted throughout the report that the index percentage increased from (46.9%) in the fourth quarter of 2022 to (51.9%) in the same quarter of 2023.
4. **Money Multiplier:** It represents the desire and ability of banks to convert their deposits into credit, and as such it represents banking activity within the real sector. The monetary multiplier recorded a decrease in the fourth quarter of 2023, reaching (1.09) after it was (1.16) for the same quarter of 2022, due to the increase in the excess reserves of banks operating with the Central Bank from (48.4) trillion dinars to (49.0) trillion dinars, with a growth rate of (1.2%) during the same period.

5. **Non-Performing Loans to Total Cash Credit:** This index is measured by dividing non-performing loans to total cash credit. The report shows that the ratio of non-performing loans to total cash credit in the fourth quarter of 2023 decreased to (6.26%) after it was (7.19%) for the same quarter of 2022. This decrease is due to the increase in the credit granted, as its growth rate reached (14%).
6. **Net Open Position in Foreign Currency for Banks:** This index measures the net foreign assets of operating banks, by calculating the difference between their foreign assets and foreign liabilities divided by capital. The report shows a decrease in the indicator ratio for operating banks from (21.5%) in the fourth quarter of 2022 to (18.0%) in the same quarter of 2023, because of a decrease in net foreign assets by (5%) with an increase in capital by (13%).

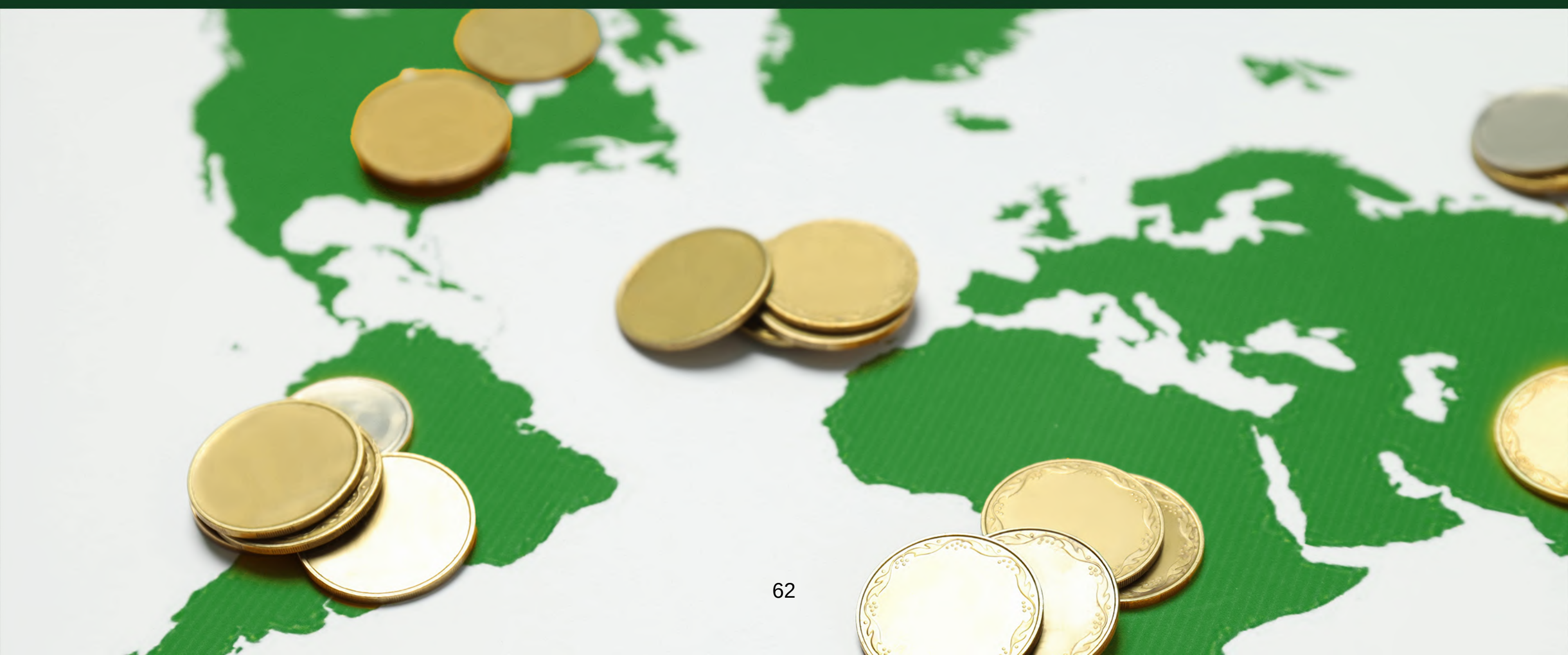
Chapter Three: Analysis of Macroeconomic Performance Indices:

Macroeconomic variables are one of the most important variables affecting the financial system. They also directly and indirectly affect the banking sector, so the early warning report analyzed the most important macroeconomic indices, including:

1. **Inflation Rate**: Inflation is a quantitative measure that expresses the change in the general price level of goods and services during a specific period, as is measured by calculating the change in the consumer price index (CPI). The inflation rate in Iraq recorded a slight decrease during Q4 2023 to record (4%) compared to the same quarter of 2022, as the percentage was (4.4%), due to the increase in foreign transfers for the purpose of import after the improvement in the foreign currency selling window operation.
2. **Internal Debt Growth Rate**: This index reflects the government's obligations towards banks and the Central Bank. The report shows an increase in total internal public debt, reaching IQD (70.6) trillion in Q4 2023, after it amounted to IQD (69.5) trillion during the same quarter of 2022, due to the increase in government borrowing from

state-owned banks by IQD (3) trillion, during Q4 2023.

3. **Gross Domestic Product (GDP) Growth:** GDP represents a measure of a country's economic performance, as it expresses the level of economic activities during a certain period of time, as GDP at current prices in Iraq recorded a decrease during Q4 of 2023 by (7.3%) to reach IQD (89.3) trillion compared to the same quarter of 2022 which amounted to IQD (96.3) trillion, This is attributed to the decrease in the output of crude oil activity.
4. **Monetary stability coefficient:** The monetary stability coefficient index shows the extent of inflationary pressures faced by a country's economy, and can be reached by dividing the growth on (M2) to growth in GDP at current prices, as monetary stability is achieved when the value of this index is equal to one while the economy faces inflationary pressures (a rise in the general level of prices) when its value is greater than one. This is on the one hand. On the other hand, the economy suffers deflation when its value is smaller than one. The report shows a decrease in the value of this index, as its value decreased to (6.2) in Q4 2023 from (9.9) in the same quarter of 2022. This decrease was due to a decrease in the growth rate of (M2) to reach (7.5%) in Q4 2023 after it was (20.3%) in the same quarter of 2022.



Summary of Iraqi Balance of Payments Report 2023 (Preliminary)

It is a statistical statement that summarizes transactions between residents and non-residents during a certain period and according to the double entry system. Each transaction is recorded and has two entries, and the sum of the credit entries is equal to the sum of the debtor entries. A distinction is made between the different accounts in balance of payments according to the nature of the economic resources that are provided and obtained. Balance of payments is the window from which the national economy overlooks the global economy and vice versa. The balance of payments is important based on the economic analysis of any country because it reflects the overlap of the national economy with the global economy and consists of (current, capital, financial account and net of omission and error account).

The results of the Iraq balance of payments during 2023 showed a surplus of US$ (20078.8) million because of the increase achieved in the assets reserve managed by the Central Bank during this period. Several factors have contributed to achieve this surplus, which is reflected through our review of the components of the Iraq balance of payments and as follows: -

First- Current Account:

The current account index in the balance of payments reflects the behavior of the state through the state's budget and behavior of private sector through available data. The current net account recorded a surplus of US$ (28374.6) million during 2023. Below is a review of the detail’s components of this account:

1. **Trade Balance:** During the year 2023, trade balance achieved a surplus by US$ (43,196.7) million, whereas total exports recorded an amount of US$ (99149.2) million, including the value of in-kind crude oil paid to foreign oil companies with a value US$ (13388.2) million, while the total imports recorded an amount of US$ (65826.4) million on the basis of CIF and US$ (55952.5) million on the basis of FOB, whereas the value (15%) of total imports was deducted for shipping and insurance costs to transfer them from CIF to FOB.
2. **Net Services Account:** During the year 2023, the net services account showed a deficit of US$ (16524.0)

million dollars. This deficit was due to the increase in payments of US$ (25226.7) million, most of which were payments related to travel, transportation, and insurance costs. While the receivables amounted US$ (8702.7) million, most of which were achieved in the travel item, including those coming to Iraq from Arab and foreign nationals for the purposes of tourism and visiting the Holy Places.

3. **Primary Income Account:** The net primary income account during 2023 achieved a surplus of US$ (973.3) million.

The following is a detailed statement of this account:

A- Workers' compensation: represents the amounts transferred by workers who have been working outside their home country for less than one year. The net workers' compensation account during the year 2023 achieved a surplus of US$ (71.3) million.

B- Investment income: The net investment income achieved a surplus of US$ (902.0) million because of an increase in receipts, which is represented by interest in investments in both the Central Bank and the Ministry of Finance.

4. **Secondary Income Account:** During the year 2023, the net secondary income account achieved a surplus of US$ (728.6) million as a result of the increase in the receipts of US$ (614.6) million, the decrease in payments US$ (63.1) million and the increase in net private transfers US$ (177.1) million for family assistance provided by non-residents to their families and remittances of workers who work outside their home country for more than a year.

Second - Capital account:

During the year 2023, the net capital account achieved a deficit of US$ (41.2) million. This account represents capital transfers resulting from the disposal of fixed assets and capital grants provided by governments and international organizations.

Third - Financial accounts:

During the year 2023, net financial accounts achieved an amount of US$ (25988.3) million, as it appeared with a positive sign because of the changes that occurred in both external financial assets and liabilities.

The following is a review of the components of this account:

1. **Net Direct Investment:** During the year 2023, this net account achieved a surplus of US$ (5649.7) million, as a result of increasing in external financial assets by US$ (286.2) million, with a decrease in financial liabilities of US$ (5363.5) million, over the payment of capital costs of oil fields provided by the contractors of the service contracts for foreign oil companies operating in Iraq.
2. **Net Portfolio Investment:** During the year 2023, the net portfolio investment achieved a surplus of US$ (243.1) million because of the decrease in government liabilities by US$(348.3) million and the increase in the assets of other sectors by US$ (12.5) million.
3. **Net Other Investment:** During the year 2023, the net investment achieved a surplus of US$ (16.7) million, as a result of the decrease in the financial liabilities of the official sector by US$ (5903.6) million and decrease in the net of investment of ODC by US$ (3970) million and the increase in net Deposits abroad by US$ (325.5) million.
4. **Assets Reserve (Official Reserves):** During the year 2023, the assets reserve of The Central Bank of Iraq achieved a surplus of US$ (20078.8) million, because of the increase in foreign assets managed by the Central Bank of currency and deposits with foreign banks.

Fourth: Net Omission and Error Item

During the year 2023, net omission and error item achieved an amount of US$ (2345.1) million. This item appeared with a negative sign, i.e., there are debit transactions not recorded in the balance of payments or were not fully covered because they were not available from the source, or there may be credit restrictions estimated more than their value.

Summary of the Financial Stability Report 2023

Prepared by: Monetary and Financial Stability Division

This financial stability report focuses on the Central Bank's efforts to maintain financial stability, analyze potential risks to the financial system, and develop the financial infrastructure to support financial stability and economic growth. The report includes a comprehensive analysis of global developments and changes affecting the Iraqi financial system, including the impact of climate change. It provides recommendations to enhance its stability and performance in the face of international and domestic challenges.

The report also comprises varied chapters that focus on the changes affecting the financial system and their impact on the overall economy, as detailed below.

Chapter One: Developments in the Iraqi Financial Sector:

This chapter presents an analysis and interpretation of the developments that took place in the financial sector throughout the year, based on ratios, indicators, and financial amounts specific to the sector. The financial sector consists of both banking and non-banking institutions. The Iraqi banking sector witnessed growth in 2023, with total assets rising to IQD 205.25 trillion dinars, compared to IQD 198.66 trillion dinars in 2022, thus recording a growth rate of 3.3%. Despite a decline in the share of government banks in the total assets from 81.31% in 2022 to 78.61% in 2023, the total capital of the banking sector increased by 6.6% to reach IQD 19.07 trillion dinars.

Total deposits in the banking sector increased from IQD129.1 trillion dinars in 2022 to IQD133.50 trillion dinars in 2023, representing a growth rate of 3.42%, primarily due to IQD 5.2 trillion dinars (5.13% increase) in current deposits. Similarly, the total credit extended by banks also grew in 2023, from IQD 90.96 trillion Iraqi dinars in 2022 to IQD 95.66 trillion dinars in 2023, marking a 5.2% increase. This growth was influenced by the Central Bank's initiatives to finance various sectors.

The most significant increase was observed in cash credit, which grew by 14.32% from IQD 60.57 trillion dinars in 2022 to IQD 69.25 trillion dinars in 2023, hence reflecting the Central Bank's role in supporting bank financing. The report also includes an analysis of the non-banking financial sector, both under and outside the Central Bank's supervision, which plays a crucial role in achieving economic growth and financial stability by lending institutions with a significant presence in the Iraqi economy.

Chapter Two: Household Debt:

The ratio of credit extended to the private sector to the Gross Domestic Product (GDP) in Iraq increased to 11.9% in 2023, compared to 7.6% in 2018. This credit is distributed between the household and corporate sectors. While the credit to the household sector accounted for 9.3% of GDP in 2023, the corporate sector accounted for 2.6% during the same period. From a financial stability perspective, this indicates that the credit extension to the household sector does not pose a significant risk to financial stability and can be expanded without major concerns.

Chapter Three: Financial Safety Indicators (FSIs)

Financial safety indicators are crucial for monitoring the financial status of the banking sector. They help analyze vulnerabilities in financial systems and provide an assessment of the sector's stability in Iraq. These indicators showed stability in the banking sector for 2023, with the capital adequacy ratio increasing to 41.9% compared to 34.1% in the previous year, thus exceeding the regulatory requirement set by Basel III. This reflects the sector's efficiency and ability to withstand risks. While the Liquidity Coverage Ratio (LCR) decreased to 131% in 2023 from 231% in 2022, it still exceeds the minimum requirement of 100%, hence indicating banks' ability to manage liquidity-related risks. Additionally, the ratio of credit to deposits increased to 51.9% in 2023 compared to 46.9% in 2022, falling within the regulatory limit set by the Central Bank of Iraq, which should not exceed (75%).

Furthermore, asset quality indicators have improved, as the ratio of non-performing loans to total credit decreased from 7.19% in 2022 to 6.26% in 2023. Similarly, the ratio of non-performing loans to total assets decreased from 2.19% to 2.11%, hence reflecting an improvement in asset quality and a decrease in the ratio of non-performing loans relative to capital.

Chapter Four: Developments in Financial Infrastructure and Financial Inclusion:

The central bank has significantly contributed to developing the financial infrastructure and promoting financial inclusion in Iraq. In early 2023, it launched an electronic platform to facilitate foreign transfers and the sale of cash dollars to travelers, as part of a policy aimed at facilitating foreign trade financing, securing foreign currency for legitimate beneficiaries, and achieving exchange rate stability.

Furthermore, sub-accounts were opened for electronic payment service providers from the Central Bank of Iraq's main account at JPMorgan Chase. Additionally, the security infrastructure for retail payment systems was developed, and a platform for selling gold bullion and coins was established. Cybersecurity management center tools were also developed, and an advanced approach was adopted to enhance cybersecurity in the bank and the banking sector. Moreover, a cyber monitoring, response, and analysis unit was established."

Chapter Five: Macroeconomic Stress Tests:

The results of macroeconomic stress tests are analyzed according to two models. The first model analyzes the impact of shocks on variables such as the parallel exchange rate, which significantly affects the financial situation in Iraq. The exchange rate of the US dollar against the Iraqi dinar has a direct relationship with liquid assets, as the value of foreign assets, which are part of liquid assets, will increase as the value of the dollar rises against the dinar, which in turn depends primarily on public expenditures and affects overall consumption and investment. It also has a direct relationship with the ability to fulfill financial obligations.

Risk-weighted assets are reflected in the liquid asset ratio. The second model includes the impact of the parallel exchange rate and cash credit on non-performing loans of banks operating in Iraq. In general, the analysis of the tests shows how these factors affect the sustainability and stability of the financial system, and how these shocks can lead to changes in the liquid asset ratio and the non-performing loan ratio, which affects the amount of credit provided to the private sector and will reflect on the overall economic variables, especially since the exchange rate is no longer dynamically pegged to inflation after the implementation of the electronic platform for foreign transfers.

Chapter Six: Measuring the Composite Index of Financial Stability

The index maintained its level with a slight decrease to 0.402 in 2023 compared to 0.427 at the end of 2022. This reflects the stability of the financial system and its lack of exposure to potential risks. There was improvement in some stability indicators, as the banking sector index and the global economic index increased to 0.223 and 0.015, respectively, in 2023, compared to 0.188 and 0.014, respectively, in 2022, while the macroeconomic index, the capital market index, and the financial cycle index decreased to 0.114, 0.052, and 0.0, respectively, in 2023.

Chapter Seven: The Impact of Climate Change on Financial Stability

Climate change significantly affects financial stability. Rising temperatures and severe droughts lead to the deterioration of the agricultural sector and related projects, thus contributing to a decline in the relative importance of the agricultural sector in GDP and affecting farmers' income.

Desertification and dust storms negatively impact agricultural crops, thus leading to increased migration from rural to urban areas. This puts pressure on urban infrastructure and services. Addressing these challenges requires significant investments in infrastructure and technology, which puts pressure on the financial resources of the government and the private sector. All these factors when combined contribute to the creation of an unstable economic environment that affects Iraq's ability to achieve sustainable economic growth and financial stability.

This bank's role is highlighted in a set of measures and initiatives to mitigate climate risks, including initiatives for afforestation, and the use of renewable energy sources to reduce carbon emissions, as well as the rehabilitation and development of parks and the issuance of regulations to finance renewable energy generation systems.

Economic Monitor Report for January 2024

Prepared by: Abdul Hamid Abdul Hadi Hamid/ Researcher

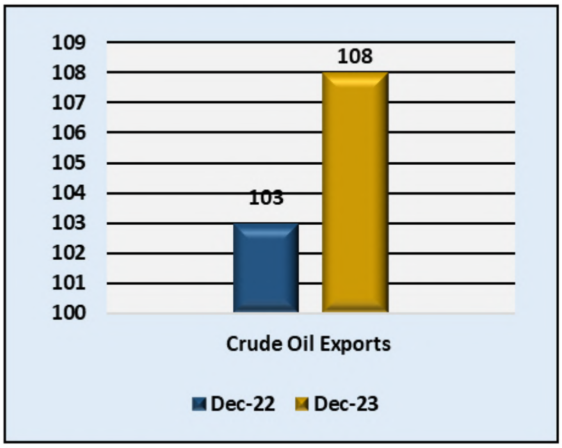
Introduction

The Iraqi Economic Monitor Report for January 2024 included Iraqi economy sectors, through indices of (oil, real growth rate, inflation, global and Iraqi food prices, financial budget, money supply, total foreign exchange reserves, private cash credit provided by commercial banks, foreign currency deposits in the banking sector, foreign auction sales, in addition to the monitor's expectations for the coming years (2024-2029) for the economies (Iraq, emerging countries, developing countries) and according to the following details:

First: The most Important indicators for the Iraqi Economy

1. **Oil Sector:** Crude oil exports for December 2023 recorded (108,056,509) barrels compared to December 2022 (103,281,459) million barrels; an increase of (4.62%), while the average price of exported oil during December recorded 2023 USD$ (76.91) compared to the previous year for December 2022 USD$ (74.63) at an increase rate of (3.06%), as shown in Figure No. (1).

Figure No. (1): Crude oil Exports 2022-2023 (Billion Barrels)



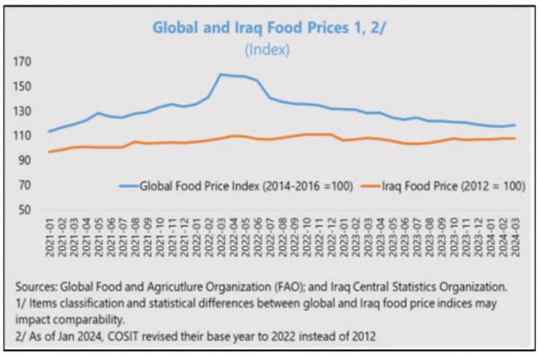
2. Real Growth Rate

Real GDP increased from IQD (52,026.20) billion in the second quarter of 2023 to IQD (52,712.90) billion in the third quarter of the same year, as shown in Figure No. (2), with a growth rate of (1.32%), due to the increase in the growth rate of non-oil GDP by (11.2%), despite the decrease in crude oil production by (11.5%) due to the decrease in the production share under the (OPEC +) agreement. The increase in non-oil GDP in the third quarter of 2023 is attributed to the implementation of the general budget, in addition to the increase in growth rates in the sectors (social development services, construction and building, agriculture, forestry, hunting and fishing, manufacturing industry, electricity and water) by rates of 33.6%, 38.9%, 28.9%, 16.7%, 9.7% respectively, compared to the same quarter of 2022.

Figure No. (2) Real GDP during Q2 & Q3 2023 (Trillion Dinars)

3. **Sectoral Contribution to GDP Growth rate without Oil** Construction and building ranked first with a percentage of (38.9%) in the non-oil GDP. The contribution of social development services was ranked second with a percentage of (32.6%), while agriculture, forestry, hunting and fishing, manufacturing, electricity, and water recorded a percentage of (28.9%), (16.7%), (9.7%) respectively.
4. **Inflation**: The general inflation rate for the consumer price index recorded a decline of (45%) in Q3 of 2023, reaching (3.6%) compared to Q1 of 2023, which amounted to (6.6%), and inflation is expected to stabilize in the coming months, that is due to the Central Bank of Iraq tighter monetary policy, the impact of raising the exchange rate of the Iraqi dinar, the decline in global food prices, and the return of trade financing operations to their normal state.
5. **Iraqi and Global Food Prices:** Food prices in Iraq have remained the same over the year, at a rate lower than global rates, according to the Economic Monitor Report shown in Figure No. (3), because of the regular distribution of the food basket on time, in addition to the decline in the inflation rate. In contrast, global food prices have been on a continuous decline, which is the lowest level in two years.

Figure No. (3): Global and Iraq Food Prices

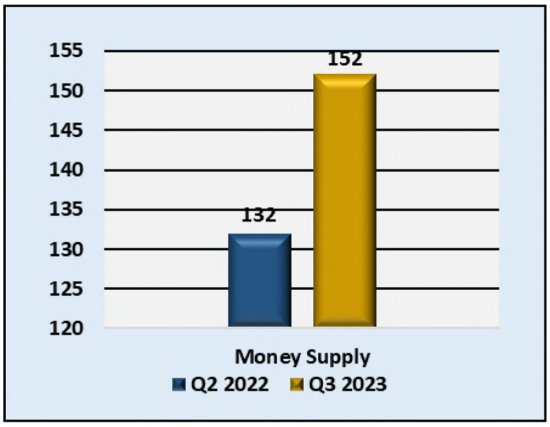


6. **State Financial Budget:** Public expenditures witnessed an increase

of (3.0%) in the third quarter of 2023 compared to the same quarter of 2022, as a result of the approval of the three-year general budget for the years (2023-2024-2025) and an increase in total current expenditures by (2.3%), while public revenues in the budget recorded a noticeable decrease of (11.9%) during the same period due to a decrease in oil revenues by (17.8%).

7. **Money Supply Growth Rate:** The money supply balance in its narrow sense recorded an increase of (14.8%) at the end of Q3 2023 to record IQD (152,418) billion compared to IQD (132,769) billion for the same quarter of last year due to the increase in the current deposits and currency outside banks, as shown in Figure No. (4).

Figure No. (4): Money Supply during Q2 & Q3 2023 (Trillion Dinars)



8. **Total Foreign Reserves:** The balance of foreign reserves for Q3 2023 recorded an increase (18.3%) to reach IQD (143.6) trillion compared to IQD (121.4) trillion for the same quarter of the previous year.
9. **Cash Credit to the Private Sector Provided by Commercial Banks:** The balance of cash credit granted to the private sector provided by commercial banks for Q3 2023 recorded an increase of (22%) to reach IQD (39.3) trillion compared to IQD (32.3) trillion for the same quarter of the previous year.
10. **Foreign Currency Window Sales:** The quantities of US dollars sold through the Central Bank's foreign currency window (electronic platform) for Q3 2023 recorded a decrease of (41.5%) to reach USD $ (8.3) billion compared to USD $ (14.2) billion for the same quarter of the previous year. This is attributed to the decrease in the bank's sales of transfers and to the strengthening of the balance by (44.7%) due to audit procedures (restrictions imposed on the platform), while cash sales for Q3 2023 decreased

by (23.1%) to reach USD $ (1.6) billion compared to USD $ (2.1) billion compared to the same quarter of the previous year.

Second: The Iraqi Economic Monitor's Outlooks for Some Economic Indices for January 2024:

1. Real GDP Growth and Real Non-Oil GDP: The Economic Monitor Report indicates a future outlook for the real GDP growth rate in the medium term with a stable growth rate between (3-4%) during the years (2024-2029) in line with and identical to the growth rate in oil-exporting countries and emerging and developing countries, in addition to a future outlook for the real non-oil GDP growth rate in the medium term with a stable growth of (3.5%) until 2026 and then it decreases below the rate as in Figures No. (5) & (6).

Figure No. (5): Real GDP Growth Outlooks

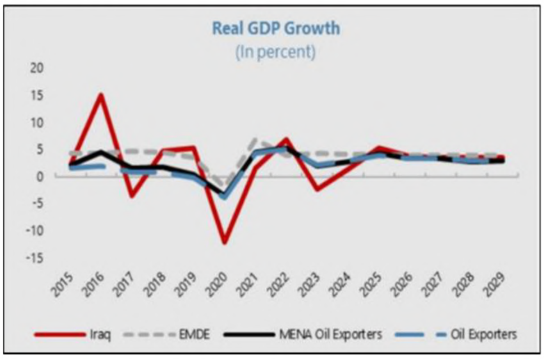
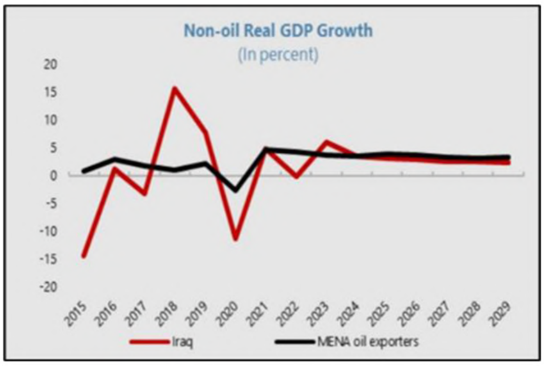
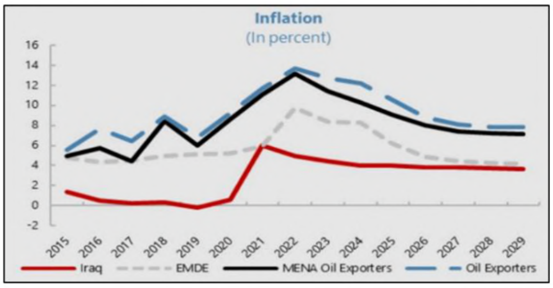


Figure No. (6) Real non-oil GDP Growth Outlooks



2. Inflation: Figure No. (7) shows a stable outlook for inflation rates in Iraq at around (3-4%) during the years (2024-2029) and a percentage lower than oil exporting countries and emerging and developing countries, due to the monetary policy measures, government support, and controlling fuel and food prices.

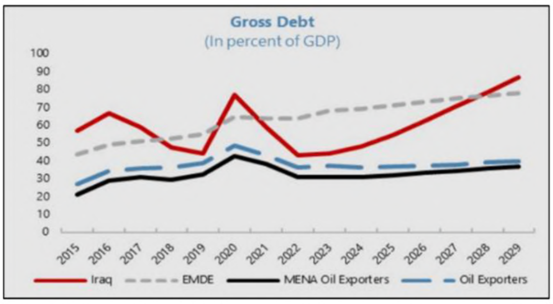
Figure No. (7): Inflation Rate Outlooks



3. Debt to GDP Ratio:

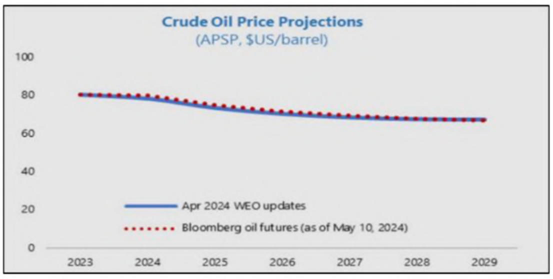
Figure No. (8) shows a general upward trend in the debt to GDP ratio during the years (2024-2029), due to the decline in oil sales because of OPEC+ decisions to reduce production or the decline in oil prices during the aforementioned years between (70-60) dollars per barrel, in addition to the approval of the three-year budget for the years (2023-2024-2025) and the increase in the budget deficit, as well as the emerging countries, where the total debt is expected to rise, while North African countries and oil-exporting countries are expected to maintain the same level during the years (2023-2028).

Figure No. (8): Debt to GDP Ratio Outlooks



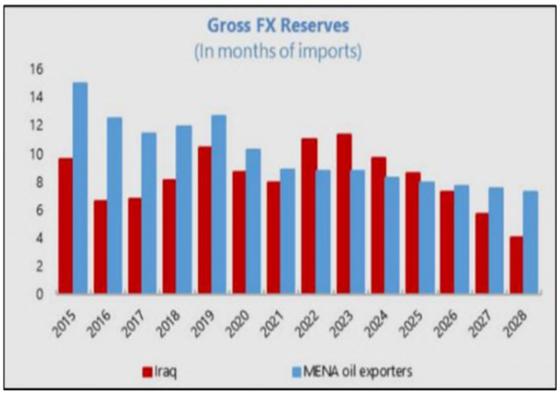
4. Global Oil Price Forecasts: Global oil price forecasts for the years (2024-2029) indicate a decline in their rates from (80-65) dollars, as shown in Figure No. (9).

Figure No. (9): Oil Price Outlooks



5. Gross Foreign Exchange Reserves: Iraq's Gross foreign exchange reserves are expected to decline for the years (2025-2027) because of the continued expected decline in oil sales, while the oil exporting countries from the Middle East and North Africa are expected to continue at the same rates for the years (2025-2027) as shown in Figure No. (10).

Figure No. (10): Total Reserves Prospects



Conclusion

The report indicates a positive outlook regarding the rise in non-oil GDP, and a decline in inflation rates, as well as an increase in the total foreign exchange reserves and growth in the private sector monetary credit. However, there is a pessimistic outlook for oil prices with an increase in public debt despite the increase in the growth driven by public spending, and the Ministry of Finance can mobilize non-oil revenues and activate collection and fines to be more effective.

Publication Guidelines

- Word Count: 1000–2000.
- Font Type: Simplified Arabic.
- Font Size: 14.
- The topics must not have been previously published.
- Submitted papers will be reviewed by the editorial board for selection.
- Articles should be sent as a Word document to the email address: stat.dept@cbi.iq

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