IRAQ DURABLE COMMUNITIES AND ECONOMIC OPPORTUNITIES

Political Economy Analysis, with programmatic recommendations

April 24, 2020
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<td>AQI</td>
<td>Al-Qaeda in Iraq</td>
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<tr>
<td>BOC</td>
<td>Basrah Oil Company</td>
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<tr>
<td>DCEO</td>
<td>Durable Communities and Economic Opportunities</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<tr>
<td>GIZ</td>
<td>German Cooperation for International Cooperation</td>
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<td>GOI</td>
<td>Government of Iraq</td>
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<td>ICT</td>
<td>Information Communication Technology</td>
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<td>IDP</td>
<td>Internally Displaced Person</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IIA</td>
<td>Iraq Innovation Alliance</td>
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<td>INBC</td>
<td>Iraqi National Business Council</td>
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<td>IOM</td>
<td>International Organization for Migration</td>
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<td>KRSO</td>
<td>Kurdistan Region Statistics Office</td>
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<td>INBC</td>
<td>Iraqi National Business Council</td>
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<tr>
<td>ISF</td>
<td>Iraqi Security Forces</td>
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<td>ISIS</td>
<td>Islamic State in Iraq and Syria</td>
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<td>IT</td>
<td>Information Technology</td>
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<td>KDP</td>
<td>Kurdistan Democratic Party</td>
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<td>Kurdistan Regional Government</td>
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<td>KRI</td>
<td>Kurdistan Region of Iraq</td>
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<tr>
<td>LSE</td>
<td>London School of Economics and Political Science</td>
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<td>MENA</td>
<td>Middle East and North Africa</td>
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<td>NCCI</td>
<td>NGO Coordination Committee for Iraq</td>
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<td>NDI</td>
<td>National Democratic Institute</td>
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<td>NGO</td>
<td>Non-Governmental Organization</td>
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<td>NDP</td>
<td>National Development Plan</td>
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<td>NTU</td>
<td>Northern Technical University</td>
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<td>PEA</td>
<td>Political Economy Analysis</td>
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<tr>
<td>PMF</td>
<td>Popular Mobilization Forces (Hashd ash-Sha’abi)</td>
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<tr>
<td>PUK</td>
<td>Patriotic Union of Kurdistan</td>
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<tr>
<td>SME</td>
<td>Small- and Medium-sized Enterprise</td>
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<tr>
<td>SOE</td>
<td>State-Owned Enterprise</td>
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<tr>
<td>SOFI</td>
<td>State-Owned Financial Institution</td>
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<tr>
<td>TA</td>
<td>Technical Assistance</td>
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<td>TVET</td>
<td>Technical and Vocational Education and Training</td>
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<tr>
<td>UN</td>
<td>United Nations</td>
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<td>UNESCO</td>
<td>United Nations Educational, Scientific, and Cultural Organization</td>
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<td>UNFPA</td>
<td>United Nations Population Fund (formerly UN Fund for Population Activities)</td>
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<td>UNHCR</td>
<td>United Nations High Commissioner for Refugees (also The UN Refugee Agency)</td>
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<td>USAID</td>
<td>United States Agency for International Development</td>
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I. EXECUTIVE SUMMARY

This Political Economy Analysis (PEA) provides a baseline set of findings, analytical conclusions, and programmatic recommendations to support USAID and its implementing partner Chemonics International in preparing to implement the Durable Communities and Economic Opportunities (DCEO) project.

The PEA was conducted from mid-January to mid-April 2020, and is based on information collected and analyzed from primary field-level data collection across seven priority governorates in Iraq, Key Informant Interviews (KII)s with a wide range of Iraq-based stakeholders, and more than a hundred secondary sources.

1.1 FINDINGS

Iraq’s oil-dependent rentier state is the central driver of distortions and failings in its national political economy. The huge volume of oil-derived money available within Iraq’s state – at both federal and provincial levels – has created powerful incentives amongst Iraq’s fractious post-2003 political actors to compete for control of political institutions and state-owned enterprises (SOEs), and therefore power to fund sprawling patronage networks and extract financial rents. This competition is typically short-termist – preventing longer-term state planning and investment to meet Iraq’s current and future needs outside of the oil sector – and is often violent and destabilizing. It has led to the rapid and continuing expansion of the public sector, which now approaches 40 percent of all employment and 90 percent of all formal employment. Recent efforts to decentralize some aspects of governance, in part to reduce this competition, have likely instead increased it.

This political competition has been exacerbated by a post-2003 constitutional order that has encouraged ethno-sectarian identity politics – both in popular mobilization and in elite rent-seeking and patronage-extension. Since 2010 and especially since 2018, there has been a growing popular demand from Iraqi citizens for a politics that transcends identity. While this has weakened explicitly ethno-sectarian language from Iraq’s political elites, it has not stopped their rent-seeking and patronage-extension. Rather, Iraq’s post-2003 elites continue to fail to move towards a political culture of effective, inclusive, issues-based governance, and have increasingly turned to violent coercion to suppress popular frustrations at this failure.

Iraq’s post-2003 political competition and its bloated public sector have both heavily suppressed the size and vitality of its private sector. The private sector was already struggling from a pre-2003 legacy of a statist economy and the damage done to it by sanctions and regime-survival imperatives during the 1990s, leaving it ill-equipped to compete in the post-2003 economy, when both domestic markets and international trade were liberalized, and a new era of political competition was set in motion. Since 2003, the private sector has continued to be hindered by a number of factors that stem from Iraq’s distorted politics:

i. Limited access to finance from a dysfunctional, state-dominated finance sector.
ii. Pervasive corruption in government procurement and administration which affects huge parts of the private economy, given the state remains a large player as both supplier and consumer in many markets.
iii. A complicated, expensive, and unfair regulatory system.
iv. Unfair competition from SOEs (which are at best inefficient and at worst credit-hungry employment schemes) and, increasingly, ‘crony companies’ that are fronts for political parties.
v. A widespread labor preference for typically lower-effort but higher-paid and more secure public sector employment.
Political instability, including recurrent mass protests against corruption and governance failures.

Weak or unreliable provision of key utilities, particularly electricity and water, transport and other physical infrastructure, and access to commercial land.

The continued stifling of the private sector from an over-dominant state, and the almost total reliance on oil revenues as a source of government revenue, has meant that the Iraqi state – and therefore Iraqi society more broadly – continues to be highly vulnerable to swings in international oil prices. While this vulnerability has been recognized in a number of government plans that aim to diversify sources of wealth and income away from oil, Iraq’s political elites and institutions have not succeeded in putting those plans into practice. And when oil prices decline and the government’s fiscal position worsens, as occurred in March 2020, this typically leads to the deferment or cancellation of investment that is precisely intended to reduce Iraq’s dependence on oil.

Recurrent bouts of violent conflict (especially 2004-7 and the 2013-17) have reflected Iraq’s post-2003 politics in having a heavy ethno-sectarian overlay. Early conflict in the post-2003 era saw the formation of armed groups often defined along ethno-sectarian lines, including: a) dozens of Shi’a, Sunni, and Kurdish militias, each with connections to political patrons, and b) Sunni insurgents, especially al Qaeda in Iraq (AQI), with virulent sectarian ideologies. Many of these militias have been subsequently integrated into state institutions while retaining a degree of autonomy over their command and organizational identity; they have therefore often acted in competition with the state even while being part of it. This includes Sunni tribal militias in Anbar in 2006 under the Anbar Awakening, and Shi’a militias from as early as 2004 through to the integration of Hashd ash-Sha’abi (or Popular Mobilization Forces/PMF) units in 2018. This dynamic has caused further factionalization of the state at federal and provincial levels, and further weakened Iraq’s ability to provide effective and inclusive governance to its citizens.

These bouts of violent conflict also further disrupted Iraq’s private sector, through mass death and displacement; extensive damage to infrastructure, housing, utilities, and commercial buildings; and widespread declines in education levels and vocational skills. The resulting slumps in production, consumer demand, and levels of business capital formation pushed many workers into the more precarious informal economy and likely led to the collapse of large numbers of private enterprises. The integration of militias into the state, and in particular the efforts of some militias since 2016 to engage in sectors such as construction, cross-border trade, and other small business through formal economic offices, has added further distortions and constraints on legitimate private sector activity.

The Iraqi state cannot meet its growing social and economic pressures by buying off popular frustration with public sector employment, as it has sought to do in the past. The scale of the country’s current youth bulge means Iraq needs to create hundreds of thousands of jobs every year, only a fraction of which the public sector can realistically absorb even in the best-case scenario of the government’s fiscal health. And even if Iraq’s political elites were inclined to create the required jobs by investing in priority infrastructure and enacting reforms to enable the private sector to grow as it needs to – and there is little evidence of this – they have been highly politically and financially constrained by the urgency and cost of the campaign to defeat ISIS and rebuild affected parts of the country in its wake.

The most recent protest movement, starting in October 2019, has been the most acute recent manifestation of popular unhappiness with the political class’s inability to meet Iraqis’ social and economic needs and desires, especially among Iraq’s rapidly expanding youth demographic.
The protests are reflective of the wider collapse in public trust and faith in a political elite seen as corrupt and ineffective in the past five years, which is also visible in the slump in voter turnout and in increasingly negative sentiment in public polling. The protesters have been pushing for Iraq’s political elites to move to an issues-based politics, but Iraq’s fragmented, factionalized state and distorted political culture is unable to meet this demand in the way it should: i.e. by catalyzing the structural transformation of the country’s political economy away from dependence on oil and the dominance of the public sector. Instead, it has fallen back on a familiar combination of:

i. seeking to buy off some with jobs in the public sector, at the expense of investing those public funds in critically important infrastructure;

ii. an intra-elite blame-game to position themselves in the ongoing political competition; and

iii. using state security forces and militias to violently repress the most active protesters.

The protesters themselves have been hampered by a lack of cohesion, and through their own maximalist political demands for the total replacement of Iraq’s political elite.

Even with the protest movement, 2019 featured some positive economic signs for the first time since the twin 2014 shocks of Daesh insurgency and declining oil prices – even though economic growth continued to be heavily skewed towards the oil sector. However, Iraq is likely to be tipped back into protracted economic difficulty by the twin March 2020 shocks of a COVID-19-induced nationwide lockdown and the steep oil price decline. While it is too early to understand how exactly the public health crisis will affect Iraq, it is likely to tip the country into a deep recession or depression, given the nationwide curfew is likely to last months rather than weeks. In addition, the steep decline in oil prices is likely to heavily damage the health of the government’s balance sheets – which had already tipped into deficit in 2019 because of the public sector expansion it undertook – just at a time when fiscal stimulus will be most needed. Even if oil production can be heavily cut back, the sharp global economic downturn from the COVID-19 pandemic is likely to continue to press oil prices below what Iraq needs to balance its budget for the remainder of 2020 and potentially into 2021.

The primary effect of these most recent twin shocks will likely be to further stall the reforms needed to improve Iraq’s politics and diversify government revenues and national economic activity. Even in a non-crisis moment, cutting back the public sector – especially now the recently-integrated militias – would constitute an existential threat to the state’s existence. In times of crisis, Iraq’s state has typically played the role of ‘stabilizer of last resort’, so it is even less likely it will now attempt to engage in infrastructure and service investment, and shrink the public sector, in the ways necessary to meet its longer-term social, economic, and political challenges. Instead, it is likely that the central government will run down its central bank reserves, seek to borrow on international markets, and increase its efforts to secure external financial assistance. The KRG may be more capable of getting its citizens to accept austerity; if so, this will likely reduce its fiscal vulnerability relative to the rest of Iraq.

While these twin shocks will likely tamp down the protests in the short term, making that particular political issue less a source of immediate instability, they will likely only push expressions of popular frustration and anger into the future, as they are unlikely to go away. Iraq continues to need to make major structural reforms, but continues to have a political economy that incentivizes destabilizing, short-termist elite political competition for control of the state. It is possible that the government’s weakening fiscal position – which may reduce elite incentives to rent-seek – and a widespread popular desire to move towards an issues-based politics, may combine to provide space
for the new government to generate momentum towards political and economic reforms. The chances of this, however, are low.

1.2 RECOMMENDATIONS

Even without the twin shocks of COVID-19 and the oil price decline, the best opportunities to expand the private sector without engaging in deeper structural reforms are in agriculture, construction, and the service economy. These sectors: a) have a history of significant private sector engagement, b) are by their nature labor-intensive, c) have large actual or latent domestic demand potential, and d) have capital- and knowledge-intensive parts of the value chain that can provide investment and innovation opportunities. Agriculture in particular is also pro-poor and highly female-inclusive. Furthermore, supporting entrepreneurship and innovation across Iraq is a high priority, given its ability to generate longer-term systemic improvements in the dynamism of the private sector.

With the current crises, agriculture takes on an even greater importance, as food security should be understood as a critical element of Iraq’s stability and national security, and exceptional permissions have been given to work in the sector even during the nationwide lockdown. As such, DCEO recommends prioritizing agricultural development in the near term above all other private sector development initiatives, in particular in the traditional agricultural regions of Wasit, Kirkuk, Ninewa, and the southern marshes. This may include support in areas such as: a) manufacturing of agricultural inputs; b) improvements to Iraq’s irrigation systems and practices; c) labor-intensive cultivation of agriculture and livestock; and d) more capital- and knowledge-intensive processing and distribution.

DCEO also recommends supporting construction and services as priority sectors. Support to construction may include: a) manufacturing of domestic construction materials; b) improving construction skills in the domestic labor force; c) improving labor conditions; and d) enabling innovation in new construction techniques. There is a particular opportunity to do so in Anbar and the south. Support to the service economy should focus on ICT, retail, food and beverages, and tourism, and may include: skills development; improving access to finance; and enabling innovation. Cross-cutting support to both of these sectors should include mobilizing greater domestic and foreign investment, and supporting greater management capacity.

In addition, DCEO recommends supporting private sector entrepreneurship and innovation in major population centers across Iraq. A larger entrepreneurial class can positively influence the wider private sector by demonstrating the benefits of private wealth-creation and shifting mindsets away from the public sector. DCEO should build on existing efforts already underway, and support may include: a) facilitating greater foreign and domestic investment in start-ups through a dedicated, bespoke investment fund; b) developing partnerships with U.S. universities to disseminate education on and access to innovation technology; and c) supporting a national television program where entrepreneurs compete for investment in their start-ups.

Finally, DCEO recommends using Iraq’s nascent alliance of innovation actors to lobby for wider business environment changes, such as in registration, taxation, and copyright protections, which other business associations such as the Iraqi National Business Council (INBC) could support.
2. INTRODUCTION

2.1 PROJECT BACKGROUND
In January 2020, USAID began the Iraq Durable Communities and Economic Opportunities (DCEO) project to support Iraqis in their efforts to re-establish stable and resilient communities. This five-year project has two main objectives, each of which has two sub-objectives, as follows:

1) Increase adaptive capacity of vulnerable communities
   1.1 Mitigate drivers of conflict in target communities
   1.2 Enhance community leadership of inclusive development
2) Advance the economic well-being of communities
   2.1 Improve private sector networks
   2.2 Increase micro, small, medium enterprise (MSME) development

DCEO began implementation with three assessments – political economy, conflict, and gender – in seven provinces across Iraq: Anbar, Baghdad, Basrah, Dhi Qar, Dohuk, Erbil, and Ninewa. These initial provinces were selected in recognition of Iraq’s diversity and to encompass important population centers. These assessments will inform project activities which will be designed in line with DCEO’s stated objectives and in response to the specific needs on the ground. DCEO will work with local businesses to identify potential areas for growth that will expand their operations, in turn creating new jobs and contributing to an improved local economy. DCEO will also work with communities and local leaderships to identify specific, local drivers of conflict and to propose and enact practical solutions. Similarly, the project will support local business associations and networks, in collaboration with the business community, to identify shared impediments to growth and trade and collectively advocate. These activities will be supported through capacity building and grants.

2.2 SCOPE
This document represents the DCEO political economy analysis (PEA). This PEA analyzes how the structure of Iraq’s political institutions and norms interact with economic incentives within and beyond the Iraqi state, and together influence how political elites interact with one another and the wider citizenry, and the form and level of national economic activity. It does so in order to arrive at a series of findings and analytical conclusions that generate timely and actionable program recommendations for the DCEO program, and provide an initial evidence base which further political economy analysis builds out as program implementation progresses. In doing so, the PEA seeks to identify the deeper structural characteristics of Iraq’s politics and economy, even while grappling with shorter-term economic and political patterns that are present today.

As the PEA is intended to be programmatically actionable, it does not provide a detailed historical background; it instead focuses Iraq’s political economy in the post-2003 period, referring to earlier historical events and trends where relevant. And the PEA’s operationally focused nature means we have closely aligned our analysis with DCEO’s technical objectives and implementation approach, as summarized below.
A focus on community-level programming. Our understanding of the DCEO program is that it will primarily focus delivery at the community level: community leaders and members for Objective 1, and private sector firms and supportive business associations for Objective 2. Therefore, while this PEA describes and analyzes the common characteristics of the national-level political economy below, it also analyzes the seven sample governorates (highlighted in the map below)\(^1\) to account for the highly different conditions present across Iraq’s regions, which are critical

\(^1\) Annex 2 has more detail about how these governorates were selected.
to account for in order to arrive at practical programmatic recommendations to assist Iraq’s diverse communities and their needs.

**A focus on programming that emphasizes tangible impact within prevailing structural constraints.** It was clear to DCEO, even before the completion of this detailed PEA, that deeply structural governance failures are at the root of Iraq’s political and economic dysfunction, and its vulnerability to outbreaks of violent conflict. It is also the DCEO team’s understanding from the project’s stated objectives that our mandate does not, at least as of yet, extend to directly tackling these structural failures through technical assistance to governance reform, but rather to generate positive outcomes through our programming within prevailing structural constraints, or to support our identified beneficiary groups to tackle these constraints. This means that, while we analyze these structural issues in some depth in this PEA, we have prioritized the identification of a) tangible job-creation and private sector development opportunities which are least constrained by these structural problems, and b) opportunities for structural reform that private sector and business association actors can engage in directly themselves.

**2.3 METHODOLOGY**

A detailed description of the methodology DCEO used for the PEA is found in Annex 2, but to summarize, we collected three sources of information for this PEA. These were:

- Secondary literature, including academic articles, policy papers, program documents, news articles, and development actor research papers on Iraq.
- Key Informant Interviews (KIIs) with more than 40 Iraqis and non-Iraqi analysts, officials, businessmen, and others.
- Field research in the seven selected governorates through DCEO consortium partner iMMAP, where 133 respondents from the private sector provided information and their perceptions on public and private sector employment conditions, attitudes towards relevant political economy issues, constraints on the private sector, and opportunities for growth. Note that due to the COVID-19 lockdown across Iraq, DCEO was unable to complete the field research in Erbil, so the PEA uses data from six of the seven governorates.

The findings from these information sources were analyzed using an analytical framework adapted from the USAID Applied PEA methodology (see Annex 2 for more details), and guided by the DCEO technical parameters described in Section 2.1. More detailed governorate-level analysis of the seven priority governorates has been provided in Annex 1, which has been used to inform the national-level analysis provided in the main body of the PEA.

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2 These governorates were agreed with USAID in February 2020.
3. IRAQ'S POLITICAL ECONOMY

Iraq’s post-2003 political economy has featured all the major, interlocking characteristics that comprise national ‘fragility’, which we define here as the following: 

1. Zero-sum thinking by social groups who have opposing (rather than shared) identities, and who tend towards seeing the state as a resource to be plundered, rather than as a locus for inclusive national decision-making and non-violent dispute resolution.
2. Many citizens viewing the state as illegitimate, and therefore frequently not complying with it.
3. A lack of state capacity to perform basic functions, including providing security and public services, generating taxation, and investing in infrastructure.
4. Sporadic outbreaks of violence that the state cannot or will not prevent/quickly suppress. This also lowers the cost of resorting to violence in political or economic bargaining in general, because weaponry, knowledge of how to enact violence, and the organizational and physical infrastructure of security actors are already a strong part of the landscape.
5. An under-developed private sector, and therefore low incomes overall, a narrowly-based economy, weak government revenues, and a lack of job opportunities.
6. Exposure to political and economic shocks which set the country back even when there has been some progress.

Nearly all of these characteristics were present prior to 2003, and are rooted in the longer history of Iraq’s 20th century state formation process – which from independence until 2003 was characterized by (increasing) domestic authoritarianism and regional military aggression, and a central role for oil in government revenues.

However, the first of these characteristics – political competition among elites divided on identity lines – only emerged in the post-2003 era. The authoritarian nature of Saddam Hussein’s rule meant there was little competition for control of the central state – although periodic uprisings, in particular from Kurdish and Shi’ite communities, did signify political dissatisfaction with Baghdad by groups partly defined by their ethno-sectarian identity. But since 2003, the vacuum left by the demise of Hussein’s highly centralized state has been filled by a shifting and expanding set of political factions and armed groups vying for control of the state. This competition has arguably been the most important political economy characteristic in Iraq in the past two decades – as it heavily influences all of the other characteristics of fragility.

3.1 IRAQ’S OIL-DEPENDENT RENTIER STATE

This political competition is however itself in large part a consequence of the enormous financial rewards of state control that stem from Iraq’s unparalleled dependence upon oil. With 58 percent of the country’s total GDP and 90 percent of government revenue coming from oil, and oil exports

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3 These are taken from the Commission on State Fragility, Growth and Development, Escaping the fragility trap, International Growth Centre (April 2018), pg. 16
4 Frank Gunter, “Iraq – Asking the Right Questions about Civil Disorder,” Foreign Policy Research Institute (2019), pg. 6
comprising fully 99.5 percent of total exports,⁵ Iraq has been rightly described as “the most oil-dependent state on earth.”⁶ Prior to 2003, oil revenues played a critical role in allowing Hussein’s regime to fund a large state through which he enriched himself and regime loyalists, and doled out patronage and co-opted interest groups through public sector employment, including through the armed forces. The Hussein regime also took a heavily statist approach to economic policy and production, and maintained “a policy of the state being ‘employer of first resort’” as an extension of its authoritarian rule; this is visible in more than a hundred state-owned enterprises (SOEs) and financial institutions that remain a central part of the economy today.⁷

However, the rebuilding of the Iraqi state and the liberalization of its economy after 2003 enabled intense and often violent competition between became Iraq’s new political elites for control over the state’s many political, economic and security institutions. These elites mostly defined their identities and constituencies along ethno-sectarian lines – in particular Sunni, Kurd, and Shi’a as the main such identity groups (even while there are dozens other smaller ethnic and sectarian groups in the nation). The political incentives for Iraqi elites and their patronage networks to compete in this way have been reinforced by the muhasasa ethno-sectarian quota system, a post-2003 constitutionally enshrined division of power at the top of the state across Sunni, Shi’a, and Kurd,⁸ which resulted in large part from a Shi’ite-Kurdish elite compromise that substantially excluded the minority but formerly dominant Sunnis.⁹ And this political incentive has been complemented by the powerful economic incentive that government oil revenues have provided – which in 2003 comprised nearly 50 percent of national GDP as Figure 1 shows.

These incentives have driven Iraq’s leading political actors and their parties, initially organized around monolithic ethno-sectarian blocs, to engage in populist identity politics undergirded by zero-sum thinking; that is, focusing their rhetoric on ensuring their identity group is appropriately represented, and often demanding much more for their group than would allow for a stable cross-group political settlement to take hold. And they have done so even while their primary focus is often more

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⁵ World Bank, Iraq Systematic Country Diagnostic, World Bank Group (February 3 2017), pg. 13  
⁷ Gunter, “Iraq - Asking the right questions,” pg. 8  
⁸ Eaton et al, “Conflict Economies,” pg. 24  
⁹ Mansour, Renad, “Iraq After the Fall of ISIS: The Struggle for the State,” Chatham House (July 2017), pg. 5
narrowly on using the state to secure rents and extend patronage to loyalists, rather than standing on issues-based platforms that don’t discriminate by identity.\textsuperscript{10} This competition in the formal political arena has also often been augmented by the use of affiliated armed groups to mobilize their identity groups and exert coercive influence (including violence) over other groups and the state itself.\textsuperscript{11} These armed groups include: Sunni tribal militias in western Iraq; mostly Shi’a units that now fall under the PMF umbrella, such as the Ba’thi brigades, Asa’ib Ahl al-Haq (AAH), Sadrist ‘Peace Companies’, and Kata’ib Hezbollah; and Kurdish peshmerga.

In the formal political arena, this combination of maximalist identity politics and rent-seeking has led to sustained political instability, and damaged perceptions of the state’s legitimacy. Winning in a particular election has led parties to reward loyalty through employment in ministries and SOEs, government contracts to companies run by their allies, and kickbacks from those contracts – fostering widespread political and bureaucratic corruption.\textsuperscript{12} Iraq today ranks as one of the most corrupt countries on the planet, falling 162 out of the 180 countries that Transparency International assessed in 2019,\textsuperscript{13} and many of its citizens are acutely aware of this fact. Similarly, electoral and political losers have had a strong incentive to agitate against the government – and often by extension the state which opposing political elites have captured – by describing it as illegitimate or repressive, and to promote disruptive protests or armed activity to demonstrate strength and extract concessions.

This has at times damaged popular perceptions of the state and, by weakening it, left Iraq more vulnerable to instability and violence. This became particularly acute after the U.S. scaled back its military presence and diplomatic attention in 2011, where diminished international oversight allowed then Prime Minister Nouri al-Maliki to expand his power base at the expense of rival Sunni and Shi’ite political factions.\textsuperscript{14} The resulting anti-Baghdad and anti-Iraqi Security Forces (ISF) political messaging by Sunni elites both in and out of power in Sunni-majority governorates such as Ninewa and Anbar between 2011 and 2014 played an important role in damaging Sunni views of the state, and thereby making local public opinion more conducive to the rise of ISIS.\textsuperscript{15}

Another example of how this politics generates disenfranchisement is the recent protest movement, which is the most acute manifestation of the wider collapse in popular trust and faith in Iraq’s

\textsuperscript{12} As Ali Al-Mawlawi notes, “it is worth noting the lack of sufficient empirical evidence to substantiate the dynamics between political parties and the exercise of patronage through public sector employment,” in part because much of this occurs “behind closed doors” and because of a “pervasive culture of impunity.” But its existence is a widely known fact in Iraq. Al-Mawlawi, Ali, “Public payroll expansion in Iraq: causes and consequences,” LSE Middle East Centre Report (October 2019)
\textsuperscript{14} KII with Sulaymaniyah-based political analyst, Mar 31\textsuperscript{16} 2020
\textsuperscript{15} Saleem, Zmkan Ali and J. Mac Skelton, “Mosul and Basra after the protests: the roots of government failure and popular discontent,” Institute for Regional and International Studies, American University of Iraq Sulaimani (October 2019), pg. 14
politicalelites—visiblene voter participation and polling in the past five years.\textsuperscript{16}Even asthe protesters have called for a replacement of the whole of the country’s political class, the protests have been supported by many, mostly Shi’a, political elites who see it as a useful means to advance their own positions within elite politics, after the previously more united Shi’a political bloc progressively fragmented into competing factions after 2010. This fragmentation further weakened the central state, as then-Prime Minister al-Maliki concluded Shi’a demographic majorities were not sufficient to guarantee their—and his—political dominance, and moved towards diversifying Shi’a political power into being partly based on an Iran-style ‘shadow’ state security apparatus of favored Shi’a militias.\textsuperscript{17}These Shi’a militias have in turn played a critical role in violently suppressing the protests.

Another important consequence of the use of Iraq’s oil-rich state to extend patronage and extract rents is a vast public sector, which currently accounts for approximately 40 percent of all employment in Iraq, and more than 90 percent of all formal employment. The public sector includes Iraq’s 176 SOEs, which in 2017 employed 550,000 people and enjoy huge privileges within their economic sectors.\textsuperscript{18}However, only a quarter of SOEs are profitable; many of these have little rationale to exist other than to provide employment.\textsuperscript{19}The Prime Minister’s own finance adviser has acknowledged that manufacturing sector SOEs have “have accumulated more than $10 billion in debt but contribute less than one percent of GDP.”\textsuperscript{20}

The public sector has grown enormously since 2003; the cost of financing Iraq’s public sector rose from five percent to nearly 51 percent of total government expenditure between 2004 and 2019—or approximately $57 billion of a total government budget of $111.8 billion.\textsuperscript{21}Since 2016, the primary driver of this growth has been PMF integration into the Iraqi Security Forces (ISF), and further expansion of SOEs and ministries to accommodate large numbers of recent graduates from technical universities.\textsuperscript{22}Two factors that appear to amplify the pace and scale of this expansion are 1) that no one political actor has managed to turn the state into an uncontested fiefdom,\textsuperscript{23}with the state instead reflecting consecutive governing parties who expand their own numbers without fully clearing house of their predecessors, and 2) the tendency of those in power to attempt to buy off current or potential unrest by parts of the population, whether youth, non-state armed groups, or others.


\textsuperscript{17}Mansour, “Iraq After ISIS,” pgs. 7-8

\textsuperscript{18}As of 2015, it is not actually clear how many currently exist. See Al-Mawlawi, “Public payroll expansion in Iraq,” pg. 10

\textsuperscript{19}World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 70

\textsuperscript{20}Al-Mawlawi, “Public payroll expansion in Iraq,” pg. 10

\textsuperscript{21}World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 52; World Bank, “Turning the corner in Iraq: Sustaining Growth and Creating Opportunities for Youth,” \textit{Iraq Economic Monitor} (Fall 2019) pg. 6; Cambanis et al, “Hybrid Actors,” pg. 28

\textsuperscript{22}World Bank, “Turning the corner in Iraq,” pg. 6; Cambanis et al, “Hybrid Actors,” pg. 28

\textsuperscript{23}Al-Mawlawi, “Public payroll expansion in Iraq,” pg. 14
This easy access to oil-derived revenue has also weakened the need to collect taxes from citizens and businesses; this has created a narrow tax base and weakened the accountability link between the state and its citizens.\textsuperscript{24} The dynamic of this weak social contract has been characterized as “no taxation and therefore no representation,” and conversely many Iraqis are resistant to any government move to increase taxation given the poor state of political representation in the country.\textsuperscript{25} The weak social contract and the tendency for the state to buy off citizens through public sector employment has also hurt the development of service provision across Iraq — whose quality and geographical coverage is well below the MENA average, and far below other upper-middle income countries, as Figure 2 indicates. Core services such as electricity and water are provided cost-free – another way the state buys off its citizens – which makes it difficult to raise their cost as one way to finance their improvements.

Iraq’s narrow revenue base has also weakened the ability of successive governments to invest in major public works that pays longer-term dividends, even if they had the vision to prioritize this over short-termist investment in expanding the oil sector.\textsuperscript{26} Iraqi researcher Ahmed Tabaqchali captured this succinctly when he described this approach as “depleting the country’s wealth without building its infrastructure”\textsuperscript{27} – at least, outside of the oil sector – and prevents the state from building the wider capital base upon which greater long-term economic stability should be built.

\textsuperscript{24} World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 15
\textsuperscript{25} Constantini, Irene, “A Neoliberal Rentier System: New Challenges and Past Economic Trajectories in Iraq,” in \textit{The International Spectator} (January 2017), pg. 8
\textsuperscript{26} World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 15
3.2 IRAQ’S WEAK PRIVATE SECTOR

A further critical consequence of Iraqi elites’ focus on controlling an ever-expanding state is the ongoing suppression of the private sector; rather than act as an independent engine of increased prosperity and resilience, the formal dominance of the state in many sectors – and its substantial market power as a supplier and customer even in private sector-involved sectors such as agriculture, retail, construction, and transport – has stunted the private sector and made it a terrain in which political elites and their networks extend their influence and enrich themselves.

State dominance in the economy has been true over the long-term in Iraq, given its historically statist economy. It especially worsened during the stringent economic sanctions regime of the 1990s, when the sanctions themselves heavily damaged Iraq’s private enterprises, forcing many to migrate overseas (especially to Jordan) and getting SOEs to fill the gap. And the state’s focus on regime survival during sanctions de-prioritized society’s wider economic wellbeing, for example neglecting investment in vital sectors such as agriculture, and enabled politically-connected individuals to establish protected business interests, particularly in illicit cross-border trade, as a means by which to evade the sanctions.28

But it has further worsened post-2003, as political competition intensified and with it came the large expansion of Iraqi’s oil production and public sector. This expansion took place at the same time as Iraq’s economy underwent liberalization reforms, which allowed cheap imports into Iraq, from Iran and Turkey in particular. This undercut local businesses which – being inefficient, antiquated, and participating in a market historically dominated by the state – were ill-prepared to compete on either price or quality, even as the country’s large and inefficient SOEs remained largely unreformed. These factors led to declines in activity across Iraq’s private economy after 2003, from rural agriculture to manufacturing and the urban economy. In 2012, as Figure 4 captures, the state remains a powerful player in many of Iraq’s sectors.

28 Eaton et al, Conflict Economies, pg. ix
At present, the private sector accounts for approximately 60 percent of all employment in Iraq, but only a very small part of this is in the formal economy; more than 90 percent of private sector workers have informal jobs with no social security benefits, reflecting the fact that nearly half of private sector workers are informally self-employed. 29 Reflective of this is the requirement for many Iraqis to maintain multiple jobs in order to earn sufficient household income, as DCEO respondents noted when polled.

The private sector also features a very low female participation rate; apart from agriculture, where women make up more than 50 percent of the labor force, 30 the public sector is the destination for the overwhelming majority of Iraqi women who participate in the labor market (especially those who are graduate educated), and those women that do work in the non-agricultural private sector are heavily concentrated in low-wage informal work. DCEO’s primary data collection bore out the female participation challenge for the private sector, with absolute majorities agreeing with the statement “It is harder for women than men to work in the private sector” across all governorates surveyed.

In the wider private sector ecosystem, there are very low levels of new firm creation, entrepreneurship, and business growth, even compared to similar MENA countries. The broad absence of medium-size businesses in Iraq’s private sector is one important manifestation of limited business creation and growth; the private economy is characterized by large numbers of informal micro-enterprises and small businesses, and a few large conglomerates typically run by powerful, connected families. As the World Bank has noted, “[i]n a context where firms do not grow over

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30 World Bank, “Turning the corner in Iraq,” pg. 20
their life cycle, the result is an ecosystem with a large number of small and medium old firms, leading to low firm turnover, and a lack of creative destruction. That is, small firms stay small, failing to contest the few large firms that are mainly SOEs, and do not create sufficient high-quality jobs. As a result, many economic sectors are characterized by a few large old firms and myriads of micro and small.”

The specific ways in which Iraq’s over-sized, oil-dependent public sector constrains and stunts Iraq’s private sector are numerous and complex. Iraqi private sector respondents have outlined, in a number of studies in the past decade, other common ways in which their ability to establish and grow viable businesses are hurt by the political economy, and DCEO’s own primary data collection has further developed this picture. The most important are described below, and Figures 7 and 8 summarize the views of respondents across a range of technical and political factors.

### Access to finance

Access to finance was seen as the biggest single constraint for private businesses in a 2018 World Bank study, especially smaller firms, and was the leading technical factor cited by our own respondents. This is a major issue, because starting a business is very expensive in Iraq, even beyond the normal imperative of raising funds to invest in capital, staff, etc. It is estimated that fewer than seven percent of SMEs have ever received bank loans and half of all businesses have reported having “great difficulty” obtaining financing of any kind (especially small and micro-enterprises), and instead primarily rely on small amounts of retained earnings. The principal reasons for this grim finance picture are:

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31 World Bank, “Bringing Business Back,” pg. 6
33 World Bank, “Bringing Business Back,” pg. 21
34 World Bank, Iraq: Investment Climate Assessment 2012, pg. xiv
• The privileging of credit provision to SOEs by the state-owned financial institutions (SOFIs) that dominate the financial sector. Because of the SOEs’ political connections, and because most of them are loss-making, SOFIs are often directed to fill holes in SOE balance sheets, leaving little attention and lending capacity for genuine private sector businesses.\textsuperscript{35}

• Onerous regulations and collateral requirements for bank lending. Banks impose strict and often impossible criteria for accessing loans; for example, firms are often required to provide cash or personal real estate collateral as the basis for a loan, and this has been an insurmountable hurdle for many firms.\textsuperscript{36} This constraint means that business owners frequently must raise funds through joint equity partnerships with SOFIs, or through reinvesting profits, which often come much later in the lifespan of a business, thereby constraining early-stage growth.

• A culture of ‘investor dominance’. Similar to banks, many investors expect they will get a controlling equity share in a business in exchange for their investment and immediate return on investment. This stands in contrast to the approach, common in more developed business environments, of receiving a minority stake that is understood to be ‘patient capital’ – i.e. that the entrepreneur must be given space to develop the business, and returns may be further down the line.\textsuperscript{37}

• The low registration rates for businesses in Iraq, especially among micro- and small enterprises. Given the regulatory burden firms face (described below), many prefer to remain unregistered, especially at the crucial early-life stage when they often most need debt or equity financing.

While credit provision to the private sector has been increasing since early 2017, by the end of 2019 the growth rate of this credit provision had fallen just one percent after a high of 10 percent during 2018, making this a very live constraint in Iraq at present.\textsuperscript{38}

**Service interruptions.** This was identified as the joint biggest issue for medium-size and large firms in 2018\textsuperscript{39} – electricity above all, but also water, IT and solid waste management – and a major issue for DCEO respondents in small- and medium-size enterprises. This likely reflects the more capital-intensive nature of medium/large-business operations when compared to small and micro-enterprises. Unstable electricity supply had also been reported as a critical constraint for business in 2012, indicating the persistence of this issue and the weak incentives the Iraqi state has had to invest in its utilities, in spite of its profound energy abundance.

In addition to electricity, frequent interruptions to “phone, Internet, water, and garbage collection services” were cited as common problems for businesses.\textsuperscript{40} Recent GOI deals with Siemens and General Electric worth $14bn to upgrade Iraq’s energy infrastructure represent important

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\textsuperscript{35} World Bank, \textit{Iraqi Systematic Country Diagnostic}, pg. 70
\textsuperscript{36} World Bank, “Bringing Business Back,” pg. 16
\textsuperscript{37} KII with Director of Start-Up Incubator, Mar 10\textsuperscript{th} 2020
\textsuperscript{38} World Bank, “Turning the corner in Iraq,” pg. 10
\textsuperscript{39} World Bank, “Bringing Business Back,” pg. 21
\textsuperscript{40} World Bank, “Bringing Business Back,” pg. 14
progress, but it is likely this constraint will remain important in the medium term given how poor provision is currently – especially given Iraq’s rapidly growing population.

**Shortage of skilled workers.** The vast majority of SME employees are unskilled short-term laborers, while those with higher levels of education often lack appropriate professional or vocational skills. Many of Iraq’s university graduates continue to prefer employment in the public sector, given its relatively high wages, job security, and perceived ease. Skills have also significantly declined in recent years, driven in part by declining standards in the educational system and by the human displacement and economic disruption caused by outbreaks of widespread violent conflict. This has led to the import of skilled foreign workers from Turkey, Iran and South Asia, even in the context of high national unemployment.

**Supply chain/logistical issues.** Firms report difficulties transporting goods within the country as a critical constraint – in part due to poor infrastructure, and in part due to internal political tensions that increase transport time and have led to the erection of additional tariffs between regions within Iraq. Iraq ranks 147th of 160 on the 2018 Logistic Performance Index – far below where an upper middle-income country should be – and neglect and violent conflict has further worsened this situation through the degradation of the country’s commercial capital stock. This is one reason for the perverse situation that it can often be more efficient to acquire imported goods than source them domestically.

**Physical damage and insecurity.** This was cited as roughly equal to service interruptions for medium and large firms in the 2018 study. We discuss this in more detail in our analysis of the

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41 World Bank, “Turning the corner in Iraq,” pg. 1
42 World Bank, Iraq Systematic Country Diagnostic, pg. 72
43 World Bank, Iraq Systematic Country Diagnostic, pg. 64
44 World Bank, Iraq Systematic Country Diagnostic, pgs. 78-82
45 Author KIIs with Iraqi analysts, UN officials and development organization staff members, February and March 2020
46 World Bank, “Bringing Business Back,” pg. 19
47 World Bank, “Bringing Business Back,” pg. 21
effects of violent conflict below. However, it is worth noting at this stage that among DCEO respondents, crime and violence were reported as one of the less pervasive business challenges at present, although this was not distributed evenly across the country, as Figure 9 indicates.

A stifling regulatory environment. Iraq is one of the worst countries on the planet to do business, falling 172nd out of 190 across a range of metrics, and regulations and procedures around business licensing, labor, customs, and trade were all cited as major challenges by DCEO respondents. The expensive, complicated, and arcane business registration process is notorious, and includes, for example, a requirement for an official from a relevant ministry to understand the business model and pronounce it viable before granting permission to register; this drives many start-ups to avoid registering for years after start-up. Even shutting businesses down is very expensive, while Iraq's weak and corrupt legal system stymies businesses' ability to protect copyright and property rights.

One consequence of such a regulatory system is widespread resort to political connections, by those who have them, to cut through the bureaucracy; DCEO respondents were in broad agreement across Iraq of the importance of political connections to running a successful business, as shown in Figure 10.

Competition from SOEs. SOEs have remained heavily protected and broadly unreformed, given their importance to Iraq's economy.
political elites as a source of rents, a means to extend patronage, and a necessary part of regime stability. As such, the state remains heavily involved in sectors outside of core public administration and service provision, as the chart on page 6 illustrates. These typically large, loss-making SOEs have continued to compete with, and crowd out, private business in the same sector, in part because they enjoy political favor, which they can translate into considerable market power.51

**Political and financial corruption.** Myriad forms of corruption remain a major issue in Iraq, from small bribes that must be paid to access government services and transport goods, to bigger, more political corruption in government procurement processes. The government is the main customer for many private sector firms, given its overall size and investment across Iraq’s economy, so it has the capacity to exercise considerable power over who wins and who loses in any economic sector – fixing procurement processes to the benefit of favored allies and excluding those without social capital or from the ‘wrong’ group.

Furthermore, an important recent development in this area has been the emergence of what the World Bank has called the ‘pseudo private sector’, and what we here call ‘crony companies’; that is, private firms started by political parties or politically connected militias. These firms then use their political relationships to obtain government contracts, rather than any expertise or competitive advantage, and often then sub-contact the delivery of the work to a legitimate firm that is actually qualified to implement the work.52 As Figure 11 indicates, DCEO respondents were in clear agreement everywhere except Dhi Qar that this practice has grown in the past two to three years across Iraq.

**Competition from informal firms.** The very high levels of informality is reported to have hurt those in the formal sector, as firms operating informally typically don’t pay the same fees or abide by...
the same regulations that formally registered firms must.\textsuperscript{53} Furthermore, their informality doesn’t necessarily stop them competing for and sometimes obtaining government contracts, given that government procurement is often a political rather than technical process.\textsuperscript{54}

### 3.3 IRAQ’S VULNERABILITY TO RECURRENT BOUTS OF VIOLENT CONFLICT

All of these economic constraints have been worsened by the sporadic outbreaks of widespread violent conflict that have afflicted Iraq in the past two decades. Prior to 2003, violent domestic repression of uprisings and inter-state conflicts similarly reinforced the centrality of the state to Iraq’s economic life. For example, Saddam’s 1991 draining of the southern marshes in reaction to a Shi’ite uprising heavily damaged the private agricultural sector in southern Iraq and therefore increased the importance of the state in food provision, and his efforts to bypass sanctions put much economic activity – such as cross-border trade – into the hands of politically-connected businessmen.\textsuperscript{55}

Since 2003, the two largest outbreaks of widespread political violence – insurgency and civil war from approximately 2003 to 2008, and the rise and fall of ISIS from 2014 to 2017 – are substantially the result of the intense political competition between identity groups described above. But these have in turn reinforced the role of Iraq’s state as the locus of political competition, and entrenched its bloated public sector as a pillar of social and economic stability.\textsuperscript{56} This violent conflict has also further enhanced the strength of armed groups in Iraq, and in particular allowed them to acquire more and more formal state authority – even as these armed groups have retained substantial autonomy to operate in their narrow factional/ethno-sectarian interests.\textsuperscript{57}

The period 2003-8 saw many political factions across the country use their armed wings as instruments of political competition. For example, Kurdish peshmerga were deployed to control territory outside Kurdish-majority areas across northern and western Iraq in order to support the expansion of Kurdish political authority outside Kurdish-majority areas.\textsuperscript{58} Similarly, Shi’a militias competed with one another for dominance in southern Iraq and east Baghdad; while the 2008 Operation Charge of the Knights helped weaken the dominant militias in Basrah, it did so in part by enabling other militias connected to the dominant Shi’a bloc in Baghdad at the time to gain power there.\textsuperscript{59}

In that period too, al Qaeda in Iraq (AQI) played on Sunni resentment towards a U.S.-influenced and Shi’a- and Kurdish-dominated central state to wage a potent insurgency in western and central Iraq, which only began to be quelled when the central government and the U.S. empowered Sunni tribal

\textsuperscript{53} World Bank, \textit{Iraq Investment Climate Assessment 2012}, pg. xiv
\textsuperscript{54} World Bank, “Bringing Business Back,” pgs. 20-21
\textsuperscript{55} Eaton et al, \textit{Conflict Economies}, pg. 48
\textsuperscript{56} World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 13
\textsuperscript{57} Cambanis et al, “Hybrid Actors,” pg. 25
\textsuperscript{58} NGO Coordination Committee for Iraq, \textit{Ninewa Governorate Profile}, NCCI Governorate Profile Series (2010), pg. 6
\textsuperscript{59} Saleem, Zmkan Ali and J. Mac Skelton, “The politics of unemployment in Basra: Spotlight on the Oil Sector,” Institute for Regional and International Studies, American University of Iraq Sulaimani (June 2019), pg. 3
militias to take a central role in security provision from 2008 onwards, in particular in Anbar.\(^{60}\) These tribal militias remained powerful stakeholders in security in Sunni-majority governorates for four years, but their organizational and political divisions were ruthlessly exploited by ISIS in 2013 and 2014 as it took control of these governorates.\(^{61}\)

More recently, political parties associated with the most powerful PMF factions emerged as major winners in the 2018 elections, in large part because of the understandable national esteem they gained from leading the fight to defeat ISIS, after large segments of the ISF had collapsed during ISIS’s rise.\(^{62}\) In these elections, in a break from established post-2003 pattern, no obviously largest single Shi’a political bloc was able to emerge victorious, and instead a less formal understanding between the Moqtada al-Sadr-led Saairun Coalition and Hadi al-Ameri’s Fateh Alliance developed – both figures being leaders of powerful militias. A compromise figure was installed as prime minister, Adil Abdul-Mahdi, who has not had a power base independent of these parties, and many PMF officials were installed in office around him.\(^{63}\)


\(^{61}\) Malkasian, “Anbar’s Illusions”

\(^{62}\) Cambanis et al, “Hybrid Actors,” pg. 30

\(^{63}\) Under the muhasasa ethno-sectarian quota system, the prime minister – most important of the three senior roles in government, alongside the president and speaker of the parliament – is typically a representative of the Shi’a political party/ies that have formed the largest political bloc. See Mansour, Renad, “Iraq’s 2018 government formation: unpacking the friction between reform and the status quo,” LSE Middle East Centre (2019) for more details.
Amongst the most important consequences of this election were a) the integration of these militias into the national army – even if they retain substantial autonomy from ISF command and control – and b) these parties and their allied militias were able to further capture important SOEs and other state revenue streams, especially the enormous PMF budget, consolidating their power within the state. As such, powerful militias have become both of the state – being paid by it, and having the authority and access to revenues being inside grants them – and in competition with it – for example, by continuing to generate money from illicit activity away from the capital. Key to this latter form of rent-seeking is illegally taxing trade into Syria and Jordan through Anbar, and into Iran via Diyala, as well as maintaining influence over berths at Basrah’s critical Um Qasr port facility. Figure 12 indicates the main smuggling routes, and where the most significant militia checkpoints are located.

64 KII with London-based Iraqi political analyst, Feb 18th 2020
65 Eaton et al, Conflict Economies, pg. 27
The (incomplete) integration of armed groups have not only expanded the state, but also further fragmented the state and further entrenched the rent-seeking and patronage-making behavior that has characterized Iraq’s central government since 2003. This is reflected in DCEO respondents’ views on the presence of militias along roads and transport routes, as Figure 13 shows, and how this impedes businesses’ operations; unsurprisingly, Anbar stands out, as do Baghdad and Basrah, where many militias are concentrated, and Ninewa, where many continued to be operationally deployed.

3.4 THE EFFECT OF VIOLENT CONFLICT ON IRAQ’S PRIVATE SECTOR

Beyond the consequences on the Iraqi state’s size, coherence and focus, and the terrible human cost, violent conflict has had multiple severe consequences on Iraq’s private sector too. For the most recent period of conflict – that of ISIS’s occupation and the military campaign to defeat them – one of the most important is the widespread physical damage to large swathes of the north, west and center of Iraq. Figure 14 shows the distribution of damage and needs across social, productive, infrastructure and government sectors in the seven governorates directly impacted by ISIS occupation and the military campaign against them.66

At a more granular governorate level, Figure 15 shows the percentage of total residential buildings destroyed in each of the same seven governorates, across both urban and rural locations, which gives a reasonable approximation of the level of overall conflict-caused damage in these governorates. Since 2018, reconstruction has been patchy. There has been reasonable progress in Anbar, largely due to good Anbari elite representation in Baghdad, and in parts of Mosul city.

66 These governorates are Ninewa, which had the highest level of damage overall, as well as Anbar, Kirkuk, Salahaddin, Diyala, Baghdad, and Babil.
because of heavy international investment. However, much of Mosul and wider Ninewa’s basic economic infrastructure remains heavily damaged, and Diyala and Kirkuk have seen little attention paid to their reconstruction needs, given that Ninewa has taken up so much attention.67

Furthermore, capital formation has also substantially declined as investment has shrunk. So did sales; 85 percent of firms polled by the World Bank’s 2018 Rapid Enterprise Survey reported a decline in sales when compared to 2014,68 and as this figure is only from those businesses that survived during this period, we can also assume many others went out of business. The drop in sales reflects weaker demand from a poorer population, companies’ lowering of prices to attempt to offset some of the decline in demand, and lower investment in plant and equipment given the more difficult political and economic conditions.69 In terms of sectors, the construction sector saw the greatest decline in sales, employment, and cancelled investment, following by services and manufacturing.70

Violent conflict has also had a tremendous human cost, which, beyond the intrinsic suffering this has caused to Iraqis, has also heavily damaged the size, skills levels, and composition of the labor force. First, it has heavily hurt both Iraqis’ income levels and their level of skills, which has continued the

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67 KIs with Sulaymaniyah-based political analyst and Anbar-based UN official, Mar and Apr 2020.
68 Quoted in World Bank, “Bringing Business Back,” pg. 11
69 World Bank, “Bringing Business Back,” pgs. 11-12
70 World Bank, “Bringing Business Back,” pg. 13
enormous collapse in education and human capital level begun in the early 1990s. Second, conflict has also pushed many more private sector workers into informal work, increasingly their economic precariousness and vulnerability to further economic or social shocks. Third, displacement from western and northern Iraq has led to a greater population concentration in cities, exacerbating an existing nationwide trend caused by environmental degradation that has resulted from historic mismanagement and overuse of agricultural lands and natural resources, in particular water. This means that demand for jobs has also shifted towards increasingly crowded urban areas where there is heavier pressure on services and greater competition for jobs – even while many of the more vulnerable and neglected populations remain in rural areas, including those who return from displacement once conditions – especially security conditions – have improved in their places of origin.

3.5 IRAQ’S LIMITED CAPACITY TO MEET CURRENT SOCIO-ECONOMIC CHALLENGES

All of this adds up to a picture of continued political, social, and economic fragility in Iraq, even if the country has been slowly recovering from the end of ISIS rule. Iraq’s economy had a reasonably good year in 2019, and returned to positive real GDP growth after two years of contraction, outperforming its regional peers. This includes non-oil GDP growth; while non-oil nominal GDP growth became positive again in 2018, as Figure 16 indicates, in real terms Iraq’s non-oil GDP growth remained negative until 2019.

As Figure 17 indicates, there were also some signs of positive outlook across multiple segments of the private sector concerning the future (although still a minority view), and plans to hire by a significant percentage of firms. This was reflected in the broadly positive sentiment found amongst DCEO respondents, shown in Figure 18, about their economic fortunes over the coming two years; only in Dhi Qar did the Iraqis surveyed believe that their situation was more likely to worsen than to improve.

However, while some growth during 2019 did come from productive sectors – principally agriculture (benefitting from good rainfall) and electricity – most of this growth stemmed from an

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71 World Bank, Iraq Systematic Country Diagnostic, pg. 78
73 World Bank, “Turning the corner in Iraq,” pg. 3
increase in crude oil production. It also stemmed from an expansionary fiscal policy, focused on increasing public consumption and public sector employment – in particular by bringing the PMF onto the public payroll, and the Ministry of Oil’s hiring of large numbers of new graduates. This has driven a decline in Iraq’s fiscal position from a 7.9 percent budget surplus in 2018 to 4.6 percent budget deficit in 2019.74

This short-termist approach – buying peace amid weak private sector job creation – is limiting the ability of the government to finance growth-enhancing public investments; in 2019, the only growth in public investment has been oil-focused, and non-oil investment has significantly declined.75 And this in turn is only reinforcing Iraq’s continued – indeed enhanced – dependence on oil revenues, and therefore its vulnerability to oil price drops and other economic and political shocks.

Unfortunately, a number of these have struck Iraq since Fall 2019, specifically: the protest movement

74 World Bank, “Turning the corner in Iraq,” pg. 6
75 World Bank, “Turning the corner in Iraq,” pgs. 6-7
that has spread across central and southern Iraq since October 2019; and the twin March 2020 shocks of a Coronavirus-driven nationwide lockdown and a steep decline in oil prices.

**Protests.** Politically speaking, ethno-sectarian and sub-national tensions have eased somewhat as a source of political instability since 2018. Relations between the central government and the KRG have improved after the fallout from the September 2017 independence referendum, even while disputes remain over territories in Kirkuk, Ninewa, and Diyala.76 And at the societal level, polling surveys have indicated much weaker public support for ethno-sectarian identity politics, and a rise in popular desire for Iraqi politics to provide jobs and services – i.e. the emergence of a more issues-based politics.77

However, Iraqi elites’ inability to effectively respond to this shift, and a not-inaccurate popular perception that elites continue to engage in divisive and corrupt political competition, has driven a rapid collapse in popular faith in Iraq’s post-2003 political system and governing class. While this has been building for the past five years, and is visible in steep declines in voter turnout at elections, this erupted in a protest movement focused on Baghdad and the southern governorates in late September 2019.

The protests were initially sparked by the demotion by Prime Minister Abul Mahdi of a popular military commander who had become a national hero for his role in leading the Counter-Terrorism Service (CTS) in the war against ISIS. Many Iraqis saw this as caused in part by the increasingly loathed Shi’a militias who now have a prominent place in government, especially those most strongly aligned with Iran and

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76 World Bank, “Turning the corner in Iraq,” pg. 1
77 See for example, NDI, “Parliamentary Elections”
therefore seen as having helped cede Iraqi sovereignty to its larger eastern neighbor. However, this quickly escalated into wider youth-led protest against the perceived corruption of Iraq’s political elites, who they blame for a lack of job opportunities and services, enabling the rise of ISIS, the widespread corruption of the Iraqi state in spite of its enormous resources, and selling the country’s sovereignty to Iran.

While many protesters were young, they comprise a mix of ethno-sectarian and class identities, and share a view, borne out of experience over the past fifteen years, that “voting in elections cannot deliver change,” which is also evident in collapsing levels of voting in consecutive rounds of elections. As such, many demonstrators see a protest movement as the only way in which they can break the cycle of political failure. As Figures 19a and 19b indicate, there was widespread agreement amongst our respondents with the statement “the protests are useful” across our surveyed governorates, especially among the young, even while strong majorities outside KRI agreed that there were economic costs to the protests (Figure 20).

Yet their demands for the wholesale removal of Iraq’s governing class makes it very hard to see how they can realize their objectives of political change, at least in the form they have taken since October 2019, given that the structures, norms, and incentives of Iraq’s post-2003 political system make it extremely difficult for political elites to change how politics is done – even if they had the vision to do so. Instead, the government’s crackdown, using in particular Iran-aligned PMF units, has at times been brutal, with more than 600 deaths (including alleged targeted assassinations), kidnappings, and torture, especially against leaders and those providing material assistance to the protesters.

It is notable that protests have not extended to Sunni-majority areas. This is primarily because of the experience of people in these parts of the countries of how past protests and civil instability enabled the rise of ISIS, as well as effective non-violent suppression by local security forces. Similarly, many

79 KII with KRI-based political analyst, Mar 19th 2020
80 ICG, ‘Widespread Protests’
81 ICG, ‘Widespread Protests’
82 KII with KRI-based political analyst, Mar 19th 2020
young Kurds have demanded political reform of the Kurdish political duopoly in the past half-decade, even though the rise of ISIS and the associated threats to the KRI, as well as heavy suppression by KRG security forces of nascent demonstrations, dampened this movement.\textsuperscript{84} However, it remains, as our field research confirms, the case that large segments of these populations are as frustrated and disillusioned with Iraq’s political class as active protesters elsewhere in the country; this is true even in Ninewa and Anbar, the two governorates most damaged by the extremist violence that was enabled by previous protest movements across much of Iraq’s Sunni-majority areas in 2011-2.

An underlying structural driver of the protests is the extremely challenging population dynamics that Iraq faces. Already, at least 2.5 million Iraqis are currently unemployed (or approximately eight percent of the workforce) and this heavily skews young; youth unemployment rates are nearly double that of wider adult unemployment.\textsuperscript{85} Iraq has a very young and rapidly expanding population; between 2015 and 2030, there will be an extra 12 million adults and a 100-180 percent increase in job demand. As the World Bank has noted, “[e]ven if the bloated public sector remains the same, there will still be a large jobs shortfall” by 2030 – estimated at nearly 5 million.\textsuperscript{86}

This means Iraq must achieve and sustain much higher economic growth rates – and more specifically, growth in jobs – than either its neighbors or that it is currently able to generate, even under the most optimistic scenarios of oil production and price growth.\textsuperscript{87} Given GDP per capita has hardly grown since 2013, and Iraq’s political economy remains oil-dependent, deeply factionalized, and short-termist in its economic planning, its chances of spurring higher growth rates without major structural changes to enable the private sector are slim.

\textbf{Coronavirus and oil price decline.} It remains early in the process of Iraq’s response to the novel coronavirus COVID-19, so it is difficult to draw robust conclusions about the effect of this shock on Iraq’s political stability and economic wellbeing. However, it is highly likely that necessary shuttering of businesses and restrictions imposed on movement will reduce incomes and employment for large sections of the population, and be particularly damaging to private enterprise outside of the food retail sector. This is likely therefore to drive up unemployment and push many Iraqi citizens below

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{iraqi_youth_population.png}
\caption{Iraqi youth population (millions)}
\end{figure}

\footnotesize
\begin{itemize}
\item \textsuperscript{84} Salih, Cale, and Maria Fantappie, \textit{Kurdish Nationalism at an Impasse}, The Century Foundation (February 2019), pg. 5
\item \textsuperscript{85} World Bank, “Jobs in Iraq,” pg. 6
\item \textsuperscript{86} World Bank, “Jobs in Iraq,” pg. 2
\item \textsuperscript{87} World Bank, “Bringing Business Back,” pg. 3
\end{itemize}
the poverty line or further into poverty. Moreover, it will likely tip Iraq back into recession by mid-2020, and may result a deeper economic depression from the second half of the year.

Furthermore, this much-deteriorated macroeconomic climate may be compounded by a government fiscal crisis resulting from the sharp decline in oil prices in March 2020; these fell to roughly half of what Iraq’s draft 2020 budget requires them to be in order to balance its books. At the time of writing, it was not assessed to be likely that oil prices will recover within 3-6 months, in part because the COVID-19-induced global recession the International Monetary Fund and others are now forecasting will also continue to restrain global demand well into 2021. The global downturn is expected to put sustained downward pressure on oil prices, even if key oil exporters agree to scale back production beyond the unprecedented cuts agreed upon in mid-April. As such, this much more challenging fiscal picture for the Iraqi government is anticipated to last well into 2021.

Having already entered a fiscal deficit in 2019, this further deterioration in its fiscal position will make it even harder for the government to blunt the effects of the pandemic-induced nationwide shutdown. These twin shocks pose a major risk to Iraq’s current and future economic wellbeing, and therefore to its political stability, because of how high up income and employment are on Iraqis’ priority list. Initial measures to shore up government balance sheets in the face of the oil price decline were announced in late March, including halting investment spending, delaying local and international debt repayments, and collecting debts owed by telecommunications companies. However, these will amount to small changes, leaving the major components of government expenditure – especially its large public sector – unaddressed.

It is already clear from the halting of planned investment spending that a major effect of this growing crisis will likely be to further stall the reforms needed to improve Iraq’s politics and diversify government revenues and national economic activity. Even in a non-crisis moment, cutting back the public sector – now including well-armed, politically powerful militias – would constitute an existential threat to the state’s existence. In times of crisis, Iraq’s state has typically played the role of ‘stabilizer of last resort’, so the likelihood the government will now attempt to engage in the infrastructure and service investment, and public sector reform, necessary to meet longer-term challenges has reduced even further. Instead, it is likely the central government will run down its central bank reserves, borrow heavily while deferring some of its liabilities, and increase its efforts to secure external assistance.

While these twin shocks have tamped down the protests in the short term, making that particular political issue less a source of immediate instability, they will likely only push expressions of popular frustration and anger into the future. Iraq continues to need to make major structural reforms, but continues to have a political economy that incentivizes destabilizing and corrupt elite competition for

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89 See for example the IMF April 2020 World Economic Outlook: https://www.imf.org/en/Publications/WEO/Issues/2020/04/14/weo-april-2020
91 Saadoun, “Is another economic crisis looming in Iraq”
government institutions and revenues, the growing fragmentation of the state, and short-termism in government economic planning. And Iraq’s continued vulnerability to shocks further complicates its ability to enact these reforms. It is possible that the government’s weakening fiscal position – which may reduce incentives to rent-seek by elites and their political factions – and a widespread popular desire to move towards an issues-based politics, combine to provide space for the new government to generate momentum towards political and economic reforms; perhaps in particular in sectors considered critical to national security in the midst of extremely challenging national and global economic conditions. But it is more likely instead that the current shocks only reinforce the structural distortions of Iraq’s political economy. One respondent captured the sentiment felt by many respondents about Iraq’s fate in the wake of these two latest shocks: “Maybe we need a miracle to pass this period.”

The picture may be slightly different in the KRI, where KRG’s stronger governance capacity and greater ability to mobilize its citizens in a crisis has allowed it to be more honest in its communications about its limited capacity to deal with this unprecedented public health crisis, especially when compounded with the sharp drop in the price of oil. This makes it more likely that it can shed some of its similarly high levels of spending on public sector employment, and at least moderately reduce its fiscal vulnerability relative to the rest of Iraq.

4. CONCLUSIONS AND RECOMMENDATIONS

4.1 CONCLUSIONS

Even before the recent pandemic and oil price shocks, it was widely recognized that Iraq needs to reform its political institutions and diversify its economy away from its current overwhelming dependence on revenue from oil in order to reduce its fragility and increase national prosperity.

This recognition nominally extends to the Iraqi government itself, whose National Development Plan (NDP) 2018-22 identifies a number of clear, coherent, and realistic strategic objectives about enabling more effective, accountable, and transparent governance, rebalancing the economy, diversifying away from oil, increasing employment, and enabling the private sector. The World Bank has similarly noted the importance of enabling the private sector, and how central governance reforms are doing so; “[t]he first-best solution for large-scale private sector job creation hinges on structural reforms that must begin now, but are achievable only in the medium to longer term.”

However, there is little evidence that the government as a whole – if it is possible to speak of a coherent government – has the commitment or ability to realize the NDP’s objectives. Indeed, the NDP itself recognizes there have been major shortfalls in the achievement of the objectives laid out in previous national and private sector development plans (even if this is not explicitly stated), just as earlier NDPs had done about their own previous iterations. Similarly, as Iraqi analyst Renad

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92 KII with Babil-based Iraqi development organization staff member, Mar 31st, 2020
93 KII with Sulaymaniyah-based Iraqi political analyst, Mar 31st, 2020
95 World Bank, “Jobs in Iraq,” pg. 1
96 Costantini, “A Neoliberal Rentier state,” pg. 12
Mansour noted, Prime Minister Abdul Mahdi “promised an ambitious program of gradual reform to the system” but was unable to navigate the complex terrain of powerful political parties. This caused Abdul Mahdi’s reform program to fail even before the protests bit, just as his predecessors failed, and is testament to the powerful binding constraints Iraq’s distorted political economy places on all aspects of Iraq’s political and economic life.

However, there are significant opportunities for private sector growth without undertaking major structural reforms, even if these are likely to be much more limited in their ability to drive systemic economic change. These exist particularly in agriculture, construction, and parts of the service economy, especially ICT, tourism, and urban retail. Each of these sectors are:

- Labor-intensive, although have more capital- and knowledge-intensive elements.
- Accustomed to significant private sector involvement and therefore relatively less dependent on the state than other sectors.
- Inclusive across Iraq’s diverse demographics.
- Viable given national resource endowments and actual/potential domestic demand.

They also exist in wider efforts to encourage entrepreneurship and innovation across all sectors of Iraq’s private economy. We briefly analyze each of these in turn.

4.1.1 THE AGRICULTURAL SECTOR

Agriculture is a critical component of Iraq’s economy, and has historically had a high level of private sector engagement, even though the state was an active player in the sector during the 20th century: providing or subsidizing agricultural inputs, fixing prices, and being a major consumer of the country’s agricultural produce. This statist legacy left many farmers dependent on the state and ill-equipped to compete with Turkish and Iranian imports post-2003. Since then, the scale of the agricultural sector has declined, with environmental mismanagement and degradation also contributing – pushing many farmers to abandon their land and seek employment in the informal urban economy.

Other important constraints are access to clean, non-saline water; damaged irrigation systems; access to and cost of inputs; a weak capital stock; agricultural land being built on for industry or housing; limited compensation for losses due to fighting; and difficulty accessing credit.

As a result, only a small percentage of Iraq’s cultivable land is currently being utilized, and much of the sector is characterized by smallholders who often produce for domestic or local community consumption. Given that agriculture is relatively labor-intensive and also disproportionately benefits the rural poor, especially women, there is therefore an opportunity to support the expansion of agriculture throughout the value chain across multiple regions of Iraq. And doing so has taken on significantly greater importance with the arrival of COVID-19, given the sector’s role and its ability to help reduce Iraq’s dependence on other countries for its food, which may emerge as a major

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97 Mansour, “Iraq’s 2018 government formation.” pg. 21
99 See World Bank, “Turning the corner in Iraq,” and CIPE’s provincial business agendas for more details on these constraints.
challenge in the coming year; the government’s recognition of its essential role has led to the agricultural sector receiving exemptions to many of the lockdown provisions imposed more widely since February 2020. The protest movement also placed heavy emphasis on the agricultural sector in its messaging about its wishes for Iraq’s economic future, as they consider it a critical means by which Iraq can reduce Iran’s influence over the country.100

However, DCEO should not solely provide support at the labor-intensive end of the sector. There are opportunities to support more capital-intensive parts of the agriculture sector, including manufacturing of inputs, food storage facilities, food-processing and distribution, and the reconstruction of market facilities where they have been damaged due to conflict.101 This is relevant across the main agricultural areas of Iraq, and in particular in the southern marshes, Wasit, Kirkuk, and Ninewa.

4.1.2 THE CONSTRUCTION SECTOR

The construction sector is another labor-intensive sector with a history of significant private sector participation. Furthermore, there is a clear domestic demand for the products that the construction sector provides across Iraq, whether it is supporting reconstruction of civic infrastructure and residential and commercial building stock in Ninewa, Anbar, Salahaddin, and Diyala, or reducing the acute nationwide housing shortage.

There is also significant potential for further development and innovation in the domestic manufacturing of construction materials, such as concrete, bricks, and glass, including those that use Iraq’s own natural resources,102 and the introduction of new building techniques and technologies for higher-income customers, such as more heat-resistant architecture and more efficient residential heating and water systems.103

Furthermore, a significant percentage of Iraq’s higher-skilled construction workforce is comprised of Turkish and Iranian workers (particularly concentrated in the north and south, respectively), as there are huge unmet needs in the construction sector for Iraqi “bricklayers and stonemasons, building construction labourers, heavy truck and lorry drivers, carpenter and joiners, and concrete workers.”104 There is therefore an opportunity to increase the domestic skills base to reduce the need to import foreign workers, potentially through partnerships with existing regional private vocational education institutes. As many construction firms are small, individual or family enterprises,105 there is also clearly an opportunity to support investment in existing firms to enable them to grow into larger, more formal businesses managed along professional lines.

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100 KII with Iraqi development organization staff member, April 8th 2020
102 World Bank, _Damage and Needs Assessment_, pg. 60
103 KII with multiple Iraqi businessmen, April 2020
104 UNESCO, _Assessment of the Labour Market & Skills Analysis in Iraq and Kurdistan Region-Iraq_, UNESCO (2019), pg. 48
105 World Bank, “Turning the corner in Iraq,” pg. 10
4.1.3 THE SERVICE SECTOR

The service sector is the third part of Iraq’s economy in which there is historically significant private sector engagement and for which there is significant domestic demand potential. The sub-sectors with greatest potential include ICT, retail, food and beverages, and tourism. ICT can benefit from Iraq’s relatively technologically-literate graduates, and is an innovation-friendly sector with widespread commercial and consumer markets. Retail and food and beverages both have the potential to support distribution and consumption of produce from the agricultural sector described above, especially if connected to the sale of more processed domestic produce, which can benefit from both higher value-addition and appeal to national pride.

And there is significant potential to expand tourism to Iraq’s myriad historical sites, including by approaching it in ways that enable local community employment, especially in rural communities such as around archeological sites in central and southern Iraq, or amongst religious minority communities in northern Iraq. Across all of these sectors, there is significant potential to provide indirect support through: a) business and vocational skills development; b) improved access to finance and investment; c) easier business registration, taxation, and copyright constraints; and d) more innovation and new business incubation.

4.1.4 CROSS-CUTTING ENTREPRENEURSHIP AND INNOVATION

Beyond specific sectors, there is a major opportunity to support wider systemic change in the private sector through supporting the further expansion of existing efforts to promote entrepreneurship, innovation, and business incubation and acceleration.

Iraq has not had an entrepreneurial class in the way that it exists in countries with less economically-dominant states; much of what we could consider ‘entrepreneurship’ prior to 2003 was the result of new business practices by politically-connected businessmen who supported regime efforts to bypass sanctions, which is one reason why there are residual popular suspicions about new forms of business across Iraq. But a proper entrepreneurial class – and the imagination, risk-taking, and creative destruction that comes with it – can have a critical conditioning effect on the wider private sector, through demonstrating the power of wealth-creation and shifting attitudes away from a focus on the public sector and oil as the primary means by which to generate wealth.

There has been considerable progress in promoting entrepreneurship and innovation in Iraq in the past five years, in particular through the work of 51 Labs in Sulaymaniyah, The Station in Baghdad, Recoded in Erbil, and to a lesser extent Basrah’s Science Camp and the Mosul Makerspace. This has included: supporting start-ups with investment, management training, guidance on navigating government bureaucracy; experimenting with technological innovation; enhancing technical and engineering skills; and, most recently, the first effort to provide an accelerator support function to later-stage businesses that have reached size and duration metrics. GIZ has also recently supported the creation of an Iraq Innovation Alliance (IIA) to act as a collective body promoting the interests of these stakeholders; even after GIZ funding for the IIA ended in early 2020, IIA members have continued to coordinate their activities and lobby government to make the business environment more supportive of start-ups and businesses in general.

There are a number of attractive opportunities for DCEO support in this space. They include: supporting an expansion of the IIA’s advocacy and lobbying efforts, especially in the areas of: a) simplifying registration, strengthening copyright protections, and reducing the early-stage taxation burden; b) facilitating smaller-scale, early-stage investment (circa $50-150,000) that many start-ups need, via either domestic or foreign investors; c) supporting the development of partnerships with
U.S. education institutions that can facilitate access to better technology and higher-quality innovation education; and d) using the media to disseminate the culture of entrepreneurship and innovation to Iraq’s rapidly expanding youth population.

However, it is important not to take entrepreneurship and innovation too far. Creative destruction and risk-taking have their limits even in more developed societies, and the lower job security typically involved makes them more suited to those higher up the socio-economic spectrum. As such, any support in this area will need to be balanced with support to less dynamic but more stable forms of private sector employment for those lower down the socio-economic spectrum, as outlined in Sections 4.1.1-4.1.3. The interlocking nature of Iraq’s political economy challenges means that there is not one solution to its fragility. Instead, it is necessary to make progress – which in many places will be slow and subject to reversals as Iraq is struck by further political, economic, and social shocks – across a wide range of areas over the medium term.

As DCEO does so, success will be heavily influenced by how effectively the private sector and development actors can protect the economic activities involved from becoming assets over which political actors compete. Political actors remain oriented towards intense competition for control over any asset that allows them to capture wealth and enhance their political power. While most political attention has been focused on the state because it is the primary source of wealth and patronage, some of this has affected private sector activity too. Especially as the state becomes more fiscally constrained, there is a significant risk that political actors will increase their attention on private sources of wealth-creation, which risks raising costs and risks to DCEO partners, and more fully impeding or corrupting DCEO support.

4.2 RECOMMENDATIONS

Based on these findings and conclusions, we have identified the following geographical and sectoral priorities for the DCEO project. These are grouped under each of DCEO’s four sub-objectives.

4.2.1 SPECIFIC PROGRAMMATIC RECOMMENDATIONS

<table>
<thead>
<tr>
<th>SUB-OBJECTIVE</th>
<th>PRIORITY PROGRAMS</th>
<th>DESCRIPTION AND NOTES</th>
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<tbody>
<tr>
<td>1.1 Mitigate drivers of conflict in target communities</td>
<td>1. Support a forum where protesters and political elites attempt to reconcile differences and forge agreement on priority political reforms.</td>
<td>The single biggest social cohesion issue in Baghdad and the southern governorates is the protest movement. Any effort to help provide more constructive engagement between this social movement and the government will be extremely challenging, and results will be heavily dependent on finding the right institutional mechanism and working with the right actors.</td>
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<tr>
<td>1.2 Community leadership of inclusive development enhanced</td>
<td>1. Support reconstruction of the University of Mosul and/or Northern Technical University (NTU).</td>
<td>Ninewa is already heavily invested in by international actors, and as such many sectors of support are crowded. However, there is an opportunity to support the rebuilding of the University of Mosul, which continues to need heavy investment despite already receiving funding from UNDP. Areas of priority are the library and sciences faculty. NTU has received less funding, but is an important vocational and technical institution with branches across northern Iraq.</td>
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<tr>
<td>2.1 Private sector networks improved</td>
<td>1. Support the Iraq Innovation Alliance (IIA) and, potentially, the Iraqi National Business Council (INBC) to lobby for priority business environment reforms.</td>
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<td></td>
<td>The IIA is representative of the young and the new entrepreneurial class, and is not stunted by outmoded thinking or corrupted by political elites. It has already demonstrated its ability to enact reforms that support entrepreneurship. The INBC, as the body representing Iraq’s most elite businessmen, is connected to international business and therefore dynamic in a way that the Chambers of Commerce are not. While further due diligence would need to be conducted, the INBC appears to be the most effective and reform-minded of Iraq’s more established business associations. DCEO should support the IIA (and potentially the INBC) to lobby for priority business environment reforms, especially: a) simplifying registration processes, b) strengthening copyright and trading name protections, and c) lowering taxation on start-ups and small enterprises.</td>
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<tr>
<td>2. Facilitate domestic and foreign investment, including through a dedicated SME investment fund.</td>
<td>DCEO should support the creation of a dedicated investment fund that focuses on SMEs, and especially start-ups. These SMEs can operate in any sectors, but those working in the sectors listed under Objective 2.2 should be prioritized to benefit from sectoral synergies. This fund should focus on providing innovative financing solutions in the $50,000–150,000 bracket, whether through managing an investment fund that acts as intermediaries between domestic/regional investors and businesses, and/or providing matching capital and equity guarantees for domestic/regional investors in specific SMEs. DCEO should also complement this SME focus with consortium partner CrossBoundary’s efforts to facilitate larger scale foreign investment in larger, more established Iraqi businesses.</td>
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<td>3. Invest in private providers of vocational skills training.</td>
<td>DCEO should support private sector providers to offer training courses to Iraqi workers, especially in construction and agriculture, but also the other sectors mentioned under 2.2. It should also ensure that any skills development is done in conjunction with a post-training job placement program, so that learned skills are immediately deployed directly into the private sector. This may involve bringing established regional technical and vocational education and training (TVET) providers to open a branch in Iraq, or facilitate TVET for Iraqis in relevant neighboring countries.</td>
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<tr>
<td>2.2 MSME development increased</td>
<td>1. Invest in agricultural value chains.</td>
<td>DCEO should support the development of priority products/value chains in the agricultural sector, split across the critical agricultural areas of Ninewa, Wasit, Kirkuk, and the southern marshes. At the center of this support should be the expansion of labor-intensive agricultural businesses by helping them overcome their binding constraints – whether finance, agricultural inputs, processing or market facilities, or others. However, we should invest across the value chains in order to improve the full market system for that crop or product. This will likely include more capital- and knowledge-intensive components, such as manufacturing of inputs and food processing (i.e. agribusiness), as well as food storage facilities, distribution, the reconstruction of physical market facilities, and the introduction of technical and technological innovations. This must stay in the mid-sized realm in order to avoid being pulled into the corrupt political elite, or going so small that DCEO involvement has low overall efficiency and impact. If DCEO engages in small scale, our focus should be exclusively on those who are vulnerable for other reasons – for example, women, minorities, or those at risk of involvement in violent extremism.</td>
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<tr>
<td>2. Invest in construction.</td>
<td>DCEO should support the development of the construction sector, especially those firms working in housing, commercial buildings, and light infrastructure (such as irrigation). In Ninewa, Diyala, and Salahaddin, this should support reconstruction; in central and southern Iraq this should address service provision and housing shortfalls; and in KRI, Anbar, and the south, this should look for opportunities to introduce innovations in techniques and products. At the center of this support should be the expansion of labor-intensive construction businesses by helping them overcome</td>
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their binding constraints — whether finance, agricultural inputs, processing or market facilities, or others.

However, we should invest across the value chains in order to improve the full market system around it. This will likely include more capital- and knowledge-intensive components, such as manufacturing of construction materials from domestic natural resources, the improvement of construction skills (see Objective 2.1), and the introduction of new construction techniques and products through innovation.

Longer term, the legitimate private construction sector should be supported in lobbying for reforms in government construction contracting, for example by prioritizing SMEs in some categories, and shifting to a land-grant rather than cash-payment modality.

<table>
<thead>
<tr>
<th>3. Invest in ICT, tourism, food and beverages, and retail trade.</th>
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<tr>
<td>DCEO should support the formation of stronger service sector SMEs in the ICT, tourism, food and beverage, and retail sectors. With vocational skills in these sectors already covered under Objective 2.1, and potential innovation support in these sectors covered below, the priorities should be:</td>
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<td>- Supporting better business planning and managerial skills.</td>
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<td>- Supporting better soft skills.</td>
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<tr>
<td>- Supporting businesses in these sectors which link to other areas of support in order to generate market synergies (such as food and beverages that sell the agricultural products we support, or tourism connected to marshland agriculture).</td>
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<tr>
<td>- Supporting greater female engagement in these sectors through a job placement and Women in the Workplace champions scheme for businesses.</td>
</tr>
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</table>
4. Invest in entrepreneurship and innovation in key urban centers.

DCEO should support the expansion of the existing entrepreneurship and innovation ecosystem. Priorities are:

- Facilitating small-scale ($50,000-150,000) venture capital financing to early stage entrepreneurs who already have confirmed revenue, across any sector (as described under Objective 2.1).
- Building bigger and better technology labs and technology education in Iraqi universities, potentially through U.S. universities.
- Supporting a Shark Tank-like television program on Iraqi TV to disseminate the mindset and skills needed to be a successful entrepreneur to a wider audience, especially among the young.

Table 1 Specific Programmatic Recommendations
4.2.2 RECOMMENDATIONS ON DELIVERY APPROACH

To complement the above recommendations on what DCEO should focus on, it is valuable to also assess in some detail the technical approaches DCEO should use to implement these programmatic recommendations. To do so, it is worth briefly noting that there is a reasonably robust evidence base for what types of private sector development programs have had more or less impact in fragile and conflict-affected environments such as Iraq. This will enable DCEO to not only focus on the right geographical and sectoral priorities, but also adopt best practice in how it delivers against these objectives.

Most importantly, an International Finance Corporation (IFC) study of 56 private sector development program evaluations across multiple fragile or conflict-affected environments found that direct investment as a program methodology led to significantly higher rates of successful impact than either purely technical assistance (TA)/advisory services, or a mix of TA/grant with investment. As the IFC notes, the \textit{“strongest results occurred in projects with direct investments – and by a large margin [italics in original].”} However, the mixed approach of investment and TA/grant did lead to success in a majority of programs (see Figure 24).

For types of intervention, infrastructure development support and SME development support were roughly equally tied as most likely to deliver successful impact, with the difference accounted for in a higher rate of failure for SME support (see Figure 25). Support to an improved business environment was found to be significantly less likely to lead to clear success, as was supporting financial institutions.

\[\text{Figure 22 Success by types of instruments}\]

\[\text{Figure 23 Success by types of intervention}\]

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Given DCEO’s mandate of supporting SMEs and business associations, these findings bear out DCEO’s programmatic recommendations above, namely:

- A leading role for investment, while coupled with grants and some technical assistance where desirable.
- A leading role for direct SME support, complemented by support to business associations who can lobby for improvements in the business environment.

In terms of the process by which DCEO should implement, the programmatic recommendations above are similarly borne out by the wider international evidence base on how to design a private sector assistance program in a fragile and conflict-affected environment. In particular, the World Bank’s Independent Evaluation Group (2013) noted that key success factors in delivering programs such as DCEO included:

- “Focusing on a few key priority issues to address major constraints, taking a cross-sectoral approach to tap synergies.”
- “Prioritizing investments around vital infrastructure, finance, and human capital and in dominant sectors such as agriculture and natural resources,” and
- “Linking local skills development activities with private sector needs.”

Finally, it is worth noting that the dominance of politics and the state in all aspects of Iraqi social and economic life will require that strong political navigation on the part of the DCEO program team,107 in close collaboration with the Mission and wider USG. This is consistent with wider USAID and other donor thinking about the importance of adaptive management in fragile and unpredictable contexts,108 and will require balancing engaging the government to generate buy-in and support for implementation, without allowing existing government dysfunction to compromise program objectives.

And specific to this project, when selecting which private enterprises to support, DCEO must carefully investigate any potential political patronage links between the enterprise and a political party, and determine whether that is or is not an obstacle to providing them support (i.e. will supporting them improve or worsen political influence in the operation of the private sector).109

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107 KII with Iraqi political analyst, Mar 31st 2020
109 KII with Iraqi political economy expert, Feb 17th 2020
ANNEX 1: GOVERNORATE-LEVEL ANALYSIS

AI. INTRODUCTION

Befitting a fractured, divided country, while each of the governorates we analyze in this report is influenced by the national-level political economy, there is also substantial diversity of political and economic conditions in each province. As Iraqi analysts Saleem and Skelton note, “[u]nderstanding governmental failure across Iraq’s vastly different regions is too massive a task to generate illuminating analysis.”

As such, this section explores the specific political economy characteristics of the seven governorates DCEO selected for more detailed study, in order to surface some of the specific political economy conditions, challenges and opportunities across Iraq’s diverse regions and peoples.

I. BASRAH

Like Iraq’s other southern provinces, Basrah has not directly suffered the same sporadic violent conflict and displacement that has affected much of the north and west of the country since 2003, in large part because of its relative ethno-sectarian homogeneity (being comprised almost exclusively of Arab Shi’a). Instead, its political economy has been characterized since 2003 by fierce and at times violent competition between Shi’a political parties and their associated militias for control over local government institutions and many of the wider formal and illicit revenues from the province’s hugely dominant oil sector – which accounts for 80 percent of Iraq’s total oil production – and a rising tide of popular frustration at these actors for the growing economic stagnation and inequality that this competition has led to.

None of these political parties – such as Hikma, Da’awa, the Sadrist, and Fadhilla, and increasingly Badr and Asaid Ahl al-Haq too – have been dominant in this competition over others; rather, competition and control has been continuous. The focus of their competition has been over power within the governorship, line ministries, the all-important Basrah Oil Corporation (BOC) and other SOEs, and the Provincial Council – and over important sources of economic rents, such as the

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110 Saleem and Skelton, “Mosul and Basra After the Protests,” pg. 3
111 Ibid, pg. 26
112 Ibid, pg. 26
Um Qasr port, border crossings, checkpoints, oil and gas subcontracts, and other government contracts.\textsuperscript{113} Frequently, the parties have deployed their armed wings to use violence, or the threat of it, to achieve these political and economic objectives — and in this way, Basrah is very much a provincial-level microcosm of the same national dynamic of competition for patronage and rent-seeking opportunities within and beyond state institutions.

After 2003, the occupying British military and diplomatic presence tacitly accepted the growing power of these parties and their militias — privileging stability over political inclusivity — but in 2008 the Nouri al-Maliki-led federal government executed Operation Charge of the Knights to weaken the power of the militias, the Sadrists in particular.\textsuperscript{114} The GOI succeeded in reclaiming some control from more localized political and militia actors, but in practice only replaced one set of powerful political/armed actors with another, rather than establish more effective and inclusive governance in Basrah. The GOI did promise from 2009 onwards to increase employment and economic well-being in Basrah, and focused its attention on modernizing and expanding its dilapidated and under-producing oil sector; through this, the BOC established a number of service contracts with large international oil companies that were required to recruit primarily from the local population.\textsuperscript{115}

This created some local jobs, but far short of what was needed to meet the level of demand — and many of these jobs were recruited on the basis of tribal and political patronage networks by the politically connected companies that secured the service contracts with BOC and the international oil companies.\textsuperscript{116} And this focus on the oil sector came at the neglect of the non-oil economy; the expansion of oil production, as prioritized by the GOI, strengthened rather than weakened the dependence of Basrah’s economy on oil and its associated services, rather than building a broader-based economy.

Disappointment in government employment creation efforts in the oil sector generated protests at oil fields and in the city in 2015. Protests re-emerged shortly after the 2018 elections, when what were originally demonstrations sparked by unhappiness over worsening provincial access to non-contaminated, non-saline water expanded to wider expressions of frustration over unemployment,\textsuperscript{117} and escalated into attacks on political party buildings (including those connected to the PMF) and the Iranian consulate.\textsuperscript{118} In some ways, this was the first outbreak of what would become the wider protest movement from October 2019, and it is understandable that Basrah is where this happened; along with other southern provinces, Basrah is the only part of the country where the poor, often unemployed or stuck in low-skill, low-wage pay, are actively getting poorer,\textsuperscript{119} even while gains from the oil sector by a narrow section of Basrawi society has creating a new rich and driven residential rents in parts of the city higher than their equivalents in Dubai.\textsuperscript{120}

\textsuperscript{113} Saleem and Skelton, “The Politics of Unemployment in Basra,” pg. 2

\textsuperscript{114} \textit{ibid}, pg. 3

\textsuperscript{115} \textit{ibid}, pg. 4

\textsuperscript{116} \textit{ibid}, pg. 5

\textsuperscript{117} KII with Basrah-based UN official, Mar 3\textsuperscript{rd} 2020; Cambanis et al, “Hybrid Actors,” pg. 35

\textsuperscript{118} Mansour, “Iraq’s 2018 government formation,” pg. 12

\textsuperscript{119} World Bank, \textit{Iraq Systematic Country Diagnostic}, pg. 33

\textsuperscript{120} Eaton et al, \textit{Conflict Economies}, pg. 44
Economically, Basrah has a mixed economy, with an approximately 80 percent urban / 20 percent rural population distribution. Beyond the part of the economy closely connected to oil production and supporting services, and trade through Um Qasr port, Basrah has a sizable urban retail sector, and a moderately sized agricultural sector that spans both rural and urban parts of the governorate, producing fish and livestock in the marshes, and date palms, tomatoes, and honey elsewhere.\textsuperscript{121} It also has a sizable albeit dilapidated manufacturing and industrial sector, in particular in agribusiness and food processing, metallic product fabrication, and non-metallic construction material fabrication.\textsuperscript{122} The 10 percent of these industrial enterprises that employ 94 percent of Basrah’s industrial workforce are large, decrepit SOEs likely used primarily as a means of employment provision. The remaining 90 percent comprise primarily small- and medium-size private sector enterprises that are likely to have capacity to grow and recruit if they can overcome the constraints they face.\textsuperscript{123}

Basrah faces a number of significant constraints to expanding the private sector beyond its deeper structural dependency on oil. The governorate shares the same challenges that were identified at the national level, but some particular constraints are worth highlighting. Electricity provision remains unreliable, and unstable electricity also has had a negative knock-on effect on access to clean and non-saline water.\textsuperscript{124} Water is, as mentioned, a critical issue in Basrah, as the 2018 protests indicated; other factors hurting clean water access are damming higher up on the Tigris and Euphrates, which has had a knock-on of allowing salt water to flow through the Shatt al-Arab and further inland into agricultural areas, as well as industrial dumping of unclean waste water straight into the rivers.\textsuperscript{125} This collapse in access to clean water is also causing disruptive displacement of many more rural areas in southern Iraq to urban Basrah, increasing pressure on its local economy, and negatively impacting the health of Basrah’s population.\textsuperscript{126}

There is also, as in much of Iraq, foreign competition for locally produced goods, and foreign labor competition too; while detailed data are not available, it has been reported that Iranians have entered the Basrah labor market since 2003, given they are often less expensive and have higher skills than equivalent Iraqi labor market participants.\textsuperscript{127} The pervasive presence of militias is another important challenge; with militias unable to interfere directly with oil production because of the power of the international oil companies, they often focus their efforts on extortion at checkpoints and border crossings with Iran and Kuwait, and via control of jetties at Um Qasr, all of which has an economic cost to private enterprises using these critical transport nodes.\textsuperscript{128}

While some reforms have been implemented in response to the protests – such as increasing the governor’s authority to sign off on development projects\textsuperscript{129} – provincial politics has not stopped being a zero-sum competition over extending patronage and rent-seeking. And with the greater

\textsuperscript{121} CIPE, Basrah Provincial Business Agenda, Centre for International Private Enterprise, pg. 26
\textsuperscript{122} \textit{ibid}, pg. 45
\textsuperscript{123} CIPE, Basrah Provincial Business Agenda, pg. 47
\textsuperscript{124} World Bank, “Bringing Business Back,” pg. 14
\textsuperscript{125} NCCI, Basrah Governorate Profile, NCCI Iraq Governorate Profiles Series (2015), pg. 5
\textsuperscript{126} Social Inquiry et al, “When Canals Run Dry”
\textsuperscript{127} KII with Iraq-based foreign researcher, Mar 6\textsuperscript{th} 2020
\textsuperscript{128} KII with Basrah-based UN official, Mar 3\textsuperscript{rd} 2020
\textsuperscript{129} Saleem and Skelton, “Basra’s political marketplace,” pg. 2
power that the PMF and Fatah Alliance have gained in Basrah since 2018, in particular over Basrah reconstruction – reflecting the greater national influence they enjoy from leading roles in the military campaign against ISIS – these devolutionary reforms may actually only “heighten the ferocity of this competition among factions rather than dampen it.”

Furthermore, the policies the governor has enacted in response to the 2019-2020 protests have followed a typically short-termist approach; instead of trying to expand the private sector, Governor Aydani has reportedly allocated 30,000 new public sector jobs to Basrawis, and used the provincial budget to fund the first month of these, with the expectation that the GOI will provide all future months of salary provision. Local government officials have reportedly said these jobs are not required, and it is likely that these jobs are not actually jobs at all but rather ‘hidden unemployment’ – and at a cost hundreds of thousands of dollars from the provincial budget that could have been used for capital investment or something else with longer-term returns. He has also reportedly allocated 11,000 plots of government land to citizens to build properties on, given the acute housing shortage.

Finally, there has also been a violent crackdown on local protest leaders; many have fled to Erbil or Turkey after threats or violence towards them, including some journalists who covered the protests. While tribes remain socially powerful in Basrah, they are – unlike in Dhi Qar – reluctant to back the protesters because this would put them in conflict with the powerful political parties and their armed groups. With the protesters lacking unity of organization or purpose, and continued factionalization of government, it seems unlikely that the protesters’ demands can be met, even without the budget crisis that may now be coming due to the March 2020 oil price crash and the economic slowdown that the COVID-19 lockdown will likely impose.

**Programmatic priorities.** Given that Basrah’s poor are growing poorer, and that civic unrest continues to threaten its stability, DCEO recommends investing in a combination of labor-intensive pro-poor growth and some support to wider entrepreneurship and innovation. We therefore think the following types of programming are priorities in Basrah:

1. **Agricultural rehabilitation and development.** Support to the agriculture and livestock sector in the wider marshes around Basrah and in neighboring governorates is an opportunity to increase labor-intensive private enterprise in the south’s rural economy, and could be connected to an expansion of food processing and agribusiness industry in urban Basrah. It could also have important positive environmental side-effects if it involved the introduction of better water-management infrastructure and practices, such as hydroponic and aquaponic systems, and reduce rural displacement. Support could include: a) facilitating private investment in more market-based/formal agricultural and agribusiness practices, b) supporting capital formation and access to agricultural inputs and markets, and c) addressing the critical clean water constraint.

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130 Saleem and Skelton, “Mosul and Basra After the Protests,” pg. 31
131 *ibid* pg. 30
132 KII with Basrah-based UN official, Mar 3rd 2020
133 *ibid*
134 *ibid*
2. Support to construction SMEs. Another labor-intensive sector, a more dynamic private construction sector could help meet both Basrah’s critical low-income housing needs, and provide local capability to upgrade civic infrastructure such as water and electricity. This could include a) supporting growth of existing construction companies, b) introducing new construction techniques, including those that use domestically produced materials, c) supporting constructions materials manufacturing firms, and d) supporting TVET training to increase Basrawis’ participation in higher-skilled construction techniques.

3. Entrepreneurship and innovation. Complementing pro-poor growth should be support to higher value-added and potentially more transformational support to Basrah’s private sector. This could include a) extending start-up incubation and innovation support programming to Basrah, b) identifying and facilitating innovative private sector approaches to improve electricity provision and water quality, for example through micro-grid solar energy provision in more rural areas across the wider south, and c) supporting start-ups spun out of technical ideas emerging from Basrah’s Science Camp.

4. Investment facilitation in small-, medium-, and large-scale private manufacturing and industrial enterprises. Basrah’s proximity to an international port facility and relatively developed (if dilapidated) manufacturing and industrial sector makes it a strong candidate for supporting SMEs and larger firms setting up new manufacturing and other industrial enterprises.

2. DHI QAR

Dhi Qar is the poorest governorate in Iraq,\textsuperscript{135} befitting the wider fact of southern Iraq being the region with the highest poverty rates in the country.\textsuperscript{136} Of the southern governorates, Basrah receives the overwhelming majority of political attention and government resources, given the high financial and political importance to the GOI of its oilfields and port, its larger population and the presence of industry and international companies.\textsuperscript{137} By contrast, Dhi Qar, as with Maysan and Muthanna, has many fewer strategic resources, and an undynamic, most rural economy; the costs to governmental neglect have therefore historically been relatively low – compounded by the pre-2003 favoring of Iraq’s Sunni provinces by the Saddam regime.

Dhi Qar can be understood as a satellite governorate to the dominant Basrah, and so was similarly influenced by the rise of Shi’a militias in southern Iraq after 2003.

\textsuperscript{135} NCCI, \textit{Thi-Qar Governorate Profile}, NCCI Iraq Governorate Profiles Series (2015), pg. 4
\textsuperscript{136} World Bank, “Where are Iraq’s Poor: Mapping Poverty in Iraq,” World Bank Group (2015), pg. 22
\textsuperscript{137} KII with Basrah UN official, Mar 3\textsuperscript{rd} 2020
The 2008 crackdown on these militias in Basrah extended to Dhi Qar, with “militias briefly taking control over [the main urban center] Al-Nassiriyah [sic]. After an agreement was reached between Sadrist leader Moqtada Al-Sadr and the Iraqi government, the situation has remained relatively peaceful, with Shia factions mainly competing through the ballot box.”\textsuperscript{138}

That being said, Dhi Qar has been an important source of political movements within Iraq in the past century; it was an important incubator for communist politics in the 1930s and Baathism in the 1950s, and the 1991 Shi’a uprising against Saddam also originated in Dhi Qar.\textsuperscript{139} It is not therefore surprising that, with a legacy of political activism and a dire economic situation, Dhi Qar has been a major center for protests since they started in October 2019, with their heavy focus on unemployment and services. After Baghdad, provincial capital Nasiriyah has seen the highest death toll of any protest sites so far, and the highest relative to population.\textsuperscript{140}

Prior to the COVID-19 pandemic, there were significant risks of civil disorder spreading in Dhi Qar, because the dynamics of protest there are different to other centers of protest. Nasiriyah saw some of the earliest attacks on political party offices when in early October 2019 protesters set fire to the offices of a number of leading Shi’ite Islamist parties (including Daawa, Hikma, and Asaeb Ahl al-Haqq).\textsuperscript{141} And unlike the political quietism demonstrated by Basrawi tribes, some of Dhi Qar’s tribes backed the protesters and threatened the GOI and its PMF supporters with armed rebellion in November 2019 after a heavy security force crackdown killed 32 protesters.\textsuperscript{142} This makes providing viable economic opportunities in Dhi Qar in some ways more urgent than in other centers of civil unrest, even if the pandemic has likely temporarily lowered this urgency for some months.

Dhi Qar remains a highly rural agricultural economy, revolving around its extensive marshlands. The agricultural sector, which had focused in particular on livestock, dairy, and fish, suffered heavily as a result of the Saddam regime’s food subsidies in the wake of the 1990 Iraqi invasion of Kuwait, which pushed down prices of staples and made them unprofitable for local farmers to produce.\textsuperscript{143} The Saddam regime also drained a majority of the marshland in the early 1990s to punish a popular uprising across the south, heavily damaging the farming and fishing sectors that characterize the majority of marshland agriculture. Some marsh restoration has occurred since then, but ongoing water shortages and high levels of salinity remains a major issue, as does Iraq’s wider shift to import of cheap food produce from Iran and Turkey.\textsuperscript{144}

Provincial capital Nasiriyah is small, with some artisanal industry, and benefits from lying along Highway 8, which connects Baghdad and Basrah (and then Kuwait). Notably, Dhi Qar has some of Iraq’s most important Sumerian, Akkadian archaeological sites, in including the ancient cities of Ur and Larsa and Eridu. At present, approximately one-third of Dhi Qar’s population are under the poverty

\textsuperscript{138} NCCI, Thi-Qar Governorate Profile, pg. 4
\textsuperscript{139} Al-Salhy, Suadad, “Dhi Qar: The southern province at the heart of Iraq’s uprising,” Middle East Eye (Feb 2nd 2020), accessed at: https://www.middleeasteye.net/news/demonstrators-iraqs-dhi-qar-say-they-are-inspiration-iraq
\textsuperscript{140} Al-Salhy, “Dhi Qar: The southern province at the heart of Iraq’s uprising”
\textsuperscript{141} Fantappie, “Widespread Protests Point to Iraq’s Cycle of Social Crisis”
\textsuperscript{142} Al-Salhy, “Dhi Qar: The southern province at the heart of Iraq’s uprising”
\textsuperscript{143} NCCI, Thi-Qar Governorate Profile, pg. 2
\textsuperscript{144} ibid, pg. 2
line, and access to clean water and other basic services is well below the national average. Fewer than 30 percent of its citizens depend on public electricity, given the majority experience more than 12 hours of cuts a day, and most people use “private or shared generators to complement their electricity supply.”

**Programmatic priorities.** As one of the poorest parts of Iraq, and home to an economically frustrated and politically restive citizenry, DCEO recommends a focus on pro-poor private sector growth in both its rural and urban economies. We think the following are priorities:

1. **Agricultural development.** The marshes’ historical agricultural practices focused on livestock, dairy, and fish, so we think prioritizing the expansion of these agricultural sectors will also have important ecosystem and social benefits. This should include a) improving access to water and introducing less water-intensive irrigation techniques in the marshes, b) supporting access to agricultural inputs, and c) supporting greater connections between local producers, manufacturers, and consumer markets.

2. **SMEs in Nasiriyah.** We do not know enough about the urban economy of Nasiriyah to draw strong inferences about what sectors could be supported, but supporting SMEs that participate in the agricultural value chain, especially if involved in food processing and distribution to larger markets outside Dhi Qar, are likely to be priorities.

3. **Tourism.** There is an opportunity to support greater domestic and international tourism (likely accessed via Basrah) to Dhi Qar’s rich historical sites, particularly if implemented in a manner designed to primarily benefit local communities.

3. **NINEWA**

The defining characteristic of Ninewa in the past five years has been its place at the heart of ISIS’s rule in Iraq and the extreme levels of human and physical destruction that ISIS and the campaign to retake Ninewa from it caused. One important metric of Ninewa’s centrality to the destruction wrought by ISIS is the continued large numbers of internally displaced persons (IDPs) in and from the governorate. At the end of December 2019, Ninewa had the most IDPs – approximately 335,000 – of any Iraqi province, or nearly one-third of all IDPs remaining in the country.146 Almost all of these IDPs are from Ninewa itself, as are all of Dohuk’s 320,000 and roughly half of Erbil’s 240,000147 – amounting to 55 percent of all displacement in the country, and indicating how much its citizens have

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145 ibid, pg. 5
been affected by extremism and conflict since 2014. And these are only the current numbers of displaced; a million people have already returned to Mosul – the largest concentration of returnees anywhere in the country – while another 342,000 have returned to Tel Afar and 164,000 to Hamdaniya.148

Similarly, the World Bank outlined how Ninewa has overall suffered more physical damage to its housing stock, physical and social infrastructure, and productive economic sectors than any other province; 43 percent of Iraq’s housing that was partially or fully destroyed by the conflict is in Ninewa. That damage is heavily concentrated in Mosul, where 65 percent of all houses have been partially or completely destroyed.149 A similar picture exists for Ninewa’s health and education infrastructure (45 percent and 26 percent of all of Iraq’s damage, respectively), and its agricultural sector (33 percent). Its industrial and commercial sector has also suffered heavily, comprising 20 percent of the damage across affected governorates – less than Anbar’s share of destruction (55 percent) only because of Ninewa’s comparatively smaller industrial sector. Furthermore, 314,000 people were made unemployed and another 224,000 underemployed, heavily hitting economic wellbeing and tipping many into poverty, especially those who had previously had private sector employment; IDPs with public sector jobs continued to be paid their salaries and benefits.150

The wider effect on Ninewa’s economy has been similarly large and negative. Ninewa historically had a mixed economy, encompassing agriculture on the rainfed plain, in the irrigated areas around Rabia in the northwest, and around Sinjar; and Mosul’s robust urban economy, which featured a large manufacturing and industrial sector in addition to vibrant retail, trade, and education sectors. Ninewa’s agriculture focused in particular on wheat and barley, as well as seasonal fruit and vegetables (especially tomatoes). In Sinjar, livestock (sheep and goats in particular), fruit, and vegetables have also been an important part of Sinjar’s local agricultural economy.151

Given the destruction of the ISIS period, the GOI and international community have committed large sums to finance reconstruction across Ninewa. However, even if important progress has been made – including establishing a reasonable level of safety and security in the economically critical Mosul city – the overall pace of reconstruction is widely recognized to be slow; as one official noted, most hospitals remain non-functional, and the main bridges are still being rebuilt.152 Rehabilitation of the rural economy outside of Mosul has been similarly slow, and is in part held back by ongoing GOI-KRG disputes over territorial ownership. Many IDPs from Ninewa, especially from minority communities and including those from Mosul’s wealthy mercantile community, remain reluctant to return given the trauma they have suffered and the destruction of their communities, places of worship, and businesses.153

Much of the drag exerted on the pace of reconstruction lies in the same political economy issues that enabled the rise of ISIS in the first place; a dysfunctional and competitive set of national and

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148 ibid, pg. 5
149 World Bank, Damage and Needs Assessment, pg. 16
150 ibid, pg. 32
152 KII with Mosul-based UN official, March 11th 2020
153 KII with Moslawi businessman from a minority community, Apr 7th 2020
provincial political actors, which has translated into weak, exclusionary governance and high degrees of popular grievance towards state authorities. Saleem and Skelton (2019) note that “[i]n Mosul, the stalled reconstruction process cannot be understood apart from a post-2003 political order defined by rivalries between many different actors, including Sunni Arab political factions, the two main Kurdish blocs, the Americans and Coalition, the Prime Minister’s Office, the Iraqi Security Forces, and most recently, the Popular Mobilization Forces and their political proxies.”[^154]

Some ascribe the specific source of failure to the lack of Moslawi representation at the Baghdad level, and contrast this with the greater political power and consequent better pace of reconstruction enjoyed by Anbar.[^155] Others however have ascribed it not to “inadequate ‘Sunni representation’ in positions of influence,” but instead a result of how “power is obtained and utilized at the expense of others, and in neglect of governmental performance.”[^156] Both of these have elements of truth to them. Some Moslawis DCEO spoke with did indicate that perceived Sunni exclusion was a source of resentment for them, and indicated the negative views many Sunnis feel towards the PMF who continue to be present across the governorate — “accusing us of being ISIS even while asking for our gratitude for liberating us” — and noting, for example, that many important local Sunni and Assyrian religious and historical sites are being taken over by Shi’ite charitable foundations and Shabak business interests.[^157] But it is likely also that even with strong Moslawi representation in Baghdad, the complicated and fractious politics of Ninewa and the reconstruction process would still exert a considerable drag on the governorate’s political and economic recovery and development. And it was reported by the National Democratic Institute (NDI) that citizens in Ninewa felt relations between ethno-sectarian groups were improving, but that politicians were continuing to sow “divisions along sectarian lines for their own benefit.”[^158]

Post-2003, Ninewa saw a succession of periods of rule by ethno-sectarian factions who, each time they were politically and militarily powerful, took a maximalist approach to rule that excluded rivals rather than arriving at a stable settlement, while those out of power tended to use anti-state rhetoric, civic unrest, and at times violence to attack those in power. This included: the Kurdistan Democratic Party (KDP) and peshmerga in the early post-2003 period, whose authority well outside their Kurdish-majority heartlands fueled an early insurgency primarily anchored in the Sunni community; a GOI-backed Sunni Arab political coalition from 2009; and then an alliance between KDP and a local Sunni powerbroker from 2013. In each case, those in power spent too much time on political competition and not enough on governing, including providing security. After exploiting similar dynamics in Anbar, ISIS began taking territory in Ninewa in 2014 by exploiting the anti-Iraqi Security Forces rhetoric that local out-of-power Sunni political leaders had themselves propagated in the preceding years.

When Ninewa and Mosul city were finally retaken in 2017, similar political dynamics re-emerged. With the military campaign against ISIS and the subsequent 2018 elections, the power of the PMF

[^154]: Saleem and Skelton, “Mosul and Basra after the protests,” p.g 3
[^155]: KII with Mosul-based UN official and entrepreneur, March 2020
[^156]: Saleem and Skelton, “Mosul and Basra after the protests,” p.g 7
[^157]: KII with Mosul-based entrepreneur, Mar 18th 2020
[^158]: NDI, “Citizens Continue to Demand More Responsive Governance: Key Findings of Qualitative Public Opinion Research Conducted in Five Provinces in Iraq.” NDI (2019), pg. 5
and their associated Shi’a political parties has significantly increased, and at the expense of traditional Sunni powerbrokers in Ninewa.\textsuperscript{159} Furthermore, Sunni political elites from neighboring Anbar and Salahaddin have recently begun to exercise greater influence over Sunni politics in Ninewa – exploiting Baghdad’s desire to avoid local Sunni powerbrokers re-emerging and capitalizing on Kurdish political weakness after the 2017 referendum, and further restricting the ability of its indigenous Sunni population from being adequately represented at the national level.\textsuperscript{160}

These political dynamics have dragged on the reconstruction process. While a reasonable level of safety and security has been re-established in Mosul city and large parts of the Ninewa Plain, allowing many IDPs to return home, significant pockets of contested territory remain – including Sinjar, where PMF, PKK (specifically the military wing of Turkey’s Kurdistan Workers’ Party), and other armed groups are competing for influence, and in the areas bordering Dohuk and Erbil governorates that are disputed between the KRG and GOI.

The private sector in Ninewa continues to suffer from these adverse political conditions and fragmented security environment, even as the citizens of Ninewa, as in other post-ISIS governorates in northern and central Iraq, identified job opportunities to improve their economic situation as the most pressing need; NDI found that economic opportunities are seen “as a precondition for satisfying other necessities, which the government is failing to provide, mainly water and electricity.”\textsuperscript{161} DCEO respondents in Ninewa similarly most identified a lack of overall economic opportunities as the challenge in finding private sector employment, above insecurity, a lack of social or political connections, and a lack of relevant skills – although both connections and skills were identified as important constraints, too.

In spite of the challenging political and economic circumstances in Ninewa, it has only seen one small outbreak of civil unrest in recent years, in March 2019, and has notably not had any protests since the emergence of the wider protest movement in October 2019. As in Anbar, this appears to be because of a fear, derived from popular experience of the unrest that enabled the rise of ISIS, that protest in Iraq can destabilize and ultimately destroy their communities. As one local businessman noted, for this reason “people won’t protest here for another 10 years.”\textsuperscript{162} This may be helped by the reportedly positive relations in Mosul between the people and ISF, who are heavily composed of local Sunni militia – even though the PMF remain a significant drag on movement and business outside the city,\textsuperscript{163} and the PMF reportedly retain the power to enter Mosul on operations or other activity without the ISF stopping them.\textsuperscript{164}

**Programmatic priorities.** Given the level of destruction and the slow pace of reconstruction, as well as the high level of ongoing displacement, political complication, and social cohesion challenges, Ninewa is an obvious priority for DCEO programming. However, it is also the case that many other national and international actors are investing at scale in Ninewa’s social, economic, and political

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\textsuperscript{159} Saleem and Skelton, “Mosul and Basra after the protests,” p.g 15
\textsuperscript{160} KII with Mosul-based UN official, March 11\textsuperscript{th} 2020; Saleem and Skelton, “Mosul and Basra after the protests,” pg. 18
\textsuperscript{161} NDI, “Citizens Continue to Demand More Responsive Governance,” pg. 4
\textsuperscript{162} KII with Mosul-based entrepreneur, Mar 18\textsuperscript{th} 2020
\textsuperscript{163} KII with Mosul-based entrepreneur, Mar 18\textsuperscript{th} 2020
\textsuperscript{164} KII with Mosul-based entrepreneur, Mar 18\textsuperscript{th} 2020
recovery and development. As such, DCEO recommends identifying a niche that is not currently saturated with international effort, and has therefore identified the following areas as priorities:

1. **Supporting social cohesion in Mosul city.** With large amounts of funding already being provided, DCEO should focus on restoring parts of the University of Mosul that have not yet been rebuilt, especially the sciences faculty and library. The university is a diverse space, and so can support DCEO’s social cohesion objectives. This can also generate synergies with any SME support DCEO provides, particularly in the entrepreneurship and innovation space.

2. **Private sector development in Sinjar.** This is likely to be important in facilitating return of Yazidi IDPs from Dohuk. This could include assistance to the agricultural sector, as well as direct or indirect assistance to Ninewa construction companies (including those producing construction materials) to support the rehabilitation of housing and light infrastructure.

3. **Agricultural development in a) the Ninewa Plain and b) Rabia.** Priorities are investing in farm machinery, improving access to markets (including market places), rehabilitating/expanding irrigation systems (especially in Rabia), and providing capital in the form of livestock, greenhouses and warehouses, and replanting of orchards and date palm plantations. This should be linked to Mosul-based food processing factories where possible, in order to support greater value-addition in the entire value chain.

4. **Governorate-wide private sector support.** This should have particular emphasis on Mosul city, and focus on a) expanding the private construction sector, b) expanding agribusinesses that process local agricultural produce for domestic production (in Ninewa and across Iraq), and c) supporting entrepreneurship and innovation, especially new SMEs entering the market with business skills. Key means to do this are funding and capital investment, as well as matching grants and challenge funds.

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165 World Bank, *Damage and Needs Assessment*, pgs. xix-xx; KII with Mosul-based UN official, Mar 11th 2020
166 World Bank, *Damage and Needs Assessment*, pg. xix
4. ANBAR

At approximately one-third of Iraq’s landmass, Anbar is the largest governorate in Iraq; much of this, however, is made up by its large desert, with its citizens concentrated along the Euphrates river valley. It also has one of the most homogenous populations in Iraq, being made up of almost exclusively Arab Sunnis, and its traditional decentralized tribal social organization remains an important characteristic of the governorate.

In part due to the heavy role of Anbar’s population in Saddam’s Baathist regime, Anbar was also the location of the fiercest early opposition to coalition forces, with fighting there in 2003-4 a major reason why U.S. forces were relocated out of Mosul leaving peshmerga forces in charge. This fighting led to heavy early destruction of Anbar’s infrastructure, in particular centered on Fallujah, but inevitably affecting the governorate’s wider social and economic wellbeing. With the Anbar Awakening’s recruitment of local tribal militias to lead the fight against al Qaeda in Iraq (AQI) from January 2006 onwards, there was a gradual transition to GOI management of security across Anbar through to late 2008, as part of the then Prime Minister Nouri al-Maliki’s wider efforts to assert state security primacy above local armed groups across Iraq. The Maliki government finally demobilized the tribal militias in 2010 out of concern for the strength they had gained in the province, but did so in a manner that kept tribal leadership on-side.

During the period 2008-11, Anbar therefore saw much reduced violence, which allowed local political elites greater space to engage in governorate-level and national politics. However, with the 2011 departure of U.S. forces, the GOI under then-PM Nouri al-Maliki took an increasingly maximalist approach to government at the expense of Sunni political elites, which drove – as in Ninewa – leading Anbari politicians, including tribal leadership, to support anti-Baghdad protests and, at times, armed clashes between tribal fighters and the Iraqi army. By weakening local political elites’ influence in Baghdad, and therefore reducing the resources they received from the central government that they could in turn spend on their supporters, this opened up space for AQI/ISIS to rally anti-government protesters in Anbar.

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167 NCCI, Anbar Governorate Profile, NCCI Iraq Governorate Profiles Series (2011), pg. 3
168 ibid, pg. 3
169 Badawi, Tamer, “Why Arab Sunnis are disengaged from Iraq’s protests,” Atlantic Council (2020), accessed at: https://atlanticcouncil.org/blogs/menasource/why-arab-sunnis-are-disengaged-from-iraqs-protests/
With protests across Anbar in 2013 against the GOI’s alleged use of anti-terror legislation to target the Sunni minority—a as occurred in Sunni areas elsewhere in central and northern Iraq—clashes between tribal militia and the Iraqi army escalated in 2013, and—with tribal leadership divided between support and opposition to the GOI—ISIS began to take territory in Anbar in early 2014, with Fallujah being one of the earliest major population centers to fall to the group. However, Anbar’s main population centers were reclaimed from ISIS by mid-2016, significantly earlier than those of Nineveh, allowing many IDPs to return home; as of December 2019, there were 571,000 returnees in Ramadi, and 537,000 in Fallujah. As such, while Anbar was the source of a large percentage of displacement early in the period of ISIS occupation, relatively few IDPs remain there at present; only 35,000, with another 20,000 Anbaris in Baghdad (where approximately one million people of Anbari origin live).

The human and physical damage from ISIS’s occupation of Anbar and the GOI campaign to retake it was extensive. Many Anbaris continue to fear what they perceive to be a sustained ISIS presence in the governorate, which is one reason Anbar has not been affected by the protests that have hit Baghdad and the south since 2018; one source noted that the local police have been keeping demonstrators from protesting within Anbar by telling them that the unrest this would cause could be exploited by ISIS to re-emerge, as well as through the more coercive measures of detention and intimidation. But the absence of protests has also been reported to stem from popular fatigue with civil unrest, and an acute awareness from recent experience that it can lead to widespread violence and displacement, even if the anti-government sentiment is shared by parts of Anbar’s population.

Physically, across areas of Iraq occupied by ISIS, Anbar is overall second only to Nineveh in the levels of destruction of its residential, civic, educational, health, and other infrastructure; and Anbar lost the most of its industry and commerce facilities of any ISIS-affected areas (55 percent). However, more positively, the progress of reconstruction in Anbar has been reported to be significantly better than other heavily battle-damaged governorates such as Mosul and Salahaddin. Respondents put this down to the strong representation of Anbari politicians in the federal government—in particular in current Speaker Mohamed al-Halbousi—who have been able to push the GOI to allocate and disburse funds for Anbar in a way other provinces have not; other respondents noted that the absence of disputed territories like those in Nineveh has also facilitated population returns and good security conditions.

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172 Malkasian, “Anbar’s Illusions”
174 KII with Anbar-based UN official, Mar 10th 2020
175 Badawi, “Why Arab Sunnis are disengaged”
176 Al-Jazeera, “Fallujah residents in Iraq: ‘We have had our share of protests,’” Al-Jazeera Online (Jan 31st 2020), accessed at: https://www.aljazeera.com/news/2020/01/iraq-fallujah-residents-share-protests-200131160550400.html
177 World Bank, Damage and Needs Assessment, pg. 59
178 KII with Anbar-based UN official, Mar 10th 2020
179 KII with Ninewa- and Anbar-based UN officials, Mar 10th and 11th 2020
Another consequence of the recent period of ISIS occupation and conflict is the sustained presence of predominantly Shi’a militias in Anbar. However, they do not play a role in the main population centers of Anbar, where the local police are the primary security force; rather, their presence focuses on maintaining checkpoints on the edges of the governorate and along key highways, and maintaining larger presences in the border towns of al Qaim and Akashat, in order to control strategic roads and supply routes into Syria.  

As such, Anbaris were the most satisfied with the present and optimistic about the future of the respondents DCEO surveyed, indicating a desire to move on from recent periods of violent conflict and destruction and enjoy the improvements in their daily lives. However, they were by no means without concerns about the many political and economic challenges that Iraqis of all stripes face – and there has also been a wider deterioration of Arab Sunni views of their situation in post-ISIS Iraq in the past two years.

Anbar has a mixed economy. Home to one-third of all agricultural land in Iraq, it has extensive irrigated agriculture along the Euphrates, although as with other parts of the country this sector has shrunk due to trade liberalization and the post-2003 removal of subsidies, as well as neglect, under-investment and the governorate’s repeated bouts of conflict. Anbar is also home to an extensive industrial sector, having been a favored location for SOEs during the Saddam era – including phosphates, cement, glass, and weaponry – and also has one of the largest concentrations of construction contractors in Iraq. It is also home to the Akkas gas field in Qaim, which was only reclaimed from ISIS in late 2017. Finally, important roads leading to Saudi Arabia, Jordan, and Syria run through it, and it is therefore important both economically and politically for trade and transport; the presence of PMF on the peripheries of the governorate reflects this.

Overall, Anbar is a relatively wealthy governorate, with its relatively small pockets of poverty concentrated in Karma in particular, as well as Ramadi and Fallujah districts. Indeed, Anbar is part of the only region in Iraq – the central region – where incomes are rising almost uniformly across the wealth spectrum. Even so, things could improve; NDI found that in Anbar and the four other formerly ISIS-held provinces, Iraqi citizens identified job opportunities to improve their economic situation as the most pressing need, which is seen “as a precondition for satisfying other necessities, which the government is failing to provide, mainly water and electricity.” Electricity was cited separately by the World Bank in 2018 as Anbar’s key service constraint.

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180 KII with Anbar-based UN official, Mar 10th 2020
181 Badawi, “Why Arab Sunnis are disengaged from Iraq’s protests”
182 CIPE, Anbar Business Agenda, CIPE Provincial Business Agendas Series, pg. 32
183 ibid, pg. 32
184 KII with Anbar-based UN official, Mar 10th 2020
186 World Bank, “Where are Iraq’s Poor,” pg. 34
187 World Bank, Iraq Systematic Country Diagnosis, pg. 33. In the World Bank categorization, the central region excludes Baghdad, which as the national capital is taken separately.
188 Specifically Diyala, Kirkuk, Ninewa and Salahaddin.
189 NDI, Citizens Continue to Demand More Responsive Governance, pg. 4
190 World Bank, “Bringing Business Back,” pg. 14
Programmatic priorities. Given the reasonable progress of Anbar’s overall reconstruction efforts, and that its poverty rates are relatively low by Iraqi standards, there is less urgency to focus programming here if DCEO’s priority is pro-poor growth. However, Anbar presents an opportunity for DCEO to build on relative success, as in the KRI. Priorities for the governorate are as follows:

1. Agricultural and agribusiness rehabilitation and development. This includes restoring farm machinery, improving access to markets, rehabilitating irrigation systems, and providing capital, as well as rehabilitating Anbar’s historically large manufacturing base to provide agricultural inputs and process agricultural produce for domestic consumption.

2. Construction sector development. Given the presence of many construction contractors in Anbar, there are opportunities to a) expand the size and geographical scope of these companies, b) introduce new construction techniques, including those that use domestically produced materials, c) support firms to increase the manufacturing of construction materials, and d) support TVET training to increase Iraqis’ participation in higher-skilled construction techniques.

3. Support to SMEs. This can include: a) support to innovative start-ups in agriculture and construction that can add competition and innovation into these sectors, and b) support entrepreneurship and innovation in any sector of Anbar’s urban economy.

5. BAGHDAD

The national capital, Baghdad, is naturally where all central government institutions are headquartered, and where all major political parties, ethno-sectarian groups, and large businesses are present. In the past two decades, Baghdad’s districts have become much more demographically homogenous, due in large part to the sectarian violence there between 2003 and 2008, but this is also part of a wider pattern of a demographic change in the city; now a majority-Shi’a city, prior to the 1950s it had been a diverse city with large Muslim, Jewish and Christian communities, until low-income Shi’a from the rural south began to come in search of employment.191

While the violence has declined significantly in Baghdad since the end of ISIS territorial authority in the country, armed groups also remain an important feature of the city’s political and economic life, given that a number of the largest PMF factions are now very much in government. As in Basrah, political elites and their supporting armed groups who can tap into government revenue streams are driving much of

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the development in the city, rather than the majority of ordinary residents, which is enriching the wealthier segment of Iraq’s population even as the poor stagnate; inequality is widening quickly in the city. This is true even if, overall, Baghdad has higher than national average human development indicators – less than three percent under the poverty line and unemployment slightly lower than the national average (10 percent versus 11 percent). The large informal settlements in the Baghdad al-Jadid district makes that the city’s poorest.

Given the state’s heavy presence, public sector employment makes up a large percentage (exact figures are not available) of employment in the city, including in numerous SOEs and SOFIs. Given the sheer scale of the city, its private sector is diverse, although 79 percent of all private firms remain in the informal sector. And its private sector has expanded as a result of recent bouts of conflict, with many firms previously based in the north and west relocating to Baghdad (as to Erbil) to escape ISIS-related violence.

Despite this, its private sector remains undynamic, and Baghdad’s large and growing youth population are particularly ill-served; while official estimates are of 20 percent unemployment, officials in the Ministry of Planning informally indicated to a London School of Economics and Political Science (LSE) researcher that their data indicate it is more like 46 percent. This is one reason why Baghdad has seen such strong protests since mid-2019, with Shi’a youth playing a leading role in criticizing a government dominated by ‘their own’ identity group, but with the protests cutting across ethnic, sectarian, class, and education lines. These protests, revolving around demands for more employment opportunities, have been met by heavy repression by PMF groups, and have also had the effect of hurting Baghdad’s private sector.

Programmatic priorities. As the largest urban area in the country, DCEO thinks the priority should be to support Baghdad-based entrepreneurship and innovation, focusing on the longer-term transformational potential of this type of private sector activity within Baghdad’s economy, and serving as an example to similar entrepreneurial efforts in the rest of central, western, and southern Iraq.

An additional priority is encouraging greater female participation in the private sector, especially in the service economy, for example through a job placement program for talented female graduates.

192 World Bank, Iraq Systematic Country Diagnosis, pg. 33
193 NCCI Baghdad Governorate Profile, NCCI Governorate Profiles Series (2015), pg. 4
194 World Bank, “Bringing Back Business,” pg. 20
195 ibid., pg. 22
Erbil is in many ways a proto-capital city, given the significant degree of devolved political and economic authority that the KRG has. But unlike the much more severe political competition in Baghdad, the political settlement over institutional control between the predominant KDP and the Sulaymaniyah-based Patriotic Union of Kurdistan (PUK), is more stable. A key reason for this greater stability is that “the system of resource distribution and patronage” present in the KRI is based on a broadly clear and agreed division between the two parties, who are politically constituted rather than defined by their (identical) ethno-sectarian identity.\footnote{Saleem, Zmkan Ali, and Mac Skelton, “The Kurdish Duopoly: The Political Economy of Two-Party Rule,” Institute for Regional and International Studies, American University of Iraq Sulaimani (April 2019), accessed at: \url{https://auis.edu.krd/iris/publications/kurdish-duopoly-political-economy-two-party-rule}}

While the two parties have a history of military conflict between them, their shared political and economic interests and the absence of any viable alternative power formation in the Kurdish region has enabled them to maintain their political settlement during both economic booms and downturns since the 2003 transition. This political stability, and the less divisive underlying ethno-sectarian tensions in Kurdistan, has meant that they have been better able to weather more challenging economic conditions, and agree to a friendlier business and investment climate. This is useful, because the KRI is in effect “a rentier state within a rentier state,” deriving its government revenues from both its own oil exports and the fiscal transfers it receives from the GOI from the latter’s oil export; across KRI, and in its capital Erbil, the public sector accounts for half of all employment, a rate that is in fact slightly higher than in the rest of Iraq.\footnote{KRSO, IOM and UNFPA, \textit{Demographic Survey – Kurdistan Region of Iraq}, Kurdistan Regional Statistics Office (2018), pg. 41}

As such, the KRI remains vulnerable to the vagaries of international oil markets and domestic crises that impede oil production just as Baghdad does, but its less competitive, more stable politics provides it with greater resilience in the face of such shocks than the federal government enjoys. It does, however, remain vulnerable to tensions with the federal government. For example, while the twin 2014 shocks of a global drop in oil prices and the rise of ISIS negatively affected Erbil and the wider KRI after it had enjoyed economic boom from 2010 onwards, it was in fact KDP efforts in 2013 to unilaterally export local oil to Turkey that had first tipped the KRI into a downward economic trend, by pushing the GOI to cut off its mandated fiscal transfers and blowing a large hole in the KRG’s state budget.\footnote{Saleem and Skelton, “The Kurdish Duopoly”; DeWeaver, Marc, “Iraqi Kurdistan Economic Report 2016: Kurdistan’s Great Recession,” (2016) available at \url{https://www.marcopolis.net/iraqi-kurdistan-economic-report-2016-kurdistan-s-great-recession.htm}}

This multi-layered crisis stopped much government and private investment – in infrastructure, expansion of oilfields, and housing and commerce – in its tracks, and much of this stalled
construction remains visible across Erbil today. It also significantly increased poverty rates in Erbil and wider KRI even as the region’s poverty rates remain low by Iraqi standards, and badly hurt the private sector; with government employment so high any reduction in government revenues hits public sector salaries and therefore consumer spending.

Further tensions around the September 2017 KRI independence referendum, conducted by the KRG in the immediate post-ISIS period, further hurt Erbil’s economy, after the GOI instituted a travel and goods blockade of the region; this was only lifted in 2018 by the then Prime Minister as part of an elections-related clearing of the decks. Since then, the political duopoly has maintained a broad stability even if tensions over rent-distribution occasionally erupt. This has been supported by a younger demographic who, while in many ways as unhappy with their political elites’ failure to provide jobs, services, and a voice as other Iraqis are, have been willing to afford them a greater degree of tolerance since seeing their defense of the KRI from ISIS. The KRG has also been quite effective at quickly suppressing any nascent public demonstrations on these issues since 2011. A final factor helping tamp down popular unrest is a widespread recognition that life in the KRI is much better than under Saddam, when Kurdish communities were heavily and often brutally repressed.

Erbil’s economy has reflected this improved political stability. UNESCO’s 2019 enterprise and skills survey indicates that Erbil was the governorate where the highest percentage of companies across multiple sectors planned to hire in the next five years. However, the twin March 2020 shocks of the COVID-19 lockdown and oil price decline are likely to hurt Erbil as they will the rest of Iraq, even though there are positive signs that the KRG will be politically able to push through some degree of cuts to its public sector wage and benefits bill in order to reduce the fiscal impact of the decline in oil-derived revenues.

**Programmatic priorities.** Given that Erbil city is by far the dominant population center in the governorate, and conditions in its rural areas are poorer but more stable, DCEO assesses that the priorities for Erbil are as follows:

1. **Supporting entrepreneurship and innovation.** We should use Erbil as place to implement systemic changes in the private sector of the KRI (and wider Iraq). Key areas include a) investment facilitation between local and/or international investors and early- and later-stage start-ups and established businesses, building on existing entrepreneurship and innovation options; b) supporting the introduction of innovative new products and services; and c) exporting KRI-based business practices to less developed parts of wider Iraq.

2. **Promotion of women in the white-collar workplace.** Given the more permissive cultural attitudes to female education and employment in Kurdistan, there is an opportunity to support greater female

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201 World Bank, “Where are Iraq’s Poor,” pg. 27
202 DeWeaver, “Iraqi Kurdistan Economic Report”
203 Salih and Fantappie, *Kurdish Nationalism at an Impasse*, pg. 8
204 KII with Dohuk-based NGO worker, Mar 9th 2020
participation in the private sector service economy. This could focus on a job placement program for talented female graduates in Erbil’s largest private enterprises.

7. DOHUK

Dohuk has, like other governorates in the KRI, seen relative peace and stability since 2003, given the Kurdish political authorities and security forces have been close allies to U.S. and western partners, and the reasonable degree of internal political stability afforded by the Kurdish political duopoly. This helped protect Dohuk from much of the sectarian violence in the mid-2000s, and broadly insulate it from being directly affected by ISIS violence away from its, at times, conflict-affected frontiers with ISIS-territory.

However, ISIS’s occupation and violence have hurt Dohuk, in particular through its ongoing shouldering of a large IDP burden. Almost all of the 315,000 IDPs currently living in Dohuk – primarily in camps and informal settlements, with some in host communities – are from Ninewa, and a large percentage of these are the Yazidi and Christian minority communities who were actively persecuted by ISIS. Many of the IDP camps and informal settlements arose in the vicinity of local settlements of the same ethno-sectarian identity, and it remains unclear how many of them will be willing to return to Ninewa even if the economic situation improves there.206 Dohuk is also home to two Syrian refugee camps.207 These displaced populations have placed a considerable burden on a local economy that is already small and relatively underdeveloped, especially now as support to the IDPs has reportedly decreased in the past two years as the peak of the crisis is seen to have passed.208 While it has benefitted from reasonable stability, Dohuk was also likely hurt by the 2015 economic crisis, with the consequent recession driving up poverty rates just as the IDP influx added an additional socio-economic burden.209

At present, Dohuk’s economy is a mix of agriculture, particularly in livestock and fruit,210 an urban retail and commercial sector, and some industrial activity, in particular clay construction and consumer products. However, as with Erbil, nearly half of all working citizens are employed by the public sector, and its formal private sector is considerably smaller than those of other KRI governorates – constituting only 4.7 percent, with 13.7 percent self-employed and 23.3 percent workers on daily wages (both of which constitute informal forms of labor).211

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206 KII with Dohuk-based NGO worker, Mar 9th 2020
208 KII with Dohuk-based NGO worker, 03/09/20
209 See DeWeaver, “Iraqi Kurdistan Economic Report” for the wider picture of the oil price crash’s effect on Kurdistan’s economy.
210 NCCI, Dohuk Governorate Profile, NCCI Governorate Profile Series (2015), pg. 3
211 KRSO et al, Demographic Survey, pg. 41
Furthermore, Dohuk plays an important part in the cross-border goods trade, as Highway 2, which connects Turkey with northern and central Iraq, runs through Dohuk city after crossing at Zakho – and ultimately passes through Erbil, Kirkuk, and Baghdad. However, the governorate has little in the way of agri-processing or other manufacturing, and its easy access to Turkish products have likely suppressed both domestic agricultural and industrial activity.

Socially, as with the rest of the KRI, Dohuk has better than average schooling, employment, poverty rates, and access to services, than the Iraqi average. However, its literacy levels are noticeably lower, which appears to be driven primarily by rural women non-school graduates; one respondent noted they thought this may be a result of parts of the governorate’s citizens – the Yazidis in particular – continuing to place low emphasis on female education. And it continues to have relatively poor electricity provision, with 94 percent of the population using a shared or private generator to supplement poor state provision. Its unemployment rates are higher than in Erbil and Sulaymaniyah, which is primarily driven by lower female labor force participation. However, the new Erbil-Dohuk highway currently being constructed is expected to significantly half the travel time between the two cities, and that is likely to bring Dohuk more into the more dynamic Erbil economy.

Programmatic priorities. Reasonably stable and not suffering from high levels of poverty and deprivation, Dohuk presents an opportunity to support more innovative approaches to private sector development in a more rural economy, as well as support to the large numbers of displaced minorities present in the governorate. The two priority areas should be:

1. Support to construction and agriculture SMEs. DCEO should support Dohuk-based SMEs working in particular in the agriculture and construction value chains. Priority areas for SME support include:
   a) manufacturing of construction materials from local natural resources;
   b) house building, especially through the introduction of new techniques and domestically-produced materials;
   c) livestock rearing, and more value-added industries associated with livestock, such as leather and woolen carpets; and
   d) processing industry for agricultural goods coming from Ninewa. This should include IDPs wherever possible.

2. Tourism and cultural heritage. DCEO should support the development of employment opportunities for minority communities, especially those with significant displaced populations. This may include:
   a) community-inclusive tourism, benefitting from the KRG’s more permissive security and political environment and access to nearby Erbil airport; and
   b) promotion of artisanal arts and crafts that are connected to the cultural heritage of Dohuk’s diverse communities; and
   c) minority community (re-)engagement in agriculture and other local sectors.

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212 NCCI Dohuk Governorate Profile, pg. 4
213 KRSO et al, Demographic Survey, pg. 34
214 KII with Dohuk-based NGO worker, Mar 9th 2020
215 KRSO et al, Demographic Survey, pg. 50
216 ibid, pg. 39
217 KII with Erbil-based businessman, Mar 7th 2020
ANNEX 2: RESEARCH METHODOLOGY

The Political Economy Analysis was conducted in coordination with the GESI and Conflict Assessments. The technical lead for the PEA was Rory Brown. The GESI Assessment was led by Gender and Social Inclusion Specialist Kaelan Sullivan from Chemonics’ Gender Equality and Social Inclusion team, and the technical lead for the Conflict Assessment was Beezie Dallas.

The assessment leads were also supported with inputs and reviews by Garrett Dorer, Assessment Coordinator and Director, Martha Myers, DCEO COP, Saeed Uri, Deputy Chief of Party for ICRI Ta’afi, Wisam Khaleefah, and Senior Program Development Officer on ICRI Ta’afi. The team from IMMAP that led the data collection in Iraq and provided technical inputs to the reports consisted of Magdalena Paddock, Christopher Marrs, and Yasir Abbas.

The PEA lead used a mixed-methods approach to gather, analyze, and present the information contained in this PEA. Sources included:

- **Secondary literature.** This includes more than 80 academic articles, book chapters, policy papers, program documents, news articles, and development actor research papers, some of which have not been explicitly referenced in footnotes through the report.
- **Key Informant Interviews.** The author interviewed 23 Iraqis and non-Iraqis based in Iraq, including businesspeople and members of business associations, donor and implementer organization staff members, UN officials, political analysts and others with relevant specialisms. The author also accessed transcripts of another 20 KIIs conducted by the authors of the Conflict and GESI Assessments.
- **Field research.** The author worked with DCEO consortium partner IMMAP and their local partner IIACSS to design and deploy a field research instrument that was used by IMMAP enumerators in DCEO’s seven priority governorates to complete 133 surveys of private sector employees and employers of small and medium size businesses, including entrepreneurs who have recently entered the market. The instrument included both qualitative and quantitative data on public and private sector employment conditions, attitudes towards relevant political economy issues, constraints on the private sector, and opportunities for growth.

GOVERNORATE SELECTION

The priority governorates were selected in consultation with USAID in early February, with the rationale outlined in the DCEO deliverable submission, *Political Economy Analysis - Approach and Methodology* (February 9, 2020). This noted that “DCEO has provisionally selected the following six provinces as the focus for the baseline PEA:

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*Table 2 GOVERNORATE SELECTION*
These provinces have been selected on the basis of the following criteria:

1. They encompass a combination of:
   
a. Larger urban environments – where financial and human capital, businesses and economic opportunities, and political institutions and actors, as well as a large percentage of Iraq’s most poverty-stricken population, are concentrated; and

   b. Important peripheries – where many community-level conflicts are centered, large segments of marginalized and vulnerable communities are concentrated, and service provision and business and economic opportunities are much more limited.

2. They exclude the very highest security/political risk environments, as DCEO anticipates it will focus early implementation of TOs in provinces with low-to-medium levels of risk in order to 1) increase the likelihood of impact, and 2) lay foundations for implementation in Iraq’s highest risk locations as and when required.

They incorporate the majority of areas affected by recent major political events, including Daesh occupation and violence, Iranian influence, and unrest and demonstrations against the Government of Iraq.”

Subsequently, USAID requested DCEO to include Dohuk.

ANALYTICAL FRAMEWORK

The analytical framework used for this PEA was derived from the USAID Applied Political Economy Analysis guidelines, with some modifications to fit the SME- and business association-focus of the DCEO program. This involved the following elements:

METHODOLOGY
Within this overall analytical framework, the PEA placed particular emphasis on questions related to:

- How have the structure and norms of the state conditioned both political processes and the relative roles of the public and private sector in Iraq’s economy?
- How has the shape of the private sector influenced political organization and mobilization, and economic dependence on the state?
- How have armed actors and violent conflict interacted with public and private sector sources of income?
- How and in which ways is Iraq’s private sector more or less dependent on the state?

LIMITATIONS

There are two important points to make about the limitations of the information used to arrive at the findings, analytical conclusions, and programmatic recommendations contained in this PEA.

First, robust, up-to-date economic data in Iraq is limited, as previous research by both national authorities and multilateral institutions has been relatively limited and sporadically conducted, and conflict and economic shocks have been so large and frequent as to cause major changes in Iraq’s economy since earlier rounds of research were conducted. There is therefore significant uncertainty in the representativeness and generalizability of these data, and inferences based in this should therefore be seen as providing an outline guide to be further confirmed and refined through more focused research.

Second, the nationwide lockdown imposed across Iraq in mid-February curtailed the overall scale of the field research, including by preventing us from gathering any useable field data from one of our seven priority governorates (Erbil). Furthermore, it particularly limited our ability to interview women, who are in general harder to identify, and because the lockdown early in the data collection process therefore disproportionately impacted the number of women we could interview before all field access was lost.
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IRAQ DURABLE COMMUNITIES AND ECONOMIC OPPORTUNITIES
Political Economy Analysis Update

Analysis of the impacts of COVID-19 and the new government formation on DCEO programming

July 26, 2020
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ACRONYMS

BCJCI    Iraq Business Competitiveness and Job Creation Initiative
GoI     Government of Iraq
IDP     Internally Displaced Persons
IOM     International Organization for Migration
ISIS    Islamic State in Iraq and Syria
KDP     Kurdistan Democratic Party
KII     Key Informant Interview
KRG     Kurdistan Regional Government
KRI     Kurdistan Region of Iraq
NGO     Non-Governmental Organization
OPEC    Organization of Petroleum Exporting Countries
PEA     Political Economy Analysis
PKK     Kurdistan Worker’s Party
PMF     Popular Mobilization Forces
PUK     Patriotic Union of Kurdistan
SME     Small and Medium-sized Enterprises
SOE     State-Owned Enterprises
UN      United Nations
UNDP    United Nations Development Program
UNHCR   United Nations High Commissioner for Refugees
1. INTRODUCTION

In April 2020, Chemonics International completed a country-wide Political Economy Analysis (PEA) that provided a baseline set of findings, analytical conclusions, and programmatic recommendations to inform the Durable Communities and Economic Opportunities (DCEO) project. This update is meant to:

1. build on the findings of the baseline PEA by providing analysis of key contextual changes that have impacted Iraq’s political economy between April and July 2020;
2. help inform the project’s geographic focus by exploring governorate-specific political economy descriptors; and
3. illuminate opportunities, challenges and considerations for DCEO in designing the project approach to supporting the private sector and community cohesion at this point in time.

This PEA update was conducted between June 26 and July 22, 2020 and is based on information collected and analyzed from 36 key informants from DCEO’s selected governorates of focus. Key informants were mostly Iraqi political analysts, activists, camp managers, and non-governmental organization (NGO) workers or business owners in different sectors. A small number of interviewees (4) were international United Nations (UN) officials or NGO workers. In addition, information from more than 60 secondary sources was included in this analysis.

1.1 MAJOR DEVELOPMENTS IN IRAQ’S POLITICAL ECONOMY SINCE APRIL 2020

Two important events have impacted the Iraqi political economy since the publication of the baseline PEA report in April 2020: the coronavirus pandemic and increasing prevalence of COVID-19 cases and the formation of a new government by Mustafa al-Kadhimi, former director of the Iraqi National Intelligence Service. As of July 22, 2020, there were 99,865 COVID-19 cases in Iraq, the vast majority in Baghdad (33,900), with Sulaymaniyah and Basrah governorates reporting 7,900 and 7,500 cases respectively. The nationwide lockdown that was imposed on March 17, 2020 appeared to have effectively curbed cases in the initial stages, but economic pressure on the millions of Iraqis who depend on daily wage labor combined with Iraq’s lack of capacity to effectively enforce lockdown measures, has resulted in rapid growth in the number of cases, particularly since June. According to simulation models run by the Ministry of Planning, poverty levels are expected to rise from 20 percent in 2018 to 32 percent, attributable to the economic impact of COVID-19.1

Compounding the economic challenges, COVID-related decrease in demand for oil and a conflict between Russia and Saudi Arabia in the Organization of Petroleum Exporting Countries (OPEC) translated in a sudden drop in oil prices from $50 per barrel to $20 per barrel. This has has resulted in a significant budget deficit for the Government of Iraq (GoI) and translated to delays in payment of public sector salaries, exacerbating the economic fallout due to the coronavirus lockdown measures. In May, the government only saw $2 billion in oil revenues, less than a third of what it needs to keep the government running.2 The new government has sought to reduce spending by implementing austerity measures on its massive state welfare packages that constitute something of a social safety

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1 These are: Basrah, Baghdad, Erbil, Dohuk and Ninewa.
net to already economically stressed Iraqis. The austerity measures were met with protests in Baghdad and other southern cities where public servants demanded their full salaries and some blocked the Baghdad-Basrah highway. The closure of Iraq’s border with Iran in an effort to contain the pandemics has shown in stark relief the Iranian penetration of the Iraqi economy and particularly the agriculture sector. Protected by the border closures, Iraqi products have become abundant in the markets.

Finally, on May 7, 2020, Mustafa Al-Kadhimi was appointed as the new Prime Minister after five months of political stalemate. Al-Kadhimi’s first months in office have been characterized by his attempts to rein in Iranian-backed militias, perhaps, at least in part, as an effort to preserve relations with the United States and to increase government revenues from the corruption-riddled border crossings with Iran. While some political analysts remain skeptical of Al-Kadhimi’s willingness and ability to control these militias and see him as yet another face of the old guard⁴, others view him as “more independent” than previous prime ministers and are approaching his rule with cautious optimism.⁵

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⁴ A political analyst for UNAMI commented, “The factions agreed that he will only be in office for one year… he comes during a time when the Government doesn’t have any money to pay salaries, so how can we expect him to do anything different? The factions are beyond his control. I don’t think he will be able to do anything different and feel disappointed with him. Plus, he started bringing back old, corrupt politicians.”

⁵ Three analysts interviewed believed Al-Kadhimi to be “more independent” than his predecessors and commented that his actions against militias have won him popularity. One said, “Every time he makes a move
Below, the impact and implications for DCEO of the coronavirus pandemic and the ascendancy of Mustafa Al Kadhimi are examined in more detail.

2. IMPACT OF COVID-19 ON IRAQ’S POLITICAL ECONOMY

In mid-March, the Government of Iraq (GoI) and the Kurdistan Regional Government (KRG) imposed federal lockdowns that mandated the closure of non-essential businesses, imposed curfews and closed both international borders and inter-governorate borders, severely restricting the movement of people and goods. As of mid-July, most land crossings were open for some commercial transit, but closed to passenger travel. Airports are open for cargo planes and periodic charter flights. In reality, enforcement of measures to combat COVID-19 across the country have been inconsistent and erratic, varying widely by governorate.

COVID-19 has dramatically impacted Iraq’s political economy, primarily in negative ways, but with arguably positive effects too. The sudden drop in oil prices due to decreased demand following the imposition of lockdowns internationally created a significant deficit in the Iraq’s public budget. Since 6.5 million Iraqis receive some form of government salary and/or social security benefits, the reduction in GOI capacity to meet the public sector payroll and benefits obligations has and will continue to substantially diminish overall purchasing power. Austerity measures introduced by the government to address the deficit will inevitably further reduce incomes. For example, the measures announced by the government on June 17 included cutting the monthly disbursements to ex-political prisoners who fled Saddam Hussein’s regime and are living in Rafha, Saudi Arabia as well as limiting pensions to one per person, ending a previous practice of double-pension paying for people who were receiving both a government pension and a former political prisoner pension.6

Despite the fact that any cuts to government spending are deeply unpopular and these measures were blocked by Parliament,7 Al-Kadhimi’s finance minister Ali Allawi has said he plans to propose a full reform plan to parliament within three months, including austerity measures that could last two years.8 Although these changes may be a necessary response to the pandemic-induced budget crisis, it remains to be seen whether Al-Kadhimi’s government will have the political will to push through these unpopular reforms and whether the negative impact of reduced purchasing power and spending has unintended knock-on impact across the economy.

As lockdown measures have eased in many countries in June and July, oil prices are slowly climbing again. Despite having agreed a production cut as per an OPEC+ agreement to stabilize prices, revenues for June stood at $2.86 billion, up almost $800 million from May’s $2.09 billion. As of July 22, Iraq was still producing above the OPEC+ agreement level, but said it was “committed” to complying.9 Although the budget deficit may slightly improve in the coming months, oil exports will

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7 Ibid.
still be far below the planned barrel price, meaning it is likely that salary delays and reductions will continue for the foreseeable future.

Depression of consumer demand has been a natural consequence of reduced household incomes as a result of late and/or reduced payroll and benefits to the large number of Iraqis whose household income is wholly dependent on government employment. This dependence and its attendant risks were explored in some detail in the DCEO April PEA. Sluggish consumer demand has, in turn, compounded the deleterious effects of the COVID-19 lockdowns on business with reduced revenues and significant employee lay-offs for small and medium-sized enterprises (SMEs). According to a study of 456 small and medium-sized enterprises (SMEs) completed by the International Organization for Migration (IOM) in June, the average weekly revenue declined by 79 percent and the number of paid employees was reduced, on average, by 40 percent.10

COVID-19 has also had clear implications for relations between Iran and Iraq, exposing the breadth of Iranian economic control and highlighting political leaders who are willing to put Iranian interests before Iraqi public health concerns. Analysts at the Carnegie Center argue that “the pandemic is widening the gap between political forces susceptible to Iranian influence and those seeking a more independent Iraqi policy.”11 As borders open up again for trade, it remains to be seen whether this trend was a fleeting result of the pandemic or whether components of it will endure.

While COVID-19 has had an overall negative effect on economic activity in Iraq, some analysts believe there could be a “silver lining” of increased economic self-reliance, particularly in the agriculture sector, which has been dominated by imports from Iran and Turkey. According to an article published by France 24 on June 14, despite having to sell at lower prices, Iraqi farmers reported successfully marketing their production locally for the first time in years.12 This was corroborated by multiple respondents of this study who said that COVID-19 had reignited a popular consciousness around buying Iraqi goods that had initially emerged as a result of the October 2019 protests against outsider interference in Iraqi affairs.13 Iraq is under significant pressure to reopen the rest of its borders and fully resume trade with Iran,14 but at the moment there is potential for Iraq to capitalize on the opportunity the pandemic has presented to regain more control of its non-oil industries, and possibly even to use the momentum to diversify its economy.

3. MUSTAFA AL-KADHIMI AND ECONOMIC SECURITY

The formation of a new cabinet on May 7, 2020 with Mustafa al-Kadhimi as the Prime Minister is also an event of tremendous potential consequence to Iraq’s politics and economy which has occurred since the DCEO PEA Baseline report April 2020. A lawyer by trade, journalist, and former director of the Iraqi National Intelligence Service, Al-Kadhimi is widely viewed as a pragmatist who is able to maintain good relations with players across the Iraqi political spectrum. Other analysts,

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11 Carnegie Center, “Iraq’s Silver Lining Amid the Pandemic”, 7 July 2020.
however, caution that he is part of the old guard who, even if his intentions are genuine, will ultimately be unable to implement reforms within the current political system.  

The appointment of Al-Kadhimi, who is seen as relatively less linked to Iran than his predecessors, could put tension on Iran-Iraq political and economic relations already strained by COVID. Since his appointment, Al-Kadhimi has been signaling his interest in reining in the Popular Mobilization Forces (PMF) which gained power and influence during the rule of his predecessor, Adil Abdul-Mahdi. On June 26, Al-Kadhimi ordered a raid on a Kataib Hezbollah headquarters and weapons cache in the Dora district in southern Baghdad, sending the message that his government is not afraid of such confrontations. However, this move was met with strong backlash from the militias who paraded around the Green Zone burning American flags and photos of Al-Kadhimi and successfully demanding the release of the detained militia members.  

Al-Kadhimi has a delicate balancing act in which he must appease protesters who demand less foreign interference in Iraq while attempting to navigate the tensions between the United States and Iran. While the deeply complex nature of his position will likely continue preventing him from making any fast, sweeping political moves or reforms, his initial steps seem promising.

If successful, efforts by the new government to assert the power of the state military and the Counter-Terrorism Forces over the PMF could have direct economic benefits. One concrete example of this would be if the central government were able to gain full control of the border crossings. In a country that imports billions of dollars’ worth of goods from Iran on a yearly basis, a clear source of non-oil revenue should be customs tariffs. According to a member of the Parliamentary Finance Committee, the government loses ten billion dollars annually due to corruption at the border crossings. Iraq’s borders are often described as “porous”. In practice this means there are dozens of informal border crossings controlled by various tribes and militias who at least partially fund themselves through extorting companies seeking to import goods.

Better government control over Iraq’s entry points could translate to implementation of clearer economic policies. As it has stood, it has been very difficult for Iraq to control or protect its economy because much of importation is beyond the Government’s oversight. Al-Kadhimi has tweeted frequently about the illegal economic activities of the militias and political parties, vowing to impose the laws to break their corrupt economic activities. On July 12, Al-Kadhimi appeared at the

15 In an interview, a think tank analyst said of Kadhimi, “He doesn’t come from strong political bloc. Whenever he does something that harms their interest, [the other bloc] turn against him. He needs to lobby for support among them.”
reopening of the Mandali border crossing in Diyala and said his visit was “a message to all corrupt people that they would not have a foothold at the border crossings”. The coronavirus has made the issue of border crossings more acute, and the Prime Minister at least wants to seem willing to take on the militias. This could be an opportune time to increase control over the border crossings and provide space for Iraqi goods to compete in the domestic market. The sanctions and cost of COVID upon Iran has, furthermore, weakened their hand enough that they have been forced to reduce payments to the top four militia groups in Iraq.

4. GOVERNORATE UPDATES

This section takes a closer look at the impact of COVID-19 and the new government on the political economy, as well as any other relevant governorate-specific developments that DCEO should consider in proceeding with implementation.

4.1 BASRAH

As of July 22, Basrah had reported 7,500 cases of COVID-19. According to local sources, the Basrah Police Command and Emergency Departments are enforcing a lockdown in the city center, local police in the sub-districts, and the army is patrolling the highways and out-roads. Curfews are often announced at the last minute and are often imposed for weekends or holidays. They are inconsistently enforced and possibly enforced along patronage lines, where those with connections to those responsible for enforcement are able to get around requirements. This has led to complaints from many citizens and business owners. One shop owner interviewed by local news outlet, Al-Sumaria, said, “Shops in other areas of Basrah are open, but in my area shops aren’t even allowed to make deliveries.” A respondent in Basrah confirmed, “Businesses stay open [during the lockdowns] based on their connections with the police command, intelligence and national security.” Lockdown measures seem to be at best inconsistent nuisances to get around for business owners and at worst a tool to reinforce patronage.

Economic shocks due to COVID-19 have hit Basrah particularly hard, as Basrah is one of Iraq’s poorest governorates. A very high percentage of the population depends on daily wage labor, meaning restrictions on movement and pauses on projects are highly destabilizing for people who are amongst the least resilient and most vulnerable. A business owner in Basrah said, “The soldiers and police officers cannot impose movement restrictions on [daily workers] because then it would have been a crisis of hunger and not corona.” According to IOM, SMEs in Basrah reported the highest reductions in both employment and productivity of any governorate. Unsurprisingly, lockdown measures in Basrah are being ignored or worked around because more pressing economic concerns override the potential impacts of the virus.

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19 Reuters, “Coronavirus and sanctions hit Iran’s support of proxies in Iraq”, July 2, 2020. According to this article, Iran reduced these payments to between $2 million and $3 million from $4.5 million to $5 million per year.
21 KII with Basrawi UN worker, July 2, 2020.
COVID-19 has had arguably positive and negative impacts on Basrah’s agriculture sector. Since industrial farming is still uncommon in Basrah and families typically work on small farms together, key informants observed that COVID-19 movement limitations did not impact agricultural production as much as it would in more industrialized places. Moreover, it appears that border closures due to COVID-19 may have helped limit competition Basrawi farmers face from foreign agricultural products. Local reporters interviewed the owner of an ice cream company who said the work of his company grew because no ice cream was being imported from Iran. According to the same report, fishermen in Shatt al-Arab reported similar growth in business because no fish was being imported from Iran and Kuwait. This trend is in keeping with a well-documented nationwide trend of border closures being a boon to local production.

However, movement restrictions and closures between governorates have presented challenges to agriculture and meant that farmers have been unable to enjoy the full benefit of better protected markets. Being unable to easily transport products between governorates has forced agricultural and livestock producers to sell at low prices on the local market. One Basrawi resident noted the price of the standard bulk purchase unit (20 kilos) of vegetables decreased from $15 to $5 because farmers are forced to sell in hyper-local market. Similarly, buffalo herders in the historic marshes outside of Basrah who sell milk and yogurt reported in June that the price of 30 liters of buffalo milk had dropped from $28 to $12, and that many were being forced to sell their animals to survive. While COVID-19 restrictions may have limited competition, not being able to sell products in other parts of Iraq has ultimately harmed many local producers.

COVID-19, along with the ushering in of a new government highlighted both the need for more support to modernize agriculture, as well as the need to control the illegal entry of goods; and nowhere is this more apparent than in Basrah. The GoI publicly admits that it has limited control over Basrah’s ports and border entries, and since his appointment, Al-Kadhimi has made efforts to re-assert control. During a 15 July cabinet session held in Basrah, Al-Kadhimi announced the re-appointment of four of the managers and their assistants working at the Um Qasr Port and stressed that “legal measures should be taken to prevent financial abuse at the Safwan border crossing with Kuwait”. At this session, he also reiterated his intention to rein in militias by banning “parties and tribes” from carrying weapons, having ordered the Iraqi army to control the spread of weapons. In addition, he directed work to begin on several infrastructure projects in the province including the Great Basrah Water Project, which is set to be the primary source for potable water in Basrah amid water shortages.

The fact that the announcement about limiting militias’ control was made in Basrah is no coincidence. Statements such as these are in keeping with Al-Kadhimi’s efforts to appease the

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23 KII with UN official from Basrah, 9 July 2020.
25 KII with Basrawi business owner, 5 July 2020.
27 Shafaq, “After 4:00, border crossings are outside the control of the Iraqi Government”, 19 May 2020.
28 Skypress, “Iraq reveals a plan to support domestic products and prevent smuggling and entry of unofficial goods”, 17 July 2020.
29 Al-Jazeera, “Despite protests, Al-Kadhimi issues important decisions from Basrah”, 16 July 2020.
30 DCEO weekly report, July 10-16.
protesters and his alleged plans to increase state revenues and protect local production through tackling corruption at the border crossings. As Iran has been forced to cut funding to many of its proxy militias due to the economic impact of sanctions and COVID-19\(^{31}\) forcing militias to increasingly provide for themselves, control over these crossings is likely to remain a key political and economic issue in Basrah and the rest of Southern Iraq for the foreseeable future.

It seems protesters are both skeptical of Al-Kadhimi and waiting to see what he will do. Small protests broke out on May 11 following Al-Kadhimi’s appointment. The protesters demanded an overhaul of the political system and, after a protester was killed, issued a statement demanding the resignation of the Governor. Smaller protests occurred periodically throughout June and July with similar demands. Al-Kadhimi has made efforts to appease protesters by ordering the release of detained demonstrators and by promising to hold perpetrators accountable for violence during the 2019 rallies.\(^{32}\) However, it remains to be seen whether he will be able to secure meaningful support from the streets.

### 4.2 BAGHDAD

As Iraq’s capital and most populous city, Baghdad has the highest rate of COVID-19 cases nationwide. As of July 22, Baghdad had nearly 34,000 cases and 97 deaths. As in other parts of the country, containment measures appeared to be initially effective but slowly eroded as the economic consequences became more pronounced. Officially, as of July 22, restaurants, cafes, and entertainment facilities were only allowed to open for delivery services, and essential stores such as bakeries, groceries and pharmacies remained open. However, these guidelines were only being enforced sporadically, and it has ultimately been left to individual businesses in Baghdad to set their own policies and procedures for COVID-19 control.

COVID-19 is particularly difficult to contain in Baghdad’s poor, overcrowded neighborhoods. Although COVID-19 data is not available at the neighborhood level, reportedly the virus is spreading the fastest in the crowded neighborhoods of Karkh and Rusafa. For this reason, since April, there have been sporadic GoI efforts to impose full lockdowns on these areas. According to a Baghdad-based political analyst, many people in the poor neighborhoods were either unwilling or unable to respect social distancing requirements, which led to the June spike in cases. “When you watch TV and the anchor asks people why they’re not wearing a mask, they say 1) it [COVID] doesn’t exist and is an American conspiracy or 2) they have families to feed and no alternative income to daily wage work.” A Baghdad-based UN official corroborated this, pointing out how those living in rural areas or slums like Rusafa, are unable to quarantine because houses are small and overcrowded.\(^{33}\) It is likely that cases of COVID-19 will continue to increase in these areas for the foreseeable future and that little can be done to contain it. As in many countries, COVID-19 is disproportionately affecting Iraq’s poorest, who must work in order to survive. In addition to killing many residents of these impoverished areas, COVID-19 is likely deepen the presence of multi-dimensional poverty.

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\(^{33}\) Interview with Baghdad-based UN official, July 8.
Lockdown measures have been imposed, lifted, then re-imposed numerous times with little warning. According to the owner of a popular Baghdad restaurant, the constantly changing restrictions has been detrimental to many food service businesses that lose out on stocks. “I have meat and vegetables worth around $30,000. I had to give it away because I couldn’t use it. Then suddenly the government says we can deliver, so I opened. But then they didn’t allow bikes in the street, and then they started the odd and even license plate altering. So should I close or open?” They are also being selectively enforced: one respondent said, “If I go out with my family or my wife, the situation will be different because I have my family. But if I’m alone they will question me and hold me accountable.” There are no clear directives or enforcement patterns for the COVID-19 response, which has led to the increase in cases and also forced many businesses to close.

Because of the low trust in the government, pressing economic needs, and a population habituated to patronage and favoritism, COVID-19 control measures are being perceived by many, not so much as a life-saving measure, but rather as yet another government-imposed hoop through which to jump. One respondent observed that in order to skirt the measures, some shops began selling trivial amounts of food items in order to qualify as “essential businesses”. Another said, “In my neighborhood, there’s a guy who runs a furniture shop. He started selling foodstuff in the building so he can keep his place open during the day.” France 24 reported that many shop owners were opening their shops in secret, but still struggling to find customers.34 Respondents in Baghdad shared the observation held in other parts of the country that the border closures led to more Iraqi products being available in the market.35 One observer commented, “Since the beginning of the demonstrations until now we have seen more Iraqi products in the market, like dairy. When we closed the border with Iran and Turkey, we started to see more Iraqi products.” This builds on momentum built during the protests, when activists in Baghdad led campaigns to boycott imported goods.36 There is a growing conscientiousness around the importance of buying Iraqi products that began during the protests and has been buoyed by seeing how closing Iraq’s borders during COVID-19 led to more local products on the market.

Corruption runs very deep in some Baghdad businesses. A Baghdad business owner described how businesses navigate a complex patronage environment where one must pay rents to various armed groups in order to do business. This respondent said, “Many restaurants are not real restaurants, or that’s not their main purpose. They’re for money laundering. Militias will expropriate buildings belonging to people who left Iraq, use the buildings of their supporters who don’t charge rent, or force owners to hand over control and don’t pay rent. If someone doesn’t comply, the group will likely try and use a governmental process to close the restaurant, such as claiming the business is not compliant with a specific policy. If these types of efforts don’t work, then the groups may resort to violence.”37 Although efforts are being made at the level of the individual consumer, the broader structure is one in which rent payments to non-state armed actors is normalized as incidental.

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35 KII with Baghdadi political analyst, July 4, 2020.
expenses of doing business. Of course, this corruption also opens avenues to flout COVID related attempts to limit people in public space, exacerbating inequality and perceptions of patronage.

Some analysts have also observed growing Iranian influence in Baghdad’s private sector. One study respondent provided the example of dairy companies: “We have two or three brands of dairy we produce here in Iraq. On the surface you see an Iraqi guy investing, but there’s an Iranian guy with Iranian money behind it.” While there may be a growing consciousness around using economic power to protest foreign interference, the forces protecting the interests of foreign actors in Iraq are still very strong.

Although there was a relative lull in protests in the first month of the COVID-19 lockdown, protests have picked up again since late April. Some protests, such as those following Al-Kadhimi’s appointment, have been under the same banner of the October 2019 protests. However, government employees who were not paid or whose entitlements were cut have also turned out in significant numbers.\textsuperscript{38} Though probably at lower numbers due to COVID-19, it is likely that protests in the capital will continue should Al-Kadhimi fail to meet their demands and over the plethora of more acute economic concerns arising from the economic fallout of the pandemic.

4.3 NINEWA

As of July 22, there were no reliable figures on COVID-19 cases in Ninewa governorate. Because of the persistent closures of Ninewa’s borders with Turkey and Syria as well as closures with the KRG and other governorates, it is likely that cases in Ninewa are not as high as in southern and central Iraq. While cases are almost certainly higher than the reported figures, there have been no reports of hospitals being overwhelmed in Mosul or surrounding areas, suggesting things are still within a manageable range. Testing and care for people in Ninewa is only available in Mosul, meaning many rural residents of Ninewa would have to travel for hours in order to be tested or receive treatment. In Mosul, testing is being done at the al-Shifaa hospital established by the WHO in the eastern district of the city.

Restrictions on inter-governorate travel continue to limit business movement. With some exceptions, travel between the KRI and federal Iraq was still restricted as of mid-July and this negatively impacts labor and material supply chains. Negative test results and 14-day quarantines are now required for travelers between the KRI and federal Iraq, although the exact implementation mechanism is, like most COVID-19 management measures in Iraq, opaque. The closures particularly impact many Kurdish, Christian and Yazidi workers who commute from villages in the Ninewa Plains to Dohuk or Erbil for work.\textsuperscript{39} Road closures have impacted prices of agricultural items, since many farmers who would normally export their goods to other parts of the country are forced to sell on the local market. At the time of reporting, the price for a kilo of tomatoes was $0.10, down from $0.50-0.75 before COVID-19.\textsuperscript{40}

\textsuperscript{39} KII with an NGO worker in Bashiqa, July 21, 2020.
\textsuperscript{40} Ibid.
As is the case throughout Iraq, the lockdown in Mosul has been inconsistent. Sometimes the local Crisis Cell provides directives that conflict with directives from the federal government. Measures are imposed suddenly and randomly, creating a very challenging environment for businesses, denying them any form of predictability and therefore undermining coping responses. The Governor has occasionally imposed full-weekend lockdowns in order to limit common weekend activities such as weddings, family visits and sports. However, despite a de jure curfew, as of mid-July respondents reported the de facto situation inside Mosul and in surrounding areas like Bashiqa, Al-Qosh, and Bartella had “almost returned to normal” with some social distancing and mask requirements in place for certain private businesses.

Respondents in Mosul and the surrounding areas reported that many business owners find ways to circumvent the lockdown measures due to livelihood concerns. One respondent in Bashiqa said, “My brother owns a café. In the first months of COVID-19, he used to open the back door, turn off the lights, and put up curtains to try and hide that he was open. He got caught by the police two or three times, but he had to keep working because he had to provide for his family.” Furthermore, some respondents felt that lockdown measures have been selective, where if a business owner has the right connections with the local police he or she is able to get around them and stay open.

Construction works in Mosul city were briefly on pause during the initial lockdown period, but have picked up again. Because many construction materials such as concrete, marble, bricks and quarried rocks are available on the local markets, these supply chains were not badly interrupted. Furthermore, it appears Ninewa Governor al-Jubouri has been determined to push on with reconstruction projects in the city. According to UN officials, the government in Ninewa felt continuing reconstruction works, particularly for health centers and infrastructure, was too important and has issued exemptions from the road closures.

Border closures and demand for medical products due to COVID-19 has had some impact on the Mosul industrial sector. Notably, the Al-Waladi textile factory in Mosul, which was heavily damaged during the war and then partially rehabilitated by United Nations Development Program (UNDP), has begun producing medical masks and hospital gowns. There are other reports of State-Owned Enterprises (SOEs) across the country, namely textile factories, being re-appropriated to make COVID-19 medical equipment. While aspects of the current circumstances would present opportunities for increased private sector activity, it would be difficult for private companies to compete with the better equipped and capitalized SOEs.

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41 Ibid.
42 KII with an NGO worker in Mosul, 20 July 2020.
43 KII with a UN official working in Mosul, 14 July 2020.
44 As per information obtained from UNDP.
45 Bawabaa, "Iraqi factories produce more than 12 million masks", 22 April 2020.
Road closures and job losses due to COVID-19 have reportedly led to a spike of returns to Sinjar, which had previously been very low. Between 8 June and 16 July, IOM’s Displacement Tracking Matrix reported the return of 10,165 individuals to Sinjar and Al-Baaj districts. According to UN officials working in the area, many of the returnees were traveling back and forth from Dohuk to Sinjar to farm, but were forced to return permanently due to the road closures. Others who were employed in Dohuk, returned when they were laid off their jobs in the shrinking COVID economy.

Although Sinjar’s post-conflict economy is still largely agricultural, the return of significant numbers of residents may present an opportunity to rebuild other industries. Before the conflict, the Sinjar economy was more diverse and included small factories producing goods like aluminum, gypsum and ice cream, most of these value chains were heavily damaged by ISIS and have not yet been restored. Moreover, because previously there has been such limited return, business owners who did return struggled with a lack of demand. As more residents return to Sinjar, there is potential for agricultural production to increase and other small businesses may begin to reestablish as demand increases.

Little is known about COVID-19 in other parts of Ninewa such as Tel Afar and the primarily Arab villages around Hatra, Hamam Al-Alil, and Mahalabia. However, according to a news report on July 22, two cases were identified in Hamam Al-Alil camp, raising concerns that COVID-19 may start spreading in camps in these areas. Since testing and treatment is only available in Mosul, it would seem likely these areas have unreported cases. It is also worth noting that these areas have been chronically underserved by reconstruction efforts, according to a UN official who works there, and are therefore highly vulnerable.

Al-Kadhimi has yet to prove himself to Moslawis, although some analysts have ventured to say sentiments towards him are more positive than those towards his predecessors. He paid his first visit to Mosul on June 10, where he met with the Council of Ninewa Tribes to discuss their demands and grievances. These included new bridges, compensation for homeowners and businesses whose properties were destroyed in the fighting, and the reconstruction of religious sites, hospitals, and

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66 IOM Iraq, Displacement and return to Sinjar and Al-Baaj districts, 16 July 2020.
67 KII with a UN official working in the Nineewa Plains, 16 July 2020.
51 Carnegie Center, “Iraq’s Silver Lining Amid the Pandemic”, 7 July 2020.
clinics.\textsuperscript{52} He also met with Christian leaders in Bartella and Hamdaniya, tweeting “Christians are an authentic part of Iraq and we lose a part of our soul when they migrate out of the country.” The Ninewa Government has reportedly asked the Minister of Finance to allocate $17 million for compensation schemes, but has yet to receive funding. According to analysis put forward by the Carnegie Center, the pandemic response and Al-Kadhimi’s “tough on militias” stance may be winning him trust in Sunni areas such as Mosul and surrounding areas, but he will need to follow up on these promises to solidify support in these areas.

4.4 ERBIL

Overall, the COVID-19 response in the KRI has been better than that of federal Iraq. The KRG established a hotline early in the pandemic and has relatively high testing capacities at approximately 1,700 tests per day. However, like the rest of Iraq, Erbil saw a spike in cases beginning in early June as the lockdown measures were relaxed. As of July 22, more than 3,000 people had contracted COVID-19 in Erbil, more than triple the cases one month ago. Officially there is still a curfew and business limitations in place, but according to sources, the lockdown is no longer being enforced. Some government offices and some businesses are implementing measures such as taking temperatures, mandatory masks, and social distancing, however.

As the trade hub of the KRI, closures of roads to and from Erbil as well as the airport closure have been particularly detrimental to businesses across the Region. The Erbil airport was closed for passenger travel on 17 March and has remained closed apart from periodic charter flights as of July 22.\textsuperscript{53} As the main international airport in the KRI, this closure has driven up the cost of importing materials across the Region. One owner of a clothing store in Dohuk said the price of importing goods via the Erbil airport had doubled from $5 to $10 per kilogram since COVID-19 began.\textsuperscript{54} However, as of July 22 the KRG was reportedly considering reopening borders between its three governorates as well as the airport, requiring negative COVID-19 test results and a 14-day quarantine upon entry.\textsuperscript{55}

Delays in paying salaries, due to the fiscal deficit resulting from the March drop in oil prices, are another pressing issue affecting the Kurdish regional economy and its relationship with Baghdad. COVID-19 may have sped up the process of reaching a budget agreement, as Kurdish officials stated there was “no other alternative to the crisis than agreement on an urgent solution with Baghdad.”\textsuperscript{56} Indeed, after a series of visits by the Kurdish delegation to Baghdad (and a series of internal squabbles between PUK and KDP factions), on July 1 the KRG came to an agreement with the GoI to send oil revenues from the KRI in exchange for Baghdad handing over the 17 percent of the budget allocation the KRG was due, enabling the payment of one outstanding civil servant salary.

\textsuperscript{52} New York Times, “\textit{In Iraq, a new prime minister takes stock of his bloodied land}”, 16 June 2020
\textsuperscript{53} However, according to local news such as this article, the airport may open on 23 July.
\textsuperscript{54} KI with business owner, 6 July 2020.
\textsuperscript{56} Al-Araby, “\textit{The financial crisis is pressuring the Kurdistan Region: A new delegation visits Baghdad to resolve the outstanding issues}”, 22 June 2020.
As such, civil servants received their January 2020 salaries in April and February salaries in July, and the February salaries were reduced by 21 percent. One Kurdish analyst said COVID-19 was contributing to the growing disillusionment many Kurdish citizens feel toward the KRG and that the pandemic was being used as “yet another excuse” not to pay government salaries. Lack of consumer purchasing power resulting from the non-payment of government salaries is likely to be a salient negative factor for the private sector and contribute youth disillusionment with the KRG for at least the medium term.

The agriculture sector has featured front and center in the KRG’s political economy discourse since COVID-19 appeared in Iraq. Across the KRI, agricultural products went to waste when farmers who had previously sold their produce in other governorates were unable to sell their stock on the local market. On July 6, farmers threw their tomatoes onto the streets of Erbil in protest of the low prices resulting they were getting. Some protesters took this a step further, protesting the lack of support for finding international markets to sell their products. Despite the limited market options, there is some evidence that more Erbil residents may be turning to farming in response to economic uncertainty. According to statistics from the District Agricultural Administration of Soran, a mountainous region northeast of Erbil City, the number of farmers working in mountainous areas has increased to 1,600, up from 900 last year. If more workers hope to farm while prices remain low, the KRG will face increasing pressure to increase subsidies for agricultural production.

As in central Iraq, there may be a growing consciousness in the KRI around the importance of agricultural self-sufficiency. In response to the farmers’ protests, the KRG announced it would reopen the Harir tomato paste factory and buy from the farmers in bulk, although on an unspecified timeline. Additionally, in mid-July, the KRG Investment Board and Ministry of Agriculture and Water Resources announced that it has been developing plans for over 100 new agricultural projects across the KRI. Mohammed Shukri, the Head of the Board, said this was in order to become as “food independent as possible” after seeing the effects of the coronavirus and previous embargoes imposed by Baghdad in response to the 2017 referendum. A “buy Kurdish” mentality may be emerging. A respondent in Erbil said, “Many people here in Erbil, my family included, are starting to refuse buying Iranian products.” COVID-19, along with the protest movement, may end up spurring along industrialization and diversification of the KRI’s agriculture sector.

4.5 DOHUK

Of the three Kurdish governorates Dohuk has reported the fewest cases of COVID-19, perhaps due to being the farthest away from Iran, the likely major source of COVID-19 infections in Iraq. As of 22 July 22, Dohuk had less than 80 active cases. Movement restrictions between governorates and on the border with Turkey were still in place as of mid-July. Dohuk’s Fishkhabour and Ibrahim al-Khalil border crossings remained partially closed and non-essential travel between governorates was

58 KIL with Kurdish political analyst, 7 July 2020.
62 Kurdistan 24, “Kurdistan Region planning over 100 new projects to develop agriculture”, 19 July 2020.
formally banned. As of July 22, the Dohuk local government had lifted the lockdown, meaning some economic movement may soon return – although the price may be the potential for increases in cases.

Despite initial fears of the virus spreading in Dohuk’s 11 formal camps for internally displaced persons (IDPs) and 2 Syrian refugee camps, as of mid-July there had been no confirmed cases in the camps. However, according to the United Nations High Commissioner for Refugees (UNHCR), camps in Zakho and Sumeil were at particularly high risk of COVID-19 exposure due to failure to enforce movement restrictions and due to higher concentrations of elderly, persons with disabilities and those with chronic illnesses.63 While COVID-19 may not have hit Dohuk’s camps yet, the risk of this happening remains high as cases continue to increase.

As discussed in the Ninewa Update, COVID-19 has been a significant factor in the return of Yazidi IDPs from Dohuk to Sinjar in June and July, since many IDPs who had been working in the city lost their jobs.64 According to a Yazidi community leader interviewed by Reuters, “Young men from his community who used to earn up to $17 a day working at restaurants and factories in Dohuk can no longer find work because of the lockdown’s impact on the economy.”65 While more than 10,000 individuals left Dohuk since June, more than 300,000 IDPs and 87,000 Syrian refugees still remain, but the trend of return may continue to grow. Job loss and reductions in humanitarian assistance due to the COVID-19 recession in donor nations are disproportionately affecting Dohuk’s large population of IDPs, and may continue pushing them to return, even though services and infrastructure are still largely destroyed in many of their origin locations.

As is the case in Erbil, not having received government salaries has compounded the economic downturn in Dohuk. Public sector employees had only received two salaries in seven months and at a reduced rate, limiting their purchasing power. Business owners interviewed in Dohuk described sustaining significant losses due to the lockdown measures and the delayed salaries. One woman who runs a nursery in Dohuk described how before COVID-19 she had 85 children in her nursery while now she only has 8, and that she hasn’t received payments from many mothers who are government employees.66 Accounts such as these are widespread due to the fact that half of Dohuk’s population is on government salaries.

The latest bout of tensions between Turkey and the KRG has the potential to impact Dohuk’s political economy. These tensions flared up in June when Turkey launched a new military operation against the Kurdistan Workers’ Party (PKK), which it considers a terrorist group, in the Zakho and Amedi areas of northern Dohuk. In addition to these areas, the Turkish military has targeted the Qandil Mountains, Sinjar and a refugee camp for Turkish Kurds in Makhmour, Erbil governorate. According to a map released by the Turkish communication directorate on July 6, Turkey had set up 24 new bases throughout the month of June.67 At least one civilian was killed in these operations.68

63 UNHCR, COVID-19 Camp Vulnerability Index, 15 June.
64 Reuters, “Displaced Yazidis head back to Sinjar as coronavirus lockdown bites”, 6 July 2020.
65 Ibid.
66 KII with Dohuk business owner, 7 July.
67 Al-Monitor, “Baghdad’s row with Ankara could benefit each side”, 8 July 2020.
68 Al-Jazeera, “Turkish airstrikes kill civilian in northern Iraq”, 19 June 2020. Official numbers are contested, and range as high as 7.
Some analysts believe the emboldening of Turkish military operations in the KRI could serve to strengthen Al-Kadhimi’s and the central government. Al-Kadhimi, who has a good relationship with the KRG, is under pressure to respond decisively to this encroachment, but he cannot risk straining his ties with Turkey, which wields enormous economic influence. How his administration responds to the current situation along the Dohuk border will be a key determinant of Iraq and the KRG’s political and economic relationship in the coming months.

5. CONCLUSIONS

DCEO programming is commencing during an unprecedented time for Iraq, one that comes with serious challenges but also with unique opportunities. The pandemic has profoundly impacted Iraq’s economy, leading to significant job losses and increasing levels of poverty that will likely persist through 2021 at least. Iraq’s fiscal deficit due to oil price declines has delayed and reduced its payments to Iraq’s millions of public sector employees. This has exacerbated the effects of COVID-19 on the economy and will likely continue, despite the attempted introduction of highly unpopular austerity measures, as oil prices are still far too low to balance the budget. Considering the reduced purchasing power of a third of Iraq’s population and the widespread job losses due to COVID-19, DCEO could consider partly or fully orienting itself toward preserving jobs that would have been lost, versus creating new ones.

At a more logistical level, COVID-19 lockdown restrictions continue to hinder supply chains within Iraq due to restricted inter-governorate travel, border closures and airport closures. While restrictions are likely to be lifted in the coming months, it is unlikely that full trade movement (or

BUSINESS OPPORTUNITIES IN IRAQ’S DIGITAL ECONOMY

Like in the rest of the world, COVID-19 is highlighting the importance of the digital economy in Iraq and its potential for growth. The World Bank outlines five pillars to improving a country’s digital economy: digital infrastructure, digital finance services, digital platforms, digital skills and digital entrepreneurship. While the first two pillars are highly dependent on heavy infrastructure development and supportive government policies, there is potential for the DCEO to support in the latter three categories.

Many businesses have increasingly turned to selling their wares via WhatsApp or Facebook. It is rare for an Iraqi company to have its own website or streamlined online purchasing mechanism. Companies post their items on their Facebook pages and then send the goods with delivery drivers. According to multiple respondents, marketing strategies are often limited and delivery is done “randomly”. Businesses would likely benefit from articulating better marketing strategies and through finding ways to streamline the delivery of goods.

Delivery service applications have, unsurprisingly, seen a business boom as a result of COVID-19. The founder of DCEO’s partner 51 Labs, a business incubator based in Sulaymaniyah and Erbil, mentioned how a pharmaceutical delivery service application that had recently completed their incubation program saw downloads go up by 250 percent after it launched in the first week of March 2020. There is very likely a market for similar services in other parts of the country and for other sectors as the pandemic drags on.
the movement of human capital) will be fully restored in the near future. It is therefore important for businesses to factor this into their strategic planning for the next year.

The sporadic and unpredictable nature of the COVID-19 lockdown measures, which are announced at the last minute, are inconsistently enforced, and are likely to be further eroded in the coming months, will also continue to hinder businesses – as well the almost inevitable upick and associated costs of infection rates. Problems enforcing the lockdown are partly due to the GoI’s lack of enforcement capacity, but also a tacit recognition that many daily wage workers could go hungry as a result of strict measures. For these reasons, most citizens are not abiding by them; on the contrary, they appear to be seen as nuisances to scheme around at best and at worst yet another way for the GoI and militias to antagonize and extort businesses and reinforce their patronage. In the absence of clear government policies, it will ultimately fall to individual businesses to set ethical guidelines and procedures for handling COVID-19. DCEO should bear these realities in mind as it goes through its business selection process and develops guidelines for working with businesses.

The closure of international borders due to COVID-19 appears to have had some benefits for the Iraqi economy and highlighted the need for economic diversification. More Iraqi agricultural products began appearing on the market, but at lower prices due to farmers’ inability to transport their crops to other governorates. Both the GoI and the KRG have paid attention to this development and have at least paid lip service to improving protections on agriculture and allocating funding to further developing the sector. It remains to be seen whether they will succeed, or whether they were serious in the first place. Regardless, DCEO is launching at a time when popular consciousness around buying Iraqi goods is growing alongside recognition of the importance of food self-sufficiency, two factors that can leveraged in advocacy efforts.

Prime Minister Al-Kadhimi has only been in office for a short time, but already has made some promising commitments to rein in the militias that wield significant control over Iraq’s economy. A main focus for this is combatting corruption at the border crossings, many of which are informal and beyond government control, meaning significant customs revenues are lost and seriously limiting the Government’s oversight of goods entering the country. The importance of strengthening Iraqi rule of law and economic diversification has become more acute than ever, with a large if currently rather dormant protest movement behind these concepts, a pandemic that has made this more urgent, and a prime minister who has centered these issues in his platform. Although working within the confines of a pandemic will be challenging for the DCEO, the potential for change also appears higher than it has been in years past.

6. RECOMMENDATIONS

Cross-cutting recommendations for DCEO’s Iraq Business Competitiveness and Job Creation Initiative (BCJCI) and 100 Solutions activities:

1. Consider supporting businesses to design advertising campaigns under the “Buy Iraqi” and/or “Buy Kurdish” concept, which has currency and is critical for market growth.

2. If DCEO works with SOEs, design courses for former and/or current employees on the basics of privatized markets, since the prevailing mentality is that of working within a planned economy and there has been limited business exposure to the idea of the private sector.

3. Ensure DCEO has in-house technical and digital marketing know-how in order to advise businesses on their digital strategies, since due to the inconsistent, patchwork lockdown measures and emerging market trends it is highly likely that many businesses DCEO may work with will see building an online presence as a priority.
Area-specific recommendations for BCJCI and 100 Solutions:

1. Conduct an assessment on the economic needs of recent returnees to Sinjar, considering the recent return wave, including a specific conflict analysis. Consider assisting businesses such as restaurants, groceries and fruit and vegetable shops that are likely to start or re-start to respond to the increased consumer demand for both the Marla Fund activities as well as BCJCI.

2. Consider expanding project coverage to areas southwest of Mosul such as Tel Afar, Hatra, Hamam Al-Alil and Mahalabia, since there are opportunities for improved agricultural production and need for community reintegration in these areas.

3. Consider working with actors like UNDP and IOM to rehabilitate SOEs in Mosul and surrounding areas, as these have high potential to generate jobs. Since completely rebuilding these is beyond the scope of the DCEO, it could focus on those that were either not badly damaged during the conflict or that have received rehabilitation support from other agencies. For example, DCEO could provide necessary equipment while another agency (or the GoI) covers the structural reconstruction.

In order to account for the effects of COVID-19 on DCEO programming, DCEO should:

1. Require contingency plans for COVID-19 lockdowns as well as ethical health and safety practice criteria as part of the company selection criteria. Since government guidance is not well-enforced, ultimately it will fall to individual companies to ensure the health and safety of their employees and customers.

2. Develop short term and long term COVID-19 contingency planning guidance for different sectors. This should include procedures for what businesses should do if there is a confirmed positive case in their business as well as how they should handle the sporadic nature of the lockdown enforcement in terms of storing goods, employee salaries etc.

3. Try to ensure selected businesses are as compliant with lockdown policies as possible, since many businesses are finding creative ways around it and that could have a negative impact on the DCEO’s reputation and government relations.
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