

Iraq Economic Monitor

Navigating the Perfect Storm (Redux)



*With a Special Focus on Laying the Foundation for a
New Economy in Iraq: Digital Transformation*

SPRING 2020

Middle East and North Africa Region



WORLD BANK GROUP
Macroeconomics, Trade & Investment

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The *Iraq Economic Monitor* provides an update on key economic developments and policies over the previous six months and presents findings from recent World Bank work on Iraq, placing them in a longer-term and global context and assessing the implications of these developments and other changes in policy regarding the outlook for Iraq. Its coverage ranges from the macro-economy to business environment and private sector development. It is intended for a wide audience, including policy makers, business leaders, financial market participants, and the community of analysts and professionals engaged in Iraq.

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ACRONYMS

BOC	Basra Oil Company	GEN	Global Entrepreneurship Network
Bpd	Barrel per day	GER	Global Entrepreneurship Registration
CAB	Current Account Balance	GoI	Government of Iraq
CBI	Central Bank of Iraq	GSM	Global System for Mobile Communications
CACH	Cheque enabled Automated Clearing House	GSRS	Government Securities Registration System
CMC	Communications and Media Commission	GW	Giga Watt
CNPC	China National Petroleum Corporation	HRP	Humanitarian Response Plan
CPA	Coalition Provisional Authority	ICA	Investment Climate Assessment
CPI	Consumer Price Index	HDI	Human Development Index
COSIT	Central Organization for Statistics and Information Technology	HRMIS	Human Resource Management Information System
COVID	Coronavirus Disease	ICT	Information and Communications Technology
CSD	Central Securities Depository	IOM	International Organization for Migration
DB	Doing Business	ISIS	Islamic State of Iraq and Syria
DE	Digital Economy	ITPC	Iraq Telecommunications and Post Company
DFS	Digital Financial Services	KRG	Kurdistan Regional Government
EMDEs	Emerging Market Developing Economies	KYC	Know Your Customer
EU	European Union	LPI	Logistics Performance Index
FDI	Foreign Direct Investment	MBPD	Million Barrel Per Day
GCC	Gulf Council Countries	MEES	Middle East economic Survey
FTTH	Fiber to the Home	MENA	Middle East North Africa
IEM	Iraq Economic Monitor	MoO	Ministry of Oil
GCC	Gulf Cooperation Council	MoF	Ministry of Finance
IDPs	Internally Displaced Persons	MOED	Ministry of Education
GDP	Gross Domestic Product	MSME	Micro Small Medium Enterprises
GEDI	Global Entrepreneurship and Development Institute	MW	Mega Watts
GEI	Global Entrepreneurship Index		

NBP	National Board of Pensions	PPP	Public-Private Partnership
NEET	Not in Employment, Education, or Training	PSSD	Pensions and Social Security Department
NGO	Non-Government Organization	RPSI	Retail Payments Systems Infrastructure
NPLs	Non-Performing Loans	RTGS	Real Time Gross Settlement
NPS	National Payment System	SOEs	State-Owned Enterprises
NSDC	National Skills Development Cooperation	SSS	Securities Settlement System
UNOCHA	United Nations Office for the Coordination of Humanitarian Affairs	TVET	Technical and vocational education and training
OPEC	Organization of Petroleum Exporting Countries	WBG	World Bank Group
PDS	Public Distribution System	WDI	World Development Indicators
PHCC	Primary Health Care Corporation	WGI	Worldwide Governance Indicators
PP	Percentage Point	UNHCR	United Nations High Commissioner for Refugees
PPE	Personal Protective Equipment		

EXECUTIVE SUMMARY

Recent Economic and Policy Developments

Iraq, once again, is facing a combination of acute shocks which the country is ill-prepared to manage. The collapse in oil prices has considerably reduced budgetary revenues and reversed the fiscal surpluses accumulated since 2018. COVID-19, and the lockdown measures needed to contain the pandemic have dealt a severe blow to economic activities especially the services sectors like transport, trade, banking and religious tourism, which constitute around half of the non-oil economy. The growing discontent over poor service delivery, rising corruption, and lack of jobs persists and is coupled with political impasse over the formation of a new government.

Iraq's pre-existing conditions going into this crisis limit its ability to manage and mitigate the socio-economic impact. A large dependency on oil revenues coupled with built-up budget rigidities limit Iraq's fiscal space to respond to the COVID-19 outbreak and offer a stimulus package to re-start the economy. An undiversified economy, highly dependent on oil outcomes, as well as large presence of the state in economic and commercial activities, make it hard to create the needed private sector jobs for a predominantly young population. Furthermore, rampant corruption and weak governance and service delivery fueled large scale protests across

the country calling for better public service delivery and jobs. As a result, all signs indicate that this multi-faceted crisis will have a protracted impact.

The outlook for Iraq, which was already negative prior to the COVID-19 shock, has markedly worsened since. Near-term economic growth will be subdued by low oil prices, a new OPEC+ agreement that has reduced oil production quotas, and unfavorable global and domestic conditions including disruptions from COVID-19 spread. As a result, the economy is projected to contract by 9.7 percent in 2020, down from a real GDP growth of 4.4 percent in 2019, with both oil and non-oil sectors contracting by 13 and 4.4 percent respectively.

The unsustainable stimulus package introduced since October—including a rising public sector employment, lower retirement age, and various transfers—coupled with weaker oil revenues are expected to have detrimental fiscal effects. In case oil prices stabilize in the low-30s and no reform measures are taken, the budget deficit would exceed 29 percent of GDP in 2020 and gross financing needs would reach of US\$67 billion (over 39 percent of GDP). Under this situation, Iraq may have no choice but to resort to a mixture of domestic and foreign sources to finance the deficit. Heavy reliance on local banks will crowd-out the available liquidity for private sector credit, while access to international markets may prove to be difficult given global market

conditions and a weak macro-framework for Iraq. Closing the gap through local currency bonds will weaken CBI's balance sheet and create pressures on the exchange rate and inflation. The accompanying current account deficit, estimated at 18.8 percent of GDP in 2020, could also draw-down CBI's foreign currency reserves to below 3 months of imports by 2022, exacerbating further the vulnerability of the country to external shocks.

Amidst this situation, implementing reforms in Iraq has become even more crucial for the sustainability of growth and job creation. A comprehensive forward-looking economic reform agenda can signal willingness to create the enabling environment for private sector led growth, diversification and job creation, and center around two focus areas:¹

- i. Tackling cross-cutting impediments for private-sector led diversification through:
 - Fiscal Sustainability and Economic Governance.
 - Financial Sector Reforms.
 - Business Environment Reforms.
 - Improving Human Capital outcomes.
 - Social Protection and Labor Systems Reforms.
- ii. Reforming governance and promoting private sector participation in selected productive sectors:
 - Agriculture and Agri-Industries reforms.
 - Electricity Sector Reforms.
 - Gas Sector Reform,

Laying the Foundation for a New Economy in Iraq: Digital Transformation

This special focus on digital economy (DE) highlights the importance of digital transformation for Iraq and the urgency behind it. Iraq's economic condition was gradually improving following the deep economic strains of the last three years. However, the recent protests and unrest highlight the continued fragility of the country and the high priority of improving economic opportunities, particularly for youth. Leveraging the DE will help Iraq address some

of its citizens' concerns as well as accelerate the achievement of its development objectives.

The benefits of a robust DE are numerous, and often unexpected, such as stronger resilience in the face of pandemics, as illustrated with COVID-19.

Innovative digital solutions are being deployed to sterilize hospitals, identify and monitor affected populations, offer home-based educational and employment opportunities among others to facilitate the necessary social distancing. A critical element to benefitting from these technologies is the underpinnings of a strong digital economy that also addresses the digital divide between those who have access to digital devices (such as computers, mobile phones, tablets) and the Internet, and those who do not.

The special focus covers the five foundational interconnected elements of a DE. The World Bank Group (WBG) defines the DE framework,² as consisting of 1) Digital Infrastructure, 2) Digital Financial Services (DFS), 3) Digital Platforms, 4) Digital Skills, and 5) Digital Entrepreneurship. Across all five pillars, the paper identifies challenges, opportunities, and proposes short-to-medium term recommendations.

The priority reform areas in Iraq are governance and promoting private sector participation in productive sectors (and diversification). This can subsequently boost Iraq's participation in the DE. These priority reform areas cut across all five elements of the DE framework and are meant to boost accountability, transparency, and trust.

Transitioning Iraq towards a resilient and inclusive DE will require economic reforms and longer-term development priorities along the five pillars: ensuring affordable access to high-speed internet, achieving widespread adoption of cashless payments, delivering digital government services and improving access to data, upskilling youth with technological know-how, and scaling up the digital entrepreneurship ecosystem. The relevance and urgency of these reforms are all too visible during the ongoing COVID-19 global health crisis.

¹ World Bank "Strategic Note on Priority Reform Areas, Towards a more resilient and inclusive economy in Iraq", forthcoming.

² World Bank Digital Economy Diagnostic Framework.

الملخص التنفيذي

التطورات الاقتصادية والسياساتية الأخيرة

مرة أخرى يواجه العراق مزيجاً من الصدمات الحادة التي يبدو أن البلد ليس على استعداد جيد لمواجهتها. فقد أدى انهيار أسعار النفط إلى انخفاض كبير في إيرادات الموازنة وإستنزاف الفوائض المالية المتراكمة منذ عام 2018. وجاءت جائحة فايروس كوفيد - 19 (الكورونا) وإجراءات الحجر المنزلي المترافقة بها لاحتواء الوباء لتلحق ضربة قاسية بالأنشطة الاقتصادية وبخاصة قطاعات الخدمات مثل النقل والتجارة والمصارف والسياحة الدينية ، والتي تشكل حوالي نصف الاقتصاد غير النفطي. وإلى جانب ذلك، يتواصل الاستياء الشعبي المتزايد حيال سوء تقديم الخدمات ، والفساد المتزايد ، ونقص الوظائف ، وقد أقتزن بالمأزق السياسي حول تشكيل حكومة جديدة.

إن ظروف العراق القائمة أصلاً والتي تغذي هذه الأزمة تحد من قدرته على إدارة وتخفيف الأثر الاجتماعي والاقتصادي. فهناك اعتماد كبير على عائدات النفط يصاحبه جمود متراكم في الموازنة، وهذا يقلص من الحيز المالي للعراق الذي يملكه من خلاله الاستجابة لجائحة فايروس كوفيد - 19 ، كما يقلل من إمكانية تقديم حزمة حوافز لإعادة تفعيل الاقتصاد. إن الاقتصاد الذي يفتقر إلى التنوع ويعتمد بشكل كبير على إيرادات النفط ، فضلاً عن حضور كبير للدولة في الأنشطة الاقتصادية والتجارية ، يجعل من الصعب عليه خلق وظائف في القطاع الخاص التي يتوجب إيجادها لسكان غالبيتهم من الشباب. وعلاوة على ذلك ، فإن الفساد المتفشى وضعف الحوكمة وسوء تقديم الخدمات أسهم في تغذية احتجاجات واسعة النطاق في جميع أنحاء البلاد تدعو إلى تحسين تقديم الخدمات العامة وتوفير فرص العمل. ونتيجة لذلك ، تشير جميع الدلائل إلى أن هذه الأزمة المتعددة الجوانب سيكون لها تأثير طويل الأمد.

إن التوقعات الخاصة بالعراق ، التي كانت سلبية أصلاً قبيل صدمة فايروس كوفيد - 19، راحت تزداد سوءاً وبشكل ملحوظ منذ ذلك الحين. فالتقديرات أن يتراجع النمو الاقتصادي على المدى القريب نتيجة لانخفاض أسعار النفط ، واتفاقية (أوبك +) الجديدة التي خفضت حصص إنتاج النفط ، والظروف المحلية والعالمية غير المواتية بما في ذلك الاضطرابات التي ظهرت جراء تفشي فايروس كوفيد - 19. ولذلك ، من المتوقع أن ينكمش الاقتصاد بنسبة 9.7 % في عام 2020 ، بانخفاض عن نمو الناتج المحلي الإجمالي الحقيقي الذي بلغ 4.4 % في عام 2019 ، وحيث سينكمش القطاعين النفطي وغير النفطي بنسبة 13 و 4.4 % على التوالي.

أن حزمة المحفزات غير المستدامة التي تم طرحها منذ تشرين الأول - بما في ذلك زيادة التوظيف في القطاع العام ، وخفض سن التقاعد ، والتحويلات المالية المختلفة - إلى جانب تراجع إيرادات النفط الضعيفة، يُتوقع أن يكون له تأثيرات مالية ضارة. ففي حالة استقرار أسعار النفط في نطاق الثلاثين دولاراً وعدم اتخاذ أي تدابير إصلاحية ، سيتجاوز عجز الموازنة 28 % من الناتج المحلي الإجمالي في عام 2020 وستصل احتياجات التمويل الإجمالية إلى 67 مليار دولار أمريكي (أكثر من 39 % من الناتج المحلي الإجمالي). وفي ظل هذا الوضع ، قد لا يكون أمام العراق أي خيار سوى اللجوء إلى مزيج من المصادر المحلية والأجنبية لتمويل العجز. ولكن الاعتماد الكبير على المصارف المحلية سوف يقلل من السيولة المتاحة لإثمانات القطاع الخاص ، في حين أن الوصول إلى الأسواق الدولية قد يكون صعباً نظراً لظروف السوق العالمية وضعف إطار الاقتصاد الكلي للعراق. كما إن إغلاق الفجوة من خلال سندات العملة المحلية سوف يضعف الميزانية العمومية للبنك المركزي العراقي مما يولد ضغطاً على سعر الصرف والتضخم. وقد يؤدي العجز المصاحب في الحساب الجاري ، الذي يقدر بنحو 18.8 % من الناتج المحلي الإجمالي في عام 2020 ، إلى خفض احتياطي العملات الأجنبية في البنك المركزي العراقي إلى أقل من 3 أشهر من الواردات بحلول عام 2022 ، مما يزيد من هشاشة البلد أمام الصدمات الخارجية.

في خضم مثل هذه الحالة يصبح تنفيذ الإصلاحات في العراق أكثر أهمية لاستدامة النمو وخلق فرص العمل . ويمكن لأجندة إصلاح اقتصادي شامل تتطلع نحو المستقبل أن توظف الهدف المتمثل في خلق بيئة مواتية لنمو يقوده القطاع الخاص، والتنويع، وخلق فرص العمل، ويتمحور حول اثنين من مجالات التركيز¹:

أ. معالجة المعوقات الشاملة للتنويع الذي يقوده القطاع الخاص من خلال:

- الاستدامة المالية والحوكمة الاقتصادية.
- إصلاحات القطاع المالي.
- إصلاحات بيئة الأعمال.
- تحسين محصلات رأس المال البشري.
- إصلاحات نظم الحماية الاجتماعية والعمل.

¹ البنك الدولي، « مذكرة استراتيجية حول نطاقات الإصلاح ذات الأولوية - نحو اقتصاد مرن أكثر شمولية في العراق»، ستصدر قريباً.

ب. إصلاح الحوكمة وتعزيز مشاركة القطاع الخاص في قطاعات إنتاجية مختارة:

- إصلاحات الزراعة والصناعات الزراعية.
- إصلاحات قطاع الكهرباء.
- إصلاح قطاع الغاز .

إرساء قاعدة لاقتصاد جديد في العراق: التحول الرقمي

هذا العدد الخاص حول الاقتصاد الرقمي (digital economy) يسلط الضوء على أهمية التحول الرقمي بالنسبة للعراق والضرورة الملحة التي تكمن وراءه . ذلك أن الوضع الاقتصادي في العراق راح يتحسن تدريجياً بعد الضغوط الاقتصادية العميقة التي عانى منها في السنوات الثلاث الماضية. ومع ذلك ، فإن الاحتجاجات والاضطرابات الأخيرة تسلب الضوء على استمرار هشاشة البلد والأولوية العالية التي يجب أن تركز لتحسين الفرص الاقتصادية ، وبشكل خاص للشباب. وتكمن الاستفادة من الاقتصاد الرقمي على مساعدة العراق في معالجة بعض مخاوف مواطنيه وكذلك تسريع تحقيق أهدافه التنموية.

إن فوائد وجود اقتصاد رقمي قوي متعددة، وغالباً ما تكون غير متوقعة ، مثل بلوغ مرونة أقوى في مواجهة الأوبئة ، كما تجلّى ذلك فيما يتعلق بفيروس كوفيد 19-، حيث يتم استخدام الحلول الرقمية المبتكرة في تعقيم المستشفيات ، وتحديد ومراقبة السكان المتضررين ، وتقديم فرص التعليم والعمل عن بعد من بين أمور أخرى لتسهيل تحقيق شروط التباعد الاجتماعي . وهناك عنصر حاسم للاستفادة من هذه التقنيات يتمثل في تمكين أسس الاقتصاد الرقمي الذي يعالج أيضاً الفجوة الرقمية بين أولئك

الذين لديهم أجهزة رقمية (مثل الكمبيوتر والهواتف المحمولة والأجهزة اللوحية) والإنترنت ، وأولئك الذين لا تتوفر لديهم مثل هذه الأجهزة.

يغطي العدد الخاص العناصر الخمسة الأساسية المترابطة للاقتصاد الرقمي . وتعرف مجموعة البنك الدولي إطار العمل للاقتصاد الرقمي²، على أنه يتألف من (1) البنية التحتية الرقمية ، (2) الخدمات المالية الرقمية، (3) المنصات الرقمية ، (4) المهارات الرقمية ، و (5) زيادة الأعمال الرقمية. وفي جميع هذه الركائز الخمس، تحدد الورقة التحديات والفرص والتوصيات المقترحة على المدى القصير إلى المتوسط.

تتمثل مجالات الإصلاح ذات الأولوية في العراق في الحوكمة وتعزيز مشاركة القطاع الخاص في القطاعات الإنتاجية (والتنوع). وهذا يمكن أن يعزز لاحقاً مشاركة العراق في الاقتصاد الرقمي. وتغطي مجالات الإصلاح ذات الأولوية هذه جميع العناصر الخمس لإطار الاقتصاد الرقمي، وهي تهدف إلى تعزيز المساءلة والشفافية والثقة.

يتطلب تحول العراق نحو تطوير اقتصاد رقمي يتسم بالمرونة والشمولية إجراء إصلاحات اقتصادية واعتماد أولويات إنمائية طويلة المدى تغطي هذه الركائز الخمس. سيستلزم ذلك على ضمان الوصول بأسعار معقولة إلى خدمات الإنترنت عالي السرعة، تحقيق اعتماد واسع النطاق للمدفوعات غير النقدية ، تقديم الخدمات الحكومية الرقمية وتحسين الوصول إلى البيانات ، رفع مستوى مهارات الشباب من ذوي الخبرة التكنولوجية ، وتوسيع نطاق النظام البيئي لريادة الأعمال الرقمية. لقد بدت أهمية هذه الإصلاحات وطابعها العاجل جليين خلال الأزمة الصحية العالمية المتواصلة والتي نتجت عن تفشي فايروس كوفيد - 19.

² البنك الدولي - إطار العمل التشخيصي للاقتصاد الرقمي.

RECENT ECONOMIC AND POLICY DEVELOPMENTS

Introduction

Iraq, once again, is facing a combination of acute shocks which the country is ill-prepared to manage. Following the twin shock of 2014-[17] where Iraq faced both the Islamic State (IS) and the sharp collapse of the oil price, the country is once again facing another major economic and social crisis combining several large shocks: namely the collapse in international oil prices, the spread of COVID-19, as well as persistent social and political turmoil. Iraq's pre-existing structural conditions, along with long-standing economic mismanagement, going into the pandemic-related shock severely constrain the country's current ability to manage and mitigate its impact. Large dependency on oil revenues coupled with built-up budget rigidities—such as a budget dominated by wages and pension payments—constrain fiscal space for a resilience package, let alone a stimulus one; an undiversified economy and large presence of the state in economic activity is making it harder to create jobs in the private sector for a predominantly young population; rampant corruption and weak governance structures prompted large scale protests calling for better public service delivery and jobs. As

a result, this multi-faceted crisis is expected to have protracted impact going forward and reverse some of the progress and reforms made through early 2019.

Even prior to COVID-19, the social and humanitarian conditions were critical in many parts of the country. The pandemic has hit Iraq in a time where the country is still facing daunting challenges to rebuild its infrastructure and provide needed public services to its population. It also came when the country was facing major development and humanitarian challenges. Indeed, Iraq ranks poorly at 120 of 189 countries in the 2019 Human Development Index (HDI). The poverty rate stood high at 20 percent in 2018; while the unemployment rate, which was falling before the ISIS crisis, had risen beyond the 2012 level to 9.9 percent in 2018. This also came on the back of a very low labor force participation rate, especially for women (12 percent),³ and in times where more than a fifth of the economically active youth do not have a job and are neither in employment nor in education or training. Furthermore, the humanitarian situation is still precarious with 1.4 million internally

³ World Bank staff estimates, MNA, Poverty and Equity Global Practice.

BOX 1 • COVID-19 Impact on the Humanitarian Response and Support to Vulnerable Displaced Populations in Iraq.

There are over 1.4 million internally displaced people in Iraq, 25.4 percent (or 359,000) of which are residing in one of the 67 camps. In addition to this, as of end 2019, there were 286,949 refugees in Iraq. 245,810 are Syrians, and 41,139 from other nationalities (70% children), with most Syrian refugees living in Kurdistan Region of Iraq. 41% of who are living in the 10 refugee camps in KR-I and the rest living in urban areas.

There is currently no strategy at the local, federal, or international level on what to do with these families, who prior to the COVID-19 pandemic, faced protection, (re)radicalization risks inside the camps and now face a startling health risk. With the support of UN agencies and NGOs, most camps have COVID-19 preparedness measures in place, training to Primary Health Care Corporation (PHCC) staff in camps, awareness raising and sensitisation messages are being disseminated, masks, soaps and hygiene material distributed and camp sterilisation has been carried out. There are currently no reported cases of COVID-19 infection within the camps, however this is expected to change as the situation evolves.

In mid-March, to control the COVID-19 outbreak, the GoI and the KRG, imposed extensive measures including significant movement restrictions and nationwide curfews. The restriction on movements, the lack of clarity and enforcement, especially at the Governorate level is now starting to limit the movement of the UN and NGO organizations who are providing essential lifesaving services to displaced communities in and outside of camps. Such services include health awareness campaigns, distribution of basic hygiene, Personal Protective Equipment (PPE), relief, medication to IDPs with chronic diseases; individual case management, counselling, and psychiatric services, support on gender-based violence—which will be at a heightened risk due to the “curfew” imposed across the country; establishment or reinforcement of health structures in IDPs in camps etc.

UN agencies report that several IDP camp management teams have requested for support to increase preparedness to deal with a COVID-19 outbreak within the camp. IDPs, overall, are becoming anxious due to a lack of access to information, rumours, fears of exclusion or neglect, lack of clarity in certain cases about what to do should cases be suspected in camps, restrictions on movement in and out of camps.

Based on a survey among 196 NGOs operating in Iraq, 93% of respondents said that their operations were affected by COVID-related restrictions on movement. 93% said they had suspended activities all together while 70% cited the inability to reach out-of-camp beneficiaries as an obstacle to implementing activities and 63% indicated that their activities have been impacted by a reduction in the ability of national staff to move.

Lack of awareness and information on COVID-19, misdiagnosis, poor referral systems or PHCCs in camps not permitted to transfer suspected cases out of the camps and the limited capacity of the public health system to receive cases from refugee and/or IDP camps is a serious concern. The restrictions of movement that staff are facing will impact their ability to access persons of concern and there is a risk that instances of refoulement, deportation and/or rise in discriminatory practices can begin to affect the displaced. Finally, if the banking system is affected this can limit their ability to pay staff, implementing partners and suppliers.

Sources: This information has been developed with inputs directly from the NGO coordination committee for Iraq, UNHCR and IOM as well as the WB.

displaced persons (IDPs), 4.5 million returnees and over 286,000 refugees (UNHCR 2020). These populations are susceptible to food insecurity,⁴ with poor access to quality health care and education.

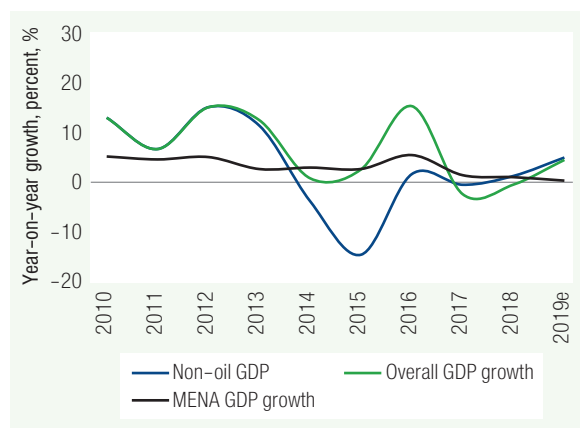
This situation is currently aggravated with the ongoing COVID-19 pandemic. As of April 26th, there has been 1,761 confirmed cases in Iraq with 86 fatalities according to the UNOCHA. The virus spread puts additional strains on the under-invested healthcare system and deepens economic downturn as the strict containment measures forces closures of business. The pandemic is expected to have a larger impact on the most vulnerable segments of the population especially the displaced (Box 1).

Output and Demand

Oil, agriculture and electricity generation have been the drivers of growth in 2019. Real GDP grew by 4.4 percent in 2019, reversing two consecutive years of contraction (Figure 1). The lynchpin was the oil sector which grew by 4.2 percent year-on-year (y/y), while the non-oil economy grew by 4.9 percent (y/y). Agriculture was the largest contributor to growth of all non-oil sectors (Figure 3) after it expanded by a staggering 39 percent. This performance reflects above-average rainfall and

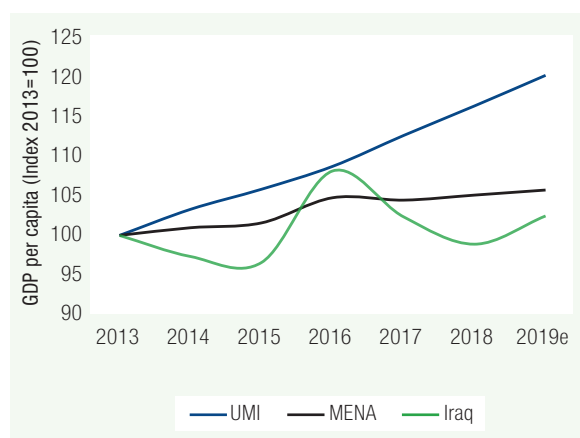
⁴ United Nations, Food and Agricultural Organization (FAO), March 2020.

FIGURE 1 • Non-oil GDP Has Grown by Nearly 5 Percent in 2019, Outperforming Previous Three Years



Sources: Iraq COSIT; WDI; and World Bank Staff Calculation.

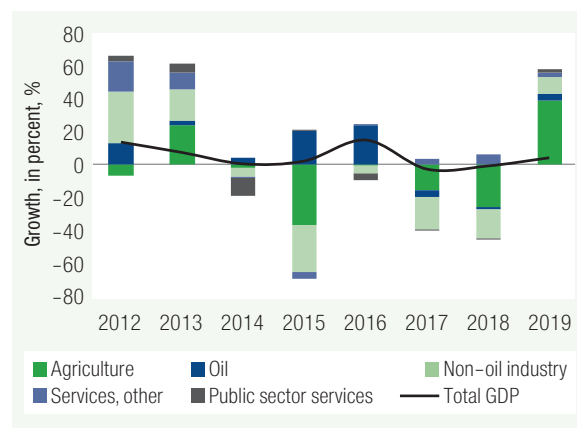
FIGURE 2 • Nevertheless, Growth Was Not Sufficient to Make a Change in Per Capita Terms



Sources: Iraq COSIT; WDI; and World Bank Staff Calculation.

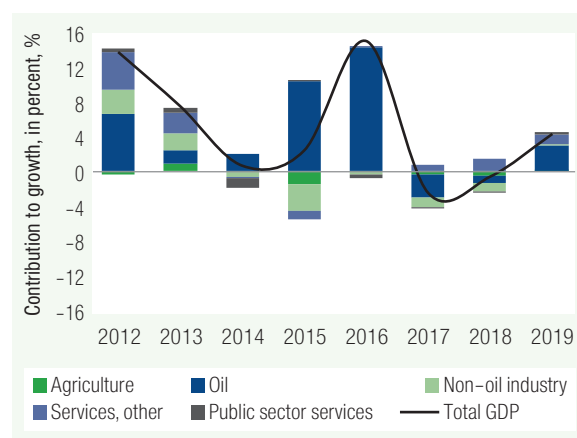
subsequent record wheat production that reached 4.8 million metric tons for 2019–20,⁵ up by 60 percent from 2018. This boosted farmer's disposable income and had positive gains for import substitution. There was also significant progress in expanding the electricity supply by increasing generation to an average of 16 GW (up from 12 GW in 2018) and boosting peak generation by nearly 20 percent, well above its 15 percent target. Nevertheless, power generation remains well below total demand of 26 GW⁶ with frequent interruption in services delivery given problems linked to transmission, distribution, and bill collection.

FIGURE 3 • Oil, Agriculture and Services Have Been the Pillars for Growth in 2019



Sources: Iraq COSIT; WDI; and World Bank Staff Calculation.

FIGURE 4 • ... with Oil Recording the Largest Contribution Given Its Weight in the Economy



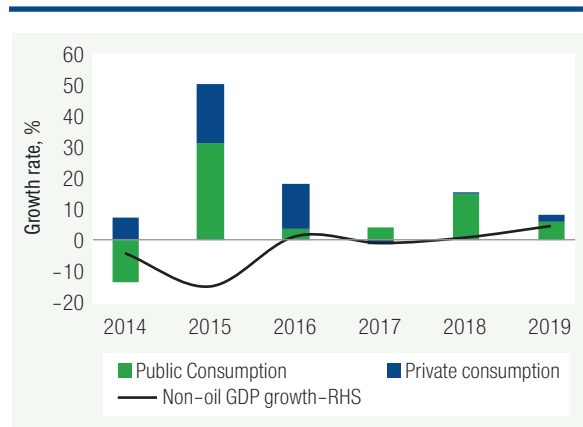
Sources: Iraq COSIT; WDI; and World Bank Staff Calculation.

On the demand side, 2019 was characterized by a consumption-led growth due to Gol's fiscal expansion. Private and public consumption picked up in 2019 driven by a sizable expansion of public spending which included public sector wage bill and pension. Such an expansionary fiscal policy coupled with a low-inflation environment and a boost in income for agriculture sector workers, supported household

⁵ USDA Foreign Agricultural Service, Dec 2019.

⁶ Source: Central Bank of Iraq; and Middle East Economic Survey (MEES).

FIGURE 5 • Private Consumption Picked Up in 2019



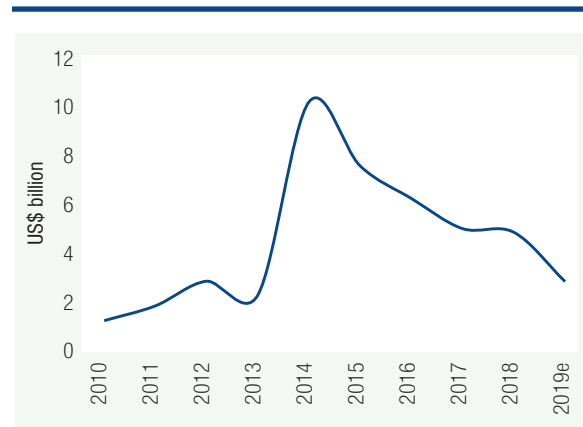
Source: World Bank staff calculations.

purchasing power and therefore increased private consumption only to be partially offset in the last quarter of the year following the protests. Hence, private consumption grew by 2 percent in 2019, from 0.3 percent in 2018 (Figure 5). This also increased imports of goods to about 43 percent of GDP in 2019, up from 38 percent in 2018.

Investment remained subdued amidst persistent public investment management constraints and an unfavorable business environment. Despite an allocation of IQD33 trillion (12 percent of GDP) in the 2019 budget law, 74 percent of public investment was executed with most attributed to investments in the oil sector. Limited absorptive capacity, inefficiencies in public investment management, and weak capacity at the governors' level have contributed to such a poor outcome.⁷ Moreover, an unfavorable business environment, corruption, cumbersome bureaucracy, and an opaque regulatory environment,⁸ nearly halved foreign direct investment (FDI) to only US\$2.9 billion in 2019 (1.2 percent of GDP) (Figure 6).

Iraq's (volatile) economy outperformed that of regional peers in 2019, but its population dynamics requires much higher growth to sustain the current level of welfare. Iraq's growth has outperformed the Middle East and North Africa's (MENA) average growth of 0.1 percent (Figure 1). With a fertility rate of 4.1 though, GDP has barely grown in per capita terms over the past few years (Figure 2). For Iraq to reap its demographic dividend, it needs to consistently grow its non-oil economy at a much faster pace (since

FIGURE 6 • While FDI Halved to US\$2.9 Billion in 2019



Source: CBI.

the oil economy is not labor intensive). Only then would Iraq be able to close the gap with peers and more importantly maintain a constant level of economic activity and welfare gains for its growing population.

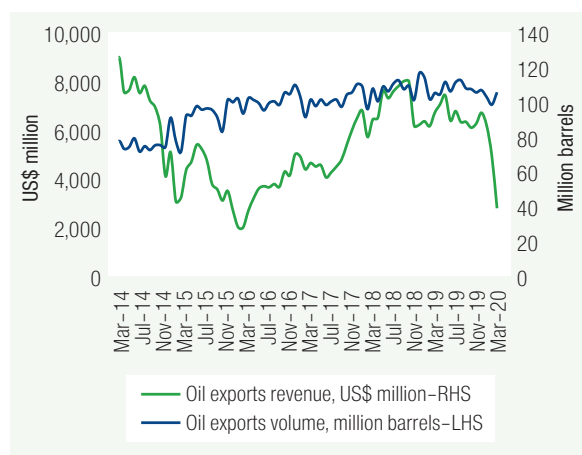
The protests that started in October 2019 and subsequent events linked to the COVID-19 pandemic in early 2020 have dampened economic activity especially in the services sectors. Protests had a considerable impact on the services sector which decelerated by 0.9 percent in Q4-19 (y/y). Sectors that were mostly impacted were transport, trade, banking and tourism. Together they account for a sizeable 48 percent of non-oil GDP.⁹ These benefitted earlier in 2019 from a stable security situation and a consumption boost given fiscal loosening. The undesirable conditions for services were exacerbated further in early 2020 as the COVID-19 pandemic reached Iraq and strict containment measures were put in place including curfews, limitations on inter-governorate movement and closure of borders. One example is religious

⁷ Weak project preparation, procurement and contract management, limited absorption capacity, as well as weak coordination between federal and local governments are all institutional constraints impeding the fast disbursement of public investment.

⁸ Iraq indeed ranks as 172 out of 190 countries in the 2020 doing business ranking.

⁹ It also accounts for 17 percent of overall GDP.

FIGURE 7 • The Collapse in Oil Prices Has Outpaced the Rise in Production, Putting a Large Toll on Revenues



Sources: Iraq Ministry of Oil and World Bank Staff calculations.

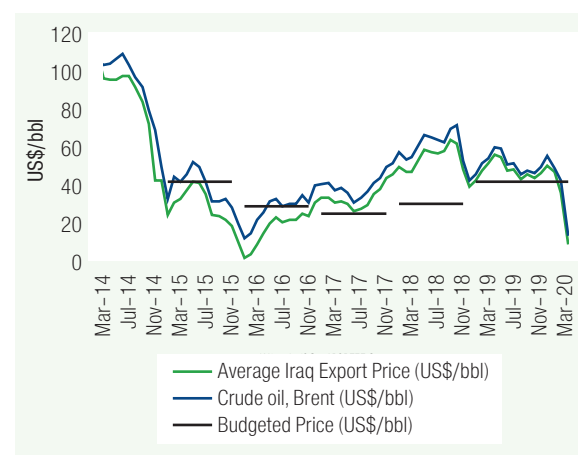
tourism which is concentrated in the southern governorates and is often reported to be second largest source of revenues after oil. According to Najaf's head of the association for hotels and restaurants, the city hosted more than 5,000 visitors per day. Because of protests and now the corona virus, 300 of the city's 350 hotels have closed with those who remained open seeing their occupancy rate drop to 10 percent.¹⁰

Oil and Gas Developments

While Iraq's oil industry was largely unaffected by the demonstrations, the turn in global conditions following COVID-19 is taking a toll on production.

On December 29th, the Ministry of Oil (MoO) confirmed that the Nasiriyah field in Dhi Qar province, which produces 80,000–85,000 barrel/day had been shut down after protesters blocked access to the site. The loss in production was compensated, however, by Basra fields. Aligned with OPEC+ quotas, Iraq's oil production was up 5 percent (y/y) in 2019 reaching 4.8 million barrel per day (mbpd). Crude oil exports remained stable though and reached 3.5 mbpd (about 74 percent of total production), up by only 1 percent from 2018. This difference reflects primarily growing electricity generation and usage of domestic oil to

FIGURE 8 • Oil Prices Stood at US\$5 Above the 2019 Budgeted Price, Compared to a US\$19.5 Spread in 2018, and Continue to Plunge as COVID-19 Situation Develops in 2020



Sources: Iraq Ministry of Oil and World Bank Staff calculations.

substitute for declining gas imports from Iran. It also reflects growing domestic demand especially on subsidized gasoline and kerosene material, a subsidy that is not typically pro-poor and does not contribute to job creation. The significant turn in global oil demand since the start of the COVID-19 is taking a toll though on Iraq especially that China, one of the hardest hit countries, is the largest importer of Iraqi crude (28 percent of oil exports at end-2019).¹¹ As a result, Oil exports declined by over 4 percent in the Q1–2020 (y/y), down to an average of 306 million barrel, compared to over 319 million barrels in 2018 (Figure 7).

Softer global prices since August 2019 have also slashed oil revenues. Iraqi crude was sold at an average price of US\$61.1 per barrel in 2019 compared to US\$65.5 per barrel in 2018, bringing exports value down by 6.2 percent (y/y) in 2019 (Figure 8). The Saudi-Russian price war over the extension of the OPEC+ agreement, as well as the outbreak of COVID-19 that weighed down on an already soft global demand for oil has exacerbated

¹⁰ Agency France Press (AFP) and Daily Times <https://dailytimes.com.pk/566257/virus-strikes-another-blow-at-religious-tourism-in-iraq>.

¹¹ Bloomberg, March 2020.

the situation further. As a result, Iraq's crude oil export prices crashed to US\$28.4 per barrel in March 2020, bringing the average price for Q1–20 to US\$47 dollar per barrel and slashing revenues by more than half. At this price, Iraq will face extreme difficulties in financing basic expenditures planned for 2020.

Iraq continues to develop its oil and gas industry, despite challenges. With the spread of violence in early 2020 and later COVID-19, a number of foreign workers had left the oilfields and some oil firms have been working in less than maximum capacity. This situation prompted once again the MoO to utilize spare capacity in other fields to replace lost production. Further developments in oil and gas are planned though across the country. This includes a US\$203.5 million contract awarded to China National Petroleum Corporation in March 2020 to build a 155 million cfd sour gas treatment facility at Majnoon field,¹² as well as the installment of an advanced system to detect leakages from pipelines carrying petroleum products with the objective of limiting smuggling. However, boosting oil and gas production requires significantly higher investment than the Gol can support with the present oil prices. Under these global conditions and given that Iraq exports 70 percent of its crude to Asia, the Basra Oil Company has proposed that all international oil companies cut the budget of developing oil fields by 30 percent during the first half of 2020.

Public Finance

Iraq's fiscal position deteriorated substantially as the Gol authorized additional non-discretionary spending, building further budget rigidities. The rapid expansion of the public wage bill, pensions and social assistance programs coupled with falling oil revenues has shrunk the 11 percent of GDP budget surplus in 2018 to 1.3 percent of GDP in 2019. MOF data shows a substantial 26.4 percent (y/y) rise in recurrent spending following Gol's decision to expand public employment, reduce the retirement's age (see Box 2) and offer numerous cash transfers following the demonstrations of October. As a result, the primary fiscal surplus shrunk from 12 percent of GDP (IQD32.6 trillion) in 2018 to 2.4 percent of GDP in 2019 (IQD6.6 trillion) (Figure 9).

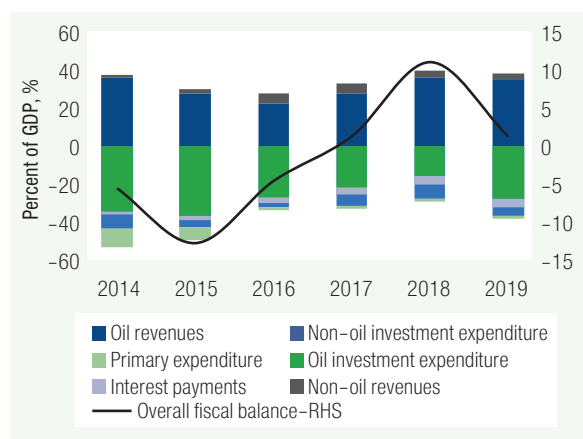
Fiscal loosening prioritized boosting consumption at the expense of public investment and its ability to effectively respond to COVID-19 economic downturn. Iraq continues to allocate a significant portion of the budget toward non-discretionary spending especially the wage bill and transfers. In 2019, recurrent spending accounted for over 77 percent of total budget, largely due to transfers hike and additional public sector hiring (Figure 10). The public wage bill rose by over 13 percent (y/y) in 2019 and now stands above that of the MENA region oil exporters and high income economies' average (Figure 11). Both goods and services, and transfers—namely pensions and Public Distribution System (PDS)—increased by 127 and 18 percent (y/y), respectively. This leaves a small fraction of funding for much-needed public investment in infrastructure and human capital programs. It also erodes the fiscal buffers available to respond to the expected economic downturn in the aftermath of COVID-19 crisis. At this current rate, Iraq will require an oil price of US\$76 per barrel to finance its recurrent spending for 2020.

Public investment remains below the needed levels to close the infrastructure gap notably those for public service delivery in times of crisis like COVID-19. Investment spending increased by almost 77 percent (y/y) in 2019. While this is an improvement, it represents only 8.8 percent of GDP and falls short of the infrastructure needs of the country. Moreover, there is a persistent under-execution of the investment budget (Figure 12) with most of capital spending going towards the oil fields. For public investment related to non-oil sectors, execution stood at 30 percent reaching only 2 percent of GDP. This raise concerns over service delivery, rising infrastructure gap, and stalled reconstruction program. Such results not only put a drag on long-term sustainable growth but also increases social vulnerabilities especially in times where boosting human capital systems is essential to manage the impact of COVID-19.

Deteriorating domestic revenue mobilization takes away one of the fiscal tools available for Iraq to face this unrepresented multifaceted crisis. The Iraqi budget remains largely dependent on oil-related receipts as they constitute 92 percent of total

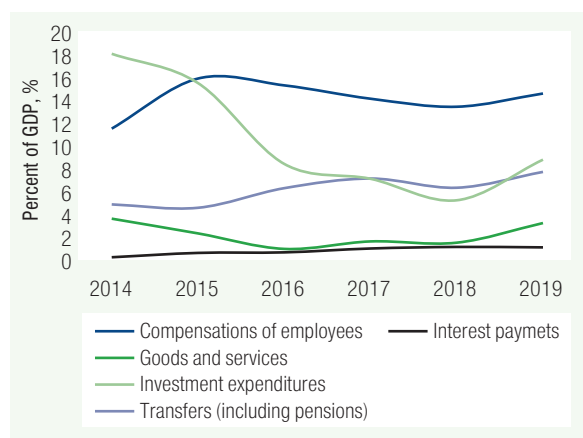
¹² MEES, March 2020.

FIGURE 9 • Fiscal Loosening Has Markedly Reduced the Budget Surplus in 2019



Sources: Iraq Ministry of Finance and World Bank staff calculations.

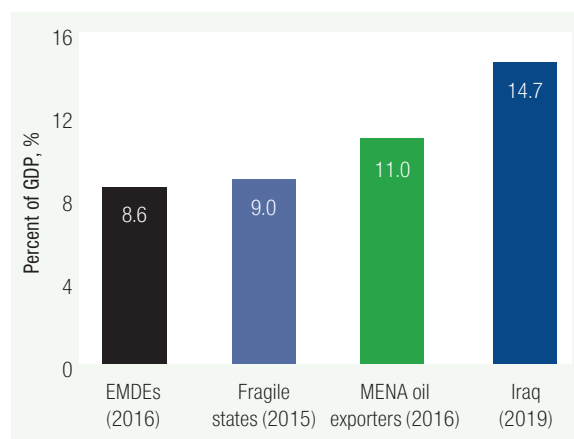
FIGURE 10 • The Wage Bill Dominates Recurrent Spending



Sources: Iraq Ministry of Finance and World Bank staff calculations.

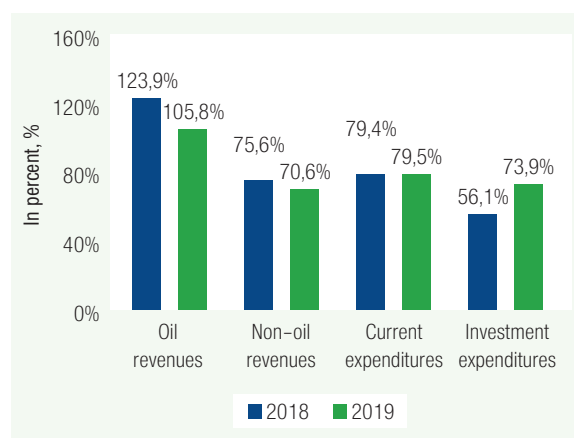
budgetary revenues. The US\$4 dollars drop in the average price of oil exports translated into a US\$5 billion loss in oil revenues in 2019. Furthermore, non-oil revenues have been well below budgetary expectations and have declined by 24 percent (y/y) over the year. The decline reflects problems in domestic revenues mobilization attributed to poor tax compliance and collection efforts, expansion of customs exemptions, and low growth affecting income tax. At 3 percent of GDP, non-oil tax revenues in Iraq is one of the lowest in the world. Expanding domestic revenue mobilization will be key to reduce reliance on oil, create a more stable

FIGURE 11 • ... and Is Among the Highest in the World



Sources: Iraq Ministry of Finance and World Bank staff calculations.

FIGURE 12 • Despite the Improvement in Public Investment Execution Rates, It Remains Below Recurrent Spending



Sources: Iraq Ministry of Finance and World Bank staff calculations.

budgetary revenues base, and most importantly create fiscal space for investments in human and physical capital to mitigate this protracted crisis.

The favorable debt dynamics in 2019 could be short-lived. The fiscal surplus and high nominal GDP growth lowered the public debt-to-GDP-ratio to 44.6 percent of GDP in 2019, a drop of 4.7 percentage points of GDP (ppt) compared to 2018. External debt¹³ is the largest share of Iraq's

¹³ External debt is defined as legacy external debt, external debt and guarantees external.

BOX 2 • Pensions and Social Insurance in Iraq

The contributory system in Iraq comprises two pension schemes covering public and private sector employees, both designed as pay-as-you-go, defined-benefit schemes. The public scheme is managed by the Ministry of Finance's National Board of Pensions (NBP) and includes civil servants, security forces, and survivors of martyrs. The private scheme is managed by the Ministry of Labor and Social Affairs Pensions and Social Security Department (PSSD) and covers a small proportion of private sector employees. In addition to the two schemes, there are currently almost 1M people still receiving pension benefits from the general budget. They are mostly those who retire before 2006 (when the current public pension scheme was created) or their beneficiaries. These payments are supposedly phasing-out.

While total spending on pensions is high (approx. 4.2 percent of GDP in 2019), the current scheme covers less than 48 percent of the total labor force, most of whom are in the public sector (around 3 million contributors). The private sector scheme has a limited number of contributors (only 4 percent of private sectors employees, or around 200,000 people out of the 5 million working in the private sector), and there are not yet any social insurance schemes for self-employed, part time or flexible workers.

In addition to low coverage, the system faces a number of financial/fiscal, economic, and social challenges: First, the schemes are financially unsustainable, given that revenues from contributions and investment returns will not be sufficient to cover pension spending. In fact, based on latest projections run by the World Bank, the public sector scheme is expected to reach deficit in 2025, therefore increasing reliance on the general budget and crowding-out resources for other relevant programs. Second, the current system produces considerable inequities, including those between private and public sector employees, the last ones being covered by a more generous scheme. The system also produces perverse incentives, including incentives for early retirement. Third, the current system does not provide adequate pensions. For instance, the pensions amount is not automatically indexed, which exposes beneficiaries to the risk of losing their purchase power due to inflation.

The current system is governed by Law 9/2014, a law that does not respect the good principles of pensions design. With the support of the World Bank, the NBP and PSSD worked on a new draft social insurance law, which would have introduced considerable improvements to the previous 2014 law. The new draft law was approved by the Iraq Council of Ministers in November 2016. However, the complex political economy for such reform hindered the passage of the new draft law, which is still pending approval of the Council of Representatives. Instead, the Government of Iraq introduced in November 2019 an amendment to Law 9/14 that would further compromise the financial sustainability and fairness of the pension system, as it entails generous increases of some benefits and does not address some of the above-referenced key design challenges of the pensions system.

The need to revamp the pension law in Iraq, which would now entail reversing some of the amendments introduced in 2019, is now more urgent than ever. Absence of reforms would entail a very large fiscal burden or a sharp cut in benefits in a few years. In addition to the existing challenges of the pension system, the current economic downturn sparked by the COVID-19 pandemic and the related expected worsening of labor market outcomes is likely to lead to a further deterioration of the pension system. Therefore, the introduction of short-term emergency measures to address the COVID-19 crisis, in combination of course with the adoption of appropriate long-term measures, will be critical to make the pension system sustainable as well as social and economic equitable.

Source: WB staff.

debt stock (Figure 13). Its structure makes solvency risks manageable despite the country's limited debt carrying capacity (Figure 14). Interest payments are relatively small at 1.1 percent of GDP in 2019. The budget surplus of 2019 had helped contain financing needs at an estimated US\$3.5 billion (1.5 percent of GDP). Nevertheless, this improvement could be short-lived as deteriorating fiscal conditions in 2020 have worsened both debt dynamics and financing needs (see outlook section for a detailed discussion).

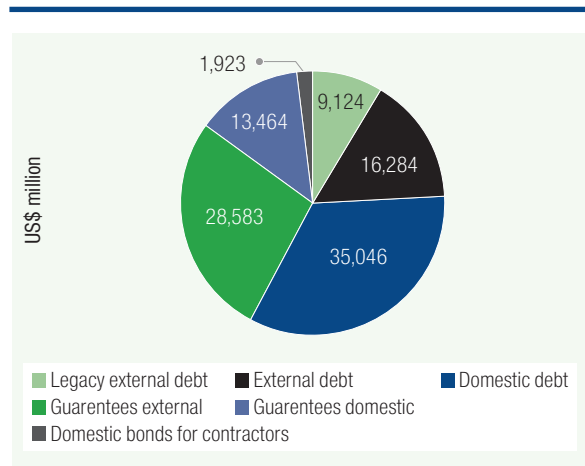
External Sector

Less favorable terms of trade coupled with fiscal loosening have weakened Iraq's external position.

The current account balance (CAB) is expected to turn from a 2.5 percent of GDP surplus in 2019 to 18 percent deficit by end 2020 (Figure 15). This large swing is attributed to two factors. First, the less favorable terms of trade where the collapse in international oil prices have already reduced Iraq oil exports value by 26 percent in Q1-20 (y/y) (Figure 16). Second, to a loosening of the fiscal stance resulting in a notable rise in imported goods and services especially those conducted by the government agencies. This weakens Iraq's external position.

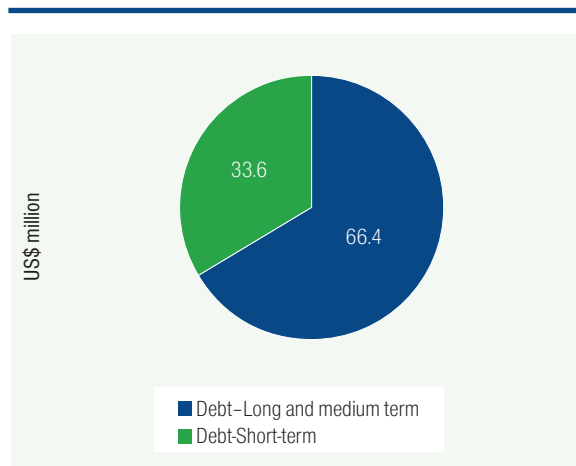
Worsening global and domestic conditions reduce external financing options, putting pressure on Central Bank of Iraq's (CBI) international reserves. The unfavorable business environment and weak execution of public investment through project

FIGURE 13 • Fifty Two Percent of Total Debt Stock Is External



Sources: Iraqi authorities; and World Bank staff calculations.

FIGURE 14 • Sixty Six Percent of that Stock Is Long Term and 9 Percent Is Legacy Debt Prior to 1990



Sources: Iraqi authorities; and World Bank staff calculations.

finance are behind the poor performance of foreign direct investment (FDI) and official investments, the two main sources of external financing for Iraq. Combined, these inflows have dropped by 15 percent in 2019 (y/y).¹⁴ While the CAB surplus in 2019 had boosted CBI's foreign currency (FX) reserves to US\$68 billion (covering 10 months of imports and 1.9 times short-term external debt), the trend has reversed in early 2020 as domestic and global conditions rapidly deteriorated (Figure 17). The weakened global demand for oil, the spread of COVID-19 and its implication on capital flows for emerging markets, the persistence of domestic and political turmoil as a push factor for investments, as well as worsening CAB already cut those reserves by US\$9 billion in the first 2-months of 2020 (lowering coverage for 5.9 months of imports) (Figure 18).

Monetary Policy and Prices

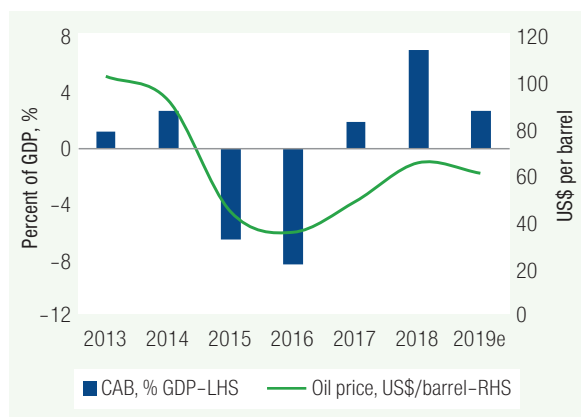
Inflation remains muted despite disruptions caused by the spread of COVID-19. The fiscal stimulus that boosted domestic demand combined with increased usage of more expensive private operators have put pressure on the prices of services such as education (up 9.7 percent), recreation (up 5 percent) and health (up 2.9 percent) in 2019 (y/y) (Figure 20). Nevertheless, inflationary pressures

remain largely muted due to cheaper consumption goods. This follows a continued depreciation of both Turkish and Iranian currencies, the two main trading partners for Iraq. Items like food prices declined by an average of 0.1 percent during the year, while consumer goods like “apparels” and “house supplies and appliances” prices dropped by an average of respectively 0.9 and 1 percent over the same period. These three items alone constitute on average 41 percent of the household's total consumption basket. While the easing in prices was favorable to Iraqi consumers, especially the poor, calls from the impacted domestic producers pushed the GoI to raise tariffs and impose import bans on selected food items. Furthermore, the GoI seems to have succeeded in cracking down on illegal price hikes keeping prices in 2020 subdued despite border closures following COVID-19 containment measures. As a result, headline and core inflation registered only 0.5 and 1.1 percent rise in January (y/y, latest data) (Figure 19).

Money supply increased, but private sector credit remains tepid. Broad money (M2) experienced rapid growth of almost 8 percent (y/y) in 2019 driven by the pickup in non-oil economic

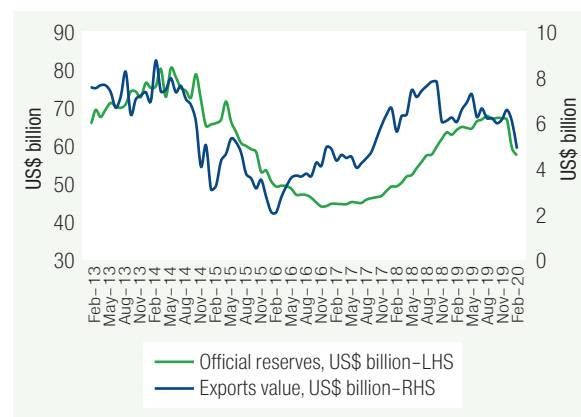
¹⁴ Latest available data are for 2019. CBI data also reveals a contraction of 6 percent (y/y) for official investment.

FIGURE 15 • CAB Is Expected to Turn from a Small Surplus in 2019 Into a Markable Deficit in 2020



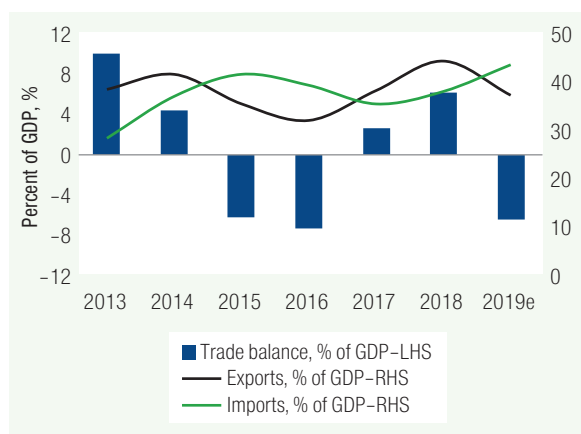
Sources: CBI, Ministry of Oil; and World Bank staff calculations.

FIGURE 17 • The Decline in Oil Prices Due to COVID-19 Caused the Official Reserves to Decline in the Start of 2020



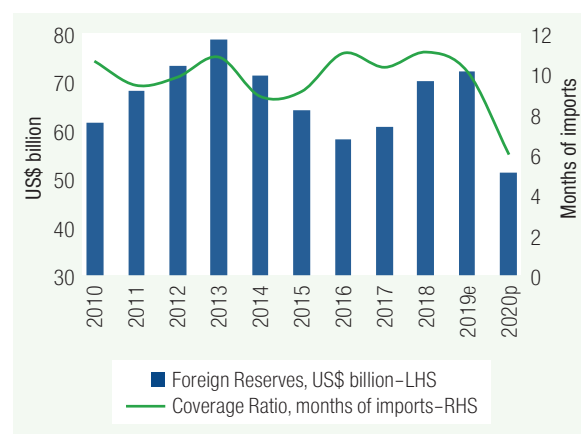
Sources: CBI, Ministry of Oil; and World Bank staff calculations.

FIGURE 16 • Driven by Less Favorable Trade Balance



Sources: CBI, Ministry of Oil; and World Bank staff calculations.

FIGURE 18 • Reserve Coverage Is thus Expected to Decline from 10 Months of Imports in 2019 to 6 Months in 2020



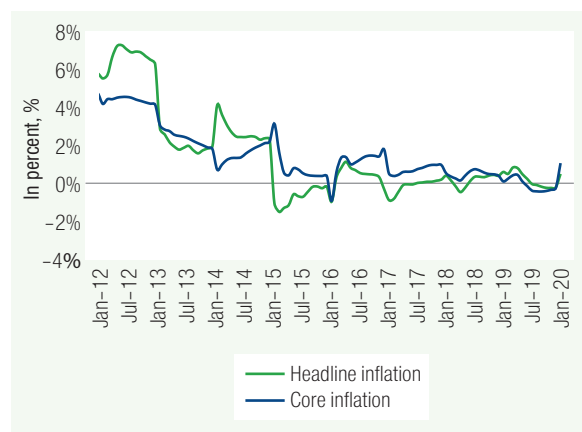
Sources: CBI, Ministry of Oil; and World Bank staff calculations.

activity (Figure 21). Credit to the private sector, on the other hand, remains constrained in part by weak banking sector that tend to cater primarily to large and inefficient State-Owned Enterprises (SOEs), and in other part by increased borrowing by the public sector. Indeed, credit to public sector was up 6 percent (y/y) in 2019 compared to 3 percent for that of the private sector (Figure 22). Credit to the private sector is at 8 percent of GDP, well below that of MENA average (57 percent) and Upper Middle-Income countries (123 percent). This

reflects in part deficiencies in financial architecture including legal and institutional frameworks and credit information.

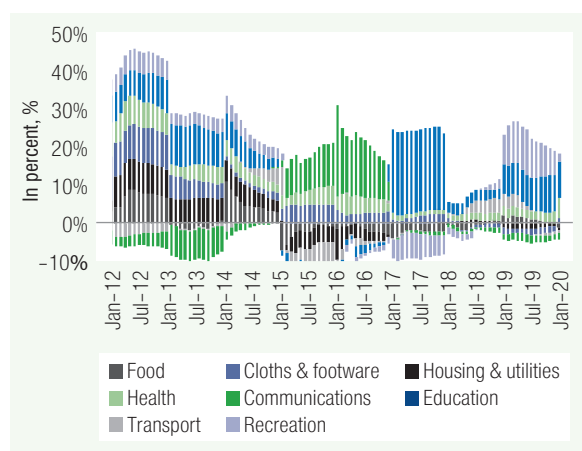
The CBI has taken multiple measures to mitigate the impact of the crisis on households and businesses, but a larger stimulus package is still needed to re-start the economy. To participate in the fight against COVID-19, the CBI has hosted donation accounts dedicated for healthcare spending and donated itself IQD30 billion (roughly US\$26 million). The CBI has also issued instructions on new

FIGURE 19 • Inflation Remained Subdued in 2019, but Slightly Edged Up in the Start 2020



Sources: COSIT and World Bank Staff Calculations.

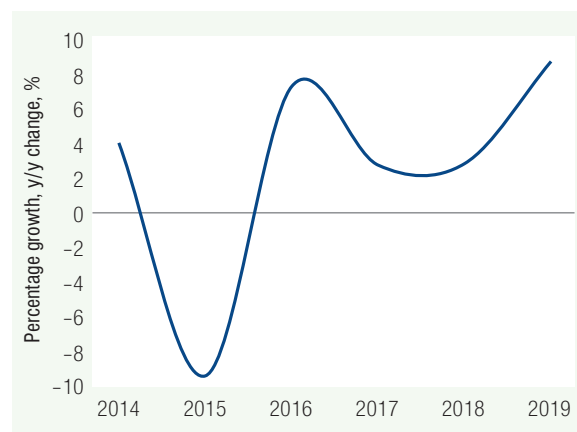
FIGURE 20 • Higher Prices of Some Food and Non-Food Items Continued in 2019 and Jan. 2020



Sources: COSIT and World Bank Staff Calculations.

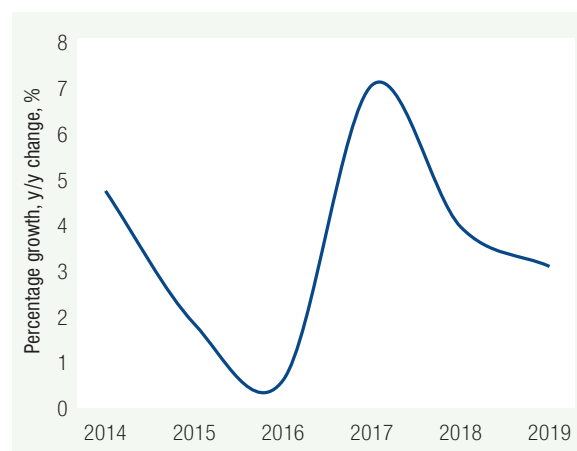
operational modalities for banks to serve clients under the CODID19-imposed curfew and resumed its services for all payment systems and the investment window on daily basis. The CBI has also decided to resume external transfers functions through the specialized window to meet the requests of both citizens and Gol as well as appease the financial burden on Iraqis stranded abroad after the shut-down of airports. To boost liquidity in the market and support households and SMEs alike, the CBI has applied a three months moratorium on interest and principal repayments for

FIGURE 21 • Broad Money Increased in 2019 Driven by the Pick-Up in the Overall Economic Activity



Source: Central Bank of Iraq.

FIGURE 22 • But Credit to Private Sector Remains Constrained



Source: Central Bank of Iraq.

both consumer and SMEs loans, suspended all fines imposed on commercial banks, and enhanced banks' cash liquidity by an amount of IQD1 trillion. It also suspended vendors commissions on electronic payment tools for a period of six months and reduced reserves requirement of banks to 13 percent over the same period. While these measures are a step in the right direction to soften the impact of some aspects of the crisis, a larger stimulus package will be needed to restart the economy and allow businesses to resume operations.

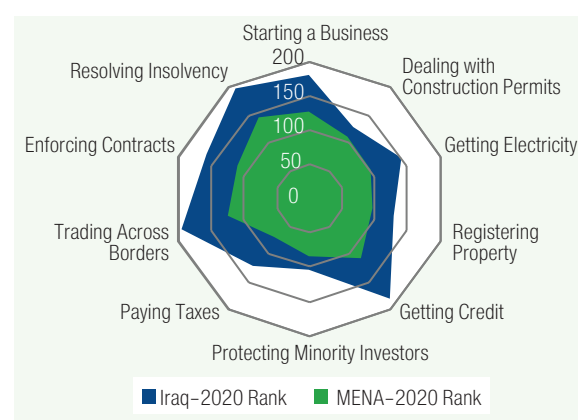
Iraq continues to face structural challenges, and suffers from limited financial intermediation, which constrains lending to SMEs. Iraq ranks 186 out of 190 in terms of ease of getting credit on the World Bank's 2020 Doing Business report. The banking system is dominated by under-capitalized and under-provisioned state-owned banks (SOBs) primarily used for quasi fiscal operations (NPLs stand at an estimated 37+ percent). Most private banks are small in size, lack credit risks analysis skills, and rely on currency arbitrage as their main revenue source as well as limited fee-based exchange services than lending. As a result, credit intermediation is at a very low level. The non-banking financial sector is also at an early stage of development. The number of functioning Micro-Financing Institutions (MFIs) has declined over the last 3 years, leaving only three MFIs operating in the microfinance sector. Combined these MFIs have outstanding portfolio of US\$110 million and 63,530 active borrowers.¹⁵ With 7.36 million poor (22.5 percent of population), out of which 2.5 million are economically active (8 percent of population), MFIs likely fulfill only a small fraction of potential demand. Despite this situation, the CBI has put in place a US\$5 billion line of credit extended to SOBs for on-lending to SME's, agriculture and or infrastructure projects. Nevertheless, fewer than 5 percent of SMEs in the formal sector have received bank loans.

Business Environment and Private Sector Development

Iraq's unfavorable business environment constrains private sector activity. In the World Bank Doing Business 2020, Iraq ranks 172 out of 190 countries, one position down from the previous year. It is also one of the lowest ranking amongst the MENA region and Upper Middle-Income Countries (UMIC) peers. While it ranks relatively favorably on some topics such as dealing with construction permits (103) and protecting minority investors (111) indicators, it fares particularly poorly on getting credit (186), trading across borders (181), and resolving insolvency (168) (Figure 23). Notable progress has been made on electricity access, with improved production, and in making starting a business easier by streamlining some procedures.

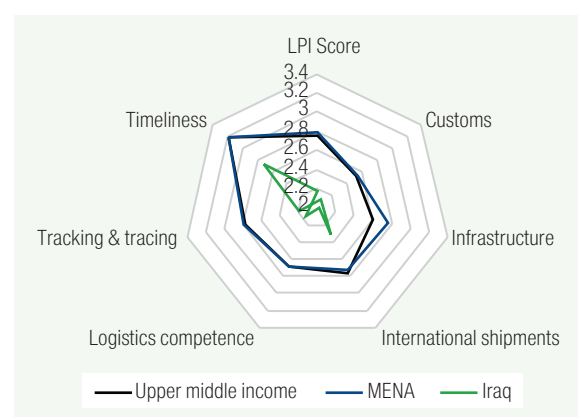
Conflict and limited investment resulted in a deteriorating quality of logistics, which is a key component to reduce the costs of doing business in Iraq. The World Bank Logistics Performance Index (LPI) 2018 shows Iraq lagging the region and other UMIC in trade logistics efficiency. It stands at 147th out of 160 countries. This situation implies high operational cost, a colossal deficit in infrastructure, and rising pressure on service delivery. (Figure 24).

FIGURE 23 • Iraq Continues to Rank Unfavorably on All Doing Business Indicators Compared to MENA



Sources: Iraq Doing Business 2019; and Logistics Performance Index 2019.

FIGURE 24 • Logistics Quality Has Deteriorated with the Conflict



Sources: Iraq Doing Business 2019; and Logistics Performance Index 2019.

¹⁵ Syed Mehdi Hassan, WB, Iraq Financial Sector Note, March 2020.

Outlook and Risks

Outlook

The economic outlook for Iraq has markedly worsened especially amidst a collapse in international oil prices. Since the last Iraq Economic Monitor published in October 2019, the country has suffered from a protracted social and political turmoil, a collapse in international oil prices, and the outbreak of COVID-19. All have tilted the economy's outlook downward. As a result, GDP growth is now projected to contract by 9.7 percent in 2020, making it the country's worst annual performance since the fall of the Saddam regime in 2003. Growth is projected to return in subsequent years, partly due to a low-base effect, to 1.9 and 7.3 percent in 2021 and 2022, respectively. Under the new OPEC+ agreement reached on April 9; Iraq's oil production is expected to be reduced from 4.8 mbpd in 2019 to 4 mbpd in 2020. As a result, the oil sector's is projected to contract by 13 percent in 2020 amidst a markedly worsened outlook for international oil markets. Both prices and exports are expected to be significantly lower given lower global demand and a projected recession worldwide as COVID-19 containment measures are extended. Since oil represents 67 percent of the overall economy,¹⁶ Iraq is highly susceptible to its variations. The report estimates that every dollar increase in international oil prices could bring up to 0.14 ppt of additional growth in Iraq. As such, any development that increases oil prices will improve the growth outlook.

The non-oil economy is also expected to be hit by the multitude of crises. The non-oil economy represents slightly more than a third of the Iraqi real economy. The persistence of strict containment measures to manage the COVID-19 spread, including mandatory lockdown, curfew as well as closure of airport and government facilities, will lead to closure of businesses and reduced domestic demand as household suffer from labor income shock. As a result, the services sectors, such as trade, transport, financial sector, religious tourism and others will continue to be the hardest hit. Furthermore, the precarious fiscal position of Iraq will limit the ability of the GoI to introduce a fiscal stimulus package

that will weather the shock on the private sector. It will also force the government to scale back public investments on key basic services, making the situation worse. Overall, this is projected to lead to a contraction of non-oil GDP by 4.4 percent in 2020. As conditions gradually ease over the near-term, and in the absence of structural reforms, non-oil economic activity is expected to slightly rebound to an average of 4 percent over 2021–2022.

Iraq's fiscal loosening is unsustainable going forward and risks critical funding on public investments. Iraq's build-up of non-discretionary spending throughout the past years and the absence of measures to boost domestic revenue mobilization has increased reliance on oil revenues windfalls, leading to an unsustainable fiscal position in 2020 and beyond. Indeed, the stimulus package that was introduced late 2019 coupled with weaker oil prices are projected to have detrimental fiscal effects. If oil prices remain in the low-US\$30s per barrel and in the absence of any measures that will curb the public wage bill and pensions, the budget deficit for 2020 is projected to exceed 29 percent of GDP. To showcase the severity of the fiscal situation, Iraq would need at least a US\$58/barrel oil price to meet its wage and pension obligations alone.¹⁷ Unless there is a significant reorientation in fiscal policy in the delayed 2020 budget law to tackle spending rigidities and domestic revenue mobilization, there will be limited fiscal space to finance COVID-19 response, invest in human capital and long-term development as well as financing post-war reconstruction. Moreover, investments in the development of oil and gas fields could also be at risk as government will be forced to undertake public investment cuts.

Securing budget financing will be challenging in the absence of a fiscal consolidation plan. Deteriorating fiscal conditions coupled with debt amortization, especially the rollover of domestic treasury bills, worsen debt dynamics (Table 1) and signal that Iraq's gross financing needs may reach US\$67 billion (over 39 percent of GDP) in 2020. External

¹⁶ In real terms.

¹⁷ This follows additional public sector hiring and changes to the pension law introduced last October.

BOX 3 • COVID-19 Impact on Poverty in Iraq

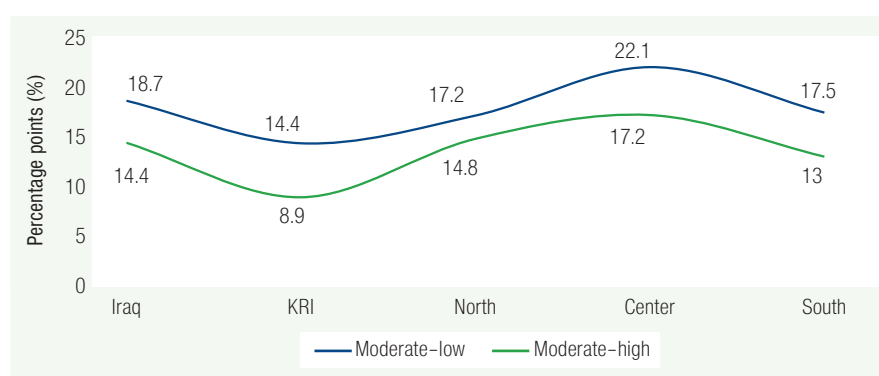
Besides the immediate and tragic impacts of the COVID-19 pandemic on health, the preventive behavioral responses by households and the government's transmission control policies are likely to affect Iraqi households' livelihoods and welfare through multiple channels. First, the need to attend sick family members or to recover from the illness and the sharp decline in economic activities will reduce households' labor earnings from wages and self-employment. Second, the economic slowdown will reduce domestic and international remittances, impacting households' non-labor income. In addition, fiscal pressures due to significantly lower oil prices could affect food (Public Distribution System – PDS) and public cash transfers. Third, disruption in domestic and international supply chains may increase prices, particularly for food, while reduced access to education, healthcare, transport and other services will also significantly impact the welfare of the Iraqis. These short and medium-term effects can have lasting impacts on economic growth, intergenerational mobility and the ability to escape poverty or remain above it.

We assess impacts of the crises on poverty in Iraq using the 2017–18 Rapid Welfare Monitoring Survey (SWIFT) and micro-simulations. The analysis focuses losses in labor income and food price increases as the most likely channels. We assume no change in PDS transfers.^a

The analysis examines a 20 percent increase in food prices with the value of PDS held constant. We also use the employment status of the household head to classify households into five categories: self-employed in rural areas; self-employed in urban areas; public sector; private sector; and not working. Under a “moderate-low” scenario, employees in the public sector and self-employed in rural areas are assumed to maintain full incomes while employees in all the other sectors are assumed to lose 20 percent of pre-crisis income. The “moderate-high” scenario is same except public sector employees also lose income by 20 percent due to fiscal pressures from much lower oil prices. Results are presented in Figure a. Under the moderate-low scenario poverty in Iraq would increase by 14.4 percentage points, and by 18.7 points under the moderate-high scenario, a near doubling of national poverty. These impacts vary across regions. The impact is highest in northern and central Iraq where there are many households living just above the poverty line. In Kurdistan, low initial poverty rates mean fewer vulnerable households while in the south higher initial poverty rates mean many vulnerable households are already poor.

This initial analysis assumes only moderate economic impacts. However, employment-related income losses could be significantly higher. At the same time, household resilience has been tested by years of conflict and displacement. High numbers of displaced, a lack of economic opportunities, political turmoil and fiscal pressures had already left many vulnerable before the start of the current pandemic. Many households are may lose all their incomes, especially those in the informal private sector. The longer the crisis continues, the more any savings or coping mechanisms will be exhausted. In the absence of a significant government response, it is possible that over half of the population could fall into poverty.

FIGURE A • Impacts of Twin Crises on Poverty



Source: WB satff estimates.

^a The microsimulation employed is a partial equilibrium analysis and does not account for behavioral responses. A one-to-one income to consumption adjustment is assumed. Household expenditure is used as the measure of welfare, in line with national poverty estimates, and household welfare is nowcasted based on macroeconomic outcomes to create a current baseline for the simulation.

financing is very limited considering the capital flight from emerging markets. This means global market conditions are unfavorable for Eurobond issuances or other commercial debt, and project financing is expected to decline especially with cuts to public investment. As a result, financing is expected to be originated from domestic sources primarily. This comes with several risks. Over-reliance on local markets for financing the budget increases the cost of debt service and repayment risks given that domestic debt is more expensive and mostly short-term. They also increase liquidity risks as they would crowd-out private sector credit. The report projects a financing gap that could reach up to US\$54 billion in 2020 under the current oil price assumption (US\$30 per barrel). In the absence of any adjustment, monetizing the deficit through CBI could be the only government recourse. Doing so weakens the CBI's balance sheet and creates pressures on the exchange rate and inflation. Large financing needs are also projected to persist in 2021 and 2022,¹⁸ raising sustainability questions over the current fiscal policy trend.

Iraq is also expected to face a persistent current account deficit driven mainly by lower oil prices and rigid imports structure. Amidst a negative global outlook for the oil market, the twin deficits in Iraq are projected to lead to a protracted current account deficit (Table 1.). This is expected to be financed partially from CBI foreign currency reserves, increasing the country vulnerability to external shocks during the forecast period as those reserves drop below 3 months of imports by 2022. Iraq could increase oil production and not abide by the new OPEC+ agreement, to mitigate the widening of the deficit, albeit at the risk of further reducing oil prices.

Risks

Prolonging fiscal loosening policies pose significant risks. In the absence of consolidation, the fiscal and external positions will sharply deteriorate as operational expenditures remain at an unsustainable pace, and uncertainty surrounding oil markets prospects

mounts. These imbalances will further constrain fiscal space critically needed for non-oil investment, limit the government's ability to use discretionary fiscal policy, and if left unaddressed, will raise concerns about the sustainability of policies. Further deterioration of the fiscal position arising from the revenue shortfalls and high fiscal deficit would further crowd out private sector credit, push public debt to unsustainable levels, and thus increases the risk of spending arrears re-emergence.

Downside risks could worsen macro-financial dynamics. If oil prices decline further which, particularly if combined with further delays in fiscal adjustment, Iraq could also be faced with a tradeoff of issuing more domestic debt or drawing down external buffers at the risk of affecting domestic liquidity and reduce investor confidence. This situation could also entail pressures on the exchange rate peg, sovereign rating downgrades, higher financing costs, and thereby hindering growth prospects.

The outlook is also subject to significant political and social risks. Lower oil prices may force Gol to consider austerity measures, a move that could spark more social unrest with already poor public services and high unemployment. This would subside the non-oil growth prospects and further limit long-awaited reforms and negatively affect confidence and economic prospects. The country's weak healthcare system and close relations with Iran will make Iraq's ability to respond to COVID-19 crisis more challenging.

¹⁸ The report projects budget financing needs to reach 55 and 51 billion respectively in 2021 and 2022. This is equivalent to 26.7 percent of GDP in each year.

TABLE 1 • Iraq: Selected Economic and Financial Indicators, 2017-2022

	2017	2018	2019e	2020p	2021p	2022p
Economic Growth and Prices						
Real GDP (percentage change)	-2.5	-0.6	4.4	-9.7	1.9	7.3
Non-oil real GDP (percentage change)	-0.6	1.2	4.9	-4.4	5.5	2.7
GDP per capita (US\$)	5,058	5,641	5,841	4,282	4,858	5,273
GDP (in ID trillion)	231.0	265.0	276.7	202.4	229.7	249.3
Non-oil GDP (in ID trillion)	144.3	180.5	156.3	151.0	161.7	169.4
GDP (in US\$ billion)	195.5	224.2	234.1	171.3	194.3	210.9
Oil production (mbpd)	4.46	4.61	4.84	4.03	4.02	4.44
Oil exports (mbpd)	3.33	3.50	3.54	2.84	2.78	3.03
Iraq oil export prices (US\$ pb)	49.1	65.5	61.1	30.0	39.8	42.3
Consumer price inflation (percentage change; average)	0.2	0.4	-0.2	1.3	2.0	2.2
In percent of GDP						
Public Finance						
Government revenue and grants	33.5	40.2	38.9	22.1	24.5	25.7
Government oil revenue	28.2	36.1	35.9	18.2	20.8	22.2
Government non-oil revenue	5.3	4.1	3.0	3.9	3.7	3.5
Expenditures	32.2	29.0	37.6	51.8	45.1	42.7
Current expenditure	25.1	23.8	28.8	45.3	39.4	37.4
Wages and salaries	14.2	13.5	14.7	25.7	23.4	22.2
Goods and Service	1.6	1.5	3.2	2.9	1.8	1.7
Interest payment	1.0	1.1	1.1	2.0	1.7	1.7
Other	8.2	7.7	9.8	14.7	12.5	11.9
Investment Expenditure	7.1	5.2	8.8	6.5	5.7	5.3
Oil investment	5.4	4.0	6.9	5.3	4.6	4.3
Non-oil investment	1.7	1.3	2.0	1.2	1.1	1.0
Primary fiscal balance, cash basis	2.3	12.3	2.4	-27.7	-18.9	-15.3
Budget balance	1.3	11.2	1.3	-29.6	-20.6	-17.0
In percent of GDP, unless otherwise indicated						
Public Debt						
Total government debt (percent of GDP)	58.9	49.3	44.6	81.2	84.4	87.4
Total government debt (US\$ billion)	115.2	110.4	104.4	139.0	163.9	184.3
External government debt (percent of GDP)	35.6	30.6	23.1	n/a	n/a	n/a
External government debt (US\$ billion)	69.5	59.0	54.0	n/a	n/a	n/a
Monetary Indicators						
Growth in broad money	2.6	2.7	8.4	-2.2	6.0	4.6
Policy interest rate (end of period)	4.0	4.0	4.0	4.0	4.0	4.0

(continues on next page)

TABLE 1 • Iraq: Selected Economic and Financial Indicators, 2017-2022 (continued)

	2017	2018	2019e	2020p	2021p	2022p
In percent of GDP, unless otherwise indicated						
External Sector						
Current account	1.8	6.9	2.5	-18.0	-10.7	-4.5
Trade balance	2.7	6.1	-6.3	-10.9	-3.6	-0.4
Exports of goods	38.1	44.0	37.1	19.1	21.8	23.4
Imports of goods	35.4	38.0	43.4	30.1	25.4	23.8
Gross reserves (US\$ billion)	49.0	64.3	67.6	33.9	13.2	3.6
In months of imports of goods and services	10.3	11.1	10.1	6.0	2.3	0.7
Exchange rate (dinar per US\$; period average)	1182.0	1182.0	1182.0	n/a	n/a	n/a

Sources: Iraqi authorities; and World Bank staff estimates and projections.

LAYING THE FOUNDATION FOR A NEW ECONOMY IN IRAQ: DIGITAL TRANSFORMATION

Introduction

This special focus of the digital economy (DE) highlights and explains the importance of digital transformation for Iraq and why this transformation needs to happen now. Iraq's economic condition was gradually improving following the deep economic strains of the last three years. However, the recent unrest highlights the continued fragility of the country context and the high priority of improving economic opportunities, particularly for youth. Leveraging the DE will help Iraq address its citizens' concerns as well as accelerate the achievement of its development objectives.

The paper will cover five foundational, interconnected elements of a DE as defined by the World Bank Group's (WBG) DE framework,¹⁹ which are: 1) **Digital Infrastructure:** The wide availability of affordable and quality Internet will be instrumental

to bringing more people and businesses online.

2) **Digital Financial Services (DFS):** The ability to pay, save, borrow, and invest through diverse digital financial tools is crucial for financial inclusion, for the growth of the e-commerce market, or for the transition of Iraq to a cashless economy. 3) **Digital Platforms:** The presence and use of digital platforms that can support greater digital exchange and transactions, as well as boost online access to public services will simplify civic functions and national ID systems. 4) **Digital Skills:** The development of a tech-savvy workforce that possesses the digital skills necessary for the jobs of the future as firms shift to increased technology adoption and innovation. 5) **Digital Entrepreneurship:** Critical to the widening and deepening of a digital economic transformation is the

¹⁹ World Bank Digital Economy Diagnostic Framework.

presence of an ecosystem with high-quality support to entrepreneurs, startups and bigger companies to generate new products and services that leverage new technologies and business models.

The report provides an overview of each foundational element, highlighting strengths and weaknesses and proposing illustrative policy recommendations for the Government of Iraq (GOI). It also examines where the country is today and sheds light on where it should be, given the imperative to catch up with Iraq's peer countries and the need to address structural challenges facing the economy.

Digital transformation is reshaping the global economy, permeating every sector and aspect of daily life—changing the way we learn, work, trade, socialize, and access information and services. In 2016, the global DE was worth some \$11.5 trillion—equivalent to 15.5 percent of the world's overall GDP. This is expected to reach 25 percent in less than a decade, outpacing global economic growth. However, countries such as Iraq are capturing a mere fraction of this growth and need to invest strategically in the foundational elements of their DE to keep pace.

There are signs of a nascent DE in Iraq but taking these promising developments to the next level will require important policy decisions and well-developed action and implementation plans. The challenges and opportunities presented by the DE should be accessible to the general public via clear and simple analyses that can be understood by a variety of audiences. This special focus is an attempt to make the Iraqi public aware of the importance of such policies and the role of government in proposing and implementing this agenda.

The Importance of the Digital Economy

Universal adoption and effective application of digital technology is expected to characterize economies of the future. It will shape their ability to succeed in the global marketplace and offer a better quality of life for their citizens. Well-functioning digital economies are expected to achieve faster economic growth, offer innovative products and services, and

create additional job opportunities. Assessing where strategic investments and interventions need to be made is a critical first step to enabling DE growth.

While digital technologies are spreading, digital dividends and inclusion—the broader development benefits from using these technologies, are not. Over 60 percent of the world's population remains offline and cannot participate in the DE. Digital divides persist across gender, geography, age, and income level. Many advanced economies are facing polarizing labor markets and rising inequality because technology augments higher skills while replacing routine jobs, forcing many workers to compete for low-paying jobs.

The development of an enabling DE needs to be broader than the creation of an ICT strategy. Connectivity for all remains an important goal and a tremendous challenge, but attention must also be paid to regulations, skills, and governance. Digital investments need the support of regulations, improved skills, and accountable institutions. Digital technologies can, in turn, augment and strengthen these complements, and accelerate the pace of development.²⁰

In Iraq, building a vibrant DE is a critical step on the path to economic diversification and sustainable progress. As discussed previously, Iraq needs to lessen its oil reliance. Other countries in the Gulf and North Africa are moving towards a digitally enabled economy, and Iraq runs the risk of being “left behind” if the necessary interventions are not made, especially in light of the recent COVID-19 health crisis. Diversification of the economy can build on Iraq's comparative strengths and demographics to foster the development of digitally enabled sectors and industries, such as connectivity, trade-in services, and construction. It can also help strengthen the Iraqi government, as an institution, by digitizing critical civic functions in order to better serve the Iraqi population.

Poor governance has transformed Iraq's strengths—oil wealth and diversity—into twin liabilities of oil dependence and ethnic and sectarian

²⁰ World Development Report 2016: Digital Dividends, World Bank.

BOX 4 • COVID-19 Impact on the Digital Economy

The COVID-19 health crisis further highlights how technology plays an increasingly important role in adapting to the new reality of life during a pandemic. In fact, this health crisis proves that broadband is no longer a luxury but a necessity.

Innovative technological solutions are being deployed in (1) telemedicine and health—including for prevention, diagnostics, and treatment, (2) accommodating an isolated work environment as the public and private sector shifts to home-based work, (3) managing global supply-chains and logistics—especially for hard to reach populations and regions, (4) increasing use of digital financial services and decreasing reliance on cash, (5) delivering educational content to primary, secondary, and tertiary students through virtual classrooms, to name a few.

In the era of “social distancing”, individuals will increasingly rely on mobile apps, online platforms, and the Internet to receive basic supplies and perform other day-to-day transactions such as banking, paying taxes, or even to receive social welfare payments and/or receive stimulus payments from the government.

fragmentation.²¹ Iraq’s institutions have been severely debilitated by decades of wars, sanctions, and conflict. Poor governance has contributed to undermining the state’s legitimacy, leading to political and sectarian divides resulting in further weakening of an already fragile governance system.²² Incorporating digital technologies and platforms, coupled with other measures such as providing public officials with incentives to effectively use technology,²³ can help increase transparency and rebuild trust between the Gol and its citizens.

The development of an enabling DE needs to be broader than the creation of an ICT strategy. Connectivity for all remains an important goal and a tremendous challenge, but attention must also be paid to regulations, skills, and governance. Digital investments need the support of regulations, improved skills, and accountable institutions. Digital technologies can, in turn, augment and strengthen these complements, the pace of development.

The current COVID-19 pandemic is likely to further exacerbate some of the challenges faced by Iraq. Unemployment is likely to rise as businesses shut down either because of preventive measures enforced by the Gol (or because of a loss in demand for goods and services. Low-productivity and informal workers will be at high risk of falling into deep poverty, further complicating Iraq’s reconstruction efforts. It is expected that corporations and public offices will shift to home-based work and the Gol will need to rely on digital technologies to ensure that public services, businesses, and individuals are able to withstand “social distancing”, ensure business continuity, and

prevent service interruptions. Thus, critical DE reforms are now a prerequisite for ensuring Iraq’s survival during this global health crisis.

Current State of Iraq’s Digital Economy

Digital Infrastructure

Digital infrastructure refers to the availability, quality, and affordability of high-speed Internet. It also serves as the backbone of the DE. Countries are unable to realize the full potential of digital transformation without reliable and affordable connectivity, so the latter is a highly critical prerequisite for Iraq’s DE to thrive. Once it is deployed, the five foundational elements can benefit from mutual synergies. Infrastructure that provides reliable and fast Internet access is needed for entrepreneurs to create value, students to build their skills, and the government to improve service delivery platforms.

High speed connectivity increases output and productivity in other sectors and enables a more competitive economy overall. Evidence from several global studies indicates that broadband penetration enhances economic growth, with the

²¹ World Bank. 2017. *Iraq – Systematic Country Diagnostic*. Washington, D.C.

²² Ibid.

²³ World Bank. 2016. *World Development Report 2016: Digital Dividends*. Washington, DC.

impact estimated to be, on average, around 0.85 to 1.16 percent increase in GDP for every 10 percent increase in Internet penetration.²⁴ The impact in the Iraqi context could be even greater, since there are opportunities for Iraq to adopt “leapfrogging” technologies when broadband access is coupled with interventions that promote digital skills and entrepreneurship. In Iraq, broadband demand has long since outstripped its supply, indicating a need to improve infrastructure to meet the demands of consumers and grow the other elements of the DE. As a result, interventions must focus on each of these elements, though a fundamental prerequisite is infrastructure.

Challenges & Opportunities

Digital infrastructure can accelerate Iraq’s economic recovery through several channels:

- **Investing in digital infrastructure deployment creates immediate opportunities to boost employment.** Evidence further suggests that for every job created in broadband infrastructure deployment, between 1.83 and 3.42 additional jobs are indirectly added or induced in the economy—higher than most other infrastructure investments.²⁵ Though employment generation alone is generally not considered sufficient rationale to undertake an infrastructure project, such projects can improve quality of life for Iraqis in a holistic manner.
- **Access to digital infrastructure augments trade and economic diversification.** Economic diversification away from oil is a key priority for Iraq, and there is evidence that improving Internet penetration in developing countries will promote service industries and increase exports.²⁶
- **Increasing Internet penetration is associated with higher private-sector productivity, which is of immense importance in the context of Iraq.** Research indicates that firms that adopt digital technologies are 26 percent more profitable than their competitors who do not. The development of digital infrastructure is thus a vital intervention for Iraq to strengthen its economic competitiveness.
- **Improving and facilitating service delivery, including to refugees and host communities.**

Digital infrastructure enables important services such as e-health, e-education, energy payments, and financial inclusion, among others.²⁷ These avenues also improve transparency and public engagement and can help rebuild public trust in the government.

Comparison with Other Countries; Iraq’s Potential

The difference between the adoption levels of fixed and mobile broadband is flagrant in Iraq as much as it is in other countries in the MENA region. Lebanon and Jordan are leaders in the use and adoption of fixed and mobile broadband services, and Iran has a comparatively high broadband penetration rate. Yet overall, a considerable gap remains in the adoption, speed, usage and affordability of fixed broadband services between Iraq and the MENA region, as well as between Iraq and emerging economies such as Turkey, Romania, and Bulgaria—countries that compare positively in terms of DE development.

Several institutional and regulatory hurdles have constrained broadband Internet adoption and the DE at large. The telecommunications sector falls under the purview of Ministry of Communications and the Communications and Media Commission (CMC), which have conflicting and insufficiently defined roles. This can be traced to the absence of a comprehensive telecommunications law. The CMC itself was founded in 2004 by an order of the Coalition Provisional Authority (CPA) following the war, and subsequent Iraqi governments have not been able to pass a thorough telecommunications law since then.

Due to these institutional shortcomings and to the damage caused by extended conflict, Iraq’s fixed broadband market has not reached its

²⁴ Mashreq 2.0.

²⁵ Katz, Raul, and Stephan Suter. “Estimating the economic impact of the broadband stimulus plan.” *Columbia institute for tele-information working paper* 7 (2009).

²⁶ Clarke, George R. G. 2008. “Has the Internet increased exports for firms from low- and middle-income countries?”. *Information Economics and Policy, Elsevier, Vol. 20, No. 1, pp16–37. <https://ideas.repec.org/a/eee/iepoli/v20y2008i1p16–37.html>.*

²⁷ Mashreq 2.0.

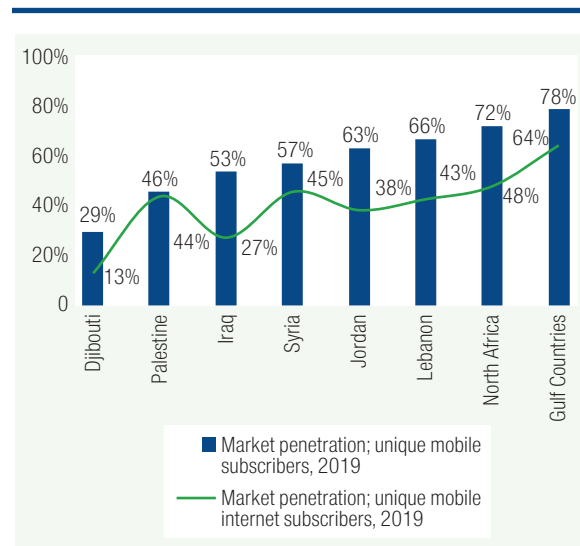
potential. Fixed broadband penetration stands only at 17.4 percent. As a step in the right direction, the GOI has since 2014 prioritized the deployment of fiber-to-the-home (FTTH) in certain urban centers such as Baghdad. However, this initiative is being rolled out on a limited, ad hoc basis and has yet to create any sweeping impact.²⁸ Moreover, telecom networks—especially in the densely populated capital—have been under an unusual amount of stress due to violent conflict, including competition from illegal operators and prevailing signal jammers,²⁹ severely impacting the quality of broadband service for Baghdadis.³⁰

Despite these adversities, Iraq’s mobile broadband sector is among the most competitive in the MENA region. There are three main licensed mobile operators in Iraq: Zain Iraq (42.4 percent market share), Asiacell (37.4 percent market share), and Korek Telecom (20.2 percent market share).³¹ Though mobile penetration is high (near 100 percent, indicating that many SIM cards are sold and used), mobile broadband penetration is much more modest (19 percent of the population).³² Moreover, all three major operators offer only Global System for Mobile Communications (GSM) and 3G connectivity. The only provider of 4G services is Fastlink, which operates exclusively in the semi-autonomous region of Iraqi Kurdistan. Iraq’s mobile market has shown further interest from the private sector, and Iraq’s cabinet approved plans to relaunch attempts to auction a fourth mobile license, after its previous attempt in late 2015 stalled due to political instability and conflict.

Releasing and allocating 4G frequencies is essential for digital services in Iraq to take off and meet the aspirations of the citizens and effect economic development. Many countries worldwide—including Gulf Cooperation Council (GCC) nations—are already testing 5G technologies that enable faster speeds, better quality, and a whole new range of applications that connect devices and systems at a large scale. In an effort to “catchup” through the allocation of 4G frequencies, mobile operators would be able to upgrade their networks and provide faster, more reliable, and higher-quality mobile broadband services.

There is a gap between basic mobile adoption and mobile broadband adoption in Iraq (Figure 25.

FIGURE 25 • Penetration of Mobile and Mobile Broadband Services (per 100 Inhabitants)



Source: Global System for Mobile Communications Intelligence (GSMA), 2018.
^a Cited in Mashreq 2.0, pg. 23.

Penetration of mobile and mobile broadband services (per 100 inhabitants)). The stark gap between basic mobile penetration and mobile broadband penetration is a commonality in countries that have faced prolonged conflict, such as Djibouti and Syria. However, the market in Iraq is competitive and would leapfrog much faster than those comparator countries if the right policies and reforms were put in place to allow mobile operators to invest in new technologies in a regulated environment.

Iraq’s location at the crossroads of the highest-growth segment of global data connectivity—the Europe-Asia Internet traffic route—offers an opportunity for Iraq to develop a regional data hub. International connectivity will link Iraq to the worldwide Internet infrastructure. In most countries, including in the MENA region, international connectivity

²⁸ Telegeography.

²⁹ This refers to blocking transmission or reception of signals resulting in loss of signal quality for the end user.

³⁰ <https://www.wired.com/2014/02/spectrum-warfare/>.

³¹ Telegeography.

³² Unique broadband subscribers.

is provided through submarine cables, with a smaller percentage provided through terrestrial fiber, microwave, or satellite. However, redundancy and alternative routes are rising in importance and demand, since any interruption in international connectivity inflicts considerable costs on affected countries and the world economy at large. The strategic position of Iraq stems from its connection to the submarine cables at Al Faw at the Persian Sea and its borders with Turkey, Syria, Jordan, and Iran, allowing it to provide alternative terrestrial connectivity from the Persian Sea to Europe. International connectivity is owned and managed by the Ministry of Communications through the Iraq Telecommunications and Post Company (ITPC), which has yet to expand international connectivity and take full advantage of the competitive edge that Iraq's geographic position entails.

Digital Financial Services (DFS)

A robust cashless payments ecosystem is a critical pillar of any DE. DFS refers to transitioning to a cashless economy. DFS is an important avenue for the transactions and payments of goods and services between users, and between citizens and governments. While payments in Iraq are still mostly made in cash, the growth of digital payment methods has been exceptional. The share of the adult population that has made at least one digital payment a year nearly quadrupled between 2014 and 2017 and reached 19 percent in 2019. However, growth can only be sustained if Iraq supports it with the necessary infrastructural investments and regulatory reforms.

The GOI has pledged its support for a cashless economy. It committed to establishing a conducive regulatory and policy framework for digital payments, investing in an interoperable infrastructure, and striving towards universal financial access.

Challenges & Opportunities

The Iraqi National Payment System faces multiple challenges. Infrastructure—including electricity provision and network connectivity—is not always reliable, hampering access to digital payments. This problem is compounded by a human resources crisis, with many qualified Iraqis having immigrated abroad

and specialist engineering or analytics vacancies remaining unfilled. This gap affects the GoI's ability to implement, manage, and oversee the regulation of digital financial transactions. The economy is cash-based as a result of the most recent conflict, and the financial system and its institutions enjoy little trust.

Despite the above, Iraq has in recent years made considerable progress toward developing its payment systems, but gaps remain. With assistance from USAID, as well as strong commitment from the CBI and the GoI, the Iraqi National Payment System Strategy (NPS),³³ discussed below, was developed to help Iraq transition toward a cashless system.³⁴

A clear regulatory framework is also critical to attracting private sector and telco participation. To that end, the CBI has enhanced the legal, regulatory, and oversight framework, but several gaps remain, notably the lack of a statutory law that covers all payment and settlement systems topics in a holistic manner, as well as the lack of an articulated oversight framework and the necessary oversight tools. The GoI is at the final stages of passing its NPS Act that will establish firm legal foundations for payment and settlement systems. Other secondary legislation, specifically CBI regulations, must also be reviewed to ensure compliance with the new law.

Comparison with Other Countries: Iraq's Potential

Despite efforts by the GoI, Iraq trails its MENA peers on most cashless economy indicators. Consequently, the most important task of all NPS stakeholders is to restore trust in the system. Iraqis must feel with certainty that money held in their bank accounts is as safe as

³³ The NPS Strategy is intended to guide the CBI in its role as regulator, overseer, operator and catalyst of the National Payments System.

³⁴ In technical terms, this includes: a real time gross settlement (RTGS) system; Cheque enabled Automated Clearing House (CACH) for clearing and settlement of cheques in truncation mode; the Government Securities Registration System (GSRS)—a Central Securities Depository (CSD) and Securities Settlement System (SSS) for Central Bank and Government securities; and Retail Payments Systems Infrastructure (RPSI), an integrated card, mobile payments, and electronic funds transfer system.

that stored in banknotes, and that electronic payment instruments are as reliable as cash payments. Some of the required actions, such as setting up an effective deposit insurance scheme, lie beyond the scope of NPS regulations and oversight, and should be taken up by other parts of the CBI. Nonetheless, there are many other improvements that can be affected with relatively little cost, such as the establishment of a consumer protection framework and improved monitoring of the operational reliability of payment systems' participants.

Iraq has set ambitious targets in its NPS Strategy to catch up in the next five years on debit card ownership, cashless transactions, mobile money and electronic payments. The NPS Strategy for Iraq aims to guide a range of diverse stakeholders in their actions and goals to develop payment systems, instruments, and regulations. The stakeholders range from the CBI to commercial banks, government agencies, non-bank e-money issuers, telecommunications and technology companies, as well as the end users of payment products: Iraqi citizens and businesses.

A recent positive development is the issuance of e-Wallets: the GoI through the CBI has licensed two Payment System Providers (PSPs) to deliver this service. In addition, as part of its COVID-19 initiatives, CBI facilitated the process for Iraqi citizens to open e-wallets from their homes through a simplified e-KYC³⁵ process using only their IDs. The GoI is currently running a campaign to promote the usage of cashless and contactless payments solutions (i.e. e-wallets/ POS/ POC and ATM's) through the launch of the e-wallet scheme, the issuance of a promotional public information campaign including video etc.

Digital Platforms

Digital Platforms is a broad category that explores two main types of platforms: public-sector platforms and private-sector platforms. Digital platforms help governments streamline civic functions such as filing taxes online and starting a business. For domestic firms, platforms provide stronger productivity and innovation through competition in the global digital market. Public-sector digital platforms include e-government services such as e-procurement and national ID systems that enable citizens to access

social services. Private-sector digital platforms includes DFS and e-commerce.

Digital services also have the potential to increase inclusiveness and transparency. The automation of business processes and improved monitoring can reduce bureaucratic discretion and opportunities for petty corruption. Frontier technologies such as blockchain for e-governance can also be deployed to improve accessibility to critical services such as digitally enabled healthcare and education to improve social welfare outcomes.

The use of technology in governments tends to be successful when it addresses straightforward information and monitoring problems. For more demanding challenges, such as better management of providers or giving citizens greater voice, technology helps only when governments are already responsive. Closing the gap between evolving technology and bureaucratic institutions requires initiatives that strengthen the transparency and accountability of governments.³⁶

In the context of Iraq, critical digital platforms include:

- **An e-Government** platform that simplifies administrative processes while eliminating administrative corruption and red tape. This includes online business registration with an online payments function. Iraq currently ranks 172 out of 190 overall on the 2020 *Doing Business* Ranking and 154 for starting a business.
- **Digital ID** systems to enable Iraqis to exercise their rights and access services. It also helps the country realize the transformational potential of inclusive, robust, and responsible digital identification systems. Including tangible benefits across a range of areas, such as financial inclusion, health services, social protection for the poorest and most vulnerable, and empowerment of women and girls.

³⁵ This stands for Know Your Customer/Client guidelines. Financial services require that professionals make an effort to verify the identity, suitability, and risks involved with maintaining a business relationship.

³⁶ Cited in the World Development Report 2016: Digital Dividends., p. 24.

- **Public Digital Transactions** refers to digital infrastructure and processes critical to public administration such as revenue collection, budget management, treasury, civil service payroll, and Human Resource Management Information System (HRMIS) at all governmental levels (central, local, and municipal).
- **Cybersecurity:** as economies become more dependent on digital technologies, they also become more vulnerable to network attacks. The most serious cybersecurity risks are those that threaten the functioning of critical information infrastructures, such as those dedicated to financial services, control systems for power, gas, drinking water, and other utilities; airport and air traffic control systems; logistics systems; and government services. A robust cybersecurity framework as per international best practices must be co-developed and implemented alongside any digital platform.
- **Data Protection** or the process of safeguarding important information from corruption, compromise, or loss. The importance of data protection increases as the amount of data created and stored continues to grow at unprecedented rates. The implementation of a successful Digital ID system also hinges on a robust data protection framework.
- **E-commerce** can unlock significant downstream employment in novel areas, such as digital advertising, as well as in traditional areas such as logistics, warehousing, and shipping. Chinese e-commerce giant Alibaba, while directly employing just over 85,000 employees, created 14 million jobs for sellers on its platforms in 2017, and a further 22 million downstream jobs in areas such as R&D, design, manufacturing and logistics.³⁷ These benefits are particularly important in Iraq's context, where labor force participation is amongst the lowest in the world, at 48.7 percent.³⁸

Challenges & Opportunities

Iraq is still in the early phases of building various digital platforms. Public-sector platforms such as e-government services, including online business registration, are still in early phases, and private-sector platforms such as e-commerce are still nascent in Iraq.

A critical, forthcoming public platform is the digitization of the Public Distribution System (PDS). The PDS is Iraq's biggest social safety net, providing food entitlements to almost the entire population, supported by the UN's World Food Program. This digitized system will ensure citizens' data is safely encrypted and stored, and the security is enhanced using fingerprints or iris scans. These safeguards will allow the GoI to identify and remove duplicate records as well as to conduct biometric verification at the time of food collection. The new system will replace the current paper-based system. A complementary mobile application, myPDS, will also be developed to help Iraqis collect their benefits and update their family information about births, deaths and marriages—using personal smartphones.

To increase the formal participation of firms in the Iraqi economy, the Global Entrepreneurship Registration (GER) project,³⁹ will soon be launching an eRegistration software system. This will allow the GoI to build online databases of formally registered firms and digitize the firm registration process in Iraq by creating an online single window for business registration. This system allows entrepreneurs to see their current registrations, apply for licenses, update their data, and make declarations and payments—either to link a bank account or mobile money system. The eRegistration system will also deploy an innovative donor funding model for private sector development by funding entrepreneurs directly, versus through the government: the user's administrative account can receive money from the government (in the form of subsidies, tax credits or refunds, etc.) or a national development institution (e.g. a foundation), or an international aid agency. The system is anticipated to launch in Spring 2020.⁴⁰

³⁷ Alibaba Group. 2018. *Foundations for Sustainable Growth: ESG Report 2018*. <https://esg.alibabagroup.com/>.

³⁸ <https://www.worldbank.org/en/country/iraq/overview>.

³⁹ A joint initiative of the Global Entrepreneurship Network (GEN), the United Nations Conference on Trade and Development (UNCTAD), and the U.S. Department of State. This software system is already operational in several countries.

⁴⁰ Source: Global Entrepreneurship Network Global Team.

BOX 5 • Sri Lanka's nCoV Surveillance System to Monitor COVID-19 Outbreaks

Example of government implementing a digital platform to monitor COVID-19 outbreaks among its population

The Ministry of Health of Sri Lanka developed a web-based District Health Information Software (DHIS2) solution to capture information on high risk passengers entering the country from at-risk countries for active COVID-19 surveillance.

The nCoV Surveillance System captures demographics, immigration, symptoms of COVID-19 disease, and possible contacts at all ports of entry, for local public health officers, based on their geographic area. From 0–14 days, it captures potential symptoms of COVID-19 disease and any action taken. After 14 days, it captures symptoms of COVID-19 disease and any action taken at the end of the surveillance period.

The Government of Korea has also implemented a similar surveillance system as part of “Special Entry Procedures” for travelers arriving from China that went into effect on February 4, 2020. Other governments, such as Nigeria, have also implemented similar monitoring systems.

Currently, the uptake of private-sector platforms is low. E-commerce could improve the standard of living in Iraq, enabling Iraqi citizens to compare goods in order to find the best prices, stirring an influx of foreign goods and commodities, and creating a more transparent market. Although e-commerce is the easiest digital opportunity that startups can seize in nascent ecosystems, it has been slow growing in Iraq for several reasons, mainly low Internet and banking penetration, and preference of consumers for cash. Another major problem contributing to slow adoption of e-commerce is the low level of literacy among Iraqis, especially the inability to read and write *English*—the primary language of trade and e-commerce globally. In this context, the most popular platforms are emerging Iraqi and MENA-focused e-commerce websites, such as Miswag, Dakakkena, ShopYoBrand, and Opensooq.

Magnitt, a digital platform that has gained traction in the MENA region, was launched by Iraqi expats based in Dubai (UAE). Magnitt has developed a data platform for investors, and currently hosts 5,500 startups and over 12,000 users including over 300 individual investors and over 150 funding institutions.⁴¹ Unfortunately, Magnitt cannot monitor and produce data related to entrepreneurial activity in Iraq yet.

Comparison with Other Countries: Iraq's Potential

Iraq has made considerable progress in the mobile market, but, as discussed above, its broadband access indicators remain weak. Since digital infrastructure is

the basic enabler of digital platforms, low broadband access will hinder the implementation and adoption of digital platforms in Iraq. Across all government platforms indicators, Iraq is 34 percent below the MENA average and 97 percent below the MENA average for private-sector platforms.⁴²

Digital Skills

Digital skills are essential to prepare for the jobs of the future, which will be anchored in the DE.

This in turn promotes economic growth, job creation, and poverty reduction. Investments in digital skills create new opportunities through the creation of new markets and innovative solutions. Digital skills also constitute a key element for social inclusion. As the world moves towards heightened use of technologies, for work or social life, those who do not have the skills to adapt are likely to feel an even bigger sense of isolation.

Digital skills are increasingly important for promoting digital employment opportunities for young Iraqis, especially when job opportunities for youth are very limited. Skills upgrading is critical to prepare young Iraqis for possible digital employment jobs such as online freelancing, microwork, outsourcing, etc. Beyond digital employment, given that the future of work depends on a certain level of digital literacy and an aptitude to advance digital skills for higher

⁴¹ Mashreq 2.0.

⁴² WBG.

value-added work, the fact that many Iraqi youth work in basic occupations further emphasizes the importance of upgrading their skills for the future of their work.

Challenges & Opportunities

The ICT sector in Iraq is small and the little employment it creates (3–5 percent) does not cater to youth. In fact, only 20 percent of the jobs in the ICT sector are occupied by youth. This is surprising given that the younger age group is familiar with the use of Internet and technologies (25 percent of the population aged 15–24 years) much more than the older generation (less than 15 percent among the population aged more than 40 years).

A key challenge is the poor labor market outcomes, especially among youth. Out of the approximately seven million youth aged 15–24, around 48 percent are Not in Employment, Education, or Training (NEET). Compared to the national unemployment rate of 16 percent, youth unemployment is about 36 percent.⁴³ Among youth, the unemployment rate is higher for women (65 percent). There are also high levels of underemployment, affecting 32.4 percent of youth between the ages of 15 and 24. Most youth who have jobs are employed in low quality jobs either as low-productivity self-employment or as informal sector wage employees.

Conflict and instability have further exacerbated the situation and resulted in high youth unemployment. Iraq's fast-growing youth population,⁴⁴ means high labor force growth and accelerated demand for youth employment. The dominance of public sector employment (represents 42 percent of jobs) and youth's preference for public sector jobs causes significant labor market distortions. The private sector is undiversified, under-developed and uncompetitive and, therefore, does not create sufficient quality jobs. In the absence of relevant education and training systems, skills mismatches remain a significant challenge, with individuals not having the right skills to match the requirements of available job openings, or of limited opportunities to access high quality pre-employment or skills upgrading training programs.

The skills mismatch gap remains largely in the education system's failure to equip youth with jobs-relevant skills in general, and digital skills,

in particular. In fact, public sector training providers, including universities, are not well prepared to support the development of digital skills in Iraq. They are constrained by traditional academic curricula that were tailored for public sector jobs and do not meet the requirements of the DE. For example, the Ministry of Communications has its own training institution, the Higher Institute for Communications and Post,⁴⁵ and employs many of its own graduates in its workforce of approximately 13,000.⁴⁶

The annual skills supply to the ICT sector from formal Technical and Vocational Education Training (TVET) institutions at all levels amounts to more than 11,000 graduates. The largest proportion (over 3,000) is low-level computer repair graduates from the Ministry of Education (MOED) schools and the Ministry of Labor and Social Affairs' vocational training centers. Electronics programs produce the second largest cohort of graduates (over 2,000) for the sector. Computer systems and information technology programs produce more than 1,000 graduates each. Less than 1,000 students graduate each year for networks, databases, software, and media occupations though there is evidence of sector demand for these specific services.

However, formal qualifications do not seem to be highly valued by employers, and qualifications are not a high-ranking selection criterion for employment, suggesting a disconnect between TVET institutions and employers. Additionally, 77 percent of ICT employers offered training to their employees, presumably in areas where graduates lack skills, suggesting that formal training institutions should bridge the gap with employers to (1) improve the curricula and ensure they meet market needs, and (2) facilitate job placement for graduates.

⁴³ Dhiraj S., Wai-Poi M. G. (2019). Arrested Development: Conflict, Displacement, and Welfare in Iraq.

⁴⁴ Nearly 50 percent of Iraqis are younger than 19 years, and 60 percent are below 25 years of age.

⁴⁵ It offers three-year diploma courses for preparatory education graduates. While most technicians employed by the Ministry are graduates of the institute, some graduates do enter private sector.

⁴⁶ UNESCO "Assessment of the Labor Market & Skills Analysis Iraq and Kurdistan Region-Iraq".

BOX 6 • Case Study on Digital Skills Providers

Examples of private-sector and public-sector initiatives to facilitate digital skills acquisition

(1) 1337 via École 42 in Morocco: Example of a private-sector initiative facilitating digital skills acquisition

1337 is a coding school established in 2018 by Paris-based École 42 in Khouribga, Morocco. The training covers programming languages such as JavaScript, HTML, or CSS, is completely free of charge. 1337 offers 300 workstations (including the best bandwidth in the market) and staff is available 24 hours a day, 7 days a week.

Impact: With no attendance fees, widespread accessibility, and top-ranked training, 1337 allows social as well as economic mobility.

1337 School is part of the larger 42 Network, which was established in Paris in 2013 by the famous serial entrepreneur Xavier Neil. With 20 partner campuses worldwide, the 42 network represents an international community for digital learning. In 2017, the 42 Network was ranked as the best computer science training program by the CodeinGame computer programming platform.

(2) India's National Skills Development Cooperation: Example of government-driven initiative facilitating digital skills acquisition

The National Skills Development Cooperation (NSDC) was established as a PPP company with the mandate of catalyzing the skills landscape in India. Its objectives are to upgrade the skills of 150 million people to international standards and to develop frameworks for curriculum and quality assurance. NSDC focuses on industry involvement (operational and financial), supports private sector initiatives, and plays the role of a “market-maker”.

Impact: To date, NSDC has trained over 5.2 million students, built 235 private sector partnerships, and introduced vocational training in 10 states, covering over 2,400 schools and benefitting over 2.5 million students. To ensure alignment of education standards, NSDC is working with 21 universities and community colleges and assures National Occupational Standards and certifications. Relatedly, NSDC approved 38 Sector Skill Councils to issue certificates to entities complying with standards and frameworks. Furthermore, it developed and maintains a Skill Development Management System with 1,400 training partners, over 28,000 training centers, 16,000 training, 20 job portals, and 77 assessment agencies.

To address gaps in existing curricula, digital training activities have emerged in the Iraqi ecosystem. Donors and international organizations have launched tech-related events and digital skilling activities that target the youth, students, refugees, and women, with the aim of equipping them with technical skills such as coding, and maker skills, and soft skills, including leadership and entrepreneurship. These activities are emerging across the country, including in Baghdad, Erbil, Mosul, and Sulaymaniyah.

However, corporate and public involvement in digital skills development initiatives remains weak. The potential of corporate involvement remains important and should be mobilized through digital transformation seminars that involve government and banking, oil and gas, and agriculture sectors.

Comparison with Other Countries; Iraq's Potential⁴⁷

Iraq is not currently ranked on the World Economic Forum's Global Competitiveness Index,⁴⁸ which, among many things, measures digital and other skills needed to thrive in the Fourth Industrial

Revolution. Top ranked economies for the MENA region are the United Arab Emirates (27) and Qatar (30). Moving forward, Iraq should address the existing skills gaps to allow youth to reach their potential, and leverage partnerships with the private sector to both grow the digital sector and absorb more digitally skilled labor.

Digital Entrepreneurship

Innovative technology entrepreneurs and start-ups also provide employment and instill an enterprising mindset. This is especially crucial in the context of Iraq where labor force participation is one of the lowest in the world (48.7 percent), especially

⁴⁷ Ibid.

⁴⁸ The Global Competitiveness Index assesses the competitiveness of 140 economies in the context of the Fourth Industrial Revolution. It measures the enabling environment, including ICT adoption, markets, human capital, and the innovation ecosystem. <http://reports.weforum.org/global-competitiveness-report-2018/>.

BOX 7 • Startups on the Rise: Spotlight on Two High-Growth Iraqi Digital Startups

Miswag: An E-Commerce startup founded in 2014 (<https://miswag.net/>):

- The first e-commerce service in Iraq, “Amazon of Iraq”, with delivery service to all major Iraqi cities.
- Miswag’s online shopping platform sells more than 15,000 products from over 250 companies and agencies across 150 departments.
- Miswag is known for displaying and marketing high quality original products that meets the company’s quality control standards.
- Company traction: Miswag has a turnover of more than USD \$2 million.

Sandoog: A Logistics & Last Mile Delivery startup founded in 2017 (www.sandoog.net):

- Sandoog is a last-mile delivery and order fulfilment startup tackling daily challenges faced in Iraq’s logistics using advanced technological and operational solutions.
- It enables businesses and organizations of all sizes to deliver their goods and mail efficiently inside cities and to all corners of the country through its digital platform.
- Sandoog crowdsources its delivery drivers with 10 in Baghdad and 15 throughout the rest of the country.
- Its business model is pay-per-use, with cash on delivery (approximately USD \$7 fee).
- Company traction: Sandoog has over 750 clients and completed deliveries to over 50,000 people since April 2018.

Sources: WBG Interviews; Magnitt.

for youth (26 percent) and women (12 percent).⁴⁹ Through competitive wages, flexible work hours, and a focus on technical skills, many digital industries in other contexts have improved female participation in the work force. In Egypt for example, a smartphone factory created by SICO in Assiut, Upper Egypt, employs over 200 women, who are paid above average wages higher than average for the area.⁵⁰ Innovations such as mobile ride-hailing services are also providing flexible work for women,⁵¹ and a female-only ride-hailing startup has been launched as well was recently launched.⁵²

In August 2019, the acceptance of the first Iraqi startup, Lezzoo, into the Silicon-Valley-based, Y Combinator (YC) accelerator program signaled Iraq’s developing entrepreneurial ecosystem. YC is considered the world’s most prestigious acceleration program, with an acceptance rate of 1.5 percent. Lezzoo was selected based on its scalability, market traction, and potential for international expansion.

Challenges & Opportunities

Due to an unfavorable investment climate, Iraq’s high entrepreneurship potential remains largely

untapped. Digital entrepreneurship is beginning to thrive, and there is an opportunity for a complementary venture capital ecosystem to fund Iraqi entrepreneurs.

While Iraq’s start-up ecosystem is still nascent, it has shown promising signs and has at its disposal, an important domestic market of 40 million consumers. In April 2019, startup hubs in Baghdad, Basra, Mosul, Erbil, and Sulaymaniyah hosted the Iraq Innovation Hackathon, where over 700 young tech entrepreneurs competed for prizes

⁴⁹ <https://www.worldbank.org/en/country/iraq/overview>.

⁵⁰ Abou el Atta, Nadine. 2019. “Technology, Talent, and Upper Egyptian Women.” *Business Monthly*, March.

⁵¹ World Bank. 2018. *Driving toward equality: women, ride-hailing, and the sharing economy*. <http://documents.worldbank.org/curated/en/856531520948298389/Driving-toward-equality-women-ride-hailing-and-the-sharing-economy>.

⁵² Samir, Salwa. 2018. “Female-only ride-hailing app to compete with Uber, Careem in Cairo.” *Al-Monitor*, December 27, 2018. <https://www.al-monitor.com/pulse/originals/2018/12/egypt-fyonka-all-female-ride-hailing-service-uber.html>.

that included financing, coworking spaces, and mentorship.⁵³ Though there is still a long way to go—in 2018, Iraq created only 1 tech startup per million Iraqis, which is 12 times less than in Egypt—the hackathon networks indicate that Iraq has the potential to engage young entrepreneurs. This is especially important in the context of Iraq, where 42% of all jobs are in the public sector. The DE can help shift this status quo of seeking public sector employment toward increased employment in start-ups.

Despite the growing number of entrepreneurship initiatives, the ecosystem still lacks maturity and depth. These manifests itself in the quality and number of services provided by business development support (BDS) organizations such as incubators and accelerators, and in the dearth of early-stage investors that provide much needed startup capital to emerging entrepreneurs.

Comparison with Other Countries: Iraq's Potential

Due to political instability and fragility, Iraq is not currently ranked on leading global entrepreneurship indexes, including the Global Entrepreneurship Index (GEI) developed by the Global Entrepreneurship and Development Institute (GEDI), Startup Genome's Global Startup Ecosystem Report, and the Seedstars Index. However, Iraq's emerging ecosystem could soon be benchmarked against comparable countries. A strong signal is Seedstar's recent Investor Masterclass⁵⁴ conducted in Baghdad in August 2019, sponsored by the CBI.

In the MENA region, the United Arab Emirates (UAE) is considered the most advanced entrepreneurship ecosystem due to its enabling business environment, regional prowess as a leading financial center, and the proliferation of entrepreneurship support organizations BDS providers that cover the entire value chain of entrepreneurship support ranging from pre-incubation to acceleration programming. As demonstrated in other WBG-supported regional entrepreneurship activities,⁵⁵ Iraq should increase linkages with mature ecosystems to 1) showcase local startups to leading investors, corporates, and the media; and 2) attract private-sector actors into its national market. Programs such as Iraqpreneurs are already establishing these types of

linkages, but similar efforts could be further amplified by the Gol.

Conclusion

The WBG and the Gol have jointly identified priority reform areas that have the strongest potential for achieving the objectives of 1) private-sector-led diversification and 2) reforming governance and promoting private-sector participation in selected productive sectors that can subsequently boost Iraq's participation in the DE. These priority reform areas cut across all five elements of the DE framework and are meant to boost accountability, transparency, and trust.

Transitioning Iraq towards a resilient and inclusive DE will require economic reforms and longer-term development priorities along the five DE pillars: ensuring affordable access to high-speed Internet, achieving widespread adoption of cashless payments, delivering digital government services and improving access to data, upskilling young Iraqis with technological know-how, and scaling up the digital entrepreneurship ecosystem.

The proposed short- and medium-term improvements below are prioritized by promoting actions with the highest potential to keep Iraq on track with its commitment to boosting its DE across the five pillars. These eighteen (18) critical recommendations are also included in the Strategic Note on Priority Reform Areas (aka "Iraq White Paper"):

⁵³ ArabNet Team. 2019. "Hubs at Iraq Coordinate to Launch the 1st Nationwide Hackathon". March 27, 2019. <https://www.arabnet.me/english/editorials/events/hubs-iraq-hackathon>.

⁵⁴ Investor Masterclasses are workshops that build knowledge and capacity of local investors. These investors are critical sources of early-stage financing for digital startups who do not qualify for loans from commercial banks.

⁵⁵ Such as the XL Africa and l'Afrique Excellence acceleration programs for African digital startups seeking financing of \$250,000 up to \$5MN. These programs were anchored in Cape Town, South Africa and Paris, France to leverage an international audience.

- **Immediate- to short-term measures:** 1) removing restrictions on private operators to build, own, and operate domestic and international **fiber infrastructure**; 2) promulgating the **Payment Systems Law** to facilitate digital payments; 3) providing a timetable to update the 2012–15 **e-Gov Strategy** and Action Plan for a paperless government; 4) building confidence with **online disclosure of information** on public tenders and contract awards, starting with major transactions, and allowing for public feedback; 5) mandating **start-ups and tech companies registration** to select eligible support structures; 6) adopting a national law on **private equity** and venture capital funds; 7) establishing a **Seed Capital Fund**; and 8) in partnership with the private sector, **piloting digital training programs** for youth to increase their access to digital wage employment opportunities such as online freelancing, microwork, telework, outsourcing, etc.
- **Short- to medium-term measures:** 9) allocating **4G spectrum**; 10) developing and implementing **PPPs** in the rebuilding of critical fiber infrastructure to achieve 10 percent fiber connectivity by 2023; 11) rolling out **National ID** cards, 12) strengthening the existing cash payment systems through upgrading technologies for **improved governance and efficiency**; 13) developing regulations to implement the **Payment Systems Law**; 14) reforming the curriculum for **digital skills** across the education spectrum, ranging from primary to tertiary institutions, including TVETs; 15) introducing programs that provide **demand-driven digital training** opportunities for youths; 16) establishing an electronic system for **e-visa** issuance to attract foreign investors, 17) streamlining current legal requirements to **start a business**; 18) addressing government accountability in delivering services such as simple **e-government tools** (example: a mobile-based citizen feedback platform).

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