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Abstract

This study analyses the causes of the Iraqi economy's difficulties in rebuilding, provision of basic services and generally declining performance over the last decades. In contrast to accounts that lay stress on Iraq's statist past, we argue that the sustained decline in formal institutions and human capabilities is the best explanation for Iraq's economic decline. That is, weakened political institutions and restricted political space in the 1970s and 1980s along with protracted economic sanctions in the 1990s facilitated conflict and damaged Iraq's developmental institutions and structures. Moreover, the US, when it occupied Iraq in 2003, relegated many of the existing, if deficient and imperfect, institutions and promoted policies that worked against the established political economy, aggravating conflict and instability. Consequently, broken institutions have remained unrepaired, while new institutions that the US created, with the help of new Iraqi elites, often proved fragile. In addition to select micro-economic interventions, we recommend policies that more dependably and equitably distribute oil rents, such as a universal basic income. Our recommendations thus contrast sharply with approaches that emphasize a reduced role for the state. The aim is to facilitate development of institutions and human capabilities under conditions of lowered conflict and greater stability, a binding constraint on development.

Keywords: Country Studies, Conflict, Capabilities, Economic Development, Entitlements, Institutions and Growth, Iraq, Basic income, Sanctions, Transfers.
JEL Classifications: F02; F63; I38; J06, J24; O43; O53.

1. Introduction

This study analyses the reasons behind the decline of Iraq's economy over the last decades, identifies bottlenecks and constraints that have hampered recovery, and offers remedies going forward. A country that at one time was a regional leader in terms of human capital and skills formation, with perhaps the most advanced and effective medical care that was provided free of charge, today faces problems in reconstruction and provision of basic services, electricity, sanitation and, crucially, law and order. As the IMF (2004: 34) has noted

> . . . after attaining middle income status in the 1970s, Iraq's nominal GDP per capita had dropped to about US$700 by 2002, and many of Iraq's human development indicators are now the lowest in the region.

Indeed, a traveler to this country returning after decades of being away would scarcely recognize her own country. In what follows, we track the trajectory of Iraq's economy, outline our approach to the study and engage in various talking points. It is important to stress that Iraq's present circumstances have come about over decades of decline and are unlikely to be solved easily or rapidly. In 1980, Iraq attacked Iran, initiating eight years of bloody conflict; in 1990, it invaded Kuwait resulting in the 1991 Gulf war and debilitating economic sanctions. Since 2003, the state, despite rising oil prices and hence revenues (until 2013), has failed to deliver basic services such as electricity and safe water, not to mention peace and security. Since 2014, Iraq has experienced budgetary difficulties, induced by collapsing oil prices, exacerbated by an expanding public sector and internal conflict (a war with the Islamic State of Iraq and Syria (ISIS) or Daesh). This has further complicated longstanding problems of low investment rates and poor quality of public services. These hardships need to be placed in the context of long-term decline in human capabilities and institutions, including the state institutions (Yousif, 2016), and the result of frequent, sudden and discontinuous institutional changes affecting the country for decades (El-Joumayle, 2018).

2. Conceptual foundations and historical background to 2003

2.1. Long-term decline in capabilities and institutions

Capabilities are the set of things that people are able to do or be (physical mobility, numeracy, literacy, etc . . .) that one is able to choose (Sen, 1983: 754 - 756). Capabilities, including knowledge and skills, health and nutrition, are important inputs into the development process; at the same time, expanding capabilities is the ultimate objective of the development process. Human capabilities, e.g. a literate, skilled and well-nourished workforce, provide critical inputs to realize economic growth; the latter is not the same as development and is not viewed as a goal in itself, although it may provide a means to expand capabilities. As explained below, we view development as expanding human capabilities, mediated by institutions. We follow Hodgson in defining institutions broadly to include organizations, in addition to Douglass North's definition of "humanly devised constraints that shape human interaction" (Quoted in Hodgson, 1998: 179-180). Institutions can be formal, e.g. humanly devised procedures, rules and laws, or informal, e.g. customs and mores. While formal institutions may change rapidly, informal institutions are thought to be slower moving. Institutions may evolve slowly or change abruptly at times of war or revolution, in which case institutional change is 'discontinuous.'

(North, 1990: 4-6). We contend that enduring decline in formal, including state, institutions and capabilities is the best way to understand Iraq's present circumstances.

Given this, two points are pertinent. First, following Stewart and FitzGerald (2001a: 11 & 2001b), we suggest that economies emerging from a period of prolonged conflict are unlikely to respond in the same way as they did when at peace, in part because institutions may not function properly or are non-existent. Policies should not therefore assume their orderly functioning. Similarly, reconstruction policies ought to consider local conditions and constraints, in that they try to reinforce and make use of, rather than work against, existing domestic political alignments and institutions; they should also try to ameliorate existing horizontal inequalities to reduce the likelihood of conflict (Stewart and FitzGerald, 2001b: 226 & 228).

Second, we posit that political decisions—taken in Iraq and outside—rather than choice of economic strategy are what primarily accounts for Iraq's economic decline, because these decisions induced discontinuous institutional change that is often harmful to development and economic growth (North et al., 2009: 252). We thus distinguish between developmental and political institutions or structures. The former include rules, methods, planning and statistics collection mechanisms, etc. . .—all expanded and sustained by human capabilities and knowledge, including in the public sector; this relates to the notion of state capacity or effectiveness, which we define as the ability of the state to carry out its policies. In contrast, political institutions are responsible for formulating public policy. Distinguishing developmental from political institutions and structures allows us to analyze their effects, vis-à-vis the frequent discontinuous institutional changes that Iraq has experienced—hence the deteriorating economic performance.

This stands in contrast to the construction of an artificial dichotomy of activist versus minimalist state economic strategy (see Yousif, 2016). We thus contest explanations of Iraq's economic decline that are based on rationales that emphasize Iraq's statist past. For example, the Coalition Provisional Authority (CPA) (see Foote et al., 2004), the IMF (2004: 5) and post-Saddam Iraqi governments (IMF, 2004: 32) have all located Iraq's poor economic performance in overly intrusive Ba'th-era economic policies (1968-2003) or economic planning. Economic planning actually precedes the Ba'th party's coming to power in 1968, with the 'Development Board' established in 1950 to manage and plan the investment of oil income. While we briefly discuss the inefficiency and waste associated with Iraq's statist economic policies, we postulate that they do not account for Iraq's developmental collapse: discontinuous institutional changes brought about by actions of defective political institutions do. That is, Ba'thi political—rather than economic, i.e., institutional—policies, internationally imposed economic sanctions and the actions of the Coalition Provisional Authority (CPA) together account for most of Iraq's decline.

2.2. Oil, developmental institutions and the state

Like other oil exporters, Iraq's central government has traditionally owned or controlled the production and export of oil and its revenues;[4] the state is consequently a key and large player in the economy. This explains why state involvement in oil economies tends to be extensive in relation to GDP, despite variance in political and economic ideologies, e.g. as in Saudi Arabia, Iran, Iraq and Algeria. The key question thus concerns the nature of state involvement—what it does with oil revenues—rather than the size of state in the economy, which is inevitably substantial. Largely financed by oil revenues, an implicit social contract has developed over time whereby the state has provided public goods, including education and health, as well as employment, particularly to better educated workers. Oil has been seen as a main tool to diversify economic activity, hence the large state investments in infrastructure and the non-oil economy since the 1950s (see Alnasrawi, 1994: 17-34). The greater the state's capacity or effectiveness, the larger its ability to invest the income from oil and the more pronounced the effect on the economy.[5] According to Fukayama (2013), higher levels of education, professionalism and, to some degree, autonomy of the state bureaucracy from political pressures, tend to enhance state effectiveness. Human capabilities, more generally, are a key input into the development process. The process that transforms human capabilities into development and economic growth that in turn contributes to still more expansion in capabilities is mediated by institutions: customs, laws, policies, political constraints and decisions, and processes.

This process of development or underdevelopment is usually multifaceted and rarely linear (Rodrik, 2005). We argue that rapid physical and human capital formation and steadily rising primary and secondary enrollments in education in the 1970s likely strengthened Iraq's developmental structures and institutions. At the same time, there was poor political decision-making, likely reflecting declining political institutions and associated with the narrowing of the political space—and this, along with prolonged economic sanctions, eventually induced a severe decline of developmental structures and outcomes. By the 1990s, developmental institutions and state capacity began to atrophy sharply, along with an economy-wide gradual loss in human knowledge and skills. Consequently, the experience of Iraq over the last four decades has been one of declining institutions, including, importantly, state institutions—which are central to economic policy formation and implementation, not to mention protecting property. This partly explains why rebuilding since 2003 has been difficult (see Yousif, 2016). Given the pervasive decline today, it is tempting to assume a generalized 'state/development' failure. We argue instead that uneven development of political and developmental institutions accounts for Iraq's decline.

[4] Before the nationalization of oil in 1972, Iraq received royalties from international oil companies rather than directly controlling oil sale. Central government control of revenues mostly continues today, although there is disagreement about who (regional versus central government) owns oil resources and revenues under the Iraqi Constitution of 2005 (see Constitute, 2019). Three main factors determine oil revenues: the quantities of exported oil, the trading price of oil in international markets and the purchasing power of the US$ vis-à-vis other currencies (Alnasrawi 1994: 156).

[5] The Iraqi state can and has sub-contracted development work to private (national and international) firms. This still requires government to identify priorities, establish rankings and coordinate investments, viz. state capacity.

2.3. Institutional decline, the social contract and development

Hence, Iraq's long-term institutional decline ought not to be confused with outdated social contract or state failure. Problems with Iraq's social contract did not cause its institutional decline and one should be careful about making spurious causational connections about these. We instead show that Iraq's existing social contract, where the state provides increasing numbers of government jobs (at rising pay) along with some services, as the primary ways to distribute oil revenues is unsustainable. First, the state is simply unable to provide sufficient jobs given Iraq's rapidly expanding labor force and its funding constraint of existing or projected revenues. Second, only a segment of the population (typically the better educated) is able to take advantage of government jobs. We locate the reasons for past conflict in defective or declining political institutions, not the social contract per se. In fact, the start of the Iran-Iraq war in 1980 occurred in the context of rising living standards, egalitarian income distribution and political repression, rather than a social contract that was obviously in crisis.[6] This marks the start of deleterious discontinuous institutional change.

2.4. Oil and the rise and collapse of development

During the 1970s, Iraq experienced both rising prices of its primary export oil as well as increasing output and exports, with the result that oil revenues exploded from $1 billion in 1970 to $21 billion in 1979 (OPEC, 2005: 13). The state, through its development apparatuses and the civil service, successfully transformed much of the revenue into investments in human and physical capital as well expanded private consumption, with investment growing faster than consumption (Yousif, 2012; Yousif, 2016: 216). This was facilitated by growing education and skills in society generally and in the public sector especially, responsible for much of the investment. At the Ministry of Planning, for instance, staff (many of them Western-trained technocrats) rose from 639 in 1968 to 2,932 in 1976 (Savage, 2013: 36). This reflected improved educational capabilities in Iraq as a whole, where literacy in the 10 year and older population rose from 30 percent in 1965, to 47 percent in 1977 to 73 percent in 1987 (Yousif, 2012: 65).

At the same time however, there was rising state-sanctioned political violence and perceptible narrowing of the political space. We posit that political actions or decisions worked to undermine developmental institutions and induced eventual declines in both those institutions and in human capabilities. While a detailed analysis of political institutions of this period is beyond the scope of this work, political actions, including the attack on Iran and later Kuwait, provide evidence of poor or declining decision-making mechanisms. This coincides with a

[6] This relates to a shortcoming of the thesis Acemoglu and Robinson (2012) have advanced in regards to how development is achieved, through 'inclusive' as opposed to 'extractive' institutions. Depending on how one defines these, Iraq's institutions, in for example 1980, might appear inclusive in many respects and extractive in others. Iraq's provision of free health and education and rising incomes is arguably economically inclusive; but Iraq's repressive political and security institutions were arguably extractive. The fact that Iraq invaded Iran in September 1980 is not in itself evidence that its institutions were in general extractive (or inclusive for that matter). One has to define such categories specifically and explain how the specific category of institution (e.g. extractive) generated (or ameliorated) social or international conflict; otherwise, it would be impossible to falsify the contention that institutions of a certain category cause conflict.

period of deteriorating rights and freedoms for most Iraqis. The Polity IV Country Regime measure, with a scale of 10 for most democratic to -10 for most repressive, for Iraq declines from -5 to -7 during the 1970s and further to -9 in 1980 (see Polity, 2014). Likewise, Yousif (2012: 144-150) utilizes an index of political freedoms and rights to illustrate the decline during the 1970s and 1980s. There was a parallel narrowing within the political leadership itself, with more power concentrated in the hands of Saddam Hussein and his close associates and family (Davis, 2005: 176-78; Yousif, 2012, 143). We contend that this limited governing base made policy errors more likely and less reversible. The causes of the Iran and Kuwait conflicts are complex and we want to avoid over-simplification; [7] our point is that existing political institutions made policy mistakes more likely and corrective measures more difficult.[8]

The beginning of the Iran-Iraq war in 1980 interrupted oil exports, which recovered only gradually; central government revenues declined, with the result that Iraq relied on foreign exchange reserves to finance the war, pay for imported goods, including food (sold to the public at subsidized rates), and carry out the state's ambitious investment plans. These multiple demands exhausted reserves by 1982 to 1983, and Iraq started to borrow heavily from its Arab neighbors and internationally to finance the war and sustain domestic social spending and consumption; the government dropped its extensive investment plans (see Yousif, 2012: 47-53). Even so, there remained a commitment on the part of the state in the 1980s to pay for extensive social spending, part of the existing social contract: infant mortality, life expectancy, caloric consumption, immunization rates, the provision of safe water and most education indicators continued to improve (at varying rates) under war conditions (see Yousif 2012).

Overall, however, even though military priorities supplanted development spending in the 1980s, economic organizations and state institutions retained some degree of robustness. It is important to emphasize that state effectiveness is central for Iraq's oil-producing economy, where government provided a plethora of services, consumer and producer subsidies and has been responsible for a large part of capital formation. Higher levels of professionalism and education, as well as a degree of bureaucratic autonomy tend to promote state capacity (Fukayama, 2013). Thus, two opposing forces were influencing state effectiveness. On the one hand, increased education and skills in the civil service and society more generally worked to expands effectiveness. On the other, there was rising politicization of the civil service (and society in general) after the 1970s, when the Ba'th government started to undercut meritocracy in government service by favoring and promoting party members.[9] That is, political institutions tended to check effectiveness. Nevertheless, state involvement in the economy and society and

[7] There were geo-political logics at work in Iraq's calculations: the Ba'th leadership viewed revolutionary Iran as a threat to Iraq and to its own power; and Iraq had longstanding border and other disputes with Kuwait. Whether conflict provided a rational (i.e. cost minimizing) solution is another matter.

[8] Sen (1983: 757-760) notes that popular pressures for corrective actions to policy errors in pluralistic India have precluded the occurrence of famines, unlike in totalitarian China, even though in general terms China has done better than India in terms of improvements in nutrition.

[9] The Ba'th even created parallel (and often-secret) budgets to direct resources to particular priorities such as internal security (Savage, 2013: 37-40).

gains in human capabilities[10] imply that government retained some degree of effectiveness in the 1970s and 1980s.[11]

The Iran-Iraq war and the invasion of Kuwait was followed by two shocks, namely the 1991 war to eject Iraq from Kuwait and comprehensive economic sanctions (1990-2003). We can quibble about whether these were internal or external shocks, brought about by the Iraqi or US or coalition decisions; from the perspective of Iraqis, the distinction is immaterial. The 1991 war itself, especially the 42-day bombing campaign, while ostensibly intended to drive Iraq out of Kuwait, actually destroyed the country's civilian infrastructure, including power-generation, oil and transport networks, and fertilizer and iron and steel plants. Targets were deliberately chosen to "amplify the economic and psychological impact of sanctions on Iraqi society" and if they were likely to need foreign expertise to repair (Alnasrawi, 2002: 67). The UN describes the economic and social consequences as "near-apocalyptic results upon what had been, until January 1991, a rather highly urbanized and mechanized society" (quoted in Alnasrawi, 1994: 119). Moreover, comprehensive economic sanctions precluded rebuilding. Iraq's oil exports, prohibited under sanctions, paid for a variety of items, including imports of food and medicine; in 1989, for example, imports of food and medicine were US$ 2.36 billion (Gazdar and Hussain, 2002: 73). In fact, the prohibition on export worked effectively to deny the ability to import, as sanctions foreclosed access to international lending. Per capita GDP (at constant prices) declined by more than 50 percent from 1990 to 1995 (see UN Statistical Database, 2019). The decline in incomes, among other reasons, induced people to emigrate, notably those with higher levels of education and skills (see Yousif, 2016: 226), a process that would continue and possibly accelerate after the 2003 invasion (as we shall see). Based on UN data, Yousif (2016: 223-224) calculates that Gross Fixed Capital Formation as a portion of GDP averaged 6 percent in 1991 to 2002, very likely less than the rate of capital depreciation economy-wide and inadequate for rebuilding. Sanctions decapitalized Iraq, in human and physical terms, with dreadful implications for later reconstruction.

In prohibiting exports, sanctions created a shortage of foreign currency, with the result that the value of the domestic currency plummeted with respect to foreign currencies, making imports (notably food and medicine) expensive. The public distribution system (PDS), which remains today, was set up to provide a basic level of consumption; the program purchased (mostly) domestically produced grains at set prices, which were then rationed to the public. Because Iraq was (and remains) a net importer of grains and lacked funds to import food, the PDS provided only a portion of the caloric requirement of the population. Inadequate nutrition (see

[10] Fukayama (2013: 355-6) actually argues that output measures like these are imperfect to gauge state effectiveness because they, e.g. infant mortality, may improve as a result of technology and despite reduced governance. One measure of state capacity that does not apply well to an oil-economy such as Iraq is taxation. Accuracy and frequency of census data can serve as an alternative measure (Lee and Zhang, 2016). In this regard, it worth noting that while censuses were conducted at regular intervals in Iraq (usually every 10 years), the last census, of 1997, was partial and did not include the Kurdish region where the central government had no authority. Political impasse and instability have precluded the administration of a census since, and one is planned for 2020 (Kurdistan 24, 2019).

[11] An interesting question that is beyond the scope of this study is whether expanded state capacity and effectiveness (at least in war-making and related activities) provided the Iraqi government with an impetus to engage in conflict that later destroyed capabilities.

Garfield and Waldman, 2003: 9-10), decline in water quality and electricity along with shattered infrastructure resulted in a spike in infant and child mortality, which had been declining during the 1970s and 1980s, rising to 102 per thousand in 1999 (Garfield and Waldman, 2003: 16-17). The Oil for Food program implemented in 1998 was supposed to improve humanitarian outcomes but was both too limited in size and too late to substantially reverse these trends (Gazdar and Hussain, 2002: 70-74; Cortright, Millar and Lopez, 2002: 205). As Joy Gordon (2010: 138) notes, by the time needed medical equipment imported under the program "arrived there was often no longer adequate personnel to use it effectively . . ."

While the economy, society and the civil service was losing trained personnel, there was a decline in professionalism in the civil service, as corruption became a survival mechanism for many, gradually becoming widespread and ingrained. This, along with the withdrawal of the state from most activities that it previously engaged in (except for the PDS), and increased reliance on what Tripp (2003; 11) calls the 'shadow state' tracked the decline of the public bureaucracy. The consequences were severely weakened developmental institutions, reduced state capacity and declining human capabilities—the initial conditions the US faced when it invaded Iraq in 2003.

3. Occupation, upheaval and aftermath—actions, outcomes and trends, 2003-2018

3.1. Coalition Provisional Authority (CPA) policies

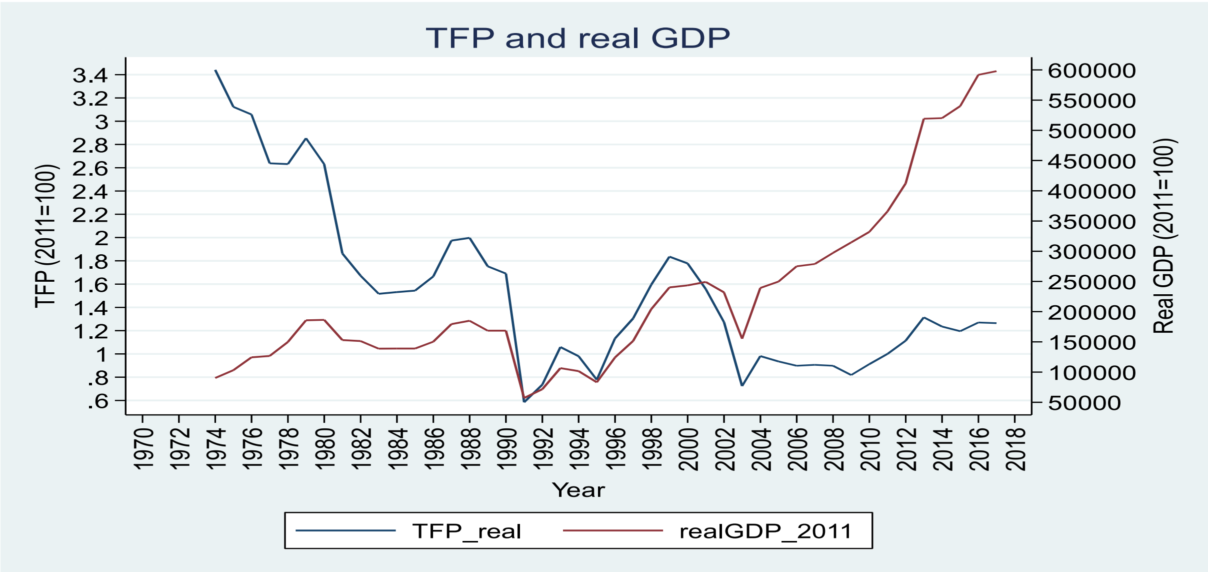
In March 2003, the United States and allies invaded Iraq, overthrowing the Ba'thist regime, in power since 1968, and appointing the CPA to rule the country. The CPA, along with the international financial institutions (IFIs), quickly identified economically interventionist Ba'thist policies as the reason behind Iraq's economic decline, minimizing the effects of conflict and economic sanctions, in effect until 2003 (see Mahdi, 2007: 2; IMF, 2004: 5). With extensive powers to reconfigure Iraq's political economy, the CPA attempted reform along free-market lines. However, it faced legal and political constraints; as its own officials recognized, an occupying power is restricted from selling Iraq's public assets. The CPA was concerned that future Iraqi governments might reverse its reforms without support for the reforms from Iraqis (Foote et al. 2004: 58-9). While it held real power, the CPA was still obligated to consult with the Iraqi Governing Council, which it established in July 2003.

The CPA implemented some positive measures, such as sponsoring the write-down of Iraq's foreign debt, establishing an independent central bank and introducing new currency (Yousif 2016: 225). However, there was little recognition of the effects of decades of conflict and sanctions on markets and institutions and the imperfect ways that they might function. Instead, the CPA's program took the form of extreme shock therapy, a rush to liberalize prices and markets with Eastern Europe as a model. The stock aim was to achieve allocative efficiency, encourage investment, notably foreign direct investment (FDI), and so accelerate economic growth. Hence, various CPA measures were enacted: allowing foreign firms to own assets in Iraq (except in the politically sensitive oil sector), cut corporate taxes, relax foreign exchange restrictions, and apply a low common import tariff (see Yousif 2007; Yousif 2016). In addition, orders 1 and 2 in May and August 2003, respectively, enforced de-Ba'athification and the dissolution of Iraq's armed forces (CPA, 2003). Together, these two measures laid-off about

500,000 people, or 8 to 10 percent of the labor force (Yousif, 2007: 49). In civilian work, de-Ba'athification resulted in the expulsion of 30,000 civil servants, of which 15,000 were re-hired; in addition, all army officers above colonel and 100,000 intelligence officers lost their jobs (Alaaldin, 2018: 7). Thus, the disbanding of the army and de-Ba'athification made jobless hundreds of thousands of trained military and intelligence personnel and deprived the country of managerial and professional skills, inflaming insecurity and complicating rebuilding.[12]

The CPA substantially increased public sector wages in an attempt to appease the populace (Allawi, 2007: 123). This move was in tension with the neoliberal emphasis on efficient resource allocation as no one thought the wage rises reflected enhanced public sector productivity. Indeed, most of the rise in real GDP since 2004 is attributable to higher oil extraction, which employs less than two percent of the labor force, not leaps in Total factor Productivity (TFP) as shown below.

Figure 1. Total factor productivity and real GDP



Source: University of Groningen and University of California, Davis, Total Factor Productivity at Constant National Prices for Iraq [RTFPNAIQA632NRUG], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/RTFPNAIQA632NRUG,December 14, 2019.

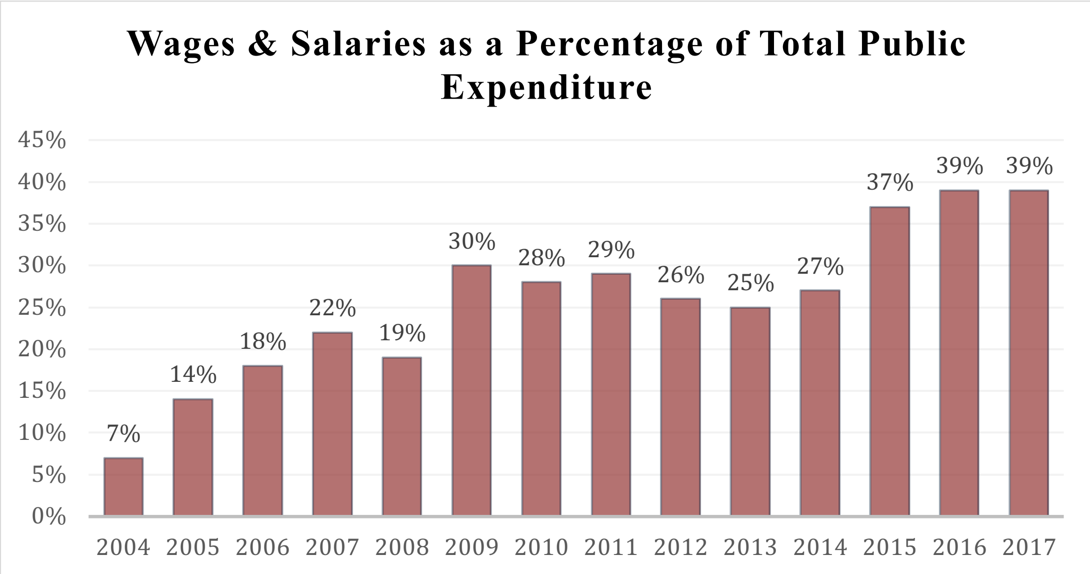
At the same time, the CPA put forward its plans for the privatization of state owned enterprises (SOEs), firms that nominally produced a wide variety of consumer and producer goods and employed roughly 500,000 workers.[13] Many of the SOEs were dilapidated or insolvent, and thus unattractive to investors. These brusque attempts at privatization incensed the public to such an extent that even the Iraqi Governing Council was unable to support the CPA's privatization initiatives. Consequently, the CPA abandoned its privatization plans in November 2003. It did not attempt to repair or rehabilitate SOEs, let alone ready them for privatization,

[12] To be fair, the CPA is only partly responsible for de-Ba'athification, as the Iraqi 'Higher National De-Ba'thification Commission' expanded the application of the policy. See Sissons and Al-Saidi (2013: 12-14 & 21-22).

[13] In addition, in 2003, 1,000,000 were employed in the Iraqi civil service as teachers, accountants, physicians etc. . . (IMF, 2003b: 9).

and in fact denied them capital. Even so, the CPA continued to pay SOE workers, even though many SOEs were non-productive. (Henderson, 2005: 10-12). This reinforced the notion that SOEs be subsidized regardless of output. Subsequent Iraqi administrations expanded both employment and pay in government service more generally, with the result that the public payroll has consumed a growing share of public expenditure, as illustrated below.

Figure 2. Wages and salaries as a proportion of public expenditure



Sources: World Bank (2018b: 9). Iraq Economic Monitor, From War to Reconstruction and Economic Recovery.

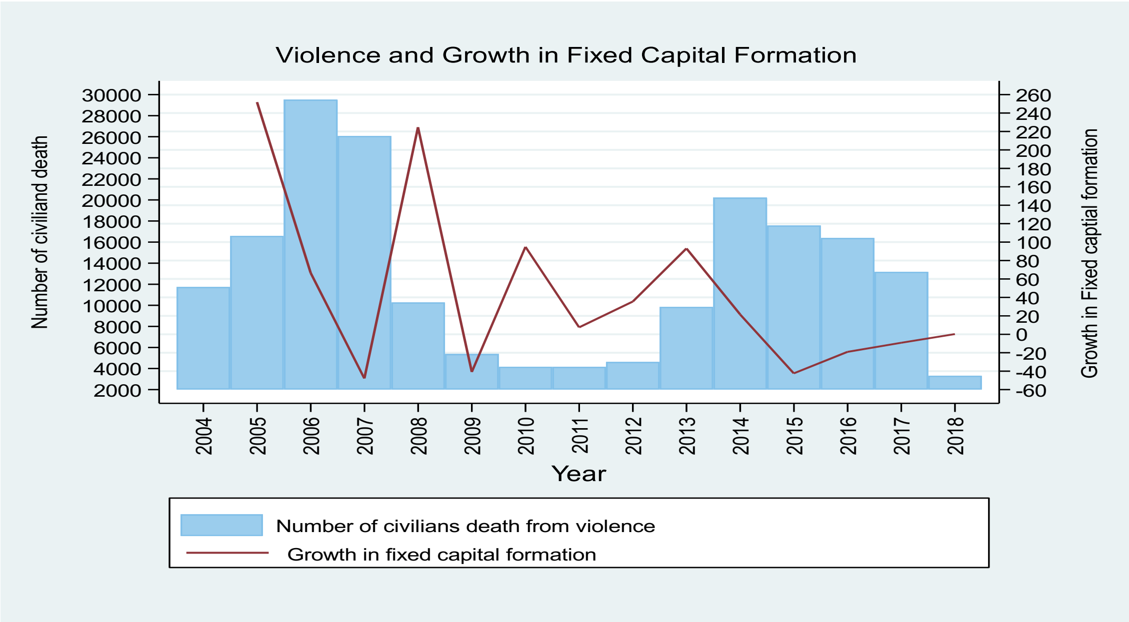
3.2. Political impasse and insecurity

De-Ba'athification and the disbanding of Iraq's armed and security services placed large numbers of disgruntled men trained in violence on the streets.[14] At the same time, the CPA picked Iraq's Governing Council from among returning exiles, based on a system of ethno-sectarian apportionment whereby Sunni, Shi'is, Kurds and other groups received set allocations. Alaaldin (2018: 7) notes that the fall of the regime created an 'ideological and political void' in addition to the security vacuum. This, along with the CPA's sectarian distribution, allowed ethno-sectarian and religious groupings to mobilize support based on sect as opposed to political ideology. Sectarian political groupings came to dominate specific government ministries, allocating jobs and other patronage to their supporters. As Al-Qarawee (2014: 6) notes, some previously exiled political groups had little domestic support, so their political viability depended on cultivating "sectarianism and communal fears to create new constituencies." Politics became polarized along ethno-sectarian lines, as cronyism and corruption characterized governance, a system that continues today (Kuoti, 2016; Herbert, 2018).

[14] For an exploration of the reasons or rationale of these policies, see Yousif (2007). It is not possible to view these actions as the result of ignorance or bad advice. According to Zinn (2016), US government officials, including at the National Security Council, were aware of the potential risks of throwing hundreds of thousands of unemployed and armed young men onto the streets of Iraq's cities.

In this atmosphere of rising violence, sectarianism and criminality, hitherto mixed neighborhoods in Baghdad became virtually exclusively Sunni or Shia (Alaaldin, 2018: 17). The table below reports the number of civilian deaths resulting from violence and illustrates the extent of sectarian violence in the 2005 to 2007 period, when roughly 16,000 to 28,000 people died per year, or about 45 to 75 per day. The US invasion of Iraq is not to blame for the origins of Iraq's sectarianism, but CPA actions inflamed it.[15]

Figure 3. Violence and growth in fixed capital formation



Sources: Gross fixed capital formation: Calculated from World Bank data about Iraq. Accessed 05/01/2019. https://data.worldbank.org/country/iraq?view=chart. Number of civilian death from violence is from Iraq body count database. Accessed 20/07/2019.
www.iraqbodycount.org/database.

3.3. Brain drain and slow reconstruction

Rising insecurity made rebuilding more difficult and costly. A number of factors were at work here. First, there was a high degree of waste and inefficiency characterizing US-led reconstruction efforts (SIGIR, 2009: viii). Second, insecurity was rife. Contractors and donors involved in reconstruction reported that providing security for capital projects often reached 30 to 50 percent of total cost (IMF, 2005: 7). Finally, there was continued loss of skills and capabilities, with a notable brain drain following the Gulf War in 1991 and a likely larger outflow after 2003 (Yousif, 2016: 223).

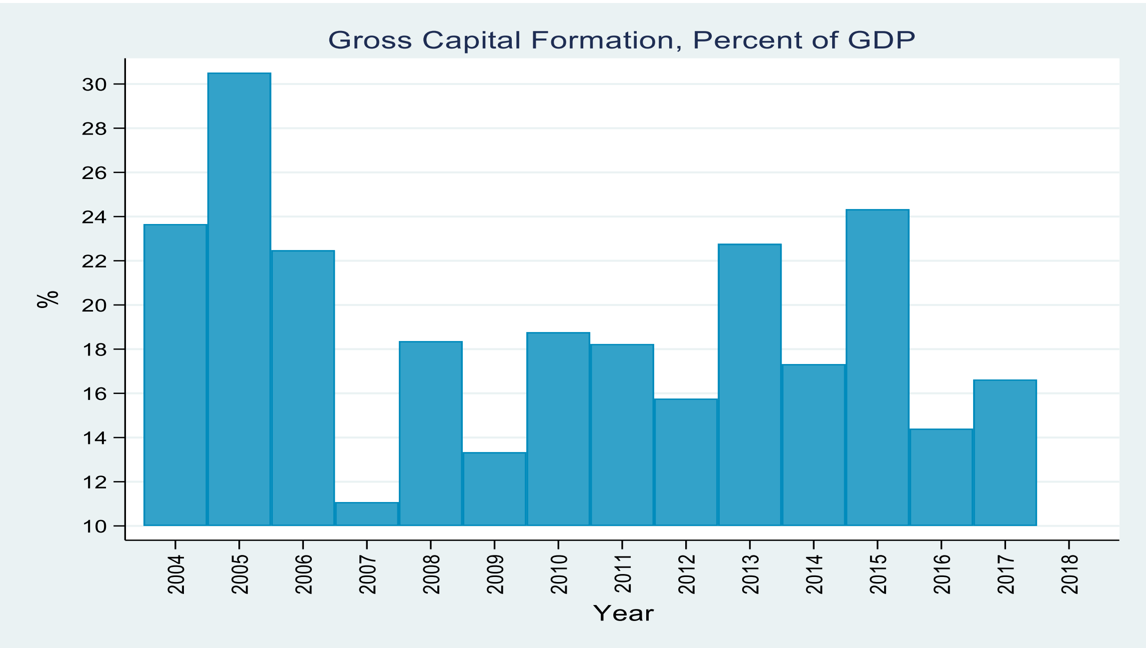
In Iraq, the state has historically has had a pre-eminent role in terms of investment spending (Yousif, 2012: 55-59). It undertakes most capital spending, especially large-scale reconstruction projects, and accounted for roughly two-thirds of Gross Domestic Investment in 2013-2015 (World Bank, 2017: 63). Hence, loss of skills, notably in the state sector, is bound to affect capital formation. For example, the technical capacity of the Ministry of Oil to monitor large contracts, and the Ministry of Electricity's expertise in various areas ranging from

[15] See Yousif (2010) for an exploration of this theme

engineering supervision to budgetary skills has been lacking (USAID, 2012: A-25). A look at Iraq's emigres explains why. According to one survey conducted by Fafo (2007: 20-21) in Jordan (a main destination for Iraqi emigrants), 42 percent of Iraqi women and 51.5 percent of men over the age of 16, had at least a bachelor's degree—much higher than in Iraq and or elsewhere in the Middle East. Three-quarters of those surveyed arrived in Jordan after 2003, that is, to escape violence and insecurity (Fafo, 2007: 17). As the World Bank (2017: 79) has stated: "the flight of educated Iraqis in search of better opportunities abroad has had and will continue to have severe negative long-term consequences for the Iraqi economy and for the education sector specifically." Nor has the desire to leave abated. According to the Iraq Human Development Report (2014: 179-181), the desire to emigrate among Iraq's youth is 22.2% nationally—higher in Baghdad at 31%, 41% for males, all seeking better job opportunities and security.

For these reasons, capital formation has been low. As shown below, excluding 2005, gross fixed capital formation has hovered roughly between 11 and 24 percent since 2003, mostly at or under 18 percent—anemic for a country recovering from decades of war and sanctions. According to Idris (2018: 2), the weak governance, which Iraq has experienced, is, at least partly, the result of emerging shortages in human capital, caused to some degree by the post 2003 CPA policies.

Figure 4. Gross capital formation as proportion of GDP

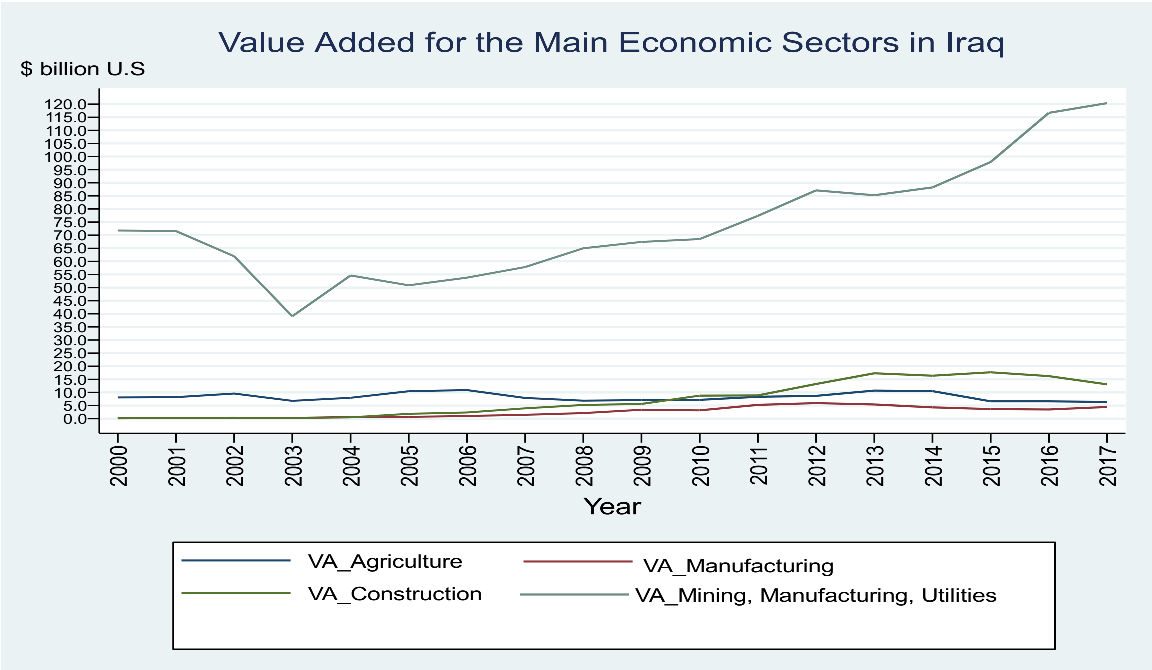


Source: calculated from United Nations (UN), National Accounts and Main Aggregates Database (2019). Accessed 05/01/2019. http://unstats.un.org/unsd/snaama/Introduction.asp/.

Both the US and Iraqi governments have engaged in investment spending. US capital spending would eventually rise to $60 billion, from an initial $20 billion. One third of the $60 billion was spent on re-building and equipping Iraq's new security apparatuses, dismantled after the invasion in 2003. Much of the $60 billion investment fund was misspent, according to the

Special Inspector General for Iraq's Reconstruction (SIGIR) (CBS, 2013). The Iraqi government also has invested oil revenues. Until 2014, when collapsing oil prices created budgetary difficulties, the binding constraint on government capital spending has been the availability of skills and expertise as well as violent conflict rather than funding. Since 2003, goods producing sectors of agriculture and manufacturing have stagnated, partly due to slow repair of dilapidated infrastructure; in contrast, value added in oil has been steadily rising, the result of higher production, as shown below.

Figure 5. Value added by economic sector



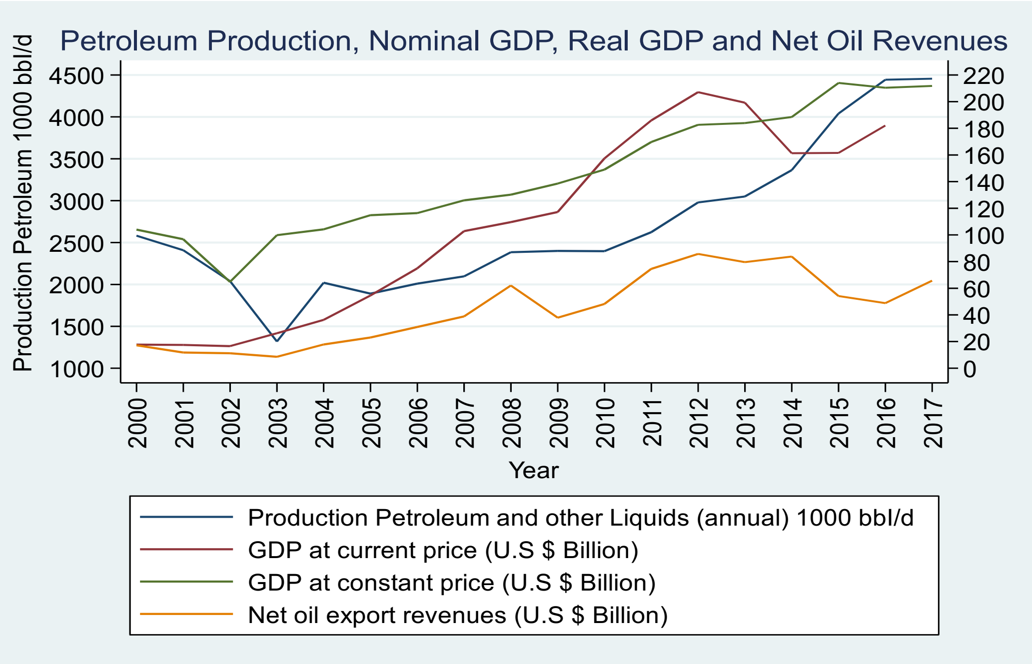
Source: calculated from United Nations (UN), National Accounts and Main Aggregates Database (2019). Accessed 05/01/2019. http://unstats.un.org/unsd/snaama/Introduction.asp/.

3.4. Oil dependence

As shown below, oil production rose steadily after 2003, reaching a historic high of 4.9 million barrels per day in August 2019 (Paraskova, 2019). Oil generated more than 90% of total revenues in the period 2013 to 2015 (World Bank, 2017: 63), providing finance for social spending, capital and infrastructure spending, the PDS, and buttressed private consumption by paying the salaries of public workers.

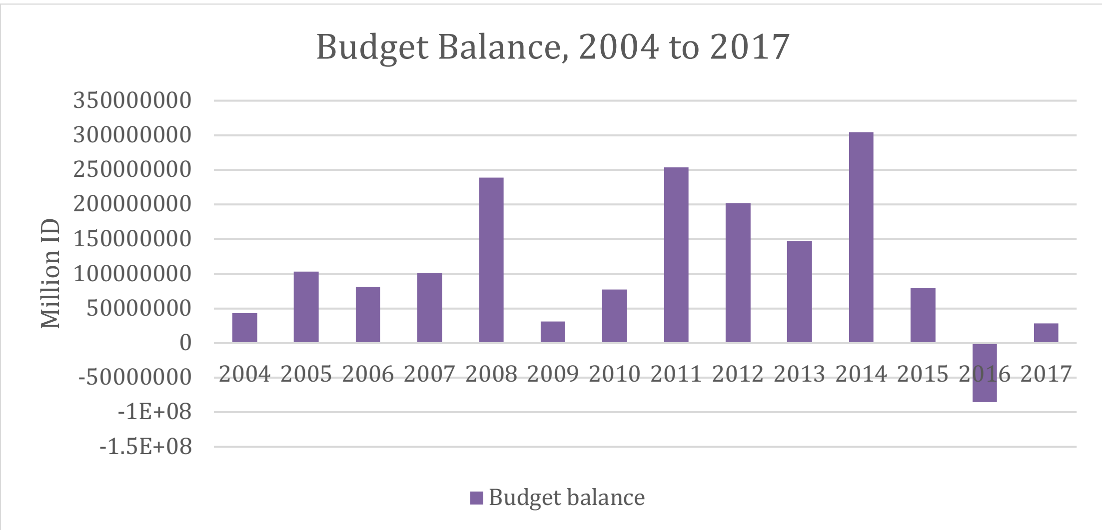
The figure below illustrates how traditional money-metric macroeconomic measures can be misleading in an oil economy. Rising real GDP comes about when oil output rises, regardless of what happens to the oil price; together output and price determine nominal GDP and government revenues. Thus, paradoxically, rising oil output since 2014 is reflected in expanding real GDP, even as the war with ISIS and falling oil revenues created fiscal strain and hardship, leading to cutbacks in public investment. In fact, rising oil output was unable to offset collapsing oil prices and nominal GDP declined in 2014 to 2016. Thus, there is often little correspondence between nominal and real GDP and state revenues, and rising real GDP can be a misleading indicator.

Figure 6. Oil and key macroeconomic variables



Sources: oil production and revenues: Calculated from U.S Energy Information. Petroleum and Other Liquids (annual) (1000 bbl/d): 1980-2018 production and consumption. Accessed 20/10/ 2019. https://www.eia.gov/beta/international/data/
GDP: Calculated from World Bank data about Iraq. Accessed 05/01/2019. https://data.worldbank.org/country/iraq?view=chart.

Figure 7. Central government budget balance, 2004 to 2017



Source: Calculated from CBI (2019), accessed 11/4/19.

The central bank has managed to maintain price stability through a managed peg of about one $ to 1,200 ID and liberal import regime. Price inflation was high after the invasion in 2003 and for some years after, but prices have stabilized since 2008. Higher inflation in Iraq than the US has raised the real effective exchange rate of the Iraqi Dinar (ID) (IMF, 2017: 47). However, the run-down state of key sectors, such as manufacturing and agriculture, and insufficient infrastructure and inputs, e.g. electricity, means they would respond only limitedly, in terms of import substitution and exports, to a nominal ID devaluation (see IMF, 2017: 19). On the other hand, a devaluation would abruptly reduce the purchasing power of ordinary Iraqis, who rely on imports. Exchange rate stability is a notable factor in encouraging FDI, but so is security; FDI rose steadily after 2004, reaching a peak of $6 billion in 2013, but collapsed thereafter (World Bank, 2017: 58-9).

Figure 8. Real GDP, unemployment and consumer prices

Source: calculated from IMF Country Data and Meta Data. Accessed 07/01/2019. http://data.imf.org/?sk=4FFB52B2-3653-409A-B471-D47B46D904B5&sId=1485878802128
GDP, Unemployment: Calculated from World Bank data about Iraq. Accessed 05/01/2019. https://data.worldbank.org/country/iraq?view=chart.

3.5. Overstaffed and under-skilled public sector

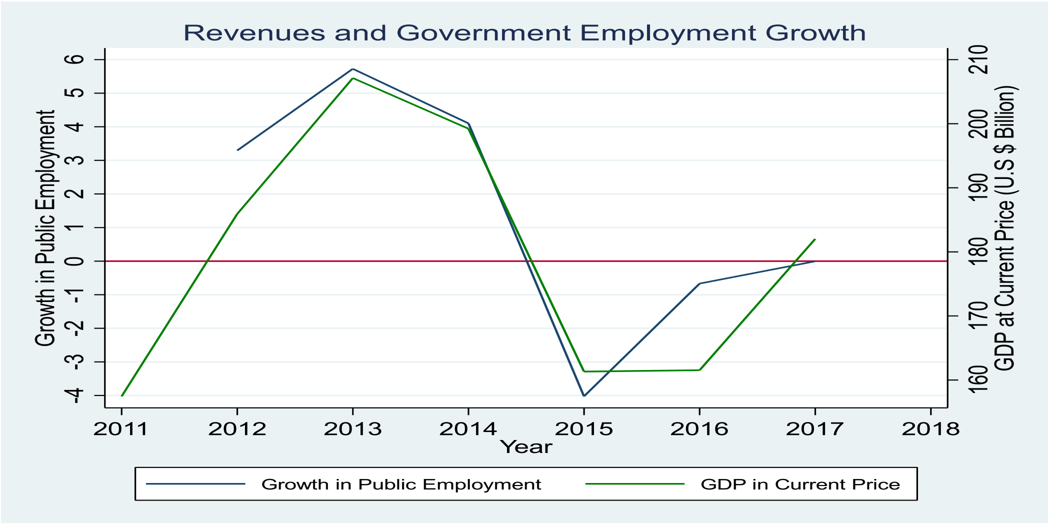
According to the World Bank (2017: 63-65), and not counting employees in SOEs, there has been a sharp rise in the number of people employed in the public sector: from 900,000 (or 22% of all workers) in 2003 to more than 3 million in 2015 (or 42%). As shown earlier, public sector employees' wage bill rose from 7 % of total government expenditure to 37% in the same interval, financed by oil revenues. Some of this expansion, as reflected in rising spending below, relates to the need to hire personnel in the security and military fields, notably in relation to the conflict with Daesh in 2014 to 2017. However, much of the hiring in the public sector is the result of nepotism or patronage of sectarian parties that control certain ministries (World Bank, 2017: 19), and is higher than the average in the MENA region (World Bank, 2018b: 9). The result is that the public sector is both inefficient and overstaffed (Jiyad, 2015).

Figure 9. Military and health expenditures

Source: Calculated from World Bank data about Iraq. Accessed 05/01/2019. https://data.worldbank.org/country/iraq?view=chart.

Moreover, much of its expansion is unrelated to development logic and or even security priorities. Demands for more government jobs from the public at large, especially university graduates (Jiyad, 2015), explain most of the rise in public sector employment. Iraq's budget law of 2019 exemplifies this, with projected spending of $111.8 billion (a 45% increase over the preceding year), with public sector salaries and wages taking up $52 billion of total spending (Turak, 2019). Especially in times of expanding oil revenues, governments come under increasing public pressure to create more public sector jobs. This creates a permanent liability and leaves less money for other priorities, including investment and social spending, aggravating budgetary crises when oil prices decline later. Since 2014, funding has become a salient constraint on investment, in addition to the lack of capacity, skills and expertise. The state has slashed its capital budget and even social spending has declined as a portion of GDP, as shown above in declining health expenditures. The central government has exhausted fiscal surpluses accumulated in prior years and increased its borrowing; debt as percentage of GDP was 32 percent in 2014 and expected to rise to 65% percent in 2018 (IMF, 2017: 13).

Figure 10. Growth in government revenues and jobs growth



Source: Public employment, Al-Mawlawi (2018), Analysing Growth Trends in Public Sector Employment in Iraq. Accessed 20/03/2019. https://blogs.lse.ac.uk/mec/2018/07/31/analysing-growth-trends-in-public-sector-employment-in-iraq/

GDP in current price: Calculated from World Bank data about Iraq. Accessed 05/01/2019. https://data.worldbank.org/country/iraq?view=chart.

Despite the rise in the number of people employed in the public sector since 2003, the capacity and efficacy of the public sector has probably declined, continuing a deterioration that started in 1990. We have noted the effects of emigration of large numbers of skilled personnel. At the same time, political parties and their militias that control ministries have dispensed largesse. Writing in 2005, Le Billon (2005: 687) noted that the confluence of oil and political authoritarianism would leave Iraq vulnerable to corruption and mismanagement. Indeed, Transparency International's Corruption Perception index—a measure of corruption, as reflected in public opinion polling and the views of experts—has been low and declining since 2003.

Table 1. Transparency International's Corruption Perceptions index

Year	Rank	Countries surveyed
2003	113	133
2004	129	145
2005	137	158
2006	160	163
2010	175	178
2014	170	174
2018	168	180

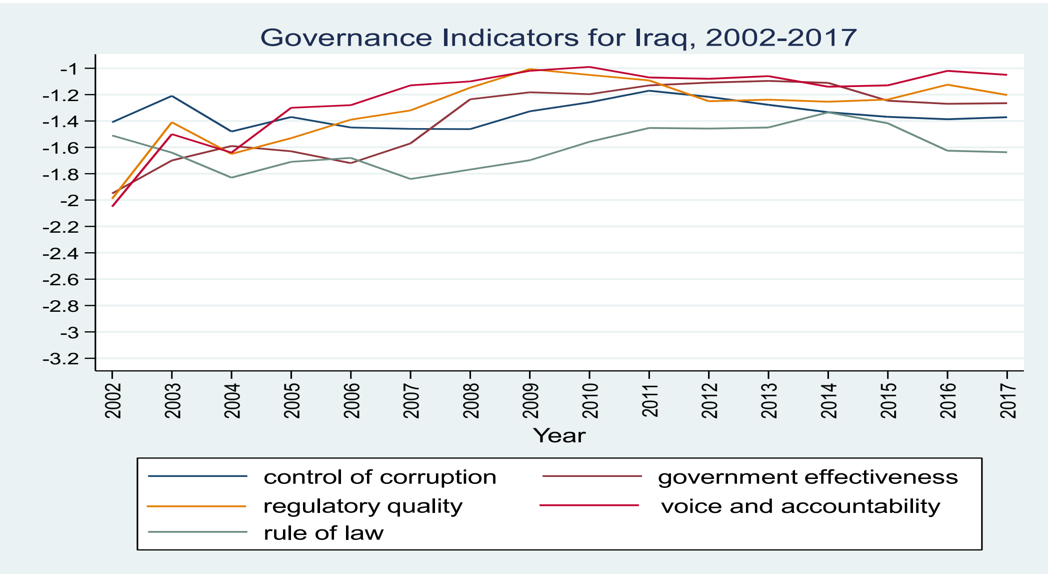
Source: Transparency International (2019)

The World Bank has published Worldwide Governance Indicators since 1996 for over 200 countries and territories. These are six aggregate indicators: Voice & Accountability, Control of Corruption, Governance Effectiveness, Political Stability and Absence of Violence/Terrorism, and Rule of Law, five of which we show below. Although criticized for, among other things, bias towards investors and markets (see Arndt and Oman, 2008: 6), it paints a similarly dim picture of stagnant or declining governance and rule of law. As Cordesman (2015: 6) notes, despite:

> the many claims the U.S. and Iraqi government have made since 2003, the World Bank is almost certainly correct in estimating that little or no progress has been made in the overall quality of governance since the fall of Saddam Hussein. A combination of fighting, political power struggles, sectarian and ethnic tensions and conflict, poor security and a tenuous rule of law, poor execution of all of the major functions of government from the local to national level, and the failure to develop and implement effective budgets and development plans have left a track record at least as bad as Saddam's authoritarianism and helped ensure a continuing state of civil conflict that has nothing to do with ISIS.

Indeed, according to Dodge (2013), ordinary Iraqis see successive post-2003 governments as having failed to meet their basic needs, including employment. There are also signs of declining faith in elections as vehicles to attain popular demands with turnout in the 2018 parliamentary elections at only 44.5 percent, a 40 percent decline over two preceding elections (Patel, 2018).

Figure 11. Governance indicators, 2002 to 2017



Source: World Bank, aggregate Governance Indicators, 1996-2017. Accessed 28/07/2019. www.govindicators.org.

3.6. Social welfare and public services

The main welfare program of note in Iraq is the public distribution system (PDS), which allocates essential food items, such as flour, rice and sugar, to Iraqi households. The program has had near universal coverage, serving 99.4% of poor and 98.6% of non-poor Iraqis in 2018; for the poorest 10 percent of the population it provides a subsidy equal to 30% of that segment's income (World Bank, 2018c: 28). The in kind nature and universality of the program has raised concerns among the World Bank and IMF, which since 2003 has advocated a targeted and cash scheme instead (IMF, 2003: 20-21). Yet, the universality of the program explains its huge popularity and successive Iraqi governments have found it difficult to cut the program substantially; in contrast, Iraq's targeted Social Protection Net provided a cash benefit to only 11% of Iraq's poor in 2012 (Alkhoja, Neman and Hariz 2016: 1). Under IMF pressure to reform the program, some high-ranking public sector employees have been excluded from the PDS (World Bank, 2017: 86); otherwise, all Iraqis, regardless of religion, sect or class, are eligible to participate in this program. The program cost 1.8 percent of GDP in 2014 (World Bank 2017: 86), but was still criticized as cumbersome as it requires procuring goods then reselling them at subsidized prices, it is one of the few programs that have raised the welfare and income security of ordinary Iraqis.

In contrast, Iraqi public services have suffered from both low allocations and low project completion, aggravated by insecurity and deficient skills. Electricity provision has been lacking since the 1990s and only recently, since 2014, started to improve (Al-Khatteeb and Istepanian, 2015: 1), with power shortages severely hindering manufacturing. Security of course continues to be a concern: for example, in the war with ISIS, 67,000 civilians were killed as of 2018 (World Bank Group, 2018b: 2) and 6 million people were internally displaced from 2014 to 2017 (Iraq Humanitarian Response Plan (HRP), 2019: 6). Waves of population dislocation and displacement since 2003, such as the sectarian war of 2005-2007 and the conflict with ISIS of 2014-2017, have induced a sharp rise in illiteracy among the youth, as evinced below. Internally displaced persons have had reduced access to education, especially in ISIS affected areas, with fewer parents sending children to school (Saadoun, 2018). Regarding health, life expectancy at birth actually declined slightly from 2000 to 2007 but has increased since that time (FRED, 2019). The Institute for Economics & Peace (2018:11) estimates the economic cost of violence was 51% of GDP in 2017.

Table 2. Literacy in Iraq

	Illiteracy rate (%)	
Year	15 years and older	15-24
2000	25.95	15.20
2013	56.32	47.68
2018	49.86	43.66

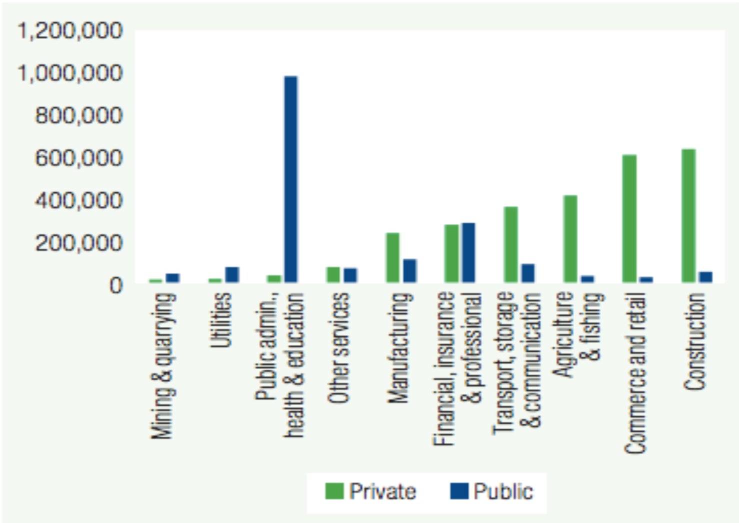
Source: Calculated from UNESCO (2019).. http://uis.unesco.org/en/country/iq. Accessed 21/10/2019

Much like capital formation in other sectors, investments in health and education have proven to be difficult to realize; in contrast, increases in salaries and staff have been easy to undertake (World Bank, 2014a: 45). The quality and reliability of education and health, and public services more generally, are low and geographical coverage is poor. In one World Bank (2017: 14-15) study, Iraq's public services scored roughly two-fifths of the average of Middle East and North Africa (MENA) countries on quality and 43 percent on coverage.

3.7. Job creation and poverty

As in other MENA countries, Iraq faces insufficient employment creation in both the public and private sectors. Iraq has one of the youngest populations anywhere, with half the population aged under 19 years (Bandiera et. al, 2018:7), and the economy has found it hard to generate private sector jobs given the conditions of conflict and low investment. Public administration, health and education, are mostly public and employ the most people, followed by construction, commerce and agriculture, which are mostly private.

Figure 12. Employment by economic sector and employer



Sources: World Bank (2018b: 9). Iraq Economic Monitor, From War to Reconstruction and Economic Recovery.

The number of people entering the labor force has been high, with the result that unemployment has remained high, albeit lower than its peak in the middle 2000s. Youth unemployment (among 15 to 24 year olds) stood at 16.6 percent in 2018 (FRED, 2019). According to Iraq's 2012 Household survey, household poverty depends on the sector in which one is engaged rather than whether one is working full or part-time; agriculture and construction sectors are associated with higher household poverty and public administration with a much lower rate (World Bank, 2017: 36). This explains the public pressure that governments are under to provide more government jobs as well as the queueing that happens for those jobs.

Even so, government jobs are an inefficient way of promoting general welfare and not enough jobs can be created to make a serious dent in poverty. Thus, in the context of rising oil revenues and real GDP from 2007 to 2012, 750,000 new jobs were created in Iraq, four-fifth of which were in the public sector; the main effect of this economic expansion however was raising incomes for those employed rather than providing jobs for persons not working. Consequently, the corresponding decline in poverty, as measured by Headcount, was limited and reversed with the onset of conflict and violence in 2014 (World Bank, 2017: 27-29). This underlines the enormous insecurity that Iraqis experience and the high cost of violence.

This brings us back to our discussion at the start of the study, vis-à-vis the need for rebuilding to reinforce rather than go against prevailing political economies and the poor functioning of institutions and markets post-conflict. Space does not allow for a detailed exploration, but the next section identifies general parameters of solutions intended to 1) increase economic security for households, 2) reduce horizontal inequalities and hence the likelihood of conflict and 3) allow investments in human and physical capital, and institutions, to recover.

4. Analysis and recommendations

4.1. Dangers, opportunities and the importance of oil

In the short to medium term, the immediate threat to Iraq's economy lies in another collapse in oil prices or renewed conflict, especially one that affects oil exports. Looking ahead, oil will continue to be the mainstay of Iraq's economy, providing funds to pay public employees, finance social spending, pay for public investment and provide security. Iraq's oil reserves are sizable and estimated at 143 billion barrels or almost 10 percent of global proven reserves (IEITI, 2019). Although in a tussle with other nodes of authority, the central (federal) government retains control of most oil revenue and will need to manage oil resources with care to maintain and increase oil output.[16]

Iraq's oil sector actually stands out as a notable example of success in the face of difficult circumstances: oil output has risen substantially since 2003 despite serious legal-political challenges and technical obstacles. But Article 112 of the 2005 Iraqi constitution is frustratingly ambiguous on the respective roles of central and regional governments in the management of oil resources (see Constitute, 2019). Attempts to resolve this uncertainty have largely failed, with the central government in Baghdad and the Kurdish Regional Government (KRG) engaging in contesting claims and actions about which governmental entity is allowed to explore, extract and market oil. The KRG in fact enacted its own oil law in 2007, and has awarded about 50 extraction and exploration contracts (unrecognized by Baghdad) to international companies (Cordesman and Khazai, 2014: 284), built oil export pipelines and sold oil in international markets at a discount (which Baghdad regards as stolen oil). Unlike Baghdad's oil service agreements, these contracts are mostly production-sharing type arrangements. Oil policy in Iraqi Kurdistan has been murky, with the KRG unwilling to disclose who it sells oil to or other aspects of its operations, as Baghdad withdrew financial support for the KRG in 2014 (Osgood, 2018). This dynamic between Baghdad and the KRG has curbed oil exports and revenues.

The issue of control over oil is intertwined with Kurdish aspirations for independence, reflected in its vote for independence in 2017. Viewing the vote as illegal, the central government took control of Kirkuk (an ethnically diverse and oil rich region) in response.[17] While most of Iraq's oil reserves lie outside the Kurdish region, Kurdish independence is not viable without Kurdish control over some of Iraq's oil. However, only 17 percent of Iraq's oil reserves lie in northern

[16] US and UK pressure for Iraq to de-nationalize and privatize its oil sector in 2006 and 2007 largely failed because of a popular backlash (Muttit, 2012; Nalman, 2007).
[17] Kirkuk itself had come under the control of Kurdish forces (fighting the Islamic State) in 2014.

Iraq (Cordesman and Khazai, 2014: 328), only part of which the KRG controls. According to Article 140 of Iraq's Constitution, Kirkuk, which is presently not part of the KRG, is supposed to vote on whether to join the KRG or remain within Iraq (Raheem and Rubaie, 2019); because of the sensitive implications of such a vote, none has occurred. In reality, Baghdad fears making the concessions over oil to the KRG, including control over exploration, extraction and sale, for fear of encouraging regionalism elsewhere, notably in Basra where most of Iraq's oil is produced (Cordesman and Khazai, 2014: 342). The thorny issue of control of oil remains unresolved and Iraq presently operates under divergent oil management regimes, with the ever-present threat of conflict or violence.

In addition to the political, there are administrative and technical challenges. Cordesman and Khazai (2014: 327) note that violence, sabotage and poor infrastructure have all contributed to limiting Iraq's oil exports; engineering difficulties abound with water having to be brought inland to Iraq's southern oilfields from the Gulf, which has proved difficult at times (see Shubbar, 2016). There is a need to improve oil marketing as Iraq is still using the same marketing techniques as in the 1970s and 1980s (al-Badran, 2017). These capacity issues will take investment and time to overcome, but are complicated by factionalism and political deadlock in Baghdad.

4.2. The centrality of the state and the policy landscape

Attempts to encourage the private sector notwithstanding, state controlled oil revenues remain central to Iraq's economy. Thus, the question is not whether state involvement in the economy is substantial, but what form the involvement takes. There is no contradiction in principle between an active state and a vibrant private sector. In the short to medium-run, we advocate an expansion of the state and strengthening of its institutions rather than its withdrawal, although the ultimate objective of course is to encourage economic diversification and that requires private sector development.

Rodrik (2011) notes that there is no single method to achieve prosperity (239) but that alleviating the binding constraints that hamper development is key (176). Countries following mainstream polices advocated by the Washington Consensus, he adds, have often fared worse than those that deliberately and strategically violated its precepts. Policy thus should be flexible, undogmatic and experimental. Measures that reduce the odds of violent shocks and that use and develop local institutions and resources ought to be favored. Iraq has benefited from IMF technical assistance and World Bank funding, but should avoid formulaic policy pitfalls that at times emanate from IFIs.

Concerning the labor market, we contend that, first, the continued expansion of the public sector as a welfare program is neither an efficient nor an egalitarian way to distribute oil revenues: the state is simply unable to employ half a million Iraqi youths (Patel, 2018: 7) that enter the labor market annually. Using the state in this way, Fukuyama (2013) suggests, also damages professionalism in the public sector and reduces state effectiveness. Ideally, hiring and wages in the public sector ought to be frozen, as Gunter (2018) advocates;[18] however, exceptions for essential personnel, as in health and education, would need to be made. This entails, second, developing alternative welfare programs. We argue that Iraq eschew IMF calls, made since 2003 (IMF, 2003: 20-21), to reform the PDS from an in-kind and comprehensive program to a targeted cash scheme. IFIs have long had a preference for targeted as opposed to universal programs, citing expense and the waste involved in providing benefits to the non-poor. In contrast to IFI thinking, we view universal coverage as a potential benefit, especially as limited state capacity in Iraq makes identifying who is poor costly and difficult. Because of numerous advantages, we instead suggest expanding the PDS into a basic cash income. First, the basic income scheme would use existing institutions built around the PDS, utilizing the latter's near universal coverage, and require little in terms of additional capacity. Second, like the PDS, it would distribute oil revenues to all regardless of ethnicity, sect or geographic location, reducing horizontal inequalities. Third, it would work to reinforce Iraq's political economy, where the public expects the state to distribute oil wealth equitably, strengthening the sense of nationhood. Fourth, such a scheme would also reduce pressure on government to provide jobs. Fifth, a cash as opposed to an in-kind program would reduce opportunities for corruption and inefficiency related to the PDS, vis-à-vis procurement and resale of goods, although the administrative cost of the PDS are modest.[19] A central intent of the proposal then is to enhance stability and allow investment and economic growth to proceed.

While space does not permit a detailed exploration of a basic income scheme, we provide a preliminary outline in three scenarios (see Van Parijs and, Vanderborght, 2017, pp. 11-17). Extension of coverage might be gradual, starting with specific demographic groups and cater to circumstances (Standing 2017, pp. 292-293).[20] In the table below, the scenario 1 represents a basic income of 25 percent of GDP per capita, as Van Parijs and Vanderborght (2017) suggest; in 2018, the basic income would be $1,075 per person per annum. Scenario 2 represents 'Cost of Basic Needs,' based on the result of 2007 Household Survey; this translates to $732 per person per annum, $324 for food and $408 for non-food items (Latif, 2015: 9). Scenario 3, based on the World Bank's former poverty lines of $1.25 and $2 per day, implies a basic income of $456 and $720 respectively per person per annum, almost identical to the cost of basic needs in 2007. Based on Iraq's age structure data (see Worldmeters, 2019), we estimate that extending $2 per day to every Iraqi would cost 18 percent of GDP in 2018; targeting 20-34 year olds costs 4.6 percent of GDP.

[18] Gunter (2018: 395) calls for a hiring but not pay freeze, probably in recognition of the political difficulties that a pay freeze would involve.

[19] The program cost 1.8 percent of GDP in 2013, of which 0.3 percent was administrative (IMF, 2015: 16) The IMF (2015: 15-20) advocated reform of the PDS as the program creates 'distortions' to the extent that it purchases domestically produced wheat at double the price of imported wheat. But the price of imported wheat is itself distorted from heavy subsidization in producer countries and any saving in abrupt reductions of subsidies for wheat in Iraq would have to compare against the decline in an already weakened agricultural sector.

[20] Because of limitations of data, we use estimates of population (of 39.34 million in 2018) and GDP (for 2016) from UNData (2019) to calculate figures in the 2018 column. Scenario 2 is based on 2007 prices.

Table 3. Basic Income: three scenarios (all in US $)

	2005	2010	2018
Gross domestic product (million current $)	36,268	117,138	160,021(a)*
GDP per capita (current $)	1,343	3,808	4,301*
Scenario 1 one fourth of GDP per capita	336	952	1,075*
Scenario 2 Cost of basic needs	732 **		
Scenario 3 World Bank Poverty lines of $1.25 and $2 per day			456 (for $1.25)* or 720(for $2)*

* Based on 2018 population and 2016 GDP estimates.
**Scenario 2 is based on 2007 prices; scenario 3 is based on 2018 prices. One US $ = 1,254 ID in 2007.
Sources: UNData (2019), Van Parijs and Vanderborght (2017), Latif (2015).

We ought to stress that we do not view this proposal as a panacea and do not downplay its costs. On its own, a basic income will not improve public services nor substitute for sector specific policies (e.g. in agriculture or industry) (see Mirza, 2011). Although a rise in unearned income is supposed to increase leisure demand, a study of the effects of basic income on labor supply in Iran shows no reduction in supply (Salehi-Isfahani and Mostafavi-Dehzooei, 2017).[21] Training and skills acquisition of electricians, plumbers, etc. . . , disrupted with internal and outward migration, ought to be pursued in unison to facilitate expanded investment rates (Gunter, 2013: 104).

Parallel to labor market and income reforms, Iraq, among the least diversified oil-exporters in MENA (IMF, 2019: 4), should gradually diversity its sources of budget revenue away from its near complete dependence on oil; non-oil revenue, including income tax and other items, varied between 2.1 and 3.5 percent of GDP in 2013 to 2015 (IMF, 2017: 36). In addition to providing revenue, taxation helps build a sense of accountability between the public and government, lacking in Iraq's reconstruction (Matsunaga, 2019: 16-18).

A major obstacle to tax collection is Iraq's enterprise registration rules that are lengthy and complicated. According to the World Bank (2019: 178), Iraq ranks 171 out of 190 in terms of 'ease of doing business' and 155 out of 190 for 'ease of starting a business.' Much of the private sector thus remains unregistered and untaxed, which adds to labor force informality. Iraq has medium to high levels of informality in comparison to other MENA countries. A quarter of economically active Iraqis are self-employed and two-thirds do not have access to the pension system, both somewhat higher than MENA comparators; because of the decline in agricultural labor, only 2.6 percent of the labor force is unpaid, lower than MENA comparators (Angel-

[21] Salehi-Isfahani and Mostafavi-Dehzooei (2017, 12-13) argue that the basic income actually raised labor supply among service sector workers, because some credit-constrained service sector firms used the basic income to expand operations.

Urdinola and Tanabe, 2012: 8). Registration of employees might be facilitated by, for example, offering a tax holiday of a few years, instituting online registration and making bank credit contingent on registration. Reducing informality and integrating businesses into the national pension system, will make the private sector more attractive as an employer, alleviating the political pressure for government jobs.

Concerning credit, a long overdue restructuring of state-owned banks is required over the longer-term. As things stand, these banks lack sufficient capital and their ability to lend to small and medium sized firms, in principle significant generators of employment and output, is restricted (see IMF, 2017: 22-23). Banks stay in business by charging for services and in the buying and selling of currency; they lend to SOEs, many of which are not viable commercially and overstaffed, which introduces a distortion in the credit market.[22]

It may not be possible to do all of these at once: vested interests in Iraq's bureaucracy or elsewhere may resist change because they benefit from the status quo, for example, as they receive bribes to expedite business registration. We contend that conflict and violence—not static economic inefficiency, per se—have acted as binding constraints on development. Hence, policies likely to reduce conflict, e.g. the equitable distribution of oil rents in a basic income, ought to be prioritized.[23] In the longer term, the repair of development capacity and institutions is vital, and there is a need for a body that assists in coordinating and overseeing public and private investment activities, as the Development Board did in the past (see Al-Marsoumi, 2019).

5. Conclusion

The recent protests that erupted in Baghdad and most of Iraq's southern provinces reflect popular frustrations with high youth unemployment, dire public services and chronic corruption. What we have attempted to do here is to give context to this reality and explain why it has been difficult to escape.

Iraq has been subject to multiple violent shocks, including wars, economic sanctions, invasion, civil war and internal displacement. Eggertsson (2008: 48) notes that negative external shocks are most destructive to developing countries because rudimentary technology in those countries restricts their ability to respond to shocks. Likewise, North et al. (2009: 252) writes:

> Over the last two centuries, sustained economic growth results from the reduction of negative shocks to social output rather than a marked increase in the rate of growth in years when output is growing.

Institutional decline along with loss of human and physical capabilities account for Iraq's lackluster economic recovery; this decay is unlikely to be reversed quickly. We argue that

[22] According to the (World Bank 2014a: 30), nonperforming SOEs have often received on an annual basis more funds than sectors such as health, education, water, and sanitation.

[23] On binding constraints see Rodrik (2007: 62-74).

deteriorating political institutions and narrowing political space in the 1970s and 1980s, along with protracted economic sanctions in the 1990s resulted in the decline in developmental institutions and structures. Reconstruction, notably under US occupation, sought to sideline existing institutions in Iraq and worked against the prevailing political economy; it neither constructed stable new institutions nor repaired existing but broken ones, aggravating conflict and establishing instead a fragile and fragmented polity. Subsequent Iraqi governments have not done better. The challenge—and it is a substantial one—is to encourage conditions where Iraq's human capabilities and institutions can develop.

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