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The Iraq Economic Review

**The Business of Education: Examining the
Growth of Private Schools & Universities**

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ABOUT IRIS

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ABOUT THE AUTHORS



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LETTER FROM THE EDITORS: ABOUT THIS ISSUE

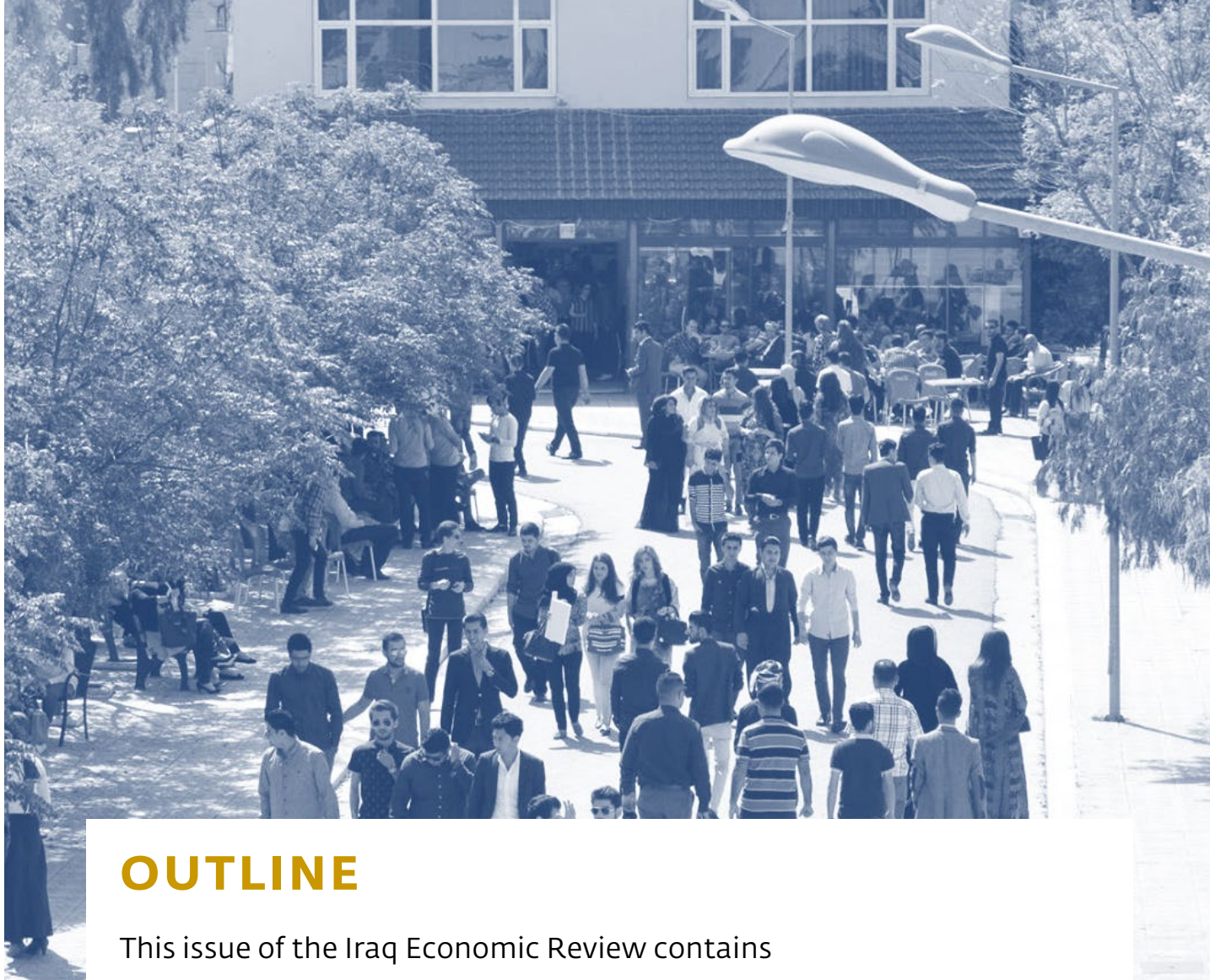
As the Iraq Economic Review now enters its second year of publication, we look forward to including a wide range of voices and perspectives from across Iraq on various aspects of the economy. These perspectives may not always agree with one another, and this is precisely the point. There are no easy policy solutions to address the enormous challenges Iraq faces in generating employment, promoting local production and industry, and preparing for the energy transition. Across different segments of Iraqi society, there is little agreement around what a healthy economy would look like — and whether it is even possible to build a robust non-oil economy in a country where both the private and public sectors are dominated by the post-2003 ruling elite.

One goal of the Review is to move beyond general commentary about the growth potential of a given sector and instead to view the sector from within. Accordingly, this issue of the Review includes two contributions (from Nabil Al Tememi and Abdurrahman Wahab) focusing on private education as a growing sector in the economy, both in federal Iraq and the Kurdistan region. Both pieces raise questions about the sustainability and societal impact of the business model upon which this new sector is based, and they call for a renewed policy framework that sets a clear vision for private and public education alike. The Review concludes with a piece from Ahmed Tabaqchali that reflects upon the broader trajectory of the economy in 2022 based on the lessons of the pandemic.

Finally, we encourage analysts and researchers (Iraqi nationals only) with interest in contributing to future Reviews to contact us at iris@auis.edu.krd. We also encourage letters to the Editor that respond to any previously published piece.

Sincerely,

The Editors of the Iraq Economic Review



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SECTION I

Private Education in Federal Iraq: Growth due to Neglect of the Public Sector

Nabeel Jabbar Ali Al Tememi

INTRODUCTION

The for-profit private education sector has grown in Federal Iraq since 2003, both at the primary/secondary school and university levels. This policy brief explores this growth through economic and legal analyses. First, the brief argues that demand for the private sector has grown in direct relationship to the neglect of the public sector. Government spending on public education since 2014 has flatlined, despite steady population growth, with negligible investments in education infrastructure and expansion. The private sector at the primary/secondary level has benefited handsomely, growing merely by offering seats that the government has neglected to provide. As interviews with Iraqi families conducted for this study indicate, the main reason parents and students opted for private education was the deteriorating conditions and overcrowding of public educational institutions. At the university level, similar dynamics are at play. Public universities offer limited slots for more prestigious degrees (medicine, engineering, law), thereby incentivizing students with resources to turn to the private sector for improved chances at admission. In

other words, private universities have absorbed overflow capacity at a premium.

Second, the analysis turns to the education policy and legal framework. Underlying the pervasive neglect of public education, and the resultant growth of the private sector, is a flawed educational policy framework instituted in the years following 2003. The post-2003 years saw the rolling back of legal restrictions on the establishment of private education institutions. With a short time, all manner of businesses and individuals began opening for-profit schools and universities. Powerful businesspeople and political actors, with little in the way of credentials in the education sector, were now permitted to launch for-profit schools and universities, all the while guaranteeing a steady flow of customers by neglecting to advocate for adequate investments in the public sector.

This interdependent public-private relationship has led to the stagnation of both the public and the private education sectors. The public sector is declining under government neglect, and the private sector has little motivation to

invest or innovate due to the artificial demand generated by the collapsing public sector. This policy brief calls for a renewed policy framework governing the public and private education sectors.

EXAMINING THE NUMBERS

Enrollment in Private Education Institutions

Private education is on the rise in Iraq. In 2003, the number of private universities did not exceed ten and included approximately 20,000 students. Today there are 75 private universities and approximately 220,000 students, representing a ten-fold increase. As for private primary and secondary schools, they were almost non-existent before the US-led invasion in 2003; today, such schools boast a cross-country network of 2,700 institutions, hosting approximately 5% of the total number of students in Iraq.¹

Limited Spending on the Public Sector

One factor explaining the growth of the private sector is the government's neglect of the public sector. Spending for public-sector education has flatlined in the years since 2014, despite the explosion of demand. Since 2014, the annual expenditure for education has hovered around 10 trillion IQD annually (approximately \$6.75 billion USD).² Of that 10 trillion IQD, approximately 7.5 trillion IQD goes to the Ministry of Education (primary and secondary schools) whilst 2.25 trillion IQD goes to the Ministry of Higher Education (universities). The stagnation in funding levels is entirely out of alignment with demand, as the total number of students in educational institutions increases by approximately 4.4% annually.³ (During the same period, expenditures for security institutions continue to increase on an annual basis, despite Iraq ostensibly transitioning to a post-conflict phase.)

Not only is the total amount of expenditure worrisome, but the category of spending is also troubling. Iraq's education budgets for the last six years have focused

heavily on operational costs related to staff salaries and expenditures on goods and services. The investment expenditures necessary to maintain facilities and technology have decreased to a negligible amount during the 2014-2021 period. Consequently, school buildings are literally crumbling, and parents are concerned for their children's safety.

WHAT PARENTS AND STUDENTS SAY

The choices of parents showcase the lack of investment in public education. Interviews with parents of students in private primary and secondary schools revealed that the leading reason parents opted for a private education was the relative deterioration and overcrowding of public schools; the second reason parents cited was the low quality of teaching and levels of attention to students. The interviews suggest that dire conditions in public schools place parents in a moral and financial bind in which private schools become the only viable option.

Interviews: Parents of Primary School Students

Mr. Qasim, who lives in Baghdad, reported that he was forced to enroll his young son in a private school despite low wages and lack of assets because of the unacceptable and unsafe situation in the local public school:

“ A single class often contained 90 students or more, while the capacity of the typical class should not exceed 35 students.

Qasim added,

“ I was shocked by the condition of the school and the sight of students sitting on the ground and the yard crowded with students, which basically turned into an open taekwondo arena.⁴

1 "National Development Plan 2018-2022," Republic of Iraq Ministry of Planning, June 2018. [https://mop.gov.iq/en/static/uploads/8/pdf/1545900842d4e4eef48c6122449898d79a86b841fb--\(الكلبي\)20%التنمية20%الوطنية20%\(الكلبي\).pdf](https://mop.gov.iq/en/static/uploads/8/pdf/1545900842d4e4eef48c6122449898d79a86b841fb--(الكلبي)20%التنمية20%الوطنية20%(الكلبي).pdf).

2 This represents an average expenditure of 3.5 million IQD (\$2,300 USD) for each student, a number that pales in comparison to some of Iraq's poorer neighbors.

3 Republic of Iraq Ministry of Planning, Central Statistical Organization, <http://cosit.gov.iq/en/>.

4 Nabeel J. Al Tememi, direct interview by author, November 5, 2021.

Students waiting to enter their classrooms in a public school in Baghdad, Iraq. Nov. 21, 2021. Reuters.



Other interviews repeated the same theme. Mr. Walid from Dhi Qar Province noted that he saves about 25% of his monthly salary to cover the annual installments for his three children who are enrolled in private schools, and that the main reason for attending private schools is the lack of suitable public school options in his area. He spoke of being “forced” to “bear the additional spending burden to provide a suitable education opportunity for his children,” when “only the affluent have the resources to bear such burdens.”⁵

Notably, parents making these financial sacrifices rarely had much to report about the educational assets offered by private schools. Instead, parents suggested that these schools provided the same basic academic offerings but with less overcrowding and safer building facilities. Far from providing parents and children a robust education with enhanced options, the private sector succeeds merely by offering less crowded spaces and a marginally better resourced educational experience. Importantly, this is not to say that all public schools are in a state of duress. Anecdotally, some public schools have relatively appropriate numbers of students and sufficient building facilities, but these accounts are the exception, not the rule.

Interviews: University-level Students

As for higher education, the generation of demand in the private sector largely has to do with the limited slots available in public universities for prestigious degrees such as medicine, engineering, and law. In interviews with university students, respondents reported that such degrees are regarded as the only guaranteed path to high-paying public employment. Since public institutions accept degrees from public and private universities equally, interviewees noted that there is major long-term upside to paying for a private degree in a prestigious specialization, given the long-term financial benefit after graduation. While this arrangement may open career opportunities for a narrow subsection of society, it ultimately creates further inequalities by granting elite families greater access to prestigious degrees.

5 Nabeel J. Al Tememi, phone interview by author, November 7, 2021.

6 Abdul-Razzaq Hilali, *History of Education in Iraq during the British Mandate 1921-1932*. Lebanon: Al Rafidain Printing. ISBN 9781773223063.

7 Teachers College was changed to College of Education and annexed to Baghdad University. University of Mustansiriyyah was annexed to the People's University but later became a separate public university.

EDUCATION POLICY BEFORE AND AFTER 2003

Underlying this pervasive neglect of public education, and the resultant growth of the private sector, is a flawed educational policy framework instituted in the years following 2003. Private education underwent decades of slow and piecemeal development beginning in the early 20th century. Understanding this development over time offers insights into the current policy framework, and how it may be corrected.

The Origins of Private Education

During the 1920s, private schools and universities witnessed little growth due to the concerns of British military authorities, who feared that such schools would be “sponsored by parties, personalities and associations opposed to and against the British presence in Iraq.”⁶ Such restrictions were lessened during the 1932-1958 mandate period, allowing for moderate expansion of private institutions. The 1958 revolution introduced the slogans of socialism and a fair amount of skepticism around the role of private education in the Iraqi state.

Parameters Put in Place

While some private institutions were nationalized during the post-revolution period,⁷ the successive governments after 1958 made no attempt to abolish private education altogether. Instead, parameters were placed on the growth of private institutions through legislation issued in 1968 that limited the entities legally eligible to found universities and schools. These entities were limited to unions, federations and charitable societies characterized as non-profit institutions. Perhaps because of these constraints, the growth of private education did not witness significant development until the late 1980s, when several private universities were established in quick succession. Public education remained the priority, and private education could only exist within well-defined parameters.

The Wholesale Removal of Parameters After 2003

While pre-2003 legislation stated that only non-profits (working in concert with state ministries) were eligible to establish schools and universities, post-2003 legislation removed all such barriers. The new rules allowed all manner of individuals and businesses to establish educational institutions and to seek profit from the endeavor. Whereas the term “private education” pre-2003 referred to schooling conducted by non-profit or charitable institutions, the same term became synonymous in the post-2003 period with the for-profit educational sector. The problem with the wholesale removal of barriers and standards to entering the field of education is that business-oriented institutions have been given no incentive to think beyond profit. Investments in scholarly research, pedagogical innovation, and international partnerships—the kinds of investments needed for Iraqi educational institutions to compete regionally—are essentially nil because such pursuits do not directly benefit investors or the bottom line.

CONCLUSION AND RECOMMENDATIONS

Developing a healthier relationship between the public and private education sectors is essential for Iraq to build an education system that can meet the needs of families as well as cultivate new generations of leaders, educators, and skilled professionals. Two recommendations are made:

Reinvest in Public Sector Education

First, a significant reinvestment in the public sector is needed to benefit both public and private educational institutions. A robust public sector will ensure that growing demand for the private sector is based on substantive advantages rather than artificial demand. The permissive posture of the post-2003 governments towards the private sector has allowed the state to side-step responsibility for dealing with increased population growth. The state has especially neglected its responsibility to establish more schools and create or expand universities, meaning that there is simply a lack of available seats and, consequently, widespread overcrowding.

As the interviews with families indicated, many parents would rather suffer personal financial ruin than see their children in overcrowded and dilapidated classrooms. Shifting this huge financial responsibility onto families emerging from three decades of war compounds other burdens and exacerbates societal inequalities. It also allows private educational institutions a steady flow of customers without the incentive to innovate and mature into robust educational institutions that are truly worth the price tag of a diploma.

Restore Parameters on Private Sector Education

Second, parameters must be put in place to regulate the entities that can establish schools and universities. After 2003, the wholesale removal of all meaningful barriers to entry into the education space has invited an explosion of for-profit entities to establish schools and universities. This is not to suggest that the pre-2003 limitations should simply be replicated, but rather that a set of standards appropriate for the present moment should be developed. In Iraq’s political economy, defined by collusive relationships between political actors and the private sector, it is untenable to incentivize dismantling public-sector education to enrich poorly regulated private-sector businesses. Not all growth is good growth. Rather than allowing this chaotic situation to continue, the government must reimagine a sustainable, fair, and balanced policy framework for public and private education alike.



SECTION II

Private Universities in the Kurdistan Region: When Policy & Profit Stifle Development

Abdurrahman Ahmad Wahab

INTRODUCTION

The Kurdistan Region of Iraq (KRI) witnessed significant growth of private universities in the years after the 2003 US-led invasion. The majority of the 18 existing private universities were established between 2007 and 2014, a time when the KRI was going through an economic boom due to growing oil-based revenues as well as to international investors' interests in the local market. Most reports have described the KRI's private universities in two very different ways: as tools in the hands of the corrupt political elite,^{8, 9} or as magic wands that will help usher in economic development via the growth of the free market.^{10, 11} This policy brief neither dismisses nor lauds private education, and instead attempts to examine how and why the sector has developed in the

Iraqi Kurdish context, and what this growth might mean for education and economic policy.

In terms of policy, it is evident that the Kurdistan Regional Government (KRG) has not yet offered a coherent vision for the private education sector. The current policy framework is flawed because it permits—even incentivizes—owners of private universities to prioritize profit and cost-cutting over educational excellence. Consequently, KRI's private universities have increasingly become little more than for-profit instructional institutes offering degrees as the product and attracting students as the consumers, almost entirely ignoring the broader research and innovation components found among regional and

8 Kamaran Haji Omer, "Online studies at the private universities in the Kurdistan Region" [Kurdish], Kurdistan24 Production, June 16, 2020. https://www.kurdistan24.net/public/index.php/ckb/tv_episode/كوردستان-خوتندى-ئۆنلانى

9 Barham Lateef, "Business under the guise of knowledge" [Kurdish], Roj News, February 27, 2020. <https://rojnews.news/كوردستان/زانكۆ-ئەهلبەهەكان-بازرگانی-لە-ئێ-ر-بە>

10 Waqar Ahmad, "The Role of Private Universities in the Economic Development of Kurdistan: An Explanatory Study," International Conference on Accounting, Business, Economics and Politics, 2019. <https://business.tiu.edu.iq/icabep-archives/wp-content/uploads/2019/07/32.pdf>

11 Catherine Honeyman and Hannah Zuzek, "Iraq ELITES Rapid Labor Market Assessment (RLMA) Report," World Learning, December 14, 2020. <https://www.worldlearning.org/wp-content/uploads/2021/01/Iraq-ELITES-Rapid-Labor-Market-Assessment-2020.pdf>

global institutions. This cut-rate model has stunted private universities from developing into mature institutions that can mold the KRI's next generation of leaders. While such dynamics are likewise characteristic of private universities in Federal Iraq,¹² the KRI is a unique context with a distinct educational policy framework that must be understood on its own terms.

THE BUSINESS OF INSTRUCTION

New Laws Yield a New Business Model

The private university sector in the KRI was set up for confusion from the start due to an ill-advised Investment Law No. 4 of 2006. This law, which allowed private universities to be established by investors and run as for-profit entities, set off an explosion of investor interest. Instead of ensuring the slow and regulated growth of private universities under robust guidelines and parameters, these institutions were essentially allowed to operate for the first several years according to the for-profit model that promised the surest return for the political and economic elites who had invested. The winners in this equation were elites tied to the dominant Kurdish political parties seeking to profit off the post-2003 turn towards rampant and unregulated privatization.

Cost-cutting in Service of the Bottom Line

With a few notable exceptions,¹³ what emerged from this business model were essentially low-cost instructional institutions that offered a simple but much sought-after product: a university diploma. Most investment capital was directed towards low-maintenance instructional classrooms that accommodated as many students as possible. Programs required instructors to deliver course content

to students using minimal instructional tools. Many private universities started their operations in temporary or make-shift structures, accumulating revenue years before securing campuses of their own. With costs kept to a minimum, private universities broke even and reached self-sufficiency within a few years after their founding. According to a former top private university leader, these institutions gradually became “cash machines.”¹⁴

Quality Suffers

This same situation stands today. The problem with this business approach is that the KRI's private universities were never incentivized to develop into modern universities meeting global standards. Operating the low-cost, instructional university model does not compel expenditures in long-term research ventures that might raise a university's regional or international profile. For many investors, any expenditure beyond salaries and basic maintenance would contradict their long-term aspirations to convert these institutions into real estate assets. As a private university representative posited, “Private university owners acquire profit, whether through the increased number of students or through the added value of the university buildings, and many times through both.”¹⁵

Artificial Demand

If quality is mediocre or worse, one may wonder: Why is there a market demand? Private universities tend to tout themselves as gateways to better employment, but most university-aged students interviewed for this paper acknowledged that ties to political patronage networks are far and away the most important predictors of job placement.¹⁶ More than the promise of employment or a better-quality education, the demand for private universities in the KRI is essentially

12 See this issue's companion article, “Private Education in Iraq” by Nabeel Jabbar Ali Al Tememi.

13 There are private universities in the KRI founded by charities/non-profits such as the Catholic University in Erbil, the American University of Iraq, Sulaimani, and University of Human Development in Sulaimani.

14 Former president of a private university, direct interview by author, Erbil, October 27, 2021.

15 Member of Board of Trustees at a private university, direct interview by author, Sulaimani, October 29, 2021.

16 The students' claim resonates with other reports on the ability of the KRI patronage system to control the job market. See: Zmkan Ali Saleem and Mac Skelton, “Assessing Iraqi Kurdistan's Stability: How Patronage Shapes Conflict,” London School of Economics, Middle East Centre (MEC) Paper Series 38, July 2020. https://auis.edu.krd/iris/sites/default/files/MEC_assessing_iraqi_kurdistans_stability_published.pdf.

guaranteed by the neglect and scarcity of seats in the public university sector. Even though the number of public universities in the KRI has increased since 2003, they have not grown proportionally with the KRI's population. According to data from the Ministry of Higher Education, around 63,300 students graduated from high school in 2021,¹⁷ 52,500 of whom are expected to attend one of the 14 public universities.¹⁸ Between 10,000 to 12,000 students are also expected to attend one of the 32 private post-secondary institutions in the KRI, 18 of which are universities. Private universities are expected to admit about 15% of all university students.¹⁹ In sum, private universities do not need to innovate or pursue excellence because demand is generated by limitations placed on the public sector.

THE PURSUIT OF ORDER BACKFIRES

The 2013 Law of Private Universities

Seven years after the Investment Law, the Law of Private Universities No. 2 of 2013 attempted to regulate a space that was already set in its ways. On the surface, the Law of Private Universities sought to apply much needed order upon institutions that had never been required to uphold serious quality standards. The Law allowed the KRG Ministry of Higher Education to shape instructional policies, monitor curriculum, set quality standards, and generally oversee the private universities' operations. The Law also dictated how academic programs are established and managed, how academic staff are hired, and how leaders are appointed.



Private university in Erbil, Iraq. Oct. 7, 2017. Facebook.

17 "Zankoline is ready for high school graduates" [Kurdish], Binar Media Channel, September 30, 2021. <https://www.bmctv.krd/details/35141>.

18 "The Ministry of Higher Education solved twelfth graders' issues," [Kurdish] Press Release, Ministry of Higher Education-KRG, November 2, 2021. <https://gov.krd/mohe/activities/news-and-press-releases/2021/november/کرد-دوانیزه‌ی-چاره‌سه‌ر-بۆلی-دەرچووانی-کێشه‌ی-دەرچووانی-بۆلی-دوانیزه‌ی-چاره‌سه‌ر-کرد>.

19 According to speculations from an official at the Ministry of Higher Education-KRG, phone interview by author, Erbil, November 23, 2021.

The Law Sows Discontent

However, the attempt to impose regulations on private higher education failed to change the power dynamics and economic interests undergirding the sector. Arguably this assertive interventionism on the part of the government further entrenched the worst qualities of the business-first model. To navigate the overregulated space and restrictive bureaucracy, private universities have relied on their political patrons to use their leverage to circumvent the rules. Meanwhile, pro-reform private university administrators argue that they were left incapacitated by the new regulations, incapable of making necessary changes to promote quality enhancements. Even government officials find themselves confused by the policy framework. Since policies are often vague, KRG Ministry of Higher Education officials are left to interpret the policies according to the bureaucratic tools with which they are most familiar. As a result, toxic relationships have developed between the private university leaders and KRG officials overseeing higher education. KRG officials argue that private universities with powerful political support are not compelled to follow the rules, and that influential patrons often shield the private universities from government accountability. A member of the Educational Committee at the Kurdistan Parliament reported that powerful political leaders have often interfered on universities' behalf when the committee members have tried to follow up on allegations of rights violations of teachers and staff, or during legal and financial disputes.²⁰ For their part, private university owners and leaders object to the government's interference into their operations. One private university leader lamented, "The Ministry [of Higher Education] wants the private universities to be like the public universities by micromanaging them."²¹

Collusion

These two sides are not always so far apart. University leaders and KRG officials establish formal as well as collusive relationships to navigate bureaucratic and political hurdles. The Ministry's National University Ranking

system (NUR) is a prime example, established in 2015 to provide "the definitive list" of the KRI's "best universities" according to seven weighted criteria ranging from the quality of academic staff to student satisfaction.²² Private university leaders have confessed that special committees and administrators overseeing the application of regulatory and evaluative procedures become prone to collusive relationships through their political affiliations, exploiting the existing systemic corruption to help some universities score against their competition in the NUR. Ultimately, both the KRG and private universities operate in a system where the Kurdish political elite dictate the winners and losers, and neither is immune from playing the game.

CONCLUSIONS

As a result of these failed regulatory attempts and entrenched political interests, the KRI's private universities have plateaued in terms of developing into the kind of mature research and education institutions that would allow the KRI to contribute regionally and internationally. A new approach in policymaking is needed if the sector is to move towards a more robust education model that spurs research, innovation, and development. Though political constraints will inevitably place obstacles in the way of reform, reform-minded officials in the KRG should revisit and amend the 2013 Law of Private Universities, which over-emphasized bureaucracy, regulation, and proceduralism. Instead, government should develop a legal framework for universities that encourages forward-looking investments in international partnerships, research collaborations, and pedagogical excellence. Furthermore, the new legal framework would also need to incentivize a non-profit private university model, one that values the role of education in promoting broader cultural, political, and society development. As long as the KRI's private education sector is dominated by the current set of for-profit entities, the low-cost instructional model will remain the dominant paradigm, and overall educational quality will continue to suffer.

20 Member of Education Committee in the Kurdistan Parliament, phone interview by the author, Erbil, October 24, 2021.

21 Member of Board of Trustees at a private university, direct interview by author, Sulaimani, October 29, 2021.

22 "Methodology," National University Ranking (NUR), Kurdistan Region - Iraq, Website: <https://www.nur-krq.net/methodology>.



SECTION III

Economic Roundup: What the Pandemic Tells Us About Future Growth & Volatility

Ahmed Tabaqchali

INTRODUCTION

The rapid spread of the COVID-19 Omicron variant disrupted consensus expectations for sustained near-term global economic growth after the strong rebound in 2021. As such, expectations have also fallen for an uninterrupted recovery in global oil demand. Global economic growth will continue for now, but will moderate significantly into 2022-2023, as the world learns how to deal with—and ultimately contain—this variant. However, the likely emergence of new variants means that similar disruptions to the global economy, and by extension to the global demand for oil, may be a common occurrence for the next few years. Negative effects on economic growth will likely moderate as a fuller understanding emerges about the virus. Still, global growth fluctuations will be keenly felt within Iraq's economy given its extreme leverage to oil demand. This quarterly forecast explores the enduring impact of the COVID-19 pandemic on Iraq's economy,

drawing insights from this tumultuous period to make speculations about near-term and long-term prospects for economy growth and volatility.

LOOKING BACK TO 2020: THE EARLY DAYS OF THE PANDEMIC

The global spread of COVID-19 in 2020 shocked the world's economies. The consequent sharp decline in global oil demand dealt a hard blow to Iraq, with reverberations that hampered economic growth.

The First Shock: Lockdowns

Lockdown measures to contain the spread of the virus restricted most domestic economic activities and had severe negative consequences for the private sector, comprised of micro, small, and medium enterprises (MSMEs)²³ that

²³ These mostly operate in retailing (wholesale and retail), basic manufacturing (textile, home furniture, metal works, etc.), agriculture and animal husbandry, construction, hospitality (hotels, cafés and restaurants, tourism), services (beauty salons, hairdressers, car and bike repair shops, etc.), and various professional and administrative services. Few MSMEs exist in the traded goods and services sectors (i.e., industry and service sectors whose output in terms of goods and services can be traded internationally or regionally).

predominantly operate in the informal economy and depend entirely on the domestic market. As such, they bore the economic brunt of lockdown impact.²⁴ The slowdown in economic activity in these sectors was particularly pronounced between March and October 2020 (see Figure 3).

The Second Shock: Crash in Oil Revenues

The second and more consequential dynamic was the erosion of government revenues—the bulk of which come from oil sales—from the crash in oil prices. Iraq's oil

sales in 2020 dropped from USD \$6.1 billion in January to just USD \$1.5 billion by April, before gradually recovering to USD \$4.1 billion in December 2020. This drop limited the government's ability to meet its expenditures—in particular, for salary and pension payments which averaged USD \$3.7 billion a month,²⁵ as well for other crucial expenditures such as social security, and goods and services. For 2020, salary and pension payments alone accounted for 95% of full-year oil revenues, while spending on goods and services accounted for another 18% (see Figure 1).²⁶



Workers at Iraq's Majnoon oilfield near Basra, Iraq. March 31, 2021. Reuters.

24 The only bright spot for the informal sector was in agriculture and animal husbandry which account for about 20% of all jobs in the economy, in a country where 30% of the population lives in rural areas. The closure of border posts with neighboring countries, a feature of the lockdown measures, allowed Iraqi producers of agriculture and animal husbandry to sell without competition from cheaper imports—in particular, those from Iran and Turkey. See “[Breaking out of Fragility: A Country Economic Memorandum for Diversification and Growth in Iraq](#),” International Development in Focus. Washington, DC: World Bank, September 30, 2020. <https://openknowledge.worldbank.org/bitstream/handle/10986/34416/9781464816376.pdf?sequence=4&isAllowed=y>.

25 Using the exchange rate USD 1 = IQD 1,182 which prevailed until the last 10 days of 2020.

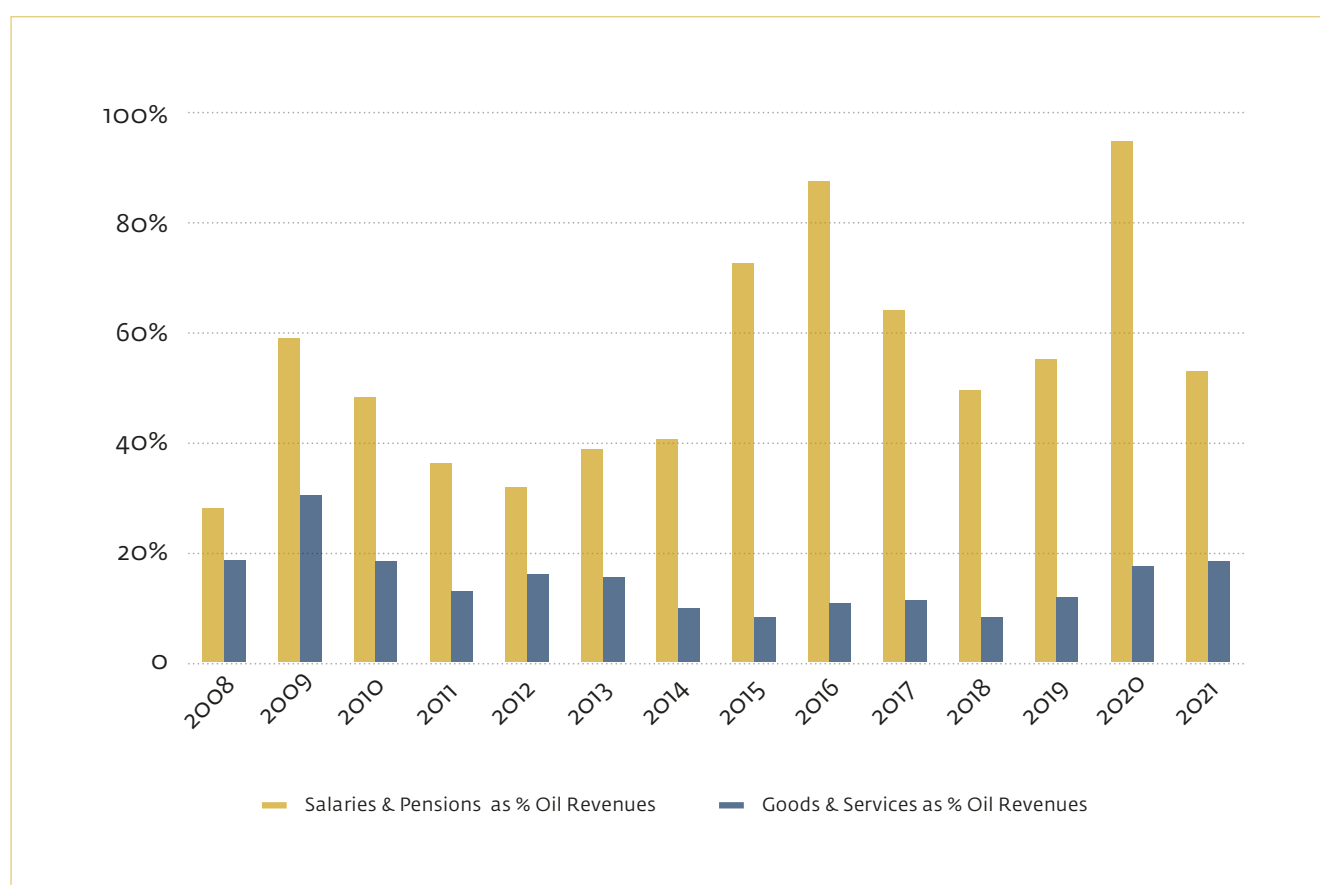
26 Spending on goods and services was at a bare minimum in 2020, but recovered to normal levels in 2021, which explains why it accounted for 19% of much higher oil revenues in 2021 versus 18% in 2020.

The Government's Response

As a result of steep drops in oil prices, the government resorted to borrowing domestically USD \$22.8 billion, in June and October of 2020,²⁷ most of which was through indirect monetary financing by the Central Bank of Iraq (CBI).²⁸ However, the process required two successive authorizations from parliament,²⁹ which were not synchronized with payment schedules. As such, the government held back on spending on most goods and services, and delayed salary and pension payments. All

of this magnified the woes of the private sector, given the outsized role that public-sector employees play in domestic consumer spending and the centrality of government spending, with the result that non-oil GDP declined by 20% in 2020.³⁰ With salary and pension commitments remaining constant, the percentage burden these commitments placed on the country's oil revenues surged from just under 60% in 2019 to 95% in 2020 (see Figure 1).

Figure 1: Salaries & Pensions and Goods & Services as % of Oil Revenues 2008 - 2021



Source: IMF for 2008-2020, Ministry of Finance (MoF) for January-November 2021. Estimates for December 2021 based on MoF data.³¹

27 Primary sales of Treasury Bills (T-Bills), plus borrowing from State Owned Banks (SOB's).

28 Indirect monetary financing of debt happens through the issuance of T-Bills that are bought by SOB's which are subsequently sold to the CBI.

29 Ahmed Tabaqchali, Hamzeh Al-Shadeedi, and Ai al-Saffar, "The National Budget: Short and Medium-Term Prospects," *Iraq Economic Review*, Institute of Regional and International Studies (IRIS), American University of Iraq, Sulaimani. February 2021. <https://auis.edu.krd/iris/sites/default/files/h8%20Feb%2021%20Iraq%20Economic%20Review.pdf>.

30 "Iraq Economic Monitor: The Slippery Road to Economic Recovery," Washington, DC: World Bank, November 24, 2021. <https://documents1.worldbank.org/curated/en/981071637593726857/pdf/Iraq-Economic-Monitor-The-Slippery-Road-to-Economic-Recovery.pdf>.

31 Oil revenues are from sales of crude oil exports, transfers of profits from oil related public enterprises, and taxes on oil companies.

LOOKING BACK TO 2021: UPTICK IN ECONOMIC ACTIVITY

Liquidity Injections

Starting in mid-2020 and into 2021, the government induced economic recovery through massive liquidity injections. Government borrowing in 2020, through indirect monetary financing, injected substantial liquidity into the economy. The CBI's adoption of an accommodative monetary policy to support borrowers and the economy in countering the negative effects of COVID-19 further increased liquidity. This policy contributed to a substantial increase in private-sector borrowing: loans to the private sector increased 22% by the end of 2020, and by a further 9% by October 2021,³² for a total increase of 31%. Ultimately, the most important source of liquidity came from sustained oil price increases from October 2020 onwards, which allowed the government to raise spending significantly.

Oil Brings Even More Money into the Economy

In 2021, oil sales increased from USD \$4.8 billion in January to an estimated USD \$7.3 billion in December; the government was thus able to meet its significantly increased expenditures following the passage of the expansionary 2021 budget in mid-April.³³ The devaluation of the IQD against the USD in December 2020 increased these revenues in IQD by 23%, further enhancing the government's ability to make these expenditures. Actual government spending on current expenditures (salaries, pensions, goods and services, social spending, and other categories) increased 22% by November 2021 versus the same period in 2020. While

18% less than what was projected by the budget up to then, it nevertheless represents an injection of liquidity estimated at 10% to the non-oil economy in 2020.³⁴ The combination of the three liquidity injections – i.e. government borrowing, CBI's accommodative monetary policy and recovering oil revenues – led to a substantial increase in the amount of money circulating in the economy,³⁵ as measured by broad money, from October 2020 throughout 2021 (see Figure 2).

Improvements in the Non-oil Economy

This provided a meaningful stimulus to the non-oil economy, whose effects can be seen from the noticeable increase in economic activity from October 2020 onwards (see Figure 3)–coinciding with a similar noticeable increase in the year-over-year change in broad money (see Figure 2)–as the economy continued to rebound. Crucially, activities in retail and grocery–accounting for a sizeable percentage of the informal economy, largely driven by MSMEs–recovered by the end of December by up to 90-170% of pre-COVID levels. Available data show that the non-oil economy increased by over 21% in the first half of 2021 versus the same period last year, with current indicators suggesting a continuation of the recovery, but at much lower rates in the second half than the first half of 2021.³⁶

32 Relative to the prior year, the slower growth rate in private-sector borrowing in 2021 was the result of the CBI unwinding its accommodative monetary policy as the economy recovered.

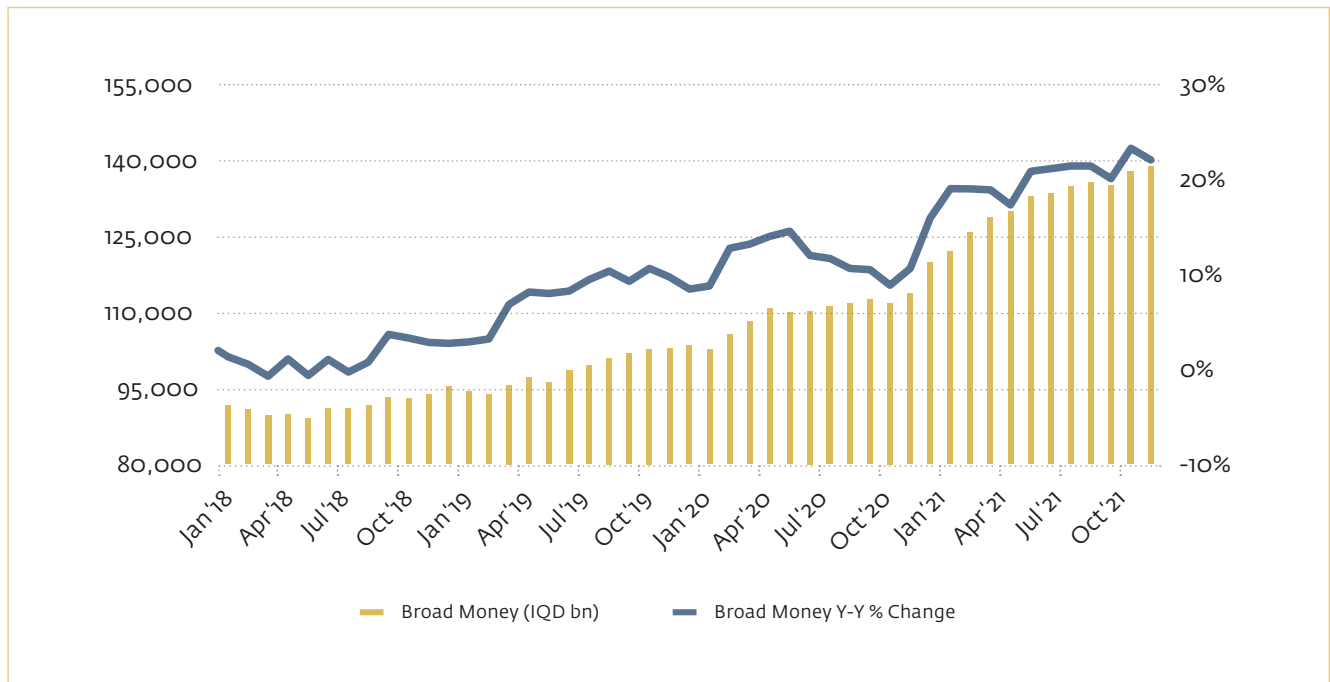
33 Tabaqchali, Al-Shadeedi, and al-Saffar, "The National Budget."

34 The delayed passage of the 2021 budget until mid-April 2021 accounted for a significant part of the discrepancy between budgeted expenditures and actual expenditures. However, a gap would remain given the country's challenges of converting planned expenditures into actual expenditures. Such a gap is much higher for non-oil investment spending, as actual non-oil investment spending was up 73% by November 2021, versus the same period in 2020. However, it is 86% less than what was projected by the budget up to November 2021.

35 Ahmed Tabaqchali, Hamzeh al-Shadeedi, Muhammad al-Waeli, and Marsin Alshamary, "Expanding Access to Banks in Iraq: Challenges & Pathways to Reform," Iraq Economic Review, IRIS, American University of Iraq, Sulaimani. September 2021. https://auis.edu.krd/iris/sites/default/files/iris_iraqeconomicreview_digital.pdf.

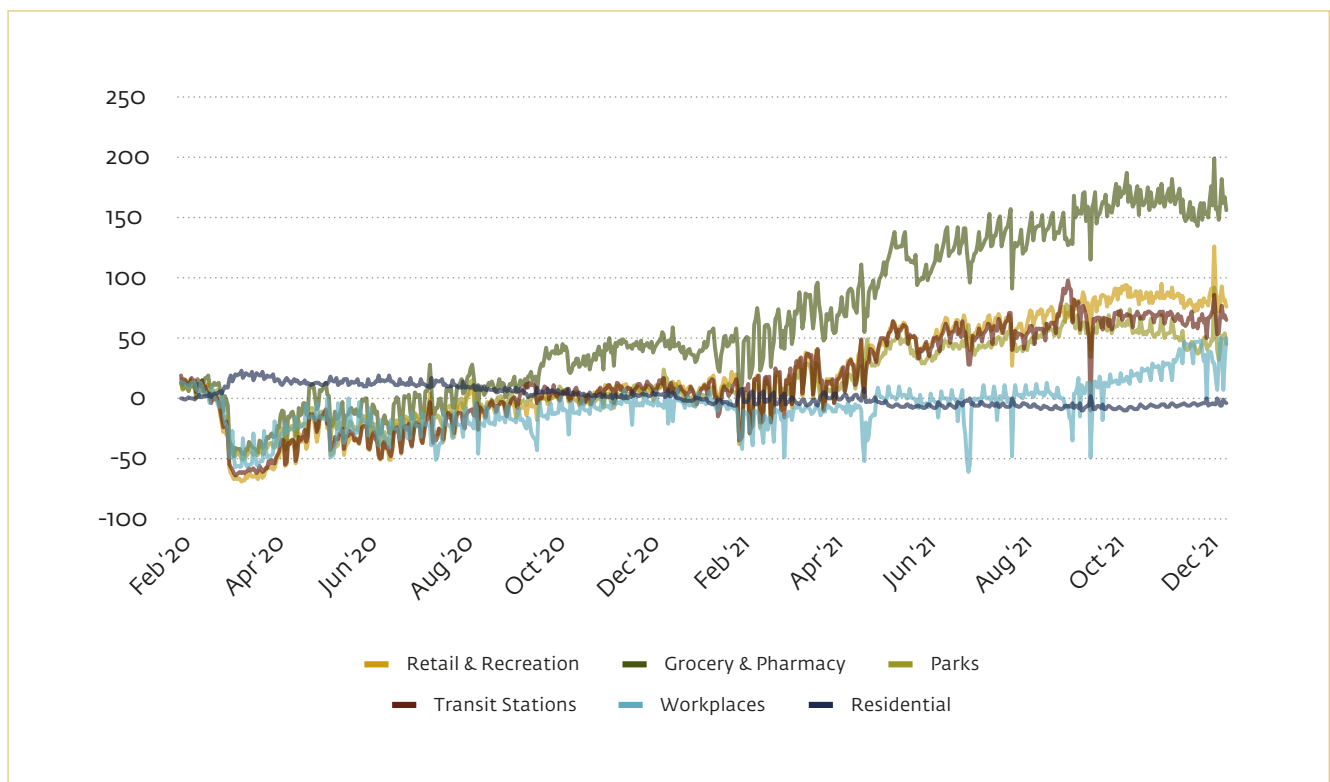
36 Non-oil GDP growth of 21% in the first half of 2021 was in comparison to the extreme lows in the same period in 2020, which included the first extended lockdown period. Growth in the second half of 2021 reflects an economy in the processes of returning to post-COVID activity. The World Bank estimates 2021 growth of 2%, although the figure is likely to be meaningfully higher. See also, "Iraq Economic Monitor: The Slippery Road," World Bank.

Figure 2: Money Circulating in the Economy



Source: CBI, data as of the end of November 2021.

Figure 3: Economic Activity in Key Non-Oil Sectors



Source: Baseline is the median, for the corresponding day of the week, during January 3-February 6, 2020. Google, data as of January 8, 2022.

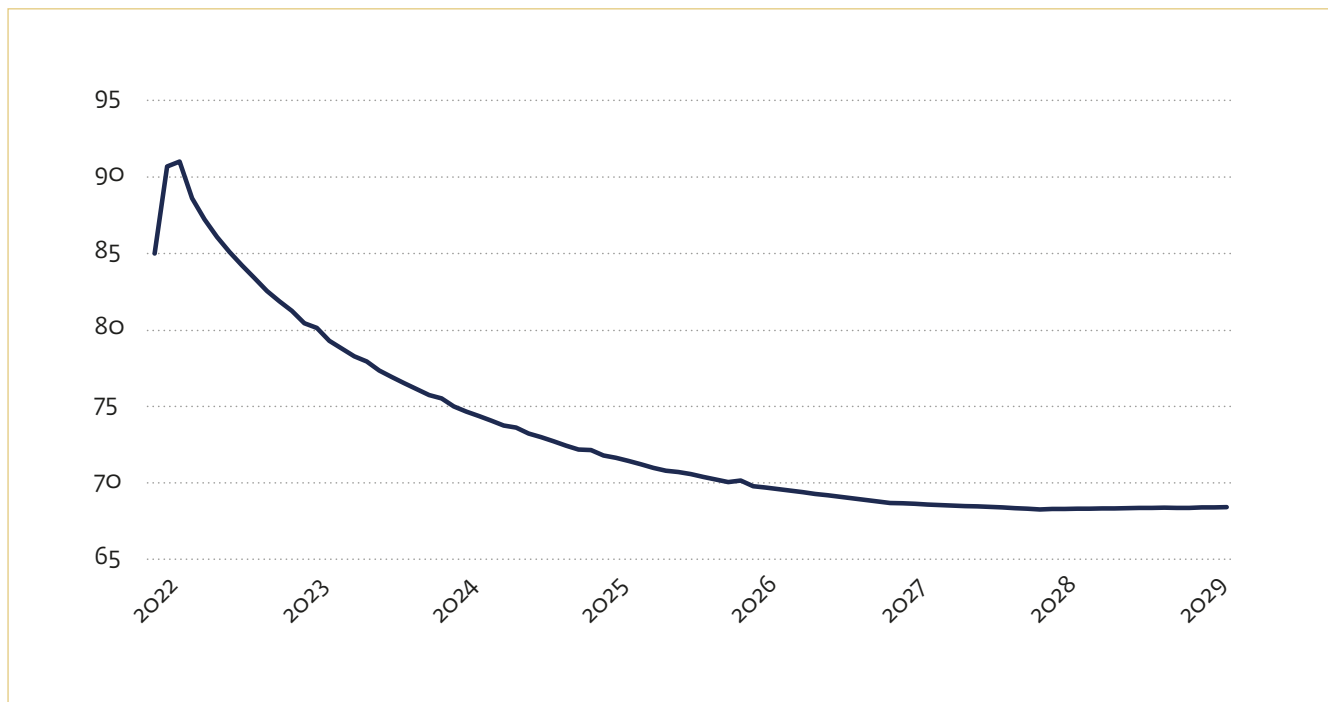
IRAQ'S ECONOMY IN 2022 AND BEYOND

Short-term Growth

The effects of the liquidity injections into the economy over the last two years will likely be amplified in 2022 and 2023 by the upcoming government's policies, which are strongly influenced by robust oil demand—driven by global economic recovery and by the oil market's favorable near-term supply-demand dynamics. This promising backdrop is reflected in long-term futures contracts, which show Brent crude prices above USD \$70 a barrel into 2024, moderating to about USD \$65 a barrel in early 2029 (see Figure 4).

The near-term world economic fundamentals support current expectations (see Figure 4)³⁷ for high oil prices throughout 2022-2023.³⁸ Such prices, following those of 2021, would provide the upcoming government with the revenue wherewithal to continue current expansionary economic policies into 2023, while also allowing for the accumulation of budget surpluses. These dynamics would substantially improve Iraq's balance of payments that would lead to multi-year positive balances in its current account, which would then lead to meaningful increases in foreign reserves. Such budgets would support the current consumer-led economic rebound into more sustainable economic growth, as long as oil prices are high.

Figure 4: Forward Brent Contracts \$/bbl Jan 2022 - Mar 2029



Source: Investing.com, data as of January 7, 2022. Available at: <https://www.investing.com/commodities/brent-oil-contracts>.

37 "Global Growth to Slow through 2023, Adding to Risk of 'Hard Landing' in Developing Economies," Press Release, Washington, DC: World Bank, January 11, 2022. <https://www.worldbank.org/en/news/press-release/2022/01/11/global-recovery-economics-debt-commodity-inequality>

38 "OIES Oil Monthly: Short-Term Outlook," Oxford Institute for Energy Studies, no. 10 (December 8, 2021). <https://www.oxfordenergy.org/publications/oies-oil-monthly-issue-10/>

Political Obstacles to Reform

Nevertheless, such an approach to the annual budgets would deepen the country's structural imbalances and make it more vulnerable to future economic shocks.³⁹ The 2020 economic crisis exposed not only the severity of Iraq's vulnerabilities, but also the advanced stages of its economic structural imbalances. Drastic measures were necessary to stave off collapse. The "White Paper for Economic Reform: Vision and Key Objectives"⁴⁰ – in a first for any Iraqi government – identified the causes of these structural imbalances, and the umbilical cord that ties them to the country's post-2003 political establishment. However, herein lies the weakness of the White Paper or any other substantial economic policy reform effort: the country's cohort of political elites is more influential over parliament and government ministries than are the formal authorities (i.e., the Prime Minister) and these elites fiercely resisted and hindered the implementation of the White Paper throughout 2021.⁴¹

Iraq's Next Government: The Catch-22 of Oil Price Recovery

The recovery of oil prices (in a replay of all such prior recoveries) is reducing the sense of urgency for such reform. The upcoming government will be saddled with similar contradictions and tenuous compromises that bedeviled the 2018-2021 governments. In pursuing expansionary policies, the government ushered into power in 2018, helped by high oil prices, reversed the economic reforms implemented under the 2016 IMF Stand-By Arrangement, thereby exacerbating the country's vulnerabilities to the economic shocks of 2020. Aware of the dangers of a similar fate in a similar high oil price environment, the White Paper's authors followed up with the "White Paper for Economic Reform Volume II"⁴² which included a governance structure for implementation of reform measures. The months following the formation of the upcoming government will test the robustness of this structure – whether it can implement reform, or whether it will become yet another reform package quickly forgotten once the economic crisis passes.

The debate on the White Papers may continue for years to come, with urgency waxing and waning inversely with oil prices. The dilemma for Iraq is that while interest in economic reform gains traction when oil prices are low, implementing lasting and meaningful reforms in such periods is difficult because the government must expend all of its resources on staving off short-term financial collapse. Impetus for economic reform is soon forgotten once oil prices recover, but this is precisely when the government should leverage stability and budgetary flexibility towards passing reforms that can stand the test of time, and crucially, endure the inevitable oil price volatility on the horizon.

39 Ahmed Tabaqchali, "How Demographics Erode the Patronage Buying Power of Iraq's Muhasasa Ta'ifia," Arab Reform Initiative, July 30, 2020. <https://www.arab-reform.net/publication/how-demographics-erode-the-patronage-buying-power-of-iraqs-muhasasa-taifia>

40 "The White Paper for Economic Reform: Vision and Key Objectives" [Arabic], Emergency Cell for Financial Reform, Government of Iraq, October 22, 2020. <https://gds.gov.iq/ar/iraqs-white-paper-for-economic-reforms-vision-and-key-objectives/>

41 Tabaqchali, Al-Shadeedi, and al-Saffar, "The National Budget."

42 "White Paper for Economic Reform Volume II: Reform and Implementation Plan," Government of Iraq, January 2021. English summary: <https://gds.gov.iq/iraqi-government-to-begin-implementation-phase-of-the-white-paper-for-economic-reform/>. Arabic full document: <https://rnc.gov.iq/assets/ViewerJS/#../pdfs/white-iraq.pdf>

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