ECONOMIC AND FINANCIAL REQUIREMENTS FOR RECONSTRUCTION

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Introduction

In the large grouping of developing countries, few have inexhaustible natural resource endowments like Iraq which has considerable oil reserves.

Although Iraq's oil reached the world market in the first half of the twentieth century, it was not until the second half of that century that oil became the central force in the economic life of the country and its people. In this context one can make the case that oil, or more precisely, the management of oil wealth was responsible in varying degrees for all the major political and economic changes which engulfed Iraq, be it the economic development or the Iraq-Iran war or the invasion of Kuwait and the economic sanctions or the 2003 US-led invasion of the country.

In the first part of the paper a summary review will be made of the forces which transformed Iraq from a relatively prosperous country to a country with a failed economy, struggling to regain its recent past. The second part of this paper will be devoted to the analysis of the difficult options facing economic policymakers as they attempt, in the aftermath of the 2003 war, to guide the economy along the path of reconstruction and development.

Oil and the State in the Recent Past

In Iraq, oil and all other sub-soil minerals belong to the people of Iraq. This means that the state is called upon to obtain, on behalf of the people, the maximum possible benefits through the exploitation of this natural resource. The nature of Iraq's political system and the fact that Iraq was ill-equipped to develop its oil reserves paved the way to a consortium of multinational oil companies which were given a long-term concession to develop the country's oil reserves. Under these arrangements and for a good part of the last century, the government was a passive recipient of a fixed sum of revenue obtained per barrel of oil produced.

The second half of the last century, especially the decade of the 1970s, brought about fundamental changes in the oil industry, including a significant increase in the share of the government in the economic rent from oil, the nationalization of the oil industry, the OPEC-led increases in the price of crude oil and the transformation of the Iraqi economy to an oil-dependent economy. The first-stage increase in oil revenue, from a mere $20 million in 1950 to $521 million in 1970, was brought about by changing the fiscal terms in favor of oil producing countries. This change prompted the government to utilize the revenue to build a modern infrastructure and improve the performance of other sectors of the economy. Towards this end a development board was created which was tasked to see to it that the oil income was spent according to a series of development plans intended to spur growth and diversify the economy.

As the revenue from oil continued to rise in the decades of the 1960s and the 1970s and as political changes brought new leaderships from the middle classes, the role of oil in government finance continued to rise. This phenomenon was accentuated by the desire on the part of the new leaders to expand the military on the one hand and to fund social programs especially in the ever-growing urban centers on the other.

The decade of the 70s witnessed major qualitative and quantitative changes in the oil sector and the relationship of the government to it. The first major change was the success of the government in nationalizing the oil sector in 1972 thus completing the initial steps taken in 1961. This nationalization which gave the government the full amount of the oil rent was followed by the 1973/74 OPEC-led price increases. Suffice it to say that Iraq's income from oil jumped twenty-six fold from $1 billion in 1971 to $26 billion in 1980.

The state under the leadership of the ruling Baath party, which came to power in 1968, was quick to utilize the windfall in many directions and at many levels. In the first place the state no