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February 4, 2021

**Statement by Ms. Shortino and Ms. Senich on Iraq
(Preliminary)
Executive Board Meeting
February 8, 2021**

We thank staff for the thorough reports and thank Mr. Mohieldin, Mr. Alhosani, and Ms. Choueiri for their helpful Buff statement. Staff's assessment of Iraq's economy is sobering, and we agree with their analysis of the massive and urgent challenges facing the country. The shock of a sharp fall in oil prices added to the COVID-19 pandemic has amplified the domestic budget imbalances and exacerbated the struggles of the most vulnerable. While we welcome the sweeping vision and ambition of the White Paper, delivering on these reforms seems a daunting task, particularly in the current environment.

For many years staff have rightly pointed out that civil service and pension reforms have been among the most pressing issues that the authorities need to address. We regret that spending on these sectors have assumed an even larger share of fiscal space during the past year, even as the fiscal response to sectors most affected by the crisis has been weak. There remains an urgent need to improve the execution of healthcare spending—without such improvements the health crisis is likely to enter a new wave before vaccinations are widely distributed. We were also disappointed to see a large increase in arrears in 2020. We strongly concur with staff that the distributional impact of fiscal policy should be recalibrated to focus more on protecting the vulnerable, and we welcome the authorities' plans as outlined in the Buff statement. Staff's baseline projections that nominal expenditures will be held roughly constant while non-oil revenues rise over the next six years are based on implementation of White Paper reforms. *Given that the 2021 budget has yet to be passed by Parliament and the ever-looming threat of political instability, could staff elaborate on the realism of achieving the measures needed to reach the baseline scenario?*

We welcome the authorities' decisive action on the exchange rate, which should help to address overvaluation of the dinar and narrow the large spread between the official and parallel exchanges rates. *What is staff's view of the impact of devaluation on inflation and*

how this will affect vulnerable households? Staff project an annual drawdown of international reserves to finance a persistent balance of payments deficit. Staff also expect the Central Bank of Iraq to indirectly finance most of the fiscal deficit each year. *Do staff see the reserve stock, and by extension the new currency peg, as sustainable in the long-term under the planned reform measures?*

In addition to civil service wage reform and pension reform which are paramount, we concur with staff's emphasis on the importance of reforms to the financial sector, such as restructuring of state-owned banks and improving the AML/CFT framework. We also agree with staff's emphasis on reform to public financial management and in the electricity sector. Many of these have been on the agenda for years or even decades. We urge the authorities to ready concrete short- to medium-term reform plans on these items as the pandemic subsides, and we agree with staff that the durability of these reforms would be helped by embedding key fiscal measures in permanent legislation.

We note that from the Buff statement that the authorities have requested emergency financing under the Rapid Financing Instrument and have expressed interest in a follow-up Extended Fund Facility. We urge the authorities to continue discussions with staff on these instruments and confirm their willingness to undertake the strong adjustments needed to address the root causes of the imbalances. Finally, we encourage the authorities to consent to the publication of the report and wish the authorities success in their endeavors.