

BUFF/08/187

December 18, 2008

**The Acting Chair's Summing Up
Iraq—Second Review Under the Stand-By Arrangement and
Financing Assurances Review
Executive Board Meeting 08/111
December 17, 2008**

Executive Directors commended the Iraqi authorities for the considerable progress achieved in implementing their economic program in an improved, but still fragile, security and political environment. With this improvement, oil production and exports have increased, and non-oil activity has started to recover. Directors welcomed the subdued inflation in 2008 and stressed the need to maintain macroeconomic stability, while speeding up the pace of implementation of key structural reforms.

Directors welcomed the authorities' commitment to rebuild the economy and preserve fiscal sustainability over the medium term. These objectives have become more challenging in light of the recent sharp fall in oil prices and the expected decrease in oil export revenues. In this context, Directors supported the scaling back of initial budget spending plans for 2009. Noting the currently lower oil prices than assumed in the draft 2009 budget submitted to Parliament and the projected substantial fiscal deficit, Directors welcomed the authorities' announced early consideration of additional measures to further cut nonpriority spending. In particular, they stressed the need to contain current outlays, especially the wage bill and transfers, while allowing for adequate investment and security spending. The authorities should also finalize the census of public service employees in the near future and streamline the costly and untargeted in-kind Public Distribution System.

Directors noted the reasons for the authorities' decision to delay fuel price increases. Nonetheless, most Directors considered that the authorities should press ahead with their efforts to develop a fuel price adjustment mechanism, aimed at creating a transparent framework for future fuel price adjustments that could further reduce indirect fuel subsidies and free resources for economic reconstruction.

Directors concurred with the central bank's intention to maintain a tight monetary policy stance and continue to manage the exchange rate in order to bring core inflation down to single-digit levels. It remains important to keep the central bank's policy interest rate positive in real terms. In this context, Directors emphasized the importance of implementing the planned improvements in the CPI.

While welcoming the adoption of a comprehensive action plan to modernize public financial management, Directors underscored the need to accelerate the pace of structural reform in other key areas. They highlighted the importance of adopting comprehensive restructuring programs for Rafidain and Rasheed banks, based on their financial and operational audits; completing the set of prudential regulations for commercial banks; and continuing the implementation of the recommendations of the IMF Safeguards Assessment Report.

Directors urged the authorities to continue their efforts to strengthen governance and fight corruption, in particular in the hydrocarbon sector. They stressed the need to continue the extension of metering systems to all oil sector activities. The full implementation of the procedures under the Extractive Industries Transparency Initiative and the establishment of a new legislative framework for the hydrocarbon sector will also be essential.

Directors welcomed the authorities' efforts to conclude debt agreements with official and private creditors. They encouraged the authorities and those non-Paris Club creditors yet to provide debt relief to expeditiously conclude agreements on terms comparable to those of the 2004 Paris Club Agreement.