

# Reflection of Economic Shocks on the Diversification of Income Sources in Iraq

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## Abstract

Iraq's dependence on the commodity and its revenues as a major commodity to finance its operational and investment programs has made its economy vulnerable to the impact of fluctuations or shocks in the world oil markets, whether positive or negative. The global financial crisis caused the oil prices, which recorded a significant decline either by the volume of aggregate demand, or the decline in global prices of the commodity, where the unexpected decline from about 140 dollars / barrel to about \$ 40 / barrel, which affected the economy Iraq, which depends on the commodity extraction and export of crude oil to finance its development programs, what the management of its leadership and its policy of water resources to be ambitious. This research analyzes the financial and economic situation of the decline in oil revenues and its relationship to the relevant economic variables within a special perspective of the Iraqi situation and the options open to them to deal efficiently with the crisis and reduce the negative consequences.

**Keywords:** economic shocks, rent economy, economic inflation, oil prices, diversification of income sources.

## Introduction

The political change in Iraq in April 2003 is the turning point of the economy built on the system towards the economy based on the principle of decentralized system, in other words, the restructuring of the economy on the basis of market mechanisms, and thus increased structural imbalances and reflected on all economic variables, the Iraqi economy suffers from imbalance in The structure of government spending, as the state treasury is distributed spontaneously for each item of the budget, that is, not to adopt a scientific strategy is calculated to divide the budget items, as the operating expenses get a large area of these allocations (Hassan, 2010, p. 27), which led to the destruction of infrastructure and economic establishment and vital facilities, and increased distortions and imbalances significantly in the economy, the most prominent of which are institutional imbalances in the management of the national economy, and imbalance in the structure of production and imbalance in the structure of the budget, And external indebtedness (Shatha and Najm, 2015, p. 11), and these imbalances constituted an obstacle to development and economic reform, and the most important of those obstacles that hindered the Iraqi economic development after 2003 (Al-Attayah, 2012, p. 359).

The impact of the oil shock in the macroeconomic variables in two directions, when the shock towards the rise in world prices, will work that the rise in oil prices globally, which is the result of high oil revenues at the beginning of last year 2008, the economies of the oil countries, including Iraq in the problems or fundamental variables

## Research Importance

The importance of the research is reflected in the impact of the shock of the decline in oil prices on the economic development process. The reliance on the depleted resources, which can lead to financial surpluses capable of achieving huge capital accumulation, if the prices fall in the world market will be reflected on indicators of economic growth.

## Search Goal

Measuring the impact of the economic shocks faced by the Iraqi economy due to the decline in oil prices in the global market on the importance of diversification of sources of income.

## Research problem

Embodied the research problem in the absence of an effective oil policy in the field of production and export, and the lack of oil infrastructure development, making the Iraqi oil industry teetering under the weight of prices, Iraq's oil has not invested in serving development processes and economic growth due to the global market dominance of prices and the lack of oil companies high technology in the production and export capable of upgrading the oil industry into the ranks of developed countries, as well as a lack of oil policies in the development of this resource optimally, not to mention terrorist operations that target refineries and pipelines has continuously causing a Z to disrupt the production and sustainability of export.

## Search Hypothesis

The research is based on the premise that achieving sustainable growth in Iraq is directly linked to the balanced

growth of the oil sector and other sectors of the economic structure )

### **The first axis: the economic shocks that faced the Iraqi economy**

In 2009, the Iraqi economy faced negative effects due to the low contribution of the crude oil sector to the GDP of the public sector (63.7%). In addition, the financial turmoil in the international financial markets has had a negative impact on the economic development in Iraq during 2009 (Ministry of Planning, The economic instability of 2010-2013 continued to rise and fall, affected by the fluctuations in oil prices, which led to imbalances of economic stability due to the failure of balanced economic growth of all sectors in the country, And the neglect of the rest of the economic sectors.

As for 2014, there have been significant developments in the Iraqi arena and global In the Iraqi arena increased security tension, which led to the displacement of thousands of people, leaving a heavy burden on the financial resources of the state.

As for the global development, there was a sudden drop in world oil prices to reach (60) dollars a barrel after it was more than (\$ 100) a barrel, so the rate of growth in GDP to reach (- 3.9), and the impact of government on activity Economic decline during 2014 because the Iraqi economy can not exploit resources well

In general, the Iraqi economy has passed since the beginning of the occupation in 2003 the most serious economic crisis and its future is threatened so that (80%) of the federal budget goes to the operational expenses of salaries and wages and pension system (pensions) and other expenses to meet the requirements of state institutions, in return for the allocation of (20%) of The budget for investment expenditures and even this amount will not be available because of the country's need for large amounts to buy weapons and military supplies to counter the threat of terrorism.

### **The second: the role of government spending in controlling the inflation of the Iraqi economy**

There is a strong correlation between the changes in inflation rates and the stability of the economic environment, and Iraq has witnessed severe fluctuations in inflation rates after 2003 when it moved towards the market economy, which led to increased inflation due to structural imbalances suffered by the lack of serious implementation of programs and economic and investment plans and the failure Implementation of the economic development plan for years -2010 and lack of mobilization for the implementation of the development plan for the years 2010-2014 (David, 2012, p. 280), and the performance of fiscal policy dominated the performance of macroeconomic policy, including on the face of monetary policy specifically, which was keep pace with the requirements of the funding policy deficit in the general budget through the mechanism of linkage between monetary expansion and finance its deficit, which resulted in that policy accumulated enormous treasury transfers - represent the basis of the internal public debt - to rise to 5.5 trillion dinars until the year 2003. to become a source of expansion of monetary and release (al-Shara, 2014, p. 5), but I got developments positive price reflects the relative decline in the direction of the phenomenon Altd Scientific and moderation in relative prices during the period 2003-2006 in which inflation was almost 37% per annum (Saleh, 2006, p. 1), so note that inflation in the Iraqi economy during the years leading up to the 2008 function of the state of security and the concomitant scarcity of private fuel, petroleum products and commodity supply, since the beginning of the occupation of oil prices played a key role in the escalation of inflation until 2007 (on Ibrahim and 2015, p. 173)

t attributed the upward trend in inflation is also attributed to the rise of consumer nature of government expenditures, as well as increasing salaries and wages, which means that the total demand of total spending pressures contributed significantly to maximize the risk of inflation (Chaoui, 2013, p. 42), Valastrashad fiscal and monetary policy by the government at the same time making inflation rates in the decline during the period 2008-2010, regardless of the expansion of continuous economic growth, but it returned to witness a rise in inflation after the year 2010, recorded inflation rate (5.6%) in 2011 and ( 6.1%) in 2012, attributed the reasons for the increase to the spending Kumi operational and investment, both, and can clarify the inflation rates of the Iraqi economy during the period (2004- 2014)

Table (1) Inflation in the Iraqi economy for the years 2004-2014

Annual inflation rate%	years
27.0	2004
37.0	2005
53.2	2006
30.8	2007
2.7	2008
(2.8)	2009
2.5	2010
5.6	2011
6.1	2012
1.9	2013
1.4	2015

Source:

1- Ministry of Planning, Central Statistical Organization, Statistical Group for the years 2012-2013

2. The Central Bank of Iraq, annual publications for the years (2004-2015)

inflation rates accelerated during the period 2004-2007 until the average rate (37.0%). The trends in inflation in Iraq were characterized by an escalation, especially at the beginning of the occupation due to high oil revenues and increasing volume of current operating expenses. In Iraq, which provides the opportunity for the Central Bank of the operations of the open market to pump more dollars to reduce the general level of prices and vice versa, which made the inflation rates fluctuated and decreased after 2007

Therefore, the strenuous efforts must be borne by the Iraqi economy to correct the structure of production and move towards abandoning the rent situation, as this requires achieving the efficiency of investment medium, which makes the ratio of capital to marginal output (3%), and the ratio of capital formation to GDP (27%). The perception is accompanied by the prospect of no balance of payments constraints on development and economic stability in Iraq (Radhi and Hasan, 2013, p. 186)

### The third: the stages experienced by the Iraqi economy

The first phase: the period (2004-2006):

This period witnessed a remarkable growth in GDP, with an average rate of 22.9% during this period. This indicates the recovery of the Iraqi economy as a result of political change and the opening of the Iraqi economy to the outside world, as well as the government's adjustment of the salary scale, creating a high demand for consumer spending contributed to the revitalization of all economic sectors

This is due to the openness of the Iraqi economy to the outside world and the flow of various consumer goods, which was reflected in the market demand increase after depriving the Iraqi markets of these resources for a period of time. And the lack of material possibility of the Iraqi citizen because of the imposition of the blockade, which affected the economic situation of the country and then on the level of the individual.

As for the unemployment index, it appears to have taken a high average (20.7) ladder, as noted earlier, due to the demobilization of large numbers of armed forces as well as the dissolution of military manufacturing establishments and other factories. This is due to the lack of flow of oil exports very effectively due to the existence of some gaps and obstacles in the oil fields, as it has not been maintained and developed long ago because of the economic blockade and the inability to export oil, which reflected The balance of trade in Iraq

Therefore, we can conclude that the period 2004-2006 does not enjoy the relative stability of the economy according to the box like the magic circle with the exception of economic growth index, which is one of the best periods of economic growth over the past three decades, and note the other indicators that they are not good for the Iraqi economy because their rates will not Serves the economy

The second phase: the period from (2007-2009)

This period witnessed a slower growth in GDP than in the previous period, with an average of 4.6. This indicates a decline in the growth rates of the Iraqi economy as a result of what is happening to the global economy from the recession of a large economy in 2008 on the one hand, on the other hand, the security tension has reached a peak during this period and thus reflected negatively on the rates of economic growth in Iraq, Price levels (inflation rates) declined during this period until the average rate (11.2) compared to the period (2004-2006), And this is due to the stability of the Iraqi dinar exchange rate as a result of the increase in public revenues due to the recovery of the oil market, and the central bank's auctions to support this dinar on the one hand, and the diversification of sources of imports to the degree of market obscurity on the other hand. The unemployment rate has also fallen, despite the absorption of a significant portion of underemployment through government institutions.

With regard to the balance of payments has tended to a positive direction and this is due to the increase in the flow of oil exports profusely to the outside world after rising prices.

### Phase III: Duration (2010-2014)

The Iraqi economy during this period was characterized by relative stability of most indicators except for the unemployment rate, which is still high due to the government's lack of seriousness in eliminating or reducing unemployment. The security sector has the lion's share in absorbing these large numbers of the unemployed army. This sector has not been able to provide serious and radical solutions to address the unemployment crisis. It is noted that the price levels (inflation rates) during this period were characterized by a kind of stability despite a slight increase during the years 2011 and 2012. This relative stability in price levels is due to the full opening of the Iraqi economy to the outside world and the flow of various consumer goods at competitive prices, as well as the government's control of monetary supply and curb inflation. The deficit in the capital and financial account, especially during the years 2013 and 2014, had a negative effect on the balance of payments situation until it reached an average of 4.4,

### Fourth: Diversification and sustainability of sources of income

The oil resource is a major source of revenues of the federal budget and then covering public expenditure, which is one of the priorities of the financial policy of any country no matter how different the economic system applied to it, whether it is a developing or advanced country, as a direct relationship between fiscal policy and government spending in terms of the latter's reliance on revenues. The general budget, which consists of oil and non-oil revenues. Although Iraq has not been developing and diversifying its revenues as effectively as in developed countries, taxes are the main revenue in their economies. However, this does not mean emptying the structure of the Iraqi budget from the non-oil supplier at a time dominated by the oil and mining sector (90%)

Of government revenues, and to simplify the presentation of revenue components during the period of study requires the convergence of doors converge to facilitate the process of discrimination to the composition of public revenue, and on this basis must be based on the nature of these sources and relying on the Iraqi economy through the following

### First: Oil revenues

Iraq is one of the oil countries that occupy an advanced position between the Arab and world oil producing countries to the size of its reserves as well as one of the founding members of OPEC and the following table shows the location of Iraq globally for the oil reserves issued by the British Petroleum for the global energy in 2011. (Report of the Iraqi Ministry of Finance , 2009, p. 5).

The secret of Iraq's dependence on the oil resource as a major source in the revenue structure of the public budget is due to the availability of this resource in large quantity as well as lower cost of extraction compared to other oil countries such as the United States of America, for example. This is reflected in the increase in oil revenues compared to the revenues of other resources

Therefore, the Iraqi economy relied on crude oil, especially in the early years of the new millennium and specifically after 2003, the prices rose year after year until the oil revenues in 2007 (33.5) billion dollars, which accounted for (88%) of budget revenues after it was disappointing. To the hopes and does not commensurate with the size of the reserves possessed by the Iraqi economy and surrounded by challenges, while explaining the large increase of the budget in 2008 because of high oil prices in international markets. It was supposed to double the budget figures to (80) billion dollars for the year 2009. However, the unexpected collapse of the oil prices caused the determination of (59) billion dollars, and continued impact of volatility in oil prices on the federal budget for 2010, decreased to (52) billion dollars, while the figures for 2011 to (69) billion dollars after the rise. Relative to global oil prices. The following table shows the volume of production, export and financial revenues during the period (2004-2014)

Table (2) Production, export and returns of crude oil sources during the period 2004-2014

Ratio of oil revenues from total revenues%	public revenues Million ID	annual percentage increase%	oil revenues (million dinars)(	value of exports Billion dollars	Quantity of exports Million barrels per day	<b>Oil production</b>	years
99.1	32988850	-	32687839	17.751	1,4	2,107	2004
98.5	40435740	22.0	39880890	21.480	1,4	1,912	2005
94.9	49055545	16.7	46534310	30.465	1,4	1,663	2006
97.6	54964850	14.5	53306884	39.433	1,6	1,851	2007
98.6	80641041	48.4	79131752	56.843	1,8	2,428	2008
93.7	55243526	-34.6	51719059	39.307	1,9	2,442	2009
95.2	70178223	29.2	66819670	51.589	1,8	2,340	2010
94.3	103989089	46.8	98090000	79.043	2,1	2,668	2011
96.9	119817224	18.4	116160781	94.103	2,4	2,928	2012
96.3	113840076	-5.6	109650692	89.402	2,3	3,280	2013
92.1	105386623.1	-11.5	97072409	84.333	2,1	3,100	2014

The bulk of oil produced by Iraq is exported. Crude oil revenues accounted for 98% of Iraq's total export revenues. Exports of oil increased since 2004, rising to 17.75 billion dollars, or 99.1% The total revenue to reach (30.465) billion dollars in 2006, and continued to increase until 2008 and then declined in 2009 The decline in export revenues due to the reflection of the impact of the global financial crisis on prices and global demand for crude oil, thus reducing the revenues of oil exports to (39,307) billion dollars after it was (56,843) billion dollars in 2008, then continued increase in the revenues of oil exports, In the field of oil and energy that the period from 2011 until the beginning of 2014 2014 is a golden period for the world oil markets in terms of demand and price for this resource. This has been reflected in the Iraqi economy in terms of economic prosperity, which the government has not been able to invest enough efficiently in its financial policy. The average export revenues reached 87.516 billion dollars, In the year 2012, which reached the export revenues to (94.103) billion dollars, which is the highest level reached by oil export revenues since the year (1970), the beginning of the date of export of oil by the Iraqi government (Majid, 2009, p. 51).

That oil has shifted from a strategic commodity to finance budget revenues to a commodity does not serve the economy as required after 2013 as a result of the loss of its price by more than 70% of the world price to reach (60) dollars by the end of 2014 after the price of more than \$ 100 before In 2014, and thus did not achieve adequate returns to achieve export revenues during the period 2011-2013

Despite this, the increase in oil revenues is not an indicator of the improvement in levels of production and exports, but due to the significant rise in oil prices in the global market, hardly less than the amount of public revenues, and this is evidence that the Iraqi economy relied entirely on this This is the best proof of the Iraqi economy and this type of economy is more vulnerable to economic fluctuations once there is any negative change in oil revenues (Ministry of Finance, 2009, p. 11).

#### **A. Conclusions**

1. The hypothesis of research has been proven and we have reached the conclusion that there is an increase in the financial burden of the government in a way that exceeds the capacity of the Iraqi economy throughout the years of study, and the adoption of an appropriate strategy of financial policy by the government contribute to the revitalization and diversification of the economy by making it more able to absorb the financial burden, Achieving high growth rates for public revenues.
2. The post-occupation Iraq's fiscal policy did not have an important place in contemporary economic policy as a result of political interference in economic activity and the absence of a clear vision for successive governments on the country's financial and economic situation.
- 3 - Increasing the financial burden of the government during the period of study 2004-2014, which increased the value of the deficit in the general budget of the Iraqi government, as a result of the increase in the amount of government spending ongoing ongoing.
- 4 - instability of fiscal policy trends after 2003, as well as the absence of a clear government program that diversifies and sustains the sources of public revenues, increasing the correlation between fiscal policy and the oil resource, which caused serious problems of fiscal policy supported by improper direction of resources available through different channels of the Convention.
- 5 - Despite the existence of the capacity and adequacy of the financial policy through its tools, especially rent income to bear the financial burden of the government, but the existence of a state of confusion and lack of clarity to see the fiscal policy followed in Iraq and inaccuracy led to the failure of financial policy to overcome the financial situation previously
- 6- There is no future planning to control the financial burdens that the government may face in the future.
- 7 - The imposition of a new economic system after the occupation, under which the priority was given to preference for consumer welfare as an initial preference for growth and stability, and second preference for social and economic reasons stemming from the suffering of Iraqi society during the decades of deprivation, which reflected the volume of government spending by increasing employment and grants And tax cuts.
8. The public budget in Iraq has achieved a financial surplus for most of the study years. In other words, the financial situation in Iraq is relatively stable in theory, despite the existence of financial gaps and obstacles to the government in practice. Hence, the government budget is unable to cover the financial barriers. Effectiveness of fiscal policy as a result of the dominance of financial corruption and administrative bureaucracy over all economic sectors.

#### **B- Recommendations**

- 1- Building a strategy based on diversification of the economy, in order to ensure reliance on various financing tools that devote total non-reliance on oil revenues in order to avoid fluctuations in oil markets.
- 2 - Attempt to benefit from international expertise and experience in the field of public money management, which contributes to cover the large financial burdens that may be borne by the government.
- 3 - the need to rationalize public expenditure in accordance with a correct mechanism and strict control to ensure

the abolition of all public expenditures and the appearance of non-essential that are not related to the process of production.

4 - The government in preparing public budgets should note that the definition of public expenditures must be made in the light of the possibility of the country and its ability to finance these expenditures appropriately and in accordance with the possibility of the national economy and not rely too much on its sovereign capacity to collect the resources necessary to cover this financial burden Government.

5 - activating the control of public money through the establishment of strong and independent institutions supported by the three presidencies in order to fight corruption of all kinds of favoritism and Mnsobih, in order to be helpful to the austerity and excessive waste without justification.

7 - To find the appropriate conditions to attract foreign direct investment to the countries of research in general and Iraq in particular, through the creation of the necessary infrastructure, as well as directing this investment in the right manner through the structure of exemptions and tax niches to be a guide for investors to move towards targeted investments and contribute effectively to Diversifying the national economy.

8 - Attempt to reduce unnecessary expenses (expenses of depositions to officials, expenses of Hajj and Umrah, the expenses of the three presidencies, the expenses of government departments unproductive, and military expenditures and other expenses and excessive unexplained).

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