

Iraq Business Forecast Report Q1 2015

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Abstracts

Core Views

Risks of a return to full-blown civil war are elevated following the takeover of jihadist group Islamic State (IS) of the country's north and west.

Robust headline growth of the Iraqi economy in 2014 and 2015 will result from accelerating oil exports. Conversely, domestic expansion will be sluggish and uneven; consumer spending and capital formation will be hit hard by political instability, and declining oil prices will hinder the government's ability to prop up spending.

Major Forecast Changes

Iraq's current account surplus will narrow significantly in 2015 as declining oil prices will hit the value of hydrocarbons exports. We forecast Iraq's current account to come in surplus of 6.5% of GDP in 2015, from our previous forecast of 10.0% of GDP and compared to surplus of 10.7% of GDP in 2014.

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New Government Short Of A Game Changer

The formation of a new Iraqi government will lower risks of a collapse of central authority, and we have increased the country's Short-Term Political Risk score as a result. However, the cabinet will fail to win trust from the Sunni minority, and jihadist group Islamic State will remain a resilient fighting force. Although relations with the Kurds will improve, risks that Erbil will push for full independence over the coming years remain salient.

Table: Political Overview

Long-Term Political Outlook

Rising Risk Of State Collapse - Scenarios Assessed

Iraq will maintain formal unity within a more fragile federalised state over the coming decade, but risks that the country will return to full-blown sectarian civil war are high. The situation in Iraq and in neighbouring Syria will remain the major risk to systemic stability in the Middle East over the coming years.

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Robust headline growth of the Iraqi economy in 2014 and 2015 will result from accelerating oil exports. Domestic expansion will be sluggish and uneven; consumer spending and capital formation will be hit hard by political instability, and declining oil prices will hinder the government's ability to prop up spending. Decelerating exports, the result of a lack of investment as oil prices decline, will result in declining GDP growth

from 2016 onwards.

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Fiscal Policy

Resolution In Sight For Baghdad-Erbil Salary Payments Row

The resolution of a dispute between Baghdad and Erbil on salary payments for Kurdistan public employees will lead to the approval of the 2015 budget. Iraq's fiscal surplus will narrow over the next five years as declining oil export growth hits government revenues.

Table: Fiscal Policy

Monetary Policy

Inflation To Accelerate In 2015

Consumer inflation in Iraq will accelerate gradually over 2015 in areas under central government control, and spike dramatically in regions under the control of jihadist group Islamic State. We project CPI inflation in areas governed by Baghdad to average 3.5% in 2014 and 4.5% in 2015, compared to 1.8% in 2013.

Table: Monetary Policy

Balance Of Payment

External Position Worsening As Oil Prices Decline

Iraq's current account surplus will narrow significantly from 2015 onwards, as oil prices are weak and crude production growth slows. Foreign direct investment inflows will also fall sharply, as the challenging operational environment and elevated political risks hinder confidence. Low oil prices will hit FDI in the oil sector, particularly in southern Iraq.

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Iraq's potential as a regional economic outperformer has faded as a result of elevated political instability, and we project real GDP expanding by a yearly average of 4.3% over the 2014-2023 period. The oil and gas sector will be the lifeblood of the economy over this timeframe despite declining oil prices.

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