Directorate of
Intelligence

~~Secret~~

[redacted] 25X1

Iraq: An Economy Under Siege [redacted]

25X1

An Intelligence Assessment

~~Secret~~

NESA 84-10027
January 1984

Copy 400

Page Denied

Directorate of Intelligence

Secret [redacted] 25X1

Iraq: An Economy Under Siege [redacted]

25X1

An Intelligence Assessment

This assessment was prepared by [redacted] 25X1
Office of Near Eastern and South Asian Analysis,
with contributions from [redacted] 25X1
[redacted] Office of Global Issues. It was coordinated with 25X1
the Directorate of Operations. Comments and
queries are welcome and may be directed to the Chief,
Persian Gulf Division, NESA, [redacted] 25X1

Secret
NESA 84-10027
January 1984

[redacted] 25X1

Iraq: An Economy Under Siege [redacted] 25X1

Key Judgments

Information available as of 3 January 1984 was used in this report.

Iraq is trapped in a costly war of attrition that is strangling its economy. On the threshold of an oil-driven economic takeoff before it embarked on its war with Iran, Baghdad has seen its oil earnings and foreign exchange reserves plummet. The regime has slashed imports, virtually abandoned its development program, and even terminated combat pay. It now depends on foreign aid and credits to stay afloat financially. Economic problems combined with growing casualties and a relentless enemy are increasingly pressing President Saddam Husayn to escalate the war. [redacted] 25X1

The austerity program has created potential political problems for Saddam. Shortages of consumer goods are becoming more widespread and are fostering hoarding and black-marketeering. They have contributed to an annual inflation rate of perhaps 50 percent. Along with cuts in imports, other unpopular measures include increased taxes, gasoline rationing, and a campaign to collect gold from the citizenry. [redacted] 25X1

The populace seems resigned to the economic situation for now, and we believe the Gulf states and Western creditors will help enough to allow Iraq to meet basic import needs in 1984. If, however, they are not as generous as in 1983, imports will have to be reduced further, increasing consumer dissatisfaction. [redacted] 25X1

Iraq's prospects for increasing revenues by opening new oil outlets within the next year are remote. The only positive development will be a 300,000-barrel-per-day increase in the capacity of the Turkish pipeline expected to be ready by April. [redacted] 25X1

Athough Baghdad has extracted an agreement from Riyadh to build a spur linking Iraqi oilfields to the Saudi pipeline to the Red Sea, the Saudis still may delay construction. We believe Saudi Arabia is reluctant to commit itself to a long-term involvement with Iraq. Even if the Saudis permit construction to begin soon, the pipeline would not be ready before 1985. If such a pipeline is completed, however, the Iraqi economy would improve markedly. [redacted] 25X1

Several Gulf states have approached Syria to reopen the pipeline from Iraq through Syria to the Mediterranean, but discussions with Damascus are at a standstill. The proposed Jordanian pipeline is unlikely to be completed before the end of 1985 even if construction begins early this year. [redacted] 25X1

 25X1

Economic difficulties will not be enough to topple Saddam. If necessary, he will resort to repressive measures to maintain control over the population. The more immediate threat to Saddam is a breakdown in the military situation. [redacted] 25X1

Iraq's economic problems probably will impel it to improve relations with the United States and moderate Arab states. Baghdad might seek military equipment and financial aid as well as US diplomatic efforts on Iraq's behalf. At the same time, Iraq will continue to look to the USSR, especially for military aid. Iraq probably hopes its threats to escalate the war will spur diplomatic efforts to achieve a cease-fire and allow it to resume oil exports through the Gulf. [redacted] 25X1

Iraq: An Economy Under Siege

25X1

Before its war with Iran, Iraq was planning an ambitious development program projected to cost $133 billion for the period 1981-85. High on the list of priorities were housing development, transportation and communications improvements, and modernization of the agricultural sector. Iraqi President Saddam Husayn's economic policy also called for massive welfare spending and a steady flow of consumer goods to help secure his power. The government regularly announced wage increases for state employees to mobilize additional support for the Ba'th Party.

Iraq was able to maintain a business-as-usual attitude through the first year of the war, thanks to oil exports through the Syrian and Turkish pipelines, drawdowns from foreign exchange reserves, and massive Gulf state aid. Imports peaked at $20 billion in 1981.

The economy, however, suffered a marked deterioration in 1982. Damascus closed the Iraqi pipeline across Syria in April, and the flow of Gulf state aid slowed. Moreover, foreign exchange reserves were being depleted. As a result, Saddam imposed spending cuts in the civilian sector. Low-priority development projects were canceled or postponed, and late payments on existing projects became epidemic by the end of the year. Baghdad also restricted sales by state retail stores, introduced new restrictions on the import of luxury goods, and even eliminated some military benefits.

Harder Times at Home

The war affected all areas of economic life in Baghdad in 1983. The development program and consumer activity were particularly hard hit. The Ministry of Finance called for a reduction in spending of 40 percent in the 1983 budget from the previous year's expenditure levels, according to the US Interests Section in Baghdad. 25X1

The government has almost abandoned its economic development program, a sharp reversal from the guns-and-butter approach it maintained during the first year of the war. Baghdad has canceled nearly all new contracts not related to the military effort or the petroleum sector and postponed several nonessential projects already under way, according to the US Interests Section. 25X1 As a result, many projects are standing idle, including housing, hospitals, and irrigation work, according to press reports. Among the few projects where work is continuing are two $1 billion power plants at Al Yusufiyah and the $3.5 billion Baghdad–Umm Qasr railroad. 25X1 In our view, the slowdown or cancellation of most infrastructure development will set back Iraq's plans for rapid industrialization and self-sufficiency by several years.

The Iraqi consumer has increasingly been affected. 25X1 Indeed, the growing preoccupation of society is obtaining scarce goods, according to the Interests Section. Imported staples—especially foods—are more frequently scarce or exorbitantly priced, according to the US Interests Section and press reports. The list of scarce commodities in government shops often includes dairy products, eggs, sugar, cooking oil, and potatoes. 25X1 Widespread shortages also exist for automobile spare parts, cigarettes, and beer. Gasoline queues have cropped up, according to press reports, largely 25X1 because the fuel demands of the military take priority. Gas stations have been guarded by armed soldiers, according to the press, a sign of potential disquiet. Luxury goods are also scarce. 25X1

The shortages have fostered a thriving black market and are fueling an inflation rate we estimate could be as high as 40 to 50 percent annually. With too many dinars chasing too few goods, consumers are briskly bidding up the price of available items. Eggs, for example, cost about $19 a dozen, and mutton, an important meat in the Iraqi diet, brings about $7 per pound, according to the Interests Section [redacted] Many scarce items are available only to those with connections with the Army, the Ba'th Party, or the local shopkeeper, according to the Interests Section. [redacted]

An upswing in hoarding has worsened shortages in the marketplace as consumers respond to an uncertain future for supplies and prices as well as growing rumors of government rationing. Private retailers also have been holding back goods in anticipation of higher prices or to save them for favored customers, according to the Interests Section. Still, although life has become more spartan, the average Iraqi can meet most basic needs. [redacted]

Pent-up frustrations with the war and its impact on the economy occasionally have surfaced. Members of the National Assembly, Saddam's rubberstamp parliament, have criticized exorbitant prices in the private sector, according to the Interests Section. Buyers at a dairy outlet shouted antigovernment chants when the Army took the day's supply of dairy products, according to an unconfirmed report to the Interests Section. So far, however, the decline in the standard of living has not resulted in public resentment that could threaten the regime. [redacted]

Saddam has been quick to purge those in or out of the government who question his domestic policy.[1] He sacked the Minister of Finance, Thamir Razzuki, last August, according to the press. Interests Section sources report that Razzuki disagreed with Saddam's economic policy and had become too independent. [redacted]

Consumer Policies

We believe the regime is attempting to improve the economic situation to quash growing discontent. Saddam's major concern as of November was not the battlefront but the economy, [redacted]

[redacted]

[redacted] Deputy Prime Minister Tariq Aziz has publicly described the conflict with Iran as an economic war of attrition. [redacted]

25X1
25X1

The regime so far has rejected comprehensive rationing. Administering a national rationing scheme efficiently and equitably would overextend a bureaucracy already strained by manpower requirements for the war, in our judgment. Moreover, with most retail distribution in the hands of the private sector, the government probably fears the potential for abuse. [redacted]

25X1
25X1
25X1
25X1

Baghdad, however, has had to restrict the sale of certain commodities. The government began issuing coupons for oil and gas products last October, according to the local press. The government also is restricting electricity use in Baghdad, [redacted] Moreover, the regime is introducing "specialized agencies" to distribute milk products produced by public-sector dairies. Plans call for the creation of over 100 of these outlets, which will be privately owned, according to the Interests Section. [redacted]

25X1
25X1 25X1
25X1

The government is relying on local citizens' organizations to help stem hoarding and at the same time deflect criticism from the regime. Baghdad is using People's Councils—government-created citizens' groups in various urban areas—to monitor private shop deliveries and sales. People's Councils in Baghdad already have distributed goods confiscated from shopkeepers accused of hoarding free to local neighborhoods, according to the Interests Section. Some of the councils also are using identity cards to restrict sales to customers living in their areas. In some rural villages, the local manager of the government store distributes food based on his interpretation of the requirements of the local inhabitants, [redacted] Nonresidents are not allowed to purchase food at the village stores. [redacted]

25X1
25X1
25X1
25X1
25X1

The regime has adopted other measures that almost certainly are testing popular resolve. Baghdad has increased income taxes for wage earners to help finance the war [redacted] Baghdad also has launched a campaign to collect

25X1
25X1
25X1

"voluntary" gold contributions from the citizenry. Popular response has been poorer than anticipated. Teams of Ba'th Party militia representatives have used intimidation during nighttime collection visits, according to the Interests Section.

25X1

Other steps Baghdad has taken highlight the severity of its foreign exchange dilemma. Baghdad has restricted the amounts of foreign exchange its many foreign workers can repatriate as well as jobs they may hold. These controls are hastening the flight of foreign labor, compounding Iraq's chronic shortage of skilled manpower already sapped by the war. Women, largely unskilled, are increasingly used to fill the labor gap. The government also has reduced salaries and benefits of its diplomats and closed several smaller embassies, with a commensurate decline in morale among Foreign Ministry employees.

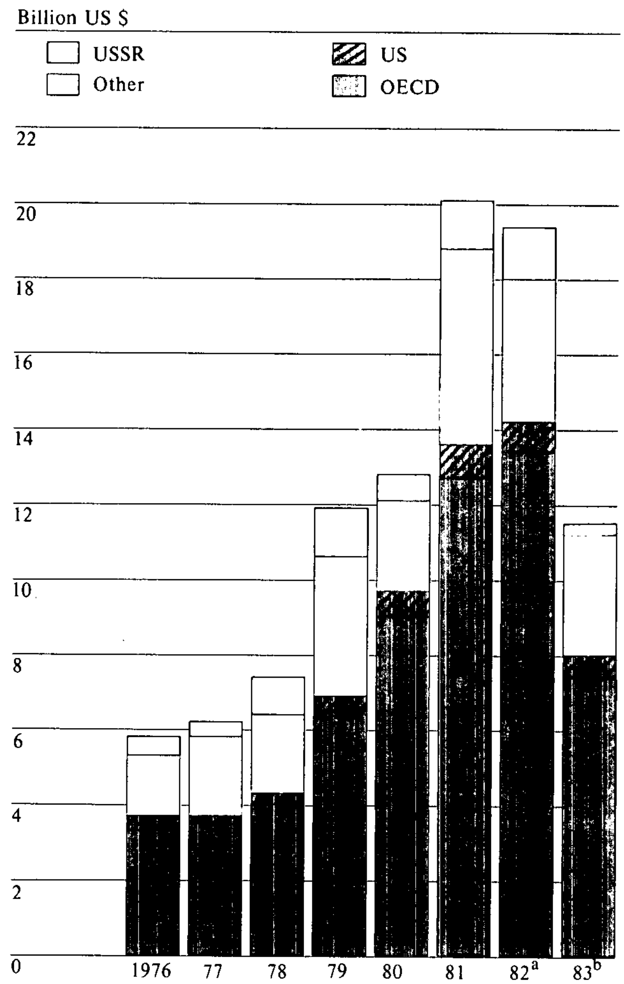
25X1

Military Spending

Saddam has even been forced to cut the military budget. Iraq has had to reduce overall military expenditures as much as 25 to 30 percent in comparison with the early months of the war, according to the Interests Section. Saddam terminated combat pay for all military personnel last October, a calculated risk that came when Iran was pressing its attack along the Iraqi border. These cuts probably included spending on equipment and materiel already in sufficient supply. We believe Saddam is counting on the professionalism of his officer corps and the fear of punishment to help ensure the loyalty of the approximately 600,000 regulars in the armed forces.

25X1

Figure 1
Iraq: Civilian Import Trends, f.o.b., 1976-83



[a] Preliminary.
[b] Estimated; based on partial third-quarter trade data.

25X1

301128 (A03959)1-84

Import Cuts

A sharp curtailment in imports is the immediate cause of Iraq's domestic economic problems. Iraq reduced import spending in 1983 to some $11-12 billion, in our judgment, compared with $19 billion in 1982. The regime restricted private-sector imports by delaying the issuance of import licenses and limiting their value to only 30 percent of 1982 allocations, according to the US Interests Section in Baghdad. Early 1983 trade data for Iraq's most important Western trading partners indicate that their sales of manufactured goods—including heavy industrial machinery, electrical equipment, and transport equipment, which have accounted for roughly 90 percent of their exports to Iraq—were well behind the 1982 pace. Imports of raw materials for the light industrial sector and most consumer goods were also reduced. Consumer goods imports from Japan, Iraq's second-largest trading partner, were down 85 percent during the first half of 1983 from the same period in 1982. [redacted]

Iraq's imports from the industrialized West probably amounted to only some $7-9 billion in 1983 compared with $14 billion in 1982. OECD trade data indicated that Iraq's imports from the West fell by over half to $4.9 billion in the first nine months of 1983 from the same period in 1982. The big losers were Japan, West Germany, and France, which accounted for 54 percent of the drop, largely because projects involving these countries were postponed or canceled. Oil barter deals and deferred payments may have allowed Iraq to increase imports in the second half of 1983—especially for arms imports. [redacted]

We believe trade with most Third World countries and Iraq's regional friends, was much lower in 1983 than 1982, based on early trade data. In 1982 Iraq received roughly 15 percent of its imports from the Third World. Turkey's exports to Iraq, once Ankara's second-largest customer after Iran, were down 60 percent to $190 million during the first three quarters of 1983 compared with the same period in 1982, [redacted] We believe Jordan's 1983 exports to Iraq, once its largest foreign market, also were below the $80 million level of 1982, a 60-percent drop from the 1981 peak. According to the US Embassy in Amman, Baghdad and Amman agreed in early 1983 to reduce by nearly 80 percent the target for Jordanian exports through Jordan's official trade center, which handles about one-fourth of Amman's exports to Iraq. [redacted]

Several of these countries have suffered other economic consequences because of Iraq's financial straits. Baghdad's clampdown on imports has crimped the revenues that Jordan, Kuwait, and Turkey received from the lucrative transit trade in Iraqi-bound goods, according to Embassy reporting. Only 10 percent of the 200 transport companies in Turkey were expected to survive to the end of 1983 unless trade picked up, [redacted] Iraq also has defaulted on its Baghdad Summit commitments—worth $242 million to cash-short Jordan—as well as scrapping foreign aid payments to other LDCs. In contrast, Iraq disbursed a total of $1.5 billion in development aid and military assistance in 1980. [redacted] 25X1

25X1

Civilian imports from the USSR in 1983, mostly for machinery, probably fell well short of the 1982 level of $1.4 billion, in our judgment, as Iraq wound down its development program. Soviet deliveries to Iraq plummeted to $137 million in the first three quarters of 1983 compared with about $1.2 billion for the same period in 1982, according to Soviet trade data. Military deliveries, on the other hand, probably reached some $1 billion, based on first-half data. After initial difficulties, Moscow and Baghdad settled on a payment scheme for Soviet military deliveries, according to the US Interests Section. The USSR is Iraq's most important arms supplier; last year, Baghdad signed arms deals with Moscow worth about $3 billion and received $1.7 billion in military hardware. [redacted] 25X1

25X1

Oil Revenues Continue To Decline

Reduced oil revenues are at the root of Iraq's worsening economic situation. As a result of lower export volumes and reduced prices, we estimate oil revenue plunged to less than $8 billion in 1983 compared with nearly $10 billion in 1982 and a peak of over $25 billion in 1980. Baghdad has only the pipeline across Turkey as a route for its oil exports. Iran virtually destroyed Iraq's two Persian Gulf oil export terminals at the outset of the war, and Damascus, allied with Tehran, has blocked oil deliveries through the pipeline across Syria. [redacted] 25X1

25X1

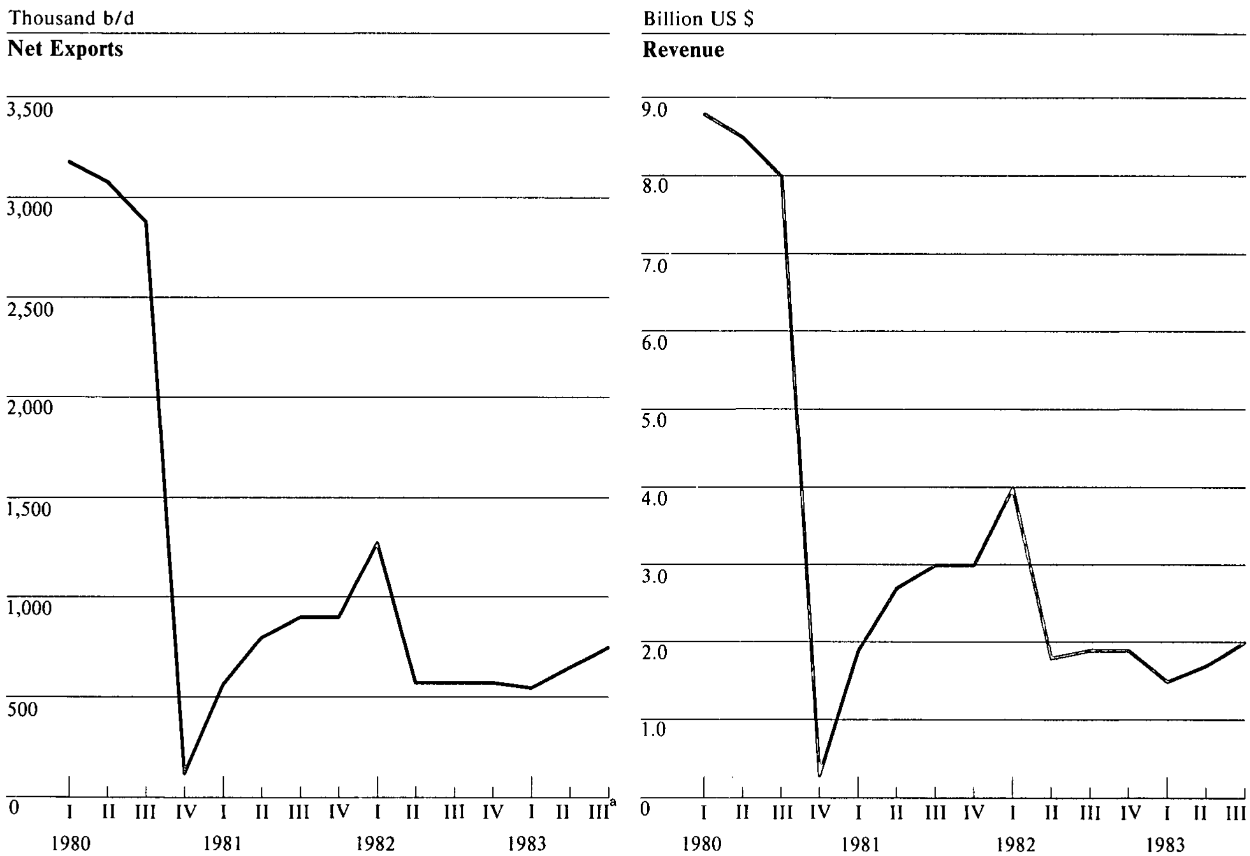
25X1

Moreover, Iraq was forced to lower the price of its oil $5 per barrel to about $30 to conform with the OPEC market realignment last March, according to the press. The price cut has cost Iraq almost $100 million a month in oil revenue. Despite the lower price, Iraq, along with other producers, has had difficulty selling its oil in a weak market in recent months, [redacted] 25X1

25X1

25X1

Figure 2
Iraq: Oil Exports and Revenues, f.o.b., 1980-83



[a] Estimated.

[redacted] 25X1

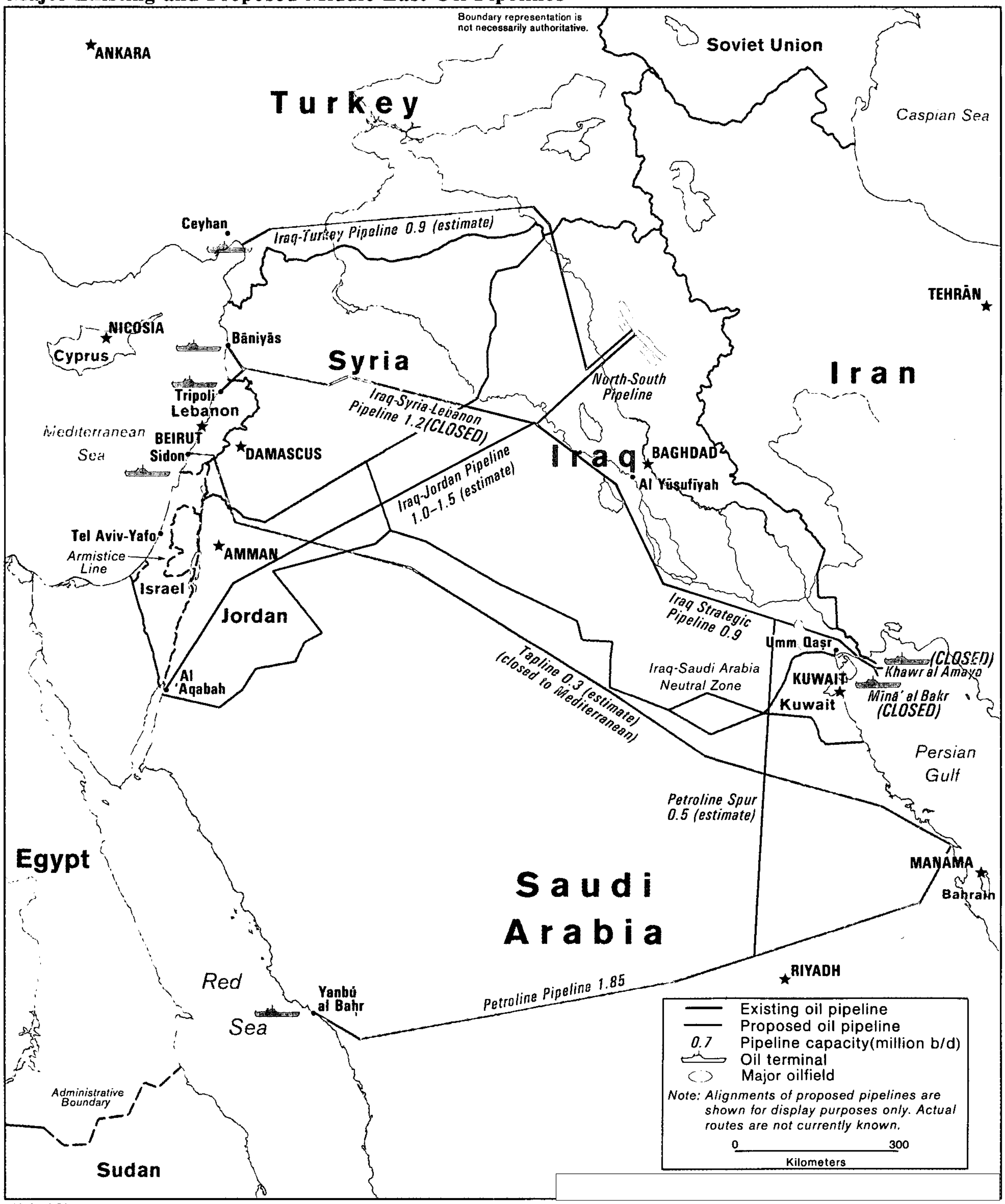
301127 1-84

Attempts To Increase Oil Exports [2]
Iraq is trying to boost oil sales to alleviate its economic problems. Iraq is in the midst of a program to expand the capacity of the Iraq-Turkey pipeline. According to Iraqi officials, the line now can carry 900,000 barrels per day of crude oil and will reach its planned maximum capacity of 1 million barrels per day by mid-1984. To encourage liftings from the Mediterranean, last April Baghdad dropped the transit fees it charges on oil pumped through the pipeline by 40 cents per barrel—a cut of almost 50 percent. Although isolated incidents of sabotage since 1980 have caused only brief closures, the 980-km-long line is still extremely vulnerable to terrorists or commando-type attack. [redacted] 25X1

Iraq also has arranged for the transport of oil overland by truck through Jordan and Turkey, [redacted] 25X1 [redacted] The oil is then shipped from Al 25X1

[2] See appendix for further details [redacted] 25X1

Figure 3
Major Existing and Proposed Middle East Oil Pipelines



700795 1-84

25X1

Aqabah and ports in Turkey. Only small quantities—about 50,000 barrels per day—can be delivered in this manner, however, because of congestion and damage to the roads. Indeed, Jordan is stopping Iraqi oil traffic to Al Aqabah that does not conform to maximum weight limits. Moreover, trucking the oil costs Iraq about $8 per barrel, nearly 30 percent of what it earns [redacted]

Baghdad is pursuing several longer term options to increase exports, including the possible construction of new oil pipelines through Saudi Arabia, Jordan, and Turkey. Negotiations are under way with Riyadh to build a spur capable of moving up to an estimated 500,000 barrels per day of oil to Petroline, the Saudi pipeline to the Red Sea. The spur would take advantage of unused capacity in Petroline—currently running well above 1 million barrels per day—and could also be the first part of a project involving a separate Iraqi line with a volume of 1.5-2 million barrels per day parallel to Petroline. [redacted]

The Saudis, however, fear a separate pipeline will ultimately cause friction between themselves and Baghdad and become a target for Iranian military action. [redacted] We believe the Saudis will attempt to delay the project at every opportunity. [redacted]

The other pipeline options are even less advanced. The line across Jordan to the Red Sea port of Al Aqabah is only at the feasibility study stage. According to Embassy reporting, estimates of construction time run from 16 months to three years, with a cost of about $1 billion. Capacity figures have not been made public, but we believe it would be about 1.5 million barrels per day. As for a new Turkish line, Embassy reports indicate that Baghdad and Ankara signed a preliminary protocol late last year to study the construction of a liquefied petroleum gas pipeline that would parallel the existing crude-oil line to the Mediterranean. [redacted]

Iraq is not optimistic that the Syrian pipeline will be reopened, [redacted] So long as Iran continues to provide Syria with oil worth about $1.8 billion on concessionary terms, Damascus has little financial incentive to reopen the pipeline. Saudi Arabia's efforts to mediate the dispute have, so far, failed [redacted] Other Gulf Cooperation Council states' attempts to resolve the issue are making no headway. [redacted]

25X1

25X1

25X1

Bartering

Iraq has bartered, using oil from Saudi Arabia and Kuwait through 1984. We estimate Saudi and Kuwaiti oil sales on Baghdad's behalf—in effect a form of financial aid—probably averaged approximately 200,000 barrels per day in 1983, worth about $2 billion. Saudi exports are going to Iraqi customers primarily in the USSR and Japan [redacted] Saudi Arabia and Kuwait also are providing smaller amounts of oil using production from the Neutral Zone, which is shared equally between the two countries. In most cases, Iraq's customers pick up the Saudi or Kuwaiti crude and send payments directly to Baghdad. [redacted]

25X1

25X1

25X1

Two such deals highlight the importance of such arrangements to Iraq's financing of the war while avoiding sharper cuts in civilian imports. The bartering has helped Iraq find customers in a soft world oil market and, we believe, may disguise some price discounting:

25X1

25X1

- France agreed last June to accept 80,000 barrels per day of Iraqi crude, worth about $860 million, in partial payment for the approximately $1 billion in outstanding debts Iraq had to pay for French military equipment in 1983, according to press reports.

25X1

- The USSR contracted last May for deliveries of at least $1.2 billion worth of Saudi crude to cover payments primarily for military hardware due in 1983, according to the US Interests Section in Baghdad. The Soviets, in turn, used the oil to fulfill their own oil contracts, mainly with India. [redacted]

25X1

Iraq also has bartered with civilian trading partners. Three Japanese trading companies, the largest recipients of the Saudi and Kuwaiti crude, are taking

25X1

25X1

Table 1
Iraq: Current Account Balance and Financing Arrangements

Billion US $

	1981	1982 [a]	1983 [b]	1984 [c]	
				Scenario A	Scenario B
Trade balance	−9.1	−9.7	−3.1-4.1	0.8	−2.2
Exports (f.o.b.)	11.0	9.7	7.9	8.8	9.8
Oil	10.8	9.5	7.6	8.5	9.5 [d]
Nonoil	0.2	0.2	0.3	0.3	0.3
Imports (f.o.b.) [e]	20.1	19.4	11.0-12.0	8.0	12.0
Net services and private transfers	−6.0	−7.1	−5.5	−4.6	−4.8
Freight and insurance	−4.0	−3.5	−1.5	−1.3	−1.5
Investment income [f]	3.2	1.6	0.5	0.2	0.2
Other	−5.2	−5.2	−4.5	−3.5	−3.5
Grants	−2.0	−1.0	0	0	0
Current account balance	−17.1	−17.8	−8.6-9.6	−3.8	−7.0
Financing the current account	18.0	18.5	8.6-9.6	3.8	7.0
Gulf state aid	8.0	5.5	1.6	1.0	2.0
Saudi and Kuwaiti oil sales	0	NEGL	1.7	0.5	1.0
Commercial and other loans	0	0	0.8	0	0.5
Trade credits	0	0	1.0-2.0	0.8	1.5
Reserve drawdown	10.0	13.0	3.5	1.5	2.0
Other, including errors and omissions	−0.9	−0.7	0	0	0

[a] Estimated.
[b] Estimated; based on preliminary three-quarter data.
[c] Alternative scenarios for import spending and current account balance depend in part on our assumed levels of foreign assistance and reserve drawdowns.
[d] Assumes Turkish pipeline expansion completed in early 1984.
[e] Imports are understated to the extent they do not include military purchases from every country.
[f] Represents earnings on official foreign assets only.

[redacted]

25X1

delivery of oil to cover Iraqi import bills for civilian goods in both 1982 and 1983, according to the US Interests Section in Baghdad. A South Korean firm agreed to take oil for project payments of $800 million due in 1983, [redacted]

Closing the Current Account Gap

We believe Iraq had a roughly $9-10 billion deficit in its 1983 current account, down considerably from the $18 billion deficit in 1982 and the $17 billion deficit in 1981. Iraq was able to reduce the deficit only by sharply cutting imports in 1983. Iraq had a trade deficit of $3-4 billion and experienced other foreign exchange outflows of about $6 billion—most of it in remittances by Iraq's still sizable foreign labor force. [redacted]

25X1

25X1

25X1

Financial assistance from abroad helped offset the deficit. Because official subventions—including Gulf state assistance—fell short of Iraq's overall requirements, Baghdad has had to rely increasingly on deferred payments to its foreign suppliers to avoid politically intolerable import cuts. [redacted]

Deferred Payments

We estimate Iraq has negotiated deferred payments—or simply been late in paying—some $1-2 billion owed foreign companies for a wide range of imports in 1983. Iraqi payments have often run as much as six months late, and Baghdad generally negotiated for deferral of payments to 1985 at interest rates below commercial levels, according to the US Interests Section. [redacted]

Many foreign firms are under financial pressure to come to terms with Iraq to protect their investments, [redacted] Prospects for participation in postwar development also motivate the companies to accede to Iraq's demands. To avoid piling up its own debt, Baghdad is requiring foreign firms to find their own financing for the deferred payments, according to the US Interests Section. [redacted]

Iraq is negotiating with a host of foreign suppliers. By insisting on dealing with individual companies rather than their governments, we believe Baghdad hopes to force the firms to meet its terms by playing one against the other. The Iraqi strategy has had some success, but not enough to prevent the sharp decline in imports in 1983:

- A French banking consortium agreed to an Iraqi request for a $1 billion credit to cover the deferral of payments due French civilian contractors in 1983. Still to be resolved, however, are payments for an additional $500 million in war-related costs owed French firms.

- Italian firms have agreed to defer payments owed in 1983-84 for most of a $2 billion contract for warships [redacted] Iraq, however, has yet to sign the agreement, probably because of difficulty in meeting the downpayment requirements. The Italians also have agreed to refinance a $300 million power project.

- Canadian and Australian companies agreed to defer over $100 million due in 1983 for agricultural products, according to the US Interests Section. 25X1

- Most payments totaling an estimated $3 billion owed to Japanese, West German, and British suppliers remained unresolved as of late 1983. [redacted] 25X1 [redacted] 25X1

Other countries—many of which can ill afford to advance the funds—are participating in the Iraqi bailout. To protect their own firms, Jordan and Turkey provided Iraq with supplier credits of about $365 million to help finance imports in 1983, according to the US Embassies in Amman and Ankara. Iraq 25X1 also asked South Korea to defer some of the over $1 billion in payments owed in 1983, according to the US Interests Section. Baghdad, in addition, agreed to 25X1 defer 1982 obligations owed the largest Brazilian firm in Iraq and is receiving food and other commodities from the Philippines and Thailand through deferred payments. [redacted] 25X1

Commercial Loans 25X1

Commercial loans from the international banking community in 1983 amounted to about $620 million. Many Western banks, already concerned about their overexposure in other LDCs, are reluctant to lend to Iraq until the war is over, in our judgment. Only one French and two US banks participated in the largest commercial credit Iraq received in 1983—a $500 million, five-year loan last March from a bank syndicate; the rest of the 10 leading managers of the loan were Arab banks. Arab financial institutions—which may be more willing to lend to Iraq—probably have less funds available than in the past because other OPEC countries are withdrawing funds to cover their own financial needs. Baghdad received only a $120 million loan for the expansion of the Turkish pipeline from a syndicate headed by the Arab Banking Corporation and the Arab Petroleum Investments Corporation, according to the press. [redacted] 25X1 25X1

Government Loans 25X1

After months of negotiations, the United Kingdom agreed in October to provide Iraq with a $388 million loan with payments spread over the next five years for the purchase of civilian machinery and equipment, according to the Embassy in London. In return, Iraq must pay about $46 million of 1983 debt owed British firms, according to the press. The only other Western loan Iraq has obtained is a $50 million railroad project loan from West Germany, according to a press report. [redacted]

The Japanese agreed last August to extend for five years the deadline on Iraq's use of a $2.5 billion credit that originally was to expire on 15 August, according to the US Embassy in Tokyo. Tokyo, however, has been dragging its feet in response to Iraqi requests to disburse the funds. Iraq had used only about $700 million of the funds before the war with Iran started, and Japan froze additional disbursements. [redacted]

Regardless, the loan extension did not help cover Iraq's cash needs for 1983 because the credit is tied to new project spending. Japan will not allow Iraq to draw on the loan to pay existing debts. Moreover, Tokyo probably will offer no new sizable credits until the existing loans are fully disbursed. [redacted]

Gulf Nonoil Aid

We estimate Gulf state aid—other than oil sales on Iraq's behalf—in 1983 amounted to about $1.6 billion. Almost one-third of these disbursements were late payments for commitments made during 1981-82. The Gulf states have their own revenue problems because of the weak world oil market. [redacted]

Baghdad is demanding that its Gulf state benefactors provide more aid if they wish to prevent an Iraqi escalation of the conflict with Iran. Deputy Prime Minister Ramadan apparently warned Kuwait's Amir Sabah that Iraq would strike Iran's Khark Island oil terminal if additional financial support were not forthcoming from the Gulf states, according to US Embassy sources in Kuwait. Baghdad also attempted at the November OAPEC meeting to extort $1 billion per month from the Gulf states to forestall an Iraqi raid on Khark Island, [redacted]

International Organizations

Iraq has not received a response to its request for a $225 million loan from the International Monetary Fund (IMF). The IMF has not decided whether Baghdad qualifies for the loan under its criteria for helping a country with "temporary" export shortfalls "due largely to circumstances beyond its control," according to State Department reports. Even if the IMF loan agreement could be reached in principle soon, negotiating the details would take several months. Iraq would have to meet other conditions, probably including import restraints and fiscal reforms, which Baghdad would be loath to accept. The Arab Monetary Fund has provided $90 million to Iraq, [redacted]

25X1

25X1

Foreign Reserves

We believe Iraqi foreign exchange reserve drawdowns totaled more than $3 billion in 1983. Iraq drew down its assets to about $4-5 billion by September, [redacted] It is now selling gold, an indication that Iraq has little cash remaining. The government drive to collect gold from the citizenry is not making a significant contribution to government coffers, in our judgment. [redacted]

25X1

25X1

25X1

25X1

Iraq's reserve position has deteriorated markedly in the last few years. Foreign exchange assets amounted to about $31 billion before the war and $8 billion at the beginning of 1983. Most of Iraq's remaining reserves are held as loans to less developed countries, which will be difficult for Baghdad to convert to ready cash. [redacted]

25X1

25X1

25X1

Outlook

Iraq's financial squeeze will continue in 1984. Oil exports will increase somewhat, but financial aid and credits from abroad could fall. With foreign exchange reserves near depletion, Baghdad may have to further reduce imports at the expense of the consumer. [redacted]

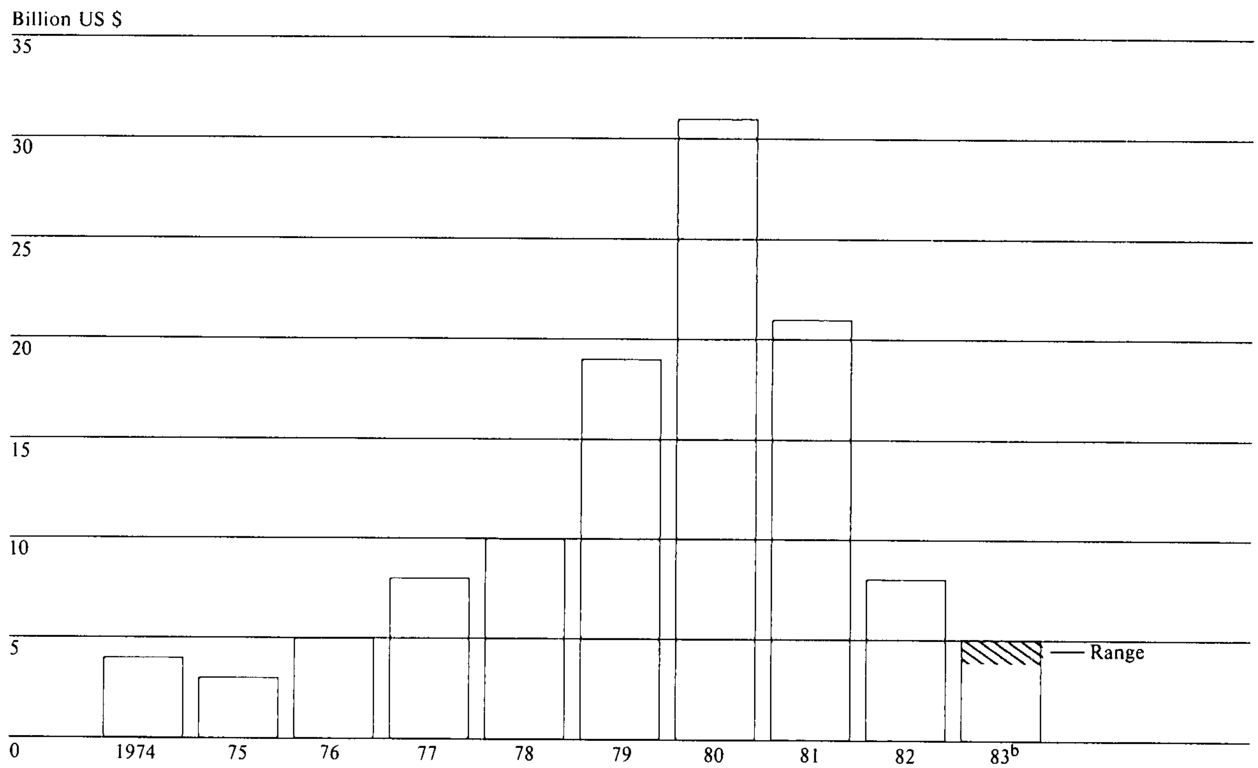
25X1

A sketchy outline of Iraq's 1984 budget, approved in January 1984, points to another year of strict austerity for the economy. Minister of Trade Hassan provided no data but stressed that top priority will be given to import spending for defense and the supply of basic commodities. The investment program will focus on the completion of strategic projects that support the

25X1

25X1

Figure 4
Iraq: Official Foreign Exchange Assets,[a] 1974-83



[a] End of year.
[b] Estimated.

301126 (A03710) 1-84

war. Spending for the consumer will center on basic services such as water, electricity, and health services. The plan's emphasis on increased productivity and efficiency probably results from serious war-related manpower shortages as well as the desire to save money.

Increased exports through the Turkish pipeline could add $1 billion to revenues in 1984, but Iraq probably will be unable to resume significant oil exports through the Gulf until the war ends. Repairs to the offshore oil terminals at Mina al Bakr and Khawr al Amaya will require Western technicians who are unlikely to begin work while the war continues. Four temporary single-point mooring buoys are in long-term storage in Singapore. Even if the war were to end tomorrow, it would take about 10 months to install the buoys and even longer to repair the terminals. Syrian President Assad's deeply rooted hostility for Saddam will preclude an immediate reopening of the Syrian pipeline, in our judgment.

Even in the unlikely event construction on the pipeline through Saudi Arabia began soon, it would not be available in time to help Iraq in 1984. Construction of a pipeline to connect to the existing Petroline pipeline probably would take about a year, after which Iraq could export an additional 400,000 to 500,000 barrels per day, [redacted] The decision is difficult for Riyadh. Saudi Arabia and Iraq were adversaries before the war, and we believe Riyadh does not see an Iraqi pipeline across its territory in its long-term strategic interests. Moreover, increased Iraqi oil exports will compete with Saudi oil sales. The construction of new pipelines across the Arabian Peninsula to the Red Sea or the Gulf of Oman would take at least three years. Other pipeline alternatives also would not be ready in time to help ease Iraq's financial problems in 1984. [redacted]

Iraqi oil exports will also be affected by world demand. We project only a modest increase in demand for OPEC oil over the next few years. As a result, Iraq probably will soon experience difficulty in marketing its increased production at current market prices. [redacted]

Baghdad will probably get enough foreign help to meet its basic import needs in 1984—Iraq continues to depend on imports for about half of its grain consumption alone—but not much more. The Gulf states' oil sales are not likely to recover enough in 1984 to prompt them to increase their direct financial aid to Iraq substantially unless they perceive a threat to Iraqi political stability. Commercial banks probably will refrain from giving major long-term loans to Iraq while the war continues. [redacted]

Iraq probably will be able to obtain enough trade credits to match last year's level. Baghdad has lined up 1984 credits worth at least $500 million from several countries including Austria, Great Britain, West Germany, and Australia, according to the US Interests Section and the press. Iraq will continue to negotiate with other countries, especially France and West Germany, for more deferred payments, but it is likely to encounter resistance from financially less able or willing contractors and suppliers. Several West German firms, for example, have stated they anticipate serious obstacles to financing in 1984, according to the press. Moreover, should Baghdad renege on 1983 payments due in 1984, it will probably cause many creditors to shy away from giving new loans. [redacted] 25X1

To maintain its superiority in military equipment—and offset Iran's manpower advantage—the government probably will resist further reductions in defense-related spending. Military contracts signed in 1982 for nearly $5 billion are likely to ensure high levels of arms spending. [redacted] 25X1 25X1

Iraq's economic problems will not be enough to loosen Saddam's tenacious hold on power, in our judgment. We believe growing war weariness among the populace and declining morale in the military will pose at least as serious a threat to Saddam as the economy in the months ahead. If his ability to attract popular support significantly wanes, he will resort to repressive measures to maintain control. [redacted] 25X1 25X1

Iraq's economic prospects for 1985 and beyond would improve if Saudi Arabia allows construction of the pipeline spur from Iraq to begin soon. Oil exports through the pipeline would earn Iraq $4-5 billion annually, assuming the oil is sold at today's prices. Saudi Arabia and Kuwait would then probably curtail oil sales on Iraq's behalf, but Iraq would still have an initial net revenue addition of about $2 billion. [redacted] 25X1 25X1

Implications for the United States

An important part of Iraq's diplomatic strategy to alleviate its economic difficulties and end the war is an improvement in relations with the United States. Iraq believes US leadership is needed to elicit increased Western support for Baghdad. Baghdad probably also will seek economic help from Washington. 25X1
[redacted] 25X1

Iraq has received only modest economic assistance from the United States. Following Iraqi Minister of State Muhammadi's visit to Washington in February 1983, the United States extended an additional $210 million package of interest-free loans and export credit guarantees to Iraq to import US food. The United States imports virtually no oil from Iraq, and US exports to Iraq are modest. During January-September 1983, US sales to Iraq amounted to $440 million, less than 9 percent of total OECD exports to Baghdad. [redacted]

Iraq probably will also urge the United States to help Baghdad gain additional economic support from the Gulf states and Western creditors. Baghdad sought Washington's assistance to obtain Riyadh's approval of the pipeline across Saudi Arabia. [redacted] 25X1

Iraq also will continue its close ties with the USSR. Baghdad and Moscow signed a comprehensive trade agreement last November that will give the Soviets an expanded role in Iraq's development and petroleum projects. Iraq's sizable arms deals also ensure Baghdad's dependence on the Soviets. While affirming Iraq's right to export oil through the Gulf, the USSR indirectly has warned the United States not to intervene in the region, according to the US Embassy in Moscow. Moscow will probably try to use closer military cooperation with Baghdad as an entree for expanding its political influence in Iraq—especially now that Soviet relations with Iran have soured. [redacted] 25X1

Baghdad, for its part, will remain distrustful of Soviet intentions and will prevent any spread of Soviet interference in Iraqi internal politics—especially attempts to strengthen Communist Party influence in Iraq, in our judgment. Baghdad has warned the Soviets not to attempt to parlay its dependence on arms into strategic alliances. Moreover, Baghdad has not forgotten Moscow's refusal to ship arms to Iraq during the first six months of the war. [redacted] 25X1

If Iraq cannot ease economic and military pressures, it may decide to escalate the war in the Gulf, threatening oil exports vital to the West. The delivery of French-produced Super Etendard aircraft armed with Exocet antiship missiles in October and Baghdad's attacks on oil tankers servicing Iran in the Gulf represent a major attempt to break the economic stranglehold. The Iraqis, we believe, are prepared to make good on their threat to cut off Iranian oil exports in the hope that this will force Iran into negotiations to end the war. [redacted] 25X1

More realistically, however, the Iraqis probably would count on major Western powers to intervene to stop an escalation of the war and enable Iraq to resume exporting oil from its Gulf ports. Baghdad does not believe that Iran will voluntarily permit Iraq to use its Gulf terminals, [redacted] 25X1 Meanwhile, Baghdad's threats 25X1 serve as a form of blackmail against the Gulf states. Iraq wants these states to increase substantially their subsidies. If this coercion works, we believe the Iraqis would hold off escalating the war with Iran. [redacted] 25X1

Appendix

Iraq's Oil Export Facilities

Before the war, Iraq's crude oil export network was the most flexible in the Middle East, with a total system capacity of about 5 million barrels per day—some 1 million barrels per day above Iraq's prewar productive capacity. The bulk of the capacity was located in the two sea-island export terminals of Mina al Bakr and Khawr al Amaya, each capable of loading 1.6 million barrels per day. Severely damaged at the onset of the war, these facilities could be repaired by utilizing existing subsea oil lines in conjunction with single-point mooring buoys. This would provide Iraq with a Persian Gulf export capacity of 1.5-2 million barrels per day within about 10 months. Lacking any specific guarantee of a moratorium on attacks on Gulf oil facilities, however, Baghdad would find it difficult to hire the Western expertise needed to install the temporary loading equipment or rebuild the permanent structures. [redacted]

The 1.2-million-barrel-per-day-capacity Iraqi pipeline across Syria was closed by Damascus in April 1982 to bolster Iranian attempts to topple Iraqi President Saddam Husayn. Because of the longstanding animosity between Saddam and Syrian President Assad, there appears little hope that the line will be reopened in the near term. Even in the unlikely event the pipeline is reopened, possible constraints on the export capacity of the Syrian oil terminal at Baniyas and apparent damage to facilities at the other terminal in Tripoli, Lebanon, may have substantially reduced the line's effective oil throughput capacity. [redacted]

Expanding the Iraq-Turkey Pipeline

The Iraq-Turkey pipeline is in the midst of an expansion that will increase its capacity by almost 300,000 barrels per day—to just under 1 million barrels per day by mid-1984. Iraqi officials announced in December that the first phase of the expansion—involving installation of new pumps at the existing five pumping stations—is complete, raising the line's capacity to almost 900,000 barrels per day. We are uncertain, however, whether the pipeline can handle the higher volume. In late summer 1983 Iraq reportedly was pushing as much as 850,000 barrels per day of oil through the pipeline with the aid of drag-reducing chemicals, but the increased pressure apparently caused leaks and a fire, which closed the line briefly in September. The current phase of the expansion involves addition of more pumps and parallel pipe to several sections of the pipeline, which will reduce operating pressures in certain critical areas. When completed, the extra capacity could yield Baghdad up to $3 billion annually in oil revenues; there are no apparent plans for additional capacity expansion beyond the current program. [redacted] 25X1

New Export Options: Pipelines Through Saudi Arabia and Jordan

The Saudi Link

Baghdad's best option for a sizable increase in oil exports in the next year or so would be a link to Petroline, the Saudi oil export pipeline to the Red Sea. An 800-kilometer connector line into Petroline at one of three pump stations would use a portion of the excess capacity in the line, estimated at over 1 million barrels per day. [redacted] 25X1 25X1

At Iraq's request, a major international construction company did a rush analysis on this proposal over the past few months. [redacted] crash construction would take 10 to 14 months. Industry experts believe that meeting this compressed schedule would require a single firm to serve both as project manager and engineer, allowing design and engineering work to be conducted as construction proceeds. Pipelaying would also have to be done simultaneously in three or four areas. Pipe and other long-leadtime items—primarily valves—would have to be ordered immediately because delivery could take up to eight months. [redacted] 25X1 25X1 25X1

Cost estimates for the Iraq-Petroline link vary significantly, primarily because detailed design and price

Table 2
Iraq: Petroleum Export Options [a]

Export Option	Volume (*thousand b/d*)	Leadtime (*months*)	Cost (*million US $*)	Remarks
Saudi Petroline link	300-1,200	10	700	Throughput volume depends on where the connection with Petroline is made; average throughput is estimated at 500,000 barrels per day. Cost estimate is based on an accelerated construction schedule.
Iraq–Red Sea pipeline	1,600	54	3,600-4,500	Based on a 1981 feasibility study.
Tapline link	500	10	NA	Would require Iraqi crude to be commingled with Saudi crude.
Jordan pipeline	1,000-1,500	36	1,000	Line is still in preliminary study stage.
GCC pipeline	2,500	NA	NA	GCC has endorsed a study to examine the possibility for a line bypassing the Strait of Hormuz.
Persian Gulf SPMs	1,500-2,000	10	110	Based on current plans which assume no further damage and sufficient onshore pumping capacity.

[a] Detailed design work on all projects still needs to be either initiated or completed. As a result, cost and construction schedules are subject to change.

[redacted] 25X1

25X1

estimates have not yet been prepared. According to one rough US Government estimate, based on historical experience, the cost of the pipeline, including pumping facilities, would be about $360 million. This estimate assumes the project is completed in 18 months. [redacted] the cost would more closely approximate $700 million if a 10-month timetable is established. Factors that would drive up costs under these circumstances include the need to purchase equipment and material without going through an extended bidding procedure, the need to pay delivery premiums, and extensive overtime for labor. [redacted]

Phase Two: The Parallel Line
Baghdad views the link to Petroline as only the first phase of the project, which it eventually hopes will include construction of a separate Iraqi pipeline parallel to Petroline, extending from the linkup point to the Red Sea. The second phase is estimated to take about four years and cost as much as $4.5 billion. Certain aspects of this proposal resemble alternatives put forth in a 1981 feasibility study initiated by Baghdad for an Iraq–Saudi Arabia pipeline. The 1981 plan never overcame the financial and political roadblocks thrown up by Riyadh, and, by the beginning of 1983, it was a dead issue. [redacted]

Saudi Hesitancy
[redacted] 25X1
Riyadh has made the political decision to proceed with the construction of a linkup to Petroline. [redacted] 25X1
negotiations with the Iraqis are under way to establish 25X1
rules governing the pipeline's ownership and operation. 25X1
In our judgment, Saudi leaders probably calculate that they can maintain full control over the spur, given its limited capacity and dependence on the Saudi pipeline. Riyadh probably hopes that its approval of such an arrangement—although offering no immediate financial relief to Baghdad—would ease 25X1
Iraqi concerns over export limitations, diminish Baghdad's growing sense of desperation, and preclude a major military escalation by Iraq in the war with Iran. Saudi leaders may also envision some financial dividends accruing to them from a linkup to Petroline through oil transit fees and the need for reduced monetary aid to Iraq. [redacted] 25X1

We do not rule out the possibility, however, that Riyadh will drag out negotiations over the spur and try to postpone the project. Such tactics would be

25X1

Table 3
Iraq–Saudi Arabia: Industry Capacity Estimates of Proposed Iraq-Petroline Link [a]

Million barrels per day

Pipeline Diameter (*centimeters*)	Connection Point With Petroline		
	Pump Station 1 (West of Abqaiq)	Pump Station 3 (Khurais)	Pump Station 6 (160 kilometers west of Riyadh)
140	1.2	0.7	0.3
120	0.7	0.4	NA

[a] Volumes assume no intermediate pumping.

[redacted]

consistent with the Saudis' underlying lack of enthusiasm for the project and would be characteristic of how they operate when confronted with unappealing requests for assistance. We believe Saudi leaders also worry that a more extensive commitment to Iraq might prompt a backlash from Iran, possibly including Iranian strikes against Saudi oil installations. If Riyadh's commitment to an Iraqi spur to Petroline is serious, positive evidence in the form of signed contracts for the purchase of equipment and services should be forthcoming. [redacted]

The Jordanian Connection

During the past year, Baghdad and Amman have been exploring the possibility of an export route across Jordan to the Red Sea. Few details of the project—which has received only a preliminary study—are available, [redacted] The trans-Jordan pipeline apparently would run about 800 kilometers from near Baghdad to the port of Al Aqabah. We believe its capacity most likely would be about 1.5 million barrels per day, similar to that of the proposed Saudi line to the Red Sea. To handle crude volumes of this magnitude, an export terminal would also be needed. Although no detailed design work has been done on this proposal, an Embassy source estimated it would take about three years and cost at least $1 billion. We believe a shorter work schedule might be possible, albeit at a higher cost. [redacted]

Financing the Pipelines

Funding for the projects does not appear to be a major problem. [redacted] 25X1
several companies—primarily Italian, British, and Japanese—have indicated a willingness to take on the task and that short-term supplier credits will be made available. These firms are eager to keep experienced engineering and construction crews employed and would be willing to take the risk of helping to finance the projects if work could begin soon. [redacted] 25X1

A New Turkish Line 25X1

In October, Baghdad signed a protocol with Ankara covering construction of a 95,000-barrel-per-day, 18-inch liquefied petroleum gasline parallel to the existing crude-oil pipeline. Feasibility studies, which the Embassy in Ankara reports are being paid for by Iraq, are under way. Baghdad also will be responsible for arranging financing for the pipeline, which an industry estimate places at $300-400 million. The Embassy cautions, however, that the project is still tentative, and much will depend on the results of the feasibility 25X1 study. If a decision is made to proceed, the project is expected to take about three years. [redacted] 25X1

Other Iraqi Oil Export Pipeline Proposals

Although the possibility of a Saudi link or a Jordanian pipeline appears to be the best way for Baghdad to boost oil exports significantly, other options have been 25X1 put forward. [redacted] 25X1

Iraq could link into Tapline, a line through Saudi Arabia, utilizing unused capacity in the line's southern section. Tapline is essentially unusable as an export route to the Mediterranean. Damage has closed the Lebanese section, and, in recent years, only about 50,000 to 60,000 barrels per day of crude oil has been sent through the line to Jordan. Iraq could link into Tapline near Qaysumah, the initial pumping

25X1

station, and run crude south into the main Saudi pipeline network at the Qatif junction. This section of line is reported to need refurbishment, however, if it is to carry its rated volume of 500,000 barrels per day. Aramco can be expected to oppose this option since the company intends to use the lower portions of Tapline to feed crude oil north to its 250,000-barrel-per-day refinery at Jubail, due for completion late next year. [redacted] 25X1

Earlier this year the heads of state of the Gulf Cooperation Council (GCC) endorsed the study of construction of a GCC oil pipeline linking all six members to an export terminal on the coast of Oman, bypassing the Strait of Hormuz. [redacted] 25X1
[redacted] the proposed line would have a 25X1
capacity of 2.5 million barrels per day, but no estimate of cost or construction time was available. Baghdad—which is not a GCC member—has expressed interest in tying into the pipeline system, causing doubts about the scheme among some members. Given this problem, along with the probable enormous expense of the project and the fate of previous proposals to build a "trans-Oman" oil pipeline, we believe there is little hope for this project's proceeding beyond the preliminary study phase. [redacted] 25X1
[redacted] 25X1