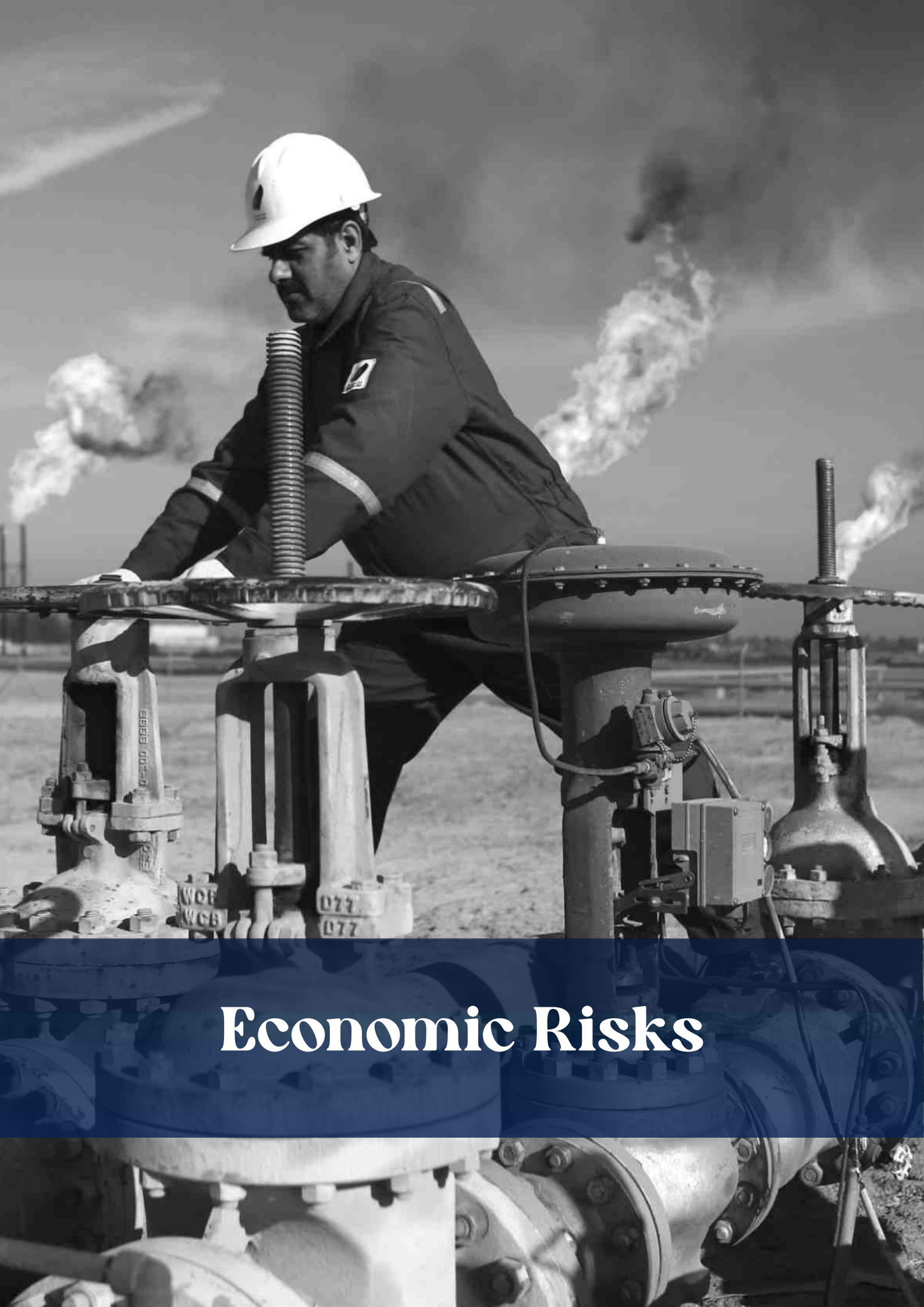
AVERROES POLICY FORUM

Arab Center for Research

Averroes Policy Forum

Iraq White Paper



Economic Risks

Oil-Dependent Economy:

Iraq remains one of the most oil-dependent economies globally, with oil accounting for over 90% of government revenue, 96% of exports, and 40% of GDP in 2023. This excessive reliance exposes the country to severe economic volatility and limits fiscal flexibility. The recent extension of OPEC+ restrictions further reduces Iraq's oil output, exacerbated by stagnant global demand and falling prices. Iraq's heavy gas deficit and underdeveloped industrial sector hinder economic diversification, reinforcing its vulnerability to external shocks.

Fragile Banking System Limits Economic Growth:

Iraq's banking sector remains predominantly state-controlled and structurally weak, limiting its ability to support economic development. With credit to the private sector accounting for only 19.4% of GDP, access to financing remains severely restricted, particularly for small and medium-sized enterprises (SMEs). The dominance of public banks, coupled with weak regulatory oversight and limited financial inclusion, hampers private sector growth and investment. This underdeveloped financial system constrains economic diversification, leaving Iraq heavily reliant on oil revenues and vulnerable to external shocks.

Persistent Unemployment Crisis:

Iraq faces a severe unemployment crisis, with an overall unemployment rate of 15.5%, disproportionately affecting women (30%) and youth (32%). Structural economic weaknesses, a dominant but capital-intensive oil sector, and a fragile private sector limit job creation. The lack of economic diversification further exacerbates the issue, leaving many young Iraqis without viable employment opportunities. Women, in particular, face significant barriers to workforce participation due to social and institutional constraints. Meanwhile, a large and growing informal sector absorbs much of the remaining workforce, offering low wages, job insecurity, and little social protection.

Large Public Sector:

Iraq's labor market is dominated by a bloated public sector, which employs 37% of the workforce and accounts for over 50% of government expenditure. This heavy reliance on public jobs strains fiscal resources and limits investment in critical infrastructure and services. The imbalance between an oversized public sector and a weak formal private sector hampers economic diversification and sustainable job creation.

Political Risks

Iran-Backed Militia Influence Undermines Iraqi Sovereignty:

Iran-backed militias, part of Iraq's state institutions through the Popular Mobilization Forces (PMF), operate autonomously, undermining government policies. These groups have been involved in violent actions, including the 2021 assassination attempt on PM al-Kadhimi, attacks on U.S. targets, and repression of protests. Despite U.S. support for Iraq's security forces, militia power remains a key challenge to sovereignty. In November 2023, the removal of Sunni leader Muhammad al-Halbousi by the Supreme Court alongside the ousting of another political rival, further highlighted the deep political divisions exacerbated by militia influence.

High Level of Corruption:

Corruption remains rampant in Iraq, with political parties siphoning funds, accepting kickbacks, and monopolizing sectors, while obstructing anti-corruption efforts. Iraq ranks 140 worldwide according to Transparency International. The judicial system, hindered by politicization, addresses only a fraction of cases investigated by the Integrity Commission. Whistleblowers, journalists, and activists face intimidation and legal threats. The deadly September 2023 fire in Qaraqosh, caused by safety violations linked to corruption, underscores the severe consequences of the pervasive corrupt practices. Despite anti-corruption rhetoric, the system remains largely unaccountable, fueling public unrest.

Political Instability:

Iraq remains plagued by political and social instability, driven by Iranian influence, deep sectarian and ethnic divisions, and spillover from regional conflicts. Armed militias operating outside state control further destabilize the country, while the threat of an Islamic State resurgence looms. Tensions between the ruling Shia majority and other groups, including Sunnis and Kurds, fuel ongoing unrest, often erupting into protests against government corruption and inefficiency. This volatile environment weakens state institutions, deters investment, and hinders economic and social progress, making long-term stability increasingly difficult to achieve.

Iraq's 2025 Elections:

Risks of Political Exclusion and Rising Tensions: Iraq is set to hold parliamentary elections in 2025 under a revised electoral law introduced in 2023, which reduced the number of constituencies. This change appears to favor major parties, particularly those in the ruling coalition led by Prime Minister Shia al-Sudani and the Iranian-backed Shia Coordination Framework (CF), as well as allied Sunni and Kurdish parties, at the expense of smaller parties and independent candidates. The December 2023 provincial elections, held under this system, reinforced CF-aligned parties' dominance, suggesting

a similar outcome at the national level. While the political climate remains relatively calm, this shift risks deepening public frustration and undermining representation, potentially fueling future unrest.

Environnemental Risks

Water Scarcity:

Iraq is the fifth-most vulnerable country to climate change, facing soaring temperatures, droughts, water scarcity, and extreme weather. The water availability per capita is expected to be 479 cubic meters by 2030 – a far cry from the WHO standard of 1700 cubic meters per year. Water policies in neighboring countries have reduced vital water sources, while rapid population growth and inefficient water use increase demand. By 2021, around 20,000 people were displaced due to water shortages and poor quality, with migration driven by drought. Over the past 40 years, output from the Tigris and Euphrates-which provide up to 98% of Iraq's surface water, has decreased by 30-40%. This decline is driven by reduced rainfall, increased evaporation induced by warming temperatures, and upstream damming by neighboring countries. Iraq faces a significant water deficit, with projections indicating a shortfall of 10 billion cubic meters by 2035, threatening access to drinking water, sanitation, and agriculture.

Biodiversity loss:

Iraq's biodiversity has been severely impacted by a combination of human activities and environmental changes. Unregulated hunting and the illegal trade of endangered species have decimated wildlife populations, while high salinity levels and pollution have degraded vital ecosystems. Uncontrolled urban development has led to habitat destruction, particularly in Iraq's most biodiverse regions, such as the marshlands, once a UNESCO World Heritage site. The lack of effective conservation measures has further compounded these challenges, leaving many of Iraq’s native species and ecosystems at risk of irreversible damage.

Conflict Pollution:

Beyond the immediate loss of life and infrastructure, conflict pollution leaves long-lasting environmental damage. In Iraq, successive conflicts, including attacks on its oil and industrial assets, have created environmental pollution hotspots. The World Bank’s 2018 report revealed that 47% of Iraq’s natural forests were destroyed, and 2.4 million hectares of land became unusable due to landmines. A recent report indicates 76 pollution hotspots (51 sites contaminated by oil pollution, 23 by hazardous chemicals, and 2 by waste). This environmental damage costs Iraq an estimated US$1.5 billion annually, with severe economic and social consequences.

Desertification:

Prolonged droughts and poor soil management have caused significant soil degradation in Iraq, with over 39% of land affected by desertification. Iraq's once UNESCO-listed marshlands have also suffered, with more than 70% of the area now desert and 20% converted to agricultural fields, leaving only 10% of the marshlands intact.

Geopolitical Risks

Instability in Syria:

With Assad out of Syria, Iraq faces increased security risks, particularly along its 372-mile border with Syria, where hostile armed groups operate. The collapse of the U.S.-backed Syrian Democratic Forces (SDF) and the al-Hol camp, housing 40,000 ISIS-linked detainees, many of whom are Iraqis, pose a direct security threat to Iraq. Iraq must secure its border while managing internal pressures, as Turkey's rising influence could challenge Iran's hold on Iraq, and the U.S. troop withdrawal agreement may need reassessment.

The Israel-Palestine conflict:

The conflict which escalated in October 2023 between Israel and Hamas in Gaza, triggered attacks on several American military bases in Iraq, Syria, and Jordan by Iraqi militias, many of which are aligned with Iran and connected to CF parties. These militia groups, supported by Iran, have repeatedly targeted U.S. military and diplomatic assets, exacerbating the complexity of the situation. Ongoing attacks by Iraqi militias on U.S. positions in the country, amid the Israel-Hamas war in Gaza, threaten to undermine the recent security gains made in Iraq.

Turkey-PKK conflict:

The Turkish army maintains a presence in Iraqi Kurdistan, where it conducts operations against the PKK with minimal response from either the central Iraqi government or the regional government. The latter is currently plagued by internal tensions between rival factions, with the dominant Kurdistan Democratic Party (KDP) accused by the Patriotic Union of Kurdistan (PUK) of supporting Turkey. These divisions are further intensified by the approaching regional elections.

Trump Second-Term Strategy:

Trump is likely to bring a U.S. strategy aimed at countering Iranian influence in Iraq by disarming Iranian-backed militia, prioritizing sanctions and financial intelligence over military intervention. His administration will leverage economic measures to target Iran-backed militias and disrupt Iraq's oil sector. Iraq's leaders will navigate a transactional relationship with Washington, with their alignment with Tehran becoming a key factor in U.S. assessments, as the U.S. works to curb Iran's influence without resorting to direct military action.