Medium Term Debt Management Strategy

Ministry of Finance, Iraq

Abbreviation of Acronyms

ATM	Average Time to Maturity
IMF	International Monetary Fund
CBI	Central Bank of Iraq
CPI	Consumer Price Index
ID	Iraqi Dinar
IDPs	Internally displaced persons
GDP	Gross Domestic Product
MTDS	Medium Term Debt Management Strategy
USD	United State Dollar

Introduction

The debt management for 2015 and 2016 exclusively focused on finding funding sources, domestic and external, to finance the overwhelmingly large size of the fiscal deficit, -12.3% of GDP in 2015 and -%13.8[1] in 2016. The large deficit of the last two years was brought about by falling oil price US$ 42.8 per barrel in 2016 and the invasion by ISIS[2].

Against this situation, the government took an immediate action to curtail public expenditure. In fact, the government expenditure was curbed from 48% of GDP in 2013 to 41.5%[3] in 2016. However, protracted low oil prices and depleted domestic liquidity in the banking sector forced the government to resort to indirect monetary operation by the Central Bank of Iraq to finance the budget deficit.

This 2017 MTDS is a plan that the Iraqi government intends to implement over the medium term (i.e. ([5] years) in order to (i) provide financing of the government fiscal deficit at the lowest cost and the acceptable level of risk; (ii) achieve a desired composition of the government debt portfolio in accordance with the objective of debt management of the government; and (iii) develop the domestic debt market, namely reducing and eventually eliminating the government's reliance on indirect monetary financing and issuing longer denominated government securities.

The Objective of Debt Management

The main objective of public debt management at the Ministry of Finance is to ensure that the gross financing needs of the government are timely met at the lowest possible cost, and also to ensure a reasonable degree of risk, to keep the ratio of public debt to GDP within a reasonable level while reducing the cost of borrowing, taking also into account the stability of current quasi-US dollar pegged foreign exchange rate regime .

The second objective of the public debt management lies in promoting the primary market of the government securities by expanding liquidities, diversifying investor base and instruments and improving market infrastructure, thereby supporting the development of liquid bond secondary market.

The Scope of the Public Debt

The medium term debt management strategy applies to public and publicly guaranteed debt of the central government, but excludes foreign debts before 1990, which are unsettled yet in the framework of the Paris Club agreement.

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[1] Estimated from Iraqi Authorities and IMF.
[2] The oil price data is taken from the Iraqi authorities.
[3] Estimated from Iraqi Authorities and IMF.

Table 1. Macroeconomic Indicators and Public Debt

	2010	2011	2012	2013	2014	2015 [1]	2016 [1]
Real GDP (% change)	5.9	8.6	13.9	7.6	0.7	4.8	11.0
Non-oil real GDP (% change)	9.7	5.7	15.0	12.4	-3.9	-9.6	-8.1
GDP (in ID trillion)	158.5	211.3	254.2	273.6	273.6	209.7	202.7
GDP (in US$ billion)	135.5	180.6	218.0	234.6	234.7	179.8	171.7
Consumer price inflation (% change; period average)	2.4	5.6	6.1	1.9	2.2	1.4	0.4
Exchange rates	1170.0	1170.0	1166.0	1166.0	1166.0	1167.0	1180.0
Total public debt (US billion)	70.8	73.4	75.7	73.1	75.2	98.0	114.6
Total public debt (% to GDP)	52.3	40.6	34.7	31.2	32.0	55.1	66.9
o/w foreign-currency denominated	45.0	33.8	28.3				
External debt (US billion)	60.9	61.0	60.3	59.3	58.1	66.1	67.5
External debt (% to GDP)	44.9	33.8	27.7	25.3	24.8	36.8	39.3
External debt (% to international reserves)	120.4	99.8	87.0	76.2	87.1	123.1	149.3
Effective Interest Rate	..	2.6	1.6	1.1	0.8	1.5	1.2
Interest payment in ID (government expenditure)	0.8	1.6	1.0	1.0	0.7	1.3	1.4
Domestic debt (US billion)	9.9	12.4	15.4	13.8	17.1	27.1	47.1
Current account balance to GDP in %	3.0	12.5	6.7	1.1	2.6	-6.5	-8.7
Gross international resrves (US billions)	50.6	61.1	69.3	77.8	66.7	53.7	45.2
Oil production (mbpd)	2.4	2.7	3.0	3.0	3.1	3.7	4.6
Iraqi Oil price (US$ pb)	79.0	104.0	105.0	102.9	96.5	45.9	35.6
Oil Exports (mbpd)	1.9	2.2	2.4	2.4	2.6	3.4	3.8

Source: the Ministry of Finance and IMF

Notes:

1. 2015 and2016 figures are estimated by Iraqi Authorities and IMF.

Table 2. Public Finance - Central Government

	2010	2011	2012	2013	2014	2015 [1]	2016 [1]
			Fiscal Account (tn ID)				
Gavernment: revenue and grants	73.6	104.6	119.4	115.4	104.4	63.5	55.5
Revenue	68.9	102.4	119.4	115.4	104.4	63.5	55.5
Oil revenue	59.9	93.4	109.4	105.7	98.5	57.7	47.2
Grant	4.7	2.1	0.0	0.1	0.0	0.0	0.0
Government: expenditure	80.3	94.3	109.0	131.2	119.0	89.3	84.1
Current expenditure	56.2	66.8	75.5	83.7	69.9	57.6	61.1
Capital expenditure	24.1	27.4	33.6	47.6	49.2	31.6	16.6
Overall fiscal balance [2]	-6.7	10.3	10.4	-15.8	-14.6	-25.8	-28.6
Financing	7.6	-7.0	-9.3	17.2	18.8	26.4	28.6
External financing	4.6	-11.2	-3.6	12.7	5.9	3.3	2.1
Domestic financing	3.0	4.2	-5.8	4.5	12.9	23.0	26.5
			Fiscal Accounts (% of GDP)				
Gavernment: revenue and grants	46.4	49.5	47.0	42.2	38.2	30.3	27.4
Revenue	43.5	48.5	47.0	42.2	38.2	30.3	27.4
Oil revenue	37.8	44.2	43.0	38.6	36.0	27.4	23.3
Grant	3.0	1.0	0.0	0.0	0.0	0.0	0.0
Government: expenditure	50.7	44.6	42.9	48.0	43.5	42.6	41.5
Current expenditure	35.4	31.6	29.7	30.6	25.5	27.5	30.1
Capital expenditure	15.2	13.0	13.2	17.4	18.4	15.1	8.2
Others	0.0	0.0	0.0	0.0	0.0	0.0	3.2
Overall fiscal balance	-4.2	4.9	4.1	-5.8	-5.3	-12.3	-8.2
Financing	4.8	-3.3	-3.7	6.3	6.9	12.2	8.2
External financing	2.9	-5.3	-1.4	4.6	2.2	2.0	-0.8
Domestic financing	1.9	2.0	-2.3	1.7	4.7	10.2	9.0
Overall fiscal balance (% to GDP)	-4.3	4.9	4.1	-5.8	-5.4	-12.3	-8.2

Notes:

1. 2015 and2016 figures are estimated by Iraqi Authorities and IMF.
2. The difference between overall fiscal balance and financing is statistical errors.

Source: the Ministry of Finance and IMF

Table 3. External Debt (mn US$)

	2014	2015	2016
Total External Debt Outstanding and Disbursed (mn US$)			
Total external debt	58,100	66,100	67,500
Of which,			
Restructured Paris Club Debt	7,437	6,602	5,979
Restructured Non-Paris Club	2,379	2,212	2,045
Commercial Debt Swap (bond)	2,790	2,790	2,790
Small Commercial Creditors	769	769	769
Arab Monetary Fund (AMF)	246	197	153
Commercial Debt- Japanese Creditors	78	72	68
JICA	1,427	1,730	2,282
World Bank	574	1,771	1,789
IBRD	238	1,421	1,445
IDA	336	350	344
Italy	0	45	45
IMF	737	1,297	2,510
Total External Debt Outstanding and Disbursed: Creditor Composition (%)			
Total external debt	100.0	100.0	100.0
Paris Club Debt	12.8	10.0	8.9
Restructured Non-Paris Club	4.1	3.3	3.0
Commercial Debt Swap (bond)	4.8	4.2	4.1
Small Commercial Creditors	1.3	1.2	1.1
Arab Monetary Fund (AMF)	0.4	0.3	0.2
World Bank	1.0	2.7	2.7
IBRD	0.4	2.2	2.1
IDA	0.6	0.5	0.5
Japan	2.5	2.6	3.4
Italy	0.0	0.1	0.1
IMF	1.3	2.0	3.7

Source: the Ministry of Finance and JICA.

Recent Macroeconomic Development

A sharp fall in oil price from US$ 102.9 in 2013 to US$ 22 in 2016 severely hit on and resulted in subsequent steep slow-down of the Iraqi economy where the oil accounts for more than 90% of the government revenue and exports. Moreover, the ISIS attacks starting in 2014 affected more than 10 million of Iraqi, a quarter of the total population and endangered the security of oil sites on the western border of the country, leading further slow-down of the economy, adding further cost on international trade and weakening investor sentiment in the financial market. In 2014, the Iraqi economy recorded 0.7% of real GDP growth rate, the lowest since the war in 2003 ended.

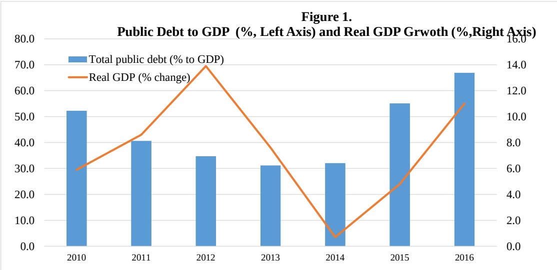


Figure 1.
Public Debt to GDP (%, Left Axis) and Real GDP Grwoth (%,Right Axis)

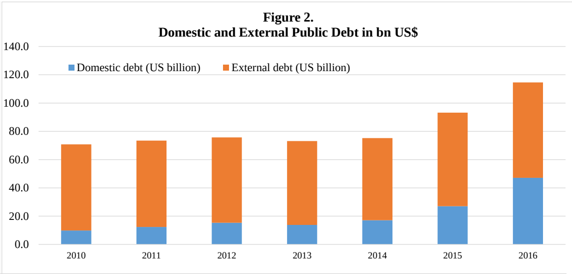


Figure 2.
Domestic and External Public Debt in bn US$

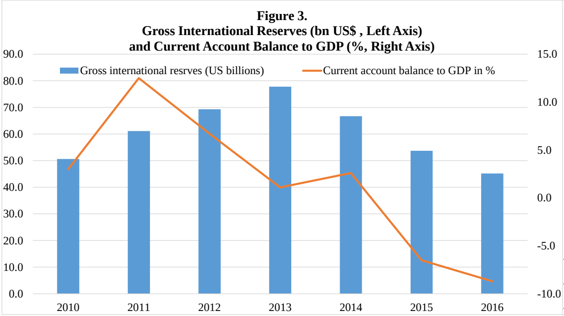


Figure 3.
Gross International Reserves (bn US$, Left Axis)
and Current Account Balance to GDP (%, Right Axis)

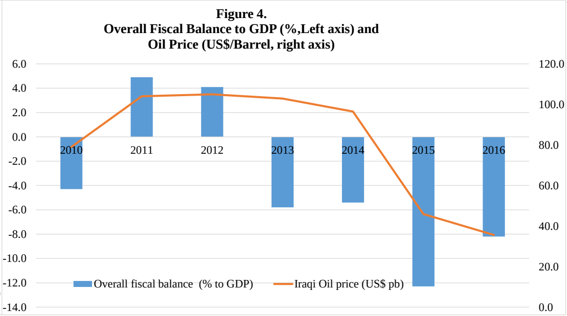


Figure 4.
Overall Fiscal Balance to GDP (%,Left axis) and
Oil Price (US$/Barrel, right axis)

A plummeting oil revenue and mounting fiscal pressures derived from the fight against the ISIS and internally displaced persons (IDPs) overwhelmed a cut down of the fiscal expenditures by the government and led the government to a widening fiscal deficit greater than 10% of GDP in 2015. As a consequence, the total public debt increased rapidly from 32.0% of GDP in 2014 to 66.9% at the end of 2016.

A sluggish export tuned current account into deficit in the balance of payments, -6.5% of GDP in 2015 for the first time since 2005. As a consequence, a downward trend in gross international reserves was further intensified, falling from US$ 66.7 billion, 10.9 months of imports, in 2014 to US$ 45.2 billion (estimate), 6.7 months of import in 2016.

In 2016, the Iraqi economy has bounced back with oil production and exports rising from 3.7 mbpd[4] in 2015 to 4.6 mbpd in 2016 and from 3.4 mbpd to 3.8 mbpd, respectively with a tailwind of gradual recovery in oil price. However, the profound and adverse impact of two shocks, namely, the fight against the ISIS and the sharp downturn of oil price, are projected to continue to affect the country in public finance, gross international reserves and debt management.

[4] "mbpd" indicates million barrels per day.

Current Debt Portfolio Analysis

External Debt

The external debt was on steady downward trend to 24.8% of GDP in 2014. However, external debt outstanding switched to the upward trend up from US$ 58.1 billion in 2014 to US$ 67.5billion (39.3% of GDP) in December 2016.

An increase in external debt from 2014 to 2016 reflects US$ 2.7 billion and US$ 1.8 billion disbursements by the World Bank and IMF, respectively in response to rapidly deteriorating public finance of the government. As a consequence, the share of the World Bank and IMF in total external debt more than doubled from1.0% to 2.7% and 1.3% to 3.7% between 2014 and 2016.

The restructured Paris Club debt as of end of December 2016 stands US$6.0 billion, accounting for 8.9% of the total external debt. As a bilateral sovereign creditor, Japan stands the largest with 3.4%[5]of the total external debt[6].

Investor Base: The Iraqi external debt portfolio has a high concessional investor base. In fact, international institutions and bilateral creditors including debt applied with the Paris Club framework account for 81.1%[7] of the total debt portfolio at the end of 2016. The Paris Club restructured debts have long repayment periods, mostly up to 2028 or even longer, indicating that they are highly concessional.

Moreover, the creditor base for the Paris Club restructured debt is well diversified with more than 15 sovereign creditors to whom the Iraqi owns more than US$ 100 million. The effective interest rate for the Paris Club restructured debt is 3.2%, very low. However, it has to be noted that some of the Paris Club restructured debt have a higher effective interest rates such as 5.4% for Belgium and 5.6% for Russia.

Refinancing Risk: Average time to maturity (ATM) is 15.7 years. A relatively longer ATM reflects a highly concessional portfolio and large share of sovereign bilateral creditors, the World Bank and the IMF. Moreover, the share of debt maturing in 2017 is very low, 1.5% of the total external debt. These indicators suggest that refinancing risk is relatively low as of the end of 2016. However, over the five-year horizon, the repayment profile is projected to gradually go up, hit the peak around 2020 and subsequently go down slightly. The refinancing risk is projected to be higher at the later period of the MTDS horizon.

Table 4. Restructured External Debt Currency Composition (in %)

Currency	2011	2012	2013	2014	2015
Totald debt	100.0	100.0	100.0	100.0	100.0
USD	45.6	52.4	49.6	54.3	56.2
EUR	19.7	22.3	20.7	19.0	15.0
JPY	20.8	19.9	15.9	17.6	17.6
GBP	2.1	2.4	2.2	2.2	1.8
Others	11.8	3.0	11.5	6.9	9.4

Note: Others include Sweeden Crona, Swiss Franc, SDR and others.

Foreign Exchange Risk: The US dollar dominates 56.2% of the currency composition of the external debt, followed by Japanese Yen, 17.6% and by the Euro, 15% in 2015. Since the Iraqi dinar is quasi-pegged with US dollar, currency risk is expected relatively low and the Iraqi external debt portfolio is

[5] This figure includes Japanese commercial creditors.
[6] This figure includes Paris Club restructured debt.
[7] International institutions and bilateral creditors include Paris Club Debt, Restructured Non-Paris Club, the World Bank, IMF, Japan and Italy, excluding US$41 billion of non-Paris Club creditor which have not agreed with Paris Club term settlement.

resilient to a rise in interest rates by the US Federal Reserve Bank expected in 2017 and 2018.

While foreign exchange risk is relatively low, it has to be noted that the gross international reserve, which support quasi-pegged Iraqi dinar, has been rapidly falling from US$ 77.8 billion in 2013 to less than two third in 2016 in spite of the fact that the sale of foreign exchanges by the CBI was restricted[8]. Consequently, foreign exchange risk at the later stage of the MTDS horizon will hinge on the level of international reserves and therefore, oil prices.

Interest rate risk: Average time to refixing external debt (ATR) is 15.1 year in 2016. The share of debt refixing in 1 year for external debt is 11.5% in 2016, reflecting variable rate debt accounting for 10.2% of the total external debt. The share of the variable rate debt has been on the rise in 2015 and 2016[9], indicating rising interest risk. Interest risk will be elevated for upcoming US Fed monetary tightening phase. While a large share of variable rate debt has been rising, effective interest rates for external debt are 3.0%[10] in 2016, very low and much lower than the current Iraqi risk premium higher than 700 bp as of end of 2016.

Domestic Debt

Iraqi domestic debt amounts to ID 46.6 trillion (US$ 39.5 billion) at the end of December 2016, jumping from ID 31.9 trillion (US$ 27.1 billion) in 2015. The domestic debt grew much faster than external debt from 2014 to 2016. The part of this increase in domestic debt is attributed to indirect monetary operation, i.e., issuing T-bills, which are first purchased by Rafidain Bank and Rasheed Bank, which are the state owned banks, and then sold to the Central Bank of Iraq at a discounted price. In the middle of rapidly deteriorating public finance and sentiment of the international capital market toward Iraq, overwhelming financial needs forced the government to resort to this indirect monetary operation, which reached 34.6% of total domestic debt in December 2016.

Investor Base: Rafidain Bank, Rasheed Bank, the Trade Bank of Iraq and the Central Bank of Iraq account for 59.0%[11] of the total domestic debt at December 2016. Rafidian and Rasheed banks which account for 71% of bank's deposits are major investors in government debt market. Investor base for domestic instrument is relatively small in size and less diversified.

Re-financing Risk: Short-term debt accounts for 96.6% of the domestic debt in 2016. However, a majority of the government securities held by Rafidain Bank, Rasheed Bank, the Trade Bank of Iraq and the Central Bank of Iraq are automatically rolled over by agreement between the Ministry of Finance and these banks without formal auction process. Therefore, the share of short-term debt is high but actual refinancing risk is much less than the indicator suggests. It also has to be noted that the Government of Iraq started to issue government bonds which has a maturity longer than one year from August 2016 and the government long term bonds accounts for 3.4% of total domestic debt in 2016.

[8] The part of the reason for the restriction on sale of foreign exchange including the limit to foreign exchange sale per day by the CBI lies in the concern that these foreign exchanges can be used to finance terrorism and illegal activities. However, the CBI has mitigated these restrictions on foreign exchange sales since August 2016.

[9] The rise of variable debt is attributed to a large borrowing from the World Bank, IMF and JICA in 2016.While their lending is variable rates, concessionality is very high with interest rate much lower than market rates and longer maturity including grace periods.

[10] This excludes US$41 billion of non-Paris Club creditor which have not agreed with Paris Club term settlement.

[11] This figure is taken from the MOF.

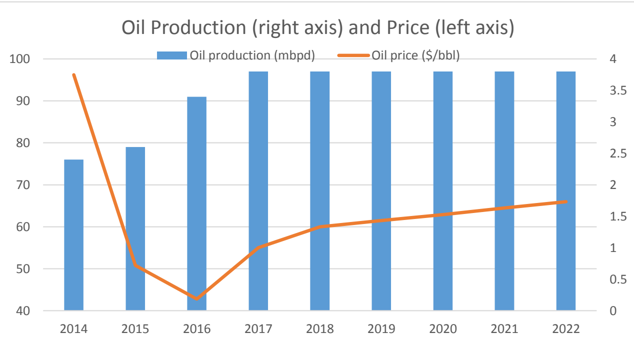
Table 5. Domestic Public and Publicly Guaranteed Debt in bn ID

Debt Instruments	2014	2015	2016											
			Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Total dometic public and publicly guaranteed deb (bn ID)														
Total domestic debt	19,958	31,925	34,425	36,810	38,194	38,579	38,675	40,675	41,044	42,069	43,098	44,456	44,636	46,575
T-bills -Auctions	2,119	348	348	733	1,117	1,502	1,598	1,598	1,966	2,348	2,424	2,382	2,562	2,501
T-bills discounted from the CBI, Rafidein and Rasheed	0	6,225	8,225	10,225	11,225	11,225	11,225	13,225	13,225	13,225	13,225	14,725	14,725	16,725
T-bills Old debt by the CBI	2,456	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356	2,356
T-bills from TBI	0	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
T-bills to finance projects and deficit	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837	4,837
T-bills according to budget law (Funding the Defense Ministry)	0	0	0	0	0	0	0	800	800	800	800	800	800	800
T-bills deducted from the legal reserve	0	4,353	4,353	4,353	4,353	4,353	4,353	4,353	4,353	4,353	4,353	4,218	4,218	4,218
Bonds (Extradition term dollar bonds)	0	15	15	15	15	15	15	15	15	15	15	15	15	15
National Bonds	0	0	0	0	0	0	0	0	0	643	643	643	643	643
Bonds pay dues of farmers	0	0	0	0	0	0	0	0	0	0	953	953	953	953
Electricity Loans [1] and other loans from TBI	703	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035	3,035
Loans by SOEs guaranteed by the central government from Rafidein and Rasheed	9,844	9,557	9,557	9,557	9,557	9,557	9,557	9,557	9,557	9,557	9,557	9,592	9,592	9,592
Publicly guaranteed debt			500	500	500	500	500	500	500	500	500	500	500	500
Short-term debt	19,958	31,911	33,911	36,296	37,680	38,065	38,161	40,961	41,329	41,711	41,787	30,518	30,698	32,637
Medium-long term debt	0	15	15	15	15	15	15	15	15	658	1,611	1,611	1,611	1,611
Total domestic debt (Million Dollar)	17,115	27,084	28,779	30,800	31,974	32,300	32,364	34,754	35,066	35,935	36,807	37,675	37,827	39,470
(% of total dometic public and publicly guaranteed debt)														
Total domestic debt	100	100	100	100	100	100	100	100	100	100	100	100	100	100
T-bills -Auctions	10.6	1.1	1.0	2.0	2.9	3.9	4.1	3.9	4.8	5.6	5.6	5.4	5.7	5.4
T-bills discounted from the CBI, Rafidein and Rasheed	0	19.5	23.9	27.8	29.4	29.1	29.0	32.5	32.2	31.4	30.7	33.1	33.0	35.9
T-bills Old debt by the CBI	12.3	7.4	6.8	6.4	6.2	6.1	6.1	5.8	5.7	5.6	5.5	5.3	5.3	5.1
T-bills from TBI	-	3.8	3.5	3.3	3.1	3.1	3.1	3.0	2.9	2.9	2.8	2.7	2.7	2.6
T-bills to finance projects and deficit	24.2	15.2	14.1	13.1	12.7	12.5	12.5	11.9	11.8	11.5	11.2	10.9	10.8	10.4
T-bills according to budget law (Funding the Defense Ministry)	0	0	0	0	0	0	0	2.0	1.9	1.9	1.9	1.8	1.8	1.7
T-bills deducted from the legal reserve	0	13.6	12.6	11.8	11.4	11.3	11.3	10.7	10.6	10.3	10.1	9.5	9.4	9.1
Bonds (Extradition term dollar bonds)	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
National Bonds	0	0	0	0	0	0	0	0	0	1.5	1.5	1.4	1.4	1.4
Bonds pay dues of farmers	0	0	0	0	0	0	0	0	0	0	2.2	2.1	2.1	2.0
Electricity Loans [1] and other loans from TBI	3.5	9.5	8.8	8.2	7.9	7.9	7.8	7.5	7.4	7.2	7.0	6.8	6.8	6.5
Loans by SOEs guaranteed by the central government from Rafidein and Rasheed	49.3	29.9	27.8	26.0	25.0	24.8	24.7	23.5	23.3	22.7	22.2	21.6	21.5	20.6
Publicly guaranteed debt	0	0	1.5	1.4	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.1	1.1	1.1
Short-term debt	100.0	100.0	98.5	98.6	98.7	98.7	98.7	100.7	100.7	99.1	97.0	68.6	68.8	70.1
Medium-long term debt	0	0	0	0	0	0	0	0	0	1.6	3.7	3.6	3.6	3.5

Source: The Ministry of Finance

Interest Rate Risk: Effective interest rates are 2.6%, very low in 2016 while the policy rate of the CBI is 4%. However, considering that short-term debts account for a large share of domestic debt, the interest hike will have significant impacts on Iraqi interest payment in future.

Outlook over the MTDS Horizon:



Source: Oil production from IMF and Iraqi authority and oil price from the World Bank as of February 2017

Over the five-year horizon from 2017 to 2022, oil prices are projected to recover gradually from US$ 49.0 per barrel in March 2017 to US$ 54.8 in 2021[12]. With stable oil production at 4.6 million barrels per day and implementation of fiscal consolidation, fiscal balance is expected to turn to surplus in 2020 from -12.3% of GDP in 2015. However, the government finance is projected to still need indirect monetary operation by the Central Bank of Iraq even at the later period of the MTDS horizon although the size of the needed operation is much smaller than 2016.

[12] The projection by the IMF as of July 2017 - http://www.imf.org/external/np/res/commod/index.aspx .

Medium-Term Debt Management Strategy

The first priority of the MTDS for 2017-2021 lies in reducing indirect monetary operation, which mounts to ID 16.2 trillion[13] in the end of 2016. The reduction in indirect monetary operation must be implemented in a way that it does not adversely affect meeting debt service. Accordingly, the government will focus first on finding external budget support loans from bilateral and multilateral sources and then, second on market-based borrowing in the international financial market including Euro bonds. The downside of this strategy is a rise in the variable rate debt component since borrowings for 2017-2021 from multilateral institution such as the World Bank and IMF are mainly in the form of variable rates, which may increase interest risk as the US Federal Reserve Bank raises interest rates in near future. The impact of interest rate hike has to be carefully monitored.

Secondly, investor base for domestic debt has to be diversified to reduce heavy dependency on Rafidain Bank, Rasheed Bank, the Trade Bank of Iraq and the Central Bank of Iraq. This is a medium-term target rather than short-term target in order to achieve a more stable funding base. One of the instruments being considered is to issue Sukuk, Islamic bonds, to tap into the unexploited liquidity available in Islamic banks in both domestic and more importantly international markets.

Furthermore, a significant share of the government securities held by financial public institutions are currently automatically rolled over without formal redemption and auction process. The government has a plan to gradually consolidate these debt by replacing them based on formal auction in order to improve transparency in the bond market.

In the domestic market, the government issues securities mainly at the short-end. The short-term securities account for more than 90% of T-bills and bonds with relatively low effective interest rates, 2.6%, which suits to government pending needs to reduce current expenditures. This strategy is justified in a short-run. However, refinancing risk will be high if this strategy is pursued in a long-run. As fiscal balance improves in a medium term, the government needs to shift to issuing bonds longer than one-year maturity not only to control refinancing risk but also to diversify the borrowing instruments and to promote primary government bonds markets.

The government of Iraq will continue to negotiate with creditors to reach the agreement on old debt unsettled yet in Paris Club terms. The Iraqi government realized that settling down these debts is critical to improve its credit rating and so funding conditions.

The government of Iraq also intends to redeem or roll over gradually its borrowing from the reserve requirement at the Central Bank of Iraq, which stands ID 4.2 trillion in 2016. The government has a plan to gradually consolidate these debt.

Finally, choices of interest rates, “variable or fixed” and that of the maturity, “short-term or long-term” still heavily depend on specific market conditions at the time of borrowing. On one hand, a rise of the US interest rates is expected in the first half of the MTDS horizon, which is expected to increase interest rate risk. On the other hand, outlook of the risk premium for the Iraqi debt is projected to improve if the oil price rises and the fight against the ISIS subsides.

[13] This figure is taken from the Ministry of Finance.

Summary of Borrowing Strategy

1. Reduce indirect monetary operation.
2. Find external concessional borrowing for budget support loans as the first borrowing priority.
3. Find external low interest rate loans and borrowing for financing projects through official creditors.
4. Find external non-concessional borrowing including Eurobonds as a second priority.
5. Find external non-concessional borrowing guaranteed by export credit agencies for financing projects as second priority.
6. Set the ceiling for sovereign guarantee in the public budget law to be submitted by the ministry of finance to SOEs.
7. Diversify the instruments as well as investor base, issuing Sukuk and Eurobonds.
8. Reduce automatic roll-over through consolidation of the debt or restructuring to improve transparency of the bond primary market.
9. Elongate the maturity of domestic government securities to promote government bond market.
10. Follow up the negotiation to reach the bilateral agreement on the unsettled legacy debt in Paris Club terms.
11. Reduce using the legal reserves for financing government deficits.

Note: Decision on the maturity and interest rate choices depends on specific market condition at the time of borrowing.