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IRAQ RECONSTRUCTION: WITHOUT ADDITIONAL FUNDING, PROGRESS LIKELY TO FALL SHORT, UNDERMINING WAR EFFORT

By Steven M. Kosiak

Over the past three years, the United States has appropriated about \$220 billion for military operations in Iraq and \$29 billion for Iraqi reconstruction and security assistance.¹ Of this latter funding, some 80 percent has already been obligated (i.e., committed by contract to particular projects), and more than half of it spent. Unfortunately, while substantial progress has been made in some sectors, in many areas Iraq remains far short of achieving the relatively modest goals set out for reconstruction in the immediate aftermath of the US invasion in 2003.

Unless the United States provides additional funding, reconstruction-related activities in Iraq are likely to slow considerably over the next several years, and many of these goals will be left unmet. It is difficult to determine how much additional funding would have to be provided to complete all or most of the objectives for reconstruction identified after the invasion. However, a reasonable estimate is that some \$18-28 billion or more is required. Even assuming, perhaps optimistically, that this gap could be covered by drawing equally upon US, international and Iraqi resources, this suggests that an additional \$5-10 billion in US reconstruction assistance might need to be provided.

This is far more than the \$2.2 billion the Bush Administration has included for Iraqi reconstruction in its recently submitted fiscal year (FY) 2007

¹ These estimates include all funding appropriated to date. They do not include funding requested for Iraq in the Bush Administration's recently submitted FY 2006 supplemental request for military operations. For a discussion of DoD funding for military operations to date, see Steven M. Kosiak, "The Cost of US Military Operations in Iraq and Afghanistan Through Fiscal Year 2006 and Beyond," CSBA, January 3, 2006.

budget request (\$700 million)² and FY 2006 supplemental appropriations request (\$1.5 billion).³ However, it is far less than the administration has requested to support military operations in Iraq in 2006. The Department of Defense (DoD) is likely to be provided a total of some \$120 billion in special war-related funding in 2006.⁴ Of this total, as much as \$85 billion appears to be related to conducting US military operations in Iraq. Given the critical importance to the war effort of winning the “hearts and minds” of the Iraqi people, and the generally strong support among Iraqis for reconstruction-related assistance,⁵ such a lop-sided approach seems, at best, risky.

Ultimately, even if US force levels are substantially reduced, the United States is likely to spend some \$100-200 billion more on military operations in Iraq over the next several years.⁶ It would be unfortunate—but far from inconceivable—if this treasure, as well as thousands of American lives, were squandered and the war lost, because the United States proved unwilling to invest even a small fraction of that amount to help complete reconstruction efforts in Iraq. Providing additional funding for reconstruction will certainly not guarantee success. But without this relatively small additional investment in reconstruction, the odds of success may be substantially lower than they would otherwise be.

The Cost of Reconstruction—Initial Estimates

In an October 2003 assessment, the World Bank and United Nations estimated that Iraq would need some \$55 billion for reconstruction and stabilization efforts over the FY 2004-07 period.⁷ This level of funding was expected to be sufficient to restore Iraqi infrastructure (e.g., electricity, water

² Department of State FY 2007 budget request, p. 459, www.state.gov/documents/organization/60654.pdf

³ Joshua B. Bolton, Director of the Office of Management and Budget (OMB), “Request for FY 2006 Supplemental Appropriations,” February 16, 2006.

⁴ This includes \$50 billion provided in the FY 2006 defense appropriations act and some \$70 billion included in the administration’s recently submitted FY 2006 supplemental request for military operations.

⁵ Michael O’Hanlon and Nina Kamp, “Iraq Index: Tracking Variables of Reconstruction & Security in Post-Saddam Iraq,” February 13, 2006, www.brookings.edu/iraqindex, p. 40.

⁶ Kosiak, pp. 8-9.

⁷ For a discussion of various initial estimates of the cost of Iraqi reconstruction, including the World Bank/UN assessment, see Eric J. Labs, *Paying for Iraq’s Reconstruction* (Washington, DC: CBO, January 2004). For the text of the *United Nations/World Bank Joint Iraq Needs Assessment* (October 2003), see, www.sitersources.worldbank.org/INTRAQ/Overview/20147568/Joint%20Needs%20Assessment.pdf

and sanitation, transportation, and oil industry) to its state prior to the 1991 Gulf War and provide a foundation for further economic, social and political development. The estimate included \$35.8 billion for reconstruction requirements identified through an independent survey, plus \$19.4 billion for other needs identified by the Coalition Provisional Authority (CPA).⁸ The total included about \$50 billion for the reconstruction of key areas of infrastructure and \$5 billion for training and equipping Iraqi security forces. This estimate has, unfortunately, proven to be overly optimistic. For a variety of reasons, it is likely that substantially more funding will be needed to meet the 2003 reconstruction targets.

The Cost of Instability and Other Factors

According to a 2005 report by the Office of the Special Inspector General for Iraq Reconstruction (SIGIR), a survey of about 100 reconstruction projects indicated that actual costs have typically exceeded initial estimates by some 20-85 percent.⁹ Even applying this lower multiplier to the initial cost estimates for Iraq's reconstruction, and excluding funding for Iraqi security forces, the SIGIR data suggest that at least \$60 billion would be needed to complete the reconstruction projects outlined in 2003, rather than the \$50 billion projected by the World Bank, the UN and the CPA.

Although this cost growth stems from a range of factors, the most important cause is almost certainly the unanticipated level of violence and instability that has taken hold and persisted throughout much of Iraq. Since the initial estimates of Iraqi reconstruction costs were made at the end of 2003, the security environment has dramatically worsened. During the summer of 2003, when the initial cost estimates were being generated, attacks on US and Coalition forces averaged only about 15 a day. However, by May 2004 the number of attacks had reached some 65 a day, and they have remained near or above that level in most months since then.¹⁰

As a result of the poor security situation, many existing areas of infrastructure, as well as completed reconstruction projects, have been subject

⁸ The CPA, constituted by the United States and the United Kingdom, was recognized by the UN as the authority responsible temporarily for the governance of Iraq between May 2004 and June 2004, when it was replaced by Iraqi interim government.

⁹ SIGIR, *Report to Congress*, April 30, 2005, pp. 75-76.

¹⁰ Joseph A. Christoff, Director, International Trade Division of the Government Accountability Office (GAO), testimony before the Senate Committee on Foreign Relations, "Rebuilding Iraq: Stabilization, Reconstruction and Financing Challenges," February 8, 2006, p. 6.

to sabotage, theft and vandalism. For example, in 2004 nearly 1,200 electrical towers were toppled in Iraq.¹¹ The violence and fear of violence has also caused many aid workers to flee the country, and substantially impaired the ability of many of those remaining to work efficiently and effectively. In addition, security concerns have caused managers of reconstruction projects to devote substantially greater resources to protecting their workers, equipment and facilities than had been originally projected. According to State Department data, security costs now represent 16-22 percent of the overall cost of major infrastructure projects in Iraq.¹²

The heightened level of violence in Iraq has probably been the greatest factor leading to delays and cost growth in reconstruction efforts. But it has not been the only factor. Some sectors of the Iraqi economy and infrastructure were more severely degraded, as a result of more than a decade of sanctions, than had been initially expected. Management problems and corruption have also contributed to delays and cost growth.

US and International Reconstruction Assistance

Over the past three years, the United States has provided Iraq with about \$29 billion in reconstruction and security assistance. Other countries and international organizations have pledged another \$13.9 billion in reconstruction assistance (primarily loans), bringing the total to some \$43 billion. This is substantially less than the \$55 billion initial estimate of reconstruction costs made by the World Bank, the UN and the CPA. Moreover, the gap is much greater if aid for training and equipping Iraqi security forces is excluded.

Reflecting the unanticipated worsening of the security situation, Iraq's nascent security forces have absorbed a substantially higher share of the assistance provided to Iraq than had been initially projected. Altogether, equipping and training assistance to Iraqi security forces has accounted for 38 percent, or \$11 billion, of US aid to Iraq over the past three years.¹³ Thus, of the \$43 billion provided or pledged by the United States and other countries, only some \$32 billion has been for reconstruction. This suggests a gap of some \$18 billion between initial estimates of reconstruction costs (\$50 billion) and US and other foreign assistance. The gap would grow to some \$28 billion if, as

¹¹ Curt Tarnoff, "Iraq: Recent Developments in Reconstruction Assistance," Congressional Research Service (CRS), January 4, 2006, p. 14.

¹² GAO, p. 8.

¹³ The FY 2006 supplemental appropriations request includes \$3.7 billion in additional assistance for Iraqi security forces.

discussed in the preceding section of this analysis, it is assumed that actual reconstruction costs will be at least 20 percent higher (i.e., around \$60 billion).

Iraqi Resources for Reconstruction

In theory, this funding gap could be filled by the Iraqi's themselves. Prior to the US invasion in March 2003, it was anticipated by some that Iraq, because of its massive oil deposits, would be largely able to finance its own reconstruction. For a variety of reasons, however, this has turned out not to be the case. And it seems doubtful that Iraq will, at least over the near or medium term, be able to contribute the level of resources needed to close the substantial gap that appears to exist between current aid levels and projected reconstruction costs.

Iraq's oil production infrastructure was badly degraded during the 1990s, and has been subjected to frequent insurgent attacks over the past three years. As such, despite major efforts (including substantial US assistance) to repair and rebuild this infrastructure, Iraq has not been able to meet its initial goals for exporting oil. Iraq's current oil export capacity is, theoretically, as high as 2.5 million barrels per day.¹⁴ However, after peaking at 1.7 million barrels per day in September 2003, Iraq has only been able to sustain average exports levels of some 1.4 million barrels per day, and the level fell to only about 1.1 million barrels per day in January 2006.¹⁵ As a result, notwithstanding the spike in crude oil prices, Iraqi revenues from oil exports (which account for 90 percent of Iraqi government revenue) have fluctuated considerably, and have actually declined substantially since the fall of 2005.¹⁶

In any event, for the foreseeable future, Iraq's oil revenues will be needed simply to pay the day-to-day costs of operating the Iraqi government, providing social services, supporting and expanding Iraqi security forces, and repairing, rebuilding and expanding the Iraqi oil industry—leaving very little funding available for general reconstruction efforts. Fuel and food subsidies and support for state-owned enterprises reportedly cost the Iraqi government some \$11 billion annually.¹⁷ Iraq is projected to spend over \$5 billion of its own resources on its security forces in 2006.¹⁸ And, according to industry and US

¹⁴ Ibid., p.17.

¹⁵ Brookings, p. 28.

¹⁶ Ibid., p. 29.

¹⁷ CRS, p. 5.

¹⁸ GAO, p. 18.

experts, an estimated \$30 billion will be required over the next five years (i.e., about \$5 billion a year) to expand Iraq's oil production capacity.¹⁹

Taken together, the estimates for these three areas alone suggest total annual costs of some \$20 billion²⁰—just shy of the \$23 billion in oil revenue Iraq received last year.²¹ This does not mean that Iraq should not, and cannot, contribute funding to its own reconstruction efforts. It does, however, suggest that Iraq will be unable to cover more than some fraction of the costs associated with completing the reconstruction projects deemed necessary by the World Bank, UN and CPA. Efforts to reduce subsidies for the Iraqi people and state-supported enterprises might allow the Iraqi government to allocate a greater share of its resources to reconstruction. However, such changes would be difficult to implement politically and, at least if pursued aggressively, might prove counterproductive to US and Iraqi government efforts to win the support of the Iraqi people. In any case, such changes are unlikely to yield substantial savings over the next few years.

Conclusion

Iraqi reconstruction efforts will probably cost substantially more to complete than earlier estimates indicated. Indeed, the analysis above suggests that a gap of \$18-28 billion may exist between likely costs and available funding. It should be possible to cover some of this gap through greater international assistance and by drawing on Iraqi resources. However, if this gap is to be closed, and closed within the next several years—during which time the success or failure of US efforts in Iraq is likely to be determined—it will almost certainly be necessary for the United States to provide additional funding for Iraqi reconstruction.

If this gap were covered by drawing equally upon US, international and Iraqi resources, the US share of additional Iraqi reconstruction assistance would amount to \$5-10 billion. This would represent a significant increase in US reconstruction aid. On the other hand, as noted earlier, it would represent a small fraction of total US costs related to the war in Iraq. And the failure to provide such assistance could fatally undermine the far more costly efforts of US and Iraqi military forces to defeat the insurgency in that country.

¹⁹ Ibid., p. 15. The initial estimate of Iraqi reconstruction costs included \$8 billion for the oil sector over the 2004-7 period, or about \$2 billion a year.

²⁰ The ability of Iraq to contribute to its own reconstruction efforts is also hampered by the need to repay \$84 billion in external debt and war reparations.

²¹ Brookings, p. 28.

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