

**Speech by Deputy Prime Minister Qubad Talabani
CWC Kurdistan Oil and Gas Conference, London
5 December 2016**

Distinguished guest, ladies and gentlemen.

I'd like to warmly thank CWC for inviting me back again this year.

As we approach 2017 I want to outline to you our vision, our plans and our reform initiatives intended to address the many challenges Kurdistan faces today.

Last year, I had the pleasure to address you and I frankly presented to you the challenges of Kurdistan's fiscal and economic situation.

I emphasized how Kurdistan was being tested by political, economic, humanitarian and security crises.

I stressed how the triple shocks of Baghdad cutting our budget in 2014,

the war with ISIS,

the subsequent influx of almost 2m refugees and IDPs into Kurdistan;

And how our cumbersome and ineffective bureaucracy were all contributing to make our fiscal situation unsustainable and in need of major reform.

I then outlined some of the steps that we had undertaken, or had planned to undertake to address our fiscal imbalances and restore our economic growth, including our government's top three reform priorities at that time, which were to :

Restructure government expenses,
Reduce and eventually eliminate petroleum product subsidies
And carry out a major overhaul of our electricity sector.

But almost immediately after last year's conference, we were dealt yet another devastating blow.

Oil prices plummeted even further, and so, the combination of Baghdad cutting our budget, war, the burden of IDPs on our society and economy, our own visible deficiencies, and added to that \$25/barrel oil prices left us with growing debts and monumental fiscal challenges.

In January this year, we had a monthly operational deficit of over \$460m!

So our plans had to be re-examined and we needed to act fast.

And we did.

Urgent austerity measures and continued direct oil exports improved our Government's immediate cash balance, while structural reforms began to tackle the longer-term challenge of transforming the public sector and promoting diversification of the Region's economy.

Recognizing the need for further austerity to close the gap between cash revenues and expenditures on a monthly basis, we announced a new measure to withhold a significant percentage of government salaries, pensions and stipends—excluding Peshmarga and other security forces.

These cuts have been sustained since, reducing the average total monthly payment for salaries, pensions and stipends by more than one-third, from almost \$750m to approximately \$450m US.

Needless to say this decision was very hard to make, and understandably unpopular with our massive civil service workforce.

My Government has also moved to increase non-oil revenues by raising fees, penalties, water charges and electricity tariffs for industrial consumers; as well as by slashing petroleum product subsidies.

The overall result has been an 80% drop in the consolidated fiscal deficit—measured on a cash basis—from 6.5bn US in 2014 to an estimated 1.3bn US in 2016.

But while our austerity program and shift to direct oil sales have substantially narrowed the gap between monthly operating revenues and expenditures, we still continue to struggle to pay monthly salaries, pensions and stipends on time.

Austerity is expected to continue in 2017 with the ultimate goal of generating an operating surplus in order to restore funding for critical public investments and over time to repay government debts, including advances from the banking system.

The lack of financing has exacerbated the social pressures inherent in any crisis response, while scarce technical expertise imposes important hurdles to program design and implementation.

So along with the World Bank, we have prepared a comprehensive roadmap for structural reform in the Kurdistan region.

Within that framework, we have focused on priority areas that include:

1. Institutional Modernization of our Ministry of Economy & Finance (MOEF) to equip the ministry to lead fiscal policymaking and become a driver for reform.

The program covers five reform streams: macro-fiscal, customs, tax, public financial management (PFM), and IT infrastructure and services.

- In the macro-fiscal area, the reform aims to establish a macro-fiscal framework to guide the formulation of annual budgets for the KRG.

A key step will be to prepare a budget for 2017 that sets clear targets for non-oil revenues and resizes expenditure envelopes in line with progress achieved under the austerity program.

- For customs, we have begun to connect customs posts across the KR (Turkish border, airports and Iran border) to improve service standards, expedite customs clearance processes and provide real-time information on revenue collection.

Attention is also being given to improved coordination with the Federal customs authorities.

- In taxation, the priority is to improve tax administration by establishing a new service center for large taxpayers.

This large taxpayer office (LTO) to be set up in 2017 will support a shift in procedure from presumptive taxation to self-assessment in line with international standards. The LTO is expected to promote modernization of the accounting industry in Kurdistan.

- The immediate goal of PFM reform is to strengthen control over public expenditures, while improving management of government liabilities.

As a key step, a new chart of accounts compatible with international standards (GFS) has been prepared and will be put in place in 2017-18.

Regular annual and quarterly reports on the consolidated budget (including both MOEF and MNR operations) will be published starting by the end of 2016.

- Improvements in IT infrastructure and services within MOEF will drive the transition to automation and away from outdated manual procedures.

As such, it will underpin the entire modernization effort by equipping the ministry with an international standard, integrated financial management information system (IFMIS).

2. Biometric Registration of government employees, pensioners and other citizens receiving monthly stipends (e.g., students, families of martyrs).

Rightsizing government stands out as a long-term goal of the KRG's reform program.

Biometric registration represents a first step down this road that answers the question: who are we paying and how much?

This will open the way to more complex questions of 'why and to do what' under subsequent civil service reforms.

The registration process—encompassing government employees, pensioners and beneficiaries of stipends—is now underway after an intensive start-up phase with a three-month window to complete.

After 2 weeks of actual operation, we have today registered over 150,000 government wage earners, so we are on track to meet our targets.

The result will be an Identity Management System that drives broader reform of government payroll, and eventually human resources.

Through this initiative, we will identify those who are unlawfully receiving more than one salary from the government, of which we likely have many.

We will also identify and eliminate ghost employees, of which we surely have many!

This will pave the way to subsequent e-payroll and e-payment systems that will further enhance administrative performance and transparency, as part of the ultimate objective of transitioning to modern e-government services in Kurdistan.

3. On Electricity Sector Reform, we are executing a two-pronged strategy.

The immediate goal is to cut costs and improve financial sustainability, while developing a medium-term reform plan also in cooperation with the World Bank.

Starting in 2015, we have undertaken steps to curtail costs for electricity generation, including:

- (i) a shift in supplying natural gas to the power stations in place of diesel fuel,
- (ii) the introduction of more fuel efficient combined-cycle technology by IPPs, and
- (iii) voluntary renegotiations to lower take-or-pay penalties in light of excess generation capacity.

As a result, total costs have been cut by as much as \$1.5 billion in 2016.

The immediate focus is now shifting to revenue improvement. Tariff adjustments for industrial consumers came into effect in 2016.

However, revenue performance remains very low, hampered by high losses (including theft) and poor collection.

The government intends to turn the situation around in 2017 through a program centered on the introduction of smart metering and more robust billing and collection.

The medium-term reform plan aims to improve and sustain the quality of service for all electricity consumers through a transition to a modern institutional and regulatory framework that:

- (i) clearly delineates generation from transmission and distribution;
- (ii) strengthens financial discipline and energy accountability; and
- (iii) promotes private sector participation and investment in downstream activities.

This transition will encompass a shift to fully cost-reflective tariffs that protect vulnerable groups in line with international practice.

The KRG's ultimate goal is to ensure consumers are provided with better electricity service without recourse to fiscal or quasi-fiscal subsidies.

4. Enhanced Government Transparency and Citizen Engagement to strengthen credibility and build public support for the KRG's programs.

We recognize that enhancing government transparency and citizen engagement are key to building and sustaining popular support for our programs.

Governance is never a popularity contest, and this is particularly true in situations of crisis.

Popular support has to be earned through government actions that strengthen credibility and promote participation.

We are working to step up our citizen engagement and public communications efforts.

A cornerstone is the introduction of international audit of Kurdistan's oil & gas operations.

Contracts with international auditors have now been signed and initial work is underway.

The audits will cover oil exports, IOCs, and domestic operations (e.g., local sales of crude and refined products).

To promote public engagement and awareness, an observatory encompassing key representatives of civil society will be established to follow the audit process and help disseminate the results.

You will receive a special presentation on this initiative later on in the program.

Finally...

5. Reform of the social protection framework aims to deliver on the KRG 2020 Vision to 'put people first'.

It encompasses plans to:

(i) strengthen the labor market—including accelerating private sector job creation,

(ii) expand pensions and social insurance—including introduction of pensions for private sector workers and creation of unemployment insurance, and

(iii) improve the (non-contributory) social safety net—including using poverty as a main determinant of eligibility.

The Social Protection Strategy is a long-term one for KRG that will put in place systems to address the social impact of the current crisis and to respond more effectively to future shocks that may affect the Region.

The new strategic framework has been developed in cooperation with the World Bank, which is now supporting the implementation phase.

We know what needs to be done. Moreover, we know that we must lead these reforms.

Unfortunately, the uncondusive politcal climate in Kurdistan, while not an absolute obstacle to reform, certainly makes implementation more difficult.

To our international partners, we express deep appreciation for the financial and technical support provided to date, including for the Peshmarga.

However, given the extent of the crisis and reforms required, further support is urgently needed in order to increase the odds of success, and alleviate social and other risks.

We welcome guidance and technical expertise from the international community, including learning from other country experiences.

The KRG also remains fully open to engagement and cooperation with Baghdad in all areas, and reiterates its right to benefit from the program of international support currently being provided to Iraq.

So, looking at the broader picture, while the world is focused on war and turmoil in the Middle East, we are steadfastly addressing our own issues head on, all the while being in the eye of the regional storm.

While fighting a war, managing continued inflows of displaced people, and constantly navigating geo-political minefields, we are steadfastly tackling our own massive economic challenges, and forging ahead to secure Kurdistan's political and economic viability.

As members of the international coalition support Kurdish and Iraqi forces engaged to defeat ISIS in Iraq, we must be clear that only by ensuring a politically and economically viable Iraq, and Kurdistan, can we cement military victory won on the battlefield.

This requires more strategic global engagement including by key partners such as the US and UK on Iraq and specifically in Kurdistan.

It necessitates a more comprehensive and holistic approach, to include facilitating consensus among the leading political forces in the country and ensuring economic sustainability that in particular creates job opportunities for the youth in the private sector.

Ultimately, progress in diversifying the economies of Kurdistan, Iraq and the wider Middle East region will depend on progress in building a common economic space for all peoples living there.

In closing, we have proven to be resilient in the face of adversity; resolute in delivering on our plans and vision; and unrelenting on the battlefield.

We are thankful for the continued confidence you have in us.

Especially you in the Oil & Gas Community who have invested in Kurdistan. Despite our financial pressures, we are doing all we can to ensure timely payments to you.

Through credible reform efforts, we want to show you, by actions not words, that we are a worthy partner.

We seek your continued and increased investment.

Our strong partnership with you in the oil & gas sector is crucial for Kurdistan's continued progress and our mutual success.

With your sustained support during these difficult times, together we will overcome today's challenges, and forge a permanent foundation for peace and prosperity in the future.

End.