

# Development obstacles of the Private sector in the Kurdistan Region of Iraq

(The experience from SMEs in Erbil)

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**Abstract:** Diagnosing the obstacles of the private sector developments is the main purpose of this study, while the data will be taken from the private sector directly in this respect. For this purpose, through this research vital questions are addressed to the companies of the private sector so that we can have a clearer understanding about the obstacles on the private sector developments. In this research both primary and secondary data have been used; data have been collected by analyzing of literature from journals and research papers, as well as an exploratory research; questioners have been chosen in order to obtain relevant and quantitative data from primary sources. In this respect the data collection process is done by Erbil Chamber of commerce and Industry in collaboration with the Department of Studies and Research, Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI) in Erbil. In this respect, questionnaire have been prepared and distributed between 250 business in Erbil. Moreover, important and lively areas have been identified to be assessed with companies and commercial institutions in categorizing the hinders may hamper their development to be active in focusing on the below: banking system, insurance systems, financial services as well as public sector services. So, it is necessary to measure the efficiency of these sectors so that corrective steps can be taken to improve the health of the banking system, financial services, insurance systems, database, and public Sector services; therefore, the main purpose of this research is to obtain related and accurate understandings in regards with the main development obstacles of the private sector in the KRI.

**Keywords:** Banking system, Insurance systems, Financial services, Public sector services

## I. INTRODUCTION

Undoubtedly, the development of the private sector can be seen as a priority of the majority of the countries worldwide. Private sector is the main pillar and supplementary for the public sector and establishing a strong economy as well as sustainability. The trends witnessed in the world, Iraq and Kurdistan region have direct and indirect impacts on the business environment including local and foreign companies' operations in the region. In most cases the obstacles are uneasily can be predict, this leads to not capable of mitigating of their impacts or taking protection actions at least. Although in most cases the trends hinder the development process of private sector in Kurdistan, the government plays a vital role in identifying and lessening the hinders and providing support and solutions for developing private sector if it is seen as the main work plan of the government (Majed et al., 2020).

The banking sector is the modern economy's lifeline. The financial sector is one of the key pillars of the economy, which plays an integral role in the workings of an economy. It is very important for the economic development of a country that its financing requirements of Public sector services the ability to implement legislation related to insurance systems, trade, investment and development and existing mechanisms for implementation are met with an Engagement and accountability are higher. The growth of a nation is therefore related integrally to the growth of the banking system and financial services. In a modern economy, public sector services are not to be regarded as cash traders, but as growth leaders (Othman et al., 2020).

Governments play a significant role in mobilizing deposits and paying loans to various industries of the economy. The banking sector represents the country's financial fitness. The efficiency of an economy depends on how powerful and effective a financial system is and how safe and stable the banking system depends. A sound banking system that effectively mobilizes productive sector deposits and a stable banking system guarantees that the bank is in a position to meet its depositor obligations. In Kurdistan, banks need to play better role in the socio-economic developments; and public sector services, the ability to implement legislation, insurance systems, trade, investment and existing mechanisms for implementation progress of the country after independence needs to be addressed. The banking sector is dominant in Kurdistan as it accounts for more than half the assets of the financial sector. Kurdistan banks have been going through a fascinating phase through rapid changes brought about by financial sector reforms, which are being implemented in a phased manner. The current process of transformation should be viewed as an opportunity to convert Kurdistan banking into a sound, strong and vibrant system capable of playing its role efficiently and effectively on its own without imposing any burden on the government.

After the liberalization of the Kurdistan economy, the Government has announced a number of reform measures on the basis of the recommendation of the committee to make the banking sector economically viable and competitively strong. The current global crisis (covid-19) that hit every country raised various issues regarding the efficiency and solvency of the banking system in front of policymakers. Now, the crisis has been not over, the Government of Kurdistan (KRG) and Reserve Bank of Kurdistan are trying to draw some lessons. KRG, through public services, try to do necessary changes in his policy to ensure stability in the economy (Khatab et al., 2019).

One of the main questions in the KRI and its economy is unavailability of data, in most case the trends are positive and fast and bring in changes in many aspects while due to having enough data it complicates the process of conducting an accurate assessment and even it cannot identify the hinders that hamper the development process.

There are complications noticed in Kurdistan that hamper the private sector to act as an active sector and to be seen as a key partner of alongside the public sector. Part of the issue is related to banking system and lack of financial support. In addition to that, lack of insurance system which is considered as another obstacle on the development of the private sector. Lack of data and database as a source of information is considered as a neglected area. Most importantly, the steps taken by the KRG in implementing the rules and utilizing mechanisms in imposing rules and laws that support the development of the private sector in the Kurdistan region. Kurdistan lacks the capacity to produce internationally-minded people without study. Kurdistan has been unsuccessful in offering required priority to the development of the various resources needed for research activities in spite of recognizing the importance of the role of research in the banking system, financial services, insurance systems, database, public sector services, trade, investment, mechanisms for the implementation development process. Thus, this research emphasizes on diagnosing and finding out the barriers and obstacles that hamper the development process of the private sector in the Kurdistan region in terms of the economy and business environment and the support of the public sector as well (Majed et al., 2020)..

## **II. Literature review**

### **KRI Economic development backgrounds**

Since 2003, the Kurdistan region has created its own system of economic, which is lead to the name of Kurdistan region became a title of the many international presses, precisely in the economic and financial presses, and this is due to increase in the economic openness worldwide. Starting by the issuance of the investment law in 2006, which regulated and facilities investment in general (Doski, 2015 and Cortoba, 2015).

During the past few years, the amount of money that invested in the Kurdistan region of Iraq (KRI) in various economic sectors has seen a potential increase, whether by the local or foreign investors. Furthermore, according to the authorized statistics the amount of money has invested in Kurdistan region during the period 2006 to 2013 surpasses 31 Billion U.S. dollars, that divided in to three different economic sectors. Firstly, housing sector with

more than 14 Billion U.S. Dollars, followed by industrial sector more than 8 Billion U.S. Dollars, then tourism sector with 3 Billion Dollars. (Doski ,2015). In addition to that, the under-implementation projects were more than 613 (26 joint venture, 44 foreign and 513 national). (KRG, Investment Board, Department of information and studies, 2012). However, according to MRI (2015), Kurdistan region economically has confronted sever downturns as the data showing economic growth rate decreased by %5, trade and investment movements dropped around %30, as well as youth unemployment drastically increased by %9. This economic downturn at the end of 2014 were a result of three simultaneous crises. Firstly: 'the financial crisis A financial crisis that has left the Kurdistan Regional Government unable to finance its budget, as Kurdistan's share of the federal budget is suspended in Baghdad by the Iraqi Federal Government. 'Second, "an economic paralysis in Kurdistan due to the internal conflict in Iraq, which has raised insecurity, displaced thousands of families who are now in need of assistance, affected trade routes and decreased investor confidence. The fiscal crisis is significantly compounding such impacts as the KRG and public services are incapable of dealing with rising demands and higher military costs for the growing population. Third, "political competition within the government of Kurdistan national unity splits the Council of Ministers and leaves no formal opposition to balancing executive power in a parliamentary term. The KRG has been unable to formulate and implement new policies "and has been hampered by ongoing disagreements and lack of accountability between the governing parties." This uncertainty and volatility which has caused by these crises are considering as difficulties of economic growth, consequently, private sector development. Despite of the crisis the Kurdistan region in order to achieve accelerate economic development and growth has initiated the vision of the regional strategy in 2020, which is represented in long term plan under the name Kurdistan region of Iraq 2020, thus consequently it will make private sector the number one sector in creating jobs and economic growth, as well as attractive more national and foreign investment in coming years. (Doski, 2015).

### **III. Financial system and data availability**

According to World Bank Group (2015) an inclusive and efficient financial system is critical of private sectors development and this is due to a well-established financial system would fund greater investment for larger number of people. Therefore, Kurdistan region in his 2020 vision intensely focused on the banking system. According to the Kurdistan board of the investment %16.67 of the region capital investment is dedicated to the banking sector, which constitutes approximately 2.3 Billion Dollars in investment project (Cortoba, 2015). Furthermore, many foreign banks entered the region, 3 state owned banks working actively, 19 local private banks, 11 foreign private banks and 6 local and 1 foreign Islamic bank nowadays operating in the region. (Doski, 2015).

USAID (2015) stated that, despite the involvement of the foreign branches and continued growth of the local banks. The banks sector in the KR has limited role in business transaction. For example, the banks in Kurdistan region uses more often for the public sector payments (salaries and pensions) instead of using by the majority households and business. (MRI, 2015). This is as consequences of a poorly developed a financial sector including, weak financial infrastructure and low access to finance especially for the small and medium sized enterprises. (World Bank Group, 2015). The lack of local finance it can be one of the critical challenges faced by the local business including early stage working capital and equipment loans. This severely limits the number of business that can enter the market and expand. Accordingly, the confidence in the financial sector is extremely low among household and to a significant extent, local and micro business as well, and as a consequence these groups prefer to keep money in liquid assets and they have a strong preference for cash in business transaction, which is only three percent of companies depend on banking system for investment and working capital. (MRI, 2015; World Bank Group, 2015 and Sindi, 2013).

The Kurdistan region is also facing other critical challenges within its financial system, which is missing insurance and mortgage industries as well, which are important supports for the developments of the private sector. In addition to that, the limit access of data and information by the private sectors is another barrier. However, Kurdistan region on its 2020 vision plan works on increasing availability of data and information and this is throughout eliminating the barriers as well as regularly publishing information about its economy and allowing the private sector to carry out their own market research. (Sindi, 2013).

### **IV. Methodology**

This research sheds light of diagnosing of the main development obstacles of the private sector in the Kurdistan Region/Iraq and taking Erbil as an example. The researchers, in the light of the importance of the objectives and the questions, depends on the descriptive analytical methods in the preparation of the research as follow:

The first approach is based on extrapolation and analysis of literature (books, letters, Arab and foreign periodicals and researches on the international information network) related to the social knowledge financial market aspects of the research for the purposes of rooting scientific research topic.

The second approach depends on an exploratory study by scanning the field for several persons in private sectors from CEO., managers, financial and administrative stuffs. using a questionnaire to determine: Development obstacles of the Private sector in Kurdistan region of Iraq. For this purpose, a questionnaire has been administrated and randomly distributed amongst 250 companies and commercial institutions located in Erbil at the level of (SMEs) and many important factors are indicated in the sense of diagnosing the development obstacles, so that we can test them through this research and so that we can narrowly focus of the subject, business environment status in terms of economic and financial infrastructure and also supporting public sector in general; and the main focus was on the following: availability of banking system and financial services, availability of insurance systems, existence of a database, implement legislation and mechanisms for implementation.

The questioner has been distributed to these industries: small and Medium sized general trading companies, small and medium sized stores and malls, Bricks factories, Medicine Stores, Pharmacies, Bakeries, agricultural equipment and Machines supplies, agricultural material and medicines trading, Goldsmith Stores, Real estate bureaus, farmland and residential land as well as Automobile, Spare Parts Agencies and Batteries suppliers.

The data collection process is done by: Department of Studies and Research, Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI) as a key role player in private sector in the region.

#### **V. Findings and Data analysis**

In this part, the research findings and data analysis will be considered. There are five main themes that highlighted in order to explain the answers for development obstacles of the private sector in KRI; which are: the availability of banking system and financial services, the availability of insurance systems, the existence of a database and related information, the ability to implement legislation related to trade, investment and development, and the existing mechanisms for implementation.

Table (1) illustrates the availability of banking systems and financial services, the answer shows that most businesses assumed that services and capacity is on the primary level which the number of responses are (101) which is equal to (40.4%). Based on the data, the greater number the responses support that services and capabilities are not available and/or primary services or capacity available, which goes to up to (74.8%); due to only (19) responses said services and capabilities are good which refers to (7.6%).

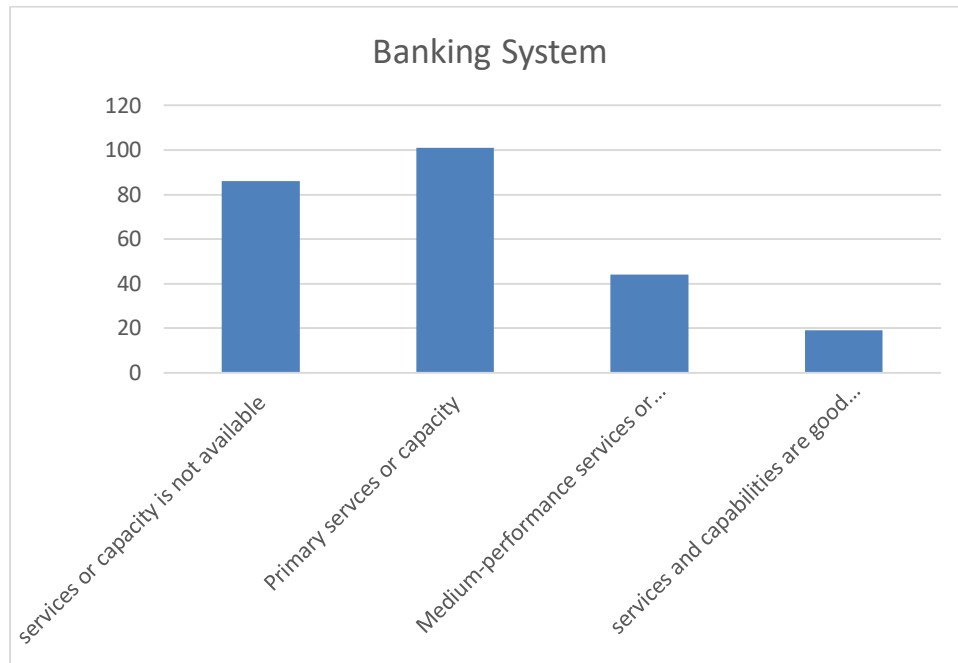
**Table (1)**

#### **Availability of banking system and financial services**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

<b>Availability of banking system and financial services</b>		
	<b>Frequency</b>	<b>Percent</b>
Services or capacity is not available	86	34.4
Primary services or capacity	101	40.4
Medium-performance services or capacity	44	17.6
Services and capabilities are good and as required	19	7.6
<b>Total</b>	<b>250</b>	<b>100.0</b>

Furthermore, graph (1) also illustrates that availability of bank and financial services, the answer show that most SMEs supposed that the services and capacity is on the primary level, whereas based on responses, services and capabilities are not good as required ranked in a lowest level.



**Graph (1)**

**Availability of banking system and financial services**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

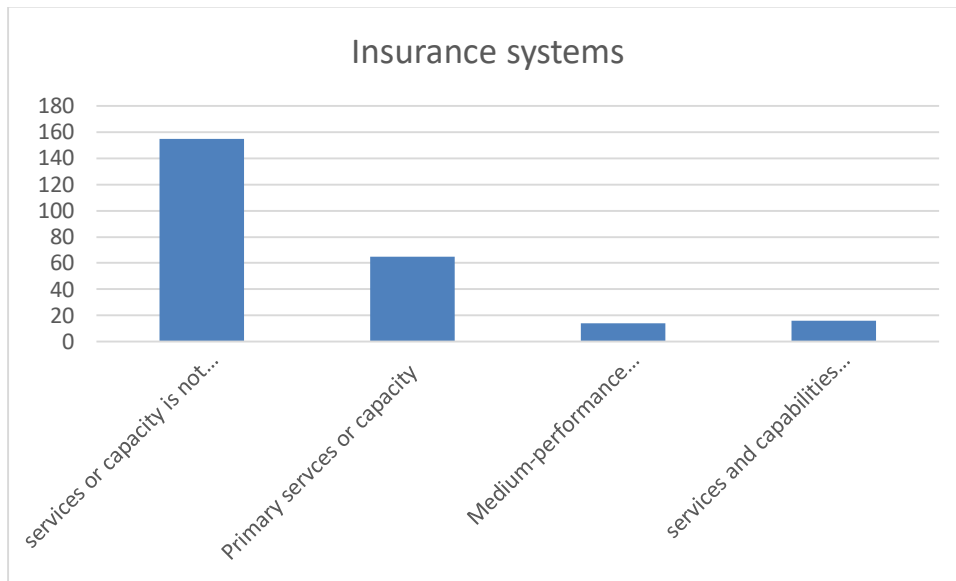
Related to the availability of insurance systems, most business assumed that services and capacity is not available which the number of responses are (155) it become (62%). Moreover, based on the responses; the medium performance services and capabilities are only (%5.6), due to only 14 responses replied medium performance services or capacity, see the table (2) and graph (2).

**Table (2)**

**Availability of insurance systems**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

<b>Availability of insurance systems</b>		
	Frequency	Percent
Services or capacity is not available	155	62.0
Primary services or capacity	65	26.0
Medium-performance services or capacity	14	5.6
Services and capabilities are good and as required	16	6.4
Total	250	100.0



**Graph (2)**

**Availability of insurance systems**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

Table (3) illustrates that existence of a database and related information. The response shows that the greatest number of SMEs considered that services and capacity is not available which the number of answers are (110) which refers to up to (44%). On the other hand, based on the data; the rate of services and capabilities are good as required obtained only (5) responses; which refers to only (2%) from the participants.

**Table (3)**

**The existence of a database and related information**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

<b>The existence of a database and related information</b>		
	Frequency	Percent
Services or capacity is not available	110	44.0
Primary services or capacity	107	42.8
Medium-performance services or capacity	28	11.2
Services and capabilities are good and as required	5	2.0
Total	250	100.0

Furthermore, another question which directed to SMEs in Erbil was the ability to implement legislation related to trade, investment and development. The business’s answer’s display that most of them assumed that services and capacity is on the primary level which the number of responses are (143) and (57.2%). If we calculate both primary services or capacity and services or capacity is not available, the rate reach up to (62.4%). On the other hand, the

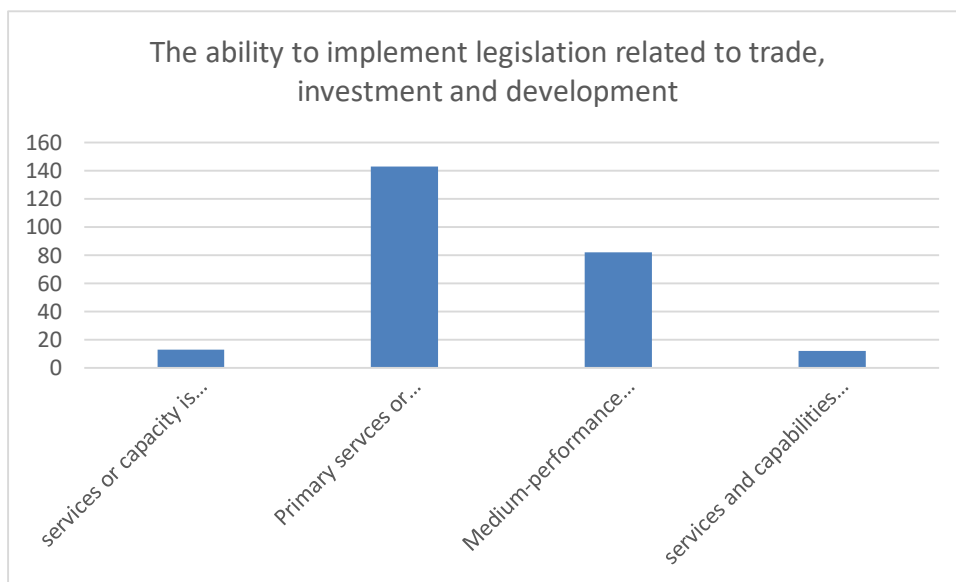
services and capabilities are good and as required, is the lowest rate which is only (4.8%), and only (12) businesses supported this (see table 4, graph 3 and 4).

**Table (4)**

**The ability to implement legislation related to trade, investment and development**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

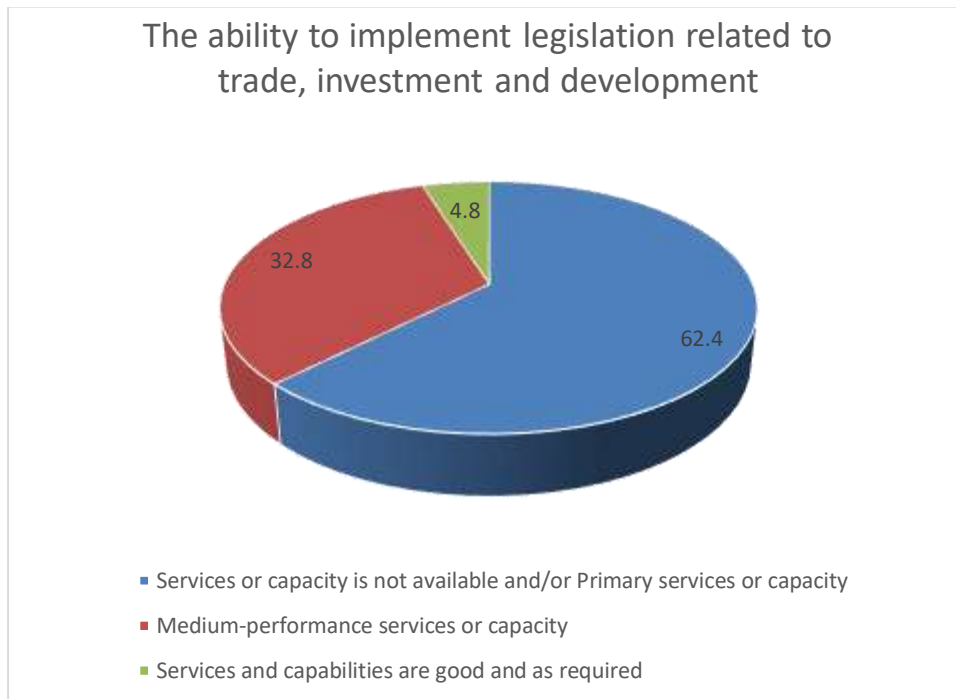
<b>The ability to implement legislation related to trade, investment and development</b>		
	Frequency	Percent
Services or capacity is not available	13	5.2
Primary services or capacity	143	57.2
Medium-performance services or capacity	82	32.8
Services and capabilities are good and as required	12	4.8
Total	250	100.0



**Graph (3)**

**The ability to implement legislation related to trade, investment and development**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**



**Graph (4)**

**The ability to implement legislation related to trade, investment and development**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

Finally, the existing mechanisms for implementation, was another question which is related to the services that provide by the public sector. In the table (5), clearly can be seen that out of (250) SMEs, (106) considered that only primary capacity is available which is (42.4), is the highest rate among other 3 choices. Furthermore, if collectively calculate services or capacity is not available and primary services or capacity, it reaches (78%), due to only (3) responses thought that the services and capabilities are good as required, which refers to only (1.2%) from the businesses, (see table 5, and graph 5)

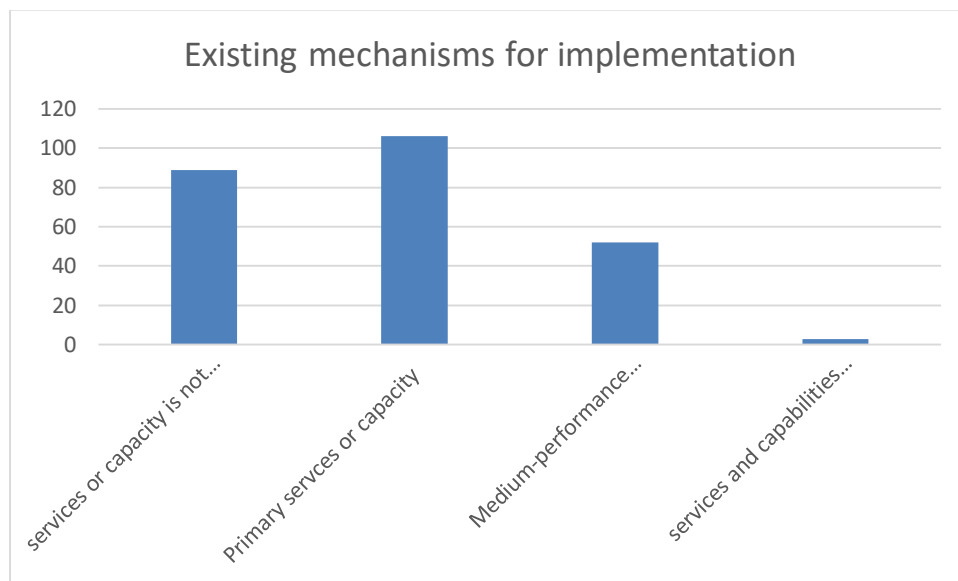
**Table (5)**

**Existing mechanisms for implementation**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

Existing mechanisms for implementation		
	Frequency	Percent
Services or capacity is not available	89	35.6
Primary services or capacity	106	42.4
Medium-performance services or capacity	52	20.8
Services and capabilities are good and as required	3	1.2
Total	250	100.0





**Graph (5)**

**Existing mechanisms for implementation**

**Data from Kurdistan Federation of Chambers of Commerce & Industry (K-FCCI)**

**VI. Conclusion**

After witnessing noticeable economic and political trends in the area, Iraq and Kurdistan Region and arising private sector as the main partner in development of economy in the past, and now it is essential to identify the key obstacles and difficulties on developing this sector accurately, so that it can take positive steps. It is necessary to pay attention to the private sector to have a clear and precise understanding of the hinders and main issues facing the development process of the SMEs. KRG is trying to make necessary public sector service changes in policy to ensure the stability of the economy. Thus, this research paper is indispensable, first to diagnose the development obstacles on the development of the private sector, secondly, the research depends on the data extracted from the private sector in the region.

Related to the availability of banking systems and financial services, the great number the responses support that services and capabilities are not available and/or only primary services or capacity available, which goes up to (74.8%). Furthermore, (62%) of the SMEs considered that services and capacity is not available in related to insurance systems. Moreover, based on the data; the rate of services and capabilities are good as required in related to the existence of a database and related information; is only (2%) from the participants. Additionally, up to (57.2%) of the businesses assumed that the ability to implement legislations related to trade, investment and development; only on a primary level is available which the number of responses are (143). While, only (4.8%) supported that the services and capabilities are good and as required related to the ability to implement legislations related to trade, investment and development. Finally, related to the existing mechanisms for implementations; only (1.2%) of the SMEs assumed that the services and capabilities are good as required is available.

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