

FT REPORT - FT FUND MANAGEMENT: Iraq's harsh realities and opportunities

By John Dizard
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The American involvement in Iraq is just reaching the top of the roller coaster before starting on the downslope. The differences over timing are measured in months, and not many months at that.

So what is the likely future of Iraq? And, since this is the Financial Times, is there any money to be made or lost from that future?

There are a lot of people with opinions about Iraq, but few who actually know what is going on. One of those is Ali Allawi, whom I met in Baghdad when he was defence minister, and who subsequently was finance minister, and a key figure in the renegotiation of Iraq's sovereign debt. That remains one of the few well executed postwar operations in Iraq.

Presently, Mr Allawi lives most of the time in London, and is the chairman of a company that has partnered in the development of Progas, a Karachi-based liquefied petroleum gas importer and distributor. Dr. Allawi, 60, was educated at MIT and Harvard Business School, and spent his early career at the World Bank. His family is at the centre of the Iraqi elite, in particular of the Shia community. They had left Iraq after the rise of the Ba'ath party and Saddam.

He has just published a book, *The Occupation of Iraq*, which I recommend to anyone interested in an unvarnished account of the first phase of this war and what followed. He remains, formally, an adviser to Prime Minister Al-Maliki, but, as he says, "I am dormant as an adviser".

I asked Mr Allawi how the situation has developed since he finished the book.

"The symbolic significance of the so-called national unity government is that it keeps the hope alive that some basic agreement can be reached in key issues. What is holding it together is the presence of the US in force. Now this is a quixotic venture that has reached the end of its useful life.

"The current administrative structure is incapable of managing the state or reconstruction."

A key problem, is what Mr Allawi calls the "human resources gap". There just are not many people who know what they are doing. "The government doesn't recognise that they have [this gap]. There are all sorts of people descending on Baghdad from the Iraqi diaspora, not just carpetbaggers and ne'er do wells, but mainly looking for jobs. If you bring in people who pretend to manage and cover up mismanagement with oil money, then you get policies that beggar belief."

What comes next?

"We haven't yet reached the exhaustion point [with the war] in Iraq, but I don't think we are far from the bottom. The only way it can go further down is if there is overt support for the insurgency, as a state policy [of neighbouring countries]."

What follows an American pullback? "That will strengthen the central government's control over the army and security forces, but it will be a sectarian central government that will drive the Sunni into far greater hostility." But that fight will have its limits. "That kind of army will not be able to conquer Sunni territory, like Mosul. In time it will be seen on both sides that the state cannot control the Sunni parts, and it will be seen on the part of the insurgents and their backers that attempting to take back control of the state is futile."

Mr Allawi believes that outsiders could have a role in negotiating and securing an eventual peace. "If there is an Iraqi political settlement, it could take the form of a treaty that not only binds the local contenders, but the region, maybe one in which the distribution of oil revenues is insulated from a capricious central government."

For portfolio investors, Mr Allawi believes the rescheduled foreign debt is secure. "The commercial debt renegotiation was a good deal for Iraq," which any successor governments will want to keep in place. "The total amount of remaining debt to the Gulf states is not as much as originally believed. Net of interest, it is in the \$20bn-\$25bn range. If that is renegotiated on similar terms, stretched over many years, that is not a significant drain." The 2028 issue, currently trading in the 64-65 range, yields about 10 per cent, or 520 off the US Treasury curve. That's a little lower yield than Ecuador, but, I would agree with Mr Allawi, good value.

As for commercial interests, Mr Allawi says: "I think that if you are in a fast-moving consumer goods business, for example, Iraq has a lot of opportunities. There is a lot of cash there, and a lot of resources."

I can vouch for the cash-richness of the country, and for the size and skills of a diaspora that is just over the horizon. Disastrous as Iraq's situation seems now, we're probably within a year of its worst moment, and post-conflict recoveries can be remarkably quick.

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