Economic fallout of the war

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By Sultan Ahmed

LEADING US economists have spoken strongly against a unilateral US-led war on Iraq and warned President George Bush that it would have adverse economic consequences and increase the risk of future instability and terrorism.

The economists, including seven Nobel prize winners for economics, have voiced their concern over the immediate human tragedy and devastation of war. The war, said the statement issued by the Economists Allied for Arms Reduction, a New York based research group, could drive up interest rates and energy prices and unleash a major consumer retrenchment.

The Nobel Laureates, who include Kenneth Arrow, Lawrence Klein and Joseph Stiglitz, said "given the precarious state of our own economy, America requires the attention and focus of leadership and resources to address economic problems at home." They also said the priority given to the military sector "would hurt the recovery of the ailing technology sector."

And Prof. James Galbraith said the Bush administration was not playing it straight with the American public as to the potential economic consequences of the war.

The fear of a rise in interest rates is real after a long period of cutting interest rates in an effort to boost the sagging economy which has not been particularly responsive to such efforts by the Federal Reserve. Latest figures of the US economy are demoralising to the people who find unemployment at a high 5.8 per cent and the dollar at its lowest exchange rate against the euro in four years. While share prices are slipping in New York, gold prices are going up.

While the US may be able to afford a short war despite such economic trends and the possible gains from the post-war world, what will be the cost of the war for Pakistan and other developing countries in the region? And that depends on how long the war will last or how short will that be, and how disruptive or destructive will that be for the region.

President Bush himself wants a short and decisive war. So the US talks of bombing Baghdad ten times more than it did in 1990-91 while sparing the oil wells of Kirkuk and the Kurdish region in the north.

But can a war be fought totally according to the US script more so if it wants to spare heavy civilian casualties?

The world knows the proposed US strategy but not Saddam's strategy to stand up and fight or evade and resist. A poll taken in California says that 71 per cent of the people

If the US economy is hit hard by the war it can affect Pakistan's exports to that country as well, particularly the textiles. Pakistan has been experiencing difficulties in exporting its textile to the US since 9/11. At a time when our exports are doing so well and have increased by almost 20 per cent in the current financial year compared to last year's in the same period, we may not be able to afford a major setback in the US sector.

fortnights. The government has said it would not reduce the heavy duties on oil and taxes. If it did so it would have to raise taxes elsewhere to balance the budget. And the IMF and World Bank would not allow lowering of the duties on oil so that the macro-economic balance is not disturbed.

Experts predict if the war is short the world price of oil may come down to 25 dollars a barrel. That is if the oil installations in the region are not destroyed.

Economists estimate that every increase in oil price by five dollars a barrel would reduce the growth of the US economy by half a per cent. In such a case with the US economy in the doldrums it would not be able to sustain a 40 dollars a barrel oil price for long. Hence the rush to war.

If the growth of the US economy would be hurt that much by the world oil price even when it produces half the oil it needs a steady oil price rise would hurt the economic growth of Pakistan a great deal, more so when most of our needs are met by imports.

However, the generous Saudi oil facility of a billion dollars a year is very helpful, more so at these critical times.

Pakistan received 891 million dollars from various countries led by the US for its cooperation in the war against terrorism, says Shaukat Aziz, Advisor to the Prime Minister on finance. That is the direct cash benefit. The indirect benefit, inclusive of debt relief, has been sizable. But all that is a patch compared to the 30 billion dollars offered by the US to let its troops enter northern Iraq from Turkey. Turkey sought far larger funds as it argues it lost over 40 billion dollars trade and economic losses following the 1990-91 Gulf war. So many Pakistanis think the country has been sold short by the leaders. And yet we keep on handing over Al Qaeda prisoners to the US including Khalid Shaikh Mohammed which has been greatly appreciated by America.

and free to act on merit in Baghdad?

The Americans have said they will favour in the post-war Iraq those who had sided with them in the war. So will Pakistan abstain in the voting in the UN Security Council on the war or vote with the Americans finally as the second resolution is put to vote?

The issue is not only the share of Pakistan in the future external trade of Iraq but also the share in the post-war reconstruction of Iraq. Will that be small or substantial?

Earlier we had spoken of our share in the economic reconstruction of Afghanistan where we supported the US fully and continue to do so. Yet we don't seem to matter much in the reconstruction work, while we sell some cement or other construction materials to Afghanistan, and the Karzai regime is not well rooted.

Unlike Afghanistan Iraq has plenty of resources. The second largest producer of oil after Saudi Arabia with a 2.5 million to 2.8 million barrels of oil a day its capacity could rise to four million barrels a day after the oil wells and he refineries are rehabilitated. And after the reconstruction and expansion the capacity could rise to 7 million barrels over the years. So Iraq would not need prolonged external aid, although the aid would be essential in the earlier period.

Not only the US but also the World Bank and other donor agencies are ready to offer such assistance. But post-war political stability in Iraq is a major issue. The Americans have spoken of reforming the regimes in the neighbouring region as well. Will that lead to regional convulsions?

The region may not be affected economically by a short and well targeted war. But will the course of war follow the American strategic planning? Even if the economies of various regions are not too directly affected by the war the American economy would be hit. And America would reduce its imports from the rest of the world. It would want to save not only its industry but also its labour in a period of rising unemployment.

The world is becoming more and more dependent on the US importing its goods. During the last Gulf war South East Asia exported 3 per cent of its GDP to the US but now its exports are 5 per cent of its GDP. Any serious reduction in such imports would hurt the newly-industrial states of Asia very hard.

Anyway the US businessmen want the nagging uncertainty in respect of the war to come to an end and that the war, if it takes place, should be over quickly so that they could resume their normal business. They

California says that 71 per cent of the people polled fear conditions of life would be far worse after the war than what it was two months ago. The percentage of those who had such fears was only 41.

President of the World Bank James Wolfensohn, on a visit to Jordan, wants the war to be avoided, but if it happens it should be very quick to minimise the damage to the global economy. He says what is affecting the global economy is the unwillingness of the people to buy, and unwillingness to invest, and a sense of fear.

He says the impact of the war on the global economy depended on the duration of the war and how it would dent confidence, prompt firms to put investment plans on hold and make the consumers less inclined to spend.

He predicted that further oil price turbulence could slow down the global economy if the hostilities caused damage to Iraq's oil industry installations. There will be concern about disruption of oil supplies, but then that depends on whether oil is destroyed or disrupted. There can be quick recovery after disruption, but in case of destruction of the facilities the recovery or reconstruction will take a long time.

World oil price has already reached 40 dollars a barrel and domestic price of oil has been raised steeply several times in recent

Higher oil prices are not only price we are paying before the war. Our exports are affected. The shipping rates have gone up, making Pakistani exports more costly. The war will bring high war risk insurance which will make both our exports and imports more costly.

While we are paying high price for a possible or imminent war, will we get a fair share of the returns from the post-war reconstruction in Iraq? The Chairman of the Export Promotion Tariq Ikram is too optimistic. He thinks the contacts we have established in Baghdad will pay full dividends after the war. He says Pakistan has a large share of the Iraqi market for batteries, wooden doors, construction materials, pharmaceuticals, textiles, wheat, stationery and surgical goods. Earlier he had hinted at the prospects of exporting a million tonnes of wheat to Iraq this year.

He says that once normality returned to Iraq Pakistan's exports would flourish further. He thinks it would be business as usual in Baghdad, certainly in respect of exports from Pakistan. But the post-war situation in Iraq depends on a number of uncertain factors. It depends on who will head the economic sector in Baghdad then. Of course, the Americans will be in charge. Will they honour the agreements reached by the Saddam regime officials. Will those officials be there

have increasing strains with European businessmen due to the political differences of their governments in respect of the war and they want such differences to come to end soon and have stable relations with Europe whose euro is appreciating against the US dollar.

If the US economy is hit hard by the war it can affect Pakistan's exports to that country as well, particularly the textiles. Pakistan has been experiencing difficulties about its textile exports to the US since 9/11. And at a time when our exports are doing so well and have increased by almost 20 per cent in the current financial year compared to last year in the same period, we cannot afford a major setback in the US sector.

What is certain is we are living in a very very uncertain world and in a very turbulent region and the world economy is moving from one convulsion to another. So we have to make our economy really strong. Building up a foreign exchange reserve of 10 billion dollars is good.

Our increasing exports are welcome. But far more has to be done in the areas of investment so that our production goes up, exports increase and become diversified and employment rise. All that has to be done on an urgent basis as what we have to do now is far more imperative than what we have achieved.