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Collateral Damage: How US Sanctions against Iran Harm Iraq

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The renewal of US sanctions against Iran in early August represents another blow to the Iranian economy, which has weakened steadily since the United States withdrew from the Joint Comprehensive Plan of Action in May 2018. The sale of gold and precious metals to Iran has been banned, as has the acquisition of dollars by the government of Iran and Iranian companies, and there are prohibitions in place on the sale of civilian aircraft to Iranian airline companies. These steps have reinforced the downfall of the Iranian currency and the damage to the local economy, against the background of the clear US message: anybody doing business with Iran cannot do business with the United States. The next round of sanctions, which will affect oil purchases and is expected to be imposed in November, is designed to strike at the heart of Iran's national product. Yet in this era of globalization, it is abundantly clear that sanctions have ripple effects beyond Iran. Given the ever-expanding economic ties between nations, sanctions imposed on one state cannot but trickle into another, affecting economic institutions and individuals invested in the state targeted by the sanctions. The example of Iran and its effect on the economies of the West, Middle East, and especially Iraq is an interesting case study. The United States must be aware of the damage these sanctions will cause to the Iraqi economy, as this is part of the broader picture of the US struggle with Iran over influence in Iraq.

The Joint Comprehensive Plan of Action, reached in July 2015 by the P5+1, provided a global imprimatur for doing business with Iran. Consequently, many nations and companies expressed an interest in large scale investments in Iran, and many even signed long term contracts. Three years later, the US departure from the nuclear deal was the official opening salvo in an economic war and resulted in the mass flight of Western companies from economic involvement in Iran. In the automotive industry, Mazda, Hyundai, and Peugeot-Citroen all cancelled contracts worth billions with Iranian companies and withdrew their investments in the country until further notice; banks announced they would close their Iranian branches and stop SWIFT transfers linked to purchases in Iran; the French company Total cancelled a contract to develop a gas field; and Boeing reneged on contracts to provide \$20 billion worth of airplanes to Iran. These are just a few examples of deals between big corporations and Iran that have collapsed

and affected not only Iran but these companies as well, which had planned on entering a large new market that could have yielded rich rewards in the short and long terms.

The US sanctions affect not only private companies, but also other nations, especially Iraq, where the United States is heavily involved in reconstruction. Iraq has long suffered from instability since the fall of Saddam Hussein in April 2003. In 2011, US soldiers withdrew from Iraq; three years later, the civil war flared up again between the regime and the Sunni rebels, this time operating as part of the Islamic State. In December 2017, Iraqi Prime Minister Haider al-Abadi announced the end of hostilities and victory against the militias. Under al-Abadi's rule, Iraq is slowly recovering and enjoying relative stability, reflected best by the fact that Iraqi refugees are returning home. Iraq also has important security ties with the United States.

However, Iran's influence over Iraq is significant, and manifested inter alia in the economic sphere. Economic ties between the two neighbors are growing closer, most importantly in three areas:

- a. Imports: The scope of bilateral trade has risen annually. Thanks to the Islamic State's ouster from Iraqi territory, trade hit an all-time high of \$6 billion last year (as of March 2018). The imports, representing 15 percent of all imports to Iraq in this period, consist of foodstuffs, agricultural products, basic building materials, air conditioners, and automotive spare parts. Easy routes and low prices make trade with Iran attractive for Iraq.
- b. Tourism, primarily religious Shiite pilgrimages, adds \$5 billion annually to the Iraqi economy, with Najaf and Karbala the most popular destinations due to their importance to Shiite history. Last year, about 85 percent of the tourists to these cities were from Iran.
- c. Financial ties: Out of concern over instability in Iraq and in an attempt to preserve the value of their assets, many citizens have moved their money out of Iraq. In 2015, the Iraqi market collapsed following the success of the Islamic State; in tandem, following the nuclear agreement, the Iranian economy began to grow. Iranian banks offered a 20 percent annual interest rate at a time that investments in Iraq were risky, leading many Iraqis to withdraw their money and deposit it in Iranian banks.

The US withdrawal from the nuclear deal, and the ensuing first round of sanctions, has affected tourism to Iraq and investments in Iranian banks. Moreover, already since April 2018, the Iranian rial has lost more than half of its value against the US dollar, leading many Iranians to cancel planned pilgrimages to Iraq. The Najaf airport, which a few months ago operated 35 flights daily between Iraq and Iran, now operates only 12. Some 300 hotels in the city are offering rooms at 50 percent discounts to lure back Iranian tourists, but this promotion has been largely unsuccessful. More than half a million Iraqis work in the tourist industry and a primary fear is that continued sanctions will lead to

mass layoffs. In addition to the troubled tourism industry, many Iraqis are worried that their investments in Iran will lose all value. Their money was converted into rials the moment it was deposited; thus with the currency devaluation, Iraqi investments are also compromised. Iranian banks today limit withdrawals to the equivalent of \$200 a day, thereby preventing the transfer of any remaining money back to Iraq.

The damage from the sanctions to tourism and private Iraqi investments has prompted grave concern in Iraq over impending economic instability. Prime Minister al-Abadi recently announced that an Iraqi delegation would visit Washington soon to reach understandings with the US administration about continued Iraqi-Iranian trade. Al-Abadi already stated that Iraq would not honor the sanctions and would continue to trade with Iran, albeit in currencies other than the US dollar. Iraq is worried that a shortage of basic products currently imported from Iran will lead to instability in the nation. For its part, Iran has a clear interest in maintaining economic ties with Iraq and is therefore expected to try to prevent Iraq from cooperating with the sanctions regime. The United States must consider a solution to the economic challenge facing Iraq while also heeding the political challenge that Iran represents. Because Iran has many means at its disposal to destabilize Iraq's internal arena, the United States will have to pay attention to that challenge as well.

Until recently, Iraq suffered from chronic instability, and Iraq's leadership is rightly worried about an economic crisis, which is liable to lead to political chaos. Having contributed much to Iraqi security and what is currently a relatively stable political reality, the United States must now think about economic stability as a means of preventing renewed instability. It must therefore not underestimate the collateral damage to Iraq caused by the sanctions on Iran. Moreover, even official Iraqi compliance with the sanctions does not guarantee there will not be smuggling facilitated by pro-Iranian elements in Iraq. Then again, it does not mean that the United States need sanction an Iraqi decision to bypass the sanctions, because this would only strengthen Tehran's ties with Baghdad, which are already stronger than Baghdad's ties with Washington. Given that the United States must treat all parties maintaining economic relations with Iran in a consistent manner, the broader strategic picture points to another round in the US-Iran fight for influence over Iraq. If the United States wages a campaign against Iran, it cannot allow the Iran-Iraq border to become a channel for bypassing the sanctions. The lack of an alternative to trade with Iran and Iraq's economic woes following the sanctions are therefore liable to plunge Iraq back into political instability and push it into Iran's waiting arms.