



## Subversive Markets: The Economic Roots of the Iraq Insurgency

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In the four years that have passed since the 2003 invasion of Iraq, insurgent elements - both restorationist and ideological - have demonstrated a disconcerting capacity for withstanding structural and organizational change. Shifting patterns of insurgent financing during the first fifteen months of the stabilizing campaign undermined the best-laid plans of the CPA and permanently distorted domestic alliance structures. From Hussein loyalist financiers to 'foreign fighters and couriers' to the present reliance on a complex array of indigenous sources, the insurgency in Iraq has evolved to become self-sustaining - and possibly self-perpetuating - generating an estimated \$70 million to \$200 million a year from illegal 'in house' activities.<sup>2</sup> For those who depend on the existence of a shadow economy - be it for operational funding or livelihood - the conflict confers a perverted legitimacy on actions that in times of peace would be punishable as crimes.<sup>3</sup> Whether violence is the product of political grievance, interethnic dispute or networked security dilemmas, the back channels of subversive markets provide the lifeblood necessary to sustain it. For as long as this parasitic opportunity structure remains viable, conflict will persist not so much *despite* the intentions of rational people, as *because* of them.<sup>4</sup>

The insurgency in Iraq has always been made up of an eccentric jumble of players - the Sunni Ba'athist underground, radical Shi'a, foreign jihadists, indigenous tribal groups and organized and petty criminals. Each has struggled for a Darwinian foothold in the local economy with interests that coincide as often as they collide. The black and grey markets at the periphery of conflict act as an incubator for these relationships and have played an important role in sustaining the insurgency by strengthening ties between ideologues and profiteers. From oil smuggling to kidnapping, counterfeiting to Islamic charity connivance, the Iraqi government and its American patrons have largely been unable to thwart the predatory rent-seekers that make their home on the fringes of the more organized segments of the economy. As a consequence, Iraq has experienced extraordinarily damaging delays in development, economic growth and job creation. The resulting surge in unemployment has fed back into the insurgency to create a downward spiral of economic collapse, criminal activity, and political violence. With the Maliki government estimating levels of unemployment at 17 per cent,<sup>5</sup> recruitment of unaligned bandits has become systematized in a franchise of 'pay scale insurgency' unique to Iraq, where as little as \$50 can buy a recruit willing to plant explosives on a highway or shoot a policeman,<sup>6</sup> \$200-\$300 will buy an attack on a Humvee, and \$1,000 a helicopter.<sup>7</sup> These are the mercenary cogs of a

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complex profit mechanism that relies on violent aggravation for the disorder left in its wake.

The conspicuous shortsightedness of the Iraqi government in neglecting what might otherwise be a manageable problem for criminal prosecution, is attributable in no small part to the prevailing climate of impunity generated by faltering mechanisms of accountability.<sup>8</sup> Corruption has become a growth industry in the new Iraq with the Special Inspector General for Iraq Reconstruction (SIGIR) estimating the cost to the country at \$4 billion a year. This erosion of the institutional capital of government continues to fuel a cycle of dependency.<sup>9</sup> Corrupt state officials need the cloak of violent unrest provided by the insurgency, and the insurgency, in turn, relies on corruption in government for political accommodation and the persistent postponement of massive infrastructure reconstruction projects. For as long as security and stability solutions lack adequate mechanisms of accountability, the wholesale looting of Iraq will continue unabated and at a cost to the Iraqi people that cannot be ignored. Oil smuggling and other criminal activity involving the state-owned oil industry is a 25 to 100 million dollar a year business alone.<sup>10</sup> About 10 per cent of the country's refined fuels and 30 per cent of its imported fuels are being stolen, in part because the subsidized Iraqi price of gasoline, about 44 cents a gallon, is less than half the regional price of 90 cents a gallon.<sup>11</sup> A further 10 to 30 per cent of the 4 billion to 5 billion dollars in fuel imported for public consumption in 2005 was smuggled back out of the country for resale.<sup>12</sup> With the cooperation of corrupt Iraqi officials, insurgents have managed to leverage their control over many of the distribution routes in the country to profit from the differential between the official subsidized price and the international market price for gasoline.<sup>13</sup> According to an Oil Ministry report leaked to the Baghdad paper *Al-Furat*, a gas station owner selling a tanker-load of gasoline at the official price could expect to make about \$340 in profit, while selling the same gas on the black market would net more than \$4,800.<sup>14</sup> Other estimates suggest the sums involved could be far higher.

The stagnation in Iraqi oil production and distribution as a revenue generator represents a paramount threat to the fledgling formal economy. Addressing the problem requires increased capacity for enforcement at the provincial level targeting smuggling, as well as a new strategy for the protection and redevelopment of Iraq's battered oil infrastructure. The success of these measures will hinge upon the willingness of 'clean' officials to institutionalize increased transparency at the political level. Sanitizing the political atmosphere in Baghdad is a necessary first step to de-legitimizing the lucrative links to the black market exploited by corrupt oil officials. The trouble is that most anti-corruption campaigns have failed. Iraq has a Commission on Public Integrity which, along with the Iraqi Board of Supreme Audit and inspector generals in the ministries, is designed to investigate corruption. Yet, of the 1370 cases the Commission had sent to the central criminal courts by July of 2006, only 40 yielded convictions, and only one of those convicted was a senior ministry official. The Chairman of the Commission, Radhi Hamza

al-Radhi, places the blame on a discreet restriction that makes it impossible to bring to justice a high-level official without the permission of his minister.<sup>15</sup> Where the ministers themselves are implicated, one might logically conclude that they might not view it as being in their best interest to offer their full cooperation. Anti-corruption campaigns must begin to address these limitations if they are to serve any purpose.

Of course, in Iraq, no one criminal activity is starved for company, and the unsavoury niche markets avoided by corrupt officials are quickly filled by those with less to lose. The drug trade, for example, after years of strict control and punishment by death under the Hussein regime, has begun making a comeback. Lacking much hard data, the United Nations' International Narcotics Control Board (INCB) has pointed to massive seizures on the Jordanian border as evidence drug smugglers have turned the country into a transit route for Afghan heroin. After being interrupted by a 2000-01 crackdown by Saddam Hussein, the weakening of border controls and security infrastructure has made Iraq into a convenient logistical staging area for traffickers. Samawah, the closest town to the Saudi Arabian border, has become a functional transit point, though only for so long as the Kingdom is occupied with the construction of a 550-mile high-tech fence to seal off its northern neighbour. By the summer of 2008 it is likely drug routes will be limited to the northern pass from Iran to Turkey (the Balkans pipeline for distribution in Western Europe) and a southern route to the Iraqi port of Umm Qasr, where it transits alongside illegally tapped oil and looted copper into the Gulf States.<sup>16</sup>

Though newly established authorities in Iraq are co-operating with drug control bodies, they lack sufficient resources and their efforts are plagued by the sheer number of entry points on Iraq's porous borders. What's more, on a list of insurgency related problems that reads like an overextended shopping list, the notable aversion to drug smuggling of high-value target groups in the insurgency, detracts from its importance as an enforcement priority. Despite the profit to be made in the drug trade, organized radical elements of the insurgency under Al-Qai'da's leadership have proven to be wary of engaging the industry for fear of detection and exposure for profit by rival drug barons.<sup>17</sup> These groups can afford to be selective. Terrorist and insurgent expenses are moderate and pose few significant restraints to armed groups in Iraq. In particular, arms and munitions costs are negligible. With a self-sufficient and potentially regenerative financial structure, jihadists have the resources to create market demand for a diverse range of illicit services. One of the more visible of these, kidnapping, has become something of an informal institution in post-Sadaam Iraq.

In early 2004, an average of two people were kidnapped every day in Baghdad with a typical ransom of about \$25,000 paid for their release. Both figures have steadily increased so that by the end of that year the average had risen to ten kidnappings per day with as much as \$36 million a year flowing into the country to pay ransoms.<sup>18</sup> Not only does this drive a street-level hostage economy, but the scale of the enterprise - 30 domestic

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kidnappings a day across the country in December 2005 - further serves to wilfully exploit popular dissatisfaction with the 'paper tiger' security presence of the national gendarmerie and the Iraqi Police Service. For a people accustomed to stifling authoritarianism under Saddam Hussein, the post-intervention upsurge in crime is fundamentally and understandably disturbing.<sup>19</sup>

When US forces entered Baghdad on April 9, 2003, they were unprepared for the rapid spread of crime and anomie. A basic misunderstanding of the psychology of totalitarianism and the passivity of long oppressed populations, led U.S. decision-makers to place unfounded trust in the post-intervention public security capacity of Iraq's least effective security force.<sup>20</sup> Failure to establish effective anticrime programs with the Iraqi Police Service (IPS) was accompanied by a greater failure to rebuild and rehabilitate the Ministry of the Interior (MOI) in an environment of rampant corruption.

Infiltration by Shiite militias in both the administration and execution of justice has fuelled sectarian tension and distrust of the police, particularly in Sunni areas.<sup>21</sup> In November 2006, the Director of the Defense Intelligence Agency (DIA) stated that the Ministry of Interior and the Iraqi police were heavily infiltrated by militia members of the Badr Organization and Mahdi Army. According to the DIA Director, the Mahdi Army often operates under the protection or approval of Iraqi police to detain and kill suspected Sunni insurgents and civilians.<sup>22</sup>

Unfortunately, despite recent developments responding to the need for fundamental reorganization - including appointment of a 'clean' Interior Minister and provision by the U.S. of a 100-member Ministry Transition Team (MTT) of American advisers - there is no Iraqi or U.S. plan that goes beyond platitudes for ministerial reform. The decentralization of operational control of the police to the provinces means Baghdad has no ability to verify the accuracy of provincial budgets or account for how the money is utilized.<sup>23</sup>

The problem is further compounded by a duality in the Iraqi personality that subordinates rules regulating conflicts of interest to tribal allegiance.<sup>24</sup> At least three quarters of the population of Iraq belong to one of the one hundred and fifty of the nation's tribes. A strong synchronized Tribal Leader engagement policy that includes local and provincial leaders in security, social and economic affairs is needed to create a committed local population in targeted areas.<sup>25</sup> Even with such a policy in place, lacking sufficient advisers to conduct effective oversight in both the ministry and the provinces, the shadow economy and the criminal infrastructure that nourishes it will continue to grow.

At the operational level, vetting and retraining of IPS and National Police gendarmerie personnel will help but they will remain limited in their capacity to address the general lawlessness that is endemic in Iraq for so long as they lack combat training and regimental discipline. Sustaining a commitment to allocating sufficient economic and political

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resources to get the job done will not be easy. It will require the indefinite presence of American advisers, political pressure, and persistence. With any luck, the calamitous alternative to addressing these problems should be sufficiently compelling to drive progress on the issue.

Daily news coming out of Iraq of economic mismanagement, vast black markets in gasoline, and increased crime do not bode well. The criminal bazaars that operate outside, and at the expense of, the legal and formal economic activity of the state, create incentives for promoting violence to defray the costs of waging war.<sup>26</sup> But an informal economy will thrive in Iraq only for so long as the formal economy remains incapable of taking its place. To date, violence, crime and uncertainty over the future have undermined investor confidence, preventing market-driven mechanisms from playing their anticipated role. Allocating sufficient resources to the police services to address these problems requires first that action be taken to address inefficiencies and legal loopholes in Iraq's accountability mechanisms. Only by sanitizing the political space of corrupted elements can the re-prioritization of public expenditures positively contribute to formal sector development and a corresponding contraction in the informal economy. A triumph of political will may go a long way to bringing the economy out of the shadows and bringing stability back to Iraq.

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<sup>1</sup> The views expressed in this paper are those of the author alone and do not necessarily reflect the corporate view of RUSI.

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<sup>3</sup> Keen, David, *The Economic Functions of Violence in Civil Wars*, Adelphi Paper 320, (London: International Institute for Strategic Studies IISS, 1998), p. 12

<sup>4</sup> Keen, 1998, p. 11.

<sup>5</sup> Espo, David, 'House OKs Plan to Withdraw US Troops,' *Breitbart.com*. Available Online:

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<sup>6</sup> Ibid

<sup>7</sup> Howard, Michael, 'It's a pay scale for the Iraqis: \$700 for an attack on a tank; \$1,000 for a helicopter,' *The Guardian*, November 3, 2003. Available Online:

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<sup>8</sup> Collier, Paul, 'Doing Well Out of War: An Economic Perspective,' in *Greed and Grievance: Economic Agendas in Civil Wars*, Mats Berdal & David M. Malone, eds. (London: Lynne Rienner Publishers, 2000); p. 103

<sup>9</sup> Transparency International, 'Corruption Perceptions Index 2006,' Available:

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<sup>10</sup> Burns and Semple, *The New York Times*, November 26, 2006.

<sup>11</sup> Pincus, Walter, 'Corruption Cited in Iraq's Oil Industry,' *The Washington Post*, July 17, 2006. Available Online: [http://www.washingtonpost.com/wp-dyn/content/article/2006/07/16/AR2006071600774\\_pf.html](http://www.washingtonpost.com/wp-dyn/content/article/2006/07/16/AR2006071600774_pf.html)

<sup>12</sup> Burns and Semple, *The New York Times*, November 26, 2006.

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- <sup>15</sup> Harriman, Ed, 'The Least Accountable Regime in the Middle East,' *London Review of Books*, November 2, 2006. Available Online: [http://www.lrb.co.uk/v28/n21/harr04\\_.html](http://www.lrb.co.uk/v28/n21/harr04_.html)
- <sup>16</sup> Looney, 2005
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- <sup>18</sup> Looney, 2005.
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- <sup>24</sup> Seventy-five per cent of Iraq's estimated 26 million people belong to one of approximately 150 tribes that are composed of about 2,000 smaller clans, with varying sizes and influence.
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