

# CAUSES OF RECENT GLOBAL CRISIS AND EFFECTS TO NORTHERN IRAQ

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## Abstract

The Crisis started in the USA which is one of the biggest economy of world has spread to the all over the world. Because of wavelength made it global by affecting financial market. Many banks went to bankruptcy and many countries were caused damaged.

We analyzed crisis under three main titles in this study: First, we studied causes of crisis. Second, we analyzed effects of it over the world economy. Third, crisis started in USA has affected firstly American economy in that case, we analyzed effects of crisis in the Northern Iraq which is under control of USA.

I have been in northern Iraq for two years. I tried to reach original sources, have interview with men charged in government and observed in order to study well the impact of crisis on people and government. As effects of crisis world production decreased, unemployment rate increased, lots of corporations went to bankruptcy... in these situations northern Iraq, especially, crucial city Erbil, has been continuing in construction site. It was seen that country's economy is based on mostly oil sector and no enough industry, agriculture, raising livestock have affected impact of global crisis on that region.

**Key Words:** global, crisis, cause, America, effect, northern Iraq

## Global Krizin Sebepleri ve Kuzey Irak'a Etkisi

### Özet

Dünyanın en büyük ekonomisine sahip ABD'de başlayan kredi krizinin finans piyasalarına yansısıyla dalganın boyu krizi globalleştirdi. Birçok bankalar tarihe karıştı, ülkeler batma noktasına geldi.

Bu çalışmamızda global krizi üç ana başlık altında inceledik: Birincisi; ekonomik krizin sebepleri üzerinde duruldu. İkincisi kısım; dünya ekonomisine nasıl etki oluşturduğu üzerine bir çalışma oldu. Üçüncü kısımda ise; Amerika'da başlayan kriz ilk olarak Amerikan ekonomisini etkilerken, Amerika etkisinde bulunan Kuzey Irak bu krizden etkilendimi ve ne ölçüde etkilendiği üzerine çalışma yapıldı. Yaklaşık iki yıldır Kuzey Irakta yaşayan biri olarak halkın ve bölgesel yönetimin krizden etkilenmesini birinci el kaynaklardan, birebir görüşmelerden ve gözlemleme yöntemine göre bir çalışma yapıldı.

Dünyanın birçok ülkesinde kriz akabinde üretim yavaşlarken, istihdam azalırken, peşpeşe iflas eden devasa şirketler sıraya girerken, Kuzey Irak bu zaman zarfında özellikle de başkent Erbil bir şantiye konumunu sürdürmektedir. Bölgenin hatta ülkenin ekonomisi petrole dayalı olması tarımı, hayvancılık ve sanayi kuruluşlarının yeterli olmaması krizin etkisini etkilediği görülmektedir.

**Anahtar kelimeler:** Evrensel, kriz, sebep, Amerika, etki, kuzey Irak

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## 1. Introduction

Iraq<sup>2</sup> ranks fourth in the world behind Saudi Arabia, Canada, and Iran in the amount of Oil reserves with its 115 billion barrels of proved oil reserves. (Shafiq, [www.iraqoilreport.com/ oil/ production -exports/ comment-analysis-iraqs-oil-and-gas-challenges-and-opportunities-3613/2010](http://www.iraqoilreport.com/oil/production-exports/comment-analysis-iraqs-oil-and-gas-challenges-and-opportunities-3613/2010)) Iraq's economy is dominated by the oil sector, which has traditionally provided about 95% of foreign exchange earnings. In the 1980s financial problems caused by massive expenditures in the war with Iran in span of eight years, and Iraq suffered economic losses from the war of at least US\$100 billion.(Wikipedia, [http://en.wikipedia.org/ wiki/Iraq](http://en.wikipedia.org/wiki/Iraq), 2010) Iraq was under Baath Party rule from 1968 to 2003; in 1979 Saddam Hussein took control and remained president until 2003 after which he was unseated by a US. Iraq which has 31,234,000 people estimated in 2009, has a number of ethnic minority groups: Kurds, Assyrians, Mandeans, Iraqi Turkmen, Shabaks and Roma.

This study mostly includes Kurds<sup>3</sup> (Hekimoğlu, 2009, p.9) have established their own autonomous region. It borders Iran to the east, Turkey to the north, Syria to the west and the rest of Iraq to the south. Its capital is the city of Arbil, The region is officially governed by the Kurdistan<sup>4</sup> Regional Government (KRG). The three governorates of Duhok, Arbil and Sulaymania accumulate a territory of around 40,000 square kilometers and a population between 4 and 6.5 million. As a major economic power in Iraq, Kurdistan has the lowest poverty rates and highest standard of living in Iraq, because of the most stable and secure<sup>5</sup> (Human Development

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<sup>2</sup> Iraq is located at 33°00'N 44°00'E. Spanning 437,072 km<sup>2</sup> (168,743 sq mi), it is the 58th-largest country in the world. Iraq mainly consists of desert, there are two major rivers -Euphrates and Tigris- are fertile alluvial plains, as the rivers carry about 60 million cubic metres. The north of the country is mostly composed of mountains; the highest point being at 3,611 metres point, known locally as Cheekah Dar (black tent). Iraq has a small coastline measuring 58 km along the Persian Gulf. Close to the coast and along the Shatt al-Arab. The local climate is mostly desert, with mild to cool winters and dry, hot, cloudless summers. The northern mountainous regions are called as Kurdistan region.

<sup>3</sup> Kurds' language is Kurdish that is spoken in Turkey, Iran, Iraq, Syria, and Armenia. Approximately 20-25 million people use that language. It is accepted as official language in Irak and KRG. According to Abdulmelik Firat Kurdish has over 100 000 words.

<sup>4</sup> The name Kurdistan literally means *Land of the Kurds*.

<sup>5</sup> Whereas, People affected by conflict and insecurity can suffer some of the worst human development outcomes of all migrants. It is estimated that, internally displaced persons number some 26 million, including 2.8 million in Iraq in 2009.

Report, 2009, p. 26) region of Iraq. There are consulates and representation offices of countries: United States, the United Kingdom, Germany, France, Italy, Israel and Russia. The relative security and stability of the region has allowed the KRG to sign a number of investment contracts with foreign companies. The first new oil well was drilled in the Kurdistan region by the Norwegian energy company DNO in 2006. And later, two other oil companies, Canada's Western Oil Sands and the UK's Sterling Energy. (Wikipedia, [http://en.wikipedia.org/wiki/Iraqi\\_Kurdistan](http://en.wikipedia.org/wiki/Iraqi_Kurdistan), 2010) The government goes on to receive a portion of the revenue from Iraq's oil exports, and the government has a aim that is to implement unified foreign investment law. The KRG also has plans to build a media city in Arbil and free trade zones near the borders of Turkey and Iran.

It is seen that three Northern Governorates' economic situation improved due to the relatively stable security situation since March 2003, and a foreigner-friendly investment law that was approved by the Kurdistan Assembly in July 2006 and aims at attracting foreign capital to the region. In particular bilateral trade with neighbouring Turkey has boomed in recent years. When we analyze annual bilateral trade, it was estimated at around US \$5 billion by April 2007 and Turkish contractors reportedly secured contracts worth US \$2 billion in northern Iraq. A total of 1,200 Turkish companies were estimated to be operating, with employing around 14,000 Turkish employees. Lots investment were done by Turkish companies; hospitals, airport, university, housing, etc (UNHCR, 2007, p.20)

In this study we analyze that causes of recent global crisis and its effect to the world economy especially Iraq and northern Iraq (Kurdistan Regional Government). We wonder how was affected that country is under control of USA where global crises was occurred first. When we search we can face lots article, books, and congress about crises. But, I have been in Erbil for two years if I observe well, maybe I can touch that topic on the other side.

### **1. Causes of Financial crises**

When we look retrospect about economic theory it is accepted that the economy never grows in a smooth. Any country's economy may enjoy several years of exhilarating economic expansion and prosperity. As I mentioned before, this situation cannot be gone on. This accomplishment

might be followed by a recession, depression or a financial crisis. Such as; in 1930s, 1990s, and recent one is 2007s.

### 1.1. Crisis and its History

When economy faces recession<sup>6</sup>, depression or financial crisis national output falls, profits and real incomes decline, unstable price of goods and services occur, and unemployment rate jumps to uncomfortably high levels. Then economy reaches bottom, and recovery begins. This situation can be named as Business Cycles are economywide fluctuations in total national output, income and employment, generally lasting for a period of 2 to 10 years, marked by widespread expansion in most sectors. Upward and downward movements in national output, inflation level, interest rate, and unemployment rate form the business cycle that characterizes whole market economies. (Samuelson and Nordhaus, 2001, p.477) In order to give right policy advice, economists should know the causes of boom and crisis. If a boom or crisis is the result of a spending or price shock GNP will be away from potential. In this situation government should interfere to the economy to speed the return to potential. So, government will use monetary policy -money stock- and fiscal policy – taxes and spending- to solve economic problem as demand shocks (Hall and Taylor, 1991, pp.204-216)

I hope that Policy makers have learned the lessons of history. Ben Bernanke, the chairman of the Board of Governors of the Federal Reserve System, is a student of the Great Depression. He understands that policy mistakes were responsible for the economic crisis of the 1930s. The economic downturn was underway in the second half of 1929, but, not until 1933 were significant steps taken to halt the fall in prices, stabilize the banking system, and encourage investment spending. The views of the current generation of policy makers are very much informed by this historical episode, when the Fed<sup>7</sup> for several years made relatively little use of

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<sup>6</sup> We call short-term fluctuations –cycles-, the actual one is irregular. It usually takes from 6 months to a year. A milder form of business downturn is a recession, which has many of the features of a depression to a lesser extent.

<sup>7</sup> The Federal Reserve System (also known as the Federal Reserve, and informally as the Fed) is the central banking system of the United States

monetary policy, allowing deflationary expectations to set in, and failed to execute its responsibilities as a lender of last resort, allowing the banking system to collapse. The economic downturn was underway in the second half of 1929, but not until 1933 were significant steps taken to halt the fall in prices, stabilize the banking system, and encourage investment spending. When the time comes the crisis erupt in August 2007 than the Fed began flooding financial markets with liquidity. The expansion of its balance sheet is unprecedented. The U.S. economy in the early 1930s was more heavily bank based than today. But, the current crisis has been a crisis not just for banks but for insurance companies, for hedge funds, and for the securities markets themselves. (University of California, Berkeley, [www.econ.berkeley.edu/~eicheng/global\\_credit\\_crisis\\_history\\_12-3-pdf](http://www.econ.berkeley.edu/~eicheng/global_credit_crisis_history_12-3-pdf), 2010)

The Great Depression of 1929 is related to the current Financial Crisis in that both originated in the U.S and have damaged the world economy at a frightful scale. For example; the financial crisis has taken a heavy toll on the US in just a few months was \$5 trillion. (Financial Forum, <http://www.financialcrisis2009.org/news/The-financial-crisis-tab-in-the-US-5-Trillion-4268.htm>, 2010) According to The Institute of International Finance's (IIF) "Capital Flows to Emerging Market Economies (EME)" report was issued in January of 2009, forecast that net private capital flows to 28 EMEs would drop sharply to \$165 billion in 2009 from \$466 billion in 2008 and the record level of \$929 billion in 2007. (Erdilek, 2009, [todayszaman](http://www.todayszaman.com)) And, one more example from a country in Europe; Spain is hitting record numbers of unemployed. Spain government says the jobless rate stands at %11.3, although the EU's statistical agency puts it at %11.9. In every respect, Spain has the highest unemployment rate in the 27-member EU. (Financial forum, <http://www.financialcrisis2009.org/news/Spain-experiences-huge-rise-in-unemployment-4240.htm>, 2010)

In my opinion one of the reasons of financial crisis was/is war; The Great Depression of 1929 emerged from the ashes of the First World War whose cost was evaluated at \$337000.000.000 by British economist and statistician Edgar Grammond. What about today's? It is the same mistake of history, the same manifestation was repeated at the dawn of the 21st century with America's war in Iraq. In 2008, Linda J. Bilmes and Joseph E. Stiglitz of the Washington Post estimated

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the total cost of this war at \$3 trillion “and more.” In their words, “The Iraq adventure has seriously weakened the U.S. economy, whose woes now go far beyond loose mortgage lending.”(Tongkeh, [http://modern-us-history.suite101.com/article.cfm/the\\_global\\_financial\\_crisis\\_in\\_perspective](http://modern-us-history.suite101.com/article.cfm/the_global_financial_crisis_in_perspective), 2010)

## 1.2. Causes of recent global crises

Another closest cause of the current financial turmoil is attributed to the sub-prime mortgage sector in the USA. The crisis could be ascribed to the persistence of large global imbalances, which were the outcome of long periods of excessively loose monetary policy in the especially advanced economies during the last decade. Global imbalances have been manifested through a substantial increase in consumption in the US, it means current deficit. On the other hand, substantial surplus in Asia, particularly in China, and in oil exporting countries in the Middle East and Russia cause global imbalance which were the major underlying cause of the crisis. (Rakesh, <http://www.bis.org/review/r090506d.pdf>, 2010) Let’s continue our topic –causes of recent crises- under three title below.

*-The bursting of the housing bubble causing a reallocation of capital and a loss of household wealth and drop in consumption.*

*-A sharp rise in the equity risk premium (the risk premium of equities over bonds) causing the cost of capital to rise, private investment to fall and demand for durable goods to collapse.*

*- A reappraisal of risk by households causing them to discount their future labor income and increase savings and decrease consumption. (Warwick and Andrew, 2009, p. 10)*

First: If the circumstance is proper the household can choose investment in a capital good. The household capital stock combines housing, and other durable goods. (Here, we take care housing) When we look near past we see that the Federal Reserve cut interest rates by a total of 550 basis points in a series of steps between 2001 and 2004. The housing bubble was the result

of a long period of low interest rates by the US Federal Reserve. From 2000 to 2006, house prices in some areas doubled to subsequently collapse. While house prices were rising so strongly, credit was supplied liberally to meet the demand as perceptions of risk fell. The rising wealth boosted confidence and spending. These changes in some areas have generated dramatic news headlines but, overall the United States index of house prices has fallen by 6.2 percent in real terms from the 1st quarter 2008 to the same quarter in 2009. Falling house prices has a major effect on household wealth, spending and defaults on loans held by financial institutions. Finally we saw that housing bubble bursting fuelled financial crisis. Here you can ask why does USA cut interest rates? Answer is this: Low interest rates were due to fears of deflation and led to a boom in US housing, and, US bond yields were also low because of low world rates (for example, Japanese bond yields at a little over 1 per cent and short term interest rates at zero). There was also an international aspect: Japan and Europe also affected US to keep interest rates low. (Warwick and Andrew, 2009, p. 1) Second: Because of the bankruptcy of Lehman Brothers in September 2008, current economic and financial environment of the world economy, the global financial system and for central banks have been faced the a very difficult time.

(Rakesh, <http://www.bis.org/review/r090506d.pdf>, 2010) Lehman has held large positions in the subprime and other lower rated mortgage markets. Brothers' failure was primarily due to the large losses they sustained on the US subprime mortgage market. Losses of \$2.8 billion have been reported by Lehman in the second fiscal quarter 2008. It was forced to sell off \$6 billion in assets. The failure of Lehman Brothers affected on equity risk premiums across markets. (Warwick and Andrew, 2009, p. 1) Third: Firms' reappraisal of risk has discounted households' labor income that fuelled increasing saving and decreasing consumption. That situation is also another cause of financial crisis.

## **2- Effects of Financial crises to world economy**

According to Paul A. Samuelson recession has some characteristics, first: Consumers decrease their consumption. Because of that producers (investors as well as foreign investors) react by curbing production. So, real GDP falls. Second: If producers curb production this causes no need more labor force. Finally, that follows layoff and higher unemployment. Third: when demand for raw materials decreases their price also decreases. Fourth: finally we see that business profits fall sharply in crisis. (Samuelson and Nordhaus, 2001, p. 479) Theoretically, financial crises effect

economy so as we counted above, now, I will try to analyze impact of recent global financial crisis among countries.

### **2.1. Effects of Crises on Developed Countries –USA-**

As everyone now well knows, the United States is facing its greatest financial crisis since the Great Depression of the 1930s. I wonder how American capitalism will be fundamentally changed by the crisis. First of all we see that the United States is in the midst of its most serious banking crisis in seventy years, stirring terrible memories of panics, bank failures, bankruptcies and mass unemployment. Fannie Mae and Freddie Mac, the two largest US mortgage providers, holding over \$5 trillion in mortgage debt. (Dornbusch and Fisher, 1994, p. 589) Then, Lehman Brothers problem..... The facts are that financial firms (e.g., Lehman Brothers, Merrill Lynch, Bear Stearns, Goldman Sachs, etc.) were significantly exposed when it came to the cycles of the economy. As long as the economy was expanding, their exposure was protected. However, when the housing industry began its radical decline, that exposure became potentially lethal. According to Samuelson: Lehman Brothers was typical example. In late 2007, it held almost \$700 billion in stocks, bonds and other securities. Meanwhile, its shareholders' investment (equity) was about \$23 billion. All the rest was supported by borrowings. (Eckman, [http://www.issuesinperspective.com/2008/Sept/08sept27-28\\_1.cfm](http://www.issuesinperspective.com/2008/Sept/08sept27-28_1.cfm), 2010) The recent report on profit loss by firms (Citicorp, Merrill Lynch, and the Bank of America) are scaring enough to spread fear around the globe. Citicorp and Merrill Lynch<sup>8</sup>, each one reported \$10 billion loss of profit, causing massive layoff of 21,000 employees, on the other hand, the Bank of America also joined to lay off 1,100 employees that will be followed by many Fortune 500 corporations. (Hubert, [http://www.koreatimes.co.kr/www/news/opinion/2008/03/160\\_21061.html](http://www.koreatimes.co.kr/www/news/opinion/2008/03/160_21061.html), 2010) That impact was seen in Brazil 654,000 jobs lost in December as the global crisis hits Latin America's largest economy. The countries worst affected sectors were industry, agriculture and construction. (Financial forum, <http://www.financialcrisis2009.org/news/Brazil-loses-654-000-jobs-in-December-4212.htm>, 2010)

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<sup>8</sup> Merrill Lynch and other financial institutions are inducing foreign investment into the U.S. from Kuwait, Saudi Arabia, South Korea and Japan.

As a result, America's domestic and foreign debt continued increasing. It was seen that both the US current account deficit and its debt-financed housing boom were unsustainable: it was unclear whether the dollar or the housing bubble would collapse first. (Skidelsky, 2009, p.1) Beginning with failures of large financial institutions in the US, it rapidly evolved into a global financial crisis, deflation and sharp reductions in shipping resulting in a number of European bank failures and declines in various stock indexes, and large reductions in the market value of equities (stock) and commodities worldwide. (JICA Research Institute, <http://www.dxal.net/effects-of-global-financial-crisis-of-2008-2009/>, 2010)

However, The outcome of the current financial crisis is clearly evident to among countries . Stock markets stopped working properly all over the world, with declines ranging from 35-40% over the past 12 to 18 months in developed countries and even more in most emerging markets. The crisis also has induced significant limitations to investment banking in the United States during the past decade, and a severe recession in most advanced countries and much slower growth in emerging markets. This is likely to be the worst economic recession since the 1930s. (Salvatore, [http://www.geam.com/common/newsdocs/The\\_Financial\\_Crisis-CEPRIS.pdf](http://www.geam.com/common/newsdocs/The_Financial_Crisis-CEPRIS.pdf) , 2010) It is clear that global financial crisis affected developed countries. Such as GDP growth rate was 5.2 (2007), 3.2 (2008), -1.3 (2009) for US, 2.7 (2007), 0.9 (2008), -3.8 (2009) for European countries. (Akrasanee, 2009, p.9) *According to The Least Developed Countries Report 2 009* argues that the impact of the global economic crisis is likely to be so severe in the least developed countries (LDCs) that “business as usual” is no longer possible. (UN, 2009 A, p.14)

## **2.2 Effects of Crises on Developing and the Least Developed Countries**

The global financial crisis is hitting developing countries hard. The financial crisis is not a natural disaster. It was made by people, and is the product of decisions made by companies and by governments. Although developing countries didn't make this crisis, it is clear that they are in the firing line when it comes to suffering its effects. For example; Action Aid has calculated that Africa will suffer a real drop in income that is predicted to reach US\$49 billion between the start of the crisis in 2007 and the end of 2009. If we compare two recent crises we see that the impact relative to GDP is nearly double the impact of the Asian financial crisis of the late 1990s.

(ActionAid,[http://www.actionaidusa.org/assets/pdfs/intl\\_policy/Where%20does%20it%20hurt%20final.pdf?window\\_id=1](http://www.actionaidusa.org/assets/pdfs/intl_policy/Where%20does%20it%20hurt%20final.pdf?window_id=1), 2010) Generally, the level of potential output in developing countries could be reduced by between 3.4 and 8 percent over the long run, compared with its pre-crisis path. (World Bank, 2010, p.1) There are several transmission channels by which the financial crisis is spreading around the world. Moreover, with recession looming in the industrialised world – which accounts for more than sixty percent of world output – exports from developing and emerging countries will take a hit. A slowdown of world growth will also affect energy and commodity prices, which will hurt energy and commodity exporting countries while importers will get some relief. Last but not least, the crisis has already affected remittance flows from industrialised to developing countries, an important source of income for many countries. (German Development Institute, [http://www.die-gdi.de/CMS-Homepage/openwebcms3.nsf/\(ynDK\\_contentByKey\)/MPHG-7LGCLP?Open&nav=expand%3AVeranstaltungen%3Bactive%3AVeranstaltungen%5CMPHG-7LGCLP](http://www.die-gdi.de/CMS-Homepage/openwebcms3.nsf/(ynDK_contentByKey)/MPHG-7LGCLP?Open&nav=expand%3AVeranstaltungen%3Bactive%3AVeranstaltungen%5CMPHG-7LGCLP), 2010) When we look carefully we see that which countries are most affected for 16 low and middle-income countries. Every single country in our sample, and sub-Saharan Africa as a whole, is predicted to see a real drop in inflows between 2007 and 2009. (ActionAid,[http://www.actionaidusa.org/assets/pdfs/intl\\_policy/Where%20does%20it%20hurt%20final.pdf?window\\_id=1](http://www.actionaidusa.org/assets/pdfs/intl_policy/Where%20does%20it%20hurt%20final.pdf?window_id=1), 2010)

**Table 1: Financial inflows and export earnings, 2007-2009 (current US\$, millions)**

Country	Total inflows 2007	Total inflows 2008	%change 2007-08	Predicted Inflows 2009	% change 2007-09
Sub-Saharan Africa	368.373	371.536	1	319.077	-13
South Africa	118.022	95.203	-19	62.307	-47
Korea	391.344	391.437	0	243.458	-38
Turkey	167.316	147.738	-12	109.871	-34
Brazil	255.005	219.845	-14	176.816	-31
Russia	481.195	500.475	4	338.667	-30
India	247.932	222.825	-10	175.344	-29
Nigeria	95.900	115.777	21	71.133	-26
Venezuela	68.934	94.021	36	52.862	-23
Malaysia	193.857	199.362	3	161.791	-17
China	1.372.763	1.446.750	5	1.075.844	-22

**Source:** ActionAid, **Where does it hurt? The impact of the financial crisis on developing countries,** UK, March 2009  
[http://www.actionaidusa.org/assets/pdfs/intl\\_policy/Where%20does%20it%20hurt%20final.pdf?window\\_id=1](http://www.actionaidusa.org/assets/pdfs/intl_policy/Where%20does%20it%20hurt%20final.pdf?window_id=1)

The financial crisis affected factors such as bank lending, equities and foreign direct investment. Of all the money that flows into developing countries, it is bank lending that has been hit the hardest. According to the Institute of International Finance (IIF) foreign bank lending to developing countries dropped sharply. In other words, net flows to developing countries were actually negative. The turmoil in financial markets has also had an impact on developing country equities markets and FDI (see Table).

Table 2: Financial Market

Type of financial flow	Predicted change for developing countries. 2007-2009 (%)
Bank lending	-115
Equities	-82
FDI	-34

**Source:** ActionAid, **Where does it hurt? The impact of the financial crisis on developing countries,** UK, March 2009  
[http://www.actionaidusa.org/assets/pdfs/intl\\_policy/Where%20does%20it%20hurt%20final.pdf?window\\_id=1](http://www.actionaidusa.org/assets/pdfs/intl_policy/Where%20does%20it%20hurt%20final.pdf?window_id=1)

On the other hand we highlight that the losses were mainly from trade revenue, and would depend on each country's mix of exports and main trading partners. However for the some low income countries, the predicted trade losses varied from a fall of up to 25% in export earnings between 2007 and 2009.

(ActionAid,[http://www.actionaidusa.org/assets/pdfs/intl\\_policy/Where%20does%20it%20hurt%20final.pdf?window\\_id=1](http://www.actionaidusa.org/assets/pdfs/intl_policy/Where%20does%20it%20hurt%20final.pdf?window_id=1), 2010)

One more tragic story from World Bank Report: *“It was really hard to live on 200 baht (approximately 6 USD) a day when I had to buy food and milk for a child, and still had to pay*

*rent as well as other expenses,”* said the 50-year-old grandmother<sup>9</sup>, recalling the difficulties of reduced wages before she found her new job. *“I never had any money left back then. Now I can relax a little bit and save a little bit every month.”* We can face such kind of tens of millions of stories such as Nit’s—and some far worse—each echoing the pain of a historically deep and synchronized recession, in which virtually no country has remained untouched by the bursting of a global financial bubble, and the poorest remain the most vulnerable. According to a new World Bank report, “Global Economic Prospects 2010: Crisis, Finance, and Growth,” the crisis is having serious cumulative impacts on poverty, Researchers Jed Friedman and Norbert Schady estimated, for instance, that between 30,000 and 50,000 additional children may have died of malnutrition in Africa in 2009 because of the crisis. (World Bank, 2010, p.4)

What about inflation in developing countries? In 2008 sharp rise was seen in food and fuel prices. But, in 2009 commodity price has resulted in the inflation rate falling dramatically. For instance, inflation in low-income countries peaked at 15.4 percent in the middle of 2008, but as of July 2009 had declined to 3.4 percent. (World Bank, 2010, p.35) When we visualize business cycle, world economy has been at bottom of fluctuation, then, after 2009, data shows that global GDP has begun recovering; output grew rapidly during the second half of 2009 and is expected to go on to do so during the first half of 2010. However, as the positive contribution to growth from fiscal stimulus, growth will slow, in part because spending by households and the banking sector will be less buoyant as they rebuild their balance sheets. As a result, global GDP growth, which is projected to come in at %2.7 in 2010 (after an unprecedented %2.2 decline in 2009), is expected to accelerate only modestly to %3.2 in 2011. (World Bank, 2010, p.2)

**Table 3: A modest recovery**  
*(real GDP growth, percentage change from previous year)*

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<sup>9</sup> January 21, 2010—Nit Ponpaengpa, a widowed grandmother who works as a massage therapist in Bangkok

Region	2007	2008	2009c	2010f	2011f
World	3.9	1.7	-2.2	2.7	3.2
High-Income Countries	2.6	0.4	-3.3	1.8	2.3
Euro Area	2.7	0.5	-3.9	1.0	1.7
Japan	2.3	-1.2	-5.4	1.3	1.8
United States	2.1	0.4	-2.5	2.5	2.7
Developing Countries	8.1	5.6	1.2	5.2	5.8
East Asia and Pacific	11.4	8.0	6.8	8.1	8.2
Europe and Central Asia	7.1	4.2	-6.2	2.7	3.6
Latin America and the Caribbean	5.5	3.9	-2.6	3.1	3.6
Middle East and North Africa	5.9	4.3	2.9	3.7	4.4
South Asia	8.5	5.7	5.7	6.9	7.4
Sub-Saharan Africa	6.5	5.1	1.1	3.8	4.6
Memorandum Items					
Developing Countries					
Excluding transition countries	8.1	5.6	2.5	5.7	6.1
Excluding China and India	6.2	4.3	-2.2	3.3	4.0

*Source:* World Bank. *Note:* e = estimate; f = forecast; growth rates aggregated using real GDP in 2005 constant dollars.

According to World Bank data recovery is seen as GDP growth rate in developing countries is projected to grow by % 5.2 in 2010, after a modest 1.2% rise in 2009 (-2.2 percent if India and China are excluded), and by a relatively weak 5.8% in 2011. GDP growth is improving, but it will be a long road to full recovery. The strength of the recovery depends on private-sector demand and fiscal and monetary stimulus. An estimated 64 million more people may be living in extreme poverty by the end of 2010 due to the crisis. Developing countries need to anticipate scarcer and more expensive capital. (World Bank, 2010, p.3)

### **3- Effects of Financial Crises on Northern Iraq**

**Iraq** is known as Mesopotamia, was home to some of the oldest civilizations in the world with a cultural history of over 10,000 years. Ottoman rule ended with World War I, and Iraq came to be administered by the British Empire until the establishment of the Kingdom of Iraq in 1932. The Republic of Iraq was established in 1958. The Republic was controlled by Saddam Hussein from 1979 to 2003. (Wikipedia, [http://en.wikipedia.org/wiki/History\\_of\\_Iraq](http://en.wikipedia.org/wiki/History_of_Iraq), 2010)

Currently, Kurdistan is the only legally defined region within Iraq, with its own government. The following governorates are within the region Iraqi Kurdistan: Duhok, Arbil, and Sulaymaniyah

The regional government can levy tax as well as collect taxes in the region, but export and import duties are responsibility of the federal authority. Kurdish regional government's share of natural resources –especially oil- and revenue from the sale of oil products in and outside the country, aid, as well as foreign loans are made by Federal Republic of Iraq in a proportion based on the relation of the region's population to the total population of Iraq. (Jabar and Dawod, 2006, p.238)

### **3.1 Economic History of Iraq**

Iraq's economy was based almost on agriculture until the 1950s, but after the 1958 revolution economic development became substantial. New regime advanced social and economic development program to increase standard of living and improve living conditions throughout the in northern Iraq up to 1959, included the following: housing, electricity, water supply, health, town planning and textile industry. (Jwaideh, 2006, p. 287). By 1980 Iraq had the second largest economy in the Arab world, after Saudi Arabia, and Iraq had developed a command economy<sup>10</sup>. The economy which depends on petroleum<sup>11</sup> exports, suffered during the Iran-Iraq War. Gross domestic product (GDP)<sup>12</sup> actually fell in some years such as; the invasion of Kuwait, Iraq's defeat in the Persian Gulf War, and the UN embargo beginning in 1990. Oil production and economic development both declined after the start of the Iraq War, and the economy has continued to experience serious problems, including a huge foreign debt. Other serious problems include a high rate of inflation; continuing political violence; a shortage of replacement parts hampered the oil sector, outmoded production methods, and outdated technology; a population that has moved away from agriculture; a high rate of unemployment; a

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<sup>10</sup> From 1968 to 2003 Iraq was ruled by the **Ba'ath** (Arabic: "Renaissance") Party

<sup>11</sup> Oil was first discovered in Iraq in 1927 near Kirkūk by the foreign-owned Turkish Petroleum Company, which was renamed the Iraq Petroleum Company (IPC) in 1929.

<sup>12</sup> Petroleum is Iraq's most valuable mineral—the country has the world's second largest known reserves and, before the Iran-Iraq War, was the second largest oil-exporting state. Oil production contributes the largest single portion to GDP

seriously deteriorated infrastructure; and a private sector inexperienced in modern market practices. Following the initial phase (2003) of the Iraq War, the oil-for-food program was ended, sanctions were lifted, and civil administrators appointed by the United States. (Britannica Encyclopedia, [www.britannica.com/EBchecked/topic/293631/Iraq](http://www.britannica.com/EBchecked/topic/293631/Iraq), 2010)

Oil production had reached a level of 560,000 m<sup>3</sup> (3.5 million barrels) per day, and oil revenues were 21 billion in 1979 and 27 billion \$ in 1980. Iraq had about 35 billion in foreign exchange reserves. But, The Iran–Iraq War depleted Iraq's foreign exchange reserves. In December 1999, the UN Security Council authorized Iraq to export under the program as much oil as required to meet humanitarian needs. So, Iraq changed its oil reserve currency from the US dollar to the euro in 2000. Oil exports were more than three-quarters of the pre-war level. However, 28% of Iraq's export revenues under the program were deducted to meet UN Compensation Fund and UN administrative expenses. The global economic slowdown and lower oil prices induced the drop in GDP in 2001. Since the peak of 1980, the nominal GDP of Iraq has steadily shrunk to merely \$12.3 billion in 2000. However, after the overthrow of Saddam, The nominal GDP had reached \$55.4 billion by 2007 due to increase in oil output as well as international prices. From the 1990s until 2003, the international trade embargo restricted Iraq's export activity almost exclusively to oil. In 2003 oil accounted for about US\$7.4 billion of Iraq's total US\$7.6 billion of export value. (Wikipedia, [http://en.wikipedia.org/wiki/Economy\\_of\\_Iraq](http://en.wikipedia.org/wiki/Economy_of_Iraq),2010) Iraq needed such kind of ways for export. So, Turkey is one of the convenient way for oil export. Because Iraq has such a short coastline, it has depended heavily on transnational pipelines to export its oil. In 1977 a large pipeline was completed to the Turkish Mediterranean coast at Ceyhan. When the first Turkish line was completed, Iraq ceased using the Syrian pipelines and relied on the outlet through Turkey and on new terminals on the Persian Gulf. (Britannica Encyclopedia, [www.britannica.com/EBchecked/topic/293631/Iraq](http://www.britannica.com/EBchecked/topic/293631/Iraq), 2010) In 2004 the chief export markets were the United States (which accounted for nearly half), Italy, France, Jordan, Canada, and the Netherlands. In 2004 the value of Iraq's imports was US\$21.7 billion, incurring a trade deficit of about US\$5.2 billion. In 2003 the main sources of Iraq's imports were Turkey, Jordan, Vietnam, the United States, Germany, and Britain. Because of Iraq's inactive manufacturing sector, the range of imports was quite large, including food, fuels, medicines, and manufactured goods. (Wikipedia, [http://en.wikipedia.org/wiki/Economy\\_of\\_Iraq](http://en.wikipedia.org/wiki/Economy_of_Iraq), 2010)

**Table 4: GDP Estimates and Projections (Iraq)**

	2006	2007	2008p	2009p	2010p	2011p
Nominal GDP (in US\$ billion)	49.5	62.4	93.8	83.5	94.8	108.1
Of which non-oil GDP (%GDP)	42.5	43.4	35.8	47.3	45.1	43.1
Real GDP growth (in %)	6.2	1.5	9.8	7.7	7.2	7.3
Per capita GDP (US\$)	1,720	2,109	3,085	2,673	2,957	3,292
CPI (% change)	64.8	4.7	12	10	8	7
Iraqi oil export price (US\$ per barrel)	55.6	63	93.3	62.5	68.5	72.8
Oil production (in mbpd)	2	2.1	2.4	2.5	2.7	2.9

**Source:** World Bank, **International Bank For Reconstruction And Development International Development Association, International Finance Corporation**, February 19, 2009, p.7

It is seen that while the direct impact of the global financial crisis on the economy remains limited, the indirect impact through declining oil prices may be significant. Iraq's banking sector is underdeveloped and centered on the domestic market. Levels of FDI<sup>13</sup> private capital flows are very low. However, the financial crisis has set off a global recession. Crude oil prices fell 25.8 percent in November 2008, averaging US\$54.0/bbl, and fell to a low of US\$40/bbl in early December 2008-down more than US\$100/bbl or 72 percent since peaking in early July. Oil prices are not expected to recover to early 2008 levels in the immediate future. Due to this recent fall in prices, the Government revised the initial 2009 spending budget twice with a lower oil export price (currently US\$50). Table above demonstrates while oil production increases year by year, nominal GDP dropped sharply in 2009. It is clear that decreasing price caused that, but immediate future shows optimistic table. (World Bank, 2009, p.7)

### 3.2 Effects of Financial Crises on Northern Iraq

<sup>13</sup> Let's look the growing impact of the crisis on large TNCs' investment plans by comparing the results of 2009's and 2008's WIPS. In the 2008 WIPS survey, only 40% of companies reported being affected by the crisis, and slightly lower than in the 2007 WIPS. This 2009's picture, in the context of the worst global recession is dramatically different. A large majority of TNCs now believe the global economic downturn and the financial crisis have had a negative impact on their investment plans. (UN, 2009B, p.11)

But, FDI inflows rose only slightly in Bahrain, Iraq and the Palestinian territory, (UN, 2009 C, p. 57)

Recent global financial crises effected all over the world at different level. Although Iraq is the not center of financial crises, Iraq was affected because of USA and low oil prices. In fact, to have rich oil reserve is the good opportunity for countries.

But now that the collapse in the world's economy has caused oil prices to drop, what does the future hold for Iraq? It is known that Iraq's economy depends on oil revenues on a large scale, we can say oil clearly lies at the heart of the country's economy. Indeed, median estimates hold that oil accounts for more than 80 percent of its revenues. Iraq now faces several challenges spawned by the global recession. Iraqi deputy prime minister Barham Saleh said that the economic crisis "has had a serious impact" on Iraq's economy, with "plummeting oil prices" forcing the country "to constrain our government spending." Impact on Iraq's economy means that impact on Northern Iraq or Kurdistan region. Because of the oil boom economy had surplus as \$35 billion from 2008 but Iraq's 2009 budget was slashed about %25 by government. It is from \$80 billion to about \$60billion. However, this budgetary shortfalls will likely directly impact Iraq's ability to maintain security and salaries. America's economic woes but, U.S. will provide additional aid to cover Iraq's budgetary shortfalls. But it is also unlikely that the U.S. will decrease substantially its current commitments to Iraq.<sup>14</sup> Iraqi Central Bank Consultant, Dr. Mazhar Mohammad Salih, said "Iraq received a grant from the IMF worth \$1.8 billion to support liquidity, achieve development and come out of the recession caused by the global financial crisis. Dr. Salih appreciated this step, which he described as 'distinctive', and the grant to push the Iraqi economy forward and enable it to overcome the recession which may affect the Iraqi economy due to the global financial crisis."<sup>15</sup>

"oil-producing countries got burned by the financial crisis, by investing in the West, and they're looking to use their capital in the region instead. Iraqi officials hope that foreign direct

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<sup>14</sup> "The New York Times reported in February that wages ate up 35 percent of Iraq's budget. Many Iraqi lawmakers now fear that the government has gone too far in cutting critical spending. The electricity ministry, for example, has had its capital expenditure budget chopped by over 80 percent, from \$6.4 billion down to \$1.1 billion. "What can we do with \$1 billion?" a ministry spokesman lamented to the Wall Street Journal." (Gartenstein and Goodman, <http://www.jewishpolicycenter.org/966/global-economic-crisis-iraq-future>, 2009)

<sup>15</sup> \$1.8 billion for Iraq to overcome the financial crisis ( IRAQdirectory.com [www.iraqdirectory.com/DisplayNews.aspx?id=10284](http://www.iraqdirectory.com/DisplayNews.aspx?id=10284), 2009)

investment<sup>16</sup> can make up the revenue shortfalls caused by declining oil prices. The "Invest Iraq 2009" conference in London earlier this year reportedly attracted more than 200 companies, including heavy hitters like General Electric and Vodafone. Iraq has also opened its oil fields to bids from multinational firms for the first time since 1973, when its oil industry was nationalized. As one British Petroleum (BP) spokesman told the *Financial Times*, "we could see ourselves back in Iraq by the end of the year barring any unforeseen delays." Bill Murray, a political correspondent for the Energy Intelligence Group in Washington, D.C., thinks that investments by foreign oil companies could help to address the Iraq's economic challenges. (Gartenstein and Goodman, <http://www.jewishpolicycenter.org/966/global-economic-crisis-iraq-future>, 2009) As Baghdad steps up oil production Kurds have been awarding contracts<sup>17</sup> to overseas companies since 2002. Today, Canada's Addax Petroleum (acquired by China Petrochemical), Norway's DNO International, and Turkey's Genel Enerji International have contracts for the Taq Taq and Tawke fields in Kurdistan. According to the Kurds these foreign investors could produce 200,000 barrels a day by the end of 2010—about 10% of Iraq's current output—up. It was 100,000 barrels daily in 2009. (Holland, [www.krg.org/articles/detail.asp?lngnr=12&smap=02010200&rn=73&anr=33488](http://www.krg.org/articles/detail.asp?lngnr=12&smap=02010200&rn=73&anr=33488) , 2010) Iraq's Prime Minister Nouri al-Maliki on 3rd January said in a statement to the press; "The revenue will be part of the national revenue that is distributed equally to all Iraqis".

The anticipated revenue that the Federal Government will receive from the oil production of the Kurdistan Region during the coming five years from 2010 to 2014 will be: \$2.75 billion (2010), \$8.23 billion (2011), \$12.45 billion (2012), \$18.27 billion (2013), and \$25.62 billion (2014). This shows that the Federal Government (Ministry of Finance) will receive in total about \$67 billion as net revenue from the oil produced by companies contracted in the Region in the coming five years (Hawrami, [www.krg.org/articles/detail.asp?lngnr=12&smap=02010100&rn=223&anr=33405](http://www.krg.org/articles/detail.asp?lngnr=12&smap=02010100&rn=223&anr=33405), 2010)

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<sup>16</sup> Iraqi Kurdistan has attracted more than 12 billion US dollars from local and foreign investors in non-oil sectors over the last three-and-a-half years, mainly in housing

<sup>17</sup>But, the Kurds can't sell their oil abroad without help from the government of Prime Minister Nuri al-Maliki, which controls export pipelines. Since the Kurds started oil exports in June, Baghdad has refused to pay the international companies for their share of the export revenue

This issue illustrates that oil revenue coming from the Kurdistan Region will expand economic development of Iraq in general, and it will increase the prosperity of all the Iraqi people. But if price of oil or demand of oil decreases in world market because of crises, that will affect all over the Iraq and directly Kurdistan region.

Arab world would cope with rapidly rising food and raw material prices that threatened their economies and social stability by using high price of oil during the first half of 2008. But, the effects of the financial crisis and expectations of much lower global growth caused a collapse in oil prices. Arab oil exporters experienced deterioration in their terms of trade, and declining surpluses on their balance of payments. OPEC basket price of oil sharply fell by 70% from a peak of just over \$130 per barrel to under \$40 per barrel. In September 2008, with the collapse of Lehman Brothers and the turmoil on Wall Street, stock markets all over the world were affected, including those in the Middle East. In April 2009, oil prices stabilized at about \$50 per barrel, despite falling demand for the international economy. The main reason for this was that oil had become a store of value for those who lost confidence in the dollar. According to the U.S. government's Energy Information Agency, oil income for Arab members of OPEC will continue to fall from \$678 billion in 2008 to \$268 billion in 2009. Iraq's export revenues are forecast to decline from \$59 billion to \$23 billion. This is the clear direct impact on the economies of the larger oil producers. On the other hand, All people experienced rising food prices as well as increases in other costs. This situation is not a manner of dying for these regions, because, According to IMF in 2009 economic growth in the Middle East will be 2.5 percent compared to 6 percent in 2008. As we mentioned before Iraq's and Regional Government's economy is dominated by the petroleum sector, which has traditionally provided about 95% of foreign exchange earnings. (Rivlin, 2009, inFocus) They are not significant exporters of non-oil products, so they are less exposed to the contraction of world trade. In generally, They were affected as much as Iraq could not export amount of oil. When we pay attention to: Prime Minister Barham Salih told that "The Kurdistan Region has been a success, and can be an economic example for development throughout Iraq. We are therefore committed to sustained contact between our governorate officials and governorates throughout Iraq. I would also like to say that a strong Kurdistan Region translates into a stronger Iraq, a stronger Baghdad, a stronger Basra. I am Kurdish, but I am also Iraqi. And as part of Iraq, the Kurdistan Regional Government

hopes you will benefit from our experience, especially in promoting investment.” ( International RepublicanInstitute, [www.krg.org/articles/detail.asp?lngnr=12&smap=02010100&rnr=223&anr=33377](http://www.krg.org/articles/detail.asp?lngnr=12&smap=02010100&rnr=223&anr=33377), 2010) This tells us Kurdistan region<sup>18</sup> has a success economic situation and wants to share that with other parts of Iraq.

In this situation FDI shows its importance as well as neighborliness –Turkey-: 241 investment licences were issued from August 2006 to February 2010. About 1,200 foreign companies working in Kurdistan, the greatest number - some 620 - were from Turkey. Housing attracted around \$4.7 billion in the same period with \$2.29 billion in banking, \$1.6 billion in industry and \$1.1 billion in tourism. (Kimball and Aqrawi, [www.krg.org/articles/detail.asp?smap=02010200&lngnr=12&rnr=73&anr=33844](http://www.krg.org/articles/detail.asp?smap=02010200&lngnr=12&rnr=73&anr=33844), 2010) At ongoing global financial crisis, According to data from the Turkish Statistics Institute (TurkStat), Turkey’s exports to seven neighboring countries -- Azerbaijan, Bulgaria, Georgia, Iraq, Iran, Syria and Greece -- were recorded as \$13.74 billion in 2009, while this figure was \$14.31 billion in 2008, representing a year-on-year fall of 3.9 %. The only neighboring countries that Turkey managed to increase its exports to last year were Iraq and Syria. (Today’s zaman, 2010 A) Exports to Iraq saw a rise of 30.9 %, increasing from \$3.91 billion in 2008 to \$5.12 billion in 2009 (Today’s zaman, 2010 B) .According to the Board of Investors of the Kurdistan Regional Government. Non-oil investment in the Kurdistan Region of Iraq totaled more than \$12 billion over the last three years. Overall, about 70 percent of foreign investment in the Kurdistan Region comes from neighboring Turkey. (PRNewswire-USNewswir, [www.prnewswire.com/news-releases/investment-in-the-kurdistan-region-of-iraq-surpasses-12-billion-84719997.html#linktopagetop](http://www.prnewswire.com/news-releases/investment-in-the-kurdistan-region-of-iraq-surpasses-12-billion-84719997.html#linktopagetop), 2010)

#### **4- Conclusion**

It was seen that there are many causes of recent global financial causes. In our paper we faced main reasons such as:

-The bursting of the housing bubble

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<sup>18</sup> Asharq Al-Awsat, London - Newroz Amin, a representative from the Kurdistan Investment Authority made public that “Over 105 investment projects worth over US \$16 billion in the regions of Erbil, Sulaymaniyah and Duhok have been recorded.” ( Fayad, [www.aawsat.com/english/news.asp?section=6&id=13044](http://www.aawsat.com/english/news.asp?section=6&id=13044), 2008)

-A sharp rise in the equity risk premium

-A reappraisal of risk by households

In my opinion, another reason of crisis is imbalance of consumption and production in the world. In west consumption is vast, in east production is vast. These cause persistence of large global imbalances which was called the greatest financial crisis in USA and spread to the other countries. If we say there is no country was not affected by crisis we don't mistake. Developed countries especially USA and European countries were affected more than developing countries. Most countries' GDP dropped sharply, some huge corporation went to bankruptcy and unemployment rate increased. It is assumed that economy saw the lowest level. Global macroeconomics must be more balanced and global financial market must be more stable.

In fact, Iraq's economic condition was so bad. Iraq's economy was/is based on oil sector. Year by year, production of oil increased, but because of low demand and low price of oil, Iraq was affected from global financial crisis. Therefore, Kurdish regional Government was affected from crisis too, because of being part of Iraq (Kurdish regional government's income comes from Iraq in a proportion based on the relation of the region's population to the total population of Iraq). If Iraq's income decrease this induces low income to that region. But, regional government saw that importance of FDI, then it tried to attract FDI to that region. Finally, Northern Iraq's people are optimistic for future. It was concluded that stability of the Kurdistan region has allowed it to achieve a higher level of development than other regions in Iraq

There are most of countries private sector especially Turkish companies are doing lots investment to this region. Such as; Hospital, airport, factories, housing, university, etc. Kurdish regional government was benefited by FDI as some advantages. Such as; employment rate increased, Kurdish labor force is becoming skillful, managerial experience, regional development, trade balance, qualified goods and services, extra income which we counted are advantages of FDI to this region's people. That's why, standard of living of people in this region is higher than others.

It was analyzed that neighborhood is so important in financial crisis time. Necessities goods, intermediate goods are still being imported by Syria and Turkey.

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