Here comes Erbil

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The devastating effects of the 2003 Iraqi War, subsequent sectarian violence and struggles for power have complicated efforts to promote foreign investment, economic growth and reconstruction efforts in the country thought to hold the “cradle of civilization”. There is, however, a city in Iraq that has managed to not only encourage investment by the private sector, but has made it the heart of its economic ambitions. Since its harsh economic sanctions were lifted, the northern, semi-autonomous Kurdish region of Iraq has declared itself open for business, enticing foreign enterprises with generous investment laws and a relatively secure business environment. Welcome to Erbil.

The Kurdish objective

With an estimated population of 1,294,000[1] , Erbil is the 4th largest city in Iraq. Located in so-called Iraqi Kurdistan, it straddles an interesting divide between the centralized Iraqi government and the Kurdistan Regional Government (the KRG). Although Baghdad’s policies and laws still reach Kurdistan, the KRG is an autonomous authority controlling the three northern governorates of Dahuk, Erbil and Sulaymaniyah. It has its own President – Masoud Barzani – elected assembly, and security forces division[2.] It has successfully unified the leadership within Kurdistan and has its own legislative powers. The KRG’s agenda has allowed for networking events and forums to promote investment and development in the region, such as international exhibitions that are oft frequented by government officials and economists. Although the KRG attempts to woo a European and American crowd, around 55% of foreign companies currently investing in the region are Turkish[3]. Kurdish officials have managed to garner support from countries such as Turkey and Iran before looking beyond the ocean. Governor Nawzad Hadi states “the true objective is to serve the citizen[4]”.

If serving the citizen is the true goal, than the KRG has indeed made significant steps to ensure that it is accomplished. Part of this effort involves putting Kurdish denizens in touch with internationally recognized brands. This requires making key information easily accessible to companies looking to open departments in the region. The KRG’s website, for example, offers documents and text in English, unlike the central governments website. It also has a downloadable and detailed investment brochure and offers translations of its important legislation.

Half way through 2011, Ernst and Young, Rotana and Standard Chartered had already established themselves in Erbil[5]. A shopping centre dubbed “The Family Mall” not only showcases products from Ecco, Timberland, and Samsonite, but also has an indoor skating rink and adjacent outdoor theme park[6]. Goods and services that were unavailable to Iraqis under Saddam Hussein’s regime are now prominently on display.

The result of the KRG’s efforts to gather investment from across the nation and beyond its borders, according to a report by Middle East business News and Data (MEED) is fruitful. During the first half of 2012, Kurdistan drew in $3.4 billion worth of foreign investment, compared to $3 billion in 2011 and $4.8 billion in 2010[7]. Since its touted Investment Law was passed in 2006, the region has attracted “$21 billion in foreign and domestic private sector investment”, $12.5 of which has gone to Erbil[8]. The primary foreign investors in the region are Turkey and Iran, followed by the US, Lebanon, UK, UAE, Jordan, Kuwait, Italy and Germany, contributing to 17% of all investments[9].

Kurdistan plays a particularly important role in trade between Turkey and Iraq, accounting for 75%

of the $12 billion trade in 2011; its contribution is “expected to increase following the opening of a second border crossing”. Local businesses and individuals made up 79% of investment, with the remaining 5% belonging to joint venture companies[10]. Of the 10,500 registered companies in Kurdistan, 11% are international[11]. Kurdistan is evidently proving to the rest of Iraq and the world that it is an economically viable region that continues to grow and prosper.

Erbil: making a name for itself

Arguably, the primary reason for Erbil’s success is the KRG’s 2006 Investment Law. This law provides for: equal treatment of foreign and local investors, the ability for investors to own all the capital of their projects and to repatriate profits in full. Furthermore, projects that meet certain criteria will receive the benefit of free or cheap land. The most enticing stipulations are likely those that give investors a 10-year tax break and the freedom for foreign companies to not have to partner with local firms or have local shareholders operating in the region. This is complemented by a 2009 Iraqi law, which allows foreigners to own land in Iraq.

The rebuilding and creation of key infrastructure has warranted the presence of a number of foreign investors from various sectors at the Erbil International Fair and has engendered construction opportunities. In 2009, the annual Construction Fair showcasing building equipment and electrical appliances amassed 300 companies from 23 countries. With its large, proven oil reserves (estimated at 45 billion barrels), Kurdistan has also garnered attention from East Asia. South Korea has had a consulate in Erbil since 2008 to promote its country’s trade interests in Iraq, and to also enable scholarship and vocation opportunities for regional inhabitants[12]. China also has plans on opening an office in the near future.

With both domestic and international attention being paid to Kurdistan’s capital, the region finds itself economically reborn. Catering for all of the unprecedented visitors, Hilton has recently announced that it will build a 300-room hotel, featuring a spa, boardrooms and both indoor and outdoor pools[13]. The Turkish Divan Hotel, having opened in May 2012, has rooms varying in price from $500 to $15,000 a night, indicating the level of international business it expects to come into the region. With its 8% economic growth in 2011, Erbil’s land prices have increased[14]. In June 2012, the city discussed spending $172 million a year to resolve a residential shortage by building 5,000 residential units a year. The Ministry of Housing and Reconstruction has already started to award contracts[15]. Apart from the incessant housing and commercial building development, foreign car companies such as Porsche and Mercedes have managed to profit from the increasing disposable income in the area. Erbil even has its own stock exchange. It is no surprise that it is often credited as the “Other Iraq” or the “New Dubai[16]”.

Michael O’Hanlon of Brookings Institution explains that influx of foreigners brings a certain market with it: “Reporters, oil workers, diplomats are willing to pay extra to sleep safely, work safely and eat safe food. If the hotel can deliver, then it makes sense for them to expand into high-risk areas[17].” The risks that foreign companies, such as hotels, are subject to are mitigated because “hoteliers are only responsible for operating a property without [incurring] the costs associated with the underlying real estate acquisition[18]”. O’Hanlon also notes, however, that the entry of investors and oil companies into Kurdistan is for the ultimate purpose of “getting a foot in the door to the rest of Iraq[19]”. Nevertheless, Kurdistan strives to differentiate itself from the rest of the country, both politically and economically.

Expanding construction opportunities

The opportunities for construction companies in Erbil are large and continue to grow. They will present themselves in a number of ways, courtesy of the various concurrent projects in operation. Fady Darwish, General Manager of the annual Erbil construction fair, notes: “with some $25 billion in housing projects, $8 billion in transportation and $5.5 billion in water and sewage, the Iraqi government is focusing primarily on reconstruction and rehabilitation[20].” Governor Hadi stresses the importance of water, stating, "the future focus of the KRG is on building dams, irrigation systems and addressing the water system[21]". Cement plants are being constructed or redone across Iraq to facilitate the growing need for "construction solutions[22]". Although the water management system in Dubai may be complex, the city had the necessary infrastructure before Erbil. In this sense, the two cities are dissimilar. Like Dubai, however, there is an influx of foreign workers for service jobs, which results in competitive pricing and a potent workforce.

Making use of the increase in foreign labour, projects currently underway include the construction of two Best Western Premier hotels to be completed in 2013 and 2014 respectively. Glenn de Souza, VP of Best Western's International Operations Asia, remarked that Erbil was the "natural first choice" for development in Iraq considering its increasing access to air transport, important roads and status as a recognized trading centre[23]. Empire Iraq is also scheduled to build an upscale Marriot hotel and series of executive apartments expected to cost over $100 million to complete[24]. Perhaps more important than the buildings are the roads connecting them. Kita, the first Turkish company to offer logistics and trucking information in Iraq, opened an office in Erbil because of its proximity to strategic oil and gas locations[25].

In relation to oil, the KRG recently agreed with Korean engineering company Posco and Korea National Oil to construct two plants for $700 million[26]. Foreign companies such as Kita and Posco, in not having to establish partnerships with local entities, are therefore able to bank greater profits.

Risk assessment

One of the biggest issues that companies face when establishing business in Erbil is ironically being affected by the same problems they are trying to fix. Services like water and electricity, although better than they used to be, are lacking. The Erbil municipality is only able to provide around 17 hours of electricity per day, while country-dwelling residents in Kurdistan may not have access to power at all. This will pose added costs and delays to any attempts at improving infrastructure.

Further fueling expenses is the "lack of local expertise [which] has partially slowed growth, forcing the Kurdish government to lure foreign players with a whole range of business-friendly regulations[28]." This would indicate that the KRG is reliant upon foreign investment to fuel and sustain its development initiatives. Conversely, the majority of Erbil's investors are Iraqi, and the work culture is something that any company needs to adapt to. In spite of these inherent flaws in Kurdistan's current setup, continued investment and growth is expected.

The Kurdish language, culture, and history aside, the most crucial and current difference between Kurdistan and the rest of Iraq is its relative safety. Retired Army colonel Harry Schute believes that Kurdistan is safer than New Jersey[29]. But Iraq has gained a reputation for violence and minimal security, a scare for tourists, investors and workers. In May 2007, two car bombs killed a total of 45 people and wounded 150. A company has to be certain that its employees are going to have physical security and peace of mind. In spite of the bombings, Lufthansa and Austrian Airlines conduct four flights a week to Erbil, and certain countries, such as the UK, have specifically mentioned that traveling to Kurdistan does not pose the same risks as traveling to the rest of Iraq[30]. Airlines in the UAE have been flying to Erbil for some time.

Regardless of a company's relations with the KRG, the KRG's relationship with the Iraqi central government is tense. A good example is when Kurdish authorities allowed Iraq's VP Tariq al-Hashimi to travel to Qatar in spite of a warrant for his arrest in Baghdad[31]. Moreover, the KRG halted oil exports through the Iraqi pipeline between April and August 2012, alleging that the KRG had not been adequately compensated for its oil by Baghdad[32]. The KRG further aggravated the situation when it unilaterally signed a contract with ExxonMobil, prompting the Iraqi government to threaten Exxon with the possibility of legal action – a threat it has, to date, not made good on[33]. Unfortunately for the KRG, it has no independent pipeline and the Turkish government, with whom it does the most business, has not yet agreed to maneuver around Baghdad's current policy on Kurdish exports[34]. Regardless of how much regional autonomy the KRG possesses, it must still respect Baghdad's authority. Tensions between regional and central government will not bode well for investment.

An added, but minor, complication to doing business in Erbil is that there is little access to ATMs that accept international cards. This limitation requires a number of dealings to be done in cash, which could pose problems for security. Cash payments also make money laundering difficult to trace. Governor Hadi admits "many things and sectors of the state have changed very rapidly, so there will be some corruption[35]." This type of illicit conduct could be subject to scrutiny from UK or US regulators (especially following the UK's Anti-Bribery Act 2010).

A final, but not fully known variable, is the impact of UN, EU and US sanctions of Iran. Iran is a heavy investor in Erbil meaning that companies affiliated with certain Iranian businesses or doing any type of business with Iran need to be cautious. The unilateral sanctions imposed by the US have been particularly strict; companies doing business in the US will be slapped with fines and possibly jail terms should they fail to comply.

How we can help

Al Tamimi & Company is well placed to assist clients with their legal needs in Iraq. With an office in Baghdad with a sizeable team of lawyers, Al Tamimi is experienced in providing the type of legal insight that gives a project in a rapidly changing economy such as Kurdistan the greatest chance of success. The firm has a strong understanding of its clients' industries and objectives and its depth of advisors and resources allows for a comprehensive and devoted approach to advisory work. Al Tamimi is experienced in assisting its clients in their ventures in Kurdistan and offers its services to local, regional and international companies alike.

Conclusion

As Erbil seeks to reinvent itself, companies across the globe are keen to reap the benefits from this unique process. Although there will be a significant number of difficulties for current and future investors, Erbil's economy is advancing at a lightening-fast pace because of its construction and development initiatives across all sectors. As business grows, so will the need for legal assistance in a variety of areas for domestic and international clients alike. Al Tamimi is ready to assist clients embrace the exciting new challenges and opportunities in Erbil.

Footnotes

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