

ECONOMICS OF CONFLICT:

IRAQ

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Overview

1. Lack of empirical work on costs and benefits of conflict
2. Framework for Assessment
3. Costs - Military
- Civilian
4. Benefits
5. Some evidence
6. Alternative solution?

Economics of Conflict

- Debates about war - and decisions to go to war - usually involve other disciplines/dimensions:
 - Political
 - Moral/Ethical
 - Legal (including UN)
 - Military
- But conflict has an Economic dimension=> Costs
 - Wars are costly - costs can be massive (e.g. WWII)
 - Cost estimates allow policy-makers and voters to make informed judgements about conflict
 - Further Economics contributions on conflict:
 - Modelling conflict and terrorism
 - Target selection in conflict - e.g. oil fields; aircraft plants (WWII).
 - But, costs relatively neglected aspect of conflict.

- Governments reluctant to publish their estimates of conflict costs:-
 - Sensitivity reasons
 - Not to deter voters => under-estimating costs gains political support
 - Uncertainty reflecting scale, duration, losses and outcome
 - Where national survival threatened => society willing to “pay any price” (e.g. UK in 1939/40)
 - Once a “cheap” war is started, further funding can’t be refused when troops in battle.
- For UK/USA conflict with Iraq, focus on
 - Published data, mainly MILITARY BUDGET COSTS
 - But military conflict costs =>only partial indicator of true economic costs of conflict.

Framework for Assessment : Iraq

An ambitious agenda

Country	Military Costs	Civilian Costs	Benefits
U.K.			
U.S.A.			
Other allies			
Iraq			

Problems of Estimating Costs

MILITARY

- Marginal costs (e.g. deployment; extra pay/allowances; fuel; ammunition
 - context: 2003/04 annual UK defence budget => £31.3 B
- Costs of replacing equipment
- Value of human life / human K losses

- Distinguish one-off costs of CONFLICT v continuing costs of PKO's
- Estimates differ from outturns:
 - conflict decisions based on estimates
 - nations over-estimate their chances of victory and under-estimate size of the undertaking
- Possible long-term costs:
 - PKOs
 - greater threat from terrorism?
 - positive / negative impacts on recruitment / retention for AVF
- Some offsetting cost savings:
 - end of UK/US military control of Iraq airspace

CIVILIAN COSTS

Short / Long Term Impacts on UK (& USA):

- Oil prices
- Share prices - confidence
- Recession effects? Reluctance of consumers / firms to spend
- Airlines / Tourism
- Public spending plans
 - HMT agreed to fund Iraq war from Reserves
- Increased defence spending / Benefits to defence industries
- Benefits to defence industries
- Benefits for private contractors
- End of Iraq sanctions => new market opportunities

Problem of COUNTER-FACTUAL?

IRAQ

Substantial costs imposed on Iraq:

- Military / Civilian
- Human / Physical capital losses
- Reconstruction - who pays?

Counter-factual:

Iraq economy with / without sanctions
 Iraq with / without Saddam Hussein

BENEFITS

Possible Benefits : as claimed / based on public statements

1. Democracy in Iraq: freedom for Iraq people / end of human rights abuses
2. End of WMD and security threats to Middle East
3. Greater security for Iraq
4. Increased trade opportunities with Iraq
5. Oil => increased Q of Iraq oil = lower oil prices
6. Spread of democracy in Middle East
7. Reduced terrorism
 - Benefits extend into FUTURE

ESTIMATING BENEFITS

- CBA => requires estimates of both COSTS & BENEFITS
- Problem: distinguish PLANS V OUTCOMES
 - Debate dominated by outcomes / hindsight
- What are likely benefits from war with Iraq and how highly were they valued?
- Could use costs to indicate minimum valuation of benefits

EVIDENCE

UK MILITARY COSTS => Marginal resource costs

Initial Estimates:

- HMT November 2002 => £1B
- HMT March 2003 => £3B
- KH November 2002 => £3.5B

Outcomes

- Actual cost of conflict => About £1.5B
- PKOs 2003/04 => £1.3B
- Estimated (KH) costs of conflict and PKOs to end March 2005 => £4B
- Estimated (KH) costs end-March 2006 => some £5B

UK MILITARY COSTS (Continued)

- Value of Life: death / injuries
 - Net impacts: adjusting for deaths / injuries in peace time
 - Data problems (injuries)
 - Estimates are broad orders of magnitude
- Value of life: DoT life => £1.3 mill
Serious injury => £147.5K
- Estimated value of UK military deaths / serious injuries =>
£58 million (2003-end March 2005)
- Total UK Military Costs => £4.2 Bill (end March 2005)
(£4 Bill, Present Value)

OPPORTUNITY COSTS

UK MILITARY COSTS OF CONFLICT => £1.5B

£1.5B as one-off sum would buy:-

- Increased child element in child tax-credit by £200+ for one year
- Abolish capital gains tax for one year
- Build 25 new hospitals (capital costs only)

UK CONFLICT COSTS => 30% of TOTAL MILITARY COSTS TO
2006

COSTS OF OTHER UK CONFLICTS

UK MILITARY COSTS (2003 prices)

	£s
Kosovo conflict	376 millions
- Total operations	951 millions
Gulf War	3522 millions
- net UK cost	662 millions
WW II	695 Billion
WW I	211 Billion

USA

US MILITARY COSTS OF IRAQ

- Initial estimate => \$100-\$200 Billion
- March 2003 to end FY 2005/06 (US/OMB)

\$250B (including Death Benefits: \$241B in PV)

- Value of Life (Possible double counting):
 - Use UK DoT estimates + 20% updating to reflect UK-USA productivity gap
 - Estimated value of life (Deaths only) to end January 2005 => \$3.0 Billion
- TOTAL US MILITARY COSTS => \$253 B

OTHER US CONFLICTS

MILITARY COSTS

First Gulf War	79.9
Vietnam	494.3
Korea	335.9
WW II	2896.3

\$2002 prices Billions (excluding pensions)

COSTS TO CIVILIAN ECONOMY

- Before conflict => Nordhaus “Most durable economic impacts of a war in Iraq are likely to be effects on oil markets” (2002)
- Pre-war => IMF model of effects of a permanent US \$5 per barrel rise in oil prices on real GDP:

	1 st year	2 nd year	3 rd year
All Industrialised Nations	-0.2%	-0.3%	-0.3%
USA	-0.3%	-0.4%	-0.4%
Euro area	-0.2%	-0.4%	-0.4%

IRAQ COSTS

HUMAN COSTS - by September 2004

- Military Deaths => 4,895 - 6,370 Iraqi soldiers and insurgents
- Civilian Deaths => 12,800 - 14,000 Iraqi civilians
- Bellany: civilian deaths => 10,000-33,000

RECONSTRUCTION COSTS

- Some estimates => \$50-100 Billion
 - But estimate recognises poor state of Iraq's infrastructure since Iraq-Iran war starting in 1980.
 - Sources of finance => Iraqi oil; international aid (including \$21.4 B from USA)
- CBO estimates (January 2004) => \$18-55 Billion

SUMMARY

	Costs	Costs
Country	Military	Civilian
UK	£4.1 B) Oil markets) Oil price rise:
USA	\$253B	\$5 pb -0.2%-0.4% GDP
Other Allies	A\$ 154 million (£65 million)	
Iraq	<u>Deaths</u> 5,600	<u>Deaths</u> 10,000-33,000 <u>Reconstruction</u> \$18-55 Billion

ALTERNATIVE ECONOMIC SOLUTION?

- Bribery / compensation principle
- Bribe S.H. to go => an offer he couldn't refuse
- Assume US willing to spend \$100B on war
- Alternative
 - Offer SH \$20B to go
 - Give Iraqi people \$50B
 - US saves \$30B
- Pareto improvement: everyone better off; no-one worse-off; and war avoided.