



# ***Socio-economic Developments under the Ahmadinejad Administration***



**Prepared for  
Woodrow Wilson Center  
June 2006**

*The following remarks were made by Bijan Khajepour in connection with his participation in the conference entitled "Iran Under President Ahmadinejad," which was held at the Woodrow Wilson International Center for Scholars on June 26, 2006. The opinions expressed here are those of the speaker and in no way represent the views or opinions of the Woodrow Wilson International Center for Scholars.*

# Introduction

- President Ahmadinejad ran on a campaign platform evolving around the concept of social justice, fighting corruption and improving economic conditions;
- In the past 10 months, his government has initiated a number of processes that are of significance for Iran's socio-economic development;
- Though socio-economic developments and trends are fluid and cannot be entirely attributed to the actions of a young administration, it is valid to analyze the direct and indirect impacts of the new policies on key areas;
- This presentation will first identify the key problems and then focus on the impact of government policies on resolving some of the country's key socio-economic challenges;

# Main Socio-economic Issues

- Ahmadinejad inherited an economy that has faced a long list of challenges with main issues evolving around the following realities:
  - High unemployment;
  - Inflation;
  - Lack of infrastructure, especially in less developed provinces;
  - Lack of genuine private sector investment activity;
  - High dependency on oil income;
  - High liquidity rates;
  - Budget deficits;
  - Inadequate subsidies;
  - Administrative and financial corruption;
  - Smuggling;
  - Weak bureaucracy and poor governance;
  - Constant politicization of economic issues;

# Indicators (CBI figures as of March 2006)

Indicator	March 2006 figures (CBI)	Projections for current year
Population	68.6 million	69.5 million
Urbanization	67%	67%
Active population	22.3 million	23.1 million
<b>Unemployment</b>	<b>12.1%</b>	<b>13%</b>
Literacy	86.5%	87.5%
GDP growth with oil (without oil)	4.2% (5.3%)	5.0% (6.0%)
Capital formation as % of GDP	28.33%	25%
<b>Inflation</b>	<b>12.1%</b>	<b>16%</b>
Liquidity growth	34.3%	33%
Growth of non-gov. savings	35.3%	35% <sup>4</sup>



# Comparative Indicators

(World Bank figures)

Indicator	Iran	MENA Average	Lower middle income countries	OECD Average
GNI per capita, (current US\$)	2,300	3,067	1,980	33,470
Access to electricity (% of population)	98	90	78	..
Electric power consumption (kwh per capita)	1,677	1,634	1,360	8,769
Improved water source (% of population with access)	93	84	85	99
Improved sanitation facilities (% of population with access)	84	77	71	..
Total telephone subscribers per 100 inhabitants	27	28	35	..

# Corruption Perception Index

Country	Rank	Score
Iceland	1	9.7
United Kingdom	11	8.6
Oman	28	
UAE	30	
Qatar	32	
Bahrain	36	
Jordan	37	
Tunisia	43	
Kuwait	45	
Turkey	70	
Egypt	70	
Saudi Arabia	70	
Syria	70	
Lebanon	83	
Iran	88	2.9
Algeria	97	
Yemen	103	
Iraq	137	
Chad	158	1.7

- A perception based index published by **Transparency International**
  - Based on the perception of business people and country analyst
  - Score below 3 represents severe corruption
  - Ratification of the United Nations Convention against Corruption (December 2005) established a global legal framework for sustainable progress against corruption

# Doing business in Iran

Country	
New Zealand	1
United Kingdom	9
Saudi Arabia	38
Kuwait	47
Oman	51
Tunisia	58
UAE	69
Jordan	79
Yemen	90
Turkey	93
Lebanon	95
Morocco	102
<b>Iran</b>	<b>108</b>
Iraq	114
Syria	121
Algeria	128
Egypt	141
Congo	155

<b>Iran composite ranking</b>	<b>108</b>
Starting a business	54
Dealing with Licences	145
Hiring and firing	112
Registering property	98
Getting credit	64

## Is the new government able to address these issues?

- The new government's initiatives in the field of social justice have been sporadic and have partly been contained by other power centers;
- It seems that the new government has not managed to impose its authority on the field of economic policy, especially as the key positions (Ministry of Petroleum, Ministry of Finance, Governor of CBI) have remained in the hand of the old technocrats;
- In response, President Ahmadinejad has tried to establish new alliances through shifting attention from Tehran to the provinces;
- While this has had popularity gains for the President, the process can turn against the government, if it fails to deliver on its promises in the provinces;
- When it comes to the relationship with other power centers, Ahmadinejad is torn between his desire to achieve populist policies and the fact that some policies step on the toes of existing power centers (example of allowing women to go to sports events);
- The President has also tried to reduce the distance between the society and the government, but it is not clear whether the emerging expectations can be met by the government;

# The government's economic policies

- Despite the existence of conflicting economic agendas in Iran, we need to identify “the common vision” which is provided in the “20-Year Perspective” Document.
- This document was:
  - Developed by the Expediency Council after months of deliberation
  - Signed off by the Supreme Leader
  - Becoming increasingly prominent (EC decree)
- Essentially, Iran strives to be the regional technological and economic powerhouse over the next two decades;
- It envisages a Knowledge-based society in Iran. Therefore, all issues relating to the generation or transfer of knowledge to Iran as well as to job creation will be welcomed by the various mindsets.
- Focus of the government will be:
  - Distribution of wealth;
  - Promotion of Investments;
  - Infrastructure investments;
  - Improving overall TPF productivity;
  - Transfer of technology and knowledge;

# Investment Activity

- The initial reaction to the election of Ahmadinejad was a massive drop in private sector investment activity, the TSE crashed and a large number of private sector projects were put on hold;
- Capital flight and relocation of entrepreneurs emerged as the key trends in economic activity;
- Also, foreign companies became more cautious with regard to investments in Iran;
- Nonetheless, there are signs that a new degree of confidence has returned among the domestic investors;
- There is also greater attention to local companies;
- More significantly, the phenomenon of Arab investments in Iran has continued strongly and Ahmadinejad has further consolidated the positive attitude of Arab investors towards the Iranian market;
- The government has also introduced some restrictions for the operation of foreign companies, especially with regard to human resources;
- It is valid to argue that the initial drop in private sector investment has been reversed, though one will find more regional investors as opposed to international investors;
- Recent protectionist laws and regulations will also have a negative impact on the operation of international companies;



# The new government and corruption

- The new government's attention to fighting corruption has had mixed success;
- On the one side, there has been a genuine push to fight administrative corruption and the effects are visible;
- On the other side, the massive sweeping of state technocrats and the emergence of a new and inexperienced generation of state officials has led to new irregularities and problems;
- Corruption in Iran needs to be micro-managed through new laws and regulations and the Ahmadinejad government has not managed to introduce new instruments for this purpose;
- The key challenge remains the coordination between power centers;
- Furthermore, the changing of the guard also produced new interest groups who are pushing to secure business interests from the government;



# Attention to Provinces

- The most significant policy shift in the new government has been the government's attention to provinces in an attempt to allocate more resources to infrastructure development in provinces;
- Though the government is heavily dependent on the Majles cooperation in allocating resources to provincial development, the continuous presence of state officials in provinces has helped the government bring its investments in line with regional needs and expectations;
- The President has also learned not to make any promises outside the existing budgets, though the public announcement of some investments makes him more popular, especially on provincial levels;
- However, there is a risk of growing provincial expectations that cannot be fulfilled in the future – the resulting frustrations will also be difficult to manage;
- Ahmadinejad has not yet traveled to the ethnically more challenging provinces and we will have to await the results of those trips, especially in the light of recent ethnic tensions;
- The government has continued the work of the previous administration on a new law on introducing new “administrative structures” – this law will be significant in order to break away from ethnic lines around provincial divisions;

# The 1385 Budget as an indicator

- Ahmadinejad's first budget bill faced major difficulties in the Majles, but it indicated the government's attitude to many issues, i.e.:
  - The new administration
    - would like to reinstate the financially strong government that becomes the central provider for the country (distributive policies);
    - would risk high inflation in the name of addressing infrastructure deficiencies;
    - would reverse other processes (such as gradual trade regime reforms) based on protectionist policies;
- Though the Majles reversed some of the government initiatives, the attitudes of the new administration are there and they will drive a policy that carries the risk of higher unemployment and higher inflation;
- The administration is trying to improve government finances through cost-cutting on one side and new revenues (customs duties and license fees on the other side);
- Privatization still remains a critical area;
- The government has announced the introduction of new budget guidelines;

## The dynamics of salary increases

- The complexities of the Iranian economy come to light when one looks at the government decision to increase the minimum wage by 50% in March 2006 (new Iranian year) – minimum salary stood at Rials 1.8 million/month;
- The increase was welcomed by the lower income classes, but it led to massive redundancies in factories and projects, hence backfiring with regard to employment patterns (based on some reports 200,000 jobs have been cut as a result of the new minimum wage);
- Consequently, the government has retracted and has now announced a new minimum salary (Rials 1.5 million = 20% lower than the original one);

# Future of Subsidies

- Like in previous administrations, there is a debate about the need for the discontinuation of blanket subsidies and the introduction of targeted subsidies, however, there are no actual solutions on the table;
- There is talk about the introduction of a new system for gasoline subsidies, i.e. rationing of gasoline for cars so that excess gasoline would be bought at international prices;
- The implementation of the proposed system of smart cards will require major investments in infrastructure which in itself may impede the process;
- Experts agree that Ahmadinejad is the courageous politician that is needed to put an end to Iran's inadequate subsidy systems, but it remains to be seen whether he will initiate a change of policy, especially as it will be unpopular;



# Populism and Socio-economic developments

- Ahmadinejad's populist agenda has led to greater attention to social health issues, such as fight against addiction anti-smoking campaigns etc. which are positive in nature, but one will have to wait for their implementation;
- Passing of the law on protection of consumer rights (including penalties for producers abusing consumer rights)
- The impact of cultural policies on the country's economy remains mixed: On the one side, some policies have put severe pressure on areas such as publishing, but other policies (such as more relaxed laws on music production, video clips etc.) have had a positive impact on employment and small scale economic activity;
- Government's attention to issues such as "marriage loans" have temporary positive effects, but won't lead to sustainable solutions in issues such as unemployment;

# Administrative Issues and Governance

- Iran has a poor regulatory and administrative environment, and poor governance and corruption are key impediments to economic development;
- Progress is difficult but can be made quickly, once the political will is there;
- The multiplicity of power centres and overlapping responsibilities lead to inefficiencies;
- The Judiciary remains the key driver behind some of the reforms, but implementation will depend on so many different institutions;
- The attention to fighting corruption is positive, but not enough in the absence of administrative reforms;
- The push for decentralization in the absence of modern laws on administrative divisions will only complicate the situation;

# Interim Balance sheet of the Ahmadinejad Government:

## Positive Phenomena:

- A changing of the guard and the emergence of younger managers/technocrats;
- Increased attention to the actual needs of provinces in investment decisions;
- Support for the anti-corruption campaign which is more feasible through the second generation of managers;
- Debate about the replacement of blanket subsidies through targeted subsidies;
- Decentralization of some government decisions could release new opportunities and energies on provincial level.

## Negative Phenomena:

- Reduced investment activity by the non-governmental sector as reaction to political uncertainties;
- Tensions emerging as a result of new interest groups pushing for interests;
- The new government's distributive policies may lead to new tensions among the social classes in Iran which would have medium to longer term effects;
- The inflationary effects of higher government finances;
- Protectionist trade policies will undermine Iran's desire to join WTO;
- The push for economic projects being controlled by Iranian companies will deprive Iran of some (western) technologies;



# Conclusions

- President Ahmadinejad has mainly focused on populist issues such as social justice and fighting corruption with very limited success;
- The most significant policy instrument remains the growing attention to provinces, but this may backfire in the medium term;
- Some of the new government's policies are negatively influencing key challenges such as inflation and unemployment;
- The government has not yet addressed the most critical issue, i.e. the country's business climate and the lack of productive investments in the economy;
- Protectionist policies will undermine the overall positive trend of the past few years in new economic activity;
- Iran's overall economic and socio-economic development will depend on the country's success in re-integrating in the world economy through breaking the deadlock over Iran's nuclear program;