CHAPTER 11

BALANCE OF PAYMENTS

Global Economy and the External Transactions of Iran

In 1388, the slowdown of the world economy continued; therefore, advanced economies after a prolonged economic growth entered the economic recession phase, which reduced world trade. Iran's balance of external payments was also affected by international developments, followed by a sharp fall in current account surplus.

In 2009, world economy had the worst environment since the recession of the 1930s. World trade, in terms of volume and value, declined in this year, followed by a sharp increase in unemployment and rise in governments' protectionist measures.

Based on IMF reports, the world economic growth decreased for the second consecutive year in 2009 to reach -0.6 percent.

Economic Growth of the World and Selected Economies

(percent)

	2008▲	2009▲	2010
World	2.8	-0.6	5.3
Advanced economies	0.0	-3.6	3.2
Emerging markets and developing economies	6.0	2.8	7.5
Developing countries in Asia	7.8	7.1	9.7
Middle East and North Africa (MENA)	4.7	2.7	4.9

Source: World Economic Outlook, IMF, April 2012

Pursuant to the sharp decline of global demand, the world trade of goods and services decreased substantially, and reduction in world trade was later exacerbated by lack of availability of trade finance facilities and the protectionist measures adopted by different countries to safeguard their economies against the crisis. In the review year, world trade, in terms of quantity, declined and reached -10.5 percent. Trade statistics indicate that the world trade of services was worse hit in 2009 than that of goods.

World Trade Growth

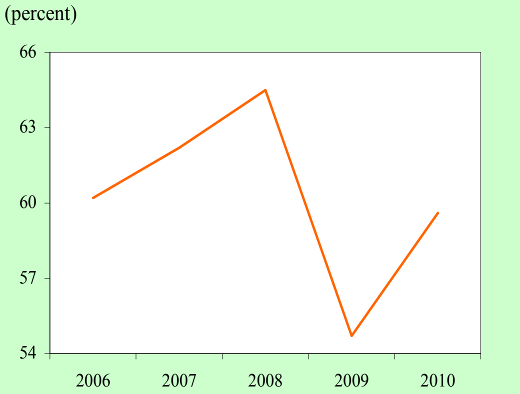
(percent)

	2008▲	2009▲	2010
Goods and services			
Quantity	2.9	-10.5	12.9
Price (in US$)	11.3	-10.6	5.5
Goods			
Quantity	2.4	-11.7	14.3
Price (in US$)	12.1	-11.8	6.6

Source: World Economic Outlook, IMF, April 2012

Share of world trade of goods and services in world GDP which had an uptrend till 2008, sharply declined in 2009. This was mainly due to rise in protectionist measures by different countries and fall in world economic growth. In 2009, the world sum of exports and imports to GDP ratio declined sharply and reached 54.7 percent.

Figure 11.1. Ratio of world trade to world GDP (sum of exports & imports of goods & services)



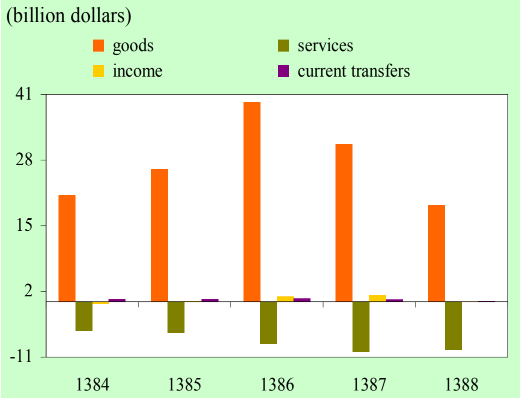
Balance of Payments Developments

In the review year, unfavorable global economic conditions adversely affected Iran's balance of external payments. In this year, current account surplus and trade balance were reduced by respectively 58.5 and 38.7 percent compared with preceding year. Adverse developments in country's foreign trade reduced CBI's foreign assets by more than $7 billion. Moreover, foreign financing through debt instruments was further restricted.

Current Account

Current account surplus declined for the second consecutive year in 1388 to reach $9,477 million. This decline was largely due to reduction in the value of oil exports owing to sharp fall in the price of oil products, as well as drop in investment income which in turn resulted from the fall in international interest rates.

Figure 11.2. Current account balance components



In the review year, current account surplus to GDP ratio reached 2.6 percent, down by 3.9 percentage points compared with

Current Account Balance (million dollars)

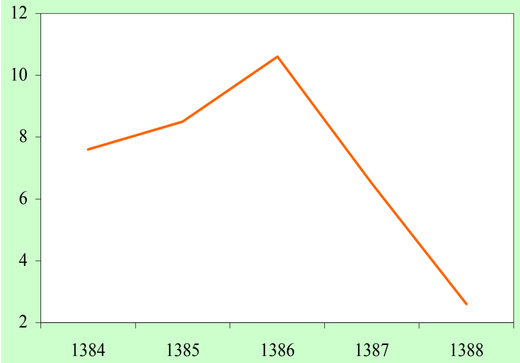
				Percentage change	
	1386	1387	1388	1387	1388
Current account balance	**32,594**	**22,837**	**9,477**	**-29.9**	**-58.5**
Goods	39,427	31,114	19,079	-21.1	-38.7
Services	-8,429	-9,974	-9,582	18.3	-3.9
Income	954	1,335	-122	40.0	θ
Current transfers	642	362	101	-43.6	-72.1
Current account balance (non-oil) [1]	**-45,663**	**-55,967**	**-53,883**	**22.6**	**-3.7**

[1] Excluding value of exports of crude oil, oil products, natural gas, condensates and natural gas liquids (tariff codes: 2709, 2710, and 2711) by NIOC, NIGC, NIORDC, petrochemical companies and others (customs and non-customs)

previous year. In 2009, this ratio was 3.8 percent in "Asian Emerging Economies" and 2.5 percent in "Middle East and North Africa (the MENA region)".

Figure 11.3. Ratio of current account balance to GDP

(percent)



In 1388, non-oil current account deficit which had an uptrend till 1387, decreased for the first time. In this year, non-oil current account deficit declined by 3.7 percent to about $53.9 billion. This was due to fall in oil exports value in tandem with rise in non-oil exports value. In the review year, non-oil foreign exchange earnings constituted 32.2 percent foreign exchange requirements of this account, up by almost 2.9 percentage points compared with the previous year[1].

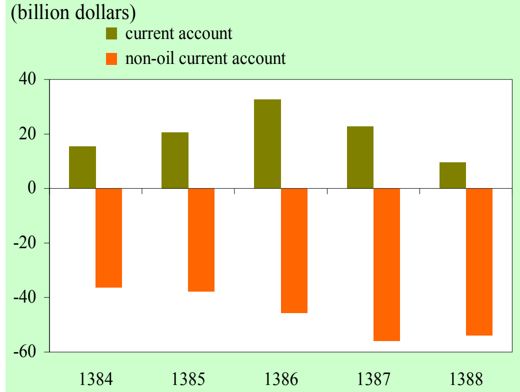
Goods Account (trade balance)

In the review year, share of goods in country's international trade was 86 percent, down by almost 1.1 percentage points compared with previous year. Moreover, share of country in world trade of goods rose merely 0.1 percentage point to 0.64 percent.

[1] This ratio is calculated by dividing the sum of "non-oil exports, services exports, and credit entry of income and current transfers accounts" to the sum of "goods imports, services imports, and debit entry of income and current transfers accounts".

Figure 11.4. Current account balance and non-oil current account balance

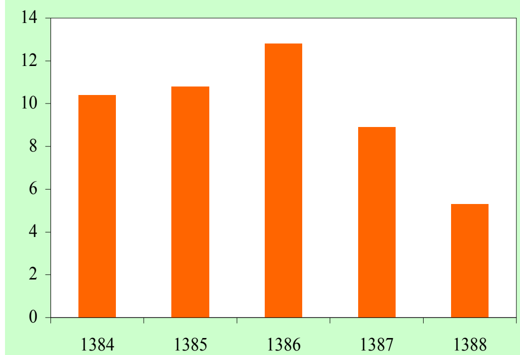
(billion dollars)



In this year, goods account (trade balance) surplus declined by 38.7 percent to $19 billion, compared with preceding year. This was due to sharp fall in oil exports, in terms of value. Thus, goods account (trade balance) surplus to GDP ratio at current prices reached 5.3 percent, down by 3.6 percentage points as compared with the year before. Furthermore, goods export-import ratio decreased by 16.8 percentage points to 127.6 percent compared with previous year. Non-oil trade balance deficit declined by 7.2 percent to nearly $44.3 billion.

Figure 11.5. Ratio of external trade balance to GDP

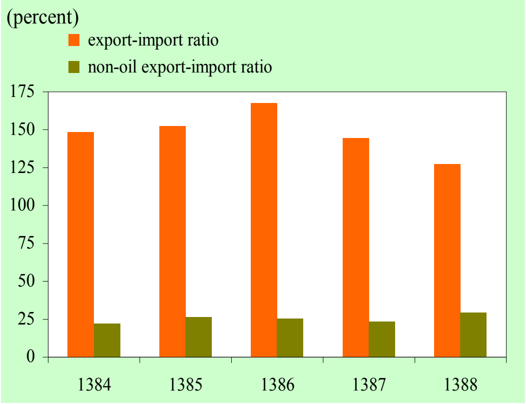
(percent)



Goods Account (million dollars)

	1386	1387	1388	Percentage change 1387	Percentage change 1388
Goods account (trade balance)	**39,427**	**31,114**	**19,079**	**-21.1**	**-38.7**
Exports	97,667	101,289	88,326	3.7	-12.8
Imports	58,240	70,175	69,247	20.5	-1.3
Non-oil goods account (trade balance)	**-38,830**	**-47,690**	**-44,280**	**22.8**	**-7.2**
Exports	13,162	14,670	18,369	11.5	25.2
Imports	51,992	62,360	62,649	19.9	0.5

Figure 11.6. Export-import ratio



Exports

In the review year, total exports decreased by 12.8 percent to $88.3 billion compared with preceding year. This was largely due to the fact that oil exports[1] were reduced by 19.2 percent to $70 billion in this year. Moreover, non-oil exports increased by 25.2 percent to $18.4 billion.

In this year, exports to GDP ratio reached 24.5 percent, down by 4.4 percentage points. This was owing to exports reduction, oil exports in particular.

Selected Indicators of Exports (percent)

	1386	1387	1388
Ratio of exports to GDP	31.8	28.9	24.5
Ratio of non-oil exports to total exports	13.5	14.5	20.8
Exports growth	28.2	3.7	-12.8
Oil exports growth	30.7	2.5	-19.2
Non-oil exports growth	14.2	11.5	25.2

Exports (million dollars)

	1386	1387	1388	Percentage change 1387	Percentage change 1388
Exports of goods	**97,667**	**101,289**	**88,326**	**3.7**	**-12.8**
Oil exports [1]	**84,505**	**86,619**	**69,957**	**2.5**	**-19.2**
Customs [2]	1,892	3,140	3,056	66.0	-2.7
Non-oil exports	**13,162**	**14,670**	**18,369**	**11.5**	**25.2**

[1] Including value of exports of crude oil, oil products, natural gas, condensates, and natural gas liquids (tariff codes: 2709, 2710, and 2711) by NIOC, NIGC, NIORDC, petrochemical companies and others (customs and non-customs)

[2] Including value of exports of condensates and natural gas liquids, and oil products (tariff codes: 2710 and 2711) by petrochemical companies and others mentioned in Customs data

[1] Including value of exports of crude oil, oil products, natural gas, condensates, and natural gas liquids (tariff codes: 2709, 2710, and 2711) by NIOC, NIGC, NIORDC, petrochemical companies and others (customs and non-customs)

Imports

In the review year, imports (fob) declined by 1.3 percent to almost $69.2 billion, as compared with the corresponding figure for preceding year. Moreover, the ratio of imports to GDP was reduced to 19.2 percent. Natural gas and oil products imports went down by 15.6 percent to nearly $6.6 billion, compared with the corresponding figure for previous year. Despite this reduction, the ratio of oil products imports to exports increased slightly to almost 9.4 percent.

Selected Indicators of Imports

(percent)

	1386	1387	1388
Ratio of imports to GDP	18.9	20.0	19.2
Share of imports through Customs in total imports	83.2	79.9	79.8
Share of imports of natural gas and oil products in total imports	10.7	11.1	9.5
Annual growth of imports	16.5	20.5	-1.3
Oil import-export ratio	7.4	9.0	9.4

Services Account

Based on the relevant data, $8.1 billion services were exported by Iranian suppliers to non-residents, up by 3.9 percent compared with preceding year. On the other hand, residents' spending on receipt of services rendered by non-resident individuals and companies remained relatively unchanged at $17.7 billion. Therefore, services account deficit reached $9,582 million, down by 3.9 percent. During this period, share of services in country's international trade rose one percentage point to 14 percent.

Selected Indicators of Services

(percent)

	1386	1387	1388
Ratio of services account deficit to GDP	-2.7	-2.8	-2.7
Share of services in Iran's international trade	12.5	13.0	14.0
Annual growth of services account deficit	35.7	18.3	-3.9
Annual growth of services exports	22.2	12.2	3.9
Annual growth of services imports	29.3	15.6	-0.5

In the review year, "transportation" by 43.4 percent, "travel" by 25.4 percent, and "construction (technical and engineering) services" by 20.6 percent accounted for the lion's share in service sector export by more than 89.4 percent.

Composition of Services Exports

(percent)

	1386	1387	1388
Transportation	48.0	49.5	43.4
Travel	24.2	22.3	25.4
Construction (technical and engineering) services	19.1	19.2	20.6
Other services	8.7	9.0	10.5
Total	**100.0**	**100.0**	**100.0**

Composition of Services Imports

(percent)

	1386	1387	1388
Transportation	24.1	23.7	20.9
Travel	44.3	42.6	44.2
Construction (technical and engineering) services	16.1	17.2	17.5
Other services	15.5	16.4	17.4
Total	**100.0**	**100.0**	**100.0**

Imports

(million dollars)

				Percentage change	
	1386	1387	1388	1387	1388
Total	**58,240**	**70,175**	**69,247**	**20.5**	**-1.3**
Gas and oil products [1]	6,248	7,815	6,598	25.1	-15.6
Other goods	51,992	62,360	62,649	19.9	0.5

[1] Including value of imports of natural gas, condensates and natural gas liquids, and oil products (tariff codes: 2710 and 2711) by NIOC, NIGC, NIORDC, petrochemical companies and others (customs and non-customs)

Furthermore, "travel", "transportation", and "construction (technical and engineering) services" constituted nearly 82.6 percent of services imports by respectively 44.2, 20.9, and 17.5 percent.

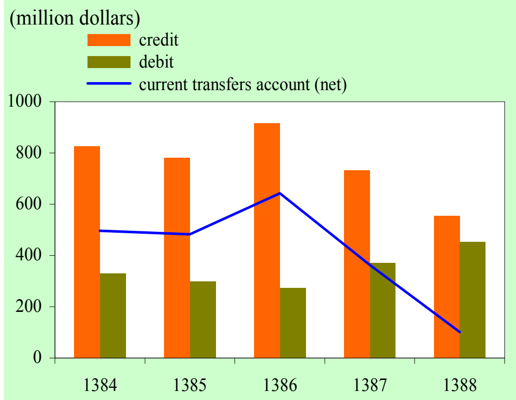
Income Account

The growing trend of income account surplus which started as of 1385 was reversed in the review year, posting $122 million deficit. This was mainly due to about 44 percent decrease in investment income, and increase in compensation of employees, including border, seasonal workers.

Current Transfers Account

In the review year, the surplus of current transfers account declined by almost 72.1 percent to $101 million. This was largely owing to 22.6 percent rise in the debit (payments) side, and 24.2 percent fall in the credit (receipts) side.

Figure 11.7. Current transfers account



Capital and Financial Account

In 1388, sharp reduction of oil exports value decreased the current account surplus; thereby reducing financial account transactions and deficit. Capital and financial account deficit decreased by roughly 66 percent to $6,460 million.

Income Account

(million dollars)

				Percentage change	
	1386	1387	1388	1387	1388
Income account	**954**	**1,335**	**-122**	**40.0**	**θ**
Credit	**3,164**	**3,270**	**1,791**	**3.3**	**-45.2**
Compensation of employees, including border, seasonal workers	561	558	270	-0.6	-51.6
Investment income	2,603	2,712	1,521	4.2	-43.9
Debit	**2,211**	**1,935**	**1,912**	**-12.5**	**-1.2**
Compensation of employees, including border, seasonal workers	276	324	496	17.1	53.2
Investment expenditure	1,934	1,611	1,417	-16.7	-12.1

Capital and Financial Account

(million dollars)

				Percentage change	
	1386	1387	1388	1387	1388
Capital and financial account	**-28,851**	**-19,135**	**-6,460**	**-33.7**	**-66.2**
Capital account	-249	-383	-744	53.4	94.4
Financial account	-28,601	-18,753	-5,716	-34.4	-69.5

Capital Account

In the review year, country's capital account ran a deficit as in previous years, which was mostly due to capital transfers. Based on estimates, capital account transactions rose nearly 94.4 percent, compared with the corresponding figure for previous year.

Financial Account

According to international standards, rise in country's foreign assets and fall in external debt are both registered at the debit side of the financial account of balance of payments. Therefore, reduction of current account surplus leads to decrease in financial account deficit. Financial account consists of foreign direct investment, portfolio investment, other investments, and reserve assets.

In the review year, financial account deficit was reduced by nearly 70 percent. This was mostly due to drop in reserve assets and sharp fall in external debt repayment.

Foreign Direct Investment (FDI)

In 1388, net FDI inflows reached $944 million as mentioned in the following table.

FDI Inflows

In the review year, foreign investment inflows in the form of foreign direct investment reached $2.6 billion, up by 76 percent compared with preceding year. Of this amount, 72 percent was related to buy-back contracts of oil and gas sector, and 28 percent to other foreign investment inflows in the form of foreign direct investment.

Financial Account

(million dollars)

				Percentage change	
	1386	1387	1388	1387	1388
Financial account	**-28,601**	**-18,753**	**-5,716**	**-34.4**	**-69.5**
Foreign direct investment (net)	-299	-193	944	-35.6	θ
Portfolio investment (net)	-1,241	-981	-199	-21.0	-79.7
Other investments (net)	-11,807	-9,351	-13,729	-20.8	46.8
Reserve assets	-15,254	-8,229	7,268	-46.1	θ

Foreign Investment Inflows in the form of Foreign Direct Investment [1]

(million dollars)

				Percentage change	
	1386	1387	1388	1387	1388
Foreign direct investment	**1,552**	**1,491**	**2,623**	**-3.9**	**75.9**
Under Foreign Investment Promotion and Protection Act	785	448	465	-42.9	3.7
Buy-back oil and gas contracts	747	987	1,878	32.1	90.2
Others	21	56	281	166.7	401.7

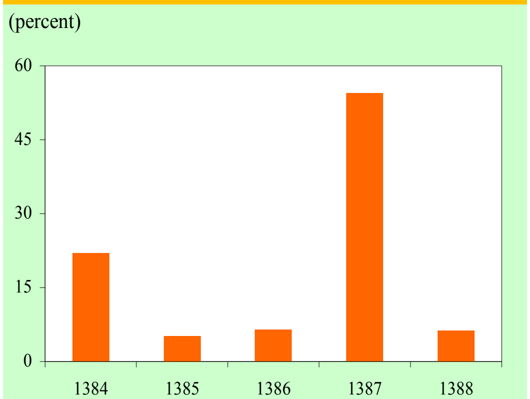
[1] The Organization for Investment, Economic and Technical Assistance of Iran (OIETAI)

Foreign Investments under Foreign Investment Promotion and Protection Act (million dollars)

	1386	1387	1388	Percentage change 1387	Percentage change 1388
Approved investments	12,091	822	7,253	-93.2	▣
Realized investments till end-1388 [1]	482	67	31	-86.1	-53.4
Capital inflows	785	448	465	-42.9	3.7

[1] Based on the date of approval

Figure 11.8. Ratio of capital inflows to approved investments



Portfolio Investment

The portfolio investment account records all purchases and sales of stocks, debt securities, derivatives, and other money market instruments by residents and non-residents. This account posted $199 million deficit in 1388, due to rise in foreign assets in the form of foreign exchange securities and purchase of foreign bonds by banks.

Other Investments

Loans, credit facilities, and foreign exchange deposits are major components of other investments account. This account ran $13,729 million deficit, mainly due to rise in credit facilities and foreign exchange cash and deposits, as well as the repayment of external debt.

External Debt

Total foreign exchange obligations (actual and contingent obligations) declined by 9.4 percent to $44,426 million at end-1388, compared with last year. In this year, share of contingent obligations in total obligations decreased by nearly 4.7 percentage points from 56.2 percent at end-1387 to 51.5 percent in 1388.

In 1388 year-end, actual obligations (external debt) amounted to $21.5 billion, remaining relatively unchanged compared with end-1387. Composition of external debt changed in favor of short-term debt, however. Share of long-term debt in total external debt declined by 10.1 percentage points to 59.2 percent.

In 1388, all indicators of external debt sustainability enjoyed a favorable position. Despite a sharp reduction in the value of exports of goods and services, due to fall in oil exports value, external debt sustainability indicators experienced no remarkable change. Increase in foreign financing constraints and the ensuing stability of external debt position kept these indicators relatively unchanged.

Foreign Exchange Obligations

(million dollars)

	1386▲	1387▲	1388	Percentage change 1387	Percentage change 1388
Actual obligations (external debt)	**28,647**	**21,502**	**21,526**	**-24.9**	**0.1**
Long-term	18,756	14,903	12,739	-20.5	-14.5
Short-term	9,891	6,599	8,787	-33.3	33.2
Contingent obligations	**21,825**	**27,537**	**22,900**	**26.2**	**-16.8**
Total	**50,472**	**49,039**	**44,426**	**-2.8**	**-9.4**

External Debt Profile (at end-1388)

(million dollars)

Maturity	1389	1390	1391	1392	1393 onwards	**Total**
Amount	11,621	2,274	1,951	1,553	4,127	**21,526**
Percent	54.0	10.6	9.1	7.2	19.2	**100.0**

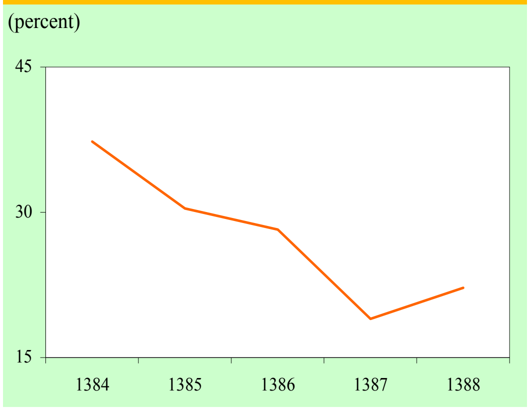
Indicators of External Debt Sustainability

(million dollars)

	1386	1387	1388
Ratio of external debt to GDP	9.3	6.1	6.0
Debt service ratio [1]	22.1	19.4	17.4
Share of short-term debt in total external debt (based on original maturity)	34.5	30.7	40.8
Ratio of external debt to exports of goods and services	27.4	19.7	22.3

[1] Including repayment of buy-back contracts of oil and gas sector

Figure 11.9. Ratio of new letters of credit issued to imports through Customs



4th Five-Year Development Plan[1]

Revision of Trade Policy

Trade policy during the 4th Plan period was based on export promotion measures, and support and expansion of trade and economic ties with the rest of the world. Export support policies included: support of export-oriented companies; direct and indirect support to export companies by designing export incentive schemes[2]; emphasis on the exports of technical and engineering services; support of export of goods with higher value-added content and technologies; support of infrastructures related to export sector; and restructuring of export information system with due emphasis on production and export opportunities[3].

Major import policies aimed towards higher transparency of import procedures and reduction

[1] As 4th FYDP projections are based on the Balance of Payments Manual, 4th edition (BPM4), figures mentioned in this chapter are not comparable with the preceding chapters.

[2] In pursuance of paragraph (b), Article 33 of the 4th FYDP Law

[3] Approval No. K37862I/81293 dated Mordad 23, 1386, by Ministers member to the High Council of Non-Oil Exports Promotion

of tariffs set for various imported products to regulate the domestic market. Main foreign exchange policies were focused on reducing the impact of international restrictions imposed on dollar transactions.

Trade of Goods and Services

Export support policies as well as price rise of crude oil and major exports led to 247 percent realization of 4th FYDP projection on goods exports. Therefore, goods worth $85,599 million were exported on average per annum, comprising oil and gas exports[1] by 81 percent and non-oil[2] exports by 19 percent. During the 4th Plan, $16,401 million non-oil goods were exported, and $58,206 million were imported on an average annual basis, indicating more than 155 and 157 percent realization of Plan targets, respectively. Moreover, 4th Plan targets on export and import of services were fully realized.

Review of the annual average growth rate of export and import of goods and services during the 3rd and 4th Plans reveals a more favorable performance of non-oil exports during the latter period than the former. Implementation and operation of chemical and petrochemical projects over the 3rd and 4th Plan periods have led to this favorable performance.

Figure 11.10. Percentage of realization of the 4th FYDP projections on trade sector

Comparison of Average Annual Growth of Exports and Imports during the 3rd and the 4th FYDPs

(percent)

	3rd Plan performance	4th Plan objectives	4th Plan performance
Exports of goods	**16.0**	**4.7**	**15.0**
Oil and gas	16.3	2.3	12.8
Non-oil exports	14.7	10.7	24.1
Imports of goods	**23.6**	**6.6**	**12.3**
Exports of services	**17.3**	**14.9**	**11.6**
Imports of services	**17.2**	**6.1**	**10.8**

Exports and Imports during the 4th FYDP

(million dollars)

	Average growth during the 3rd Plan	1384	1385	1386	1387	1388	Average growth during the 4th Plan
Exports of goods	**31,680**	**64,525**	**76,190**	**97,667**	**101,289**	**88,326**	**85,599**
Oil and gas	26,051	53,820	62,011	81,567	82,403	66,190	69,198
Non-oil exports	5,629	10,705	14,179	16,101	18,886	22,136	16,401
Imports of goods	**25,262**	**43,381**	**49,987**	**58,240**	**70,175**	**69,247**	**58,206**
Exports of services	**4,564**	**6,332**	**7,778**	**10,093**	**11,045**	**9,865**	**9,023**
Imports of services	**9,115**	**12,580**	**13,879**	**17,568**	**19,684**	**19,569**	**16,656**

[1] Export value of crude oil, natural gas, condensates, and natural gas liquids by NIOC, NIGC, and NIORDC

[2] Export value of condensates and natural gas liquids by petrochemical companies are mentioned in non-oil exports.

Despite favorable growth of non-oil exports during the 4th FYDP, non-oil exports accounted for almost 19 percent of total exports, much lower than the Plan projection of 30.4 percent. Sharp rise in crude oil prices during the course of the 4th FYDP led to this under-realization.

Comparison of Non-Oil Exports with Total Exports, Imports, and GDP

(percent)

	3rd Plan performance	4th Plan objectives	4th Plan performance
Ratio of non-oil exports to total exports	21.6	30.6	23.7
Ratio of non-oil exports to imports	22.3	28.7	28.2
Ratio of non-oil exports to GDP [1]	4.9	5.8	5.6

[1] 4th Plan objective is based on the rate of economic growth, inflation, and the dollar vis-à-vis the rial.

Balance of Payments

Comparison of balance of payments performance and the Plan targets points to a balanced and favorable position of external sector during the 4th Plan. Based on Table No. 5 mentioned in Chapter 7 of the 4th FYDP, current account of balance of payments was projected to run $4,922 million deficit on average per annum during this Plan. However, rise in global price of crude oil and other major exports as well as increase in the volume of non-oil exports resulted in current account surplus by $20,177 million on average per annum.

Furthermore based on the mentioned table, it was projected that capital account surplus should be $6,262 million on average per annum, due to foreign financing. However, rise in foreign exchange revenues due to high current account surplus in tandem with international constraints on foreign financing brought about capital account deficit of $8,940 million on average per annum during the 4th Plan.

External Debt Position

The ratio of debt service payments to export earnings is a major indicator for the evaluation of external debt position. Based on international de facto standards, a debt service ratio of 30 percent foreign debt is a permissible benchmark for developing countries' exposure to default risk. According to Article 13 of the 4th Plan, the government should schedule foreign debt financing and debt obligation repayments, including the structure of short- and medium-term debt, so that annual debt repayments (excluding the oil and gas sector buy-back contracts) do not exceed 30 percent of total government foreign exchange earnings in the last year of the 4th Plan. According to real data, foreign debt servicing in the Iranian economy never reached that critical limit during the 4th FYDP period.

Balance of Payments Position during the 3rd and the 4th FYDPs

(million dollars)

	Average performance 3rd Plan	1384	1385	1386	1387	1388	Average performance 4th Plan
Current account balance	**2,417**	**15,392**	**20,585**	**32,594**	**22,837**	**9,477**	**20,177**
Trade balance	6,418	21,143	26,204	39,427	31,114	19,080	27,394
Services	-4,552	-6,248	-6,100	-7,475	-8,639	-9,704	-7,633
Transfers	550	496	482	642	362	101	417
Capital account balance	**1,792**	**-164**	**-6,306**	**-13,597**	**-10,907**	**-13,728**	**-8,940**
Long-term (net)	1,810	1,875	2	-2,315	-3,616	-1,507	-1,112
Short-term	-18	-2,039	-6,308	-11,282	-7,291	-12,222	-7,828
Overall balance (change in international reserves)	**4,601**	**14,567**	**11,389**	**15,254**	**8,229**	**-7,268**	**8,434**

Average annual figures of external debt show that 62.3 percent of average annual external debt ($23,891 million) during the 4th Plan period had a medium- to long-term repayment schedule. Comparison of 4th Plan performance with the 3rd Plan indicates higher current value of external debt as well as an improved composition of short- and long-term repayment schedule.

External Debt Position during the 3rd and the 4th FYDPs

(million dollars-percent)

	Average performance 3rd Plan	1384	1385	1386	1387	1388	Average performance 4th Plan
Total	**14,137**	**24,264**	**23,514**	**28,647**	**21,502**	**21,526**	**23,891**
Long-term	9,447	13,578	14,414	18,756	14,903	12,739	14,878
Short-term	4,690	10,686	9,100	9,891	6,599	8,787	9,013