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IMF Staff Completes ٢٠١٥ Article IV Mission to Islamic Republic of Iran

End-of-Mission press releases include statements of IMF staff teams that convey preliminary findings after a visit to a country. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board. Based on the preliminary findings of this mission, staff will prepare a report that, subject to management approval, will be presented to the IMF's Executive Board for discussion and decision.

An International Monetary Fund (IMF) team, led by Mr. Martin Cerisola, Assistant Director of the Middle East and Central Asia Department, visited Tehran during September ١٩-٣٠ to conduct the ٢٠١٥ Article IV Consultation discussions. Aasim M. Husain, Deputy Director of the Middle East and Central Asia Department, also participated in some of the discussions. The IMF team exchanged views with senior officials of the Central Bank of Iran (CBI) and the Management and Planning Office (MPO) and other government agencies on recent developments in the Iranian economy, the near-term outlook, and the authorities' plans on macroeconomic policies and structural reforms. The IMF team also met with a wide range of public sector officials and representatives of the business community, academia, and trade unions. Based on the visit, a staff report will be prepared and presented to the IMF's Executive Board in early December.

At the conclusion of the visit, Mr. Cerisola issued the following statement:

"The agreement on Iran's nuclear program and the envisaged lifting of economic sanctions bring a unique opportunity to build on and broaden the achievements of the past two years. Prudent policies have allowed the economy to return to positive growth last year and to reduce inflation to around ١٥ percent. The authorities have also regained stability in the foreign exchange market and advanced with subsidy reform.

"However, the economy faces severe structural challenges. The sharp decline in global oil prices has cooled off the momentum in economic activity. The corporate sector confronts weak demand with large inventories and low capacity utilization. The banking system faces high nonperforming assets that have resulted in unsustainably high real interest rates and stagnant credit to the economy. Arrears accumulated by the public sector over the past two years compound these problems. As of December ٢٠١٤, unemployment remained at ١٠.٥ percent.

“The economy is weak at present. The sharp decline in global oil prices, tight corporate and bank balance sheets, and postponed consumption and investment decisions ahead of the expected lifting of economic sanctions, have significantly slowed down economic activity since the fourth quarter of ٢٠١٤/١٥. The economy may have contracted during the first half of ٢٠١٥/١٦, and as a result, real GDP growth is projected to decline from ٣ percent in ٢٠١٤/١٥ to somewhere between ٠,٥ to -٠,٥ percent in ٢٠١٥/١٦, depending on the exact timing of the expected lifting of sanctions. Point-to-point inflation has declined to around ١٢ percent in recent months, largely reflecting lower food and beverage inflation, and the inflation rate is expected to remain close to ١٤ percent by year-end.

“Prospects for ٢٠١٦/١٧ are brighter. Higher oil production, lower costs for trade and financial transactions, and restored access to foreign assets, would be expected to lift real GDP to about ٤-٥.٥ percent next year. A significant part of this growth would be the result of higher oil production (of at least ٠,٦ mbpd to an official estimate of ١ mbpd), with lower trade and financial transaction costs accounting for ٠,٧٥-١ percentage point of growth. Much of the acceleration in growth would also depend on the spillovers from higher oil production to the rest of the economy. Higher oil revenue and terms of trade, and renewed access to foreign assets and capital can lead to appreciation pressures on the real exchange rate. Continued gradual fiscal consolidation—including by sustaining tax revenue mobilization and subsidy reform efforts—and prudent monetary policy, anchored by the authorities’ goal of achieving single-digit inflation by the end of ٢٠١٦/١٧, can mitigate these upward pressures. The authorities’ intention to unify the foreign exchange market while preserving a competitive real exchange rate is welcome.

“Comprehensive reforms are critical to ensure that the envisaged lifting of economic sanctions entrenches macroeconomic stability and leads to high and inclusive growth over the medium term. The authorities have taken important steps over the past year, by completing an initial financial health check of the banking system, and by preparing drafts to reform banking and central bank laws to strengthen the frameworks for prudential supervision and monetary policy. They have also started to work on measures to address the linkages between government arrears to suppliers, nonperforming loans, and public debt to banks. Further reforms are now needed for the policy framework to be able to respond more effectively to shocks and achieve price stability, by bringing more of a medium-term perspective to fiscal policy formulation, rebuilding buffers and enhancing transparency, and by operationally strengthening the CBI to deal with unlicensed financial institutions. Enhancing the business environment, governance, and restructuring the corporate and financial sectors will enhance productivity growth and reduce unemployment, especially among youth and women. The complexity and extent of the problems require strong political leadership and support for decisive and coordinated action.

“Risks to the outlook are significant, and longer-term prospects will depend crucially on the depth of reforms that are undertaken. Uncertainties about the implementation of the nuclear agreement could constrain foreign direct investment and capital inflows. Iran’s full return to the oil market could bring oil prices down further, and force additional fiscal adjustment. Domestically, nonperforming loans and tight cash-flows in the financial and corporate sectors may undermine investment. Pent-up demands from different sectors may also pose some risks to macroeconomic stability. Ultimately, if mild reforms are implemented the sanctions relief will have only a moderate positive impact on the economy. If, on the other hand, more assertive and deeper reforms along the lines outlined above are carried out, the boost to confidence and investment inflows would put Iran’s economy on a significantly higher growth trajectory."