CHAPTER ONE

OVERVIEW

Economic policies for 1382 (2003/04) were designed within the framework of the 3rd FYDP Law. On this basis, the growth of output and investment, provision of financial resources required by economic sectors, reduction of unemployment and inflation rates were among major priorities in this year. During the review year, output and investment performance was better than the plan targets. Structural reforms appear to have been the main driving force behind this growth. These reforms include: positive impact of the Oil Stabilization Fund (OSF) on the government budget and private sector, revision of Foreign Investment Promotion and Protection Act, utilization of participation papers to finance government projects in a non-inflationary way and mopping up of excess liquidity from the market, implementation of Tax Consolidation Act since the beginning of 1382, approval of the Law for Facilitating Renovation of Industries, and implementation of policies aimed at budget transparency through making "implicit energy subsidy" explicit.

To reduce unemployment as the major challenge of the Iranian economy, certain measures were taken in this year. In this respect, facilities were extended by banks to economic sectors to be used both in providing working capital of manufacturing units and in implementing development job creating projects.

During 1382, despite recession prevailing in the world economy, continued crude oil price hike, along with implementation of the mentioned policies caused transfer of a significant amount of financial resources from international market to financial markets of developing and new emerging economies. Persian Gulf region developments and political disputes in Iraq intensified this trend. The Iranian economy was affected by the impacts of the mentioned developments through international oil and financial markets. Increase in oil revenues raised the Central Bank foreign exchange reserves markedly and also government's foreign exchange reserves in the OSF.

In the review year, external sector of the economy indicated a rapid decline in the current account surplus. The gradual weakening of the current account during the recent years is attributable to the surge in imports and lack of rebound in non-oil exports. Although liberalization of foreign trade has facilitated import during the recent years, it has not been accompanied with supporting policies aimed at maintaining the competitiveness of the national economy and export diversification. The capital account of balance of payments has been improved after repayment of rescheduled external debts was terminated. Moreover, narrow capital account liberalization is reflective of interest rate trend in international markets and utility of investment in financial markets of new emerging economies like Iran. The above mentioned measures taken and the policies adopted paved the way for significant positive developments in different sectors, including services, agriculture, manufacturing and mining and oil. Therefore, according to the preliminary estimates, GDP growth at constant 1376 prices reached 6.7 percent. This shows a realization of targets set in the 3rd plan when compared with the growth target rate of 6.7 percent for 1382 and average growth target rate of 6 percent in the 3rd Plan. In this year, gross domestic fixed capital formation including machinery and construction grew by 10.1 percent compared to the previous year. On the other hand, growth of national income compared to the relatively constant growth of population caused the per capita income of country at current and constant 1376 prices to reach Rls. 14,031 and 5,139 thousand, respectively.

Implementation of government support policies in the agriculture sector in the framework of distribution of inputs at support prices, guaranteed purchase of basic agricultural products and extending of banking facilities at preferential rates, along with increase in the rainfall raised the production of most agricultural crops.

In 1382, in conformity with the OPEC members' adherence to production quota, the average production of crude oil grew by 13 percent to 3.7 mb/d. In this year, crude oil export increased by 18.6 percent and reached 2.4 mb/d and export of oil products grew by 4.8 percent to 282 thousand b/d.

Despite structural bottlenecks in the manufacturing sector, the value-added of manufacturing and mining sectors at constant 1376 prices went up by 9.9 and 12.7 percent, respectively compared to the previous year. The comparison of these growth rates with the targets set in the 3rd plan for the year under review shows that these rates stood at higher levels.

The economic indices in construction and housing sector grew moderately in 1382. The value-added for the mentioned sectors decreased by 1.3 percent, while gross fixed capital formation for these sectors increased by 2.9 percent compared to the previous year.

Government general budget was designed in line with the targets set in the 3rd Plan while focusing on employment, restraining the growth of current expenditures, completion of semi-finished projects and preventing start of new projects, attracting private sector investment, rationalizing the size of government, improving budget structure and enhancing the budget transparency.

According to the budget figures for 1382, government revenues amounted to Rls. 78,836.6 billion and government expenditures reached Rls. 178,255.2 billion. In this year, the operating balance of government budget faced Rls. 99,418.6 billion deficit. In 1382, government receipts out of disposal of non-financial assets was Rls. 129,030.9 billion and acquisition of non-financial assets (development expenditures) was Rls. 60,982.9 billion. Thus, the net disposal of non-financial assets was Rls. 68,048 billion in 1382.

Thus, the operating and non-financial balance faced a deficit of Rls. 31,370.6 billion in 1382 which was financed through net disposal of financial assets including sales of participation papers, privatization revenues, and withdrawal from the OSF. In this year, the ratio of operating and non-financial balance to GDP was 2.9 percent.

The trade balance with the inclusion of oil exports enjoyed $ 4,430 million surplus, which compared to similar figure of the previous year showed 28.6 percent reduction. In this year, the current account balance ran a surplus of $ 816 million. Capital account of balance of payments also enjoyed a surplus of $ 4,476 million. As a result, foreign reserves of the Central Bank and OSF (the overall balance) showed $ 4,667 million surplus in 1382. Moreover, the external debt and contingent obligations increased from $ 27.2 billion (including interest and contingent obligations) at the end of 1381, to $ 34.7 billion at the end of 1382, enjoying 27.6 percent hike.

During 1382, the expected rates of return on banking facilities in different sectors of the economy changed as compared to 1381, and in certain sectors showed reduction. In the review year, a total of Rls. 29,289 billion participation papers were issued by government, public corporations and the Central Bank. In this context, to implement monetary policies and mop up excess liquidity the CBI issued participation papers to substitute for the matured papers of the previous year. The provisional rate of these papers was 17 percent per annum. Liquidity grew by 26.1 percent in the review year, due to the rise in monetary base and money multiplier.

The Tehran Stock Exchange (TSE) witnessed a significant boom in 1382 in that all major stock indices recorded unprecedented levels. Price and dividend index grew 2.4 times of the respective previous figure. Thus, in terms of market capitalization and total share price index, the TSE stood the second among world stock exchanges. The ratio of market capitalization to GDP increased to 27.3 percent.

Due to factors affecting aggregate demand and supply and inflationary expectations, the downward trend of inflation rate in previous years was reversed since the beginning of 1381 and reached 15.6 percent in the review year.