CHAPTER ONE

OVERVIEW

Despite regional tensions and international pressures, the Iranian economy performed relatively well during the 3rd FYDP ending 1383. During the 3rd Plan, the economy enjoyed a sustained growth, partly due to policy decisions and extensive deregulations to enhance private sector contribution to economic activities and partly to positive movements of crude oil prices in international markets. Foreign trade system moved toward further liberalization through revision in trade tariffs and granting more flexibility to exporters in managing their exports proceeds. The successful implementation of exchange rate unification, integration of exchange market in the form of interbank market and limiting informal market, deregulating foreign trade procedure, and improvement in the composition of external debt were among the salient achievements of the Iranian economy during the 3rd Plan period. The Tehran Stock Exchange (TSE) also experienced a relative upturn. With the inauguration of agricultural commodity exchange and expansion of provincial exchanges, the investors were further encouraged to invest in the stock exchange. Due to implementation of structural reforms in the 3rd plan, most of economic indicators showed a better performance as compared to the previous periods.

COMPARISON OF TARGETS AND PERFORMANCE OF THE IRANIAN ECONOMY DURING THE 3rd FYDP (percent)

	Average performance of the 2nd Plan	Annual growth target of the 3rd Plan	Average performance of the 3rd Plan
Annual GDP growth (at basic price)	3.2	6.0	5.5
Investment growth	8.0	7.1	9.5
Inflation rate	25.6	15.9	14.1
Unemployment rate (1)	12.0	10.7-12.6	12.5

(1) Figures for average performance of the 2nd and 3rd Plans are released by Statistical Center of Iran. The annual growth target of the 3rd Plan is related to the last year of the Plan in the framework of minimum and maximum unemployment scenarios and is calculated by the Management and Planning Organization.

The Iranian economy experienced a high growth in the last year of the 3rd FYDP, though there were signs that it lost its momentum in 1383. The moderate pace of oil price rise in tandem with the policies adopted by the government directed the Iranian economy to achieve a positive growth in output and investment. This was against the background of a relatively stagnant condition in the world, unfavorable political situation in the Persian Gulf and structural impediments to manufacturing and services units. Moreover, relatively stable domestic financial market and sustainable external sector, resulting largely from high oil price rise, played a pivotal role in bringing growth to the Iranian economy.

In the review year, reducing the unemployment rate and creating new employment opportunities were the major challenges the national economy faced. In order to encounter with unemployment problem, banking system attempted to extend large amount of facility to various sectors of the economy. These were basically utilized to finance the working capital of productive units and to implement development projects and new employment creation plans.

In 1383, world crude oil market developments and gradual implementation of new regulations for facilitating foreign trade to help the realization of 3rd FYDP targets, along with surge in imports, affected the balance of payments. In this year, Iran's interaction with the world economy was set in such a manner that the major balance of payments accounts posted a surplus. The significant growth of foreign exchange revenues from oil and gas exports was the main factor for the rise of trade balance surplus and significant increase in foreign exchange reserves of the country, despite increase in imports.

Foreign exchange receipts from oil exports, after observing legal requirements, ran a surplus and covered expenses as envisaged in the Budget Law for 1383. This was deposited into the OSF, bringing its balance to $9.5 billion at the year-end.

Further reduction in the expected rate of return on banking facilities and increase in the share of free uses of banks for extending banking facilities were major policies implemented in 1383. In this year, the Money and Credit Council (MCC), with the aim of mobilizing investments, reducing production costs and increasing productive activities, reduced the expected rate of return on facilities extended by public banks to manufacturing and mining and exports sectors by one percentage point as compared with 1382. Moreover, based on the 1383 Budget Law, the Central Bank was authorized to regulate and implement facilities extended by the banking system, the ratio of long-term to short-term credits and facilities, and credit plans of the banking system so as to realize the targets of the 3rd FYDP aiming at curbing inflation and achieving economic growth.

The economic measures taken in 1383 paved the way for GDP growth of 4.8 percent (at constant 1376 prices). Part of this increase in output served for capacity building of the economy in the framework of gross domestic fixed capital formation including machinery and construction and caused the gross domestic fixed capital formation to grow by 7 percent as compared with the previous year. On the other hand, growth of national income as compared to the relatively constant growth of population made the per capita income grow by 25.3 percent to Rls. 17,795 thousand at current prices and 7.9 percent to Rls. 5,518 thousand at constant 1376 prices.

In 1383, continuation of government support policies in the agriculture sector, in the framework of distribution of production inputs at support prices, guaranteed purchase of basic agricultural products and extending of banking facilities at preferential rates, despite reduction in the precipitation level, raised the production of most agricultural crops. As a result, production of cereals including wheat, barley, rice and corn increased by 5.0 percent as compared with the previous farming year. Livestock products enjoyed growth in the review period as well.

In 1383, in conformity with the OPEC members' adherence to production quota, the average crude oil production grew by 4.9 percent to 3.9 mb/d. In this year, crude oil export increased by 6.5 percent and reached 2.6 mb/d and export of oil products was reduced by 7.6 percent to 261 thousand b/d.

Increasing oil revenues and its ensuing effect on the import of raw materials and intermediate goods required by the manufacturing sector raised the value-added in manufacturing and mining sectors (at constant 1376 prices) by 12 and 8.8 percent, respectively, as compared to the previous year, well above the target set by the plan for this year.

The strategies envisaged in the 3rd FYDP, such as utilization of administered funds and extending foreign exchange facilities out of the OSF, while supporting private sector and government initiatives during the past years, improved manufacturing and mining activities and raised private sector investment. Therefore, the production index of large manufacturing establishments grew by 12.9 percent as compared with the previous year.

Despite a boom in manufacturing and mining sectors, activities of construction sector slackened which was due to the stagnation in housing market. Consequently, the value-added and gross fixed capital formation of these sectors plummeted by 4.1 and 3.5 percent, respectively as compared with the previous year.

According to the budget performance figures for 1383, government revenues reached Rls. 103,587.3 billion and government expenses amounted to Rls. 231,923.1 billion. Thus, the operating balance of government budget ran a deficit of Rls. 128,335.8 billion.

In 1383, government receipts from disposal of non-financial assets were Rls. 151,413 billion, with acquisition of non-financial assets (development expenditures) at Rls. 72,306.3 billion. Thus, net disposal of non-financial assets was Rls. 79,106.7 billion in 1383. Therefore, sum of operating balance and net disposal of non-financial assets in 1383 ran a deficit of Rls. 49,229.2 billion.

The government budget deficit was basically financed through net disposal of financial assets, including sale of participation papers, privatization revenues, returns carried over from previous years, and withdrawal from the OSF. In this year, the ratio of operating and non-financial balance to GDP was 3.6 percent.

In 1383, the major balance of payments accounts enjoyed surplus and some basic variables of customs faced an upward trend. Extending of facilities (in rials and foreign exchange) for the export of goods and services, exempting of exports from taxes and levies and granting of export rewards and subsidies in the context of relatively stable foreign exchange market pushed the non-oil exports up by 13.6 percent to $7,537 million in 1383. The value of imports grew by 29.2 percent to $38,199 million. As a result, trade balance, with inclusion of oil exports, enjoyed $5,653 million surplus. This shows 27.6 percent growth as compared with the previous year. Therefore, in this year, current account balance ran a surplus of $1,442 million as capital account enjoyed a surplus of $7,388 million.

Net foreign reserves of the Central Bank and the OSF (the overall balance) showed $8,731 million surplus in 1383. Moreover, the net external debt and contingent obligations (including interest) increased from $34.7 billion at the end of 1382 to $42.8 billion at the end of 1383, enjoying 23.5 percent rise. During this period, external debt grew by 39.1 percent to $16,831 million.

Liquidity grew by 30.2 percent in 1383, against 26.1 percent in the previous year. This was due to increase in monetary base and money multiplier. Composition of liquidity indicates that the share of money in liquidity fell and that of quasi-money went up. This was primarily due to reduction in inflation rate, increase in banks real profit rate and stagnant exchange market.

During 1383, public banks extended facilities to non-public manufacturing and mining, housing and construction and trade, services, and other sectors, well above the shares approved by the Money and Credit Council. In this year, private banks and credit institutions could absorb the non-public sector deposits to a large extent when compared with public banks. This was due to their freedom in extending facilities with higher profit rate.

Tehran Stock Exchange (TSE) indices in terms of value and number of shares traded, number of buyers, TSE price index and financial and industrial indices grew remarkably in the review year, although there were signs of relative slowdown in the second half of the year. The inauguration of agricultural commodity exchange, special trading floors and expansion of regional stock exchanges paved the ground for further presence of investors in the stock exchange.

Issuance of participation papers continued in the review year to finance development projects and to implement monetary policy. As a result, the government and public corporations issued Rls. 16.7 trillion participation papers for the implementation of water, electricity, road and transportation and petrochemical projects, Rls. 15.6 trillion of which was sold. The CBI in addition to the issuance of Rls. 5 trillion new participation papers substituted the previous matured Central Bank's Participation Papers (Rls. 16.6 trillion). Out of total participation papers issued by the CBI, (Rls. 21.6 trillion), a sum of Rls. 20.2 trillion was sold.

Increase in liquidity growth and decrease in economic growth trend caused the GDP deflator to grow more than that of the previous year. This increase was mainly reflected in the price of non-consumer goods and services, so that the inflation rate declined slightly to 15.2 percent.