PART ONE

ECONOMIC DEVELOPMENTS
OF IRAN IN 1384
(2005/06)

In the Name of God,

The Compassionate, The Merciful

CHAPTER 1 OVERVIEW

Iranian economy performed relatively well in the first year of the 4th Five-Year Development Plan and in the context of the Twenty-Year Vision Plan. Despite regional and international tensions during 1384 (2005/06), the economy continued its path on the basis of the economic policies drawn up in the 4th FYDP, aimed at enhancing interaction with the global economy to boost competitiveness. The GDP (gross domestic product) registered a growth rate of 5.4 percent (at constant 1376 prices) in comparison with the previous year. Real gross fixed capital formation enjoyed the same upward trend as the previous year and increased by 5.8 percent in comparison with 1383.

During this year, most economic indicators (except for stock exchange) improved. Inflation rate reached 12.1 percent, which, compared to that of the previous year, showed a decrease of 3.1 percentage points. Facilitation in foreign trade regulations and provision of various facilities and rewards to exporters caused the non-oil exports to hit a record high of $10.5 billion, while imports reached an unprecedented level of $43 billion during the review period. Depreciation of real exchange rate, leading to reduction in competitiveness of domestic products, had a great contribution to the increasing growth of imports in the review year.

Further participation of the private sector, enhancement of productivity, facilitation of trade regulations, establishment of financial discipline, further decentralization, utilization of Oil Stabilization Fund (OSF), and targeting of subsidies were the attempts made in 1384 to pave the way for long-term sustainable economic growth and improved income distribution.

The key measures and policies adopted during 1384 in monetary, foreign exchange and fiscal sectors were adjustment and unification of profit rate of banking facilities extended to all economic sectors at 16 percent; increase in the ceiling for housing facilities extended by banks from Rls. 80 to 100 million, except for Bank Maskan which increased from Rls. 120 to 180 million; allocation of at least 25 percent of banking facilities to water and agriculture sector; grant of establishment permit to Pasargad and Sarmayeh private banks; extension of facilities to Small and Medium-sized Enterprises (SMEs) by the non-public sector; enhancement of organizational efficiency and improvement of labor productivity of Tax Affairs Organization; disposal of government shares in the form of Justice Shares by Iran Privatization Organization; facilitation of trade and liberalization of foreign exchange transactions; extension of facilities (in rial or foreign exchange) for the export of goods and services; exemption of the aforesaid from taxes and levies and grant of export rewards and subsidies in the context of relatively stable foreign exchange market; as well as greater flexibility of external debts management.

The economic measures taken in 1384 resulted in 5.4 percent growth of GDP. 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, which showed a growth of 5.8 percent. On the other hand, growth of national income as compared to the relatively constant growth of population raised the per capita income by 21.0 percent to Rls. 21,548 thousand at current prices and 6.5 percent to Rls. 5,878 thousand at constant 1376 prices.

In 1384, continuation of the government support policies in the agriculture sector, in addition to the rise in precipitation level, raised the production of most farming crops by 9.4 percent as compared with the previous farming year. Livestock products enjoyed a growth rate of about 7.1 percent. In the review year, increase in the guaranteed purchase price of wheat led to purchase of 10.9 million tons of wheat by the government. On the whole, wheat production declined by 1.8 percent to 14 million tons as compared with the previous year. Horticultural produce enjoyed growth in the review period as well.

In 1384, in conformity with the OPEC members' adherence to production quota, the average crude oil production amounted to 4.1 mb/d. In this year, crude oil export increased by 2.1 percent and reached 2.6 mb/d on average and export of oil products was reduced by 6.1 percent to 245 thousand b/d. Generation and consumption of electricity grew in the review period as well.

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 by 7.1 and 10.5 percent, respectively, as compared with the previous year. In this year, support of small manufacturing enterprises, together with the utilization of administered funds, improved manufacturing and mining activities and raised private sector investment. Therefore, the production index of large manufacturing establishments grew by 4.5 percent as compared with the previous year. Similarly, production of most industrial goods rose.

Construction activities exhibited a growth of less than GDP growth in 1384. The value-added and gross fixed capital formation of this sector grew by 4.4 and 4.7 percent, respectively, as compared with the previous year. The outstanding facilities extended to the non-public "construction" and "housing" sectors in 1384 year-end grew by 25.0 and 40.2 percent, respectively, as compared with the previous year. The private sector started the construction of 176.2 thousand new buildings with 62.9 million square meters floor space in the urban areas, besides completing 168.6 thousand semi-finished buildings of 64.9 million square meters. Moreover, the number of housing units completed by the private sector grew by 52.4 percent to 479.2 thousand in the urban areas.

The Budget Law for 1384, as the first Budget Law drawn up during the course of the 4th FYDP, was prepared and formulated within the framework of the 4th FYDP and without borrowing from the banking system. According to the 1384 Budget Law and the Budget Supplements thereto, the approved revenues, including taxes and other revenues, (excluding special revenues and including approved figure for transparency in the price of energy bearers) and expenses (excluding special expenses and including approved figure for subsidy on energy bearers) amounted to Rls. 469,045.3 and 613,061.7 billion, respectively. As a result, the operating balance (approved) ran a deficit of Rls. 144,016.4 billion. Moreover, approved receipts and payments out of disposal and acquisition of non-financial assets (excluding special receipts and payments) reached Rls. 197,313.4 and 138,409 billion, respectively. Thus, the sum of operating balance and net disposal of non-financial assets (approved) ran a deficit of Rls. 85,112 billion, which was mainly financed through withdrawal from the OSF and privatization proceeds.

Review of the figures related to budget performance in 1384 reveals that general budget sources (including the figure for transparency in the price of energy bearers and excluding special revenues and expenditures) were financed out of revenues by 63.3 percent, from disposal of non-financial assets by 25.4 percent, and from disposal of financial assets by 11.3 percent. Budget uses (including the figure for subsidy on energy bearers) represented realization of 81.0 percent from expenses, 15.9 percent from acquisition of non-financial and 3.0 percent from acquisition of financial assets.

Regarding the performance of revenues and expenses and disposal and acquisition of non-financial assets, sum of operating balance and net disposal of non-financial assets ran a deficit of Rls. 60,853.4 billion. This figure, i.e. budget deficit, was financed through net disposal of financial assets. In the review year, net disposal of financial assets equaled Rls. 60,853.4 billion, financing the deficit of the operating and non-financial balance. This, with inclusion of the increase in the outstanding balance of foreign exchange obligations account, i.e. government indebtedness to the CBI, was further adjusted to Rls. 61,018 billion.

Continued rise in world crude oil price together with facilitation in foreign trade and liberalization of foreign exchange transactions as the targets set in the 4th FYDP affected balance of payments in 1384. The value of non-oil exports grew noticeably by 39.9 percent to $10,546 million in 1384. The value of imports rose by 12.8 percent to $43,085 million. Thus, the trade balance posted a surplus of $21,281 million, indicating a remarkable rise of 276.5 percent compared with the respective figure of the previous year. Current account balance registered a surplus of $16,637 million, while capital account recorded a deficit of $184 million. Total foreign reserves of the CBI surged by $13,574 million and total foreign exchange obligations (including actual and contingent obligations) increased to $41,853 million at year-end, signifying 0.2 percent growth. External debt grew by 5.2 percent to $24,264 million, while the share of short-term external debts in total debts slightly declined.

In 1384, liquidity (M2) grew by 34.3 percent, showing 4.1 percentage points increase. In this year, the share of money in liquidity declined and that of quasi-money increased. This was primarily due to rise in public confidence in banks, reduction in inflation rate, and increase in public tendency to save. Government indebtedness to banks and non-bank credit institutions decreased by 6.1 percent to Rls. 34,539.6 billion in 1384, mainly due to reduction in the stock of public sector participation papers.

Facilities extended by public banks to the non-public sector, including matured and non-performing claims and excluding profit and revenue receivables, increased by Rls. 208,877.8 billion. Non-public sector enjoyed the lion’s share of 88.3 percent of total facilities provided by banks, part of which was in the form of directed facilities. According to the 4th FYDP Law, at least 25 percent of banking facilities were allocated to water and agriculture sector. The highest amount of facilities extended to the non-public sector belonged to domestic trade, services and miscellaneous, manufacturing and mining, construction and housing, and agriculture sectors. The exports sector, on the other hand, received the lowest amount. In this year, matured and non-performing claims of banks and non-bank credit institutions on the non-public sector rose by 75.4 percent as compared with the previous year. Non-public sector deposits with commercial banks grew by 26.3 percent to Rls. 132,192.3 billion. Meanwhile, non-public sector deposits with the specialized banks grew by Rls. 37,734.3 billion.

Flourishing during the course of 1381 to 1383, the Tehran Stock Exchange (TSE) experienced a dramatic fall in the second half of 1383. The slump continued in 1384 and bottomed out by the end of the year. Against the backdrop of bubble market, certain factors were responsible for this slump, namely companies' willingness to increase their capital through revaluation, increase in P/E ratio, rise in capital of various banks and investment companies and the need for their subscription, transfer of investment companies resources to development projects undertaken by unlisted companies, supply of public corporations' shares at the last months of the year and an escalation of tension over Iran's peaceful nuclear program.

In 1384, value of shares and rights, market capitalization, the turnover ratio, and the price and dividend index declined as compared with the previous year. In this year, total shares offered by public institutions and corporations showed a reduction of 76.9 percent in the number and 90.4 percent in the value when compared with the previous year. In the review year, the foundations and banks did not offer any shares. Issuance of participation papers continued in the review year to finance development projects and to implement monetary policy. A sum of Rls. 34,800 billion participation papers were issued by the government, Central Bank, and corporations. Of this amount, 82.7 percent (Rls. 28,768.3 billion) were sold, showing a fall of 25.9 percent when compared with the previous year. Out of total participation papers sold, the share of government, the CBI and others (including Rayan Saipa Company, National Petrochemical Company, Bank Keshavarzi, Bank of Industry and Mine, and Mashad Municipality) were 40.7, 37.4 and 18.4 percent, respectively. Moreover, Iran Khodro Company issued one trillion rials participation papers of three-year maturity. In 1384, the CBI issued and sold participation papers worth Rls. 16,800 and 10,768.3 billion, respectively. The new participation papers of one-year maturity were sold in three phases.

The inflation rate declined by 3.1 percentage points and reached 12.1 percent in 1384. Despite high liquidity growth, factors such as the implementation of the Amended Law on Article 3, 4th FYDP Law, relatively stable exchange rate, recessionary housing market conditions which led to reduction in rentals, decrease in the velocity of circulation of money, surge in imports of consumer goods, and decrease in import tariffs of several fruits, in conjunction with benign climatic conditions of recent years, resulted in the deceleration of inflation rate as compared with the previous year. The wholesale and the producer price indices decreased by 5.2 and 7.3 percentage points, respectively, in the twelve-month period ending Esfand 1384 as compared with the previous period, and reached 9.5 percent. On the other hand, the exported goods price index went up by 16.2 percent compared with the previous year.