

Global Economy and the External Transactions of Iran

The performance of Iranian economy in 1387 should be assessed in light of the world economic environment which after experiencing prolonged economic growth and improvement entered a slowdown period in mid-2008. The immediate impacts of the world economic and financial crisis on the economy of Iran were the sharp decline of foreign exchange earnings and the deterioration of Iran's balance of external payments.

Although the slowdown of the world economy was evident from some leading indicators in 2007, the financial crisis showed its full impact in mid-2008. It was in the second half of 2008 that the US mortgage market crisis spread into other advanced economies in a way that the central banks in some countries had to put emergency

measures in operation. With intensification of world financial crisis, the world market prices, in particular commodity prices, started to fall. Consequently, many advanced economies experienced sharp declines in employment and economic growth, and deterioration in external trade.

As a result of the widespread world crisis, GDP growth at world level which was high and had been rising continuously for several years, faced a declining trend. Based on IMF reports, the world economic growth in 2008 was 3.0 percent, 2.2 percentage points lower than the year before. The genesis of the 2008 financial crisis was such that it imposed the most severe damage on the advanced economies in a way that most of these countries entered the economic recession phase.

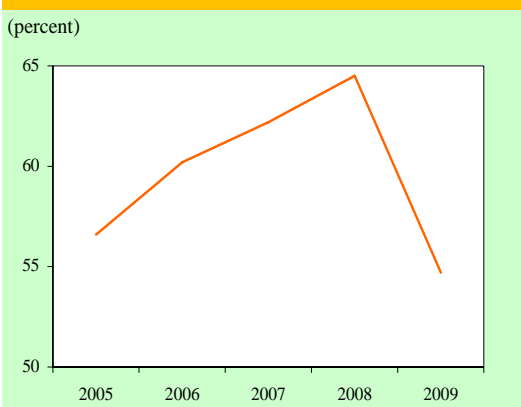
Economic Growth of the World and Selected Economies (percent)

	2005	2006	2007	2008	2009
World	4.5	5.1	5.2	3.0	-0.6
Advanced economies	2.7	3.0	2.8	0.5	-3.2
Emerging markets and developing economies	7.1	7.9	8.3	6.1	2.4
Developing countries in Asia	9.0	9.8	10.6	7.9	6.6
Middle East and North Africa (MENA)	5.3	5.7	5.6	5.1	2.4

Source: World Economic Outlook, IMF, April 2010

Pursuant to the sharp decline of global demand, the world trade of goods and services declined substantially, and the decrease 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 2008, growth of world trade declined by 4.4 percentage points and reached the exceptionally low figure of 2.8 percent. The financial crisis reached a new climax in the fourth quarter of 2008 and spilled over to the real sector of distressed economies. Trade statistics indicate that the world trade was most hit in the year 2009 and experienced declines of 10.7 percent in quantity and 10.9 percent in international prices.

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



Balance of Payments Developments

The balance of payments of Iran was adversely affected in the second half of 1387, due to inappropriate developments of world economy in the second half of 2008 and beginning of 2009. In the aftermath of world financial crisis, surplus of both current and trade accounts of Iran declined, the foreign reserve buildup decelerated, sharp constraints were imposed on foreign borrowings, and the foreign direct investment was affected adversely. However, the current account surplus of the balance of payments of Iran in 1387 was still noticeable and this development contributed to stabilizing the foreign exchange market.

It is noteworthy that the balance of payments of Iran is produced in accordance with the IMF Balance of Payments Manual, 5th edition (BPM5) published in 1993, as amended in later years.

Current Account

The current account, one of the primary components of the balance of payments, is the sum of goods, services, income, and current transfers¹. The growing trend of current account surplus, which started in 1384 following the run-up in global price of crude oil, was reversed in 1387. In this year,

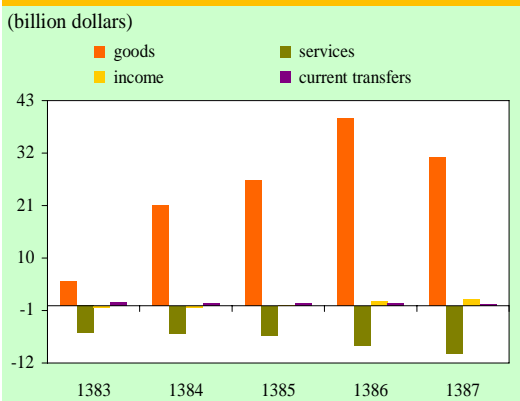
	World Trade Growth (percent)				
	2005	2006	2007	2008	2009
Goods and services					
Quantity	7.7	8.8	7.2	2.8	-10.7
Price (in US\$)	5.4	5.5	8.3	11.4	-10.9
Goods					
Quantity	7.5	8.8	6.5	2.4	-11.8
Price (in US\$)	6.2	6.2	8.4	12.2	-12.1

Source: World Economic Outlook, IMF, April 2010

¹ According to Balance of Payments Manual, 4th edition (BPM4), services account balance included income account. However, due to nature of the components and special position of income account in foreign exchange revenues, services and income are classified separately in the BPM5.

the current account surplus declined by about 30 percent to \$22,837 million, largely due to the fall in the goods account surplus and the rise in the services account deficit.

Figure 11.2. Current account balance components

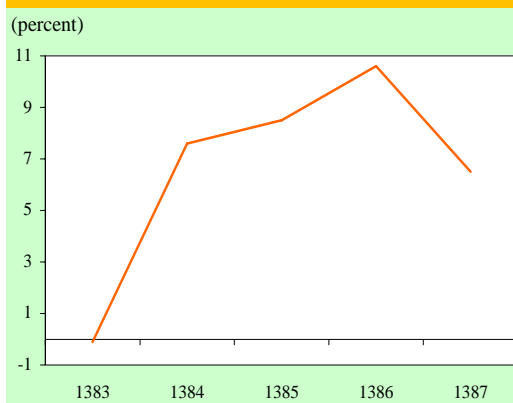


In the review year, ratio of current account surplus to GDP was 6.5 percent, down by almost 4.1 percentage points compared with the corresponding figure of 1386. This ratio in the "developing countries in Asia" and "Middle East and North Africa" declined

from 5.7 and 15.5 percent in 2008 to 4.1 and 1.8 percent in 2009, respectively.

Non-oil current account deficit with an upward trend reached almost \$56 billion, up by 22.6 percent. This rise points to the increased reliance of current account on the oil and gas exports. In this year, non-oil foreign exchange earnings constituted 29.3 percent of foreign exchange requirements of this account, which decreased by almost 2.5 percentage points compared with 1386¹.

Figure 11.3. Ratio of current account to GDP



Current Account Balance

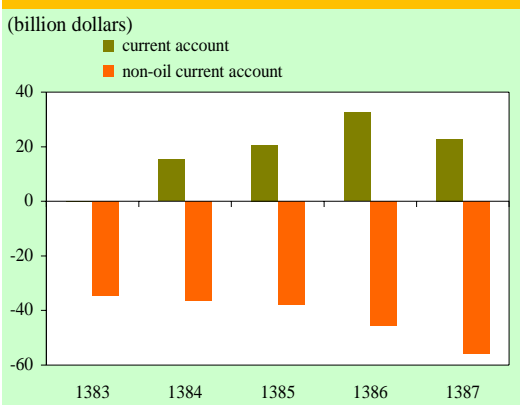
(million dollars)

	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Current account balance	-216	15,392	20,585	32,594	22,837	58.3	-29.9
Goods	5,073	21,143	26,204	39,427	31,114	50.5	-21.1
Services	-5,701	-5,841	-6,212	-8,429	-9,974	35.7	18.3
Income	-305	-407	111	954	1,335	▣	40.0
Current transfers	717	496	482	642	362	33.2	-43.6
Current account balance (non-oil)¹	-34,688	-36,306	-37,926	-45,663	-55,967	20.4	22.6

¹ Excludes 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).

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

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



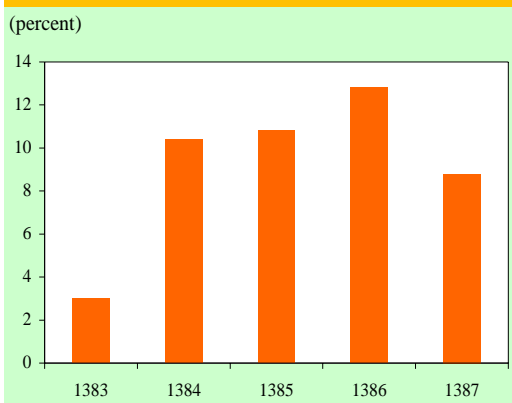
Goods Account (trade balance)

Share of goods in country's international trade was almost 87.0 percent in 1387, down by roughly 0.5 percentage point compared with the corresponding figure of the previous year. Moreover, Iran's share in international trade of goods declined slightly to 0.54 percent.

Following the slowdown in exports growth and surge in imports, the surplus of goods

account (trade balance) declined by 21.1 percent to almost \$31 billion in 1387. Thus, the ratio of goods account surplus (trade balance) to GDP at current prices decreased by almost 4.0 percentage points to 8.8 percent compared with 1386. Moreover, the export-import ratio fell by almost 23.4 percentage points to 144.3 percent, compared with the preceding year. However, non-oil trade balance deficit rose 22.8 percent to about \$47.7 billion.

Figure 11.5. Ratio of external trade balance to GDP



Box 3- Goods Account: Classification of Goods and the Statistical Sources of the IMF Balance of Payments Manual, 5th Edition (BPM5)

Based on the type of goods and the statistical sources, components of goods account (trade balance) are collected and registered by oil and non-oil goods. Therefore, data on exports and imports of crude oil, natural gas, condensates and natural gas liquids, and oil products by NIOC, NIGC and NIORDC are received from these companies. Then, data on exports and imports of gas and oil products by petrochemical companies and others are

extracted from Customs data, and added to data already mentioned.

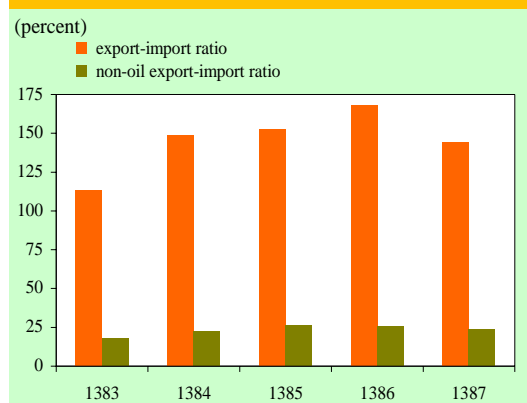
The data on non-oil trade are released by Islamic Republic of Iran Customs Administration, which after adjustments for statistical coverage are the basis for extraction of Balance of Payments statistics¹.

¹ IMF BPM5 facilitates adjustment of Customs data in terms of pricing, exchange rate, and time of reporting to analysts as well.

Goods Account

(million dollars)

	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Goods account (trade balance)	5,073	21,143	26,204	39,427	31,114	50.5	-21.1
Exports	43,835	64,525	76,190	97,667	101,289	28.2	3.7
Imports	38,762	43,381	49,987	58,240	70,175	16.5	20.5
Non-oil goods account (trade balance)	-29,399	-30,555	-32,307	-38,830	-47,690	20.2	22.8
Exports	6,386	8,734	11,525	13,162	14,670	14.2	11.5
Imports	35,785	39,289	43,832	51,992	62,360	18.6	19.9

Figure 11.6. Export-import ratio**Exports**

Total exports grew by 3.7 percent to \$101.3 billion in 1387, compared with the corresponding figure of the year before. Moreover, value of exports of crude oil, oil products, natural gas, and condensates reached \$86.6 billion, up by 2.5 percent compared with

1386, mainly due to the growth in the exports of gas and oil products. Non-oil exports rose 11.5 percent to almost \$14.7 billion.

The 3.7 percent rise in exports coincided with the sharp fall in the sale price of most exportable goods in the second half of 1387. Despite the rise in goods exports in this year, ratio of exports to GDP declined by almost 2.9 percentage points to 28.9 percent.

Imports

In 1387, imports (fob) rose 20.5 percent to over \$70 billion, compared with the corresponding figure of 1386. Meanwhile, ratio of goods import to GDP edged up to almost 20 percent. In this year, value of imports of natural gas and oil products (gasoline and gas oil) reached \$7.8 billion, up by 25.1 percent; therefore, oil products imports were about 9.0 percent of total oil sector exports.

Exports

(million dollars)

	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Exports of goods	43,835	64,525	76,190	97,667	101,289	28.2	3.7
Oil exports¹	37,448	55,791	64,665	84,505	86,619	30.7	2.5
Customs ²	519	1,044	1,339	1,892	3,140	41.3	66.0
Non-oil exports	6,386	8,734	11,525	13,162	14,670	14.2	11.5

¹ Includes 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 Includes 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.

Selected Indicators of Exports (percent)

	1383	1384	1385	1386	1387
Ratio of exports to GDP	26.0	31.8	31.5	31.8	28.9
Ratio of non-oil exports to total exports	14.6	13.5	15.1	13.5	14.5
Exports growth	29.0	47.2	18.1	28.2	3.7
Oil exports growth	31.8	49.0	15.9	30.7	2.5
Non-oil exports growth	14.4	36.8	32.0	14.2	11.5

Imports (million dollars)

	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Total	38,762	43,381	49,987	58,240	70,175	16.5	20.5
Gas and oil products ¹	2,976	4,093	6,155	6,248	7,815	1.5	25.1
Other goods	35,785	39,289	43,832	51,992	62,360	18.6	19.9

¹ Includes 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).

Box 4- Adjustments of Goods Account (Imports)

According to Balance of Payments Manual, the value of exports and imports is registered at fob prices, and services received for transportation and insurance of goods appear under services account. However, the value of imports through Customs is registered at cif prices. Therefore, to adjust merchandise imports figures from cif to fob, first insurance and transportation costs of imported goods are estimated and deducted from cif value of imports (customs) of goods to arrive at fob valuation. Then, regarding the concept of economic territory¹, and for the full coverage of imports data, non-customs imports (including imports through free

zones, smuggled imports, imports of ships and oil tankers, imports of gas and oil products not mentioned in customs, and imports of electricity from neighboring countries) are added to the fob price to calculate total value of imports. Among the major adjustments of this account was estimation of goods smuggled into the country.

¹ An economic territory refers to the geographical territory under the control of central government (air, land, sea); embassies, consulates, military bases, scientific centers, information and migration agencies, etc.; and free zones, customs warehouses and trade centers abroad which are controlled by the Customs.

Selected Indicators of Imports (percent)

	1383	1384	1385	1386	1387
Ratio of imports to GDP	23.0	21.4	20.7	18.9	20.0
Share of imports through Customs in total imports	91.3	90.5	83.5	83.2	79.9
Share of imports of natural gas and oil products in total imports	7.7	9.4	12.3	10.7	11.1
Annual growth of imports	28.6	11.9	15.2	16.5	20.5
Oil import-export ratio	7.9	7.3	9.5	7.4	9.0

Services Account

Based on the relevant data, \$7.8 billion services were exported by Iranian suppliers to non-residents. On the other hand, residents spent \$17.7 billion for receipt of services rendered by non-resident individuals and companies. In 1387, exports and imports of services, in terms of value, rose 12.2 and 15.6 percent, respectively, compared with the previous year. Services account deficit reached roughly \$10 billion, up by 18.3 percent compared with 1386. Moreover, share of services in international trade rose slightly to 13 percent.

In the review year, "transportation", "travel", and "construction services" had the

highest shares in exports of services by respectively 49.5, 22.3, and 19.2 percent, constituting 91.0 percent of total exports of services. Moreover, "travel", "transportation", and "construction services (technical and engineering)" had the highest shares in the imports of services by 42.6, 23.7, and 17.2 percent, respectively, accounting for almost 84.0 percent of total imports of services.

Income Account

The rising trend of income account surplus which started in 1385, continued in 1387 and reached \$1.3 billion, up by 40 percent. This was due to rise in revenues derived

Box 5- Services Account in BPM5

The value of exports and imports of services is registered in services account, comprising transportation; travel; communication services; construction services; insurance services; financial services; computer and information services; royalties

and license fees; other business services; personal, cultural, and recreational services; and government services. This classification of services sector account is similar to that of WTO.

Selected Indicators of Services

(percent)

	1383	1384	1385	1386	1387
Ratio of services account deficit to GDP	-3.4	-2.9	-2.6	-2.7	-2.8
Share of services in Iran's international trade	15.0	12.8	12.2	12.5	13.0
Annual growth of services account deficit	2.6	2.4	6.4	35.7	18.3
Annual growth of services exports	14.4	12.6	13.4	22.2	12.2
Annual growth of services imports	7.5	6.9	9.6	29.3	15.6

Composition of Services Exports

(percent)

	1383	1384	1385	1386	1387
Transportation	47.4	46.5	51.9	48.0	49.5
Travel	17.7	15.8	21.5	24.2	22.3
Construction services (technical and engineering)	27.3	29.5	17.6	19.1	19.2
Other services	7.6	8.1	9.1	8.7	9.0
Total	100.0	100.0	100.0	100.0	100.0

Composition of Services Imports (percent)

	1383	1384	1385	1386	1387
Transportation	18.6	21.4	24.8	24.1	23.7
Travel	37.9	34.3	39.4	44.3	42.6
Construction services (technical and engineering)	27.0	27.3	19.1	16.1	17.2
Other services	16.4	16.9	16.7	15.5	16.4
Total	100.0	100.0	100.0	100.0	100.0

from foreign assets and fall in the interest on external debt.

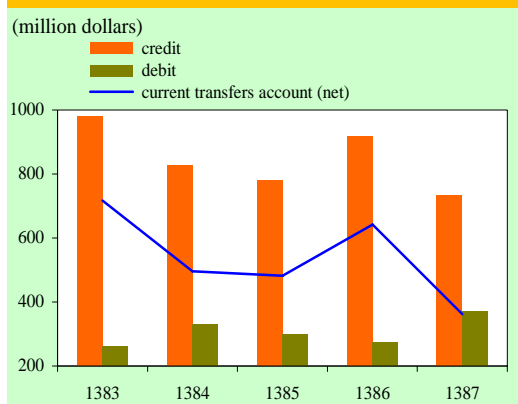
Data on investment income (including earnings from foreign direct investment, principal and profit of receivables from and payables for investment on securities, and foreign debt instruments) and compensation of employees (comprising migrant workers' wage, salary and fringe benefits) appear under income account.

Current Transfers Account

Current transfers include government transfers (typically within the framework of current international cooperation between governments and the United Nations), payment of current taxes related to income, wealth, and other transfers such as remittances of non-resident workers, gifts for non-residents, and commission for non-life insurance claims.

In 1387, the surplus of current transfers account declined by almost 43.6 percent to \$362 million. This was due to 20 percent decrease in the credit side and 35 percent increase in the debit side.

Figure 11.7. Current transfers account



Capital and Financial Account

The capital and financial account has two major components: the capital account and the financial account. The capital and financial account, owing to the rise in assets and claims of residents, as well as higher repayment of external debt in light of sharp decline of fresh money, ran a deficit in recent years. The capital and financial account deficit declined by 33.7 percent to approximately \$19.1 billion, compared with previous year.

Income Account (million dollars)

	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Income account	-305	-407	111	954	1,335	▢	40.0
Credit	1,251	1,333	2,109	3,164	3,270	50.0	3.3
Compensation of employees, including border, seasonal workers	509	427	481	561	558	16.6	-0.6
Investment income	743	906	1,628	2,603	2,712	59.9	4.2
Debit	1,556	1,740	1,998	2,211	1,935	10.6	-12.5
Compensation of employees, including border, seasonal workers	251	349	267	276	324	3.6	17.1
Investment expenditure	1,305	1,391	1,731	1,934	1,611	11.7	-16.7

Capital and Financial Account						(million dollars)	
	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Capital and financial account	-464	-14,731	-17,695	-28,851	-19,135	63.0	-33.7
Capital account	-88	-117	-185	-249	-383	34.7	53.4
Financial account	-376	-14,614	-17,510	-28,601	-18,753	63.3	-34.4

Capital Account

All capital transfers like the write-offs of external debt, investment assistance, capital transfer of migrants (non-residents), transactions on invisible assets (i.e., trademarks, copyrights, and the like), and transactions on land for foreign embassies and foreign representative offices are registered in capital account.

The valuation of capital account transactions is difficult and almost all countries around the world have difficulties in the assessment and valuation of capital account items. However, the valuation difference of some of these items is not that large compared with other items of capital and financial account. The compilation of capital account items of BOP in Iran is as difficult as it is in other parts of the world.

The Iranian capital account ran \$383 million deficit in 1387, up by 53.4 percent compared with the year before.

Financial Account

The financial account covers all transactions associated with changes of ownership in the foreign financial assets and liabilities of an economy. Such changes include the creation and liquidation of claims on, or by, the rest of the world. In 1387, financial account deficit declined by 34.4 percent to \$18.7 billion compared with the respective figure of the preceding year. This was due to reduction in reserve assets by 46.0 percent, and decrease in net other investments and portfolio investment by 20.8 and 21.0 percent,

respectively, in line with the rise in net foreign direct investment.

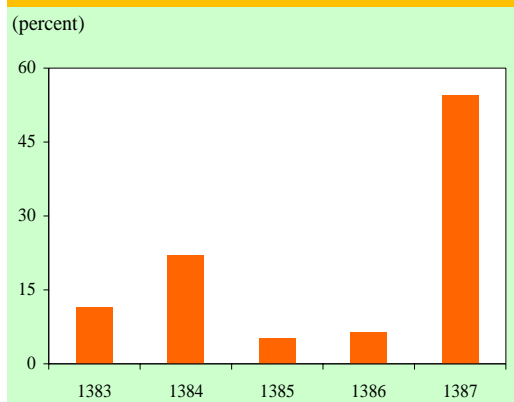
Foreign Direct Investment (FDI)

Direct investment is divided into direct investment abroad and foreign investment in the reporting economy. Thus, data on foreign direct investment include flows of capital to and from the reporting economy. In 1387, net foreign direct investment worth \$193 million exited the country, the detail of which is given below:

FDI Inflows

In 1387, FDI inflows reached \$1.5 billion, down by roughly 4.0 percent compared with the year before. Of this amount, 66.0 percent was related to investments in oil and gas projects within the framework of buy-back contracts, and 30.0 percent to investments under Foreign Investment Promotion and Protection Act.

Figure 11.8. Ratio of capital inflows to approved investments



Financial Account						(million dollars)	
	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Financial account	-376	-14,614	-17,510	-28,601	-18,753	63.3	-34.4
Foreign direct investment (net)	1,453	1,283	91	-299	-193	0	-35.6
Portfolio investment (net)	-61	-69	-112	-1,241	-981	▣	-21.0
Other investments (net)	4,877	-1,262	-6,099	-11,807	-9,351	93.6	-20.8
Reserve assets	-6,644	-14,567	-11,389	-15,254	-8,229	33.9	-46.1

Foreign Investment Inflows in the Framework of Foreign Direct Investment						(million dollars)	
	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Foreign direct investment	2,978	3,189	1,867	1,552	1,491	-16.8	-4.0
Under Foreign Investment Promotion and Protection Act ¹	308	933	530	785	448	48.1	-42.9
Buy-back oil and gas contracts ¹	2,557	2,216	1,304	747	987	-42.7	32.2
Others ²	113	40	33	21	56	-36.3	165.9

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

² Free Trade Zones Organizations

Foreign Investments under Foreign Investment Promotion and Protection Act						(million dollars)	
	1383	1384	1385	1386	1387	Percentage change	
						1386	1387
Approved investments	2,703	4,239	10,241	12,091	822	18.0	-93.0
Realized investments till end-1387 ¹	204	1,267	240	320	31	33.0	-90.0
Capital inflows	308	933	530	785	448	48.1	-42.9

¹ Breakdown of realized investment till end-1387 by the date of approval

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. In 1387, largely due to repurchase of the second phase of Eurobonds, this account posted \$981 million deficit.

Other Investments

All financial transactions not included under "direct investment", "portfolio investment", and "reserve assets", are mentioned under "other investments". Loans, credit

facilities, and foreign exchange deposits are the key components of this account, which ran \$9.4 billion deficit in the review year. Of this amount, 52.4 percent was owing to rise in foreign claims, and 47.6 percent to reduction of external debt.

External Debt

Total external debt (actual and contingent obligations) reached \$45,671 million, down by 18.7 percent at end-1387. The rise in the share of contingent obligations in total continued in 1387, reaching almost 53.0 percent

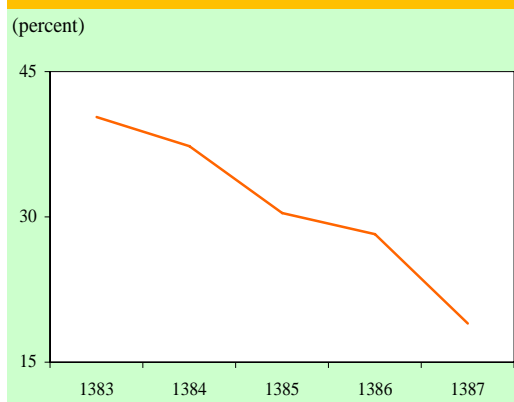
compared with the corresponding figure of the previous year (49.0 percent).

The amount of actual obligations (external debt) decreased by 24.9 percent to \$21.5 billion. This was largely owing to rise in the parity of US dollar vis-à-vis euro in the final months of 1387, repurchase of the second phase of Eurobonds issued in 1381, and further limitations on foreign financing.

All indicators of external debt sustainability improved in 1387, compared with the preceding year. Share of short-term debt in the total external debt based on original maturity declined from 34.5 percent at end-1386 to 30.7 percent in 1387 year-end. "Ratio of external debt to GDP" declined from 9.3 percent in 1386 to 6.1 percent in the review year. "Ratio of external debt to exports of goods and services" decreased from 27.4 percent in the preceding year to 19.7 percent in 1387. Moreover, "ratio of repayment of principal and profit of external debt to exports of goods and services" (debt service ratio) reached 19.4 percent in 1387, down from 22.1 percent in the year before.

Another indicator of external debt sustainability is the ratio of "external debt to central bank foreign assets". This ratio, due to more than \$8.2 billion rise in CBI foreign assets as a result of current account transactions and a reduction in external debt in 1387, declined by almost 7.5 percentage points.

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



	External Debt				(million dollars)	
	1384	1385	1386	1387	Percentage change	
					1386	1387
External debt	24,264	23,514	28,647	21,502	21.8	-24.9
Long-term	13,578	14,414	18,756	14,903	30.1	-20.5
Short-term	10,686	9,100	9,891	6,599	8.7	-33.3
Contingent obligations	17,587	21,825	27,537	24,169	26.2	-12.2
Total	41,851	45,339	56,184	45,671	23.9	-18.7

Maturity	External Debt Profile (at end-1387)					(million dollars)	
	1388	1389	1390	1391	1392 onwards	Total	
Amount	9,656	2,569	2,138	1,852	5,287	21,502	
Percent	44.9	11.9	9.9	8.6	24.6	100.0	

Chapter 11 BALANCE OF PAYMENTS

	Indicators of External Debt Sustainability					(percent)
	1383	1384	1385	1386	1387	
Ratio of external debt to GDP	13.7	12.0	9.7	9.3	6.1	
Debt service ratio	28.9	28.6	24.5	22.1	19.4	
Share of short-term debt in the total external debt (based on original maturity)	44.4	44.0	38.7	34.5	30.7	
Ratio of external debt to exports of goods and services	47.8	34.9	28.7	27.4	19.7	