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Is Iran's Currency Crisis Evidence That Sanctions Are Working?

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The regime is relatively sheltered from the current crisis, so Washington should be careful not to count on the sanctions alone to resolve the nuclear impasse.

Both the Obama administration and Iran's President Ahmadinejad have blamed the recent dramatic fall in value of Iran's currency on international sanctions. It is a convenient explanation for both -- for the White House, it suggests that U.S. strategy towards Iran is working; for Ahmadinejad, it deflects responsibility away from his own policy decisions and toward an external scapegoat.

But as my colleague [Patrick Clawson explains](#), sanctions are only partly to blame for Iran's economic travails. The currency crisis and associated inflationary spiral has its origins in the Ahmadinejad government's mismanaged subsidy reform initiative. Sanctions have indeed exacerbated the problem, both by raising the cost to foreign firms of doing business with Iran and reducing the regime's foreign exchange earnings. The increasing threat of war has also played a role, deepening Iranians' worries about economic stability and increasing their inflationary expectations, and thus leading them to dump rials and seek safe haven in dollars and other hard currency to protect their savings.

However, the regime's maladroit domestic response to the sanctions (for example, its decision to set up "foreign exchange centers," which sparked the current run on dollars) and its loose monetary and fiscal policies have made matters far worse. This is arguably the result of years of economic mismanagement in Iran, particularly under Ahmadinejad, who has subverted what little independence the Central Bank previously possessed and drained it of economic expertise.

Ironically, however, the Iranian regime is relatively sheltered from the present crisis. Although sanctions have reduced its oil exports, they remain high at 1.2 to 1.5 million

barrels per day, meaning that the regime's foreign exchange income is considerable, even if diminished. What's more, it has limited external liabilities, and in any event its oil income is dollar-denominated, protecting it from exchange rate risk. This means that as the rial plunges, the regime's fixed rial-denominated payments become effectively cheaper. Meanwhile, Iran's rampant corruption likely shields elites and their families from the worst of the country's economic woes, such as unemployment and increasing scarcity.

As a result, Iran's economic crisis is unlikely to directly cause the regime to change its nuclear calculus. Instead, the sanctions implicitly depend on domestic Iranian outcry -- or the regime's worries of unrest -- to cause the regime to make the desired strategic shift. However, as bad as Iran's economy is, there are few signs of major unrest, and fewer signs still that the regime is responsive to the concerns of the Iranian people (although this will further diminish Ahmadinejad's standing). This is, after all, the regime that showed no compunction in brutally putting down protests in 2009.

By implication, the United States and our allies should be careful not to count on the current sanctions to resolve the nuclear crisis by themselves. Nor should we abandon our focus on targeted sanctions in favor of a return to broad sanctions, which rarely succeed in inducing policy changes in autocratic regimes. Rather than hoping that giving current sanctions "time to work" will force Iran back to the negotiating table, the United States and our allies should add further pressure to the regime and the elites who comprise it, including through additional targeted economic sanctions, diplomatic isolation, bolstering the credibility of our military threat to the regime, and support for the Iranian opposition.

On their own, sanctions are unlikely to work. Instead, for the United States to succeed in its aims, sanctions must be just one part of a broad, coordinated, and disciplined policy which brings all policy tools to bear on the goal of preventing Iran from acquiring nuclear weapons.

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