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Iran's Next Budget Assumes No Nuclear Deal

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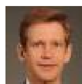

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Brief Analysis

The government seems to believe the economy will grow significantly even without sanctions relief or increased oil revenue.

On December 12, President Ebrahim Raisi submitted his proposed budget to parliament for the Iranian year 2022/23, which begins in March. According to the initial numbers, Tehran appears to assume that nothing will emerge from the nuclear talks in Vienna, and that the country will not be any more successful than it has been at evading U.S. sanctions.

For instance, the 2021/22 budget assumed oil exports of 2.3 million barrels per day, but the proposed new budget assumes just 1.2 million, a projection that is at best equal to—and more likely less than—Iran's recent estimated exports. That decrease is partly offset by the new budget's assumed 20% rise in the dollar price of oil, and by plans to fully phase out the official rial exchange rate of IRR 42,000 per dollar in favor of the market rate of about IRR 300,000 per dollar. Despite such modest oil revenue, the government is predicting that national income will grow at 8% in real terms, presumably because of recovery from the COVID-19 pandemic. In other words, Raisi's team appears to believe Iran will do just fine without sanctions relief. Whether or not this optimism is misplaced, it suggests Tehran sees little need for a nuclear deal.

The growth assumption is particularly striking given the budget's projected 62% increase in tax revenues, well above the IMF's estimated 28% inflation rate for next year. Normally, Iranian budgets make overly optimistic assumptions about collecting greater revenue from existing taxes, but Raisi is proposing steep increases, which economists tend to view as a measure that depresses growth in national income. Tax revenue from foreign travel is projected to rise fourteen-fold, implying much higher rates, while the tax on property and vehicles above certain value thresholds will be 4% per year—at least for those citizens without sufficient political connections to avoid it.

Indeed, the budget is poised to hurt the middle class in the name of national self-reliance. Raisi does not care much about this slice of society, which was the core constituency of former president Hassan Rouhani. The budget will not help the poorer classes much either, if at all: inflation will outpace the proposed spending increases, and lower income groups will be hit by some of the new taxes (e.g. revenue from cigarette sales is projected to double).

On some points, Raisi's proposal does have sound macroeconomic foundations. Unlike past budgets that claimed to eliminate deficits by predicting unrealistic oil prices, the next budget assumes $60 per barrel for exports—a quite cautious projection even if one assumes that Iran must continue offering discounts and paying money-handling fees due to continued U.S. sanctions.

Phasing out the official exchange rate is a sound idea as well, since the gap between the official and market rates has been a source of corrupt income for individuals with access to foreign exchange options. Iranian press reports suggest that a large portion of the $8 billion allocated at the official rate for imports of "essential" goods has not been used for that purpose. Raisi's government is replacing this system with a cash payment to all families of $3-4 per month, at a total cost of $3.4 billion (IRR 1,000 trillion). Given its longstanding cash payment system, Iran can easily raise monthly payouts, which will benefit families more efficiently than holding down the cost of certain essential items—an approach that has hurt domestic producers of rice and other goods.

Another sound step is the proposed reduction in bond sales to $3.4 billion, or 45% below the ridiculous figure in the 2021/22 budget. And raising the retirement age for most people—by two years to 65—is highly appropriate given Iran's rapidly aging population and decreasing number of people entering the labor market (the country's "birth dearth" cohort is now in their early twenties).

Yet the proposed budget also contains some of the usual subterfuges and eyebrow-raising changes that make it less than transparent. For one, it retains the traditional optimistic assumptions about raising money from privatization. Admittedly, various planned steps to prop up the stock market may boost the government's take from such sales, but perhaps not to the predicted level. Elsewhere, the allocation for the president's office has been increased to a whopping 2.7 times the previous amount.

More important, the semiofficial Fars News Agency reports that the budget allocates $5.1 billion to the Islamic Revolutionary Guard Corps (IRGC) from oil sales revenue, but this does not appear to be included in the actual $50 billion (IRR 15,052 trillion) government budget. The budget assumes $12.7 billion (IRR 3,818 trillion) in oil revenue, but the projected 1.2 million barrels per day exported at $60 per barrel would yield $26.3 billion. A big chunk of these earnings would go to the National Iranian Oil Company to pay for production and capital costs, but that still leaves a lot more than what is allocated to the budget. Some of this extra money is earmarked for spending at the province level, but most of it is allotted to "stabilization" and "reserve" funds, which the government usually establishes for expenditures that it pretends have something to do with investment and development—presumably the excuse for the **allocation to the IRGC (https://www.washingtoninstitute.org/policy-analysis/irans-ballistic-missile-arsenal-still-growing-size-reach-and-accuracy)** .

The Majlis is sure to make changes to the budget, some of them likely substantial. Yet Raisi's proposal is a clear indication of his thinking about Iran's economic situation—namely, that it is in fine shape even without renewing the nuclear deal. That fits with his long-held view that Iran can do well without the West, and the corollary view that European banks and the U.S. government will not allow his country to return to the global financial system.

The implications for U.S. policymakers are clear: the Raisi government sees no economic urgency to making substantial nuclear concessions, nor does it fear the punitive economic measures that the Biden administration has threatened to apply in the absence of a deal. Perhaps Washington can shake this confidence—for instance, by finding effective measures to reduce the Chinese oil purchases that make up the bulk of Iran's exports. Yet this will be no

easy task given Raisi's strong ideological conviction that self-reliance and trade with neighbors are more fruitful than chasing after normalization with the West.

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