Iran's Quandary: Economic Reforms and the "Structural Trap"

PARVIN ALIZADEH

Associate Professor of Economics
Denison University

In early 2002, the Iranian government began instituting a number of market-oriented reforms, including exchange rate unification, trade reforms, ratification of the law on foreign investment, tax reforms, and the licensing of three private banks.[1] In recent years Iran has applied for membership in the World Trade Organization (WTO). These steps are aimed at rectifying distortion and structural imbalances, which have prevailed since the Islamic revolution of 1979, and mark the first concerted effort by Tehran to shift from autarkic and isolationist economic policies of the post-revolution period to a growth-oriented approach.

Here I provide a qualitative assessment of the current economic reforms with respect to their urgency, context, content, and effectiveness. What is the "structural trap" preventing Iran from approaching its full potential in terms of efficiency and employment generation? Are current reforms facilitating the transfer of resources from low-return investments to high-yield ones? What factors and circumstances slow down the pace and effectiveness of the current reforms?

The paper consists of four sections. The first section examines the exigency of the current reforms and provides an analysis of the relative performance of the economy since 1980. Then second section highlights the structural rigidities of the economy, most notably the dominance of inefficient state owned enterprises, and the role of revolutionary organizations and labor market regulations. The last section addresses the impact and effectiveness of recent reforms.

Exigency of Belated Economic Reforms

The urgency of implementing structural reforms is articulated well by the IMF, which recently sent a team to Iran to advise the government on policy issues:

> Iran has now reached the point where a clear choice must be made between a strategy that continues to rely primarily on subsidies and government intervention...with long-term negative effects on macroeconomic stability and growth, and one aimed at sustaining long-term growth and employment creation through greater efficiency and private sector-led economic development.[2]

The current reforms, considered the first generation of structural adjustment reforms (FGSAR), are focused on greater trade and exchange rate liberalization, more openness to foreign capital, and an overall shift toward the use of market mechanisms.[3] This set of reforms—originally formulated by the World Bank and the IMF in the early 1980s—is designed to provide a market-friendly environment conducive to the development of the private sector, development of non-oil exports, removal of inefficiencies and a sharp reduction in the state's role in the allocation and distribution of resources.

It is worth noting that FGSAR have been implemented in nearly all developing countries since mid 1980s with varying degrees of success.[4] In fact, countries in South East Asia, Latin America, and several countries in North Africa and the Middle East have either completed or are in the midst of their second generation of structural adjustment reforms (SGSAR).[5]

The reasons for Iran's belated structural reform have been debated elsewhere and will not be the concern of this analysis.[6] Implementation of the recent economic reforms in Iran, however, is an inevitable response to structural rigidities and imbalances that have paralysed the economy for more than two decades.

Economic performance in comparative perspective

Iran's economy in the 1980s and 1990s experienced a marked deterioration both in absolute terms as well as relative to other countries in the region. For instance a study by Karshenas and Hakimian (2000) indicates that between 1960 and 1975, GDP per capita in Iran almost doubled. Iran was one of the fastest growing developing countries over that period, similar to South Korea and Turkey. By 1990, however, GDP per capita in Iran had declined to about 60 percent of its level in 1975, in contrast to Korea and Turkey that witnessed an improvement in their living standards.[7]

Table 1: Iran and Peer Countries

	2001 Total Population (millions)	1995-01 Life expectancy (years)	1995-01 Illiteracy	Percent Change in Inflation Rate			
				1981	1991	2000	2001
Iran	65.1	71	15	21.4	15.8	12.6	11.7
Egypt	65.2	67	44	-	14.7	2.8	2.4
Turkey	64.3	74	15	-	63.0	83.7	63.5
Morocco	29.2	67	50	12.5	8.0	1.9	2.0
Tunisia	9.7	72	28	11.4	8.2	2.9	1.9

	2001 GNI per capita ($U.S.)	Average Growth of GDP per capita (%)			
		1981-1991	1991-2001	2000	2001
Iran	1,670	-1.3	1.7	3.9	3.1
Egypt	1,530	2.4	2.7	3.1	1.6
Turkey	2,900	2.4	2.5	-7.8	4.1
Morocco	1,180	2.4	0.8	-0.8	4.8
Tunisia	2,070	0.9	3.2	3.5	3.7

Source: The World Bank online (www.worldbank.org).

A more comprehensive picture of Iran's economic performance is presented in tables 1, 2, and 3. Table 1 provides comparative data on the basic macroeconomic indicators for Iran and a number of countries in the Middle East and North Africa—including Egypt, Turkey, Morocco, and Tunisia—since 1981. Egypt and Turkey are comparable to Iran in population size, while Morocco and Tunisia are smaller. All countries in the table are classified as lower middle-income countries, although Iran used to be classified as an upper-middle income until the early 1990s.[8] Since then Iran's income per head has declined to the level of lower middle-income countries. All countries in the table with the exception of Iran, however, are well into their second generation of structural adjustment reforms.

Macroeconomic performance in Iran differs from the peer countries in three important ways. First, the growth of GDP per capita for Iran over this period is considerably lower than that of other countries in the region. In fact, Iran experienced negative GDP per capita growth during the 1980s, unlike other countries on the table. While per capita income grew in the 1990s, it nevertheless has remained below that of countries with comparable population size like Turkey and Egypt.

Table 2: Inflation and Unemployment Rates, Iran

	Consumer Price Index	Unemployment Rate
1993-94	22.2	10.0*
1994-95	35.2	-
1995-96	49.4	-
1996-97	23.2	9.1
1997-98	17.3	12.2
1998-99	18.1	14.7
1999-00	20.1	16.0
2000-01	12.6	15.8
2001-02	11.4	16.2

* belongs to 1991-92 data
Source: International Monetary Fund (2002 and 1999 reports)

Second, Iran experienced high and volatile inflation rates. Iran's inflation problem—as table 1 makes clear—is surpassed only by Turkey, which has had exceptionally high inflation. A more detailed picture of inflation in Iran is presented in table 2, which indicates over the period 1993-94 to 2001-02, inflation ranged between 49 and 11 percent. Most developed and developing countries, including Iran, have succeeded in lowering their inflation rates considerably over time.[9] Nevertheless, Iran's inflation still remains substantially above the world average. In 1998, for instance, Iran's inflation rate was double the average inflation rate in developing countries, which was 10 percent.[10]

The third imbalance in Iran's economy has been the rapidly rising unemployment rate. As table 2 shows, the unemployment has been rising in Iran since the late 1990s. While comparable data on unemployment is scant, a recent IMF study indicates "during the decade of the 1990s, job creation in Iran was slower than in many countries in the region."[11] The unemployment rate for 2002 was 16 percent for Iran compared to 7 percent for Turkey. The government's economic policies have visibly failed to create productive employment for the growing labor force, which has been expanding much faster than the growth of the employment in the 1990s.

At the micro level there is little indication that Iran has increased competitiveness in non-traditional exports. Table 3 indicates more than 90 percent of Iran's exports still consists of a primary product, of which oil alone accounts for 84 percent of total exports. In contrast, peer countries have succeeded in improving efficiency and industrial competitiveness in international markets.

Peer countries have increased the share of manufactured goods in their total exports. For instance share of manufactured exports in Turkey's total exports has increased from 23 percent in 1980 to 71 percent in 1997. Iran's economy has remained extremely oil dependent and fluctuations in oil prices exert influence on the structure of the economy (see table 4).

Table 3: Structure of Exports

Percent of Total Exports, 1997

	Primary Products	Manufactured Goods
Iran	91	9
Egypt	62	38
Turkey	25	75
Morocco	65	35
Tunisia	22	78

Source: World Development Report 1987, 2000 (Oxford University Press) and World Bank 1997.

The deterioration of economic performance in the post-revolution period has been in part induced by a number of negative external shocks. The economy not only endured the effects of disruptions due to the revolution itself but also the protracted and costly war with Iraq, the continuing economic embargo by the United States (freezing of Iranian assets), and erratic oil prices. However, the inability of the economy to adjust to external shocks not only points to the rigidity of pre-existing economic structures inherited from the Pahlavi era but also the institutional setup and policy response by the state in the post-revolution period.

The "Structural Trap" and Distributive Policies

What factors have hindered job creation and the improvement of efficiency in Iran's economy? Here I borrow the term "structural trap" from Dugger and Ubide to highlight the heart of the matter.[12] They define the term as a situation in which political and economic obstacles avert the reallocation of capital from low productivity firms to higher productivity ones. There is every indication that a "structural trap" is the main impediment to the structural transformation and the growth of the Iranian economy since 1980. There is consensus among close observers of the Iranian economy that economic development in the context of the existing inefficient state-owned production organizations and labor relations has not been conducive to efficiency and the growth of employment.[13] The presence of revolutionary organizations and the lack of a domestic or international competitive environment have further exacerbated this.

Table 4: The Structure of the Iranian Economy

	Percent of GDP at current prices				
	1997-98	1998-99	1999-00	2000-01	2001-02
Oil	14.3	8.6	14.7	17.8	15.1
Agriculture	15.0	17.4	15.0	13.6	13.4
Industry	19.6	19.1	19.1	18.9	20.1
Manufacturing	13.7	13.5	13.5	13.3	14.3
Services	51.1	54.9	51.2	49.6	51.1
	Contribution of oil (%)				
Gov't Revenue	53	35	43	67	57
Exports*	84	75	81	86	81

*Goods and Services. Iranian year begins 21 March.
Source: International Monetary Fund (2002 and 1999 reports)

It is worth remembering that the pervasive role of the state in the economy was brought about by large-scale nationalization in 1980 as well as the eight-year war with Iraq, which cemented the ascendancy of the state's role in the economy. The populist Islamic revolution of 1979 heralded an expanded role for the state to safeguard the redistributive nature of the revolution. This manifested itself in a number of ways including: large scale expropriation and reallocation of property; large scale nationalization of modern industries (which included all large-scale manufacturing industries, major mineral resources, banking, insurance, dams and large-scale irrigation networks, radio and television, and other industries in the communication and transportation sectors), and the rise of revolutionary organizations (*bonyads*) to safeguard and promote the improvement of living standards of the low-income and rural populations.[14]

The next section focuses on state-owned enterprises (SOEs), although revolutionary organizations or *bonyads* have been also a very important in implementing redistribution policies. *bonyads* are parastatal institutions, which were created after the revolution, to safeguard the ideological orientation of the Islamic state.[15] *bonyads* are the beneficiaries of assets seized from the former royal family and other exiled elites or assets nationalized after the revolution. These organizations that operate in the name of the dispossessed masses have developed into conglomerates and control a very substantial section of productive activities and employment in agriculture, industry and services. *bonyads* that are largely unaccountable to the government have been privileged to obtain implicit and explicit subsidies from the government, though this is changing with the current reforms. However there has been much discussion about the operation of *bonyads* and will not be further elaborated upon here.[16]

Table 5: Financial Losses of Selected State-Owned Enterprises 1994-1999

	Percent of Revenue	Percent of GDP
Total Revenue	100.00	5.4
Total Losses	-51.0	-2.7
	Financial Losses	
Capital Transfer from Budget	24.8	-1.3
Other Sources	26.2	-1.4

Source: International Monetary Fund (2002 and 1999 reports).

The Role of State-owned Enterprises (SOEs)

There is growing concern about the performance of SOEs in developing countries. SOEs are one of the main sources of government deficit because of their growing claims on government budgets. Public enterprise deficit has been identified as a key contributor to excessive credit creation, leading to monetary expansion and price inflation.[17] There is also much concern at the micro level with regard to efficiency and profitability.

The crux of the matter is not an unequivocal negation of SOEs or any other forms of intervention. The impressive success of the East Asian NICs (South Korea, Taiwan, Singapore) highlights the positive role of the SOEs and the state intervention in promoting capitalist development. The SOEs in Korea and Taiwan produced a number of intermediate inputs including steel for the use of private producers downstream as well as for the sale in the international markets. For instance POSCO, Korea's state owned integrated steel mill, which was set up in the 1970s and benefited from generous government subsidies, became one of the world's most efficient producer through time.[18]

However a very important characteristic of Korean and Taiwanese states has been their ability to monitor economic performance by imposing discipline on firms, which were the recipients of subsidies and other assistance from the state. This principle of reciprocity, that is labeled as a "reciprocal control mechanism" by Amsden, allow the state to influence the behavior of targeted industries by subjecting them to national policy goals as regard to their local content, export target, technical competence and prices in domestic and export markets.[19]

The developmental role of the state in these countries, however, can hardly be generalized.[20] The state-centric development of Korea, Taiwan and Singapore is in sharp contrast to the "government failure" in several other developing countries, including Iran.

Performance of SOEs in Iran

Since 1980 the Iranian economy has been characterized by prevalence of highly subsidized, inefficient and overstaffed state owned enterprises that account for a major share of the economy's output. SOEs in the industrial sector alone account for 70 percent of the sector's value added, which is equivalent to 15 per cent of GDP.[21] The dearth of information about SOEs makes it difficult to have a clear picture of their financial situation. Available data suggests that a large number of SOEs are loss making and highly dependent on substantial government subsidies. The fiscal cost of SOEs is well reflected in table 5 which shows—despite being the receiver of substantial subsidies, both implicit and explicit—SOEs are loss making. From 1994 to 1999 the financial losses of selected state enterprises amounted to 51 per cent of their total revenue, which is equivalent to 2.7 percent of GDP over the period. These losses were financed in part through budgetary transfers and in part through bank lending.

It worth noting that subsidization of most SOEs in Iran cannot be rationalized on "infant industry" grounds. Most of these SOEs, particularly in the manufacturing sector, used to be privately owned and profit making firms before the revolution. For instance, several firms in the automotive industry have been operating since mid 1960s. There is hardly any economic logic for the provision of subsidies to loss making firms, which are into the "senility phase" of their life cycle.

Prior to the recent reforms, SOEs were also shielded from domestic and international competition. On one hand, SOEs inhibited the growth of the private sector with their access to subsidies, which is subject to hard budget constrains. On the other hand SOEs operated in a highly protected domestic market, which until very recently, was sheltered by tariff and particularly non-tariff barriers.

The prolongation of SOEs in Iran has been made possible by the absence of hard budget constrains, the lack of competition, and the absence of monitoring and performance standards by the state. There is little resemblance between the operation of the Iranian SOEs and the operation of SOEs in Korea and Taiwan. There has been little incentive for SOEs to restructure and to reduce their costs. Furthermore most SOEs operate with excess labor and obsolete technologies.[22]

The dominance of SOEs has affected the performance of the economy in three main respects. First, the SOEs had an inflationary impact on the economy. Government budgetary transfer and other forms of subsidies that were granted to SOEs as well as to the revolutionary organizations, *bonyads*, are one of the main reasons for budget deficit, immoderate monetary expansion and subsequent inflationary pressure in the economy since 1980. This is well stated by Pesaran: "In the final analysis the main cause of excessive monetary expansion and inflation have to be found in the government unwillingness to oppose the credit demand of politically powerful groups (both inside and outside the government)."[23]

The second negative impact of SOEs on the economy arises from their inability to create jobs for the rapidly growing labor force. During the 1990s about 70 percent of the employment creation was in the private sector, despite the dominant contribution of the SOEs in the production of goods and services.[24]

Above all, operation of SOEs is typified by the lack of fiscal transparency, which has been one of the main factors contributing to pervasive corruption. In September 2002 the financial operation of Iranian Radio and Television, which has been the largest receiver of budgetary transfer form the government to cover its losses, has come under the parliament's scrutiny.[25] It appears that there has been substantial disparity between the actual revenue and the declared revenue of the company.

Labor market regulations

Another aspect of government redistribution policies, which exacerbated the misallocation of resources, was—and remains—government regulation of the labor market. The Labor Law introduced in the 1980s is highly restrictive and entails rigidities in hiring and firing in both public and the private sectors. The present labor law, which is highly protective of incumbent employees, has discouraged growth of employment. There are no independent labor organizations to deal with labor regulation and wage compensation. Nevertheless, government regulations make it extremely costly to fire workers, even in the private sector.

Recent Economic Reforms

The overall objectives of current reforms are to reduce the system of subsidies and protection, to reduce the administrative red tape, to increase the role of the private sector and to depart from the redistribution policies of the earlier period.

Let us start with the unification of the exchange rate, which is the focal point of the reform program, formulated in consultation with the IMF. Multiple exchange rates were at the heart of government implicit subsidies to SOEs and revolutionary foundations for more than two decades.

Although serious attempts at exchange rate unification began with the introduction of Third Five Years Development Plan (TFYDP) in 2000, it became effective in March 2002.[26] The government has adopted a market-based floating exchange rate and relinquished the multiple exchange rate system (MERS). MERS prevailed from the start of the war with Iraq in 1980 until March 2002, except for a short period of unification in 1993.[27] By March 2000 there were three officially recognized exchange rates applying to different categories of transactions.[28] For instance, imports were subject to different exchange rates depending on the type of import and its users. The official floating rate of 1750 rials (RLs) per U.S. dollar applied to import of essential goods, a fixed or "export" rate of RLs 3000 per U.S. dollar applied to capital goods imports of public enterprises and a variable Tehran stock exchange (TSE) rate of RLs 8180 per U.S. dollar applied to other imports. In addition, there was an active informal market that was reflected in a parallel exchange rate with a significant mark-up above the TSE rate. The MERS provided implicit foreign exchange subsidies to those groups who had privileged access to official exchange rates, particularly the first two rates that were considerably below the TSE and the informal market rates.

MERS generated massive implicit subsidies for state owned enterprises and big importers of basic commodities, and several revolutionary foundations *(bonyads*), which are also among importers of essential goods and capital goods for their productive activities. There was anecdotal evidence, of the sales of foreign exchange in the informal markets by revolutionary foundations. MERS was one of the main channels for rent-seeking activities by diverting the resources into non-productive activities.[29] MERS also strengthened the political and economic position of the aforementioned groups.

Hence, exchange rate unification is an important step toward rectifying the system of subsidies. Nevertheless, for unification to succeed the government has assumed the entire cost of the exchange rate difference arising from the unification on imports of essential goods and capital imports. In other words, the previously implicit foreign exchange subsidies associated with these imports have been now made explicit in the 2002-03 budget.[30] This policy increases the fiscal transparency and paves the way for reform in the subsidy system. Making implicit foreign exchange subsidies explicit can also provide a system of checks and balances over the pervasive corruption arising from the lack of fiscal transparency. On the down side, however, exchange rate unification imposes substantial fiscal costs, around 3 to 6 percent of GDP.

The next important reform is trade liberalization. This is designed to reduce protection of domestic industry and shift resources from inefficient production units into more efficient ones. Iran is still at a very early phase of trade liberalization, similar to that of Turkey in the early 1980s. Non-tariff barriers have been replaced with tariffs, which is a less distorted form of protection. Furthermore, tariff rates (i.e. custom duties and commercial benefit tax) as well as other charges on imports were reduced in most cases, resulting in a combined average tariff rate of 27 percent for many commodities, though the tariff structure is not yet rationalized. Furthermore, import-licensing requirements have been streamlined. This has reduced bureaucratic procedures and red tape. Recent reforms also include simplification of corporate and income taxs, provision of incentives for foreign investors, and licensing of three private banks.

A realistic exchange rate and trade liberalization are the first steps toward removing the "structural trap" in Iran.

The Pace of Reform and the "Structural Trap"

Can the current reforms produce efficient resource allocation and provide a suitable environment for the development of a dynamic private sector? While the direction of current reforms is clear, the pace and sequence of reforms are far from satisfactory. I argue here that the presence of a realistic exchange rate combined with trade liberalization is the first step toward removing the "structural trap" in Iran. Nevertheless the scope for successful economic reforms depends on complementary reforms not only in financial and labor markets, but also in the political environment and institutions.

The Third Five Years Development Plan intends to reform the SOEs by removing subsidies, opening SOEs to competition, and, above all, by privatization of SOEs. The current reforms also intend to create a suitable environment for the development of the private sector. Effective reform of the

SOEs through privatization will take time to materialize. Although the legislative and regulatory environment governing privatization has been established, the progress of privatization has been very limited. Privatization has been confined to sales of government equity share to the private investors and *bonyads,* without the transfer of majority control of the private sector. Progress has been slow despite the fact that privatization has been underway since mid-1990.

The gradual advancement of privatization, nonetheless, is not confined to Iran and has been one of the impediments to removal of the "structural trap" in several developing countries and the transitional countries of Eastern Europe and Central Asia.[31] The SOEs are politicized institutions in which both workers and managers strive to prolong subsidies and perpetuate of redistribution policies. Large-scale privatization will increase unemployment and is not politically feasible in the short-term. Moreover, privatization in Iran has been also hampered by political uncertainty, which will be discussed below. Hence, SOEs are going to a be burden on government resources for sometimes to come

Yet prolonging subsidies would accentuate inflationary pressure arising from the monetary and fiscal expansion, even if subsidies were reduced. This fuels macroeconomic instability by distorting prices, which harms the "credibility" of the reform process.[32]

Current reforms have had a limited impact on private sector investment in productive activities. Undoubtedly a managed floating exchange rate and trade liberalization are important steps toward a more efficient and export-oriented industrialization (assuming the government can prevent the real exchange rate from appreciating). But, as the experience of several other developing countries has shown, these reforms are not sufficient to enhance large-scale private investment.[33]

This is not to deny that private sector investment in the manufacturing industries has been expanding in the 1990s. Although there is scant data on the share of private investment in the manufacturing sector, anecdotal evidence indicates such investment is small-scale and primarily in assembly operations satisfying the growing domestic demand for consumer non-durables. Large-scale private investment in productive activities, similar to that of the pre-revolution period, is a rarity.

Complementary reforms in financial and labor markets are also crucial for the enhancement of the private investment in productive activities. Ten state-owned banks dominate Iran's financial sector, although recently three private banks were licensed. The state-owned banks have been incapable of providing financial support to the private sector. These banks, which have been satisfying the credit requirements of loss making SOEs, lack adequate regulatory and prudential regulations, and their loan portfolios, have been deteriorating over time. There is a strong possibility of non-performing loans fueling a banking crisis.

Another impediment to the development of private investment is the presence of a highly regulated labor market addressed earlier. Reform in the labor laws and deregulation of the labor market, however, are politically sensitive issues. "Populism" still plays an important part in maintaining a "revolutionary façade" of the Islamic Republic.

Above all, the main hindrance to private sector development in Iran is political instability combined with the lack of ideological clarity on property rights. Since the inception of the Islamic Republic there has been tension between the "Islamists" and the "modernists" within the regime. Despite the apparent victory of the modernist in the election of President Khatami in May 1997, the conflict between the two camps has intensified over time. The ongoing power struggle within the regime has handicapped the state—the organization that defines and enforces property rights—to create an institutional framework conducive to large-scale private investment in productive activities. For instance, the wrong "signaling devices" by the government accentuate the sluggishness of the privatization process. The objectives of privatization—increased productivity and enhanced profitability of the private sector—are not clearly stated by the government. This reflects the ideological ambiguity vis-à-vis "big capital" and "profiteering."

There are stories of arbitrary imprisonment of successful, independent (not related to or supported by the religious hierarchy) private industrialists, whose extent of capital accumulation has exceeded the politically acceptable level. A Bank Markazi Iran official describes the private sector eloquently:

> "There is very capable entrepreneurial capacity inside Iran. But they do not want to risk their life. Once an entrepreneur, who is not from them [meaning related to the religious elite], is significant enough to be visible he is under serious threat. This is what happened to Mr. M (anonymous) who is in jail, charged with ridiculous accusations. They [the religious elite and their associates] do not allow the development of a sizable private sector, unless it belongs to them. The private sector in Iran is dominated by *bonyads* that have purchased shares in privatized public enterprises."[34]

"Crony capitalism" is not particular to Iran. Experience of countries in Southeast Asia indicates that capitalist development in developing countries is not the product of market mechanisms. Instead the states in countries like Korea instigated the process by "picking the winners" and promoting them. Nevertheless the ideological facade of Islamic Republic, with the negation of "profiteering and consumerism" obscures the importance of an efficient private sector. "Crony Islamic capitalism" combined with the lack of ideological clarity on the extent of private capital accumulation in productive activities undermine the effectiveness of reforms in Iran.

Above all, the credibility of reforms is undermined by the sheer fact that a highly disillusioned public is sceptical about the merits of economic reforms in the Islamic Republic.

Notes

1. For a comprehensive discussion of current reforms see International Monetary Fund (approved by G.T. Abed and L.P Ebrill), "Islamic Republic of Iran, Staff Report for 2002 Article 1V Consultation," (Washington: IMF, 2002); International Monetary Fund (preparted by A. Jbili et all), "Islamic Republic of Iran, Selected Issues and Statistical Appendix, IMF Country Report No. 02/212," (Washington: IMF 2002); J. Jensen and D. Tarr, "Trade, Foreign exchange, and energy policies in the Islamic Republic of Iran," World Bank Policy Research Working paper 2768, (Washington: World Bank 2002).

2. IMF, "Islamic Republic of Iran, Selected Issues and Statistical Appendix:" 11.

3. These sets of reforms are focused on trade openness to redirect the resources into competitive export-oriented industries. For a good discussion on the subject see: P. Mosely, J. Harrigan and J.Toye, *Aid and Power: The World Bank & Policy-based Lending*, Volume 1, (London: Routledge, 1991). Volume 2 is focused on case studies.

4. For a discussion of the second generation of structural adjustment see: World Bank Annual report 1999, (Washington: World Bank, 2000).

5. The second generation of structural adjustment reforms includes institutional reforms designed to improve the quality and effectiveness of the state and public institutions.

6. Parvin Alizadeh "Introduction", in Alizadeh (ed), *The Economy of Iran: Dilemmas of an Islamic state*, (London: I.B. Tauris, 2000): 1-25. For the discussion on the financial constraints facing the reforms in the mid 1990s see H. Pesaran, "Economic Trends and Macroeconomic Policies in Post-revolutionary Iran," in Alizadeh (ed): 63-100. The political economy side of the earlier reforms is articulated by S. Behdad, "From populism to economic liberalism: The Iranian predicament," in Alizadeh (ed): 100-145.

7. M.Karshenas and H.Hakimian, "Dilemmas and prospects for economic reform and reconstruction in Iran," in Alizadeh (ed), *The Economy of Iran: Dilemmas of an Islamic state,* (London: I.B. Tauris, 2000): 177-204.

8. For the change in the classification of Iran form an upper middle income to lower middle income country see World Development Reports, 1990 and 1993. See tables in the World Development Indicators of these two issues. (New York: Oxford University Press, 1990,1993).

9. IMF (2000), supra note 1: 72.

10. IMF (2000) supra note 1: 72.

11. IMF (2002), "Islamic Republic of Iran, Selected Issues and Statistical Appendix, IMF Country Report No. 02/212,": 62. The high growth rate of the labor force, which is supposed to continue to increase for sometimes at a rapid pace, reflects the demographic transition in Iran. During the 1980s Iran recorded very high rate of population increase averaging 3-4 percent per year. This was mainly driven as Hakimian (in Alizadeh 2000: 198) has pointed out "by a significant 'Islamic' baby boom in the early years of the revolution." Although population growth has decelerated to 1.6 per cent a year on average since early 1990s the baby boomer of the 1980s has continued to put upward pressure on labor supply.

12. Reference to these names was made in "Japan's lost decade," *The Economist*, 28 September 2002.

13. See for example Karshenas and Hakimian, supra note 7. This view is also well reflected in the 2002 IMF reports on Iran.

14. For the distributive nature of the revolution see A. Mazarei, "The Iranian economy under the Islamic republic: Institutional Change and Macroeconomic Performance 1979-1990," *Cambridge Journal of Economics* 20 (1996).

15. S. Maloney, "Agents or obstacles? Parastatal foundations and challenges for Iranian development," in Alizadeh (ed), *The Economy of Iran: Dilemmas of an Islamic state,* (London: I.B. Tauris, 2000): 145-177.

16. Y.H. Farzin, "The political economy of foregin exchange reform," in S. Rahnema and S. Behdad (eds), *Iran after the revolution: Crisis of an Islamic state*, (London I.B. Tauris: 1996): 174-203

17. R. H. Floyd et al, *Public enterprise in Mixed economies: Some macroeconomic aspects*, (Washington.D.C: International Monetary Funds, 1984).

18. D.Rodrik, "Getting intervention right: How South Korea and Taiwan grew rich," *Economic Policy* 20, April 1995: 78-84, 88-91.

19. A. Amsden, *The rise of the rest: Challenges to the west from late in dustrializing economies,* (New York: Oxford University Press, 2001): 8,140.

20. P.B. Evans, "The State as Problem and Solution: Predation, Embeded Autonomy, and Structural Change," in S. Haggard and R.R. Kaufman (eds),*The Politics of Economic Adjustment,* (Princeton: Princeton University Press, 1992): 143-179.

21. IMF (2000): 73-76.

22. IMF (2002), supra note 1: 20-30.

23. Pesaran, supra note 6 : 79.

24. IMF (2002), supra note 1: 64-65.

25. *Hayat* , 5 October 2002, (Iranian daily Farsi-language newspaper).

26. TFYDP covers the period 2000/01-2004/05. IMF (2000) supra note 1: 51-55.

27. At one point during the war there were more than seven exchange rates applicable to imports, although with the recommendation from the IMF the number was reduced to three. For the impact of multiple exchange rate on the economy see Farzin (1995).

28. IMF (2000) supra note 1: 40-42.

29. Farzin, supra note 16.

30. For a comprehensive discussion on recent reforms see both aforementioned 2002 IMF documents, supra note 1.

31. See, for instance, Chapter 8 of D. Gros and A. Steinherr, *Winds of Change: Economic Trasition in Central and Eastern Europe,* (London: Longman, 1995).

32. World Development Report, (Washington: World Bank, 1987): 109-12.

33. IMF (2002), "Islamic Republic of Iran, Selected Issues and Statistical Appendix, IMF Country Report No. 02/212."

34. Interview with a Bank official who did not want to be identified. Interview took place in London in August 2002.