

IRAN, ISLAMIC REPUBLIC

Key conditions and challenges

Table 1	2023
Population, million	89.2
GDP, current US\$ billion	401.9
GDP per capita, current US\$	4506.4
Upper middle-income poverty rate (\$6.85) ^a	21.9
Gini index ^a	34.8
School enrollment, primary (% gross) ^b	104.5
Life expectancy at birth, years ^b	73.9
Total GHG emissions (mtCO2e)	921.8

Source: WDI, Macro Poverty Outlook, and official data.
 a/ Most recent value (2022), 2017 PPPs.
 b/ WDI for School enrollment (2020); Life expectancy (2021).

Iran's economy is continuing its oil-driven growth in 2023/24, helping employment to return to pre-pandemic levels. Inflation remained elevated despite tighter monetary policy, in part due to inflationary expectations. Economic prospects are hindered by long-lasting structural challenges that are exacerbated by economic sanctions, heightened geopolitical tensions, and the impact of climate change.

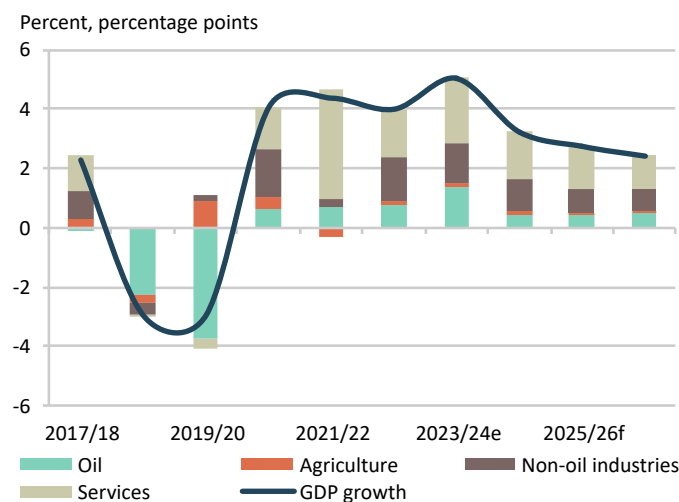
Economic growth has proven resilient over the past four years, despite ongoing economic sanctions and heightened geopolitical uncertainty. While the economy has benefitted from improved oil sector growth, the non-oil sector, notably services and manufacturing, has been the main driver of growth. Tradable sector production has shifted towards meeting domestic consumption, which has partly mitigated the impact of the financial and trade embargos and the limited access to foreign exchange reserves. Employment has also recently returned to pre-pandemic levels. Fiscal policy, notably the social protection system with its quasi-universal cash transfer, has partly buffered the impact of external shocks on the most vulnerable households and helped sustain consumption-led growth. The economy continues to face structural challenges that impact sustainable developmental outcomes. Ongoing sanctions limit technology transfer and investments to boost productivity. Energy subsidies and other administered prices are contributing to supply-demand mismatches, wasteful consumption, and allocative inefficiencies; this comes at a significant fiscal burden and at a detriment to the environment. Climate change exacerbates the energy and water shortages, negatively impacting food security and jobs in the stagnating agriculture sector. Limited job

opportunities and persistently high inflation have negatively impacted purchasing power and poverty outcomes. An estimated 40 percent of households are vulnerable, in that they have a high probability of falling back into poverty if they experience a shock. The gradual aging of the population, significant emigration of highly skilled workers, and a declining birth rate not only impact growth prospects but also strain an already struggling pension system. Financial sector challenges, including the undercapitalized banking sector and liquidity shortages, also restrict prospects of private sector-led growth.

Recent developments

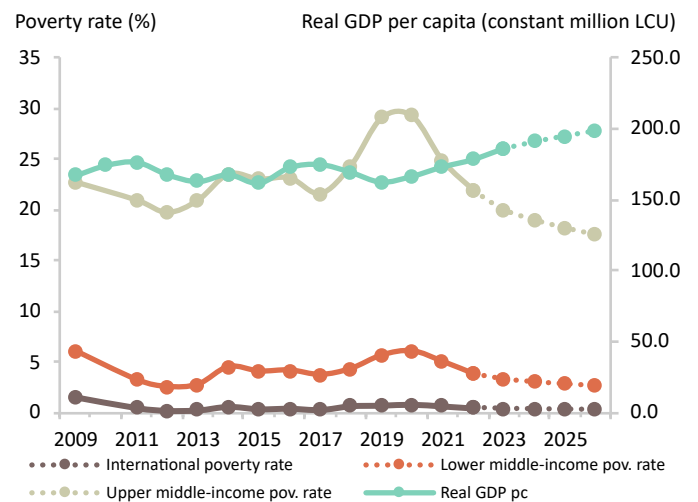
GDP growth accelerated to 5.1 percent year-on-year (Y-o-Y) in the first half of 2023/24 (Iranian year ending March 20), primarily driven by the oil sector and services. The oil sector value-added surged by 17.1 percent (Y-o-Y), fueled by a tight global oil market and greater success in marketing oil exports, including through price discounts. The non-oil sector also showed robust growth of 3.8 percent (Y-o-Y), which drove employment to pre-pandemic levels in Q3-23/24, as job creation increased by 2.9 percent and the unemployment rate reached a record low of 7.6 percent. Lower-than-expected government revenues in the first seven months of 2023/24 (Apr-Oct 2023) led to a reprioritization of expenditures. Only 72 percent of the budgeted revenues were realized in the period, as less than half of the planned

FIGURE 1 Islamic Republic of Iran / Real GDP growth and supply-side contributions to real GDP growth



Sources: Central Bank of Iran (CBI) and World Bank staff calculations.

FIGURE 2 Islamic Republic of Iran / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

oil revenues materialized due to lower Iranian oil export prices. This revenue shortfall forced the government to cut expenditures, especially capital investments, and to finance the growing deficit from the National Development Fund.

Inflation edged down in 11M-23/24 but remained above 40 percent. The decline was attributed to reduced inflationary expectations, spurring hopes of progress in nuclear negotiations, and tighter monetary policy. Headline and core CPI remained elevated, at 41.6 percent and 41.4 percent in this period, respectively, driven by high food prices and housing costs. To curb inflation, the central bank started implementing measures, including constraining bank balance sheet growth, increasing reserve requirements for riskier banks, and raising deposit and interbank interest rates.

Between 2020/21 and 2022/23, poverty declined as the economy recovered. Over two years, poverty as measured at the US\$6.85 poverty line declined by a cumulative 7.4 percentage points to 21.9 percent in 2022/23, meaning an estimated 6.5 million people were lifted out of poverty. For the lower-middle income poverty line of US\$3.65, poverty declined by 2.2 percentage points to 3.8 percent. Between 2020/21 and 2022/23, the bottom 40 percent of households experienced higher consumption growth

than the top 60 percent of households, reducing inequalities. This has also reduced overall inequality, with the Gini index dropping from 35.8 to 34.8. A combination of increased wages, an increase in self-employed earnings, and a top-up to the national cash-transfer program contributed to the growth in consumption and the corresponding reduction in poverty.

Outlook

Real GDP growth is forecasted to moderate to an annual average of 2.8 percent from 2024/25 to 2026/27. The initial boost in oil production and exports in 2023/24 is projected to moderate significantly with a similar spillover effect into the non-oil sector. Weaker global demand, ongoing sanctions, energy shortages, liquidity constraints, underinvestment, and geopolitical tensions further contribute to this outlook. While inflation is expected to decelerate further, it is expected to remain elevated. Despite government plans to consolidate the budget in 2024/25, fiscal pressures are forecast to persist, resulting in a fiscal deficit, compounded by off-budget expenditures. The current account surplus is projected to gradually decrease, influenced by lower commodity

prices, and heightened global competition in key markets.

Poverty is projected to decrease, but at a slower pace. Poverty at the US\$6.85 line is expected to drop by a further 3 percentage points over the next three years, and poverty at the US\$3.65 percentage line will decrease only slightly. Building on the last two years of inclusive growth, while ensuring a robust safety net, will help ensure the trend of poverty reduction continues.

The economic outlook is influenced by various risks, including global oil market dynamics, climate change, the intensification of economic sanctions, and prospects of conflict in the Middle East. A decline in oil prices resulting from reduced global demand would adversely affect economic prospects. Growing economic linkage with China makes the economy susceptible to fluctuations in China's economy. Increased extreme weather events threaten agricultural production and employment, posing risks to food security and livelihoods. The intensification of economic sanctions, especially impacting trade with neighbors and existing trade partners, would significantly weigh on growth. An expansion of the conflict in the Middle East would have significant ramifications for Iran and the region. Conversely, the removal or partial waiver of sanctions would significantly boost growth.

TABLE 2 Islamic Republic of Iran / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2021/22	2022/23	2023/24e	2024/25f	2025/26f	2026/27f
Real GDP growth, at constant market prices	4.7	3.8	5.0	3.2	2.7	2.4
Private consumption	3.9	8.7	3.2	2.4	2.1	1.8
Government consumption	8.3	-3.6	1.6	1.9	2.1	2.2
Gross fixed capital investment	0.0	6.7	5.8	4.5	4.2	3.1
Exports, goods and services	5.2	8.2	15.4	7.1	5.2	5.2
Imports, goods and services	24.1	7.5	1.6	1.8	2.1	2.1
Real GDP growth, at constant factor prices	4.4	4.0	5.0	3.2	2.7	2.4
Agriculture	-2.6	1.1	1.0	0.9	0.8	0.8
Industry	3.2	7.4	8.8	4.9	3.7	3.7
Services	6.5	2.7	3.6	2.7	2.5	1.9
Inflation (consumer price index)	46.2	46.5	40.8	35.3	32.0	30.5
Current account balance (% of GDP)	3.1	3.4	2.9	2.7	2.3	2.2
Fiscal balance (% of GDP)	-3.2	-1.9	-2.0	-2.2	-2.4	-2.5
Revenues (% of GDP)	11.0	11.7	11.8	11.8	11.8	11.9
Gross public debt (% of GDP)	42.4	30.1	30.7	32.3	34.1	35.9
Primary balance (% of GDP)	-2.7	-1.5	-1.6	-1.8	-2.0	-2.1
International poverty rate (\$2.15 in 2017 PPP)^{a,b}	0.7	0.5	0.4	0.4	0.4	0.3
Lower middle-income poverty rate (\$3.65 in 2017 PPP)^{a,b}	5.0	3.8	3.3	3.1	2.9	2.8
Upper middle-income poverty rate (\$6.85 in 2017 PPP)^{a,b}	24.8	21.9	20.0	19.0	18.2	17.6
GHG emissions growth (mtCO₂e)	2.9	2.9	3.1	2.0	1.8	1.6
Energy related GHG emissions (% of total)	67.8	67.6	67.8	67.7	67.5	67.3

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.

Notes: e = estimate, f = forecast.

a/ Calculations based on 2019-HEIS and 2022-HEIS. Actual data: 2022. Nowcast: 2023. Forecasts are from 2024 to 2026.

b/ Projection using annualized elasticity (2019-2022) with pass-through = 0.7 based on GDP per capita in constant LCU.