IRAN, ISLAMIC REPUBLIC

Table 1	2022
Population, million	84.7
GDP, current US$ billion	413.5
GDP per capita, current US$	4881.9
Upper middle-income poverty rate ($6.85)[a]	27.6
Gini index[a]	42.0
School enrollment, primary (% gross)[b]	109.7
Life expectancy at birth, years[b]	73.9
Total GHG emissions (mtCO2e)	947.2

Source: WDI, Macro Poverty Outlook, and official data.
a/ Most recent value (2019), 2017 PPPs.
b/ WDI for School enrollment (2020); Life expectancy (2021).

Iran's economy is set to grow for a fourth consecutive year, buoyed by the oil sector. However, persistent high inflation and scarce job opportunities compound labor market challenges. Oil-driven growth is non-inclusive; an estimated 28.1 percent of Iranians are poor, and two fifths of households are vulnerable to falling into poverty. The economic outlook is projected to remain constrained by sanctions, adverse climate change impacts, electricity and gas shortages, and weakened global demand.

Key conditions and challenges

Despite maintaining sustained moderate growth in 2022/23 - the Iranian year starts on March 20 - the economy faces entrenched structural challenges. Sluggish and jobless long-term growth, low productivity, high inflation, and imbalances in the banking and pension systems persist. These challenges have compounded longstanding socio-economic grievances that have triggered recent protests. Ongoing economic sanctions and a dominant public sector hinder the full utilization of Iran's economic potential, including leveraging a highly educated young population, to further diversify the economy towards non-oil industries and services such as tourism.

High inflation and insufficient job creation disproportionately impact lower-income households. Years of high inflation have negatively impacted poor households and eroded the real value of social assistance transfers. With only around one-third of the population employed and limited job prospects, particularly for the young and female population, labor market challenges persist; this exacerbates inequalities and contributes to a high poverty rate. Inadequate job creation has driven many Iranians, particularly women, out of the job market, resulting in a lost window of opportunity for growth. The gradual aging of the population, a notable rate of emigration of the highly skilled workforce, and a declining birth rate not only weigh on growth prospects but also pose a challenge for an already struggling pension system.

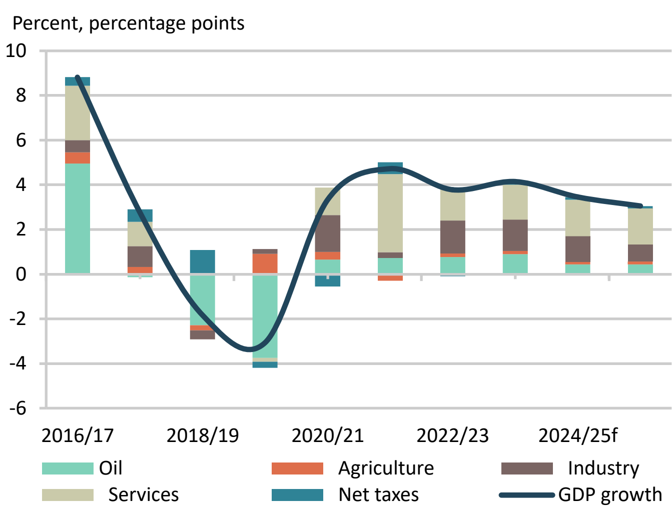
Urgent economic reforms are crucial to address critical structural issues. Priority reforms include restoring price and financial system stability, market-based lending, and minimizing unnecessary market interventions and price controls. Implementing a counter-cyclical fiscal policy would help curb budget deficits and promote investments in productive capacity, renewable energy, and economic diversification. Improved targeting of cash transfers will create fiscal space, while indexing the cash transfers for a targeted pool of eligible beneficiaries will help protect them from inflation.

Recent developments

Iran's economy maintained a moderate growth rate of 3.8 percent in 2022/23, driven by services and manufacturing. The oil industry also grew with tighter global oil markets. Private consumption served as the primary driver of GDP growth, while government consumption contracted in real terms to address the budget deficit. Both exports and imports expanded, and robust investment in machinery drove investment. Despite growing by 0.7 million year-on-year (Y-o-Y) in Q1-2023/24, employment still lags the economic expansion of the past three years.

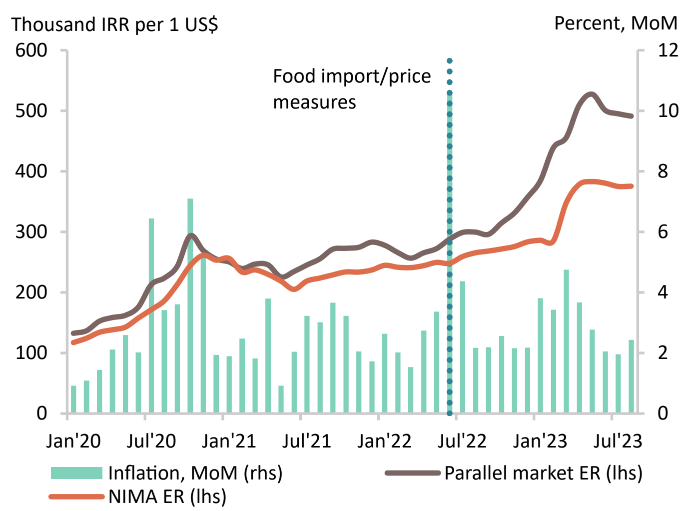
Elevated food prices and housing costs drove consumer price inflation

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 / Improved inflationary expectations have eased price pressures



Sources: CBI, Statistical Center of Iran, and World Bank staff calculations.
Note: NIMA is the CBI-administered foreign exchange auction system that facilitates transactions between exporters and importers.

to 46.7 percent (Y-o-Y) in the first five months of 2023/24. However, lower inflation expectations and the stabilization of the exchange rate helped decelerate monthly inflation, following the continuation of nuclear talks and improved access to frozen funds abroad that helped partially ease exchange rate pressures.

The recent increase in oil exports is helping to mitigate the budget deficit and improve the current account. In 2022/23 and Q1-2023/24, the government budget was constrained by lower than budgeted oil revenues in response to which the government reprioritized expenditures. Since Q2-2023/24, oil exports have recorded their highest level since the reimposition of US sanctions in 2018/19. Despite rising imports, higher oil exports in 2022/23 drove a current account surplus (US$14.4 billion), offset by a net capital account deficit (US$14.6 billion), marking the seventh consecutive year of net capital outflows. Improved oil exports in the first half of 2023/24 are estimated to have maintained the overall trade surplus, despite a non-oil trade deficit.

Outlook

GDP growth is forecast to maintain a modest pace in the medium term. Higher projected oil production and export volumes are expected to offset lower oil prices as well as China's economic slowdown in 2023/24, and to drive an oil-based growth. Non-oil growth is projected to remain constrained by ongoing sanctions, energy shortages, liquidity constraints, underinvestment, and economic uncertainty. Inadequate agricultural production, worsened by droughts and water scarcity, disproportionally harms the poor, jeopardizes food security, and drives migration to cities, increasing rural-urban disparities.

Anticipated higher oil exports and partial access to frozen funds are expected to alleviate fiscal and external pressures. Government expenditures for 2023/24 to 2025/26 are projected to outpace revenues, leading to a fiscal deficit, albeit a smaller one as a share of GDP considering the higher projected oil revenues. While the government plans to cover most of the deficit through asset sales, this is projected to partially cover the funding gap, thereby keeping the inflationary pressures from the budget deficit financing in place. On the external front, the current account is expected to remain in surplus as higher crude oil exports are expected to offset the decline in oil prices as well as rising imports. Access to frozen funds would help alleviate exchange rate pressures and inflationary expectations. High inflation and limited job creation will continue to place pressure on household welfare and challenge poverty reduction.

The economic outlook is subject to heightened risks. Downside risks include further water and energy shortages, intensification of climate change shocks, and a re-escalation of social tensions. Further sanctions and stricter enforcement of restrictions may disrupt trade and fuel further inflationary expectations. A substantial sanctions relief or an interim agreement related to nuclear negotiations could significantly improve the economic outlook.

TABLE 2 Islamic Republic of Iran / Macro poverty outlook indicators (annual percent change unless indicated otherwise)

	2020/21	2021/22	2022/23	2023/24e	2024/25f	2025/26f
Real GDP growth, at constant market prices	3.3	4.7	3.8	4.1	3.5	3.1
Private consumption	0.5	3.9	8.7	2.2	2.1	1.9
Government consumption	-0.9	8.3	-3.6	3.5	3.4	3.2
Gross fixed capital investment	3.2	0.0	6.6	5.9	5.5	5.4
Exports, goods and services	-12.8	5.2	8.2	15.4	7.9	5.6
Imports, goods and services	-29.7	24.1	7.5	8.7	4.1	3.0
Real GDP growth, at constant factor prices	4.1	4.4	4.0	4.1	3.5	3.1
Agriculture	3.2	-2.6	1.1	1.1	1.0	1.0
Industry	7.8	3.2	7.4	7.3	4.9	3.7
Services	2.2	6.5	2.7	2.9	3.0	3.0
Inflation (consumer price index)	47.1	46.2	46.5	42.6	35.8	32.3
Current account balance (% of GDP)	-0.3	3.1	3.5	4.8	3.5	2.7
Fiscal balance (% of GDP)	-5.8	-3.2	-1.9	-1.6	-2.1	-2.2
Revenues (% of GDP)	7.3	11.0	12.1	12.1	12.0	12.1
Gross Public Debt (% of GDP)	41.4	42.4	30.1	30.7	32.5	34.0
Primary balance (% of GDP)	-5.3	-2.7	-1.4	-1.3	-1.7	-1.9
GHG emissions growth (mtCO2e)	-2.4	5.7	2.7	2.8	2.4	2.2
Energy related GHG emissions (% of total)	66.2	67.6	67.5	67.4	67.2	66.9

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.
Notes: e = estimate, f = forecast.