

IRAN, ISLAMIC REPUBLIC

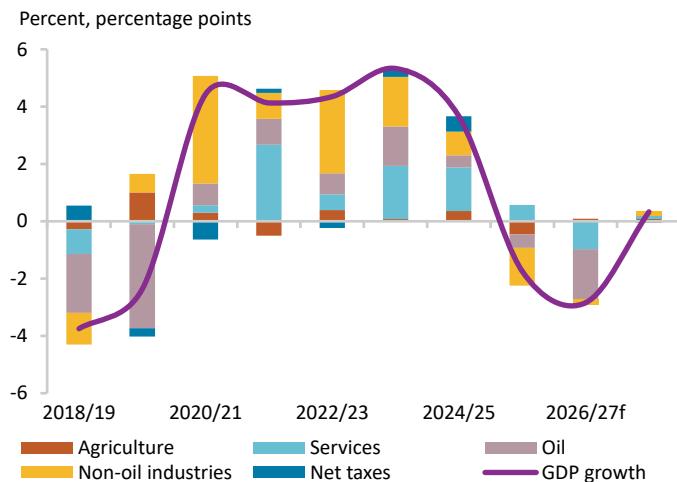
GDP growth is slowing, constrained by intensified sanctions, worsening water and energy shortages, and heightened uncertainty following the escalation in the conflict in the Middle East in June. Inflationary expectations and the financing of a growing fiscal deficit have increased inflationary pressures. Medium-term growth is projected to remain below recent trends and be exposed to heightened risks, including further economic sanctions and military tensions.

Key conditions and challenges

After four years of moderate growth, the economy is facing an unprecedented security escalation, intensified sanctions, and entrenched structural challenges. The escalation in the conflict in the Middle East in June, compounded by tighter sanctions, has triggered currency depreciation and raised inflation expectations. The stock market has fallen by 26 percent from its May 2025 peak and inflation is accelerating again. A widening budget deficit is limiting government investment despite urgent infrastructure needs.

Growing energy and water shortages have led to rationing and disrupted economic activity. Water scarcity, driven by recurring droughts, climate change, and suboptimal resource management, has depleted rivers, lakes, and aquifers, causing severe land subsidence that threatens infrastructure and long-term productivity. Precipitation has declined by 41 percent since 2024 and electricity shortages are causing frequent outages.

FIGURE 1 / Real GDP growth and supply-side contributions to real GDP growth



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

Population ¹ million	86.0	Poverty ² millions living on less than \$8.30/day	32.7
Life expectancy at birth ³ years	77.7	School enrollment ⁴ primary (% gross)	104.5
GDP ⁵ current US\$, billion	475.3	GDP per capita ⁶ current US\$	5528.9

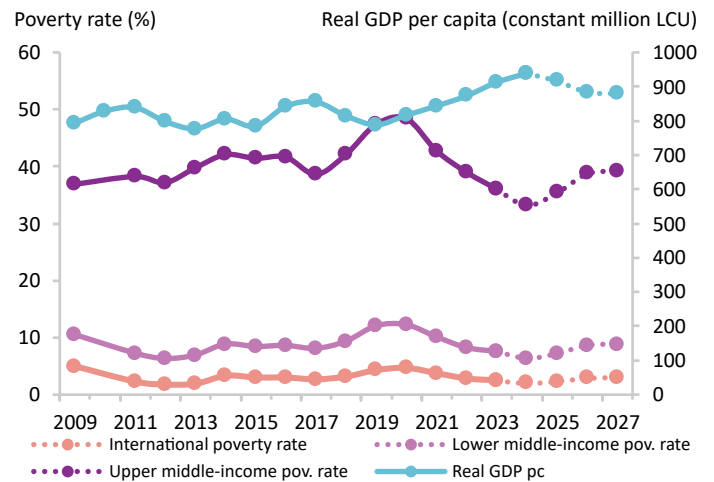
Sources: WDI, MFM, and official data. 1/ 2024. 2/ 2023 (2021 PPPs). 3/ 2023. 4/ 2020. 5/ 2024. 6/ 2024.

Recent growth headwinds add to labor market challenges. Despite moderate employment growth, on average, only 3.8 in 10 working-age Iranians are employed; for women, the rate is just 1.2 in 10. The services sector, employing over half of the workforce, has been impacted by conflict and post-war connectivity disruptions. Aging demographics and emigration, particularly among the highly educated youth, are eroding human capital and growth prospects.

Recent developments

GDP growth slowed to 3.7 percent in 2024/25 (the Iranian calendar year starts on March 20), the lowest in five years, driven by a sharp deceleration in the oil sector. Oil GDP growth fell to 4.6 percent from 18.8 percent a year earlier, reflecting weaker demand and years of underinvestment. Non-oil GDP expanded by 3 percent, supported by services, particularly in wholesale and retail trade. High-frequency indicators in 2025/26 point to a marked weakening of economic activity, amid geopolitical tensions, supply constraints, and declining investor confidence.

FIGURE 2 / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: See footnotes in the table on the next page.

Despite a planned contractionary budget in 2024/25, public spending exceeded targets by over 40 percent, resulting in an estimated fiscal deficit of 3.2 percent of GDP. To finance this gap, the government doubled planned bond issuance and tapped additional resources from the National Development Fund (NDFI) and the banking system. In 2025/26, the deficit has been widening, driven by higher spending. Oil revenues have faced pressure from stricter US sanctions, while non-oil tax revenues have been impacted by slower growth. Public debt remains modest relative to GDP and is almost entirely domestic. The ratio would be significantly higher when considering debt to NDFI (estimated at 21 percent of GDP in 2024/25).

The conflict has fueled inflationary expectations and triggered further currency depreciation, pushing inflation to 40.1 percent (Y-o-Y) in the first five months of 2025/26, driven by food price inflation of 44.5 percent. Disruptions to economic activity and limited access to foreign exchange caused non-oil exports and imports to decline by 6 percent and 16.3 percent (Y-o-Y), respectively, narrowing the non-oil trade deficit by 52 percent to US\$2.1 billion. With the economy facing stagflation and almost 90 percent of financing reliant on banks, the central bank remains under pressure to maintain monetary restraint. These pressures reinforce preexisting financial sector vulnerabilities, including the banking sector undercapitalization.

Outlook

GDP growth is projected to slow sharply in the medium term, led by a contraction in the oil sector amid stricter US sanctions and weaker global demand. Under a scenario of 500 kbpd lower oil exports for the final 7 months of 2025/26 compared to 2024/25 and a further halving of exports in 2026/27, GDP is expected to

contract by 2.3 percent on average in 2025/26-2026/27, reflecting declines in both oil and non-oil activity. This outlook assumes the return of UN sanctions and falling oil demand from China, but no further military escalation. Non-oil sectors, already constrained by trade and financial sanctions, energy shortages, and liquidity constraints, will face additional post-conflict disruptions and the repercussions of the return of UN sanctions.

This contraction in GDP is expected to push 2 million people into poverty in 2025. The share of the population living below the UMIC poverty line (US\$8.30 a day in 2021 PPP) is forecast to increase from 33.2 percent in 2024/25 to 35.4 percent in 2025/26. Poverty is projected to further increase in 2026/27 to 38.8 percent, pushing an additional 3 million people into poverty. Those living below or near the poverty line are particularly vulnerable to an economic downturn. Vulnerable households are disproportionately likely to be female-headed, have less than a high-school education and to live in rural areas. Increased water scarcity will particularly affect the livelihood of households relying on agriculture, increasing rural-urban migration and the pressure on urban service-provision.

The fiscal deficit is projected to average 4.2 percent over the projection period due to expected lower oil export revenues and higher expenditures. Inflationary expectations and monetary financing of the budget deficit are forecast to push inflation to above 50 percent in 2026-27, disproportionately affecting low-income households.

Downside risks to the outlook have significantly increased. Key risks include renewed military tensions, further intensification of sanctions, disruption to cross-border trade, a sharp cut to oil exports, and slower global growth, which could further dampen growth, depress investment, and amplify fiscal and inflationary pressures.

Recent history and projections

	2022/23	2023/24	2024/25e	2025/26f	2026/27f	2027/28
Real GDP growth, at constant market prices	4.4	5.3	3.7	-1.7	-2.8	0.3
Private consumption	5.3	1.6	3.5	-0.3	-2.0	0.5
Government consumption	-0.8	-0.6	3.8	-2.1	-3.3	1.2
Gross fixed capital investment	9.2	6.3	3.8	-4.9	-7.6	1.8
Exports, goods and services	7.7	13.2	6.0	-12.8	-16.2	-1.1
Imports, goods and services	8.8	1.5	2.7	-16.4	-24.0	2.3
Real GDP growth, at constant factor prices	4.6	5.0	3.1	-1.7	-2.8	0.3
Agriculture	3.7	0.8	3.6	-4.5	1.0	1.0
Industry	9.0	7.3	2.8	-4.3	-4.8	0.3
Services	1.2	4.0	3.3	1.2	-2.0	0.2
Employment rate (% of working-age population, 15 years+)	37.2	37.9	37.9	37.4	36.4	36.3
Inflation (consumer price index)	53.1	47.4	35.8	49.0	56.0	58.0
Current account balance (% of GDP)	3.4	1.9	2.8	-0.3	-0.1	0.3
Net foreign direct investment inflow (% of GDP)	0.0	0.0	0.0	-0.1	-0.2	0.0
Fiscal balance (% of GDP)	-2.6	-2.5	-3.2	-4.1	-4.7	-3.9
Revenues (% of GDP)	10.3	9.8	9.9	8.0	6.9	7.3
Debt (% of GDP)	28.1	26.1	24.3	26.6	29.0	29.4
Primary balance (% of GDP)	-2.2	-2.2	-2.7	-3.6	-4.2	-3.5
International poverty rate (\$3.00 in 2021 PPP)^{1,2}	2.8	2.5	2.0	2.3	2.9	3.0
Lower middle-income poverty rate (\$4.20 in 2021 PPP)^{1,2}	8.2	7.5	6.3	7.2	8.6	8.8
Upper middle-income poverty rate (\$8.30 in 2021 PPP)^{1,2}	39.0	36.0	33.2	35.4	38.8	39.2
GHG emissions growth (mtCO2e)	1.1	1.2	2.6	0.7	0.5	1.1

Source: World Bank, Poverty and Economic Policy Global Departments. Emissions data sourced from CAIT and OECD.

Notes: e = estimate, f = forecast. Data in annual percent change unless indicated otherwise.

1/ Calculations based on 2017-HEIS, 2019-HEIS, and 2023-HEIS. Actual data: 2023. Nowcast: 2024. Forecasts are from 2025 to 2027.

2/ Projection using annualized elasticity (2017-2019) with pass-through = 1 based on GDP per capita in constant LCU.