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The political economy of Iran: A conceptual, theoretical and historical analysis

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historical analysis**

Hanlon, Stacey Whitmore, M.A.

University of Nevada, Las Vegas, 1991

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THE POLITICAL ECONOMY OF IRAN:
A CONCEPTUAL, THEORETICAL AND
HISTORICAL ANALYSIS

by

Stacey Whitmore Hanlon

A thesis submitted in partial fulfillment
of the requirements for the degree of

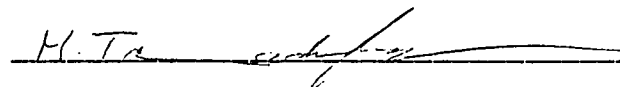
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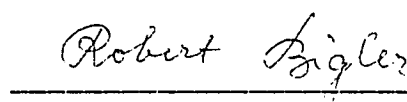
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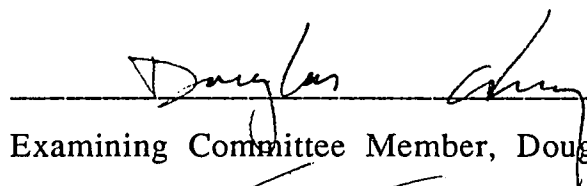
Political Science


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December, 1991


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ABSTRACT

THE POLITICAL ECONOMY OF IRAN: A CONCEPTUAL, THEORETICAL AND HISTORICAL ANALYSIS

This thesis is a case study of the political economy of Iran from 1963 to the present. It analyzes the interactions of the political and economic spheres, and the effects of those interactions on political development within Iran. For this study, political development is viewed in terms of a system's capacity to respond to economic and political demands placed upon it by the population. Various theories of political economy are reviewed in the first chapter, and their applicability to Iran's system is discussed throughout the work. The interaction between existing economic and political systems in Iran, their transformation over time, and the resulting changes in the capacity of Iran's leadership to deliver economically and politically are the focus of this study.

A historical analysis is employed to compare the politico-economic approaches and degree of development under the regime of Muhammad Reza Pahlavi Shah from 1963 to 1979, with the post-revolutionary theocratic regime from 1979 to the present. The analysis focuses on the interaction of economic conditions, political decisions, and global economic and political factors. Overall, it is argued that development has been lacking both as a result of environmental circumstances and of decisions made by Iran's leaders. The historical analysis is valuable because it provides a basis from which to speculate on the future political economy and

development of Iran. For Iran, development depends on sustained economic growth and adoption of a method of distribution in which economic gaps are narrowed. In addition, development requires that political demands of the population be addressed; this means creating avenues for interest articulation and political participation by the masses. The current leadership is aggressively pursuing economic growth; if they are successful, the political demands of the population will increase and the stability of the country will depend on successfully responding to these demands.

THE POLITICAL ECONOMY OF IRAN
A CONCEPTUAL, THEORETICAL
AND HISTORICAL ANALYSIS

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INTRODUCTION

The focus of this thesis is an analysis of how economic conditions, political decisions, and the environment (domestic and global) have interacted to shape the political economy of modern Iran, which in turn has affected the degree of development in this country. Development is an ambiguous concept. Scholars have been theorizing for several decades in an attempt to distinguish what makes one country more "developed" than another country. In the first chapter of this thesis a conceptual and theoretical framework is given in order to facilitate a better understanding of political economy and political development. A number of approaches to political economy are reviewed and their applicability to Iran is briefly examined. Further examination of how Iran has used these politico-economic methods is detailed as the paper progresses. After the review of political economy studies, a framework for political development is provided. For the purposes of this paper, development is defined in terms of a state's ability to satisfy the economic and political needs and demands of its population. Having provided the conceptual and theoretical framework for the paper, the following chapters use this framework to analyze Iran's political economy from 1963 to the present.

Chapter two examines Iran from the first year of the reform program of the Shah, known as the White Revolution to the revolution of 1979. The White Revolution's main point of change was

land reform. The Shah's program of land reform was primarily designed to decrease the power of landlords and to modernize Iran's agricultural sector, rather than to redistribute the lands to the peasants. The 1970's in Iran were characterized by a huge increase in oil revenues, followed by a slump, and by the Shah's modernization program. The Shah made a number of poor economic and political decisions, that combined with environmental circumstances, to make the 1979 revolution inevitable.

Chapter three examines post-revolutionary Iran, during Ayatollah Khomeini's decade as the leader of this country. This ten year period was dominated by an environment shaped by the revolution, the war with Iraq, and declining oil revenues. The leadership was characterized by factionalism, but Khomeini maintained his position as the final arbiter in the regime until his death in 1989. The political and economic systems of the two regimes were different in a number of ways, but there were similarities, too; in particular, it is demonstrated that both regimes showed very little development in terms of satisfying the economic and political demands of the population. The Khomeini regime might be characterized as more popular or more legitimate in the eyes of the masses, than the Pahlavi regime, but both used repressive methods to deter political opposition and the economic systems under both declined rather than seeing growth.

The fourth and final chapter of this thesis examines Iran in the two years since Khomeini's death, and speculates on the future prospects for this country. The pragmatic faction within the regime has generally prevailed in the past two years, and policies have

focused on postwar reconstruction. The changes in the political economy that are taking shape at the present time may allow for further development in Iran with practical planning and favorable environmental conditions. Using this historical analysis of the political economy of Iran, I have attempted to demonstrate that development in Iran is certainly possible, but that there has to be a willingness on the part of the leadership for this development to take place. In the long term, if steps are not taken to satisfy the economic and political demands of the people, the kind of instability that led to the 1979 revolution may be seen again.

THE POLITICAL ECONOMY OF IRAN

A FRAMEWORK FOR ANALYSIS

Since the 1960's, Iran has undergone a series of transformations in various areas, including agricultural, industrial, economic, and political. While these changes were generally designed to improve the country, Iran remains a politically and economically developing nation. This thesis will analyze the interrelationships of politics and economics and their effect on political development in Iran. After developing a conceptual and theoretical framework, the thesis will examine the political economy of Iran from the time of the White Revolution up to the present.

Much of the Western analysis of Iran has been inaccurate, particularly over the past two decades. In the 1970's many Western analysts believed Iran to be very stable, despite evidence to the contrary. Accounts of the revolution have often been oversimplified, describing it as a revolt against modernization. In addition, the factionalism of the post-revolutionary years has been largely misunderstood. In this historical analysis the development of Iran will be examined primarily in terms of the changes, or lack thereof, in Iran's political economy; obviously there are elements other than the political economy that factor into development, but due to

limitations this study will focus primarily on political and economic variables.

A conceptual and theoretical framework of modernization and political development and of political economy is necessary to proceed with this study. Numerous analysts have improperly described the 1979 Revolution as a revolt against the modernization programs of the Shah, when in reality the overwhelming Westernization that accompanied modernization and the absence of political development were much more important factors than was modernization. Since these three concepts overlap, they have often been used improperly in analysis. Political development must be distinguished from other connected concepts in order to analyze Iran's level of development. In addition, a conceptual and theoretical framework for political economy must also be employed in order to examine development in terms of political economy. Analyzing the interaction of the political and economic spheres and the policies chosen by the leadership of Iran will indicate the degree of development which Iran has achieved.

This thesis will show that the decisions which Iran's leaders have made over the past three decades have affected that country's development. An examination of the interaction between the environment and the decisions made since the White Revolution reveals the reasons for the Shah's downfall, Khomeini's rise to power, and Iran's general lack of development. Chapter one of this thesis gives a conceptual and theoretical framework for political development and political economy. This framework will be used throughout the thesis to analyze the changes in Iran's political

economy and the effects this has on development. Chapter two examines Iran from the time of the adoption of the reform program, known as the White Revolution, up to the 1979 Revolution. In particular, the economic and political environment of this time period and the decisions made by the Shah's regime will be analyzed, especially in regard to their relationship with Iran's development. In chapter three the transition from the revolution to the Islamic Republic, led by Khomeini, will be studied. In particular, the decisions made by Khomeini's regime will be examined in light of the revolution, oil revenues and the war with Iraq. Finally, chapter four will look at Iran since Khomeini's death and will examine the prospects for further development in Iran.

To become a "modern, developed nation" has been an objective of the various regimes in Iran throughout this century. Reza Shah adopted several of the same measures in Iran that Ataturk had used to modernize Turkey, including attempting to reduce the influence the religious establishment had in politics. In the early 1950's, Iranian Prime Minister Muhammad Mossadeqh tried to gain independence from Britain and the Soviet Union in order to modernize and develop Iran. Mohammad Reza Shah used the oil money in the 1970's in his drive to make Iran one of the top five powers in the world. Finally, Khomeini offered an Islamic alternative to the Western model of development that the Shah had pursued.

Modernization and Political Development

Modernization and political development are "analytically distinct but actually interrelated" processes,¹ which are related to the political and economic systems of a nation. According to Samuel Huntington's summary of David Lerner's work, the principal aspects of modernization are "urbanization, industrialization, secularization, democratization, education, *and* media participation."² The study of modernization and political development has been fraught with conceptual ambiguity and Western bias. Throughout the nineteenth and most of the twentieth centuries analysts saw Western Europe as providing the "linear map of man's progress from tradition to modernity."³ It was generally assumed that the advanced, liberal democracies had arrived and that their past provided a map for other countries to follow in their struggle to modernity. As a result, analysts often simply examined the histories of the "developed nations" and told Third World nations to follow the same steps. This oversimplified advice did little to aid the nations in their search for modernity.

Over the years, many definitions of modernization have been offered. In the late 1960's, Samuel P. Huntington stated that modernization requires both social mobilization (changes in the

¹ James A. Bill and Carl Leiden, *Politics in the Middle East*, (Boston and Toronto: Little, Brown and Company, 1979) 6.

² Samuel P. Huntington, *Order in Changing Societies*, (New Haven and London: Yale University Press, 1968) 32.

³ James S. Bill and Robert L. Hardgrave, Jr., *Comparative Politics: The Quest for Theory* (Lanham, MD and London: University Press of America, Inc., 1981) 48-49.

aspirations of individuals, groups and societies) and economic development (changes in capabilities).⁴ Once the process of modernization begins there is a fundamental shift in values, attitudes and expectations within society. Huntington refers to this as modernization at the psychological level. Traditional man expects continuity in nature and society; he does not believe man can change or control either one. Modern man, however, accepts the possibility and desirability of change. This shift in values, attitudes and expectations accompanies modernization under all circumstances.⁵

There is a plethora of definitions of modernization in development literature. Some analysts feel that Huntington's overall conceptualization of modernization has a conservative Western bias (namely his focus on stability and participation). In an attempt to move away from this bias and to further the understanding of this phenomenon, James A. Bill and Carl Leiden state that "modernization is most concisely defined as the process by which man increasingly gains control over his environment."⁶ The technological and scientific revolutions that many societies have undergone are important aspects of modernization, but this process is not limited to these changes. The increasing control man has over his natural and social environments in modernizing society has three dimensions: 1) technological - the industrialization process; 2) organizational - the differentiation and specialization of structures and functions; and, 3)

⁴ Huntington, 34.

⁵ Huntington, 32.

⁶ Bill and Leiden, 3.

attitudinal - the cultural secularization or rationalization of society.⁷ These attitudinal changes are due to the changes in lifestyle that are caused by the increasing capacity to change the environment. Modernizing man develops a cause/effect (rational) orientation from understanding the environment (an example is modern man's understanding that typhoons are caused by shifting ocean tides and winds, rather than by a supernatural phenomena).

Another characteristic of modernization is that it is "a process in which expectations necessarily race beyond their satisfaction."⁸ Once modernization begins, the attitudinal changes that accompany it produce expectations that society cannot immediately satisfy. When man comes to believe that government is a product of man rather than God, expectations of government change. The cause/effect (rational) orientation that modernizing man develops often results in expectations of change in society, such as political participation. This is often where the issue of political development is raised. However, before addressing development, it is important to realize the extent to which Western bias has affected modernization.

Much of the theorizing concerning modernization and development has been biased in that it has focused on Western systems as the final product of these processes. However, not only have the conceptualizations and theories regarding modernization been biased, but so too has the process of modernization. The adoption of Western traits, norms and values has generally

⁷ Bill and Hardgrave, 63.

⁸ Bill and Leiden, 3.

accompanied the process of modernization; this is often referred to as "Westernization". However, the developing countries of the world want modernization while they do not want Westernization. This is a point that many Western analysts have failed to recognize, including those analysts that believed the Iranian Revolution to be a fight against modernization. Many within the developing world believe that while it is inevitable that their culture will change due to modernization, it is not inevitable that their's must become a Westernized culture. One Iranian writer has referred to this adoption of components of Western culture as "Westoxication." Consequently, it is very important to distinguish between modernization and Westernization. The developing world wants to gain more control over its environment, but it does not want to lose its unique history and culture to the developed world. An example of this is the opposition to the West that is accompanying the growing nationalism in the developing world. For quite some time now, modernization and political development have been mired down in Western bias, and it has been difficult to separate the former two from the latter.

As noted above, the two processes of modernization and political development are analytically distinct, but in practice are interrelated. According to Bill and Hardgrave "development is most usefully understood in terms of a system's response capacity in relationship to demands."⁹ The increasing control over the environment and the consequent attitudinal changes that result from

⁹ Bill and Hardgrave, 67.

the modernization process produce demands on the system to which it must respond. Here the relationship between the two phenomena is apparent.

Modernization has provided the thrust behind *increasing* demands on political systems throughout the world. To effectively respond they must enhance their capacity to meet these demands -- one way or another.¹⁰

The capacity to respond, not the method of response, is the key element in Bill and Hardgrave's understanding of political development.

The earlier studies of political development were generally influenced by the work of Gabriel Almond and Bingham Powell. In *Comparative Politics: A Developmental Approach*, Almond and Powell state - "When we speak of level of political development, we really are dealing with three interrelated variables - role differentiation, subsystem autonomy, and secularization. There is a tendency for these processes of change to vary together."¹¹ According to the authors, developed systems are characterized first by structural differentiation which is the differentiation of new political functions and the development of specialized structures to perform these functions. In filling the roles to perform these new functions, developing societies begin to value achievement over ascription. In addition, increasing subsystem autonomy is a key element of developing systems. Groups that function independently

¹⁰ Bill and Hardgrave, 67.

¹¹ Gabriel A. Almond and G. Bingham Powell, Jr., *Comparative Politics: A Developmental Approach*, (Boston and Toronto: Little, Brown and Company, 1966) 306.

from the government and are able to influence that government are a distinguishing component of developed systems according to the authors. Finally, while structural differentiation and subsystem autonomy are the structural components of development, cultural secularization is the attitudinal/cultural component of development. The rationalization of authority, or viewing government as a product of man, rather than as a creation of God, is necessary for development according to Almond and Powell. The framework given by these two scholars was used for many years to measure the political development of nations until valid criticism minimized the role of this framework.

There are several problems with Almond and Powell's work. First, there is a Western bias. The reliance on subsystem autonomy as a distinguishing component of political development suggests that all non-democratic-pluralist systems are not developed. In examining a developing country like Iran, which is not likely to adopt a Western democratic-pluralist system, this Western bias suggests that there is no hope of Iran developing. In addition, cultural secularization as a key element of development takes away from the role that religion has played and may continue to play in development. For example, Catholicism in Latin America and Islam in the Middle East, particularly Iran, may be important components of political development. A final criticism comes from Bill and Hardgrave:

What they (Almond and Powell) have done in focusing on differentiation and secularization is to define political development in terms of modernization. Development

defined in terms of the vehicles of capability rather than in terms of capability itself necessarily leads to the rather clumsy distinction between positive and negative development ...¹²

Bill and Hardgrave's point here is that defining development in terms of the vehicles of capability necessarily limits and confuses one's understanding of political development. Bill and Hardgrave's definition of development in terms of capacity to respond to demands alleviates the problems that Almond and Powell encounter. At the same time, Bill and Hardgrave's definition is ambiguous. Knowing the limitations of Almond and Powell's work allows one to apply some of their ideas to a development framework without encountering the same criticism.

A second work that furthered the study of political development was Samuel Huntington's book *Order in Changing Societies*. Huntington's focus for development is institutionalization.

Political modernization involves the extension of political consciousness to new social groups and the mobilization of these groups into politics. Political development involves the creation of political institutions sufficiently adaptable, complex, autonomous, and coherent to absorb and to order participation of these new groups and to promote social and economic change in the society.¹³

While Huntington's focus is on institutions, he relies on certain elements of Almond and Powell (although Huntington places these elements under political modernization rather than political

¹² Bill and Hardgrave, 73.

¹³ Huntington, 266.

development). Huntington says political modernization includes rationalization of authority and differentiation of new political functions. Huntington adds a new dimension to political development theory, defining institutions as "stable, valued, recurring patterns of behavior," and institutionalization as "the process by which organizations and procedures acquire value and stability."¹⁴ The focus on institutionalization as the key element of development is an improvement on Almond and Powell's framework, since it focuses on general institution-building as a method of development rather than specifying democratic-pluralism as necessary for development, but there are criticisms of Huntington, too.

Huntington's focus on stability is problematic - political development is not necessarily a stable process. Critics of his work contend that Huntington is too concerned with the status quo, making his work overly conservative. In addition, just as Bill and Hardgrave criticized Almond and Powell for defining development in terms of the "vehicles of capability", one could accuse Huntington of the same mistake, since institutions can be considered the vehicles of capability rather than the capability itself. As such, specific recommendations for development might include institution-building, but institutions will not be considered necessary for defining development in this paper.

¹⁴ Huntington, 12.

Bill and Hardgrave's ideas on response capacity have been referred to, but have not been entirely explained. According to the authors,

Development demands an integrative, responsive, adaptive, and innovative capacity. Capacity involves sheer magnitude or scope in political and governmental performance; rationality in administration and effectiveness in the implementation of public policy.¹⁵

By defining political development in terms of capacity to respond to demands, rather than structural differentiation and subsystem autonomy or institutionalization, the authors have avoided the criticisms of the previously discussed scholars; however, their ambiguity makes it practically impossible to produce an operational definition and thus to determine the level of political development of a particular country. Viewing development in terms of response capacity means that as a state develops it is able to deliver when the populations makes demands. Delivering involves satisfying economic and political demands of the people.

According to Bill and Hardgrave, "Political development must involve then both the will and the capacity to initiate, absorb, and sustain continuous transformation."¹⁶ A key point here is the inclusion of the system's ability to initiate transformation, rather than simply respond to it. For Bill and Hardgrave political development is understood as the capacity of the political system not

¹⁵ Bill and Hardgrave, 73.

¹⁶ Bill and Hardgrave, 75.

only to absorb and sustain change, but also to be able to introduce and generate it.

In examining the modernization and political development of Iran, this study will view political development as it is defined by Bill and Hardgrave, focusing on the political and economic aspects of the system's capacity to initiate, absorb, and sustain transformation. Iran's system obviously lacked the capacity to absorb and sustain transformation in the late 1970's, or the revolution would not have taken place. Development in terms of response capacity means having the capability to satisfy the economic and political demands of the population. The basic needs of a developing society include life sustaining necessities such as food and shelter for the population. In addition, sustained economic growth can be considered necessary for development. Economic growth provides the system with the ability to initiate and absorb certain types of transformation and to provide the population with relative economic demands. For example, economic growth can help to meet the material demands of the population, which often increase as modernization takes place. Finally, development depends on the capacity of the system to respond to the population's political demands and/or needs. Often these demands include avenues within the system for interest articulation and political participation. There is no specific form of interest articulation or political participation that is necessary, as long as the political demands of the population are satisfied.

Effective response capacity to political demands can be somewhat measured by examining the nature and strength of the opposition to the regime. If the opposition is violent and it is strong

among the population, it would indicate that the regime has not delivered in a manner satisfactory to the people. Political development viewed in terms of response capacity depends on the environment within which the society functions, and on the decisions of the governing body. The environment and the decisions affecting the political and economic spheres of a state often contribute to determining the degree of development of that state.

In the case study of Iran, the interrelated nature of modernization and political development and political economy is apparent, particularly looking at the policies of the 1970's. Just prior to the Iranian Revolution of 1979, James Bill and Carl Leiden stated that satisfying material demands (in the Middle East) may temporarily alleviate economic discontent, but eventually there "must be an enduring capacity to satisfy continually and effectively the social and political needs of all groups and classes in the society."¹⁷ The Iranian Revolution was, at least in part, a response to the regime's failure to satisfy the social and political needs of the groups and classes in Iran. The interrelationship of the politics and economics of Iran, and its effects upon the political development of this country is the subject of this study.

Political Economy

It is obvious that modernization and political development involve numerous facets in society; for this study, the development

¹⁷ Bill and Leiden, 15.

of Iran will be examined in terms of political economy. While it has been recognized for quite some time that the political and the economic sphere are somehow interconnected, there is no single accepted theory of political economy. The concept itself is ambiguous. Some scholars, especially political scientists, underscore the political basis of economic actions whereas others, particularly economists, focus on the economic basis of political actions. For example, according to Alan Richards and John Waterbury, political economy examines the formulation of public policies that shape the allocation of resources within societies and the political consequences that flow therefrom.¹⁸ This conception of political economy is politically based, whereas the Marxist conception views politics as being determined by the economic system. According to Marx, there is a political superstructure that is entirely dependent on the economic substructure of society. For the purposes of this paper however, the definition of political economy must take into account the interaction and interdependence of the economic and political systems, both international and domestic. According to Frieden and Lake "international political economy is the study of the interplay of economics and politics in the world arena." In the most general sense and for the purposes of this paper, "the *economy* can be defined as the system of producing, distributing, and using wealth." *Politics* will be viewed as "the set of institutions and rules by which

¹⁸ Alan Richards and John Waterbury, *A Political Economy of the Middle East: State, Class and Economic Development* (Boulder: Westview Press, 1990) 2.

social and economic interactions are governed."¹⁹ This focus on the interdependence of the two areas is applicable not only at the international level, but also at the domestic level. In the case of Iran, the nation's dependence on oil sales on the international market demonstrates the high degree of interdependence of the two levels.

In this introductory chapter an evaluation of four major approaches to the study of international political economy will be presented as well as a brief summary of their applicability to Iran. The four approaches that will be examined include liberalism, Marxist and dependency theories, economic nationalism and economic internationalism. Since this chapter can only briefly examine these methods of studying political economy, further reading in each might include: Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (liberalism); Karl Marx, *Capital: A Critique of Political Economy* (Marxism); Andre Gunder Frank, *Dependent Accumulation and Underdevelopment* (dependency theory); Friedrich List, *The National System of Political Economy* (economic nationalism); and Gunnar Myrdal, *Beyond the Welfare State: Economic Planning and its International Implications* (economic internationalism). Of these four, elements of liberalism, dependency theories and economic nationalism will be most useful in the study of Iran's political economy.

The first approach is liberalism. Based primarily on the writings of Adam Smith, liberalism develops from the assumption

¹⁹ Jeffrey A. Frieden and David A. Lake, *International Political Economy: Perspective on Global Power and Wealth* (New York: St. Martin's Press, 1991) 1.

that individuals are actuated by their desire to better their condition through material gain. Smith viewed individuals as rational, utility-maximizing actors who are capable of making cost-benefit calculations.²⁰ Smith argued, assuming perfect competition, that individuals acting in their own economic interest would, as a collectivity, maximize collective well-being. Consequently, Smith placed primary emphasis on the “free and unfettered operation of the market for social well-being.”²¹ Smith argued that there was an invisible hand that would guide the market. In its original formulation, liberalism stressed laissez-faire capitalism, the rights of property, limited government, and social Darwinism.²² It is primarily this liberal approach upon which the global market economy has been structured.

There are several criticisms of liberalism that must be taken into account. First, Smith in particular and liberalism in general, focus on economic motives to the exclusion of others, including culture and politics. In addition, perfect competition may work in theory but it is not realistic; thus, the social well-being that should derive as a result of individuals seeking their own material gain in competition with one another cannot be realized. According to Martin Carnoy, “Smith never proves, or even argues that individuals

²⁰ Frieden and Lake, 6.

²¹ Martin Carnoy, *The State and Political Theory* (Princeton: Princeton University Press, 1984) 24.

²² R. Dan Walleri, “The Political Economy Literature on North-South Relations: Alternative Approaches and Empirical Evidence,” *International Studies Quarterly* 22 (Dec. 1978) 593.

seeking material gain in competition with one another is not a vice, in the sense that it tends to injure others.”²³ Consequently, one can see that the market does not function as it should and this presents problems for liberal theorists. "For it means that the 'invisible hand' does not work and that 'someone' has to take into his own hands the task of guiding the economy towards certain specific normative goals.”²⁴ This means that the interference that liberalism so vehemently opposes is needed if the economy is to function properly. Regardless of criticism, liberalism has largely shaped the global economy and is the basis of many of the developed countries' economies.

R. Dan Walleri suggests that third world countries are on the “periphery” of the global economy. The liberal solution offered to them has been further incorporation and integration into the global economy through such policies as the promotion of manufactured exports and import substitution policies.²⁵ These policies have been tried however, and while they have helped some countries improve their economic standing, those countries have generally remained in the “semi-periphery”²⁶ Iran, it can be argued, may be classified as

²³ Carnoy, 25.

²⁴ Shigeto Tsuru, "Towards a New Political Economy," *Economics in the Future: Towards a New Paradigm* Kurt Dopfer, ed., (Boulder: Westview Press, 1976) 109-110.

²⁵ Walleri, 593.

²⁶ Semi-periphery is a term used by Hooshang Amirahmadi to describe countries that are distinguished by their "expanding, but limited, home and export markets, technological dependency, and integration into the world economy. Hooshang Amirahmadi, *Revolution and Economic Transition: The Iranian Experience* (New York: State University of New York Press, 1990) 1.

either a peripheral or a semi-peripheral country. Liberalism helps explain the world capitalist economy within which Iran must operate; however, it cannot fully explain the political and economic policies under which Iran has functioned since the White Revolution.

The second approach to be examined includes Marxist and dependency theories. Marx described society as consisting of a base or substructure and a superstructure. The economic system of society is the substructure, whereas the superstructure consists of all other social systems, including the cultural and political elements. According to Martin Carnoy there are three fundamental elements in Marxism. First, Marx viewed the material conditions of society as the basis of its social structure and argued that the form of state emerges from the relations of production. Second, the state emerging from the relations of production does not represent the common good, but is the political expression of the class structure inherent in production. Finally, the state in bourgeois society is the repressive arm of the bourgeoisie which keeps class antagonisms in check.²⁷ One other important element of Marx's argument is that in observing the relations of production, Marx argued that the basis of the capitalist economy is the exploitation of labor by capital. Consequently, the relationship between these two classes is one of a zero-sum nature.²⁸ Marx argued that eventually the exploitation of labor would lead to class consciousness which would result in a social

²⁷ Carnoy, 46-47.

²⁸ Frieden and Lake, 8.

revolution overthrowing the bourgeoisie. This would be followed by a transformation of the system to socialism and then to communism.

Marxist theory has been criticized as deterministic, dogmatic and static.²⁹ History has not yet borne out the theory of Marxism, and in fact, the Soviet Union has arguably been an improper application of Marxism since it went directly from a stage of feudalism to one of socialism. Marxism is partially appropriate for an analysis of Iran because of the strong relationship it proposes between the economic and political spheres. However, the 1979 Revolution cannot be explained entirely in terms of class consciousness and dialectical materialism; indigenous cultural factors, which Marxism ignores, have to be taken into account when examining Iran's revolution. Due to certain cultural aspects in Iran, and particularly with respect to Islam, Marxism has not been incorporated into Iran's political agenda, and is not likely to be. Muslim people who strongly believe in God (Allah) cannot accept a theory that is atheistic in nature. In addition, the Islamic principle that recognizes the right of private property is contradictory to Marxist theory. As a result of these problems and others, including the fear of Soviet imperialism, which has carried the Marxist banner since the Soviet Revolution, Iran has resisted communist movements (with the exception of the Tudeh party which was very careful to avoid any connection to Marxism, and which regained some support during the 1979 Revolution). Thus, Marxism is useful in this case

²⁹ Ronald H. Chilcote, *Theories of Comparative Politics: The Search for a Paradigm* (Boulder: Westview Press, 1981), 404.

study due to the strong connections it purports between economic and politics, but the political agenda which it proposes is viewed as inappropriate for Iran.

Dependency theories, both Marxist and non-Marxist, have also made important contributions to understanding the international political economy (it should be noted that dependency arguments cannot properly be termed "theories" since they do not provide predictable generalizations; however, they are useful in describing certain phenomena). The main premise of dependency theories is that "foreign penetration has created underdevelopment."³⁰ This has created a situation in which underdeveloped states have been exploited by the more developed states. Theotonio dos Santos offered a description of dependency that was meant to describe the position of Latin America, but which can be applied to other less developed countries of the world:

By dependence we mean a situation in which the economy of certain countries is conditioned by the development and expansion of another economy to which the former is subjected. The relation of interdependence between two or more economies, and between these and world trade, assumes the form of dependence when some countries (the dominant ones) can expand and can be self-sustaining, while other countries (the dependent ones) can do this only as a reflection of that expansion, which can have either a positive or a negative effect on their immediate development.³¹

³⁰ Ronald H. Chilcote and Joel C. Edelstein, eds., *Latin America: The Struggle with Dependency and Beyond* (Cambridge: Schenkman Publishing Company Inc., 1974) 26.

³¹ Theotonio dos Santos, "The Structure of Dependence," *The American Economic Review* LX (May, 1970) 231-36, as quoted in Chilcote and Edelstein, 26.

Underdevelopment is understood to be created by and relative to the developed countries, which at an earlier time may have been *undeveloped* but were never *underdeveloped*. Since development is understood here as a relative state, those countries that are now considered developed were never underdeveloped because there were no developed states to compare them to. According to Ronald Chilcote and Joel C. Edelstein, it was the process of the expansion of capitalism, through which now developed countries progressed, which brought about the underdevelopment of many parts of Latin America (and it can be argued many other parts of the Third World).³² As capitalism expanded, parts of Latin America and many other areas (including parts of the Middle East) were seen as suppliers of raw materials and new markets for finished goods.

In order to explain inequality, dependency theories divide the states of the world into two economic categories - the industrialized capitalist developed states, considered the "core," (or center) and the developing states, which in turn are dominated by the former within the international capitalist system. These latter states are considered the "periphery." There are several different types of dependency theories. These types include the Marxist-derived world-system theory, the *dependencia* theories coming from Latin American scholars, and the structural theory of imperialism, as argued in particular by Johan Galtung. In general, the theories are similar, diverging mostly in regards to the solution to underdevelopment.

³² Chilcote and Edelstein, 27.

Galtung describes the world economy in terms of core and periphery and examines both external and internal imperialism.

Rather than focus on class formation, however, Galtung concentrates on the exploitation contained in the patterns of interaction that have arisen between the center and periphery states as a consequence of class interests.³³

He views developed nations (core) and the underdeveloped nations (periphery) as each containing a core and a periphery, where the elites within each nation formed their own core and the periphery contained the masses. Galtung argues that there are bonds between the cores of the dependent countries and the cores of the developed countries. External imperialism is the exploitation of the underdeveloped countries (periphery) by the developed countries (core), whereas internal imperialism is the exploitation of masses within a country (periphery) by that country's elites (core). This typology is helpful in describing Iran, both prior to and after the revolution. The internal and external imperialism that has dominated Iran will be examined in this study, as will its effects on development in Iran.

While many dependency theorists agree regarding this structural argument, there are differences as to whether the solution lies in the elites of the underdeveloped nations reforming themselves and breaking the ties with the developed nations or if the solution is socio-political revolution that overthrows the reigning leaders of the

³³ Walleri, 609.

underdeveloped countries and breaks the bonds of dependency with the developed nations.

Regardless of the differences ... most dependency theorists would probably argue that the particular form in which capitalism has molded the domestic class structures and external relations of the periphery states precludes the possibility of genuine national development in the Third World within the context provided by the present international order.³⁴

While there are many criticisms of dependency theories, especially since there is no single agreed-upon solution, the basic elements of dependency arguments can be applied to Iran. According to Hooshang Amirahmadi, by the time of the Iranian revolution in 1979, Iran had experienced almost three decades of a “dependent capitalist growth path.” This semi-peripheral country, as Amirahmadi describes it, had pursued, rather unsuccessfully, strategies of import-substitution industrialization and export promotion throughout the 1960’s and 1970’s.³⁵ Iran’s dependence on oil sales for the largest share of its revenues made that country dependent on the world capitalist economy in general and on the world oil market in particular. The major economic boom years of 1973-74 brought huge revenues to Iran which were mainly spent on material and human expansion of the civilian and military bureaucracies. This expansion brought several problems including

³⁴ Walleri, 611.

³⁵ Amirahmadi, 1.

personnel shortages which resulted in sharp increases in wages, and policies encouraging private accumulation which brought increased demand and thus shortages of producer and consumer goods, leading to additional price increases. In addition, the boom made Iran even more dependent on the capitalist world market for the sale of its single-commodity export. When the economic bust of 1976-77 arrived Iran was completely unprepared. The boom had extended the economy past its "material, human, institutional and infrastructural capacities." In 1975 the country was caught up in deficit spending, and with the bust, the economy only worsened.³⁶ Even after the Revolution and the policies of the new regime, which nationalized the oil industry, Iran remains a peripheral country that is dependent on the world capitalist market.

The third approach in political economy studies that will be evaluated and applied to Iran is economic nationalism. This approach concentrates on promoting national economic growth and development, primarily through an active state role. According to Friedrich List, writing in Germany in 1885, the free trade approach advocated by liberalism is only successful if all nations follow the principles of free trade. In addition, List states:

I saw clearly that free competition between two nations which are highly civilized can only be mutually beneficial in case both of them are in a nearly equal position of industrial development, and that any nation which owing to misfortunes is behind others in industry, commerce, and navigation, while she nevertheless possesses the mental and material means for developing those

³⁶ Amirahmadi, 19-21.

acquisitions, must first of all strengthen her own individual powers, in order to fit herself to enter into free competition with more advanced nations.³⁷

Even though List was writing this in 1885, in response to England's domination of world trade and Germany's poor economic position, this line of argument has become the basis of economic nationalism.

According to R. Dan Walleri, List departed from the liberal school in two significant ways. First, List emphasized the role of the state in promoting economic growth and development, rather than relying on the self-regulating mechanism of the market. He argued that the state should eliminate internal barriers to trade, subsidize the creation of infrastructure, and promote home industry and the export of manufactures. List believed this could be accomplished through the utilization of protective tariffs in order for "infant industries" to flourish and for the home government to collect revenues to further develop the economic sphere.³⁸ According to List, under a system of perfectly free competition with more advanced industrial nations, a less developed nation "can never attain to a perfectly developed manufacturing power of its own, nor to perfect national independence, without protective duties."³⁹

Since the first publication of Friedrich List's book in 1885, numerous refinements and criticisms of economic nationalism and its policies have been added. According to Walleri, economic

³⁷ Friedrich List, *The National System of Political Economy* (New York: Augustus M. Kelley Publishers, 1966) xxvii.

³⁸ Walleri, 596.

³⁹ List, 316.

nationalists seek to encourage domestically owned industries by promoting manufactured exports through import substitution. "The goal ... is to enhance national power, which is considered incompatible with foreign control over key areas of the economy."⁴⁰ George Macesich includes among the goals of economic nationalism: "as much self-sufficiency as possible, public ownership and public enterprise in key economic sectors, and/or intensive regulation and control of private and domestic and foreign enterprise."⁴¹ The specific policies that states adopt and their level of success obviously varies with social, economic and political considerations. Coughlin, Chrystal and Wood state that economic nationalism is based on protectionist trade policies which have the specific goal of expanding the domestic production in protected industries, benefitting the owners, workers, and suppliers of resources to those protected industries. Protectionist policies include tariffs, quotas, regulatory barriers, subsidies and exchange controls. These policies also benefit the government imposing them in light of the additional revenues. Those hurt by these policies, other than foreign interests, are the domestic consumers who have less choice and are hurt by lack of competitive pricing, and the other domestic producers who are not protected.⁴²

⁴⁰ Walleri, 596.

⁴¹ George Macesich, *Economic Nationalism and Stability* (New York: Praeger Publishers, 1985) 2.

⁴² Cletus C. Coughlin, K. Alec Chrystal, and Geoffrey E. Wood, "Protectionist Trade Policies: A Survey of Theory, Evidence, and Rationale," *International Political Economy: Perspectives on Global Power and Wealth* by Jeffry A. Frieden and David A. Lake, eds., (New York: St. Martin's Press, 1991) 25.

There are numerous criticisms of economic nationalism and its policies. The policy of import substitution was quite popular in Latin America in the 1950's, although it was eventually unsuccessful. In order to induce industrialization, these countries restricted imports of manufactured goods through tariff protection. There were at least two undesirable consequences that resulted from these policies:

1) the countries restricted imports to essential foodstuff and raw materials, which gave luxury items the most protection - the policies were meant to stimulate production for the home market, but the luxury items produced were not in high demand in the developing countries; 2) the firms that were developing behind the protective tariffs were often too inefficient to compete on the world market and thus had to remain protected.⁴³ Eventually, the policies were designated as unsuccessful and the countries abandoned them.

According to Melvyn Krauss, while protection is designed to give life to "infant industries" it often sets an environment in which these industries have no prospect of maturing and in which too many people benefit from the protection to give it up. In addition to the problems above, Krauss criticizes protectionism due to wasted resources, corruption of government officials by the protected and vice versa, lack of entrepreneurship and export stagnation.⁴⁴ Finally, economic nationalism has also been criticized for

⁴³ Walleri, 597.

⁴⁴ Melvyn B. Krauss, *Development Without Aid: Growth, Poverty and Government* (New York: McGraw Hill book Company, 1983) 11-12.

concentrating on industrialization that is inappropriate and unneeded, usually at the expense of agriculture.

In the case of Iran, particularly since the Revolution, economic nationalist policies were adopted but have been very limited in their success. In the summer of 1979 the Provisional Revolutionary Government (PRG) and the Revolutionary Council (RC) nationalized banks, insurance companies and major industries, including the oil industry which came under the National Iranian Oil Company.⁴⁵ There were immediate constraints on the success of these policies however. In the years immediately following the Revolution there was such factionalism within the leadership that it led to the inability on the part of the leaders to "formulate a coherent economic policy and regulate its relations with the domestic opposition and the international community."⁴⁶ There were some significant changes in the structure of the economy, including redistribution of resources and redefinition of national priorities, but constraints such as factionalism, the war with Iraq, and the limited control over the production, export and price of oil due to the world market and OPEC, left Iran in the position of a peripheral state dependent on the world capitalist economy.

The fourth and final approach in political economy is economic internationalism. Unlike the liberal and economic nationalist positions which "rest on the assumption that the key to progress in the Third World lies in a replication of the Western experience,"

⁴⁵ Amirahmadi, 23.

⁴⁶ Amirahmadi, 8.

economic internationalism, demands a fundamental transformation of the present international order.⁴⁷ This view is generally criticized as an unrealistic theory, but many scholars concerned with the Third World feel that it is at least worthy of some merit. Economic internationalism believes the solution to inequality within and between nations lies in the redistribution of resources on a global level. Economic internationalism argues that "since there is no world government to intervene in the international market to correct the uneven development among nations, it is essential that international institutions be created to deal with problems arising for the periphery states."⁴⁸ It was with this argument in mind that the United Nations Conference on Trade and Development (UNCTAD) was created in 1964 over the objections of the core nations in order to deal with the plight of the Third World.

The major objective of UNCTAD has been to secure non-reciprocal tariff reductions by the core states on manufactured exports from the entire developing world. This is viewed as an alternative to direct aid programs (which have failed for various reasons) and as a method of indirect redistribution.⁴⁹ Nonreciprocal trade agreements are designed to allow periphery states to gain a larger share of the world market, and consequently to stimulate the development of Third World economies. However, due to several factors, including the "unlikelihood that the center states will allow

⁴⁷ Walleri, 599.

⁴⁸ Walleri, 600.

⁴⁹ Walleri, 601.

such a broad and nonreciprocal liberalization in trade" and the lack of unity among the developing nations, UNCTAD has not been as successful as initially hoped.⁵⁰

There are several criticisms of economic internationalism. Some argue that it ignores the realities of the market. In addition, many (Marxists and dependency theorists) argue that in order to eliminate the mechanisms of neocolonialism between the center and periphery states, a radical transformation of the present international economic order would be required; this would include a massive redistribution of wealth. Since this would obviously hurt those in power it is likely that the powerful center states will oppose this transformation. In regards to Iran, economic internationalism is an approach that could aid in its economic development, but it is unlikely that this solution will materialize. Iran has often held an anti-imperialist attitude, but its record of disagreement with other developing nations is extensive; Iran has contributed to the disunity in OPEC and has had problems with the other countries in the Gulf area. Consequently, Iran has contributed to the lack of unity that is needed to force this redistribution. Despite the efforts of UNCTAD and other developmental programs, the prospects for an internationalist economic order to evolve are not good.

In examining the evolving political economy of Iran, all four of the above approaches must be understood. First, liberalism provides the general framework for understanding the international capitalist economy within which Iran must function. Second, dependency

⁵⁰ Walleri, 602.

theories aid in understanding Iran's position as a peripheral country in the world economy, particularly due to its status as a single-commodity exporter. In addition, protective trade policies, as espoused in economic nationalism, were adopted by the Iranian government in order to promote economic growth and development. Finally, while economic internationalism is unlikely to see its solutions implemented on a global scale it is important if only to understand Iran's and other developing countries' efforts to dispel the inequality between center and periphery states. As following chapters examine Iran's development, the role of these various arguments and their applicability to Iran's political economy will be demonstrated.

FROM REFORM TO REVOLUTION

This chapter examines Iran from the time of the reform program adopted in 1963, referred to as the White Revolution, to the revolution of 1979. The chapter analyzes the interaction of the environment and the decisions made by the regime, and the effects of that interaction on the political economy. The Shah's regime enacted a number of reforms in the 1960's in order to weaken the power of political opponents and to modernize Iran. These reforms have been regarded by many scholars to be the beginning point of the popular discontent that led to the 1979 Revolution. Later, a more intensive modernization program was pursued following the windfall of oil revenues in the early 1970's. At the same time, the Shah chose not to pursue any corresponding changes in the political sphere. Rising expectations were created as a result of modernization, but they met with economic decline and the absence of political development. Eventually, this contributed to the overwhelming popular discontent that led to the revolution.

Over the period of 1963 to 1977, the Iranian regime, led by Shah Muhammad Reza Pahlavi, made a number of poor political and economic decisions. In this period Iran grew more and more dependent on the oil market and the international capitalist economy. The country's economy experienced astounding growth

following the oil price increases in 1973, and at one point Iran's rate of industrial growth was the highest in the world.¹ However, despite this economic windfall, the Iranian regime was either unable to or chose not to address the needs of the Iranian people. The Shah employed various measures, from reform to brutal repression, in his attempt to maintain his power and realize his vision for Iran, but by 1979 none of his actions had gone far enough to save his regime.

The White Revolution

On June 26, 1963 the Shah put his new reform program, the "White Revolution", into effect.² The White Revolution was a program of reform aiming not at transformation of the Iranian society, but largely aimed at securing the Shah's position, and undermining his opposition.³ In the early 1960's, the Shah was being pressured by the United States to undertake some reform measures, since the U.S. believed that Iran would eventually fall into communist hands, and the only way to postpone this was through reform. American John W. Bowling prepared a report for the Kennedy administration which recommended the Shah adopt fourteen points of reform, including land reform and relaxation of political repression.

¹ Nikki Keddi, *The Roots of Revolution: An Interpretive History of Modern Iran* (New Haven and London: Yale University Press, 1981) 162.

² Homa Katouzian, *The Political Economy of Modern Iran: Despotism and Pseudo-Modernism, 1926-1979* (New York and London: New York University Press, 1981) 225.

³ As such, the use of the term "revolution" is misleading since it is appropriately used to indicate a fundamental transformation in society.

The Kennedy administration considered land reform an effective deterrent against communist expansion or an agrarian revolution of the Chinese type and a prerequisite for the success of any industrialization program.⁴

The Shah, feeling pressure from the United States, and seeing an opportunity to modernize Iran, while strengthening his position, chose to adopt several points of reform. Originally, the programme included six points, although over several years more were added until as many as eighteen were included. Of these, probably the most important point was land reform.

A program of redistribution of arable land was started by Prime Minister Ali Amini and his minister of agriculture, Hassan Arsanjani. Under Amini the first phase of redistribution successfully distributed land to a significant proportion of the peasantry and Amini became quite popular. As a result, the Shah saw the prime minister as a threat and forced both Amini and Arsanjani to resign.⁵ According to Nikki Keddi, "the best estimate is that something like 9 percent of Iran's peasants got land in this first phase," which is not insignificant compared to later phases. The reform was continued after Amini's removal, but it was unequal; some landlords maintained some of the best quality land whereas peasants received varying amounts of generally lower quality land.⁶ The reform was meant to undermine the semifeudal forms of landownership rather

⁴ Mohsen Milani, *The Making of Iran's Islamic Revolution: From Monarchy to Islamic Republic*, (Boulder and London: Westview Press, 1988) 80.

⁵ Milani, 84-85.

⁶ Keddi, 162.

than to distribute land on a more egalitarian basis. The landowners, or *khans*, were seen as a bar to development and to central government control of the countryside. The *khans* were often tribal leaders and had considerable influence over the peasants. They could be brutal, but they provided a support structure to the agricultural system, including providing seed, irrigation, and medical services to the peasants, that the government did not replace in its redistribution scheme.

In the second and third phases of the land reform program, reforms were much more conservative. Once the central government had undermined the landlords' (*khans*) power, regularizing the system was pursued, rather than redistribution.⁷ Phase Two of the land reform program, beginning in 1965, set limits on landowners, but provided them with options, including purchasing the peasants' rights of the use of land, assuming that the peasants were willing. Phase Three was an attempt to eliminate the tenancy relations in farming; it coincided with the government's creating farm corporations, to facilitate the mechanization of farming. The peasants were forced to transfer the use of their land permanently to the farm corporations in exchange for shares equivalent to the value of their land and other farm assets. The peasants saw this as a reversal, reverting them back to their previous status of agricultural labourers.⁸ Thus, the peasants did not receive the benefits that they

⁷ Keddi, 162.

⁸ M.H. Pesaran, "Economic Development and Revolutionary Upheavals in Iran," in *Iran: A Revolution in Turmoil*, Haleh Afshar, ed. (Albany: State University of New York Press, 1985) 28.

expected from land reform and the removal of the landlords was not as extensive as planned. In addition, the regime failed to fill the organizational and physical vacuum created by the "half-hearted removal of the landlords".⁹ The government did not provide the necessary capital for the peasants who had acquired lands and did not create a sufficient infrastructure in the rural regions to assist new landowners in managing the land.¹⁰ As a result, the agricultural sector's production declined drastically and Iran became a net importer of agricultural products.

A large part of the White Revolution was a drive towards modernization (viewed by the Shah as obtaining Western technology), both in agriculture and in industry. In the later phases of land reform Western equipment and technology were brought into Iran. Unfortunately, according to Nikki Keddi, this equipment and technology were inappropriate for Iran's soil and were improperly used.¹¹ As a consequence of this and of the overall restructuring of the agricultural economy Iran's agricultural system was badly damaged. During the second and third phases of land reform, very few peasants could make a living off the land, so they migrated to the cities. This phenomenon and its consequences will be examined later.

Muhammad Reza Shah also pursued a policy of settling the nomads, concurrent with his land reform policy. The nomads were

⁹ Pesaran, 29.

¹⁰ Milani, 86.

¹¹ Keddi, 163.

not settled through force of arms but instead were deprived of their livelihood. Nomadism was not considered "modern" in regard to economic and political considerations and as such was to be eliminated. "Land reform may never have had primarily economic goals; a major aim was to cut landlord power and bring peasants and nomads under direct government control, and this was accomplished."¹² Bringing nomads and peasants under government control, and lessening the power of the landlords was designed to strengthen the Shah and to modernize the rural areas of the country. However, the restructuring eventually demonstrated that the traditional mode of production performed better than the 'modern' system because:

both farm corporations and agri-businesses are (at different levels) purely uninstitutional and ahistorical inventions, transplanted into a given social framework from the air. Both these 'modern' systems destroyed the technical characteristics and politiconomic relations of Iranian agriculture, and replaced them with completely alien and ill-adapted technological and institutional forms. ... If it is clear why an attempt to create traditional Iranian-type village units of production in California would fail absolutely, then it should be equally clear why the uncritical application of Californian institutions and technology to Iranian agriculture failed so miserably.¹³

In his desire to make Iran into one of the most powerful states in the world, the Shah chose inappropriate methods which damaged Iran rather than strengthening it.

¹² Keddi, 225.

¹³ Katouzian, 311.

In addition to land reform there were five other original points in the White Revolution. The second most controversial point following land reform was electoral reform. This included granting women the right to vote and to be elected to the *Majlis* (other reforms concerning women's rights would later be added, including changing divorce laws). The clergy in particular were opposed to this reform. In addition, there were points concerning the nationalization of woods and forests, and the creation of a 'literacy corps'. Finally, other economic reforms included the denationalization of state monopolies in order to finance the land reform programme and company profit-sharing for industrial workers.¹⁴ While these points were seemingly in the interest of the Iranian people, they were pursued only if they were perceived to be capable of strengthening the Shah's position, or at least not weakening it.

There was an early challenge to the White Revolution that came from neither the National Front nor the *Tudeh* Party,¹⁵ but from the religious community. This challenge was unsuccessful but it provided the ulama with a learning experience that would be invaluable in the 1979 revolution. According to Homa Katouzian, there were three religious tendencies that were part of the challenge. The conservative branch was against the land reform, women's rights', and against the potential power hegemony of the Shah. The anti-despotic group within the religious community was not opposed

¹⁴ Katouzian, 225.

¹⁵ These two groups had been strong in the early 1950's and were both still in existence, although their power had been seriously reduced.

to the spirit of the reforms, but was wary of the return of despotism and secularism (as under Reza Shah). The radical-democratic tendency consisted of advocates that identified with Musaddiq and the Popular Movement; they were opposed to the 1953 coup, its resulting dictatorship, and also to the threat of despotism.

Katouzian defines despotism as the monopoly of both absolute and arbitrary power. She states that it destroys any functional distinction between the social classes, because it turns everyone into an object of the state.¹⁶ As a result of this fear of despotism the religious community spearheaded a movement against the regime. This movement gained momentum in the holy month of *Muharram* and on 6 June 1963, massive riots broke out all over Iran. The Shah ordered troops to "shoot to kill" and the massacre continued for three days. There is no proper estimate of the number killed, but the best guess is that the country as a whole had to have lost a minimum of at least two thousand.¹⁷ At the time of the uprising the Shah was in a powerful position, both militarily and politically, and was able to quickly meet the challenge. The uprising was not purely religious, nor did it come from only a single religious tendency; it was an insurrection of the people against the state, which happened to be led by the clergy. The common denominator was anti-despotism - as it would be in the 1979 Revolution.

¹⁶ Katouzian, 227.

¹⁷ Katouzian, 227-28.

Migration to Urban Areas

As suggested previously, the second and third phases of land reform did not provide adequately for many peasants; as a consequence of the land reform policies and of growing urbanization, many peasants migrated to the cities for jobs. The modernization program the Shah was pursuing was bringing in industry and the job market was broadening, especially in urban areas. In fact, Iran experienced a labor shortage; but the jobs available were mostly for skilled and semi-skilled labor. The vast majority of the migrating peasants had no training for these available jobs and consequently many were unemployed.

Between 1962 and 1971, more than two million Iranians migrated from towns to the cities. Following 1973, eight percent of the rural population left for cities each year.¹⁸ The increasing share of the population that migrated to the cities is shown below.

Urban Share of Iran's Total Population

<u>Year</u>	<u>Percentage</u>
1956	31%
1966	38%
1975	45%
1980's (expected)	60%

The figures above are based upon figures given by Charles Issawi.¹⁹

¹⁸ Hossein Bashiriyeh, *The State and Revolution in Iran, 1962-82* (London and Canberra: Croom Helm Ltd., 1984) 88.

¹⁹ Charles Issawi, "The Iranian Economy 1925-1975: Fifty Years of Economic Development," in *Iran Under the Pahlavis*, George Lenczowski, ed. (Stanford, CA: Hoover Institution Press, 1978) 138.

This massive urban migration contributed to numerous problems besides the previously mentioned unemployment. A serious housing shortage developed in the cities, particularly in Tehran. In addition, housing prices and living costs skyrocketed. This must be considered in addition to the loss of agricultural sufficiency that accompanied the changes in technology and the land reform.

Some of the economic problems mentioned above were temporarily offset by the tremendous increase in oil revenues in the early 1970's. The Shah used part of the revenues to alleviate some material demands of the population. In this same period the Shah made a number of poor economic and political decisions. These decisions combined with environmental circumstances and eventually led to the downfall of the Shah.

Economic Growth in Iran

According to Homa Katouzian, the Shah combined pseudo-modernism, pseudonationalism and despotism. His dream, pursued by oil revenues and much to his detriment and the detriment of the Iranian people, was:

to 'modernize' the Iranian political economy by means of investing in heavy industry, creating a consumer boom through import-substitution consumer durables which would keep the well-to-do and the educated classes quiet, destroying traditional forms of agriculture and the nomadic way of life, which were both difficult to control politically and a sign of social 'backwardness', and importing the latest and most sophisticated technology so

that all the world would admit ... that Iran was on the road to becoming 'the Japan of the Middle East' ...²⁰

This dream was partially realized, due primarily to the incredible economic opportunities afforded by oil wealth. However, due to poor economic and political decisions, combined with circumstances both internal and external to Iran, the Shah's dream was not entirely realized and in fact, in his pursuance of this dream, he managed to lead his people to the point of no return, where the revolution became inevitable.

Up to the 1970's oil wealth had increased gradually. Then in 1973 oil prices quadrupled, due to OPEC, and this led to a sharp rise in oil revenues for Iran.

<u>Iran's Oil Revenues</u>	
1970	\$ 1.1 billion
1972	\$ 2.4 billion
1974	\$17.4 billion
1975	\$20.0 billion(estimated)

The figures above are based upon figures given by Charles Issawi.²¹

As the figures above demonstrate, Iran's oil revenues in 1974 were more than seven times that of 1972. The result of this tremendous increase in oil revenues was explosive growth in Iran's economy. In 1973-74 the real gross national income grew by 34 percent and in 1974-75, it grew by 42 percent.²² This incredible growth afforded

²⁰ Katouzian, 237-38.

²¹ Issawi, 137.

²² Issawi, 137.

Iran great economic opportunities, but it also resulted in severe imbalances in the economy.

For a short period in the 1970's Iran experienced the highest rate of industrial growth in the world.²³ Per capita income rose from \$180 per year in 1972, to \$1,521 per year in 1974/75.²⁴ Immediately following the 1973 oil boom, the Shah adjusted the total expenditure for the Fifth Plan (1973-78) to \$120 billion, \$100 billion of which was to come from oil revenues. Compared to the Fourth Plan's actual total expenditure of \$10 billion, this adjustment was astronomical. The Shah dictated this revision of the plan despite warnings from economists;²⁵ the oil market declined drastically a few years later, and the Fifth Plan was characterized by deficit spending.

During the 1970's, the Shah decided that the oil revenues be spent on a wide array of projects (the number of projects and the amount of spending exceeded the revenues by the latter part of the decade). These included expenditures on the infrastructure, education, ventures abroad, subsidies to various industrial projects, welfare projects, and heavy military outlays.²⁶ The table below, adapted from Massoud Karshenas, gives an indication of the expenditures of the regime between 1970 and 1976.

²³ Keddi, 162.

²⁴ Norriss Hetherington, 363.

²⁵ Bashiriyeh, 86.

²⁶ Gail Cook Johnson, *High-Level Manpower in Iran: From Hidden Conflict to Crisis* (New York: Praeger Publishers, 1980) 96-7.

Composition of central government consumption expenditure 1970-1977. (Percentages) ²⁷

	<u>1970</u>	<u>1976</u>
<u>General expenditure</u>	<u>68.9</u>	<u>68.1</u>
General administration	30.9	19.6
Military expenditure	38.0	48.5
<u>Specific expenditure</u>	<u>31.1</u>	<u>31.8</u>
Education	14.6	12.2
Health	4.2	4.5
Social welfare	1.1	1.7
Agriculture	2.5	6.6
Transport and communication	3.3	1.1
Miscellaneous	5.3	9.1
<u>Total</u>	<u>100.0</u>	<u>100.0</u>
(bn Rials)	(135.2)	(1170.0)

As can be seen from the table above, in the specific expenditure category, agriculture and the miscellaneous category benefitted the most.²⁸ Overall however, military expenditures increased the most dramatically, from 38.0 percent to 48.5 percent of the central government consumption expenditure between 1970 and 1976.

Iran's military expenditures rose drastically over the years of the Shah's reign. According to Mohsen Milani, defense expenditures rose from \$77 million in 1970 to more than \$7.8 billion in 1978. In 1973 Nixon promised the Shah he could purchase America's most sophisticated weaponry, with the exception of nuclear weapons.²⁹

²⁷ Massoud Karshenas, *Oil, State and Industrialization in Iran* (Cambridge: Cambridge University Press, 1990) 195.

²⁸ Agriculture expenditures mainly consisted of food subsidies, and the miscellaneous category included art and culture, physical education, manpower, urban and rural development, public utilities, commerce, mining and housing, environmental and regional development.

²⁹ Milani, 166.

Western eagerness to sell billions of dollars of military equipment to Iran each year was reinforced by the economic drain on the West caused by the OPEC price rise; arms purchases seemed a fine way to recycle petrodollars.³⁰

The military expenditures allowed American military suppliers like Grumman, Lockheed and Westinghouse to take over key positions in Iran's economy,³¹ and Iran became nearly totally dependent on petroleum as its source of foreign exchange. The economic growth that Iran experienced at this time was advantageous to some Iranians, but it could have been more beneficial to the population in general had economic policy been better planned.

The astronomical economic growth and the modernization scheme of the regime brought numerous jobs into Iran. The Fifth Plan anticipated a serious labor shortage, especially at the professional, skilled and semi-skilled levels. Jobs were mainly in industry, mining, construction and the service industry. Efforts were made to increase female employment and to upgrade the labor force through expanded education and vocational training.³² However, in general the Iranian population lacked the training for the kind of jobs that were being created. As a result, a large number of foreigners were hired to work in Iran, particularly in the developing industrial sector of the economy. Foreigners, particularly

³⁰ Keddi, 176.

³¹ Keddi, 176.

³² Issawi, 140.

Westerners, were paid much more than Iranians, and were given benefits that citizens did not receive and could not afford. This would later lead to growing resentment of foreigners in Iran and would be an issue in the 1979 Revolution.

A great amount of Iran's oil wealth was put towards rapid industrialization. Presented with great oil wealth and with domestic demand for consumer products as a result of these revenues, the Shah chose not to take the slower path of economic growth based on labor-intensive industry. Instead, industrial expansion was guided toward developing the capital-intensive oil industry first, and industries specializing in the manufacturing of consumer durables second.³³ The oil industry was developed first because it was believed that revenues would continue to increase and that this increase could be put toward continued modernization. Higher incomes and subsidized prices, resulting from increased oil revenues, led to increased consumption - while the population grew at a 3 percent rate, the demand for consumer goods rose by 12 percent annually.³⁴ In response to this demand, not only was industrialization aimed at producing consumer goods, but a policy of trade liberalization was also adopted. In 1974, the government introduced a wide liberalization on imports; the most popular imports included food products, textiles, refrigerators, gas cookers, water heaters, furniture item, television sets, radios, and

³³ Johnson, 95-6.

³⁴ Bashiriyeh, 101.

automobiles.³⁵ Many of the trade restrictions and high-rate tariffs adopted in the 1960's were lifted and/or reduced and certain exchange controls were removed in 1974.³⁶ Problems resulted from both the rapid industrialization and the liberalization of trade, including state maldistribution. Income gaps widened throughout the country, including between the rich and poor, and between the city and the countryside.

The rapid growth of non-oil exports was a major goal of Iran's trade policy, but the "government's export-promotion activities were inadequate and ineffective."³⁷ Iran's economic foundation narrowed instead of broadening; this meant that if and when problems developed in the oil export sector, Iran would be unable to rely on other areas to balance those problems out. In the 1970's oil strength and rising prices were uppermost in the Shah's mind. The government's concern with this internal balance overshadowed the goals of export promotion. The share of the oil and gas sectors in the total government revenues rose from 55 percent in the Fourth Plan to approximately 78 percent in the Fifth Plan, and their share in total current foreign exchange rose from 76 percent in the former plan years to 85 percent in the latter.³⁸ This open door to trade and its consequent sharp rise in imports, along with rapid industrialization, led to dependency.

³⁵ Kavoussi, 458.

³⁶ Bashiriyeh, 87.

³⁷ Kavoussi, 459.

³⁸ Pesaran, 33.

Iran became dependent on the single-commodity export of oil (particularly for foreign exchange), and on the international capitalist economy, especially for imports. In turn, the increase of imports added to the huge bottlenecks the country was experiencing.³⁹ In addition, the country also became increasingly dependent on foreign technology and expertise; the growing foreign presence and the high wages paid to foreigners added to the problems of housing scarcity and increasing costs of living that Iran experienced at this time. Dependence on foreign trade and skill allowed for exploitation. For example, the Shah signed an agreement with the United States which stated that if an American committed a crime on Iranian soil, it was up to the US, not Iran, to punish that crime. The lack of any serious efforts at non-oil export expansion or import substitution in Iran's industrialization played a large role in this increasing dependence. It is probable that if either one of these policies had been successfully pursued, Iran's economy would not have fluctuated with the changing oil market. Diversifying the economic foundation through incremental steps would have meant slower modernization, but it would have also allowed Iran to train its citizens, thus reducing reliance on foreign workers, and to broaden its revenue base beyond dependence on petrodollars. Eventually, Iran was characterized by overwhelming dependency, inflation, exaggerated income inequality, and unbalanced growth.

³⁹ For example, the storage and transportation of food items that needed refrigeration was inadequate and consequently food rotted before it reached the Iranian consumer.

Economic Problems

A relationship of dependency was developed between Iran and the West, especially the United States. According to Galtung's theory of structural dependency, the international sphere is characterized by core/periphery relations, in which developed states function as the core and developing states are considered the periphery. In addition, within states there is a core/periphery relationship between the elite and the masses. Galtung's theory is quite useful in examining Iran during the 1970's. Iran was dependent on the sale of oil revenues on the international capitalist market and on the West for a variety of imports, including food and intermediate goods for its industries. By the time the oil market slowed down in the mid-1970's, Iran was already tied to the West. In order to continue the modernization program that the Shah envisioned, it was necessary to sign trade agreements with the West, especially the U.S., wherein Iran agreed to recycle its petrodollars by buying a large amount of Western goods in exchange for loans and special deals.

At the same time, there was also a core/periphery relationship within Iran. The Shah and the rest of the elite within the state made up the core, while the non-elite made up the periphery. Iran thus fit Galtung's model of internal imperialism; the state-society relationship was one in which the society was subordinate to the state. The state controlled the economic sector to a high degree through state capitalism, and the distribution of wealth was also controlled by the state. The results of this structural dependency (both internal and external) were exploitation and uneven development. Iran, as a part of the periphery in the international

scheme, was exploited by West.⁴⁰ In addition, despite the Shah's vision of a "modern" Iran, the country remained underdeveloped, and internally was characterized by uneven development. The rural areas were left far behind the urban sectors, and the lower and middle classes were not incorporated into the political structure. Iran's dependency on the superpowers and its uneven internal growth were two of the factors leading to the revolution.

As discussed above, the oil boom led the Shah to direct revenues to be spent on a wide array of projects. The Fifth Plan assumed more oil money would be incoming each year. In 1974-75 oil revenues dropped sharply and the government faced a deficit of \$1.7 billion.⁴¹ At the same time, higher incomes and subsidized prices resulted in increased consumption and demand. Where the population grew by a 3% rate, the demand for consumer goods rose by 12% annually, and consequently inflation rose rapidly.

Comparative Inflation Figures, 1973-77

	<u>Official</u>	<u>Kayhan</u>
Compound	93.8%	200%
Annual Ave.	18.0%	50%

The above figures were obtained
from Hossein Bashiriyeh.⁴²

⁴⁰ Iran imported goods that were inoperable and was still forced to pay for them, and often had domestic policy dictated by the U.S. government.

⁴¹ Bashiriyeh, 101.

⁴² Bashiriyeh, 101.

Despite the wide discrepancy, the above figures demonstrate the high inflation rate Iran experienced in these years. Price increases surpassed wage increases. The cost of living index shot up - in 1973/74 it went up by 11.2%, in 1974/75 it went by 15.5%, and it continued to climb in following years.⁴³ Accompanying the inflation and the resulting increases in the cost of living were widening income gaps.

Income gaps widened in all major dimensions in Iran, particularly after 1974. According to Nikki Keddi, the gaps between the top and bottom of the income ladder, between the city and the countryside, within the city and within the countryside, all widened. Iran still had money, but primarily the rich were subsidized.⁴⁴ Looking at the figures for the shares of national consumption in the year 1976, it is seen that the top 10% of the Iranian population enjoyed more than one-third of the country's consumption. Conversely, the lowest 10% of the population only accounted for 2-3% of the country's consumption.⁴⁵ During the 1960-70's, the poor in Iran did not get necessarily poorer, but the vast increase in the wealth of the rich and the conspicuous consumption of the elite was seen all around. Overall, the poor may have gained materially in these years, but they perceived themselves as becoming worse off in

⁴³ Issawi, 137.

⁴⁴ Keddi, 174.

⁴⁵ Norriss S. Hetherington, "Industrialization and Revolution in Iran: Forced Progress of Unmet Expectations," *Middle East Journal*, Vol. 36, no. 3, (Summer 1982) 364-65.

relation to others. This, along with little upward mobility led to increasing vocal discontent.

The poor were not the only ones left behind by the elitist social order that remained despite the Shah's ambitious modernization plan; the expanding middle class was also frustrated due to the lack of any serious political reform. Limited upward mobility and little prospect for economic improvement in the lower and middle classes was prevalent. According to Gail Cook Johnson, the continued backwardness of both public and private institutions resulted in the failure of industrialization because it did not integrate the emerging educated middle and working classes.⁴⁶ Actually, it is better to characterize this not as the failure of industrialization, but to view it in terms of modernizing society without concurrently working towards political development. The Shah wanted all the technology and expertise that could be brought in from the West, and he also even wanted some of the Western social characteristics, but he did not want any change in the political order that would result in a lessening of his power.

The Shah believed that he could make Iran one of the top five powers in the world by the twenty-first century. He increased the educational standards and the literacy rate of Iran over the 1960's and 1970's. The number of universities was increased and the quality of education was improved. More people received a university education, although it was still a small portion of the population, and this led to the expansion of the professional middle

⁴⁶ Johnson, 95.

class.⁴⁷ While improvements in education, especially Western style education, were viewed by the Shah as indispensable to modernization, he failed to realize that these same educational improvements would lead to discontent among the middle class. Students came out of the universities expecting good jobs, assuming the education they received was adequate for placement. However, the vast majority educated in Iran were limited to the lowest managerial positions, which underutilized their skills, while the foreign-educated, unless they were very well-connected, also did not find rewarding career paths.⁴⁸

The professional middle class was not only frustrated by the limited opportunities in the job market; it was also disappointed by the lack of political participation allowed it. The emerging middle class was given little if any decision-making authority, despite its' increasing expertise. The Shah was not willing to co-opt these people into the political structure. Mobilization was encouraged, but participation in actual political decision-making was very limited. The modernization of Iranian society and expanding education brought expectations of political development that the Shah was not willing to fulfill. In fact, the majority of the Shah's opponents that were imprisoned and/or executed between 1972-76 were middle class professionals.⁴⁹ Iranian politics came to be dominated by

⁴⁷ It must be noted that as with many developing nations, ascriptive rather than meritorious standards were used for recruitment to positions of authority.

⁴⁸ Johnson, 98.

⁴⁹ Hetherington, 364.

repression rather than co-optation. This was a major factor that contributed to the revolutionary environment in Iran in the latter years of the 1970's. The revolution, it can be argued, was primarily motivated by the intelligentsia of the middle class who wanted fundamental change, but could not realize it without turning to the clergy to motivate the masses.

The Shah further alienated the population by changing Iran from a two-party system (*Mardom* and *Iran Novin*), to a single-party system (*Rastakhiz*). In the mid-1970's the economic crisis (mainly a result of the sharp drop in oil revenues) affected the foundations of the regime and prompted the emergence of a short-lived political phenomena, wherein a new single political party, the *Rastakhiz* or National Resurgence Party, was imposed on Iran in an attempt at mass mobilization, particularly of the lower classes. The apparent motivation was to check the growth of "industrial feudalism", the signs of working class unrest, and the inadequacy of the ruling party to incorporate diverse interests and needs. What emerged was a populist attempt, based on some redistributive measures, but which did not make adequate changes.⁵⁰ The new party had no notable economic impact, but did carry potential for political conflict.

The Revolution

By 1977, the economic recession, inflation, urban overcrowding, government policies hurting the bazaari classes (repression of small

⁵⁰ Bashiriyeh, 90-91.

businesses), glaring income gaps, conspicuous Western-style consumption by the elite, a large foreign presence (and influence), and lack of political freedom and participation were all widely felt throughout Iran. In response to spreading economic discontent and to soften growing international criticism of his regime, the Shah appointed Jamshid Amuzegar to the position of Prime Minister and initiated a liberalization program. Amuzegar initiated a deflationary program that resulted in an increase in unemployment. According to Nikki Keddi, this increase in unemployment and other elements of the economic recession that Iran experienced in the late 1970's came after the expectations of the Iranians had been raised, and this created a classic pre-revolutionary situation.⁵¹

Other authors offer variations on this primarily economic "theory" of revolutions.⁵² Gail Cook Johnson states that the government had to convince the populace to accept the fact of slower growth and to lower their heightened expectations; the government's repressive measures and policies that maintained unbalanced growth led to social revolution.⁵³ In addition, Hossein Bashiriyeh offers the Davies theory of revolution, which is also an economic theory. This theory argues that the combination of rapid economic growth followed by sudden economic decline drives the population into a revolutionary "state of mind". Bashiriyeh states that this generation

⁵¹ Keddi, 177.

⁵² These lack validity as theories since the unidimensional focus on economics cannot account for other factors that have been essential to revolutions.

⁵³ Johnson, 97.

of economic discontent on a mass scale, in addition to the emergence of some conflict of interest between the state and the upper class, the revolutionary mobilisation of the masses, the occurrence of political alliance between diverse forces of opposition and wavering of the regime's foreign support all combined to produce the revolution.⁵⁴ Here, Bashiriyeh moves beyond the unidimensional economic argument and provides a more complete understanding of the causes of the revolution.

Another argument that has been applied to the Iranian Revolution is that it was modernizing too quickly and that the Iranian people and the clergy did not want to modernize.

The "anti-modernization" thesis, however, is extremely misleading and fails to explain why the revolution occurred in the late 1970's rather than in the two previous decades when the Shah initiated and accelerated his program of economic modernization. It also fails to explain why a number of leading mujtahids tacitly cooperated with the Pahlavi regime until the late 1970's.⁵⁵

Modernization, defined in terms of man developing his abilities to control the environment, was not the cause of the revolution. The Westernization and the absence of political development in terms of satisfying demands were more instrumental factors in the building of the revolutionary fervor.

⁵⁴ Bashiriyeh, 84.

⁵⁵ James A. Bill, "Power and Religion in Revolutionary Iran," *Middle East Journal*, Vol. 36, no. 1 (Winter 1982) 26.

According to Mohsen Milani, the Iranian revolution was a complex phenomena that involved numerous factors. Some of the primary factors leading to the revolution, according to Milani included:

- 1) political repression and the failure to build institutions
- 2) organizational and mobilizational capabilities of discontented groups
- 3) Davies theory that revolutions occur when a period of prolonged economic development is followed by a sharp reversal, which generates relative deprivation and unfulfilled expectations
- 4) the weakening of the link between dependent nation (Iran) and its main foreign supporter (U.S.)
- 5) the broad coalition forged among the opposition forces, which united divergent groups
- 6) the ideology of Shi'ism, which justified the struggle against the Pahlavis, united groups and promised a bright future, and
- 7) failure of the Shah's regime to repress the opposition⁵⁶

Milani has examined the Iranian Revolution in detail, and suggests that the complexity of this revolution has been underestimated. He suggests that the revolution occurred partially as a result of the modernization strategy of the Shah. The modernizing of Iran created a pervasive dualism in the economy and the culture, because it was incapable of destroying the traditional sector. In addition, it was

⁵⁶ Milani, 30.

characterized by uneven development of the economic and political systems - the former was modernized without changing the nature of the latter. Finally, the modernization drive had a narrow base of support and lacked a solid, supporting ideology.⁵⁷ The Shah continued in his push to modernize, alienating a large portion of the population, while at the same time he failed to effectively counter the opposition. He considered the nationalistic and communistic tendencies to be his greatest threat so he sought to secure the support of the lower classes through economic growth and concessions.

This strategy was based on the Pollyanna belief that the lower classes and the conservative ulama were an effective deterrent against the menace of the intermediary groups, ... The regime was thus unprepared to cope with the threats of the traditional forces believing, as it mistakenly did, that they were destined to be crushed beneath the wheels of progress. Consequently, the Shah's entire intelligence network allocated most of its resources to combating communism and nationalism of the Mossadeq type, thus giving the Islamic forces ample opportunity to expand and mobilize.⁵⁸

By the time of the revolution, Iran had experienced incredible economic growth, which was followed by a rapid decline as a result of the bust in the oil market in 1976-77. The Shah had already overspent, despite warnings from economic advisors, because he had counted on increasing revenues. The expectations (economic, social

⁵⁷ Milani, 127.

⁵⁸ Milani, 122.

and political) of the Iranian people had been heightened, and then the regime was unable to meet those expectations. Instead, repressive tactics were increasingly employed (there are suggestions that the Shah's secret police force, SAVAK, sometimes acted without his consent). Tensions mounted and certain events became turning points that made the revolution inevitable.

The strength of the opposition increased with these events. They included the peaceful rally in Qom, organized by the ulama because of a newspaper attack on Khomeini; this later resulted in bloody confrontations between government forces and ulama supporters in seven cities after the police violently put down the first rally. Another event which aided in the building of the opposition was the Tabriz uprising. A commemoration of martyrs was planned to take place in Tabriz but the government ordered police to block people from entering the mosques. Some protestors were killed and hundreds more were arrested; in response, protests in other cities sprung up and more people were killed. Consequently, the forty-day commemorations to the honor the dead became increasingly more politically potent.⁵⁹

A third critical event in the development of the revolution was the burning of the Cinema Rex in Abadan in August, 1978. More than four hundred people who had been locked in the theater were killed. The masses believed the government set the fire to discredit its opponents. The entire country was ignited by hatred and the

⁵⁹ Milani, 191.

government was forced into a defensive position.⁶⁰ Finally, on 7 September 1978, demonstrators refused to obey the curfew set by the government and the police opened fire on the crowd. In what has become known as Black Friday, there was no certain death count - the government stated there were 86 dead, but unofficial estimates are as high as 3,000.⁶¹ Soon after these events, strikes and more demonstrations erupted all over the country. By the Autumn of 1978 it should have been apparent that there was more than an uprising going on in Iran, there was a revolution.

The political and economic decisions of the Shah's regime combined with a variety of environmental circumstances contributed to the revolution. The land reform program of the 1960's alienated a portion of the population, in addition to destroying the agricultural economy. It also caused a large number of peasants to migrate to the urban areas, where employment was difficult to find. In large part the migrating population became urban slum dwellers. The June 1963 uprising, which was organized by the ulama, was staged to protest a number of the reform programs of the White Revolution. The uprising was brutally repressed, but it provided the ulama with a lesson that would prove to be valuable in the 1979 revolution. The White Revolution has been taken as the starting point of the discontent and frustration that was to lead to the 1979 revolution.

The 1970's saw a continuation of some of the reforms started in the previous decade. This decade also saw a tremendous increase

⁶⁰ Katouzian, 344-45.

⁶¹ Milani, 193.

in oil revenues for Iran, followed by a slump in the oil market. The quadrupling of oil prices in 1973 brought revenues into Iran that the Shah spent on a wide array of projects. Modernization and industrialization were pursued. The Shah believed that the oil money would continue to increase and that he could make Iran one of the top five powers in the world using this projected revenue. The Shah ignored economic advisors who told him to choose a strategy that would allow for slow sustained growth, and instead he opted to pursue a path focused on oil wealth and military strength. The year 1976 witnessed the beginning of the oil slump that severely damaged Iran's economy. Iran had gone into deficit spending and the Shah was unable and/or unwilling to make the economic and political changes necessary to save his regime. By the time he was willing to compromise it was too late. A multigroup coalition had formed in opposition to the Shah's regime.

The coalition was formed by a number of groups, including the *Tudeh* communist party, the liberal nationalist groups that had evolved from the National Front Party of the 1950's, the Islamic-Marxist guerrilla group known as the Mujahedin, and the ulama who were divided into at least two groups, one being the fundamentalists who followed the Ayatollah Khomeini. The groups other than the clergy did not have the organizational skills necessary to unite the masses against the regime to overthrow it. What united all these groups was the hatred of the Shah and the desire to unseat him. This unifying factor was enough to bring about a revolution, but what followed was disagreement over how the new system should

function. Each group had its own ideas for the new government, but eventually Khomeini and the fundamentalists overcame the others.

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THE KHOMEINI DECADE

This chapter examines Iran in the first decade of the post-revolution period. The political economy of this country changed in many ways, but it was not entirely transformed. The monarchy was changed to a theocratic system, and the new regime focused on ideology to the exclusion of practically everything else for quite some time. Positions were obtained in the regime through loyalty to the revolution and Islam, rather than technical expertise or skill. The economic system was also somewhat transformed. Usury was determined to be unlawful and numerous industries were nationalized. However, the nature of state capitalism that had existed under the Shah had meant a high degree of state control of the economy, and the nationalization program under Khomeini meant similar control. Private property remained intact, despite the ideas of some of the more radical elements in the new regime, and promised land reform was very limited. The political economy of the new regime (and thus the development), while perceived by many as very different than that of the Shah, in fact, contained a number of similarities.

Despite high hopes coming out of the revolution, political development did not progress as quickly as many had hoped. Throughout the first decade of the post-revolutionary period the

leadership had difficulty providing basic necessities for the masses. There were housing shortages and many staple food items, such as rice and sugar, were rationed. As will be seen in this chapter, economic growth was practically stagnant and the leadership often resorted to the use of repressive measures against any opposition. Higher positions in the regime were generally available only to those who held clerical positions and had proved their loyalty to the revolution. Participation for the masses was limited to voting in elections that generally offered very little choice. In the beginning, Khomeini and the rest of the ulama offered Islam as an ideology that promised utopia.

However,

Khomeini's early promise - that submission to God would create a just society at home, empower Iran to defeat external oppressors and reunite the Islamic world in a new power bloc - was largely unfulfilled.¹

If political development is viewed as the capacity to respond to the needs and demands of the people, the worsening economic conditions and the political repression employed during Khomeini's reign would indicate that the leaders did not deliver and thus political development did not progress at the pace that many expected. The decisions of the leadership of Iran and the environment within which the leadership functioned largely shaped the political economy and the consequent political

¹ Robin Wright, *In the Name of God: the Khomeini Decade*, New York : Simon and Schuster, 1989, 207.

development. This chapter examines that environment and the those decisions and their effects on development.

The Political Environment

The mass demonstrations, strikes by industrial and oil workers, bazaaris, civil servants and bank employees had the maximum disruptive effect on the Shah's regime. By December, 1978, the crisis-ridden regime was close to the point of collapse and in January 1979,

most major economic sectors had come to a complete halt; oil exports had practically stopped, the banking system was non-functional, only a few large industries remained operative, channels of distribution were clogged, and services had dropped significantly.²

The multiclass coalition that had come together to overthrow the Pahlavi regime finally forced the Shah and his family out of Iran in late January, 1979.

The revolution was in part a rejection of existing models of development and a search for a different, "indigenous" path of development.

The existing socialist and capitalist models were dismissed for their inappropriateness in building an Islamic society, where concerns for traditions and culture are to be integrated into the political economy. Moreover, as noted by President Hashemi Rafsanjani, "Western capitalism" is "unjust and exploitative," while "Eastern communism" "kills private initiatives" and

² Hooshang Amirahmadi, *Revolution and Economic Transition: The Iranian Experience* (Albany, New York: State University of New York Press, 1990) 90.

"instigates antagonism between the state and the populace."³

Not only was the revolution a rejection of capitalist and socialist models of development, it also involved a rejection of the despotism of the Shah, economic frustration and opposition to the emphasis on Westernization of the regime. The final choice of an Islamic system of development was not unanimously endorsed by the various members of the coalition, but it emerged as the dominant option, mostly due to Khomeini's popularity and the fundamentalists' growing power. The Islamic model was also appealing because it "demanded national independence, respect, and equal treatment in the world system."⁴ The primary problem of using Islam as a model of development is that it, like any other model, cannot give all the specifics needed for development, nor can it promise success. Islam does not give a comprehensive framework for political and economic systems and their functioning. The Quran provides certain rules and guidelines and the lives of the Prophet and his followers are taken as examples, but there are still wide areas of ambiguity and ideological dispute. Consequently, disagreements regarding political, economic and social issues arose following the establishment of the Islamic Republic, many of which are yet to be resolved.

The period immediately following the revolution and the Shah's departure from Iran was marked by a struggle for political

³ Amirahmadi, 114.

⁴ Amirahmadi, 29.

power. The Shah had appointed Shahpour Bakhtiar, a former member of the National Front, as Prime Minister in late December, 1978. Bakhtiar hoped to establish a social democracy similar to some in Western Europe, but by the time he came to the position he lacked a popular support base (he had been deserted by his former colleagues of the National Front), and the struggle between his government and the fundamentalists (the revolutionary clergy following Khomeini) ended with the military command withdrawing their support from Bakhtiar and consequently removing the last basis of Bakhtiar's power.⁵

Upon Khomeini's return to Iran on February 1, 1979, he declared Bakhtiar's government illegal and "promised to quickly announce the formation of a provisional revolutionary government to prepare the ground for the establishment of an Islamic republic."⁶ Ayatollah Ruhollah Khomeini was one of the primary figures in the revolution. Khomeini had been a critic of the Shah since the early 1960's. In June 1963, Khomeini had attacked the Shah in a passionate oratory, claiming that the regime was opposed to Islam and to the existence of the religious class. Khomeini was arrested and spent ten months in jail.⁷ His continual criticism eventually led to his exile from Iran, where he was able to vocalize his opposition to the Shah even more.

⁵ Robert Graham, *Iran: The Illusion of Power* (New York: St. Martin's Press, 1980) 48.

⁶ Mohsen Milani, *The Making of Iran's Revolution: From Monarchy to Islamic Republic* (Boulder and London: Westview Press, 1988) 230.

⁷ Wright, 50-51.

Eventually, Khomeini was recognized as probably the most tenacious opposition to the Shah.

As discontent grew stronger in the late 1970's, Khomeini encouraged revolt from his exile in Iraq, and then from France. Tapes of Khomeini's speeches speaking out against the monarchy were shipped from France to Iran, and played at Friday prayer meetings. Khomeini was identified by many within the traditional lower and middle classes as a humble and pious clergyman. Other groups in the coalition against the Shah, especially the liberal nationalists, believed that Khomeini would serve the purpose of rallying the masses to revolt, and then he would return to his existence as a simple religious teacher, probably in Qom. There were a number of factors that allowed Khomeini to take over the revolution. He represented strong, charismatic leadership, juxtaposed to the Shah's indecisiveness. His genuine charisma came from his impassioned eloquence and his absolute sense of righteousness. Khomeini was a great communicator; he appealed to the masses on a level they understood. In addition, he employed an ideological framework that dated back thirteen centuries. These factors gave the revolution legitimacy and forcefulness that the other groups of the coalition were unable to provide.⁸

It is perhaps the extraordinarily simplistic approach of Khomeini that helped to make his ideas so attractive. All that was needed, he stated, was "conviction and ethical solutions"; it is only then that the country could

⁸ Wright, 58-59.

achieve "prosperity and mental exaltation and solve its social problems."⁹

Contrary to the ideas of the other groups within the coalition, Khomeini did not return to his simple life as a religious teacher. Instead, he became the leader of Iran for more than a decade. For years he had written of *Vilayat-i faqih*, or "leadership of the jurisprudent." This neo-platonic theory proposes that an Islamic republic be established, in which the ulama (clerical establishment) is considered the proper body to interpret laws and guide society, and that the most learned ayatollah should be the final voice in this republic. When the revolution ended and the country was left to choose its leadership, Khomeini's charisma combined with the organizational abilities of the ulama created a constitutional theocracy in Iran that has lasted far longer than many believed possible.

Apart from Khomeini's leadership abilities and charisma, one of the most important factors in the ulama's gaining of power after the revolution was its organizational abilities. Unlike the other groups in the coalition against the Shah, the ulama had a built in network from which to rally the masses. The clergy had continual contact with the masses through the mosques and were able to influence the masses because of the centrality of religion. Khomeini's fundamentalist network primarily consisted of his religious students that had become clergymen with their own mosques throughout the country. During his exile Khomeini

⁹ Haleh Afshar, "The Iranian Theocracy," *Iran: A Revolution in Turmoil*, Haleh Afshar, ed. (Albany, New York: State University of New York Press, 1985) 225.

maintained contact with a number of these students and during the revolutionary buildup he sent messages to these mujtahids who in turn relayed them to their congregations at Friday prayer meetings. Shi'ism as a centuries-old ideology had a stronger hold over the people than the slim offerings of the other groups in the coalition. The clergy became the power broker during and after the revolution because of its ideological connection to the masses and its organizational network. The other groups did not offer a strong alternative nor did they have the link to the masses. However, the triumph of the fundamentalists was not simply realized with Khomeini's return to Iran, but was a slow process that took nearly two years.

Within a short time of his return Khomeini asked Mehdi Bazargan to head the provisional revolutionary government (PRG) until a new constitution could be drawn up and elections could be held. At the same time, paralegal organizations created by the fundamentalists during the revolution were increasing their power. The formation of the PRG and the continuing existence of the paralegal organizations of the fundamentalists (such as the Revolutionary Guard, the *komitehs* and the Islamic Republic Party) created a dualism of power in Iran. Milani refers to the paralegal organizations of the fundamentalists as a "state within a state." Immediately following the revolution there was a struggle for power between the fundamentalists, the Islamic liberal nationalists and the secular liberal nationalists; soon, however, the fundamentalists defeated the nationalists and by 1983 the

fundamentalists had secured power.¹⁰ According to Milani, the consolidation of power by the fundamentalists occurred over four years, in six discernable stages:

- 1) the fundamentalists created a state within a state through the paralegal organizations, which weakened the power of the PRG
- 2) the constitutional basis for a theocracy was laid
- 3) the new constitution was passed (defeating the orthodox ulama and the secular nationalists)
- 4) the fundamentalists defeated the Islamic nationalists
- 5) the Cultural Revolution was launched and the Mojahedin's violent threat was neutralized, and
- 6) Consolidation of power was completed and Islamization of the society was continued.¹¹

These six stages were not systematically planned by the fundamentalists in their search for power, but were adopted as the need arose.

The paralegal organizations of the fundamentalists developed into strong institutions over time. The power struggle between the PRG and the Revolutionary Council, formed by Khomeini and the fundamentalists, developed into a struggle between President Abol Hasan Bani Sadr (who became president with Khomeini's support following Bazargan's resignation) against the Islamic Republic Party (IRP). The IRP and other paralegal

¹⁰ Milani, 240.

¹¹ Milani, 240.

organizations consolidated their power and became governmental institutions within a short period of time. Neither Bazargan nor Bani Sadr had the popular support base to neutralize the paralegal organizations and to strengthen their own governmental institutions.

During this same time period a constitutional basis for a theocracy was created. In March 1979, a referendum was held which asked voters - "Do you favor an Islamic Republic or a monarchy?" No other choices, such as a social democracy, were given, and the government claimed 98.2 percent of the more than 15.7 million votes were cast for an Islamic Republic. The result was that May 1, 1979, was declared the first day of the "Government of Allah on Earth." The PRG drafted a constitution and elections were held for an Assembly of Experts (AOE) to revise the constitution. The fundamentalists won many seats in the AOE and thus gained a great deal of strength. The AOE was given three months to revise the constitution, which in the end turned out to be a very different version than the one submitted by the PRG.¹²

The final draft of the constitution consisted of 12 chapters and 175 articles. The constitution abolished monarchy and created a unique presidential system. In addition, the constitution revolved around the concept of the *Vilayat-i faqih* or "leadership of the jurisprudent." The position of the *faqih* (jurisprudent leader) is understood to have unlimited power, no term length

¹² Milani, 261-62.

limitations and the divine authority to rule, which means he may intervene in the affairs of any branch of the government. The constitution recognized Khomeini as the *faqih* and designated that his replacement would be either a single individual or a three to five member council. In addition, the constitution adopted an official foreign policy of nonalignment.

The constitution not only covered the structure of government and the foreign policy, it also incorporated an Islamic vision of social justice. In general terms the constitution promised to achieve independence, uproot poverty and fulfill human needs. More specifically, the goals of the constitution included: securing basic needs for all, including housing, food and health care; securing full employment for all; providing opportunities for self-improvement of individuals; preventing profiteering from the labor of others; prohibiting monopolistic, speculative and usurious dealings; forbidding extravagance in economic matters; learning from experts in science and technology; preventing foreign economic dependence; and achieving self-sufficiency in production of food and industrial products.¹³ In addition, Article 44 of the constitution divides the economic system into three sectors - public, private and cooperative. The constitution was written in the Summer and early Fall of 1979, and disputes arose immediately, particularly regarding the *Vilayat-i faqih*. Despite

¹³ Amirahmadi, 114.

the disagreements a referendum was held and the Constitution of the Islamic Republic of Iran was adopted on 3 December 1979.¹⁴

Following the adoption of the constitution, the new government concentrated on defeating its remaining opponents. Early on the regime used purges to "Islamize" the state. Purges were used to clean out the armed forces (2,000-4,000 men were purged, mostly due to suspected coup plots), the National Front (also suspected of coup plots) and the state bureaucracy.¹⁵ In addition to eliminating these threats, the regime also concentrated on possibly the worst threat to the regime, the left-wing guerrilla group known as the Mojahedin.

The Mojahedin is an opposition group which developed a three-phase strategy to overthrow the Khomeini regime. The Mojahedin first intended to destabilize the regime through eliminating key figures and exposing the regime's vulnerability.¹⁶ Second, the group chose to directly confront the regime through demonstrations and strikes, hoping to mobilize the masses. Finally, the Mojahedin believed that mass uprisings would come about as a result of the first two steps and that these would bring the government toppling down. The elimination of key figures and the demonstrations took place, but the third step did not

¹⁴ Amirahmadi, 114.

¹⁵ Milani, 288.

¹⁶ Hundreds of officials and guardsmen were killed in assassinations and bombings in this first phase.

materialize. The government met the opposition with executions, violent suppression and terror for more than eighteen months.¹⁷

Because of their miscalculation, the Mojahedin's violent encounter with the Islamic Republic produced the exact opposite of what they had hoped to realize: It proved the invulnerability of the Islamic Republic to guerrilla warfare, exposed the weakness of the opposition in general and the Mojahedin in particular, invigorated the Islamic Republic's security system, and further solidified the fundamentalists' position.¹⁸

The government responded to the Mojahedin and other opposition with violence and suppression. The violence and terror reached a peak in 1981/82, and then at the end of the latter year, it began to wane. Influenced by some of the more moderate elements within the regime, Khomeini issued a declaration to curb the worst excesses of the revolutionary organizations responsible for the violence against the opposition. The declaration banned entering homes, making arrests, conducting searches, and confiscating property without legal authorization. The revolutionary organizations were reigned in, but their authority was by no means taken away.¹⁹ The revolutionary organizations were some of the primary support bases of the regime, and Khomeini was not about to alienate them.

¹⁷ Shaul Bakhash, *The Reign of the Ayatollahs: Iran and the Islamic Revolution* (New York: Basic Books, Inc., 1990) 228.

¹⁸ Milani, 299.

¹⁹ Bakhash, *The Reign of the Ayatollahs*, 229.

The final step in the fundamentalist clergy's struggle was the consolidation of power. After Bazargan resigned as head of the provisional government, Aboul Hasan Bani Sadr was elected as the first president, primarily because he was backed by Khomeini. His term lasted less than a year and then Khomeini accepted his resignation (there had been disagreements between the two, particularly over the American hostage situation). Following Bani Sadr's resignation, the Islamic Republic Party was able to gain strength, particularly during the elections of October, 1981. Islamic Republic Party candidate, Ali Khamenei, was elected president and other IRP candidates won the Prime Minister and Interior Minister seats. Many appointed positions were also replaced with IRP men, even down to the township and district levels.²⁰

Consolidation of power, institution building, and Islamization of the society by the fundamentalists in the first four years of the Islamic Republic proceeded simultaneously with the elimination of their opponents.²¹

The consolidation of power by the fundamentalists was not entirely a smooth path, however. Opposition groups, particularly the Mojahedin, managed to inflict serious wounds to the regime, especially through assassination of key figures, and the fundamentalists themselves were divided over a number of issues. The factionalism that developed among the

²⁰ Bakhash, *The Reign of the Ayatollahs*, 224-25.

²¹ Milani, 304.

fundamentalists has presented obstacles to forming policy since the Islamic Republic was created, and is still problematic over a decade later.

One of the key elements to understanding the political economy of Iran during the Khomeini years is the international environment and Iran's foreign policy within that environment. In the first years of the regime, the foreign policy pursued was based on militant Islam, nationalism, regional ambitions, the war with Iraq and the slogan of "Neither East nor West." Iran was trying to establish independence and to pursue a policy of nonalignment as far as the superpowers were concerned. In actual policy Iran attempted to export the revolution, particularly to other Persian Gulf countries, to establish and maintain distance from the superpowers, and to better relations with the Third World and Europe.²²

The American Hostage Crisis

One of the most important events in the Islamic Republic's foreign policy was the American hostage crisis. On 4 November 1979, looking for a pretext to force the Shah out of the U.S. and to oust the liberals (Bazargan and the PRG) from the revolutionary government, a previously unknown group calling itself the Students Following the Line of the Imam (SFLI), occupied the American

²² Bakhash, *The Reign of the Ayatollahs*, 217.

Embassy in Tehran and held 52 American's hostage. The hostages were held for more than a year. The U.S. reactions over this time period included a failed rescue attempt and more successful economic sanctions against Iran. The U.S. froze Iranian assets in the U.S. valued at almost \$12 billion, it imposed trade embargoes against Iran which Western Europe and Japan also imposed, and it manipulated the international oil market through Saudi leverage. Iran was still quite dependent on the capitalist world economy in general (for food items and industrial inputs) and on oil production and sales in particular, and consequently the U.S. economic sanctions were very damaging to Iran. Both Bazargan and Bani Sadr tried to convince Khomeini to allow them to take over the hostages and to resolve the situation, but Khomeini refused and declared that it would have to wait until the *Majlis* (parliament) was elected and could resolve the conflict. This particular dispute weakened both Bazargan and Bani Sadr, and was a primary cause of both of them leaving office.

After the *Majlis* elections and more than a year of the hostages being held, the situation was finally resolved by the Algerian Accord. In exchange for the release of the hostages the U.S. agreed to not intervene in Iran's internal affairs and to prevent the hostages and their families from bringing lawsuits against the Iranian government. The U.S. also promised cooperation with the Islamic government in bringing lawsuits in U.S. courts to extradite the Pahlavi family's wealth. Finally, the U.S. released frozen Iranian assets; \$7.98 billion was transferred to Iran's escrow account in the Bank of England, while \$3.67

billion was transferred to New York Federal Reserve to cover Iran's debts to American banks.²³

The results of the hostage crisis and its resolution for Iran were both advantageous and damaging. The accord was entirely negotiated by the more radical elements within the Iranian regime which gave ammunition to the more moderate elements in their power struggle. In addition, the hostage situation was disadvantageous to Iran and its government because the U.S. sanctions badly damaged the country's economy and it hurt relations with countries other than the U.S.. The taking of the hostages made it difficult for the new regime to get any support at the international level, especially when Iraq attacked Iran in 1980. Conversely, the hostage crisis also held advantages for the new Iranian regime. The fundamentalists were able to weaken the provisional government during the crisis and were able to consolidate their own power. Also, the new regime was perceived internally as capable of humiliating a superpower, especially after the failed U.S. rescue attempt, and consequently its image and power was strengthened. The U.S. hostage situation is only one dramatic example of how intertwined foreign and domestic policy are in Iran. The factionalism that developed in the regime is interrelated with both these policies and they all affect one another in policy-making and power struggles.

²³ Milani, 289.

Factionalism and Economic Policy

While the fundamentalists were able to eliminate the opposition and to consolidate their own power, the individuals within this group were not entirely in agreement on a number of issues. Factions developed regarding particular issues and individuals shifted between categories depending on where they stood regarding single issues.

Almost immediately after the Revolution, a *dislocation*, or *noncorrespondence*, developed between the leadership and its ideology, leading to ideological factionalism within the state. This dislocation occurred when the core middle-class leadership faction tried to present a *middle-class* interpretation of the *cross-class* and universal Islam. Others within the power bloc, however, disagreed and forwarded alternative radical (lower-class) and conservative (upper-class) perspectives.²⁴

Amirahmadi's description of the factionalism that developed is open to criticism; especially problematic are his classifications according to socioeconomic standing and his failure to point out that individuals did not always stay within one category, such as radical, but shifted according to the issue. However, he is correct in pointing out that there are three main factions that have developed and rivaled for power in Iran since the revolution.

Various labels have been applied to these factions, some more accurate than others. One of the factions has been referred to as the conservatives or *hojati-yes*. The conservatives believe in less government intervention in the economy, free enterprise, the

²⁴ Amirahmadi, 98.

sanctity of private property and in moderation in the export of the Islamic Revolution and in foreign policy.²⁵ The core support for the *hojati-yes* are wealthy merchants, landlords and some high-ranking clergy. The conservatives also oppose public planning, state ownership and state management of the economy. They are against cooperatives and planned industrialization. Conservatives favor the development of agriculture and the expansion of services. This faction opposes land reform, the increase of direct taxes, limits on the private sector and policies against profiteering. However, while this group is in favor of a more open economy (the conservatives do not seem to want many changes from the economy operated under the Shah), it can also be quite culturally impermissive and ideologically strict.²⁶

Ironically, the conservatives have been referred to as liberals in some of the literature (this may be because they are in favor of liberal economic policies, i.e. free trade, which are conservative in the sense that they are a continuation of the status quo from the Shah's regime). In addition, some writers refer to this faction as non-interventionist. Non-interventionists believe that the unregulated "Islamic" market economy, relying on the private sector, is best for economic growth. Government intervention should only be a last resort and should only be

²⁵ Milani, 305.

²⁶ Amirahmadi, 118-21.

temporary.²⁶ Regardless of what title is applied, this faction experienced its peak of power immediately following the revolution, from 1979-81. During the leadership terms of Bazargan and Bani Sadr, the conservatives (or *hojati-yes/liberals*) were able to block some of the major socioeconomic reforms, that others tried to pass. Even after their most powerful period during the first two years of the new regime, the conservatives were able to maintain some strength in the government, particularly through positions in the Council of Guardians.

The second faction that developed in the Islamic Republic has typically been referred to as the radicals, or the *maktabis*. The radicals favor centralized economic planning, nationalization of major industries, limits on private property, aggressive export of the Islamic Revolution, and minimal relations with the United States. Their arguments generally focus on social justice and redistribution of wealth. Their support comes primarily from the lower and lower-middle classes, along with many of the revolutionary organizations.²⁸ The radicals, or *maktabis*, advocate public ownership and management of large enterprises and nationalization of foreign trade. However, they are not entirely against free markets or small private holdings. The radicals advocate major land, tax, and socioeconomic reforms. In addition, they are sympathetic to agriculture, for consumption

²⁶ Ali Rahnama and Farhad Nomani, *The Secular Miracle: Religion, Politics and Economic Policy in Iran* (London and New Jersey: Zed Books Ltd, 1990) 256.

²⁸ Milani, 305.

not export, and are opposed to the expansion of the service sector of the economy. Radicals have been characterized by their goal of self-reliance and their confrontational foreign policy, particularly in regards to the U.S. and the war with Iraq.²⁹

After weakening the conservatives in 1981, the radicals became the dominant faction within the regime and maintained their strong position until 1984/1985. They were particularly powerful in the *Majlis* (Iranian parliament). The radicals pursued the war with Iraq, refusing to consider a cease-fire or resolution until Saddam Hussein of Iraq was removed as the president of that country. In domestic policy, the radicals tried to push through land and tax reforms, but the laws were often struck down by the more conservative Council of Guardians, a council responsible for ensuring that laws did not violate the principles of Islam. The constitution, which was adopted in 1980, had several articles that justified socioeconomic reforms and land reform. The *Majlis* pushed through a Law for the Transfer and Revival of Land but Khomeini suspended it due to the upheaval that was caused by suggestion of any land reform. In addition, the radicals tried to increase direct taxation and tried to persuade the wealthier individuals in Iran that they should voluntarily pay more in religious taxes. However, the tax system in Iran lacks a strong collection history and very little was changed by the radicals. In their years in power, the radicals were more influential in foreign policy and cultural issues than they were in

²⁹ Amirahmadi, 18-21.

the economic sector. The radicals had the misfortune of being in power when Iran experienced some hard times, particularly setbacks in the war, and as a result they were blamed for many of Iran's problems and their power was weakened.

The third and final faction is often called the pragmatist or moderate faction. This group falls in between the other two and it is led by the current president of the republic, Hashemi Rafsanjani. The pragmatists seek to find a compromise between a laissez-faire and a state interventionist economy. The pragmatists/moderates advocate a mixed approach to the economic system. They believe in a controlled market economy, guided and regulated by state planning and limited public ownership and management, with a complementary role played by privately organized cooperatives. The pragmatists find their support base among a wide range of classes and institutions. The newer middle-class, the technocrats and a number of the religious "intelligentsia" are supportive of the moderate faction.³⁰ The pragmatists defend oil-led industrialization as the proper basis for rapid economic growth and advocate controlled free trade and guarded openness to the international economy. They are generally less ideological than the other two factions and more flexible in their interpretation of Islamic law.

The pragmatists began to gain power through Khomeini's support in 1984-85 and have generally been the dominant faction since that time. The setbacks in the war with Iraq and the

³⁰ Amirahmadi, 118-21.

economic problems that Iran was facing at that time under the radicals convinced Khomeini to support the pragmatists in their policies. The pragmatists believed that Iran had to procure weapons and parts for its American-built systems if it was going to continue its fight against Iraq. It was the pragmatist faction that was responsible for the arms-for-hostages deal, which temporarily renewed Iran's relationship with the U.S. as its arms supplier. In addition, the pragmatists have tried to turn the economy around and move it toward rapid growth, focusing on a strategy of improving trade relations, especially with other developing nations, Europe and Japan. The postwar proclamations by Khomeini supported the policies of the moderates, particularly his endorsement of factionalism and his call for a limited market economy and controlled free international trade.³¹ The pragmatists have managed to stay strong since the cease-fire with Iraq and since Khomeini's death, but their power may suffer the same deterioration that the other factions faced. It all depends on the circumstances of the time.

Whereas radicals are unfortunate to have held power during a period of general economic decline, conservatives are having a difficult time defending a more or less *a la Shah* model that failed to benefit the majority. Under these circumstances, the centrists (pragmatists) are finding it easier to defend a mixed approach.³²

³¹ One of the only exceptions to Khomeini's pragmatic leanings at the end of his rule, was the Rushdie incident, in which he declared that Salman Rushdie's book *Satanic Verses* was blasphemous and that the author should be assassinated for his anti-Islamic writing.

³² Amirahmadi, 124.

Most of the members of the three factions that hold positions within the regime come from traditional middle class backgrounds. However, the ideological conflicts within this middle class leadership are often mistaken for interclass political conflicts.³³ In addition, it is difficult to label an individual as belonging to a specific faction, since individuals shift depending on the issue. For example, a person may be regarded as a radical when the issue of private property is raised, but he may be considered a pragmatist in regard to openness to the international economy and foreign relations. As with any country adjusting to life after a revolution, there are questions of how to best approach the political and economic systems. In Iran, the shift in political power among the factions can generally be identified with periods of economic changes.

As following sections will demonstrate, there was a general decline in the economy, especially after 1984 when the recession began. As a result, those in power, the radicals, were hurt politically, and the power shifted to others, the pragmatists:

This new mood of pragmatism did not imply political liberalization, a deemphasis on Islamic orthodoxy, or greater tolerance for political opposition ... Rather, the new mood suggested a desire by the religious leaders to restore economic and administrative order and a readiness on their part to allow the technocrats to look after the economy, while the clerics retained power,

³³ Amirahmadi, 118.

controlled politics, saw after ideology, and made basic decisions.³⁴

The political economy of Iran following the revolution up until Khomeini's death was affected by a number of factors and underwent various political, economic and social changes. However, it is important to understand that up until his death Khomeini was the final arbiter in the republic, due to his charisma and his position as *faqih*. Apart from Khomeini, other factors that have affected the political economy of Iran include the dispute over land reform, the economic structure and policies adopted, oil policy and the war with Iraq.

Land Reform

Land reform has been a particularly divisive issue in the Islamic Republic. With the revolution and the breakdown of civil authority following the revolution, land seizures began to take place in the countryside. The three groups which initiated these seizures include the revolutionary government and its organizations, the landlords and the peasants. Mostly the peasants seized land early on: "They were spurred on by the breakdown of authority and the absence of landlords, and Khomeini's call on the farmers to plant extensively in the first year of the Islamic Republic."³⁵ The seizures led to extensive battles within the government over the sanctity of private

³⁴ Bakhash, *The Reign of the Ayatollahs*, 231.

³⁵ Bakhash, *The Reign of the Ayatollahs*, 197.

property versus the social justice of redistribution of wealth. In general, two government institutions represented the two sides of land reform: the *Majlis* generally argued for land reform and redistribution, whereas the Council of Guardians struck down reform measures in favor of the right to private property.

In September, 1979, the provisional government received approval of the Revolutionary Council for a Law for the Transfer and Revival of Land. The bill was very limited in nature, and basically left the private sector untouched. Then in 1980, the constitution was approved, including articles providing legal justification for more extensive land reform. Following this, a huge dispute broke out and Khomeini ended up suspending the land reform bill and the articles on land reform.³⁶ The suspension resulted in havoc across the countryside, since seizures and distribution had already begun.

Then again in December 1982, another land reform measure was approved by the *Majlis*, only to be struck down a short time later. The measure did not aim at redistribution, but at ensuring more extensive leasing under forms of contract, such as sharecropping, rental and partnerships. Landlords were allowed to hold up to three times (in some cases four times) the size of an average family farm and were allowed to lease the rest of their holdings, giving children of landlords priority. However, in January, 1983, the Council of Guardians struck down this measure

³⁶ Bakhsh, *The Reign of the Ayatollahs*, 200.

for violating Islamic and constitutional principles.³⁷ Land reform attempts continued to go back and forth in the government, leaving a legacy of disputes.

The doctrinal and constitutional disputes over land and property remained unresolved. Because of unauthorized seizures, laws approved and then suspended, very large amounts of land remained in dispute between landowners and villagers, private citizens and the government.³⁸

The ideological dispute revolves around the question of whether Islam weighs more in favor of private property or social justice (meaning redistribution of property and other wealth). Islam recognizes both, but the government of Iran has not been able to find an acceptable balance between these two. In practice, it is difficult to find this balance in most societies. Khomeini, as the *faqih*, had the power to make a final decision on the matter but he chose instead to vacillate between the two sides, never satisfactorily deciding the matter. Had he made a decision, there is no certainty that his choice would not have weakened his power and led to instability in Iran. There were many reform efforts on the part of the *Majlis*, but almost all of them were defeated by the Council of Guardians.

One exception to this pattern is the Temporary Cultivation Law of 1986. In October of that year, the *Majlis* approved a bill to transfer ownership of so-called "temporary cultivation

³⁷ Bakhash, *The Reign of the Ayatollahs*, 209-10.

³⁸ Bakhash, *The Reign of the Ayatollahs*, 211.

agricultural land" from owners to cultivators who had actually been working the land. The land seizures that followed the revolution created widespread disorder and landlord-peasant disputes. In order to deal with these problems the Supreme Judicial Council issued a decree in 1980, leaving the cultivation of disputed lands in the hands of those who had cultivated the land the previous year. This arrangement was renewed each year and the land was referred to as temporary cultivation land. By 1986, the regime had to face the pressure of settling the status of these lands, so they passed the temporary cultivation law.

In its final form, the law provided that ownership of agricultural land throughout the country, which as of March 20, 1981, was in the hands of the non-owner cultivators, would be transferred permanently to the cultivators, provided they were landless or land-poor, lacked an adequate source of income other than agriculture, and were resident in the locality.³⁹

The law was by no means aimed at a comprehensive redistribution of land; rather, it was passed to settle the status of the particular lands that fell under the category of temporary cultivation lands. In fact, landowners were still allowed to keep some land if they were considered "needy" (sometimes this amounted up to three times the amount of land considered necessary for maintaining a rural family).⁴⁰ Nevertheless, the law

³⁹ Shaul Bakhash, "The Politics of Land, Law, and Social Justice in Iran, " *Middle East Journal* 43 (Spring, 1989) 190.

⁴⁰ Bakhash, "The Politics of Land, Law, and Social Justice in Iran," 191.

still revived the whole argument of private property versus social justice, which in all probability could only have been resolved by Khomeini, but was not.

Khomeini, it turned out had spoken in favor both of social justice and of a strict interpretation of Islamic law. He had denigrated the large landowners as exploiters of the peasantry and also warned against unlawful attacks on private property, had approved the 1980 land reform law and then suspended it, had sided at times with the Council of Guardians and the narrow interpreters and at other times with the Majlis and the broad interpreters on matters of property and Islamic law ... Khomeini's rulings and views, in other words, although considered authoritative, lent themselves to varying interpretations.⁴¹

Khomeini was cryptic not only when it came to land reform, but also regarding other issues. His support of the political factions varied, as did his stand on economic questions, such as the degree of state versus private control that Iran should adopt. In describing Khomeini's political style it has been said that he would "go with the wind." When a controversy arose in the republic, Khomeini would usually wait to see which side would emerge as stronger and then would go with that side. While he can be criticized for not taking more decisive stands on certain matters, it may be that his choice not to step in and personally resolve problematic questions may have contributed to his power; whereas if he had taken one side of a controversial matter, he may have been weakened. If he had made a number of

⁴¹ Bakhash, "The Politics of Land, Law, and Social Justice in Iran," 198.

unpopular decisions, rather than avoiding conflict, he might have weakened his own position.

The Economy of the IRI

The economy of Iran, during the ten years that Khomeini guided the country, was characterized by both dependency on the international capitalist economy, and by an active state role and policies that suggest economic nationalism. As will be further examined later, Iran has been unable to fully break its dependency and become entirely self-reliant, as was hoped in the beginning of the new republic. Iran is highly dependent on its oil sales on the capitalist world market for foreign currency, which it depends on for the imports it desperately needs, the most important of which is food. One example of Iran's dependence on the world oil market is seen in the years following 1984, when the world experienced an oil glut and oil prices declined rapidly; Iran's economy was hurt and the recession which the country was entering was intensified. At the same time, the new government was still insisting that it was possible for Iran to become self-reliant and was adopting policies that were protectionist in nature; thus, the rhetoric and the policies were suggestive of economic nationalism. The economy of the Islamic Republic was affected by a number of factors during its first ten years, including the economy inherited from the previous regime, the structure and policies that the new government adopted, the international environment, oil production and price, and the war with Iraq.

The revolutionary government inherited some staggering economic problems from the Shah's regime. Months of strikes had reduced the government's revenues (i.e. oil exports, customs duties, etc.). By the time the provisional government came to power, the treasury was nearly empty and the government ended up having to print money in order to survive. In addition, the banking system was near collapse, due to massive withdrawals, huge capital flight, and many outstanding loans which would never be repaid. The departure of nearly all the foreign technicians meant numerous incomplete projects were abandoned. Finally, the Shah and his government had drawn up a \$47 billion budget for 1979-80, with a projected deficit of \$15 billion; Iran had already begun to accumulate a deficit before the new government even had a chance to take over.⁴²

Conversely, there were some economic advantages inherited. The oil industry, despite months of strikes, was still relatively intact. In addition, foreign exchange reserves (prior to the hostage crisis) were not insignificant, totalling \$13 billion.⁴³ Finally, the foreign debt which the new government inherited was relatively small. However, these advantages were not enough to outweigh the problems the economy was facing:

The crisis was, ... , symptomatic of an economy characterized by deep dependency on oil and imports, lopsided development across its social, sectoral, and spatial components, disarticulated relationship between

⁴² Bakhash, *The Reign of the Ayatollahs*, 175-77.

⁴³ Bakhash, *The Reign of the Ayatollahs*, 177.

its consumption and production systems and among economic sectors, and asymmetrical integration with the capitalist world system.⁴⁴

The clergymen coming to power were adept at mobilizing the masses, but they had very little experience in dealing with national economic problems.

In addition to these problems, Iran also had a poor export to import ratio. According to World Bank figures, between 1973 and 1983, Iran had "an average yearly negative rate of exports of about 17 percent and an average positive rate of imports of about 3.5 percent."⁴⁵ These figures represent a deterioration in terms of trade for Iran. The ten year span overlaps both regimes, so the poor record cannot be blamed solely upon the IRI. The poor trade ratio indicates that Iran is dependent on imports which it has not balanced out through exporting its own goods.

As examined previously, factionalism developed within the regime almost immediately after the Shah was overthrown; this factionalism was primarily caused by differences of opinion regarding the economic system. Recalling the descriptions of the radicals as opposed to the conservatives, the main difference between these two is their position concerning the role of the state in the economy. Factionalism has prevented any consistency in economic policies and has blocked the formation of any comprehensive development strategy. As a result, this has had a

⁴⁴ Amirahmadi, 21.

⁴⁵ Shahrough Akhavi, "Institutionalizing the New Order in Iran," *Current History* 86 (February 1987) 56.

negative impact on the economic performance of the country. Lacking specific goals and strategies for the economic development of the nation, the Islamic Republic leadership has focused on solving immediate problems. Looking to Islam and the Quran, the leaders have found some guidelines, but the Quran is not an economic treatise and it is subject to a wide variety of interpretations. This has led to a lack of unified positions and frequent policy reversals. Khomeini himself, the final interpreter, was consistently vague in his interpretations regarding economic matters. In order to properly analyze the economic performance of the IRI, it is important to examine the structure and policies adopted since 1979.

The initial goals of the new government were economic self-reliance, a restructuring of consumption patterns and realizing social justice.⁴⁶ The structure of the economic system was divided into three sectors by the Constitution of the IRI. The first is the public sector. Included in the public sector (meaning state controlled) are all major industries, foreign trade, major mines, banking, insurance, power production, dams and major water-carrying networks, radio, television, postal, telegraph and telephone services, and air/sea/land/railroad transport. The second sector is the private sector of the economy. Portions of agriculture, animal husbandry, industry, trade and services which supplement the activities of the other sectors are included here. The final area is the cooperative sector. This includes cooperative

⁴⁶ Amirahmadi, 163.

(private and public) companies and organizations in both rural and urban areas.⁴⁷ These three sectors were designed to complement one another and lead to economic growth, but instead there have been political and ideological conflicts and practical difficulties concerning the divisions.

The policies adopted by the regime have varied. Overall, the policies seem to fall under the heading of economic nationalism. Economic nationalism is a strategy in which the state plays an active role in promoting domestic economic growth and development. A major component of the policies of economic nationalism is protectionism. Economic nationalism advocates an entirely different position from liberalism - whereas the former encourages state control and regulation the latter demands the least government intervention possible.

The new regime in Iran adopted several policies increasing the state's role in the economy, particularly during the period when the radicals were the dominant faction.

the government took over large sectors of the economy through nationalization and expropriation, including banking, insurance, major industry, large-scale agriculture and construction, and an important part of foreign trade. It also involved itself in the domestic distribution of goods. As a result, the economic role of the state was greatly swollen and that of the private sector greatly diminished by the revolution.⁴⁸

⁴⁷ Amirahmadi, 114-15.

⁴⁸ Bakhash, *The Reign of the Ayatollahs*, 166.

The nationalization of large sectors, control of domestic distribution of goods, limitations on imports and subsidizing certain industries and goods are all indicators of an active state role in the economy and thus of economic nationalism. A further analysis of the policies adopted and of their effectiveness will indicate that the leadership of Iran did not go all the way in adopting economic nationalism as part of its strategy for economic development, and that some of the policies it chose were inappropriate for the nation.

The new government nationalized banking, insurance and most of the industry within the country. Industry that fell within one of three categories was brought under the ownership and management of the state: (1) "heavy" industry - metals, automobile assembly, chemicals, shipbuilding, aircraft manufacture and mining; (2) industries owned by fifty specifically named individuals and one family, who allegedly acquired their wealth through influence with the Shah's regime; and, (3) industries facing economic difficulty, whose liabilities exceeded their net assets.⁴⁹ In addition, large amounts of property were expropriated illegally by revolutionary organizations that evolved into government institutions, such as the Foundation for the Disinherited.

The leadership not only took ownership of large sectors of the economy, it also placed controls over various areas. Foreign trade was brought under strict control, and debate raged over

⁴⁹ Bakhash, *The Reign of the Ayatollahs*, 179-80.

whether it should have been nationalized. In addition, price controls were placed upon numerous areas.⁵⁰ Sometimes the government would subsidize certain producers/merchants to balance out the price controls, but often there were no subsidies. The new regime was not entirely consistent with the policies it chose. Protectionism is generally geared toward "infant industries" in order for them to develop and flourish, so that they may be competitive on the world market. However, Iran did not adopt a comprehensive policy for protecting specific industries and expanding its exports. The leadership seems to have decided that state controls would be the best thing for the economy, but then they did not move far beyond this decision in addressing economic growth and development.

The government plays a strong role in distribution, production, export and import of goods. "According to one Iranian economist, some 68 percent of the total labor force worked for the public sector in 1983."⁵¹ As with many other developing nations this is an indication of the weak private sector. Similar indicators of government control can be seen by looking at other figures. For example, nationalization and expropriation by the end of 1982, resulted in the Iran National Industries Organization controlling between 500 and 600 industries, and employing more than 150,000 people. The Foundation for the Disinherited, an arm of

⁵⁰ Patrick Clawson, "Islamic Iran's Economic Politics and Prospects," *Middle East Journal* 42 (Summer 1988) 379-80.

⁵¹ Milani, 308.

the government, shows similar figures. During the same time period, it was in charge of:

- 1) 200-300 factories
- 2) 100 construction companies
- 3) 150-200 commercial firms
- 4) 91 poultry, livestock and agricultural enterprises, and
- 5) 90,000 employees⁵²

The degree of state control over economic sectors is extensive, but the state has not played the role of the intelligent entrepreneur. It has controlled the economy, but it has not helped it grow significantly.

Not only has the state controlled various industries, it has also limited foreign trade, in order to avoid foreign debt. The figures for civilian non-oil imports, between 1981 and 1986 are given below:

<u>Year</u>	<u>Civilian Non-Oil Imports</u>
1981 (early)	\$16 billion
1981-82	less than \$10 billion
1982-83	\$11.8 billion
1983-84	\$18.1 billion
1984-85	\$13.6 billion
1985-86	\$12.4 billion

The above figures were taken from Patrick Clawson's article entitled "Islamic Iran's Economic Politics and Prospects."⁵³

As indicated by the figures above, imports were significantly decreased between 1981 and 1983, then they were increased for

⁵² Bakhash, *The Reign of the Ayatollahs*, 184.

⁵³ Clawson, 381-82.

one year, then decreased again. The marked increase in 1983-84 is due to the improved standing in the war with Iraq at that time and the improvements in the oil market. Neither factor could be sustained for very long however, and consequently, imports were restricted in the following years. Iran is a country that is quite dependent on imports; it does not produce a sufficient amount of food to feed its population and its industries are dependent on imports for raw materials and intermediate goods. Thus, the restrictions on imports were successful in avoiding foreign debt, but at the same time, they were damaging to industrial growth.

In addition to nationalizing various economic endeavors, expropriating certain properties, and controlling or limiting numerous areas of the economy, the new government of Iran also started subsidizing the costs of basic needs items, especially food, in order to mitigate rapidly rising prices and declining real income. Inflation had risen so high that many families were spending a majority of their income on food alone. The government found itself in the position of spending practically all its income on current needs and very little on development of projects aimed at modernization and economic growth. "By the end of 1987, the share of current expenditures rose to 82 percent of the general budget, while that of development expenditures declined to 18 percent, an extremely unhealthy budgetary allocation."⁵⁴ Annual budgets have been adopted instead of national planning and leaders have generally limited themselves

⁵⁴ Amirahmadi, 166.

to coping with immediate problems, without looking to future development.

The active state role of the new regime was adopted, at least in part, in order to promote economic growth and development. The initial goals of the regime included self-reliance and achievement of social justice. In order to achieve these goals, the new leaders chose many strategies reminiscent of economic nationalism. However, they did not entirely adopt economic nationalism. Factionalism has prevailed in the Islamic Republic, and as such, a mixture of approaches has been adopted for the political economy, rather than a single comprehensive approach. If economic nationalism had been fully adopted there is no evidence that it would have been any more successful than the mixed approach that was inadvertently taken. The general idea of economic nationalism and protectionism is to subsidize the creation of an infrastructure and to promote home industry and the export of manufactures. This is designed to allow "infant industries" to flourish and to increase domestic economic growth. The Islamic Republic seems to have the same goals as economic nationalism suggests, but it does not have a comprehensive plan for reaching these goals (nor does economic nationalism lay out the exact strategies a state must choose in order to be successful). The new leaders wanted to expand exports beyond oil, but this did not materialize. They limited imports in order to reduce foreign debt, but they were unable to substitute domestic products in place of the limited imports. In addition, the domestically produced goods and imports maintained were often

consumer products rather than durable goods. Finally, the goal of enhancing national power, which is considered incompatible with foreign control over important areas of the economy, was inherent in the slogans and philosophy of the IRI, but it encountered practical difficulties. The factionalism which has dominated the political economy of Iran has meant differing economic philosophies have competed for dominance, but no single approach has won.

This mixture of approaches has led to mixed results. According to Shaul Bakhash, the result of nationalization was not so much redistribution of wealth and increase of economic opportunity, but rather, the fattening of the "already overfed leviathan - the government."⁵⁵ The economy has sustained severe damage over the years, but at the same time, the regime has lasted for more than a decade, surviving the poor economy and the war with Iraq, without any serious threats to its authority. In fact, the factionalism within the regime has been more troublesome than most outside attempts to gain power. One of the most important controversial issues within the regime revolves around the degree to which the state should control the economy. Just as land reform brought up the question of social justice (intervention) versus private property, so do other economic sectors raise the issue of social justice and state intervention versus free enterprise and nonintervention in the economy. During his rule, Khomeini made proclamations regarding the

⁵⁵ Bakhash, *The Reign of the Ayatollahs*, 184.

economy, but these did not provide the other leaders with a final solution.

Khomeini's intervention did not resolve the issue of the relationship between the private and public sectors or the underlying question of how social justice is to be achieved under an Islamic republic. The proponents of private enterprise and state control, private property and distributive justice, and narrow and broad interpretations of Islamic law confronted one another over virtually every major piece of economic legislation.⁵⁶

Final answers to these debates may never be found. Within and outside of Iran, people will debate the merits of various policies regarding state intervention in the economy. The mixture of approaches has resulted in mixed performance, which has various indicators.

Of the indicators used to judge the economic standing of a nation, probably the most used is Gross Domestic Product (GDP). Gross Domestic Product is the market value of all goods and services produced in final form by residents of a nation. The GDP of Iran has been fluctuating since 1976, generally falling into three periods. From 1977 to 80, there was a sharp decline in GDP, followed by strong growth from 1981 to 83, then another sharp decline from 1984 to 87. The strong growth during the period of 1981 to 83 is mostly due to the improved oil market and the increased revenues Iran experienced during this time. Over the entire period of 1979-87, the GDP of Iran registered an annual

⁵⁶ Bakhash, *The Reign of the Ayatollahs*, 248.

growth rate of -0.7 percent.⁵⁷ The negative growth rate has meant financial problems for the general population, and for the middle-class in particular. The table below gives figures for gross domestic product between 1977 and 1984.

Gross Domestic Product in constant 1974 prices (billions of rials)								
	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>
Agriculture	340.9	352.6	356.3	362.9	404.0	436.0	429.0	446.7
Oil and gas	1,363	929.8	767.6	330.5	273.6	526.8	531.1	452.5
Industries	645.6	553.9	511.9	520.2	534.5	590.7	683.1	705.1
Services	1,753	1,620	1,560	1,475	1,504	1,546	1,833	1,871
GDP	3,922	3,266	3,070	2,568	2,639	3,040	3,417	3,421
Per capita GDP (1000 rials)	112.9	91.3	83.25	67.53	67.31	75.17	81.98	80.0
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As the chart indicates, there was a large decrease in oil and gas and in the industrial sector between 1977 and 1981, which then experienced a slow increase. In addition, the service sector saw a decline, but then in 1983/84 made a strong recovery. Overall, the GDP and the per capita GDP showed a similar decrease in the immediate post-revolution years and then somewhat increased; however, none of the increased figures were enough to match the 1977 pre-revolution figures. According to Amirahmadi's examination of Iran's GDP, "Per capita GDP has declined by 47 percent (in 1974 prices) between 1979 and 1987, at an average

⁵⁷ Amirahmadi, 133-37.

⁵⁸ Rahnema and Nomani, 280. The above chart is a modified version of that given by Rahnema and Nomani.

rate of 5.2 percent per year."⁵⁹ This decline has reduced the purchasing power of the middle and lower classes, and has blurred the line between them. According to some scholars, Iran has become a two-class society consisting of the rich and the poor, with the middle-class having virtually blended into the lower-class. The poor performance in the GDP is an indicator of the declining economic power of the country.

In addition to GDP, the Gross Domestic Expenditure (GDE) has also declined in post-revolutionary Iran. The average annual GDE showed a 15.9 percent decline (at fixed 1974 prices) during the 1979-86 period, when compared to the figure for the 1976-78 period. In addition, the overall GDE indicator averaged an annual growth rate of -0.3 percent for the 1979-86 period.⁶⁰ This is even more significant when inflation over the years is taken into account (meaning prices are higher, so the same expenditure amount buys fewer goods). The decline in both production and expenditure are general indicators of decreasing economic capability. An examination of the expenditures on consumption as opposed to productive investments demonstrates more clearly the declining economic performance of Iran. In 1985, the percentage of GDE that went to *consumption* was 71.8 percent (as compared to 64 percent in 1976). In 1985, the percentage of GDE that went to *investment* was 18.5 percent (as compared to 31 percent in

⁵⁹ Amirahmadi, 194.

⁶⁰ Amirahmadi, 155.

1976).⁶¹ While figures for other developing and developed countries are similar, this nevertheless represents a definite decline in Iran's investment since the previous decade, and due to Iran's reconstruction needs increased investment is one of the highest priorities.

Gross Domestic Fixed Capital Formation (GDFCF) is the investment in domestic capital generally geared toward infrastructure and production. GDFCF includes among other things, investment in machinery, construction, manufacturing and mining. As the figures discussed above, regarding consumption and investment suggest, the drop in gross domestic fixed capital formation (GDFCF) has been disproportionately higher than the drop in GDE, meaning a higher share of GDE is going to consumption and largely nonproductive savings. The GDE has shown a growth rate of -0.3 percent for the 1979-86 period, whereas the GDFCF has demonstrated a -8.5 percent growth rate.⁶² What this indicates, is that the drop in the GDFCF is disproportionately higher because the share of expenditures being made into investment and production are declining at an even faster rate than GDE is declining. Both the public and the private sectors have decreased investment, particularly in construction

⁶¹ Amirahmadi, 156. The figures for Iran's investment versus consumption are similar to those of other countries. According to statistics from the Europa World Year Book, consumption and investment figures for several countries for 1985/86 are: Argentina - consumption 86 percent, investment 13 percent; Egypt - consumption 83 percent, investment 15 percent; France - consumption 80 percent, investment 19 percent; and Japan - consumption 70 percent, investment 28 percent.

⁶² Amirahmadi, 154.

and machinery, especially since the beginning of the recession in 1984. This decline in investment and increase in consumption demonstrates an unhealthy budget that is not planning for future economic growth.

The decline in the post-revolutionary GDFCF is due to a number of factors (which are also partially responsible for the lack of significant growth in Iran's overall economy). Included among these factors are the declining oil revenues, the war with Iraq, private capital flight, the establishment of revolutionary institutions (increased public spending and increased consumption), the lower profit rates and longer turnover times in productive sectors (which has deterred many from investing in productive areas), and the unsettled political environment.⁶³ In summarizing the economic difficulties which Iran faced after the revolution, Shaul Bakhash wrote:

The government's economic problems were exacerbated by the war with Iraq, an inflated and inefficient government sector, the erosion of private sector confidence, the drop in both private and public sector investment, and a steep decline in oil revenues.⁶⁴

The economy of Iran, as has been demonstrated through this discussion on its structure, policies and performance, has not achieved the goals set out by the post-revolutionary leaders; self-reliance and social justice do not yet characterize Iran. While self-reliance was an often mentioned goal of the republic in the early

⁶³ Amirahmadi, 161.

⁶⁴ Bakhash, 245.

years, with the pragmatic faction gaining power, the focus has been shifted to self-sufficiency, rather than self-reliance. One of the primary blocs to achieving significant economic growth (and thus working closer towards self-sufficiency and social justice) has been the declining oil market. Iran has been very dependent on oil revenues and consequently has suffered from the world oil glut and policies in OPEC that have maintained low oil prices.

Oil and Post-Revolutionary Iran

Early in the post-revolutionary period the new regime adopted a new oil policy. The leaders terminated the oil consortium's control of Iranian oil production, export, and marketing. They then transferred control of these areas to the National Iranian Oil Company (NIOC), which was combined with other oil and gas related publicly owned companies and came under the control of the new Ministry of Oil. The goals of the new policies were to reduce the level of oil exports and prolong the life of the country's oil reserves, gradually reducing Iran's dependence on oil exports. During the revolution the oil industry had symbolized foreign control of Iran; the revolutionaries had opposed foreign control through oil, and had promised economic independence for Iran. The new oil policy was meant to realize this independence.

Soon however, obstacles to the new oil policy mounted. The recession from 1977, continued through 1980, and the domestic political struggles barred plans for the rejuvenation of the economy. The Iraqi invasion caused heavy damage to all sectors of

the economy; the Iraqis destroyed major refineries, which meant decreased exports and decreased state revenues. The state could not prune the defense budget as much as it had intended to, due to the Iraqi invasion, and consequently could not apply that money to other sectors of the economy. In addition, the new leaders demonstrated an inability to promote non-oil exports (such as natural gas and copper) and to collect taxes (which was historically the case in Iran). Finally, the most formidable constraints were found in the world oil markets and within OPEC.⁶⁵ The Saudis, through U.S. manipulation, managed to reduce world oil prices and later, to flood the market. Within OPEC they barred Iran's demands for higher oil prices, and outside they sold over their quota. As a result of all these factors, Iran's oil production and revenues were damaged.

Iran's oil revenues have fluctuated since the revolution, but overall there has been a general decline. Following the revolution and the start of the war with Iraq, Iran's oil revenues sank to their lowest value in post-revolutionary Iran (1980). Then in 1982-83, Iran experienced a strong recovery, primarily due to Iran's improved standing in the war and an improved world oil market. Figures vary between \$20 and \$23 billion for this year. However, in 1983-84, there was a sharp decline in prices on the oil market, and Iran could not offset this, despite increasing her exports. The year 1984 marked the beginning of a recession for Iran, which was largely due to the decline in oil revenues. In

⁶⁵ Amirahmadi, 174.

1983-84, oil revenues fell \$3.7 billion below projected earnings, and in 1984-85, they fell \$6 billion below projected earnings. Finally, in 1986, Iran experienced a very sharp decline in its oil revenues. The predicted revenue was \$15 billion, whereas the actual revenue was less than \$6 billion.⁶⁶

<u>Iran's Oil Revenues (\$billions)</u>	
1983	\$20
1984	\$16.7
1985	\$14
1986	\$ 5.8
<u>1987</u>	<u>\$10.7</u>

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Finally, in 1987, Iran experienced a slight recovery, as can be seen from the above figure. According to Shahrough Akhavi, Iran's oil revenues were damaged due to the oil market becoming softer and to the drop in oil prices, especially after 1983; prices dropped from the 1979 high of \$34 per barrel to \$14 per barrel in February, 1987. Worse for Iran, the quantities it has been able to produce and sell have declined sharply due to the war - from more than two million barrels per day in 1982, down to less than 800,000 barrels per day in late 1986.⁶⁸ The recovery that began in 1987 has brought hope, but revenues continue to fluctuate, and Iran has not been able to reduce its dependence on oil enough to fully recover its economy without a strong increase in oil revenues.

⁶⁶ Bakhash, 245.

⁶⁷ Amirahmadi, 224-25. Figures adapted from Amirahmadi's statistics.

⁶⁸ Akhavi, 55.

Iran's dependence on oil has been evident for well over two decades. The Shah's regime failed to diversify economically and thus allowed Iran to develop a greater dependency on oil revenues and the international oil market they were subject to. Despite the promises of the revolution, this situation changed very little. When the post-revolutionary leaders came to power they opted for a policy of *gradually* reducing this dependence; however, the previously discussed obstacles blocked this policy. Modern sectors of the Iranian economy are all dependent on earnings from oil. According to Amirahmadi, "Some 90 percent of the state's foreign exchange earnings come from crude oil exports that pay for various kinds of Iran's ever-increasing industrial and food imports."⁶⁹ Most of the raw materials, and many intermediate products of Iranian industry must be imported, which is impossible without the foreign exchange earnings from oil revenues. In addition to foreign exchange, the single commodity of oil also provides a high percentage of the total public income. In 1983-85, oil revenues were responsible for 48.2 percent of the total government revenues.⁷⁰ This is significantly high considering the tax increases and the amount of public ownership and management that the new regime had established by this time.

The constraints on Iran's control of its production, export and price of its oil are largely determined by changes in the world

⁶⁹ Amirahmadi, 70.

⁷⁰ Rahnema and Nomani, 287.

market economy (international oil market) and within OPEC. Unlike the early 1970's, when OPEC was unified in its goals and strategies, Iran is unable to lead the other OPEC powers to reduce their exports and increase their prices; Iran is unable to use oil as a tool of its policy. The superpowers, especially the US, have manipulated the oil markets (mostly through Saudi leverage), and have retaliated against Iran for demanding changes at the international level. Since Iran holds a valuable product and is dependent on the export of that product, a situation is created in which the superpowers have been able to exploit Iran. This was particularly true in the 1970's, and is still evident in post-revolutionary Iran. The declining oil prices might have been advantageous for the new leaders in their attempts to reduce dependency on oil, but they lacked a planned shift for the economy and the eruption of the war threw the economy into such turmoil that reducing dependence became less of a priority.

	Oil Exports (per capita basis)	Considering inflation (1986 prices)
1972-73	\$130	\$450
1977-78	\$650	\$1,050
1986-87	<u>\$110</u>	<u>\$110</u> ⁷¹

As demonstrated by the figures above, Iran's oil revenues (considered here on a per capita basis) declined significantly between 1977-78 and 1986-87; the 1986-87 level is even lower

⁷¹ Clawson, 372-73.

than the level in 1972-73, before the boom in oil prices.

Considering inflation, the decline is even more shocking. In 1986 prices, Iran's oil exports on a per capita basis were almost ten times more in 1977-78 than they were in 1986-87. These few figures give a general overview of the decline in oil revenues that Iran has suffered.

Declining oil revenues have resulted in a declining share of the oil sector in Iran's GDP. The average annual contribution of oil to the the GDP over the 1979-87 period has dropped by 56 percent when compared to the 1976-78 period.

Noticeable changes have also occurred in the sectoral composition of GDP as exemplified by the significant decline in the share of the oil sector and consequent improvements in those of agriculture, industries, and services.⁷²

The improvements in the agricultural and industrial share of GDP are more a reflection of the decline in oil than any significant increase in actual production in these sectors. Services, however, have shown an increase that is more than proportional to the decline in oil.⁷³ The service sector, private and public, traditional and modern, has grown to be the largest economic sector in the Islamic Republic. "In 1984, it accounted for about 55 per cent of

⁷² Amirahmadi, 138-39.

⁷³ This shift to a more service- oriented economy is unhealthy for Iran. Service economies are generally less able to provide for needs than industrial economies, and are dependent on foreign imports.

the constant Gross Domestic Product and about 45 per cent of the labour force, compared with 31 per cent in 1977.”⁷⁴

The decline in oil revenues combined with Iran's continuing dependency on these revenues has been damaging to Iran's economy. The continuing dependency on oil is problematic, but this dependency does not seem to fall into the same category of structural dependency that the Shah's regime did. Galtung's structural model of dependency, which argues that dependency creates both internal and external imperialism, was applicable during the Shah's reign. However, in post-revolutionary Iran, while external imperialism can still be demonstrated, despite efforts to cut exploitative ties to the outside, internal imperialism is not as apparent as it was in the 1970's. The internal core-periphery relationship in post-revolutionary Iran shows less evidence of core ties to the outside and of core exploitation of the masses. The masses were Khomeini's base of support and as such were not in the same position as they were under the Shah. Unlike the obvious economic gap between the elite and the masses under the Shah's regime, the post-revolutionary leadership has generally maintained a lifestyle that does not demonstrate the same conspicuous consumption and exploitation of the masses. Despite this difference in the internal situation, Iran remains a peripheral country that is dependent on oil exports and the capitalist world market. If Iran's leaders expect to change this they will have to increase their own production capabilities in

⁷⁴ Rahnema and Nomani, 279.

non-oil sectors so as to reduce imports, and expand their exports beyond the single commodity of oil. This diversification would allow Iran to become more self-reliant and would reduce Iran's openness to exploitation, since it would take more than manipulation of the oil market to damage Iran's economy. The improvement in oil revenues in 1987, and the end of the war in 1988 may open new possibilities for this to happen. The emergence of pragmatism in various sectors may lead to improved policy formation that may stimulate economic growth and allow for significant development (at least in terms of delivering economically). One stumbling block to growth and development that has been evident in the post-revolutionary years, other than oil, has been the war with Iraq. Iran's war policy has changed as has its policies in other areas.

In fact, the pattern that has emerged in nearly every aspect of Iranian policy - foreign and domestic - has been extreme rhetoric in public pronouncements balanced by calculated flexibility and utter realism in practice, at least in those areas regarded as critical to survival. The war in particular has imposed a sense of realism and practical limitations.⁷⁵

The Economics of the Iran-Iraq War

The Iran-Iraq war resulted in a variety of damage to Iran, including vast human, infrastructural and economic loss. The war affected Iran, especially causing political and economic changes.

⁷⁵ Gary Sick, "Iran's Quest for superpower Status, *Foreign Affairs* 65 (spring 1987) 700-701.

On 22 September 1980, Iraq attacked Iran, probably believing that the new regime would be unable to organize and withstand the attack. Iran surprised Iraq, and many others, however, by not only surviving the initial attack, but pulling together and retaliating. In the first years of the war, military expenditures were gradually increased. In 1980, Iran spent \$7.7 billion on military expenditures, then \$8.5 billion in 1981, and \$9.6 billion in 1982.⁷⁶ The war fluctuated over the years - early on, Iraq was stronger, then in 1982, Iran dominated, and after that there were short term shifts, but generally it was a stalemate. In 1984/85, Iran made the arms-for-hostages deal, hoping to gain the advantage, but the U.S. aided Iraq after the news of the deal was leaked. By 1988, Iran could no longer continue the war and was forced to accept the UN cease-fire.

The economic costs of the war to Iran have turned out to be astronomical. Numerous different figures have been published regarding the war, and war-related activities, but many are within close range of one another. From 1979/80 to 1983/84, the IRI's military imports were stable at approximately \$2 billion per annum.⁷⁷ "By 1983-84, the war and war-related activities were absorbing almost one-third of the budget."⁷⁸ Official figures of

⁷⁶ Amirahmadi, 42.

⁷⁷ According to Patrick Clawson (p374), this is significantly less than the Shah's arms imports of \$4.1 billion during the 1977-78 period, but the lesser figure must be considered relative to the stockpile of military imports that had been established by the Shah.

⁷⁸ Bakhash, *The Reign of the Ayatollahs*, 245.

war costs often were less than this, but these figures often left out many of the war-related costs that were part of the budget.

According to R.K. Ramazani, the costs of the war have been estimated at \$5 billion per year up to 1985; this represents one-third of all government expenditures at that time. In addition, Ramazani, estimates that by 1985, there was a total of \$150 billion in war damages.⁷⁹ A quote from the Iranian minister of Planning and Budget suggests the extent of the war expenditures up to 1986:

the war expenditures rose from 18 percent of the general budget in 1359 (1980) ... to 32 percent in 1365 (1986) and 34 percent in this year's (1987) budget bill, ... These figures ... are only a portion of the actual war expenditures as other resources of executive bodies [were] also deployed for requirements of the fronts, not stated in any official figures or statistics.⁸⁰

According to Amirahmadi, the war actually accounted for 41 percent of the general budget and 52 percent of the government's operating expenditures in 1987.⁸¹ Considering these figures, it is difficult to believe that in the years before this, the war only accounted for one-third of the budget and expenditures.

The total costs of the war, over the eight years that it was fought, are difficult to estimate. Damage was done to so many sectors that it is uncertain if the entire costs can be counted.

⁷⁹ R.K. Ramazani, "Iran Burying the Hatchet," *Foreign Policy* 60 (Fall 1985) 61.

⁸⁰ Amirahmadi, 164-65.

⁸¹ Amirahmadi, 165.

Estimates have been made however, and some must be presented if an analysis of the effect of the war on Iran's political economy is to be made. Between September 1980 and December 1986, the costs of damage to Iran's infrastructure alone were estimated to be \$369 billion; this figure does not include oil revenue lost, but does include material damages to the oil sector. An estimate of the total economic costs during the same time period, including oil revenue and GNP losses, is \$542 billion.⁸² However, official Iranian government figures "estimated that the economic cost of the war's first five years was \$309 billion."⁸³ Comparing the figure given by Kamran Mofid for the first six years of the war and the official figure for the first five years, there is a large discrepancy (\$233 billion); this discrepancy is more than would be suspected for the one year difference. It is likely that there was some underestimation on the part of the Iranian government, which may not have included some losses to oil and the GNP.

Others have estimated the war costs for the entire eight years. Amirahmadi has based his estimates primarily on Iranian official figures, and has discussed where these figures are both under and overestimated, and has tried to balance them out. Amirahmadi's estimate for the damage inflicted on Iran's economy by the war, from beginning to end amounts to \$592 billion. This includes \$210 billion of damage which was inflicted on machinery, buildings, equipment, materials, and similar

⁸² Kamran Mofid, "After the Gulf War," *World Today* 45 (March 1989) 49.

⁸³ Clawson, 373. Compare this to Iran's GNP for 1985 of \$176.6 billion.

national wealth. In this total estimate, both direct and indirect costs are counted. Considering the direct costs to be 35.5 percent of the total, Amirahmadi has concluded that this amount is greater than 19 years of oil revenue, at the 1987 earning level.⁸⁴ The reconstruction costs that Iran is facing are astronomical. However, economic changes are not the only challenges that Iran had to face as a result of the war - there were also political changes.

One of the most dramatic changes in Iran, due to the war, was the arms-for-hostages deal with the U.S. Iran desperately needed weapons and parts for its US-built weapons systems. The pragmatists within the Iranian regime, with Khomeini's support, negotiated a deal with the United States, in which Iran received intelligence briefings on both Iraq and the USSR, in addition to 1,500 TOW missiles and components for its U.S.-built Hawk air defense system.⁸⁵ Some of the radicals leaked the news of the deal with the US, partially hoping that they could later use this to unseat the pragmatists. However, with Khomeini's intervention the pragmatists were able to maintain their power. Khomeini's version of the arms deal stated that those hostile to Iran

have apparently come back today and presented themselves meekly and humbly at the door of the nation wishing to establish relations ... Right now, all big countries are competing to establish relations with Iran.⁸⁶

⁸⁴ Amirahmadi, 64.

⁸⁵ Sick, 703.

⁸⁶ Sick, 704.

The arms deal did not cause dramatic changes in the Iranian leadership, but it had the potential to have done so if Khomeini had not stepped in.

Another cost of the fighting was a war-sick population that lost hundreds of thousands of its people and was growing weary. In April 1985, anti-government demonstrations broke out in a section of Tehran and quickly spread to other areas. This was the first popular manifestation of unrest in many years - it demonstrated a simmering resentment among the masses. Ordinary people were demonstrating against the government and the war. The government contained the demonstrations quickly, but the signs of war fatigue and resentment remained.⁸⁷ The factionalism within the regime was apparent at this time and the radicals had already lost a substantial amount of power to the pragmatists. The radicals were unfortunate to have dominated the political scene when the war was going poorly and their policies left no room for negotiation.

In the Summer of 1988, Iran accepted the U.N. Security Council cease-fire. There were a number of reasons for accepting at this time:

- 1) the Iranian population was war-sick,
- 2) the costs of the war (possibly as much as \$592 billion) had severely damaged Iran's economy, and
- 3) Iran was extremely isolated in the international arena.⁸⁸

⁸⁷ Bakhash, *The Reign of the Ayatollahs*, 240-41.

⁸⁸ Iran's international isolation is best demonstrated by the USS *Vincennes* incident. An Iranian civilian aircraft carrying more than 200 people was

The cease-fire stipulations did not favor Iran, but the leadership accepted despite this. Khomeini stated that agreeing to the cease-fire was like drinking a cup of poison, but that it was necessary. Hindsight suggests that Iran should have accepted the Arab peace plan of 1982, but at the time the leaders believed that the war against Iraq could be won. The cease-fire of 1988 brought the end of eight years of fighting and the possibility of rebuilding the Islamic Republic.

During Khomeini's more than ten years as the leader of Iran, the country underwent several major changes. The constitutional structure of the state was changed from a monarchy to a republic. The ruling elites were no longer the monarch and his loyalists, but rather, the clergy. There was a significant transfer of ownership of property and wealth from the private to the public sector. And, the state extended its role into virtually every sphere of public and even private life.⁸⁹ In addition, the country withstood a war with Iraq and declining oil revenues. Despite social and economic problems and the political opposition and factionalism, the IRI lasted more than a decade under Khomeini's leadership, and remains relatively stable two years after his death.

shot down by the US ship, the USS *Vincennes* - the United Nations refused to condemn the US for its actions.

⁸⁹ Shaul Bakhash, "After the Gulf War," *World Today* 45 (March 1989) 46.

Additional Economic Challenges

The war with Iraq, the declining oil revenues, the attempts at land reform and other socio-economic reforms, and the political factionalism all presented challenges to the IRI. In addition to these there are other economic problems that Iran's post-revolutionary leadership has had to face. According to Ramazani, the economic ills which Iran has had to face include pervasive black-marketeering and corruption, the exodus of half of all Iranian physicians (leaving 15,000 doctors for more than 40 million people), an unofficial inflation rate of 35 percent, and dwindling foreign reserves.⁹⁰ These are not the extent of problems the leadership has faced.

Inflation began before the revolution and continued into the post-revolutionary period. Inflation has been most devastating to the poorer section of the country - many families spend as much as 40-45 percent of their income on food alone.⁹¹ In 1987, there was a sudden jump in prices, especially in food, health, household items and education, necessities that the poor are finding impossible to afford. The government has tried to control inflation through increasing taxes, rationing goods, cutting expenditures, placing imports under government control, and subsidizing prices, but none of these have been successful.⁹² Inflation has caused prices to soar, while salaries have remained

⁹⁰ Ramazani, 61.

⁹¹ Amirahmadi, 173.

⁹² Amirahmadi, 182.

low. The buying power of the middle-class has been decreased so much, some analysts claim that Iran has become a two-class country of rich and poor.

In addition to inflation, Iran has also suffered from a shift in the sectoral composition of its GDP. The expansion of the services sector has only partially compensated for the relative decline in oil. In the 1979-87 period, the service sector showed an annual growth rate of 0.2 percent. The service share of GDP increased from 45 percent before the revolution to 54 percent in the post-revolutionary years.⁹³ This trend is considered harmful because it diverts scarce resources away from the more productive sectors of the economy. In addition, services pay lower wages than do more productive sectors, so the workers suffer.

While the service sector increased its actual output, the industrial sector showed an increase in its share of the GDP, also.

The slight jump in the industrial sector of the GDP reflects the decline in the share of the oil sector rather than a real increase in industrial value added, which has remained sluggish throughout the postrevolutionary years, with the exception of the 1982-83 period.⁹⁴

The 1979-87 period saw an average growth rate of only 0.06 percent per year, experiencing a significant contraction from 1984-87, as a result of the continuing decline in rates of capacity utilization and capital formation. In fact, the industrial sector

⁹³ Amirahmadi, 139.

⁹⁴ Amirahmadi, 144.

suffered not only from these problems, but also from Iran's industrial dependence "on the world capitalist economy for over 57 percent of their raw materials and 63 percent of their spare parts."⁹⁵ The slow growth of the industrial sector has done very little to aid the GNP, and has done even less for the employment problems Iran is facing.

The labor force of Iran has increased rapidly, while the employment opportunities have decreased.

<u>Unemployment Rate in Iran</u>	
1976	10%
1984	18.7%
<u>1986</u>	<u>14.1%</u> ⁹⁶

The above figures are official government figures. As can be seen, the year 1986 is shown to have a decreased unemployment figures, compared to 1984. However, unofficial statistics place the 1986 unemployment rate at 28.6 percent, and indicate that there is also a sizable underemployed population.⁹⁷ The population of Iran has grown at such a rapid pace and planning has been so lacking, that employment opportunities have quickly fallen behind. In 1986, 11.1 million people, or 23.3 percent of the 49.8 million persons in Iran, were employed. This means that 2 out of 9 people were employed and were supporting the rest of the

⁹⁵ Amirahmadi, 144.

⁹⁶ Amirahmadi, 187.

⁹⁷ Amirahmadi, 188.

population.⁹⁸ These staggering figures must be changed if Iran is going to recover economically.

Besides the problems of lacking a strong industrial base, diverting resources to nonproductive sectors, especially services, inflation and a high unemployment rate, Iran also faces obstacles such as a lack of skilled labor, a suffering educational system, inadequate healthcare and housing, and an uneven distribution of wealth. As of Spring 1986, government released data reported that 20 percent of the population received half (50 percent) of the country's national income, while the remaining 80 percent is left to divide the residual 50 percent of income.⁹⁹ Ironically, many of those who expected the most change from the revolution are the same ones who have become poorer since the revolution, including the urban poor, farm laborers, construction and industry workers, and government employees. Mohsen Milani argues that Iran is a stronger state since the revolution, particularly because of the support from the lower classes and the lower-middle classes.¹⁰⁰ This may be a valid argument, but it might not be the case in the future if Iran's leaders fail to forge a path of economic growth.

Despite all the economic problems, the political opposition and factionalism, the war, and the state intervention into citizens'

⁹⁸ Rahnema and Nomani, 273.

⁹⁹ Shahrough Akhavi, "Elite Factionalism in the IRI," *Middle East Journal* 41 (Spring 1987) 198.

¹⁰⁰ Milani, 307.

private lives, Khomeini and the IRI survived much longer than many experts believed possible. A primary reason for this survival was Khomeini's charismatic leadership. He was supported by the masses, and was the final arbiter in the regime. He designed the theory of *Velayat-e faqih*, or "leadership of the jurisprudent," around which the 1979 constitution revolves. In addition, Khomeini spoke of international relations in terms of the oppressors and the oppressed. He demanded independence for Iran, and changes at the international level that threatened the superpowers, especially the United States. The IRI has been based on an active state role in the economic sphere, including nationalization of many industries and greatly increased regulation of the private sector.¹⁰¹ Khomeini's economic leanings seemed to be toward redistribution and social justice, although he avoided taking a controversial stand in regards to this and other problematic issues. Many believed that his death would bring serious turmoil to the IRI, and possibly even mean the end to rule by the clergy. Khomeini's death on 3 June 1989, however, was followed by a relatively smooth and rapid transition of power. Since then, the leadership of the IRI has remained quite stable and has focused its energies on economic reconstruction.

¹⁰¹ As suggested previously, the degree of state control and regulation has been a subject of intense debate in the IRI. An acceptable balance between the private and public sectors, between free enterprise and state ownership/management has not yet been found.

POST-KHOMEINI IRAN AND BEYOND

The Ayatollah Ruhollah Khomeini died on June 3, 1989, a little over a decade since he had triumphantly returned to Iran from exile. For years it had been predicted that his death would bring an upheaval in Iran that could possibly mean the crumbling of the Islamic Republic. In fact, Khomeini's death seemed even more damaging at the time because just three months earlier he had unceremoniously removed his chosen successor, Ayatollah Hussain Ali Montazeri. Contrary to the predictions however, a new successor was chosen quickly and the transition was quite smooth.

This chapter begins with a review of previous chapters and then: 1) examines the political economy and the development of Iran in the two years since Khomeini's death, and; 2) speculates on future prospects. This thesis has analyzed how the environment (domestic and external) and decisions have interacted to shape the political economy of Iran, which in turn has affected the degree of development of this country. For example, chapter two viewed Iran during the 1960s and 1970s, which were partially characterized by a huge increase in oil revenues, then a decline and and by the Shah's modernization program. This chapter analyzed the political and economic factors that led to the 1979 revolution. In chapter three Iran was examined in view of an environment shaped by the revolution, the war with Iraq, and declining oil revenues; this

environment affected the decisions made by the regime, which was characterized by factionalism, but which Khomeini dominated. Development in the sense of delivering economically and politically was not realized to a large degree in either of these two periods.

This chapter looks at Iran since Khomeini's death. The current environment is different in that the war with Iraq is over and oil revenues have increased somewhat. The pragmatic or moderate faction, led by President Rafsanjani, has generally prevailed in the past two years, and policies have focused on postwar reconstruction. Practical economic decisions are taking priority over ideological fervor and the changes in the political economy that are taking shape at the present time may allow for further development in Iran.

The past two chapters have offered that Iran's political economy has been characterized largely by dependency. This dependency, particularly on its single commodity export of oil and on a variety of imports for survival, has allowed outside powers to exploit Iran (especially the U.S. in the 1970's) and has been detrimental to the country's development. Despite the efforts and promises of the revolutionaries, the Islamic Republic was unable to break the ties and become self-reliant. Dependency occurs in different forms and degrees. Due to the increasing international interaction practically all countries are dependent on the international capitalist market for sale of their own products and for purchasing needed goods. However, while most developed countries, such as the United States, Western Europe and Japan, have enough power within the international system to make it practically impossible to exploit their dependency on the international market,

many developing countries are not strong enough to protect themselves from exploitation. Their dependency, especially in the case of primarily single-commodity export countries, makes it easy for developed countries to hurt them economically; and due to the overlap of the two sectors, being capable of hurting a country economically, means having the capability to hurt a country politically. Exploitation by developed countries has often been for the purpose of finding raw materials or broadening markets. During the Cold War, developing countries were also used as pawns between the US and the USSR. Finally, developing countries are sometimes damaged economically at the international level when they demand changes at the international level, such as global redistribution or increased power for the Third World. Dependency may be characterized as a phenomena to which all countries are subject, but developing countries are more easily damaged by their dependency than are developed states.

However, the nature of dependency can be changed, and therefore its detrimental effects can be reduced. In Iran's case, the foreign loans and aid that it is seeking, if used wisely, can help reconstruct the country and build a solid economic foundation that will allow Iran to become more independent. In turn, the regime, if it so chooses, can provide for the development needs of the population. Only careful planning and proper strategies on the part of the government can move the country toward a more developed status; even with these, there are an undiscernible number of variables that can intervene and set back even the most carefully laid development plans.

The Khomeini Legacy

Since 1986 there has been a general movement towards pragmatism in Iranian policy. The moderates led by Rafsanjani gained more power, deemphasizing ideology and arguing that the very survival of the revolution depended on repairing the country. In 1988 the cease-fire with Iraq was accepted and the government worked to lessen its international isolation. Khomeini called for a limited market economy and controlled free international trade. He also stated that Iran should seek relations with all other nations, excepting the United States, Israel and South Africa. However, later in that same year Salman Rushdie's book, *Satanic Verses*, caught the attention of Muslims throughout the Middle East, including Khomeini, who called for the author's assassination for his blasphemy. This incident immediately led to a reversal of the trend toward compromise and moderation.¹ Iran's relations with Britain and most of the Western world were severed as a result of Khomeini's death sentence for Rushdie, and some economic sanctions were adopted. Khomeini's death less than a year later did not lead to a revocation of the death sentence, but since then relations between Iran and the West have improved.

According to journalist Robin Wright, Khomeini failed at critical junctures and left a legacy of problems for his country. Despite his absolute authority as the *faqih*, Khomeini's "vacillation and delicate balancing of Iran's political factions often resulted in policy paralysis

¹ Miron Rezun, "The Internal Struggle, the Rushdie Affair, and the Prospects for the Future," *Iran at the Crossroads: Global Relations in a Turbulent Decade*, Miron Rezun, ed. (Boulder: Westview Press, 1990) 213.

on key issues rather than reform."² In addition, Khomeini's self-righteousness and inflexibility cost Iran the loss of international acceptability, which was desperately needed in the latter years of the war with Iraq. Khomeini's personal and political grudge against Saddam Hussein prevented any mediation of the unwinnable war between Iran and Iraq, and cost tens of thousands of lives.

Economically, he failed his own constituency, the *mostazafin* (the disinherited), who were even more impoverished at the time of his death than they had been under the Shah. Finally, he left the Islamic Republic very vulnerable by leaving the position of his successor as *faqih* completely open.³ Despite the problems that existed at the time of his death and the difficult legacy he left behind, the Islamic Republic has survived more than two years since Khomeini's death and has surprised many with its stability.

The Islamic Republic has undergone a number of changes since Khomeini's death. The political environment is still characterized by factionalism, but the pragmatists have greatly strengthened their position in the past two years. Their focus on repairing the damage that Iran has sustained and building the economy has appealed to the masses. The economy has somewhat improved and long-term planning is now being considered rather than simply responding to immediate economic problems as was the case in the past. An important strategy in developing the economy is improving trade

² Robin Wright, *In the Name of God: The Khomeini Decade* (New York: Simon and Schuster, 1989) 207.

³ Wright, 207-8.

relations with the developed world and lessening Iran's isolation. The decisions of the current administration and the environment within which those decisions have been made is the primary subject of this chapter.

The Political Environment

Contrary to the expected conflict, there was an unexpectedly quick choice of successor to Khomeini. Hojatolislam Ali Khamenei was chosen to be the next *faqih* or supreme leader of Iran, despite his lack of certain qualifications. Khamenei has proven to be a less controversial figure than Khomeini was, and he has continually supported the moderates in their policies. The moderates have also gained strength through recent elections and constitutional amendments.

On 28 July 1989, Hojatolislam Ali Akbar Hashemi Rafsanjani was elected to the office of president and a number of constitutional amendments were approved. The 1979 constitution had been a reaction to royal autocracy and despotism, and thus focused on distribution of authority and divided powers. The 1989 constitution represented a reaction to the problems created by this division and distribution. It provided for greater centralization and concentration of authority. The 1979 constitution had allowed supreme leadership to be exercised by a council of three to five jurists. The 1989 amendments revised this and stated that supreme leadership could be exercised only by a single individual. The amendments also downgraded the qualification for the *faqih*. These amendments allowed a cleric of less eminent scholarly standing to hold the office

of supreme jurisprudent and thus almost implied a separation between spiritual and political leadership of the community.⁴

For a decade Iran's clerical leaders had insisted that the legitimacy of the state derived from divine mandate granted not only to the community of Islamic jurists but specifically to the supreme jurist of the age, in light of his superior learning, grace, and sanctity. Thus, the post-Khomeini period seems likely to be characterized not only by leadership by clerics of diminished scholarly authority, but also by a diminution of the basis of legitimacy on which the Islamic Republic was founded.⁵

The supreme leader's powers were further defined to set general policies and decide issues which cannot be resolved in ordinary ways; this was meant to end the debate over issues such as trade, investment, social justice and general economic policy.⁶ The downgraded qualifications for the *faqih* and the strengthening of the moderate faction has meant a greater degree of commitment to practical considerations in policy-making. In addition to these changes, the constitutional amendments also strengthened the office of the president, centralizing his authority and eliminating the office of prime minister, which has aided President Rafsanjani in building his power.

The political environment since Khomeini's death has remained characterized by factionalism between two camps, the radicals and the pragmatists, the latter of which has proven the stronger of the

⁴ Shaul Bakhash, *The Reign of the Ayatollahs: Iran and the Islamic Revolution* (New York: Basic Books, Inc., Pubs, 1990) 284.

⁵ Bakhash, 294.

⁶ Bakhash, 285-94.

two. President Rafsanjani, who is the leader of the moderate faction, was a loyal student and supported of Khomeini for years. He began strengthening his political position several years before Khomeini's death. He was the Speaker of the Majlis for several years and was partially responsible for procuring weapons during the arms-for-hostages deal. He has acted as the leader of the pragmatic faction since it first gained power in the mid-1980s, and has since become one of the most powerful men in Iran. In order to repair the damaged economy, Rafsanjani has sought to improve relations with the developed states, especially Western Europe and Japan, and has even broached the subject of renewing relations with the United States. His primary focus thus far in his presidency has been reconstruction and economic growth.

Since Khomeini's death, the moderates have tried to finalize a peace settlement with Iraq and to begin postwar reconstruction. The total damage inflicted on Iran by the war from beginning to end in economic terms has been approximated to be \$592 billion.⁷ According to various Iranian officials the direct costs of reconstruction are now being estimated at more than \$600 billion, and President Rafsanjani has declared that additional expenses bring the total cost to one trillion dollars.⁸ There is a possibility that these figures have been somewhat inflated in order to get more money for reconstruction, but there is no doubt that the reconstruction will be

⁷ Hooshang Amirahmadi, *Revolution and Economic Transition: The Iranian Experience* (New York: State University of New York Press, 1990) 64.

⁸ *International Iran Times*, Vol. XX, no. 45, 11Jan 1991, 2.

incredibly expensive, especially since the government hopes to see a great deal of economic growth through reconstruction.⁹

President Rafsanjani has been able to push many of his policies through and to strengthen his faction in the past two years. The October 1990 elections for the Assembly of Experts were notable because the moderates controlled the selection process. As a result they were able to axe most of the radical candidates from the ballot.¹⁰ The Assembly has the power to replace the person holding the position of *faqih*, which is currently Ayatollah Ali Khamenei. Khamenei has supported Rafsanjani and the policies of the moderates for the past two years and consequently, he could be in danger if radicals were to control the Assembly. The Majlis is also dominated by moderates, although the radicals do hold some seats. The moderates seem to be unified by the need to get the Iranian economy into gear and the fear that the revolution will be destroyed if the regime "cannot stop the ever-rising inflation and create jobs."¹¹ The regime is doing what it believes will boost the economy, but the economic environment in Iran at this time is problematic, and there are no easy solutions.

The Economic Environment

As discussed in chapter three the Iranian economy was in poor shape at the time of Khomeini's death.

⁹ The moderates favor oil-led industrialization for economic growth, which the radicals oppose since they view this as remaining tied to the West for oil sales and they believe this will inhibit any moves toward self-reliance.

¹⁰ *International Iran Times*, Vol. XX, no. 37, 16 Nov 1990, 2.

¹¹ *International Iran Times*, Vol. XX, no. 39, 30 Nov 1990, 1.

Iran's per capita income fell from 114,000 rials in 1978 to 55,500 in 1988, or from \$US 1,425 to \$US 688, according to official sources using 1974 fixed prices. The reason for this decline lies partially with its 3.4 percent population growth rate, one of the highest in the world.¹²

This decline is also due to the war and the decline in oil revenues, and to the lack of policies aimed at economic growth adopted by the Khomeini regime. The acute economic problems that Iran is facing also include an inflation rate as high as 60 percent and a 25 percent unemployment rate,¹³ meaning out of the 12 million person labor force in Iran, 4 million are unemployed.¹⁴ In addition, not only is unemployment high, but the sectoral composition of employment is poor. During the past decade it has moved in favor of the service industry, which is characterized by less productive activities and low-paying jobs. The effect is depressed production and per capita income, which continues to produce more problems in the economy.

So long as the structure of the economy remains unchanged, the postwar reconstruction remains dormant, population control policies are lacking, the development budget remains low, and inflation is unacceptably high, little can be done to remedy unemployment and the structural imbalance in employment.¹⁵

The economic problems Iran is facing have been somewhat offset by increased oil revenues due to the Iraqi invasion of Kuwait and they

¹² Dilip Hiro, "Iran in the 1990's," *Middle East Insight* 7 (1990) 44-46, 45.

¹³ Hiro, 44.

¹⁴ Masoud Kavoossi, "Labor Relations in Iran: The Islamic Challenge," *Middle East Insight* 7(1990) 71-75, 72.

¹⁵ Amirahmadi, 192-93.

may be further reduced if Iran is able to obtain the loans it is currently seeking.

The August 1990 invasion of Kuwait by Iraq brought political and economic gains to Iran. Within two weeks of the invasion Iraq conceded practically all of Iran's territorial and political demands. In addition, the first few months after the invasion saw increased oil revenues for Iran, which helped pull the government out of the budget deficit. Oil revenues for 1990 amounted to more than \$15 billion and the same level was targeted for 1991.¹⁶ The pragmatists, especially President Rafsanjani and Foreign Minister Velayati maneuvered Iran's position during the build-up and the war, choosing their actions in terms of what would best benefit their reconstruction efforts. Iran remained neutral despite the radicals' calls to join Iraq in its fight against the West. The pragmatists were also alarmed at the huge Western military presence but they chose to stay out of the fighting for several reasons:

- 1) The eight year war with Iraq had left thousands dead
- 2) Iran hoped to replace Iraq as the dominant power in the Gulf region.
- 3) Reconstruction depends on aid from the West, which would certainly not have been forthcoming if Iran had joined Iraq.

As a result of its neutral position, Iran has seen a number of benefits.

¹⁶ *Christian Science Monitor*, 16 May 1991, 8 col. 2. This is a significant increase over the oil revenues of the mid-1980's when Iran hit a low point of \$5.8 billion in 1986.

The diplomatic relations that had been broken with many nations due to the Rushdie affair were reestablished during the Gulf war. The European Community lifted all its economic sanctions against Iran and the United States lifted its ban on US-based companies buying Iranian oil. In addition, Britain and Iran resumed ties despite the lack of a resolution to the Rushdie incident. Finally, there is renewed interest by the West to aid and invest in Iran. The French agreed to help rebuild Kharg Island (Iran's main oil shipping terminal which was badly damaged in the war with Iraq), and France has signed a contract allowing Iran to assemble Peugeot automobiles in Tehran.¹⁷ The pragmatists are hoping that this renewed interest by the West continues to grow and that reconstruction funds will quickly follow.

The current Five Year Plan expects resumption of work on oil refineries, petrochemicals, steel production, construction materials, motor vehicles and consumer goods plants. "Sharp differences, however, emerged within the leadership on what roles the domestic private sector and foreign capital and expertise were allowed in this endeavor."¹⁸ The radical faction argues that no foreign capital or expertise is needed since they would increase Iran's dependency and would impede the country's movement toward self-sufficiency. This faction also maintains that the private sector's role need not be increased. The pragmatic faction believes, however, that domestic resources are not enough for reconstruction and that foreign

¹⁷ *New York Times*, 10 Dec 1990, sec. A, 8.

¹⁸ Bakhsh, 278.

assistance is needed. In addition, this faction argues that encouragement of the domestic private sector is necessary for Iran's economic growth. "Their goal is to transform this highly centralized, heavily subsidized and stagnant system into a vibrant, decentralized, free-market economy."¹⁹ Prior to his death, Khomeini had called for a limited market and controlled free international trade, and he had allowed Rafsanjani to pursue economic relations with various countries, including the Soviet Union.

Since his death, the moderate faction has been able to push a number of their policies through the Majlis. Various changes have been made in the Plan since October 1990.

To allow an influx of foreign capital, the Rafsanjani administration decided last October (1990) to allow Iranian firms to sign agreements directly with non-Iranian companies. This applies to both private and public sectors, and has opened up immense possibilities for Iranian joint ventures with Western firms.²⁰

Then in November 1990, the government, in an effort to promote non-oil exports, announced that it would free private firms to import various raw materials and spare parts with foreign exchange they earn from their own exports, rather than relying on the government for foreign exchange. In addition, in May 1991, the government announced that it plans to sell an estimated \$80 million worth of shares in state owned industries by the end of the current Iranian year (March 1992). The sales to the private sector are aimed at

¹⁹ *New York Times*, 9 April 1991, sec.A, 10.

²⁰ Hiro, 45.

encouraging greater industrial investment and productivity. This is a serious reversal from the early years of the Islamic Republic when nationalization of industries was the goal of the regime. Finally, some regulations are being changed in order to allow more foreign investment in Iranian industry. The current Five Year Plan calls for as much as \$3 billion of foreign investment in heavy industries and allows foreign investors to own up to 49 percent of the shares in an Iranian industry.²¹ These reforms are aimed at boosting the economy and helping Iran rebuild itself.

In addition to these reforms the government has also moved to borrow money from abroad for reconstruction. In November 1990, the Majlis authorized the Islamic Republic to borrow \$17.5 billion from abroad over the next five years for reconstruction and development programs. The surge in oil revenues due to the August 1990 invasion of Kuwait helped bring last year's oil revenues up 30 percent from the previous year. Oil exports for 1990-91 amounted to \$16.5 billion and this income has helped Iran out of its \$2 billion deficit.²² However, it will take more than increased oil revenues to fully finance Iran's reconstruction. Borrowing from foreigners is very controversial, largely due to the historical experiences and ideological divisions. The radicals object to loans from outside, but Rafsanjani and the rest of the pragmatists are looking for a jump start to the failing economy. Some argue that the problem is not the borrowing from abroad, but the management of the funds once they

²¹ *International Iran Times*, Vol. XXI, no. 11, 31 May 1991, 1.

²² *International Iran Times*, Vol. XXI, no. 11, 31 May 1991, 1.

make it into Iran. The Iranian government has been criticized for excessive waste and some believe that a sound administrative system is needed to correctly utilize the money and channel it in the proper direction.

Thus far, the administration has borrowed only a partial amount of that approved by the Majlis. The World Bank approved a \$250 million loan for Iran for repairing the damage done to the Gilan and Zanjan provinces by the June 1990 earthquake.²³ In addition, according to central bank Governor Mohammad Hossain Adeli, Iran has borrowed more than \$12 billion in foreign loans to finance the five-year development plan which began March 1991. Adeli stated that Iran is seeking the \$17.5 billion in foreign loans authorized by the Majlis and another \$10 billion in trade credits. Despite Adeli's assurances that Iran has nailed down 70 percent of the loans, news reports suggest that foreign bankers are not attracted to Iran, and that the loans may be slow in coming. The money Iran has received so far has been borrowed from banks in France, Germany, Italy, Switzerland, Austria, Sweden, Canada, Japan and Luxembourg.²⁴

Borrowing could very well mean increased dependency, particularly in the short run. However, if the funds are used appropriately, which includes sound administration and elimination of the excessive waste of which the regime has been accused, Iran may be able to change the nature of its dependency and lessen it. Iran's Gross National Product (GNP) increased by 4 percent in 1989

²³ *International Iran Times*, Vol. XX, no. 37, 16 Nov 1990, 1.

²⁴ *International Iran Times*, Vol. XXI, no. 11, 31 May 1991, 1.

and by another 8 percent in 1990.²⁵ This is a positive sign. If Iran diversifies its economic foundation and moves to manufacture those goods which it now imports whenever feasible, Iran would increase its self-sufficiency (and become more self-reliant). It appears that the Rafsanjani administration is working to realize economic growth and that development projects are on the agenda.

The administration proposed an 18.79 trillion rial budget for this fiscal year (March 1991- March 1992). This is a 43 percent increase over the previous year, which at the official exchange rate of 70 rials to the US dollar means a \$268 billion budget for this year.²⁶ In proposing this budget increase, the Rafsanjani administration argued that the "market oriented" policies have turned the economy around and that the budget reflects the economic progress of the past year. The budget is based on projected increases in oil revenues and plans to sell many of the state owned enterprises. The proposed increase has been delegated to a number of areas, including current expenditures, such as wages and equipment of the bureaucracy, health and education, development projects, reconstruction, and defense and security.²⁷ While progress has been made over the past year, and the proposed increase is probably necessary for further development, there are still numerous economic problems that this country is facing.

²⁵ *New York Times*, 9 April 1991, sec. A, 10.

²⁶ At an unofficial exchange rate of 1000 rials to the US dollar, which is less than the black market rate, the budget would be only \$18.8 billion. *International Iran Times*, Vol. XX, no. 42, 21 Dec 1990, 2.

²⁷ *International Iran Times*, Vol. XX, no. 42, 21 Dec 1990, 2.

There are various indicators of productivity and the state of the economy. The output of factories is one important indicator. The factories operated by the Heavy Industries Ministry measured at only 30 percent of capacity for 1989/90, and were as low as 26 percent the previous year. Finance Minister Mohsen Nurbakhsh told officials that the first three months of fiscal year 1990-91 showed marked increases by a number of factories, but gave no figure for the overall economy. However, even with 100 percent increases the overall capacity would only be brought up to 60 percent, which is still considered a low figure. Some factories have shown exceptional increases, such as those producing automobile tires, refrigerators and freezers, and glass, but continued increases are needed.²⁸

Apart from production figures there are also indicators of overall economic standing of the population. The Iran Statistics Center reported that the average urban family spent approximately 49 percent of its income on housing and 35 percent on food, leaving only 16 percent for clothing, transport, entertainment, health, savings and all other expenses.²⁹ The administration has reported that there has been progress over the past year, as indicated by the rise in GNP, but this growth must continue if Iran is going to realize its reconstruction and development goals. One variable that impacts Iran's economic growth is its relations with other countries, particularly trade relations.

²⁸ *International Iran Times*, Vol. XX, no. 26, 31 Aug 1990, 2.

²⁹ *International Iran Times*, Vol. XX, no. 26, 31 Aug 1990, 2.

Due to the high degree of economic interaction between the domestic and international level, trade relations are important for practically all states, especially if they intend to experience economic growth. In order for Iran to recover economically the administration must pursue increased trade relations and foreign aid/loans. The pragmatic faction is currently fighting the isolationist tendency of the past decade and attempting to broaden its economic relations in order to put the country on the road to reconstruction.

Foreign Relations

Iran's foreign relations since the revolution have been shaped by a contest between ideology and pragmatism. Ideology has meant international isolation and a continuance of the war with Iraq, whereas pragmatism has meant a concerted effort on the part of the government in latter years to improve relations with the outside world, to end the war and to begin postwar reconstruction. As indicated previously, the pragmatic faction has been dominant in the past few years, but the radicals still hold some important positions and cannot be discounted. Improved foreign relations are seen by the pragmatists as a necessity for reconstruction. Iran does not have the necessary capital to begin vast reconstruction and improved trade relations and foreign loans are seen by the pragmatists as the only way to find this capital. Supreme jurisprudent Khamenei has stated that Iran "should use foreign resources ... we cannot prolong the issue of reconstruction for 100 years."³⁰ As a result of the

³⁰ R.K. Ramazani, "Iran's Foreign Policy: Contending Orientations," *Middle East Journal* 43 (Spring 1989) 213.

government's efforts, relations with many states have been improved.

Since the early years of the republic, Iran has sought to expand its relations with developing nations. In particular, relations with Turkey and Pakistan have been expanded. In 1985 these three countries formed the Economic Cooperation Organization (ECO); the ECO was formed to encourage trade, technology transfer, and other economic exchanges among the three countries.³¹ In addition, Iran and Turkey have plans to build a pipeline through Turkey to Europe for Iranian natural gas.

Improved relations with the advanced countries are also being actively pursued, with the notable exception of the United States. In November 1989, Iran made a deal with Germany and France in which the National Iranian Oil Company agreed to sell 300,000 barrels of oil per day for 18 months to a consortium of West German and French companies and banks in exchange for \$800 million in cash to be provided immediately. At \$15 a barrel the deal was worth approximately \$2.6 billion.³² In addition, Germany and Iran have signed a dozen development project plans recently, which are expected to inject more than a billion dollars of capital into the Iranian economy. Germany and Iran have announced differing versions of these plans, but it appears that improving port facilities and building transport facilities are two of the major projects. Iran

³¹ R.K. Ramazani, "Iran: Burying the Hatchet," *Foreign Policy* 60 (Fall 1985) 65-66.

³² Hiro, 46.

has also improved relations with Japan, which has formally announced that it will resume economic aid to Iran for the first time since the revolution.³³ Iran is now actively pursuing better relations with advanced states in hopes of realizing more economic growth.

No matter how virulent much of their rhetoric still is, the Iranian leaders finally have come to believe that the very survival of the revolution is at stake and that mounting domestic problems can be eased only by breaking down the walls of Iran's international isolation.³⁴

Years of international isolation did not see a break in the dependency of Iran, nor increased self-sufficiency. The large modern industries in Iran remained dependent on the world market for 65 percent of their input and the regime experienced foreign exchange shortages because of its isolation.³⁵ People lived under an often repressive regime much as before the revolution and for many their economic situation worsened.

The leaders of the Islamic Republic were, of course, still claiming that they were defending the oppressed people of Iran, but at the same time, the measures these people demanded for the amelioration of their economic conditions were forgotten. As far as the existing distribution of economic resources was concerned, one could find few differences between pre- and post-revolutionary Iran.³⁶

³³ *International Iran Times*, Vol. XXI, no. 12, 7 Jun 1991, 1.

³⁴ Ramazani, "Iran: Burying the Hatchet," 69.

³⁵ Amirahmadi, 87.

³⁶ Mansoor Moadel, "Class Struggle in Post-Revolutionary Iran," *International Journal of Middle East Studies* 23 (1991) 328.

Not only were economic conditions quite similar to the pre-revolutionary period, but often political circumstances for the population were also similar. As before, mass mobilization was relied upon and interest articulation was severely limited. Currently, the regime is focusing on economic growth, but eventually political development will have to be addressed, especially if the pragmatists intend to remain in power. This will mean delivering what the population demands; in particular, political participation will be demanded, and the administration will have to find a way to allow for this participation.

Prospects for the Future

This final section analyzes the future prospects for Iran's political economy and development. Nearly three decades have been examined in order to understand the interaction between the economic and political spheres in Iran. This historical analysis is necessary because it provides a basis for comprehending Iran's current political economy and level of development. With this basis practical economic and political suggestions can be made for future development in Iran. Understanding the consequences of decisions in the past will allow the current leadership to make more informed decisions. Obviously environmental factors will not be the same as before, but nevertheless a historical basis provides some foundation from which to begin.

Since Khomeini's death, probably the most important event influencing Iran's political economy has been the war between the Allied Forces, led by the United States, and Iraq. Iraq's invasion of

Kuwait increased oil prices which allowed Iran to increase its oil revenues and pull itself out of a budget deficit. Following the invasion, Iran's neutral position in this war brought it benefits that otherwise probably would have been long in coming. First, the war weakened Iran's most powerful competitor for regional dominance. After the eight year war Iran was hardly strong enough to prevent Iraq from increasing its power in the region. However, with the defeat of Iraq at the hands of the allied forces, Iraq cannot establish regional hegemony any time soon while Iran is placed in a much better position to dominate the Gulf region. In addition, Iran's neutral position in the war was rewarded with renewed relations with Western countries and economic agreements. Had Iran joined Iraq in its fight against the allied forces, which the radicals called for, the war would have been much different. Many in the West realized this and chose to encourage Iran's neutrality. President Rafsanjani maintained a neutral role in the buildup and the war because of his concerns for reconstruction. Reconstruction depends on assistance from the advanced countries, particularly Japan and Western Europe, and economic assistance would not have been forthcoming had Iran joined Iraq. The European Community lifted all economic sanctions against Iran and many of the Western nations renewed their relations with Iran. Currently, the government is trying to encourage Western investment in Iran.

The political strength of the pragmatists, especially Rafsanjani, has increased since the war and economic benefits are in evidence. Within the past few months, several individuals and newspapers have vocalized support for President Rafsanjani. In a speech against

the United States, Supreme Guide Khamenei did not attack Rafsanjani for any rapprochement with the US, but instead ordered the President's critics to shut up and stated:

It is the duty of all to support the respected President ... and the government, which, with God's blessing, is being run today by one of the most brilliant figures of the revolution and one of the most efficient brains and arms of the country.³⁷

This overwhelming endorsement for the president by Khamenei, was followed by statement from the Islamic Republic's Supreme Court in which Chief Justice Hossain Moqtadai stated that those threatening the regime can and will be punished. In addition to the statements from these two powerful men there was also "orchestrated praise" of Rafsanjani and the administration from various publications. The timing suggests that these incidents were not coincidental, but were organized by the moderates as a major offensive against the radicals.³⁸ The moderates are in a strong position and are currently trying to build upon their strength. If they are able to address the economic needs of the population quickly, the chances of the radicals usurping power will decrease substantially. However, in the long term the government, whether run by moderates or radicals, must solve a number of problems if Iran is to develop economically and politically.

³⁷ This quote of Supreme Guide Ali Khamenei was taken from the *International Iran Times*, Vol. XXI, no. 12, 7 Jun 1991, 1.

³⁸ *International Iran Times*, Vol. XXI, no. 12, 7 Jun 1991, 1.

As in the beginning of the Republic, there is still disagreement regarding the degree of state control of the economy as opposed to private enterprise. Under the moderates, many of the state owned companies are being released for private ownership and the government is seeking new ways to encourage the private sector. According to Hooshang Amirahmadi, a combination of state intervention and private sector encouragement is needed.

Clearly the situation calls for increased public intervention and investment, particularly in R&D, infrastructures, and industries. However, the success of such intervention and investment policy would depend on how efficiently it is implemented. This is why effective investment planning has become indispensable to the country. To redirect investment toward industries, the government must also introduce incentives for the private sector and implement it with vigor and rigid discipline.³⁹

The government hopes that providing incentives for the private sector will allow for economic growth. This in conjunction with effective planning could lead to the reconstruction and modernization goals of Iran.

According to Homa Katouzian, for long-term peace, stability and progress, the Iranian political economy is in need of numerous changes. Katouzian provides a list of long-term politico-economic requirements and strategies for Iran. The requirements include:

- 1) creation of an alternative export sector to reduce dependence on oil,
- 2) promotion and diversification of domestic output, reducing the country's dependence on imports of

³⁹ Amirahmadi, 162.

- consumer goods, intermediate products and capital machinery,
- 3) sustained growth rate of national income and living standards consistent with the country's politico-economic capacity to absorb, and
 - 4) a direct and indirect redistribution of income, education, health and other social goods to the poorer classes of the community.⁴⁰

To accomplish these goals, Katouzian gives a list of strategies, some of which are more comprehensive than others.

Katouzian suggests that there must be investment in many of the local, labour-intensive industries and attempts at their renovation and modernization. In addition, there must be investment in basic consumer products, old and new, which are objects of consumption of the masses, such as textiles, appliances, education, health services, and housing. Investment in industries in which the country can reasonably compete in the regional, as well as world market, is also suggested. While the author proposes increased investment in many areas (some of which will produce more capital), she does not discuss where the initial capital is to come from. Is an oil-led industrialization strategy, such as the moderates propose, the proper strategy or is something different needed? In addition to the above strategies, Katouzian also argues that a complete redistribution of land among the peasantry with the provision of financial, technical and other extension services is necessary. While this proposal would aid in the redistribution of wealth in the country which is vital to long-term stability and progress, land distribution has been a very controversial issue for

⁴⁰ Katouzian, 370.

many years and it is unlikely that the powerful landowners that have defeated previous attempts at redistribution will turn over their property any time soon. In particular, if Iran remains a republic governed by Islam, which recognizes private property, redistribution will be difficult; even if the government changes, Islam will still remain an important factor in Iran and thus will complicate redistribution. Katouzian also suggests strategies including investment in universal free education and health facilities, development of the country's existing technology and skills, and rational and realistic attempts at the extension of the heavy industrial and engineering base.⁴¹ Katouzian's list of requirements and strategies for Iran is valuable for long-term planning, but there are areas that need more specifics if they are to be used by the administration.

Over the past decade the administration has used quick fixes to economic problems, rather than long-term planning. Practical domestic economic planning is needed for reconstruction and economic growth. An overall evaluation of the resources of the country and the goals must be made. Once these are determined, strategies can be adopted to move towards these goals. For example, economic growth is obviously one goal. Some of the most plentiful resources in Iran include natural gas and minerals. One growth strategy would be to invest in developing these resources, focusing on labour-intensive methods of development, which would also aid economic growth by lowering the unemployment rate. The

⁴¹ Katouzian, 370-71.

Rafsanjani administration has started long-term planning and has tried to develop strategies that are conducive to this planning. However, policy decisions must be continually evaluated as the environment changes. A brief examination of Iran's resources will allow for strategy suggestions that may move the country towards its goals.

Iran has numerous resources, many of which have not been used. The most obvious natural resource is oil. Iran has large oil reserves, and now that the war with Iraq is over, the damaged oil production and transport facilities are being repaired so that Iran may increase its oil revenues. The invasion of Kuwait boosted oil sales, and during the crisis the United States lifted its ban on US-based oil companies buying Iranian oil. The pragmatists intend to realize economic growth through oil-led industrialization and have partially based budget increases on projected oil revenue increases. However, there are drawbacks to Iran's oil resource.

First, for more than two decades Iran has depended on oil sales for the majority of its state revenues and for most of its foreign exchange. The decline in oil prices in the late 1970's and the oil glut on the market in the mid-1980's severely damaged Iran's economy. In addition, OPEC can and has manipulated the oil markets to Iran's disadvantage. Certain members have ignored their quotas and flooded the market, thus driving prices down, and Iran's calls for reduced quotas for all members have been ignored. Separate from these problems, Iran is also at a disadvantage because while it exports crude oil it has to import refined oil, which is a drain on revenues. The Abadan refinery is scheduled to reopen soon, but it

will not be able to provide the quantity necessary for domestic use, so imports will continue.⁴² If the oil resources are used wisely and if the world market is favorable over the next few years, Iran may be able to use the revenues to expand its oil production (including building refineries to provide enough refined oil for both domestic use and exports), and to develop other industries that will lessen Iran's dependence on the oil market.

One of the industries that is being developed is petrochemicals. Iran plans to produce 9 million tons of petrochemicals in 1993, which will allow the country to begin exporting these resources for the first time. Currently, Iran is importing as much as \$2 billion worth of petrochemicals each year, but by 1993 Iran's domestic needs will be covered by 80 percent of its production and the remainder will be exported.⁴³ Petrochemicals are a resource that holds vast potential for development. However, Iran has to develop more than its oil and petrochemical resources. A diverse economic foundation is necessary for sustained economic growth.

Another resource that has great potential and has not been developed is natural gas. Iran has the second largest natural gas reserves in the world. Some quantities are being exported, especially to Eastern Europe, but there are vast reserves that could be developed. Iran and Turkey have signed an economic pact in which they agreed to construct a natural gas pipeline from Iran across Anatolia, which may eventually supply parts of Europe with gas. In

⁴² *International Iran Times*, Vol. XXI, no. 4, 12 Apr 1991, 1.

⁴³ *International Iran Times*, Vol. XXI, no. 13, 14 Jun 1991, 2.

addition to natural gas, Iran also has various mineral resources that could be mined and used for domestic purposes or could be exported. Among these, copper is the primary mineral reserve. Little effort has been made to develop copper or any other minerals in Iran, although their production could provide Iran with materials that are currently imported and their export could bring needed foreign exchange reserves.⁴⁴ Long-term planning and proper investment in the production of these various resources would aid Iran in safeguarding its economic growth.

There should also be increased investment in many of the local labour-intensive industries. These industries, such as carpet-weaving and shoe-making, have a basis in Iranian culture and if expanded could provide increased employment.

Apart from these resources, Iran also needs to examine its agricultural sector. Up until the 1960's Iran was primarily an agrarian society. By the 1970's, due to population growth and unsuitable land reforms, Iran had become an importer of agricultural products. An ambitious program of reform should now be considered, in which technology appropriate for Iran's agricultural lands could be adopted and methods of improving crops analyzed. Land redistribution among the peasants and provision of financial, technical and other extension services, as suggested by Katouzian,

⁴⁴ The capital and skilled labor required to begin mining and production of various minerals can be quite high, which may be the reason that these resources have not been developed. However, investment in this area would provide jobs, would increase productive activity and could provide long-term security.

should be a long-term goal. The controversy over land redistribution will obviously surface, but this does not mean that the other strategies for improving Iran's agricultural sector should not be pursued.⁴⁵ The current administration must focus on moving away from the service industry, towards a production-oriented economy for sustained economic growth and development.

Intelligent economic planning requires goal setting, both short- and long-term, resource analysis, and the adoption of adequate strategies. Even with these, both the domestic and the external environment can change without notice, and planning must adjust. The goals of the current administration are numerous. Primary among these goals is securing the basic needs of the population, providing food and housing in particular. Lowering the unemployment rate and the inflation rate is necessary to ensure that basic needs can be met and sustained. Reducing the high population growth rate would allow these needs to be met with a greater degree of ease in the future. Reconstruction is also a goal. The damage from the war with Iraq and from the earthquake that shook the northern provinces in June 1990, is extensive. Reconstruction includes repairing infrastructures as well as rebuilding numerous industries. Factories, oil drilling rigs, and transport facilities are areas that the administration is currently focusing on rebuilding. Once progress

⁴⁵ Land redistribution could be approached in an incremental manner, in which the redistribution spanned a number of years. During this period, peasants could be trained to understand the best uses for their land so that once the transfer was complete, there would not be a span in which lack of technical skill would mean reduced output.

towards these goals is made, the administration can focus on modernization.

The current administration must avoid the Westernization that characterized the modernization program of the Shah.⁴⁶

Modernization, recall from chapter one, is defined as man increasing control over his natural and societal environment. It involves technological and organizational changes.

Modernization must be based on what is appropriate for Iran if it is to be sustained. The technological dimension will focus on industrialization and technology transfer. Industrialization should focus on goods consumed by the masses and products which Iran can sell competitively on both the regional and the world markets. Consumer products might include housing, textiles, and agricultural products. Products for external markets that could be developed include natural gas, petrochemicals, copper and other minerals. Current exports should also be expanded. The organizational aspect of modernization in Iran will involve specialization of structures and functions. As knowledge and control over the environment increases, it is necessary to create roles/functions and structures that specialize in particular areas. This generally translates into increased bureaucratization. Modernization allows man to increase his control

⁴⁶ Given the hatred of the West, particularly the US, that has been prevalent since the revolution, it is not likely that excessive Western cultural traits will be adopted. However, the technology that Iran may eventually import should be examined in terms of its appropriateness for that country, rather than its use in other countries (recall this was a problem in the land reforms under the Shah).

over the environment, but it also brings with it demands and expectations that often race beyond the ability to satisfy them.

In order to gain control over the natural and societal environment increased education and training are necessary. Education and training must be pursued to realize increased technology and higher level organization. For example, to modernize the industrial sector, engineers and trained workers are imperative. Iran will have to expand its training to produce skilled workers and will have to further develop its educational standards. Free education to expand literacy must be accompanied by an expansion of college level educational opportunities in diverse areas. However, while education helps increase control over the environment, it also produces economic, social and political expectations and demands which are difficult to meet.

James Bill and Robert Hardgrave wrote that "development is most usefully understood in terms of a system's response capacity in relationship to demands."⁴⁷ Modernization means increased demands on the system, but even without a planned program of modernization, demands will be made. Development understood in terms of response capacity, or the ability to satisfy these demands, is an ambiguous concept. It is easier to point out when demands are not being met than it is to deliver on demands. Under the Shah, modernization was pursued without regard to the social and political demands of the population. Economic concessions were made in

⁴⁷ James A. Bill and Robert L. Hardgrave, Jr., *Comparative Politics: The Quest for Theory* (Lanham MD and London: University Press of America, Inc., 1981) 67.

hopes that this would be enough to satisfy the population. As the revolution of 1979 indicated, this was not enough. During the revolution, in which there was a coalition of groups, each of which had its own ideas on how the system should run, numerous promises were made to satisfy the demands of the population. In particular, Khomeini promised the *mostazafin*, or disinherited, that their condition would improve. The Islamic Republic was designed to produce the rule of Islam in Iran, which Khomeini argued would satisfy the needs of the faithful. However, with the revolution, the war with Iraq, and the decline in oil revenues, the Islamic Republic has not been able to meet many of the needs or demands of the people. Rather, the economic conditions of many have worsened and repressive tactics have often been employed to quiet any elements critical of the regime. Since Khomeini's death, the regime has focused on improving the economy and thus meeting the economic needs and demands of the population. However, the administration must keep in mind that once economic headway is made, political demands will be made. Satisfying demands for increased participation in the political process will eventually be necessary.

CONCLUSIONS

The central issue addressed by this thesis has been the effect of the political economy on development in Iran. Development has been defined in terms of response capacity or the ability to satisfy the needs/demands of the population. Development in terms of delivering includes fulfilling economic and political requirements. Economic demands include basic needs, such as food and shelter, and relative needs. Relative economic demands generally increase as modernization takes place. For example, as the population becomes more aware of what technology is capable of, demands increase (some examples of relative luxury demands include appliances, automobiles, and other goods that are designed to make life easier). Political demands are also part of development. Once basic needs are met, the population begins to demand avenues for social mobility and for political participation. Political participation need not come in one specific form, but a developing society must provide methods for the population to at least articulate its interests if that society is going to progress.

Development is not solely affected by the interrelationships between economics and politics; there are social and cultural factors that obviously play a role in development also. The scope of this paper however, has been limited to the relationship between development and the political economy in Iran. The dependent variable of development has been examined in terms the interaction

of economic conditions, political decisions, and global and domestic factors.

This thesis has traced the political economy of Iran from the 1960's through the present. The political economy is a product of the interaction of the decisions and the environment within which the political and economic systems function. The economic and political systems of a society are determined by a number of factors. Three of the most important factors in these systems are the decisions of the leadership within society, the domestic environment and the international environment. These three factors interact and produce changes, both negative and positive, in the political economy. This political economy in turn, helps determine the degree of development which society attains. If environmental circumstances are favorable and practical economic policies are adopted, economic growth is the result. Similarly, political development can be made if favorable economic conditions are maintained and the leadership of society responds to the economic and political demands of the population.

This paper has focused on the environmental conditions and decisions that have inhibited development in Iran. By pointing out the factors that contributed to a lack of development for this society, it was possible to suggest alternatives that may improve prospects for development. While economic growth was strong in the early 1970's, the Shah's regime did not direct revenues toward long-term economic development, and the upward trend did not last long. Neither did the Shah respond to increasing demands for cooptation into the political process, especially by the middle class. Largely as a

result of these economic and political factors the Shah's regime was overthrown in the 1979 revolution.

A similar analysis was made of the post-revolutionary period in Iran, in which environmental conditions, including the war with Iraq and the soft oil market, largely prohibited economic growth. In addition, the administration often employed repressive tactics to control the political process. Mass mobilization rather than participation was the focus. Finally, the past two years were examined and an analysis of prospects for future development was offered. Practical use of domestic resources combined with a willingness to politically coopt a larger share of the population are important steps towards economic growth and political development.

Further political development, in all likelihood, will involve providing channels for individuals and groups to articulate their interests. Demands will most likely include increasing social mobility and providing for increased political participation. There are no proven models of political development. Western democratic-pluralism is often viewed as the final product, but numerous arguments have been brought against this viewpoint. Iran will have to find a balance between ideology and pragmatism if the revolution is to survive and the country is to progress. Iran holds a great deal of potential that make its long-term prospects good if proper planning and resource management are employed.

This case study of the interrelationships of political economy and development obviously does not address a number of questions: 1) What are the social and cultural (including religious) factors in development? 2) Is the same relationship applicable to countries

other than Iran? 3) Is there a specific approach to political economy that would guarantee economic growth and political development? While this is not a conclusive list of the questions that could be addressed in conjunction with this thesis, it suggests directions for further research.

The goal of this study was to gain insight into the interrelationships of politics and economics and their effect on political development, specifically within Iran. It has been argued that the economic and political systems in society are products of the interaction of decisions and environmental conditions. Hopefully, what has been presented is an unbiased examination of Iran's political economy, followed by practical suggestions for future development.

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