

## **The Role of Oil in Contemporary Economic and Political Development of Iran (1949-79)**

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### **Abstract**

This article focuses on the political economy of oil in Iran's development planning from the First Plan following War II until the Fifth Plan of 1979. The history of economic planning in Iran from the First Seven-Year Development Plan of 1949-1955 to the Fifth Development Plan of 1973-1977 is characterized by an intimate link between oil income and planning.

Approximately 55%-90% of the Plan and Budget Organization funds came from oil (the low figure refers to the second plan and the higher number to the fifth plan). The overwhelming majority of the government's income was generated from oil. It reached 88% in 1974- and the planned percentage for 1975 was even higher. This article examines the role of oil in the national political economy this period. The term political economy refers to the method of the study that involves an interdisciplinary approach.

### **Introduction**

In the aftermath of War II the history of planning in Iran from the First Seven-Year Development Plan of 1949-1955 to the Fifth Development Plan of 1973-1977 is defined by the link to oil. Approximately 55-90% of

planning funds came from the oil sector (the two limits refer to the second and the First Five-Year Development Plans respectively). The bulk of receipts were provided by the oil sector with no other sector even a distant

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This point is emphasized by the fact that in 1974 the share of oil revenue in government income amounted to 88%. The planned percentage for 1975 was even higher (Keddie, N., *Race and Class*; Volume 21; no. 1; 1979; P. 18) as already mentioned. However, the outstanding characteristic of the oil sector throughout this period makes clear that it was not indigenous to the functioning of the economy, but rather superimposed on it. Let us first examine the international developments that surrounded Iran's political economy.

### **The effects of international events on the political economy of Iran**

The Allied invasion of Iran in the first years of World War II put in motion a process that completely disrupted national developments and reforms dating from the late 1920s and 1930s. This period completed the transformation of Iran's mode of production from oriental despotism to a relatively primitive form of rentier-state. The new model was capitalist based. The era of dramatic change in the country's political economy did not occur in and of itself, but in the context of a changing constellation of regional arrangements and international events, all of which coalesced during this same time frame in Middle East history.

In the years between 1941 and 1953, the US practically replaced both the Soviet Union and Great Britain in the region. Indeed, World War II constituted a turning point in US policy regarding Middle Eastern oil. The immediate regional consequences of this policy were the containment of Soviet influence, and the preservation of conservative local regimes. Iran was central in both these spheres.

The outstanding post-war problem faced by the US revolved around the attempt to displace British influence in the Middle East, and consequent

competition between the US and Britain for the acquisition of oil concessions in the region. Thereafter, however, the development of the Cold War, combined with the growing anxiety about the security of Persian Gulf oil, placed Iran in the forefront of American foreign policy concerns.

Some 57% of the world's oil flowed from the Middle East. Most consuming countries depended directly or indirectly on the region's energy and consequently were vulnerable to domestic economic disruption which would result from an interruption in supplies, and the threats to Middle Eastern producers were numerous with no countervailing comprehensive system for containing them.

American policy makers held that waning British power in the region was creating a vacuum that it was in the interest of the US to fill. Any explanation that ignores the attraction of Middle Eastern oil for both oil executives and national security managers of the period is deeply flawed and at great variance with the extant realities of the period.

However, in this era there were several factors signaling changes in the underlying political and economic reality. These included the 1960 organization of OPEC; the Arab-Israeli war of June 1967 and the decision by Britain in January 1968 to withdraw from the Persian Gulf. This was followed by the US decision to underwrite Iran and, to a lesser extent at that stage, Saudi Arabia as their geopolitical guarantee for the area.

Libya's September Revolution of 1969 unleashed a radical change in political confidence throughout the region that was another complicating factor. These events completely altered the political and economic climate in the region's favor and gave Middle Eastern countries a remarkably stronger degree of resolve and will in their dealing with the great powers (Stork, J., 1975, PP. 29-55).



This new era can be accurately dated from the second half of the 1960s, a period of transition for Iran. East-West tensions were relaxing and Tehran's role was shifting from an exclusive emphasis on relations with the superpowers to a preoccupation with regional affairs and internal consolidation. These changed circumstances and the attempts being made to accommodate them were influenced by a number of events occurring elsewhere in the world in mid decade.

The outstanding event was the large US troop commitment to Vietnam that began in 1965. China was facing containment through the US naval presence in the Pacific, Indian troops on their common southern border and 50 Soviet divisions along its northern border. China's Cultural Revolution that began in 1966 coincided with the British decision to pull out of Aden in February 1966. These elements taken together with the growing debate in Britain for pulling out of the Persian Gulf were seen as proof by the Soviets that a power vacuum was indeed opening up along the southern and eastern periphery of the Middle East. It was a vacuum the Soviets thought they could fill.

In surveying the Soviet position in the world following Nikita Khrushchev's removal from power in 1964, Leonid Brezhnev and Andrei Kosygin apparently concluded any further expansion of Soviet influence in Western Europe and Latin America was out of the question, at least for the time being. These areas were of vital importance to the United States, which had demonstrated clear military superiority over the USSR during the Cuban missile crisis. Similarly, the active hostility of Communist China confronted Moscow with a dangerous obstacle to the spread of their influence in south and South-East Asia.

The USSR still retained several important African footholds. Soviet leaders evidently decided that, given the expanding opportunities in the Middle East, they should begin to concentrate their military and economic

assistance there. It was an area in the near vicinity of the USSR with greater possibilities for Soviet gains (Foran, J., 1998, PP. 514-15).

At this juncture in the middle 1960s Iran's relations with the USSR had stabilized and continued to develop. The symbol of this new era was the establishment of a steel mill and the purchase of unsophisticated military transport vehicles in 1966.

Regarding US-Iran relations at the beginning of the 1960s, the Kennedy Administration sought to engage in a bit of 'social engineering' in Iran. This was most visible in using its considerable economic leverage to dictate the size of Iran's armed forces. However during the Johnson Administration relations, improved without such gambits. In terms of domestic affairs, as Iran's oil production increased and the stability of the regime was consolidated through a variety of reform programs the government became more confident. Meanwhile the imminent British withdrawal, first from Aden and then from the Persian Gulf in 1971 provided a new role to be filled. Iran quickly adapted to the new circumstance (Ambrose E. Stephen, PP. 181-200).

It was in the area of foreign policy that the Shah excelled and it was here that he increasingly placed his political emphasis. In October 1971 he announced his intention to undertake major international political and economic responsibilities in the region. The new era of Iran's willingness and ability to assume greater burdens in assuring security in the Persian Gulf meshed precisely with the Nixon Doctrine announced in June 1969, which encouraged this type of initiative. The transition from credit sales (financed by the US Import-Export Bank) to cash, completed by 1970, facilitated this and was aided by increased oil revenues (Ibid. PP. 201-265).

Before attempting an analysis of the role of oil in development planning in Iran that started only in 1949, it is essential to understand what is perhaps the



outstanding feature of Iranian society: it is a rentier state.

### **Rentier States as a Theoretical Framework**

Iran under Mohammad Reza Shah became a 'rentier state' relying on petrodollars and closely linked to the rhythms of the world capitalist economy. According to Mahdavi, 'Rentier states are those countries that receive (revenues) on the basis of substantial amounts of external rent' (Mahdavi, H., 1970, P. 248), paid by foreign governments or foreign concerns. Payments for the passage of ships through the Suez Canal or payments to countries in the Middle East, that have oil pipelines passing through their territories, are examples of external rents. Most outstandingly the oil income received by the governments of the producing and the exporting countries are included in such rents.

The significance of the oil policies of these 'rentier states' is that the money thus received has little to do with the production processes of the domestic economy. Inputs, other than raw materials from the local economy, are insignificant. In this context, the period 1950-56 is considered as a turning point in the economic history of the Middle East.

Political developments in the 1950s involving Iran and Egypt, the two largest countries in the Middle East, allowed regional governments to appropriate a larger share of the rents that previously accrued to the oil companies as profits. Precisely in this period Iran's oil nationalization movement began to gather momentum in 1950. The Suez Canal was duly nationalized in 1956.

To emphasize the point suffice it to say that oil firm payments to Iran during 1956-61 exceeded by 300% the total remuneration during the 39-year period that ended in 1950.

According to Issawi and Yeganeh, during the years 1913-49 the oil companies paid only USD 483m to Iran, as compared with the payment for the period 1956-60

that amounted to about USD 1, 160b) (Issawi, 1962, Table 39).

These increased funds allowed the governments of the oil-producing countries to embark on large public works expansion programs without resorting to taxation and running into drastic balance of payments deficits. Since oil revenues typically increased at a much faster rate than the gross national product of the local economies, the public sector of the oil-producing countries expanded rapidly.

As a result of the reliance on the petroleum revenue 'The government becomes an important-or even the dominant-factor in the economy' (Mahdavi, 1962, P. 432). The rentier oil-producing state could achieve dramatic rises in per capita income without going through the social and organizational changes usually associated with the process of economic growth, because government revenues are not gained through production as such but from oil royalties which come from outside the economy.

While the state is the chief consumer, investor and employer, it does not depend (directly or indirectly) on domestic production for the maintenance of a high level of expenditure. In fact the historical dynamic is reversed. Now the domestic economic sectors, including the private sector, are dependent upon the state for direct and indirect welfare gains through the latter's disbursement of oil revenues (Katouzian, H., *The Journal of Peasants Studies*, Vol. 5, 1979, P. 349).

This circumstance provides such governments' an exceptional relative autonomy from its social classes and other groupings. In other words, "To the extent that the oil revenues make the state dependent of the domestic means of production and the social classes, the latter becomes dependent on the state for any employment" (Ibid. P. 349).

The state thus becomes the exclusive source of economic and social power, a power moreover which is



independent of the productive effort of the community. Thus it tends to accumulate all rights and obligations, and through this process it affects the form and substance of the class structure. The formal traditional class composition may remain intact, but it loses a large part of its *raison d'être* in social relations, social mobility and income distribution.

Given this, "social stratification then becomes a function of economic dependency upon the state. In fact the classes with the highest potential independence from the state display the greatest actual degree of dependency on it. Let us call this social category the *clientele*" (Ibid. P. 349).

The concept of *clientele* has been particularly used with telling results in regard to Third World countries, "Where the political process cannot be fully accounted for in terms of horizontal class relations. To be more specific, it refers to a situation where there is no effective electoral competition, that is, no political parties, trade unions or other interest groups through which the clients can express their opinions and shift the balance of oil power to their advantages. Consequently there will be both a feeling of economic insecurity and social uprootedness among the masses and a parallel feeling of insecurity among those in power that denotes their lack of legitimacy. The *clientele* poses the greatest potential threat to the state monopoly of socioeconomic rights; it therefore takes the highest share of the state's obligations" (Le Marchand, R. and Legg, K. in *Comparative Politics*, Vol. 4, no. 2, 1973).

In the light of the above general sketch the country entered the period beginning in the mid-1950s and continued until the oil boom years, 1973-78. As might have been expected, the greater part of the non-oil economy imposed few demands on the oil industry, and responded little, if at all, to increases in the supply of oil or the demands for supply of skilled labor and other inputs needed by the petroleum industry.

Oil in and of itself fueled most socio-economic failures. The improper use of petroleum led to an uneven growth in purchasing power in the urban community, radically changed the structure of the economy, rapidly increased social and geographical mobility and brought the traditional and lower social strata into the sphere of modernist mass consumption. This raised social and material expectations that could not possibly be met and undermined cultural traditions and communal relations without replacing them with viable substitutes. It led to acute bottlenecks and imbalances, both between and within the various economic sectors and entities, and drastically separated the state from society (Halliday, F., 1987, PP. 204-212).

As we have seen the new era started in the mid 1950s, but for better understanding the above framework it is important to begin the analysis from the 1949 First Development Plan enacted by the Iranian Parliament some six months after its inception. It represented a first attempt for the organization of the national allocation of public resources according to a predefined national strategy of development. Iran's First Development Plan (1949-55) was to be financed chiefly by oil revenues. By 1950, just prior to nationalization of the petroleum industry, production was running at 31. 8m tons. Direct revenues registered £16m, i.e. quadruple the amount of 10 years before as Elwell Sutton mentioned in his book.

### **The First Economic Development Plan (1949-55)**

The First Economic Development Plan was heavily influenced by the American engineering consultants, Morrison-Knudson Company, and Max Thornburg, a US oil man. In the late 1940s, an Economic Bureau was set up in the Plan and Budget Organization. The process was aided by a group of foreign advisers under the auspices of Harvard University.



The US Foreign Operations Administration (FOA) (1) believed that, even with an oil settlement in place after the successful coup against Mossadeq, it would be three years before Iran's oil revenues would permit her to finance large-scale development from her own resources. To help Iran during this interim period in development planning, the US decided to make a sum of up to USD 127. 3m available. The FOA and Export-Import Bank were authorized to provide these resources (Alexander, and Yagnah, PP. 276-277).

The FOA was confident that the loan fund would help Iran implement her extensive plans for economic development. The scheme contained measures to guide the government specifically in its expenditures throughout this period, and, by setting up a Plan and Budget Organization (PBO), to oversee and control these disbursements according to predefined national objectives.

Part of the plan period included the nationalist era of the Mossadeq government, but despite American refusal to grant financial aid to the government during 1951-53, the administration was successful in the field of foreign trade accounts. It restricted imports without cutting them drastically, and, at the same time, initiated a great effort to boost the country's non-oil exports. Indeed Iran managed to accumulate a surplus in its non-oil trade account.

**Table 1.** Non-oil trade figures for the period 1948-53  
(in million Rials).

Year	Exports (non-oil)	Imports	Balance of Import-Export
1948	1,867	5,480	-3,613
1949	1,785	9,320	-7,535
1950	3,563	7,109	-3,546
1951	4,391	7,405	-3,014
1952	5,832	5,206	+626
1953	8,426	5,756	+2,670

Source: Ministry of the Economy; Foreign Trade Statistics; 1966.

These successes highlighted that much could be achieved in the right socio-political atmosphere, in spite of great financial and economic scarcities and deprivations. The 1949-55 plan contained guidelines for the allocation of government expenditures. Under Mossadeq's government a quarter of the proposed expenses were given to agriculture, 32% to social welfare and postal and telecommunications plans, and 24% to industrial and mining projects, including oil exploration outside the domain of the Anglo Iranian Oil Company (AIOC).

Some 60% of the required funds for financing the projects were expected to come from oil revenues and World Bank loans, and another 21% from domestic credit creation. Unfortunately, adequate funds were denied to the Budget and Plan Organization due to internal conflict, the British oil embargo and the failure of the country to raise foreign loans (Maclacklan, Keith; in Amirsadeghi & Ferrier R.W., (eds.), 1977, P. 135), forcing the Mossadeq government to essentially abandon the first plan. Indeed the oil disputes of 1951-53 left the plan for all practical purposes suspended.

However, after the coup, American aid to Prime Minister Fazlullah Zahedi's and the oil revenues of 1954-5 were generally spent on consumption and brought the economy out of recession. In the wake of that event, rapid increases in the states' oil revenues and extensive US military and economic aid enabled the Iranian economy to recover rapidly.

Iran made heavy use of foreign technicians, arms and expertise, provided by the US through the Point Four Program. In fact by June 1954, no fewer than 38 projects approved by the Point Four Mission were among the first plan projects that previously had to be postponed. This increased American involvement in Iran covered a variety of areas including agriculture, industry, public health, education and public administration. The US government also extended



financial aid to meet the deficit in Iran's operating budget. During the period 1954 to 1956, the government of Iran received the sum of USD 60m, USD 53m and USD 35m respectively (Sutton, L.P. Elwell; 1955, P. 313. and Foran, J., 1376/1998, PP. 510-11).

The state then began to use its growing revenue to promote rapid economic development through a series of development plans formulated and implemented by the Plan and Budget Organization. According to Jahangir Amouzegar, at the end of the first plan period the programs had not achieved their proclaimed objective of improving the living conditions of the Iranian masses. On the whole, the first plan accomplished little, achieving essentially no more than the setting up of planning machinery and the renovation of industries established under Reza Shah. However, the first plan priority expenditures were in fact disbursed and the expenditure pattern favored agriculture over industry and transport.

## The Second Economic Development Plan

### 1956-62

Most important steps toward economic development were taken under the Second Economic Development Plan. The scheme placed emphasis on the agriculture sector, transport and communications systems. Most allocations went to the agricultural sector in order to complete three large dams, namely Karaj, Sefid-Rud and Dez. These dams helped to provide large-scale irrigation suitable for agro-industrial company activities in Iran.

The achievements in the industrial sector were confined to the construction or modernization of large textile, sugar and cement factories. The production capacity of the textile industry rose from 60m to 480m meters of cloth by the end of the plan. Sugar production increased from 103 thousand metric tons in 1956 to 159 thousand metric tons in 1960. Finally, cement

production rose from 224 metric tons in 1956 to 797 metric tons in 1960. The plan was drafted on the basis of the agreement of 21, October, 1954 between Iran and the international oil companies (Bharier, J., 1971, P. 69 and P. 273).

The oil companies' involvement in the programming process in Iran is an indication that at the time the Iranian planners themselves believed that oil revenues would fuel the scheme. Thus it was decided to allocate an annual average of 75% of oil revenues for the period to the activities of the organization.

In addition to these revenues the country received substantial sums of foreign grants, loans and investment. Between 1955 and 1962 Iran's receipts of foreign exchange from oil and aid alone were, on average, about 17% of its annual national income. Table 2 below shows the drastic rise of oil revenue from £16m in 1950 to over £100m in 1960 and to £183m in 1965.

**Table 2.** Oil Production and Government Revenues from Oil during 1950-65.

Year	Oil production in tons	Oil revenues in £
1950	31,750,147	16,031,000
1955	16,515,000	32,323,764
1960	53,528,000	101,877,471
1965	93,300,000	183,300,000

Source: NIOC; Six Decades of Iranian Oil Industry; Tehran 1966.

The second plan was in many respects similar to the first. Although it contributed to the development and stimulated a degree of private sector industrial development, the rapid growth that characterized the period resulted in a balance of payments squeeze and rapid inflation. For instance the total current account deficits for the years 1958 to 1961 amounted to USD 236. 7m, equivalent to 66% of the country's foreign exchange receipts from oil exports in 1960 (Central Bank of Iran; Annual Reports, 1960).



The failure of the government of Iran to obtain additional funds forced her to enter into a program for economic stabilization prescribed by the International Monetary Fund (IMF) in 1959. It was obliged to accept the austerity measures relating to the restriction of imports cutting of public expenditures, and raising the rate of interest.

The immediate result of the IMF program was to turn the 1957-9 booms into Iran's first post-war industrial-type recession. This, in turn affected the traditional sectors, namely bazaar merchants, day laborers, small farmers, and the middle class. At the same time the general economic situation was deteriorating. There were widespread strikes, prominent bazaar merchants were facing bankruptcy, and there was a pervasive perception both inside and outside Iran, that the Shah's regime was faltering (Amouzegar, J., 1993, PP. 3-13).

However, the effect of the sudden increase in oil revenues on Iran's foreign trade can partly be observed from Table 3. The table shows that great changes occurred after 1955. Imports increased more than fivefold between 1955 and 1960. This sharp upward trend leaves little doubt that the country's imports had faced two basically different phenomena: the moderate rise of the first half of the century, and the marked increase since 1955. However in terms of non-oil exports no such trend is observed. Precisely, the gap between imports and exports was the result of the difference between the rates of growth of the two variables. This difference was covered mainly by oil exports.

**Table 3.** Foreign Trade of Iran, from 1955 to 1960 (Values in Million Rials)

Year	Imports value	Import volume	Exports value	Non-oil export volume
1950	6,242	504	3,563	194
1955	9,125	637	8,034	508
1960	52,657	1,914	83,600	446
1965	66,083	—	13,740	—

Source: Customs Administration Yearbooks, Tehran, Iran.

It is clear that without the receipt USD1, 278b in aid, the import of goods would not have been as high as that shown in the table. Moreover lack of a comprehensive approach to planning during this period was a major contributor to the 1960-62 recessions (Daftary, F., Iranian Studies, no. 5, Winter 1972) (2). Nevertheless the second plan did contribute to the expansion of an infrastructure network essential for the raising the overall level of economic activity, whether private or public. The priority of second plan spending was allocated primarily to four major economic sectors: Agriculture and irrigation, industry and mining, transport and communications, and social affairs.

### **The Third Economic Development Plan 1963-67**

Following the unsatisfactory experience of the first two plans, the Third Economic Development Plan was Iran's first large-scale effort at comprehensive, calibrated growth. The features of the scheme were an investment program for the public sector and certain forecasts for the private sector. The plan's primary purpose was to achieve a rate of growth of 6% per annum (3).

Planned expenditures for the public sector amounted to USD 2.5b but by the time the scheme was formally approved, it had been reduced to USD1.9b due to a decline in national revenue. In the plan a sum of USD 2b was allocated to the private sector. Table 4 indicates that during the period 1954-64, government investment declined from 48% of total expenditures in 1954 to 27% in 1964. However, various economic indicators show that both government expenditures and investment increased sharply after 1964, in the wake of a 70% per annum increase in oil revenues.

The new strategy for development concentrated on industrialization, agriculture, transport and social affairs. The investment share of industries and mines was set at below 12%, while that of transportation and communications was to be about 24%. The goal of the



plan was to promote rapid import-substitution industrialization. The allocations to agriculture and irrigation were largely taken up by the construction of large dams.

Although the plan promised that growth would be twinned to attention to social justice, the treatment of these questions in any systematic manner was never attempted. The goal of creating employment, for instance, had been ranked well below that of economic growth, and the other secondary goals mentioned earlier never seemed to have been integrated comprehensively within the framework of the plan (Plan and Budget Organization, Outline of the Third Plan; PP. 37-39).

The plan not only failed to consider the reciprocal effects between economic growth and social justice, but was remiss in providing even the most basic integration between public sector programs and private-sector activities. When considering the third plan special attention ought to be given to the crucial role of the private sector in the process of Iran's economic develop-

ment. The share of private investment (USD 2b) throughout the planning period surpassed that of public capital outlays. The period of the third plan was characterized by a number of negative features, including two years of economic recession, political instability, the Shah's White Revolution scheme, and the bloody uprising of June 1963.

The Shah's response to the situation of the country apparently arose as a result of pressure from the newly elected Kennedy Administration. According to the Kennedy program, the essential reason for supporting political reform and economic development in the Third World was to increase American influence while nullifying the appeal of Soviet communism (The Economist, 17th April 1962, P. 35) (4). Kennedy adopted a foreign policy designed to encourage peaceful reform from above in order to forestall violent revolution from below.

**Table 4.** Iran's Expenditure as percentage of total expenditure, 1954-9 and 1963-6.

	1954	1955	1956	1957	1958	1959	1963	1964	1965	1966
Defense	38	41	40	38	40	38	39	38	42	45
Education	16	14	20	22	18	18	23	21	22	23
Health and welfare	7	—	65	5	7	6	5	7	7	11
Public Investment	48	38	47	43	39	34	22	1.7	—	—

Source: Plan and Budget Organization and Ministry of Finance

However, in addition to this policy the Kennedy Administration adopted a second tactic in its attempt to deflect the communist threat in the Third World. If the reforms failed, the elites friendly to US interests would have to employ military force to smother popular uprisings. A significant counter-insurgency program was initiated during the Kennedy years. Accordingly, the friendly elites were encouraged to adopt similar approaches in case of difficulty (Bill, J., *The Lion and the Eagle*, 1988, P. 132).

Kennedy's policy toward Iran was a clear and consistent application of his general program of reform from above and ultimately buttressed by the military might of besieged Third World regimes. He had first become concerned about the political stability of the Pahlavi regime in Iran in April 1961. This was less than a month after he had first announced the idea of the Alliance for Progress and when he learnt about the results of Walter Lippmann's discussions with Soviet Premier Nikita Khrushchev. During the discussions Khrushchev singled out Iran as an example of a country



heading towards revolution despite its very weak communist party (Ibid., P. 132).

Consequently, the Kennedy Administration rose to the challenge by selecting Iran as precisely that country in which the US could and would help promote reforms. In the early months of 1961 a chorus of influential voices both inside and outside the new administration warned of possible trouble in Iran. At the Department of State Iran analyst John W. Bowling wrote two thoughtful nine-page analyses of the country's internal political situation. In the first, prepared in early February, Bowling carefully examined the gathering opposition forces in Iran and recognized the unpopularity of the Shah's regime among the burgeoning middle classes (Ibid., P. 133).

In his second paper, delivered on March 20, Bowling listed 14 specific suggestions that would enable the Shah to deflect the serious challenge of the urban middle class. This important list became to some extent the blueprint of the Shah's reform program carried out over the next two years.

Meanwhile, at other levels of government Iran specialists were warning of trouble in the country. On 2<sup>nd</sup>, April 1961, a week before Khrushchev's discussion with Lippmann, Professor T. Cuyler Young of Princeton University communicated, his reservations to Walter Rostow in the Kennedy White House. In a letter dated 19<sup>th</sup> April 1961, written shortly after he had arrived in Iran on a research visit, he commented: "This regime is considered by most aware and articulate Iranians as reactionary, corrupt, and a tool of the West (and especially Anglo-American Imperialism)" (Cuyler, T. Young; 1965, PP. 22-23, in Bill, J.,... *The Lion and the Eagle*, P. 159).

The fact that US economic and military aid had been used to shore-up the regime was ample evidence of US approval and support. Bowling and Young recommended that the Shah should:

- 1) Reduce pomp and ceremony,
- 2) Exile or hold in check those members of the royal family who were known to be corrupt,
- 3) Reduce his state visits and absences from the country,
- 4) Espouse vigorously reforms in the judiciary, the armed forces, the civil service; the planning system, land tenure, taxation system, education and foreign policy,
- 5) Remove gradually most US advisers from the Iranian government,
- 6) Withdraw from his openly pro-Western international posture with as little damage as possible to the free world's morale and to his own prestige,
- 7) Make menacing gestures against the oil consortium and extract concessions from it to give the impression that the consortium was reluctantly bowing to his power and determination,
- 8) Appoint respected moderate Mossadeq supporters to positions such as those of the Minister of Finance and head of the Plan and Budget Organization, where they could assume responsibilities without being able to reverse policy,
- 9) Open the Pahlavi Foundation to public inspection and its books to public audit, and
- 10) Proceed loudly, with at least a token land distribution program, against the big landlords (Bill, J., *The Lion and the Eagle*, PP. 134-135).

The analyses and policy considerations took on special relevance in May 1961 when violence erupted in many cities of Iran. In Tehran up to 50,000 marched to protest about their wages and working conditions. It seemed that the situation was threatening to veer out of control. The Shah reacted immediately by dismissing the cabinet of Sharif-Emami and, with strong US



encouragement, appointed, Dr. Ali Amini to head a new government.

Iran's instability deepened the concern of American policy makers, and in June, influential voices in the US Senate joined the chorus of criticism. Privately, the Shah was worried about the Kennedy Administration; he had quietly supported the Nixon candidacy and feared criticism and pressure from the Democrats. Later, in 1969, he told an American interviewer: "My difficult period was in 1961 and 1962" (Ibid, P. 159). During his first visit to the US, the Shah was impressed by the message from the Kennedy Administration and slowly began to shift, albeit temporarily, the emphasis of demands from military to economic priorities.

Yet, according to the Economist in a report published during the Shah's visit: "The Shah seeks more military assistance, while Amini is concentrating on getting economic aid. The Kennedy Administration must certainly be reluctant to pay more for the Shah's army, though the Shah may quite forcibly argue that reforms are in their nature disruptive and that therefore, if he is to support them, he must have his army strengthened against such outside dangers as Russian radio campaigns" (The Economist, 14, April, 1962, P. 130).

Kennedy was concerned to smooth out the differences between the Shah and Amini. The conditions set by the US were that Amini must remain as the prime minister, and that the aid would not be continued if reforms were not carried out. For the third plan, Iran needed USD800m in foreign aid and most of this amount had to come from the US. Hence the conditions Kennedy laid down inevitably carried weight.

On taking office, Amini made a series of controversial decisions. He dissolved the newly-elected 20<sup>th</sup> Majlis (The Economist, 1962, P. 14), many of whose members were influential conservative landlords. He exiled the notorious General Teymour Bakhtiar, the head of

SAVAK (the State Intelligence and Security Organization), and initiated discussions with the National Front (5).

Moreover, he gave three ministries to middle-class reformers who had in the past criticized the political influence of the shah as well as the corrupt practices of the landed families. These were the Ministry of Justice, Ministry of Education and the Ministry of Agriculture. The latter ministry went to Hassan Arsanjani, who had been advocating land reform since the early 1940s.

From the latter half of the 1960s, parallel to the land reform program, a series of reforms known as the White Revolution, that included the ambitious aim of restructuring the organization of production in Iranian agriculture, were introduced. The land reform was the most important policy of the White Revolution. This program was based on the principles of:

- 1) Distribution of arable land,
- 2) Nationalization of woods and forests,
- 3) Electoral reforms including the granting to women of the right to vote and to be elected to the Majlis,
- 4) De-nationalization of state monopolies in order to finance the land reform program,
- 5) Company profit-sharing for industrial workers, and
- 6) The expansion of the literacy corps, created in 1963, which sent the educated conscripts to campaign against illiteracy in the rural areas (Bharier, J., Chapter 7).

In 1964 a health corps was established along the same lines. Participation in these institutions was a form of national service, and thousands of urban residents were dispatched to the rural areas.

The immediate response to these measures was political turmoil. The most important challenges came from two sources. One group was the landlords, who saw both their economic interests and their socio-



political bases as a class threatened. The second was various groups of the religious community who opposed different aspects of the reforms. Unlike other religious figures, Ayatollah Ruhollah Khomeini did not attack the reform, but instead focused on popular issues including the regime's corruption and disregard for constitutional principles.

However not all the challenges came from the clergy. Other social and political forces such as the National Front, the Tudeh Party, the Bazaar community, the political forces such as the Freedom Movement led by Mehdi Bazargan and Ayatollah Mahmoud Taleqhani, as well as the workers and the students opposed the situation on various grounds.

Nevertheless all these came together in the form of a mass movement led by Ayatollah (later Imam) Khomeini. The common concern of all these classes and groups was the extension of the despotic power of the Shah and the hegemony of the US over Iran. The Shah's reaction was immediate and violent. In June 1962, his troops ran amok for three days. The Shah suppressed the opposition, crushed the popular revolt and banned all political activities. Despite these events the land reform was implemented, in three phases beginning in 1962 and officially ending in 1971 (Abrahamian, E., chapter 9).

Despite this background, Arsanjani was determined to carry out a comprehensive program of land distribution among the peasants. His main concern was the financing of landowners. He claimed that the compensation payable to the landowners could be carried out through the Agricultural Bank without any need for foreign borrowing or creating inflation. According to him the cost of land reform was about USD 1 billion. This was the financial sum necessary for the purchase of all the land then available for distribution (The Economist 22, December 1962, P. 121).

The rapid pace of land reform imposed a heavy financial burden on the government. In 1963 the full

implementation of the program would have cost USD 27m, but the Government obtained less than a quarter of this amount. Financing was a problem everywhere: revenues had been lower than the planned figures and the planners struggled to reduce a projected deficit of USD 160m to a more manageable figure. According to an Economist article, "Two ministers have offered to resign rather than comply with the budget reductions package, and army chiefs have not been happy about the rejection of their proposal to increase army pay by a quarter" (The Economist 14, July 1962, P. 161).

The dispute over the budget of the army had been raised for some time, though not in public. The army, comprised of 200,000 men, received about 28% of the current budget. With the inclusion of development spending, the share of the armed forces would be reduced to only 18%. The government had received a grant of USD 15m in 1962 and expected to receive another USD 9m from procurement funds (Ibid. P. 161).

Yet further cash assistance to the army from the US was highly improbable. It seems that the message was delivered to the Shah during his visit to Washington in April. While the Shah sought more military assistance, Amini concentrated on obtaining economic aid. Iran needed USD 800m of foreign aid for its third plan but was calling for a total investment of USD 1.9b, of which would have to come from the US.

Meanwhile, Washington imposed pressure and in 1964 obtained from the regime an agreement of status-of-forces granting the American military personnel in Iran diplomatic immunity. Few political observers or scholars of Iran then understood the long-term significance of what was happening. One notable exception was Cuyler Young of Princeton University, who witnessed first hand in Iran the explosive anti-Americanism that rose in reaction to the granting of immunity.



Young held that the agreement was a catastrophe for American interests in Iran, as the nationalistic and religious intelligentsia opposed the immunity bill (Bill, J., op. cit., P. 159). On 26, October, 1964 the day after the Majlis approved a USD 200m loan for military equipment, Ayatollah Khomeini publicly condemned the immunity agreement. His fiery speech stands as one of the most important political statements made in Iran in the last century.

In his remarks Khomeini forcefully and straightforwardly attacked both the Shah and America for attempting to destroy the dignity, integrity, and autonomy of Iran. The Shah's government responded quickly to the speech. He was arrested and exiled to Turkey on 4, November, 1964 (Bill, J., op. cit., PP. 158-60, and Mahdavi; in Foreign Affairs, Vol. 44, nos. 1-4, October 1965, PP. 145-6).

To sum up, the results of the land reform program, that lasted almost a decade and was organized in three phases, were as follows:

- 1) The landlords were eliminated as a political and social force in Iranian rural societies,
- 2) The reform created a new rural bourgeoisie and a new proletariat,
- 3) The intervention of the state increased in the villages,
- 4) The state was able to influence the new classes through the building of new manufacturing plants containing the most modern machinery and equipment,
- 5) The electoral support through which the former landowners could control the Majlis (Parliament) was destroyed,
- 6) The state took control of the Majlis and the links between the elite and the peasantry was severed,
- 7) Absentee landlords were removed,
- 8) The villages acted as the basis for creating a new capitalist clan system,

- 9) The state became the most powerful economic as well as political force in the countryside,
- 10) All real or possible revolutionary threats from the disconcerted peasantry were curbed, and
- 11) A new industrial class with close ties to the state and foreign capital was created formed.

During the period of the third plan, the rate of urbanization in the country grew rapidly as a result of land reform and industrialization. The average annual growth of the urban population during 1963-72, i.e. the period of the third and fourth plans, was 5.1%, whereas that of the rural population was 1.9%. Total population growth was 3.0% per annum during this period.

**Table 5.** The Overall Economic Situation in Iran during the Third Plan (Average Annual Rate of Growth)

Period	1962-67
Agriculture	4.6
Oil	13.6
Industry	13.0
Industry and Mines	11.8
Water and Power	32.2
Construction	6.9
Services	14.7
GNP	9.9

Source : Zamanian, Distribution Affairs, NIOC, 24<sup>th</sup>, June 1974, p. 1.

In sum the Third Plan's achievements in terms of economic change were determined not only by the economic plans but also by the Shah's reform program, i.e. the White Revolution that set the guidelines for the next cabinets. In practice, much of the Third Plan, 1963-1968 was actually put aside to make way for the land reform.



## **The Fourth Economic Development Plan 1968-72**

The 1968-72 plan was more comprehensive and ambitious than previous plans in terms of formulation and implementation. The total planned investment amounted to Rls. 768b (\$ 10.2b). According to the Middle East Economic Survey (MEES) this amount was to be Rls. 610b (USD 8.1b) but as a result of an increase in oil revenues stemming from the Tehran agreement of 1971, the Government made modifications in budgeting for the remaining two years. This increase of Rls. 158b (USD 2.1b) was financed from three sources: Rls. 28b (USD 373m) from the increased oil revenues, Rls. 52b (USD 693m) from foreign loans and Rls. 78b (USD 1.04b) from internal loans (MEES, Vol. 14, no. 33, 11 June 1971, P. 7).

Of the USD 10.2b, 55% was allocated to public and 45% to private investment. The contribution of oil revenues to running the plan was more than 60% (USD 6.5b) of the total planned expenditures of the Plan and Budget Organization and 80% of the total oil revenues. The income tax from the consortium companies were most crucial, not only in terms of their overall share of the basket of revenues of the producing companies, but also because of their relatively greater vulnerability to market vicissitudes owing to the large quantities of output involved.

Given these considerations it was clear that any significant fluctuation in the flow of oil revenues from the consortium could have far-reaching repercussions on the ability of the planners to meet their development targets. However, leaving aside the consortium, owing to the historic success of OPEC in the Tehran negotiations of February 1971, the Iranian government succeeded in raising its annual oil revenues far beyond the planned level of over USD 1b. It thus removed at the outset one of the most serious uncertainties regarding the plan.

During this period Iran became the leading producer in the Middle East and the third largest in the world, reaching some 191.7m tons in 1970 and 227m tons in 1971 (MEES, Vol. 15, no. 23, 31 March 1972, P. 2) (6). According to the consortium's Annual Review for 1971, Iranian revenues for the consortium raised by 70% over the 1970 figure to USD 1,937b (£ 745.1m) (MEES, Vol. 15, no. 42, 11 August, 1972, P. 5).

The vital role of oil revenues in financing the plan, and hence in capital formation and growth, is readily apparent from the data presented above. The rate of growth of the Gross National Product (GNP) of the country was 9% per annum over the five-year period (from USD 257b in 1967 to USD 359b by the end of the plan). It is important to note that GNP increased at an average annual rate of about 11% in real terms. The objectives of the plan were set in the following areas: agriculture, heavy industries, oil and gas, water and power, and services (Plan and Budget Organization, Fourth Development Plan, P. 39).

The high growth rates in the sectors of industry and mines, oil and gas, and services, even though offset by the lower-than expected growth in the agricultural sector, reflected a primary structural change in the economy. Industrial output increased sharply, most of the increases in production being due to an expansion of the automotive and electrical industries. Protected against foreign competition, the automotive industry boomed during this period accounting for a significant portion of total industrial investment. Also, Iran's investment in the petrochemicals industry rose to USD 350m.

The rapid expansion of petrochemicals had wide economic repercussions through the production of consumer goods, and obvious, far-reaching implications for agricultural development. All this was made possible by increasing oil revenues, that rose from Rls. 73.9b



(constant prices) in 1963-4, representing 50% of GNP (Central Bank of Iran, Annual Report, 1978, PP. 94-95).

**Table 6.** The Average Rate of Growth during the Fourth Plan

Year	1967-72
Agriculture	4.0
Oil and gas	16.3
Industry and Mines	13.8
Water and Power	21.2
Services	14.7

To sum up, oil revenues had been the *sine qua non* of Iran's economic development. The raising of oil revenues by 18% per annum between 1963 and 1970 helped to bring the level of national savings to more than 20% of GNP. In 1970, oil revenue was about 50% of total current public revenues and 12% of the GNP. Over the 1956-72 periods on average about 71% of the total oil revenues of the central government were allocated to the Plan and budget Organization. Five broad sectors were considered for planning; agriculture, industry, oil and gas, water and power, and services.

### The Fifth Economic Development Plan 1973-78

On 7<sup>th</sup>, January 1973 Iranian Prime Minister Amir Abbas Hoveyda presented Iran's Fifth Five-Year Development Plan to parliament. The atmosphere surrounding the presentation of the plan was charged with confidence, yet this self-assurance meant that some emerging new constraints were largely overlooked. Oil prices were assumed to remain constant or even increase in real terms. Demand elasticity for OPEC oil was implicitly assumed to be very low; existing levels of foreign growth and inflation were expected to continue, and domestic absorptive capacity was assumed to be a direct and linear function of internal investment in factories and equipment.

At the same time defense expenditures showed no sign of deceleration. Self-sufficiency in grains and other essential staples was growing more remote due to population and income increases. Bills for imports were

rising faster than oil revenues and non-oil exports seemed unlikely to make a noticeable impact on the huge import costs. The overall aim of the plan had been based on a total investment of USD 32.4b and an annual growth rate of 11.4% in Iran's GNP at constant prices. USD 17b was expected from oil revenues for the period of the plan and the oil sector was to benefit from the investment of USD 4.4b.

The prime minister speaking to parliament on 18 June 1973 noted, "Total production, at present 5.5m b/d, will reach the 8.3m b/d mark in 1977" (MEES, Vol. 16, no. 13, 19 June, 1973, P. 4).

This increase was to be accompanied by an annual growth rate in oil revenue of 16%, for a total of some USD 22b over the five-year period, providing 47% of total government revenues. In order to implement the above objectives, exports of crude oil were to increase from 281m cubic meters (4.8m b/d) in 1972 to 392m cubic meters (6.7m b/d) in 1977 (Iran's Fifth Development Plan 1973-8; Revised A Summary, May 1975, P. 266).

In practice, though, due to the oil boom, the economy set out upon a period of unprecedented growth that lasted for two years.

Increased oil revenues enabled the government to spend USD 22b from March 1974 to March 1975, a sum almost equal to its total expenditure during the three years before. Consequently the GNP, that had been risen by 8% per annum in the 1960s, increased by 14.2% in 1972-3, 30.3% in 1973-4, and 42% in 1974-5. Between 1972 and 1978 the GNP grew from USD 17.3 b to an estimated USD 54.6b, while the GNP per capita rose from \$450 in 1972 to over \$2,400 in 1978 (Katouzian, H., 1980, P. 256; Halliday, F., in *Iran Dictatorship...*, 1979, P. 138; and Keddie, N., in *race and Class*, P. 20).

The significance of the oil sector on the economy can be understood by its effect on the share of other production sectors in the gross domestic product (GDP). For example, Table 7. It shows that the share of



agriculture in the GDP steadily declined from 25.8% in 1963-4 to 9.4% in 1977-8. The share of industry, however, grew from 17.7% in 1963-4 to 19.1% in 1977-8 and that of manufacturing grew from 9% in 1963-4 to 13.1% in 1977-8, although the share of construction rose from: 4% in 1963-4 to only 5% in 1977-8 (Central Bank of Iran, Annual Report, 1971, P. 116; 1978, PP. 94-5).

**Table 7.** Distribution of GNP by Sector of Origin (percent)

Sector	1963-64	1968-69	1972-73	1977-78
Oil	21.1	25.1	51.9	35.8
Agriculture	25.8	20.6	10.6	9.4
Industry(a)	17.7	20.7	13.0	19.1
Manufacturing and mining	9.0	13.6	8.8	13.1
Construction	4.0	4.4	3.6	5.0
Water and power	1.2	2.0	0.6	1.0
Services	35.2	34.1	24.5	37.7
State services	7.8	9.7	8.1	11.2
Total GDP (b)	348.1	578.9	2,567.1	3,589.1

Sources: The Central Bank of Iran, 1971, P. 116; 1978, pp. 97-5.

- a) Some industries are not listed here.
- b) GDP at constant prices (Billion Rials)

As observed in Table 7, services have always had a significant share in the GDP of the country. Expenditure on education and housing grew fast although much of this was squandered on expensive projects. Transport and trade expanded, but road construction and the like must have been included in the figures for construction. Communications and air services expanded at a fast pace, but their share of total services remained very small. This is also true of banking and insurance activities.

As oil revenues grew, state expenditures for fixed capital formations expanded rapidly, exceeding private investments. In 1962-3, before the oil boom the state invested only Rls 18 billion, compared to private

investments of Rls. 31 billion, and Rls 58b by the private sector in 1972-3 (Annual Report 1972, P. 145).

State investment exceeded that of the private sector before the oil-boom reaching Rls. 199b in 1972-3, compared to Rls 150.6b (Annual Report 1973, P. 139).

Eventually state investment reached Rls. 647.2b in 1977-8, while private sector investments totaled Rls. 505.4b (Annual Report 1974, P. 96).

### **The Revised Fifth Plan**

As oil revenues rose in the last quarter of 1973, the Shah decided to revise the plan and ordered a second version that would take into consideration the increased income. This version cost USD 68.6b (Rls. 4,634b), twice the original sum (The Economist 28 August, 1976, P. 21) (7). The new scheme for 1974 was in essence the original fifth plan together with a list of projects originally rejected as being uneconomical. A total of USD 45.5b (Rls. 3,064b) was allocated to the public sector and USD 23.3b (Rls. 1, 570b) to the private sector (MEES, Vol. 16, no. 44, 23 August, 1974, P. 5).

Fixed investments were to be distributed in the following proportions:

- 1) Industries and mines, 18%,
- 2) Agriculture and natural resources, 6.6%,
- 3) Oil and gas, 16.8%,
- 4) Transportation and communication 10.5%,
- 5) Housing, 19.7% and other activities 28.4%.

In short, nearly 35% of all fixed investments were allocated to industries, mines, oil and gas (Central Bank of Iran; Annual Report 1979, P. 34).

The revised plan was larger than all the previous plans and was much more than an investment program. It brought about great changes in the social and economic structure of the country and eventually led to a politico-economic catastrophe. The Shah assumed that all the state lacked to implement his vision of a Great Civilization was money and, now that the money was



there, the projects needed only to be inscribed in the plan and the budget. Apparently freed from financial constraints, the Shah thus opted for a development strategy that gave priority to economic growth over basic socio-economic objectives such as price stability, equity in wealth, income distribution and a balance of activities in different sectors.

In the revised plan, the state launched several new programs that included the development of nuclear energy and the provision of foreign aid to several countries throughout the world. According to MEES and Kayhan International, Iran's total commitments in the first 11 months of 1974 amounted to USD 7.7b, 60% of which went to developing countries (Kayhan International 7 December, 1974).

Among those countries, Egypt was the largest recipient of Iran's aid, obtaining assistance of USD 1b. India with a commitment of USD 900m was the second largest and Pakistan, with USD 64m was third. Furthermore, Iran provided aid to Syria (USD 150m), Sri Lanka (USD 67m), Bangladesh (USD 15m), Jordan (USD 13m), Afghanistan (USD 10m), Senegal (USD 16m), Tunisia (USD 8.5m), as well as to Morocco, Sudan, Lesotho, and zaire (8).

Iran engaged in a number of loans for trade deals with the industrial countries in order to establish technological co-operation and show her good will in the process of oil price shocks. The major deals involved the US, Italy, France, and the UK. In the case of the US and Iran, on 4<sup>th</sup> March 1975 an agreement was signed involving USD 15b in non-oil trade over a period of five years. The trade included eight nuclear power plants with total output of 8,000 megawatts and with associated water desalination plants, 20 prefabricated housing factories, 100,000 apartments, and five hospitals with a total of 3,000 beds. The total cost of these projects was estimated at about USD 12b (Alexander, PP. 386-7).

The agreements between Iran and France were worth USD 7.8b, including USD 1.8b for two French atomic power plants. There were also other projects, but only USD 1b was actually disbursed. In addition, the Shah offered a loan of USD 1b (£ 450m) and proposed to take over a part of France's 52.8% share in the £ 700m uranium enrichment plant being built at Tricastin in southern France for the European Eurodif Consortium (The Economist, 11 January, 1975, P. 66). Italy and Iran signed an agreement involving USD 3b worth of trade and co-operation between the two countries, but no disbursements were made. In the case of financial agreements with the UK the countries agreed to a loan of USD 1.2b at commercial rates and guaranteed by the British government. Only USD 400m of this agreement was disbursed.

Such co-operative ventures were designed to be more than economic ties; they were contributions to the Shah's political goal of bringing about greater stability and self-reliance in the area between the Bosphorus and the Himalayas. This high expenditure should have enabled Iran to fill the military and political vacuum created by the withdrawal of British forces from the Persian Gulf in 1971, without any new costs to the Western Alliance, thus ensuring the long term success of the so-called Nixon Doctrine.

Consequently, between 1974 and 1978, Iran exported nearly USD 15b of long-term capital in the form of foreign aid, direct investment and government loans (The Economist 16 September, 1978, P. 96).

The results of such high rates of spending were as painful as they were predictable. The value of imports soared, fivefold to USD 15b between 1972-3 and 1975-6. However, well over USD 1b of this went into paying port demurrage charges (Graham, R., 1979, PP. 97-99). Ships queued for up to 250 days to find berths at Khorramshahr and lorries were delayed in seemingly interminable lines at the Turkish-Iranian border. More



financial resources were lost on cargoes of fruit that went rotten and were tossed into the Persian Gulf.

A reduction in oil revenues (of USD 4b), shortages of manpower (of 111,000) and construction materials, bottlenecks in infrastructure and inflationary pressures forced the government to re-assess its development priorities. Daily oil production declined, by an estimated 800,000 to 900,000 barrels in 1975 cutting revenues and necessitating new economics. The director of Iran's Plan and Budget Organization, Majid Majidi, said that although total production capacity was 6.5m b/d, the output for 1975 would fall from 6m b/d to 5.6m b/d. He added that oil exports had declined from an average of 5.88m b/d in the second quarter of 1974 to 5.16m b/d in the first quarter of 1975 (MESS, Vol. 19, no. 35, 20 June, 1975).

During the period 1963-72 the accumulated deficit of the current account amounted to USD 2.617b all of which was financed by long-term loans (Central Bank of Iran, Annual Reports, 1970 and 1972). The Shah, in an interview with the Kuwait daily *al-Siyasat* on 27, July 1975, said that the forecasted deficit would affect Iran's foreign investments, adding that the deficit would be USD 4b (MEES, Vol. 18, no. 41, 1 August, 1975).

Also by mid- 1975 the Government was beginning to anticipate a deficit in its 1976-77 budget and indeed the deficit reached USD 600m by the end of 1977 (The Economist, 13 November 1976, P. 138).

Moreover, the International Monetary Fund drew attention to the dramatic change in Iran's external position from an overall balance of payments surplus of USD 1.6b in the first quarter of 1977 to a bare surplus of just USD 190m in the first quarter of 1978. By the first quarter of 1977 the public sector's external debt was USD 6.7b and it appeared that Iran had become a net importer of capital for the first time since 1973.

Private banks lent USD 1.5b to the Iranian public sector in early 1977 but only in the form of Euro-

credits; they also made USD 7.5b of syndicated loans to other borrowers in the same period. According to the Bank for International Settlements these banks promoted over USD 3b worth of short-term loans for trade financing and other purposes. The Economist of 16<sup>th</sup> September 1979 reported that Iran's 1979 budget deficit was over USD 10b. Ironically and darkly for the regime despite a 287% increase in Iran's oil revenue from 1973 to 1975, the country was once again a borrower.

The reasons were: firstly over-estimation of oil revenues in the revised fifth plan. (For instance oil revenues for the 1973-79 period had been projected to be Rls. 6,628.5b (\$85.35b), but the actual revenue was approximately Rls. 5,334.5b (USD 67.90b, or a shortfall of 19.5%). Secondly due to the Shah's promise to raise the welfare of the Iranians in quick order the demand for imports rose considerably.

Consequently imported goods that stood at USD 4.9b in 1973-4, rose to USD 16b in 1975-76. The rate of increase in imports was much larger than the rate of increase in foreign-exchange receipts. It had taken only two years to absorb the annual capacity to import.

### **Summary and Conclusion:**

The period of 1949-79 all fell under the reign of Mohammed reza Shah (1941-79). His ambition was to make Iran one of the greatest powers in the world, inferior only to the superpowers and the other highly developed countries such as Japan and the Western European nations. Indeed, Iran after the coup in 1953 underwent considerable socio-economic development owing to its oil revenues as we have seen.

After increasing its oil revenues, and especially following the reforms of the early 1960s, the state expanded its intervention in capital allocation and accumulation that reached a peak in the mid-1970s. Owning one of the most important sources of wealth,



and as oil revenues grew the state became one of the country's most important investors. With its expanded resources, it greatly influenced the allocation of capital and, consequently, the economic development of the country (Jane Perry, Clark Carey and Andrew G. Carey, *The Middle East Journal*, Vol. XXIX, 1975).

Furthermore, as the state grew increasingly reliant upon oil revenues as a rentier state, the economy became more dependent on world markets. Both grew even, more susceptible to crises and fluctuations within the international commercial markets.

As we have seen, the reliance on petroleum revenue gives the state an exceptional relative autonomy from its social classes and other groupings. In fact the domestic economic sectors, including the private sector, are dependent upon the state for direct and indirect welfare gains through the latter's disbursement of oil revenues.

Accordingly the state becomes the exclusive source of economic and social power, a power moreover which tends to accumulate all rights and obligations, and through this process affects the form and substance of the class structure. The formal traditional class structure may remain intact, but it loses a large part of its time-honored inherited power in social relations, social mobility and income distribution.

Perhaps the largest social problem of the Shah's later years was the constantly growing gap between income strata. This increasing wealth distribution gap was felt between the urban and rural areas as well as between the lower and the upper classes. While the rich, taking advantage of the opportunities arising from Iran's huge oil revenues became much richer the ranks of the nouveau riche swelled.

The fifth plan (1973-78) was to help overcome this problem.. Despite some successes in the fields of education, health and social services, the government's capital allocation policies consistently favored the richer groups and those with higher credit ranking. This

included low interest loans or credit, tax holidays, and favorable conditions for investment (*The Economist* 28 August 1976, P. 27) (10).

Medium and small capital sources did not receive the same degree of economic resources nor were they permitted to form independent organizations of their own. Agricultural sector and rural areas were neglected by the government (from 33.3% of non-oil GDP in 1959 to 13.7% in 1977) (Llooney, R.E., and Frederiksen, P.C., *Middle Eastern Studies*, PP. 490-4). This led to a deterioration in conditions for the country's peasantry. As a result Iran, which in the early 1960s had been a net exporter of food, by the mid 1970s, was spending as much as USD 1b a year on imported agricultural products. Moreover, the regime's economic and social programs tended to increase regional inequalities.

Despite the regime's impressive recent economic growth, it failed politically for several major reasons. First, by the time of the 1953 coup, the Shah's regime was no longer legitimate in the eyes of most of the Iranian people. Second, as a result of the coup, the connections of the Shah's system with the middle and lower classes and, to some extent, with the professional associations, as well as with all independent political parties was effectively non-existent.

A third point is the system further widened this gap by implementing policies benefiting wealthy people rather than the middle and lower classes, which had no pressure groups through which they could alter or peacefully oppose government decisions. And fourth, while the Shah helped modernize the social and economic structure, he paid little attention to the development of the political superstructure. He refused to permit the formation of opposition groups, to open the political arena to organized parties, to forge links between the regime and the new classes, and to broaden the base of a monarchy which, after all, had survived only because of the 1953 coup.



But the immediate factors that set the stage for the conflicts of 1977-79 were rising inflation, reduced government oil revenues, and an economic crisis precipitated by the government's attempts to bring the economy under control. Uneven development of the oil sector led to a crisis of revenue absorption, high inflation and speculation.

In the mid-1970s, world demand for oil dropped, causing a fiscal crisis for the government, which needed additional capital to complete its ambitious development schemes. To resolve the problem, the government pursued somewhat contradictory policies. It began, borrowing funds from abroad while initiating price controls and an anti-profiteering campaign. These measures did not remedy the problem. Finally, unable to pursue its policies further, the government effected a recession that brought about an economic crisis in 1977 and set the stage for social conflict.

By this time, the government's actions had politicized many disparate groups and united the various elements of these groups against the state. Among the aggrieved were certain segments of the lower and middle classes, the urban professional class and the bazaaris. These groups provided an important base for opposition and ultimately for the revolution. The mobilization and collective action of these classes and groups and their coalition were responsible for the overthrow of the monarchy. These newly organized forces had different reasons for discontent, the resources for mobilization and as a result the nature and timing of their actions varied.

In fact, the Shah moved in the reverse direction. He narrowed the regime's political base, and, most serious of all, broke all its ties with the traditional and religious middle class. This was crucial in that this section of the middle class had social, financial, political, ideological, and historical links with the religious establishment. That establishment retained a great deal of political

influence, in part because it exercised ideological sway over the middle and lower classes and the majority of Iran's university students.

The Shah over time adapted to the delusion that he himself was not only the political leader of the nation but also maintained strong links with the religious establishment. The clerics however retained a great deal of political sway, in part because they exercised ideological influence over the middle and lower classes.

The royal misreading of his actual position and the reality of the strength of the clerical establishment's popularities with society coalesced into a genuine flood of popular hatred directed not only at the monarchy and its military establishment, but also at the ruling class and its foreign patrons.

As a result, the psycho-political atmosphere of the period between October 1978 and February 1979, when the Shah's regime was finally toppled is highly instructive, both in terms of the course of events of the Iranian Revolution and mass political movements in general.

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