The Patterns and Problems of Economic Development in Rentier States: the Case of Iran

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I

THE purpose of economic history is presumably analysis as well as collection of facts with a view to explaining certain uniformities that are believed to exist in the economic life of human societies. In other words, the art consists of formulating verifiable hypotheses and testing them against the facts of economic history. Few people have advanced hypotheses concerning the causes, prerequisites, patterns and problems of economic development that could have universal applicability, for all times and all places. The less ambitious approach consists in pinpointing and explaining certain uniformities within a more limited time span and for a more limited area. The area of our interest in this paper—that of the Rentier States—is not quite limited to the Middle East, though most countries of this region happen to belong to this category. As for the time span of our study, it is one of the objectives of this paper to suggest that the period roughly corresponding to 1950–6 represents a landmark in the economic history of the Middle East and that at least in the case of Iran the structure and sources of economic growth after this period are distinctly different from the decades preceding it.

But first let us consider what is meant by a Rentier State. Rentier States are defined here as those countries that receive on a regular basis substantial mounts of external rent. External rents are in turn defined as rentals paid by foreign individuals, concerns or governments to individuals, concerns or governments of a given country. Payments for passage of ships through the Suez Canal (after allowing for the operating and capital costs incurred) are external rents. The same holds for payments to the so-called transit countries in the Middle East that allow oil pipelines be passed through their territories. A moment's reflection will reveal that oil revenues received by the governments of the oil exporting countries can also be external rents. Some may prefer to look at oil royalties as compensation for the removal of certain exhaustible resources. This is the usual justification for the rent of mines. But apart from these so-called royalties, the governments of the oil exporting countries in the Middle East benefit from differential and monopolistic rents that arise from the higher productivity

of the Middle Eastern oilfields and price fixing practices of the oil companies.[1] What is more important perhaps is to recognize that however one looks at them, the oil revenues received by the governments of the oil exporting countries have very little to do with the production processes of their domestic economies. The inputs from the local economies—other than the raw materials—are insignificant.[2] This lack of any meaningful relationship between the level of oil production and the local economies of the producing countries can be seen from Table 1. Whereas both for Iran

TABLE 1. *Production of crude petroleum and local expenditures of the oil industry, Iran and major oil producing countries of the Middle East, 1948 and 1958.* (*Production in thousands of barrels and expenditures in millions of dollars*)

	1948	1958
Iran:		
Production	190,334	301,526
Local expenditure*	125·0	105·3
Middle East†:		
Production	405,852	1,540,716
Local expenditure*	202·0	287·9

* Includes wages and salaries, payments to local contractors, purchase of local supplies etc.

† Includes Iran, Iraq, Kuwait, Qatar and Saudi Arabia.

Source: Charles Issawi and Mohammed Yeganeh, *The Economics of Middle Eastern oil*, London 1962, Appendix, Tables 1 and 5. (Figures rearranged.)

and a number of Middle Eastern countries, the production of crude petroleum has increased considerably (by 58 per cent and 280 per cent respectively between 1948 and 1958), the local expenditures of the oil companies have actually declined in the case of Iran and have increased by only $85·9 million for the group of countries considered. The input requirements of the oil industry from the local economies—at least for the inputs that have an opportunity cost—is so insignificant that for all practical purposes one can consider the oil revenues almost as a free gift of nature or as a grant from foreign sources. In fact, it may be worth taking note of the

[1] See Charles Issawi and Mohammed Yeganeh, *The Economics of Middle Eastern oil*, London 1962, pp. 105–6 and Table 30.

[2] The net value added attributed to labour in the Middle East oil industry in 1956 were only 8 per cent of total net value added during the six years period 1948–60 was calculated to be only 8 per cent of total net value added during six years ing 92 per cent was accounted for by capital and natural resources, capital the Middle mostly by foreign concerns. See Issawi and Yeganeh, *op. cit.*, Table 30. tor'—whatever

TABLE 2. *The relative significance of the oil industry and oil revenues in a number of Middle Eastern countries, selected years*

	Value added in oil industry as % of GNP	Oil Revenues as % of total Government Revenues	Shares of oil exports as % of total foreign exchange earnings
Bahrein			
1948	—	—	—
1957	—	66	—
1958	55	83	—
Iran			
1948	10	11	65
1958	15	—	57
1960	—	41	59
Iraq			
1948	10	7·5	34
1958	28	—	59
1960	—	61	78
Kuwait			
1948	70	—	—
1958	90	87	—
Qatar			
1948	90	—	—
1950	—	90	—
1958	90	—	—
Saudi Arabia			
1948	20	65	64
1957	—	—	84
1958	50	—	87
1960	—	81	—
Jordan			
1953	—	—	11
1954	3	—	18
1962	—	15	—
Lebanon			
1951	—	—	6
1952	2	—	6
1962	—	10	—
Syria			
1949	—	1	—
1957	—	—	8
1958	4	—	13
1961	—	25	—
rees (Egypt)	—	—	12
exte...			
for the ...	3	—	12
tion for i...	—	10	—

...governmen... and 41 and Section C of Chapter viii of Issawi and Yeganeh, differential anc... ...res for certain years refer to fiscal years.

similarities that exist between external rents and foreign grants. In their economic effects, they are almost identical, so much so that countries like Jordan and Israel that receive substantial foreign grants may display a number of characteristics shared by Rentier States. However the temporary nature of foreign grants and the uncertainty attached to them introduce a different set of considerations which are usually absent in Rentier States.

Although most countries in the Middle East do receive some form of external rent, the amounts involved vary a great deal both in absolute amount and as percentages of total government revenues and foreign exchange earnings. Table 2 gives an indication of the relative importance of the oil sector in various Middle Eastern countries. If such extreme cases as Qatar and Kuwait are left aside, the value added in the oil industry as a percentage of Gross National Product varies from 10 to 55 per cent in oil producing countries and from 2 to 4 per cent in transit countries. The oil revenues as percentages of total government revenues and total foreign exchange earnings are much higher in both groups of countries. Although the stage at which a country can be called a Rentier State is determined arbitrarily, we are mainly interested in such cases as Iran, Iraq and Saudi Arabia in which the effects of the oil sector are significant and yet the rest of the economy is not of secondary importance. The 'size' of a country can clearly make a difference to the relative weight of a given amount of external rent. Typically, the Rentier States are 'small' in size; however with Algeria, Libya and Nigeria soon joining the group, the number of such countries may become quite significant.

It was stated earlier that the period 1950–6 constitutes a turning point in the economic history of the Middle East. Although the initial and terminal dates of this period are arbitrarily chosen, they are not devoid of all significance. Iran's oil nationalization movement began to gather momentum in 1950 and the Suez Canal was nationalized in 1956. The impressive changes that occurred during this period were not so much due to the normal growth of a large industry, but were rather imposed from outside as the result of *political* pressures in the Middle East. The oil industry had existed in Iran for nearly half a century and had not affected the Iranian economy in any appreciable way before. The political developments in Iran and Egypt—the two largest countries of the Middle East—enabled the governments of most Middle Eastern countries to appropriate a larger share of the rents that previously accrued to the oil companies as profits. A glance at table III will give an indication of the order of the magnitudes involved. Suffice it to say here that the current payments of the oil companies during the first five years after 1956 were over seven times as much as the payments during the entire thirty six years before 1950. Thus in spite of its relative size, the oil industry in the Middle Eastern countries cannot be considered as a 'leading sector'—whatever

TABLE 3. *Payments of the oil companies to the Governments of the Middle East, 1913–1949 and 1956–1960 (Million $)*

Period	Bahrein	Iran	Iraq	Kuwait	Qatar	Saudi Arabia	All Transit countries	Total
1913–49	18	483	135	26	1	146	12	821
1956–60	58	1,160	1,081	1,784	248	1,540	121	5,992

Source: Issawi and Yeganeh, *op. cit.*, Table 39. (Figures rearranged.)

that implies—in the usual way that certain other industries have been so labelled in the western economies. However, it can be argued that during the past decade or so the public sectors in countries that have been the recipients of external rents have affected the pace of growth and expansion of the rest of the region's economy to an extent seldom encountered in the history of this region or that of any other in the world.

The oil industry's major contribution is that it enables the governments of the oil producing countries to embark on large public expenditure programmes without resorting to taxation and without running into drastic balance of payments or inflation problems that usually plague other developing nations. And since the oil revenues typically increase at a faster rate than the GNP of the local economies, the public sector of the oil producing countries expands rapidly. This need not necessarily result in some kind of socialism, but may turn into what can be considered as a fortuitous *étatisme*. The government becomes an important—or even the dominant—factor in the economy. This is not to imply that the local economies are not dependent on oil or that any cyclical behaviour on the part of the oil industry (or even oil prices) will not affect the local economies. At least in Iran, this dependence can be observed very clearly. However, the dependence is indirect. It is through the *expenditure* side rather than through the inter-industry relationships of the oil industry with the rest of the economy that the mechanism works.

The closest problems to the case of Rentier States studied by economists and economic historians are the inflow of gold into sixteenth century Spain and the so called 'transfer problem' arising from the German reparation payments after the First World War. In modern studies of economic development, oil exporting countries are often treated as exceptional cases and are excluded from the sample of underdeveloped countries.[3] Perhaps one of the more crucial problems that needs to be studied is to explain why

[3] For an interesting exception see Nicolas Sarkis, *Le Pétrôle, Facteur d'Intégration et de Croissance Economique*, thesis (Paris 1961), Librairie Générale de Droit et de Jurisprudence, Paris 1962.

TABLE 4. *Iran's GNP and per capita GNP, 1959/60–1963/64* (*Billion Rls.*)

	1959/60	1960/61	1961/62	1962/63	1963/64
1. GNP at current prices	292·5	331·3	342·6	348·9	369·6
Year to year % change	—	+13	+4	+2	+6
2. GNP at 1959/60 prices	292·5	314·0	324·6	327·7	345·9
Year to year % change	—	+7·4	+3·4	+1·0	+8·5
3. *Per capita* GNP at 1959/60 prices	Rls. 14,300 ($191)	Rls. 15,100 ($200)	Rls. 15,100 ($201)	Rls. 14,900 ($199)	Rls. 15,400 ($205)
Year to year % change	—	+4·7	+·8	−1·5	+2·9
4. GNP at 1959/60 prices excluding oil revenues	272·9	293·0	303·9	303·7	319·5
5. Year to year % change	—	+7	+4	—	+5

Source: Preliminary Estimate of Iran's National Income, the Central Bank of Iran.
Monthly Bulletins of the Central Bank of Iran.

the oil exporting countries, in spite of the extraordinary resources that are available to them, have not been among the fastest growing countries in the world. For most underdeveloped countries, lack of savings or shortage of foreign exchange constitute some of the major constraining factors in economic growth. No such limitations beset the Rentier States. And yet at least the rate of growth of the Iranian economy during the period 1955–65 has not been at all impressive (about 2 per cent on an annual *per capita* basis). Were we to exclude the oil revenues from the GNP calculations, the results would be still less impressive. Tables 4 and 5 provide partial evidence.

TABLE 5. *Average annual rates of change in Iran's GNP and per capita GNP, 1959/60–1963/64*

	GNP (current prices)	GNP (constant 1959/60 prices)	*Per capita* GNP (at 1959/60 prices)	GNP (at 1959/60 prices) excluding oil revenues
Average Annual Rates	6·25	4·3	1·47	4·0

Source: Table 4.

The explanations for this unexceptional performance may be sought in at least two different—though perhaps complementary—directions. One approach would be to focus attention on the kind of socio-political organizations that often prevail in this kind of (usually foreign-dominated) exporting country. It could be argued that the socio-political structure of these countries, saddled with legacies of open or disguised colonialism, is not conducive to rapid growth. This means that if organizational and political factors are accepted as important factors of production in an aggregative sense, then the degree of substitution between financial and organizational resources must be considered extremely low. The abundant financial resources cannot be properly utilized until the socio-political barriers to growth are removed independently. Iran's recent experience seems to lend support to this view: after the political upheavals of 1961–4 which forced the government to introduce a number of socio-economic reforms—notably land reform—the short-run performance of the economy has improved, even though additional factors such as weather conditions and availability of excess capacity in certain industries helped the process.

A somewhat different approach to the same problem would be to enquire whether additional causes may not be at work, so that even after the removal of socio-political barriers, a different set of problems may not

hinder rapid growth. Spain was a major colonial power herself when the gold inflows were taking place; and yet, the Industrial Revolution took place not in Spain, but in England and in other European countries. Similarly, the apparent 'prosperity' of present oil producing countries should not be taken as an indicator of their performance as developing and industrializing nations. In fact this same prosperity may lull many people into believing that the problems of economic growth are much simpler than they really are.

The point to be stressed here is that extensive government expenditures *per se*, though stimulating to production by increasing demand, may not be sufficient for generating rapid economic growth. The nature and composition of this expenditure, as well as the general response from the rest of the economy on the supply side, can make a great deal of difference. Adam Smith spoke of productive and unproductive labour,[4] while Rostow insists that 'outlays for purposes other than consumption be distinguished with respect to their being productive or non-productive'.[5] Both are drawing attention to the fact that not all expenditures have equal growth effects. That an increase in demand may induce some increases in output is not being questioned here. What is being questioned is the extent and the nature of the growth that may occur. The experience of countries poorly endowed with natural resources may have interesting implications in this respect for those countries that are rich in resources. Consider the following explanation of Japan's industrialization:

> the main cause of the rise of industry has been Japan's need to overcome her limited endowment of natural resources. For this reason she has had to develop the trade pattern of an advanced country, exporting manufactured goods and importing raw materials. Although industrialization is usually attributed to changes in demand, more than 75 per cent of Japan's industrial growth is traceable to changes in supply conditions. These include substitution of domestic for imported manufactured goods, substitution of manufactured goods for primary products, and other technological changes. Although increased exports were of some importance up to 1935, increases in domestic and foreign demand together account for less than a quarter of the rise in the share of industry in GNP from 1914 to 1954.[6]

Industrialization need not of course be the only road to rapid growth. But apart from the fact that for most underdeveloped countries industrialization seems the main hope, increasing the overall productive capacity of an economy is greatly dependent on such factors as higher capital per

[4] A. Smith, *An Enquiry into the Nature and Causes of the Wealth of Nations*, Book II, Ch. III: Of the accumulation of capital or of productive or unproductive labour.
[5] W. W. Rostow, *British Economy of the Nineteenth Century*, Oxford 1948, p. 12.
[6] H. B. Chenery, S. Shishido and T. Watanabe, 'The Pattern of Japanese Growth 1914–1954', *Econometrica*, 30, 1962, p. 129.

worker, improvements in the technical skills of the labour force, greater specialization and realization of potential external economies in production. To allow technological and organizational improvements on the supply side to be effectuated and the benefits of external economies in production reaped, the input–output matrix of rentier economies has to change drastically so that the inter-industry demand part of the matrix does not remain 'underdeveloped' as compared with the final demand part. For if most of the external rent is used to import for consumption purposes, all the productive sectors of the economy will remain relatively untouched by these 'extraordinary' expenditures. The consuming sectors of the oil producing countries may consequently develop more meaningful relations with the productive sectors of the countries they import from than with their own local productive sectors. Government expenditures made possible by oil revenues thus need not induce a commensurate expansion in the rest of the economy.

This imbalance in the input–output matrix of rentier economies may not be so easy to rectify. The currencies of the Rentier States are typically overvalued and market wages do not generally reflect social costs which, in countries of ample supply of labour, are probably lower than the market costs. Imports thus become attractive and import substitution hazardous. Dudley Seers advances the theory that since the workers in the oil industry are paid higher wages than workers in other industries (which is certainly true in Iran), the level of wages is raised even further in all industries through a process of demonstration effect.[7] He further shows how unemployment and slow industrialization occur more frequently in oil producing countries than in other developing economies: 'Most non-petroleum economies have been feeling increasingly the tensions caused by a slow growth of exports and fast rise in imports: they have taken many measures which are in fact protective and employment-generating even if intended, in the first place, to protect reserves. A petroleum economy operates differently. Factors that elsewhere would express themselves in balance of payments crises, such as wage increases or inadequate initiative in developing local industry, will here cause growing unemployment.'[8] Devaluation as a remedy is not considered seriously in these countries because the governments of oil producing countries always try to maximize their foreign exchange receipts from the local expenditures of the oil companies.

In Iran, the government has recently tried to encourage industrial development by using policy instruments other than the exchange rate. Development plans are formulated—even though not fully implemented—on a comprehensive basis. In the private sector, a complicated system of imports quotas, customs duties and export subsidies has been introduced

[7] Dudley Seers, 'The Mechanism of an Open Petroleum Economy', *Social and Economic Studies*, 13, 1964.

[8] *Ibid.*, p. 236.

while monopolistic concessions in certain fields have been granted to certain Iranian or joint (Iranian and foreign) groups. Cheap loans have also been made available. Most of the latter policies are inefficient from an economic point of view, iniquitious from a social point of view, and have proved cumbersome in practice. If devaluation is not feasible because the governments are usually in too much of a hurry to unload all their foreign exchange earnings on the market, a better alternative to the above-mentioned measures may be direct subsidization of industries having employment effects or widespread inter-industrial linkages. A yet quicker and more reliable way—from the point of view of realizing external economies—may be for the governments to invest directly in well-planned industrial complexes. The technological and labour force training programmes as well as any desired expansion in employment can be incorporated in such plans. This approach may also avoid some of the abuses of subsidization and the eventual inequality of incomes that typically prevails in such countries. In brief, what began as a fortuitous *étatisme* may have to move in the direction of a well-planned semi-socialist state if some of the short-run and long-run deficiencies of the Rentier States are to be avoided.

The danger that faces the Rentier States is that while some of the natural resources of these countries are being fully developed by foreign concerns and considerable government expenditures (usually in a few cities) are creating an impression of prosperity and growth, the mass of the population may remain in a backward state and the most important factors for long-run growth may receive little or no attention at all. To take an example, as far as public education is concerned, Iran is yet to reach in the 1970's the stage Japan had already passed in the 1850's! The organizational and technological shortcomings may turn out to be even more staggering. Furthermore, the gaps *vis-à-vis* developing countries may be widening over time, rather than narrowing. Whereas in most underdeveloped countries, this kind of relative regression will normally lead to public alarm and some kind of political explosion aimed at changing the *status quo*, in the Rentier States, the increasing welfare and prosperity (of at least part of the urban population) acquired through government expenditures and large imports pre-empts some of the urgency for change and rapid growth encountered in other countries. The blatant inequalities of income and wealth may create frictions, but not as much as in other countries since exploitation of a natural resource rather than the direct exploitation of the people is the main source generating the disparities. Consequently, the economic and technological backwardness of the Rentier States may easily coincide with a more serious kind of backwardness: socio-political stagnation and inertia. Under these circumstances one must be exceptionally wary of evaluating the developmental performance of a country

on the basis of changes in such purely economic and average indicators as *per capita* income. Kuwait may have the highest *per capita* income in the world, but she will have to undergo drastic transformation in all facets of her economy and socio-political organization before she can be considered on her way to a genuine long-term growth.

II

To study the economic structure of Rentier States one may either use time series for a single country to show departures from past trends after the external rents have become significant in amount or utilize cross-sectional data to point out the deviations of Rentier States from more 'normal' patterns of growth. An attempt has been made here to apply both methods. But the low quality and inadequacy of the data—especially for the historical part—make either approach at best suggestive. The economic history of Iran, even for the more recent decades, has yet to be written.[9] Ideally, one would want to be able to trace the long-run changes in the sectoral distribution of output and labour force as well as changes in the patterns of private and public consumption and investment. But unfortunately the historical data are not available and the cross-section studies, in spite of their limitations, may prove of more help in this respect. However, a limited number of series, especially in the fields of foreign trade, government expenditure and investment, can be used to highlight certain contrasts between the two periods. Furthermore, during the period 1950–3, Iran came very close to a laboratory experiment with respect to the effects of sudden discontinuation of the oil revenues. Although the period was short and the oil revenues were not at that time as significant as they have become since, the experience is worth recalling for the light it may shed on the process of industrialization in the Rentier States. But first some of the contrasts between the pre- and post-nationalization trends have to be observed.

Table 6 shows oil production and government revenues from oil since 1910. Though the growth of production was considerable between 1915 and 1950 (from 376 thousand tons to 16·5 million tons), oil revenues did not increase rapidly. In 1950, oil revenues were still about £16 million. It is only after 1955—and in spite of the virtual denationalization of the oil industry in 1954—that the revenues shoot up to over £100 million in 1960 and £183 million in 1965. The effect of this sudden increase in oil revenues on Iran's foreign trade can partly be observed from Table 7. Iran's foreign trade before 1955 generally followed the trends of world

[9] See however *Tārīkh-i Sī-sāle-yi Bānk-i Millī-yi Īrān*, 1307–1337 (1928–1958), Bank Melli Press, Tehran 1959 (in Persian). N. Pakdaman, 'Economie Iranienne: Essai d'Analyse Structurale d'une Economie Sous-Developpée', thesis, Paris 1965; M. Agah, 'Some Aspects of Economic Development of Modern Iran', thesis, Oxford 1958.

TABLE 6. *Oil production and government revenues from the oil industry, Iran, selected years from 1910 to 1965*

Year	Oil production in metric tons	Oil Revenues of the Iranian government in £s
1910	—	—
1915	375,977	1,326,000
1920	1,385,301	469,000
1925	4,333,933	831,000
1930	5,939,302	1,288,000
1935	7,487,697	2,220,648
1940	8,626,639	4,000,000
1945	16,839,490	5,624,308
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†

* Converted from barrels into metric tons by assuming one metric ton = 7·3 barrels.
† Estimated.

Source: B. Shwadran, *The Middle East, Oil and the Great Powers*, New York, 1955.
Six Decades of Iranian oil Industry, Publication of National Iranian Oil Company, Tehran 1966.
Issawi and Yeganeh, *op. cit.*
Annual Report of the Central Bank of Iran, 1966 (in Persian).

TABLE 7. *Foreign trade of Iran, selected years from 1900 to 1960 (values in Million Rials; volumes in thousand tons)*

	Imports		Exports (excluding oil)	
	value	volume	value	volume
1900	255	—	147	—
1905	386	168	293	289
1910	485	249	375	273
1915	464	216	355	253
1920	482	131	137	49
1925	881	325	515	232
1930	610	370	459	183
1935	804	434	659	254
1940	865	317	940	215
1945	3,107	151	1,707	120
1950	6,242	504	3,563	194
1955	9,125	637	8,034	508
1960	52,657	1,914	8,360	446
1965	66,083	—	13,740	—

Source: Customs Administration Yearbooks, Tehran, Iran.

prosperity and depression.[10] It did not benefit very much from the prosperity of the decade or so before the First World War for internal political reasons (the Constitutional Revolution of 1906 and its aftermath) and it did not suffer too much during the depression periods of the interwar years because the government took over the control of foreign trade and embarked on extensive programmes of bilateral trade. Though the overall trend of exports and imports is upward during the first half of this century, it is only moderately so. The dramatic changes occur after 1955. Imports increase by over five times between 1955 and 1960 and the sharp upward trend seems to be continuing since 1965. The trend of Iran's imports leaves little doubt that we are basically concerned with two different regimes: the moderate rise of the first half of the century, and the sharp increases since 1955. As for exports, no such sharp increases can be observed. And the widening gap between imports and exports is the result of this disparity in growth rates which is of course filled out mainly by oil exports.

The government expenditures of Iran have been increasing rapidly since the 1930's. However the increases for the earlier periods given in Table 8 partly reflect the price inflation of the period just before and during the Second World War. In real terms, the expansion of public expenditure during recent years has probably been more pronounced. A further difference between the two periods which is not reflected in Table 8 is the

TABLE 8. *Government expenditures, Iran, selected years from 1930 to 1964 (in Million Rials)*

Year	Expenditure
1930	353
1935	750
1940	3,211
1945	7,762
1950	10,060
1955	23,500
1960	54,800
1964	74,700

Sources: H. Khajehnouri, *Survey of Education in Iran during the recent half century (in Persian)*, in *Survey of Manpower Problems*, Ministry of Labour and Social Affairs, Tehran 1966.
Public Finance Papers, Iran, U.N. publication, 1951.
Various reports and working papers of the Plan Organization and the Ministry of Finance.

[10] M. Djazaeri, *La Crise Economique Mondiale et ses Répercussions en Iran*, thesis, Paris, Librairie Technique et Economique, Paris 1937.

way in which government expenditures were financed. During the prewar period, expenditures were financed mainly through taxation—albeit a heavy and iniquitous indirect taxation—whereas after 1955, the oil revenues began to become the major source of revenue for government expenditures. This point will be touched on later, but the examination of Table 9 which shows the course of private fixed investment in Iran may

TABLE 9. *Private fixed investment in Iran, selected years from 1937 to 1959 (Million Rls.)*

Year	Agriculture	Industries	Construction	Transportation	Total
1937	10·0	74·9	279·3	44·9	409·1
1940	62·1	19·7	1,023·2	20·0	1,125·0
1943	134·7	10·6	491·7	9·6	646·6
1946	111·9	94·0	566·6	273·0	1,045·6
1949	246·1	369·7	1,195·3	563·7	2,374·7
1952	276·9	515·0	1,447·5	46·5	2,285·9
1955	336·6	1,267·0	4,095·9	841·2	6,540·7
1956	642·5	3,984·2	4,096·1	2,051·8	10,774·5
1957	877·9	4,999·7	4,974·8	2,448·1	13,300·5
1958	2,340·9	8,172·2	7,150·0	3,201·9	20,864·0
1959	2,711·0	14,069·6	10,175·0	3,840·3	30,795·9

Source: 'Private Fixed Investment in Iran 1316–1338 (1937/38 through 1959/60)', by Sharif Adib-Soltani, Plan organization of Iran, 1962, Table XII.

help to bring out two related points. Firstly, that the government expenditures of the prewar period, though mainly directed towards investment outlays—particularly in railways, roads and light industries—had little positive effect on private investment. Government investment in many industrial fields was competing with or even replacing private enterprise. Second, that after 1955, the rapid increase in private investment shows that not only is public sector investment not expanding at the expense of the private sector, but that its large outlays—as well as its loans and foreign exchange facilities—are to some extent inducing the private sector to follow the pace of economic activity set by the government. Between 1955 and 1959, there is a five-fold increase in private investment. In other words, the government outlays financed out of oil revenues not only did not replace private expenditures, they supplemented them. What is paradoxical however is that in spite of these heavy investments, the results over a ten or fifteen year period have not been more impressive than those obtained in less fortunate developing countries. The explanation lies only partly in corruption and waste of resources. A more

serious shortcoming may be due to the lopsided composition of the investment outlays which emphasized residential, commercial and administrative construction and large-scale transportation and irrigation projects. The latter were often favoured by foreign consultants and contractors who pressed for the implementation of such projects without being sufficiently concerned with the question of economic feasibility.

The results of this period can be compared with the developments of the 1950–3 period. During the struggle for the nationalization of the oil industry, Iran virtually lost all her oil revenues, and in 1951 the Bank of England imposed restrictions on conversion of Iran's sterling holdings. This led to a *de facto* devaluation of the Rial: the U.S. dollar rose from 40 Rials in 1950 to 124 Rials in 1953. The effects of this devaluation and the more direct measures taken to restrict imports, contrary to the expectations of many Western observers, proved stimulating to the Iranian economy. The Korean War and the availability of some foreign exchange reserves and some foreign assistance were contributing factors, but the overall effect of import-substitution and export drive cannot be denied: '1950–3 was a period of industrial recovery. . . . Good crops and larger exports kept up the mass purchasing power, while restrictive measures gave the domestic industry welcome protection. With the return of profits to normal, many factories re-opened, new plants were installed and Iran actually became an exporter of manufactured articles such as mill textiles and matches. In textiles alone, in these three years eleven new factories with 110,080 spindles and 1,600 weaving looms, were installed.'[11]

The mechanism of this brief outburst of economic activity and some of its actual and potential problems are worth analysing. The stoppage of oil exports reduced the supply of foreign exchange and hence of imports. Because of the rise in the value of imported commodities, substitution of domestic products for marginal imports became profitable. This substitution occurred both in consumption and in production. Exports of non-oil commodities were also boosted. But the bulk of the exports consisted of raw materials which typically display supply elasticity only over longer periods of time. Even in the less traditional field of industry, the process of expansion could not have continued for long without running into labour and capital bottlenecks. If a fall in national income were to be averted, the decline in the use of a natural resource (oil) had to be compensated by employment of more capital and labour and/or better utilization of the existing capital and labour. The difficulty with countries like Iran is that because of their extremely low level of technology and national education—as well as their socio-economic rigidities—either their response to opportunities of this kind is slow or its dynamism is of short duration. If a country is to become more than a producer of raw materials—of any

[11] M. Agah, *op. cit.*, p. 212.

kind—and the growth of output is to be of a sustained kind, then the entire socio-economic framework of the country has to undergo a transformation. The level of education of the population and their technological sophistication have to be raised considerably. Also the necessary political and administrative mechanism for mobilizing national resources has to be devised. The government had begun to take important steps in this direction during the 1950–3 period.

The oil revenues offer unusual prospects for development precisely because they can make certain shortcuts in socio-economic transformation and long-range economic development possible. The effort and the sacrifice required to break through the educational, technological and organizational barriers are far less when relatively ample resources are available. However, the very existence of these resources and the expectation of ever increasing revenues in the future—for that is how most of the Rentier States think of their prospects—seem to affect the time preference of the governments in such countries: if in the future external rents are going to be more lucrative than in the past, then immediate increases in consumption and welfare assume an inordinately greater weight than increases in future consumption and welfare. This deprives the development effort of any urgency and worthwhileness. If the basic premise of ever increasing external rents were tenable, there would be little disturbing in this attitude. Countries like Kuwait could then be guaranteed a perpetual state of opulence, if not quite one of bliss. However, for any number of physical, technological and economic reasons, it is safer to assume that typically the revenues of any given single oil producing country should increase for a number of years, gradually flatten out and eventually decline. Viewed in a context of this sort—even though the duration of these phases cannot be estimated—the attitudes of the oil producing countries as reflected in their growth policies and plans are at best myopic. Instead of attending to the task of expediting the basic socio-economic transformations, they devote the greater part of their resources to jealously guarding the *status quo*.

III

In this section certain aspects of Iran's economic development over a ten to twelve-year period will be compared with those of a number of other developing countries. The indices used for showing patterns of growth in 'other countries' are a number of averages derived by Professor Kuznets and summarized in Table 8.1 of *Modern Economic Growth*.[12] Professor

[12] *Yale* 1966. It would have been better if these averages could have been purged of the data relating to countries which according to our criterion may be Rentier States themselves.

Kuznets' averages refer to groups of countries arranged by *per capita* Gross Domestic Product. In the case of Iran the use of *per capita* GDP may be misleading, since the difference between GDP and Gross National Product can be as much as 10 per cent of GDP owing to the operations of foreign oil companies.

The average *per capita* income of Iran was estimated to be $192 in 1963/4 by the Central Bank of Iran.[13] The relevant group of countries for purposes of comparison with Iran would appear to be the group whose *per capita* GDP ranges between $100 and $199 rather than the next group within the $200 to $349 range. However, both groups are usually given in the relevant tables to indicate possible trends of change.

Participation in Economic Activity

The aggregate population and labour force data of Table 10 refer to the 1956 census and to the 1966 population census results. That Iran's economically active population is only about 30 per cent of her total population (as compared with 39·2 per cent for the $100–$199 group of countries) can be explained partly by the high percentage of the population (46 per cent) under the age of 15 and partly by the low participation of women in economic activity. The latter point is confirmed by the Agricultural Sample Survey of 1960 and the Manpower statistics of 1964 (see Table 10).

The low participation of women in economic activity in Iran reflects more than religious prejudices or problems of defining 'economic activity'. It may reflect the accepted ethos of a typically patriarchal state. Countries like Iran or Saudi Arabia that pass quickly from being a traditional society to being a Rentier State may achieve fairly substantial average *per capita* incomes, without going through the organizational changes which are usually associated with the process of capitalistic (or socialistic) economic growth. The same economic (or even socio-political) organizations and mores associated with such organizations may prevail for a long time before the 'expenditure effects' of external rents begin to build up enough pressures to challenge them. If the results of the 1956 and 1966 censuses are to be considered accurate, then the decline in the percentage of the economically active population would seem disturbing. Only about 50 per cent of the decline can be accounted for by the increase in the number of students.

Sectoral Patterns of Output

As shown in Table 11, Iran's pattern of growth has this peculiarity that its A-sector[14] appears much closer to that of the group of countries in the range of $200–574 *per capita* GDP than to that of the group below $200.

[13] See *Estimate of Iran's National Income*, Tehran 1966.
[14] Comprising agriculture, forestry and fishing.

TABLE 10. *Participation in economic activity: Iran and other countries*

Iran			Kuznets' averages	
			$200–349 *per capita* GDP (17 countries)	$100–199 *per capita* GDP (24 countries)
Economically active as % of total population				
	1956 census	1966 census		
1. Total	31	27·3	38·7	39·2
2. Female	10	8·2	20·6	19·6
Economically active as % of rural population (1960 Agricultural sample survey)				
1. Total	32			
2. Male	52			
3. Female	11			
Number of workers in all establishments of Iran by sex (1st Quarter 1964). Dept. of Manpower, Ministry of Labour and Social Services				
	Number of employed	%		
Total	907,439	100		
Male	864,675	95		
Female	42,764	5		

Source: Documents cited above and S. Kuznets, *Modern Economic Growth*, Yale 1966, Table 8.1.

TABLE 11. *Share of major sectors in GDP, Iran 1959/60–1963/4 and other countries, early 1950's*

	Iran					Kuznets' averages	
% of GDP	1959–60	1960–61	1961–62	1962–63	1963–64	$200–574 *per capita* GDP (5 countries)	Under $200 *per capita* GDP (12 countries)
1. A–Sector	28·7	28·6	28·0	26·1	23·8	20·5	46·0
2. M+ Sector	19·1	19·5	19·7	20·5	21·5	34·0	21·5
3. Oil Sector	15·3	15·1	15·4	16·8	17·4	—	—
4. S–Sector	36·9	36·8	36·9	36·6	37·3	45·5	32·6
% of GDP (excluding oil sector)							
1. A–Sector	33·9	33·7	33·1	31·4	28·9		
2. M+ Sector	22·5	23·0	23·3	24·6	26·0		
3. S–Sector	43·6	43·3	43·6	44·0	45·1		

The M+Sector comprises mining, manufacturing, construction, water, energy, transport and communications. For definitions of the A–Sector and S–Sector, see p. 444 note 14 and p. 447 note 15.
Source: Kuznets, *loc. cit. Preliminary Estimate of Iran's National Income,* The Central Bank of Iran, Tehran 1966.

In 1963/4, the share of the A-sector in Iran's GDP was 23·8 per cent. By contrast, Iran's share of the S-sector[15] was somewhat higher than that of the countries with less than $200 *per capita* GDP. Once the oil sector is removed from GDP, the share of the S-sector in 1963/4 reaches 45·1 per cent which is very close to that of the group of countries with the higher per capita GDP. Although the number of years (five) for which GDP figures are available is not sufficient to show any trends, nevertheless, the increase in the shares of the oil sector and the S-sector may be considered as of some interest.

The relatively larger share of the S-sector can perhaps be explained by the following considerations:

(i) Since the external rents accrue to the government without substantially affecting the local economy, it is reasonable to expect the final demand part of the input–output matrix of rentier states to be more affected by the expenditure of the external rents than the inter-industry part.

(ii) Abundance of foreign exchange reduces the relative price of all importable goods as compared with non-importables—mainly services and rents. Whereas the prices of imported commodities are not affected by changes in internal demand, in the case of non-imported goods and services, it is in fact their prices that change in the first instance.

(iii) There may also exist a considerable monopoly element in the valuation of services in rentier countries over and above the monopoly elements usually found in most underdeveloped countries. Since the external rent is paid to the government, it is tempting for the government to reward its employees and supporters with regular salary increases, fringe benefits or lucrative contracts etc.

In the long-run this distortion in the valuation of product may have the effect of shifting manpower, talent and organizational ability from agriculture and industry into services.

Sectoral Distribution of the Labour Force. Table 12 shows that the distribution of the economically active population of Iran is closer to the average shares in the labour force of the various sectors in countries with less than $200 *per capita* GDP. Over 45 per cent of the economically active population was engaged in the A-sector and 28·3 per cent in the S-sector in 1964. This, in combination with the above-mentioned sectoral distribution of product, is sufficient to cause some disparity in sectoral product per worker. That the distribution of the labour force has not adjusted itself to sectoral productivity may be an indication both of the institutional rigidities and of the speed with which Iran has been economically affected by the oil revenues.

Sectoral Product per worker. Table 13 shows relative sectoral product per economically active population for Iran in 1963/4. The productivity

[15] Comprising trade, banking, insurance, government and other services.

TABLE 12. *Sectoral distribution of economically active population: Iran 1956 and 1964 and other countries, early 1950's*

	Economically active population of Iran (1956 census)		Estimated economically active population of Iran 1964		Kuznets' averages for share in labour force excluding unpaid family labour	
	Millions	% of economically active	Millions	%	$200–574 *per capita* GDP	Under $200 *per capita* GDP
A—Sector	3·326	56·4	2·733	45·5	37·9	57·6
M+ Sector	1·396	23·6	1·570	26·2	29·8	19·5
S—Sector	1·186	20·0	1·691	28·3	32·3	22·9

Source: Iran's 1956 population Census and 1964 population sample survey. Kuznets, *loc. cit.*

of those engaged in agriculture and industry is respectively 0.53 and 0.82 of the average for the country. By contrast that of the S-sector is 1.31. Iran's sectoral product per worker would have been close to that of the more advanced countries (in the $200 to $574 *per capita* GDP range) were it not for her low product per worker in industry. The disparity between the A-sectoral and S-sectoral product per worker will probably widen, partly owing to a decline in product per worker in agriculture[16] and partly because the external rents are received and spent mainly in towns.

TABLE 13. *Relative sectoral product per economically active population for Iran 1963/64 and per worker for other countries, early 1950's*

	Iran	Kuznets' averages	
	Per economically active population	Between $200–574 *per capita* GDP (5 countries)	Under $200 *per capita* GDP (12 countries)
	per worker		
1. A—Sector to countrywide	·53	0·54	·80
2. M+ Sector to countrywide	·82	1·14	1·10
3. S—Sector to countrywide	1·31	1·41	1·42
4. S—Sector to countrywide (excluding oil)	1·60	—	—
5. M+ & S—Sector to countrywide	1·02	2·37	1·60
6. S—Sector to M+ Sector	1·61	1·24	1·29

Source: Tables 11 and 12, and Kuznets, *loc. cit.*

Manufacturing Sector. About 9 per cent of Iran's estimated labour force seems to have been engaged in manufacturing in 1963 as compared with 4·1 per cent and 13·9 per cent for the averages of groups with less than $200 and between $200 and $574 *per capita* GDP respectively (see Table 14). Iran's value added per worker engaged in manufacturing is however only slightly above that of the first group and considerably below that of the second group. The share of Iran's oil sector in value added is almost as large as that of all other industries in Iran (see Table 15). Once the share of the value added of the oil industry is excluded from the total, the share of other industries begins to approach that of the two groups of countries (Professor Kuznets' averages) given in Table 15. The higher share of textiles in Iran can partly be explained by historical reasons.

[16] The index of average productivity in agriculture dropped from 100 in 1959/60 to 94·6 in 1963/4. See *Estimate of Iran's National income*, cited above.

TABLE 14. *Number of workers engaged and value added per person in manufacturing, Iran, 1963, and other countries, 1953*

	Iran 1963	Kuznets' average (1953)	
		$200–574 *per capita* GDP	Under $200 *per capita* GDP
Number of workers engaged	837,526	—	—
Workers engaged as % of total labour force (assumed to be 0·42 of population)	9%	13·9%	4·1%
Value added per person engaged in manufacturing	$595*	$1,389†	$567†

* Excluding the oil sector and in 1963 $. † In 1948 $.

Source: Iran's Industrial Census, 1963.
Kuznets, *loc. cit.*

Paper products, printing, publishing, chemicals, non-metallic minerals and basic metals in Iran have a smaller share in value added than in the two groups of countries—which may reflect Iran's lower degree of industrialization. However, the share of metal products in value added appears twice as much as that in the two groups of countries. Over 60 per cent of value added of 'metal products' reflects value added of transportation equipment which may be related to Iran's size and the volume of her foreign trade. The non-integration of the oil industry in the Iranian economy can be seen from the low share of chemicals.

Table 16 compares value added per worker in manufacturing in Iran with that of the two groups of countries. Again, more meaningful figures for Iran are those that exclude value added in oil industry from the total value added in manufacturing. Some 58 per cent of Iran's manufacturing labour force is engaged in textiles, clothing and footwear in which value added per worker is far less than the average value added per worker in all manufacturing (·57 and ·32 respectively). Relative value added per worker in these industries is also considerably below that of the two groups of countries given by Prof. Kuznets. By contrast value added per worker is relatively high in chemicals (4·40) and leather and rubber (2·23). However only 1·6 per cent of Iran's manufacturing labour force is engaged in these industries. Metal products show also a high relative value added per worker (2·19) and also comprise 9 per cent of the manufacturing labour force.

Distribution of GNP by Type of Use. Table 17 shows that private

TABLE 15. *Structure of manufacturing: shares in value added, Iran, 1963, and other countries, late 1950's*

	Iran			Kuznets' averages %	
	Value added in billion Rls.	Share in value added % (including oil)	Share in value added % (excluding oil)	$200–349 *per capita* GDP (7 countries)	$100–199 *per capita* GDP (16 countries)
Food, beverages and tobacco	13·2	19·1	35·8	34·3	38·2
Textiles	9·7	14·4	26·2	20·2	10·8
Clothing and footwear	1·4	2·0	3·8	4·3	5·4
Wood products	·9	1·3	2·4	4·0	7·2
Paper, printing and publishing	·4	·5	1·1	4·4	4·4
Leather and rubber	·8	1·2	2·1	3·3	2·2
Chemicals (excluding petroleum products)	1·4	2·0	3·8	9·4	10·1
Non-metallic minerals	·7	1·0	1·9	5·5	6·4
Basic metals	·1	·1	·2	4·4	1·9
Metal products	7·8*	11·3*	21·1*	9·2	10·6
All other (excluding oil industry)	·4	·5	1·1	1·2	2·6
Oil industry	32·1	46·6			
Total with oil industry	68·9	100			
Total without oil industry	36·8		100		

Source: Iran's Industrial Census 1963.
Kuznets, *loc. cit.*

* About 60 per cent transport equipment.

TABLE 16. *Value added per worker engaged in major industries as relative of value added per worker engaged in all manufacturing, Iran, 1963, and other countries, late 1950's*

	Iran					Kuznets' averages	
	Number of workers engaged	% of total employed	Value added per worker engaged Rls.	Value added per worker as relative of value added per worker engaged in all manufacturing sector		$200–349 *per capita* GDP (7 countries)	$100–199 *per capita* GDP (16 countries)
				Including oil Sector	Excluding oil Sector		
Food, beverage or tobacco	159,867	19	84,000	1·03	1·84	1·16	1·34
Textiles	383,744	46	25,300	0·31	0·57	0·91	0·72
Clothing and footwear	101,012	12	13,900	0·17	0·32	0·53	0·56
Wood products	32,733	4	27,500	0·34	0·61	0·69	0·67
Paper, printing and publishing	5,087	0·6	78,700	0·96	1·72	1·05	1·86
Leather and rubber	7,997	0·9	101,000	1·22	2·23	1·06	1·00
Chemicals (excluding petroleum products)	7,168	0·8	197,000	2·40	4·40	1·59	1·80
Non-metallic minerals	32,180	4	21,800	0·27	0·49	0·85	1·00
Basic metals	2,066	0·2	48,700	0·59	1·09	1·69	1·36
Metal products	79,772	9	98,000	1·19	2·19	0·87	0·81
All other (excluding oil)	11,307	1	35,500	0·43	0·79	0·80	1·33
Oil industry	14,583	2	2,200,000	26·7		—	—
Total with oil	837,526	100	82,100				
Total without oil	822,943		44,700				

Source: Iran's Industrial Census 1963, and Kuznets, *loc. cit.*

consumption expenditure in Iran is at a level nearer to the group of countries with $200–349 *per capita* GDP than the group with $100–199. Government consumption expenditure however seems below that of both groups, while Gross Domestic Capital Formation appears above that of the two groups for the years 1959/60 and 1960/1 and below it for the years 1962/3 and 1963/4.

Owing to the economic and political crisis of 1960–4, which was caused at least partly by a fall in oil prices and a decline in the rate of increase in oil revenues, the period 1959/60–1963/4 for which preliminary estimates of Iran's National Income are available may not prove particularly useful in determining long-run trends. Various economic indicators show that both government expenditures and investment have increased sharply since 1964—after a 70 per cent increase in oil revenues. Gross National Capital Formation shows greater degree of stability than GDCF. That the former in Iran is not very much above the averages given by Prof. Kuznets is an indication that oil revenues have not been used as 'additional' savings for capital formation. They have partly replaced ordinary savings.

The relatively lower share of government consumption in GNP may also be due to the fact that during these years the government had to adhere to a stabilization programme, more or less imposed on Iran by various international monetary and development authorities, as well as a group of lending countries. Total current government expenditures have of course been rising at a rate above the rate of growth of the economy.

Government Revenues and Expenditures. Table 18 gives an indication of the dependence of the Iranian government on oil revenues as its major source of finance. The share of oil revenues in total government revenues increases from 11 per cent in 1954 to about 50 per cent in 1965. Customs duties are another important item of government receipts. The foreign exchange earned from oil export makes large quantities of imports possible.

The low share of direct taxes in government revenues (about 7 per cent for Iran) reduces the redistributional power of fiscal policy in rentier countries. The government can only act through the expenditure side. Even for stabilization purposes, the fiscal policy cannot be as effective as in other countries, and consequently greater reliance must be placed on monetary policy. It is to be noted that the government of Iran receives about 70 per cent of its revenues from oil exports and customs duties alone. Although there is no reason why the governments of the oil producing countries should not be able to exercise greater fiscal control, at least over the expenditure side of their budgets, in fact they seldom do so: they spend whatever they receive.

Tables 19 and 20 give some indication of the trend of government

TABLE 17. *Distribution of GNP by type of use, Iran, 1959/60–1963/64, and other countries, 1950's (share in GNP%)*

	Iran					Kuznets' averages	
	1959/60	1960/61	1961/62	1962/63	1963/64	$200–349 *per capita* GDP	$100–199 *per capita* GDP
1. Private Consumption Expenditures	75·4	74·0	75·3	77·1	75·7	75·6	73·2
2. Government Consumption Expenditures	9·7	9·4	9·5	9·7	10·6	11·7	11·9
3. Gross Domestic Capital Formation	18·2	19·2	17·1	14·0	13·1	16·9	16·4
4. Net Change in Foreign Claims	−3·3	−2·6	−1·9	−0·8	+0·6	−1·5	−1·2
5. Gross National Capital Formation (= 3 + 4)	14·9	16·6	15·2	13·2	13·7	12·7	14·9

Source: Preliminary Estimate of Iran's National Income 1959/60–1963/64, The Central Bank of Iran, Tehran 1966.
Kuznets, *loc. cit.*

TABLE 18. *Iran's central government finance: major sources of revenue as percentages of total revenues, 1954–1965*

Revenues	1954	55	56	57	58	59	60	61	62	63	64	65
1. Oil Revenues (and concession bonuses)	11	37	39	47	51	40	42	42	46	46	61	50
2. Customs Duties	27	23	19	18	16	22	22	19	16	18	15	17
3. Direct Taxes	5	5	4	5	7	8	8	8	8	8	7	9
4. Other Taxes and Domestic Revenues	35	28	28	26	24	24	25	26	30	28	18	24
5. Foreign Grants	22	7	10	4	2	6	3	5	—	—	—	—
Total (%)	100	100	100	100	100	100	100	100	100	100	100	100

Source: Various estimates given at different intervals of time by the Ministry of Finance, Plan Organization, USOM/Iran etc. The figures used were not fully consistent in that some referred to actual receipts while others referred to budgeted revenues. The discrepancies however are not large.

TABLE 19. *Iran's central government finance: major expenditures as percentages of total expenditures 1954–9 and 1963–6*

	1954	55	56	57	58	59	1963	64	65	66
Defence	38	41	40	39	40	38	39	38	42	45
Education	16	14	20	22	18	18	23	21	22	23
Health and welfare	7	6	5	5	7	6	5	7	7	11
Government Investment	48	38	47	43	39	34	22	27	—	—

Source: Plan organization, Ministry of Finance, USOM/Iran and AID working papers at different intervals of time.

TABLE 20. *Government expenditure for health and education, Iran, 1959 and 1963, other countries, late 1950's (% of GNP)*

	Iran		Kuznets' average	
	1959	1963	$200–574 *per capita* GDP (7 countries)	Under $200 *per capita* GDP (15 countries)
1. Education	2·0	2·7	2·0	2·7
2. Health	0·7	0·5	1·2	1·0
3. Education and health	2·7	3·2	3·2	3·7
4. Share in private consumption expenditures (%)	3·5	4·5	4	5

Source: As for Table 19 and Kuznets, *loc. cit.*

expenditures. Defence expenditures account for about 40 per cent of total government expenditures, while education and health account for about 22 per cent and 7 per cent respectively. Iran's expenditure on health seems to be below that of the two groups of countries given in Table 21.

Table 19 shows Iran's government investment decline from 48 per cent of total government expenditures in 1954 to 27 per cent in 1964. Thus while oil revenues were assuming a larger proportion in total revenues, investment was becoming a smaller proportion of government expenditures.

The allocation of government investment funds is of some interest. Table 21 shows the revised version of Iran's Third Development Plan. The share of industries and mines is below 12 per cent while that of transportation and communications is about 24 per cent and that of urban

TABLE 21. *Iran's revised third plan programmes (1962–1968)*

	Rls. 140 Billion Programme		Rls. 200 Billion Programme*		Rls. 230 Billion Programme†	
	Billion Rls.	%	Billion Rls.	%	Billion Rls.	%
1. Agriculture and irrigation	30·3	21·6	45·0	22·5	49·0	21·3
2. Industries and mines	16·6	11·9	21·9	11·0	27·0	11·7
3. Fuel and power	26·1	18·6	27·0	13·5	41·5	18·0
4. Transportation and communications	30·0	21·5	50·0	25·0	56·0	24·3
5. Education	13·5	9·6	17·9	8·9	17·4	7·6
6. Health	10·0	7·2	13·9	6·9	13·5	5·9
7. Manpower	6·2	4·4	8·0	4·0	3·6	1·6
8. Urban development	4·5	3·2	8·0	4·0	7·0	3·1
9. Statistics	0·8	0·6	0·8	0·4	0·8	0·3
10. Planning and housing	2·0	1·4	7·5	3·8	14·2	6·2
Total	140·0	100·0	200·0	100·0	230·0	100·0

* Revised in 1963. † Revised in 1966.

Source: Plan Organization of Iran.

development and housing is about 9 per cent in the last revision of the plan. The allocations to agriculture and irrigation are mainly taken up by construction of large dams.

The 'constructional aspect' of economic development and the low priority accorded to industries and mines are only accentuated when *disbursement* figures rather than planned allocations are taken into account. Table 22 shows actual disbursements for the industries and mines sector of the plan. Only 9·4 per cent of funds allocated for investment in new industries were disbursed during the first half of the Third Plan period. The Second Development Plan taken at its mid-point also showed the same characteristics: low priority to industries (8 per cent of total allocations) and high priority to transportation (35 per cent) and other constructional activities (dams, city improvement plans etc.). See Table 23.

Structure of Foreign Trade. Table 24 shows total commodity trade of Iran to have increased from 11·4 per cent of GNP in 1954 to 29·7 per cent in 1965. Total commodity trade and services have increased during the same period from 14 per cent of GNP to 35 per cent. What is relevant here is not so much the absolute size of the proportion of foreign trade to GNP

TABLE 22. *Plan organization of Iran's disbursements for industrial and mining programmes, 1962–1965/6*

	Planned expenditures %	Actual expenditures as % of planned expenditures
1. Technical assistance to private investors in industries	2·2	21·2
2. Investment in existing public sector industrial units	9·6	52·1
3. Technical assistance to private investors in mining	1·1	52·7
4. Investment in new public sector mines	1·9	36·8
5. Investment in new industries	66·7	9·4
6. Long-term credit to investors and participation in their investment	18·5	48·1
	100·0	21·9

Source: Plan Organization of Iran.

TABLE 23. *Iran's revised second seven year development plan, 1955–62*

	Billion Rls.	%
1. Agriculture and Irrigation	18·9	22
2. Transportation and Communications	30·4	35
3. Industry and Mines	6·7	8
4. Social Affairs	11·7	13
5. Regional Development	12·2	14
6. Other Expenditures	7·0	8
Total	87·2	100

Source: Plan Organization of Iran.

(which may be related to the size of the country among other factors) but its rapid increase over a twelve year period.

The same Table also shows how the oil exports have increased from 20 per cent of total commodity exports to about 80 per cent during the 1962–5 period. Not only proceeds from exports of oil, but also the local expenditures of the oil companies and bonus payments to the government for new

TABLE 24. *Proportion of foreign trade to GNP, Iran, 1954–65 (% of GNP)**

	1954	55	56	57	58	59	60	61	62	63	64	65
1. Total commodity trade	11·4	15·1	19·4	21·7	24·6	24·6	23·2	21·1	21·7	22·1	27·0	29·7
2. Total commodity trade excluding oil exports	10·7	11·7	14·7	15·0	16·4	17·0	15·8	14·3	13·2	13·4	15·9	19·2
3. Total commodity and services traded	14·0	18·5	23·1	26·1	31·5	31·5	29·0	26·7	27·0	27·5	36·0	35·0
4. Value of oil exports as % of total commodity exports	20	57	61	68	71	73	73	77	81	80	84	79

* GNP figures for the years 1959–63 are from *Preliminary Estimate of Iran's National Income*, The Central Bank of Iran, Tehran 1966. The GNP figures for 1964 and 1965 were obtained by increasing the 1963 figure by 5 and 7 per cent respectively. Similarly, the figures for 1956–8 were obtained on a 5 per cent growth rate basis and 1955 and 1954 on a 4 and 3 per cent rate respectively. These rates are no more than 'informed guesses'.

Source: Monthly Bulletins, The Central Bank of Iran.

TABLE 25. *Foreign exchange receipts, Iran, 1954–65* (Million $)

	1954	55	56	57	58	59	60	61	62	63	64	65
Oil revenues	22	92	140	208	270*	261	285	291	342	388	665†	519‡
Year to year % change	—	+320	+51	+49	+30	−3	+9	+2	+16	+13	+72	−22
Purchase of foreign exchange from oil companies	12	47	40	48	74	77	74	100	95	83	89	93
Year to year % change	—	+290	−15	+20	+54	+4	−4	+35	−5	−13	+5	+4
Ordinary exports	95	70	90	98	86	95	106	88	82	97	89	132
Year to year % change	—	−26	+28	+9	−12	+10	+11	−12	−7	+18	−8	+48
Foreign loans and grants	81	92	141	116	62	114	124	152	54	19	34	116
Year to year % change	—	+14	+54	−18	−53	+82	+9	+23	−65	−65	+64	+240
Total	237	327	430	502	551	618	653	693	626	638	933	938
Year to year % change	—	+36	+32	+23	+10	+14	+5	+6	−10	+2	+52	+0·5

* Includes $25 million concession payment. † Includes $185 million concession payment. ‡ Includes $5 million concession payment.

Source: Monthly Bulletin, The Central Bank of Iran.

TABLE 26. *Proportion of imports to GNP and changes in oil revenues, Iran, 1954–65*

	1954	55	56	57	58	59	60	61	62	63	64	65
1. Proportion of imports to GNP	·08	·11	·13	·14	·17	·17	·15	·14	·13	·13	·16	·19
2. Ratio of changes in imports to changes in GNP	—	1·0	·62	·23	·70	·23	·02	−·27	−·33	·17	·74	·58
3. Year to year changes in imports (%)	—	+38	+30	+24	+25	+6	+7	−5	−4	+7	+27	+25
4. Year to year changes in oil revenues	—	+306	+52	+48	+34	−7*	+9	+2	+18	+13	+70	−17*

* The apparent decline in oil revenues is due to a lump sum bonus received by the Iranian government in the previous year for granting new oil concession. Thus the regular revenues from oil exports have not declined.

Source: Monthly Bulletins, The Central Bank of Iran. GNP figures for 1959–63 are from *Preliminary Estimate of Iran's National Income*, The Central Bank of Iran, Tehran 1966. Figures for other years are obtained according to the procedure described in Table 24.

concessions by various foreign concerns help in providing the foreign exchange needed for the expansion of imports. Total availability of foreign exchange and the rate of growth of its component parts is given in Table 25. The predominance of the oil revenues is evident.

The proportion of imports to GNP is shown in Table 26. It increases from ·08 in 1954 to ·19 in 1965. However, it is interesting to note that as in the case of government revenues and expenditures, the proportion of imports to GNP deviates from the trend during the 1960–4 period when the rate of increase of oil revenues slowed down owing to a decrease in oil prices. With the exception of these crisis years, the ratio of changes in imports to changes in GNP is extremely high, about ·50 to ·60.

Table 26 also brings out fairly close year to year changes in oil revenues and imports. It is interesting to observe that the year 1964, in which Iran's four year economic crisis ended, was the year in which the oil revenues increased by 70 per cent and Iran's total foreign exchange availability rose by 52 per cent.

TABLE 27. *Claims of the banking system on the private and public sectors, Iran, 1954–60 (Billion Rls.)*

	1954	55	56	57	58	59	60
Claims on private sector	8·06	9·72	10·82	13·98	22·61	32·24	—
Year to year % change	—	+20	+11	+28	+62	+42	
Claims on public sector	17·05	17·31	19·34	22·90	27·00	28·93	32·35
Year to year % change	—	—	+12	+20	+18	+6	+11
Total claims	25·11	27·03	30·16	36·88	49·61	61·17	—
Year to year % change	—	+8	+11	+22	+34	+23	

Source: International Financial Statistics, June 1962.

Behaviour of the Monetary System. Quite apart from the expansionary effects of the availability of foreign assets on the monetary system, it appears that credit creation by the banking system follows the inflow of oil revenues. No consistent set of figures is available for the entire period 1951–65 (the definitions of various indicators were changed by the Central Bank in 1960, the year it came into existence). Consequently, two different series have been used in Tables 27 and 28 to show how the monetary system's advances to the public and private sectors increased at annual rates ranging from 6 to 20 per cent for the public sector and 11 to 62 per cent for the private sector before the crisis of 1960–4. The same pattern seems to be developing after 1964.

The cyclical behaviour of the monetary system as far as the private

TABLE 28. *Net claims of the banking system on the private and public sectors, Iran, 1960–65 (in Billion Rls.)*

	1960	61	62	63	64	65
1. Net claim on private sector	29·4	33·8	36·0	39·6	48·8	56·1
2. Year to year % change		+15	+6·5	+10·0	+23·2	+15·0
3. Net claim on public sector	18·0	12·3	11·0	11·9	4·1	17·4
4. Year to year % change		−32	−10·6	+8·2	−65·5	+324·4
5. Total net claims	47·4	46·1	47·0	51·5	52·9	73·5
6. Year to year % change		−3	+2·0	+9·6	+2·7	+38·9

Source: The Central Bank of Iran, *Annual Report*, 1965.

sector is concerned can perhaps be explained by the fact that a considerable proportion of the private sector borrowing is used for financing imports. Once the oil revenues do not increase rapidly enough and measures are taken to reduce imports, this automatically affects the credit demand of the private sector. Government agencies reduce their investments both for lack of funds and in order to economize on foreign exchange—which also reduces their demand for credit from the banking system. Consequently, the monetary system finds itself subjected to pressures that follow the inflow of external rents. Given the ineffectiveness of fiscal policy as described above, monetary policy becomes a very weak instrument for implementing counter-cyclical measures.

Patterns of Income Distribution. Statistics for income distribution in Iran are very scanty. The wages and salaries of urban employed population are given in Table 29. It is worth noting that the annual wages and salaries of some 389,000 government employees are about 50 per cent more than the combined wages and salaries of some 785,000 operators and non-operators in the private sector. The wages and salaries of the government employees do not include allowances for travel, housing, medical expenses etc. The difference between the income levels of the governing groups and those of the governed is thus more than what the above figures indicate. The government employees may thus be turning into a privileged rentier class.

An attempt has been made in Table 30 to calculate the share of wages and salaries in GNP. But the figure of 45 per cent must be treated as only an approximation because of the arbitrary assumptions made in its derivation. That the share of income from the property may have increased during the Second Plan period is generally recognized and was stated explicitly in the Third Plan Frame. The reversal of this trend was considered

TABLE 29. *Urban employed population and their wages and salaries, Iran, 1964/65*

	Number of employed	Average weekly wages and salaries per employed (Rls.)	Total annual salaries and wages (Billion Rls.)
A. Operators:			
1. Agricultural workers	57,068	406·5	1·196
2. Unskilled workers	168,854	343·3	3·090
3. Skilled workers	264,976	632·6	8·700
4. Specialized workers	18,220	1,452·6	1·360
5. Highly specialized	3,356	6,785·9	1·183
Sub-total	512,474		15·529
B. Non-operators:			
1. Public sector employees	389,677	1,804·1	36·554
2. Private sector employees	263,698	690·5	9·467
Sub-total	653,375		46·021
Grand total	1,165,849		61·550

Source: 'A Study of Manpower Problems of Iran's Urban Sector', *Studies in Manpower Problems*, vol. 3, Ministry of Labour, Tehran 1966.

TABLE 30. *The share of wages and salaries in GNP, Iran, 1964/65*

	Billion Rls.
1. Wages and salaries of 1·166 million urban employed	61·550
2. Imputed* wages and salaries of 51,840 urban family workers	·919
3. Imputed† wages of 641,682 urban entrepreneurs and self-employed workers	36·000
4. Imputed* wages of 4·100 million rural employed	73·282
5. Total wages	171·751
6. Estimated 1964/65 GNP	405·600
7. % share of wages in GNP $\left(\frac{(5)}{(6)} \times 100\right)$	45

* Assumed to earn the wages of unskilled urban workers.

† Assumed to earn the wages of average workers from work alone. Any divergence from this average is treated as income from human capital.

Source: Tables 1, 4 and *The Manpower Sample Survey of Iran, 1964.*

to be one of the aims of the Third Plan. However, recent studies[17] by the Central Bank of Iran—though based on a limited sample—suggest that income distribution may have become more unequal during recent years. This was found to be more pronounced in larger towns, no doubt because property incomes tend to increase more rapidly in these towns. That land distribution has not checked the increasing disparities in income distribution is also of some interest. The government may have to use fiscal policy for redistributional purposes, even though from the revenue point of view, it may have little urge to do so.

IV

Since the mid-1950's, the Iranian economy has been subjected to the expenditure effects of rapidly increasing oil revenues and/or foreign loans obtained on the strength of future oil revenues. These expenditures have created a set of circumstances that hardly bear any resemblance to Iran's past experiences in economic growth. The repercussions of these expenditures have not been uniform in all sectors of the economy. Agriculture and industry have not thrived as has the services sector of the economy. Though at some points, linkages are being established between the traditional economy and the new superstructure of foreign trade and services that has emerged from the expenditure of external rents, the process is still haphazard and without a clear direction. Whatever direction there is seems still to be aimed at attracting more foreign 'participation' and developing and exporting more raw materials other than oil. This pattern is only too evident in such cases as natural gas, petrochemicals and aluminium. The basic problems of a raw material producing country are either not fully recognized or not seriously tackled. The result is that the mass of the Iranian people are hardly touched by the so-called development programmes that do absorb a considerable amount of the country's investment outlays. The people's participation in the economic activity—especially that of women—is extremely low. Industrialization is proceeding at a slow pace providing little opportunity for employment, and whatever of the investment funds is actually used in the industrial sector is not used to develop industries with the highest value-added per worker. There is considerable disparity of income and welfare between the rural and urban populations and in towns between those employed by the government and the workers in the private sector. Not only have government expenditures and programmes become increasingly dependent on oil revenues, the consumption patterns of the people are also thoroughly geared to the utilization of imported commodities. At the same time the level of the

[17] See *Preliminary Estimate of Iran's National Income*, Tehran 1966.

economy's technology, the nature of its socio-political organization and the standards of the people's general education and training are such that little optimism is warranted as far as the long-run growth prospects of the country are concerned. These prospects can of course be changed as the result of the adoption of appropriate policies, but for the time being the Iranian economy remains, as before, at the mercy of fluctuations in oil prices and weather conditions. On a more general level, the following points can perhaps be made:

(i) If the economic performance of most Rentier States is found to be as unimpressive as that of Iran during the period 1954–65, there would appear to be sufficient justification for doubting whether the availability of capital and foreign exchange are as crucial as they are sometimes assumed to be in the process of economic development.

(ii) Since organizational and technological factors can be collapsed together in the case of underdeveloped countries (for these countries are more concerned with utilizing what is already known and not so much with achieving new break-throughs in technology) the organizational aspects of economic growth, including the social and political structure of developing countries, assumes an importance seldom accorded to it. Political change may turn out to be the factor with the highest shadow price in Rentier States.

(iii) Even with the best of organizations, Rentier States will still have a number of special problems which they will have to solve if their economic growth is to continue smoothly and not be disrupted severely when the external rents begin to fluctuate or even decline. In constructing economic models for these countries, it would be advisable to introduce external rents as a major variable and establish the functional relationships that exist between it and other variables of the system. The shift from a raw material exporting country to an industrial economy would also have to be more deliberately planned.

(iv) For reasons that are partly technological and partly socio-political and economic, few of the Rentier States can remain Rentier States for very long periods of time. By concentrating on the issue of oil royalties, the oil producing countries may discover that they have ignored the most important aspect of having such a large industry on their soil: its potentialities for generating growth. Reversal of the oil company policy of input minimization from local economies and development of ancillary industries based on gas, power and petrochemicals may appear as the most logical way of passing through this transitional stage. Refining and marketing of petroleum by the producer countries will have the same effect.

(v) The socio-political aspects of Rentier States are also of some interest. A government that can expand its services without resorting to heavy taxation acquires an independence from the people seldom found in other

countries. However, not having developed an effective administrative machinery for the purposes of taxation, the governments of Rentier States may suffer from inefficiency in any field of activity that requires extensive organizational inputs. In political terms, the power of the government to bribe pressure groups or to coerce dissidents may be greater than otherwise. By the same token, this power is highly vulnerable since the stoppage of external rents can seriously damage the government finances.

(vi) The problems of income distribution are not easy to solve in any underdeveloped country that tries to achieve rapid growth within the framework of a capitalistic method of production. The problems are more serious in Rentier States because of the concentration of vast external rents in few hands. The temptations for a government bureaucracy to turn into a rentier class with its own independent source of income are considerable.