

## The Study of Supportive Policies of Iran's Government in Energy Sector Considering the Plan of Targeted Subsidies

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### Abstract

*Issue of paying energy subsidies in various forms has been addressed in the plans of the development in Iran. According to development plan, the government was assigned to take some legal actions in order to make targeted the energy subsidies in a way that the system of subsidies is paid in the specified quantity to reach such goals as rationalizing energy consumption, preventing smuggling of these goods, reducing the proportion of social classes with high incomes and increasing the share of subsidies for classes with low-income and etc. In this respect, in the final years of the fourth plan of development, targeting subsidies was approved and it was carried out in 2011. Based on the law of targeted subsidies, the government cut all direct and indirect energy subsidy payments to energy sector and energy prices, which were previously subsidized were now priced under the new terms. On the other hand, to compensate for the purchasing power of households, a monthly cash payment of \$ 40 per person was deposited to their bank account. In this paper, the analytic issues of targeted subsidies to the energy sector, efficiency of government supportive policies in this matter has been assessed.*

**Keywords:** supportive policy, targeting, government, energy, Iran, subsidies

### 1. Introduction

The large number of the uninsured working for small businesses provides some political support for subsidizing these firms in an effort to increase coverage. However, it is argued that it is more efficient to provide subsidies directly to individuals and families than to employers. Subsidies directed specifically to the low-income population will lead to less displacement of private spending because that population has low rates of private coverage. In addition, subsidies based on income treat those in similar economic circumstances the same, eliminating equity concerns associated with treating low-income people differently based on their place of employment (Blumberg and Holahan, 2008). In addition, Ferry and colleagues have shown that providing subsidies specifically to low-income individuals and families is a more target efficient mechanism for subsidizing the uninsured and results in less displacement of existing private spending than providing subsidies to small firms or low-wage workers (Ferry et al., 2002).

An economic reform plan by the Ahmadinejad administration known as “targeting of subsidies” that has been passed in the form of a law several months ago is currently approaching its full implementation. The plan contains radical changes and many aspects of it will have lasting impacts on the Iranian economic system. One of these aspects, the provision for a revised pricing structure for energy sources, should be of particular importance for business prospectors in Iran. As regards domestic sale prices for energy sources such as gas, gas oil, fuel oil, kerosene, and LPG the law provides that these prices should not fall below the FOB Persian Gulf export price for such products by more than 10 percent (inclusive of transport, distribution, and legal charges). A discount has been considered for the sale of crude oil and condensates to domestic refineries in a way that the sale prices to these refineries shall be minimum 95 percent of the respective FOB Persian Gulf Prices.

Concerning the sale of electricity, the government has allowed to raise the prices to the level of the actual production costs within in 3 years, under the assumption of a minimum of 38 percent of output for the power plants. Although these changes will result in a cost increase for those who intend to perform projects in Iran (in terms of increased production costs as a result of higher energy costs), this may eventually help to boost feasibility of projects by increasing their prospects for better product off-takes upon operation of the projects. This aspect will no doubt be an area of increased scrutiny for project analysts in Iran<sup>1</sup>.

<sup>1</sup> [http://www.fichtellegal.com/en/news\\_article.php?news\\_id=69](http://www.fichtellegal.com/en/news_article.php?news_id=69)

According to the government, approximately \$100 billion per year is spent on subsidizing energy prices (\$45 billion for the prices of fuel alone) and many consumable goods including bread, sugar, rice, cooking oil and medicine (CSMonitor.com. 2010-04-30 and Iran daily). However, some experts believe direct subsidies are about \$30 billion, depending on oil prices (Los Angeles Times. 2010-12-18 and Bloomberg).

The subsidy system has been inherited from the Iran-Iraq war era but was never abolished. Iran is one of the largest gasoline consumers in the world, ranking second behind the United States in consumption per car (United States Energy Information Administration, 2000). The government subsidy reform has been years in the making for various reasons (Turquoise Partners, 2011, Tehran Times. 2009-12-07, Tehran Times. 2008-06-24 and Amuzegar, 2005). Iran's Supreme Leader has backed the government's latest subsidy reform plan ([New York times: Supreme Leader in Iran Supports Bid to Cut Subsidies](#)).

### Transportation industry in Iran

Tables 1,2,3,4,5,6,7,8 and 9 show the status of transportation in Iran based on information received from Central Bank of IRI, Ports and Shipping Organization, Road Maintenance and Transport Organization, IRI Railways and Raja Company and Iran's Aviation Organization.

**Table 1: Production value of transportation (fixed cost of the year 1997 - billion Rials)**

	2006	2007	Percent of changes
Road Transport	58815	64618	9.9
Air Transport	5855	6288	7.4
Maritime Transport	3189	3468	8.7
Total	67859	74374	9.6

Source: Central Bank of IRI- national accounts

**Table 2: Intermediary costs of transportation (fixed cost of the year 1997 - billion Rials)**

	2006	2007	Percent of changes
Road Transport	21014	23304	10.9
Air Transport	3178	3426	7.8
Maritime Transport	2133	2293	7.5
Total	26324	29023	10.3

Source: Central Bank of IRI- national accounts

**Table 3: Added value of transportation (fixed cost of the year 1997 - billion Rials)**

	2006	2007	Percent of changes
Road Transport	37801	41314	9.3
Air Transport	2678	2862	6.9
Maritime Transport	1056	1175	11.3
Total	41535	45351	9.2

Source: Central Bank of IRI- national accounts

**Table 4: Gross fixed capital formation of transportation (fixed cost of the year 1997 - billion Rials)**

	2006	2007	Percent of changes
Transport	39636	39290	-0.9
Building	5223	5956	14
Machinery	34412	33334	-3.1

Source: Central Bank of IRI- national accounts

**Table 5: Function of ports during 2006-2008**

Activity	2006	2007	2008	Percent of changes (2006-2007)	Percent of changes (2007-2008)
Oil & Non-oil	110150573	106993768	110112107	-2.87	2.91
Non-oil	63595729	66707933	69309905	4.89	3.9
Oil	46554844	40285835	40802202	-13.47	1.28
Loading and unloading (container TEU)	1663639	1963113	2198562	18	11.99

Source: official website of Ports and Shipping Organization

**Table 6: Performance of transit during 2006-2008**

Material	2006	2007	2008	Percent of changes (2006-2007)	Percent of changes (2007-2008)
Oil	1064681	812232	851100	-23	4.78
Non-oil	4574056	4908680	5006556	7.3	2
Total	5638737	5720912	5857656	1.5	2.4

Source: official website of Road Maintenance and Transport Organization

**Table 7: Performance of road Cargo and passenger sectors during 2006-2008**

	2006	2007	2008	Percent of changes (2006-2007)	Percent of changes (2007-2008)
Traveled passengers (Million people)	224	247.6	263.6	10.53	6.46
Person-Kilometer (Million)	56001	60107	63685	7.33	5.95
Transported cargo	273.6	301.2	319.1	10.08	5.94
Ton-Kilometer (Million)	132070	142942	152996	8.23	7

Source: official website of Road Maintenance and Transport Organization

**Table 8: Performance of rail Cargo and passenger sector during 2006-2008**

	2006	2007	2008	Percent of changes (2006-2007)	Percent of changes (2007-2008)
Traveled passengers (1000 people)	21346	24459	26225	14.58	7.2
Person-Kilometer (Million)	12549	13900	15312	10.77	10
Transported cargo (1000 Ton)	32978	30996	33031	-6	6.5
Ton-Kilometer (Million)	20542	20229	20535	-1.5	1.5

Source: official website of IRI Railways and data from Raja Company

**Table 8: Performance of airway sector during 2006-2008**

Activity	2006	2007	2008	Percent of changes (2006-2007)	Percent of changes (2007-2008)
Transporting national passengers (Million people)	12.4	12.4	12.8	0	3.2
Transporting international passengers (Million people)	5.7	7.2	7.3	26.3	1.38
Total fleet number	134	129	179	-3.73	38.75
Civilian fleet number	83	89	132	7.2	48.3

Source: Website of Iran's Aviation Organization

## **Conclusion**

This paper was concerned with some basic approaches to the status of energy carriers and targeting the subsidy payment. Considering that the role of energy cost in Iran because of the vast oil and gas resources and easy availability of them is too small in compare with other costs, there is not much sensitivity and the impetus for saving and rational use of such natural gifts. However, problems such as economic and social development, the quality of life improvement, environmental problems caused by uncontrolled and inappropriate use of energy as well as the limit in oil resources in near future and over-consumption of them are reasons for reforming the economic system of energy, optimizing its consumption and enhancing efficiency in its use in the country. Based on statistics and information, transportation sector is one of the largest energy and oil product consuming sectors. One method to modify consumption patterns is to modify prices of energy carriers along with making complementary policies to reduce the negative consequences and encourage the society to accept those policies. Due to weak economic base and the improper functioning of economic system in developing countries, energy pricing policies do not perform correctly. Subsidies are not targeted in this country and is consumer-oriented. This is while in most developed countries more subsidies are enacted for production support. Thus, for energy pricing policies in Iran, targeted and specific policies for demand management were carried along with implementation of targeted subsidies and these policies were applied for managing and directing changes in consumption patterns used in 2011. So, it seems that its consequences in future years should be analyzed.

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