

THE DUBAI INITIATIVE

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Policy Brief

IRAN'S YOUTH, THE UNINTENDED VICTIMS OF SANCTIONS



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Dubai Initiative – Policy Brief

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SUMMARY:

1. The effect of the international sanctions on Iran is to deepen its current economic recession and make recovery very difficult if not impossible. In doing so, it will inflict pain on the general population.
2. By prolonging the recession, the sanctions will hurt Iran's youth (15-29 year olds) particularly harshly, as they will bear the brunt of the resulting unemployment. They account for 70 percent of unemployment, and any improvement in their condition depends on economic recovery.
3. Youth account for 35 percent of Iran's population. In the next 15 years they will, for the most part, replace the adults (30-64 year olds) who currently run the country. Their attitudes about what kind of country they want to live in, and how it will relate to the outside world, should therefore be the key outcomes considered when assessing the potential impact of sanctions or military action against Iran.
4. Despite their hard time, large sections of Iran's youth remain hopeful about their future, as they continue to invest in education and have much more favorable views on relations with the West than the older generation they will soon replace.
5. Prolonged major economic disruptions in Iran, caused by the Western sanctions or military action, risk alienating Iran's youth, with serious long-term consequences for the U.S. and its allies in the region.

INTRODUCTION

Iran remained inexplicably calm this summer as various parts of the sanctions rolled out from the United Nations, Washington, and Brussels. The country's press was occupied with reporting on the new policy initiatives from the Ahmadinejad administration, such as removing the thirty-year old subsidies on energy; reviving population growth by encouraging families to have more children as part of its conservative agenda; relocating a large part of the government bureaucracy from the earthquake-prone Tehran to the provinces; and wresting control of Iran's mammoth private Islamic Azad University from Ahmadinejad's powerful rival, former President Rafsanjani. All these initiatives have logics of their own but, curiously, none are directly concerned with the tightening of sanctions.

Even Tehran's sophisticated middle class seemed unconcerned until the news came, on July 16, that the Educational Testing Service (ETS), the company that offers the Test of English as a Foreign Language (TOEFL) and the Graduate Record Examinations (GRE), was halting these exams in Iran because the latest round of UN sanctions prevented Iranians from paying the fees for the tests.¹ Two weeks later the problem had been resolved and the tests resumed. However, as the first widely reported effect of the sanctions, this incident helped underline the fact that sanctions have unintended consequences that could hurt those far removed from the intended target - Iran's Revolutionary Guards.

Unfortunately, not all the unintended consequences of the sanctions can be reversed this easily. Iran's youth, who came to the streets in large numbers last summer to protest fraud in the re-election of President Ahmadinejad, and who for a while not only seemed to threaten his government but shook the foundations of the Islamic Republic, may turn out to be the biggest victims of the sanction. The sanctions are not expressly intended to hurt Iran's economy, but there is little doubt that they will. The only hope for youth to find employment is the creation of new jobs but Iran's economy is in deep recession and in no position to create new jobs unless private investment resumes. Sanctions scare away private investment and thus significantly reduce any chance of economic recovery.

THE ECONOMY IN CRISIS

After more than ten years of robust economic growth, Iran's economy is in its deepest crisis since the war with Iraq. No official figures on total output have been published since the first half of 2008 -- perhaps because they are dismal -- but it is almost certain that economic growth has come to a complete halt. At the very least per capita incomes are falling at about 2 percent per year. Surveys of household expenditures published by the Statistical Center of Iran indicate a far worse picture. In 2008 average real household expenditures declined by about 10 and 20 percent in urban and rural areas, respectively.

Sanctions are not the reason for this economic crisis. The source of the crisis lies in the mismanagement of the oil boom of 2006-07, when oil prices rose to about 3 times their average for the previous five years. Misguided government policies allowed the economy to overheat, which raised the local costs of production and flooded the Iranian markets with cheap imports, hurting domestic production. On ideological grounds, interest rates were lowered and fixed at 12 percent while inflation was twice as high, leading to double-digit negative interest rates. As a result, borrowing expanded rapidly and inflation took off, reaching nearly 30 percent by mid 2008.² Real estate led in rising prices, with home prices in more affluent areas doubling and tripling in one year. To bring down inflation, and acting independently of the Ahmadinejad government, the Central Bank stepped on the monetary brakes harshly, restricting bank credit, which burst the housing bubble and sent the economy into a tailspin.

The self-inflicted pain was followed a few months later, in October 2008, by collapsing oil prices, from over \$140 to around \$40 in just a few months, dashing hopes for recovery and any private plans for investment. The government, short of cash, stopped paying its contractors, who stopped working and laid off workers. Some more established businesses, also short of cash because of tight credit, stopped paying their workers, who sometimes took to street protests to call attention to their plight.

Then, in June 2010, with no sign of recovery in sight, came the news of the fourth round of UN sanctions, followed by additional measures imposed by the U.S., EU countries, Canada, and Australia. The acquiescence of Russia and China, who had previously stood by Iran's side in opposing sanctions in the Security Council, took Tehran by surprise and raised fears in the business community that Iran was slipping deeper into economic and political isolation. The chances of economic recovery now seemed more remote than ever.

In Iran's oil-dependent economy, recessions usually end when the price of oil starts to go up again. This prospect is always there but at this time it does not look particularly bright. In addition, the government lacks the economic sophistication and the macroeconomic tools to engineer an economic recovery. Monetary policy, which worked swiftly in restraining economic activity, is not nearly as effective in stimulating it. Counter-intuitively, interest rates remain fixed even as inflation has fallen sharply, to about 7 percent per year, raising real interest rates from the negative territory to high positive values, in excess of 5 percent. As a result, credit remains tight and borrowing is difficult, which is not what a monetary authority would want to see happen when unemployment is rising.

The scope for fiscal policy is also limited because tax rates are already low and cannot be reduced much further. (Again, counter-intuitively, the government has been trying to collect more taxes from businesses, causing a wave of protests that shut down the bazaars in Tehran and Tabriz in July 2010.³) As things stand now, the government does not have the resources to spend enough to jumpstart the economic recovery.

That leaves private investors as potential rescuers, but they need cheap credit and confidence in the coming of economic recovery before they risk their money. Thanks to domestic monetary policy and international sanctions, both are lacking, so it is unlikely that they will be jumpstarting the recovery. It is precisely by dampening private sector expectations that the recent wave of sanctions will do their greatest damage to Iran's economy.

This dismal outlook is spreading at a time when Iran's middle class, the backbone of the country's modern private economy, feels alienated from the country's political leadership and is in a grim mood following the violent quelling of the protests of the summer of 2009 and the creeping power of the Revolutionary Guards in the government and the economy. The Revolutionary Guards take advantage of the weakening private sector to expand their control over key sectors of the economy and to fill in where private sector stands back. The political crisis feeds into the economic crisis, which deepens the political crisis.

YOUTH STAND TO LOSE MOST

While the stated aim of the sanctions is to target specific individuals and companies related to Iran’s military and nuclear industries, as they prolong the recession their impact will be felt much more widely. One particular group, the youth, stands to lose the most. The employment norms in Iran are such that women and youth receive the lowest priority in hiring and highest priority in layoffs. Table 1 shows the striking difference between youth and adult unemployment rates and between young men and women. Youth unemployment rates are about twice as high as adult rates globally, but in Iran they are six times as high for men and eight times as high for women.

Table 1. Youth Unemployment Rates by Gender (ages 20-29)

Year	Men		Women	
	15-29	30-64	15-29	30-64
2007	20.9	3.5	36.1	4.4
2008	25.6	4.0	45.2	5.4

Source: Author’s calculations from Household Expenditure and Income Survey micro data files provided by the Statistical Center of Iran.

The unemployment rate for young men and women (15-29 years old) in 2008 rose by nearly 5 and 9 percentage points, respectively, while unemployment for older workers (30-64) rose by only 0.5 and 1.0 percentage points (Table 1). The latest official data from Iran’s Statistical Center (based on their labor force survey) confirm the rising trend of youth unemployment into the first quarter of 1389 (spring 2010): the rate was up by 2.8 percentage points for men and 15.3 percentage points for women compared to spring 2009.⁴

In the past, unemployment rates had steadily increased for Iran’s youth, not because of a stagnant economy, but because of the unusually large cohorts born in the 1980s that Iran’s test-based education system could not properly educate, and that its rigid labor markets could not absorb (Salehi-Isfahani and Egel 2010). In fact, during 1996-2006, when, thanks to the oil boom, the economy grew at a robust rate of 5 percent per year and was able to add nearly 6 million jobs, adult unemployment rates remained steady while youth rates increased dramatically (Figure 1). Nearly 80 percent of the increase in unemployment during this period is due to higher youth unemployment. If youth bore the brunt of rising unemployment during a period when the economy was doing relatively well, they will certainly do so while it remains in recession.

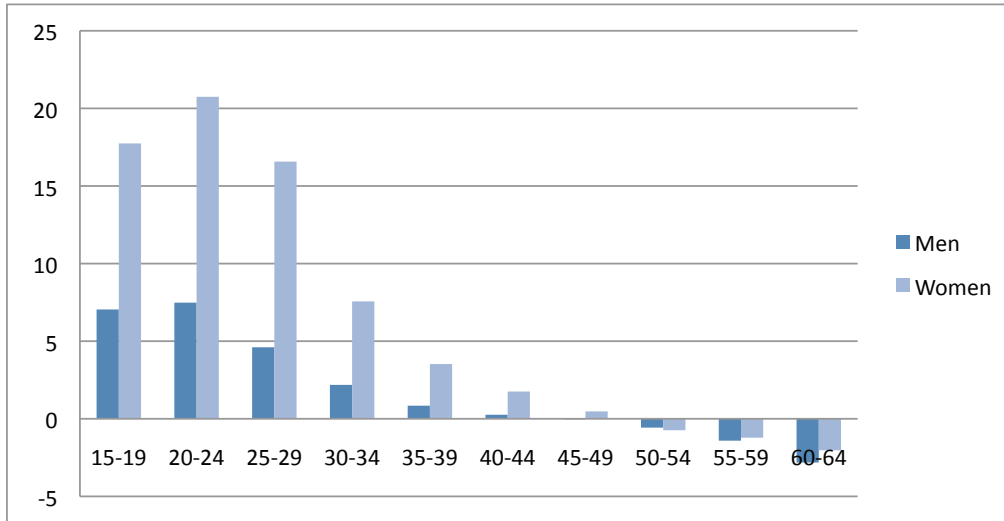


Figure 1. Percentage points increase in the unemployment rates for youth (15-29) and adults (30-64), 1996-2006
Source: The National Census of Population, Statistical Center of Iran.

IRANIAN YOUTH IN “WAITHOOD”

So far Iranian youth have waited, if not always patiently, for their turn to enjoy the opportunities that the country offers its adult citizens — regular jobs, marriage, and homes of their own. What will Iranian youth do if sanctions prolong the recession and they find out that they have to wait even longer? Most youth, especially women, who today marry much later than their mothers, use the time to climb the education ladder. They now outnumber men in universities. Universities have expanded significantly, offering twice as many spots to high school graduates as they did five years ago. But only one-third of these spots are in the coveted free public universities. Another one-third of the places are in private universities that the average family cannot afford, and the rest are in low-quality diploma mills.

However, because the increase in education is supply-driven and is not in response to greater demand from employers, the recent impressive expansion of higher education has simply raised the unemployment rates of university graduates to about the same level as high school graduates. As a result, the fastest-growing industry in Iran is the production of Master’s degrees. In 2010, the number of students taking the central examinations for Master’s level studies reached about one million, almost as many as the 1.2 million who had competed to enter college.

In addition, as the temporary halt of the ETS exams in Iran reminds us, Iranian youth are busy taking the TOEFL and GRE exams to continue their education abroad. The savings of Iranian parents are being invested in the education of thousands of Iranians in various countries from Malaysia to the United States. In 2005, nearly 15 percent of youth reported “preparing for a test” as their regular occupation (Egel and Salehi-Isfahani 2010).

Marriage and having a home of one’s own are also less accessible to this generation of Iranian youth than to any past generation. Nearly 40 percent of women born after the revolution are unmarried by age 25, compared to 20 percent a generation ago. And more than 50 percent of men 25-29 years old live with their parents (Salehi-Isfahani and Egel 2009).

This game of waiting to reach adulthood is played every day throughout the Middle East, so it now has a term of its own to describe it: “waithood,” dubbed by Diane Singerman (2007) and Dhillon and Yousef (2007). But in Iran the waiting game seems to be reaching a critical point, when the players are about to get tired of the game.

UNINTENDED CONSEQUENCES

The view among U.S. policy-makers, during both the Bush and Obama administrations, seems to be that a weaker Iranian economy is not necessarily bad for the U.S.; that indirect pressure from the sanctions, as a result of popular dissatisfaction — the supposedly unintended consequence — is as good as direct pressure by targeting specific individuals and companies related to Iran’s military and nuclear industries. But indirect pressure will come with greater political and social instability in Iran. In view of the already high level of instability in the region, where U.S. troops are engaged in their longest war, greater instability in Iran should be of concern to U.S. policy-makers and their allies. The conflicts in Afghanistan and Pakistan are still expanding and the situation in Iraq remains uncertain. As long as the U.S. views its Iran policy through the lens of containment and military confrontation, an unstable Iran seems like a reasonable outcome for the long-standing hostility between the two nations. This may be why the only warnings of possible disruptions to follow from a confrontation are in the supply of oil.

But this is a view that limits the U.S. role in the region to that of a super power, and does not see its greater role, one championed by President Obama, as the world’s leading democracy and the greatest private enterprise economy. Given this latter role, frustrating Iran’s youth to the point of having them give up on their aspirations for education, jobs, and marriage, in order to overthrow their government, seems shortsighted and a throw-back to the now discredited machinations that brought the Shah back to power in 1953, only at a much grander scale.

To envision an alternative to the current, dangerous course one must consider the fact that, one way or another, in the next 15 years, the 25 million Iranian youths' "wait-hood" will come to an end as they reach adult age. They will, for all practical purposes, replace the equal number of adults (30-64 years old) who now run the country. In one scenario, they would face 15 years of sanctions and military action, causing economic havoc and forcing them into confrontation with security forces and into uncharted territory. Certainly, they would blame their own government for the chaos that destroyed their dreams, but they would also come to distrust the West as an accomplice.

In a completely different scenario, instead of sanctions there would be Western support that helps Iran's economy rebound and resume growth, reform its education system, and give its private sector more say in the running of the country. Instead of pushing it into isolation, Iran is invited to participate more fully in the world economy and to offer its youth greater incentives to learn useful global skills, ones they can apply to global production from inside their country instead of having to leave for Canada and Australia. If this scenario were to play out — and this is a huge if — Iran's future generations might just come to see the outside world as a source of prosperity rather than destruction, and to trust it instead of fear it.

The first scenario is one in which Iran becomes more like Pakistan; in the second it becomes more like Turkey. Granted, which future awaits Iran has a lot to do with the choices that Iran's leaders will be making in the next few months, but the U.S. and its allies are not without a choice here. If the choice is between pushing Iran in one direction or the other, which course should be taken? Leaders in the U.S. can rightly debate this question as the world's only military super power, but as the leaders of the world's liberal order, their choice is clear.

ENDOTES

- 1 New York Times, “Standardized English Tests Are Halted in Iran,” <http://www.nytimes.com/2010/07/18/world/middleeast/18tehran.html>.
- 2 The Central Bank of Iran, Quarterly Reports, Tehran, Iran.
- 3 See New York Times, “Strike at Bazaar Spreads Beyond Tehran,” July 15, 2010. <http://www.nytimes.com/2010/07/16/world/middleeast/16bazaar.html>
- 4 Quarterly report of the Labor Force Survey, 1388 (Winter 2010).

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THE DUBAI INITIATIVE

The Dubai Initiative is a joint venture between the Dubai School of Government (DSG) and the Harvard Kennedy School (HKS), supporting the establishment of DSG as an academic, research, and outreach institution in public policy, administration, and management for the Middle East. The primary objective of the Initiative is to bridge the expertise and resources of HKS with DSG and enable the exchange of students, scholars, knowledge and resources between the two institutions in the areas of governance, political science, economics, energy, security, gender, and foreign relations related to the Middle East.

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