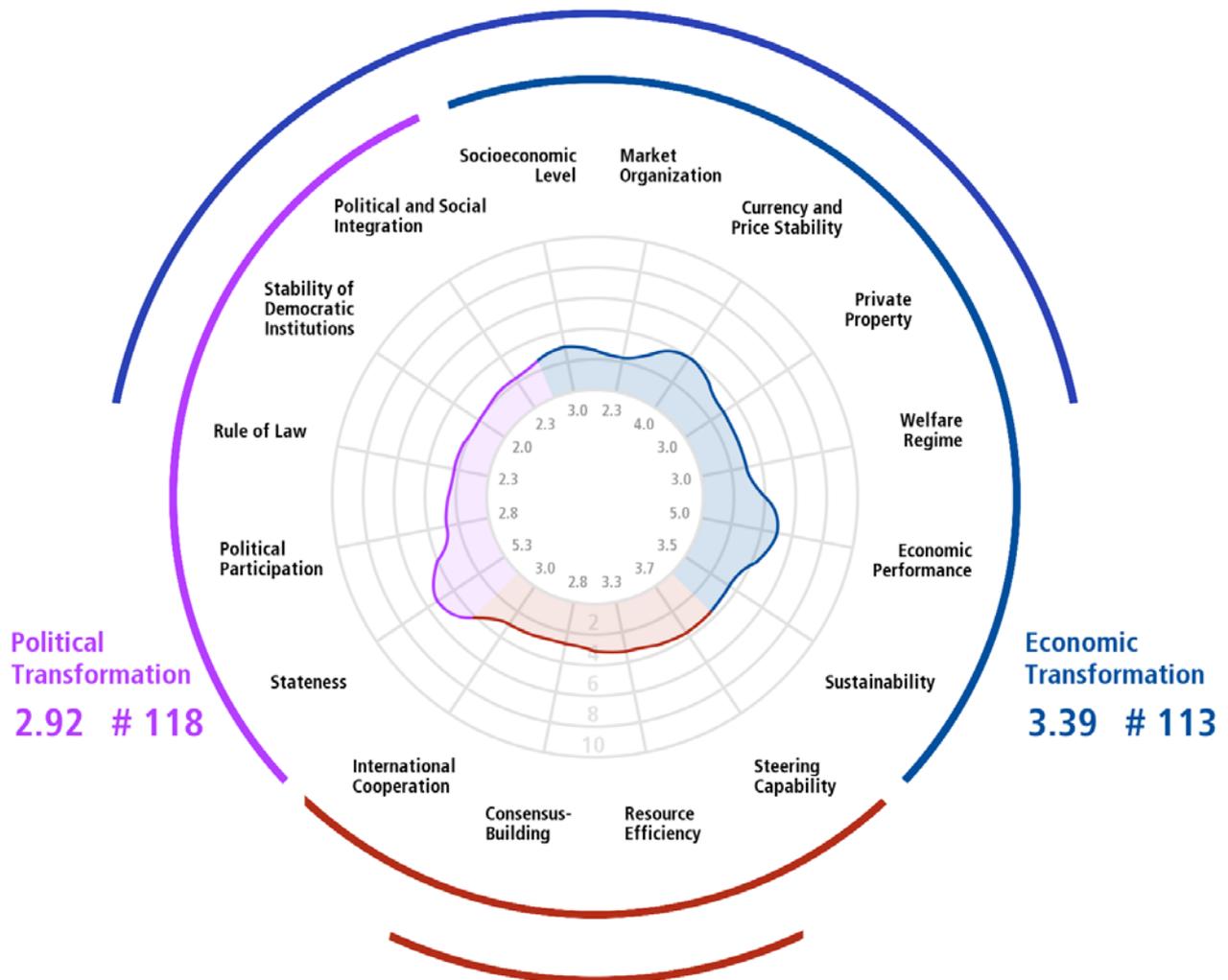


Iran

Status Index

3.15 # 118

on 1-10 scale out of 129



Political Transformation
2.92 # 118

Economic Transformation
3.39 # 113

Governance Index

2.85 # 115

on 1-10 scale out of 129

This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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Key Indicators

Population	M	80.3	HDI	0.774	GDP p.c., PPP \$	-
Pop. growth ¹	% p.a.	1.1	HDI rank of 188	69	Gini Index	38.8
Life expectancy	years	75.7	UN Education Index	0.738	Poverty ³	% 2.5
Urban population	%	73.9	Gender inequality ²	0.509	Aid per capita \$	1.4

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

Undoubtedly the Joint Comprehensive Plan of Action (JCPOA, Persian Barname Jame‘ Eqdam Moshtarak, BARJAM) marked the most important key development in the period between February 2015 and January 2017. Reached in Vienna on 14 July 2015 between Iran and the P5+1 (the five permanent members of the United Nations (U.N.) Security Council China, France, Russia, United Kingdom and United States plus Germany), it is a historic deal to ensure Iran’s nuclear program remains peaceful and improves relations particularly with the U.S. and the European Union (EU). Iran hoped the agreement would result in swift economic recovery, which the nearly bankrupt country urgently needed. The lifting of sanctions and new access to international markets was very promising. In 2016, Iran sold nearly 2.5 million oil barrels and had access to formerly frozen international capital. Indeed, certain economic indicators improved, with inflation declining and growth rates increasing. Yet, economists warn against possible imminent collapse. Whether conservative-Islamic or reformist, Iranian governments have a tradition of sugarcoating a desolate socioeconomic situation. The dramatic fall of oil prices and the persistent stagnation in some economic sectors made clear that Iran’s problems have deeper reasons, which will not to be eliminated by the nuclear deal.

The second key event were the parliamentary elections and the Assembly of Experts on 26 February 2016, where reformists triumphed impressively.

The JCPOA averted the danger of war for Iran, but also helped Iran’s intervention and war efforts in the region because Iran’s extensive interference has been tolerated by the Obama administration. Iran is fully involved in the Syrian war, with financing, war equipment and soldiers. Iran and Hezbollah have, in conjunction with Russia’s military support, held Syria’s President Bashar al-Assad in power.

Tensions between Saudi Arabia and Iran increased, particularly through proxy wars in Yemen and Syria. Protesters in Tehran set the Saudi embassy on fire after the execution of Shi’ite-Saudi cleric

Sheikh Nimr al-Nimr in January 2016. Following this, Saudi Arabia cut its diplomatic ties with Iran.

History and Characteristics of Transformation

The constitution of the Islamic Republic of Iran, enacted after the Islamic revolution of 1979, combines two contrary principles by blending republican-democratic elements with an Islamic legal system, which makes it extremely complex. According to the principle of the guardianship of an Islamic jurist (Velayat-e Faqih), a supreme leader (in Persian Rahbar) leads and governs the state, thus overshadowing the constitution's republican-democratic principles. An Assembly of Experts, whose members are directly elected by the people, elects (and may dismiss) the supreme leader. However, candidates must be approved by the Guardian Council whose six clerical members are directly appointed by the supreme leader while the remaining six members (jurists) are laymen confirmed by the parliament (upon the proposal of a chief justice who is himself directly appointed by the supreme leader).

The Guardian Council also controls the compatibility of laws passed by the parliament to Islamic law (Shariah) and decides which candidates can run for parliament or the presidency. The supreme leader must approve any revision of the constitution. Constitutional legal transformations therefore are not possible without his permission. Hence, power is concentrated in the supreme leader and the Guardian Council, both not democratically elected.

With the primary motive to protect the poor, the Islamic Republic restructured the economy along its ideology, including centralization and nationalization of formerly private banks and industries, and the establishment of "charitable foundations" to handle the investment and distribution needs of civil society. This system turned out highly susceptible to corruption.

Despite the U.S. imposed economic sanctions in the early 1980s following the hostage crisis at the American embassy in Tehran, the Iranian economy grew at a consistent rate throughout the era of pragmatism under late President Akbar Hashemi Rafsanjani (1989-1997) and the era of reform under President Mohammad Khatami (1997-2005). This was in large part due to the country's significant income both from oil and gas exports. Believed to be the world's second largest store of natural gas reserves after Russia, oil and gas revenues account for 60% of the entire Iranian budget and for 85% of the country's overall export revenue. Despite historically unprecedented oil revenues, by early 2013 Iran suffered a sharp economic setback under President Mahmoud Ahmadinejad (2005-2013) mainly because of the incompetence of, and disputes within Iran's leadership, which became less rational and secular and more ideological and religious. Frustrated Iranians protested in mass demonstrations (the so-called Green Movement) after rigged presidential elections in 2009, stopped only by massive police brutality and random arrests.

Ideological and religious dogmas are basic principles of politics and the economy in Iran, often preventing the implementation of professional strategic plans, projects and expertise. The

leadership of Ayatollah Khamenei and the entire ideological-religious foundation of the Islamic Republic are the major constraints.

Iran's aggressive foreign policy under the guidance of Ahmadinejad, especially the acceleration of its nuclear program that included the enrichment of uranium to 20% fissile purity, triggered sanctions of unprecedented severity. A collapse of the regime was only averted by the record-high levels of oil income, which enabled the government to calm people and prevent riots through massive imports of consumer goods to satisfy basic needs. This import policy though undermined domestic industries and (if continued) would have resulted in the bankruptcy of the state.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The government has full control over all security forces and almost the country's entire territory except some border areas. Traditionally, Iran's (civil) national police forces are responsible for internal security and in the event of protests or riots, are supported by the Islamic Revolutionary Guard Corps (IRGC) and the Basij militia. Yet in reaction to the increasing internal challenges, the regime has shifted more responsibility for inner security to the IRGC. Since 2016, the Kurdish Party of Iran started an armed conflict against the IRGC. This has left several victims dead or wounded on both sides. Many Iranians are very concerned that this armed conflict threatens Iran's territorial integrity.

Parliament decided in January 2017 to increase defense spending from 2% to 5% of the budget. The budget includes the Iranian Revolutionary Guards missile development program which has seen a vast increase over the last years despite international criticism.

The immediate threat of the Islamic State (IS) to Iran has been exaggerated by the regime. Whenever the body of a dead Iranian fighter from Syria was brought to Iran, the regime spread the information that IS was close to the Iranian borders or that some terrorist cells linked to IS were smashed. In reality, Iran is almost the only state in the region where IS did not carry out terrorist attacks.

Although the conservative Islamic establishment has been trying to enforce its Islamic ideology under Shariah law since the Iranian Revolution, Iran is determined by three cultures, which are Zoroastrianism, Islam and Western culture.

Most Iranians accept the nation state as legitimate and agree with the broad definitions of citizenship. The majority of Iranians do not understand the regime's hostility against (or questioning of) the ancient Iranian civilization. On the anniversary of the birthday of the ancient King Cyrus the Great in October 2016

Question
Score

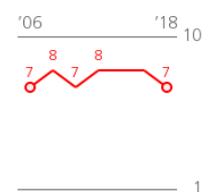
Monopoly on the
use of force

7



State identity

7



thousands of Iranians gathered around his tomb in Pasargadae, turning this event into a protest against the clerical regime's policies.

Kurds and other ethnic groups in the southeast are partly excluded from this consensus, fighting for recognition as autonomous minorities for decades. Political protests in Iranian soccer stadiums exemplify increased ethnical tensions. For instance, in the province of East Azerbaijan's capital city Tabriz fans of Traktorsazi Tabriz (a football club with the third highest fan base in the Iranian Premier league) were labeled as separatists for wearing shirts with Turkish and Azerbaijan flags. That is a very hot topic discussed in Iranian social media.

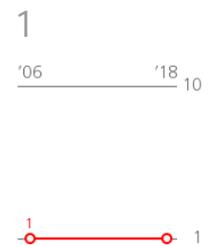
Although the cabinet of President Hassan Rouhani claimed to be pragmatic and reformist, the Islamic Republic continued to implement the Shi'ite interpretation of Islam determined by the interpretation of the ruling establishment, particularly the Guardian Council. Supreme leader Ayatollah Seyed Ali Khamenei controls foreign and domestic policy. As a result, the ruling elite's interpretation of the Shi'ite religion serves as the basis for politics and society. Khamenei has powerful representatives at the universities, in the three forces of the army, in state administrations and in many other institutions, ensuring the following of religious rules. The numerous religious institutions that are immensely funded by state subsidies constantly take action by intervening in social policies and campaigning to influence the population. For instance, extreme religious education institutions such as Howzeh Elmiye Qom and its preachers have been given more latitude for religious agitation. Qom, home to many senior clerics, most of them close to Khamenei, is considered the "religious capital" and second center of political power after Tehran. Some of the country's most significant decisions are shaped in Qom's influential Shi'ite clerical centers such as the Qom Seminary Scholars Community and the Imam Khomeini Education and Research Institute.

In September 2016, the Islamic Republic funded a huge march to Karbala where thousands of pilgrims from Iraq, Iran, Pakistan and other countries walked the main road between Najaf and Karbala to reach the tomb of Imam Hussein.

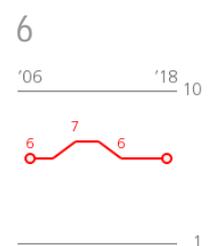
Iran has 31 provinces and a number of cities, divisions, municipality and villages but its administrative structures are highly centralized. Elected local councils are responsible for the administration of each entity; they also choose mayors and manage the heads of each administrative level.

The government delivers basic public services to the citizens in most parts of the country, but often state services and administrative institutions operate inefficiently, due to red tape, nepotism, corruption and interference by other authorities. The 2016-2017 Global Competitiveness Index places "inefficient government bureaucracy" as the third most problematic factor for doing business in Iran.

No interference of religious dogmas



Basic administration



Iran remains a state with a very weak tax system. Several gigantic state-owned or semi-independent economic enterprises including all institutions and foundations (Bonyads) that are subordinated to the supreme leader are exempt from tax. One of them is the powerful, 130,000 strong company Khatam al-Anbiya Construction Headquarters that is owned by the IRGC, which dominates the entire construction and development sector and also massively interferes in the government's policy decisions.

Police forces are also highly inefficient. Driven by religious views and affected by high levels of corruption, the police in coordination with the Basij militia and the IRGC immediately take action against socially and politically motivated protests but are less responsive when it comes to protecting citizens against criminal activity. Crime rates are rising relentlessly especially in the capital despite the judicial imposition of severe penalties as a deterrent. Criminals, especially drug addicts, alarmingly overcrowd Iranian prisons.

2 | Political Participation

Elections to the parliament and the Assembly of Experts took place on 26 February 2016. Sweeping disqualification of reform-minded candidates overshadowed the process. However, there is reason to believe that a government-friendly parliament will be established. The Assembly of Experts will remain loyal to Ayatollah Khamenei, whose ailing health is a reason for concern.

From a total of 166 approved candidates, 88 were elected to the assembly. The reformist faction sought to weaken Islamist candidates close to Ayatollah Khamenei in the belief that it had been unfairly penalized in the approval process by urging supporters to vote for less radical, well-known rivals.

At least in Tehran this strategy proved highly successful. From 16 candidates that were listed on the capital's reformist list, 15 were elected as experts of the assembly including the leaders of the reformist camp, former President Hashemi Rafsanjani and current President Hassan Rouhani. A massive surprise was the defeat of hardliner Ayatollah Mohammad Yazdi who was the chairman of the outgoing Assembly of Experts, and Ayatollah Mesbah Yazdi who is the spiritual leader of the radical parliamentary group Front of Islamic Revolution Stability. While major media outlets served the conservatives as propaganda tool, the reformist relied on social media.

The incoming parliament comprises 120 reformists, 83 Islamists, 81 independents and five representatives of religious minorities. The representative of a seat from the Isfahan district remain unclear. Although the authorities of the Guardian Council disqualified many reformist candidates to run for election, less than one-third of those included in the reformist lists are actual reformists. Two-thirds are independents and

Free and fair elections

4

'06 '18 '10



1

critical moderate conservatives whom the reformists placed on their lists, as Behrouz Khosrozadeh and Mandy Lüssenhop showed in “The Diplomat.”

Given the massive rejection of reform candidates, the elections cannot be marked as free and fair. Ayatollah Ahmad Janati took 16th place and was the last to enter the Assembly of Experts. As the Assembly of Experts was now dominated by so-called reformists, he became the president of this constitutional body. That example shows evidence over the value that is attached to those elections.

The Parliament took some government-friendly measures (for instance, there is one minister who survived two impeachment attempts by conservative MPs), but the ‘victory’ of the reformers in February 2016 faded long since. The Parliament remains powerless against Ayatollah Khamenei and numerous foundations and institutions are subordinated to him that the parliament cannot bring to account. In June 2016, a scandal of astronomically large salaries from top senior Iranian government employees and top civil servants to bank bosses was revealed. The revelations made people angry but parliament refused an investigation.

In August 2016, a corruption scandal of the City Council and Tehran’s mayor Mohammed Bagher Ghalibaf remained without parliament’s investigation as well. Evidence reveals sales of more than 1,100,000 square meters of government-owned properties (including apartments and villas) to members of the City Council, government officials and various people who are close to Ghalibaf for very low discounted prices.

Since Rouhani took office, the other two constitutional powers (judiciary and legislative) attempted to pressure him and block his reform policies. Though reformers dominate the parliament since 2016, Rouhani cannot carry out his policies without the support of the supreme leader. Khamenei backed Rouhani on foreign affairs, especially in the nuclear issue but domestically he favors a more conservative approach. Since in consequence, many sanctions unrelated to nuclear sanctions hindered the Iranian economy from making tangible progress, Khamenei a posteriori criticized Rouhani’s nuclear politics although he fully agreed to the entire nuclear negotiations.

A hard, mutual battle between President Rouhani and Sadeq Amoli Larijani (head of the judiciary) takes place, particularly since Larijani recently provided a scandal with more than 60 bank accounts of the judiciary run under his personal name, with the money sitting in his private account. Larijani raises accusations of financial inconsistencies during Rouhani’s election campaign in 2013 and of the non-transparency of financial transactions of the presidential office.

In political, economic and cultural sectors, the IRGC puts the government under enormous pressure. President Rouhani has repeatedly requested the IRGC respect the order of Ayatollah Khomeini (the founder of the Islamic Republic of Iran) to not

Effective power to govern

2

'06 '18 10

2 1

interfere in politics. In January 2017, Rouhani warned the IRGC not to interfere in the upcoming presidential elections while Ayatollah Khamenei already in October 2016 forbid any involvement of the IRGC in the elections. Islamic Revolutionary Guard Corps state that they never interfered in the election, yet hardly anyone believes them. The IRGC's own prisons and arbitrary arrests are known. Rouhani is also completely unhappy about the strong influence of the IRGC in foreign policy. Iran's Middle East policy is to a great extent led by the commander of the al-Quds Forces Major General Qassem Suleimani (who is responsible for operations of the IRGC's division outside Iran) than by foreign minister Mohammad Javad Zarif.

In summer 2016, Mohammad Shariatmadari (vice president for executive affairs) said that the government could not work due to so many obstructions.

Association and assembly rights are granted in the constitution's Articles 26 and 27, though the conformity with Shariah law acts as barrier in almost all articles. Conservative mullahs interpreting the law often consider gatherings as un-Islamic, so these rights have never been fully applied in practice. Public demonstrations and assemblies are considered detrimental to the fundamental principles of Islam.

Iran's government is terrified of social and political assemblies and acts to prevent them. Rouhani's so-called Government of Hope and Prudence was unable to improve the right to freedom of assembly against conservative forces among clerics, the IRGC and in the judiciary. However, reformists successfully established at least two new parties, namely Nedaye-Iranian and Hezb-e Ettihad-e Mellat-e Iran. In addition, the increasing usage of social media increasingly allows Iranians to bypass gathering restrictions. An illustrative example was the gathering at the tomb of Cyrus the Great in October 2016.

At the same time, lectures in front of gathered interested parties, from the most loyal to sometimes critical high-level personalities such as the current vice president of the parliament Ali Motahari, have been hindered through violent interruptions of fanatic forces.

Lately, numerous music concerts are getting canceled last minute across the country by the Ayatollahs as well as local representatives of the supreme leader. They generally consider music to be un-Islamic. Ayatollah Seyed Ahmad Alam al-Hoda even completely blocked music concerts in his northern city of Mashhad.

Though guaranteed by Article 24 of the constitution, Iranian authorities continue to restrict freedoms of expression. The structure of the Iranian media system (print and electronic) is not designed for the spread of pluralist opinion, and Facebook, Twitter, YouTube and other social media websites are still banned. The 2016 World Press Freedom Index of Reporters without Borders (RSF) ranked Iran 169 out of 180, which is still an improvement to 2015 when Iran ranked 173 out of 180. As RSF reported, 24 Iranian journalists were in prison during 2016. Only Turkey, Syria,

Association /
assembly rights

3

'06 '18 10



Freedom of
expression

2

China and Egypt were considered worse. In June 2016, the reformist newspaper Ghanoon was suspended. In April 2016, an Iranian court imprisoned four journalists, Afarin Chitsaz, Ehsan Mazandarani, Saman Safarzaei and Davoud Assadi; prominent Iranian journalist Issa Saharkhiz got imprisoned for three years. During the run-up to the nuclear deal, meanwhile, four Iranian-American journalists including Jason Rezaian were released after several years of imprisonment and were allowed to leave Iran in January 2016.

Despite these constraints, critical voices, opinions and writings circulate across society (which is, from the perspective of the state, illegal). Approximately 45 million Iranians actively use the Telegram messenger, a Russian messaging app, which has become very popular since 2015.

The three Green Movement leaders Mehdi Karroubi, Mir Hossein Mousavi and his wife Zahra Rahnavard remain under house arrest without charge or trial. In March 2016, Mehdi Karroubi wrote a remarkable public letter urging President Rouhani – and in fact indirectly Ayatollah Khamenei – to give him a fair public trial so he could prove who was responsible for the country's problems.

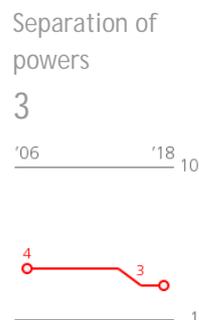
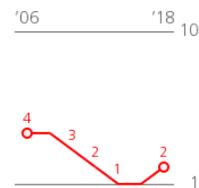
3 | Rule of Law

The constitutionally guaranteed separation of powers is not implemented in practice. The Assembly of Experts is the highest constitutional organ, responsible for appointing and dismissing the supreme leader of the Islamic Revolution, a position held by Ayatollah Khamenei since 1989. The supreme leader has absolute profane and religious authority over the political and judicial institutions of government and is above all state branches and the constitution.

Personal relations trump constitutional stipulations. The head of the judiciary Ayatollah Sadeq Amoli Larijani admittedly obeys Ayatollah Khamenei, and his brother Ali Larijani (speaker of parliament) is also completely loyal to the supreme leader. But Ali Larijani became closer to President Rouhani while his brother Sadeq acts as one of the most prominent adversaries of Hassan Rouhani.

Khamenei can annul any bill passed by the parliament, whose members are preselected by the Guardian Council loyal to him, via a so-called supreme leader order. The supreme leader also seeks to control the executive through direct orders or indirect pressure on the government through his proxies.

Though parliament and the executive are dominated by reformists since early 2016, there is hardly any chance to implement progressive ideas. In general, Iran's parliament wields only limited influence on any policies, whether foreign or domestic: decisions here are the remit of Ayatollah Khamenei who has the power to reverse parliamentary decisions by decree.



Khamenei directly appoints the head of the judiciary who in turn appoints senior judges, while the people elect the members of parliament and the president. Consequently, the judiciary is the least autonomous of the three branches of state power. The constitution provides civil, criminal, military and revolutionary courts as well as a special court for the clergy. The right of appeal is guaranteed but limited in practice, particularly in cases that affect national security or drug-related offences.

The judges are mostly clerics are trained in Islamic jurisprudence at universities or hold degrees from religious law schools particularly those in the Shi'ite stronghold Qom. They must be accepted as mujtahids (authoritative interpreters of Islamic law) by religious authorities.

However, the major issue in the judiciary is corruption. In political cases, intelligence services determine the outcome of trials. Rich and influential Iranian personalities are either spared from prosecution or can move a trial in their favor. Only the mutual conflicts between the reformist and conservative Islamist camps who want to weaken each other and bring discredit to the other side ensure that some highly corrupt personalities, such as the Iranian billionaire Babak Zanjani, are prosecuted. The lack of an independent judiciary along with the absence of a free press are the main reasons for rampant corruption in Iran. This situation has remained unchanged under Rouhani.

Office abuse is omnipresent in Iran. One of the greatest scandals during the assessment period was excessive salaries for certain exalted government officials. It proved that corruption and nepotism are not limited to one regime faction, though both camps – Islamists and reformists – work to mutually discredit each other by constantly unmasking new corruption cases.

Rouhani's brother Hossein Fereydoun was accused of abuse of power when registering for doctoral studies at the National University of Tehran. Accusations against him were strongly expressed by conservative hardliners in January 2017, shortly before the next presidential elections in May 2017. Some 46 conservative parliamentarians, the Islamist judiciary and media – subordinated to the IRGC – were behind the corruption "investigations" against him.

Among the conservatives, the head of judiciary Sadeq Larijani is accused of having 63 secret and illegal personal bank accounts with billions of Iranian tomans. Some reports suggest that the accounts had been opened with the approval of the supreme leader Ali Khamenei.

Towards the end of 2016, a large corruption scandal involved the mayor of Tehran Mohammad Bagher Ghalibaf and some members of the Tehran City Council. As well, Saeed Mortazavi, former prosecutor-general of Tehran, received a sentence of 135 lashes in November 2016 for "seizing and wasting public funds" during his tenure as head of Iran's social welfare organization under then President

Independent judiciary

2

'06 '18 10



Prosecution of office abuse

2

'06 '18 10



Ahmadinejad. However, observers criticized that he remained unpunished for much worse crimes he apparently committed against political prisoners and oppositionists after the 2009 anti-Ahmadinejad protests.

Guaranteed by Articles 19 to 27 of the constitution, civil rights are not granted in practice, including under Rouhani. NGO and U.N. reports document massive shortcomings for instance in discrimination and further human rights violations against religious minorities like Christians, Jews, Sufis and Sunni Muslims, and particularly against Bahai and their faith. Women and girls are structurally discriminated against and intimidated in law and practice.

Iran's penal code, based on Shariah, permits flogging, amputation and execution by hanging for a range of social and political offenses and is to be strictly adapted. Most of these penalties are drug-related offenses although a number of political prisoners convicted of moharebeh (enmity against God) have also received death sentences. Shahindokht Molaverdi, the vice president for women affairs, said in February 2016 that the entire adult male population of a village in southern Iran had been executed for drug offences.

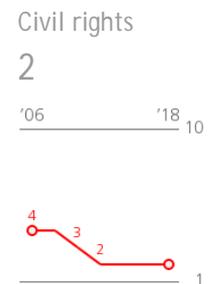
Since late 2016, Iranian prisoners Saeed Shirzad, Arash Sadeghi, Ali Shariati, Morteza Moradpour and Nizar Zakka are all on life-threatening hunger strikes. The five prisoners demand reviews of their unjust prison sentences. Nizar Zakka is a Lebanese citizen with U.S. permanent resident status.

The U.N. Special Rapporteur on the situation of human rights in the Islamic Republic of Iran, Ahmed Shaheed, former foreign minister of the Maldives, will be banned from travelling to Iran after he leaves office in 2017, because he heavily criticized Iran in his last report to the U.N. Human Rights Council, according to Amnesty International. This is despite his statement that the amount of executions in 2016 had decreased compared to 2015.

His successor, Pakistani lawyer and human rights activist Asma Jahangir, was not allowed to travel in Iran to conduct investigations. The Rouhani government also announced its refusal to the appointment of Jahangir.

However, the authorities seem to realize that the mass executions for drug-related offenses have no intimidating effect. The regime intends to revise its drug-related laws. In December 2016, President Rouhani started an offensive. He signed the Iranian Citizens' Rights Charter, which contains 120 articles. The Charter is positive progress but it has no executive guarantee.

Also, behind this seems to be a conflict about power. According to the Constitution, the president is responsible for the implementation and protection of all constitutional stipulations, including civil and citizen rights. Rouhani accused the conservative in the judiciary of torpedoing his policies by continuing fundamental rights violations.



4 | Stability of Democratic Institutions

Iran's policy, built on a unique mix of republican elements and Shariah-based legislation, provides little room for democratic institutions. The judicial procedures that are supervised by the Supreme Court are mostly unjust and undemocratic. Iran's parliament wields only limited influence on foreign and domestic policy. Decisions are the remit of Ayatollah Khamenei who has the power to reverse parliamentary decisions by decree. Nevertheless, a reformist-dominated parliament is much better than one of conservative Islamists and can support a moderate president as it currently appears to do. Rouhani's so-called Government of Hope and Prudence has inspired hope and confidence but its performance has been ambivalent so far. Aside from drawing attention to social and economic problems and criticizing the conservative camp for preventing his government to work, it has not put much effort in countering pressure from the hardliners. The domestic political field is largely left to the conservative Islamists.

The Iranian constitution contains democratic elements such as the direct election of the parliament, the president and local government bodies. It is undermined by powerful figures including the supreme leader and the members of the Guardian Council who themselves lack democratic legitimacy. The Guardian Council decides upon the candidates who may run for parliament, the presidency or local government bodies.

The reformist and pragmatist camp that is said to seek to reconcile Islam and democracy makes little progress, and the passing of Rouhani's great influential mentor Rafsanjani, who died in January 2017, was a great loss for them.

5 | Political and Social Integration

Parties play only a narrow role in Iran, and are not particularly productive. Their financing and administrative structures lack transparency, and they have little input in shaping opinion and are not able to mobilize their party members. Under President Rouhani, however, parties have gained some importance as the dominating "House of the Parties" parliamentary faction that includes the conservative Islamists, independent pragmatists and reformists, took much more action. In April 2016, Deputy Interior Minister Hossein Ali Amiri announced that between August 2013 and April 2016 twelve permissions for the formation of new parties were given.

In total, 242 political parties exist in Iran. These are divided into active, semi-active and suspended parties. The last mentioned have no significant influence on the policy and political process, except for building lobbies. Mehdi Karroubi's National Trust Party who was banned after the riots of 2009, is allowed to practice again. The other two opposition parties, the Islamic Iranian Participation Front (Jibhe Mosharekat

Performance of democratic institutions



Commitment to democratic institutions



Party system



Iran-e Islami) and the Organization of the Mujahedeen of the Islamic Revolution (Sazemane Mojahedine Enghelabe Eslami), remain banned.

A civil society that is defined by existing independent political parties and various independent interest groups acting freely does not exist in Iran. There are syndicates of teachers, bus drivers and mine workers who occasionally protest for their rights. Their demands are mostly complaints about the material and financial situation and poor working conditions and are not respected or suppressed. Otherwise, there are numerous small guild clubs and crafts in many branches. It is difficult for large interest groups to enforce their demands if they do not belong to influential lobbies. In Iran, the lobbying system prevails under which independent interest groups suffer and generating support beyond the regime remains impossible.

There is no data on the level of acceptance of democratic norms in Iran. But certainly, Iranians are disillusioned and generally have little confidence in institutions, making jokes about them. The least trust is placed in the security apparatus: the police, military and state security forces including the IRGC.

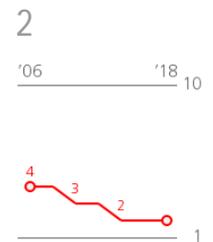
At the same time, the many years of non-democratic, religious rule means that most citizens simply do not know how democratic institutions work. Solidarity, tolerance, mutual respect or even refraining from violence in disputes are often disregarded by citizens. It is most likely that the upper-middle and upper classes generally approve democratic norms and procedures, while the lower classes are more interested in material needs.

Trust between individual citizens exists only rudimentarily. The regime has banned many NGOs with political orientation and arrested their leaders, hindering in consequence further self-organization within civil society. Nevertheless, Iranians are able to stick together in difficult times, helping each other by creating spontaneous and autonomous groups and organizations.

Hundreds of non-political NGOs are engaged in a process of socio-organizational networking, at times using online platforms. For instance, the gathering of thousands of protesters against the regime at the tomb of Cyrus the Great in October 2016 became possible via enormous utilization of social media like Telegram or Instagram.

During Rouhani's presidency, a number of aid groups have been set up to help people in need. In Tehran alone, more than 15,000 people are homeless ("Kartonkhab", poor people sleeping in cardboard boxes). A great innovation was the so-called Wall of Kindness, a place across cities where passers-by are invited to "leave what you do not need" or "take it if you need." Many Iranians decided to take matters into their own hands to help homeless people. Also, these actions gained popularity via social media networks.

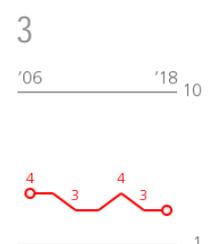
Interest groups



Approval of democracy



Social capital



II. Economic Transformation

6 | Level of Socioeconomic Development

UNDP's 2014 Human Development Index assigns Iran 0.766 points, bringing it to rank 69. And while Iran's human capital rates relatively well in the 2016-2017 Global Competitiveness Index at rank 76, and thus among the countries with 'high human development,' declining economic performance has increased poverty and exclusion levels tremendously. The economic growth rate has increased and the inflation rate has declined.

The World Bank estimates that Iran's economic growth totaled nearly 0.5% in the period from March 2015 to 2016. Against the backdrop of lifted sanctions following the nuclear deal between Iran and the P5+1 group, economic growth is expected to rise to over 4% in 2016-2017, though the sanctions imposed separately by the U.S. and the EU regarding terrorism and human rights violations remain in place. Long-standing American sanctions forbid U.S. citizens, firms, and banks from conducting business with Iran. However, the inflation rate of 45.1% in 2012 decreased to 12.6% in January 2015 – certainly Rouhani's biggest economic achievement. The unemployment rate, meanwhile, remains high, currently 11.7%. Deputy Interior Minister Morteza Mirbagheri said in April 2016 that unemployment had even reached 70% in 1,200 cities. According to Adel Azar, head of the Statistical Center of Iran (SCI), university graduates are the hardest affected with a 43% unemployment rate.

In January 2017, prominent economist Said Lailaz warned that Iranians are becoming both poorer and older. Lailaz added that in the past four decades, Iran lost the best opportunity for socioeconomic and industrial progress and development while the country possesses both crucial conditions, which are money and a young population.

These issues can be traced back to the sanctions still in place, mismanagement, corruption and the dualism within the country's power structure. The specter of renewed sanctions in case Iran does not comply with the terms of the nuclear deal has created a climate of insecurity, which acts as a deterrent to long-term investment. The Financial Action Task Force on Money Laundering (FATF) raised serious allegations of the credibility of the Islamic Republic and keeps the country on its "black list."

The 2016-2017 Global Competitiveness Index addresses access to financing, inefficient government bureaucracy, policy instability, corruption, inadequate supply of infrastructure, foreign currency regulations, restrictive labor regulations and tax rates as the most problematic factors for doing business.

Question
Score

Socioeconomic
barriers

3

'06 '18 10



The Heritage Foundation's 2016 Index of Economic Freedom with no change to the previous year ranks Iran 171 out of 178. The World Economic Forum's 2016 Global Gender Gap Index assigns Iran a score of 0.587, ranking it 139 out of 144. Apart from minor adjustments, the Gender Gap Index remained constant in the entire presidency of Rouhani. UNDP's 2014 Gender Inequality Index assigned Iran 0.515 points. In 2013, only 18.4% of Iranian women participated in the labor market (World Bank 2014 data). Despite this low rate 50% of Iran's labor forces are women.

The Global Competitiveness Index (2016-17) noted the absence of labor market efficiency (rank 134 out of 138) and of the development of the financial market (rank 131 out of 138 countries) as the two major problems for economic development. The Gini coefficient in the Iranian calendar year 1393 (21 March 2014-20 March 2015) rated 0.37.

The SCI reported that economic inequality had increased during the three years of Rouhani's presidency. According to SCI, the absolute poverty line in 2016 started at 2,300,000 toman per month (about \$690) for a household with four people, and the relative poverty line was rated with 3,200,000 toman (about \$980). Prominent economist Somayeh Touhidlu concluded on the basis of the SCI report that 40% of Iranians live under the relative poverty line and 33% under the absolute poverty line.

There is a great divide between well-situated provinces and very poor provinces, cities and villages. The main poor locations in the country are located around the border area. A large number of people in the east, west and south border area are excluded from the country's wealth and are deprived of proper education, health services, job opportunities, etc. The presidential office calculates that 38,000 villages are suffering from poverty and lack of resources. Interior Minister Abdullah Rahmani described during a visit to the southeast province Sistan and Baluchestan in summer 2016 living conditions for more than 250,000 people as close as ten minutes from the provincial capital Zahedan as being like "100 years ago."

Economic indicators		2013	2014	2015	2016
GDP	\$ M	511620.9	425326.1	393436.1	-
GDP growth	%	-1.9	4.3	-1.5	-
Inflation (CPI)	%	39.3	17.2	13.7	8.6
Unemployment	%	10.4	10.6	11.1	11.3
Foreign direct investment	% of GDP	0.6	0.5	0.5	-
Export growth	%	0.0	12.0	-	-
Import growth	%	-18.7	-5.7	-	-
Current account balance	\$ M	-	-	-	-

Economic indicators		2013	2014	2015	2016
Public debt	% of GDP	10.7	11.8	42.3	34.5
External debt	\$ M	6993.6	5758.2	6321.6	5378.3
Total debt service	\$ M	438.1	511.8	796.3	2101.1
Net lending/borrowing	% of GDP	-	-	-	-
Tax revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	10.4	10.7	12.7	-
Public education spending	% of GDP	3.2	3.0	2.9	-
Public health spending	% of GDP	2.7	2.8	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	2.3	2.3	2.7	-

Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

Iran's private sector still only represents around 20% of the country's economy. Since a number of influential clerics and their family members, especially the so-called Aghazadeh-ha (sons of the clerics and high-ranking officials), hold monopolies in lucrative areas of the economy (especially the import of certain goods), the private sector is powerless in its competition with the state-owned and semi-state-owned companies that dominate the economy (domestically produced goods are low in quality and can barely compete against foreign products).

Although the bonyads (foundations established after the revolution) are non-state bodies, they entirely operate under the control of the supreme leader. The commercial entities related to the IRGC enjoy many privileges such as tax exemptions, easy access to foreign currencies at favorable exchange rates and lucrative government contracts.

These structures did not change during Rouhani's presidency. According to the 2016-2017 Global Competitiveness Index, Iran is ranked far behind in areas such as the intensity of local competition (rank 138 out of 138 countries), the extent of market dominance (rank 75), the effect of taxation on incentives to invest (rank 78), the total tax rate (rank 94), numbers of procedures to start a business (rank 94), trade tariffs (rank 138) and the prevalence of foreign ownership (rank 137).

Market-based competition

2

'06 '18 10



Reality is worse than indicated by the Global Competitiveness Index. An example of the absolute incompetence of such powerful companies is the powerful Khatam al-Anbiya Construction Headquarters, owned by the IRGC that acquired the planning and building laws of the North Tehran highway. The building process has lasted since the late 1990s and should end not until 2022. Therefore, \$1.5 billion was transferred to Korea's Daewoo Engineering to make them cooperate with the army. The same has happened with the highway project Tehran-Qom-Esfahan.

Iran's economy also suffers strongly from the "underground economy." In August 2016, Seyed Mohsen Tabatabai Marzabadi, secretary of Iran Urban Economics Association announced that Iran's informal sector accounts for 18.9% of the GDP, creating (usually underpaid) jobs for around one-third of Iran's total labor force. This unfair competition reduces the strength of the regular economy further.

While the Iranian Competition Council and Center for National Competition are responsible for anti-monopoly measures and privatization, both depend on the government and are hence hardly effective. In fact, the IRGC monopolizes much of Iran's economy.

However, the 2016-2017 Global Competitive Index ranked Iran 45 out of 138, which is a remarkable improvement to the 2014-2015 edition, where Iran was 83 out of 144. This remarkable improvement must, however, be considered in the context of other economic indicators. Iranian economists and business magazines (like "Donyay-e Eqtesad") testify the very ineffective work of the Competition Council and the failure to enforce respective laws and measures.

As an effect of the sanctions against Iran, the Islamic Republic still is not a member of the World Trade Organization (WTO) although its application was approved in 2005. It is expected that the agreed nuclear agreement of July 2015 will pave the way for Iran's membership. As membership admission criteria, the World Economic Forum uses the average cost tariff (an international trade tariff burden) of a country, which measures customs duty levied on imports. Iran is among the 19 countries with the highest international trade tariffs. Although the Islamic Republic ranked last in the 2016-2017 Global Competitiveness, its MFN-based tariffs on 28% of its imported items increased compared to the value of 26% that was accounted in the last BTI report.

Still, the most lucrative foreign trade deals (oil, gas, automotive, etc.) are under the control of particular institutions and individuals close to the political elite. Private activities are only allowed in the fields that have been abandoned by the elites.

Several embezzlement cases in the recent years show how corrupt the banking system in Iran is. The banks function well only at the micro level (paying bills, paying salaries, keeping customers' savings, etc.) but on the large scale, they are not transparent. One major problem is that the regime, which is also directly engaged in

Anti-monopoly
policy

2

'06 '18 10



Liberalization of
foreign trade

3

'06 '18 10



Banking system

2

the banking business, essentially runs the economy. Lending policies of the state-owned banks are based on patronage, nepotism and corruption. Iran's Minister for Economic Affairs Ali Tayabnia announced in March 2016 that the country's banks were practically bankrupt, adding that although the government itself is the largest debtor, it was powerless against Khamenei and his revolutionary guards to help them.

In 2016, the Governor of Iran's Central Bank, Valiollah Seif, complained that European banks were reluctant to allow Iran gaining access to bonds or to use the SWIFT system. The optional renewal of sanctions in case Iran did not comply with the terms of the nuclear deal has created a climate of insecurity that accordingly is a deterrent for long-term investments, as Behrouz Khosrozadeh and Mandy Lüssenhop argued 2016 in "The Diplomat."

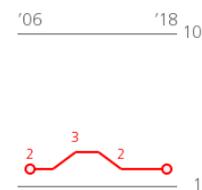
In September 2015, the government declared that it would adhere to guidelines from the inter-governmental FATF to combat money laundering. As this would not be good for the IRGC or other dominant actors, the announcement received intense attacks by the conservative forces –and for good reason, as the Basel Institute on Governance counted Iran as the world's top money laundering risk in 2016 as well as in 2015.

8 | Currency and Price Stability

Iran's central bank enjoys less control under the Rouhani government compared to Ahmadinejad's era. However, the central bank's dependence on Iran's Ministry of the Economy's remains significant. Corruption by private and state-owned banks shows that the situation has not improved significantly and prove the central bank's lack of control.

The Inflation rate of 45.1% in 2012 decreased to 12.6% in January 2015. In 2014 the rate accounted 17.2%. This is the greatest economic success of the Rouhani government. However, prices for basic food and essential goods like white rice, milk, eggs, potatoes, oilseed, cooking oil, meat, beef or bread dramatically increased at the end of 2016.

In parallel, the Iranian currency alarmingly depreciated to the dollar with a historical low exchange rate of \$1 to 4,100 toman, presumably because of the election of Donald Trump as U.S. president and some domestic factors. In December 2016, the government decided to change Iran's currency from rial to toman with a rate of 10 rials to 1 toman. However, the necessary confirmation of the Guardian Council has still not been given.



Contrary to the fact that crude oil prices remain low, the economic trend regarding foreign debts develops positively. The Iranian Central Bank (CBI) estimated the country's external debt at \$5,622 billion in the beginning of 2016, which is a decrease of \$7,682 billion as of early 2014. The needed foreign technical knowledge and investments for the Iranian energy sector as a result of the lifting of the economic sanctions after the nuclear deal are still absent. European and Asian companies fear the sanctions of the U.S. Treasury. At the beginning of 2017, only contracts for the purchase of Boeing and Airbus passenger aircrafts were concluded. In January 2017, the first new Airbus for Iran Air landed at the international airport of Tehran, marking the resumption of cooperation with the European aircraft manufacturer after 38 years.

Despite initial initiatives after the settlement of the nuclear agreement, results so far have remained lean. With President Trump, inclusion into the global economy will certainly not become easier.

In January 2017, Iran's central bank declared total government debt to banks amounted 1,432 trillion rials (\$44.2 billion), which marked a new negative record.

9 | Private Property

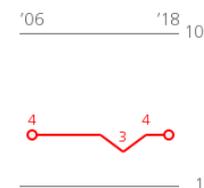
Article 46 of the Iranian Constitution guarantees the protection of property rights. Yet, the freedom to sell sizeable properties or land parcels is constrained by the patronage system. Creating private businesses such as mid-sized industrial facilities requires subsidies that are difficult to obtain. Connections and corruption (provisions, bribes) are usually the most important criteria for obtaining financial support. Basic transactions such as buying and selling real estate usually are unproblematic. The Global Competitiveness Index ranks Iran 104 out of 138 in terms of property rights, compared to rank 86 out of 144 in 2014.

The post-1979 constitution sets an economic organizational foundation of three sectors: state, cooperative and private. The private sector represents just one-fifth of the Iranian economy. Nearly 80% of fiscal expenditures are absorbed by state-owned enterprises. The extensive monopolies held by state enterprises and influential figures prevent private companies from acting and developing freely. Ongoing privatization processes suffer from corruption since many state companies are sold below their market price to their managers or individuals close to the ruling elite.

Private enterprises in Iran have claimed bad conditions in conducting their business with foreign companies, assuming to be powerless to directly participate in the market since foreign businessmen as intermediaries handle their businesses. For instance, private Iranian enterprises are not allowed to transfer payments across borders and face obstacles in completing business transactions, because they have no access to

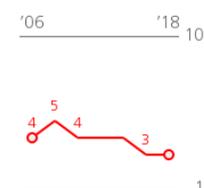
Macrostability

4



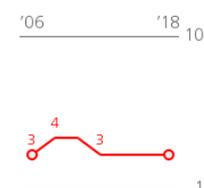
Property rights

3



Private enterprise

3



the SWIFT system. They have no access to the American banking system and cannot handle their business with dollars.

The Rouhani government made no perceptible economic progress. The lack of a competitive environment, the absence of legal and political stability, the prohibition of civil society institutions, distorted market structures and the lack of transparency are the main obstacles in the process of privatization. According to Jaafar Sobhani, director of the Iranian Privatization Organization (IPO), the privatization law, which was implemented in 2006, will terminate at the end of March 2017 if not extended by parliament.

10 | Welfare Regime

Iran's social security system suffers from massive inefficiency. Relevant institutions fail to meet citizens' demands, who often still depend on internal family assistance. The growing population, including refugees, increases the inadequacy of public services. The Global Health Observatory (WHO data 2015) noted the total life expectancy in Iran is 75.5 years (male 74.5 years, female 76.6 years).

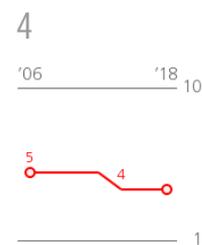
Major actors are the Social Security Organization (SSO), the Civil Servant Retirement Organization (CSRO), the Armed Forces Pension Fund (AFPF), the Organization for Treatment Insurance Services (OTIS), the Imam Khomeini Relief Foundation (IKRF) and micro-insurance funds. The IKRF covers up to six million people apart from state social welfare provision, including four million women who receive continual assistance in health care and life planning.

Corruption is widespread within the social security organizations, especially the state-owned ones. Mohammad Reza Nematzadeh, Minister of Industry and Trade, stressed in July 2016 that Iran's entrepreneurs avoid paying their tax debts to the SSO whereas companies have to pay 30% of their revenues to the SSO. A systemic change is needed for the pensions and health services which are very expensive.

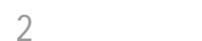
Some ease has been reached for patients who only need to pay 10% of treatment costs since 2015, compared to 40% before. However, many patients complain about the unjust medical therapy system. Cases of patients with severe diseases whose treatments had only been admitted after paying high treatment costs became public during the last two years.

The discrimination of women, ethnic and religious minorities and dissidents that markedly increased under Ahmadinejad continues under President Rouhani. This is because the government not only struggled against conservative forces around Khamenei, but also was powerless against the Basij militia and the arbitrary detention through Iran's numerous security agencies, secret services, judiciary and

Social safety nets



Equal opportunity



revolutionary guards, as Behrouz Khosrozadeh and Mandy Lüssenhop showed in “The Diplomat” in 2016.

In particular, Bahai and Sunnis face enormous restrictions in the education sector and the labor market, and particularly in public service positions. Access to higher education is barred to the Bahai and very limited for Sunnis. Sunnis still do not have a mosque in Tehran even though they represent an estimated 10% of the capital’s inhabitants. The Bahai suffer from systematic prosecution, while attacks and murder against them often remain without legal consequences.

President Rouhani appointed a number of women to top and medium public positions, such as Masoumeh Ebtekar, Shahindocht Molaverdi and Elham Amin Zadeh as vice presidents. However, there are no female ministers in Rouhani’s cabinet, and women are still banned from the positions of judge, president, supreme leader, and cannot be members of the Guardian Council and other powerful institutions. With a score of 0.587, the 2016 Global Gender Gap Index ranks Iran 139 out of 144. Even with nearly equal enrollment rates across the three educational levels, only 83.2% of female Iranians can sufficiently read and write (compared to 91.1% male literates, World Bank 2016 data). 18.3% of women were working in 2014, which is one of the lowest numbers globally. Iran is one of seven U.N. member states that have not ratified the Convention on the Elimination of All Forms of Discrimination against Women (CEDAW).

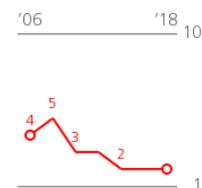
In September 2016, Iran’s Supreme Leader Ayatollah Ali Khamenei implemented a fatwa that prohibits women from riding bikes in public or in the presence of strangers.

11 | Economic Performance

Iran is the second largest economy in the Middle East and North Africa (MENA) region after Saudi Arabia with a GDP of \$425.3 billion (2014) and a GDP per capita of \$17,366 (which is significantly lower than the GDP of the oil-rich Gulf monarchies). Rouhani inherited a negative economic growth rate at market prices of -5.8% at the end of 2012. The growth rate is expected to rise up to over 4% in 2016-2017. When Rouhani was elected in 2013 inflation rate accounted for 45%; in 2015, the rate rapidly fell to 11.9% and rose to 12.6% per annum in January 2016.

According to WTO sources, Iran’s trade balance amounted to approximately \$20.5 billion in 2015, after \$37.8 billion in 2014. With an amount of \$916 million, Iran’s non-oil balance of trade became well on track in the same year – though smuggling remains an unsolved problem with estimated losses for Iran’s economy of up to \$25 billion per year.

In 2016, Iran’s labor force comprised 24 million people, increasing by approximately 840,000 annually. Unemployment, though slightly in decline, remained stubbornly



high with 11.7% in summer 2016, with men (10.4%) less affected than women (21.8%) and rural areas (7.9%) better off than urban zones (14.4%). Most affected are 20 to 24 year-olds, among which 31.9% are jobless.

The Rouhani administration submitted the planned state budget for the Iranian calendar year 1396 (20 March 2016-19 March 2017) to about \$100 billion, which is an increase of 9% from the budget plan for 1395, despite already calculated falling oil prices. Budget dependence on oil income accounted 33.2% in 1395 and is set for 35.8% in 1396.

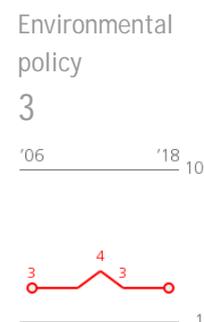
The Sixth Five-Year Plan Development, an act of Parliament in January 2017, estimates that Iran will need \$325 billion over the next five years as foreign investment, which looks ambitious considering that revenues of foreign investments since 2000 have amounted to only \$4 billion. Barriers to foreign investment in Iran have been inefficient bureaucracy, corruption and unilateral American sanctions.

The nuclear deal brought Iran back to the world oil market as one of the main suppliers. Iran's oil production rose from 2,778 barrels per day to 3,720 barrels per day at the end of December 2016, according to the Organization of the Petroleum Exporting Countries (OPEC). From July to August 2016, Iran's crude oil exports increased around 15% up to 2.11 million barrels per day. Oil and gas revenues account 60% of the entire Iranian budget and 85% of the country's overall export revenue.

12 | Sustainability

Alarming air pollution levels are almost normal in ten major cities like Tehran, Ahvaz or Khorramabad which took the third place in the WHO's air quality database of May 2016. Schools and kindergarten in Tehran and some other cities were shut down in November 2016 because of alarming air pollution levels. Habib Kashani, member of Tehran's city council, declared the use of low-quality fuel that leads to industrial pollution as the main reason for the deaths caused by pollution. Outdated cars still used in Iran are also problematic: 400,000 (out of 5 million) cars, 1.5 million motor vehicles and thousands of minibuses and buses are aged above 30 years. According to Elahe Rastgoo, former parliament member and current member of Tehran's city council, air pollution was the third leading cause of death in Tehran after cancer and chronic respiratory diseases. More than 21,000 Iranians died in 2013 from air pollution. According to the World Bank, 2.5% of the Iranian gross national income (\$30.5 billion) was lost due to air pollution.

Masoumeh Ebtekar, vice president and head of the Environment Protection Organization, declared in 2015 that the Iranian environment system faces a serious crisis especially in terms of water. Experts like Kaveh Madani warn of "drying lakes and rivers, declining groundwater resources, land subsidence, water contamination,



water supply rationing and disruptions, forced migration, agricultural losses, salt and sand storms, and ecosystem damages,” as published in The Tehran Times. Unsustainable policies regarding water resources in agriculture and the unprofessional construction of many dams are reasons for the water crisis. One of the rare achievements of Rouhani’s government so far has been a decree to stop the ongoing aridification of the Urmia salt lake in northern Iran.

Article 30 of the Iranian constitution calls upon the government to provide free education up to secondary school to every citizen and expand free higher education to the extent required for the country to attain self-sufficiency. According to the former Education Minister Ali Asghar Fani (resigned in October 2016), about 13.5 million children were registered in the scholastic year 2016. The overall literacy rate in 2016 amounted to 87.2% (World Bank 2016), compared to 84% in 2010. 89.3% of men and 80.7% of women are literate, though statistics in Iran should generally be treated with caution.

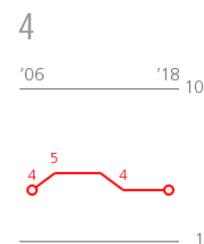
The World Economic Forum’s 2016-2017 Global Competitive Report ranks Iran 79 out of 138 in the overall quality of its education system and at 113 regarding internet access in schools.

In 2016, the total number of students amounted 4.3 million, with 46.1% being female students. Roughly 54.1% were registered in state universities and 45.9% in private universities.

The budget for the Education Ministry in the past six years decreased continuously and amounted to less than 10% in 2013 and 2014 of the entire state budget. Rouhani provided 11.5% of the state’s budget for education affairs in his draft budget for the coming Iranian calendar year 1396 (approx. 2016 AD)

No less than 2,640 universities exist in Iran, but the quality of research and teaching suffers seriously. In particular, the “free Islamic universities” have a bad teaching reputation. Besides a lack of competence, the main contributor is the underlying tendency of Iran’s political officials to act out of ideological motives rather than rationality and technical expertise. With a 43% unemployment rate, university graduates are the hardest hit by the difficulties of finding a job.

Education policy /
R&D



1

Governance

I. Level of Difficulty

Iran has the fourth largest share of proven global oil reserves with 11%, and has the second largest natural gas reserves, following Russia. This makes Iran without a doubt an energy superpower, enriched by a potentially high human capital. However, Iran does not use its potential because of rigorous religious dogmas which prevent the implementation of professional plans. More than once, the pragmatic reformist government of Rouhani has faced obstacles created by Khamenei's entourage and the IRGC. The entire ideological-religious foundation of the Islamic Republic is Iran's major constraints.

The sanctions imposed since 1979 brought heavy losses to the economy, and Iran failed to invest in its gas and oil sector. According to the Ministry of Petroleum, Iran's oil industry alone would need \$180 billion of foreign capital over the coming decade.

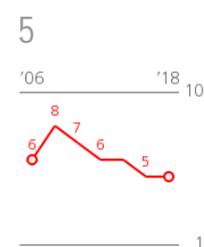
Iran's crisis has a structural character and is intensified by external troubles. The relationship to its Arab neighbors, especially to the great rival Saudi Arabia, worsened. Since Iran intensified its intervention in the Syrian war, the country's popularity in the Arab world greatly decreased.

Population growth decelerated to 1.29%, which leads experts to warn of an ageing population that comes along with the increased poverty of Iran's society. Lack of investment in rural areas, primarily at the eastern, western and southern borders, have pushed many people in these areas into poverty and deprived them of basic infrastructure.

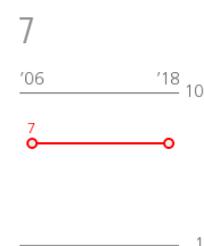
Civil society, massively suppressed in the era of Mahmoud Ahmadinejad, put high hopes in the election of President Rouhani on 14 June 2013. Yet, besides some direct and indirect criticism of existing inconsistencies, Rouhani did not trigger any improvements. Many human rights activists remained under arrest.

NGOs that flourished under reformist President Mohammad Khatami were shut down under Ahmadinejad. Many activists left Iran due to pressure and prosecution. While President Rouhani called on all exiled Iranians to come back and help their country, Nazak Afshar, Mostafa Azizi, Saraj Al-Din Mirdamadi, Hossein Nuraninejad, Sajedeh Arabsorkhi, Abdul-Hossein Harati, Bahman Dar-Alfashaie, Masumeh

Structural
constraints



Civil society
traditions



Gholi-Zadeh and Kazem Barjasteh are among those who were arrested between 2014 and 2016. Therefore, the fear of imprisonment that is connected with brutal torture prevents exile Iranians from returning to their country. Since many activists among them worked for Iranian NGO's, lots of those organizations lost capable leading cadres.

The Iranian Intelligence Ministry and the IRGC are also sensitive about people with dual citizenship. In August 2016, Intelligence Minister Mahmud Alawi announced that more than \$1 billion has been collected for the release of imprisoned Iranian-Americans. Before him, no minister ever acknowledged intercountry hostage taking and blackmail to the press before. Homa Hoodfar, a Canadian-Iranian professor who visited Iran in summer 2016 was arrested and spent 112 days in the infamous Evin Prison in Tehran before her release due to diplomatic pressure from the Canadian government. Many others are still arrested.

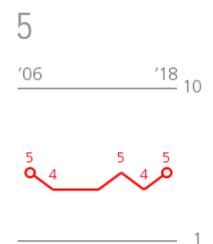
There are many civic associations and civil society unions, but they face problems like the absence of cohesion and connection among themselves. Interest groups like the Association of Teachers, the Bus Drivers' Union and Mine Workers were brutally beaten during their protests for better wages, working conditions or against poverty. The regime is trying to replace civil society with its own Islamic clubs, unions and assemblies.

In a region ravaged by ethnic and religious conflict, Iran's regime also discriminates against religious and ethnic minorities such as Sunnis, Kurds, Bahai and Baluchis. They are hindered in their religious life and excluded from positions in public services. Separatist efforts grew since the Kurds began an armed conflict along the Kurdish-Iraqi and Kurdish-Iranian border in 2016. Even citizen animosity towards religious or ethnic majorities grows since they face the establishment's harassment and accusations of impinging on Islamic values and norms.

The Party for Free Life in Kurdistan (PJAK), founded in 2003 and seeking autonomy for the Kurds in Iran, attacked border posts and engaged in military battles with the IRGC. Some officials in Iran condemn the Kurdistan Regional Government (KRG) in Iraq to protect PJAK and the Kurdistan Democratic Party of Iran (KDPI), which restarted its armed conflict in the second half of 2016.

Despite the state's so-called undeclared war against its own citizens and clashes along the border, the atmosphere in the capital and other Iranian cities remains peaceful. This comes amid growing numbers of people living in poor economic conditions, bearing the risk of increasing social cleavages.

Conflict intensity



II. Governance Performance

14 | Steering Capability

Increasing economic growth, declining inflation and unemployment rates and a gradual reduction of the dependence on oil revenues are the main strategic aims of Iran's so-called Vision 2025, drafted in 1999, assessed by the Expediency Discernment Council in 2002 and submitted to the government in 2003. Besides an improved inflation rate, the goals have not been achieved yet despite the lifting of the nuclear sanctions. During the Iranian calendar year 1394 (March 2015-March 2016), the state's budget dependence rate on oil income accounted 33.2% while the expected rate for 1396 (March 2017-March 2018) increases up to 35.8%. However, President Rouhani was able to achieve short-term goals by lifting nuclear sanctions as well as foreign policy relaxation.

None of Iran's five-year plans since 1989 have ever reached their goals. The sixth five-year development plan encompasses the year from March 2017 to March 2022, but a successful outcome cannot be expected. Lack of expertise and efficiency within the public administration are major hurdles, as well as the strong interference of security and secret services. Any profound progress, for instance the development of an effective market economy, collides with these barriers.

Against the strong conservative-Islamic opposition around the supreme leader Ayatollah Khamenei, Rouhani succeeded so far only in reaching the nuclear agreement (Joint Comprehensive Plan of Action, JCPOA), but not in domestic policies.

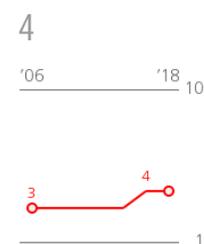
The JCPOA stopped the prospect of war. Iran's external relations with the West and some other regions of the world (except the Middle East) improved, the inflation sank drastically and global business developed new interest in Iran. This is undoubtedly the achievement of President Rouhani.

However, poverty reached new heights as well, civil liberties remained compromised and corruption continued. Rouhani did not only fail to woo foreign investments, he could not even remove the obstacles for foreign investments, as the influence of IRGC has by no means diminished.

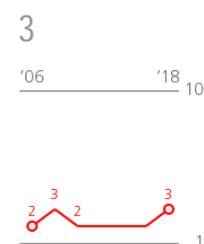
The political elite established in 1979 in both camps, reformist and conservative, consists of 300 to 400 ministers, vice ministers and exalted officials who have generally taken political action since their young days. Depending who forms the government, they change positions and offices. With an average age of 60, Rouhani's cabinet is the oldest after the Iranian revolution. Considering the current

Question
Score

Prioritization



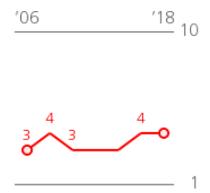
Implementation



Policy learning

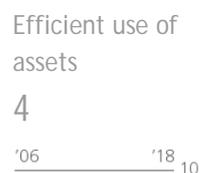
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government's missing success in achieving its promises and goals, no process of learning from previous mistakes and experiences is noticeable. While one can conceptualize Rouhani's general attitude towards politics as a learning outcome from the Ahmadinejad era with its much more confrontational style in foreign policy, for instance, the decisive clerical circles and security services apparently did not undergo this learning progress, as their almost identical aggressive tone and extended military actions abroad illustrate.



15 | Resource Efficiency

While Ahmadinejad's government enjoyed access to the considerably greatest oil revenues since the Islamic revolution in 1979, Rouhani was faced with sanctions that rapidly decreased oil exports during his first two years in office (2013-2015). During the period under review those low crude oil prices hindered urgently needed salary increases in the lower and middle levels of the public administration and the realization of the government's constructions projects, where only half the budget could be provided during the Iranian calendar year 1394 March 2015 – March 2016). As a result, high-qualified and talented Iranians left the country for higher study and work possibilities as well as better living standards. Iran remains one of the top brain drain states in the world. In the academic year 2015-2016, 12,256 Iranians studied at American universities, the highest number ever.



Although Rouhani campaigned against rampant corruption during the elections, Iran's judiciary does not show interest in taking decisive action since corruption affects the institution itself. Even Sadeq Amoli Larijani, head of the judiciary and directly appointed by Khamenei in 2009, has been under suspicion of corruption.

After the conservative-dominated parliament restrained Rouhani's government until early 2016, the new reformist parliament is more supportive; however, the judiciary, the conservative Islamists and the IRGC remain severe opponents.



Foreign Minister Mohammad Javad Zarif lacks control over military plans and operations of the al-Quds Forces under the command of General Qassem Suleimani, an IRGC division that is responsible for operations outside Iran. The expanding interference of the al-Quds Forces in several Middle Eastern countries, especially Syria, clashes with the regional détente promised by Rouhani at the beginning of his presidency. Ali Jannati, Minister of Culture and Islamic Guidance, until his resignation on 19 October 2016, had no access to local authorities and forces who prefer to refer to the so-called Friday Imams (mostly provincial representatives of Ayatollah Khamenei).

Therefore, while discrepancies within the government are less severe under Rouhani than under Ahmadinejad, the interferences of powerful bodies and lobbies close to Khamenei and IRGC, as well as the permanent intervention of Friday preachers and

representatives of Khamenei in the provinces, constitute a major obstacle to the government's effectiveness.

The lack of effective independent supervisory bodies, an autonomous judiciary or powerful watchdog media extended corruption against which Rouhani's government is powerless especially since members of the reformist and pragmatic camps have been involved in corruption scandals. Scandals make it to the public usually if exploited by the political opponents but do not necessarily have legal consequences. The vast corruption scandal about real estate that hit Tehran's city council and mayor Mohammed Bagheri Ghalibaf in August 2016 is a good example, as no investigation was undertaken.

Nepotism continued with Rouhani. Ismail Samavi, Rouhani's nephew, was appointed as an advisor to the presidential office. Another nephew, Ali Asghar Monesan, was appointed as Managing Director of Island Kish Free Zone, a lucrative trading and tourism center. Hossein Fereydoun, the brother of the president, was appointed special assistant of the president and played an important role in the nuclear negotiations. Furthermore, Abdul Hussein Fereydoun, a cousin of the president, was appointed as department head in the Ministry of Culture and Higher Education. The appointment of Ali Asghar Paywandi, another cousin of the president as rector of the important Shahid Beheshti University was also disputable. Ministers have also implemented their own nepotism in their ministries.

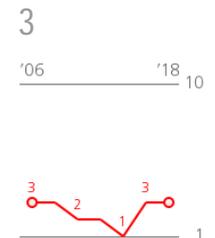
Legal action against corruption is taken only sporadically and mostly if politically appropriate.

16 | Consensus-Building

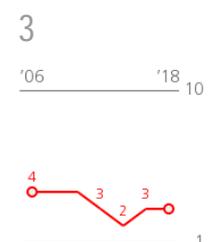
Iran's reformists around Hassan Rouhani (and before under former President Khatami) follow strategic long-term goals of a gradual progress towards democratization and a free market economy. During his election campaign, Rouhani called for referenda on key economic, social and political issues that are considered to be his medium- and long-term policy aims. However, just a few of Iran's central institutions favor the concept of liberal democracy based on the rule of law. Despite office changes after elections, related decisions need to fit the interests of the omnipotent clergy led by Ayatollah Khamenei. Therefore, the term "reformist" must be considered in the context of the Islamic Republic. To Iranian reformists, reforms equates to a loosening and liberalization of domestic policies, a freer civil society, freedom of the press and freedom of opinion. Iran's reformers do not think in terms of general democratic values and norms. With Rafsanjani's death in January 2017, the reformers lost their most important supporter.

Similarly, certain reformers believe in the principles of the market economy but cannot enact necessary reforms because of the dogmatic veto powers in the clergy

Anti-corruption policy



Consensus on goals



and security services, as well as kleptocratic networks in both camps, reformists and conservatives alike.

The Iranian anti-democratic actors form a minority in the state but their money, weapons and support from Ayatollah Khamenei makes them powerful. Conservative Islamists, hardliners, the IRGC, the Basij militia, the supreme leader's representatives and followers, including the Friday Imams and most of the clerics and religious institutions and foundations, promote Islamic attitudes and impede reform policies.

Although some of its members are suspected of corruption, Iran's city councils whose members are directly elected by the citizen rate as liberal and reformist.

Reformers have the relative majority in parliament but do not dare to push back the anti-democratic forces. They want to remain part of the power structure, so they would not risk a serious clash with the anti-democratic forces, which are close to the establishment. Therefore, it would be naive to assume that a clear and fundamental separation existed between the so-called reformers and the conservative Islamists in the context of the Islamic Republic of Iran.

The head of state, Supreme Leader Ayatollah Ali Khamenei polarizes state and society and maintains cleavages. The regime ("Nezam", "system") long opposed the interests of its citizens. The great differences between Nezam and the Iranian population manifest in numerous complaints and jokes about responsible persons and officials in social media. The regime is considered incompetent to lead and manage the state. The government was unable to reduce the gap between the rich and the poor. The luxurious lifestyle of the Aghazadeh-ha (exalted clerics and officials) and their families cause resentment among the population.

Iran's regime intentionally discriminates against religious and ethnic minorities such as Sunnis, Kurds, the Bahai and Baluchis whose freedom of religion is restricted and who are excluded from positions in public services. Internationally, the regime stirs enmity for instance in football stadiums during matches of the Asian Champions League, when they provoke anti-Arab feelings against clubs from Arab countries playing in Iran. Flags are burnt especially against Saudi Arabia, Iran's "deadly enemy." The regime propagates the term "Iran Harasi" (Iranophobia), accusing Arabs of making bad propaganda against Iran and poisoning Iran's image in the international scene. Similar, if not worse accusations are expressed against Israel.

A nostalgic symbol for many Iranians was the oldest, and at the time of its construction in the early 1960s tallest, 17-storey high-rise building called "Plasco" that collapsed in January 2017 in the center of Iran's capital Tehran by fire. The constructor Habib Elghanian, a businessman and chairman of Iran's Jewish community, was executed a few months after the revolution succeeded in February 1979.

Anti-democratic actors



Cleavage / conflict management



While Rouhani earned many credentials abroad after the achievement of the nuclear deal agreement, the need for internal reforms in the sense of a liberalization and relaxation of social policies and civil society involvement remains. An actual implementation of this goal is unlikely since Ayatollah Khamenei and his followers are extremely against it and Rouhani himself seems to be indecisive about achieving this goal.

One of the government's key actors in suppressing civil society is the Ministry of Information (MoI). In 2009, then-opposition leader Mehdi Karroubi had published a comprehensive report on the atrocities of the MoI against imprisoned protesters from the Green Movement. These dreadful atrocities included brutal torture methods, including rape of men and women.

Under Rouhani, the MoI is still strongly involved in the suppression of civil society. At the end of January 2017, 26-year-old Mahdis Mir-Ghavami committed suicide after a brief prison sentence under the MoI in the city of Kermanshah. A month earlier, 22-year-old Shalir Farhadi had also killed herself after a short prison stay.

The oppressed civil society does not play a role in policymaking and consensus building in the state. In May 2016, Narges Mohammadi, vice president of the Defenders of Human Rights Center, wrote an open letter to Hassan Rouhani in which he criticized the enormous pressure on civil society and its activists. The reports of U.N. Special Representative Ahmad Shaheed and prominent Iranian human rights activists such as Shirin Ebadi (2003 Nobel Peace Prize awardee) prove that the situation of human rights and civil society under Rouhani has not significantly improved. The old ruling elite guides the country and they do not consult free and independent civil society associations.

Due to her membership at the Iranian Center for the Protection of Human Rights, lawyer Nasrin Sotudeh was sentenced to six years imprisonment, plus eleven years imprisonment on charge for activities against national security in 2010, as well as given a three-year proscription to engage in her profession in October 2016. After having served his initial five years imprisonment, Mohammad Ali Taheri, a scholar on Erfan Keyhani (Halgheh) who was an alternative doctor and spiritual leader of Mysticism (spiritual truth), received the death penalty in August 2015. After engaging in a hunger strike in September 2016, it is unclear whether he is still alive since no contact with his family and legal supporters has been permitted.

The Islamic Republic has behaved unjustly and inadequately towards its own citizens during its 38 years of existence. Within a few days, thousands of political prisoners were executed in the 1980s. Also in 2015, Iran executed about 1,000 people, and at least 230 up to October 2016. Iran ranks first worldwide in executions per capita statistics, followed by China.

Civil society participation

2

Year	Score
'06	2
'18	1

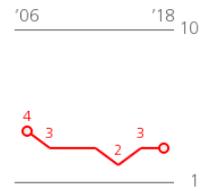
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Year	Score
'06	3
'18	1

Reconciliation

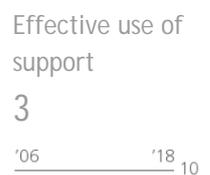
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In January 2017, 43 leading reformists who formerly held high offices took Rafsanjani's death as an occasion to call for a so-called National Reconciliation. Former ministers and parliament members who were imprisoned for several years after 2009 as well as former President Mohammed Khatami were among them. However, there are no signs that the political elite, especially the supreme leader, is seeking any kind of reconciliation with the victims. Arrested opposition leaders Mir-Hossein Mousavi and Mehdi Karroubi are still under house arrest.



17 | International Cooperation

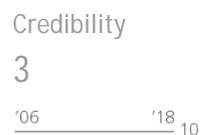
The JCPOA aroused the hope for an international political and economic opening of Iran. President Rouhani's efforts are likely to reintegrate the Islamic Republic into the international community. Several leading European politicians and economic leaders such as the Austrian president, the German vice chancellor, the Italian foreign minister, and the French foreign minister visited Iran. However, tangible results have not materialized.



In October 2016, new cooperation with the Bretton Woods institutions commenced when Iran's economy minister Ali Tayebnia met World Bank Vice President Kyle Peters and IMF President Christine Lagarde. Both institutions were satisfied with Iran's macroeconomic development, and Tayebnia received the promise to launch efforts to remove the obstacles between Iran and international banks and companies. However, the separate sanctions of the U.S. against Iran remain great barriers for Iran's economic trade with the world. Banks and companies fear punishment from the U.S. if they trade with Iran. Bilateral cooperation with many countries is therefore limited. However, if the 2017 presidential elections will bring another victory for Rouhani, this might strengthen him internally against Khamenei to continue his efforts to open up for international cooperation.



For nearly four decades Iran has proven unreliable regarding its secret nuclear activities. Also, the country's support of radical groups such as Hamas and Hezbollah as well as the repressive regime of Syria's Bashar al-Assad have severely harmed Iran's image. Although the aggressive martial government of Ahmadinejad resigned and the nuclear deal helped to increase Iran's position and credibility in the international system, the Islamic Republic is still actively interfering in conflicts of the Middle East, especially in Syria, still faces American sanctions regarding its humanitarian situation and also closely cooperates with Russia's President Putin. In January 2016, the Saudi Arabian embassy in Tehran was attacked, which harmed Iran's image and credibility in the Middle East especially among Arabs.

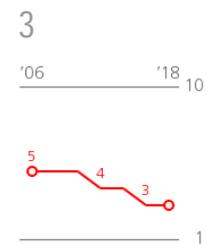


Rouhani's government is much more comfortable for international partners, especially the West, than Ahmadinejad's government. However, just one year after the nuclear deal German Minister of Interior Thomas de Maizière doubted that Iran fully adheres to its obligations, and referred to many reported illegal proliferation

activities. There were about 90 illegal attempts in Germany's largest federal state North Rhine-Westphalia to gain access to technology that would be used for nuclear weapons and launchers, as written by Behrouz Khosrozadeh and Mandy Lüssenhop in 2016 in "The Diplomat."

As a result of the nuclear agreement, Iran behaved conciliatory towards international actors. In the region of the Middle East though, Iran intensified its interventions particularly in Syria and Iraq between February 2015 and January 2017. Especially in the civil war in Syria, Bashar al-Assad would have collapsed by now without Iranian, Russian and Hezbollah support. Some Afghan authorities complain about possible cooperation between Iran and the Taliban. General presumptions that Iran used the financial means that have been released after the lifting of the nuclear sanctions to support Hezbollah and the country's allies in Syria instead of its own citizen's welfare have proven correct. The nuclear agreement de facto proved to preserve Iran's regional interventions. In order not to jeopardize the JCPOA, Obama tolerated Iran's regional behavior that the agreement was unrelated to. In April 2016 though, the Organization of Islamic Cooperation rebuked Iran and Hezbollah for their interventions in Syria, Iraq, Yemen and some other states in the region. Since Rouhani's presidency, Iran's position among the Arab states became more isolated. A crush during the annual hajj pilgrimage in Mina (next to Mecca, Saudi Arabia) that killed 717 people, among them 400 Iranians and injured 850 people on 24 September 2015, caused a dispute and mutual recriminations between Saudi Arabia and Iran. Peak of tensions was the attack against the Saudi embassy in Tehran, which was set on fire by fanatics in January 2016.

Regional
cooperation



Strategic Outlook

The JCPOA marked the most important key development in the entire period between February 2015 and January 2017. President Rouhani was able to achieve key short-term goals such as the lifting of the nuclear sanctions while there are no perceivable advancements towards democracy and free market economy as strategic long-term goals. Besides internal conflicts, both Ayatollah Khamenei and the reformists share their loyalty to maintaining the regimes, which is of greater interest than citizen welfare. The policy of Taqiyya (deception, cheating) is an integral part of the Islamic Republic of Iran since Ayatollah Khomeini's inauguration. Beyond the conservative-Islamic or reformist fractions there is no liberal, socioeconomic or communist third option in the elections that is not devoted to Khamenei. Tensions between reformers and hardliners persist for over twenty years. Although the nuclear deal neutralized the threat of imminent war and opened up new prospects for Iran, the thesis favored by Western journalists and researchers whereby Iran will be transformed into a regional stabilizer to Saudi Arabia's detriment did not come to be. The JCPOA has no positive impact on Iran's regional behavior. Iran and Hezbollah are among the major obstacles in the peace process between Palestinians and Israelis.

While relations with exalted officials in the West perceptibly improved, the provocative ballistic missile test conducted shortly after the lifting of sanctions as well as ongoing martial statements of exalted radicals and military officials prove Iran's unpredictability.

U.S. President Donald Trump's electoral campaign promise to break the nuclear agreement and reinforce pressure on Iran through spontaneous inspections ("anytime, anywhere") raises the regime's fear of losing the nuclear deal's advantages and of a possible revelation of any concealment of nuclear activity. Tougher sanctions would be Iran's Achilles' heel while a military strike would be Iran's sword of Damocles. If Trump canceled the JCPOA, Iran's protective shield for regional adventures would disappear and the power constellations in the region would shift. Presumably, Trump could maintain the JCPOA tied to further conditions. Any provocation in the Persian Gulf such as maneuvers of the Iranian patrol boats around American war ships in international waters could lead to a disaster.

Presidential elections will be held in May 2017. Despite the loss of his mentor Rafsanjani, Rouhani is likely to be re-elected. Although the Islamic revolutionary system suffers from, and provokes continued chaos outside and inside Iran's borders, a radical change of conciliation and conformity in domestic and foreign policies towards democracy and a free market economy without religious-ideological dogmas or the abolition of the revolutionary world view are highly unlikely.