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History of the Rial and Foreign Exchange Policy in Iran

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Abstract

Through the history and since 1933, the Iranian rial has declined from 11.2 rials per dollar to almost 8600 rials per dollar today in the parallel or black market. At the same time the official rate has been kept at artificial level most of the time, not consistent with other macro conditions of the country. Historically, however, the Central bank has adjusted the official rate and brought it in-line with the black market rate. This paper not only reviews the historical developments surrounding Iranian rial, but also provides an event study supporting the literature that any foreign exchange control has only short-run impact on the official exchange rate. In the long-run, the official rate must be adjusted toward the black market rate, as evidenced by the behavior of the Central Bank of Iran

Keywords: foreign exchange Policy, Iran, Rial

I- Introduction

A monetary system involves institutions, instruments, rules and procedures for handling international payments. Historically the world has experienced three distinct international monetary systems. The first was the Gold

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Standard that prevailed during 1879-1914 under which each country had to define the gold content of its currency and stand ready to buy and sell gold at a pre-announced price. This fixed exchange-rate system in which gold backed each currency, was interrupted by the World War 1 (WWI) when most countries failed to exchange their own currency for gold. What prevailed next were the floating rates during 1918-1923. During 1923-1928 countries tried to go back to the Gold Standard by stabilizing their currencies. However, this effort was interrupted by the Great Depression of 1929-1933 during which, in order to stimulate their economies, most industrial countries engaged in competitive devaluation. Thus, 1930-1935 is known as "devaluation Cycle". After this cycle, there was an effort by industrial countries to go back to the Gold Standard but the process was interrupted by the Second World War (WWII). After the WWII, delegates from 44 nations held a conference in Breton Woods, New Hampshire (USA) to discuss a possibility of a new monetary system. Two proposals were on the table. One was the British plan led by John Maynard Keynes who was in favor of creating an International Clearing Union which will have ability to create international money known as Bancor (fixed in terms of gold). Furthermore, Keynes called for interest charge on reserve accumulation by surplus countries and right of a member to devalue or revalue its currency by 5%. The American plan led by Harry Dexter White proposed creation of a "Stabilization Fund" which will begin operation with smaller amount of funds ($5 billion in gold and national currencies contributed by members) and will have no ability to create money at will. Furthermore, exchange rates will be fixed by the fund and they will change with the consent of 80% of voting power. The two proposals led to the creation of the International Monetary Fund (IMF) and the World Bank. The international monetary system that emerged was the Breton Woods system or the adjustable peg system which prevailed from 1946 till March 1973. Under this new system, most countries agreed to fix value of their currency to the US dollar and the US agreed, in turn, to fix the value of the dollar in terms of gold at $35 per ounce. However, in 1973 due to stagflation in the US and unwanted dollars accumulation by the rest of the world, the Nixon administration refused to exchange gold for the dollar and March 1973 marked the end of this era. Since the US refused to exchange gold for the dollar, most countries refused to fix the value of their currencies to the dollar and decided to float. Today, most currencies are floating with some central bank intervention;

hence, they are managed float. Of course, some countries, especially developing, have preferred still to fix their currencies to a single currency or to a basket of currencies.

What has been the performance of our rial in the muddy world of international monetary systems reviewed above? Has our currency received any international recognition in the history? What has been the response and policies of the Central Bank of Iran (CBI)? Finally, are the policies consistent with the predictions of economic theory? This paper tries to answer these questions in Section II with a conclusion in Section III.

II- Historical Developments and Policy Response by the CBI

In trying to learn about the history of any exchange rate and its evolution in any country, the most appropriate historical point to start would be the "Gold Standard". Although the rules of the gold standard varied from one country to another, one major common feature existed in countries those which were said to be on the gold standard. Each nation had to define the gold content of its currency and stand ready to exchange gold for its currency and vice versa at the defined fixed ratio. Since this had to be extended to domestic as well as to foreign individuals, the gold inflow and outflow should be free from any government intervention. Once the gold contents were announced, the relative gold values would establish the exchange rates.

The full fledged gold standard is said to be originated from England where in 1816 the British currency was fixed in terms of gold at 3 pounds, 17 shillings, and 10.5 pence (or 3.995 pound sterling) per ounce of gold. Britain was able to keep this ratio from 1816 till 1914 when the First World War interrupted the gold standard. What made this development in 1816 unique was that for first time in the history of the world, there was a fixed and stable relation between gold and a currency (pound sterling). As soon as this fixed ratio was understood by the world, it was extended to the rest of the world by means of Sterling Bill of Exchange. Such bills which were used to finance the world trade were said to be as good as gold. The implication is that even in countries like Iran where the banking system was not well developed and there was no central bank, merchants traded goods internationally by accepting the Sterling Bill of Exchange which was redeemable to gold by the Bank of England. Any country accepting the Sterling Bill of Exchange as a means of payment was said to be on gold standard or actually on the "sterling standard" and the Britain was said to be the world banker. However, the system was interrupted by WWI in 1914 and thereafter, much of the world trade was financed by the U.S. dollar and the U.S. became the world financier.

Our search of the gold content of the Iranian rial during 1816-1914 was futile.[1] Most likely the rial was non-convertible paper currency. However, it is reported in Pick's Currency Yearbook (1955, page 122) that Iran abolished the gold standard in October 1929 and introduced her first foreign exchange controls on February 25, 1930.[2] Since 1929 is a much later date than 1914, we would expect Iranian rial to be quoted in terms of the United States dollar rather than pound sterling. On May 1933, "The official rate was increased from 11.20 rials to 16.35 rials." Therefore, historically, the first exchange rate that we were able to find is 11.20 rials per dollar which prevailed on May 1933. The rial was devalued on October 1, 1941 from 16.35 to 35.25 rials per dollar and again to 35.50 on January 1, 1942. On May 14, 1942 the official rate was reduced to 32.50. Iran joined the International Monetary Fund on December 18, 1946 when the rial-dollar rates were 32.50 rials per dollar. Due to political turmoil and ousting of Premier Dr. Mossadegh in 1953, a black market was developed and the exchange rate system went through several changes. Finally, in 1955 Iran introduced eight different exchange rates. At March 21, 1955 these rates were as follows:

1. Basic rate of 32.50 rials per dollar serving only the government transaction.
2. Student rate of 41.50 rials per dollar.
3. Purchasing rate of non-commercial foreign exchange receipts set at 75.00 rials per dollar.
4. A rate for medical expenses in foreign countries at 79.50.
5. A rate for buying of export receipts at 75.00 rials per dollar.

1- Our search was restricted to Puxley (1933), Morgan-Webb (1934), Brown and Adams (1940), Kemmerer (1944), and Drummond (1987).

2- Our interpretation of abolishing the gold standard by Iran is that since U.K. had lost its world banker's status, Iranian authorities refused to accept the Sterling Bill of Exchange.

6. A rate for selling for most commercial imports set at 76.50.
7. A fluctuating rate for non-essential and luxury imports set at 85.00.

In 1955 the black market rate for trading of U.S. banknotes in Iran or transfers to the U.S. which was illegal, stood at 81.00 rials per dollar.

Finally on May 18, 1957 the officials in charge of exchange rate arrangements (i.e., the Bank Melli together with the finance minister) decided to abolish the official rate of 32.50 and computed the gold reserves at 75.75 rials per dollar. The dollar buying rate was set at 75.00 and the dollar selling rate at 76.50. They also defined the gold content of rial to be 11.732 milligrams of fine gold. These rates were effective even in 1958, 1959, and 1960. The illegal activities declined and the black market rate in 1960 stood at 75.85 rials per dollar.

In early 1962 Iran banned the import of all new cars for 5 years which again resulted in an increase in the black market activities so that dollar rose to a new high level of 98.00 rials. The rial remained weak till the late fall of 1963, when some favorable changes in economic conditions were noticed. In early 1964 new foreign exchange rules were introduced. The dollar was to be used rather than sterling for computing all foreign exchange rates. By October 1964 the rial had recovered to 78.50, but at the end of 1964 it surged to 82.50 rials per dollar. The rial fluctuated around 80.00 rials around per dollar during 1965 and the first half of 1966, improving to about 77.00 rials per dollar through the remaining of the year and into early 1967.

1967 was characterized by political stability and economic progress. Oil played the dominant role in the nation's development. Due to Arab-Israeli conflict, oil prices soared and Iran's oil revenues reached a record high of $750-$800 million. Oil production increased by 22% and Iran became the sixth largest oil producing country in the world. Because of increasing oil revenues on October 29th, the Central Bank reduced the selling rate from 76.50 to 75.50 rials per dollar.[1]

In early 1968 Iran drew $31.25 million in various currencies from IMF for balance of payments purposes. A new Development Plan for 1968-1973 began in March, calling for investment of 810 billion rials over the five year period. What is

1- In 1967 Iran's gold and foreign exchange rose 21% and currency in circulation increased by 12% which was covered to 80% by official reserves.

important about this year was that authorized banks were permitted to engage in forward foreign exchange dealings with importers and exporters. Buying and selling rates of from 74.75-74.928 to 74.25-74.425 respectively, were set for 1 to 3 months futures. Black market transactions mostly were ceased white on the free market the rial strengthened to 75.50 rials per dollar at the end of March 1968, while fluctuating between 76.10 and 77.37 through first half of 1969. Some weakening followed and by early 1970 the rial was again up at 80.00 rials per dollar. By mid 1971 it had gained somewhat and posted at 78.75. At March 21, 1971 the official buying and selling rates still stood at 76.25 and 76.50 respectively.

Iran's economy continued to boom in 1971. The price of crude oil was raised by 0.35 dollar per barrel in general ($ 0.46 for Iran) with subsequent increase of 0.05 dollar in June 1971, January 1973, 1974, and 1975, plus 2.5% increases at the same time to offset inflation. Iran received $450-$575 million in additional oil revenue. However, due to the devaluation of the dollar in August 1971, Iran lost $40 million in revenue. On January 1972, the Geneva Accord provided a special increase of 8.57% in its oil prices to compensate for the devaluation of the dollar. Iranian revenue per barrel was raised by 64%. At the same time it was announced that Iran would introduce a new basic currency called the Toman, which is divided into 10 rials.[1] Oil was the entire story for the country. While oil played a dominant role, Iran was experiencing a large inflow of foreign capital which was helping Iran to join the ranks of industrial nations as she negotiated for about 28 projects valued at over $2 billion, with the United States, West Germany, Japan, and the United Kingdom. Due to increased oil revenues and capital inflow, the rial remained stronger in the free market at 67.65 rials per dollar in June 30, 1973. The official rates were also changed to reflect the changes in the fundamentals. On June 30, 1973 the basic Iranian rial (now theoretically defined at 10.8055 milligrams of fine gold) quoted at 68.17 per dollar. The buying and selling rates were adjusted to 67.50 and 67.75 rials per dollar respectively.

The Arab-Israel hostilities of October made the price of oil per barrel reach as high as $11.65. Oil provided 80% of the foreign exchange earnings. During the first 10 months of the Persian year 1352 (1973-74), Iran had faced $125

1- Note that although public use Toman (equal to 10 rials) in their daily transactions before and after this date, no Toman currency has actually been introduced as of this writing.

millions balance of payments surplus. On January 14, 1974 a two-tier exchange rate system was established. The first rate was an official commercial rate for imports and specified approved foreign exchange transactions with buying and selling rates fixed at 67.10-67.75 respectively. The second rate was an official free non-commercial rate, applicable to all other transactions with buying and selling rates fixed at 67.60-67.85 respectively. At the same time, Iran eliminated most foreign exchange controls. Exporters would no longer have to surrender their proceeds to the Central Bank. Foreign currency transactions could be freely arranged by all banks and interested parties. All these made the black market to disappear all together making the unofficial black market rate to remain very close to the official rate at 67.95 rials per dollar. On September 18, 1974 faced with abundant supply of oil, foreign exchange and gold, Iran declared full convertibility of the rial under IMF regulations.

However, 1974 was the year that the United States was experiencing stagflation (inflation and recession) and a fluctuating dollar. To iron out the fluctuation of the rial-dollar rate, on February 12, 1975 Iran decided to break the rial-dollar rate and tied the rial to the SDR at an exchange value of 82.2425 rials per SDR. The new rial-SRD rate was adjusted whenever SDR-Dollar rate changed by more than 2.25%, implying that the rial-dollar rate would be adjusted periodically. In effect, Iran was trying to manage the rial-dollar rates by following a certain procedure, rather than by will. On March 31, 1976 while the basic Iranian rial (theoretically defined at 10.8055 milligrams of fine gold), but inoperative stood at 68.1747 rials per dollar, the controlled floating (but effective) rate based on 82.2425 rials per SDR stood at 69.70 (buying) and 69.95 (selling). At the same time the black market rate was 69.60 rials per dollar. What is an SDR?

Due to growing volume of world trade, in 1967 the International Monetary Fund (IMF) decided to give an automatic borrowing power to its members by creating the so called "special drawing rights". The initial distribution was in 1970 when one SDR was defined in terms of gold to be equal to one 1970 dollar.[1] However, following the devaluations of the dollar during 1971-73, one

1- The SDR distribution is proportional to the size of each member's quota.

SDR became $1.20. Rather than tying the SDR to gold or dollar, in mid-1974 IMF decided to adopt a new procedure for evaluating the value of one SDR, a procedure which depends on the weighted average value of 16 currencies and not just the dollar. The relative weight of each currency in one SDR (in July 1974) is presented in Table 1.

Table 1: Weight of Each Currency in One SDR in July 1974

Currency	Weight in Percent
United States Dollar	33
German Mark	12.5
British Pound	9
French Franc	7.5
Japanese Yen	7.5
Canadian dollar	6
Italian Lira	6
Netherlands guilder	4.5
Belgian franc	3.5
Swedish Krona	2.5
Australian dollar	1.5
Spanish peseta	1.5
Norwegian krone	1.5
Denmark	1.5
Austrian schilling	1
South African Rand	1

In April 1978, the IMF took a new decision. Effective July 1, 1978, IMF decided to change the composition of the SDR so that it can better reflect the relative importance of currencies in the world trade.[1] The original basket which

1- At the same time the IMF also established a method for further adjustment at every five year intervals.

went into effect on July 1 1974 (shown above) reflected the relative importance of member countries in the exports of goods and services over the 1968-1972 periods. Due to the increased importance of oil in world trade since 1973, the revised basket of currencies included in SDR was to reflect importance of trade during 1972-1976. As a consequence, the currencies of Iran and Saudi Arabia were included and those of Denmark and South Africa were excluded. The relative weight of each currency and their amount per SDR on July 1, 1978 are presented in Table 2.[1]

Table 2: Composition of SDR Including Iranian Rial.

Currency	Weight in %	Currency Amount
United States Dollar	33	0.40
German Mark	12.5	0.32
British Pound	7.5	21
French Franc	7.5	0.42
Japanese Yen	7.5	0.05
Canadian dollar	5	0.07
Italian Lira	5	0.52
Netherlands Guilder	5	0.14
Belgian Franc	4	1.60
Saudi Arabian Riyal	3	0.13
Swedish Krona	2	0.11
Iranian Rial	2	1.70
Australian dollar	1.5	0.017
Spanish Peseta	1.5	1.50
Norwegian Krone	1.5	0.10
Austrian Schilling	1.5	0.28

Today, the SDR has only limited use as a reserve asset, and its main function is to serve as the unit of account of the IMF and some other international organizations. Holders of SDRs can obtain these currencies in exchange for their SDRs in two ways: first, through the arrangement of voluntary exchanges between members; and second, by the IMF designating

1- Note that the weights come from IMF Survey, April 3, 1978, page 108 and the currency amounts from IMF Survey, July 3, 1978, page 203.

members with strong external positions to purchase SDRs from members with weak external positions. Since introduction of Euro, the composition has changed and it includes only four currencies as shown in Table 3.

Table.3: SDR Valuation on Friday May 7, 2004[1]

Currency	Currency amount under Rule O-1	Exchange rate [1]	U.S. dollar equivalent	Percent change in exchange rate against U.S. dollar from previous calculation
Euro	0.4260	1.20630	0.513884	- 0.659
Japanese yen	21.0000	110.62000	0.189839	- 1.003
Pound sterling	0.0984	1.79550	0.176677	0.112
U.S. dollar	0.5770	1.00000	0.577000	
			1.457400	
	U.S.$1.00 = SDR		0.686153 [2]	0.352 [3]
	SDR1 = US$		1.45740 [4]	

(1) The exchange rate for the Japanese yen is expressed in terms of currency units per U.S. dollar; other rates are expressed as U.S. dollars per currency unit.

(2) IMF Rule O-2(a) defines the value of the U.S. dollar in terms of the SDR as the reciprocal of the sum of the equivalents in U.S. dollars of the amounts of the currencies in the SDR basket, rounded to six significant digits. Each U.S. dollar equivalent is calculated on the basis of the middle rate between the buying and selling exchange rates at noon in the London market. If the exchange rate for any currency cannot be obtained from the London Market, the rate shall be the middle rate between the buying and selling exchange rates at noon in the New York market or, if not available there, the rate shall be determined on the basis of euro reference rates published by the European Central Bank.

(3) Percent change in value of one U.S. dollar in terms of SDRs from previous calculation.

(4) The reciprocal of the value of the U.S dollar in terms of the SDR, rounded to six significant digits.

1-This information comes from the following web site: http://www.imf.org/external/np/tre/sdr/basket.htm

In 1978 socio-political unrest mounted over frustrations which surpassed the expectations of oil boom. Efforts to crack down on corruption and mismanagement failed and many civil and economic disorders and strikes followed. Strikes erupted in the banking system and spread to industry, government and oil sector. Oil production dropped from an average of 6.1 million barrels per day (bpd) to 300,000 at year-end which was not enough at all to support the increased demand for foreign exchange. In October and November foreign exchange controls were tightened. The dollar stood at 84.00 rials at the year end, the lowest value of the rial in its history.

With most ministries on strike, at the start of 1979, the Shah appointed Shahpour Bakhtiar as the head of government. On January 16, 1979 Shah went into exile after 37-year rule and the Ayatollah Ruhollah Khomeini returned from a 15-year exile and established Iran as an Islamic Republic. Capital flight (10 billion dollar by early 1979) forced rial to drop as low as 121 rials per dollar by June 1979 and 165 rials per dollar by the end of year (in the black market). Controlled floating rate (but inoperative) based on 82.2425 rials per SDR was 70.50 (buying) and 70.75 (selling) rials per dollar on June 1979. In November 1979 there was a new political development. 52 Americans were taken hostage.

In mid-April 1980 the United State broke off diplomatic relations, imposed new sanctions on trade and finance and urged the European countries to do the same. Iran abandoned the fixed exchange rate and devalued the rial by 11%, creating a new exchange value of 92.30 rials per SDR. In September 1980 Iraq invaded Iran in an attempt to gain control of the Arvanrd waterway leading to Iran's huge Abadan refinery, the largest in the world. In November all foreign exchange dealers were closed down. War and anarchy brought Iran close to economic collapse in 1980. The oil production dropped by almost 50% to no more than 1 million bpd. Two-thirds of the nation's refinery capacity was said to have been damaged and Iran actually imported diesel and heating oil.

On January 20, 1981, Iranian assets in the amount of $7,955 million were transferred to an escrow account at the bank of London under the control of the Algerian Central Bank, and the U.S. hostages were released. About $3.7 billion was set aside to pay off old loans to international banks. The Central Bank of Iran received immediately some $2.837 billion of the estimated $12 billion in assets frozen more than a year before. Meanwhile, Iraq occupied sections of the oil-rich Khuzistan province and other neighboring provinces. Money printing accelerated to finance the war. Capital continued to fly, pushing the rial down to a new low level of 400 rials per dollar at the end of year.

The year 1982 was not a good year for Iran. Devastated by the war, many cities faced with fuel, heat and food shortages. Arms and spare parts had to be purchased in black market because of the U.S. trade embargo. The dollar reached its highest level at 500 rials. Although, the arm purchases were costly for Iran, she was able to afford, mostly because of gold reserves and investment abroad. Iran was also able to generate additional foreign exchange by selling oil at $30.20 per barrel, les than the official price of OPEC which was $34.20 per barrel. Agriculture was assisted by distributing free fertilizer and tractors to farmers which helped to increase domestic production. Due to such optimism, the dollar started to decline after mid-1982. In September, half of industrial capacity was in use and the government not only was supporting 2 million war refugees, it was sheltering 1.5 million Afghanis. By the end of year supply of essential goods was ample and international trade with Turkey, India, Pakistan, Australia, New Zealand and U.K. was booming. All these developments were followed by easing of foreign exchange controls in January 1983. Resident and non-residents were allowed to bring unlimited amounts of foreign exchange and hold it as cash or in Foreign Currency Accounts in local banks. All these helped the dollar to decline from a high of 500 rials during mid-1982 to 370 rials at the end of 1983.

During 1984 and 1985, Iraqi airplanes made repeated attacks on Kharg Island facilities which reduced production. Increased demand for oil products forced Iran to import oil resulting in current account deficit of $414 million. The overall balance of payments was in red by $4,136 million. Foreign debt of the government at the end of 1984 was said to be $3.4 billion. The rial resumed its downward spiral, reaching a new record low of 622 rials per dollar at the end of 1984 and a new low of 680 rials per dollar at the end of February 1985.

In early 1986, falling oil prices on world markets resulted in an announcement that Iran would cut its oil production by 50%. Although such drastic cut was not materialized, output was reduced to 1.4 million barrels per day (bpd) by year-end. Iraqi air attacks reduced the refinery capacity from 625,000 bpd to 420,000 bpd as all six refineries were bombed. Imports of refined oil were increased to 300,000 bpd. Stagnant income, high inflation accompanied with high rate of unemployment characterized this period, a period of pessimism which was reflected in a new low free market of the rial at 815 rials per dollar at the end of year.

In early 1987 and 1988, import regulations were tightened and only authorized traders were given permission to import goods. The parity ratio of rial and SDR remained at 92.3 rials per SDR, as before. Thus, changes of rial in terms of major currencies followed the fluctuations of SDR against such currencies. In line with economic conditions of the country, 1989 saw some adjustments in foreign exchange and foreign trade policies. Various policies were adopted to promote non-oil exports. Severe fluctuations of the rial-dollar rates in free market placed unfavorable psychological and economical effects on the society. Thus, measures were taken to organize free market and to meet the excess demand for foreign exchange. Banks were authorized to sell foreign exchange to importers at a rate near the free-market rate which stood at around 1200 rials per dollar. Thus, importers enjoyed buying foreign exchange form authorized banks as opposed to taking risk of going through outside the banking system. Furthermore, all Iranian passengers were allowed to carry up to $5000 while leaving the country.

In 1990-91 (1369 Iranian Calendar) a new set of policies were adopted. These policies were designed to achieve an equilibrium rate for foreign exchange that could result in optimal allocation of economic resources as well as coordination of monetary and financial area. A major policy was measures to unify the official rate with the free market rate. To this end, multiple exchange rates were reduced to no more than three rates:

a. ***Official rate*** of 92.3 rials per SDR for the importation of essentials, certain industrial machineries and inputs needed for development projects.
b. ***Competitive rate*** set initially at 800 rials per dollar and then was reduced to 600 per dollar and applied to the imports of raw materials, spare parts and intermediate goods.
c. ***Floating rate***, which was determined on the basis of market forces. Importantly, to promote non-oil exports, this rate was applied to purchase of non-oil export proceeds, helping to reduce black market activities and increase foreign exchange earnings.

By introducing the floating rate, the Central Bank attempted to control the free market, therefore, lead the demand toward the banking system. Following implementation of these policies, the range of fluctuation of the dollar declined from 49% in 1989 to 18.7% in 1990.

Currency unification and its implementation continued in 1991 by deregulating the importation of industrial products. Gradually many of the items that used to be imported at official exchange rate began being imported at competitive rate or floating rate. Most of the restrictions on non-oil exports were lifted and significant steps were taken to liberalize the trade. To this end, the Export Development Bank was established to finance promotion of non-oil exports. In 1992 the list of commodities that were subject to competitive or floating rate was expanded to include short governmental business trips, purchase of air tickets from airlines other than Iran Air, custom duties and fright charges of transit goods. Furthermore, during this year the obligation of incoming passengers to fill declaration forms for carrying foreign exchange in excess of $5000 was abolished. On the other hand, passengers leaving Iran were allowed to carry $10000 in the form of cash.[1] Such policies limited the range of fluctuation of the exchange rate in the free market to little over 8% (see the data in Table 4).

1993-94 was the year during which the policy of foreign exchange allocation and budgeting was eliminated in the budget law. Floating rate was used to finance most imports through the banking system. This paved the way for a successful implementation of the exchange rate unification. However, due to fluctuation in the free market rate, the exchange rate for export proceeds was announced by the Central Bank at 50 rials less than the market rate which was fixed at 2345 rials per dollar. The foreign exchange and trade policy followed three main targets:

a. Creating trade surplus for the repayment of part of foreign debt. This was supposed to be achieved by import controls and non-oil export promotion policies.
b. Expansion of trade with the Central Asian Countries.
c. Controlling fluctuation of the exchange rate in the free market.

1- Similar policies are in effect in America. Passengers can carry cash up to $10000. If the amount is in excess of $10000, they are required to report it.

These policies were continued into 1995 when the central bank was forced to adjust the export rate and fix it at 3000 rials per dollar. Furthermore, foreign exchange transactions were banned and regarded as illegal. The controls were aimed at reducing exchange rate fluctuations in the free market. Obviously due to controls and the Central Banks inability to satisfy the demand for foreign exchange, the rate in the black market began rising and it stood at about 3600 rials per dollar during summer 1995. These policies were continued in 1996-98 and foreign exchange transactions outside the official banking system were announced illegal. In 1998-99 (1377 Persian Calendar), a committee was established to recommend appropriate policies for regulation of the foreign exchange market. This committee included the president, as its chairperson. Additional members were: the Minster of Economic Affairs and Finance, Governor of the Central Bank, Head of Plan and Budget Organization and two ministers selected by the Council of Ministers. The exchange rate system was still based on the dual exchange rate practice, i.e., 3000 rials per dollar as ***export rate*** and free market rate.

In 1999-2000 there was a sharp decline of oil prices which had negative impact on the position of the trade balance and the government's obligation to pay the foreign debt. This paved the way for changing the regulations governing the external sector of the economy by paying more attention to market mechanism. Attention was paid again to controlling foreign exchange fluctuations and strengthening the external position of the country. Since these goals are mostly met through regulations, the rial continued its decline against the dollar and it oscillated around 8000 rials per dollar. However, in the following year (2001), due to boom in the global markets, oil prices rose by 36% and Iran experienced substantial increase in oil revenues and trade surplus which led to the elimination of the export rate restrictions.

Today, most transactions are financed either at free market rate or at negotiated rate and still some regulations and controls are in effect.[1] However,

1- For example, Iranians traveling overseas could only purchase up to $2000 from authorized banks. Or dollars sold by an individual to an authorized bank cannot exceed $5000 (author's experience in August 15, 2004 in Melli Bank). Interestingly enough, the rate outside the banking system was no different than the one by the authorized banks.

through repeated devaluation, the Central Bank has successfully kept the negotiated rate close to free market rate. The free market rate has been stabilized and during last 3-4 years has fluctuated between 8000 and 8800 rials per dollar. On August 15, 2004 the dollar buying rate was 8712 rials and the dollar selling rate was 8724 rials. The selling rate outside the authorized banks was 8775 rials per dollar.[1] In order to learn about the historical movement of the rial over time in the black market (now free market), Table 4 provide the historical data.

Table 4: Monthly Black Market Exchange Rate (number of rials per U.S. Dollar, end of the Month)

Month	1947	1948	1949	1950	1951	1952
January	53.000	61.500	72.000	58.500	52.000	64.000
February	54.000	57.500	78.000	61.000	54.000	67.000
March	56.000	63.750	71.250	58.500	53.250	76.000
April	56.500	65.250	65.000	59.250	54.750	91.000
May	58.500	67.500	58.500	58.250	56.500	80.000
June	54.500	66.750	54.000	59.000	57.500	82.000
July	62.500	67.250	53.000	59.000	58.250	85.000
August	65.000	68.500	52.000	58.500	56.000	78.000
September	75.000	72.500	56.500	52.000	61.000	80.000
October	76.000	66.500	58.500	51.500	62.250	87.000
November	69.000	72.500	59.000	51.000	65.500	83.000
December	68.500	76.000	57.500	54.500	66.500	86.000

Month	1953	1954	1955	1956	1957	1958
January	88.000	92.000	84.000	78.000	81.750	79.500
February	83.000	86.750	78.500	79.000	81.500	79.000
March	86.000	85.000	81.000	80.500	80.750	80.000
April	88.500	90.500	80.500	80.000	80.000	80.250
May	94.000	89.900	80.000	79.000	79.500	80.150
June	125.000	90.000	78.500	80.500	80.250	80.000
July	110.000	90.500	80.250	82.000	80.000	78.000
August	95.000	84.000	80.500	80.000	80.250	77.000
September	94.000	86.000	81.000	81.500	80.500	77.000
October	95.000	85.000	82.000	81.000	80.250	76.750
November	98.000	87.000	79.000	81.250	80.000	76.500
December	96.500	85.000	78.750	80.500	79.750	76.500

1- Again, these rates are author's observation in Tabriz, the second largest city in Iran and province of the East Azerbaijan province.

Table 4: Monthly Black Market Exchange Ratenumber of rials per U.S. Dollar, end of the Month)

Month	1959	1960	1961	1962	1963	1964
January	76.750	76.000	87.000	94.500	93.000	89.000
February	76.750	76.000	88.500	96.000	92.500	86.000
March	76.500	75.850	83.000	98.000	92.000	85.000
April	76.500	75.600	83.500	89.000	91.000	83.500
May	76.250	75.750	83.000	88.000	92.000	82.000
June	76.350	76.000	85.500	89.000	95.000	81.000
July	76.250	77.000	86.250	91.000	93.000	80.000
August	76.250	85.000	87.000	89.000	92.000	79.500
September	76.250	86.500	87.000	89.000	92.500	79.000
October	76.750	85.500	88.750	92.000	90.000	78.500
November	76.500	86.000	89.250	93.000	88.500	80.000
December	76.000	86.500	90.500	91.500	87.000	82.500

Month	1965	1966	1967	1968	1969	1970
January	81.250	80.650	77.000	75.450	77.000	80.000
February	80.750	80.300	76.500	76.000	77.000	79.700
March	81.000	80.000	77.000	75.500	76.650	79.350
April	80.500	80.500	76.900	76.480	76.350	79.500
May	80.000	80.250	76.950	77.000	76.650	79.350
June	81.000	80.150	77.000	76.650	76.950	77.800
July	81.500	78.000	76.500	76.630	77.050	77.700
August	80.650	77.000	76.000	76.250	78.000	77.800
September	80.750	77.000	75.950	76.100	78.500	79.400
October	80.650	77.500	75.900	76.150	79.700	80.600
November	80.700	77.500	75.500	77.360	79.700	79.350
December	80.750	77.500	76.250	77.370	79.700	80.000

Month	1971	1972	1973	1974	1975	1976
January	80.000	78.900	79.000	68.700	68.300	70.400
February	79.350	77.100	74.000	68.900	66.150	71.100
March	79.350	76.900	69.550	67.950	65.650	69.450
April	79.350	77.000	69.500	68.400	66.800	70.400
May	79.200	76.900	68.000	68.550	66.750	70.850
June	78.750	77.500	67.650	68.150	66.600	71.700
July	78.750	77.350	68.150	67.800	67.400	72.000
August	77.750	77.200	71.700	68.200	68.000	72.500
September	78.450	77.350	69.700	68.250	68.750	74.000
October	79.800	77.350	71.500	69.050	69.500	74.350
November	79.700	77.200	73.350	68.200	69.600	73.750
December	79.700	77.250	73.500	68.100	69.600	74.750

Table 4: Monthly Black Market Exchange Ratenumber of rials per U.S. Dollar, end of the Month)

Month	1977	1978	1979	1980	1981	1982
January	75.250	73.700	98.000	160.000	215.000	450.000
February	76.000	71.050	112.000	184.000	230.000	450.000
March	75.000	71.700	98.500	179.000	225.000	475.000
April	75.650	73.650	96.000	140.000	220.000	500.000
May	76.500	79.250	115.000	135.000	245.000	500.000
June	74.200	73.000	121.000	217.000	300.000	500.000
July	74.700	76.000	132.000	213.000	300.000	500.000
August	74.150	77.500	132.000	220.000	350.000	400.000
September	72.000	77.750	130.000	250.000	350.000	400.000
October	74.650	78.000	165.000	255.000	400.000	450.000
November	73.150	87.500	170.000	265.000	400.000	400.000
December	73.800	84.000	165.000	191.000	400.000	400.000

Month	1983	1984	1985	1986	1987	1988
January	400.00	450.00	627.00	580.00	850.00	1000.0
February	400.00	430.00	680.00	625.00	910.00	1125.0
March	400.00	415.00	615.50	636.00	955.00	1200.0
April	350.00	425.00	614.15	610.00	970.00	1100.0
May	345.00	474.00	607.10	645.00	960.00	1000.0
June	350.00	490.00	597.65	643.00	980.00	975.0
July	340.00	520.00	543.50	686.00	1050.0	900.0
August	360.00	505.25	621.35	654.00	1055.0	875.0
September	360.00	588.25	584.40	662.00	1100.0	850.0
October	355.00	590.00	578.70	770.00	1000.0	880.0
November	363.00	600.00	556.00	812.00	1075.0	800.0
December	370.00	622.20	553.50	815.00	1100.0	775.0

Month	1989	1990	1991	1992	1993	1994
January	969.0	1256.0	1429.0	1434.0	1579.0	2154.0
February	1147.0	1335.0	1395.0	1447.0	1607.0	2452.0
March	1182.0	1321.0	1375.0	1451.0	1658.0	2445.0
April	1306.0	1384.0	1385.0	1469.0	1653.0	2658.0
May	1332.0	1383.0	1394.0	1445.0	1636.0	2686.0
June	1215.0	1423.0	1366.0	1441.0	1610.0	2356.0
July	1192.0	1417.0	1395.0	1450.0	1596.0	2398.0
August	1250.0	1403.0	1438.0	1459.0	1597.0	2507.0
September	1197.0	1412.0	1460.0	1481.0	1615.0	2720.0
October	1065.0	1446.0	1462.0	1520.0	1698.0	2728.0
November	1087.0	1458.0	1440.0	1520.0	1967.0	2686.0
December	1123.0	1453.0	1422.0	1561.0	2089.0	2680.0

Table 4: Monthly Black Market Exchange Ratenumber of rials per U.S. Dollar, end of the Month)

Month	1995	1996	1997	1998	1999	2000
January	3607.0	4064.0	4644.0	4901.0	7964.0	8410.0
February	4129.0	4035.0	4621.0	5088.0	8232.0	8210.0
March	4263.0	4211.0	4866.0	5418.0	8059.0	8353.0
April	5118.0	4201.0	4748.0	5611.0	8130.0	8512.0
May	4181.0	4184.0	4825.0	5632.0	8703.0	8375.0
June	3575.0	4207.0	4750.0	5610.0	9144.0	8276.0
July	3680.0	4232.0	4730.0	5683.0	9099.0	8203.0
August	3955.0	4313.0	4710.0	6159.0	8903.0	8212.0
September	3863.0	4426.0	4622.0	6267.0	8703.0	8207.0
October	3797.0	4651.0	4702.0	6849.0	8656.0	8116.0
November	3973.0	4837.0	4839.0	7057.0	8708.0	7987.0
December	4089.0	4812.0	4826.0	7140.0	8650.0	7998.0

Month	2001	2002	2003	2004	2005	2006
January	8003.0	8014.0	8031.0			
February	8004.0	7996.0	8108.0			
March	8028.0	7996.0	8185.0			
April	8018.0	7991.0	8183.0			
May	7996.0	8002.0	8190.0			
June	7994.0	7998.0	8231.0			
July	7994.0	8000.0	8314.0			
August	8014.0	8015.0	8439.0			
September	8037.0	8013.0	8396.0			
October	8017.0	8021.0	8374.0			
November	7999.0	8026.0	8377.0			
December	7999.0	8039.0	8349.0			

Sources: From January 1947 till June 1989, data comes from different issues of World Currency Yearbook (formerly known as Pick's Currency Yearbook). From July 1989 till December 2003, they are provided by the Central Bank of the Islamic Republic of Iran. If you need the data in Excel format, please send the author an e-mail (bahmani@uwm.edu).

III- Summary and Conclusion

The review of historical developments surrounding Iranian rial and foreign exchange policies implemented by the Central Bank of Iran leads to the following conclusions:

a. Rial has depreciated over time from 11.20 rials per dollar to as low as 8600 rials per dollar. Given the evidences in Bahmani-Oskooee (2003), depreciation of the rial, even in the black market dominates the performance of other macro variables. Current stagflation in Iran could be attributed to depreciation of the rial (Bahmani-Oskooee, 1996).

b. There was a period during which (1978) Iranian rial had gained international recognition. Not only it was convertible currency, but also one of the 16 currencies included in the definition of Special Drawing Right (SDR). The inclusion was justified by the fact that Iran was becoming a major player in world trade.
c. Through the history, the Central Bank of Iran has adjusted the official exchange rate and has brought it closer and closer to the black market rate. This provides an event study supporting the literature that foreign exchange and direct controls have only short-run effect on the official rate. In the long-run, official rate is adjusted toward the black market rate. (Bahmani-Oskooee, Miteza and Nasir 2002).

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