



By: Djavad Salehi-Isfahani

# How deep are the economic roots of the protests in Iran?



The protests that erupted in Tehran on December 28 and quickly spread across Iran were triggered by a specific grievance: the collapse of the country's currency, the rial.

Currency devaluation in Iran is never merely a technical matter; it quickly drives up prices and reduces purchasing power, especially given that many wages are set annually.

In December, as the **rial's value** fell by 16% – for a total decline of roughly 84% over the past year – **food inflation** reached an annual rate of 72%, nearly double its recent average.

These developments follow decades of economic isolation. Starting in 2011, sanctions on Iranian oil sharply reduced the country's foreign-exchange earnings and slowed **GDP growth** from a respectable 5-9% annually in the early 2000s to less than 3% thereafter.

The loss of oil revenues created chronic budget deficits that the government has financed through monetary expansion, fueling inflation.

Iran's economic situation deteriorated further last year, when sanctions gave way to open confrontation.

While the 12-day war with Israel and the United States in June 2025 caused limited physical damage, it exposed Iran's vulnerability to sudden escalation, belying the regime's claims to have things under control and raising the country's risk premium.

**Investment**, already too low to compensate for rial depreciation, fell further, owing to fears of additional attacks by Israel and the US.

## Long-delayed economic reforms

Iranian President Masoud Pezeshkian's attempt to impose long-delayed economic reforms has compounded the pressure.

His **proposed budget** for the new Iranian year

(starting on March 20, 2026), submitted to parliament in November, was more contractionary than expected.

Taxes were scheduled to rise from 42% to 57% of government revenues, reflecting the anticipated drop in oil income.

At the same time, public-sector wages were set to increase by less than half of the government's projected inflation rate of 46% for the next year.

**Perceptions of rampant inequality have been reinforced by the Iranian economy's distortionary system of multiple exchange rates**

Although parliament later softened the blow, cutting the proposed value-added tax from 12% to 10% and doubling the wage increase, the message of austerity had already been sent.

While austerity is a hard sell under any circumstances, it becomes politically combustible in a society that views official corruption as pervasive and constantly confronts ostentatious **displays of wealth**.

Perceptions of rampant inequality have been reinforced by the Iranian economy's distortionary system of **multiple exchange rates**.

## Managed foreign-exchange markets

As **oil exports** fell from more than two million barrels per day before 2011 to as little as 300,000 barrels in 2019, the government allocated a portion of its scarce foreign exchange at highly subsidized rates in order to shield Iranians from the impact of sanctions.

But the system ended up facilitating rent-seeking and capital flight, with many recipients spending the money not on imports of essential goods, but rather on luxury items or

overseas travel, or reselling the foreign exchange at market rates.

Iran's government later introduced managed foreign-exchange markets, which enabled licensed exporters to sell their foreign-currency earnings to importers under government supervision, at rates that are between subsidized and market prices.

But it remained reluctant to eliminate the multiple exchange-rate system, fearing backlash from influential traders with privileged access.

### Pezeshkian's move to eliminate one of Iran's most visible sources of corruption undoubtedly angered entrenched interests

Pezeshkian, however, was willing to take this step. But his move to eliminate one of Iran's most visible sources of corruption undoubtedly angered entrenched interests, possibly contributing to the initial strike among merchants in Tehran's Grand Bazaar, which triggered the broader protests.

While that strike might have been politically motivated – reformers have often accused their conservative rivals of using their institutional power to resist change – the protests quickly spiraled into a crisis so acute that both factions are now looking for a way out.

The challenge is economic as much as it is political. The government's efforts to increase revenues, narrow the budget deficit, and reduce its reliance on money creation could eventually lower inflation.

But, in the short term, the reforms will carry economic costs. Eliminating foreign-exchange subsidies immediately raises prices for certain goods, potentially fueling broader inflation and putting downward pressure on the rial.

### The benefits of Pezeshkian's

### reforms are uncertain

To **compensate households**, the government has introduced monthly transfers of ten million rials per person (about \$7, or \$40 in purchasing-power-parity terms).

It has already deposited payments for roughly 80 million beneficiaries, excluding only the wealthiest decile. But whether this will be enough to tame the protests is far from clear.



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The objectives of Iran's last nationwide uprising – the “Women, Life, Freedom” movement of September 2022 – were more straightforward.

Sparked by the killing of 22-year-old **Mahsa Amini** by the country's morality police, the protests were met with a brutal crackdown.

Nonetheless, they are widely considered to have achieved at least one of their goals: to stop the enforcement of the hijab law. A growing number of Iranian women and girls now choose not to wear the hijab in public.

By contrast, the benefits of Pezeshkian's reforms are uncertain, likely to materialize only in the longer term, and difficult to communicate to a population battered by years of economic volatility.

Iran's government cannot credibly promise to

stabilize exchange rates or tame inflation any time soon.

The one move that could offer relatively quick economic relief – and to which the government could credibly commit – is a cessation of hostilities with Israel and the US.

But this might prove far more difficult for Iran's leadership than compromising on hijab enforcement.

In any case, ordinary Iranians are wary of any promises from Israel, especially after its devastation of Gaza, occupation of Syria, and intense bombing of Iran last year, which reportedly killed more than a thousand people.

The same goes for the US, which has proven under President Donald Trump that it cannot be trusted even by its closest allies.

Iran's protests reflect not only economic despair, but also the tension between mistrust of internal reform and fear of external pressure. As such, they may not be easily subdued.

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