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UN Sanctions and Iranian Arms Imports

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It is not clear as yet how the new UN sanctions on Iran will affect its arms imports. What is clear is that Iran's conventional forces are now heavily worn, obsolescent, and often were delivered before the fall of the Shah. Moreover, Iran lost some 60% of its land weaponry during the final battles of the Iran-Iraq War, and has never been able to replace and modernize its conventional forces.

Iran has faced serious financial problems in funding its force modernization, compounded by the systematic mismanagement of its economy. Iran's economy is overdependent on oil export revenues, with such revenues representing around 80-90 percent of total export earnings and 40-50 percent of the government budget; according to one source, revenues from oil monopoly rents comprised 63% of Iranian state revenues in 2004.ⁱ

The Impact of Rising Oil Export Revenues vs. Economic Mismanagement

Reporting by the U.S. Energy Information Agency shows, however, that strong oil prices have boosted Iran's oil export revenues and helped Iran's economic situation over the last few years. Iran's oil export revenues have increased steadily, from \$32 billion in 2004, to \$45.6 billion in 2005, with estimates for 2006 at \$46.9 billion. Estimates for the Iranian year from March 2006 to March 2007 are about \$54 billion. As a result, Iran's real GDP increased by around 6.1 percent in 2005.ⁱⁱ

Iran's state-run, oil-rentier economy has run into structural problems that, if it continues, will adversely affect the development of the armed forces. The official figure for inflation is around 16 percent per year, and unofficial estimates place the figure at 40-50 percent. Iranian budget deficits remain a chronic problem, in part due to large-scale state subsidies on foodstuffs and gasoline. The Iranian parliament (Majlis) decided in January 2005 to freeze domestic prices for gasoline and other fuels at 2003 levels.ⁱⁱⁱ

In March 2006, parliament reduced the government's gasoline subsidy allocation for FY 2006/07 to \$2.5 billion, compared with a request of \$4 billion and costs of over \$4 billion for imports in the previous year. On March 7, 2007, the Majlis voted to freeze annual subsidies for gasoline at \$2.5 billion, which will lead to a price hike by about 25%, projected to take effect in May 2007.^{iv} In 2006, the NIOC said it has used nearly its entire \$2.5 billion budget for gasoline imports, but legislators have stated their opposition to providing the additional \$3.5 billion necessary to pay for imports through the end of the fiscal year, in March 2007.

The EIA reports that the lack of job opportunities for the country's young and rapidly growing population is another major problem. Official unemployment in Iran was reported to be around 11 percent in 2006, but was significantly higher among young

people. Iran has attempted to diversify its economy by investing some of its oil revenues in other areas, including petrochemicals.

Iran has also sought to attract billions of dollars worth of foreign investment by creating a more favorable investment climate, by reducing restrictions and duties on imports and by creating free-trade zones. However, there has only been very limited progress and Iran has fallen far short of its goals. Badly structured incentive programs, overambitious project requirements, poorly structured incentives, a hostile reaction to Iran's new president, and the ongoing debate over Iran's nuclear programs have all been significant factors.^v

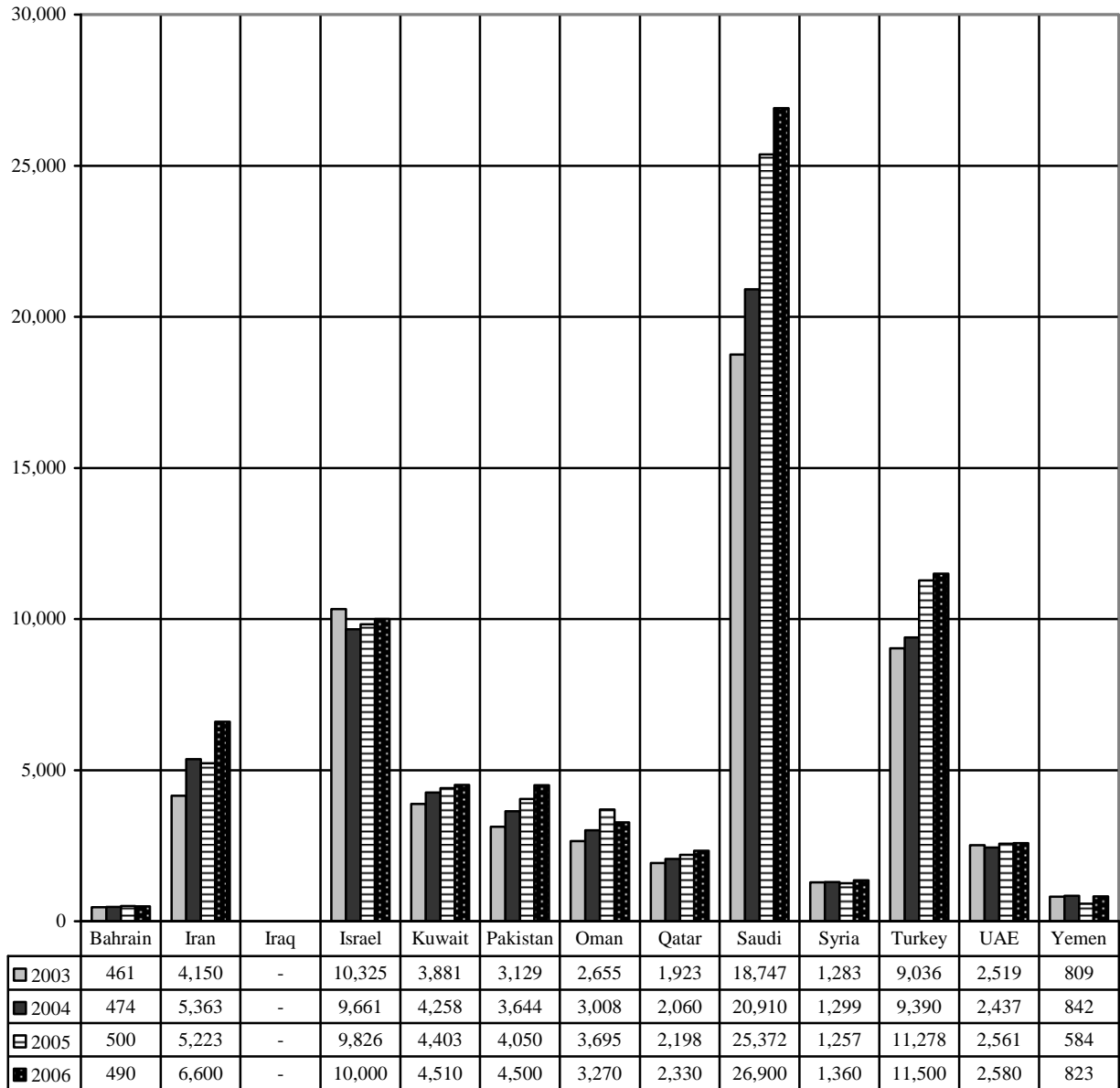
Rising Iranian Military Spending

As **Figure One** shows, Iran has used its rising oil revenues to finance higher military spending. According to the International Institute for Strategic Studies (IISS), Iran's military budget has been steadily increasing over the past few years, rising from \$2.3 billion in 2000, to \$3.36 billion in 2003, and to \$6.2 billion in 2006 – this represents a 170-percent increase in Iran's military budget since 2000.^{vi}

Figure One also shows, however, that the other Gulf states have also increased their military spending as well, and Iranian spending lags far behind Saudi Arabia and even farther behind the total spending of the Southern Gulf states.

Figure 3.1: Comparative Gulf Military Spending

(In Millions of Current \$U.S.)



Note: Israeli, Pakistani, Turkish, and Yemeni military spending totals do not include U.S. military assistance.

Source: IISS, *Military Balance 2007*.

Plans for More Arms Imports with Major Deliveries Already Pending

The increase in military spending also has led to an increase in Iran's arms imports. **Figure Two** shows the trend in new Iranian arms deliveries by supplier from 1993 to 2004. There has been a steady contraction in new arms deliveries from \$2.6 billion during 1993–1996, to \$1.9 billion during 1997–2000, and to \$0.5 billion during 2001–2004, yet this number can be expected to increase because of an underlying recent increase in settled agreements.

Russia and China, Iran's two major suppliers, have experienced sharp declines in their exports to Iran. For example, Russian arms exports to Iran declined from \$1.3 billion during 1993–1996 to \$0.1 billion during 2001–2004, while China's arms deliveries to Iran declined from \$0.9 billion during 1993–1996 to \$0.1 billion during 2001–2004.

In 2005, however, Russia concluded arms and technology transfer agreements with Iran that increased Iranian imports considerably. Russia agreed to deliver 29 comparatively modern TOR-M1 SAM as well as provide technological upgrades on Su-24 and MiG-29 aircraft and T-72 main battle tanks.^{vii} The TOR-1 SAMs reportedly were received in early 2007.^{viii}

Iran's new arms agreements have illustrated a more mixed trend.

As shown in **Figure Two**, the combined value of new agreements over arms purchases increased from \$1.2 billion between 1993 and 1996, to \$1.5 billion between 1997 and 2000, fell to \$0.8 billion between 2001 and 2004, before the total of new agreements almost tripled to \$2.2 billion during 2002–2005. Russia's share in the total value of arms imports rose from \$0.2 billion between 1993 and 1996 to \$0.4 billion between 1997 and 2000, and then remained the same at \$0.4 billion between 2002 and 2004, but more than quadrupled between 2002 and 2005, which represented an almost 80% share of all new delivery agreements.

China's new arms agreements with Iran increased from \$0.4 billion during 1993–1996 to \$0.60 billion during 1997–2000, and then dropped to \$0.20 billion during 2001–2004. China has long been known to be a significant provider of missile technology to Iran. Western European countries had no new arms agreements during 2001–2004, and the amount coming from "All Others" decreased from \$400 million during 1997–2000 to \$100 million during 2001–2004.

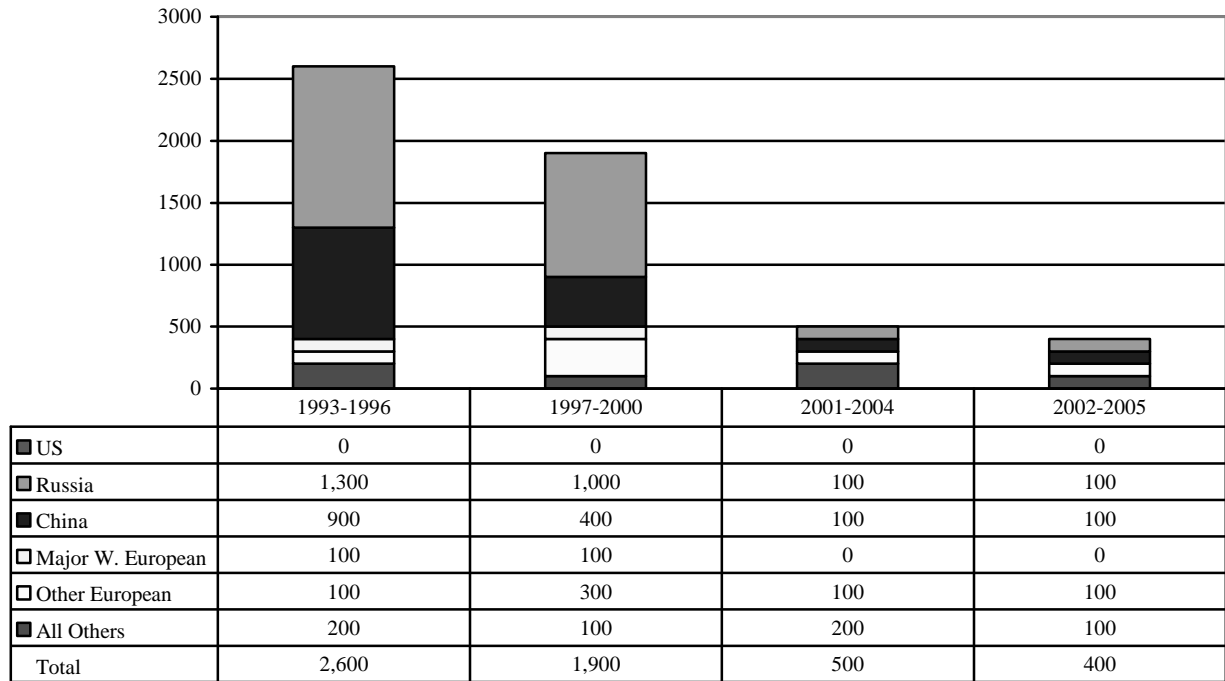
These expenditures have led to carefully focused purchases that have increased Iran's military capabilities in several important areas. They have not, however, been large enough to offset the steady aging of most of Iran's military inventory, its inability to obtain parts and upgrades for much of its Western-supplied equipment, and anything close to parity with the level of weapons and technology in U.S., British, and many other Gulf forces. Iran has tried to compensate this by creating its own military industries, but such efforts have as yet had only limited impact.

As **Figures Three** and **Four** show, however, they have not come close to bringing Iran's arms imports up to the levels of several other Gulf powers, or close to the total imports of the GCC states.

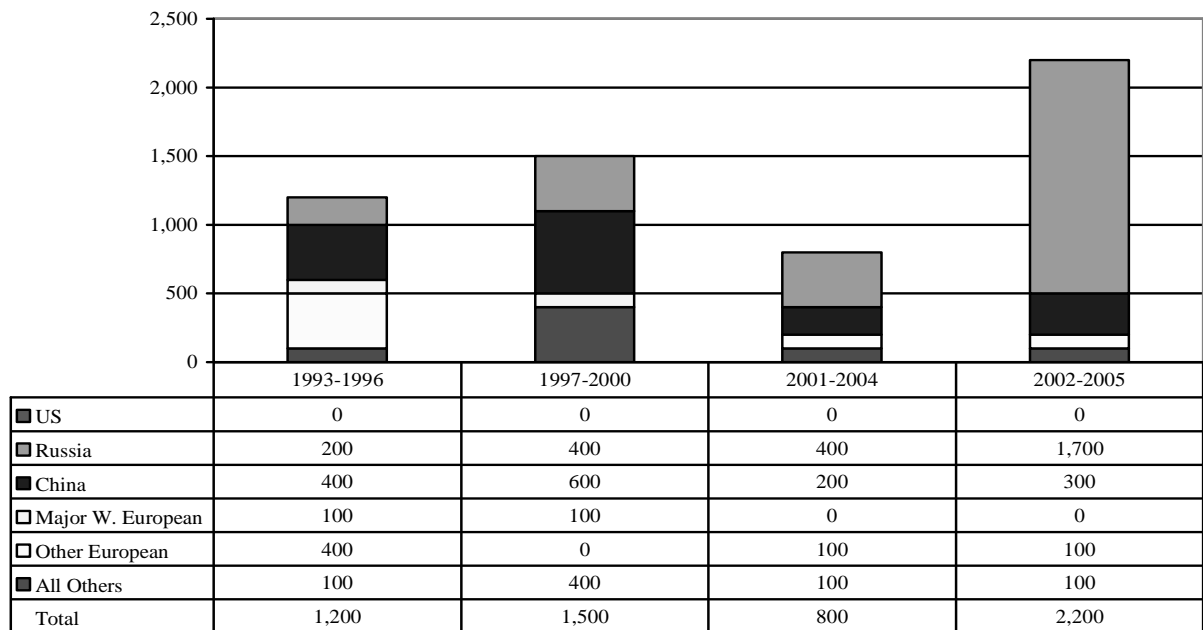
Figure Two: Iran's Arms Imports by Supplier, 1993-2005

(In Current Million \$U.S.)

Deliveries



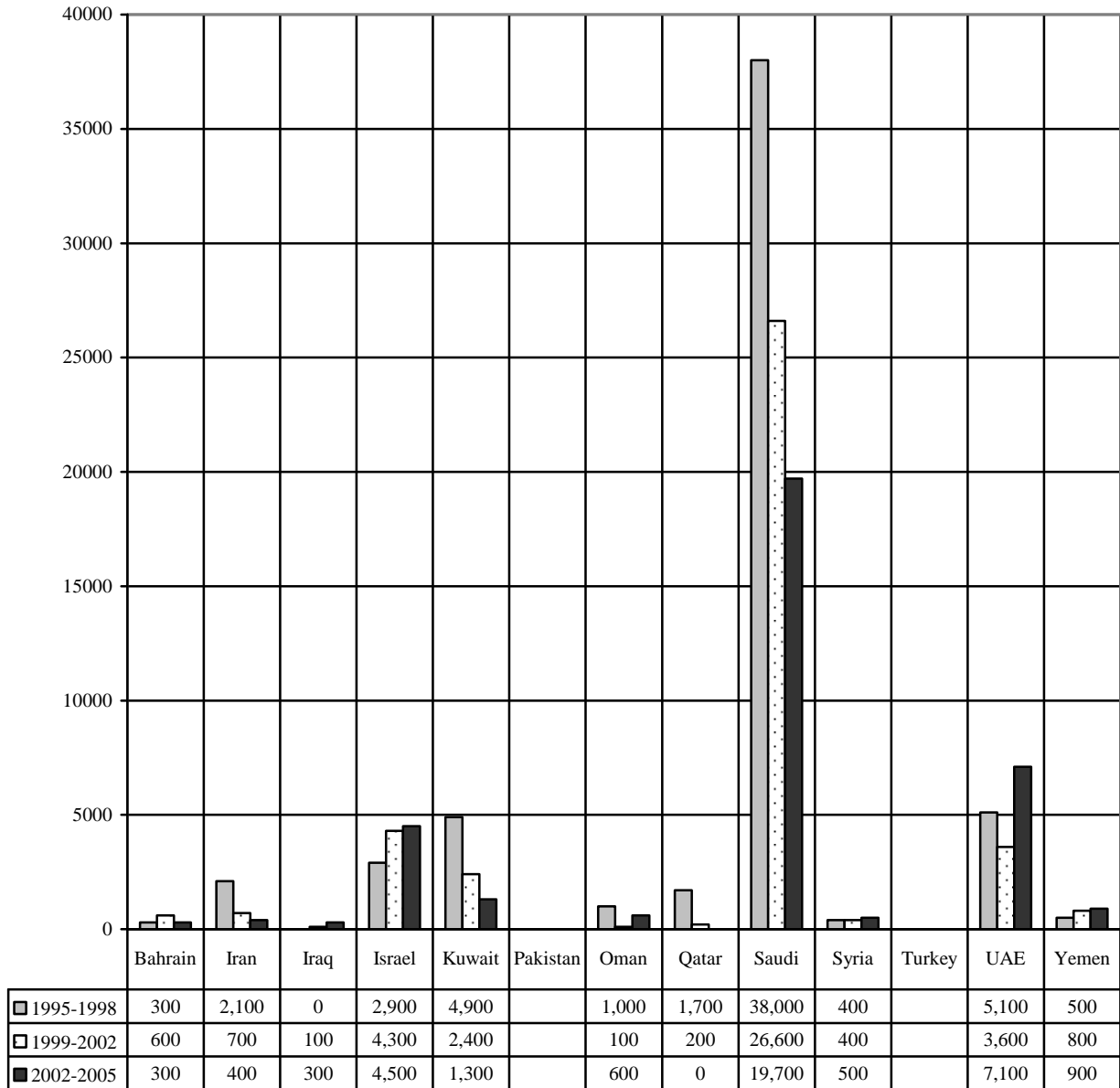
New Agreements



Source: Richard F. Grimmett, Conventional Arms Transfers To Developing Nations, 1998-2005, CRS, October 23, 2006; Richard F. Grimmett, Conventional Arms Transfers To Developing Nations, 1997-2004, CRS, August 29, 2005; Richard F. Grimmett, Conventional Arms Transfers To Developing Nations, 1993-2000, CRS, August 16, 2001.

Figure Three: Comparative Gulf New Arms Deliveries

(In Millions of Current \$U.S.)

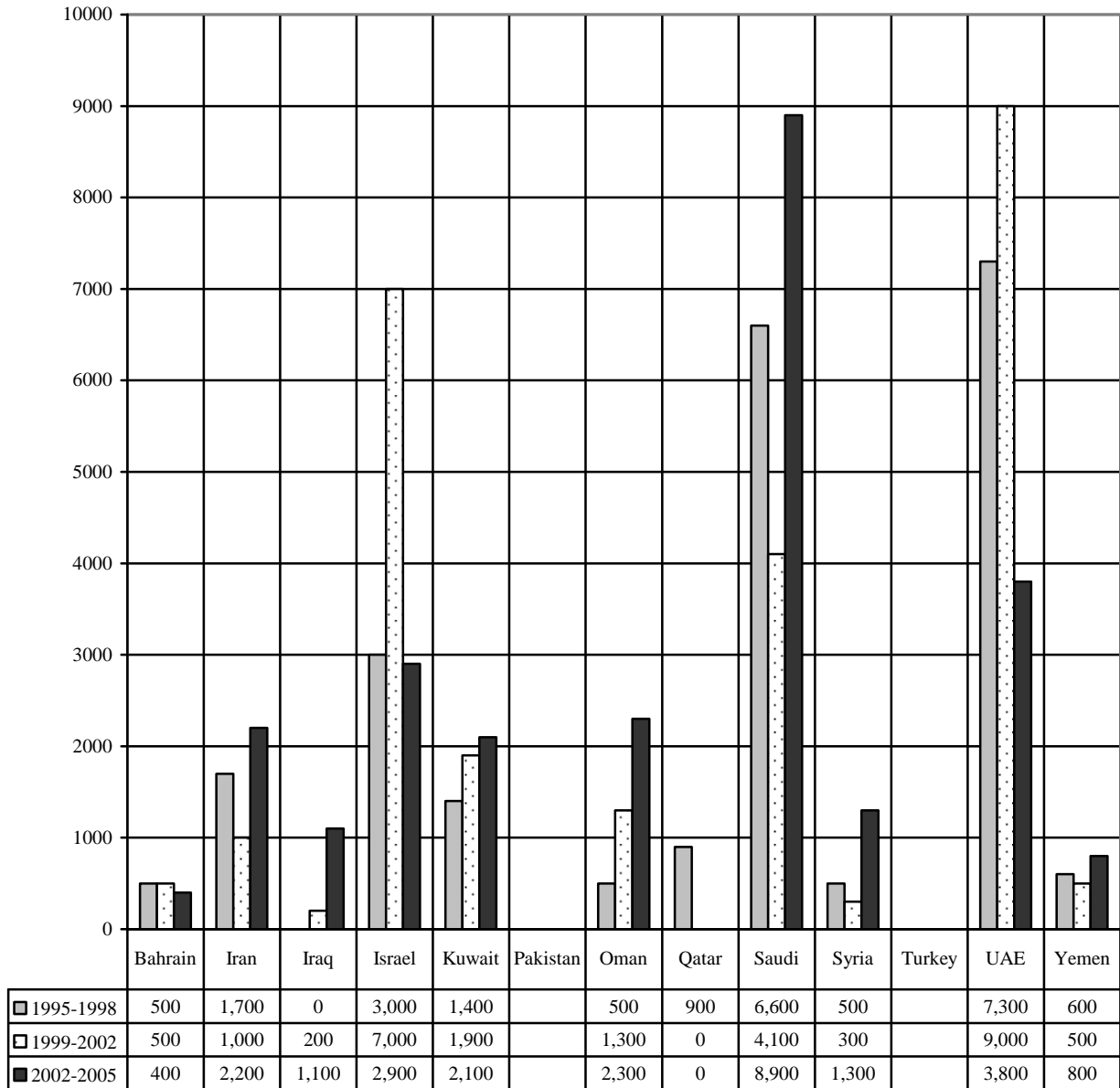


Israeli and Yemeni totals do not include U.S. military assistance.

Source: Richard F. Grimmett, Congressional Research Service, various reports.

Figure Four: Comparative Gulf New Arms Import Agreements

(In Millions of Current \$U.S.)



Israeli and Yemeni totals do not include U.S. military assistance. UAE total for 1998-2001 includes an agreement for licensed production 80 F-16 aircraft worth \$6.432 billion.

Source: Richard F. Grimmett, Congressional Research Service, various reports.

ⁱ Roger Stern, "The Iranian petroleum crisis and United States national security", *Proceedings of the National Academy of Sciences of the United States of America*, vol. 104, no. 1, January 2, 2007, p. 377.

ⁱⁱ Energy Information Agency (EIA), "Country Profile Iran," Department of Energy, Washington, August 2006, <http://www.eia.doe.gov/emeu/cabs/Iran/Background.html>.

ⁱⁱⁱ Energy Information Agency (EIA), "Country Profile Iran," Department of Energy, Washington, August 2006, <http://www.eia.doe.gov/emeu/cabs/Iran/Background.html>.

^{iv} Gareth Smyth, "Tehran to ration petrol and put up pump prices", *Financial Times*, March 9, 2007.

^v Energy Information Agency (EIA), "Country Profile Iran," Department of Energy, Washington, August 2006, <http://www.eia.doe.gov/emeu/cabs/Iran/Background.html>.

^{vi} IISS, Military Balance, 2005-2006, 2006, CIA, The World Factbook, 2006, "Iran," <http://www.odci.gov/cia/publications/factbook/geos/ir.html>.

^{vii} Richard F. Grimmett, *Conventional Arms Transfers To Developing Nations, 1998-2005*, CRS, October 23, 2006.

^{viii} Keri Smith, *Iran receives final TOR-M1 deliveries*, Jane's Defense Weekly, 24 January 2007.