

CONSEQUENCES OF TARGETED SUBSIDIES ON ENERGY PRODUCTS

Masoud Baradaran Nasiri¹, Shahram Gilaninia^{2*}

¹*M.A. Student of Executive Management, Islamic Azad University, Rasht Branch, Rasht, Iran*

^{2*}*Associate Professor of Department of Industrial Management, Islamic Azad University, Rasht Branch, Rasht, Iran (Corresponding Author)*

Abstract

Targeted subsidies are one of the biggest changes that have occurred in recent decades in the field of Iran economy. Given the importance and scope of energy subsidies effects and since most studies conducted found that this part is most influential part from project targeted subsidies, accordingly effects of this project in the form of removal of energy subsidies has been seen that removing other subsidies could also have similar implications but smaller scale for the country's economy. It is noteworthy which by implementing the policy of energy products price reform; many economic variables will be affected directly and indirectly from it that in this paper will be mentioned some of the most important changes.

Keywords: Energy Products, Targeted Subsidies, Economic, Trade, Government

1. Introduction

Targeted subsidies are one of the biggest changes that have occurred in recent decades in the field of Iran economy (Pajoyan, 2010). Plan of targeted subsidies is the most important and the most challenging part of economic developments project that has considered more than other areas for expert meetings and government policy (Dadgar & et al, 2012). One effect of reduction in subsidies and increase energy products prices is the consumption pattern reform of households and manufacturers. From this perspective, the liberalization of energy products prices to households and producers will lead changing their production and consumption patterns and moving towards energy efficiency. The purpose of energy management in order to achieve organization goals is efficient use of energy with the lowest cost (Asefzadeh & et al, 2014). According to the fourth development plan act for the prices of petroleum products and in order to achieve the objectives of vision in Iran, the liberalization of energy products prices and removal of subsidies paid to this products is inevitable needs of Iran's economy and due to the fact that in our country, government by subsidizing energy products and relative change prices of goods and services has affected development and production of various sectors of the economy, thus determine the relationship between energy subsidies payment with the growth of various sectors of the economy seem to be essential (Abasian & Asadbeygi,2011).

2. Targeted Subsidies

With successful revolution and 19 months after the war on Islamic nascent revolution, began political and economic sanctions, investors fled affiliated with the former regime, close many financial centers after the revolution and especially after the war and reduce the level of foreign and domestic investment, the Iranian economy faced with the crisis. Many economists to check the economic situation of each country use many indicators. The main indicators are: GDP, national income, per capita income, the income gap and inflation rate. For reasons mentioned above, many of the Iranian economy indicators found the situation bad; so that in 1980- the first year of the war has had lowest GDP. Reducing production lead to many problems that most important of them include a decrease in income, rising inflation, and the rise in the unemployment rate. To manage this crisis, officials decided to take economic policy and the management of many centers. Thus Iranian economy was state-owned high speed. Government after war, which became famous a government building, policy of privatization and economic restructuring was on top of its work. Privatization means transfer of government outsourcing in the economic sphere to the public and the adjustment is adjust prices based on the current rate dollars. Gradually exchange or current rate is given to manufacturer and manufacturer offered the goods with current rate. Reform government continued this process. The policy of economic liberalization and a reduction in governmental functions in the second, third and fourth development planning continued as a general policy and macro. But implementing this policy faced a legal obstacle. Article 44 of the constitution outsourcing many infrastructure activities and important economic was placed at the disposal of the government. To solve this problem on the orders of Iran's Supreme Leader, the expediency council was in charge of expert work to overcome this obstacle. Implementation of these policies was accompanied by the rise of conservative government to implement these policies attempt to develop a bill called the bill of targeted subsidies. This bill after long debates and a lot of ups and downs between the government and the parliament finally was approved and as the law of targeted subsidies was notified to run from the beginning of 2010 to the government. Project of targeted subsidies that is the most important government action to address and resolve challenges of subsidies, with large cache and arches, finally implemented (Niromand, 2011).

3. Advantage and Problems of Targeted Subsidies in the Country

Targeted subsidies, as an inevitable necessity in the country, also have positive effects and the negative consequences.

Some of the benefits and problems of law in the country's economy will be as follows:

A major advantage of the law of targeted subsidies:

- 1 - Achieving social justice
2. Optimal allocation of resources
3. Consumption management
4. Prevent the waste of resources
5. Reform production and distribution system of banking and wealth resources (financial disclosure)
6. Improve the efficiency and effectiveness in activities and the economy at macro and micro levels
7. Strengthening the national currency
8. Stabilizing the economic and investment growth
9. Participation of people in the management of national resources

10 increase the country's export because of the growth to domestic consumption

B) Problems of targeted subsidies law:

1. The possibility of rising inflation and unemployment in the short term
2. Negative impact on public health and consequently increase government cost in long-term
3. Transfer of increasing costs imposed upper income higher income classes to others (Alizadeh, 2010).

4. Targeted Subsidies History in the Country

First time after Iran Islamic Revolution in paragraph 4, the general policies law the first development plan (approved in 1989) had explored the issue of the quota changing of essential goods, so that subsidies paid in the context of the country's social security system gradually was considered only at people with low income. in law of second development plan (approved in 1994) was emphasized and as well continue subject policy of payment of subsidies for basic goods and medicines, and possible publicizing subsidies hidden part and at the same time strengthening the social security system, insurance, assistance and establishing and providing direct assistance in case of need also in the third development plan (Article 46), the government is obliged to take legal action to targeted payment of subsidies essential goods and energy products and the other. In addition, chapter VIII of the fourth development plan (approved in 2004), in this article government is obliged to review the regulations and providing rules for this purpose. About petrol and gas oil as well as according to article (1) of the public transport development law and management of fuel consumption (approved in 2007) government is responsible for exit gasoline and diesel of support basket. Article 16 of general policy system in course of perspective refers to changes in the system of subsidies payment and government transfer payments and transparent of hidden subsidies in country economy along with compensation policies and the strengthening of social security systems and support deprived segments (www.hadfmandsazi.ir).

Table 1) Comparison of systems based on the existence of subsidies and system based on distribute targeted subsidies

<i>Approaches</i>	<i>system based on the existence of subsidies</i>	<i>system based on targeted subsidies</i>
<i>Realization of social justice</i>	Inappropriate and inefficient and low portion of the lower deciles of subsidies	To identify correctly, target population can be fair.
<i>optimal allocation of resources</i>	the possibility of corruption and rents and increase waste of resources	Elimination of corruption and rent due to lack of targeted subsidies and reduce waste resources
<i>consumption management</i>	Excessive consumption of goods and energy due to the low price	Creating the right culture and rational consumption among population
<i>Economic growth</i>	Slowing economic growth	Prosperity, and economic growth in the long term
<i>Environment</i>	Environmental pollution due to indiscriminate use of energy	Reduce pollution due to optimization and correctly use of energy and replacing energy with clean energy and positive
<i>Investment</i>	Smuggling and parallel markets and reduce investment	Investment expansion or growth
<i>Transparency</i>	Gap between domestic prices and	Loss gap between prices and increase the

<i>price</i>	<i>regional</i>	<i>country's export</i>
<i>Efficiency of the economic system</i>	Price distortions and inefficiency of the economic system	Increase the efficiency of the economic system through the reform of prices and optimal allocation of resources

5. The consequences of the implementation of targeted subsidies

According to the discussions the importance and scope of energy subsidies effects and since most studies conducted found that this part is most influential part from project targeted subsidies, accordingly effects of this project in the form of removal of energy subsidies has been seen that removing other subsidies could also have similar implications but smaller scale for the country's economy. It is noteworthy which by implementing the policy of energy products price reform; many economic variables will be affected directly and indirectly from it that in this section will be mentioned some of the most important changes (Gilaninia & et al, 2013 & Amiri & et al, 2010).

5.1. Effects of reform energy products prices on inflation

As noted, all studies show that rising energy products prices has a direct and indirect positive impact on the general price level which of course will depend on the changing and reforming prices of these products. But among key macro-economic variables, energy products price reform (proportional to the changing it in certain price or change prices growth globally) indicate that inflation rate is as main core of influences the implementation of this policy and other variables will be affected as a result inflation rate.

Price reform factors, depending on the final consumption or intermediate can be involved in changing general level of prices. In other words, some of the energy products that are in final consumption basket of families, modifying their prices change directly the consumer price index (CPI). While some of these products as intermediate products are used for economic enterprises which their price reform affect producer's price index (PPI), that finally change in the indicators PPI, can be effective raise the price of manufactured goods in firms.

In addition, changes in energy products prices and subsequent by increases in the prices of commodities and finally general level of prices (inflation rate), in turn, leads to the formation of inflation expectations (IE) and this contributes to the escalation of inflation. The experience of some countries confirms that in some cases, a large part increase prices resulting from the implementation of the policy mentioned is resulting from inflation expectations. In case once implementation of energy products price reform policy, people not have expect to increase prices in many years and so increase price resulting from increase inflation expectations in the coming years will not happen.

5.2. Reform effects of energy products prices on economic growth

Most empirical studies suggest that reform energy products prices have a negative impact on economic growth in the short term. This impact can be discussed from two aspects of supply and demand. Of the total supply of three areas, including energy input price changes in the manufacturing process of the firm, the wages and the price of capital is affected. in the total demand, rising energy products prices as a direct is led to reduction in actual consumption of energy in the whole economy and as a result, will reduce consumption of total demand and also increasing general level of prices of other goods and services by reducing the purchasing power of households is led to reduce real tenable income and thus reduce the consumption of other goods and services. Therefore, it is expected that reduce the total consumption of goods and

services. The most important changes have been changes in values supplied to consumer (Gilaninia & et al, 2012). In addition to these discussions, rising inflation resulting from reform products price is led to increase the interest rate as a result, investment demand (and even consumer demand) will be reduced, moreover, it should be noted which public spending in term of investment and consumption is not as well as the private sector because invest in the public sector isn't affected by the real interest rate of the domestic market and will change just actual consumption of energy in the public sector. Overall reform energy products prices in the short term will be reduce total demand of economy and but in long-term changes of mentioned variables looks very different from the past.

5.3. Effects of energy products price reform on the labor market and wages

In general, the labor market takes relative effect from implementing the policy of energy products price reform like other economic markets. This influences is analyzed both the supply and demand for labor. In term of the labor supply must say that due to the structure of country labor market and structural unemployment, labor supply severity and the response is different in comparison to competitive market. Energy products price reform and consequently increase the general level of prices makes that decline the purchasing power of labor force and labor to compensate for this reduction in purchasing power are forced which be applicants for new opportunities of job. In macro level, these changes will be increase the labor force participation rate.

As well as changes in the general level of prices causes that in the process of determining wages (even by delay of several months) will increase wages by workers or labor union. At reviews impact of rising prices for energy products on labor demand can be noted that will increase costs of energy products prices, and will reduced production levels. As a result, in the short term could reduce employment which outcome of supply and demand for labor in the short term will be increase the unemployment rate because with the increase wages will increase the cost of economic enterprises and will decreases labor demand by these enterprises. This situation is more evident in user's economic enterprises.

However, due to stickiness of wages and lack of flexibility country labor market may affect implementing reform policy of energy products prices in comparison to other markets by delays more. But in the long term because of the possibility of changing the structure of production and technology in Iran, there is the possibility of replacing the factors of production.

5.4. The effects of energy products price reform on income distribution

In term of macro dimension, energy products price reform and consequently increase the general price level can affect income distribution and is led to deterioration of income distribution situation and increase inequality among income ranks of the community. However, in case energy products prices rise, higher income decile in terms of consumption will be lose more than total energy consumption, but the group through fixed assets and non-monetary income will be compensated this loss. But in the low income group and fixed employees of energy consumption has a significant share in household consumption basket, thus increase the prices of these products will lead to reduce their purchasing power. While compensating for these losses (due to the lack of fixed assets and non-monetary income) for groups mentioned is not such as the top income decile and from outcome of these changes intensifies the income gap between high and low income groups. Also energy products prices reform, through economic slowdown and rising unemployment in the short term can lead to increase inequality and deterioration of the situation in income distribution. However, addition to this case distribution revenues obtained of the

reform in prices for the state can have a very positive impact on income distribution that should be considered its final estimation. This estimate is depends on a large extent to the implementation of these reforms.

5.5. The effects of energy products price reform on trade balance

Foreign trade includes trade in goods and services. Commodity trade includes oil trade and other goods. By rising cost of energy products and subsequently general level of prices is expected to reduction in non-oil exports and increase imports. reduction in non-oil exports can be attributed to most exporters tend to sell non-oil exports in domestic because earn more profit than before the increase in prices, reduction in the competitiveness of domestic goods at the international level and increase production capacity unemployed inside. In front increasing profitability imported goods due to lower relative prices will lead to increase import. In addition to the general level of prices other factors could change the trade balance. These changes can be estimate based on import and export behavioral equations as a function of economic growth, exchange rates, inflation and ratio of price levels inside to outside.

5.6. The effects of energy products price reform on the General State Budgets

General government budget is consists of two parts resources and expenses. The structure of general budget in Iran such a way that components of resources and expenses seriously affected by the exchange rate, effective tariff rates, the growth of wages in the public sector and private, growing costs, and finally to increase prices of products and services provided by the government in state enterprises. Course addition to the above items, it is necessary to add change resulting from the oil income sources. It is noteworthy that the public enterprises are connected to general budget through two channels including the cost of construction projects and help losses. As a result of changes in exchange rates and increasing costs indexes and the government's decision will be effective to increase price of products in their dependence on general budget.

5.7. Other changes

In addition to the above-mentioned changes other variables such as the money market, foreign trade, etc. are also affected that each of these variables requires extensive study and wide investigation (Amiri & et al, 2010).

6. Discussion and Conclusion

Plan of targeted subsidies is the most important and the most challenging part of economic developments project that has considered more than other areas for expert meetings and government policy. Targeted subsidies are one of the biggest changes that have occurred in recent decades in the field of Iran economy. Given the importance and scope of energy subsidies effects and since most studies conducted found that this part is most influential part from project targeted subsidies, accordingly effects of this project in the form of removal of energy subsidies has been seen that removing other subsidies could also have similar implications but smaller scale for the country's economy. It is noteworthy which by implementing the policy of energy products price reform; many economic variables will be affected directly and indirectly from it. They include effects of reform energy products prices on inflation, economic growth, the labor market and wages, income distribution, trade balance, General State Budgets, Other changes (money market, foreign trade, etc).

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