

Currency Friction and the Erosion of Production Planning

Why the Iranian Business Environment is Unpredictable

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For any business or investor intending to enter the Iranian market, the primary question usually revolves around “exchange rates.” However, reducing Iran’s currency crisis to mere fluctuations in the US Dollar rate is a strategic fallacy. The fundamental issue within Iran’s production ecosystem is not just the price of foreign exchange (FX); it is the multi-tiered nature of exchange rates, the lack of certainty regarding the timing and method of allocation, and the resulting progressive erosion of production planning capabilities.

When we speak of “currency friction,” we refer to a mechanism where monetary and regulatory tools, instead of facilitating trade, act directly as a brake on production, swallowing a company’s ability to survive, price its products, and invest.

The Evolution of the Exchange Rate Regime: From Stabilization Policies to Market Realities

Understanding this crisis is impossible without looking at the roots of FX supply in Iran. The country’s primary FX lifeline is heavily dependent on oil revenues; this means any shock to exports or oil prices (including the return of sanctions) leads directly to a reduction in FX supply, a depreciation of the Rial, and, with a time lag, a surge in domestic inflation.

A look at the 35-year evolution of the exchange rate regime (1990–2025) reveals the depth of this instability. The Iranian economy has slid from the short-term, single-tier rate periods of the early 1990s and 2000s (with the Dollar at 799 Tomans) into multi-tiered systems during periods of intensified sanctions. From the stabilization of the Dollar at 4,200 Tomans in 2018 to the formation of a three-tier system in 2025 (comprising 28,500 Tomans for essential goods, 38,000 Tomans for commercial transactions, and a free-market rate nearing 94,000 Tomans), policymakers have been in a constant state of trial and error with mechanisms that have ultimately only resulted in rent distribution and a deepening of the crisis.

The NIMA system, launched in May 2018 to manage FX resources, ultimately became a platform for further friction. The insistence on command-based rate controls failed

to withstand free-market realities, and these policies eventually culminated in a massive surge in exchange rates in late 2025. At that point, the gap between the official and free-market rates became so profound, breaking unprecedented records, that the then-Governor of the Central Bank was forced to resign.

The Working Capital Crisis and the Paralysis of the Supply Chain

In the boardrooms of manufacturing companies—ranging from fast-moving consumer goods (FMCG) and tobacco to construction equipment and pharmaceuticals—the greatest concern is no longer “sales,” but “procurement.” When a country’s FX system is built on quotas, prioritization, and long queues for allocation, manufacturers face three fatal challenges:

1. Allocation Delays and Inventory Stagnation:

According to the Purchasing Managers’ Index (PMI) report by the Iran Chamber of Commerce in May 2026, the index for purchased raw materials in the industrial sector fell to 36.3, one of the lowest records ever recorded. The report stated:

“The purchased raw materials inventory index remains in a recessionary and declining range. In May, as in previous months, it sat at one of its lowest levels, indicating a persistent and deep crisis in raw material procurement. On one hand, companies face restrictions on importing raw materials through ports and sea routes; on the other, they suffer from the damage caused by FX instability, import restrictions, internet outages (impacting financial transfers and order registration), customs clearance issues, instability in export/import regulations, and other FX limitations such as non-allocation of funds and the blocking of order registrations.”

2. Liquidity Traps and the Working Capital Crisis:

When a manufacturer cannot predict when or at what rate their required FX will be provided, they are forced to lock their Rial liquidity in allocation queues for months. This means capital that should be deployed for development or marketing instead stagnates in blocked accounts.

3. Erosion of Bargaining Power with Suppliers:

One of our greatest structural challenges in Iran is the weakness of domestic suppliers. Due to these same fluctuations and liquidity shortages, they lack the capacity to modernize equipment or maintain quality standards (such as sourcing transparency). When a manufacturer cannot pay a supplier on time, or a supplier cannot import their own raw materials, the entire supply chain becomes fragile. This leads to “single-sourcing,” where the exit of competitors creates monopolies and allows the few remaining suppliers to impose irrational pricing.

The Domino Effect: From Production Halts to Negative Margins

Unlike many developed economies, inflation in Iran is not merely demand-pull; it is directly transmitted to domestic prices through exchange rates and balance sheet constraints.

When the supply chain is disrupted, the cost of production rises sharply. However, at this juncture, regulators intervene with pricing controls. The manufacturer procures raw materials at free-market rates or at an extremely high cost of capital, yet is forced to sell the final product at a regulated low price. In the May 2026 PMI report, the input price index was 92.4, while the output price index was only 78.1. This gap means companies cannot pass their costs on to the consumer, leading to a rapid erosion of profit margins.

How Can Business Leaders Respond?

In such an ecosystem, classical supply chain models (such as Just-in-Time) are practically obsolete; “forecasting” becomes the primary key to survival. Managers must maintain a “macro view” and avoid being deceived by short-term stability in exchange rates. For companies—especially those whose fiscal years end in December—it is essential to factor in the surge in labor and raw material costs during the budgeting process.

Furthermore, one must beware of regulatory traps. For example, suppose your company's turnover is calculated at €100 million at the start of the year; the protracted process of obtaining transfer permits and allocation, combined with the depreciation of the Rial, may cause the real value of that revenue to plummet to €50 million by the time funds are accessible. Similarly, the solution of "importing via the export earnings of others" carries significant practical challenges; heavy transfer fees and the presence of multiple intermediaries often mean that the FX reaching the manufacturer ends up being more expensive than the free-market rate.

In response to these pressures to preserve income, many organizations resort to the most immediate strategy: cost-cutting. Marketing budgets and Human Resources training are often the first victims of this financial contraction. However, this is a fatal error; in the medium term, it leads to a loss of market dynamism, a decline in specialized skills, and a severe reduction in the company's competitive edge.

Ultimately, Iran's currency crisis is not a simple financial variable; it is a systemic risk. Survival requires moving beyond a purely financial perspective and building negotiation and analytical capacities at the highest levels of Communications & Corporate Affairs. Managers must accept that in Iran, inventory management and pricing strategies are inextricably linked to "currency diplomacy" and a sophisticated understanding of political economy. Therefore, the primary challenge is not the volatility itself, but the inability to plan amidst volatility—a state that turns every currency shock from a mere price change into a crisis for production and business continuity.

