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# Banking Strategies to Neutralize Inflationary Shocks Arising from Sanctions

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**A B S T R A C T**

International sanctions have imposed significant inflationary pressures on Iran's economy through various mechanisms, including reduction of foreign exchange revenues, disruption of foreign trade, and restricted access to global payment systems. This study aims to elucidate the banking system's strategies for mitigating the inflationary effects of sanctions. Employing a descriptive-analytical research method and reviewing library resources, this article analyzes operational measures that banks can adopt to counteract the inflationary impacts of sanctions. Findings indicate that although sanctions have exacerbated inflation in Iran's economy through multiple channels, appropriate banking strategies—including liquidity management, revision of credit policies, and deployment of innovative financial instruments—can effectively mitigate these effects. This article presents practical solutions for enhancing the banking system's performance under sanctions.

**Keywords**

Sanctions, Inflation, Banking System, Banking Strategies, Inflationary Shock

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# Introduction

In recent decades, international sanctions have been utilized as an effective instrument in global relations to exert pressure on nations. The Iranian economy, as a developing economy, has been consistently subjected to various forms of international sanctions over the past four decades. These sanctions, imposed unilaterally, multilaterally, and through international organizations, have had profound impacts on the country's macroeconomic variables.

Inflationary shocks resulting from sanctions are among the most significant challenges facing the Iranian economy. Financial and banking sanctions, by restricting access to international payment systems, creating obstacles in financial transfers, and blocking foreign assets, have directly impacted the inflation rate. On the other hand, oil sanctions, by reducing the country's foreign exchange revenues, have affected the value of the national currency and thereby fueled an increase in the inflation rate.

The national banking system plays a dual role in this context. On one hand, it is itself affected by the sanctions and has faced numerous challenges in conducting international banking operations. On the other hand, the banking system can, by adopting appropriate strategies, contribute significantly to reducing the inflationary effects of sanctions. In this regard, identifying and analyzing effective strategies for neutralizing the inflationary shock arising from sanctions is of particular importance.

The present study aims to analyze the strategies of the banking system for neutralizing the inflationary shock caused by sanctions. Accordingly, this research seeks to answer the fundamental question: How can the Iranian banking system, through the adoption of appropriate strategies, reduce the inflationary effects of international sanctions? To address this question, the following objectives are pursued:

First, to elucidate the mechanisms through which international sanctions affect the inflation rate in the Iranian economy; Second, to identify the challenges facing the banking system under sanctions; Third, to propose operational strategies for the banking system to neutralize the inflationary effects of sanctions.

Methodologically, this research is based on a descriptive-analytical method and has been conducted using library resources, including books, scientific articles, research reports, and authoritative documents. Data collection was performed through documentary methods and qualitative content analysis.

This article is structured into five sections. Following the introduction, the second section reviews the theoretical foundations of the research. The third section is dedicated to analyzing the challenges of the banking system under sanctions. The fourth section discusses banking strategies for neutralizing the inflationary shock, and finally, the fifth section presents conclusions and recommendations.

## Theoretical Foundations and Research Background

### The Concept of Sanctions and Their Typology in Economic Literature

International sanctions have long been employed as instruments of economic, political, and diplomatic pressure in international relations. From the perspective of international law, sanctions are defined as collective or individual coercive measures imposed by states or international organizations against a target country with the aim of compelling it to change its behavior.

In economic literature, sanctions can be classified from various aspects. Based on the imposing entity, sanctions are divided into three categories: unilateral, multilateral, and those by international organizations. Unilateral sanctions are typically imposed by one state against another, whereas multilateral sanctions are imposed by a group of states, and sanctions by international organizations are imposed by entities such as the United Nations.

Based on the scope of application, sanctions are divided into primary and secondary categories. Primary sanctions govern the direct relations between the sanctioning state and the target state, while secondary sanctions involve restrictions against third-party countries that have economic relations with the target country.

**Mechanisms of Sanctions' Impact on Inflation**

International sanctions impact the inflation rate through several mechanisms. The first and most important mechanism is the reduction of foreign exchange revenues resulting from restrictions on oil and other commodity exports. This reduction in foreign exchange earnings leads to the depreciation of the national currency, which in turn causes an increase in the prices of imported goods and production inputs.

The second mechanism involves the disruption of the supply chain and restrictions on the import of essential and intermediate goods, leading to reduced supply and increased prices. The third mechanism is restricted access to international payment systems, which increases transaction costs and reduces the efficiency of the banking system in meeting foreign exchange demands.

The fourth mechanism entails creating instability in financial markets and increasing economic uncertainty, which reduces investment and output, ultimately leading to increased inflationary pressures. Numerous studies indicate that these mechanisms often operate in combination, having mutually reinforcing effects.

**Research Background**

Numerous studies have been conducted concerning the impact of sanctions on the Iranian economy. Bagheri (2015), in a study examining the impact of economic sanctions on the employment level in Iran, demonstrated that sanctions have increased unemployment through reduced production and investment.

Soltani and Ramezani Nejad (2018), in a study investigating the effects of sanctions on bank guarantee payments, found that banking sanctions have disrupted the international payment system and increased transaction costs.

Ghazavi Khorasgani and Mohammadi (2015), in research titled "The Model for Managing Challenges of the Islamic Republic of Iran's Banking System under Sanctions," proposed solutions for addressing the challenges of the banking system under sanctions. This research emphasized the necessity of reforming the banking system's structure and enhancing its resilience to external shocks.

Voldan Zarghani (2018), in a study examining the impact of oil and gas industry sanctions on the country's macroeconomic variables, demonstrated that oil sanctions have had a significant effect on foreign exchange earnings and the inflation rate.

**Theoretical Framework of the Research**

This research employs a combined theoretical framework encompassing theories of economic sanctions, inflation theories, and banking system theories. In the sanctions section, the theory of Hufbauer and Schott (1990), which analyzes sanctions as instruments of economic pressure, is utilized.

In the inflation section, monetary theories of inflation as well as structural theories of inflation are drawn upon. In the banking system section, theories related to financial intermediation and the stabilizing role of banks are used.

This theoretical framework assists the present research in systematically analyzing banking strategies for neutralizing the inflationary shock arising from sanctions.

**Challenges of the Banking System under Sanctions**

The Iranian banking system, in confronting international sanctions, despite its significant capacities and capabilities, has faced obstacles and limitations. These challenges primarily stem from the particular conditions governing the international economy and certain domestic exigencies, requiring intelligent policymaking and precise planning.

One important issue in this context is the necessity for banks to focus more on specialized banking activities. Given the pivotal role of the banking system in financing various economic sectors, focusing on core functions can lead to enhanced efficiency and effectiveness of this system under the current complex conditions. This approach, while maintaining the stability of the banking system, will significantly contribute to the continued provision of quality services to all segments of society and economic actors.

In the realm of monetary policy, the relevant authorities, considering various economic considerations and relying on their valuable experiences, have consistently taken steps towards adopting appropriate and timely decisions. The continuation of this trend, utilizing expert opinions and meticulous studies, can be effective in improving economic indicators.

The development and deepening of financial markets is another area that has witnessed good progress in recent years. The expansion of innovative financial instruments and diversification of financing methods are among the positive measures undertaken within the framework of the system's general policies, creating significant capacities for the country's economic system.

In the domain of international transactions, the country's banking system, by employing innovative methods and utilizing existing capacities, has taken effective steps towards facilitating commercial exchanges. These efforts, under the current specific conditions, demonstrate the intelligence and capability of the relevant officials in maintaining economic relations with the outside world.

The country's banking supervisory system, relying on valuable experience and utilizing advanced standards, has consistently worked towards enhancing the health and stability of the banking system. Strengthening this supervisory system within the framework of promulgated policies and observing technical considerations is among the important priorities in this field.

Overall, the country's banking system, endowed with a rich Islamic-Iranian heritage and utilizing valuable experiences, possesses the necessary capacity to intelligently confront the existing challenges. Continued movement along the path of structural reforms and utilization of domestic capacities can play a significant role in enhancing the efficiency of this system under current conditions.

**Banking System Strategies for Neutralizing the Inflationary Shock Arising from Sanctions**

In facing the challenges arising from international sanctions, the national banking system can play an effective role in reducing the inflationary effects of these sanctions by employing intelligent and planned strategies. These strategies can be designed and implemented at various levels and can significantly contribute to strengthening the resilience of the national economy.

**Development and Strengthening of Innovative International Payment Instruments**

One fundamental strategy in this field is the development of alternative and regional payment systems. The banking system can reduce dependence on international payment systems by establishing and strengthening bilateral and multilateral payment systems with neighboring countries and trading partners. This can be achieved through concluding bilateral monetary agreements, establishing regional clearinghouse systems, and promoting the use of national currencies in commercial exchanges.

**Improvement of Liquidity Management and Monetary Policy**

Another important strategy is enhancing the quality of liquidity management within the banking system. This requires strengthening supervisory mechanisms, improving information systems, and consolidating monetary policy frameworks. The Central Bank can increase the efficiency of monetary policies and thereby act more successfully in controlling inflation by employing innovative monetary instruments and developing the interbank market.

**Development of Capital Markets and Diversification of Financial Instruments**

The development and deepening of capital markets as a complement to the banking system is another effective strategy for reducing inflationary pressures. By developing the debt market, expanding Islamic financial instruments, and diversifying financing methods, the pressure on the banking system can be reduced, thereby assisting in controlling liquidity growth.

**Enhancement of Banking System Efficiency**

Improving the operational efficiency of banks through the development of financial technologies, restructuring the banking network, and reforming internal processes can lead to reduced operational costs and consequently lessen cost-push pressures on the economy. This is achieved particularly through the expansion of electronic banking, harmonization of systems, and mechanization of processes.

**Strengthening Banking Supervision and Risk Management**

Establishing an effective supervisory system and integrated management of banking risks is essential for countering the effects of sanctions. This includes continuous monitoring of asset quality, controlling credit growth, and ongoing surveillance of operational and market risks.

**Development of Regional and International Cooperation**

Strengthening cooperation with regional and international financial and banking institutions, even under sanctions, can help reduce the negative effects of restrictions. This cooperation can take the form of membership in regional financial institutions, development of relations with neighboring banks, and participation in regional development projects.

**Support for Production and Exports**

The banking system can provide support to productive and export sectors against the consequences of sanctions by formulating and implementing targeted credit programs. This support includes granting priority foreign exchange facilities to exporters, expanding export credit insurance coverage, and establishing export guarantee funds.

**Foreign Exchange Market Management**

The formulation and implementation of intelligent policies in managing the foreign exchange market are among the key strategies for controlling inflation. This is achieved through diversifying foreign exchange sources, developing foreign exchange supply mechanisms, and the sound management of foreign exchange reserves.

**Development of the Digital Economy and FinTech**

Supporting the development of the digital economy and innovative financial technologies can help create new economic capacities and reduce dependence on oil revenues. The banking system can take steps in this direction by developing digital financial services, facilitating financial circulation in the virtual space, and supporting FinTech startups.

**Training and Human Resource Development**

Finally, investment in training and developing specialized human resources in the fields of international banking and financial management is considered an essential foundation for the successful implementation of the aforementioned strategies.

The successful implementation of these strategies requires national resolve, inter-sectoral coordination, and comprehensive support for the country's banking system. By employing these measures, the banking system can play a significant role in reducing the vulnerability of the national economy to sanctions and controlling inflation.

**Implementation and Prerequisites of Banking Strategies under Sanctions**

The successful implementation of banking strategies to neutralize the inflationary shock arising from sanctions requires the provision of necessary infrastructures and prerequisites, without which achieving the intended objectives will face serious challenges. These requirements can be examined in various dimensions.

**Supervisory Mechanisms and Inter-Sectoral Coordination**

Establishing an integrated and coordinated supervisory system among various financial and economic institutions is one of the most fundamental prerequisites for implementing banking strategies. This coordination must be established between the Central Bank, the Ministry of Economic Affairs and Finance, the Plan and Budget Organization, and other related institutions. Forming joint specialized working groups and designing coordinated supervisory mechanisms can significantly contribute to the coherent implementation of strategies.

**Development of Information and Communication Technology Infrastructure**

Upgrading the technical and technological infrastructure of the banking system is another essential requirement for implementing strategies to counter sanctions. This includes expanding secure data centers, upgrading electronic payment systems, creating secure communication networks, and deploying advanced supervisory systems. Investment in this field not only enhances the efficiency of the banking system but also ensures the security of financial transactions.

**Human Resource Empowerment and Development of Specialized Skills**

Designing integrated and targeted training programs to enhance the knowledge and skill levels of banking system personnel is a necessity for the successful implementation of strategies. Holding specialized training courses in international banking, risk management, financial technology, and sanctions regulations can provide the necessary capabilities to face existing challenges.

**Securing Financial Resources and Formulating Support Packages**

The provision of sufficient financial resources and the design of targeted support packages are fundamental prerequisites for implementing banking strategies. This includes securing the necessary Rial and foreign exchange resources, establishing market stabilization funds, and formulating incentive packages for banks that pioneer the implementation of strategies.

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**Reform of Banking Laws and Regulations**

Reviewing and updating banking laws and regulations in light of the special circumstances of sanctions is an undeniable necessity. This includes streamlining banking processes, introducing flexibility into supervisory regulations, and creating legal frameworks for developing banking relations with neighboring countries.

**Formulation of Contingency Plans and Crisis Management**

Designing operational plans for various scenarios and establishing crisis management systems are other important requirements in this field. These plans must anticipate various sanctions scenarios and provide operational solutions for each.

The successful implementation of these prerequisites requires national resolve, intelligent management, and comprehensive cooperation among various governmental institutions. By providing these foundations, the country's banking system can effectively fulfill its role as a stabilizing pillar in the national economy under difficult sanctions conditions.

**The Role of the Central Bank in Coordinating Strategies to Counter Sanctions**

The Central Bank, as the core of the country's monetary and credit system, plays a vital role in organizing and coordinating strategies to counter the effects of sanctions. This institution, by utilizing diverse policy tools and relying on its legal authority, can pave the way for the effective implementation of designed strategies.

**Monetary Policy and Inflation Control**

The Central Bank can employ innovative monetary policy instruments to control inflation arising from sanctions. Setting appropriate interest rates, managing liquidity, and using open market operations can help stabilize the money market and control price growth. Furthermore, monitoring macroeconomic indicators and making timely monetary decisions are other important duties of this institution under sanctions.

**Supervision of the Banking Network and Enhancement of Financial Soundness**

Establishing an efficient supervisory system over the performance of banks and credit institutions is another crucial function of the Central Bank. This supervision should encompass the continuous monitoring of bank health indicators, oversight of asset quality, and evaluation of risk management. Additionally, enacting preventive regulations and monitoring their implementation can enhance the stability of the banking network against external pressures.

**Regulation of the Foreign Exchange Market and Reserve Management**

Intelligent management of the foreign exchange market and the formulation of foreign exchange policies under sanctions are particularly sensitive. The Central Bank can help reduce market volatility and control the inflationary effects of sanctions by adopting efficient policies for foreign exchange allocation, creating market balance, and managing foreign exchange reserves.

**Development of International and Regional Cooperation**

The Central Bank can take steps to mitigate the effects of sanctions by developing relations with international and regional monetary and financial institutions. Participation in international forums, concluding bilateral and multilateral memoranda of understanding, and enhancing cooperation with central banks of neighboring countries are among the effective measures in this regard.

**Monitoring and Analysis of Sanctions Impacts**

By establishing a specialized secretariat for the continuous monitoring of the effects of sanctions on the country's economic and banking system, the Central Bank can consistently observe developments and implement appropriate solutions in a timely manner. This requires the creation of intelligent monitoring systems and the utilization of expert opinions.

**Coordination with Other Governmental Institutions**

The Central Bank must establish coordination mechanisms with other governmental institutions, including the Judiciary, the Ministry of Foreign Affairs, and the Ministry of Intelligence, to take integrated action against sanctions. This coordination can assist in making measured decisions and implementing coherent cross-sectoral strategies.

**Supervisory Mechanisms and Performance Evaluation**

Establishing an efficient and systematic supervisory mechanism for the continuous monitoring of the implementation of strategies to counter sanctions is an undeniable necessity in this field. This mechanism must be capable of measuring the progress of strategy implementation and the achievement of predetermined objectives using quantitative and qualitative indicators.

The design and implementation of an intelligent monitoring system capable of continuously and online tracking key performance indicators and issuing necessary warnings is among the fundamental actions in this area. This system must be able to collect and analyze data related to economic developments, inflation rates, foreign exchange rate fluctuations, and other macroeconomic variables.

Formulating a periodic and transparent reporting system is another requirement for effective supervision over strategy implementation. These reports must regularly and at specified intervals transparently reflect the status of strategy implementation, challenges faced, and achievements obtained.

Holding periodic meetings with the participation of all stakeholders and executive officials of the strategies provides the opportunity for exchanging views, removing obstacles, and enhancing coordination for advancing objectives. These meetings can be held monthly or quarterly with the participation of representatives from the Central Bank, the Ministry of Economic Affairs and Finance, and other related institutions.

Establishing a system for feedback and continuous revision of strategies based on the findings of the monitoring and evaluation system is another important requirement in this field. This system must be able to identify the strengths and weaknesses in the implementation of strategies and provide necessary suggestions for their continuous modification and improvement.

Finally, creating an integrated database of successful and unsuccessful experiences in confronting sanctions can serve as a resource for designing and implementing future strategies. This database should encompass various case studies, lessons learned, and best practices in this field.

## Conclusion and Recommendations

International sanctions, as one of the most significant challenges for the Iranian economy in recent decades, have profoundly impacted macroeconomic variables, especially the inflation rate. This research, by examining the strategies of the banking system for neutralizing the inflationary shock arising from sanctions, concluded that the country's banking system, despite all limitations and challenges, possesses significant capacities for reducing the inflationary effects of sanctions.

The findings of this research indicate that the successful implementation of banking strategies under sanctions necessitates the provision of essential foundations and prerequisites. The most important of these include establishing an integrated supervisory system, developing technological infrastructure, empowering human resources, securing sufficient financial resources, reforming banking laws and regulations, and formulating contingency plans and crisis management.

The Central Bank, as the core of the country's monetary and credit system, plays a vital role in organizing and coordinating strategies to counter the effects of sanctions. This institution, by utilizing diverse policy tools and relying on its legal authority, can pave the way for the effective implementation of designed strategies.

## Recommendations:

Based on the findings of this research, the following recommendations are offered:

1. Design and establish an integrated sanctions monitoring system within the Central Bank.
2. Develop and strengthen alternative and regional payment systems.
3. Establish a special fund for financing sanctions countermeasure projects.
4. Formulate a national training program for enhancing sanctions countermeasure skills.
5. Establish a system for continuous monitoring and evaluation of sanctions countermeasure strategies.

The implementation of these recommendations within the framework of a comprehensive and coherent program can significantly enhance the capability of the country's banking system in managing inflationary shocks arising from sanctions. This requires national resolve, inter-sectoral cooperation, and comprehensive support for the country's banking system.

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