Real Interest Rate Differential and State Capacity: Russia, Iran, and the Limits of Governance

Abdulqasem Bakhshi

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Introduction

The Real Interest Rate Differential (Real IRD) provides a quantitative measure of a country's real economic return relative to others. Beyond conventional economic indicators, the Real IRD captures a state's capacity to mobilize resources, sustain governance, and maintain military engagement. Historical and contemporary evidence demonstrates that positive Real IRDs support strategic autonomy, while negative Real IRDs constrain operational and institutional capacity.

Russia: Economic Resilience Enables Sustained Military Engagement

Current Real IRD data for Russia highlights a significant advantage relative to key economies:

- **Russia vs EU:** +9.85
- **Russia vs US:** +8.60
- **Russia vs Israel:** +8.05

Despite the ongoing Ukraine war and international sanctions, Russia's positive Real IRDs indicate the economy remains capable of sustaining prolonged military operations. This aligns with the broader strategic dynamics outlined in Managing Asymmetry: Poland, where frontline states maintain operational independence and absorb localized risk while leveraging economic and structural resilience. Russia's ability to convert its economic capacity into strategic action demonstrates that successful management of national finances is central to sustaining protracted conflict.

Iran: Economic Strain and Institutional Fragility

In contrast, Iran faces severe economic constraints:

- **Iran vs EU:** -25.65
- **Iran vs US:** -26.90
- **Iran vs Israel:** -27.45

These figures mark the worst Real Real IRD levels since 2013, with a clear deterioration beginning in Q4 2018. Past periods of positive Real IRD, such as 2013–2018 under the JCPOA, coincided with economic stability, improved international relations, and enhanced domestic legitimacy. The current negative trajectory underscores the consequences of mismanagement and the re-imposition of sanctions.

As noted in IRGC, Iranian Identity, and the Prospects of a Sassanian Revival, Iran's historical challenge has been the persistent mismatch between governance and cultural continuity. Past regimes—from the Safavids to the Pahlavis—oscillated between ideology, external validation, and institutional fragility. Contemporary governance, heavily influenced by clerical authority, privileges ideological primacy over national integration. This raises a critical structural question: as clerical authority faces pressure from economic collapse and domestic discontent, which institution is positioned to inherit effective power?

Institutional Dynamics and Strategic Risk

The IRGC represents the principal institutional actor capable of assuming systemic authority in a post-clerical scenario. If it manages to prioritize national stability over defense of ideological clerical interests, Iran could gradually restore economic management, rebuild legitimacy, and avoid fragmentation. However, failure to do so—continuing to defend clerical prerogatives without addressing economic collapse—risks a trajectory toward internal disintegration, where radical Islamist actors such as ISIS or Taliban-style movements could exploit power vacuums.

This scenario mirrors historical lessons drawn from Afghanistan (Regime Collapse, Institutional Continuity, and the Risk of Fragmentation) and Ideology, Power, and the Persistence of Radical Islamism: economic weakness amplifies the influence of non-state actors, while poorly managed governance can precipitate systemic collapse.

The Role of U.S. Policy and International Alignment

Unlike Afghanistan, the U.S. has no strategic interest in regime change in Iran if the state demonstrates responsible governance. Cooperative engagement with Israel and other regional actors is feasible if Iran prioritizes coexistence over absolutist ideology. Nevertheless, negative Real IRD trends signal that Iran's capacity to sustain economic autonomy and institutional integrity is under severe pressure. President Pezeshkian's recent appeal for dialogue, and the Central Bank head's resignation in December 2025, reflect recognition of the urgent need for reform.

Implications for Strategic Stability

The Real IRD provides a predictive lens:

- **Positive Real IRD (Russia)** → Enables sustained conflict, operational autonomy, and resilience to external pressure.
- **Negative Real IRD (Iran)** → Constrains capacity, increases the probability of internal fragmentation, and amplifies the risk of radicalization.

Historical experience demonstrates that Iran is not facing a simple choice between regime continuity and regime change. Rather, success depends on structural adaptation: the IRGC must act as a stabilizing proto-state, economic reforms must be implemented, and governance must integrate national identity and institutional capacity (IRGC, Iranian Identity, and the Prospects of a Sassanian Revival). Failure to address these dynamics could trigger cascading consequences across multiple orders, potentially forcing external intervention.

Conclusion

The Real IRD provides a predictive framework linking economics, war sustainability, and strategic programs like nuclear development. Russia's positive Real IRD enables continued military engagement, while Iran's negative Real IRD reveals structural vulnerabilities, constrained capacity for nuclear management, and risks of internal fragmentation. Integrating insights from Power, Knowledge, and Nuclear Proliferation underscores that economic health, institutional capacity, and strategic prudence are inseparable: Iran's survival and regional stability depend on coherent economic reform, balanced institutional leadership, and careful engagement with global and regional actors.

Appendix: Figures

Figure 1: Real Interest Rate Differential of Selected States: Indicators of War Sustainability and Risk of Internal Fragmentation.

The IRD highlights divergent economic resilience: Russia maintains positive differentials supporting sustained conflict, while Iran's negative differentials indicate economic strain, institutional stress, and heightened risk of fragmentation.