

Assessing the Investment Climate in Iran

An Overview of the Political, Economic, Legal and Social Conditions

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Welcome Note

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Overview

- Significant economic potential from foreign investment and opportunities are limitless.
 - The impression of a 'gold rush' immediately after the lifting of nuclear-related sanctions in 2015 seems to have dampened. Investors are gradually realizing that entering the Iranian market, especially the energy sector, is not as easy as originally thought because of a combination of factors including the political risk.
 - In order to make a learned decision, any investor needs a comprehensive understanding of different variables that will affect the risk-reward balance, including: political condition (internally and externally), economic challenges, legal dimensions, and social aspect.
- contradictory statements. He also said that Iran was on its last leg economically, but this is far from the truth.
- Unclear what Trump's attitude towards Iran is but the attitude of his advisors is. General Mattis ("Mad dog Mattis") has expressed suspicion of Iran as a malign influence on the region many times. The Foreign Affairs advisor and Mr. Pompeo, Central Intelligence Agency (CIA) director, has also given a negative view on Iran.
 - Iranians have remained calm, despite the expectations.
 - It would be a huge mistake if the deal is torn up. It may not be a perfect deal, but most experts agree that it does cut off nuclear route for Iran. Some say the agreement is too short lasting only for 15 years, but that is enough to improve the relationship with Iran, and some provisions last to 2026 or 2041. Declaration treaty says that Iran will remain committed to the Non-Proliferation Treaty (NPT). The International Atomic Energy Agency (IAEA) will acquire a lot of understanding of what is going on in Iran.
 - Though Saudis/Israelis are critical of the deal, reports say that Israel has changed its mind (Mossad declared that it is much better to have the agreement in place). The best cause of action for the West is to make the agreement work.

Political conditions

- It could not have been a better time (or worse time): very serious moment in the relations between the West and Iran.
- Trump's attitude towards Iran during the elections: Joint Comprehensive Plan of Agreement (JCPOA) was a lousy deal, and must be torn up. But there were also

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- Iran has complied with its obligations under the agreement. Before the agreement, Iran had enough uranium to build 10 bombs, today it has none.
 - Iran has kept its side of the bargain and complied, but the Iranians consider that the West has not fulfilled its part of the contract. The US has retained primary sanctions that everyone knew at the time but did not see the consequences: finance (process payments with Iran) which international banks are terrified of doing; they are frightened of spill-over effect of US sanctions. Companies won't have access to banking facilities. The Iranian embassy in London does not even have a bank account to pay its bills.
 - The Obama administration tried to help by clarifying the rules under which some banks are infringing sanctions, but such assistance is unlikely to continue.
 - At the time the deal was signed, there was tremendous enthusiasm in Iran (moderates of President Rouhani) but now the country feels double-crossed, and re-election of president Rouhani must be in doubt because of the non-implementation of the deal from the West's side.
 - The recent missile test is of complete irrelevance, magnified beyond of what is reasonable. From a legal point of view, sanctions were not broken. Iranians regard their ability to test missile as a red line, after their experience with the Iraq war, where Iran was subject to missile attacks from Iraq, and had to buy missile from the open market. Saudi Arabia and the UAE have a missile arsenal.
 - The idea that Iran is trying to interfere negatively with its neighboring countries, and reshape the Middle East in its own image, has been deeply embedded in our mind. The real cause for the Shia unrest in Bahrain is not because of Iran but because of how the Shias are treated in Bahrain.
 - The benefits of the JCPOA are not materialising for the Iranians. There's a fear of confrontation and miscalculations. It is a tricky time if the US tears up the agreement. Europe may go on its own and should try to preserve trade.
- ### Economic conditions
- Iran's economic performance has been improving since the entry into force of the JCPOA: faltered post tightening of sanctions then rebound in oil production and exports (pre-2009 level).
 - Economic growth is driven mostly by the oil sector, and has recovered from 0.4% year-on-year (y/y) in Fiscal Year (FY) 2015/2016.
 - Gross Domestic Product (GDP) growth reached 7.4% y/y in the first half of FY 2015/2016. Non-oil sector: positive growth (2.5%) in second quarter of 2016 after it has been contracting for the last three years. This recovery is important as it created jobs.
 - Ministry of Economy announced it is expecting 6.2% growth and around 9% inflation, in the next fiscal year (end of March).
 - Inflation has fallen sharply and is now hovering around 8.6% y/y, though recent currency depreciation could add to inflationary pressures in the coming months.
 - Iran has been able to cope with episodes of prolonged low oil prices, adjusting its fiscal spending downwards in line with falling oil revenues and keeping its deficits manageable (less than 2% of GDP), while total government debt remains below 16% of GDP and external debt in the low single digits as a percentage of GDP - much lower than other oil exporters in the region (Saudi Arabia 11% and 14% in Oman). Iran is better equipped to deal with its macro, external and domestic challenges than its neighbours.
 - One of the key challenges for the authorities is to create jobs for its young Iranians (<30 yrs old), which account for more than 60% of the total population. The unemployment rate remains at around 11%, but youth unemployment is close to 30% (according to the ILO), similarly to Saudi Arabia, but better than Egypt (42%). For that, raising investment levels is critical.
 - The outlook for the economy in the short to medium term depends on four key factors:
 - First, the oil trajectory for oil prices which is clouded by risks to the OPEC agreement, the energy policy of the new US administration, and the expected increase in shale oil supply as well as the intensity and speed of market re-balancing.
 - Second, the prospects for continued trade and financial sanctions relief which started last year and which look increasingly at risk. Risk of reversal can significantly impact Iran's ambitions to bring billions of dollars of investment into its oil and non- oil sectors.
 - Third, the domestic resolve to pursue aggressive structural reforms needed to improve the business environment and unlock Iran's growth potential, particularly financial sector reforms, improvement in corporate governance and modernisation of infrastructure. Iran scores low on international competitiveness.
 - Fourth, progress on Iran's geo-economic ambitions to deepen trade and investment integration with its Eastern partners in Asia (Free

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Trade Agreements (FTAs) with Commonwealth of Independent States (CIS); the International North-South Transport Corridor; the expansion of the Chabahar port with support from India; China's One Belt, One Road agenda...). Trade patterns shifted in 10 years; more balanced between Asia and West with China dominating exports and imports.

Sanctions

- One year after the nuclear deal we are still talking about the sanctions. Still a lot of misunderstanding of what sanctions allow you to do or not.
- Under Obama Office of Foreign Assets Control (OFAC): more open to given guidance to non-US business to do business in Iran: now open to question.
- 'Reasonable effort in commercial due diligence to find a real owner of the business' so rules are helpful but the problem is when potential investors do the due diligence work but do not keep the evidence.
- **European sanctions:**
 - Iran is generally open for business for Europeans subject to prohibition on:
 - Dealing with Iranian proscribed entities and individuals;
 - Supply of military related services and products.
 - UK compiled Iran list during the sanction period; it has not been updated since October 2015 and needs clarity from the UK government.
- **US sanctions:**
 - Generally, no US person may do business with Iran – this includes foreign nationals when in the US.
 - Under General Licence H, foreign subsidiaries of US parent companies may do business in Iran provided there is no US involvement in the business.
 - Wide prohibitions on supplying US goods and technology to Iran.
 - The US financial system cannot be used for Iran business which generally means no US dollar payments.
- **Localisation** is a very strong underlying theme to Iran's expectation of foreign investors.
 - IOCs signing the new IPC (Iran Petroleum Contract) will be required to joint venture with a pre-qualified local partner.
 - Under the Iran Tender Process Act and the Iran Maximisation of Local Content Act, there are clear requirements under state contracts to source local

goods and services and for preference to be given to local suppliers where available. This is reflected contractually in the IPC.

- Similarly, there will be stringent requirements in the IPC to train local work force and share technical know-how.
- High youth unemployment in Iran leading to high level of local content (partnering with and sourcing from an Iranian entity in any sector).
- It is important that any foreign investor understands and has a clear plan as to how to comply with these rules and source from the Iran market to give it a competitive advantage.

Cultural considerations when doing business in Iran

- Religion, culture and history are intertwined and important in the Iran business environment, some examples include:
 - **Tarof** – the Iranian custom of politely denying your will to please your counterpart i.e. fighting over who pays for the bill at a restaurant.
 - **Understanding Iran's history and politics** – a basic level of understanding of recent politics can be helpful to understand Iran's international commercial strategy and decision making. You may find this provides new opportunities for your business.
 - **Establishing relationship of trust** – a great pitch and proposal will not take you very far in Iran unless the Iranian's have developed a level of comfort in you on a personal level.
 - **Hospitality and gifts** – do not be surprised if you receive extravagant gifts at business meetings. Ensure that this is reciprocated to show how much you value the gesture and respect the relationship.

Practical considerations when doing business in Iran

- **Compliance** – highly advisable to understand your corporate policies on gifts (receiving and giving) and to understand the implications of Foreign Corruption Practices and other compliance-based legal requirements and restrictions.
- **Make sure your proposal/strategy is mutually beneficial** – Iranians understand the value of their economy to potential investors. They want to feel valued as a partner and as an equal.

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- **Negotiations take longer** – Iranian's are natural negotiators and will want to always achieve the best deal.
- **Plan your schedule thoroughly** – make business appointments 3-4 weeks in advance to show you respect their time and are dedicated to working with them.
- **Create Farsi business cards** – this not only shows that you have made the effort to develop relationships in Iran, it also shows that you frequently visit the market.
- **Local partner** – consider the benefits and legal requirements of having a local partner.

Access for Women in Energy (AccessWIE) aims to establish a community of practice, offering women a peer-group platform to meet with their contemporaries both female and male in the private and the public sectors across the world of energy.

The group engages its members in regular informed debates on global energy related issues and provides educational support to those who want to venture into new aspects of the energy industry or simply expand their knowledge. The group also provides energy experts a valuable networking platform and offers an opportunity for graduates to establish useful connections within the industry as they shape their careers and carry forward their own projects.

AccessWIE was founded in 2007 by Dr Carole Nakhle, who is the director of Crystal Energy. The group is co-chaired by Lady Judge (The Hon. Barbara Thomas), who also chairs the Pension Protection Fund, and Lord Howell, President of the Royal Commonwealth Society and of the UK Energy Industries Council.

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