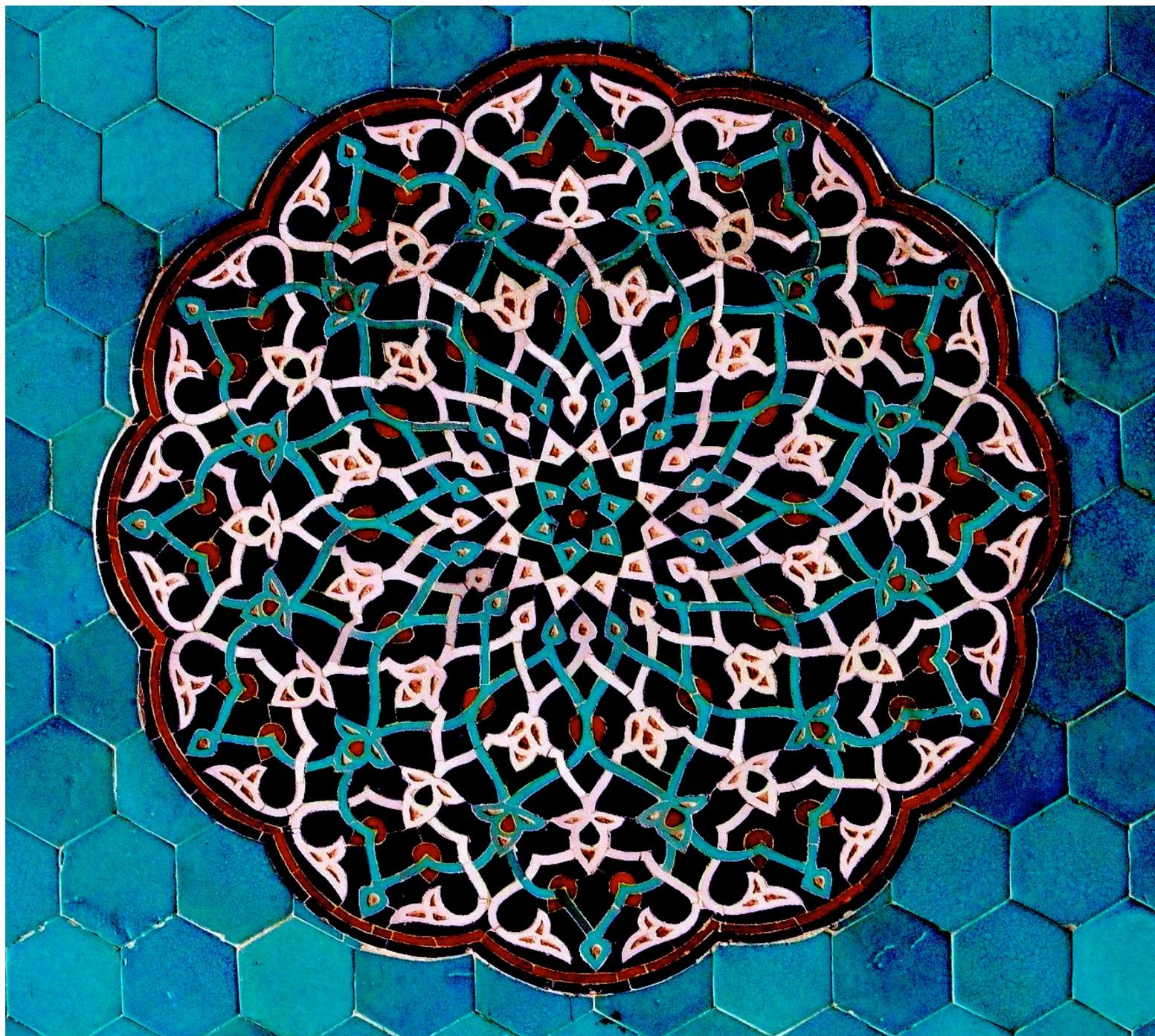


IRAN



COUNTRY RISK REPORT / JUNE 2019

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Acronyms

ARAMCO: Saudi Arabian Oil Company

Bcm: billion cubic meters

Bpd: barrels per day

BRI: One Belt, One Road Initiative

CNPC: Chinese National Petroleum Company

CPEC: Chinese-Pakistan Economic Corridor

EOR: Enhanced Oil Recovery techniques

EU: European Union

FDI: Foreign Direct Investment

GCC: Gulf Cooperation Council

Groupe PSA: Group Peugeot S.A.

HDI: Human Development Index

IEA: International Energy Agency

IKCO: Iran Khodro Company

Instex: Instrument in Support of Trade Exchanges

IOC: International Oil Company

IPC: Iran Petroleum Contract

IRGC: Islamic Revolutionary Guard Corps

JCPOA: Joint Comprehensive Plan of Action

LNG: Liquefied Natural Gas

Mbpd: million barrels per day

Mcm: million cubic meters

MENA: Middle East and North Africa

Mot: millions of tons of oil equivalent

MoU: Memorandum of Understanding

MPs: Members of Parliament

NICT: National Iranian Tanker Company

NIOC: National Iranian Oil Company

NLA: National Liberation Army in Libya

NOC: National Oil Company

NPT: Non-Proliferation Treaty

OPEC+ Agreement: Diplomatic agreement to reduce oil output among OPEC, Russia and other oil producers.

R&D: Research and Development

SAIPA: Société Anonyme Iranienne de Production Automobile Citroën

SMEs: Small and Medium Enterprises

SPV: Special Purpose Vehicle

SRE: significant Reduction Exception

SWIFT: Society for Worldwide Interbank Financial Telecommunication.

TANAP: Trans Anatolian Pipeline

TAP: Trans Adriatic Pipeline

TAPI: Turkmenistan-Afghanistan-Pakistan-India Pipeline

UN: United Nations

UNCTAD: United Nations Conference on Trade and Development

UNGA: United Nations General Assembly

UNSC: United Nations Security Council

US: United States

WTI: West Texas Intermediate barrel

Executive Summary

The US unilateral withdrawal from the JCPOA on May 8, 2018, reshaped the Iranian domestic and international reality. On the one hand, the JCPOA enabled Iran to increase its GDP above 7% in the period of 2016-2018, more than double its oil exports and maintained President Rouhani in office after the 2017 elections. On the other hand, the US reimposition of the previously lifted sanctions demonstrated the deep vulnerabilities of the Iranian economy and its huge diplomatic isolation.

US sanctions will affect the whole of Iran's foreign relations due to its extraterritorial nature. The EU will try to avoid its effect through legal protection of its companies and citizens with mechanisms such as the SPV, whose scope and effectivity is yet to be proved. China, as it is less exposed to the US financial and political influence, will be able to better circumvent sanctions but still far from being totally unaffected. Other countries such as India, Turkey or Russia will find difficulties to handle secondary sanctions, but will be able to maintain a certain degree of trade with the Islamic Republic. Japan or South Korea will have to follow US demands because of its strategic alliance in the Asia-Pacific region and resume energy imports and investments.

The Iranian economy is expected to enter into recession during 2019, GDP growth is expected to be -4.5% and unemployment rate will increase to the 15.4%. This economic hardship will concentrate the political debate in the 2020 legislative and 2021 presidential elections, whose result will determine if a moderate or hardliner political faction seizes power. Social unrest from ethnic minorities and opposition is expected to rise if the economic conditions do not improve, challenging the current political equilibrium of the country.

The energy sector will be deeply affected by US sanctions as it banned all countries from investing and purchasing Iran's energy products. Sanctions are expected to reduce Iran oil exports to 1million barrels a day from the 2017 levels of 2.4 mbdp, decreasing governmental revenues drastically and freezing most foreign investments. The lack of FDI and technology will aggravate the problems of the Iranian energy sector with possible irreversible effects depending on the sanctions duration.

US-Iran relations are expected to worsen at least until the US 2020 Presidential elections, when a more dialoguing candidate could substitute the hawkish Trump administration. The United States is expected to maintain its current strategic alliances with Saudi Arabia and Israel, whose common goal of pressuring Iran can have unexpected consequences for the Middle East. Domestic politics in Iran, US, Israel and Saudi Arabia will play a major role in the evolution of the events.

IRAN

ISLAMIC REPUBLIC OF IRAN

Country Briefing



BASIC DATA

General characteristics

Official name: Islamic Republic of Iran

Surface: 1,745,150 Km²

Borders: to the North with Armenia, Azerbaijan, the Caspian Sea and Turkmenistan; to the East with Afghanistan and Pakistan; to the West with Turkey and Iraq and to the South with the Persian Gulf and the Gulf of Oman.

Language: Farsi or Persian is the official language. Furthermore, about the 25% of the population has a variety of Turkish as a mother tongue.

Currency: Iranian Rial.

GDP: \$439,51 billion (2017)

Religion: Islam is considered as the official religion under the current Constitution. The majority of Muslims in Iran are Shi'a.

Form of Government: The 1979 Constitution defines Iran as an Islamic Republic. The system is based in the distinction between an Executive headed by the President and composed by the different ministers and a Legislative elected by the Iranians. Above this republican reality seats the Supreme Leader, elected by the Experts Assembly. He is the expression of the principle of *velayat-e faqih* or Jurisconsult Government.

Administrative division: the country is divided in 5 regions and 31 provinces.

POLITICAL SITUATION

Internal politics

The arrival of Hassan Rouhani to the presidency of the country in August 2013 marked the beginning of a new era. The first and undisputed objective of the new executive was the economy. Since sanctions, with the notable decrease in oil revenues and the progressive international economic isolation, especially from the financial and banking systems, public accounts were placed in a difficult situation. At the same time, the productive apparatus had been affected by the shortage of goods and by the lack of a circuit of external payment systems. President Rouhani was re-elected for a period of 4 years with 57% of the votes in the first round on May 19, 2017.

His program was focused on the defence of the Nuclear Agreement (JCPOA) and on economic policy: creating jobs, improving the living conditions of those most in need, and specially seeking Iranian access to the international financial market, among others. Finally, after the announcement on 8 May 2018 by US President D. Trump to withdraw from the Nuclear Agreement (JCPOA), a new stage is opened which is not without difficulties for the Rouhani government. The EU-E3 plus China and Russia remain committed to the Agreement and Iran indicates it will remain in it if certain conditions are met.

Foreign policy

Since its inception in 1979, the foreign relations of the Islamic Republic of Iran have been marked first by an abrupt and radical rupture of the alliance of the Shah's regime with the United States, second by the indelible mark of the war between this country and Iraq (1980-1988) and, finally, by a difficult coexistence with many of its neighbours, added to the bad relations with the Western world. The signing of the JCPOA in 2015 was a historic milestone and a success of the diplomatic negotiation that must be preserved given that it is a key security issue, not only for Iran, but for the entire region.

1. EFFECTS OF SANCTIONS

- Iran won't comply with the reimposed US sanctions. The EU will try to find commercial and financial alternatives to circumvent US sanctions. China, Russia, Turkey and India are not cooperating with Washington, although China, Turkey and India have reduced their oil purchases.
- Global US leadership is in the spotlight. The EU, one of its strongest allies, is seeking for enforcing mechanisms to avoid its sanctions. China is likely becoming the main financial alternative for Iran.
- The economic consequences of the reimposed US sanctions will be highly dependent on what happens on the political arena. Economic forecasts are not easily predictable, however, they suggest that Iran, in 2019, is going to experience a -6% of GDP growth and its unemployment rate will increase from 13.9% (2018) to 15.4% (2019).

1.1. Avoidance of United States extraterritorial or secondary sanctions globally

Sanctions are administrative acts, often imposed by an International Organization, such as the United Nations (UN). It means the application of pre-existing law by an administrative body to a factual situation. However, the US has its own sanctions regime, binding worldwide. The ones referred in the text ahead are the *extraterritorial or secondary* sanctions. Extraterritoriality refers to the unilateral use of measures that are taken under a state's sovereign powers to enforce its own law in a territory other than its own, for actions committed outside its territory by entities or people from other countries¹.

The reasoning for this worldwide sanction regime is the following: as American companies have to follow US rules, a similar standard must be applied to their foreign competitors, lest they gain an unfair competitive advantage. With these actions, the US has withdrawn from the Joint Comprehensive Plan of Action (JCPOA), signed in 2015 by the E3/EU+3 (China, France, Germany, the Russian Federation, the United Kingdom and the United States with the High Representative of the EU for Foreign Affairs and Security Policy) recorded in the UN Security Council Resolution 2231 (2015).

Iran. Although sanctions are affecting Iran, the Islamic Republic is willing to ignore the reimposed secondary sanctions. President Rouhani asserted that this time they “*are breaking the sanctions with pride, as what the US is doing is cruel and contrary to law, treaties and against UN resolution*”. Nevertheless, the European Union (EU) is having difficulties to block the United States (US) sanctions and Iran might establish a stronger stance *vis a vis* with the US, withdrawing from the JCPOA, the Non-Proliferation Treaty (NPT) and resume high-level enrichment. Furthermore, Iran may shut down the Strait of Hormuz, which entails one-third of the global crude oil. However, Tehran wants to believe that Trump will be a one-term President, and the following one will go back to what was already established in the JCPOA. There are some paths Iran could take to avoid the impact of US sanctions, but they are highly dependent on what the EU and China do. The possible scenarios will be addressed later in this report.

European Union. The US extraterritorial sanctions don't directly affect the EU and European companies in theory, because of the Blocking Statute. The Blocking Statute is covered in the Regulation (96/2271)² introduced in 1996 aimed at countering the effects of United States sanctions on EU economic operators engaging in lawful activity with third countries³. The Blocking Statute prohibits EU residents and companies from complying with the listed extra-territorial legislation unless they are exceptionally authorized to do so by the Commission. However, there have been some cases of European companies not complying with the Regulation 96/2271. For instance, Renault and Citroen, French companies, have suspended their post-JCPOA \$1 billion investments in a joint venture with two Iranian firms.

The prohibition to comply with US extraterritorial sanctions has never been applied in practice. That is why the EU is looking to enforce existing mechanisms to face US sanctions. Some steps have been already taken according to the commissioner for Justice, Consumers, and Gender Equality Věra Jourová: the EU has updated the Blocking Statute through a Commission Delegated Regulation (EU) 2018/1100⁴. Furthermore, the EU has extended the European Investment Bank's lending mandate in order to allow them to lend Iran in the future. Finally, the European Commission is elaborating a range of activities to strengthen the activities of SMEs between the EU and Iran⁵, as SMEs are the least exposed to US secondary sanctions.

Notwithstanding, there is a measure in the short-term which may be the most effective but needs from technical work apart from the political one. This is the Special Purpose Vehicle (SPV), which means in practical terms that the EU Member States could create a legal entity to facilitate financial transactions with Iran, to allow EU companies to continue trading, besides, this SPV, called Instex, will be open for third countries outside the EU to facilitate trade with Iran. This vehicle would operate as a barter system allowing Iran to supply, for instance, oil and, in return, to purchase the goods or technology it needs, using a credit account. To carry out payment processing between trade partners, so as to balance out different amounts and varying payment periods, the mechanism may require a banking license. The EU seeks to ensure that the SPV would be able to provide export loans to facilitate economic projects and humanitarian trade⁶.

Nonetheless, the SPV currently only allows to trade in areas not sanctioned by the US, so Europe should look for other mechanisms to trade oil, for example, by expanding this SPV mechanism. The EU is also thinking about a mechanism to the Iranian-banned SWIFT system as French Finance Minister stressed: *"Our priority is to build independent, sovereign European financial institutions which would allow financing channels between French, Italian, German, Spanish and any other countries on the planet. It is up to us Europeans to choose freely and with sovereign power who we want to do business with. The United States should not be the planet's economic policeman"*.

China. China is Iran's largest oil consumer and has always imposed only those sanctions required by the UNSC, meaning they won't recognize extraterritorial sanctions. The great Asian power is part of the JCPOA and said it is not going to cooperate with reimposed US secondary sanctions. However, Iran's crude sales to China fell 21% between May and August 2018, a fact that suggests a certain degree of compliance with Washington⁷. Nevertheless, it is unclear how long China will stick to that tendency. Trump's administration gave China a "significant reduction exception" (SRE) sanction exception (or waiver) to recognize the import reduction, which finished the 1st of May 2019. China may be waiting for an effective mechanism to trade safely with Iran, or even wait for the Europeans to withdraw from the deal to take the place that EU companies will leave behind. The opportunities for Chinese leadership in the region are addressed below.

Table 1.1. Non-compliance with US sanctions scenarios⁸

	Scenario 1 (base)	Scenario 2 (best)	Scenario 3 (worst)
EU-Iran	The EU develops an effective Special Purpose Vehicle (SPV) which will function as a barter system. This will be used also by third countries outside the JCPOA. However, this will work only in the short-term and in products not sanctioned by the US. The US does not give waivers anymore. This may cause Iran lose its patience.	While the SPV is working, the EU develops an effective alternative for the SWIFT system, allowing Iran to trade in euros and other currencies with no risk to suffer the effects of US sanctions.	The SPV fails to satisfy Iran’s desires and it withdraws from the JCPOA and the NPT, resuming high-level enrichment. Iran increases its military influence in Yemen, Syria and Lebanon. They will trade only with partners outside the JCPOA such as Turkey and India. Economic recession and poverty will shake Iran.
China-Iran	As a member of the JCPOA, China will use the SPV established by the EU as a mean to trade with Iran. Even though it will only work in the short-term, China will continue to trade with Iran in yuan through the <i>Petroyuan</i> strategy and develop its <i>One Belt One Road</i> (BRI) strategy in Iran. It is easier for China because of the low exposure to the US market.	The effectiveness of the new SWIFT system permits China to trade with Iran with zero risks of US sanctions. Besides, this trading method allows China to develop their BRI strategy even faster, accelerating trade not only with Iran but also with other Middle East countries.	Iran stops trading with all the JCPOA members after it withdraws from it. China is Iran’s largest oil customer and Iran supplies around the 6.3% of China’s imported crude. This scenario will really hit Iranian economy, losing its main customer.

1.2. US leadership in the spotlight

“Confronting multilateralism is not a sign of strength. (...) It betrays an inability to understand a complex and interconnected world.” President Hassan Rouhani stressed this sentence to the US president in the United Nations General Assembly (UNGA), the 25th of September, 2018, as Tehran is committed to continuing with the deal and is claiming that the US is coercing other countries to violate the nuclear deal. However, countries such as India, Russia, Turkey, and China are challenging US sanctions by arguing that the US is the one knocking down the agreement.

Turkey. Turkey's economy minister Nihat Zeybekci has been clear stating that *"the decisions taken by the US on this issue are not binding for us. (...) We recognize no other (country's) interests other than our own"*. Turkey buys about 40% of its oil from Iran and it has reiterated that it is not cooperating with the reimposed US sanctions but reduced their oil import in about 33% in 2018. That is why Turkey was also given an SRE sanctions exemption on 5th November, 2018⁹. Turkey is a crucial market for Iran and vice versa. It may be a commercial alternative but not the sole one, as it lacks from many resources that Iran might need in the future.

India. The New Delhi's government has always complied with sanctions coming from multilateral mechanisms such as the UNSC. Nonetheless, it is uncertain how Indian firms and government are coping with the reimposed secondary sanctions. Indian leaders believe Iran is not violating the JCPOA. However, India's oil imports from Iran have been decreasing during 2018 and 2019, and that is why it is one of the eight countries with an SRE sanctions exception from the US. India could be a commercial alternative for Iran as, for instance, they are cooperating in the Chabahar Port which will connect India and Afghanistan without going through Pakistan, and disregarding US sanctions, Indian firms are no longer in a risky position. Furthermore, Nikki Haley, the then US Ambassador for the UN, on the 27th of June 2018, stated the commitment of the US to join the project as a means for the *"Afghanistan reconstruction"* exception. Moreover, both countries have been recently trading in rupees, the Indian currency. Iran was exporting oil and India exporting raw materials such as sugar, which does not make a durable exchange in the long term, leaving India in no position to become Iran's sole commercial partner.

China. China is increasingly becoming a huge commercial alternative for Iran. This is due firstly to the low exposure of Chinese firms in the US market and second to the European Union's struggle to find ways to avoid or mitigate the impact of US sanctions on their companies. Although it has been mentioned that China has significantly reduced its Iranian oil imports, it remains uncertain how events will develop. While the US is trying to maintain its leadership through sanctions, China is quietly gaining power in the foreign exchange market, and US sanctions are only exacerbating this process, because commercializing with yuan avoids any US sanction for both countries. China /

wants to negotiate and is seeking to strengthen the yuan as a deposit currency to consolidate it in the international market. Possibly, the most significant implication is how sanctions have led to widespread de-dollarization, whereby the dominant global status of the dollar has been challenged¹⁰. This strategy is the so-called “*Petroyuan*”. China’s “*One Belt, One Road*” initiative might undermine US global leadership. Commercial ties between Iran and China are old and recent. Old in the sense that the ancient silk road crossed Tehran, and recent in the sense that the formal relationship between both countries was established in 1971. Iran considers this initiative as an important opportunity to rebuild its domestic economy and enhance its role and status in the global economy¹¹.

The Asian Giant is one of the best choices for the replacement of the US in Iran as a commercial partner. It is motivated not only because of the “*Petroyuan*” to avoid US sanctions and the BRI initiative but also by the split of the Western world after the withdrawal of the US from the JCPOA, an event that China will use to take the place of the European firms in the Islamic Republic.

Russia. The strategic partnership between Iran and Russia is on the rise. Their relations have reached an unprecedented peak, fuelled by military cooperation in Syria, a shared vision of the global order, and mutual criticism of Western policy in the Middle East¹². Moscow has made it clear that it will not comply with US reimposed sanctions. Russia is part of the JCPOA and is unwilling to submit to Washington’s pressure. In fact, in December 2018, Iran signed a free trade deal with the Russia-led Eurasian Economic Union¹³. As for China, both countries may want to cooperate without paying attention to US sanctions because of their limited US exposure.

As many other countries, Russia’s statement is that sanctions are violating international law, especially Resolution 2231 (2015) of the UNSC. Russia is continuing to trade with Iran although it has not a US waiver to do so. Surely, Russia can become a commercial alternative for Iran, especially because of the bonds both countries already share. Iran needs the support of Russia in the Middle East. Russia will seek, together with the EU and China, an alternative to the trade with Iran. If the JCPOA fails, Russia will still cooperate with the Islamic Republic as it is a strategic partner and especially with the /

support of China. Furthermore, a victory of al-Assad in the Syrian war will make Russia even stronger in the region. However, if the agreement fails and Iran seeks to build the nuclear bomb, Russia and China may pressure Iran with new worldwide binding UN sanctions.

1.3. Economic consequences of US sanctions in Iran

Iran's economy is one of the most diversified in the Middle East, but it is also highly dependent on oil. Sanctions took a substantial toll on Iran's economy, especially after 2012 and sanctions relief caused Iran's economy to rebound, after 2015 although perhaps not to the extent that Iranians expected. That said, the nature and extent of the consequences of the US withdrawal from the JCPOA at this point are highly uncertain. Medium-term prospects are negative, based on a reversion of oil exports due to the reimposition of US sanctions. Iran would be one of the few countries which could enter a period of recession and raising prices in 2019. However, the US is experiencing that sanctions are easier to state than impose because of its lack of the international community's support. While Iran, will still suffer significantly, Europe, China and Russia have pledged to soften the blow to the highest degree possible¹⁴ Iran is willing to remain in the nuclear deal despite of the disadvantages of the re-imposition of US sanctions and its commitment will depend, especially, on Europe's ability to circumvent US secondary sanctions.

1.3.1. Most affected sectors

The Banking sector. These sanctions will not only affect Iran but also third countries willing to trade with the Islamic Republic. There is a ban on Iranian access to the US financial system/use of dollars, this comprises direct access to the US financial system and the prohibition of access of foreign banks or persons that pay Iran for goods in US dollars. Notwithstanding, the inability of Iran to the use of the SWIFT system is the main concern currently. As previously mentioned, the EU is seeking for a legal alternative to ensure transactions between Iran and the EU as well as among third countries. German Foreign Minister Heiko Mass stated the need of "*strengthening the /*

European autonomy by establishing payment channels that are independent of the US, creating a European Monetary Fund and building up an independent Swift system."

The Energy sector. As mentioned above, Iranian economy is highly dependent on oil and sanctions in the energy sector and the inability to trade these goods will make the Islamic Republic's economy shake. There are plenty of different sanctions concerning Iran's energy sector such as: the prohibition on investment to develop Iran's oil and gas fields, the prohibition to sale gasoline to Iran, the ban to provide equipment or services for oil, gas, and petrochemicals production and the forbiddance of transporting Iranian crude oil (not applied in cases of transporting oil to countries granted with an exemption). This subject will be further developed later in the report.

Trading sector. One of the main consequences of US sanctions is the prohibition to Iran to access the international shipping insurance industry and financial markets for Iranian Oil Company (IOC) and National Iranian Tanker Company (NICT). Obtaining shipping insurance is crucial to Iran's expansion of oil and other exports. A pool of 13 major insurance organizations, called the International Group of P&I Clubs, dominates the shipping insurance industry and is based in New York. As a response, Iran is offering since August 2018 Iranian shipping and insurance in a ship-on board contract basis through NICT in very favourable terms. This model is being used by India and China oil imports. By dint of the previously exposed, the forecasts are the following:

Table 1.2. Iran Economic Indicators

	GDP growth	Budget Deficit	Unemployment	Public Debt	Trade Balance
2018	-1.9%	-3.06%	13.9%	44.2%	\$ 4,545 million
2019	-4.5%	-4.11%	15.4%	40%	\$ 1,408 million
2020	0.9%	-5.17%	16.1%	30%	\$ 1,454 million

Data source: Global Economic Prospects, International Monetary Fund (June 2019), World Economic Outlook, International Monetary Fund (April 2019) and data retrieved from the Central Bank of Iran.

Table 1.3. Short-term Economic Forecast

	Political implications	Economic consequences
Scenario 1 (base)	The EU develops an effective Special Purpose Vehicle (SPV) which will function as a barter system. This will be used also by third countries outside the JCPOA. However, this will work only in the short-term and in products not sanctioned by the US. The US stops granting waivers to purchase Iranian oil.	Economy will experience a big decrease due to sanctions but Iran will keep on trading worldwide in non-sanctioned goods and will reinforce its alliance with China and Russia which with whom it will keep on trading not obeying Washington.
Scenario 2 (best)	While the SPV is working, the EU develops an effective alternative for the SWIFT system, allowing Iran to trade in euros and other currencies with no risk to suffer the effects of US sanctions. Or, the US starts a more conciliatory policy, facilitating a renegotiation of the deal hearing all the proposals and grants waivers to purchase Iranian oil again.	Economy will experience a slight decrease, and as soon as trading starts, Iranian economy will gain strength and confidence.

2. ENERGY ANALYSIS

- Sanctions will hit hard on foreign investment, reducing notably future projects and leading to many cancellations of existing ones. This situation will aggravate the situation of underinvestment that the sector is suffering.
- Oil exports will be severely hampered by US sanctions with a reduction of around 1.4 million barrels per day (mbpd). EU, South Korea and Japan will stop importing oil from Iran if sanctions waivers are not given. India and Turkey will reduce considerably oil imports but far from reaching a total reduction. China may be able to maintain the bulk of its oil imports. Sanctions may not reduce gas production in absolute terms but will affect negatively its potential output by delaying and cancelling many investments and ongoing projects, however it is expected to rise by around 41.3 millions of tons of oil equivalent in the coming years.
- Brent barrel is expected to stabilize around \$70 along the year, being the US a major market player with its control over 2 mbpd due to sanctions, its rising oil industry and its bargaining position with OPEC's de facto leader Saudi Arabia.
- Iran's energy industry will suffer in the long term to maintain current level of exports and output if the country is not able to attract foreign investment and reduce its current international isolation.

2.1. Effects of sanctions on foreign investment in the Energy Sector:

Thanks to JCPOA and the lifting of sanctions, FDI during 2017 hit a decade record with more than \$5 billion according to UNCTAD, most of it in the oil and gas sector. However, the reimposition of sanctions by the Trump administration paralyzed most of the investments made by EU, US, South Korean and Japanese companies on the sector. Even the investments made by Chinese, Russian or Indian companies are struggling to obtain the financial and legal security required to develop the planned projects and as under-Obama sanctions era, they are trying to make limited investments just not to be expelled¹⁵. This reality puts Iranian hydrocarbon industry in a tough situation considering the officially stated, by oil minister Zanganeh, necessity of \$200 billion in /

the oil industry¹⁶ in the coming years. The industry requires urgently investment to compete globally after sanctions and isolation from world markets during 2012-2016.

The maturity of many of the country oil fields (approximately 60% of Iran's crude oil production comes from oil fields that were discovered before the nationalisation of 1951¹⁷), requires enhanced oil recovery (EOR) techniques such as gas injection to maintain current production. Currently, in the absence of that technology, only 20-25% of the oil in place is feasibly extractable. Equally, the downstream sector demands investment and technology to assure national self-sufficiency of basic goods such as gasoline, a national strategic goal achieved recently thanks to the Persian Gulf Star Refinery, which had to be funded exclusively with Iranian resources. The repeatedly stated goal of diversifying the national economy and increase high-valued petrol products output will be difficult to reach in the short term, despite the existence of highly potential neighbouring export markets such as Pakistan, Afghanistan or Iraq. The gas sector is also in need of foreign investment to reach the potential offered by the natural gas reserves and strategic location of the country. Further developments of South Pars and other offshore reserves, as well as exporter facilities such as LNG terminals, require huge financial and technological investment if the country wants to become a natural gas exporter and energy hub. In general, the entire energy sector demands for investment and technology that appeared to arrive during JCPOA and the more attractive Iran Petroleum Contract (IPC, with a structure similar to buy-back contracts), have been heavily blocked under US sanctions. Equally, in this context, the governmental efforts made to reduce the influence of the IRGC on the energy sector will not have the desired effects in terms of transparency and FDI attractivenessⁱ. Some examples of these failed investments are listed below.

- *South Pars field phase 11*¹⁸ development was given to TOTAL (50.1%), CNPC (30%), PetroPars (19.9%) in July 2017 in a \$4.8 billion deal. TOTAL abandoned the project and its participation was replaced by CNPC on November 2018, however, the Chinese company abandoned too the project on December due to US pressures under /

ⁱ On 20 January, Defence Minister Amir Hatami told a local newspaper that Khamenei had instructed the Revolutionary Guards (IRGC) and other branches of the Armed Forces to divest from those economic activities “irrelevant” to their core purpose.

trade talks negotiations. This mega project was expected to boost gas and condensates production. It was the first concession to a European company in decades and a strategic bet for TOTAL.

- *Aban and West Payedan oil fields*¹⁹ were given to Zarubezhneft Russian state-controlled oil company (80%) and Dana Iran private company (20%). The deal signed on March 2018 was expected to produce 48,000 bpd with a total investment of \$750 million. It was the first time a Russian company obtained developments rights in Iran and the first Iranian private company involved in the oil sector. By October 2018 Zarubezhneft left this pioneer project due to pressure from US sanctions²⁰.

- *Siraf Refining Park Project* was signed by South Korea's Hyundai and Japan's Chiyoda Corporation in July 2017 to cover the funding and construction of eight condensate splitters with a combined capacity of 480,000 bpd. The project budget was \$2 billion covered by a Korean-Japanese consortium²¹. In October 2018 the project was cancelled due to US sanctions on Iran²².

Other potential projects have been frozen by foreign companies after signing a Memorandum of Understanding. The Toyo-Petropars MoU on Salman field signed on July 2017, Eni-NIOC MoU on Darkhovin oil field signed on June 2017²³ or OMV-Gazprom-Dana MoU on Zagros field signed on June 2017²⁴ are some examples. Iran has had several difficulties to materialize MoU into actual projects during the last decades.

One of the most painful effects of 2012 and current sanctions is the underdevelopment of LNG export terminals in Iran. Among different reasons, the financial and technical isolation of the country is creating a paradoxical situation in which Qatar, a country that shares a big portion of its gas fields and geographical conditions with Iran, is an LNG powerhouse while Iran is unable to develop this technology.

As a general overview, the oil industry in Iran will lack the needed foreign investment under the current sanctions regime. As shown, no matter where the companies are from nor the nature of their ownership, most of them are reluctant to continue with their /

investments. Not even through the proven competence and resilience of Iranian engineers and its energy sector, will the country be able to maintain current oil production without foreign investment²⁵.

2.2. Energy sector in the 2019-2020 period

2.2.1. Oil production and exports for 2019-2020 period

Upstream output in the upcoming two years will heavily depend on oil exports under the sanctions regime. As it happened during the 2012 sanctions, the upstream industry will cut liquids production in a similar amount of oil exports decrease. This would lead to an average production for the 2019-2020 period of 3.5 mbpd considering oil exports reductions, internal demand, technical limitations and storage facilities. This means that Iranian oil output will be 25% less than the 4.6 mbpd of 2017.

Table 2.1 summarizes the predictions on Iran oil exports for 2019-2020 period. Waivers May-Nov answers to the already established waivers by the US in November 2018. On April 22nd, the Trump Administration decided to eliminate all waivers on Iran exports. Non-compliance scenario refers to a situation in which countries do not follow US sanctions, a different colour depending on its likelihood is address to each case. China is expected to be the only country willing and capable of circumventing US sanctions, while India and Turkey will probably reduce oil purchases without reaching a zero level goal due to strategic and logistical limitations. A strict reduction of EU, South Korea and Japan to zero imports as a consequence of its strong alliance and dependence from the US financial system is very likely. Total oil exports are expected to transition from an average of 1.5 mbpd at the beginning of 2019 to 1 mbpd by mid 2020 if sanctions remain in place despite Iran's efforts to offer discounts, free insurance, a free on-board contract and 60-day credit for payments. Nevertheless, under current trade talks and Indian elections, an important reduction of oil imports from Iran can be expected during May and June 2019. As mentioned, despite US efforts, many countries will backslide from US waivers and will purchase more oil from Iran. According to Tanker-tracking websites, Iran is being able to export a higher amount of oil than expected through opaque trade mechanisms.

Table 2.1. Iran Oil exports in the 2019-2020 period and scenariosⁱⁱ

Country by destination	Waivers Nov-May 2019	Waivers from May 2019 and 2020	2020 real purchases estimation	Non-compliance scenario	Previous 2018 Jan-June
China	360,000	0	500,000	700,000	615,000
India	300,000 ²⁶	0	200,000	700,000	600,000
South Korea ⁱⁱⁱ	200,000	0	0	350,000	317,000
Japan	80,000 ²⁷	0	0	150,000	150,000
Taiwan	15,000	0	0	30,000	27,000
EU ^{iv}	180,000	0	0	450,000	450,000 ²⁸
Turkey	150,000	0	150,000	200,000	150,000
Other ^v	-	-	50,000	300,000	300,000
TOTAL	1,290,000	1,000,000	1,000,000	-	2,400,000

Highly likely
 Not expected
 Highly unlikely

180-days Waivers were lifted in November to 8 countries in order to avoid an oil price peak, assure a smooth transition for Iran oil buyers to *the zero-imports goal* and reward those countries which showed commitment to the import reductions²⁹. As mentioned, in last April those waivers were not extended, augmenting US pressure on the Iranian economy. In this context, the Islamic Republic would likely be able to maintain some shipments for debt repayment to China and India while smuggling another significant /

ⁱⁱ All units in barrels per day. Figures might not reflect actual deliveries due to reported activities by Iran and various oil customers to conceal purchases or avoid tracking of oil tankers. This figures may differ from other major sources as condensates are included, sometimes referred to as Natural Gas production.

ⁱⁱⁱ The estimation includes condensates in the case of South Korea

^{iv} Waivers extended in November 2018 to Italy and Greece.

^v Iraq swaps, Syria, UAE, Singapore, Sri Lanka, Malaysia, Indonesia and unknown.

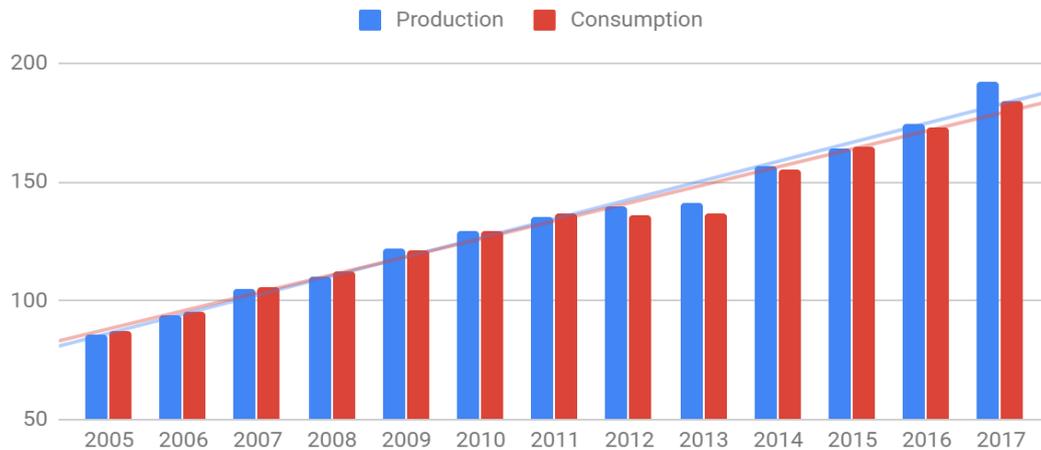
amount. Nevertheless, the significance of Chinese imports will depend on the development of US-China trade talks and the level of disengagement of these two countries.

2.3. Gas production and exports 2019-2020

2.3.1. Gas production 2019-2020

Overall, natural gas developments have been a constant in the Islamic Republic, which has been able to double natural gas production since 2006 with an annual growth of 6.3%, always absorbed by similar levels of consumption in the country³⁰. Despite sanctions and foreign investment reduction, gas production will continue to grow supported by ramping-up production from the giant South Pars field. In contrast with the oil sector, the exceptional geological conditions of Iran and the level of development of national companies allow the country to keep a steady increase in production despite sanctions, as it occurred during the 2012-2016 period. A further five South Pars phases are expected by mid-2019. Phases 12, 14, 22, 23 and 24 currently in the final development phase by Pars Oil Gas Company will add around 41.3 millions of tons of oil equivalent to new production capacity in the coming years, enabling Iran to keep up with its increasing demand and modest exports³¹. Despite this positive description, the mentioned failed project of South Pars phase 11 was expected to increase production by 20 mot of oil equivalent. Up to 30 MOUs were signed with IOC in the post-sanctions era, however, they are not legally binding and under the current sanctions regime are highly unlikely to be developed.

Figure 2.1. Natural gas production and consumption in Iran in the period 2005-2017 in million tons of oil equivalent



Source: BP statistical review of world energy

2.3.2. Gas trade under US sanctions

Natural gas exports and imports are much more isolated than oil from US sanctions as most of the contracts are done through pipeline, take-or-pay and in a long-term basis. Historically, Iran imported natural gas from Turkmenistan during the winter for the northern regions, nevertheless, the recent construction of the Damghan-Neka pipeline connecting different regions internally has put an end to that need³². Equally, improvements in storage capacity are helping to handle the very seasonal demand of the country. The 2010 fiscal reform to promote domestic consumption efficiency is providing Iran with more capacity to export, still very limited to 6% of its production.

Since 1996 Turkey is the main destination of Iranian gas exports with an intermittent and complicated relationship due to legal and political disputes. Currently, the Tabriz-Ankara pipeline has a capacity of 14 bcm/y but with an average use of 7 bcm/y, representing 4.3% of Iran gas production. The future of this trade partnership is likely to continue under sanctions as it happened during 2012 when Turkey used a gold-payment method that bypassed sanctions effectively. The need to reduce energy imports from Russia is a strategic priority to Turkey and Iran for that plays an important role³³.

Since June 2017, Iraq is the second destination of gas exports with a volume of 9.1 bcm in a ten-year gas agreement or 25 mcm per day. The current volume is higher than scheduled, around 36 mcm per day. Iraq's starving electric and residential system considers the pipeline of strategic importance and has asked the US for sanctions exemptions. After hard negotiations, Iraq started to pay Iran in Euros as a way of circumventing sanctions. Therefore, it is highly likely that gas flows will continue despite sanctions and repeated warnings from Trump administration to stop electricity and gas imports from Iran³⁴.

2.3.3. Impact of US sanctions on energy prices in 2019

The development of the oil market will depend on several interconnected forces and will be highly influenced by US foreign policy:

Iran sanctions. Depending on US waivers and traditional customers response to sanctions, oil exports of the Islamic Republic can vary from 0 to 1.800.000 bpd. Estimations are that Iran will export an average of 1,000,000 bpd, and there will be reduction of 1,400,000 bpd from Jan-June 2018 levels. US management of waivers will be done according to oil prices and in particular to US-Saudi negotiations.

OPEC+ cuts. According to the last quotas, 21 countries will reduce its production up to a total of 1,200,000 bpd during the first half of 2019. Saudi Arabia and Russia will assume 45% of the total reduction. Venezuela, Iran and Libya are not included. Further cuts may occur in June 2019 if higher prices require more market tightening. The necessity to balance public budgets may push these countries to further cuts, however, OPEC agreements have been difficult to implement effectively in the last decades, and it is highly unlikely to see cuts further than 1 million bpd.

Libya. Facing a permanent turmoil since 2011 and now on what seems to be one of the last stages of the civil war, it has produced around 1 mbpd in the lasts months. Insecurity in remote areas where important oil fields are located, such as Sharara of 300,000 bpd capacity, may remain. However, under the slow but constant advance of /

NLA headed by General Haftar, oil output may reach 1.3 mbpd, adding 300,000 bpd to world production during 2019.

Venezuela. The Caribbean country is trapped in a deep spiral of political instability with a clear impact on its oil production, which is dramatically decreasing since 2015. The recent US sanctions will aggravate the situation, however, current waivers in place are reducing its impact in the short-term. The expected decrease in production is considered to be near 300,000 bpd.

North America oil boom. Non-conventional production in the US and Canada is surprising the oil industry year by year. US production is estimated to have grown around 1.4 mbpd totalling 12.45 mbpd by the end of 2019 and become the largest world oil producer, meanwhile Canadian output is programmed to decrease temporarily to adjust production to transportation capacities. Under the current fiscal favourable conditions and the expected reduction in pipeline and transportation bottlenecks, North American oil output is likely to increase more than expected during 2019, becoming the most important force pushing oil prices down.

World demand. Under the current trade frictions and an expected economic slowdown, oil demand in 2019 is still difficult to estimate. According to OPEC and IEA figures, oil demand will rise 1.3 mbpd coming mostly from developing countries. The world economy is demonstrating some weaknesses and there are warnings of a possible crisis in 2019-2020 with oil demand shrinking from developing countries.

Oil prices may stabilize during 2019 compared to the highly volatile context of 2018. More than ever, energy markets will be driven by political forces, with the US as a central actor. Currently, US-Saudi talks are being held regarding Iran waivers and OPEC+ cuts. If Saudi Arabia wants a damaged Iranian economy due to sanctions, cartel reductions must be in line with US strategic interests, which are currently to moderate oil prices. The market position of the United States leaves the country in a very favourable bargaining position: its extraterritorial sanctions control more than 2 million bpd and its oil industry is hitting world records. Saudi Arabia and Russia need higher oil

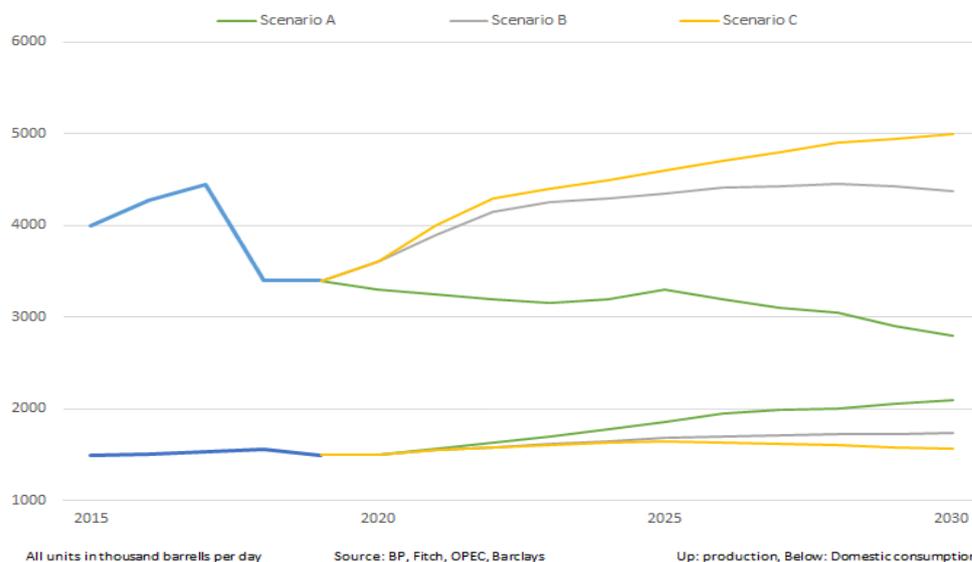
prices to develop their national long-term strategies: the Saudi 2030 vision and public offer of ARAMCO and Putin's goal to improve living standards during this presidency.

According to market signals, a more stable 2019 Brent barrel price at somewhere around \$70 with a reduction of WTI gap price is expected as export facilities are being developed in North America. Oil price will be in between 2018 October peak of \$84 and December \$52 and similar to the average 2018 prices of \$71. The geopolitical intensity of current energy markets makes it hard to predict future oil prices and some degree of uncertainty must be assumed during 2019.

2.4. Energy sector outlook 2030

To offer a complete analysis of the Iranian energy sector in 2030, three scenarios are presented below depending on production and domestic consumption levels. To design these scenarios, different variables have been taken into account such as major world political events, domestic policies to attract foreign investment, internal consumption trends and Iranian foreign policy and negotiations with the international community regarding sanctions and the nuclear deal. Some others have been assumed as constant or without relevant disruptions such as oil price because of its level of unpredictability.

Figure 2.2. Iran oil production and consumption scenarios 2030 Outlook



Scenario A: Low production, high consumption.

Oil production declines due to sanctions with oil wells reaching maturity without technological investment in EOR and lack of new productive field discoveries. Gas production stabilizes at current levels thanks to ongoing South Pars developments but around 10 bcm per year have to be imported from Turkmenistan. The petrochemical industry suffers to maintain current levels of output, without reaching gasoline self-sufficiency and becoming less competitive in export markets. Inflationary trends pressure the Government to maintain energy subsidies, leading to low levels of energy efficiency. The internal oil and gas consumption keep growing reducing dramatically export capability and revenues. The continuity of hawkish political leaders in Iran, US, Saudi Arabia and Israel leads to powerful economic pressure from sanctions that lasts for more than 5 years. Under a hostile international community and an increased internal pressure the Islamic Republic closes more the economy to outside actors, reducing foreign investment and international trade with a very devalued Rial.

Scenario B: High production, moderate consumption (Most likely)

After 2 years of sanctions oil production recovers and stabilize at 4.4 mbpd by the end of the decade with considerable investments from European and Asian IOCs. Gas production increases, enabling the country to export via pipeline. Internal demand is contained through fiscal policies and the development of alternative sources of energy. A shift in US foreign policy by 2022 allows a similar deal such as JCPOA. The end of the Yemen and Syrian Civil War reduces the intensity of the IRGC action and Iran foreign policy. The economy is moderately opened to foreign investors and some degree of regional energy connectivity is developed successfully with Turkey and Iraq.

Scenario C: Great production, low consumption.

The country produces 5 mbd by the end of 2020's reaching the highest output since the Revolution. Natural gas production ramps-up and allows the Islamic Republic to export around 50 bcm yearly via pipeline and in the form of LNG. The petrochemical industry receives strong financial support from NIOC and foreign firms making the sector a /

profitable exporter. Internal demand is contained through aggressive fiscal measures which promote energy efficiency and alternative sources of energy, in particular, wind and solar power generation. Sanctions are lifted by 2022 and a new deal is signed. The IRGC are removed from the energy sector easing foreign investment and a much more pragmatic foreign policy is developed. The economy is liberalized and a more attractive oil and gas contract substitutes the IPC. Electricity interconnection with Iraq and Pakistan allows the country to become a regional exporter.

2.5. Neighbouring cooperation and infrastructure

2.5.1. Pakistan, India and China

The idea of connecting natural gas-rich Iran with the energy-starving Pakistan arrived in the early 90's as part of the Iran-Pakistan-India pipeline³⁵, a mega-project that was expected to assure natural gas demand of the growing industry located in the Indian subcontinent. However, the irreconcilable India-Pakistan relation and US pressures on India, condemned the project to fail in 2011 with the Indian withdrawal. The discoveries of natural gas reserves in Pakistan reduced the country's interests until recently, in light of the electricity crisis they are facing.

The project is commercially feasible and more convenient than other alternatives such as TAPI pipeline or LNG imports. Nevertheless, the increasing financial and military dependence of Pakistan on the Gulf Cooperation Council limits severely the geopolitical viability of the project in the current context of an Iran-Saudi cold war. Even though Iran finished its part of the pipeline by 2014, the Pakistani side is still in very early stages and it seems it will remain in this situation for the coming years. Energy security is currently a top priority for Pakistan, which suffers from an increasing electricity shortage estimated above 3.000 MW. It is very likely that this project will be latent during the next decade as the China-Pakistan-Economic-Corridor develops the projected coal-fired power plants and GCC continues its financial assistance to Pakistan oil purchases and TAPI as a countermeasure to any Iranian attempt to increase its leverage on Pakistan. Nevertheless, its future potential should not be overlooked if the Iranian natural gas output increases according to its potential and Pakistan follows its /

current path of structural power scarcity. Iran is expected to be an important actor in CPEC as a reliable supplier of oil and natural gas for both Pakistan and China in the medium term.

As an alternative to this route, a hypothetical pipeline connecting Iran Chabahar port, currently in development by India, to Oman Ras al Ratan port and Oman LNG export facility has been repeatedly proposed in the last years. This infrastructure could be integrated into an undersea pipeline Oman-India that would bypass Pakistan. The future of this project is difficult to determine, regarding Saudi and US pressures on India and Oman to isolate the Islamic Republic of Iran.

2.5.2 Turkey and the EU

Turkey. Turkey aims to become an energy hub that connects Russia, the Middle East, Central Asia and Europe through pipelines and LNG export-import terminals. Iran gas exports to Turkey are limited to around 7 bcm/y in spite of the 14 bcm/y capacity of Tabriz-Ankara pipeline. The long term arrangement between the two countries will conclude by 2026 and its renewal will be problematic regarding the constant legal disputes during the current deal. A capacity increase is not expected, taking into account the future extra gas availability in Turkey thanks to the Turkstream and Trans Anatolian Pipeline in the coming years. However, the role that Iran can play in the future of Turkey as an energy hub must be considered.

TANAP, TAP and the EU. Iran has suffered in the last decades from a constant marginalization in the pipeline network connecting the Caucasus energy producers with Europe³⁶. The South Caucasus Pipeline, crossing Azerbaijan and Georgia, and TANAP, in Turkey, are currently available to supply from Azeri Shah Deniz II natural gas in 16 bcm per year, 6 of those will remain in Turkey and 10 will be exported to Italy, Greece and Bulgaria via Trans Adriatic Pipeline (TAP) when finished. The project, whose main ambition is to reduce EU dependence on Russia, is expected to increase its capacity to 31 bcm/y by 2026 and 60 bcm by 2050³⁷. As a consequence of the existing doubts about the capacity of Azerbaijan to be the single supplier of this project³⁸, an undersea pipeline connecting Turkmenistan with Azerbaijan is proposed, which has become a /

matter of dispute between these two countries, Iran and Russia, despite the 2018 Convention on the legal status of the Caspian Sea. Even though it is far from feasible in the short-term, Iran could be a future supplier of this pipeline if Turkmenistan natural gas is not available, considering the existing pipelines connecting the Iran with Turkey (14 bcm/y) and Azerbaijan (10 bcm/y). In the last years, Iran has repeatedly stated its intentions to focus on the Asian natural gas market instead of looking to Europe. Nevertheless, in a context of improved Iran-West relations and the possibility of supply disruption from the volatile North African region or Russia, Iran could become a possible partner of this project. In any case, the low likelihood of this option in the short and medium-term must be highlighted.

2.5.3 Caucasus and Caspian Basin

Armenia and Georgia. Iran currently exports a very small amount of gas to Armenia through the Iran-Armenia pipeline, an underused infrastructure of 2 bcm per year capacity. Among plausible options, is to revive this Soviet-era pipeline to increase exports of Iranian natural gas to Armenia and Georgia, transiting Armenian pipes. A very complicated manoeuvre that would have to deal with the control of Gazprom over most of the Armenian gas sector since 2015 and the lack of clear economic returns. The geopolitical interest in obtaining an alternative natural gas and oil supplier from Russia in Armenia and Azerbaijan in the case of Georgia is a major opportunity for Iran to increase its influence in this region.

2.5.4 LNG export facilities

The 2018 US sanctions forced to cancel two ongoing projects connected to South Pars natural gas field that had already developed storage and gas intake facilities but lacked liquefaction technology. Under current sanctions, Iran will not be able to develop LNG terminals because most of the companies that control liquefaction technology and property rights are US, EU, Japanese or South Korean based. Firms such as ExxonMobil, ConocoPhillips, Shell, Total, Marubeni, and Mitsui³⁹ which developed Qatar LNG industry will not work in Iran if sanctions remain. However, the huge natural gas reserves of Iran and its strategic locations are strong arguments to believe in

Iran as an important LNG player in the late 2020's as LNG technologies become more affordable and accessible. The two existing Persian LNG and NIOC LNG projects are above 50% developed, if finished, they would have a 12 bcm/y of export capacity. In a context of post-US sanctions similar to the JCPOA, LNG terminals working in Iran could be expected in a short period of time.

3. DOMESTIC SCENE

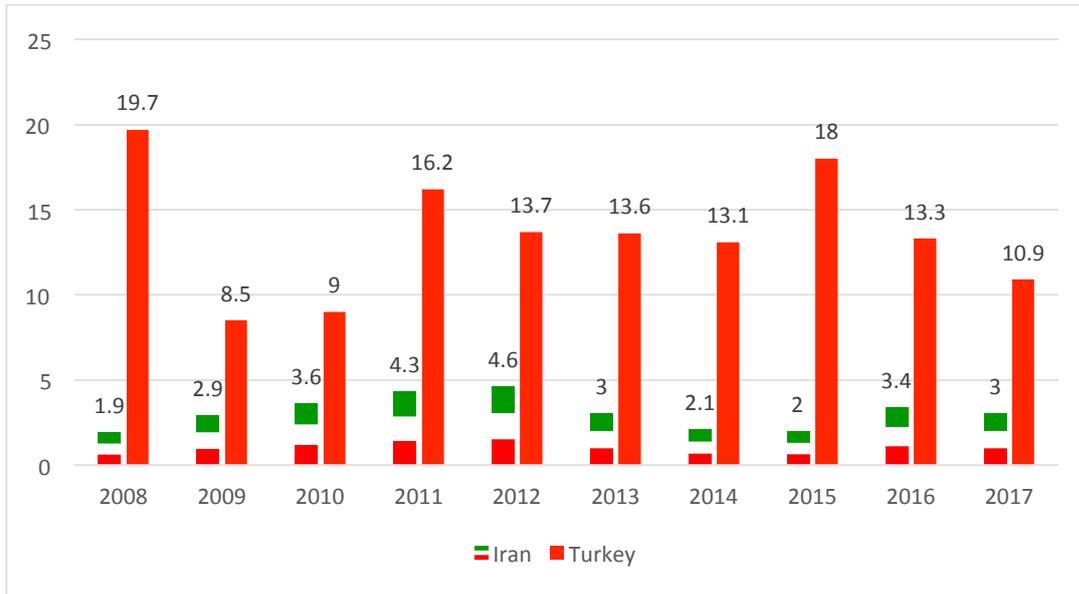
- Domestic policies in regards to foreign investment have created a challenging scenario for external companies.
- Social unrest reached a high point during 2018 and it will remain latent at least until the upcoming elections take place in 2020 and 2021. Hardliners are using this discontent to challenge the current government.
- The fate of the JCPOA and US presidential elections in 2020 will be determinant for the outcome of Iran's future leaders. Khamenei, aged 79, will not be able to hold power much longer and the question to whom his successor will be has been raised.
- Regional upheaval fostered by ethnic minorities' discrimination has become a main source of tension for Iran's geopolitical strategy.

3.1. Domestic policies affecting foreign investment

Despite usual assumptions, Iran is an interesting country with many opportunities for investment. It has a wide range of different markets that haven't been exploited yet. However, its turbulent foreign reputation has occasioned several downfalls on the country's potential. The severe effects that sanctions have had on its economy have discouraged many foreign companies from investing in the country. This section will attempt to map the business atmosphere that domestic legislation, regardless of external sanctions, has laid out for foreign investment.

The economic sanctions imposed by the United States have diminished economic growth and decreased the chances for foreign investment in the country as it has already been developed in previous sections. The following chart represents a comparison of the Foreign Direct Investment figures between Iran and Turkey in the last decade. This analogy has been made due to both countries similarities in culture, population size, and attempts to gain more influence in the region. Despite any existing differences, this graph clearly shows the unexploited potential of Iran as compared to Turkey, which is due to both the effect of economic sanctions and to those of domestic policies and corruption.

Table 3.1. FDI: Iran v. Turkey^{vi}



3.1.1. Political factors

Every aspect of daily life in Iran is somehow controlled by the system and intervention in any field can occur without warning. Iran’s market mechanisms are yet not developed to meet higher international standards. This poses a relatively high threat to any investment in the country. Protectionism is often used for the preservation of certain industries by the imposition of tariffs or customs duties on foreign competition.

In the energy sector, for instance, the National Petrochemical Company underlines the necessity of supporting local manufacturers and even states the possibility of banning foreign-made items if they can be produced domestically instead⁴⁰. However, protectionism does not always have to be harmful to foreign companies. The automobile sector, only second to the energy sector, is highly protected by trade barriers ultimately accounting for 80% of the value of an imported car. Iran’s car manufacturing industry is one of the biggest in the region, however, its size does not automatically mean it is competitive yet. Only two companies account for 94% of the total output: IKCO and SAIPA. IKCO has a joint venture with French companies Groupe PSA and Renault, meaning that through their agreements with local manufacturers, they are able to circumvent Iran’s strict trade barriers⁴¹.

^{vi} Data source: World Bank. Data units are in billion USD.

3.1.2. Economic Factors

Iran's economy is one of the major issues to be taken into account when it comes to doing business in the country. It has been undeniably affected by foreign sanctions which have made it very difficult for the country to thrive. Inflation is one of the major problems the Iranian administration is facing. It is one of the main reasons for the current social unrest and it poses a threat to foreign investment. As of June 2019, one Euro equals for 47,569.60 Iranian Rial. Interest rates vary from 12 – 15 %, while deposit interest rates are at 16-18%. Islamic Treasury Bonds are offered at a rate of 28%, diminishing banks' competitiveness. High-interest rates do not suggest investment financing through banks. Purchasing power has weakened for the bulk of the population, although luxurious markets still hold enough demand to prosper⁴².

3.1.3. Technological factors

Iran's society and businesses are progressing towards a more developed and technologically sophisticated environment. Surprisingly, sanctions have played a role in the boom of this industry. Tehran has followed for years a policy of R&D investment supported by Supreme Leader Khamenei, which has enjoyed relative consensus unlike most of the economic decisions in the country. The high prices of foreign items forced producers to search inside, which has fostered the rapid development of the sector. Since 2013, \$5.3 billion have been spent by the government in technology infrastructure and 1% of the economy is now composed by start-ups which attract foreign funding and top graduates⁴³. It isn't hard to predict that the technology sector will play a fundamental role in Iran's economy in the years to come.

3.1.4. Main risks

Iran represents a complex scenario for foreign investment for which preparation is key to find the available opportunities. The main risks revolve around the poor performance of the economy due to the consequences of sanctions, the government's lack of transparency and liability, the absence of stricter standards and proper infrastructure and the heavily government-run market. However, there are many opportunities especially in the unsaturation of the market which translates in low competition and room for new

actors. Avoidance of sanctions can be done through collaboration with local companies and trading with currencies other than the dollar. Iran's current inflation also envisages the chance to buy existing facilities at a relatively low price for foreign currency.

3.2. Social and demographic situation

Understanding the complexity of the history of a country whose citizens have been so powerful and determined in its own shaping is essential to get a grasp on the current situation.

3.2.1. Demographic analysis

Iran has a population of more than 82.5 million people, out of whom 89% are Shi'a Muslim, 10% Sunni and the remaining 1% is composed by Christian, Zoroastrian, Baha'i and Jewish. Iran also holds one of the world's largest populations of refugees with over a million Iraqis and Afghans that find protection within its borders. In terms of population pyramids, Iran is one of the few developing countries in the world that has reached the end of the demographic transition. A family program launched by the government after the Iraq-Iran war decreased the number of children a woman would bear throughout her life from 5 to 2 in just two decades. This means that the number of people who are able to work and contribute to the country's growth clearly outnumbered that of children and elders⁴⁴. However, the bulk of Iran's population is still mostly youth. Over 60% of the whole population is under the age of 30⁴⁵. The youth unemployment rate is currently at approximately 28.3%⁴⁶, which given the previous figures, poses a threat to the stability of the country as young people are among the main driving forces of change and protest in the country. Besides unemployment, the youth is heavily concerned with the regime's control of sexuality and other individual freedoms.

3.2.2. Recent events

When Rouhani came to power in 2013, he did so with promises of a more liberalised system and fewer restrictions on daily life. While there have been minor improvements,

certain issues such as women's rights or minorities' rights are still highly controversial and therefore restricted. At the end of 2017, and beginning of 2018, several protesters went to the streets of major Iranian cities to criticise the government and the regime itself, on what have been the biggest protests since 2009. The poor performance of the economy, the rise in prices, unemployment and the many strict rules such as the imposition of a dress code for women, have left a sensitive part of the population with no choice but to rebel against the system. On top of all is the high expenditure that the regime has exercised on foreign affairs by providing weapons and fighters to Syrians and financially supporting Hezbollah in Lebanon⁴⁷. Unlike the protests of the green movement in 2009 who gathered around 3 million Iranians to rally against the reelection of President Mahmoud Ahmadinejad, who would later crash them with the use of force. These recent events sprung protests around the country that were composed by young working-class people instead of intellectual elites. A few months later, in August 2018, there was a new wave of protests claiming the same as those earlier that year.

3.2.3. Future prospect

The situation has not changed much and it is likely that social unrest will increase in the upcoming months prior to the parliamentary elections of 2020 and the following presidential elections of 2021. As it was seen in 2009, elections are often sensitive times where many things can happen. The reasons behind Iranian protests last year are still present today and in some cases, such as the severe effects of sanctions, it has even worsened. Therefore, it is possible that a new wave of protests will arise in the next two years triggered by the same reasons as those of last year. Depending on the scale of the demonstrations, more international attention could be attracted to the playground of Iranian politics. The regime's legitimacy both inside and outside its borders will depend on its ability to prepare for such a scenario. A change of events in favour of a continuation of the nuclear deal would allow for the current unrest to cool off. However, in regards to the state of individual liberties, it does not seem feasible much would be done before the end of Khamenei's rule.

3.3. Upcoming elections

Iran will hold in the next two years both parliamentary and presidential elections. Amidst the current turbulent political, economic and social situation, it is hard to predict what could happen as different scenarios could take place. This section will attempt to shed some light on how the electoral system works, what has happened until now and what could be the most likely scenarios in the future.

3.3.1. Electoral system

Iranian law establishes that the president is the second-in-command after the Supreme Leader. He is the chief executive and is in charge of implementing the constitution. The treasury is at his disposal and the legislature, judiciary and armed forces receive their budget directly from the president's administration. The Guardian Council, a body composed of 6 clerics and 6 jurists, which could be the equivalent of a Western supreme court, has the power to veto any candidature that they reckon to be inappropriate. In the last 2017 election, only 6 of the more than 1.600 registered were given approval⁴⁸. All women were disregarded. Elections are held on a Friday where any Iranian over the age of 18 can vote. The candidate that obtains an absolute majority wins. If that percentage is not reached, a second round will be held between the first two. Once elected the president will then choose 18 ministers to form government. The law establishes a limit of two consecutive terms.

The Iranian parliament or Majlis, as it are commonly known, is in charge of legislation and oversight of the executive. However, it has limited competence. The Guardian Council has the power to veto any law permanently. In fact, due to this constant conflict between the Majlis and the Guardian Council a third legislative body, the Expediency Council, was created to mediate between the two. The president's signature is then required for a law to come in place. The Majlis also approve the annual budget, scrutinise the ministers, may impeach the president and approve international treaties⁴⁹. 290 members are elected by direct popular vote every four years. In addition, 5 extra seats are reserved for the representation of religious minorities. As it was the case with the presidential election, the Guardian Council has to approve all candidates.

3.3.2. Background

In the past presidential elections of 2013 and 2017, current president Rouhani was elected by wide margins. The nuclear deal was a key component of his reelection campaign, an unprecedented approach between the two countries in the post-revolution era. However, Trump's irruption in the White House along with the later withdrawn from the agreement and reimposition of sanctions has been costly for the Iranian government. Street demonstrations as previously discussed have created a climax of tension that benefits the opposition. Back in August, Rouhani was summoned to parliament for the first time and faced an intense interrogation from MPs over high unemployment, rising food prices and inflation. In response, he stated that "More important than that [poor economic situation] is that many people have lost their faith in the future of the Islamic Republic and are in doubt about its power"⁵⁰.

In regards to the Majlis elections, it is worth noting that although political parties exist, coalitions are usually formed around two main poles, the more conservative who support a higher role of the Supreme Leader, and the more progressive-minded reformists⁵¹. The nuclear deal also had an impact on the 2016 parliamentary election. Reformists and moderate conservatives won a majority against hardliners. Another key element is that the moderate faction also won a majority in the Assembly of Experts, the 88-member body that is in charge of electing the next Supreme Leader. This organ is elected every 8 years and with the current delicate health state of Khamenei's, who recently went through prostate surgery, it could play a vital role in the future of the regime⁵².

3.3.3. Future prospect

Due to Iran's strict procedures in the appointment of candidates for both presidential and parliamentary elections, it is almost impossible to determine the names of the candidates that will be running. However, what can be identified in both electoral processes, is the ideological basis of the winners.

Scenario 1: Moderation (most likely)

Although the current course of events suggests that Iranian politics may undergo a transition towards a more radical approach, there are still reasons to believe moderates will retain power. The outcome will very much depend on how the nuclear deal issue is solved. The European Union has repeatedly shown its support for the agreement and is constantly working on ways for it to continue in place. There have been several protests against the current government, but that renovation could be found within politicians of the same ideological faction. Progressive candidates could take advantage of both the population's discontent and international pressure for a more democratic and liberalised system. This could also be backed by a growing opposition for Donald Trump in the US who will have to act carefully before the US presidential elections of 2020. Both Iran and the EU are hoping that a change in US leadership will improve things considerably, as they will be held before the Iranian.

Scenario 2: Radicalization

The opposition has gained strength in the last months due to the regime's instability. The poor performance of the economy and the growing social unrest have created an opportunity for hardliners to step in and take control. The West has proved yet again to be untrustworthy. Ebrahim Raisi, who already competed against Rouhani in 2017, could use the failure of the JCPOA as the most powerful tool for his campaign. As custodian of the Astan Quds Razavi^{vii}, he has the advocates of radical Islam on his side. There are even speculations of him being one of the possible successors of Khamenei, so winning the election would be a huge milestone in his career. However, the outcome of US elections will influence the situation in Iran. If Trump stays in power, it is very likely that Iranian society will adopt a more radical approach triggered by the consequences of sanctions. In this scenario, the Islamic Revolutionary Guard Corps could play a vital role. US threats to brand the IRGC as a terrorist group has infuriated Tehran and could elevate the possibilities of an armed conflict. The body has never had good relations /

^{vii} Wealthiest charity in the Muslim world. The organisation is also in charge of Iran's holiest shrine, Imam Reza, in Mashhad. Retrieved from <https://www.theguardian.com/world/2017/may/16/iran-presidential-elections-everything-you-need-to-know>

with Rouhani due to their radical anti-Western ideology, which was contradicted by the president's approach with the US and the EU. The IRGC have grown in political activity in the last decades contrary to Khomeini's initial wishes and hardline candidates could use their power to repress any social protest as it already happened in 2009.

3.4. Geopolitical analysis

Resting at the heart of the Middle East, Iran is surrounded by neighbours in a key strategic position. It borders Iraq, Turkey, Armenia and Azerbaijan to the west and northwest, Turkmenistan to the northeast, and both Pakistan and Afghanistan to the east. It also shares maritime borders with Bahrein, Kuwait, Qatar, Oman, Saudi Arabia and the United Arab Emirates. From a geopolitical perspective, having so many neighbours in such a volatile region poses a constant threat over the security of the country. To tackle its foreign affairs, Iran first faces the challenge of managing the regional upheavals by ethnic minorities in those bordering areas.

3.4.1. Differences across provinces

Iran is divided into 5 regions and 31 provinces. Each of these provinces varies greatly from one another in terms of ethnicity, resources and development. A report⁵³ published by the Iranian Journal of Public Health in 2013, analysed the distribution of resources across Iranian provinces in regards to their Human Development Index. The results found that even though Iran's HDI as a country was high, inequality among provinces had increased. Distribution of natural resources is one of the main causes of this disparity. The government has tried to implement measures to mitigate the differences across oil-rich provinces, such as Bushehr and Khuzestan, and the underprivileged, such as Ilam and Kohgiluyeh & Boyer-Ahmad. In 2006, a rule established that one per cent of oil income would be distributed to the inhabitants of the provinces that did not have such resources. However, the measure increased migration to those provinces, negatively affecting neighbouring areas. More counter-effects have emerged from government policies. Subsidies programs directed at almost every Iranian regardless of their income or social status, have left inequality untouched⁵⁴. This poor distribution has had a huge impact on the stability of the country. The previously discussed street /

demonstrations were heavily influenced by these differences. As opposed to those of 2009, protests in Iran are occurring throughout the five regions and will likely keep on happening at least until the upcoming elections. There are some specific cases to which the regime needs to pay special attention to.

Figure 3.1. Main protests in Iran (2018) and ethnic minorities' population⁵⁵



Iran-Iraq border: the Khuzestan case

Iraq shares its entire eastern border with the Iranian provinces of West Azerbaijan, Kurdistan, Kermanshah, Ilam and Khuzestan. This border was mutually recognised in 1847 after decades of disputes⁵⁶. However, more recent time have also witnessed the /

consequences of war. The Iran-Iraq war of 1980-1988 had huge implications for the current situation of the region. Khuzestan province was a key strategic point for the conflict. The territory comprises the highest concentration of energy resources in the country, with an estimated 85% of oil reserves and 60% of gas reserves⁵⁷. However, this has not translated into economic prosperity for its citizens, being the province with the third-highest rate of unemployment⁵⁸. The province is populated by Iranian-Arabs, who account for less than 2% of the total population⁵⁹. It was precisely these ethnic roots that motivated Saddam Hussein to take control over the region during the war. The province suffered greatly from the conflict, which caused the death of thousands of inhabitants and destroyed several cities. Iran finally managed to keep control over the region but instability has remained fuelled by political, social and economic marginalization. Several separatist movements often supported by foreign powers in an attempt to destabilise the country have emerged in the last decades. However, despite general unrest, secessionists lack the support of the majority who identify themselves as Arabs but also Iranians. Whatever the case, it is clear that the situation in Khuzestan is a source of instability for the regime and should be taken into account for the future of the country.

Iran-Afghanistan-Pakistan border: the Balochistan case

The region known as Balochistan is currently divided between the borders of Iran, Afghanistan and Pakistan. It is inhabited by the Baloch people, whose culture dates back to ancient times. The region holds enormous deposits of gas, gold and copper, untapped sources of oil and uranium, as well as 1000 km of coastline near the entrance to the Strait of Hormuz⁶⁰. However, this has not translated into prosperity for its inhabitants who live in deplorable conditions at each side of the border. In Iran, the Baloch live in the Sistan & Baluchestan province, the poorest in the country by far. It has the lowest per capita income in Iran, causing 80% of its population to live below the poverty line⁶¹. The systematic discrimination against this Sunni minority has triggered the creation of radical groups fighting for their independence. Their neighbours in both Pakistan and Afghanistan have experienced a similar situation. The Taliban have heavily repressed Balochis in fear of their secessionist goals, which has triggered several terrorist attacks. In March 2019, the Baloch Liberation Tigers, which is a pro- /

independence group, claimed the responsibility for a railway blast in the Balochistan province of Pakistan where four people were killed⁶². In addition, the border between the three countries has a huge problem with drug trafficking. Afghanistan produces 90% of the world's illicit opium, which is delivered through Iran. This has cost Iran not only the lives of 4.000 security forces but it has also created a huge addiction problem in the country itself⁶³. It seems evident that the region is a significant source of instability for the Iranian regime, and unless a more inclusive approach is taken to allow the region to develop, it could become a major source of conflict not only in Iran but in the whole region.

Iran-Azerbaijan border: the Azeris case

The border region between Iran and Azerbaijan is a high-voltage zone. The area is majorly populated by the Azeris, Iran's largest ethnic minority, which are estimated to account for 25% of the total population⁶⁴. There are three times more Azeris in Iran than in Azerbaijan itself. Although this particular group has not caused as much struggle as the minorities previously discussed, tension has recently escalated. Azeris are mainly Shi'a, a fact that has contributed to their relatively quiet coexistence with the rest of Iranians, however, Azeris have long suffered discrimination on the media and other platforms. The use of their language has been highly restricted in education, leading to several protests registered by the World Directory of Minorities and Indigenous Peoples⁶⁵. The key for Iran though lies in Azerbaijan's increasing relation with Israel. Both countries have strengthened ties by exchanging gas and oil from Azerbaijan to Israel who in turn receives weapons and intelligence technology. Iran perceives this as a threat and is afraid that its own Azeri population could be turned against the regime by Israeli influence. The situation does not seem serious enough to cause conflict in the short term, yet Iran should pay close attention to the issue for their medium and long-term security.

Iran-Turkey border: the Kurds case

The Kurdish cause has gained international reach due to their participation in the Syrian conflict. Their fight for independence in the bordering territories of Turkey and Iraq are

well-known. This issue has also affected Iran to a certain degree, although its Kurdish population is relatively low compared to that of its neighbours. As every minority in Iran, Kurds have suffered from repression and restriction of their culture. This has in some occasions translated into violent encounters with the authorities. Amnesty International has reported the executions of several Kurds sentenced to death in Iranian prisons after dubious trials⁶⁶. The situation of the Kurds will be likely affected by the aftermath of the Syrian conflict, which seems to be coming to an end. It is not amongst Iran's first concerns but it cannot be put aside for too long or a new regional conflict could burst out.

4. IRAN-US RELATIONS

The signing of the Joint Comprehensive Plan of Action (JCPOA) in 2015 was undoubtedly a major milestone in the context of Western-Middle East relations. Since the 1979 revolution, Iran had been identified by the United States as a dangerous enemy to US interests. George W. Bush made it clear in his 2002 State of the Union speech when referring to Iran, Iraq and North Korea as the “axis of evil”. After decades of enmity, Barack Obama came to power and initiated an unprecedented approach towards the Islamic Republic of Iran. Followed by an internationally supported period of heavy sanctions in 2010-2013, Iranian officials initiated talks with US representatives in Oman to begin drafting a hypothetical agreement. Hassan Rouhani bet for this option and made it the central argument of his 2013 election campaign. His victory was key to achieve the accord.

Article IV of the JCPOA’s preface stated that its success “will enable Iran to fully enjoy its right to nuclear energy for peaceful purposes under the relevant articles of the nuclear Non-Proliferation Treaty (NPT) in line with its obligations therein, and the Iranian nuclear programme will be treated in the same manner as that of any other non-nuclear-weapon state party to the NPT”. However, the agreement received broad criticism from the opposition in both Iran and the United States. The change of US administration only a year later the treaty was signed, started a phase of uncertainty in regards to the agreement’s durability. Trump’s threats became real on May 8th, 2018, when he announced that the United States would withdraw from the JCPOA and reimpose all secondary sanctions that were in place before the accord. This section will attempt to identify the motivations behind US moves and map the different scenarios that could take place in the short and medium term.

4.1. US strategy

The strategy followed by the Trump administration, outlined in a report by the Congressional Research Service, aims to put pressure on the Iranian economy to the point where they have no other choice but to renegotiate a new deal. This updated /

agreement would be used by the United States to limit Iran's military presence in the region and stop, or at least reduce, its ballistic missile program and nuclear development. Iran is regarded by the US as a funder of terrorism in the Middle East that supports pro-Iranian governments and armed factions. It is also developing nuclear-capable missiles in defiance of UN Resolution 2231 and could still maintain the ambition of developing a nuclear weapon. The US also accuses Iran of conducting illicit financial activities and cyberattacks. In addition, human rights related issues are often used as an argument for US hostility towards the Islamic Republic.

To achieve its goals, the US has reimposed all secondary sanctions that were in place before the deal was signed. These penalties aim to reduce Iranian oil exports to zero to choke the Iranian economy. This loss of revenue is expected to affect the budget devoted to spread the Iranian influence in the region and the development of conventional and unconventional weapons, such as ballistic missiles or small fast-attacks crafts prepared for asymmetrical warfare in the Gulf. In addition, the marginal economic ties between US and Iran incentivizes the reimposition of sanctions by the US administration, as they do not affect the domestic economy, in contrast to the EU case. However, this has not been the only measure that the US has taken. In addition, the Trump Administration has opted for maintaining a strong US military presence in the region, with around 35,000 U.S. forces deployed to Persian Gulf states' military facilities. This move is part of the US strategy to enhance capacities of allied governments and supporting their actions against Iranian activity. US financial assistance of \$1.34 billions during 2011-2016 period to the Iron Dome short-range anti-rocket system is a clear example.

Renegotiation of the agreement will only be carried out by the US under certain conditions and Iran is not willing to cooperate, at least, with Trump's Administration. The conditions Iran has to satisfy were addressed by Secretary of State Michael Pompeo in the Heritage Foundation in May 2018. In that speech, Pompeo stated twelve points the Islamic Republic should comply with in order to renegotiate the JCPOA. These twelve points could be summed up in the following demands:

- Dismantling all nuclear infrastructure.
- Ending development of nuclear-capable ballistic missiles.
- End support to terrorist groups and regional armed factions, including Afghan Taliban.
- Completely withdraw its forces and militias from Syria.
- Release all U.S. citizens and dual nationals.

On the other hand, as mentioned above, neither Iran is willing to renegotiate the deal. Tehran has demonstrated its compliance with what was established in the JCPOA, specifically in nuclear issues, as the International Atomic Energy Agency (IAEA) has reiterated eight times. The Islamic Republic has dismantled more than two-thirds of installed centrifuges and shipped out 98% of its enriched uranium. Iran is also implementing the IAEA's Additional Protocol, which subjects it to restrictions and strict monitoring regime. Furthermore, the EU has also showed its rejection for a renegotiation of the deal, which enhances Iran's position.

There are some who argue that the US strategy has the hidden objective of overthrowing the Iranian regime. It is evident that no United States government has completely accepted the Iranian system of government since the 1979 revolution. Opposition was clear until Barack Obama opted for a more tolerant approach by acknowledging the country as the Islamic Republic of Iran for the first time. However, during the 2009 Green Movement protests, the US president showed public support to the demonstrators with a message directed to the Iranian youth: "young people of Iran... I want you to know that I am with you". The negotiations of the JCPOA contributed to a wider international acceptance of Iran's regime for the viability of the agreement. The current administration has officially declared that it does not seek a regime change but a shift in behaviour instead. Yet some speeches by Secretary of State Pompeo suggest that even if the US may not directly participate in a direct intervention to overthrow the regime, it would surely support a transition towards a more democratic and liberalised state demanded by its own population. This latter option seems like the most reasonable taken into account the outcomes that regime changes have had in Middle East countries in the last years.

The US currently finds itself in a very comfortable position for two reasons: the reimposition of sanctions are putting Iranian economy on the verge and at the same time Iran remains a part of the JCPOA, which legally guarantees their commitment not to develop enriched uranium at least until 2025. This suggests that Iran has a more urgent need to change the course of events to recover from its current situation.

Table 4.1. Iran-US relation scenarios

	DÉTENTE	DISENGAGEMENT	RADICALIZATION
US presidential election (2020)	Democrats win the elections thanks to a huge mobilization of its voters against a Trump's second term.	Trump remains in office. A highly divided democrat vote in the party primaries, frees the way to victory for Republicans.	Trump remains in office. His unfiltered approach does well again among certain sectors of society and the lack of an strong opposition candidate gives him the win.
Iran presidential election (2021)	The US change in government gives moderates a second chance to convince their population and they retain power.	Despite the US continuity in government, Iran's strengthening ties with Europe + China + Russia, gives moderates enough support to continue in power.	Hardliners take advantage of the poor economic and social situation and win the elections. The candidates' screening leaves the population no choice but to vote for that option.
Iran's internal situation	Sanctions are lifted and economic growth leads to social stability. Hardliners lose political support among Iranians.	The effects of sanctions are mitigated. Social unrest decreases but hardliner opposition remains strong.	Iran enters into deep recession triggering social unrest and political repression. The nuclear program resumes high level uranium enrichment.
European role	New wave of EU investments and trade in Iran. The EU supports negotiations and a rapprochement towards the Islamic Republic.	EU develops financial mechanisms with other States to bypass US sanctions. EU-US relations deteriorate as a consequence of strategic disagreement on Middle East policy.	The EU supports US positions on counteract Iran's foreign policy and nuclear program. Furthermore, the EU complies with US sanctions.
Chinese and Russian role	China and Russia support the renewal proposal to safely trade with Iran. China and Russia won't disengage from the EU and the US and will cooperate with the international community.	International cooperation against US extraterritorial sanctions with Iran and the EU. Increasing presence in the Middle East through a strong Sino-Russian alliance backed by the UN. UN Blockage of the UNSC	Strengthening of the Sino-Russian alliance and support of Iranian position to undermine US power. China is motivated by economic guarantees and Russia by the strategic presence in the region. Blockage of the UNSC
Future of the JCPOA	The US rejoins the JCPOA and there is a proposal of renewal under multilateral negotiations.	Continuity of JCPOA without the US and proposal of renewal.	Iran leaves JCPOA and it leads to its termination without further negotiations.
Regional context	Iran's foreign policy balances to a more conciliatory approach prioritizing economic interests over ideological ones. The end of the Syrian Civil War reduces regional tensions. Progressive disengagement of US from the Middle East.	Cold war between Saudi Arabia's coalition and Iran, backed by Russia and China, without direct military conflict. Fragile regional stability subjected to deterrence of a total war.	Saudi-Iran relations escalation of tension. Iran intensifies intervention in proxy war despite economic hardship and hardliners propose the closure of Hormuz Strait.

CONCLUSIONS

The present report has attempted to provide an analysis of Iran by addressing: (1) the consequences of sanctions, (2) the current and future state of its energy sector, (3) the internal situation of the country and (4) the future prospect of the Iran-US relations.

1. In regards to the effect that sanctions have occasioned, this report has stressed the unwillingness of Iran to comply with the reimposed US sanctions. Furthermore the European Union will seek to provide Iran commercial alternatives to circumvent sanctions. Washington might find itself isolated because of the opposition of global and regional powers such as China, India, Russia and Turkey to comply with the reimposed secondary sanctions. As a consequence, US international leadership will be in the spotlight and other powers such as China, could replace the US seat as the big elephant in the room. Notwithstanding, the Great Asian power is becoming a commercial alternative for Iran even if in the future the JCPOA fails, and its presence in the Middle East may banish US influence in the region. The economic consequences are going to be determined by what happens in the political arena. However, forecasts sign, no matter the political events, at least in the short-term, a decrease in the economy portrayed in the GDP growth, unemployment and balance of trade in the upcoming years.

2. Iran's energy sector, as one of the main targets of US sanctions, will see its revenues fall meanwhile foreign investment and technology stop flowing into the country. The effects of this financial shortage, added to the previous international sanctions during 2012-2015 period, will undermine the oil and gas production with negative short and medium-term consequences. The reduction in hydrocarbon export revenues means Rial devaluation, inflation, fiscal disequilibrium and, ultimately, a sharp drop in the living standards of most Iranians. The isolation of the regime from the majority of the regional energy infrastructure, may lead to future frustrations if new export markets need to be found. The huge potential of the oil and gas industry in Iran is not a guarantee for future economic success if the Islamic Republic is not able to develop its foreign policy towards a more pragmatic and a less belligerent approach.

3. The Islamic Republic of Iran is currently facing a serious internal political, economic and social crisis. Despite the numerous effects of sanctions, the regime needs to pay close attention to other internal issues that are causing as much instability in the country. The West-is-to-blame argument will not convince the population much longer and there are already signs that it is not working anymore. Social unrest has grown and it will possibly keep on doing so at least until the upcoming elections. Iranians, especially the youth, are tired of the government's excessive restrictions and advocate for a change towards democratisation. Khamenei's delicate health state suggests that a period of transition will soon come in which the system of government will be surely challenged to the point where some argue no other Supreme Leader would be elected. These prospects will inevitably be affected by Iran's ability to manage the current turbulence.

4. The Iran-US relations are under high pressure. Trump's unilateral decision to withdraw from the JCPOA has left Iran in an uncomfortable position. The Islamic Republic must collaborate with the EU and other potential partners to circumvent sanctions and maintain the agreement in place. The future of the bilateral relationship will be determined by the outcome of both presidential elections in the two countries.

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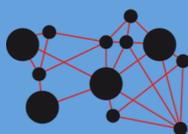
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