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LEADING INDEPENDENT ANALYSIS OF IRAN'S ECONOMY

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In this Issue

- March overview
- Inflation reaches new high
- Impact of 6 February sanctions: Halk Bank
- India to cut imports of Iranian oil
- CBI concerned at impact of oil sanctions
- USD 80 billion inaccessible
- Statistics

March overview

Currency under pressure

Fluctuations in value have continued to plague the Rial. The positive rhetoric following the E3+3 talks with Iran in Almaty at the start of March led to a temporary rise in the value of the Rial. On 5 March, the rate was reported to have reached IRR 32,700:1 USD, up from a low of IRR 38,000:1USD in the previous week. The news since, however, has been less positive. Iranian officials have moved to suggest the prospects for a deal on the nuclear programme remain as far away as ever. Oil exports remain far below their 2012 level, and media reporting has demonstrated how billions of dollars of oil revenues and assets remain beyond Iran's reach. By 19 March, the rate had fallen to IRR 33,700:1 USD. Without a breakthrough in the next Almaty talks, on 5-6 April, VERITY expects the Rial to continue to fall against the dollar, particularly as the consequences of the measures introduced by the US on 6 February become more apparent.

Budget delay

A three-month interim spending bill was approved by the Guardian Council and the Majlis on 17 March, to allow the government to continue to function on the basis of revenue and expenditure as set out in the previous budget. The Majlis refused to consider the full budget bill after it was submitted by the government 84 days late, a record-breaking delay. An earlier attempt by the Majlis to pass an interim spending bill had been rejected by the Guardian Council because it neglected to account for the June 2013 Presidential Election.

The full budget bill included a plan by President Ahmadinejad to issue USD 10 billion in bonds to raise money for energy projects. Those plans must now be in doubt. The budget is unlikely to be approved before July, by which time

Iran will have voted in Iran's next President.

VERITY Exclusive: Inflation reaches new high

CBI Governor Bahmani has admitted publicly that inflation has risen to about 32%. Privately, VERITY has learned, the CBI estimates that the true nationwide rate of inflation is in excess of 70%. The government, however, will not let the published rate exceed 35% for the time being.

Impact of 6 February sanctions: Halk Bank

Halk Bank has continued to comply with the US measures implemented on 6 February. Bank officials have refused to process third country oil payments for Iranian oil. VERITY has learned that the absence of EUR payments from Indian customers, in particular, has resulted in a shortage of revenues for the Turkish Bank. Halk Bank currently has insufficient funds to honour several billion dollars worth of Letters of Credit issued on behalf of Iranian customers.

India to cut imports of Iranian oil

Indian daily, *The Hindu*, reported on 18 March that India may cut imports of Iranian oil by 27% this fiscal year, because US and EU sanctions have made it difficult to ship Iranian oil. Separately, *Reuters* reported on 8 March that insurance concerns might force India to halt all crude imports from Iran. The biggest beneficiary of a halt in Iranian oil exports to India may be Iraq; Iraqi oil is a similar grade to Iranian. *The Hindu* reported that Iraq is now exporting nearly double Iran's exports.

The Iraqi experience offers a cautionary tale for potential investors in Iranian oil. Iraqi underinvestment in its oilfields from the First Gulf War until after the fall of Saddam Hussein, ruined Iraqi oil production and refinement facilities, and ultimately cost Iraq its place in the oil market. It has taken almost a decade of massive foreign investment and expertise for Iraq to begin to recover. VERITY has reported previously and often on the inadequate investment of the Iranian government in maintaining and developing existing oil fields, and identifying new oil fields. Iran's existing fields are ageing and in decline. Once identified, it can take between 5 and 15 years, and considerable investment, to develop new fields. With sanctions unlikely to disappear soon, VERITY judges it will take Iran even longer to return to its former place in the market.

CBI concerned at impact of oil sanctions

VERITY has learnt that senior Iranian officials assess that the various sanctions imposed on Iran are creating problems for receiving banking services, including in oil and oil product sale revenues. From early 2012 through the end of the year, the revenue from oil sales decreased nearly by half. The Iranian officials are concerned that a continuation of current conditions could cause long-term, and possibly permanent, damage to foreign currency reserves, and harm Iran's ability to meet its foreign currency liabilities.

USD 80 billion reserves inaccessible

More than USD 80 billion of CBI reserves held outside Iran are now inaccessible, VERITY's sources have reported, further adding to Iran's liquidity crisis. This money is either frozen, blocked or in long-term non-disposable assets. CBI officials are trying to access and move these reserves, but, with no end to banking sanctions in sight, the prospects for unblocking these funds appear increasingly remote.

As noted in our monthly overview the Rial has weakened again following its short bounce at the time of the initial Almaty talks. As the pressure on the currency continues to build and with no solution to the nuclear problem in sight, the government will find it increasingly difficult to sustain the official exchange rate (IRR 12,260) for imports of food and medicine. Over the coming months the currency centre rate (IRR 24,580), currently used for imports of livestock, metals and minerals, may be used for food and medicine too. Effectively abolishing the official rate in this way, however, may prove too embarrassing for the Government pre-election. VERITY expects to see the free market rate drift until the Government is compelled to take action.

Statistics

GDP Growth
-0.9% (IMF estimate for 2012)
0.8% (IMF estimate for 2013, as of October 2012)

Inflation
Estimated at c.75% across Iran
vs. Official figure: 32%

Liquidity Growth
Estimated to be 25%+ for 2012
vs. 21% (Official estimate)

Unemployment
Between 30-35%
Vs. Official figure: 14.1%

Exchange Rates
Rial:USD
CBI figure: IRR12,260:USD1
Currency Centre rate: IRR 24,580: USD1
vs. Unofficial rate: c.IRR 33,700:USD1