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JCPOA still worth fighting for

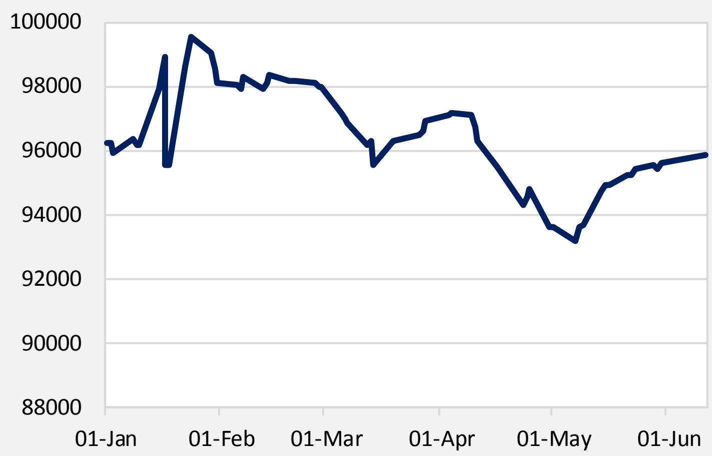
There is *widespread international agreement that the US withdrawal from the nuclear deal was without grounds, but Iranian businesses will need to see tangible commitments from its European partners to accompany those political statements. Iran has made clear what it needs from European partners to keep the JCPOA alive. But Iran has a role to play too. Its regional military footprint, ballistic missile programme and plans to expand nuclear enrichment will quickly stifle what remains of the deal.*

"Impulsive, unlawful and provocative" is how Iranian Foreign Minister Zarif described the US withdrawal from the nuclear deal in a letter to the remaining signatory nations. In the month since President Trump's announcement, Iran's leading diplomats have made their case to a broadly sympathetic international audience that the termination of the JCPOA is unjust. But they have also acknowledged that political commitments from foreign leaders can only take them so far. Iran's leaders have stated that they will effectively withdraw from the agreement themselves unless they see those commitments turned into tangible measures.

Iran has set out in no uncertain terms what it demands from European partners to keep the deal alive. The primary ask is for the European Union to "stand up" to US sanctions. The extraterritorial powers of the US Treasury mean it can effectively punish companies anywhere in the world for breaching US unilateral sanctions. The European Union is exploring the feasibility of blocking those measures within their own legal jurisdiction to provide protection for EU companies. This was done successful in the 1990s in response to US sanctions against Cuba, but the US legal framework has since grown more complex.

The progress of a small group of major European companies active in Iran, such as Total and Peugeot, will be crucial. French car-maker, Peugeot, announced its plans to wind down its joint-venture activities in Iran by August, reversing the commitments it made in the wake of the 2016 deal. French oil giant, Total, has also publicly considered withdrawing from the international consortium agreement it entered to develop the South Pars Phase 11. The National Iranian Oil Company has offered Total a limited window for deliberations before it seeks alternative investors to take over its stake, with some interest already announced from a Chinese partner. Just as significantly, albeit with less fanfare, the likely withdrawal of major European insurance firms from commitments in Iran will leave a substantial gap in the market.

Fig 1. TEDPIX (All Shares) index
1 January 2018 to present



Iran has also demanded guarantees that its oil exports and banking relations endure. Currently less than one third of Iranian oil exports go to Europe, but the pivotal role played by European entities in insurance, shipping and payments means their influence extends far beyond that share. In banking, European authorities are considering euro-denominated oil trade, new credit lines with Iranian banks and new energy cooperation agreements. The designation of CBI governor Valiollah Seif following Mr Trump's announcement, for allegedly assisting Iran's Islamic Revolutionary Guards Force (IRGC), demonstrates the complexities these sanctions present. European banks and financial authorities will have to navigate a treacherous (and potentially expensive) path to sustain meaningful financial cooperation with Iran.

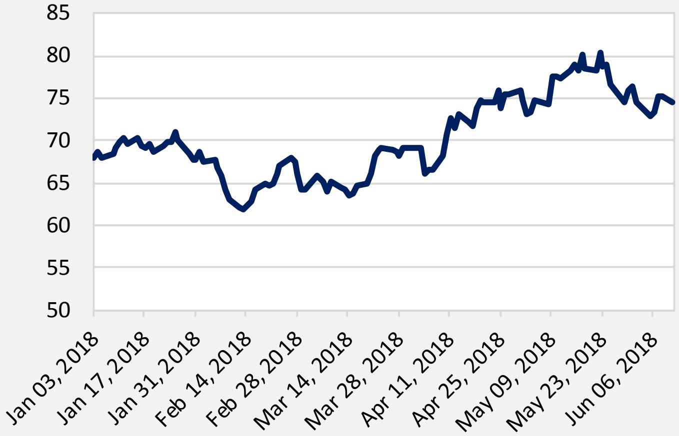
Fig 2. Iranian Rial exchange rate

(Rial to USD) 1st April 2018to present

In addition, the Supreme Leader insisted that the Iran's missile defence and presence in the region's countries was not up for negotiation. He insisted in a high-profile address to senior officials that control over the Islamic Republic's defensive capabilities is something it cannot give up, stating that "no sane government would".

Fig 3. Brent Crude spot price

(FOB, Dollars per barrel, 1st January to present)



Unfortunately, the good will required to maintain the JCPOA will largely depend on Iran's military posture. Whilst outside the terms of the JCPOA, it was objections over Iran's missile capabilities and regional military activity that created the dynamics for the US withdrawal. For the EU3 to deliver on the various financial, energy and business aspects of the JCPOA, they will need a considerable degree of leeway from their US counterparts. By announcing plans to restart uranium enrichment at its Fordow plant and install new centrifuges at Natanz, Iran is effectively weakening the EU's hand in those discussions. An EU spokesperson commented that whilst not a violation of the terms of the JCPOA per se, Iran's recent statements and actions on its nuclear programme handicap the case that European diplomats can make in Washington DC to build confidence in the nature of the programme.

Nevertheless, a post-US version of the JCPOA is, at this stage, still a cause worth fighting for. The Majles Research Centre recently released a new study on capital flight, identifying that $60bn had been sent abroad in the last two years. That is equivalent to 83 percent of Iran's annual non-oil export revenues and will surely worsen if Iran heads back down the road to economic isolation. One has to look back only five years to recall the damage such isolation did to the Iranian economy: rapid depreciation in the exchange rate driving up inflation in imported products, which lowered living standards for Iran's lower and middle income families; cash-flow crises in business as the most lucrative export revenues dried up and industries failed to access foreign exchange; economic stagnation as foreign investors withdraw from new ventures in manufacturing, energy and transport; knock-on effects through the banking sector as credit default rates rose, exposing woefully inadequate capital ratios and leading to a credit crunch – at risk of a widespread default. The hard won progress the Rouhani administration has made in settling inflation and stabilising the financial system could be quickly undone. The likelihood of this dismal scenario will be determined by progress with international partners, especially in Europe, in the coming weeks.