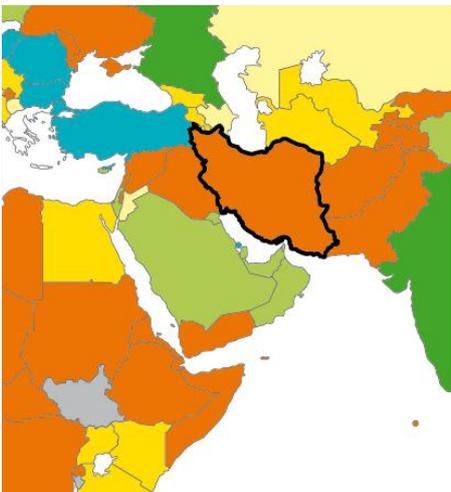
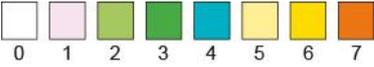


# Iran

	<b>COUNTRY RISK CATEGORY</b> <h2>7/7</h2> <p>The country risk categories range from 0 to 7. The lower the number the better the credit rating the country has.</p> 	<b>EKN'S POLICY</b> <b>Sovereign risks:</b> No provision of guarantees <b>Other public risks:</b> No provision of guarantees <b>Bank risks:</b> No provision of guarantees <b>Corporate risks:</b> No provision of guarantees <p style="text-align: right;">See "EKN'S POLICY" section</p>
	<b>EKN'S OUTSTANDING GUARANTEES IN THE COUNTRY</b> <b>Short-term transactions:</b> SEK 0 million <b>Medium and long-term transactions:</b> SEK 1,449 million	<b>DATE</b> <b>14/05/2013</b>

## Sanctions isolating Iran

The presidential elections in June will likely result in a winner from the conservative camp as reformist candidates have been rejected as candidates for election. The green protest movement is weakened and is expected to play a minor role. Talks between Iran and world powers on its nuclear programme continue, but a breakthrough is not likely in the coming year. The sanctions by the US and EU against Iran's oil and banking sector are slowly breaking down the economy as oil exports decline and the country's financial system is isolated. A total economic collapse is remote in that the state controls the economy, but the more time that passes without a political solution, the harder the recovery will be when sanctions are eased. EKN remains closed for new guarantees for Iran.

### STRENGTHS

- Very large oil and gas reserves.
- Strong international reserves.
- Low public and external debt.

### WEAKNESSES

- The sanctions are posing serious difficulties for payments from Iran.
- Mismanaged economy with inflation, currency speculation and unemployment as a result.
- Reduced oil exports are suppressing growth and investment.
- Iran's problematic relationship with the outside world.

## POLITICS

**Presidential elections and nuclear negotiations**

The religious leadership will, by all accounts, prevent reformist candidates from participating in the presidential elections in June 2013. Retiring President Mahmoud Ahmadinejad's own candidate is likely to be refused participation, reflecting Ahmadinejad's deteriorating relationship with Iran's supreme leader, Ayatollah Ali Khamenei. The weakened green protest movement, that demonstrated against fraud in the 2009 presidential elections is expected to play a minor role. The regime's credibility has fallen following the failure in attempts to deal with the economic crisis, but none of the green movement's candidates will be participating in the elections and many of its leaders are in exile, in prison or under house arrest. The popularity of the movement among the people has declined because of the oppression of the regime and that the movement lacks a charismatic leader. The election will likely result in a winner from the conservative camp. There are political differences within this group, but there is no will or capacity to challenge the prevailing political system.

The US has used its influence over the international financial system to create some of the most comprehensive sanctions ever. The aim is to force Iran to the negotiating table and get the country to suspend its nuclear programme. The regime admits that sanctions are having a negative impact on the economy, but this has not stopped Iran's nuclear programme. The domestic political environment, where every concession in the negotiations leads to accusations of a capitulation to the West, is hampering an agreement. Ayatollah Khamenei depicts the US and EU as brutal and immoral countries trying to keep Iran dependent on the West. This continues to characterise the approach of the Iranian political elite. A deal with the West must not only be acceptable to the political elite, but it must also be presented as a victory. The prospects for a deal are small in the short term, especially given that any decisions regarding the nuclear programme are taken by the highest religious leadership.

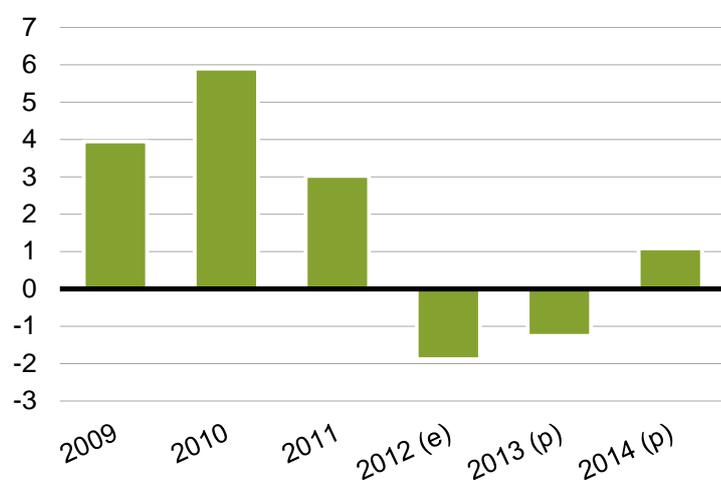
The likelihood of a US or Israeli military strike against Iran's nuclear facilities in 2013 is very small. Diplomacy and continued negotiations are limiting the risk of military interventions and US President Obama seems to have calmed the Israelis by stating the US's determination to prevent Iran's nuclear ambitions.

## ECONOMY

**Sanctions gradually breaking down the economy**

Exports of oil and petroleum products, Iran's primary source of revenue, have dropped significantly following an EU boycott along with a decline in sales to the Middle East and East Asia. Oil production has fallen to its lowest level since the war with Iraq in the 1980s and will continue to decline in 2013. Falling oil production has contributed to economic stagnation in 2012 and will restrict growth next year. The loss of oil revenues has had serious consequences with the hoarding of commodities and speculative attacks on the currency as a result. The informal economy, which has always operated in parallel with the state-dominated economy, has been crucial for the supply of essential goods and services. A continued impasse in nuclear negotiations will lead to further deterioration in Iran's economic situation with the exodus of capital to the black market as a result.

## GDP GROWTH (% PER YEAR)



*Declining oil production and high inflation have led to economic stagnation. Data: IMF.*

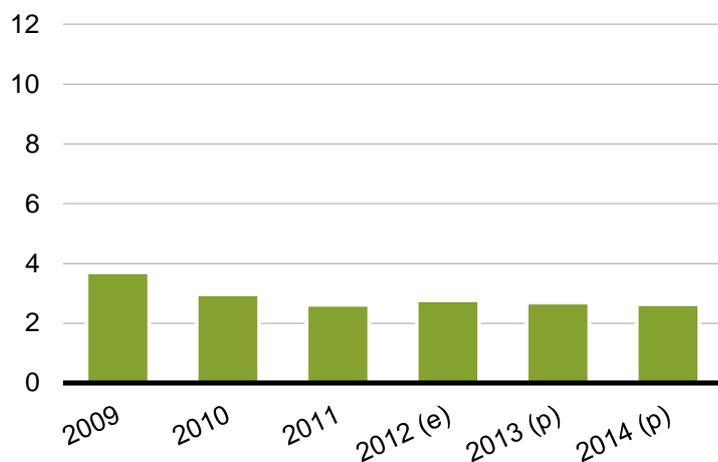
In response to the sanctions, the government has imposed severe restrictions on foreign exchange and import transactions, but political tensions in the run-up to the presidential elections have prevented a more coherent response. A short-term interim budget has been enforced due to the lack of political consensus on the annual budget. In the debated annual budget, government spending will be increased by 28 per cent in nominal terms. Fiscal policy is still tight in real terms as inflation is at 30-40 per cent. Although sanctions and currency depreciation have accelerated price rises, the basic problems stem from further back in time. After the 2008 financial crisis, the government spent its way out of recession with increased public investment and infrastructure projects, and liquidity injections into state banks. Public finances will remain strained as long as sanctions are in place. The increased budget deficit is likely to be financed by the oil fund and increased borrowing from state banks. With an almost non-existent public debt, the risk of a fiscal crisis is low, despite the sanctions.

## BALANCE OF PAYMENTS AND DEBT ISSUES

**Sanctions causing payment problems**

The high oil prices in the 2000s resulted in large current account surpluses, which helped Iran to build up large international reserves and pay off its foreign debt. The impact of sanctions on oil exports is serious as crude oil accounts for about 80 per cent of the country's export earnings. Falling oil revenues with declining foreign investment and increased capital outflows have now begun to deplete the international reserve. In 2011 the reserve was equivalent to 13 months of import coverage but it is expected to drop to only four months in 2014. The low external debt is reducing the need to have large buffers. Capital controls will ensure that the international reserve is not completely eroded.

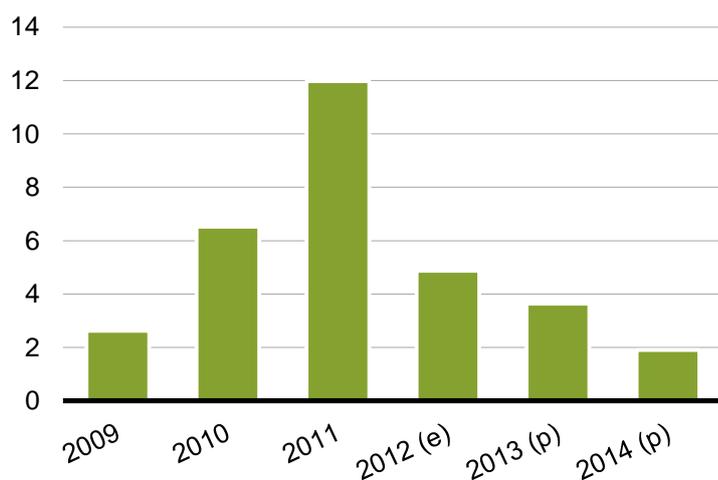
## EXTERNAL DEBT (% OF GDP)



*Iran's external debt is very small in terms of GDP. Data: Datastream.*

The sanctions have led to transactions between Iranian banks and the global financial system being almost completely blocked. Although the willingness to pay and the money is there, international transactions are very difficult to carry out. Iran has to some extent been forced to switch to bartering by selling oil in exchange for raw materials and other commodities. Using import controls and a greater use of domestic financial resources, the regime has still managed to maintain a positive trade and current account balance. Trade with countries that still have normal relations with Iran, particularly China, Russia and India, will still be a factor and will continue to be a source of foreign exchange earnings. Overall, the risk of a balance of payments crisis is restricted by the country's low debt and surpluses in trade with the outside world.

## CURRENT ACCOUNT BALANCE (% OF GDP)



*The current account surplus has declined sharply with the fall in oil exports. Data: IMF.*

## CURRENCY POLICY

**Devaluation and black foreign exchange market**

Through revenues from oil exports, the state, rather than the private sector, is the main recipients and distributors of foreign currency. The central bank is able to control the amount of foreign exchange sold to the domestic market and set the price. This strategy was used during the Iran-Iraq war and has now returned with the introduction of two exchange rates in addition to the official exchange rate. Importers of food, medicine and essential industrial input goods are allowed to purchase foreign exchange at the official and most favourable rate. Other importers are assigned foreign currency at a less favourable exchange rate while the rate on the street is several times more expensive than the official one.

Currency depreciation on the black market is a symptom of a lack of confidence in the currency. The triggering cause was when the central bank began treating importers of staple foods more advantageously. The change was interpreted as a sign that the government was short of foreign exchange, and people began to exchange their Rials for other currencies, which weakened the Rial on the black market. The official exchange rate has been devalued by about 20 per cent since 2010, but a massive collapse is less likely in view of capital controls and international reserves remaining reasonably large. New initiatives from the central bank are unlikely to restore confidence in the currency and the black foreign exchange market will therefore remain.

## FINANCIAL SECTOR

**Banks isolated from the outside world**

The tougher sanctions mean that most of the Iranian banks, including the Central Bank, are blacklisted by the US and EU. The Iranian banks that are listed by the EU are also prohibited the use of the electronic communication tool SWIFT, which makes it difficult for these banks to conduct international business. International payments have been forced away from the banking sector to the unofficial financial networks and Iranian exporters have been forced to barter.

The Iranian state is channelling its oil revenues into the economy mainly through the state banks who have become over-leveraged. The five largest state-owned banks' total lending is 2.5 times greater than their deposits, and eleven times higher than their own capital. Government banks will not be allowed to go bankrupt, but they are forced to lend money to borrowers with poor repayment ability. Data from 2011 indicates that the proportion of bad loans in the banking sector represented 13 per cent of total loans. The percentage is probably higher today. Rising inflation and falling exchange rates have encouraged depositors to withdraw money to buy gold and hard currency. The central bank has raised its key interest rate and is now allowing banks to set deposit rates above the inflation rate, which is helping to retain the deposits of customers in the banking system. Overall, the banking sector is in need of government support, which it almost certainly will get.

## BUSINESS ENVIRONMENT

**Increased difficulties for the corporate sector**

Economic sanctions by the EU and US against Iran have had an adverse impact on the possibilities of doing business in Iran. Currency depreciation and inflation have both led to increasing costs for imports and difficulties for companies to export their products. The sanctions and the lack of hard currency are raising the cost of doing international business in Iran as international payments are difficult to implement. The World Bank classes the Iranian business climate in position 145 of 185 countries, behind the vast majority of countries in the Middle East.

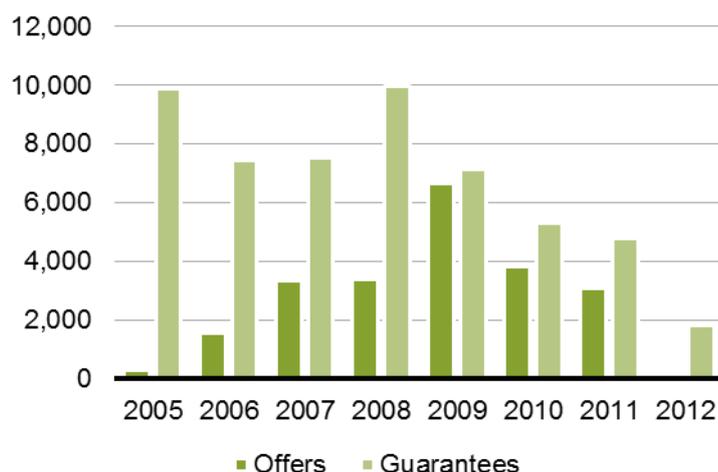
Increased uncertainty about economic policies is impairing the prospects for private investment in the oil and gas sector and in other activities. Sanctions, risk of war and general economic mismanagement have caused most of the major oil companies to delay or halt new investment in exploration and production. Add to this the problems that have emerged due to the Revolutionary Guard strengthening its grip on the economy in recent years by taking control of many larger companies.

## EKN'S EXPOSURE

**Exposure being phased out**

EKN has a large existing exposure in Iran but it is being completely phased out. In the period 2008 until the beginning of 2012, EKN issued guarantees for 232 transactions totalling SEK 12.1 billion for Swedish companies exporting to Iran. Exports have gone to sectors such as petrochemicals, power and transport. All guaranteed transactions have been made in accordance with applicable sanctions and in line with statements from the ISP, the Swedish Agency for Non-Proliferation and Export Controls. EKN is closed to providing new guarantees since early 2012 and no offers are now outstanding.

EXPOSURE AT 31/12 (SEK MILLION)



*Exposure fell substantially in 2012 when EKN became closed for new guarantees. Data EKN*

## PAYMENT EXPERIENCE

**Sanctions obstructing payment**

The current situation where buyers and banks want to pay and have the money, but cannot complete transactions because of sanctions against the country is unique. EKN has visited Iran several times in 2012 to get the views of the banks on the situation. Money is there but the Iranian banks need help finding correspondent banks that are able to transfer the payments. EKN is working with guarantee holding banks to identify these payment channels. Doing business with Iranian buyers where payment is made outside of Iran is more likely to work as the sanction problems with Iranian banks are limited.

EKN has extensive and positive experiences with payments from Iran. Payment problems earlier than the present go as far back as the early 1990s. At that time Iran had liquidity problems due to the very low oil prices. The claims were renegotiated and repayment, including interest on arrears, was made in full after only a few years. Even today, claims are expected to be paid once the sanctions have eased.

## EKN'S POLICY

EKN classifies Iran in country risk category seven, an assessment undertaken in collaboration with the OECD. The country was downgraded from category 6 in early 2012 when EKN also became closed for new provisions for guarantees. The sanctions and resulting payment problems justify a continued closed country policy.

## OFFICIAL COUNTRY DATA AND CREDIT RATINGS

OFFICIAL COUNTRY DATA	CREDIT RATING
<b>Area:</b> 1,648,000 km <sup>2</sup> (3.7 times Sweden) <b>Population:</b> 78.9 million (2012) <b>Population growth:</b> 1.2 % (2012) <b>GDP:</b> USD 482 billion in 2011 (Sweden USD 545 billion in 2011) <b>GDP/capita:</b> USD 6,420 in 2011 (Sweden USD 57,638 in 2011)	Iran has no credit rating from any credit rating agency

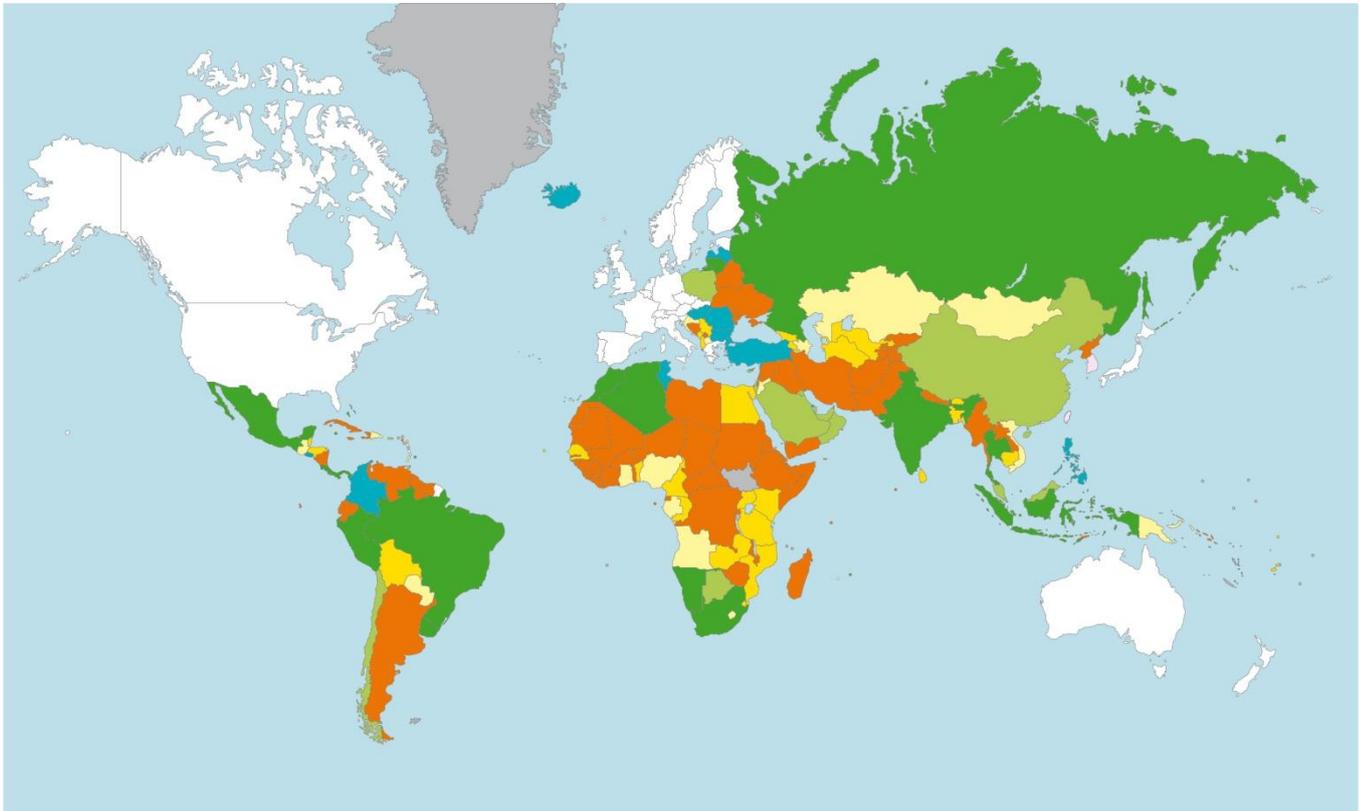
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**DISCLAIMER**

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## EKN'S VIEW OF THE WORLD



The country risk categories range from 0 to 7.

The lower the number the better the credit rating the country has.

**EKN – CREATING CONFIDENCE IN YOUR EXPORTS**

EKN is a government agency that supports Swedish exports and the internationalisation of Swedish industry. This we do by offering exporting companies and banks guarantees for payment and financing, together with advice on business structure and risk management. Our services provide an extra level of confidence, increased competitiveness and more opportunities for successful export transactions.

The Swedish Export Credits Guarantee Board

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