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## Economic Implications of Iran Sanctions Relief

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**EXECUTIVE SUMMARY:** The lifting of sanctions on Iran will allow Teheran to increase its support for terrorist groups across the region, and bolster Iran's political and military power.

### The Impact of Sanctions on Iran

In 2012, Iran's banks were expelled from the SWIFT banking transaction system and were isolated from the international banking system. In addition, assets worth tens of billions of dollars were frozen.

As major Western foreign investments slowed, it was primarily the private sector that suffered. However, despite this drop in foreign investment from Western nations, the U.N. Conference on Trade and Development estimated that direct foreign investment in Iran is on the rise, reaching \$5 billion in 2012, funded primarily by Chinese, Russian and Turkish companies. Nevertheless, unemployment has risen sharply in recent years, especially among women, who tend to be more well-educated than their male peers.

While Iran holds the fourth largest oil reserves worldwide, its oil production was hurt in two ways. First, overall oil exports were capped at one million barrels per day (Mbd) over the last years. Second, prices dropped from an all-time high of \$120 at the end of 2014 to \$50 currently. All of this has badly damaged the Iranian economy.

Furthermore, in 2012 and 2013, Iran's GDP contracted (-7% in 2012 and -4% in 2013) and inflation rose to 35% in 2013.

The government's key constituencies – the Revolutionary Guards, the military and supreme leader Ayatollah Ali Khamenei's inner circle – control large segments of the economy. The high level of corruption prevalent in Iran has allowed these groups to benefit despite Western sanctions.

It should be noted however that the government managed to keep the overall poverty rate in Iran below one percent, which is a remarkable achievement under the given circumstances.

### **The 2013 Interim Agreement and 2015 Framework Agreement**

Iran's economy has markedly improved since the 2013 interim agreement with the P5+1. U.S. President Barack Obama coined the interim agreement a "key victory for American foreign policy." Yet the main impact of the agreement has been to free-up the Iranian economy. U.S. warnings against Iranian efforts to circumvent the sanctions regime have faded since the agreement. Over the last year, the Iranian economy started to grow again at a moderate rate for the first time since an economic contraction between 2010 and 2012.

Following the follow-up April 2 "framework agreement" reached in Lausanne, the impending removal of many or most sanctions appears ever more likely. While a final agreement may yet prove difficult, if sanctions are substantially lifted Iran will enjoy a veritable economic boom. Already, a multitude of European and American companies are planning to enter the lucrative Iranian market.

In the automotive industry, for example, virtually all Western manufacturers had withdrawn as a result of sanctions, though there remains a huge incentive for them to return. Various international carmakers, including Mercedes-Benz, Volkswagen, Renault, Peugeot, Kia and Toyota have already voiced their interest in reentering the Iranian market. In addition, the export of pistachios – still is one of Iran's flagship products and exports – have almost doubled in 2014.

Third, while the Iranian inflation rate is still high and the currency weak, a downturn trend – at the moment the inflation rate is 17.3% - can be currently registered.

Furthermore, Iran is likely to double its oil exports from 1 Mbd to 2 Mbd after the termination of sanctions.

However, even before a deal has been reached, Tehran has managed to circumvent the sanctions in key areas, such as by laundering cash through Dubai. Iranians arrive in Dubai with suitcases full of cash and convert it to U.S. dollars in order to enter international financial markets.

### **Iran's Allies: Russia, China, and Turkey**

Russia has a significant interest in ending sanctions on Iran so that it can expand trade and investments. Tehran has yet to pay Russia's state nuclear company Rosatom, which has been contracted to erect eight atomic nuclear reactors in Iran.

Meanwhile, China has emerged as a key trade partner for Iran, enabling it to circumvent sanctions. And Turkey, whose relationship with Iran is complex and fraught with tensions, signed a preferential trade agreement with the Shiite state in January 2015. Due to sanctions, bilateral trade with Turkey collapsed from \$22 billion in 2012 to about \$4.5 billion at present. Iran's aim is to triple this figure within a few years.

### **Economic Boom, Regional Hegemony?**

A strengthened Iranian economy in the wake of sanctions removal might carry very negative implications for the situation in the Middle East. While Iran continues to be a major sponsor of terrorism, it has been forced to reduce its assistance to terror groups throughout the Middle East because of economic constraints.

An improvement of Iran's economic situation and increasing oil exports would bolster Iran's political and military power in the region.

In the Middle East, three state blocks are currently competing for power: The Saudi-Egyptian axis, Turkey, and the Iranian Shiite axis. The Obama administration's behavior is strengthening Iran – a grave policy blunder that could allow the country to more efficiently spread its revolutionary ideology. A nuclear deal and the end of sanctions would facilitate Iran's power ambitions in the region.

Iran has an estimated GDP of \$406 billion, which is the second largest in the Middle East after Saudi Arabia. It has a population of 80 million people, making it the second-most populous country in the Middle East after Egypt.

Saudi Arabia, which has an extremely tense relationship with Iran, may face a challenging strategic outlook over the long-term. With the decline of U.S. dependence on Riyadh's oil, Iran is well set to become the dominant regional power if a nuclear deal is reached and sanctions are removed.

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