



**CENTRAL BANK OF THE ISLAMIC REPUBLIC OF IRAN (CBI)**

**CHAMBRE DE COMMERCE LUXEMOURG**

**Country Seminar “ Iran- Luxembourg: Partners in changing world”**

# **Iran Economy, JCPOA, Opportunities and Challenges**

**Dr Ahmad Azizi**

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# Iran – The road ahead

- Why Investing in Iran?
- Economy
  - Market Prospects
  - Foreign Investment
  - Challenges
- Banking
- Plans
- JCPOA
- ... take away message



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## Why Iran? – Strategic & Stable Partner

- 18<sup>th</sup> largest economy (GDP – PPP - £1'400b source: IBRD)
- Diversified economy (oil only 15% , Service 53% of GDP)
- GDP growth 3% year ending March 2015 – Predicted to grow around 5% to 8% until 2020
- Resource rich, Fossil fuel (Oil & Gas combined 1st) / alternative to Russia
- Strong infrastructure (need for modernisation)
- Market size, High GDP **growth** and **return** potentials
- Young, educated & welcoming population of 79m
- Highly-skilled labor force
- Privatisation & deregulation plans



# Economy

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## Recent Performance;

- GDP growth 3% / capacity utilization 50% / Low P/E
- Inflation: CPI May 2016, 10.4% / PTP 7.3% increase  
PPI Jan 2016, 4.3% / PTP 3.1%
- Currency stability
- TSE Index growth
- Share of Setors: Oil 15%, Agriculture 9%, Industry 23% & Services 53%
- Unemployment 11.8% (1<sup>st</sup>Q 2016)
- Liquidity growth 30% (March 2016 – YOY)
- Monetary base 17.1% (March 2016 – YOY)
- Net foreign assets of CBI 26% YOY increase
- Increase in Oil exports to 2.5 mbpd (Faster than projected)



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## Economy - Advantages

- Strategic location, 16 neighboring countries, land and sea access
- Very low foreign debt & Low government debt
- Impeccable payment track record despite revolution, war, sanctions etc.
- Historical surplus in all sections of BOP
- Sizeable & capable banking sector (Pre JCPOA setback)
- Re-emergence after lifting of Sanctions (market potentials)
- Young & educated workforce
- Stable in a turbulent region
- High Growth & return potentials
- Vibrant and peaceful society (multi-ethnicity) / Elections, etc



## Economy: Positive Prospects

- Major Analysts are forecasting considerable GDP growth for 2016:
- Iran plans for 8% GDP Growth

	FT	Economist	World Bank	IMF
IRAN	4.1	4.5	5.8	5.5
WORLD	2.8	2.7	2.8	3.4



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## Economy: Positive Trends

- Recovery (GDP growth of 2015 – Y/E March 2015)
- Monetary and fiscal discipline
- Reduction of Inflation (from highs of 40s to below 10%)
- Stability of FX market
- Market stability – Inflationary Expectation Management
- Reduction of interbank rate (from 29% to 19%)
- Planning currency unification, countercyclical policies (debt & tax)
- Improving relations with the world post JCPOA (FATA recent meeting)



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# Foreign Investment,

## FIPPA

- Sovereign guarantee (FIPPA)
- Repatriation guarantee
- Equal treatment with local investors
- International arbitration, courts
- Need for :
  - Rating
  - Currency Unification & hedging instruments (IRR-EUR NDF is quoted)
  - local financial system interaction with International Financial Markets
  - More transparency, IFRS, Basel II & III, FATF, etc





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# Foreign Investment

- Investment opportunities:
  - Earnings - Capacity utilization 50-60%, Expansion Plans, green fields
  - FPIs – P/E 7.5 V frontier markets 12
  - Fixed income return, minimum 20%
- Sectors:
  - Oil & Gas
  - Energy Saving
  - Aviation
  - Industries & Mining (Auto , ...)
  - Hospitality
  - Financial sector
  - Environment



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# Foreign Investment

## Tax

- Flat corporation tax of 25%
- No distinction between Foreign & Local firms
- Personal tax maximum 35%
- VAT 9%
- Very low tax burden 9% GDP (France 44%)

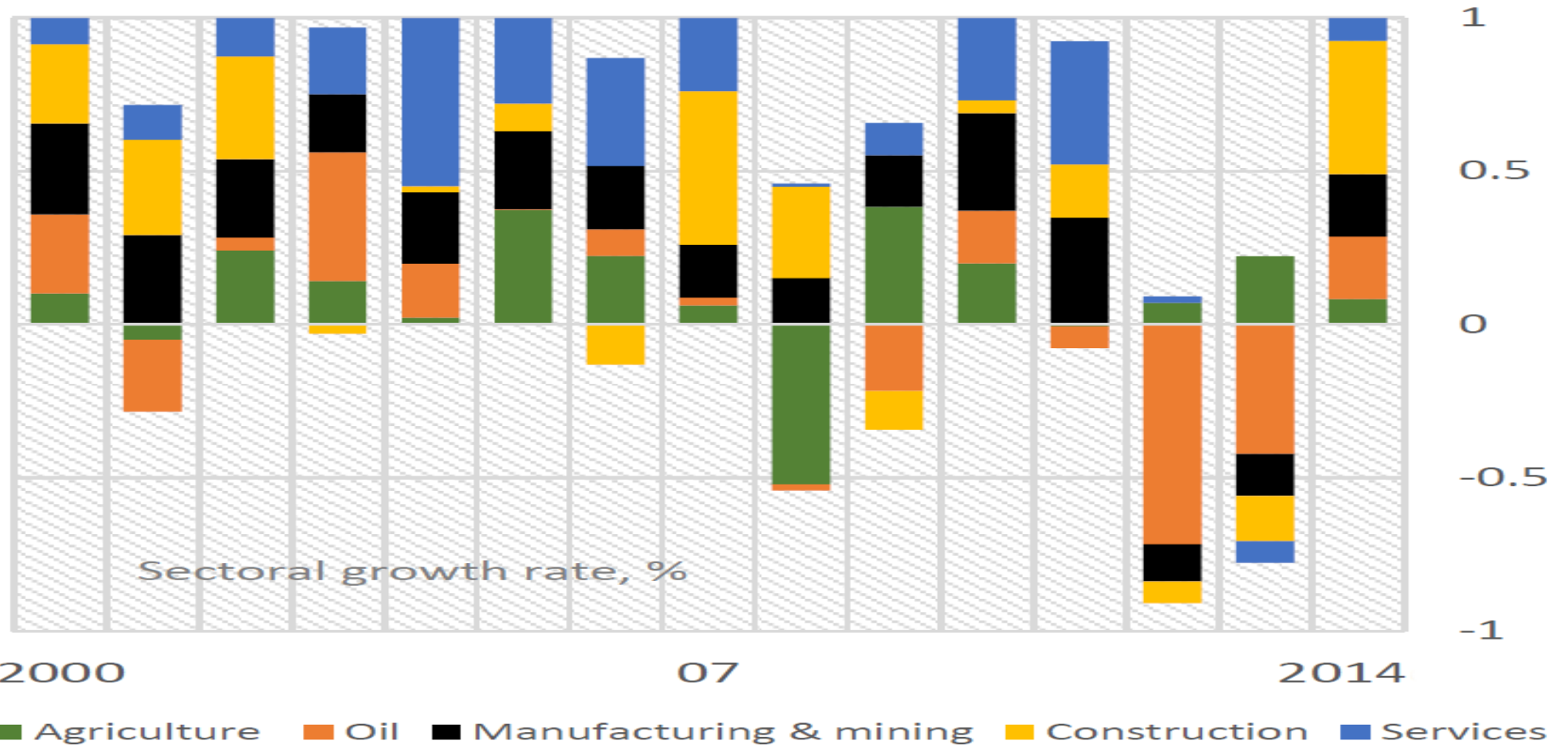


## Economic Challenges— weak recovery





# Share of sectors in GDP Growth





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# Economic Challenges

1. Low oil prices
2. Overcoming years of disconnectedness, Remaining Sanctions, etc
3. Structural reforms; including financial sector reform
4. Business environment; Governance, Legal system reform, Transparency, Anti corruption
5. Policy credibility, productivity, privatisation,
6. Financial sector reform (credit crunch, shadow banking, NPL, low capital adequacy, Gov debt, correspondent banking, regulation and supervision, resolution regimes, etc)
7. Underdeveloped capital market(including Gov. debt market)



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# Economic Challenges

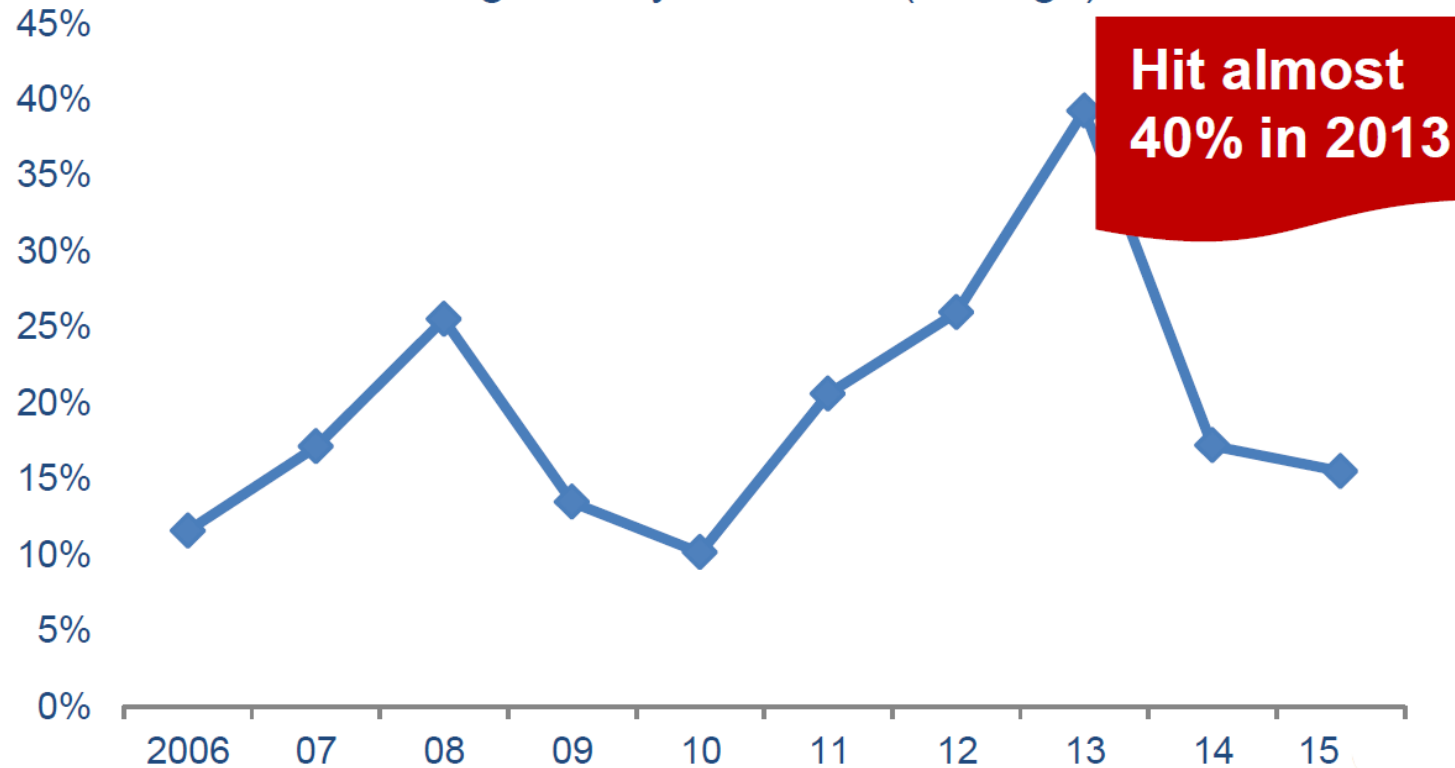
1. Severe credit crunch (50% of assets are hardly churning)
2. Financial markets is not well integrated into world market
3. Nominal exchange rate (ER) as historical anchor of monetary policy
4. Failed nominal ER , pro-cyclical fiscal & credit policy: Real Exchange Rate appreciation, Dutch Disease & tradable output contraction
5. Oil revenue makes FX a political economy consideration
6. FX parity , speculative attacks, lack of hedging instrument
7. Debt Market Development
8. Bad Bank V Good Bank
9. Profit (Interest) rates, Inflationary expectation & Monetary discipline



# Economy: Challenges

## Inflation

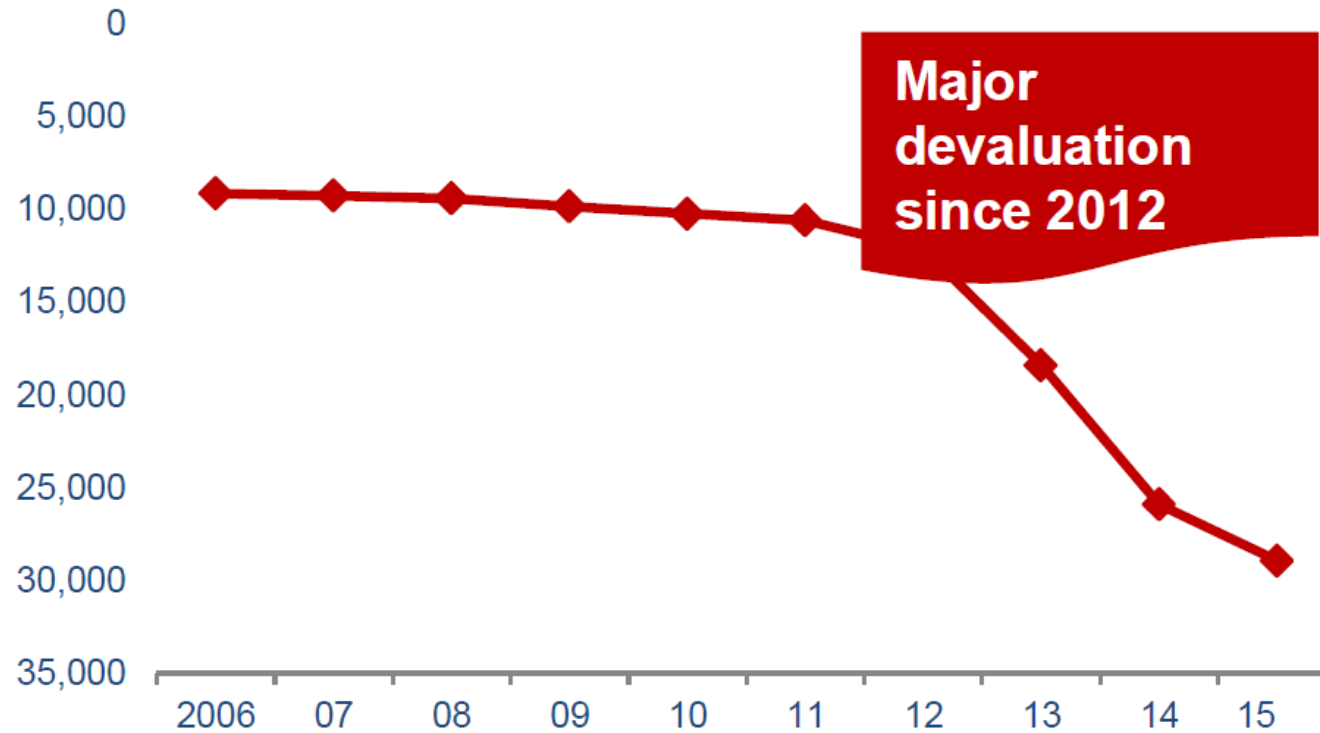
% change on a year earlier (average)





# Economy: Challenges

**Exchange rates**  
Riyal: US\$ (Official)







# Banking Landscape

Ownership Structure	No.	Loans	Assets	Deposits	Liabilities
Government owned	3	17%	17%	19%	17%
Specialised Banks	5	26%	21%	13%	21%
De-nationalised Banks	4	34%	33%	34%	32%
Private Banks	18	22%	27%	32%	27%
Credit Institution	2	1%	2%	2%	2%
Total	32	100%	100%	100%	100%



# Banking- Challenges

- Past ten years;

	2004	2012	2015
NPL	7.2%	14.7%	12.8%
CAPITAL ADEQUACY	13.1%	9.6%	7.6%
Government Debt to Banks / Total assets	2.4%	6%	6.8%
Banks' debt to CBI / Total asset	1.6%	6%	5.2%

- **Sanctions:**

- Technology & Know how deficits
- Higher transaction costs
- IFRS, Compliance, Banks' health indices
- Governance, regulatory and supervisory standards



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## Banking (Challenges - continued)

- Financial suppression
- Government debt to Banks
- Mandatory facilities & Mandatory rescheduling
- Mandatory Interest rates
- Investments in real market: Projects & property market
- Resulted in Credit and liquidity crunch
- Fairly developed payment systems



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## Banking – Future plans

- Banking Law and Central Bank law reforms
- Exchange rate unification
- Recapitalisation of Banks
- Development of markets and financial instruments, MBS, etc
- Other reform areas: Governance, Prudential Regulations (Macro & Micro), Basel, IFRS, AML, CFT, Improving risk management, etc
- Banks' balance sheet reform, including NPL, non-operational assets
- Rebuilding strong relationship with international markets



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# GDP Target & Financial Sector Reforms

- GDP target growth 8% for 2016 to 2020
- Enabling, providing and consistent enforcement of business laws
- Strengthen CBI to maintain monetary & financial stability, financial development, strong regulation and supervision
- Reform corporate governance, including IFRS
- Exchange unification
- Financial safety net, including: Deposit protection, Credit bureau, rating agency etc
- Debt market reform
- Promoting FDI
- Integrating with the global financial system



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## JCPOA

- Landmark deal entails full termination of all Nuclear Related sanctions; trust building process, momentum to cooperate
- P5+1 Commitments (sec28): Good faith and constructive atmosphere
- Refrain from any action inconsistent with the letter, spirit & intent of JCPOA
- Make every effort to support successful implementation
- Normalisation of trade and economic relations (Section 29-EU)
- Ensure access in areas of trade, technology, finance and energy
- Facilitate trade, project financing and investment in Iran



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## JCPOA (continued)

- Lifting of sanctions is comprehensive (annex 5)
- Consultation with Iran in drafting the JCPOA Guidelines
- Snap back would not apply retroactively
- Problems: Remaining USA sanctions (mainly primary)
  - US\$, SDN list
  - US firms prohibited but their subsidiaries may be allowed
  - Implementation risk; Snap-back V Huge investment by parties
- Result: Availability of Correspondent banking services, starting point



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## JCPOA - Upsets

- Slow provision of correspondent banking services
- **Why:**
  - Political maneuvering e.g. US congress ...
  - Settlement agreement
  - Fines & fear of USA Government
  - Ongoing investigations
  - Extraterritoriality in application of American laws
  - Guidelines (not effective reflection of commitments made under JCPOA)
  - FATF statement on Iran (suspension of counter measures) June 2016





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## ... message

- Investment, Tourism & other attractions
- Iran is a rear opportunity with huge potential with reasonable risk
- Removal of sanctions Provides a spring board
- More to be done by US & EU to ensure delivery of JCPOA promises
- Need for structural reform to ensure higher growth trajectory
- Expectation Gap/management:
- Strong infrastructure is available for higher growth
- Risk-reward equation skewed in favor of investors (Arbitrage opportunity)
- Stability & Security



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## ... quotes on Iran

- EIU: No market in the world has the same level of untapped potential
- Federica Mogherini: The EU should strive to create a broader network of key actors in the Middle Eastm including Iran



Thank you