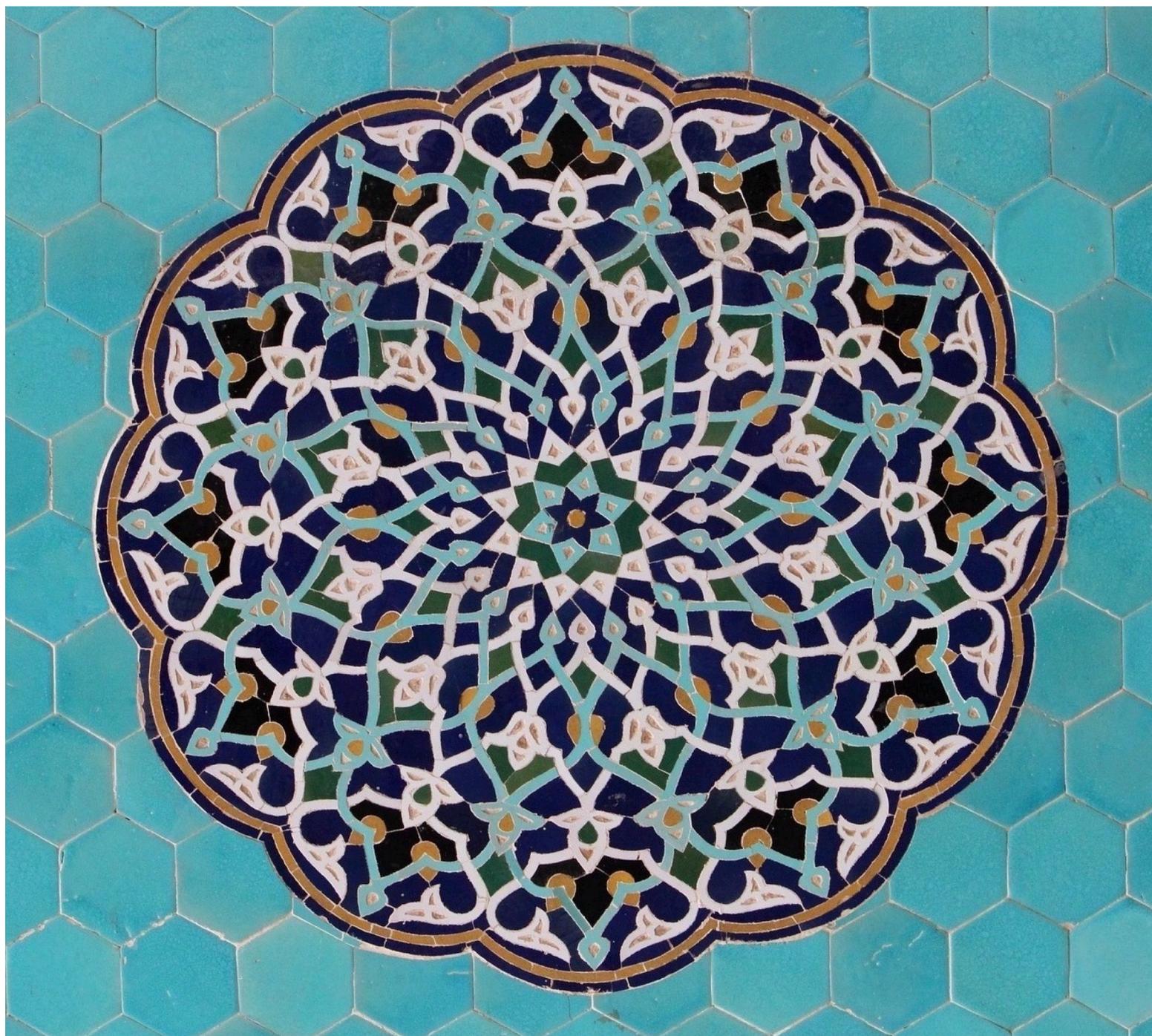


IRAN



COUNTRY RISK REPORT / MAY 2019

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PREFACE

Two years after the presidential victory of Hassan Rouhani in Iran, on July 14, 2015, Iran, the EU and the P5+1 (the United States, the United Kingdom, France, Russia, China, and Germany) agreed in Vienna on a Joint Comprehensive Plan of Action (JCPOA) regarding Iran's nuclear program.

It was implemented on January 16, 2016, but lasted less than three years before President Trump of the United States withdrew on May 8, 2018.

Consequently, 90-day wind-down period on August 6, some sanctions were implemented. Thereupon, November 4, 2018 marked the final day of the 180-day wind-down period following its announcement. One day later, the United States fully re-imposed and intensified the sanctions on Iran that had been lifted or waived under the JCPOA¹.

These are the toughest US sanctions ever imposed on Iran, which threaten to cut off foreign countries and companies dealing with Iran from the US financial system in order to deter business with Iran so to curtail the impact of proxy groups on the Middle East's security and stability².

The aim of this country report is to provide the most recent analysis of the Iran's economic and political situation; and estimate its evolution in the short and medium term.

It presents an overlook of specific clues about matters related to political risk, as well as the effect that sanctions may have on the Iranian economy, and the prospects for political stability all over the region.

1. SUMMARIES

EXECUTIVE SUMMARY

Effects of sanctions

- The re-imposition of US sanctions will maintain the Iranian economy in recession during the remaining months of 2019. Notwithstanding the foregoing, the economic meltdown will be very unlikely to happen, as the volume of oil exports is still significant, crude prices are going to continue to rise and other major powers' opinion will still differ from the US's. The multinational companies dependent on US financial system will continue leaving the Iranian market, partially leading to declining of the foreign investment, but SMEs will be almost unaffected and new forms of trading are likely to emerge soon.

- Iran is likely to build stronger economic and political ties with India, China and Russia, thus giving them more power and openness to new trading opportunities, basically due to lack of any other possible partner on the horizon in the mid-term.

- The prices are likely to keep growing up in the following months reaching the average inflation of 31.2% in 2019-20; still the risk of hyperinflation is discarded due to the fact that Iran is able to meet a significant share of local demand through local production.

- Backed by support from the EU, Iran is promised to obtain in the mid-term a special mechanism of payments (Special Purpose Vehicle) for its oil and other exports (possibly through a barter system) in order to conduct trading outside of the competence of the US sanctions. This is likely to create some tensions between Europe and the US but they will not be powerful enough to split the long-lasting alliance between the two.

Oil and gas

- The Iran's production of oil will probably continue to decrease affecting the world's oil price.

- Five from the eight initial major buyers (Italy, Greece and Taiwan have already stopped their purchases from Iran) are and will be buying Iranian oil now that the waivers have been extended for the following 90 days. Thereby, the Iranian oil will still remain in demand during the following years, and Iran's government is likely to find solutions for its selling and exportation, even though illegally, in the mid and long-term. Thus, the United States is unlikely to meet its earlier target of driving Iranian oil exports to zero³.

- Iraq will continue to buy natural gas from Iran in order to use it in the production of electricity, becoming the second largest customer. Taking into account the fact that there is a sort of competence between US and Iran for the influence over Iraq, it can fuel a further deterioration of their relations. It is also plausible that more buyers will emerge if some new forms of trading, which do not rely on dollar, appear soon.

- Even though the modest production growth is likely to continue, Iran won't be able to unilaterally monetize its natural gas resources due to lack of financial partners and the investment, especially from the West. However, it will be able to fulfil its domestic demand and sustain trade with Turkey⁴.

- Iran's ability to increase production and exports of natural gas will be almost improbable, unless the relations with the United States are improved or support from international partners in defiance of sanctions is reinforced. Nevertheless, if Iran manages to accomplish current development projects, its export pipeline capacity will increase from 46.4 bcm/year in 2018, to 119.7 bcm/year to the regional and global markets in a long run. China, India and Pakistan will play a significant role in Iran's natural gas sector.

The domestic scene

- Iran will continue demonstrating considerable resilience in coping with US sanctions, and is likely to continue to fully implement the commitments of JCPOA as long as China, Russia, or countries which are non-members of the deal, such as India, continue to trade with it, and if EU continues maintaining its constructive attitude. In this case, even a greater international support and United Nations diplomatic intervention is expected in the mid-term. However, on a longer run, the JCPOA future will depend upon the economic situation and complex political battles between moderates and hardliners in Tehran⁵.

- The current deterioration of the economic conditions in Iran, the rial devaluation and growing inflation, together with already-high unemployment will provoke a further popular discontent which is likely to maintain the protests but without any considerable probability to threaten the Iranian political stability or lead to leadership's rupture during the upcoming years.

- The sanctions are likely to produce some adverse effects on the political local scene over the longer term, as Iranian hardliners may take advantage of them and the popular frustration and obtain the victory in the coming 2020 parliamentary elections and the 2021 presidential poll. As a result, any possibility for future cooperation with US will equal zero.

COUNTRY RISK SUMMARY

Economic Risk Index

Iran's economy will be weakened and conducted to recession by the re-imposition of US sanctions during the following few years, which will continue to hit the country's oil exports and investment inflows. The high inflation will remain and the rial will continue being devaluated, weighing on domestic investment and consumption. The government will neither be able to give a fast answer to a large-scaled unemployment. As a matter of fact, Iran won't be able to appreciably mitigate or avoid in its totality the adverse effects of US sanctions in the scope of its economy in the foreseeable future.

Political Risk Index

Iran's political outlook appears uncertain in the context of deteriorating economic conditions. High inflation and unemployment are key drivers of popular discontent, and core factors behind the frequent protests that are very likely to repeat successively in the medium and long run. The political opposition in the country is heavily fragmented, so popular unrest is unlikely to pose a national security. However, its escalation and risk are strictly depending on the further economic evolution.

SWOT ANALYSIS

Economic SWOT-Analysis

Strengths

- Iran has the world's fourth largest proven oil reserves, and the world's second largest proven gas reserves after Russia.
- Iran is rich in other resources, such as coal, chromium, copper, iron ore, lead, manganese, zinc and sulphur; and has a strong agricultural sector in addition to automotive and mining industries⁶.
- It has particular geostrategic significance owing to its location in the Middle East and central Eurasia. The population is large and relatively well educated⁷.

Weaknesses

- Sanctions are having a negative effect on trade and foreign investment.
- The banking sector is highly fragile and under-competitive in terms of governance and transparency⁸.
- The military retains a large presence in the economy, making it difficult for private actors to compete.⁹
- Large firms dependant on US withdrew from Iran, causing considerable lack of foreign investment.

Opportunities

- The gas sector still remains underdeveloped, but there is a set of promising projects that will attract new partners.
- Iran represents a large consumer market and is supported by all the remaining signatories of JCPOA.
- Once the sanctions will be lessened, the economic growth will become extremely fast.

- National Development Fund of Iran, once supplanted the Oil Stabilization Fund (OSF), is working diligently on managing external shocks and insulating the Government's budget against oil revenue fluctuations. It currently has \$91 billion in assets and is among the 20 largest sovereign wealth funds in the world¹⁰.

Threats

- Lower oil production may affect the economy as a whole.
- If Iran decides to stop its commitment to JCPOA, the trade relations with China, Russia, India and others will become almost improbable.
- The lack of regional commitment and investment threatens the gas sector development and moves Iran away from becoming a world energy hub.

Political SWOT-Analysis

Strengths

- The wealth distribution in Iran has significantly improved in the last few years.
- Iran feels an emotional boost from its supporters and the government does effort to maintain social stability.

Weaknesses

- The generalized negative framing of Iran in terms of human rights, electoral fraud and public protests, discourages the international community from opposing the US policy of sanctions.
- Structures of state-run firms are inefficient and bureaucratic, which slows down the production process.

Opportunities

- US setbacks in Iraq and Afghanistan have given Iran an opportunity to assert greater strategic influence in the region.

- Any normalization of relations between Iran and the US could become a major catalyst for a huge reform of the banking sector.
- A long-term potential in Iran across a range of sectors is enormous due to its large and young population, as well as its strategic location.

Threats

- Youth unemployment is very high and the future outlook is disappointing.
- Further deterioration of US-Iran relations cannot be dismissed in light of all the evidences presented.
- A unique possibility for reforms to happen in a short run lies in the victory of Iran radicals, BUT their output won't be the expected and the most pleasant ones.
- The Iranian hardliners victory could break down any further dialogue with US.

2. ECONOMIC OUTLOOK

US SANCTIONS

US sanctions and the EU companies

The re-imposed US sanctions are binding not only on American citizens and companies, but also apply to non-American individuals and firms, as a direct consequence of a legal concept known as extraterritoriality. That is to say, any company based outside of the United States must comply with American sanctions if it uses dollar for its financial transactions and/or oil purchases, has a subsidiary in America or is controlled by the US¹¹. However, while Trump's decision will not have a major impact on American commercial interests as the US economic presence in Iran is quite limited, America's allies in Europe, which have benefited significantly from growing trade with Iran since 2015, will be significantly affected.

Despite the fact that the European companies are backed by a Joint Statement, also known as Blocking Statute, in force since 7 of August 2018, in which the EU foreign policy chief and the foreign ministers of France, Germany and the UK openly admitted to protect European companies engaged in legitimate business with Iran from US penalties¹², large multinational corporations that belong to or wish to remain in US enormous financial market, would either choose to pull out their economic and trading activities from Iran's unstable market¹³. This tendency will continue from now during the following two years, the period when the sanctions' effect is the most harmful for Iranian economy. Such decision is a result of well-founded fear of US reinforced secondary sanctions and lack of confidence in EU supporting solutions.

In light of this evidence, an immunity provided by the EU Blocking Statute in support of Iran nuclear deal is generally considered as a theoretical and symbolical measure, to some extent, ideal for small and medium-sized enterprises of regional or national implementation not exposed to US market or international circuit¹⁴, which are likely to continue penetrating and establishing in the Iranian market.

For larger businesses, a unique but very unlikely solution for the short-term lies in negotiating waivers or exemptions with the United States. As a result, in September of 2018, 31 European and Asian firms in the Global 500 announced they would be leaving the Iranian market or hinted their exit was imminent¹⁵.

US sanctions and the third countries

Nowadays, there are merely eight countries allowed by the Trump administration to be exempt from US sanctions on importing limited amounts of Iranian oil during six following months, until May 2019. Among these countries are China, Greece, India, Italy, Japan, South Korea, Taiwan and Turkey¹⁶. They are and will be buying Iranian oil at least until May. Once the waivers expire, only Italy, Greece and Taiwan are likely to be left without additional waivers. This means that China, the largest customer of Iran's oil, will almost certainly continue to purchase oil for the coming years.

Furthermore, there are also some important exceptions for large corporations in terms of compliance with sanctions. They consist of state-owned or state-controlled firms in Russia and China which are determined to withstand the impact of sanctions. The most significant examples are China's state-owned energy giants, CNPC and Sinopec, Chinese railway firm CREC, and the Kremlin-controlled energy companies, Gazprom and Rosneft. These are the only five firms in the Global 500 whose actions indicate they will resist sanctions¹⁷. Russia's support is of high importance for Iranian current situation, mainly in the LNG projects.

Moreover, Turkey, the country which had completely stopped importing Iran's oil the very month sanctions were imposed, now is still buying Iranian crude, even though in reduced amounts (54,000 bpd in December)¹⁸ and is estimated to continue trading with Iran during 2019 and onwards, fitting its behaviour in terms of hostility toward the US and extensive influence in the corporate sector. Together, China, Russia, and Turkey account for a large proportion of firms likely to stay in Iran.

Thereby, Iran is going to keep trading relations with a number of countries, whereas the Iranian oil will still remain in demand during the following years, and Iran's government is likely to find solutions for its selling and exportation, even though illegally, in the mid and long-term. Thus, the United States is unlikely to meet its earlier target of driving Iranian oil exports to zero.

US sanctions and alternatives for Iran

Iran is likely to build stronger economic and political ties with India, China and Russia, thus giving them more power and openness to new trading opportunities, basically due to lack of any other possible partner on the horizon in the mid-term.

China

China has demonstrated a willingness to invest in Iran's energy sector to support its expanding economy. Once the Paris Agreement enters into force in 2020, it is estimated that the fight for reducing the CO₂ emissions in Asia will become tougher. Consequently, China, the main coal consumer¹⁹, will be obligated to find a coal-gas substitution. According to ExxonMobil, from now to the next 10 years, the demand for natural gas will steadily increase and it will become the second largest source of energy.

Pakistan

A number of other countries, such as Pakistan and India are also searching for a solution to a short-term energy demand and create long-lasting energy security. These are favourable circumstances for Iran as, at the moment, is one of few viable options to obtain an investment required for its future flourishing. In addition to already existent pipeline connections in Iran, there is a couple of projects, such as Iran-Pakistan-India (IPI) pipeline which may allow an export capacity of roughly 40 bcm per year. It could be also extended to China, affording Iran a major export corridor. However, its short or mid-term success is very doubtful due to Pakistan's indecisiveness and given the luring tactics of US support and Saudi Arabian investment in TAPI (Turkmenistan–Afghanistan–Pakistan–India Pipeline), which is said to be finished by 2020²⁰.

India

India, despite some reducing in oil purchases, seems optimistic about going forward with Iran-India project gas pipeline to Oman. It will support up additional 10.22 bcm per year of natural gas. Moreover, India will stay supporting the development of Chabahar Port²¹ aiming to use it as a distribution centre for agricultural products with Afghanistan and Central Asia, allowing Iran to interact closely with bordering partners. In addition, Indian banks are being pressured by the local government to continue working with Iran.

Iraq

Moreover, a case with Iraq has to be mentioned too. Iran shares a 900-mile border with Iraq and at times they have had difficulties and disputes as a result of their geographic cohabitation. The Iran-Iraq war of the 1980s showed that it would be better for both to have close and cordial relations, the ones they appear to maintain today. Hence, Iran is likely to reinforce its already existing trading relations with Baghdad by building one additional pipeline to Basra. Therefore, Iraq will continue to buy natural gas from Iran in order to use it in the production of electricity, becoming the second largest customer. Taking into account the fact that there is a sort of competence between US and Iran for the influence over Iraq, it can fuel a further deterioration of relations between the two countries and with hardliners in positions of influence on both sides, the potential for an unplanned clash still remains high, particularly in Iraq. As a proof of that, on 7th May of 2019 Mike Pompeo has visited Iraq in order to discourage it from cooperating and trading with Iran. Yet, even though Trump has stated that the US presence in Iraq should be used to “watch” Iran, this is unlikely to pose any considerable risk as long as Iran will remain attached to JCPOA.

Overall, it is likely that these projects will add up to 59 bcm per year to Iran’s natural gas export capacity once finished; nevertheless, their prosperity was disrupted by US sanctions (for instance, France’s Total withdrawal from the region braked the South Pars Field investment) and they are still highly dependent on substantial geopolitical commitments and financial investments, as well as another five Iranian LNG projects that have been stopped for the same reason.

Turkmenistan

Another fact to be pointed out is that despite of a gas dispute between Iran and Turkmenistan, the trade between two countries in January 2019 accounted for \$312 million and several Caspian Sea joint projects, in both gas and oil, have recently been carried out²². For instance, one of them (the Kazakhstan-Turkmenistan-Iran transnational railway) has already been completed.

This demonstrates some improvements in their bilateral relations, which will be moderate in future, probably having a positive outcome for Iranian gas transportation from south to north. However, Iran's current economic situation is very unlikely to allow paying a debt that dates back to 2007 and 2008, when freezing winters led to severe shortages across Iran, and thus increased gas imports from its north-eastern neighbour²³. It means that even if their trading relation will positively impact Iran's gas sector, it would not be in the short run.

So once again, there is a considerable lack of investment and thus development of infrastructure necessary for this purpose. As a result, even though the modest growth is likely to continue, Iran won't be able to unilaterally monetize its natural gas resources due to lack of financial partners and the investment, especially from the West. However, it will be able to fulfil its domestic demand and sustain trade with Turkey²⁴.

Azerbaijan

The recent visit of Iran's Chief of General Staff of the armed forces to Baku (first time since the Azerbaijan's independence) in January 2019 seems to signal a new phase in Iranian-Azerbaijan relations²⁵.

The two countries have agreed to expand bilateral relations, further strengthen their military and security cooperation, increase trade, and work mutually on the completion of the North-South Corridor, which aims to expand regional trade by ship, rail, and road. The North-South Corridor seems to be a feasible alternative for Iranian maritime trade and, once completed, would also benefit India, Russia and Azerbaijan.

Moreover, the strategic location of Azerbaijan, which bridges Turkey, Russia and Iran to each other over land, may play an important role in their trilateral relations. Probably

this relationship would help Iran to slightly mitigate the effect of US sanctions or, at least, prepare it for greater trade openness once the sanctions are ceased.

In exchange for this partnership, Azerbaijan hopes to have the support of the regional power in the Nagorno-Karabakh conflict and ultimately regain control over its occupied territories. For Iran, Azerbaijan is the most stable neighbour and a more reliable partner to construct a number of mutual dams and power plants, especially on the Aras river²⁶.

It is worth noting that improved relations with Azerbaijan and Turkmenistan may permit to double the current 50,000 b/d of oil passing through Neka (Iran's Caspian Sea port used to facilitate swap agreements with Azerbaijan, Kazakhstan and Turkmenistan. Under these agreements, Iran receives crude oil and later exports the same amount from Kharg Island) in the longer term.

Russia

In addition, it is almost certain that in an anticipated future Iran will also rely on a huge financial backing from Russia who, according to Gazprom, is interested in helping Iran with both pipelines and LNG plants. Russia's aim is to kill two birds with a stone: to gain a share of Iran's future revenues and draw Iranian attention away from Russia's influence in the European market toward the Far East market.

In conclusion, Iran's ability to increase production and exports will be very unlikely, unless the relations with the United States are improved or support from international partners in defiance of sanctions is reinforced. Nevertheless, if Iran manages to accomplish current development projects, its export pipeline capacity will increase from 46.4 bcm/year in 2018, to 119.7 bcm/year to the regional and global markets in a long run. China, India and Pakistan will play a significant role in Iran's natural gas sector.

SHORT AND MID-TERM FORECAST (LOCAL REACH)

Note: Short-term states for 24 months; mid-term states for 2-5 years

The re-imposition of US sanctions will send and maintain the Iranian economy in recession during the remaining months of 2019. However, an economic meltdown will

be unlikely, as the volume of oil exports is still significant, crude prices are going to continue to rise and other major powers' opinion will still differ from the US's. The multinational companies dependent on US financial system will continue leaving the Iranian market, partially leading to declining of the foreign investment, but SMEs will be almost unaffected and new forms of trading are likely to emerge soon.

As a result of a quick glimpse at former events, whereas large Spanish corporations, reliant on oil industry, like Cepsa and Repsol, have already made a decision to leave the Iranian market, other smaller independent firms, such as Meliá, Taim Weser and Tubacex are very likely to remain in Iran and seek for new projects and perspectives.

The EU support will continue as long as Iran would not cross the red line, for instance, in the case of the ballistic missiles program, serious human rights violations or engagement in any new conflict in the Middle East. The bilateral relations can be broken down if European companies begin losing tenders or contracts, but this is very unlikely for the following years because of joint effort on SPV project. However, any radical change in the Iranian regime in the elections may alter the EU-Iran relations.

China, Russia, Turkey and India are and will continue playing a colossal role in Iran's future economic blooming, as well as other emerging actors, such as Pakistan, in the development of its gas sector and further trading relations. As a result, Iranian net exports are likely to increase from 2020 onwards.

According to the Secretary of US State Michael Pompeo, the waivers will aid Iran to offset some of the revenues lost because of export reduction and allow the Iranian oil to remain in demand during the following years.

The sanctions affect, to the major extend, Iranian oil sales, whereas Iran's Central Bank and insurance sector, together with its wider energy industry, airlines, shipping and shipbuilding sectors remain targeted as well. However, agricultural commodities, food and pharmaceutical industry, are said to be totally liberated from US sanctions.

From the negative and domestic perspective, due to still considerable lack of foreign investment, the inflation and rial weakness will continue within Iran, adversely affecting

private business activity, consumption and unemployment rate; thus fuelling further social frustration and popular protests from now till 2021 approximately.

Overall, the re-imposition of US sanctions will have some consequences on the political and social stability, affect different sectors- even though in different scale-, and have an impact:

On GDP

In a short-term, a real GDP growth is projected to experiment a decline similar to that of period from 2012 to 2014, but not as sharp as it was in 2012, after the implementation of US sanctions on the Iran's Central Bank²⁷ and the EU imposed economic and financial sanctions in 2012²⁸. We agree with the IMF in its forecast and affirms that Iran's GDP growth is likely remain at its actual rate of -3,6% for the rest of the 2019, whereas from 2020 onwards a slight recovery will take place with a modest growth within the following two years.

Nonetheless, the Iranian plan for an annual economic growth rate of 8 percent within the scope of sixth five-year development plan (2016-2021) seems already impossible in face of current sanctions. However, there is a high expectation that once the sanctions will be lessened, the economic growth will become slightly faster and could probably reach the same peak of 12,5% as in 2016, while JCPOA was giving its fruit.

On budget deficit

Iran recorded a Government Budget deficit equal to 3.10 percent of the country's Gross Domestic Product in 2018²⁹ and we forecast a similar sustained fiscal deficit over the coming years, primarily on the back of lower oil revenues and gradually increasing general spending.

Should risks of widespread popular unrest elevate, than a sharper increase in spending levels is likely to take place, in order to address some of the Iranian people's economic needs, or fund military crackdowns. Any rapid improvement is very unlikely due to lack of banking sector reform in a short-term.

On unemployment

Iran benefits from a large and well-educated population in the age of working (between 27 and 36 years old). Nevertheless, the unemployment rate in Iran has always been a significant problem and one of the underlying causes for popular discontent. Iran's population grows (82.8 million people in March 2019), meanwhile the labour force participation rate falls drastically to its lowest levels over the last 10 years. Even though there was starting some moderate improvement, the current unemployment rate has been kept at high levels, almost 12%, and a gender gap in the labour market is still perceived. The most alarming figure is the youth unemployment, which stays at 28 %³⁰.

According to the website Bonbast, which tracks the unofficial market, the dollar was being offered for as much as 138,000 rials in 2018, meanwhile the official rate, cited by the Central Bank website, is IRR42,000/USD and we expect it to remain at this level in the near term. This rial weakness, coupled with decreased foreign currency inflow, is likely to maintain the already existent inflation at significant levels. Moreover, the prices are likely to keep growing up in the following months reaching the average inflation of 31.2 percent in 2019-20; still the risk of hyperinflation is discarded due to the fact that Iran is able to meet a significant share of local demand through local production. Nevertheless, the government's ability to create jobs will be restricted as a direct consequence of the implementation of sanctions.

Consequently, youth unemployment is likely to remain elevated, near 30 %, during the forthcoming months and, certainly, for the next three years. As it is especially high among young people, there is more probability that the social protests and demonstrations are to take place in the mid and long run. In a consequence, the vicious circle is formed, where government can do nothing to prevent the unemployment from rising, and where the very unemployment is the main catalyst for social protests.

On public debt

Iran recorded a government debt equivalent to 44.20 percent of the country's Gross Domestic Product in 2018. From 1996 until 2018, the Government Debt to GDP in Iran averaged 19.13 percent, reaching an all time high of 47.50 percent in 2016 and a record low of 8.90 percent in 2011.

Our estimation is that once the US sanctions are back in power, the public debt will remain at 40-42 % of the country's GDP till the end of 2020.

On trade balance

Iran has been recording trade surpluses since 1999 due to increased shipments of energy resources, especially oil. Whereas, the 2012 sanctions had a dramatic effect on Iran's exports, reducing the overall trade surplus, in the second quarter of 2018 Iran recorded a trade surplus of \$12,983 million³¹.

Looking forward, the BOT is likely to slightly diminish in proportion, as the exportations are to remain reduced in the short term. Nevertheless, the larger-term estimations indicate that Iran will continue with considerable trade surpluses if it succeeds in all the ongoing projects aimed to increase its exporting capacity.

OPERATIONAL RISKS

In addition to the direct effects of sanctions, there are still some additional deeper-rooted risks for foreign companies. These mainly lay in a difficult operational environment – with high corruption, bureaucracy and nepotism– and persistent political and social risks that cause uncertainty. In case of Spain, for instance, US sanctions which target financial transactions on practically all bilateral goods and services operations are the main reason for the withdrawal from the Iranian market today³². These threats are certainly going to remain, at least before the oncoming elections and some years afterwards.

Moreover, it is important to consider some other external factors that may affect the Iranian domestic field. For instance, Iran has long feared the United States will use Afghanistan as a strategic ground for a strike on its nuclear facilities. Now, with the US sanctions on Iran in force, Tehran remains more anxious about the US presence in Afghanistan. This may promote a strengthening support from Tehran to the Taliban and whatever response from US can pose the nuclear deal under threat, as well as the whole Iran's stability.

Below there is an overlook for the Operational Environment in Iran. An Operational Risk Matrix provides a comprehensive overview of potential risks facing investors operating in a country. It evaluates Energy Development Risk, Stability Risk, Trade and Investment Risk, Crime and Security Risk and Structural Risk. Below are sections from these reports.

Energy Development Risk (45/100)

The lack of investment and consequently, of new technological modernization within energy industry, diminishes Iran's potential of becoming a centre for oil and gas distribution. Iran's LNG capability, for example, has been under construction for years, and without it, Iran does not currently possess the means to export all of its surplus gas. As a result, Iran cannot exploit its resources to the maximum, nor become competitive exporter in the sphere.

However, it is almost certain that once the effects of sanctions are eased and if Iran gains more support and local commitment, the currently frozen projects will change the situation completely.

Stability Risk (50/100)

The struggle between hardliners and moderates is inevitable in Iran and the economic and trading openness is highly dependent on who will be in power after the coming elections. Moreover, the age of the Supreme Leader draws some additional doubts on what the Iranian regime would be like after him.

The popular protests pose another risk, but their current character seems less alarming as the ones in the previous years. Yet, their further threat cannot be discarded in the longer run.

Trade and Investment Risk (55/100)

The US sanctions and their binding effects to non-US companies and individuals have already posed Iran in danger as many large international corporations pulled their business out of the country.

The isolation, even not total, makes companies more indecisive about their future activities in the country and drives them towards other partners within the region.

Though, Iran is still keeping good trading relations with countries such as Russia, China and India as well as with those that have been granted waivers; it is strongly supported by the EU and some new partners are very likely to emerge once the SPV enters into force.

Crime and Security Risk (30/100)

The risk of interstate conflict remains high, as the country has poor relations with US and its rivalries Israel and Saudi Arabia. The future of US or Israeli military action against Iran's nuclear facilities seems very unpredictable over the decade ahead.

Businesses also face danger from non-state actors such as Sunni insurgent groups in the border region with Pakistan. The risk for a terrorist attack still remains considerable.

Moreover, grievous human rights abuses and arbitrary detention of foreigners have always persisted in the Iran.

In addition and according to the European Union Agency for Network and Information Security (ENISA) in its recent report, “newly imposed sanctions are likely to push Iran to intensify state-sponsored cyber threat activities.”

Structural Risk (30/100)

In addition to rial devaluation, inflation and unemployment, the extensive presence of the state in the economy, caps on foreign ownership in key sectors, a high tax burden, bureaucracy and rampant corruption, are likely to remain unresolved in the mid-term.

It is also worthy to highlight the existence of a network of “parallel institutions” on behalf of both the IRGC and the ordinary police, namely in the services and construction sectors. While spending most of Iran’s revenues on military expenditures at home and in neighbouring conflict zones, it arises many doubts for companies operating in the country.

(Figure 1) OPERATIONAL RISK MATRIX



Note: 100 = lowest risk. 0 = highest risk

SHORT AND MID-TERM FORECAST (GLOBAL REACH)

According to EIA, Iran's crude oil exports and production have already declined since May 2018. Iran's exports of crude oil fell from its peak of nearly 2.7 million (b/d) determined in June³³, to 1.2 million b/d in December. Nevertheless, taking into account the Iranian proved natural gas reserves and rising consumption, Iran is and will be able to fulfil its domestic demand and sustain trade with Turkey. Yet, due to lack of modernized equipment, poor development and inexistence of financial support, the idea of solid trading relations with countries such as Pakistan, China and India seems more difficult for the next two years, but not impossible in the longer term.

Moreover, the countries provided with waivers from the US sanctions will still consume Iranian oil. Thus, the United States is unlikely to meet its earlier target of driving Iranian oil exports to zero. What is more, the waivers are going to avoid any disruption

of the global oil market from now and onwards, according to US Secretary of State Mike Pompeo.

Although the Iran's production of oil will probably continue to decrease affecting the world's oil price, its downturn won't be as rapid as it has been in the previous months since the announcement of sanctions, provided that Iran has to fulfil its high domestic energy consumption, which can only slightly decrease for the coming months. In terms of exportation, shipping operators have decreased operations with Iran, but Iran has continued to export largely through the state-run National Iranian Tanker Company (NITC) and the Islamic Republic of Iran Shipping Lines (IRISL).

Even though the future of oil and gas exports remains uncertain, there are sufficient reasons to estimate that the overall situation won't be too dramatic, at least in the short and medium run. Moreover, backed by support from the EU, Iran is likely to obtain in the mid-term a special mechanism of payments (Special Purpose Vehicle) for its oil and other exports (possibly through a barter system) in order to conduct trading outside of the competence of the US sanctions. However, this dream is very unlikely to come true in the near future.

LONG-TERM FORECAST (ENERGY INDUSTRY)

Note: Long-term states for 10 years

In a longer term, without weighting up any extreme cases within both political and social spheres, the Iranian oil and gas will still remain in demand during the following years, and Iran's government is likely to find solutions for its selling and exportation, even though illegally, in the mid and long-term.

The sanctions on Iran's energy sector have mostly affected its oil trade; however, Iran's natural gas production has continued to rise despite sanctions, mostly because of the need to satisfy its growing domestic demand. If the OPEC Oil Outlook and general forecasts vary widely for the oil sector, it is certain that the global demand for natural gas will be increasing drastically during the next twenty years. In any case, Iran will always have an alternative.

It is of high importance to highlight the fact that, according to exports, natural gas is going to become the second largest source of energy behind oil by 2025 and a global demand for natural gas is going to triple until 2040³⁴. The demand will be particularly strong in China, India and the Middle East³⁵. Having the world's second largest proven gas reserves after Russia accounted for 33.2 TCM³⁶, the potential for Iran to emerge as a major natural gas supplier will become very possible as natural gas becomes more important for those seeking supplies. This means that its gas production and exports are likely to increase in the long-term future, if it succeeds with all current projects that remain temporary frozen due to lack of investment.

Unfortunately, in the case of Iran, recent technological advancements in extracting unconventional sources of natural gas, lack of local commitment and investment, as well as the US sanctions pose it in a long way away from becoming a major exporter of natural gas. Nevertheless, its expansion is not discarded within the 10-years period of time.

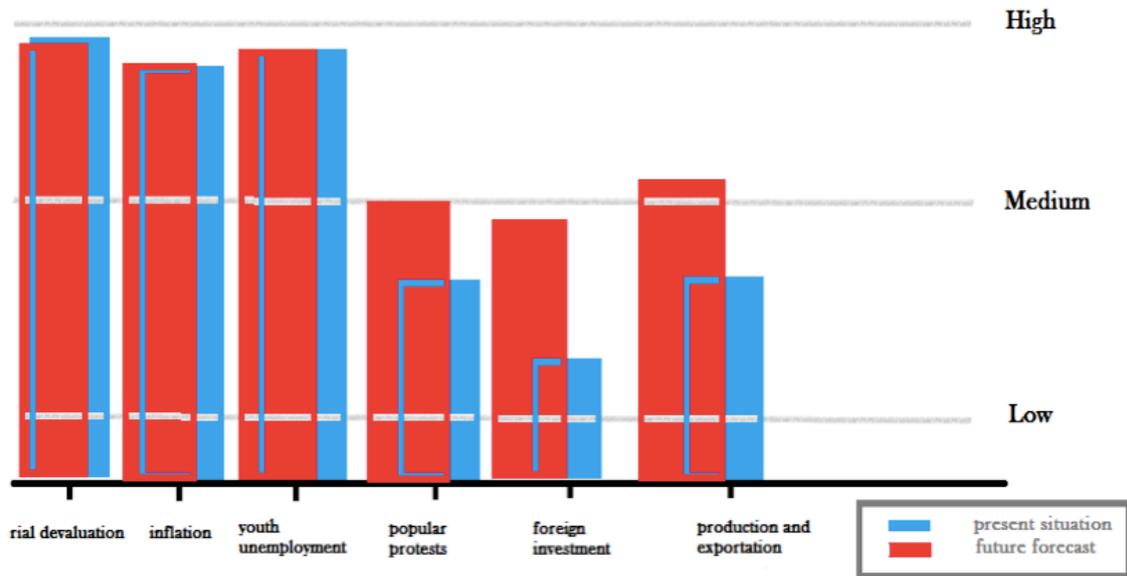
In a nutshell, even though the modest growth of Iranian gas is likely to continue in a short-term, Iran won't be able to unilaterally monetize its natural gas resources due to lack of financial partners and the investment, especially from the West³⁷.

Only by attracting new partners and by improving its technological abilities can Iran fulfil its expectations within energy field. This seems only possible for five years from now.

Iran's ability to increase production and exports will be inconceivable, unless the relations with the United States are improved or support from international partners in defiance of sanctions is reinforced. Nevertheless, if Iran manages to accomplish current development projects, its export pipeline capacity will increase from 46.4 bcm/year in 2018, to 119.7 bcm/year to the regional and global markets in a long run.

(Figure II) IRANIAN ECONOMY: PRESENT AND FUTURE

Each of these columns reflects March 2019 situation and mid-term forecast for specific unit. Considered altogether, they provide an outlook of the overall economical stability of Iran at present (March 2019) and in the mid-term (2-5 years from now).



Note: -Rial devaluation now: IRR42,000/USD mid-term: IRR42,000/USD ; -Inflation now: 31% mid-term: 31,2%;
 -Youth unemployment now: 28% mid-term: 30% .

3. POLITICAL OUTLOOK

DOMESTIC POLITICS

The re-imposition of US sanctions will have consequences on the political and social stability of the regime, albeit not epochal.

The past-years experience in terms of the mass protests in the aftermath of June 2009 presidential election (Green Movement), and those in response to accelerating inflation but with anti governmental character in December 2017/January 2018, have demonstrated that there is considerable dissatisfaction with the authorities and the general situation within the country.

However, there is a slight difference between these two mass revolts in terms of participants, causes and goals. Whereas the former had an official leader in figure of Mir Hossein Mousavi³⁸, had a clear purpose and was supported by approximately three millions of participants, the latter is more amorphous and remains leaderless, with no central movement behind.

Iranian economy is highly dependent on external forces (for instance, US sanctions), thus its minimal alteration can result in a new popular uprising over the coming years due to public frustration. Such massive discontent can be triggered by any "shock event", such as a sharp decline of living standards, an abrupt worsening of the economic situation, or a further rise of youth unemployment, among others.

The current deterioration of the economic conditions in Iran, the rial devaluation and growing inflation, together with already-high unemployment will certainly provoke a further popular discontent which is likely to maintain the protests alive in the mid-term but without any considerable probability to threaten the Iranian political stability or lead to leadership's rupture any time soon. It is very unlikely that some new major popular protests would take place in the next 24 months. Yet, any intermediate demonstrations would have a character very similar to that of 2018; they are relatively small in numbers, disorganized and, most importantly, have no a clear aspiration for bringing

down the system. Consequently, they won't be able to threaten the Iranian political stability and regime, in any case, during the short and mid-term period.

On the same line, Iran has many powerful institutions: Supreme Leader, president, Majlis (parliament), Expediency Council, Assembly of Experts, armed forces, Islamic Revolutionary Guards Corps (IRGC), Basij militia and intelligence service. Still the Iranian regime remains alarmed as the US sanctions have led to heightening tensions. Moreover, government's unfulfilled promises have already lost their power. In such circumstances, the regime has two main options: to adapt itself to public demands and carry out certain civilian reforms, or increase domestic repression to maintain its power.

Be that as it may, the prospects for violent and revolutionary change in Iran remain low³⁹. Although we have lamentably no access to popular sentiment data, it believes that there is no a strong desire for revolution among inhabitants given their high level of education, fear of being cracked down by the IRGC and the Basij, as well as the unpleasant experience lived during the Arab Spring uprisings. It is very implausible that current popular frustration and future protests fuelled by US sanctions would turn into powerful movement capable of putting the political stability and regime under risk, at least during the Trump's administration and unless Iranian economy is being continuously reanimated by Russia and China.

Yet, there is a wide range of possible consequences that could derive from such protests. First of all, they will affect the operating environment, making it less attractive for foreign companies; meanwhile the divided opinion within population may cause social instability. Secondly, such protests founded on growing frustrations and an enormous desire for a major reform may produce some adverse effects on the political local scene over the longer term, as Iranian hardliners may take advantage of them and the popular frustration and obtain the victory in the coming 2020 parliamentary elections and the 2021 presidential poll. As a result, any possibility for future cooperation with US will equal zero.

From the optimistic point of view, any future uprising may elevate the Iran-US relations to a higher level, meaning a further dialogue could be viable. Nevertheless, this option

looks very unlikely as long as the Supreme Leader Ayatollah Khamenei remains in power.

Looking from a nuclear perspective, Iran will continue demonstrating considerable resilience and ingenuity in coping with US sanctions, and is likely to continue to implement the commitments of JCPOA as long as China, Russia and India continue to trade with it, and if EU continues maintaining its constructive attitude. Nevertheless, taking into account Rouhani's announcement of abandoning two principles of the nuclear deal (on 8th of May of 2019), we estimate that not all of the commitments are going to survive. What is more, on a longer run, the JCPOA future will depend upon the economic situation and complex political battles between moderates and hardliners in Tehran⁴⁰.

SCENARIOS FOR POLITICAL CHANGE

(2020 Parliamentary and 2021 Presidential Elections Outlook)

The Supreme Leader of Iran Ayatollah Ali Khamenei, elected for life-term, is not only the head of state but also the ultimate political and religious authority of the Islamic Republic of Iran. He is the successor of Ayatollah Ruhollah Khomeini, who was the leading figure of the 1979 Islamic revolution. Sitting at the top of the power ladder, he is responsible for the projecting and supervision of "the general policies of the Islamic Republic of Iran", according to Iran's Constitution. In order to ensure that the Supreme Leader's authority is respected, his power is extended through his clerical representatives, an estimated number of 2,000, that have "infiltrated" throughout all sectors of the government. In some spheres they are even more powerful than the president's ministers and have the authority to intervene in any matter of state on the Supreme Leader's behalf.

The lack of liberal democratic institutions and clerics' tendency to control the electoral process prove the fact that little can be changed even after the expected elections. As we have already mentioned above, the past-years experience in terms of the mass protests, have demonstrated that there is considerable dissatisfaction with the authorities and the general situation within the country. Nonetheless, these events coupled with sanctions

and isolations, have also manifested the regime's solidity and ability to withstand the continuous threats.

However, given that Khamenei is 79 years old, it may occur that shortly he may be replaced by another leader, who may (or may not) mark a new dynamic for Iran.

It is important to bear in mind that, according to Article 111 of the Constitution, if the position of Supreme Leader becomes unoccupied for any reason, a body comprised of the president, the head of the judiciary and an expert in Islamic law from the Guardian Council chosen by the Expediency Council must discharge the duties of the Supreme Leader. If any of the other members of this body are unable to discharge their duties, the Expediency Council can choose a replacement.

While proceeding from the condition that the Supreme Leader will be gone in a short period of time, the possible scenarios are the following ones:

a. Hard-liners in power

The most possible scenario would be Ebrahim Raisi succeeding Ayatollah Ali Khamenei. Being hard-liner, he is also a former student of Khamenei and remains loyal to him. He is politically well-connected and acceptable to the Islamic Revolutionary Guards Corps (IRGC) on account of his conservative views. He has undergone both clerical as well as university education and he is a custodian of the holiest shrine in Iran known as Imam Reza⁴¹. Since 7th of March, he is officially holds a post of a "chief justice", meaning there is a high probability of Raisi being chosen as a successor of Khamenei.

He will preserve the sacred principles of the Islamic Revolution, considering a high priority not a civilian reform but an economic improvement. Any further popular protests calling for a major political freedom are not discarded, and they will face a police intervention and massive arrests.

In a hypothetical case of Raisi being the Supreme Leader and the main opponent of Rouhani, the probability of hardliner victory in presidential elections of 2021 is significant. As a result, any possibility for future cooperation with US will equal zero.

In the Parliamentary elections in 2020, a new Majlis will be elected but without any considerable change in its composition. The vast majority will continue remain conservatives, but any moderate feature will be replaced by hard-liners' vision.

b. Moderates in power

In case of a more moderate successor, the future of Iran will go in parallel with increased economic liberalisation, lower social tensions, international openness and greater disposition for Iran-US relations improvement. Hassan Khomeini, the first Supreme Leader's grandson and Iranian cleric, could be one of the alternatives. He will be in favour of evolutionary rather than revolutionary change, conscious about the idea that a reform is needed for further preservation of the Iranian unity and stability. With him in power as Ayatollah, the popular protests will be considerably less in both number and frequency and thus, there will be no need for repression. In his fifties he is ideal candidate for Khamenei's replacement; nevertheless, the probability remains low due to lack of support and the fact that he can be opposed by the Guardian Council or by the IRGC due to the policies he is likely to adopt.

Nevertheless, it is almost certain that Supreme Guide's representatives, together with Assembly of Experts and the IRGC will remain under conservative control and resistant to the liberalisation. In addition, the transition period will take years or even decades for some significant changes to take place. A small chance of more moderate Supreme Leader will undoubtedly have some effects on parliament and presidential elections, as less control to be exercised and more transparency throughout electoral process are expected. It will widen the possibility of newly elected president to be a moderate and his policies will go in line with Rouhani's current ones.

The Parliamentary elections will bring no significant change, but its renewed composition may have more significant moderate character. Ali Larijani, brother of former head of Judiciary, may be re-elected as the speaker of Parliament. Nevertheless, he may also try to position himself for the presidential elections as he has already done in 2005. He is likely to obtain support from the reformists⁴². Within this story line, the first Vice-President of Iran, Es'haq Jahangiri, may also become president and follow Rouhani's policy strategy.

c. IRGC in power

Very unlikely, but still attainable candidate for substituting Khamenei is the IRGC. Backed by the current Supreme Leader, they are extremely powerful and keep under their control almost 25% of economy and business in Iran (energy, construction, telecommunication, media, mining, electronics, automobile, banking, agribusiness, etc).

Their victory becomes only possible if the death of Khamenei would cause a popular turmoil and aggressive demonstrations. In face of such scenario, they may assume that their intervention is the unique way to stop uprisings and restore the order. In the opposite case, their intention to overtake the seat will be considered as a major violation to the Iranian Constitution.

Qasem Soleimani, current Major General in the Islamic Revolutionary Guard Corps and commander of its Quds Force, who serves in Iranian politics since 1979, could become a potential aspirant. Soleimani attended the meeting during Assad's visit to Tehran last February and his rising public profile is an indicator that Iran's response to pressure by the United States and its allies is going to be in the direction of taking a harder line⁴³ rather than a moderate approach.

In the implausible case it happens, the escalation of demonstrations and popular uprisings will become inevitable and immediate and they will be similar to those of 2009. The repression will come instantly, with massive arrests, oppressions and even assassinations. The IRGC will follow the policy of strong state interference; will try to partially ban a social media and any chance for undertaking negotiations with US will be rejected. The breakdown of JCPOA and Iran-EU relations will follow without delay.

When all is said and done, on the other side, a scenario without Khamenei's death must be considered as well.

At this stage, it is too early to identify viable candidates for the 2021 elections, but we can make some estimation. While the three possible scenarios will remain, the probabilities will slightly change. It is very likely that Khamenei will prefer to keep the same order within regime as it is today so to avoid internal divisions and any future popular uprisings. Thus the chance for moderates' victory in the presidential elections

2021 is going to be higher. Then, the newly elected president will follow policies similar to Hassem Rouhani's and hardliners will have to wait till another "shock event" to occur. This would be the most agreeable option for JCPOA to survive under EU support and even a dialogue with US can follow lately. Having gained support from Iranian reformists, Ali Larijani opened the possibility that he could be a consensus reformist-pragmatist candidate to succeed Rouhani after the next presidential elections in 2021. However, at this stage little can be said or forecasted.

Nevertheless, the radical candidates do have a chance of winning elections if both: the deterioration of the economy takes a very sharp rhythm followed by social instability, or if a turnout is low as occurred with the 2005 election of Mahmoud Ahmadinejad (62%)⁴⁴. In this case, Ebrahim Raisi appears very likely to obtain the victory in presidential elections, as he has already tried to do back in 2017. The protests will be inevitable as well as the overall outcome for the country. JCPOA will become very close to be abandoned, the EU would be very likely to cease its support and, consequently, Iran will have no manoeuvre for withstanding the damaging effect of sanctions which are going to be reinforced.

The possibility for the IRGC is still very small and the output remains the most extreme and damaging for all the actors involved in the plot. Meanwhile, and in light of all the above mentioned evidences, the probability of hardliner victory is significant.

Additionally, on a longer run, the JCPOA future will depend upon the economic situation and complex political battles between moderates and hardliners in Tehran⁴⁵. In very unlikely case of the JCPOA being abandoned, we estimate that Iran will not aggressively pursue a nuclear weapon, as this would be likely to affect its trade ties with countries supporters. Still, the future of US or Israeli military action against Iran's nuclear facilities seems very unpredictable over the decade ahead.

In a nutshell, the Supreme Leader Ayatollah Khamenei is well-known for playing a key role in striking a "balance between different factions", even though his position is very clearly conservative and revolutionary orientated. Supreme Leader Ayatollah Ali Khamenei will not live forever, but his policies may due to his representatives and supporters within the regime. That is to say, whoever "inherits" the seat of the Supreme

Leader, will not be as powerful as Khamenei currently is and he will spend years in adopting a new posture.

We concludes that in any case the Iranian political system is likely to continue to be characterized by internal power struggles, especially between those who are elected and the unelected figures⁴⁶

Khamenei's demise or the election of a new president with a different political orientation could bring about a significant change in the interaction within the regime and affect its stability in the long term future⁴⁷.

(Figure III) THREE-POINT ESTIMATION

The three-point estimation provides three possible scenarios, one of which is the most likely estimate, another is the best case estimate and the last one is the worst case estimate. There are also possible consequences for each of these cases, and their probability measured in percentage (%)

	Rise of popular protests	Economic improvement	International openness	Iran-US dialogue	JCPOA attachment	Reinforced sanctions and total isolation
Hardliners The most likely estimation	85%	65%	25%	5%	>5%	80%
Moderates The best case estimate	25%	45%	80%	75%	85%	40%
IRGC The worst case estimate	90%	10%	0%	>5%	0%	95%

Source: Author's elaboration

Note: 0% means almost impossible; 50% means possible and 100% means almost certain

Critical Beneficial

ANNEX

US withdrawal from JCPOA

President Trump's main justification for withdrawing from "the stupidest deal of all time" was that Iran's regional policies violated the "spirit" of the agreement⁴⁸. The President stated that JCPOA "does nothing to constrain Iran's destabilizing activities, including its support for terrorism."⁴⁹

Historically, US policy toward the Islamic Republic of Iran has rested not on a single objective—whether confrontation or engagement—but on the broad-spectrum priorities. These include nuclear non proliferation, regional stability and counterterrorism, human rights and democracy inside Iran, and the normalization of US-Iranian bilateral relations.⁵⁰

In view of all the ongoing events, it may appear evident that today the ways and means to tackle the conflict have changed. Nowadays the US is playing exclusively to a domestic audience and its main priority is to safeguard its own interests in both energy and security fields, rather than helping Iran to improve its domestic sphere and become a world energy hub.

On one hand, the United States withdrawal from the JCPOA demonstrates the current administration's willingness to bring Iran back to negotiating a more comprehensive agreement, even though, Iran's complicated domestic politics make such initiative very difficult, primarily due to hardliners vs. moderates struggle. Moreover, the ultimatum issued by Secretary of State Mike Pompeo will be never accepted by the Iranian regime.

On the other hand, its controversially unilateral character, Trump's announcement about a naval deployment (on 5th of May of 2019) and the scope of US dozen demands, suggest that the Trump administration's real goal is somehow to produce a regime change in Tehran. Iran has been complying with the JCPOA and the deal has brought a considerable economic and trade improvements to Iran, as well as opened a door for negotiation with the West and the US. Consequently, the EU and other major countries opposed to US decision and started to work jointly on the SPV in order to overcome the

sanctions and guarantee Iranian economy its survival. This is likely to create some tensions between Europe and the US but they will not be powerful enough to split the long-lasting alliance between the two.

The Administration's goal to reduce Iranian oil exports to zero— hitting Iran where it hurts most- is just one of the means to reach the final end.

Such US decision about abandoning Iranian nuclear deal and re-impose sanctions, has met different critics. Whereas some guess this action can damage the United States' legitimacy as a nation that is "unwilling to abide by its diplomatic agreements" established during previous administrations⁵¹, others portray such "maximum pressure" approach as the unique way to avoid any possible threat from Iran.

Additionally, there are some experts, such as Jarrett Blanc, who claim the following: "At the end of the day, the problem is the administration has no real plan. They know how to make use of one tool, i.e. sanctions, but they lack any semblance of a broader strategy."

What if?

Regardless what the US main purpose is, there is already a vast range of consequences left after the sanctions and, on the other side, US withdrawal does not allow many scenarios for future.

First and foremost, re-imposed sanctions block Iran's efforts to gain the sufficient investments to expand its capabilities and capacities needed to improve its energy sector, project regional influence and solidify trade relationships with bordering countries⁵². For the US, the confrontation with Iran goes in line with the core elements of the New Iran Strategy (neutralizing the Government of Iran's destabilizing influence and constraining its aggression, denying the Iranian regime – and especially the Islamic Revolutionary Guard Corps, countering threats to the United States and the allies from ballistic missiles, etc)⁵³. But, as things stand, such confrontation will surely forbid US

from becoming an “energy dominant” nation by promoting energy exports and ensuring energy security⁵⁴.

Secondary, if the aim of US is to renegotiate the deal, Rouhani would be the sole person to agree meeting with Trump. However, the opposition and pressure from the hardliners will come forthwith, as they strongly believe that the US is the cause of all Iranian ills. After a long-lasting rancour, it will not take them long to overthrow Rouhani and occupy his place. This will provoke popular uprising and, shortly after, the scenario with IRGC in power cannot be ruled out (See: Figure III). Consequently, we forecast further escalation of tensions between Iran and the US and the outcomes for Iranian stability would be irreversible.

Thirdly, if the US seeks to destabilize and make a shift within Iranian regime, the Iranian hardliners could perceive it as an existential threat and follow the most radical and extreme approach of abandoning the JCPOA and advance further with a high-level enrichment of uranium and plutonium. This would also escalate tensions with Israel, the Gulf States and the US.

Finally, if, in very implausible case, the US manages to reduce Iranian oil exports to zero; Iranian leaders may shut down the Strait of Hormuz, a strategic passageway for about 35% of global crude oil traded by sea. Therefore, its closure, even for a brief period, will impact massively on the global economy⁵⁵ and, specially, on the American allies. This adverse effect on the global economy is, precisely, the situation that Trump wholeheartedly tries to avoid, as it had been witnessed after the allowance of waivers to eight countries. It is not the first time that Iran threatens the US by closing the Strait of Hormuz, however, this time the probability of this to happen appears greater because for Rouhani this tactic can mean a closer rapprochement with hardliners and IRGCs, who would certainly support this decision. This will enable Iranian President to peacefully serve his term till 2021 elections; yet, he will undoubtedly lose the EU support and, probably, the relationship with Russia and China.

In a nutshell, a US strategy of "maximum pressure" through sanctions remains not a hundred percent effective since there is a lack of congruence between allies. In a short span of time, the lingering effects of sanctions manage to keep Iran weak, but at the

same time such circumstances give Iran time to look for other partners and ways to monetize its resources. Moreover, Iran will likely continue to further its support of asymmetric proxy forces in the region⁵⁶.

It is, of course, true that the confrontational approach Trump opts for would limit, if not prevent, competition from Iran and increase the prospects for US LNG in the European market. But on the negative end of the spectrum, it would deny the global economy, especially the US's European allies and partners, with an alternative source of natural gas. This case is unacceptable in front of the present growing demand. But should the confrontation occur, then energy crisis, arms race and continuous exercise of power are very likely to take place in the mid-term.

Barring such scenarios, there is no room for a total cooperation between the two. For the United States, cooperation would only work if Iran agrees to negotiate along the Trump Administration's 12 demands; for the Iranian regime, which is influenced by hardliners, any amicable relationship with the US would put under risk its legitimacy.

Last but not least, there is a historical lack of trust between them.

Solution

In-depth knowledge of the fact that a global demand for natural gas is increasing and that Iran owns the second largest proved natural gas reserves in the world (33.2 trillion cubic meters), a hybrid approach towards Iran becomes the most adequate one.

It aims to cooperate through the competition and it should be orientated towards the Iranian youth population, which is considered to be the Iranian major strength and potential opportunity (as well as the gas sector). In this line, it is of high importance to put as a focal point Iran's desire for change and for monetization of its reserves. This would also be the unique and the most peaceful way to repress the hardliners and avoid the stagnation of the economy.

To conclude, only if the US and Iran change their minds and opt for a hybrid approach, would they enter into a period of detente and succeed in all the security and energy issues. Unfortunately, this advancement and a genuine diplomatic progress appear very unlikely during the Trump's Administration.

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