



Iran nuclear talks likely to be extended beyond July deadline

There is a strong chance that Western countries and Iran could secure a deal on Tehran's nuclear disarmament issue by early autumn, extending the period for negotiations beyond the July 20 deadline, according to a risk management consultancy.

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A deal is crucial for the Iranian government to stave off an economic crisis and popular unrest. Gross domestic product contracted 5.8% last year and is set for a further fall of 1.7% this year, according to the International Monetary Fund.

The Eurasia Group believes talks will likely be extended, until perhaps September. The latest crisis in Iraq could also give both parties excuse to extend negotiations.

"International diplomats and Iranian sources have told Eurasia Group over the past month that Iran no longer expects repeal of US sanctions to occur quickly after a final deal," said Eurasia's Cliff Kupchan. "Iran would conclude a deal in which it receives cash and waivers and suspension of key sanctions in return for steep, but reversible constraints on its nuclear program."

"Those constraints would become irreversible when sanctions are lifted, a formulation that is more flexible than previous Iranian positions. We continue to believe that the return of some Iranian crude to the market would follow shortly after any deal," he added.

For now, Iran's ability to export its crude oil as part of the interim deal has staved off any crisis. The International Energy Agency (IEA) notes that Iran crude output stood at 2.81 million barrels per day in the first quarter of 2014, compared to 2.68 million bpd in 2013.

According to IEA estimates, based on tankers' deliveries at their destinations rather than loadings in Iran, including condensates, Iranian exports averaged 1.11 million bpd in April, down from 1.58 million bpd in February and compared with 1.29 million bpd in March.

"Failure of these negotiations is still the primary potentially bullish wildcard for crude oil, since it would almost inevitably lead to a move to tighten the sanctions regime and reduce Iranian exports, but the likelihood of an extension if the deadline is not met effectively pushes back the timeframe for such an impact," said Greg Priddy, director, Global Oil at Eurasia Group.

"If a deal is reached, the sanctions relief would probably come in [multiple] tranches based on implantation by Iran, but the initial tranche would probably be on the order of 500,000 bpd above current levels."

Tehran has been unable to access USD 4.2 billion worth of frozen oil revenues that were expected to be released under the interim nuclear deal with western countries, according to Iranian officials.

BACKLASH

Iran's currency - a bellwether for business confidence among the country's investor community - remains depressed. The rial had fallen to 39,000 against the US dollar, but contracted to IRR 35,000 after President Hassan Rouhani's election. Earlier this year, the rial stood at IRR 29,700 on hopes of a deal, but has since fallen to around IRR 33,000.

Inflation in the country remains above 20%, according to central bank data released on June 1, although it has eased from 28% at the start of the month as Rouhani focuses on domestic economic issues.

"Rouhani's administration has delivered on exactly what it promised, but now Rouhani is running into popular resistance to his administrations' proposed cuts in fuel, electricity, and food subsidies," said Steve Hanke, analyst at Washington-based Cato Institute

Although Iranians are no longer hoarding food and basic items in panic as they did at the height of the crisis with Western powers, the Economist Intelligence Unit (EIU) has warned that the risk of unrest would become more acute if a deal with the West is not reached. It said a draft austerity budget for fiscal year 2014/2015 has provoked complaints from rural members of parliament.

"The government's subsidy reforms in March-April also present some risk of a public backlash. In the medium term, if a more complete breakthrough on the easing of sanctions is not made, the risk of unrest will become more acute and probably more difficult for the authorities to contain as high unemployment and anaemic economic growth persist," the EIU added.

Authorities are also looking to recover bad debts. The central bank say bad debts have reached 15.6%, as corruption and favoritism by the previous regime comes back to bite the banking sector. The authorities have reportedly handed over the names of around 600 people that collectively owe banks USD 33 billion.

Rouhani's promise to the electorate was to reduce inflation, stabilize the currency and strike a deal with the West. It is also important for Rouhani to keep more conservative elements at bay.

"Since he assumed office in August of 2013, Rouhani's mandate has been to pursue a nuclear deal. He remains strong on that bellwether issue. If the sides reach a final deal, Rouhani's

political clout would increase dramatically and he could well undertake some domestic liberalization," Kupchan said.