Political and economic impact of nuclear-related sanctions on Iran and its foreign policy options

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Introduction

Sanctions constitute a very important part of the international community's strategy to deal with Iran and its nuclear ambitions. These sanctions have invariably been used as an economic tool short of war. While the economic dimension of sanctions can have an impact, their working is always a political question. Evaluating the impact of sanctions, therefore, is a complicated exercise, made even more so by disagreements over what sanctions are meant to achieve. The many objectives cited in the case of Iran include:

1. Signalling international disapproval of Iran's nuclear programme
2. Delaying and disrupting Tehran's nuclear and missile programmes
3. Persuading Iran to halt its uranium enrichment efforts
4. Crippling the country, or at least the government
5. Using sanctions as a leverage to open fruitful negotiations on the nuclear issue, or a broader set of issues such as human rights abuses in Iran
6. Deterring other countries from taking the same nuclear route as Tehran has.
7. Helping the democratic opposition

In the vigorous debates about sanctions, particularly in the United States, all parties agree in principle that the prime target of sanctions has been the Iranian regime rather than the Iranian people, in order to encourage Iran to engage and compromise. However, one cannot deny the collateral damage in terms of making life difficult for innocent Iranian citizen, who have seen the prices of many basic foodstuff more than double since 2011 and who are struggling to access even life-saving medicines.[1] Officials in the U.S. are quick to point out that the chokehold on Iran's economy and the resultant economic pain will arouse the Iranians to defy and challenge the regime, forcing it to rethink their nuclear programme.

In the third and final U.S. presidential debate on October 22, 2012, the two candidates - President Barack Obama (Dem) and Governor Mitt Romney (Rep) –

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with all their differences on national and international issues - concurred on onething: the American sanctions against Iran have been successful. President Obama noted during the debate that in order to deter Iran from getting a nuclear weapon, the United States of America "organized the strongest coalition and the strongest sanctions against Iran in history, and it is crippling their economy. Their currency has dropped in value against the dollar, and their oil production has plunged to the lowest level since they were fighting a war with Iraq 20 years ago. So, their economy is in a shambles. And the reason we did this is because a nuclear Iran is a threat to our national security and it's a threat to Israel's national security."[2]

His rival, Mitt Romney, underscored Obama's point that the U.S. will stand with Israel and that a nuclear Iran is unacceptable to America. He contended that crippling sanctions against Iran are something that he had called for five years ago, and if he is elected as president, he "would tighten those sanction. I would say that ships that carry Iranian oil can't come into our ports. I imagine the EU would agree with us as well. Not only ships couldn't, I'd say companies that are moving their oil can't, people who are trading in their oil can't. I would tighten those sanctions further."[3]

Although the three decades of the various rounds of bilateral and multilateral sanctions have had a debilitating effect on the quality of life for a majority of the Iranian population, these have not been able to prevent the Iranian regimes, particularly President Mahmoud Ahmadinejad, from pursuing and developing a nuclear and missile programme. The West has long accused Tehran of developing nuclear weapons, but Iran insists its nuclear programme is for civilian purposes and denies it is trying to develop an atomic bomb.

The comments on Iran were a 'feel good' moment in an otherwise bleak year for both U.S. foreign policy and the economy. However, besides election rhetoric, pertinent questions remain: have the U.S. and its allies been smart and powerful enough to bring Iran around to their way of thinking after decades of trying? Has the threat of American financial and military power been the decisive factor in deterring Iranian President Mahmoud Ahmadinejad from pursuing a nuclear programme?

What has been the impact of sanctions on Iran? Although the three decades of the various rounds of bilateral and multilateral sanctions have had a debilitating effect on the quality of life for a majority of the Iranian population, these have not been able to prevent the Iranian regimes, particularly President Mahmoud Ahmadinejad, from pursuing and developing a nuclear and missile programme. The West has long accused Tehran of developing nuclear weapons, but Iran insists its nuclear programme is for civilian purposes and denies it is trying to develop an atomic bomb.

Iran and the sanction regimes

For over three decades now, Iran has been living under economic and military sanctions in one form or the other imposed on it by the United States of America and the international community, specifically, the European Union and the United Nations. The first of these sanctions were imposed on Iran in November 1979, when, for the first time, the U.S. President, Jimmy Carter, following the takeover of the U.S. Embassy in Tehran by the Iranian students as a response to a impending coup and reinstallation of King Raza Shah Pehlvi, issued Executive Order 12170 freezing about $12 billion in Iranian assets, including bank deposits, gold and other properties.

As the Islamic governments of the Ayatollahs strengthened their hold over politics in Iran, the consequent sanctions, particularly bilateral sanctions by the United States of America, encompassed the oil embargo, restrictions on the Iranian banking sector and its ability to carry out international transactions, the import of industrial and construction equipment, and even luxury goods. Over the decades of 1980s and 1990s, U.S. opposition to the Iranian nuclear ambitions grew, and after 2005, under the administration of George W. Bush, the U.S. issued a series of orders to freeze the assets of firms and individuals suspected of being involved in Iran's nuclear and missile programmes, its alleged support for terrorism, and its role in destabilizing Iraq. Sanctions under the Bush and consequently Barack Obama administrations covered not only Iran, but also dozens of foreign entities, particularly Chinese and Russian companies, for helping Iran's nuclear and missile programmes.

New sanctions have become increasingly severe in a bid to thwart Iran’s pursuit of nuclear weapons and their delivery systems. These are joined by a host of United Nations Security Council (UNSC) and European Union measures. In August 2012, the Obama administration announced new measures to pressure the Islamic Republic of Iran over its controversial nuclear programme, and the U.S. Congress passed additional sanctions seeking to further stifle Iran’s oil exports. According to the chairwoman of the House Foreign Affairs Committee, Ileana Rso-Lehtinen, the new sanctions, the toughest ever imposed on Iran; seek to "tighten the chokehold on the regime beyond anything that has been done before."[4]

A rapid deterioration of Iran's oil-driven economy has bandied the U.S. Congress and various governmental and academic circles around the idea of gasoline sanctions called Refined Petroleum Sanctions Act. The idea being that Iran lacks the refining capacity to meet its domestic demand and, as such, imports at least one-third of its gasoline. Therefore, banning those gasoline imports would begin to throttle Iran's economy, thus forcing it to cooperate on its nuclear programme.[5]

Sanctions on Iran: Quick Reference Timeline

Year	Sanctions
November 1979	U.S. imposes the first sanctions after Iranian students stormed the U.S. embassy in Tehran and took diplomats hostage earlier in the year. Iranian products are banned from import into the United States apart from small gifts, information material, foodstuffs and some carpets. $12bn in Iranian assets are frozen.
January 1984	U.S. prohibits weapons sales and all U.S. assistance to Iran
October 1987	President Reagan issues Executive Order 12613 prohibiting the importation and exportation of any goods or services from Iran.
March 1995	President Bill Clinton issues executive orders preventing U.S. companies from investing in Iranian oil and gas and trading with Iran.
May 1995	Clinton bans U.S. trade with and investment within Iran.
April 1996	Congress passes the Iran and Libya Sanctions Act (ILSA), a law requiring the U.S. government to impose sanctions on foreign firms investing more than $20m a year in Iran's energy sector. On September 30, 2006, the act was renamed to the Iran Sanctions Act (ISA), as it no longer applied to Libya, and extended until December 31, 2011. As of March 2008, ISA sanctions had not been enforced against any non-U.S. company; the act allows the president to waive sanctions on a case-by-case basis, though this waiver is subject to renewal every six months
December 2006	After having called on Iran to halt its uranium enrichment programme in July, the UN Security Council imposes sanctions on Iran's trade in nuclear-related materials and technology and freezes the assets of individuals and companies involved with nuclear activities. The sanctions are mainly an effort to curtail Iran's growing nuclear capacity, but while programmes to enrich uranium were stopped in 2002, they restarted in late 2005.
March 2007	UN Security Council votes to toughen sanctions by banning all of Iran's arms exports and extending the freeze on assets of those associated with the enrichment programme. One month later, the EU publishes an expanded list of Iranian individuals and companies deemed persona non grata in the bloc.
October 2007	The U.S. announces a raft of new unilateral sanctions against Iran, the toughest since it first imposed sanctions almost 30 years ago, for "supporting terrorists". The sanctions cut more than 20 organisations associated to Iran's Islamic Revolution Guard Corps from the U.S. financial system and three state-owned banks – Bank Melli, Bank Mellat and Bank Saderat. The

	Revolutionary Guard is branded as a proliferator of weapons of mass destruction
March 2008	UN Security Council passes further sanctions, including the monitoring of Iranian banks and all Iranian cargo planes and ships suspected of carrying previously sanctioned items. It also extends asset freezes.
June 2010	UN Security Council imposes fourth round of sanctions against Iran over its nuclear programme, including tighter financial curbs and an expanded arms embargo. The measures prohibit Iran from buying heavy weapons such as attack helicopters and missiles. US Congress pass the Comprehensive Iran Sanctions Accountability and Divestment Act of 2010 (CISADA). This act substantially amends, expands and extends the Iran Sanctions Act of 1996.U.S. Congress imposes new unilateral sanctions targeting Iran's energy and banking sectors. Penalties are instated for firms that supply Iran with refined petroleum products worth over a certain amount.
August 2010	EU prohibits the creation of joint ventures with enterprises in Iran engaged in oil and natural gas industries, as well as the import and export of arms and equipment related to nuclear activities. The sale, supply, and transfer of equipment and technology used for natural gas production is also banned.
May 2011	U.S. blacklists the 21st Iranian state bank, the Bank of Industry and Mines, for transactions with previously banned institutions.
November 2011	The U.S., UK and Canada announce bilateral sanctions on Iran. While the U.S. expands sanctions to companies that aid Iran's oil and petrochemical industrials, the UK mandates all British financial institutions stop doing business with Iranian counterparts.
January 2012	U.S. imposes sanctions on Iran's central bank, the main clearing-house for its oil export profits. Iranian in turn threatens closing off the transport of oil through the Strait of Hormuz. The European Union announces an oil embargo on Iran unless it curtails its nuclear programme. Saudi Arabia promises to fulfil EU gas needs
June 2012	U.S. bans the world's banks from completing oil transactions with Iran, and exempts seven major customers – India, South Korea, Malaysia, South Africa, Sri Lanka, Taiwan and Turkey – from economic sanctions in return for their cutting imports of Iranian oil.
July 2012	EU ban of Iranian oil exports takes effect.
August 2012	President Obama extends sanctions to the purchase or acquisition of Iranian petrochemical products. The sanctions are authorized in part for those who provide support to the National Iranian Oil Company and the Central Bank of Iran. New U.S. sanctions are also announced against foreign banks that help Iran sell its oil. The foreign banks include China's Bank of Kunlun and Iraq's Elaf Islamic Bank.
October 2012	EU tightens sanctions on the country's banking, trade, and energy sectors. The package prohibits any transactions with Iranian banks and financial institutions and includes an embargo on Iranian natural gas.

Source: www.fas.org; www.csis.org*; Wikipedia; Reuters*

Economic and political impact of sanctions on Iran

Some hard facts suggest that Iran is feeling the pinching effects of the Western sanctions. Hit by an inflation rate of 20-25 per cent, the Iranian Rial lost 40 per cent of its value against the dollar in October 2012, and Iranian oil exports have dropped by about one million barrels a day in the past 12 months, which is a 60 per cent drop in revenue. Iran's unemployment level remains officially around 11.1 per cent[6] (according to *Reuters*, it could be as high as 25 per cent). Poverty rate has increased since the Smart Subsidy Plan, in which the government cut subsidies. Because of the Plan, 80 per cent of labourers in the country live under the poverty line. [7]

As Iranians struggle with rising inflation and unemployment, demonstrators in Tehran clashed with police in October 2012 during protests about the declining value of the Rial, and there were protests reported in the city of Nishapur over the rising price of chicken – a main staple food for the Iranian working class – in July 2012 sending the government scrambling to stabilize the chicken market.[8] Workers protests have continuously occurred in Iran, and there is no doubt that the sanctions regime has had an impact in terms of the ability of the economy to perform. According to senior Iran analysts at the International Crisis Group, "Although it's not clear if there will be more protests, one thing is certain: Iran will experience a much more securitized environment in the run-up to the 2013 presidential elections."[9]

Nevertheless, even as the Iranian economy reels under financial warfare and psychological operations, these have failed to produce the one result that everyone in the Western world wants, which is Iran giving up on its nuclear ambitions. In February 2012, President Ahmadinejad claimed that Iran had loaded its first domestically made fuel rod into a nuclear reactor at Tehran Nuclear Research Centre signalling mastery of the nuclear fuel cycle and a new generation of centrifuges.[10] However, according to atomic chief Ali Akbar Salehi, the sanctions "may slow down Tehran's nuclear programme and could pose difficulties for its main uranium enrichment work, but will not stop the activities. This is a certainty."[11] At the same time, the International Atomic Energy Agency's quarterly report on Iran's nuclear programme shows that while Iranian oil revenue was declining, there was a simultaneous and dramatic increase in the number of centrifuges at Iran's once-secret Fordow nuclear site.[12]

But, even as Iran continues with the development of its nuclear programme despite economic troubles, there have been reports that as a last ditch effort to avert a military strike on Iran, the United States and Iran have agreed for the first time to one-on-one negotiations over the latter's nuclear programme.[13] The agreement is a result of intense, secret exchanges between U.S. and Iranian officials since the beginning of President Obama's first term in 2008. Statements from Iranian Foreign Ministry spokesman, Ramin Mehmanparast, have also signalled a modest move forward in negotiations.[14]

While President Mahmoud Ahmadinejad accuses the Western sanctions for the economic chaos in Iran, his political opponents actually blame Ahmadinejad's mismanagement of the economy for the precipitous currency collapse. Iranian opposition leader, Mir Hossein Mousavi, has lashed out at President Ahmadinejad for dismissing the sanctions as a "used hankie", and urged the government to tell the people about the impact of the sanctions. According to Mousavi, the sanctions will decrease GDP, increase unemployment, create more hardships for people and widen the gap between Iran and the developing nations, especially Iran's neighbours.[15]

Overcoming sanctions: Iranian options

Although short-term economic development in Iran has been undermined by sanctions; subsidy reforms, mismanagement and pre-election paralysis (Ahmadinejad's second term is due to end in the summer of 2013), growing public discontent and decreasing exports, Iran's economy is too big and complex to collapse. As of December 31, 2011, the regime is believed to have an estimated foreign currency and gold reserves of some $109.7 billion.[16] The petroleum sector, while currently experiencing slowed production, is seeing a shift towards producing energy-related goods and services for domestic consumption, lowering Iran's costs on energy overall.

Additionally, Iran is reported to have stockpiled about four month reserve of gasoline and also receives imports now from China and Mayaysia, both of whom would be reluctant to agree to enforce the sanctions.[17] Even if the Western sanctions were to set out at crippling Iranian petroleum exports, with the second largest reserves of natural gas in the world, many experts see the future of Iran in natural gas, and argue that growth in these sectors, attributable in part to sanctions, would boost Iran's economy in the long run.[18]

Also, while industry is suffering at the moment due to the increased cost of transportation, the devaluation of Rial is expected to lead to new opportunities such as increased domestic production, which could reduce Iran's reliance on imported goods and make its own exported goods more competitive on the global market. Short-term pressures will no doubt continue, but will ultimately contribute to greater Iranian self-reliance and shift to free market approach.

Regarding the effects of the sanctions on Iran's financial sector, while David S. Cohen, the U.S. Undersecretary for Terrorism and Financial Intelligence, speaking before the New York University of Law on "*The Law and Policy of Iran Sanctions*" on September 12, 2012, said that the accumulated effects of sanctions has disrupted Iranian banks and their access to international financing, thereby impeding their ability to facilitate Iran's illicit activities and creating unprecedented financial and commercial isolation for Iran, it has not been able to deter Iran from financing groups such as Hezbollah, the Shiite militia that emerged as Lebanon's most potent, or Hamas, the Palestinian militant group that now governs the Gaza Strip. Indeed, it is still sending billions in aid to prop up the Syrian regime of President Bashar al-Assad. Sanctions have instead shifted trade away from official banking system to foreign exchange bureaus.

The impact of UN and EU sanctions has also been minimized. For example, the nations that supported UN Resolution 1737 in 2006 continue to trade with Iran - China, India, Russia and Turkey have helped Iran to steer clear of the negative consequences of the sanctions. Following pressure from the U.S., Turkey and India announced in April 2012 that they are looking to lower their trade levels with Iran. Measures by the EU have not been a success story either. The EU has at times been unable to completely restrain nations from dealing with Tehran. More importantly, Iran has been one of Europe's major foreign oil exporters. This need for crude oil has allowed Iran the manoeuvrability to get around sanctions, as profit from sales lessens the financial impact of sanctions. In January 2012, however, the EU passed an "unprecedented" resolution to embargo all Iranian oil and, to support its implementation, set to begin in summer 2012. (*See Quick Reference Timeline above*)

Even as the U.S. and other multilateral sanctions to dissuade Iran may have pushed the two countries for the first time to one-on-one negotiations over the latter's nuclear programme, according to Jim Richards, author of the book *Currency Wars*, nothing that the U.S. has done up to now has worked, "We've tried everything: cyber warfare, financial warfare, psychological operations, assassinations and sabotage. It's not like we haven't been trying. But because the [Ahmadinejad] regime is so brutal, so entrenched, so powerful and so rich, it has not produced the thing everyone wants, which is Iran giving up on its nuclear ambitions. It's very clear diplomacy has failed and Iranians use the promise of negotiations just to buy time."[19]

Even if the U.S. and Iran sit down for talks, America officials worry that Iran could prolong the negotiations to try to forestall military action and enable it to complete critical elements of its nuclear programme, particularly at underground sites. Moreover, Iran has indicated that it wants to broaden the agenda of talks on its nuclear programme to include Syria, Bahrain and other issues that have bedevilled relations between Iran and the U.S. since 1979.[20]

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For the Western world, the current round of sanctions and their impact is based on rationalist assumptions, i.e., by making the cost of pursuing a nuclear programme greater by inflicting pain on the Iranian economy the Western hopes are that Iran will rationally realize that it is not in its interest to continue the programme. That the West has so far desisted from attacking Iran directly or indirectly shows that this perspective persists.

Iran, on the other hand, has not responded passively to the decades of sanctions, and has instead responded in ways that defy Western rationalist assumption.

For example, the Iranian government has threatened to close the Strait of Hormuz, which is a key strategic point for global transportation of oil.[21] There have also been references to the fact that Iran could board every super tanker transiting its territorial waters under the pretext of inspecting for weapons smuggling. Secondly, it has also recently sought to build new and stronger trade alliances with China, Malaysia and South American countries. It has also recently found different partners to avoid disturbing its transport flow by making use of Turkish seaports. It has reinvested in its infrastructure to depend more on Central Asia and Transcaucasia, and has become largely self-reliant in certain parts of the economy, such a weapons production.

And, finally, the sanctions have not been able to split the Iranian government or the people to the extent where the economic hardships caused by the sanctions would lead to a regime change. While the Iranians blame the Ahmadinejad government for incompetence and mismanagement of the economy, the nationalist feelings run too deep bringing people to rally around the flag following Western chiding. At the most, the recent spate of demonstrations in Iran have thrown up speculations that the coming elections in 2013 would bring forth candidates who would represent the technocratic approach to the management of the economy as well as better relations for Iran abroad.

Some of the possible choices being talked about include Hashmi Rafsanjani; Ali Larijani, the parliament speaker; the mayor of Tehran, Mohammad Baqer Qalibaf; forme speaker of parliament, Gholam Ali Haddad-Adel; Saeed Jalili, the current nuclear negotiator; and reformists such as former vice president Mohammed Reza Aref. But, even a change of the regime in Iran will not prompt Iranian leaders to surrender the nuclear programme that has been among their long-term priorities. To expect Iran to do so would require a considerable leap of faith.

To conclude with that million dollar question: Will this make an attack on Iran inevitable? Based on indicators by Intrade Contracts, bettors see a 12 per cent chance of a U.S. and/or Israeli air strike against Iran before December 31, 2012, and a 39 per cent chance before June 30 and a 51 per cent chance before December 31 of 2013. Whether this is true, will be played out in the coming months of 2013.

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