

Prospects of Pakistan-Iran Relations: Post Nuclear Deal

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Abstract

Now that the threat of Western sanctions on Iran has been removed, the prospects for improved relations between Pakistan and Iran provide increased opportunities. Both the countries have the opportunity to expand their bilateral political and economic relations as well as to move towards a broader integration of regional and international markets, particularly through the reinvigoration of the long awaited and long delayed Iran-Pakistan gas pipeline. Indeed, while there are many challenges, there are also bright prospects that this pipeline, dubbed as the ‘peace pipeline,’ can eventually be merged into the China-Pakistan Economic Corridor initiative that is underway to link China with the other regional markets, including Iran, through Pakistan.

Keywords: Nuclear Deal, Sanctions, Economic Integration, CPEC, Gas Pipeline.

Introduction

In July 2015, Pakistan welcomed¹ the nuclear deal between Iran and the six major powers hoping that with the lifting of sanctions on Iran following the deal, there will be increased opportunities for both Pakistan and Iran to expand their bilateral political and economic relations. The eventual lifting of sanctions on Iran will allow for the Islamabad-Tehran relationship to be increasingly driven by economic and geographic realities, rather than the interests of exogenous actors. In anticipation of the lifting of sanctions on Iran, Islamabad and Tehran are

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¹ “Pakistan, global powers welcome Iran nuclear deal,” *Express Tribune*, July 14, 2015, <http://tribune.com.pk/story/920778/pakistan-global-powers-welcome-iran-nuclear-deal/>

moving forward with the two major energy projects: a natural gas pipeline and an electricity transmission line. Together, both the projects will help alleviate Pakistan's crippling shortages of both electricity and vehicle fuel.

Following the landmark nuclear deal with the P5+1, the Iranian Foreign Minister, Javad Zarif visited Pakistan in August 2015 to explore opportunities for greater economic and security cooperation in the region. In extended meetings between Sartaj Aziz, Advisor to the Prime Minister on Foreign Affairs and the Iranian Foreign Minister Javad Zarif, both the countries agreed to expand mutually beneficial cooperation on a number of issues including expansion of economic linkages, enhancing bilateral collaboration in the energy sector, progress on the Iran-Pakistan gas pipeline, increasing regional cooperation, and carrying out joint efforts in the fight against extremism and terrorism. Both the countries agreed that economic integration and connectivity within the region should be improved in order to achieve better economic and commercial activity not just between Iran and Pakistan, but among all the neighbouring countries.²

In February 2016, Pakistan decided to revive economic and commercial relations with Iran including trade, investment, technology, banking, finance, energy.³ Moreover, in March 2016, Prime Minister Nawaz Sharif welcomed the Iranian President Hassan Rouhani to Islamabad, which set the course of future relations between the two countries.⁴

Pakistan and Iran had signed a US\$1.5 billion natural gas pipeline deal in 2013. However, because of the western sanctions on Iran, the project could not move ahead despite the stipulations of the deal that Pakistan would be fined up to US\$3 million a day if it failed to complete construction of the pipeline by the end of 2014. During his visit to

² "Iran wants expanded relations with Pakistan: Zarif," *Dawn*, August 14, 2015, <http://www.dawn.com/news/1200373>

³ "Pakistan lifts sanctions against Iran," *Dawn*, February 19, 2016, <http://www.dawn.com/news/1240603>

⁴ "PM, Iranian president hold delegation-level talks in Islamabad," *Express Tribune*, March 25, 2016, <http://tribune.com.pk/story/1072617/iranian-president-hasan-rowhani-arrives-in-islamabad/>

Pakistan in March 2016, President Hassan Rouhani revealed that while Iran has already completed the work on the pipeline on its side of the border,⁵ construction of the Pakistan portion did not begin until the summer of 2015 following the Chinese consent to fund and build the pipeline.⁶ It is important to note here that Iran has not opted to exercise the gas deal's penalty clause, indicating its keenness to become an energy partner with Pakistan.

With a population of close to 200 million, Pakistan is a large and growing energy and economic market. An important element for Iran to go through with the deal is Pakistan signing of a US\$46 billion China Pakistan Economic Corridor (CPEC) initiative. The project seeks to connect not only the Pakistani port of Gwadar with the northern Chinese province of Xinjiang, but also extend the rail and road networks of the project to regions beyond Pakistan to West and Central Asia, the Middle East, Africa and Europe. The project eventually hopes to bring in Iran to connect with the CPEC. The Iranian Ambassador to China has already expressed his country interest in extending the Pakistan gas pipeline to China. Already, Iran is connected to Gwadar by road and a freight rail connection between Pakistani and Iranian Balochistan has now also been restored.

In addition to the gas pipeline, Tehran is also making additional investments in the stability of Balochistan. Iran and Pakistan are close to finalising a 1000MW electricity transmission deal that would supply Pakistan's Balochistan province, which faces, along with other parts of Pakistan, the most severe electricity blackouts. Iran, which presently supplies Pakistani Balochistan with at least 75MW of electricity, has expressed interest in expanding the 1000MW supply to 3000 MW.⁷

⁵ “Iran’s Rouhani says can provide Pakistan gas through pipeline within months,” *News International*, March 26, 2016, <http://www.thenews.com.pk/latest/108153-Irands-Rouhani-says-can-provide-Pakistan-gas-through-pipeline-within-months>

⁶ “China to build pipeline from Iran to Pakistan,” *Wall Street Journal*, April 9, 2015.<http://www.wsj.com/articles/china-to-build-pipeline-from-iran-to-pakistan-1428515277>

⁷ “Iran can export 3,000 MW electricity to Pakistan,” *Express Tribune*, January 2, 2016,<http://tribune.com.pk/story/1020529/senate-question-hour-iran-can-export-3000mw-electricity-to-pakistan/>

Approach to the Study

A review of literature and news reports reveals that Pakistanis overall has a favourable view of Iran. A 2013 Pew Poll found that 69 per cent of Pakistanis had a favourable view of Iran, the highest percentage of 39 countries polled worldwide on perceptions of the Islamic Republic. According to a survey, conducted by the Pakistan Institute of Peace in 2013, political and religious parties in Pakistan hold on to the notion that Pakistan's ties with Iran should not be determined by the fears of upsetting the US but need to be based on Pakistan's own national interest. It will not only improve relations with Iran, but also promote security, economic cooperation and, sectarian harmony. According to a report by the International Monetary Fund (IMF) in 2013, while Pakistan ranked as the 11th largest trading partner of Iran, trade between the two countries has been well below its true potential despite geography and the infrastructure available under the Economic Organization Cooperation (ECO) framework. There is, however, a high volume of trade between the two countries through third country channels, smuggling and other illegal modes of financial transactions, mainly because of the western imposed sanctions on Iran, and the threats of penalties on the countries doing business with Iran.

In the framework of cooperative theory, this study attempts to make an overview of the current nature of relations between Pakistan and Iran in the background of the lifting of sanctions on Iran, and the potential for increased political, trade and economic ties. It also aims at analysing the issues that will and can form the basis of relations between Pakistan and Iran beyond 2016 including regional political issues and the potential for trade and investment between the two countries. A major question that this study seeks to answer is whether the (CPEC) and the politics of the two important ports – Gwadar and Chabahar – will become a uniting factor or lead to divisive politics between Pakistan and Iran.

The purpose of the study is to attempt a contemporary overview of the extended region in which the two countries are situated so as to analyse the geostrategic realities of their shared neighbourhood which call for a much greater cohesion in their policies. Due to the nature of the relationship, most of the analyses and arguments relating to economic relations between Pakistan and Iran are based on reports extracted from

newspaper sources and conversations with officials at Trade Development Authority of Pakistan (TDAP) and businessmen and women at the Islamabad Chamber of Commerce and Industry (ICCI).

The study while introducing the subject, is divided into two sections. The first section, “The Nature of Pakistan-Iran Relations” looks at the nature of relations between the two countries since the 1950s. The second section, “The Future of Pakistan-Iran Relations” deals with the new opportunities for both the countries that are now available in terms of bilateral trade as well as the prospects presented by the development of the CPEC.

Nature of Pakistan-Iran Relations

The starting point for this section is based on the realisation that the security and economic well-being of Pakistan and Iran are closely linked. The two countries were a source of strength to each other whenever they cooperated in dealing with important regional security issues. Both of them suffered when they worked at cross purposes. The mutual sentiments of friendship between Pakistan and Iran are based on the solid foundation of historical ties spanning several centuries, ethnic links, shared strategic outlook, close cultural bonds, and economic complementarities buttressed by alliances such as the Southeast Asia Treaty Organization (SEATO), the Central Treaty Organization (CENTO) and Regional Cooperation for Development (RCD). The advent of the Islamic Revolution in Iran brought about a paradigm shift in Iran’s internal and external policies. While Pakistan remained allied with the West despite the differences because of the former’s nuclear programme, Iran left the Western alliance and adopted an independent foreign policy. So, instead of a shared strategic outlook, Pakistan-Iran relationship became the victim of strategic divergence with its inevitable negative consequences. Economic cooperation between the two countries lost its substance and military-to-military links lost their warmth.

Political and Strategic Ties

The extent of Pakistan's relations with Iran and its standing in the Pakistani society is evident in various aspects ranging from language and culture to religion. Even the national anthem of Pakistan is almost entirely written in Persian language. The foundations of relations between the two countries were laid down in the Pakistan-Iran Friendship Treaty signed in May 1950. Throughout the 1950s, the relations grew closer as the two countries signed a cultural agreement in March 1956, an air travel agreement in 1957, and a border agreement in February 1958. High-level contacts blossomed over 1950s and the 1960s. These contacts were cemented even further with the signing of the US-led Baghdad Pact in 1954 between Pakistan, Iran and Turkey, which was renamed as CENTO in 1955. Despite the fluctuations in political and strategic relations, economics continued to hold sway in the bilateral relations which got further impetus with the signing of the RCD in July 1964 between Pakistan, Iran and Turkey in order to strengthen their socio-economic development. A new association known as the ECO in January 1985 replaced the organization. Over the Cold War years, the relations were strongly influenced by regional and global shift of alliances.

Both the countries, however, had divergent security perceptions. Iran's main security interests lay, primarily in West Asia, especially in the Persian Gulf region. Whereas, on its northern and eastern sides, Pakistan's principal security concerns revolved around India, and in the 1980s, Afghanistan. Therefore, developments either in the Persian Gulf or South Asia had a direct bearing on relationship between Pakistan and Iran largely due to regional contiguity and security complexes that played an important role in the formation of relations largely influenced by their relations with Saudi Arabia, India, and the United States.

Thus, while Pakistan and Iran had worked together to support the Afghan Mujahedeen, against the Soviet Union, Pakistan's anti-USSR efforts that were heavily supported by Saudi Arabia, Kuwait and the US, did not sit well with Iran. Pakistan and Iran extended full support to the Afghan pushback against the Soviet invasion in 1979, and together supported the Bonn Agreement for the reconstruction of Afghanistan in December 2001, even though the bilateral relations were constantly

tested, following the rule of the Taliban and the civil war in that country. Subsequently, the Soviet military withdrawal from Afghanistan emerged as a bone of contention between Iran and Pakistan over their respective influence in Afghanistan.

Following the Islamic Revolution, the departure of Mohammad Reza Shah Pahlavi in January 1979 and the subsequent US sanctions, and Pakistan's close relations with Saudi Arabia, the 1990's were an unequal patch in the bilateral relations due to competing and diverging geopolitical and ideological interests.

After the establishment of the Taliban government in most parts of Afghanistan in 1996, the relations between the two countries further deteriorated that further led to a climate of mistrust. Though a peaceful and stable Afghanistan was in both countries' interest, Pakistan was more inclined to support the Pashtun groups of the Mujahedeen whereas Iran extended its help to the Northern Alliance comprising other ethnic groups that held its sway over north-eastern Afghanistan. This support for the opposing groups worsened relations between the two. As Tehran was not comfortable with the radical Sunni Taliban regime, it felt insecure and perceived it as a serious threat to its national security, consequently adopting a proactive policy towards Afghanistan.

The murder of six Iranian diplomats and some agents by the Taliban in August 1998 was a watershed as President Mohammad Khatami sought to thaw relations between Iran and both the US and the Taliban.

In a visit to Tehran in December 1999, President Musharraf formally invited President Khatami to Islamabad. Nearly two years after his invitation, in December 2001, the Iranian Foreign Minister, Kamal Kharazi visited Pakistan, which led to an improvement of relations between the two countries. In his meeting with Kharazi, Pakistan's Foreign Minister, Abdul Sattar told his Iranian counterpart that the "sun was shining" on ties between the two countries, and both the countries needed to put the six years of Taliban rule behind them by taking full advantage of the new beginning in Afghanistan.⁸ The two countries moved towards not only developing a common understanding on

⁸ "Pakistan and Iran hail new era," BBC, November 30, 2001, http://news.bbc.co.uk/2/hi/south_asia/1682654.stm.

Afghanistan but also to revive a number of joint ventures including a multi-billion dollar gas pipeline.

Moreover, both the countries decided to establish a joint Pakistan-Iran committee for the reconstruction of Afghanistan under the UN development programme and other international aid agencies. During a visit by President Khatami in December 2002 and the follow up visit to Tehran by Prime Minister Shaukat Aziz in February 2005, both the leaders focused on developing economic and trade relations which stood at US\$376 million with Pakistan's export to Iran amounting to US\$92 million for 2005.⁹

Though the then Pakistan Foreign Minister Khurshid Kasuri set the tone of taking concrete steps to promote economic ties, Afghanistan continued to hamper closer relations with the emergence of a new militant Sunni Baloch group – Jundallah (Soldiers of Allah) – claiming to fight for the rights of Iran's ethnic Baloch and minority Sunni population. The group's violent operations put Iran on the defensive and a more rigorous monitoring of its border with Pakistan.

The activities of the group, along with drug and gasoline smuggling led Iran to build one of the world's most fortified barriers including a new fence and a 700 km long and three metres high concrete wall including deep ditches, barbed wire and watchtowers.¹⁰ As militant sectarianism grew as a phenomenon on the border with Pakistan, the menace became a headache for both Pakistan and Iran.

While sectarian violence and terrorism rose between 2007 and 2013 in Afghanistan, Pakistan has managed to insulate itself from the regional sectarian war following the launch of the Operation Zarb-e-Azb by the Pakistan Army in June 2014 in North Waziristan, which served as a safe haven for the anti-state TTP and a medley of other sectarian, regional and transnational jihadist groups. The government of Prime Minister Nawaz Sharif has also begun a comprehensive, nationwide crackdown on Tehreek-e Taliban Pakistan (TTP) and its expressive anti-Shia

⁹ "Four agreements to be signed with Iran," *Dawn*, February 19, 2005, <http://www.dawn.com/news/383128/four-agreements-to-be-signed-with-iran>

¹⁰ "New Walls Rise After Iron Curtain Falls," *Radio Free Europe Radio Liberty*, <http://www.rferl.org/content/new-walls-rise-in-europe-iron-curtain-/27214403.html>

partners, Lashkar-e Jhangvi, which has weakened their ability to target Shia Muslims. Consequently, sectarian terrorists, now, find far less operating space inside the country than before. Since the beginning of 2016 sectarian terrorism continues to decrease in frequency following the elimination of several hardcore sectarian terrorist leaders including Usman Kurd, the leader of the Balochistan wing of prime anti-Shia terrorist group, Lashkar-e Jhangvi, and Malik Ishaq and Ghulam Rasool Shah, the prime Ahle Sunnat Wal Jammat (ASWJ) militants in Punjab. There is now an unprecedented intelligence sharing and coordination between the civilian and military security agencies in Balochistan and Karachi, where most of the sectarian violence has taken place in recent years. Since the launch of counterterrorism military operations by Pakistan in North Waziristan and nationwide, the incident of terrorism, including sectarian violence, has dropped to a considerable extent.¹¹

It is pertinent to mention that Pakistan's decision of not to play an active combat role¹² in the Saudi-led Yemen war has, and will continue to have, mitigating effect on Iran. Additionally, there is an alignment in how Iran and Pakistan view stability in Afghanistan. Iran has expressed support for the Pakistan-backed reconciliation process in Afghanistan, and which has been evident in Tehran's hosting of multiple Afghan Taliban negotiations. At the same time, both the countries see the so-called rise of the Islamic State, which has an embryonic presence in South Asia as a threat.¹³

Trade and Economic Cooperation

Since the Islamic revolution in Iran in 1979, economic and trade relations between Pakistan and Iran have remained marginal because of many reasons. It includes the lingering mistrust, the American pressure, the complexity of the Afghanistan situation, the discord between the US and Iran concerning Iran's nuclear programme, and the Western

¹¹ Ibid.

¹² "Pakistan won't rush to join anti-Iran alliance," *Dawn*, March 15, 2015, <http://www.dawn.com/news/1169671>. Also see 'Pakistan will not participate in conflict that divides Muslim Ummah: KhawajaAsfi, *Dawn*, March 27, 2015. <http://www.dawn.com/news/11722>

¹³ Ibid.

economic sanctions against Iran which did not allow Pakistan and Iran to take full advantage of the opportunities that became available after 9/11.

In 2014, overall trade with Iran was US\$217 million out of which exports from Pakistan amounted to US \$53. The key export items of Iran to Pakistan included: iron ore, iron scrap, dates, detergents, transformers, chemicals, bitumen, polyethylene, propylene, etc. while export items of Pakistan to Iran include rice, fresh fruits, meat cloth and mechanical machinery.

**Table No. 1
Pakistan's Trade with Iran (Million USD)**

Year	Exports	Imports
2009	400	922
2010	207	962
2011	162	572
2012	153	153
2013	98	168
2014	53	164

Source: Pakistan Bureau of Statistics, quoted in 'Trade with Iran, Criterion Quarterly, vol. 10, no. 4, February 1, 2016.

A number of reasons contributed to the low trade volumes. These included: high non-tariff barriers in Iran; high customs duty on items in which Pakistan has comparative advantage (e.g. textile); slow process of import approvals in Iran; lack of enabling infrastructure that can facilitate trade on Pakistan's side; poor rail, road and air connectivity between the two countries; and less number of land border trade posts.¹⁴

Despite the abysmal trade relations, Pakistan and Iran have, over the years, been able to develop a broad range of institutionalized steps under the ECO framework that provide tremendous opportunities for widening the scope of their trade relations. In the 1990s for example, both the countries conceived the Iran-Pakistan Gas Pipeline project that was eventually signed in March 2009 by the then President Asif Ali Zardari and President Mahmoud Ahmединajad. It was formally inaugurated in

¹⁴ "Trade with Iran," *Criterion Quarterly*, vol. 10, no. 4, February 1, 2016.

March 2013. The project dubbed as ‘Peace Pipeline’ that envisaged delivery of gas from Pars gas field to Pakistan through a 1,150 km pipeline on the Iranian side, and a 781 km pipeline on the Pakistan side of the border to be joined eventually to the domestic pipeline network in Pakistan. The construction of the pipeline was scheduled to be completed by December 31, 2014. However, while Iran has almost completed the portion of the pipeline on its side of the border, the pipeline on the Pakistani side of the border could not be completed because of the lack of funds and the sanctions on Iran.

Import of electricity from Iran has also been on the cards. In 2002, Pakistan and Iran signed an agreement for import of 74 MW of electricity from Iran. This project was postponed due to the sanctions on banking transactions with Iran. Pakistan signed a Memorandum of Understanding (MoU) in 2012 to import 1000 MW of electricity from Iran, and according to the National Electricity and Power Regulatory Authority (NEPRA) of Pakistan imported 31.3GWh of electricity from Iran in December 2014. The transmission of electricity was carried out through a 132KV transmission line from Iran to Pakistan.¹⁵ In March 2015, Iranian company Tavanir and the National Transmission and Dispatch Company (NTDC) approved the feasibility report on 1,000 MW electricity supply from Iran to Pakistan for which a 500 kV Iran-Balochistan line will be laid at a cost of US\$700 million.¹⁶ In August 2015, Iran also offered to export 3000 MW of electricity to Pakistan.¹⁷

An agreement, Economic Cooperation Organization Trade Agreement (ECOTA) was signed between Pakistan, Iran, Turkey, Afghanistan and Tajikistan in 2003, which envisaged the establishment of a free trade area that represents another framework that holds the potential of bringing Pakistan and Iran closer. However, this agreement has not been implemented yet, due to different interpretations of the articles of the agreement on tariff.

¹⁵ “Power Supply From Iran To Balochistan,” *Pakistan Economist*, July 2009, <http://www.pakistaneconomist.com/pagesearch/Search-Engine2009/S.E506.php>.

¹⁶ “Nepra approves purchase of 1000 megawatts power from Iran,” News Channel, March 11, 2015, <http://www.pakissan.com/english/news/newsDetail.php?newsid=28438>

¹⁷ “Iran again offers 3,000 MW electricity to Pakistan,” *News International*, August 11, 2015, <http://www.thenews.com.pk/print/14040-iran-again-offers-3000mw-electricity-to-pakistan>)

Pakistan and Iran had also signed a Preferential Trade Agreement (PTA) in March 2004. According to officials at TDAP, the agreement would be finally converted into a Free Trade Agreement (FTA). The purpose of the agreement is to strengthen economic and political relations between the two countries and to promote a more secure environment for sustainable growth of trade and expand mutual trade by exploring new areas of cooperation. The trade embargo on Iran was another reason why PTA could not achieve its full potential. Also, a substantial amount of trade had to be routed through a third country – Dubai and the UAE in this instance – despite that fact that Pakistan, Iran and Turkey have established the Istanbul-Islamabad-Tehran railway network proposed in the 18th Regional Planning Council of the ECO held in Islamabad in 2008. This 6,500 km long rail network is one of the major projects of ECO with the aim of connecting Central Asia with Europe. While Pakistan Railways is now running freight operations between Zahidan in Iran and Quetta in Pakistan, the decision for the revival of the ‘Gul Train’ – an Islamabad-Istanbul via Tehran freight train – is still pending.

Under the ECO framework, Pakistan, Iran and Turkey have also established a number of initiatives including the ECO Trade and Development Bank headquartered in Turkey and representative office in Karachi. A comprehensive Transit Transport Framework Agreement (TTFA) – an ECO Fund for the implementation of the TTFA has already been established, and the joint ECO Secretariat and Islamic Development Bank (IDB) regional project for the implementation of TTFA is in its final stages of implementation.¹⁸ Moreover, an ECO truck caravan initiative was launched in 2010 in Islamabad under TTFA besides the establishment of ECO Reinsurance Company for the purpose of promoting regional linkages and to support economic development. Unfortunately, all these initiatives have yet to achieve the goal of increasing trade within the ECO member countries.

Pakistan and Iran have also signed five MoUs in December 2014 to enhance trade cooperation, which include a Joint Investment Committee to identify areas for investment in both the countries. Furthermore, both

¹⁸ Criterion Quarterly, op.cit.

the countries agreed to open bank branches and facilitate a currency swap for bilateral trade. It was agreed that cooperation between Pakistan's Small and Medium Enterprise Development Authority (SMEDA) and Iran's counterpart organization would be enhanced. An agreement was reached to establish a sister port relationship between Karachi and Chabahar ports. Trading centers along the Iran-Pakistan border were also identified that could be used as common markets to sell goods at concessional rates of customs and other duties in order to control illegal cross border trade.¹⁹

Despite the huge potential for cooperation and the infrastructure for economic linkages, the trade volume between the two countries remained low due to the reasons mentioned in the previous paragraphs. In April 2015, both Pakistan and Iran agreed on a five-year trade facilitation plan to enhance bilateral trade to \$5 billion, and an early elimination of all non-tariff barriers under the 2006 Preferential Trade Agreement to fulfill the shared vision of Prime Minister Sharif and President Rouhani to increase bilateral trade from \$1b to \$5bn. Both the sides also agreed to form a working group to suggest widening of the 2006 Pakistan-Iran Preferential Trade Agreement.²⁰

Future of Pakistan-Iran Relations

Pakistan is especially interested in improving and coordinating its economic relations with Iran. With the lifting of the international sanctions on Iran, all legal hurdles of doing trade with Iran have now been removed. This will give a boost to economic relations between the two countries and both the countries would no longer have to rely on indirect trade. While economic relations will be the major focus of future relations, there will be many foreign policy issues that will impact such relations. Of particular concern would be China's efforts to develop the China-Pakistan Economic Corridor (CPEC), and Iran's growing relations with India.

¹⁹ "Pakistan, Iran sign 5MoUs to enhance bilateral cooperation," *Pakistan Today*, December 9, 2014, <http://www.pakistantoday.com.pk/2014/12/09/business/pakistan-iran-sign-5-mous-to-enhance-bilateral-cooperation>

²⁰ "Pakistan, Iran eye trade at \$5 billion," *Dawn*, April 23, 2015, www.dawn.com/news/1177635

Prospects for Emerging Bilateral Ties

Pakistan has always endeavoured to maintain a special bond with Iran. Keeping in view, the sanction on Iran and repercussion for the states doing business with Iran and the subsequent lifting of sanctions on Iran in January 2016, presented opportunities for Pakistan to widen and deepen the scope of the 2006 Preferential Trade Agreement with Iran. The changing regional and global environment in terms of security and the growing prospects of economic cooperation between states in the region would have both implicit and explicit impact on such relations. Pakistan-Iran relations are now increasingly being defined by economic realism²¹ and cooperative framework of interaction. One can see two major opportunities in this regard:

1. Trade and energy cooperation between Pakistan and Iran can be increased through the revival of the Iran-Pakistan gas pipeline. The gas pipeline could meet 25 per cent of Pakistan's energy needs. The total cost of the project is estimated at US\$7.50 billion with the cost, on the Pakistani side, of about US\$1.25 billion. The project would supply 750 mcft daily through its 1700 km length, and it is estimated that at least 5000 MW of electricity could be generated through the use of Iranian gas.²² The pipeline can also become a part of the larger China-Pakistan Economic Corridor initiative;
2. The increased cooperation of Iran can be sought to extend and develop the China-Pakistan Economic Corridor from Gwadar to Chabahar.

The geo-political situation is undergoing a remarkable paradigm shift. Iran has become a prominent player in this new configuration.

²¹ Realism is one of the oldest paradigms in International Relation and International Political Economy. It is “a spectrum of ideas” based on shared principles about what determines states behaviours towards one another. For further elaboration on economics and realism, please refer to contributions made by Robert Gilpin: *The Politics of Transnational Economic Relations* (1971), and Kenneth Waltz: *Theory of International Politics* (1979).

²² “Iran has not much gas for sale, Pakistan must act swiftly,” *Express Tribune*, August 24, 2015, <http://tribune.com.pk/story/943391/iran-has-not-much-gas-for-sale-pakistan-must-act-swiftly>

Pakistan's increasing cooperation with Russia, the efforts for reconciliation in Afghanistan, and the expanding economic ties with China call for an inclusive approach. The change of guard in Iran, where a reformist like Hasan Rouhani has replaced hardliner Mahmoud Ahmadinejad, has also introduced new dynamics in Iran's national agenda.

Iran, under President Rouhani, has displayed pragmatism that will usher in an encouraging environment. President Hassan Rouhani has been quick to conclude six MoUs, including a "Five-Year Strategic Trade Cooperation Plan" with Pakistan to bolster bilateral relations in the areas of trade, economy and energy. The two sides have also agreed to deliberate on the ways to boost bilateral trade by means of preferential trade and to move forward for a free-trade agreement through an opening of two additional crossing points along their border to encourage and facilitate trade and people-to-people contacts that have suffered due to sanctions. President Rouhani also agreed to explore the possibility of sea trade through Pakistan's Gwadar Port and Iran's Chabahar Port.²³

China Factor

The growing ties between China and Iran is an important factor that needs to be weighed by the leadership in Pakistan to immediately take necessary steps to ensure a trilateral cooperation among Pakistan, Iran and China. There is an added factor to push this kind of cooperation forward.

During a visit to Iran by Chinese President Xi Jinping in January 2016, both Iran and China signed a US\$600 billion trade deal. Both agreed to expand multidimensional ties and increase bilateral trade more than tenfold in the next decade. The two countries signed seventeen accords including agreements on cooperation in nuclear energy to become a part of China's 'One Belt, One Road' initiative.²⁴

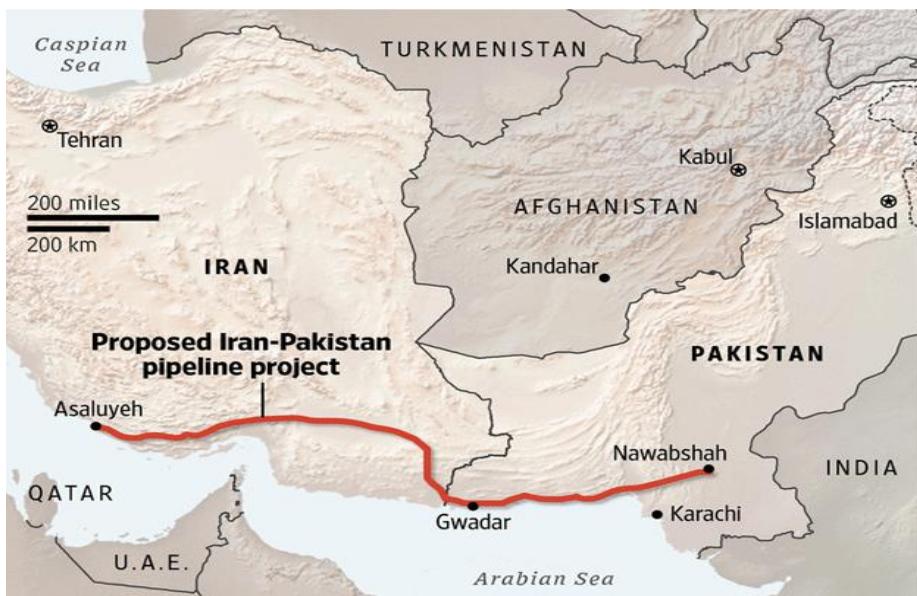
China Petroleum Pipeline Bureau, a subsidiary of Chinese energy giant China National Petroleum Corporation (CNPC), has already agreed

²³ "Pakistan, Iran eye trade at \$5 billion."

²⁴ "Iran, China agree \$600-billion trade deal after sanctions," *Dawn*, January 23, 2016, <http://www.dawn.com/news/1234923>

to build Iran-Pakistan gas pipeline on the Pakistani side under the CPEC initiative. The 435 miles (700 kilometers) of pipeline from the western Pakistani port of Gwadar to Nawabshah in the southern province of Sindh will connect to Pakistan's existing gas-distribution pipeline network, and is expected to cost US\$1.5 billion to US\$1.8 billion. Under the deal, 85% of the financing will be provided by a Chinese loan, with Pakistan coming up with the rest.²⁵

Iran-Pakistan Pipeline Project



Source: Sui Northern Gas Pipelines Limited

Concisely, Iran has agreed to consider options of involvement with the proposed CPEC, with the aim to improve and upgrade links via railways as well as road, targeting to widen scope of goods transit.

²⁵ "China to build Pakistan-Iran gas pipeline: Report," *Express Tribune*, April 9, 2015, <http://tribune.com.pk/story/866893/china-to-build-pakistan-iran-gas-pipeline-report/>.

Indian Factor

Although, there are growing prospects of increased economic cooperation and connectivity between Pakistan and Iran, the growing Indian influence and ties with Iran may present obstacles as India pushes ahead in its relations with Iran, particularly in the context of developing the Iranian port of Chabahar, both as a competitor to Gwadar and a means through which India can access Afghanistan and Central Asia.

India's relations with Iran center on two main issues:

1. Entrepreneurial opportunities that are particularly in the oil and gas sectors;
2. Regional issues, notably Afghanistan and Pakistan, which are pursued mainly by Indian intelligence agencies.

India backed out of the multi-billion dollar IPI gas pipeline project in 2009. This was done largely due to Indo-US nuclear deal, the US sanctions and the fact that the pipeline would traverse Pakistan. However, it continued to develop economic and political relations with Iran using the exemptions from the US sanctions provided especially to India.

In the attempts to forge more direct links with and through Iran, onto Afghanistan and countries of Central Asia, Indian Prime Minister Narendra Modi has now pledged up to US\$ 500 million to develop the port of Chabahar as part of the trilateral transit agreement between India, Iran and Afghanistan. Iran and India have also signed a number of agreements to enhance cooperation in technological fields including aerospace, biotechnology, and nanotechnology, petrochemical, counter-terrorism, and banking cooperation.²⁶

Chabahar port, which is a symbol of Indo-Iran economic and strategic cooperation, will give India access to Afghanistan, bypassing Pakistan entirely. Chabahar port is also linked to India's receiving natural gas imports from Iran as the port would also serve as the point of origin for the proposed Iran-Oman-India pipeline. India's strategic

²⁶ "India and Iran sign 'historic' Chabahar port deal," BBC, May 23, 2016, <http://www.bbc.com/news/world-asia-india-36356163>

thinkers also view the port as a strategic counterweight to China's pursuit of Gwadar port in Pakistan.²⁷ Reports have also emerged over the likelihood of India sealing a new US\$ 4.5 billion deal with Iran that will see the construction of a direct 1,400 km undersea gas pipeline from the Iranian port city of Chabahar to the Gujarat coast.²⁸

Although India's presence in Iran is substantial, however, after the lifting of sanctions, it is bound to lose the advantage it gained over the sanctions period to the other trading partners of Iran including Pakistan and China. Pakistan has already won a political victory by not taking side in the Iran-Saudi spat, and it must avoid India-centric moves. On the contrary, India must be met with this competition on economic grounds rather than muddy it with sentiments of political rivalry. For that to happen, it is also necessary that our borders with Iran are properly monitored to discourage smuggling and anti-state elements. Pakistan would need to establish normal trading relations with both Iran and India.

So far as geopolitical rivalry over construction of Chabahar (by India) and Gwadar (by China) is concerned, it is more imaginary than real and raises unnecessary concerns. Both the ports can be complementary to each other rather than competitive. The more the regional actors get engaged for development, the better it would be for the prospects for peace in the region.

Saudi Factor

Pakistan has a history of cooperation with Saudi Arabia against Tehran's interests in Afghanistan. Pakistan, Iran and Saudi Arabia, therefore, make a complicated triangle. Pakistan, keeping in view the international dynamics of Shia-Sunni schism, faces the dilemma of balancing between Iran and Saudi Arabia. However, given the changing dynamics of its relations in the present context, it cannot afford to embroil itself directly

²⁷ "Cooperation or competition: Gwadar versus Chabahar," *Foreign Policy News*, January 31, 2016, <http://foreignpolicynews.org/2016/01/31/cooperation-or-competition-gwadar-versus-Chabahar/>

²⁸ "India, Iran close to strike \$4.5B undersea gas pipeline deal," *International Business Times*, March 17, 2016,<http://www.ibtimes.co.in/india-iran-close-strike-4-5b-undersea-gas-pipeline-deal-671072>

in the most sensitive aspect of Iran-Saudi cold war. Pakistan's decision not to play an active combat role in the Saudi-led Yemen war was, in fact, the test of its diplomatic skills that have proved successful in keeping Pakistan out of the Iran-Saudi tussle. It has urged restraint in the current Iran-Arab tensions and has opposed any military action.

On top of all this, there is now a growing alignment in how Iran and Pakistan view stability in Afghanistan that had once been the hotbed of proxy war between Saudi Arabia and Iran. The shift in Tehran's stance over reconciliation talks with Taliban is one of the major reflections of Iran's pragmatism. Iran, who had disapproved any kind of negotiations with the Taliban till 2009, has offered to play its role in mediating with the Taliban. It has now expressed support for the Pakistan-backed reconciliation process in Afghanistan. Tehran has hosted multiple Afghan Taliban negotiations. At the same time both Iran and Pakistan see the so-called Islamic State, which has an embryonic presence in South Asia, as a threat.

However, balancing Iran-Arab relations will be a difficult and uphill task for Pakistan, especially when Pakistani guest workers are employed in the Gulf and it is mostly their remittances that keep the country's economy afloat. Notwithstanding these difficult circumstances, Pakistan will have to remain neutral and alert against the import of toxic ideology of fresh violence at home.

Conclusion

The times for Pakistan and Iran are challenging, but they equally provide the opportunity to close their ranks. In order to achieve the objective, the two sides need to develop a joint strategy to secure their land and maritime interests. Even as the two countries move to improve and upgrade their transportation and communication linkages, those trying to create differences between them are creating a negative impression of presenting the Gwadar Port in Pakistan and Iran's Chabahar as rival international trade ports. The joint waterways have more than enough real and potential trade volume. Viewed through the lens of cooperation, both the ports present an opportunity that must be tapped by opening up discussions on building links between Chabahar and Gwadar, as well as enhanced road links between Iran, Pakistan and Iran.

There is a lot of room for trade and business dealings between Pakistan and Iran. However, both countries need to strengthen their banking connection and currency swap to promote trade. Iran has already offered that Iran's Bank Milli and Pakistan's National Bank could open branches on reciprocal basis, but this process is taking time and remains pending. It would be far more profitable for trade to be permitted in local currencies.

Also, the ongoing security issues such as smuggling, drug trafficking and encroachment of non-state actors along the border areas need to be handled through positive cooperative efforts including joint security exercises both on land and sea on a regular basis. To this end, border control technologies need to be incorporated in manning cross-border check posts and streamlining rules against smuggling and illegal cross-border traffic. The construction of walls to seal illegal movements or smuggling is no longer an enduring solution. When border trade and development takes place in enough quantum and frequency, the issues of insurgency would subside, if not totally ceased. At least it would provide lesser temptation to outsiders in meddling or acting as spoilers.

Opportunities for trade and industry must not take these in a complacent manner. Pakistan and Iran have joint chambers of commerce, and these must work to divert informal trade to legal channels by checking smuggling, revision of trade policies and tariff and non-tariff barriers. It is difficult to check smuggling through administrative measures only. The best way would be to work through elimination or reduction of tariff and non-tariff barriers. As an additional step forward, both the countries must extend trade relations by arranging trade fairs and exhibitions.

Pakistan and Iran have to become major players in the region. The goalposts have moved, but the bond of brotherhood, cooperation, and economic survival still remains firm. History is being created in the neighbourhood of Pakistan and Iran, and now that the menacing albatross of economic sanctions has been removed, the two countries must move swiftly to ensure that it favours the future of not only both the countries but the larger regions connected to them.