Investing in Iran

2.2. Social Indicators

Population -The years following the 1979 revolution saw a raprd increase in the population of Iran. The latest official figures for the Iranian year that ended in March 2001 show that the annual growth has now been stabilized at about 1.1 %. The present population size, provided by the Iran's Statistic Centre, is about 65.5 million. (It is worth mentioning that the same statistic estimated by the United Nation Information Centre surpasses 70 million; though, when contacted, the UN said that they are currently studying the discrepancy.)

Demography -What appears very important in Iran's population figures is the fact that 51 % of the country's population is under 20 years old. This demographic structure exerts pressure on the Iranian government to reform the Iranian economy in such a way as to meet the needs of the expanding workforce. Even though over the past few years the population growth has slowed, due to the demographic structures, the rate is still high and according to some estimates Iran will have close to 100 million people by the year 2050.

The diagram below shows the demographic age distribution of the population based on 1996 figures, the last year that a national census was taken.

Graph: Demographic Age-Distribution of Iran's Population (in million)

Urbanization -Another interesting development is the urbanization of the country. Traditionally a rural society, Iran has developed into a modern urban society over the past 30 years. In 1956, 69% of the population lived in rural areas; today, 63% are urban dwellers and more than 50% of the urban population has already grown up in an urban environment. With urbanization, Iran is developing the need for modern systems and products, among other things.

Table: Projected Demographic Profile

DEMOGRAPHIC PROFILE	**YEAR**		
	2000	**2005**	**2010**
Population(mln)	64	72	81
Males(mln)	33	36	41
Females(mln)	31	36	40
Age profiles(% of population)	**2000**	**2005**	**2010**
0-14 years (mln)	43	40	37
	YEAR		
15-64 years (mln)	52	56	58
65+years(mln)	4	4	3
Median age (years)	18	19	20
Young-age dependency ratio	0.8	0.7	0.6

Old-age dependency ratio	0.1	0.1	0.1
Working-age population(mln)	34	40	48
Labour force(mln)	19	24	30

Source: Plan & Budget Organization

Ethnics -Iran's unique location at the crossroads of Arabia, Turkey and Central Asia has resulted in many ethnic groups being found within its borders. Just over half of the population is of Persian origin, while a quarter is Turkish-speaking Azeris of Azerbaijan. A large group of Kurds, and smaller minorities of Lors, Bakhtyaris, Arabs, Armenians, Turkmen and Baluchis also exist in certain regions. There are four main religions in Iran: Islam, Christianity, Judaism and Zoroastrianism.

2.3**. Macroeconomic Indicators**

GDP -Following a sharp decline in output immediately after the revolution and a significant increase in oil prices in 1979, the economy enjoyed moderate growth up to 1985. However, following the 1988 ceasefire, substantial rehabilitation and reconstruction projects, expansionist monetary policies and an overvalued exchange rate, coupled with rationing and pricing controls, led to economic distortions. Growth resumed in the early 1990s partially fuelled by short-term external borrowing. The resultant need to repay debt restricted imports of crucial production inputs and contributed to weaker GDP growth in the mid-1990s. GDP growth was further impacted by weak oil prices in 1997-1998 and, in 1999, by reduced oil exports to comply with OPEC quotas and the impact of drought on agricultural production before increased exports and a stable oil price stimulated GDP growth in 2000.

Iran's GDP for 2001 was about $107 billion, up 4.8% compared to the previous year. The country's GDP per capita for 2001 was $1,631. The following table sets out *the growth rate in real terms* of *Iran's GDP for the periods indicated.*

Table: **GDP** Growth (1997-2001)

	1997	**1998**	**1999**	**2000**	**2001**
At current prices (Rial billions)	280,908	324.358	428,298	567,591	662,514
At current prices (U SD $ billions)	101,0	101.2	102.7	99.0	106.9
Real GDP Growth (%)	3.4	3.9	1.6	5.7	4.8
Per capita:					
At current prices (Rial	4.545	5,050	6,670	8,967	10,115

thousands)					
At current prices (US$)	1,635	1,575	1,599	1,565	1,631

Source: ***Central Bank***

1 Using IMF weighted average rates of IRR 2,780 = USD $1.00 in 1997, IRR 3,206 = USD$1.00 in 1988, IRR 4, 172=USD$1.00 in 1999, IRR 5,731=USD$1.00 in 2000 and IRR 6,200=USD$1.00 IN 2001.

The following table sets out GDP in current prices and real GDP growth (using the expenditure approach) and in percentage terms for the period indicated:

Table: **GDP** Breakdown 1

Billion Rials	**1997**	**1998**	**1999**	**2000**	**2001**
Private Consumption	139,969 (49.8%)	180,327 (55.5%)	219,030 (51.1%)	259,975 (45.8%)	302,264 (45.5%)
Public Consumption	40,516 (14.4%)	50,166 (15.4%)	61,385 (14.3%)	79,802 (14.0%)	97,219 (14.6%)
(Gross Fixed Capital Formation	82,035 (29.2%)	98,711 (30.4%)	131,417 (30.7%)	172,089 (30.3%)	197,834 (29.8%)
Change in Stocks	12,212 (4.3%)	2,012 (0.6%)	12,991 (3.0%)	21,764 (3.8%)	56.549 (8.5%)
Domestic Demand	274,731 (97.7%)	331,216 (102.0%)	398,841 (93.0%)	533,630 (93.9%)	653,866 (98.4%)
Net Exports of Goods & Services	6,343 (2.3%)	6,420 (2.0%)	29,898 (7.0%)	34,567 (6.1%)	10,913 (1.6%)
Private Consumption	2.7%	6.8%	1.1%	4.8%	4.4%

Public Consumption	3.2%	5.6%	1.8%	1.9%	1.3%
Gross I Fixed Capital Formation	0.2%	3.9%	7.8%	8.3%	9.9%

Source: Central Bank

GDP Distribution -The structure of Iran's GDP continues to be determined by its reliance on oil. As the recipient of crude oil revenues, the State remains the dominant economic actor. The oil sector's share of GDP has declined from between 30-40% in the 1970s to between its more recent levels of 10 & 20%, principally as a result of policy decisions taken at the time of the revolution to reduce production and exports and diversify the production base of the country as well as a lack of investment in the oil sector. However, oil revenue still provides approximately 80% of export earnings and nearly half of government revenue. As a result, this sector is the prime recipient of foreign

2 Assuming a population of 60-mn in 1995 growing at a constant 1.5% per annum (the growth rate of 1995).

and domestic investment. Iran currently produces oil to the limit of its OPEC quotas.

The graph below represents the breakdown of key sectors in the Iranian economy for 2001 and shows that Iran has today a well-diversified economy.

Graph: **GDP** Breakdown 2

Source: Statistical Centre of Iran

The table below presents the breakdown of service sector branches in the Iranian economy for 2001.

Table: GDP Breakdown 3

Service Sector	**Share (°/0)**
Trade, restaurants & hotels	14.3%
Real estate & professional services	13.9%
Public services	11.4%
Transport, storage & communication	9.0%
Financial & money institutions	2.2%
Social, personal & household services	2.5%

Source: Statistical Centre of Iran

The following table shows Iran's GDP by economic sector in current prices and by percentage contribution for the periods indicated:

Table: GDP Breakdown 4

Billion Rials	**1997**	**1998**	**1999**	**2000**	**2001**
Agriculture	40,341 (14.4%)	56,364 (17.4%)	64,140 (15%)	77,159 (13.6%)	89,125 (13.5%)
Oil	40,725 (14.5%)	27,952 (8.6%)	62,839 (14.7%)	101,055 (17.8%)	100,262 (15.1%)
Manufacturing & Mining	55,900 (19.9%)	61,880 (19.1)	81.816 (19.1%)	107.615 (19.0%)	133.456 (20.1%)
Mining	1.522 (0.5%)	1.914 (0.6%)	2.398 (0.5%)	2.943 (0.5%)	3.667 (0.5%)
Manufacturing	38.951 (13.9%)	43.960 (13.5%)	57.924 (13.5%)	75.758 (13.3%)	94.773 (14.3%)
Electricity, gas & water	2.892 (1.0%)	3.401 (1.0%)	419. (1.0%)	7.219 (1.3%)	8.592 (1.3%)
Construction	12.625 (4.5%)	12.606 (3.9%)	17.301 (4.0%)	21.695 (3.8%)	26.424 (4.0%)
Services	147.239 (52.4%)	182.211 (56.2%)	226.083 (52.8%)	291.301 (51.3%)	352.901 (53.3%)
Trade, Restaurants & Hotels	45.888 (100%)	53.640 (100%)	67.036 (100%)	82.690 (100%)	94.787 (100%)
Transport,	23.607	26.088	30.619	47.385	14.502

Storage & Communications	(8.4%)	(8.0%)	(7.1%)	(8.3%)	(2.2%)
Financial Monetary Services	3.140 (1.1%)	4.694 (1.4%)	7.006 (100%)	10.456 (100%)	14.502 (100%)
Real Estate & Professional Services	35.088 (12.7%)	50.204 (15.5%)	62.499 (14.6%)	74.756 (1.8%)	14.502 (2.2%)
Public services	32.088 (11.4%)	39.317 (12.1%)	47.718(11.1%)	61.740 (10.9%)	75.480(11.4%)
Social, personal and household services	6.814 (2.4%)	8.296 (2.5%)	11.204 (206%)	14.005 (2.5%)	16.287 (2.5%)
Bank Service charge	3.386 (1.2%)	4.049 (1.2%)	6.580 (1.5%)	9.539 (1.7%)	13.231 (2.0%)
Total	280.908 (100%)	324.358 (100%)	428.298 (100%)	567.591 (100%)	662.514 (100%)

Source: ***Central Bank***

In 1997, real GDP rose by 3.4% reflecting a moderate increase in the non-oil sector and a substantial decline in the oil sector as a result of the decline in world oil prices. In 1998, real GDP grew by 3.9% principally as a result of growth in the agriculture and services sectors with oil recording only a small increase and manufacturing and mining recording nearly zero growth. In 1999, growth in real GDP was 1.6%. The manufacturing and mining sector grew by 10.6% as a result of increased construction activity and the services sector grew by 3.8% as a result of an increase in transportation, warehousing and communication.

The oil sector recorded a decline in growth of 6% and agriculture a decline of 9.4% as a result of a drought in that year in the east and southeast parts of the country. In 2000, real GDP grew by 5.7% with the oil sector growing by 4.8% as production increased in line with OPEC quotas and prices strengthened. Manufacturing and construction and services also recorded significant growth. In 2001, real GDP grew by 5.7% with manufacturing and construction growing by 10.0% and 12.3% respectively. Agriculture and services each grew by approximately 5%, whilst oil declined by 8.4% reflecting reduced production in line with agreed OPEC quota reductions designed to achieve price stability.

The non-oil industrial sector has suffered from uncertainties in the privatization process as well as from a suppression of imports through much of the 1990s as Iran sought to conserve foreign exchange to meet its debt repayment obligations.

In 2001, the four most significant contributors to GDP growth were construction, manufacturing, trade and transportation, which together accounted for 4.1 % of GDP growth.

The following table sets forth the growth in real GDP (at constant 1990 prices) for the periods indicated:

Table: **GDP** Breakdown 5

Real GDP Growth	**1997**	**1998**	**1999**	**2000**	**2001**
Oil	5.3	2.2	6.0	8.4	8.4
Non-Oil	4.7	4.0	2.3	5.5	6.0
Agriculture	3.5	6.2	9.4	2.8	4.7
Manufacturing & Mining	5.4	0.1	10.6	7.4	10.4
Services	5.1	4.5	3.8	5.6	4.8
GDP	3.4	3.9	1.6	5.7	4.8

Source: Central Bank

Growth rates in the oil sector have been significantly impacted by changes in the price of oil and the level of production as Iran conforms to revised OPEC quotas from time to time. In the non-oil sector State investment in agriculture and wider production export-based items produced significant growth in this sector over much of the 1990s although successive years of drought in 1999 through to 2001 caused a contraction in real terms in 1999 and restricted growth in subsequent years. The manufacturing and mining sector has grown strongly in recent years led principally by increased construction activity and increased imports of raw material. The services sector has also seen consistent growth in recent years but has been affected by currency exchange restrictions, excessive bureaucracy and uncertain long-term planning.

Inflation -Inflation in Iran, measured by the consumer price index in urban areas, has been in double Figures since 1991 and peaked at approximately 50% in 1995. In recent years monetary expansion due to financing the budget deficit, the depreciation of the market exchange rate, the removal of some subsidies and the suppression of imports have all contributed to rising prices. In 1997, average annual inflation was 17.4%. This increased slightly to 18.1 % and 20.1 % in 1998 and 1999 respectively before falling sharply to 12.6% in 2000 reflecting improved economic conditions and enhanced public confidence in the stability of economy as well as the implementation of non- expansionary monetary and fiscal policies. In 2001, the downward trend in inflation continued and at the end of the year it stood at 11.4%.

Exchange rate reform in March 2002 is not expected to have an inflationary impact. This is because government financing has been made available which is designed to replace implicit subsidies with explicit ones so as to ensure that there are no price increases. In addition, there should be no significant monetary expansion as a result of the government's decision to finance the increased cost of settling existing debt obligations. At the time of exchange rate unification, tariff reductions were also implemented which offset the increased cost of imports caused by unification.

It is possible; however, that budget deficit financing could increase inflation if the ambitious revenue targets set in the 2002 budget are not met.

Wages -There are only limited statistics available on wages. The table below sets out the index of wages, salaries and fringe benefits for construction workers in the private sector produced by the Central Bank.

There is a statutory minimum wage set by the High Council on Labour every year. In real terms, the statutory minimum wage has increased from Rls. 242,919 per month in 1996 to Rls. 320,405 per month in 2001. The statutory minimum wage for 2002 is Rls. 700,000 8

Table: Wages (1998-2002)

	1998	**1999**	**2000**	**2001**	**2002**
Index (1997=100)	104.1	118.1	133.4	146.6	163.3

Source: Central Bank

Unemployment -The unemployment rate for 2001 was 15.7%. The unemployment rate is relatively higher among females and, in recent years, in urban areas as opposed to rural areas. It is very likely that the official unemployment figures understate its true position as a result of the methodology used in the surveys.

Based on the most recent census, the total population aged 10 years and over in Iran numbered approximately 45 million, of which the economically active part was approximately 16 million (estimated by December 2001 to have increased to 18.6 million). The remaining 29-mn million were classified as students, homemakers (all men or women not being economically active or students) or income recipients (those not being economically active, students or home-makers but who received a pension or other income).

Employment among the economically active population (those aged 10 years or over who are either employed or unemployed but actively seeking work) was 86.9% in 1997. This increased to 87.5% in 1998 before falling in 1999 and 2000 to 86.5% and 85.8%, respectively. The rate of employment is marginally higher among males and, in recent years, in rural areas as opposed to urban centres. It is likely that the official figures overstate the true employment position as a result of the methodology used in the surveys.

Approximately one-half of Iran's population at the time of the last census was under 20 years of age, a fact that is expected to result in increased pressure on employment rates in the future. The government has sought to address this by financing job creation projects and implementing measures to raise production and investment. The 2001 budget law allocated U.S. $1 billion from the Oil Stabilization Fund to the private and co-operative sector in this respect as well as a further US$ I billion specifically for job creation projects.
Notwithstanding these initiatives, the existing labour law makes it extremely difficult to terminate established employment contracts and the combined tax and social security costs of employment are equivalent to approximately two- thirds of each employee's wage.

Foreign Debt -In 2001, Iran's foreign debt was about $8 billion, constituting only a mere 7% of the GDP, confirming a healthy economy.

Foreign Reserve -Iran's foreign reserves principally comprise its foreign exchange balances, which have grown significantly in recent years following the establishment of the Oil Stabilization Fund3, The country's net foreign reserves are about $12.6 billion. The reserves have grown in recent years reflecting improved oil earnings and reduced external debt repayment obligations, as rescheduled external debt has been paid.

Exchange Rate -Iran's exchange rate system used to be based on multi- layered system, where state and para-state enterprises would benefit from the preferred rate and hence creating an unhealthy competition environment. However, as of March 2002, the multi-tiered system has been replaced by a unified single market driven exchange rate. The official rate on 4 March 2003 was 7,970 Rials for US$1. The following chart demonstrates the US dollar fluctuations from September 2001 to September 2002. The Central Bank of Iran plans with the assistance of the **IMF** to make the Rial fully convertible in the course of 2003.

Graph: Exchange Rate from 1 Mar 2002 -1 Mar 2003

Source: Iran Financial Times

Liquidity -In general, the Iranian monetary policy has been aimed at curbing the liquidity and hence controlling the inflation. Despite a target liquidity growth of 16.4% in 2001, a range of factors, including the need to accommodate higher than expected economic growth and to finance the Rial resources of the budget, the liquidity grew by 28.8% over the mentioned year. The target liquidity growth for 2002 is 15.7%.
The following table displays the liquidity and money supply (in billion Rials) for 2000 and 2001.

Table: Liquidity

Description	**2000**	**2001**
Money (M1)	114,420	142,957
Notes and coins with the public	25.158	29.188
SIGHT deposits	89.262	133.768
Quasi money	134.690	178.000
Interest free loans savings deposit	22.014	29.848
Term invest deposits	103.346	141.066
Short-term	50.443	66.983
Long-term	52.921	74.083
Miscellaneous deposits	9.312	7.087
Liquidity (M2)	**249,111**	**320,957**

3 Money put aside, from the sales of higher that projected oil prices, to offset future oil price fluctuations.

Price Indices -Various price indices and their breakdowns for 2000 and 2001 (percentage change over previous period) are presented in the table below.

Table: Price Index Break Down

Description	**2000(%)**	**2001(%)**
Cescription Price Index	**12.6**	**11.4**
Goods	9.0	5.8
Services	17.1	20.4
Housing, Fuel& Lighting	18.4	18.8
Wholesale price Index	**14.7**	**5.1**
Domestically Produced Goods	14.8	6.8
Imported Goods	13.3	0.8
Exported Goods	19.7	-0.5
Producer Price Index	**16.3**	**10.9**
AgricultureForestry,Husbandry& Fishing	17.9	8.3
Industry	15.6	5.2
Mining	17.1	-4.4
Water, Electricity& Gas	14.3	10.9
Services	16.0	23.1

Subsidies -While the government has been relatively successful in controlling prices, subsidies remain high with approximately $5.5 billion allocated to basic commodities and $10 billion to energy in 2002.

Government Budget -The budgets (in billion Rials) for 2000 and 2001 and planned budget for 2002 are presented in the table below.

Table: Governmental Budget

Description	**2000 Actual**	**2001 Actual**	**2002 Planned**
Revenues	121,122	148,196	218,216
Oil and Gas	59,449	74,957	100,060
Tax	33,298	38,797	62,416
Non-tax	11,895	11,726	22,752
Earmarked Revenue	16,481	22,717	32,988
Expenditure and net lending	123.846	148.983	243.424
Current Expenditure	93.968	102.314	155.635
Development Expenditure	23.560	24.088	54.987
Net Lending	(163)	(136)	(186)
Earmarked expenditure	16.481	22.717	32.988
Deficit	(2.724)	(787)	(25.209)
Financing	2.724	787	25.209
Foreign	77	120	413
Domestic	2648	677	24.796

In an effort to have a more transparent monetary policy, the Central Bank of Iran in 2002, for the first time, has outlined the budget complying with many of IMF's rules and standards. Up to the 2002 budget, domestic borrowing from the banking system, the issue of participation papers and oil pre-financing largely financed deficits. The two most significant sources of financing for 2002 deficit, however, are the Oil Stabilization Fund and privatization proceeds.

2.4. Credit Rating

On 10 May 2002 Fitch Ratings (UK) Ltd., the international rating agency, has assigned the Islamic Republic of Iran Long-term foreign currency and local currency ratings of 'B+' and a Short-term rating of 'B'. These ratings apply to senior unsecured debt issues of the Islamic Republic of Iran. The Outlook on the Long-term ratings is Stable. Related Press Release reads as follows:

'Iran is among the world's largest oil producers, and the economy has benefited markedly from higher prices over the past two years. In 2001 GDP grew by about 5% and the current account and fiscal surpluses are estimated at 5% and 3% of GDP, respectively. The current account has been in surplus for seven of the past eight years, leading to a continual accumulation of foreign exchange reserves, the establishment of an Oil Stabilization Fund (OSF) in 2000 and a steady reduction in gross external debt -all with positive rating implications.

As a share of GDP (7%) and foreign exchange receipts (CXR, 28%), Iran's external debt compares exceptionally well not only to its rating peers, but in fact to all sovereigns rated by Fitch. Only Taiwan (A+) has a lower debtfCXR ratio, and no sovereign has a lower ratio of debt to GDP. Iran's position as a large net external creditor is also one of its fundamental rating strengths, comparing favourably with other sub-investment rated sovereigns. Finally, in a major step forward in the economic reform process, the multiple exchange rate regime was discontinued in March 2002 in favour of a single rate determined in a new inter-bank market.

Against these rating strengths, Iran faces serious rating weaknesses associated with the structure of the economy. State control extends to most

4 Does not include IRR 19,250 billions which have been earmarked by the government to compensate public sector entities which incurred external debt to fund public sector projects for the difference between the IRR 1,752 exchange rate (preferred rate that existed before 21 March 2002) at the date of contracting and the market rate at repayment in 2002 following exchange rate unification.

major industries, including banking where lending is directed to particular sectors, consistent with objectives outlined in the Five-Year Development Plan. The role of the state is also evident in an extensive subsidy system that costs the government an estimated 20% of GDP annually, although exchange rate unification should reduce subsidies and increase fiscal transparency. The oil sector generates 80% of export receipts and 50% of government revenues, exposing the economy to oil price volatility even with the OSF. Foreign exchange reserves of about USD15bn and an estimated OSF balance of USD9bn provide a sizeable short-term cushion. Diversification efforts have yielded few results and are not likely to succeed in the absence of foreign investment. Finally, mounting demographic pressures presage the need for large-scale employment generation, which does not appear forthcoming.

The sovereign ratings are constrained primarily by the interaction of complex international and domestic political developments. Iran borders some of the world's most potentially volatile countries, and stakes in the region's geo- politics are exceptionally high. Tensions have heightened across the Middle East in recent months, reinforcing Fitch's view that international security issues and their implications for Iran remain unpredictable and prone to change quickly. Moreover, relations with the United States, which continues to impose strict bilateral economic sanctions, have deteriorated with the intensification of the Israeli-Palestinian conflict.

Although US views on Iran are not necessarily shared by other members of the international community, Fitch believes they are a significant element of Iran's international risk profile.

Domestic political risks centre on active debates between reformers and conservatives on the degree of political, social and economic liberalization that should be fostered within the Islamic Republic. Given the turbulent regional environment and the current US stance toward Iran, Fitch believes the reform debates could be affected by international developments, possibly prompting conservative elements to take an even less conciliatory approach, and there is a risk that this could be extended towards external credits. It should be noted, however, that Iran has had ongoing international commercial relationships in which debt payments have not been affected by domestic politics. Fitch does not judge domestic political risks to be a threat to the regime at present, but opines that reforms could be caught up in broader debates.'

Iran's first sovereign Eurobond in the amount of Euro 625 million, issued in July 2002 had at the date of issuance a yield of 8.95% and was heavily oversubscribed. The second Eurobond issued in December 2002 hat a coupon of 7.75%.

With regards to Export Credit Agency (ECA) covered financing, the Club of Berne (coordinating the policies of all ECAs of the DECO region) has recently lowered Iran's country risk from category 5 to 4 (a rating of 7 is assigned to the highest risk countries)

2.5. **Foreign Investment Promotion and Protection Act**

Following months of dispute between the Parliament and Guardian Council, the Expediency Council ratified the final version of a new foreign investment law in Iran coined as the Foreign Investment Promotion and Protection Act ("FIPPA") on 26 May 2002.
Under FIPPA and similar to the previous foreign investment law, commercial risks are not covered but any expropriation or nationalization will be compensated by the government. In some cases, if an act of the government disrupts the business activity, the government will be under obligation to make payments for any loan instalments that are due on behalf of the project company. The law also permits more options for repatriation of profits in hard currency combined with a broader definition of foreign investment. For the first time, project financing schemes such as buy back agreements and BOT projects (only under an operator status) are specifically covered under the foreign investment law.

Conditions of FIPPA -Under FIPPA, any foreign natural or legal person - including Iranian expatriates -importing capital into Iran, enjoy the benefits and privileges of this law as long as:

The investment leads to economic growth, promotes technology, promotes quality of products, increases employment opportunities, increases exports and assists Iran in entering the international markets.

The investment does not jeopardize national security and public interests or harm the environment or disrupt national economy.

The investment does not involve the granting of any special rights resulting in a monopoly.

The value ratio of goods and services produced by aggregate of foreign investments does not exceed 25% in any economic sector and 35% in any economic sub-sector.

FIPPA is applicable based on the nationality of the capital as opposed to the investor. As long as the capital comes from foreign sources, anyone importing it will be eligible for FIPPA protection including Iranians residing in Iran or abroad.

Definition of Foreign Capital -For the purposes of the FIPPA, foreign capital is defined as:
Sums in cash entering the country in the form of exchangeable currency though the Iranian banking system or other means approved by the Central Bank of the Islamic Republic of Iran.

Equipment and machinery.

Tools and spare parts, raw materials, manufacturing parts, additives and auxiliary material.

Patent rights, technical know-how, trade names, trademarks and specialized services.

Transferable dividends of stocks belonging to the Foreign Investor.

Other authorized cases with the approval of the Council of Ministers.

Types of Foreign Investment -FIPPA provides for two types for foreign investment which are protect able. These are:

Foreign Investment in all sectors within the schemes of "civil partnership," "buy back," and "build, operation and transfer (BOT)" where the return of principal and profit arises solely through the activity of the same investment project and does not rely on any guarantee by the government, government companies or banks.

Protections Available -Once an investment is authorized and registered under FIPPA, it enjoys full protection of the law including a sovereign guarantee in case of nationalization or taking. Article 9 of this law provides that:

Foreign Investments shall not be deprived of ownership or nationalized unless for the public good, through a legal due process, in a non-discriminatory manner, and against payment of appropriate compensation based on the real value of the investment immediately before the appropriation.

As indicated above, the compensation must be based on the "real value" of the investment and as such there has been inclusion of objective standards in determining what the compensation should be. This is a major shift from the previous 'LAPFI' requirement of "fair compensation" which left the door open to arbitrary and subjective treatment.

A new protection provided in this law is the so called business disruption compensation by the government if it causes such disruption. In this regards, FIPPA provides:

In the case of investments subject to Clause B of Article 3 of this Law [i.e. civil partnerships, Buybacks and BaTs as described above], should laws or government regulations lead to prohibition or cessation of approved financial agreements, then the government shall procure and pay the resulting damages with the ceiling being the matured and due instalments. Limits of the reimbursable undertakings according to this Law shall be approved by Council of Ministers.

This means if any act of the government disrupts the investment company's activities it will have to make the payments for loan instalments while the disruption continues. It should be noted that this does not include commercial risks or changes in law that affect the profitability of the venture. Neither does this protection seem to apply in cases of direct foreign investment but rather it is applicable to project financing scenarios. An example of this protection would be where the government cuts the gas supply to a privately owned power plant as a result of which the operation ceases. During this time the government is obligated to make the payments for any loan instalments of the power plant.

Finally, **FIPPA** has for the first time permitted -subject to restrictions -for resolution of conflicts other than Iranian courts. Article 19 of the **FIPPA** provides:

Any disputes which may arise between Foreign Investors and the government over the reciprocal undertakings in the framework of investments mentioned in the present Law, and which can not be settled through negotiations, shall be examined by domestic courts of law, unless another mode of settlement of disputes has been agreed upon within a law on bilateral investment agreement with the government of the Foreign Investor.

Based on the above, a foreign investor can seek arbitration only if there is a bilateral investment treaty between Iran and the country of the foreign investor. This is also subject to the Constitutional restriction as provided for in Article 139 where arbitration with the government and instrumentalities can only occur with the permission of the Parliament.

Export of Capital -FIPPA provides legal permission for the foreign investor to export both its dividends and principal investment in hard currency. Article 13 of the FIPPA provides:

The principal and interest of Foreign Capital or any portion of the capital remaining in Iran may be transferred abroad with a three-month notice to the Board upon fulfilment of all outstanding obligations, payment of legal deductions and the approval of the Board and confirmation of the Minister of Economy and Finance.

Therefore, the Foreign Investor will be entitled to transfer in hard currency both the earned dividends of the investment as well as the principal amount imported into Iran.

Based on the above, a foreign investor can seek arbitration only if there is a bilateral investment treaty between Iran and the country of the foreign investor. This is also subject to the Constitutional restriction as provided for in Article 139 where arbitration with the government and instrumentalities can only occur with the permission of the Parliament.

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