

Iran Business Forecast Report Q3 2014

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Abstracts

Core Views

Recent improvements in relations with the West bode well for the country's economy. That said, uncertainty over the outcome of negotiations over Iran's nuclear programme will ensure that risks to the outlook remain elevated.

The economy will return to growth in 2014, as improving relations with the West and better macroeconomic management, coupled with low base effects, will lead to an improved outlook for exports and increased business and consumer confidence.

Despite some improvements, the Iranian rial will remain sensitive to developments in nuclear negotiations over the coming quarters.

Major Forecast Changes

We have revised our real GDP growth forecasts this quarter, and are projecting the economy to expand by 2.9% in real terms in 2015, up from our previous forecast of 3.4% growth. Our view that negotiations on the nuclear programme will be protracted over the next years underpins the downward revision.

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Nuclear Talks: Protracted Negotiations Likely

Following recent progress in talks on Iran's nuclear programme, we reaffirm our core view that talks will continue over the coming year s, with potential for a long-term agreement to be found. However, we cannot preclude a breakdown in talks over the coming quarters, which could unleash a Western military response.

TABLE: Political Overview

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Long-Term Political Outlook

Regime Change Likely By The Next Decade

Although Iran's Islamic regime has proved resilient in the face of tremendous domestic and external pressure, we believe that it cannot continue in its present form indefinitely. Consequently, we expect to see 'regime change' by the next decade, either through gradual reform or a popular uprising.

CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis

BMI Economic Risk Ratings

Economic Activity

Back To Positive Territory In 2014

We forecast real GDP growth of 2.8% and 2.9% in real terms in 2014 and 2015, respectively, from a 2.9% contraction in 2013. The return to growth will result from improving relations with the West, more effective macroeconomic management and low base effects. That said, the expansion of the economy will remain below potential over the coming quarters, with risks tilted mainly to the downside.

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Improving macroeconomic conditions and high base effects will contribute to declining price pressures over the coming quarters. While a decision to cut cash subsidies payments will contribute to lowering price pressures, a recent move to slash energy subsidies will result in higher transportation and fuel prices in H214.

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Although declining inflation and an improved macroeconomic environment will alleviate systemic risks in Iran's banking industry in 2014, the sector will remain in a crisis situation. We forecast deposit growth to increase by 2.0% in real terms in FY2014/15, from a 2.0 %decline in FY2012/13, while loans growth will remain negative. We expect structural reforms to the industry taking effect only over the medium term.

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The inability of Iran to fully exploit its enormous oil & gas wealth will keep real GDP growth rates averaging 4.0% over the next 10 years, below the strong potential of the country's economy. Iran's youthful demographics mean that private consumption and investment will primarily drive this growth.

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