Economic Analysis

U.S. Negotiates Historic Deal with Iran

Amanda Augustine / Nathaniel Karp / Marcial Nava

- **The White House is committed to implementing the deal despite fierce opposition**
- **Iran can increase oil production and exports, resulting in downward pressures on oil prices**
- **However, impact is dependent on Iran's compliance and volatile dynamics in the region**

"Either the issue of Iran obtaining a nuclear weapon is resolved diplomatically through a negotiation or it's resolved through force, through war."
-President Obama

"Instead of making the world less dangerous, this 'deal' will only embolden Iran—the world's largest sponsor of terror—by helping stabilize and legitimize its regime as it spreads even more violence and instability in the region."
-Speaker John Boehner

President Obama held a press conference yesterday to defend the historic nuclear deal, which was struck between Iran and the U.S., the UK, Russia, China, France and Germany, following negotiations and deadline extensions over the last two years. Calling the deal "the most vigorous inspection and verification deal that has ever been negotiated," Obama claimed that the agreement effectively stifles Iran's ability to develop a nuclear weapon. As a result, Iran is required to reduce its stockpile of uranium by 98% and to limit its enrichment of uranium for 15 years. In addition, Iran has also committed to reduce its number of centrifuges for 10 years and to cooperate with inspections and continuous surveillance of its nuclear program by the International Atomic Energy Agency.

The deal now heads to Congress, which has 60 days to review and pass judgment; however, Obama has stated his intention of vetoing any rejection of the agreement. Opponents of the deal include Republicans in Congress as well as several U.S. allies in the Middle East. Israeli Prime Minister Netanyahu condemned the deal as "a stunning political mistake," saying, "I think Iran has two paths to the bomb: One if they keep the deal, the other if they cheat on the deal." On the domestic side, the deal has come under fire from Republicans, with Senate Foreign Relations Committee Chairman, Bob Corker, stating, "I begin from a place of deep skepticism that the deal actually meets the goal of preventing Iran from obtaining a nuclear weapon."

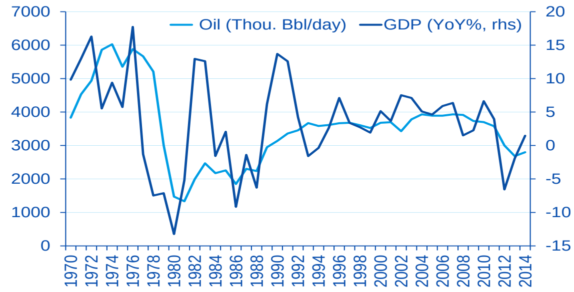
Restrictions on the purchase and sale of weapons could be lifted within five years given that Iran complies with the requirements set forth in the agreement. On the economic front, Iran would be able to rejoin the international financial community by reconnecting to financial messaging networks, such as Swift, opening branches and subsidiaries abroad, issuing bonds, and participating in insurance and reinsurance services, among others. Iran would also be allowed to access previously frozen assets and purchase embargoed items such as aircraft, naval equipment, auto parts, steel and technology. In the energy sector, Iran would also be allowed to sell more oil abroad, but it needs vast amounts of foreign investment to revamp production from existing wells that were shut down after sanctions were imposed and even more funding to develop new infrastructure. The increase in international trade and foreign direct investment will benefit private companies in both the U.S. and EU.

Chart 1
Iran - Selected Indicators & World Ranking

	Value	Ranking
GDP (2014)	$415.3 billion	28th
GDP per Capita (2014)	$16,500	96th
Population Size (2014)	80.8 million	19th
Imports (2007)	20% of GDP	209th
Exports (2007)	29.9% of GDP	141st
Crude Oil Production (2014)	2.8 million BBL/day	7th
Oil Exports (2013)	2.2 million BBL/day	6th
Oil Reserves (2014)	157.3 billion BBL	4th
Natural Gas Reserves (2014)	1,194 cubic Ft	2nd

Source: BBVA Research, World Bank, CIA, EIA, Haver Analytics

Chart 2
Iran Crude Oil Production & GDP



Source: BBVA Research, Haver Analytics

The impact of Iran's re-entry into the energy markets is two-fold. First, upon completion of several proposed pipelines originating from the South Pars gas field, Iran could become a major supplier of natural gas to European markets, reducing their dependency on Russia. The Iranian side of the field is estimated to contain 500 trillion cubic feet of gas in place. Western multinational oil and gas companies have expressed interest in developing the field after unsuccessful attempts from Indian, Chinese, and Russian entities. Second, increased supply from Iran would exert downward pressures on oil prices; however, any impact on prices would happen at a gradual pace. Iran would start by selling off its inventories of 7-35 million barrels and then move on to revamping oil production from existing wells and developing new ones. By the end of 2017, the country's crude oil production is expected to increase by 500-1,000 thousand barrels per day (0.6%-1.2% of world supply). However, these estimates carry a high level of uncertainty, as they are ultimately dependent on the successful implementation of the deal.

Bottom Line

The deal does not completely dismantle Iran's nuclear capability, prevent the country from intruding on neighboring nations, force Iran to end its rogue activities worldwide nor result in its transition to a modern democracy. Moreover, there are no guarantees that Iran won't backtrack on any of its concessions, even with more rigorous inspections in place. According to Obama, "This deal is not built on trust. It's built on verification."

Notwithstanding the political implications, the deal raises uncertainty about the potential negative impact in crude prices considering the current context of oil oversupply. Assuming its successful implementation, the deal opens opportunities for trade and investment. The impact on oil prices will be modest, as other factors like Chinese growth, OPEC market strategies, or technological innovations will play a more important role in determining oil prices in the short- and mid-run.