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# Russian Economic Interests in Iran between Partnership and Sanctions

Asma Hassan Alkhoulī

Specialist researcher in Energy and International Affairs

**H**istorically, Russia-Iran relations have oscillated from cooperation and friendship to rivalry and conflict influenced by the international developments and self-interests of both countries. However, due to the current events in the Middle East, Moscow and Tehran have found accommodation and understanding based on their domestic priorities and external strategies. Iran believes that Russia is a balancing force to Western hegemony in the Middle East and has made significant concessions to Moscow while Russia strives to expand its influence in the Middle East and protect its strategic interests and economic cooperation with the Republic of Iran.

The Russian position toward Iran is determined by several factors such as Iran severing relations with the United States, Russian national security, the Iranian nuclear deal, and Russian economic interests in this country. Indeed, Iran is an important economic partner for Russia. Russian government corporations, supported by President Putin and his administration, signed several agreements and maintained strong economic ties with Tehran (Kozhanov)<sup>1</sup>, which raises many questions about the reasons behind this rapprochement and its dimensions, fields, and reflections on both countries.

This research sheds light on the strategic importance of Iran for Russia. It handles the history of Russia-Iran relations to date, including the 2017 agreements on exchanging oil for food, the Iranian sectors Russia is willing to control, the strong military cooperation and the role both countries play in the Middle East crises, and the future of these relations.

### First: The Iranian Strategic Importance for Russia

Historically, Iran has been considered a vital geopolitical sphere and national interest for Russia. The Russian Caesar, Peter the Great,<sup>2</sup> and all his successors expressed their will to access the warm waters of the Arabian Gulf and the Indian Ocean via Iran. Although the Czarist time is over and the new Russian leaders have taken over the Russian presidency—and hold current beliefs regarding globalization, labor unions, and good neighboring relations—Peter’s principles about Russian interests still exist. These principles lead to constant border disputes with Iran to date but with no real confrontation on the ground because of mutual interests of both countries<sup>3</sup>.

Iran’s regional and international geopolitical importance is essentially twofold:

- 1- It bridges Mid and East Asia with West Asia and the Mediterranean Sea.
- 2- Its strategic position makes it able to blockade Hormuz Strait, a bottleneck on the world’s most important oil sea route.<sup>4</sup>

Specifically, Iran has approximately 2,500 kilometers of coastline along three major water bodies—the Arabian Gulf on the southwest, the Arabian Sea and the Indian Ocean on the south, and the Caspian Sea on the north,—giving Iran a strategic location on international



Source: The Geopolitics of Iran: Holding the Center of a Mountain Fortress, <https://goo.gl/v86XrM>

oil transport routes.<sup>5</sup> Furthermore, Iran has the fourth largest oil reserve in the world after Siberia and the Arabian Gulf. This fact attracted Russia and its oil corporations to expand their investments in the Iranian oil fields to secure the Russian position in the world oil market and extend its influence in this globally significant region.<sup>6</sup>

## **Second: Evolution of Russia-Iran Economic Relations**

Economic relations between the two countries are bound by politics and regional and international developments. Russia-Iran relations were severed after the Iranian revolution in 1979 until 1986 when the two nations resumed cooperation, signed a \$15 billion agreement, and exchanged official visits on all levels.<sup>7</sup> Russia-Iran relations peaked in 1995 when Moscow agreed to build the Iranian Bushehr nuclear plant after the withdrawal of Germany and Ukraine under American and Israeli pressure. It also decided to build three more nuclear plants for approximately \$2 billion by the end of the 1990s.<sup>8</sup> Indeed, Iran believed that Russia was a strategic ally and a source of armament and support to diminish the international pressure on Tehran under the leadership of the United States.

Both countries signed multilateral agreements to supply Tehran with defensive arms and spare parts and to share the contentious Caspian Sea resources between the five countries overlooking this sea. They also rejected the presence of foreign forces in this region and agreed to extend a petroleum pipeline up to the Caspian Sea.<sup>9</sup> In fact, Russia used the Iranian nuclear deal that allowed Tehran to take approximately \$100–140 billion US of its frozen assets out of the country and the huge funds Iran would gain by resuming its oil exports after the lifting of sanctions imposed on Tehran because of its nuclear program.<sup>10</sup>

The oil for goods agreement between Iran and Russia reflects the Russian support of the Iranian torn-out economy. This agreement has been changed more than once since the beginning in 2014. At first, it stated that Russia was to buy 500 thousand barrels of Iran's oil per day for \$1.5 billion of goods per month. Nevertheless, the agreement was put on hold to avoid obstruction of the nuclear talks between Iran and the P5+1 group. In May 2017, Russia decreased the agreed-upon amount from 500 thousand to 100 thousand barrels of Iran's oil per day in exchange for railroad equipment, heavy machinery, and aerial technology for 50% of total price while the remaining amount was to be paid in cash to Tehran.<sup>11</sup>

The Iranian persistence to continue its barter trade with Russia was the result of Tehran's fears of the US's divergent positions on the nuclear deal and the possibility of renegotiating its terms and increasing international sanctions and isolation of Tehran by the Trump administration. Indeed, the US position toward Tehran severed the Iranian economy and prevented it from reintegrating into the world economic system. For example, the United States did not lift sanctions on Iranian economic sectors such as banking transactions, which prevented international banks from doing business with Iranian corporations. However, Russia took a middle ground between the West and Iran and resumed negotiations with Tehran on the 2014 agreements to enhance its economic ties and expand its influence and presence in the Middle East.

## **Third: Indicators of Cooperation and Trade Exchange Rates**

With the beginning of the second millennium, many Russian corporations started

doing business with Iran in fields such as oil, gas, mining, steel, and automotive. This cooperation between the two countries steadily increased until it peaked in 2010–2011 for about \$3.7 billion US with \$3.4 billion US in favor of Russia.<sup>12</sup>

After the imposition of new Western sanctions on Iran in 2012, Iran broke from the Society for Worldwide Interbank Financial Telecommunication (SWIFT) system, leading to several problems for Russian corporations concerning the fiscal adjustment with their Iranian partners. This increased business running costs and decreased the bilateral trade exchange between the two countries to \$1.5 billion in 2015.<sup>13</sup>

During the international sanctions on Tehran, the steel industry absorbed the biggest share of Russia's exports to Iran. To settle the issue of foreign currencies and do the math, Russian steel manufacturers appointed international mediators. After the lifting of international sanctions, Russian corporations resumed their activities in Iran due to the removal of banking obstacles and limitations. Trade exchange between the two countries jumped from \$1.2 billion in 2015 to approximately \$2 billion in 2016, especially in armament, non-oil products, development of Iranian infrastructure<sup>14</sup>, and other industrial projects that amounted to \$40 billion US.<sup>15</sup> Furthermore, Russia and Iran signed customs agreements for the so-called "Green Passage" and exchanged data about the flow of goods between the two countries while the trade exchange jumped to \$155 million per month in 2017.<sup>16</sup> All in all, the International Monetary Fund registered 0.9% growth rate in Russia-Iran non-oil trade exchanges concentrated on wheat, barley, and rolled steel in 2016–2017.<sup>17</sup>

In December 2016, Russia and Iran agreed to use their national currencies in trade exchange, open corresponding accounts for the two credit foundations in the two countries, and discussed opening a joint Islamic bank to facilitate economic cooperation. They also agreed to counter money laundering and all funds received through illegal channels and financing of terrorism.<sup>18</sup> However, the Iranian banking system is wholly based on the "Islamic principles" that bind foreign companies, which might obstruct some of its banking agreements with Russia.

#### **Fourth: Areas of Economic Collaboration between Russia and Iran**

Iran became a significant agricultural source for Russia, especially after European agricultural exports to Moscow were suspended as part of international sanctions due to Russia's annexation of the Crimean peninsula. Moscow strove to invest and open new markets in Asia, especially in Iran—the Russian gateway to expand its influence in the Middle East. Accordingly, Moscow sought to control many of Iran's economic sectors due to Tehran's need for foreign investments, funds, and new markets to promote economic recovery after long-term sanctions that harmed the Iranian infrastructure and economy. The fields of cooperation between Russia and Iran include the following:

##### **1- Nuclear**

After the Iranian revolution in 1979 and the fall of Shah, the United States

renounced developing Iran's nuclear program, which provoked Tehran to turn to Russia to accomplish Iran's nuclear ambitions. In 1995, Russia built the first and only Iranian nuclear plant in the city of Bushehr, which reached its full production capacity in 2012 and handed it over to Iran in April 2016. Moreover, Iran has another plan to commence the second and third plants in Bushehr in 2024 and 2026 respectively and expand the number to six nuclear plants later.<sup>19</sup>

Similarly, the Russian government agreed to supply Iran with an initial amount of nuclear fuel for \$30 million US for the first stage of the Bushehr nuclear plant this year until the Iranian TEFL Corporation for nuclear industries starts producing material by the end of November 2017.<sup>20</sup> This agreement would provide all Iran's nuclear fuel needs and avoid the risk of transporting this crucial substance via Iran's neighboring countries.

## **2- Military**

Russia played a major role in the Iranian nuclear negotiations with the P5+1 group, which ended with signing the nuclear deal in Vienna in July 2015. With the implementation of the terms of the deal and the lifting of the international sanctions on Tehran at the beginning of 2016, Russia agreed to supply Iran with the Russian S300 missiles—Iran's strongest defense system after being prohibited by international sanctions<sup>21</sup> for \$800 million US. Russia handed them over to Tehran in April 2016.<sup>22</sup>

Furthermore, Russia and Iran are intensely involved in the Syrian civil war and fight side-by-side against the Syrian opposition despite the minor conflict of interests between both countries.

## **3- Energy**

In June 2017, Iran's Deputy Minister for Trade and International Affairs, Alamir Hussein Zamani Nia, and the Russian Deputy Minister of Energy, Kirill Molodtsov, signed an agreement of cooperation in the energy sector. Tehran needs a significant investment to increase its exports of oil and gas because it has the third largest oil reserve in the world after Saudi Arabia and Siberia and the second largest reserve of gas after Russia. According to Zamani Nia, Iran could develop fifty oil and gas projects for about \$185 billion US until 2020, which, along with Iran's strategic location, represents a strategic priority for the Russian economic decision maker.<sup>23</sup> Indeed, Iran's lack of experience in this field and European companies' fears about doing business with Tehran paved the way for Russian corporations to expand their businesses and control Iran's energy sector. Russia and Iran have 50% of the world's natural gas reserves, which motivated Moscow to invest in the Iranian oil and gas sectors to take the lead in this field and diminish the US's attempts to reduce the Russian influence in Central Asia.<sup>24</sup>

Several times, Russia has rejected joining the Organization of Petroleum Exporting Countries (OPEC) to avoid abiding by this organization's rules and resolutions. Russia sought to control the Iranian, Iraqi, and Venezuelan oil sectors to use them as forces

of pressure and face the policies of Kingdom of Saudi Arabia that seek balance in the world oil markets.

#### **4- Food supply**

In 2014, Russia resumed exporting wheat to Iran, who became one of the biggest importers of the Russian cereal crops later in 2016. To transport these products to Iran and Turkey, Russia and Azerbaijan agreed to establish the joint Azerustrans Corporation and build a grain terminal with an initial capacity of thirty thousand tons annually on the Azeri-Iranian borders to revive the Russian grain exports.<sup>25</sup>

Due to rising wheat prices and the decline of its exportation, Russia planned to build grain warehouses in Iran to lower the costs and decrease prices of this material by 20–30% as stated by André Locanski, representative of the Russian sales to Iran.<sup>26</sup>

#### **5- Pharmaceutical Industry**

In 2016, Russia and Iran signed a number of new contracts to make human flu vaccines and establish a medication factory for chronic and terminal illnesses in Iran<sup>27</sup> and to produce a vaccine for the hepatitis-B for Iran in Russia.

#### **6- Tourism**

Russia and Iran signed a tourism agreement to streamline procedures of visas between the two countries. With the depreciation of the ruble, the number of Iranian tourists coming to Russia increased. Almost 67 thousand Iranian tourists visited Russia in 2016, with a 72% growth rate in compared to the previous year, and the Russians expect the number to jump to about 100 thousand visitors in 2017.<sup>28</sup> To attract Russian tourists to visit Iran, the Iranian government canceled visas on Russians coming into Iran; however, only about 25 thousand Russian tourists visited Iran in 2015.<sup>29</sup> Indeed, Russia stands to benefit most from these procedures, and Iran is struggling to attract Russian tourists because of the nature of the Iranian regime and other limitations on the Russian tourists.

#### **7- Heavy Industries and Infrastructure Projects**

In 2016, machinery replaced agricultural products as Russia's top exports to Iran, representing 60% of total Russian exports to this country. In the same year, Russia agreed to grant Tehran a loan of \$2.2 billion US to improve the Iranian infrastructure, establish a PowerStation in Bandar Abbas, and accomplish the Rasht-Astara railroad and electrification of Garmzar-Ensh Boron railroad line.<sup>30</sup>

#### **Fifth: Future of Russia-Iran Economic Relations**

The Russia-Iran economic partnership is expected to boost in the next phase. Russian president Vladimir Putin was one of the first presidents to congratulate Rouhani on winning the Iranian presidential election on May 19, 2017, and express willingness to improve the partnership on all levels—infrastructure, industry, energy, and banking. On May 18, 2017, the Iranian authorities stated that Iran and Russia had

taken the first step toward combining credit card systems to streamline tourism, micro-enterprises, and visa requirements between the two countries.<sup>31</sup>

Russia is the greatest beneficiary of economic relations with Iran, but the following are some limitations on this cooperation<sup>32</sup>:

**1-** Lack of clear policies for constant cooperation. Russia and Iran negotiated many economic agreements and protocols; however, most of them are still unimplemented.

**2-** The Iranian regime's nature, economic agenda, and military and security organizations' control of the economic decision-making process in the country. These factors made Iran an unsafe environment for investment and drove the Russian and other countries' corporations to abandon doing business with Tehran.

**3-** International sanctions on Iran and companies cooperating with this country. Although Western countries signed the nuclear deal, they are still wary of Iran's nuclear ambitions and its hostile behavior in the Middle East. Indeed, the economic sanctions are a significant force against Tehran to stop its hostilities against its neighbors.

**4-** Russia-Iran historic relations. Historically, Russia has never been a close friend to Iran. It has been considered an occupying force and threat since the czarist times, which was evident when Russia renounced Iran and prioritized relations with the US and Europe during President Medvedev's era.

**5-** Russia's keenness to balance its relations with all rival powers in the Middle East. As a strategic policy, Moscow tries to found a middle ground in its dealings with other influential powers in the Middle East such as Israel and the Gulf States, which could be the reason behind Russia's limited cooperation in terms of nuclear energy with Tehran.

**6-** The drawback of the Russian economic indicators after the price of oil sunk to decade lows of about 60%. This decline hindered Russia's ability to meet Iran's requirements and needs for billions of US dollars and state-of-the-art technology for economic relief.

**7-** Banking transactions. Because of the problems facing banks in Iran, hindering them from returning to the international financial markets, Russian corporations are still reluctant about doing business with Iran for fears of international sanctions and a lack of a way to do transactions with this country.

The future of Russia-Iran relations is tied to domestic and external developments. As soon as Tehran returns to the world market and recovers its economy after the lifting of all international sanctions, Russian corporations will be ready to enhance economic cooperation and do business with Iran. Additionally, Russia needs to improve its capabilities to meet Iran's needs and battle with American and European companies that have means to access any big developing markets.

However, if the Iranian regime continues its hostile practices to destabilize the Middle East and challenges the international community by violating the terms of the

nuclear deal, it will be exposed to more sanctions and isolation, which will drive all economic partners to cut off ties with Tehran. Furthermore, Iranian internal economic policies are controversial; the Iranian supreme leader calls for economic resistance and self-sufficiency while President Rouhani and his team of reformers call for openness and integration into the global economy. Indeed, the Iranian economy will remain disrupted and does not allow Russia or any other strategic partner to enhance economic ties other than military and strategic cooperation.

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