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Veröffentlichungsversion / Published Version
Zeitschriftenartikel / journal article

the small size of the community and its relative lack of economic leverage (the Georgian and to a certain extent the Armenian case) have prevented these communities themselves, entrepreneurs and the Iranian state from taking full advantage of the linguistic comparative advantage that these communities possess and that could help foster economic ties. Geographic proximity trumps alleged cultural proximity in the case of Iranian Azeris and Armenians.

About the Author

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The Unfreezing of Iran: Economic Opportunities for Georgia

By David Jijelava, Tbilisi

Abstract
In the aftermath of the Iran deal, there has been considerable speculation about the likely impact of the deal on the Caucasus. In Georgia, there has been speculation about the degree to which Iran could drive economic growth through development of the energy sector by providing a new market for Georgian exports or by becoming a source of FDI or tourists. This article looks at each of these areas and concludes that none of them are likely to be major drivers of growth in the short to medium term.

Introduction
Since the collapse of the Soviet Union, Georgia has engaged relatively little with Iran. Instead, it has focused its aspirations on the West and its worries on Russia. In recent years, even modest engagement has been made challenging by the increasingly stringent sanctions put into force by the international community. However, in July of 2015, the Joint Comprehensive Plan of Action (hereafter, 'the Iran Deal') was signed, and nuclear-related sanctions were suspended 6 months later.

This has led to a resurgence of discussions about Iran's potential role in the region. With a population of approximately 80 million and the 18th largest economy in the world (in PPP terms), as well as large oil reserves and the world's second largest proven stocks of natural gas, Iran certainly seems like a potential source of economic opportunity. Iran has been discussed as a means of diversifying Georgia's energy supply, a market for Georgian exports and a source of tourists and foreign investment.[1]

This paper will consider each of these options within the broader geopolitical context. In general, it concludes that while there may be short-term opportunities in tourism, other areas are unlikely to see significant opportunity until the deal has been in place for at least a few years, as the Iranians know that, based on previous experience, if sanctions are re-applied, Georgia will not choose its relationship with Iran over its relationship with the West.

Oil and Gas
Georgia might benefit from Iranian oil and gas resources, from diversifying its own supply of oil and gas, from acting as a transit hub or from serving as a location to produce value-added exports. At the beginning of 2016, Georgian Minister of Energy Kakha Kaladze created a media storm by suggesting that it might be possible for Georgia to diversify its gas supplies and buy some gas from Iran. This built on previous suggestions by Iranian state officials that Iran might develop its gas supplies to Armenia as a transit route to Georgia. Georgia is overwhelmingly dependent on Azerbaijan for its gas supply, with a small percentage coming from Russia. Most of

1 See, for example, Economic and Policy Research Center (April 2016), Georgia and Iran: Opportunities for "Finding Keys to the Door", and Tbilisi and Charles Johnson and Lasha Lentava (Sept 2015), "Un-Muzzling the Persian Panther: Where Georgia Stands to Gain from an Iran without Sanctions." ISET Policy Institute Blog.

the following discussion surrounded whether it was wise to make new deals with Gazprom, but in the process, Iranian gas transited through Armenia was also suggested as a possibility.

Georgia could also benefit as a transit country for Iranian gas heading for Europe. The South Corridor Pipeline is currently being upgraded by BP in a consortium that includes Azerbaijan's SOCAR. The upgraded pipeline, SCPX, is intended to increase the capacity of gas transited across Azerbaijan and Georgia to three times its current level, with the ultimate intent of supplying Europe through the Azeri/Turkish-owned TANAP pipeline. This pipeline was originally planned to transport Azeri gas from the Caspian Sea, but it will have far more capacity for transit than Azerbaijan can supply. Its two most likely sources for supplementing that gas are Iran and Turkmenistan.[2]

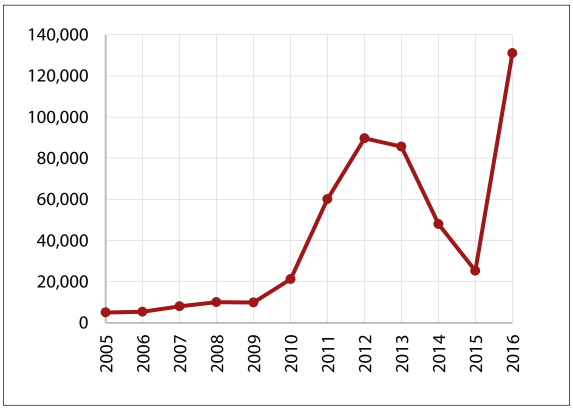
Finally, Georgia could gain from Iranian oil and gas sources if it chooses to pipe oil and/or gas across Georgia (via Azerbaijan or Turkey) for processing on the Black Sea coast, allowing easier access to Europe.

None of these options seem likely in the short to medium-term. In gas terms, Iran is unlikely to supply across Armenia for export to Europe, as the pipeline it would have to use is owned by Gazprom. Iran is also unlikely to export gas to Europe across Georgia using SCPX, as their stated preference is exports to Asia, and even if they did want to connect to TANAP, there is a more direct route that avoids Azerbaijan and Georgia and connects at Erzurum. However, this is by no means certain. There was some subsequent softening of the 'Asia first' policy, but in May 2015, Petroleum Minister Zanganeh's public statements strongly suggested an 'Asia-First' Policy for the Export of Iranian Gas. Similarly, the Erzurum route may be extremely difficult to upgrade.[3] Finally, value-added activity in Georgia (such as LNG or a refinery) may happen in the future, but Iran has currently signalled that they want to first build up their local capacity in both areas.

Export of Goods and Services

After oil and gas, the next focal point for discussion of the opportunities presented by Iran is tourism. Following the removal of the need for visas to travel from Iran to Georgia in November 2010, the number of visitors increased significantly. This dropped off dramatically, once the need for visas was reintroduced in 2013, but it quickly returned when visa-free travel was reintroduced in the aftermath of the Iran Deal in early 2016, as Figure 1 indicates.

Figure 1: Iranian Tourists to Georgia (2005–16)



Source: Georgian National Tourism Administration (reviewed December 2016)

Iranians are attracted to Georgia for a range of reasons. As Stuart Nelson, the General Manager of the Hilton Batumi says, 'Iranians like the fact that there is no visa, it's close, that it is safe, the countryside is green and they can behave more Western'. To keep or expand on this growth, Georgia will have to upgrade its service provisions. As Michael Kerschbaumer, General Manager of Tbilisi Marriott Hotels said, 'Now we need to make sure that the quality of service and infrastructure outside of the hotels is as good as it is inside the hotels'.

The sector will also have to cater to specific cultural needs, particularly culinary and linguistic. This should be possible—Iran has a Consulate in Batumi, which should help, and thanks to a strong tradition of philology, Georgia has a fair number of Farsi speakers.

However, it is important to keep in mind that while this growth is dramatic, it only represents approximately 2% of the visitors to Georgia in a given year. Therefore, it has quite a long way to go before Iranian tourists will really start to be a driver of growth in the sector as a whole.

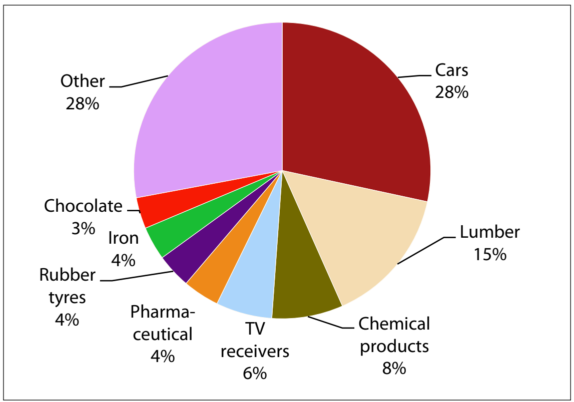
Outside of tourism, current exports to Iran from Georgia are slim across the board. While 2016 was a fairly good year, export to Iran is still only approximately 2% of total exports. Moreover, the categories of goods exported do not reveal much consistency in terms of opportunity or comparative advantage, as Figure 2 overleaf indicates.

Given this variety, instead of looking to current exports to see opportunity, one could look to the economic fundamentals. Georgia has three very obvious advantages that could make it a producer of exports to

2 Micha'el Tanchum (Sept 2015), A Post Sanction Iran and the Eurasian Energy Architecture: Challenges and Opportunities for the Euro-Atlantic Community, Atlantic Council, p. 8.

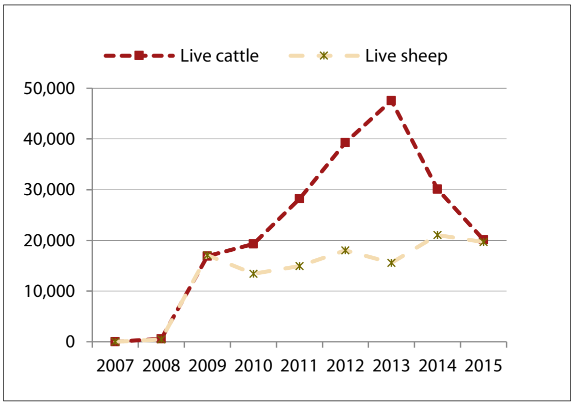
3 Micha'el Tanchum (Sept 2015), A Post Sanction Iran and the Eurasian Energy Architecture: Challenges and Opportunities for the Euro-Atlantic Community, Atlantic Council, p. 8.

Figure 2: Breakdown of Georgia's Exports to Iran 2015



Source: United Nations Conference on Trade and Development (reviewed December 2016)

Figure 3: Live Cattle and Sheep Exports from Georgia (2007–2015), thousand USD



Source: GeoStat (reviewed December 2016)

Iran and a potential recipient of FDI: climate, business environment and geographic location.

These different benefits combine in a range of ways. The most obvious opportunity would seem to be in agriculture. Georgia has approximately five times the rainfall of Iran, so one might think that Iran would be a large importer of agricultural products. However, opportunities for agricultural export to Iran seem rare. While opportunities may exist for agricultural exports to the rest of the Middle East, despite its limited water supply, Iran continues to be a large agricultural exporter, with exports in fruits and vegetables of $2.2 billion in 2015, the country's largest non-oil export. This included export to Georgia of $4 million in wheat, $3.8 million in fruits and nuts and $1.3 million in vegetables.

However, Georgia has benefited from increasing demand for live animals in the Middle East, particularly for sacrifice at the end of Ramadan and the Hajj. This has been driven by increasing demand for and the increasing challenges of transporting live animals internationally for animal welfare reasons. As a result, in 2007 Georgia went from having more or less no recorded live animal exports to over $1 million in 2008 and $34 million in 2009, as Figure 3 shows.

This sudden increase in exports of live animals was great for farmers. Georgia also managed to continue supplying itself with meat by importing cheaper frozen products, thereby mitigating some of the potential negative social consequences of this trade.

However, further increases are limited by the availability of grazing and undeveloped meat production processes. This partially explains why, despite higher prices, exports in sheep have not increased dramatically since 2009. Also, Georgian animals have a number of endemic diseases, and while a 24-day quarantine is used to ensure that diseased animals are not exported, failures in this system have led to sporadic bans on the export of live animals from Georgia to the Middle East. This, therefore, also seems an unlikely driver of economic growth.

Foreign Investment

The final obvious option for Iranian impact on Georgia is FDI. The reported amount of Iran's frozen assets varies from $30 to $100 billion. Whatever the number, these sums are significant, particularly since Iranians have experience dealing with Georgia and might be well placed to help develop products and services, based on regional skill sets, that are targeted at the Middle Eastern population.

However, the numbers so far do not give much reason for optimism. The official FDI has never been more than 2 million USD, and it was only approximately 0.5 million USD in 2015, which is more or less irrelevant in FDI terms. However, these figures provide a distorted picture. According to our discussion with the Georgian National Investment Agency and with one large Iranian investor, it seems as though Iranian FDI is coming from ethnic Iranians who left Iran after 1979 and are now located in other places, particularly Iraq.

These Iranians may offer opportunities for Georgia as business people experienced with working in the region, particularly as the world becomes less nervous about Iranian investment generally. One example that could offer a model for future ethnic Iranian investment in Georgia is the investment in pistachio production currently underway by Aric LLC. Aric is owned by an ethnic Iranian who has ties with the US and the UK.

This investment is built on Georgia's comparative water advantage. Pistachio production is hugely water intensive, consuming as much as 3 litres of water per nut. Its production is dominated by California and Iran, two places that are rapidly running out of water, so global production is currently hitting supply constraints. Therefore, exporting Iranian expertise to produce pistachio nuts in Georgia makes sense. This also plays to existing strengths in the country. Nuts have overtaken wine as Georgia's largest agricultural export category, with $176 million, or 8% of total exports, in 2015.

Beyond that, it is difficult to predict where opportunities may emerge. The holy grail for Georgian FDI and economic development growth is generally considered to lie in Georgia's access to the EU. When Georgia signed the EU Association Agreement two years ago, it was not clear exactly how they would benefit from it. While the agreement opens the EU market for Georgian goods and services, looking around the country, there do not seem to be many areas where Georgia has the productive capacity to take advantage of this opportunity.

However, the hope is that large industrial manufacturers operating outside of the EU might see Georgia as a low-cost, predictable environment with access to the EU's developed market. In the first instance, China is usually discussed in these terms. The true value of the much-discussed Silk Road is not transit, which yields only modest returns to the economy, but it would be if China decided to engage value-adding activities to secure tariff-free imports to the EU. A similar effect occurred in the UK in the 1980s when Japanese car manufacturers set up production facilities in the relatively libertarian UK labour market to gain access to the EU market. Similar shifts happened when new Eastern states entered the EU.

Iran might offer similar opportunities. Although Iran is not an industrial powerhouse on the scale of China, for an oil-rich state, it does have a fairly diversified economy, producing large quantities of gas and oil-based, or energy-intensive, industrial products, including plastics, iron, fertilizers and even automotive products. Any one of these might present an opportunity for value added in the Georgian market.

What, then, are the hurdles to Iranian FDI-led growth? The greatest challenge probably remains the uncertainty of the geopolitical environment. Georgia has shown on numerous occasions that while it appreciates positive engagement with Iran, its Western relationships, particularly its relationship with the United States, take clear and unqualified precedence. Kornely Kakachia has suggested that 'Iranian officials perceive Tbilisi as a "Westoxicated" regime, subservient to the national interests of the United States'.[4]

This has been made clear several times in recent years. In 2008, Georgia–Iran relations were frozen for a year when Georgia agreed to extradite an Iranian citizen to the United States. Similarly, in 2013, after a negative Wall Street Journal article suggested that Iranians were investing in Georgia to avoid sanctions, the Georgian Government cancelled its visa-free regime (allegedly under pressure from the US Government). This created considerable consternation for investors and students who had settled in the country.

This will certainly create concerns for any investment coming from Iran proper. According to Serhan Unal, who wrote a report on Iran for the Turkish Energy Foundation, Iran is still driven by an 'economy of resistance', and as a result, its short-term investment policy will be driven by a desire to use this opportunity to help itself prepare for 'the next crisis'.[5] This makes large-scale investment in Georgia unlikely because, in the event of the 'next crisis' (presumably some kind of re-application of sanctions), Georgia is likely to align itself with the West, the US in particular.

This will affect both actual Iranian investment and the likelihood of ethnic Iranian investment. The ethnic Iranian investor behind the pistachio investment explained that one of the greatest impediments to ethnic Iranian investment in Georgia is anti-Iranian feeling. This probably results from long-standing cultural biases, and it has been reinforced by concerns about the Iran sanctions.

Outlook

The situation has been made even more confusing with the election of Donald Trump as US President, as this has opened the real possibility that the United States may try to rescind the deal, push for a harsh interpretation of it, or impose new non-nuclear sanctions. It is difficult to know what the EU will do in such a situation or what a country like Georgia could do. However, the increased prospect of this policy shift may ensure that Iran remains fairly insular for the time being, focusing its resources on developing internally. This could limit the benefits that Georgia can gain, at least in the short-term.

About the Author

David Jijelava has been with GeoWel Research since 2009 and has been designing and running research projects for large development assistance organizations. David is also working as a social safeguard consultant for the World Bank in Georgia, supervising the implementation of the bank's social safeguard policies in the country. He is currently completing his PhD at the University of Groningen in Social Impact Assessment.

4 Kornely Kakachia (Sept 2011), Iran and Georgia: Genuine Partnership or Marriage of Convenience?, PONARS Eurasia.
5 Serhan Unal (Feb 2016), Post Sanctions Iran and Regional Energy Geopolitics, Turkish Energy Foundation, Ankara.