

# On Shifting Sands: Iranian Strategy in a Changing Middle East

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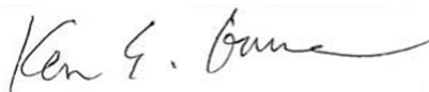
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## Executive summary

The Middle East is central to Iran's strategic goals. The Islamic Republic's tensions with the United States, its simmering conflict with Israel, and its ongoing rivalry with its Arab neighbors (particularly Saudi Arabia), make the region the primary target of Iran's strategic efforts to build influence and establish deterrence against its enemies. Iran has relied on its robust activities in the region to help it make partnerships, create a client base supportive of its strategic goals, gain leverage over its rivals and competitors, and build links between its economy and those of its neighbors. Although Iran has had success over time in advancing its strategic agenda through these actions, the dramatic upheaval of the Arab Spring and the immense pressures facing Iran (such as sanctions) have forced it to adapt to a turbulent strategic environment.

This report examines Iran's Middle East strategy and how this strategy has been impacted by a variety of factors. We argue that a confluence of pressures and changes to the Middle East have proved challenging to Iran's national security and undermined its strategic efforts in the region. Although we look at the historical roots of Iran's strategic perspectives, our temporal and geographic focus is more fixed. Geographically, we look at how Iran's strategy plays out west and south of Iran, primarily in the Persian Gulf (including Iraq and Yemen) and the Levant. Temporally, our concentration is on events of the last few years and especially since the emergence of the Arab Spring in 2011. These parameters enable us to examine the effects of contemporary regional political dynamics on Iran's strategy and behavior in the areas most vital to Iran's interests and deterrence efforts against America and Israel. Though parts of Central, South, and East Asia are also important to aspects of Iranian strategy, they are secondary to Iran's interests in the Middle East, and are beyond the limited scope of this study.

## Overview

Our report addresses these issues along thematic lines. We begin with an assessment of the three primary concerns driving Iran's strategic

agenda in the Middle East: Iran's fear of foreign domination and the United States, its tensions with Israel, and its rivalry with Saudi Arabia. Here we examine how Iran understands its major strategic challenges and provide background for the main considerations shaping Iranian activities and behavior in the region. Second, we consider the broad goals of Iran's strategy and how these are advanced through a variety of mechanisms: Iranian military operations and nuclear program; alliances and partnership building; covert operations; religious and information operations; and regional trade.

We also examine external pressures on Iran and the changing strategic environment of the Middle East. We assess how the disparate pressures on Iran (especially sanctions, but also sabotage and assassinations aimed at weakening its nuclear program, domestic unrest following 2009 elections, and provincial insurgencies, particularly in Baluchistan region) and regional change via the Arab Spring have affected Iran's threat perceptions and strategic landscape.

Finally, we explore how these factors have impacted Iran's behavior and could shape its actions down the road. We first examine how external pressure and regional tensions have provoked changes in Iranian behavior, particularly in two divergent ways: escalated direct-action covert operations and renewed diplomatic efforts with the West. Then we look at how changes to Iran's strategic environment have created both constraints to and opportunities for Iran, and discuss how these dynamics could affect Iran's ability to act and the actions it takes in the future.

## Findings

Drawing from our analysis, we make some observations of how Iran's response to shifting dynamics in the contemporary Middle East might affect Iran's strategic behavior in the near to mid-terms. These are not meant to be predictive or to be prognostications of future Iranian behavior, but rather are presented as possibilities of how Iran might or might not respond to its situation in the months to years ahead.

- **Sanctions have taken a toll, and Iran is probably serious in its effort to seek sanctions relief.** The election of Hassan Rouhani

has given Iran the space and opportunity to change tracks in its engagement with the West. It is quite possible that Rouhani will have suitable backing within the regime to offer some sort of compromise on Iran's enrichment program. But it is not yet clear that Iran is willing to go as far as the West requires. Short of dramatic concessions on its nuclear program, it is difficult to envision circumstances that could lead to the removal of economic sanctions on Iran.

- **Short of a mutually agreed upon political solution to the Syrian conflict, it will be difficult for Iran to regain goodwill from its Arab neighbors.** Economic interaction with GCC states was once an important part of Iran's strategy in the region. But sanctions, outside pressure, sharp political differences over Syria, and rising sectarianism have eroded Iran's ties to the Gulf. Absent areas of legitimate and productive interaction such as trade, the political ramifications of the Syrian conflict and metastasizing sectarianism in the region will continue to impact Iran's relations with its neighbors.
- **Iran will continue to rely on the pillars of its strategic activities to retain deterrent efforts against America and Israel, and will continue to compete with Saudi Arabia for regional influence.** Although Iran might be seeking sanctions relief via warmer political ties and interaction with the West, it remains at odds with Israel, the United States, and its Arab rivals on a number of issues. Thus, even with a constrained budget, Iran is unlikely to drastically change its military investments, posture, or activities in Gulf, particularly those aimed at deterrence. Its religious and information efforts will also likely remain consistent with their present trajectory. Iran might also continue to expand its client base in places such as Yemen and perhaps in the Gulf in order to retain pressure on its neighbors. Yet, increasing sectarianism could make such activities riskier for Iran to pursue, especially in GCC countries. How Iran chooses to navigate that risk will likely depend on how it perceives external threats to its national security—the more immediate or intense Tehran feels outside threats to be, the more likely it will be to adopt more aggressive policies.
- **Iran will continue to rely on its partnerships with Syria and non-state actors such as Hezbollah to advance its interests in the**

**Levant, challenge the influence of its rivals, and threaten Israel.**

Syria is key to Iran's strategic efforts in the Middle East. Iran will not abandon its equities there easily and is likely to expand its role in Syria should the Assad regime survive. Moscow's support for Assad and its joint plan with Washington to secure Assad's chemical weapons arsenal provide cover and a certain degree of legitimacy for Iran's activities in Syria. It is unlikely that Iran will feel enough pressure to draw down its support for Assad as long as such international political cover exists. If the Syrian conflict devolves and begins to cost Iran increasing amounts of blood and treasure, then domestic pressure in Iran could begin to influence Tehran's policies toward Assad. But for the foreseeable future, Iran appears set to stay the course in Syria and is likely committed to supporting Assad even if Western powers (such as the United States) should enter the conflict militarily on the side of the rebels—something that Tehran must surely recognize as a fading possibility.

- **One area that might change is Iran's covert behavior.** The shift toward direct Iranian participation in kinetic activities outside Iran's borders (e.g., assassination attempts on Israeli and Saudi diplomats) was not successful, and continuing such an approach would not help Iran achieve sanctions relief. Therefore, it is possible that Iran might decelerate the type of covert operations that could de-rail diplomatic efforts under Rouhani in the short to mid term.
- **But Iran could return to provocative behavior if its diplomatic efforts fail and pressure increases.** That is, if Iran is unable to strike a deal with the West under Rouhani, sanctions continue, and Iran's interests are slowly rolled back in the Levant through external support for the rebellion, Iran could resurrect a forward-leaning covert operations strategy that includes both violent activity and increased engagement with clients and partners that harm the interests of its enemies and rivals. Such behavior could also reemerge if hawks within Iran's security establishment (especially within the Qods Force and intelligence services) become hostile to and seek to scuttle any potential compromise between Tehran and Washington.

# Introduction

This report examines Iran's strategy in the Middle East and how it has been impacted by a variety of factors. We argue that a confluence of pressures and changes to the Middle East have proved challenging to Iran's national security and undermined its strategic efforts in the region. Iran has done its best at navigating these turbulent seas, but still finds its equities in the region at risk.

The Middle East is central to Iran's overall strategy vis-à-vis its main enemies and rivals. It is where Iran has established the pillars of its deterrence strategy against the United States and Israel and where it continues to vie for influence, often in competition with Saudi Arabia and other rivals. Because the region is part of Iran's immediate neighborhood, it is of course important to the Iranians for a number of reasons; however, this report focuses on how the region fits into Iran's larger strategic imperatives of deterrence, leverage, and influence. It is these issues that drive Iran's activities in places such as the Levant; underpin its attempts at trade relations with the Gulf; and shape its military posture, activities, and investments.

Although we briefly look at the historical roots and development of Iran's regional strategy, our temporal and geographic focus is more confined. Of issue here is how Iran's strategy plays out south and west of Iran, primarily in the Persian Gulf (including Iraq and Yemen) and the Levant. We concentrate on events of the last few years, particularly since the emergence of the Arab Spring in 2011. These parameters enable us to examine the effects of contemporary regional political dynamics on Iran's strategy and behavior in the areas most vital to Iran's interests and deterrence efforts against America and Israel. Though parts of Central, South, and East Asia are also important to aspects of Iranian strategy, they are secondary to Iran's interests in the Middle East, and are beyond the scope of this study.

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# Approach

We adopted a sequential approach, beginning with an analysis of the various factors driving Iran's strategic agenda in the Middle East, including Iran's fear of foreign domination and the United States, its tensions with Israel, and its strategic rivalry with Saudi Arabia. Though this study focuses on the contemporary period, and touches on the historical antecedents of Iran's aims and behavior only in certain parts, we suggest that understanding Iran's history is crucial for making sense of its present threat perceptions and regional policies. In developing our thinking on both Iran's historical experiences and its contemporary behavior, we broadly examined the scholarly literature on Iran and its strategic behavior, statements by Iranian officials in Iranian media, and third-party reporting on Iranian activities in the region. Based on our understanding of these strategic drivers, we then assessed the broad goals of Iran's regional strategy and how these are advanced through a variety of mechanisms: Iranian military operations and nuclear program; alliances and partnership building; covert operations; religious activities and information operations, and economic activity and trade.

After establishing a baseline of Iranian interests and objectives in the region, as well as the tools that Tehran uses in pursuit of those objectives, we then examined how Iran's threat perceptions, regional strategy, and behavior have been impacted by current events. Our analysis focused heavily on the factors that appear to have had the greatest impact on Iranian behavior in recent years: external pressure, including sanctions, sabotage, and assassinations aimed at weakening its nuclear program; and the changing regional landscape that has accompanied the Arab Spring. The unrest and rising sectarianism that has accompanied the latter has created both constraints to and opportunities for Iranian strategic action in the region. We also looked at how certain outgrowths of this changing environment could benefit or at least be exploited by Iran to achieve its strategic ends.

## Sources

As mentioned above, this study draws from a variety of sources and scholarly literature. These sources include:

- Studies on Iranian strategy and decision-making: The scholarship and analysis on Iran's strategy and decision-making has proved useful in both helping define our study and structuring our discussion. This literature was also useful in providing perspectives (both external and internal) on Iran's strategic interests, and highlighting differences between Iranian rhetoric and behavior.
- Iranian and Arab media reporting: These sources, which include everything from standard reporting on political affairs, to interviews with Iranian leadership and other regional power-brokers, were valuable in providing Iranian and other regional perspectives on particular issues.
- Scholarly literature on Iran and regional topics: There is a robust and growing scholarship on the contemporary Middle East. These secondary sources were helpful in contextualizing our study and providing analysis on a number of current topics, particularly the Arab Spring and its immediate effects in the region.
- Western media reporting: Western journalism has been especially helpful in forming an understanding of the tumultuous and shifting political dynamics in the Middle East. It has also been valuable in helping us form an understanding of the less overt actions taken by Iran and other states in the region.
- Economic databases: In order to form an understanding of Iran's trade relations within the region, we relied on data provided by the International Trade Centre (an agency run jointly by the World Trade Organization and the United Nations) and the United Nations Comtrade databases. These data were vital to us in understanding the trajectory of Iran's trade with its neighbors and for indications of how this trade might have been impacted by international sanctions.

- Interviews in the region: Our analysis was aided by interviews and conversations with a variety of officials, elites, analysts, and academics in the region. Some of these interviews were conducted on previous research trips, but some were held on recent visits to Dubai, Abu Dhabi, Muscat, Ankara, and Tel Aviv in April 2013 and to Lebanon in August 2013. Although we reference these interviews only when no other adequate source is available, they nonetheless helped shape our study and influenced some of our arguments and suggestions.
- Expert roundtable: CNA hosted a roundtable discussion in July 2013, which brought together several analysts and academics who study Iran and other issues in the Middle East. While not cited as a source, this discussion aided in our approach to this study and helped us define its parameters.

## Organization

This study proceeds thematically (rather than chronologically) through the following chapters. The first chapter focuses on three primary concerns driving Iran's strategic agenda in the Middle East: Iran's fear of foreign domination and the United States, its tensions with Israel, and its rivalry with Saudi Arabia. These sections discuss how Iran understands its major strategic challenges and provides background for the main considerations shaping Iranian activities and behavior in the region. The next chapter looks at the broad goals of Iran's strategy and how these are advanced through a variety of mechanisms: Iranian military operations and nuclear program; alliances and partnership building; covert operations; religious activities and information operations, and regional trade.

The next two chapters examine external pressures on Iran and the changing strategic environment of the Middle East. Chapter 3 focuses on sanctions and their impact on Iran's economy and trade relations in the region. Chapter 4 discusses how pressures on Iran (via sanctions, sabotage, and assassinations aimed at weakening its nuclear program, domestic unrest following 2009 elections, and provincial insurgencies, particularly in Baluchistan region) and regional change via the Arab Spring have affected Iran's threat perceptions and strategic landscape.

The remaining chapters discuss how these issues have impacted Iran's behavior and could shape its actions down the road. Chapter five examines how these factors have provoked changes in Iranian behavior, particularly in two divergent ways: escalated direct-action covert operations and renewed diplomatic efforts with the West. The final chapter examines how changes to Iran's strategic environment have created both constraints to and opportunities for Iranian strategic action in the region. We look at the broad impact that these changes have had on Iranian strategy and discuss how the ongoing conflicts, sectarianism, and other shifting dynamics in the region could affect Iran's ability to act and the actions it takes in the future. We also look at how certain outgrowths of this changing environment could benefit or at least be exploited by Iran toward strategic ends. The study concludes with some thoughts on how present conditions could be affecting Iran's strategic calculus and what this could mean for Iran's strategic behavior going forward.

## Iran's strategic concerns

Like other states, Iran has deep interests in its geographic region, with the Middle East (essentially the west side of Iran's neighborhood) being of primary importance. (See figure 1.) Although Iran's activities in this region serve a broad purpose for the regime, Iran's interests in the Middle East are inexorably tied to its larger strategic concerns. In order to understand the impact that such factors have on Iranian behavior, it is important to first briefly discuss the form and basis of Tehran's concerns. To that end, this section examines three chief issues driving Iranian strategic policy from Iran's perspective: fear of foreign domination and the United States; the threat posed by Israel; and Iran's rivalry with Saudi Arabia. These factors are the basis of Iranian decision-making in the strategic realm and directly impact Iran's policy and actions in the Middle East. They are not the only considerations influencing Iran's policies, but they are fundamental to its strategic actions in the region. Below we look at how Iran understands this threat environment and briefly discuss the historical roots and contemporary flashpoints of these concerns.

Figure 1. The Greater Middle East



## Fear of foreign domination and the United States

Since 1979, Iran's leaders have viewed the United States as the most serious and enduring threat to the Islamic Republic. It is impossible to appreciate Iran's fear of America and of external influence more broadly without first understanding Iran's historical experience with foreign intervention and domination.

In the 19<sup>th</sup> century, the Qajar Iranian state lost significant northern territory to Russian imperial expansion, and lost parts of western Afghanistan (including Herat) in similar encroachment by the British. In the early parts of the 20<sup>th</sup> century, Iran suffered the indignity of domination by both foreign powers when Russia began to effectively control northern Iran and the British exerted power over Iran's south.<sup>1</sup> The British used this opportunity to secure a 100-year monopoly over Iran's southern oil fields, the profits of which Tehran received but a fraction. The oil issue came to a head when Iran's then democratically elected prime minister, Mohammad Mossadegh, nationalized Iranian oil in 1951 and kicked the British out of the country. Eventually a blockade was put on Iranian oil by the United States and Britain, which sapped Iran of its main source of revenue and ravaged its economy. The resulting domestic political turmoil culminated in an American- and British-engineered coup d'état that removed Mossadegh from office and returned Mohammad Reza Shah to power.<sup>2</sup>

Without a democratic base of support, the Shah became reliant on American backing to secure and maintain his position in Iran. He invested heavily in American military technology, which brought numerous American advisors to Iran, and trusted American guidance for much of his major domestic and foreign policies.<sup>3</sup> As the Shah's regime grew more repressive and anti-democratic, his opponents saw

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<sup>1</sup> See Nikki Keddie, *Modern Iran: Roots and Results of Revolution* (New Haven: Yale University Press, 2003).

<sup>2</sup> On the 1953 coup, see Stephen Kinzer, *All the Shah's Men: An American Coup and the Roots of Middle East Terror* (Hoboken: Wiley & Sons, 2003).

<sup>3</sup> See Abbas Milani, *The Shah* (New York: Palgrave Macmillan, 2011).

Washington as the ultimate source of injustice in Iran. The 1979 revolution was an outgrowth of exploding discontent with American (and other foreign) influence in Iran and with the Shah's oppressive style of rule.<sup>4</sup> Islamists loyal to the Shiite cleric Ayatollah Khomeini gained control of the post-Shah regime, and established an Islamic state that was vehemently anti-America and anti-Israel (which they deemed a Western colonial project in the heartland of Islam).

After the revolution, the Islamic Republic worried that the United States would try to topple the regime and return the Shah and his supporters to power. This fear culminated in the seizure of the U.S. embassy in Tehran and the taking of its staff as hostages—an act which succeeded in breaking U.S. ties with the Islamic Republic. The invasion of Iran by Iraqi forces in 1980, which ignited an eight-year war between the two countries, was seen by Iran's leaders as an American-engineered and foreign-backed campaign to destroy the fledgling Islamic regime. The war cemented the belief that the United States and other foreign powers (such as France and the Arab sheikhdoms in the Gulf, who all backed Saddam in the conflict) would not allow the Islamic Republic to exist and would exploit any opportunity to see it uprooted. It further radicalized an entire generation of Iranian war veterans against America—and this generation still dominates Iran's leadership circles today.

Although the immediacy of the American threat to Iran subsided somewhat through the 1990s, it returned and became a prominent theme in Iranian and American politics after 9/11. The Bush administration's hawkish view of Iran, its hardnosed diplomacy over the Iranian nuclear issue, its willingness to go to war with Iraq and the Taliban in Afghanistan, and its continuous pronouncements about the threat posed by Iran (including the "axis of evil" speech), made war with Iran seem like a growing possibility to both Iranian

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<sup>4</sup>See Nikki Keddie, *Modern Iran*. Also see S. A. Arjomand, *The Turban for the Crown: The Islamic Revolution in Iran* (New York & Oxford: Oxford University Press, 1988); and Ervand Abrahamian, *Iran between Two Revolutions* (Princeton: Princeton University Press, 1982).

leaders and Western publics.<sup>5</sup> Indeed, in 2006 and 2007, numerous articles and books were published in the United States warning of the Bush administration's intentions to attack Iran militarily or topple its regime to stop Tehran's nuclear program.<sup>6</sup>

The election of Barack Obama decreased the immediacy of such action, but Tehran remained concerned about possible U.S. intervention. Despite direct overtures by the Obama administration to Tehran,<sup>7</sup> the popular protests that erupted in Iran after its contested 2009 presidential election were seen by Iranian leaders as an outgrowth of covert American influence aimed at regime change via a manufactured "velvet" revolution. Iranian security officials warned that the United States was working to weaken and topple the Islamic regime through a "soft war," or by spreading Western cultural values and fomenting pro-democratic political dissent.<sup>8</sup> The harsh sanctions imposed on Iran by the Obama administration have been seen as further evidence that Washington wants to cripple the regime if not destroy it altogether.<sup>9</sup>

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<sup>5</sup> Afshon Ostovar, "Guardians of the Islamic Revolution: Ideology, Politics, and the Development of Military Power in Iran (1979-2009)" (PhD diss., University of Michigan, 2009), pp. 158-87.

<sup>6</sup> See *ibid.*, pp. 180-81. Examples include Ali M. Ansari, *Confronting Iran: the Failure of American Foreign Policy and the Next Great Crisis in the Middle East* (New York: Basic Books, 2006); Scott Ritter, *Target Iran: the Truth about the White House's Plans for Regime Change* (New York: Nation Books, 2006); and, David Barsamian, with Noam Chomsky, Ervand Abrahamian, and Nahid Mozaffari, *Targeting Iran* (San Francisco: Open Lights Books, 2007).

<sup>7</sup> See Trita Parsi, *A Single Role of the Dice: Obama's Diplomacy with Iran* (New Haven and London: Yale University Press, 2012).

<sup>8</sup> Afshon Ostovar, "Iran's Basij: Membership in a Militant Islamist Organization." *Middle East Journal* 67, no. 3, summer 2013.

<sup>9</sup> See, for instance, Hesamoddin Borumand, "In Pixelated Color!" *Keyhan* in Persian, 22 October 2012; English translation, "Iran Commentary Accuses Israel, United States, Europe of Plotting Against Iran," OSC, 22 October 2012.

## Israel: the near enemy

Iran views Israel (alongside the United States) as its most immediate hostile adversary. Iran and Israel have not always been at odds, and in fact were relatively close prior to the revolution. The Shah's Iran cooperated with Israel on a number of levels, particularly in the areas of intelligence and defense. However, political resentment against the establishment of Israel and anger over the plight of the Palestinians remained strong in the anti-Shah movement. Ayatollah Khomeini was particularly vocal in criticizing Israel—seeing the Jewish state as the spearhead of American imperialism in the region—and made anti-Zionism a fundamental element of his political ideology. The Islamic revolution brought these sentiments to the center of Iranian state policy, and the Islamic Republic has never wavered in its antipathy for Tel Aviv.<sup>10</sup>

Yet, in the last decade, perceptions of the Israeli *threat* to Iran have rapidly increased. Before Saddam Hussein was toppled in 2003, Iraq was viewed as Iran's foremost foe in the region. The Taliban, who were driven out of power in 2001, were also viewed as chief antagonists on Iran's borders. But after these two regimes were defeated and replaced by regimes friendlier to Tehran (particularly in Iraq), Israel emerged as more than a political problem for Iran's leaders.<sup>11</sup>

The Islamic Republic has always viewed Israel as a regional proxy for the United States, but as tensions have heated up over Iran's nuclear program, so too has a covert war between Iran and Israel. Tel Aviv has been explicit in saying that a nuclear-armed Iran would pose an existential threat to Israel. Israeli leaders, particularly Prime Minister Benjamin Netanyahu, have pressured the United States to prevent

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<sup>10</sup> On Iran-Israel relations, see Trita Parsi, *Treacherous Alliance: The Secret Dealings of Israel, Iran, and the U.S.* (New Haven and London: Yale University Press, 2008).

<sup>11</sup> See Dalia Dassa Kaye, Alireza Nader, and Parisa Roshan, *Israel and Iran: A Dangerous Rivalry* (Santa Monica: RAND, 2011).

Iran from gaining a nuclear weapon<sup>12</sup> and have suggested that if all else fails, Israel would be willing to strike Iran's nuclear facilities itself.<sup>13</sup>

Because of this, Iran holds Israel (along with the United States) to blame for the harsh international sanctions that have sapped its economy. Beyond sanctions, Tehran also believes that Israel has been behind a number of acts of sabotage against its nuclear program (such as the Stuxnet virus), has been involved in the assassination of Iranian scientists, and has supported anti-regime terrorist organizations such as the Mujahedin-e Khalq (MEK) and Jondollah—accusations that Western journalism has more or less confirmed for Tehran.<sup>14</sup> These incidents, and the looming prospect of possible Israeli military action against Iran's nuclear facilities, have made the threat posed by Tel Aviv more acute than it has ever been for Iran.

## Saudi Arabia and regional competition

Outside of the United States and Israel, Iran competes with its neighbors for regional influence. Tehran's main competitor was once Iraq, but since the ouster of Saddam Hussein, Baghdad has been more of an ally than a rival. While Iran has grown closer to Iraq, its relations with its other Persian Gulf neighbors have grown increasingly sour. Iran's unclear nuclear intentions and its continued clash with the United States and Israel have been seen by its neighbors as destabilizing for the region. Further, Iran's involvement in the Lebanon and Yemen, its support for the Shia in Bahrain, its backing of Shia politics in Iraq, and its alliance with Bashar al-Assad in Syria, make its regional agenda run counter to that of Saudi Arabia and other Gulf Cooperation Council states (i.e., Qatar and the United Arab Emirates).

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<sup>12</sup> "PM to push US for 'more credible military option' on Iran," *Times of Israel*, 13 July 2013, <http://www.timesofisrael.com/pm-to-push-us-for-more-credible-military-option-on-iran/>.

<sup>13</sup> "Netanyahu to Iran: We will attack if necessary," *Israel Today*, 15 July 2013, <http://www.israeltoday.co.il/Default.aspx?tabid=178&nid=23981>.

<sup>14</sup> For instance, see Mark Perry, "False Flag," *Foreign Policy*, 13 January 2012.

Khomeini came to power as a sharp critic of Saudi Arabia and other neighboring countries. His anti-monarchical revolution was seen as a threat by Riyadh and the Sunni monarchies of the Gulf, which formed the Gulf Cooperation Council (GCC) in 1981 as a formal alliance in contradistinction to the Islamic Republic. The GCC strongly backed Saddam in the Iran-Iraq war and offered critical financial support that enabled Baghdad to continue the war without losing much ground. Because of this support, Iran's leaders viewed Saudi Arabia and other Gulf states as in league with America in trying to topple the Islamic regime through their Iraqi proxy.<sup>15</sup>

Despite that perception, after the war, Iranian presidents Akbar Hashemi Rafsanjani and Muhammad Khatami both moved to strengthen ties with Riyadh and the Gulf sheikhdoms. Though relations slowly improved, they remained hampered by contradicting regional agendas. Saudi Arabia continued to see Iran as an unwelcome interloper in the Palestinian-Israeli conflict, and remained concerned that Iran's regional aspirations might include radicalizing Gulf Shia communities. The fall of Saddam Hussein saw both Riyadh and Tehran compete for influence in Iraq, with Iran's Shia allies emerging as the more powerful political bloc. With Shiites in power in Iraq, Riyadh became even more anxious about Iranian influence spreading to other Shia communities in the Gulf.<sup>16</sup> For Saudi and other GCC states, the uprising of the Zaidi Shia Huthis in Yemen and the pro-democracy movement among Bahrain's Shia community confirmed this fear.<sup>17</sup> In this context, the Syrian civil war has been viewed by Riyadh and its major GCC partners as another example of Iran trying to assert its Shia-centric will in the region to the detriment of Sunnis.<sup>18</sup>

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<sup>15</sup> See Hooshang Amirahmadi, "Iranian-Saudi Arabia Relations since the Revolution" in *Iran and the Arab World*, eds. Hooshang Amirahmadi and Nader Entessar (New York: St. Martin's Press, 1993), pp. 139-160.

<sup>16</sup> "Saudi's Syria role driven by fear of Shi'ite 'full moon,'" Reuters, 19 June 2013, <http://www.jpost.com/Middle-East/Saudi-role-in-Syria-driven-by-fear-of-Shiite-full-moon-317019>.

<sup>17</sup> Interviews of GCC defense officials with CNA researchers, Dubai, 2011.

<sup>18</sup> "Saudi's Syria role."

Iran sees these regional political dynamics in largely opposite terms. It views Saudi Arabia as a puppet for American interests and the chief instigator of sectarianism in the region.<sup>19</sup> It points to Riyadh's support for Sunni rebels in Syria and its backing of Bahrain's harsh crackdown on the largely-Shia pro-democracy movement in that country as evidence of its sectarian, pro-Sunni agenda.<sup>20</sup> Further, Iran views the U.S. military presence in the Gulf countries as detrimental to its own security and inherently destabilizing for the region.<sup>21</sup> Saudi Arabia and (to a lesser extent) some other GCC states, therefore, are viewed as not only regional competitors but also part and parcel of the overall strategic threat posed by the United States and Israel.

## Drivers of strategy and behavior

Although some external threats (e.g., Saddam Hussein's Iraq and the Taliban prior to 2003) have come and gone, Iran's fear of the United States, hostility towards Israel, and rivalry with Saudi Arabia have endured. These concerns are not the sole drivers of Iran's behavior in the Middle East, but they are inextricably entwined with Iran's strategy in the region. The presence of U.S. forces in parts of the Middle East, especially in the Persian Gulf, is a primary anxiety for Tehran, which considers it a direct threat both to Iran and to regional security.<sup>22</sup> Washington's close ties and security relations with Arab Gulf states implicitly connect those states to the threat posed by

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<sup>19</sup> Such attitudes are regularly reflected in Iranian media. For instance, see "Saudi Arabia supports al-Qaeda to incite sectarian war in the region," Press TV (Tehran), 10 August 2013, <http://www.presstv.com/detail/2013/08/10/318088/ksa-aims-to-incite-sectarian-war-in-me/>.

<sup>20</sup> Jubin Goodarzi, "Syria: the view from Iran," European Council on Foreign Relations, 16 June 2013, [http://ecfr.eu/content/entry/commentary\\_syria\\_the\\_view\\_from\\_iran137](http://ecfr.eu/content/entry/commentary_syria_the_view_from_iran137).

<sup>21</sup> See, for instance, "US vows to keep warships in PG," Press TV (Tehran), 4 January 2012, <http://www.presstv.com/detail/219263.html>.

<sup>22</sup> See for example, "Iran Criticizes U.S. Missile Deployments In Gulf," Radio Free Europe/Radio Liberty, 2 February 2010, [http://www.rferl.org/content/Iran\\_Criticizes\\_US\\_Missile\\_Deployments\\_In\\_Gulf/1946428.html](http://www.rferl.org/content/Iran_Criticizes_US_Missile_Deployments_In_Gulf/1946428.html).

the United States. In the context of mounting international pressure on its nuclear program, including the United States' "all options on the table" rhetoric, Iran's nervousness about the U.S. force presence in the region is not unfounded.

Unwilling to capitulate to what it sees as unreasonable demands by the West—which would theoretically solve the root of Iran's most existential security threats—Iran relies on a variety of strategic actions in the region to keep pressure on its enemies, discourage collaboration between its neighbors and Washington, and deter external attacks. For example, while Iran's cultivation of a loyal client base among Shia militants in Iraq served a number of purposes, it was regularly utilized to keep pressure on U.S. forces in that country. By showing that it could regularly target U.S. forces through proxies in Iraq, Iran was able to establish a credible deterrent against possible U.S. military action against Iran's nuclear program. Iran's ties to Hezbollah and Hamas offer it a similar point of leverage against Tel Aviv. Likewise, Iran's ability—or at least the *perception* of Iran's ability—to influence events outside its borders (such as among neighboring Arab Shia populations) might give it some leverage vis-à-vis neighboring states such as Bahrain and Saudi Arabia. Even though its reputation for interfering in the affairs of its neighbors has been one source of Iran's relative isolation, it is a tradeoff for whatever strategic benefits Tehran feels it gains from having such a reputation (or the actual ability to interfere).

Thus, while Iran aims to grow its influence in the region, this influence, however it is derived, can also serve strategic functions. For instance, Iran relies on a number of mechanisms to make itself an attractive partner or patron to certain constituencies. This includes support for non-state client organizations and encompasses legitimate activities such as cultural promotion and trade relations. But as pressures (e.g., sanctions) and contemporary regional dynamics undermine Iran's ability to build influence through legitimate means (e.g., trade), its reliance on other forms of strategic influence could grow stronger. These issues are discussed at more length in the following chapters.

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## Iranian strategy and strategic activities

In fact, Tehran's foreign policy has its own strategic logic. Formulated not by mad mullahs but by calculating ayatollahs, it is based on Iran's ambitions and Tehran's perception of what threatens them. Tehran's top priority is the survival of the Islamic Republic as it exists now. Tehran views the United States as an existential threat and to counter it has devised a strategy that rests on both deterrence and competition in the Middle East.

— Mohsen Milani, "Tehran's Take," *Foreign Affairs* 88, no. 4 (July 2009)

Iran's key concerns underpin its overall strategic agenda. Of primary concern to Iran is to deter military attacks from the United States and Israel. Second, Iran wants to grow its role and strengthen its position as a regional heavyweight. This includes competing with its main rival, Saudi Arabia, on a variety of levels, and forming strategic alliances with both states and non-state actors to help it secure a dominant regional position. Third, Iran wants to secure its borders and fight against cross-border activities such as sectarian or ethnic-based insurgencies. Finally, Iran has aimed to make its economy more connected to its neighbors, in order both to grow the importance of its regional economic role and to buffer itself from Western pressure.

Iran engages in various activities to advance these goals. Its primary strategic-minded activities can be divided into five main areas: (1) military development and its nuclear program; (2) political partnership-building; (3) covert operations; (4) religious, cultural, and information operations; and (5) trade and economic activity. This chapter focuses on the first four parts of this typology—the fifth, on trade and economic activities, is covered briefly, but will be discussed at more length in the following chapter. It examines how Iran's regional activities in these areas are engineered to advance the

major strategic goals outlined above.<sup>23</sup> Our aim is not to offer a measurement of Iranian regional influence through these tactics, but rather to look at how these activities help Iran strategically respond to its overriding strategic concerns.

## **Military operations and nuclear program**

Since the 1979 revolution, one aspect of Tehran's worldview has remained constant: its belief that the United States and its allies pose an existential threat to the Islamic Republic, whether through soft power, internal subversion, or external armed intervention. In order to minimize the prospect of the latter, Iran has been bolstering its military capabilities and tailoring its strategies to confront the United States, and, to a lesser extent, Israel. The concept of deterrence figures prominently in Iranian military thinking. Tacitly acknowledging that its armed forces cannot compete "toe-to-toe" with the U.S. military in a conventional manner, Iran has instead opted for a asymmetric strategy that plays to Iran's strengths—for instance, the ability to mass forces in confined operating areas, large manpower reserves, shorter mobilization times and lines of communication—and perceived U.S. vulnerabilities (e.g., Washington's aversion to risk and its dependence on regional partners for basing and access).

The primary objective of Iran's military strategy is to deter an attack by the United States. However, in case this strategy fails and the United States does attack, Iran has positioned itself to be able to respond in a number of ways. For example, its military could target forward-deployed U.S. forces in the Gulf, seeking to inflict a psychological defeat that could inhibit Washington's willingness to fight, or constrain Washington's ability to flow additional forces into the theater of operations. Iran could also combine such conventional tactics with forms of irregular warfare. Guerrilla tactics, decentralized operations, mine warfare, and small boat swarming operations all play a prominent role in Iranian strategic thinking and could be deployed against U.S. or other hostile forces.

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<sup>23</sup> Iran's general diplomacy—such as activity within international fora—is also an important arena for Iranian strategy; however, this is a much broader topic and beyond the scope of the present study.

To support its strategy, Iran has been bolstering the capacity of its military to target forward-deployed U.S. forces and to threaten U.S. allies, including Israel and certain Gulf states. Iran's missile and naval forces in particular have benefitted from these efforts. Iran has invested at least \$1 billion in its missile programs since 2000.<sup>24</sup> It now has the largest and most diverse inventory of ballistic missiles in the Middle East. Several of the medium-range ballistic missiles (MRBMs) in its inventory, including the Shahab-3 family of liquid-fueled MRBMs and a solid-fueled, two-stage variant—the Sejil-2—could reach Israel. Iran is also believed to be working on an anti-ship ballistic missile, the Khalij-e Fars (“Persian Gulf”).<sup>25</sup> Although Iran's ballistic missiles are only armed with conventional warheads and are too inaccurate to be used effectively against precise military targets, they could be used against larger industrial or infrastructural targets. Most of them are also road mobile, making it difficult for an adversary such as the United States to track and target them in a contingency.

In the maritime realm, Iran has developed an anti-access, area denial (A2/AD) strategy that leverages the confined geography of the Persian Gulf, coupled with advanced weapons systems and asymmetric tactics, to threaten world energy supplies and constrain the ability of conventional navies to maneuver. In support of this strategy, Iran has integrated multiple sea-, land-, and air-based weapons and platforms to create a layered defense that features an increasingly dense web of overlapping threats the closer one gets to the Iranian coastline. In a conflict, Iran's naval forces could engage in concentrated, massed attacks, featuring swarms of small boats and salvos of anti-ship cruise missiles (ASCMs) to overwhelm and confuse their adversaries. Iran has also acquired a large inventory of mines, which could be used to disrupt civilian shipping and channelize enemy forces into kill zones.

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<sup>24</sup> *Iran's Ballistic Missile Capabilities: A Net Assessment* (London: International Institute for Strategic Studies, 10 May 2010).

<sup>25</sup> According to the National Air and Space Intelligence Center (NASIC), the Sejil MRBM (solid fuel, two stage), and the Shahab-3 MRBM (liquid fuel, single stage) both have a maximum range of 2,000 km. See “Ballistic and Cruise Missile Threat,” NASIC 2013.

Iran's military often uses exercises, weapons tests, aggressive rhetoric, and force posturing as a tool to advertise its capabilities and enhance the credibility of its missile and naval deterrents. For instance, the Noble Prophet series of exercises—a semi-routine joint training event with air, land, and sea components—routinely features ballistic missile tests and naval live-fire events in or near the Strait of Hormuz. Iranian media outlets are incentivized to cover such events and their reporting is inevitably picked up by foreign news services. Iranian officials also regularly suggest that Iran could close the Strait of Hormuz if they wished.<sup>26</sup> Whether they would actually do so, given the potential impact on Iran's economy, is doubtful, except perhaps in dire circumstances. Threatening to do so, however, enhances the credibility of Iran's deterrent while at the same time making Washington's regional allies nervous about the prospect of the United States provoking Iran.<sup>27</sup>

Iran uses its military to support its strategic agenda in other ways as well. For instance, the regime's conception of itself as a regional heavyweight is underscored by the military's ability to project power beyond its borders. Again, Iran's missile and naval forces figure prominently in this regard. The Iranian regular navy has engaged in several high-profile out-of-area deployments in recent years. While these deployments are of questionable tactical or operational significance, they are primarily designed to enhance Iran's standing on the regional stage.<sup>28</sup> By "planting its flag," so to speak, in areas ranging from the Mediterranean Sea to the Western Pacific, Iran signifies that it can compete with its rivals regionally and globally.

Theoretically, Iran could also leverage its nuclear program to support one of the objectives outlined above—deterrence—presuming it

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<sup>26</sup> See for instance, "Iran renews Hormuz threats," Reuters, 15 July 2012, <http://www.reuters.com/article/2012/07/15/us-iran-hormuz-idUSBRE86E0CN20120715>.

<sup>27</sup> Afshon Ostovar, "Iran's Kamikaze Hormuz Threat," *Foreign Policy*, 9 January 2012, [http://www.foreignpolicy.com/articles/2012/01/09/iran\\_s\\_kamikaze\\_hormuz\\_threat](http://www.foreignpolicy.com/articles/2012/01/09/iran_s_kamikaze_hormuz_threat).

<sup>28</sup> Michael Connell, "The Artesh Navy: Iran's Strategic Force," *Middle East Institute Viewpoints* (November 2011).

could achieve at least a breakout capability. Although it is not certain that Iran's leaders have decided to develop nuclear weapons, Iran appears to be taking steps to drastically reduce the time required to obtain such weapons if the decision is made to do so.<sup>29</sup> In 2009, for instance, the IAEA concluded that Iran had amassed enough low enriched uranium to build the bomb.<sup>30</sup> Iran already has a viable means of delivery with its arsenal of ballistic missiles, although the warheads would have to be modified to accommodate a nuclear payload. Regardless of whether Iran uses such a device, a nuclear weapons capability alone would provide Tehran with a considerable deterrent against its adversaries, including Washington.

It is most likely that Iran would prefer never to use its military capabilities against U.S. forces in the Gulf, against Israel, or against anyone else. Iran understands that if it were to engage the United States or U.S. allies in open militarized warfare, it would lose much more than it would gain. But Iran's military investments retain strategic value because they afford Iran a broad set of options and capabilities that could be utilized to respond to any military aggression. In other words, such military capabilities give Iran a credible military component to its overall deterrent strategy vis-à-vis the United States and Israel.

## Strategic alliances

Despite the Islamic Republic's emphasis on independence, Tehran strongly values partnerships with regional and extra-regional states, as well as with non-state actors, to help further its strategic interests. As Volker Perthes argues,

“Iran tends to be remarkably pragmatic in dealing with its direct neighbors, as well as with important international partners... Iranian policy makers and pundits have repeatedly stressed that Iran's national interest demands stability on its borders, good relations with neighboring

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<sup>29</sup> Steven A. Hildreth, *Iran's Ballistic Missile and Space Launch Programs*, Congressional Research Service, 6 December 2012.

<sup>30</sup> Julian Borger, “Iran Has Enriched Enough Uranium to Make Bomb, IAEA Says,” *The Guardian*, 19 February 2009.

states, and in fragmented societies such as Iraq, good relations with all constituent groups....”<sup>31</sup>

Beyond its immediate neighborhood, Iran has relied on its ties to foreign powers Russia and China as bulwarks to Western pressure, and it has sought ties with emerging powers in India and Brazil, and other states such as North Korea, Sudan, and Venezuela, to raise its profile in the international community and grow opportunities for its economic and industrial sectors. Iran has used these ties to help internationalize its ongoing dispute with Western powers over its nuclear program and to mitigate, albeit with decreasing success, the impact of sanctions imposed upon it by the West.

Iran’s regional ties are above all targeted to address its overriding strategic concerns, and, in particular to counter Israeli and American interests, outmaneuver Saudi regional influence, and undermine America’s security arrangements with its regional allies. Iran’s attempt at regional “economic diplomacy” (discussed in the next chapter), for instance, has been one method that Tehran has employed to try to draw its Arab neighbors away from the United States.<sup>32</sup> Beyond this, Iran has maintained close ties with Syria, and with sub-state actors such as Lebanese Hezbollah, assorted Iraqi political factions, and Hamas, as a form of strategic leverage against Iran’s enemies and regional rivals. Kayhan Barzegar terms this Iran’s “alliance policy,” and contends that by “building relationships with friendly states (e.g., Syria) and political movements (e.g., Hezbollah and Shiite Factions in Iraq), Iran [has] tried to deter the U.S. or Israeli military threat in the short term and to prevent the institutionalization of a U.S. role in its backyard in the long term.”<sup>33</sup> To this end, the ties that are most vital to this angle of Tehran’s strategic policy are those to its partners in the Levant (including Hamas) and Iraq.

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<sup>31</sup> Volker Perthes, “Ambition and Fear: Iran’s Foreign Policy and Nuclear Programme,” *Survival* 52, no. 3, June-July 2010: 98.

<sup>32</sup> Nader Habibi, “The Impact of Sanctions on Iran-GCC Economic Relations,” *Middle East Brief*, Crown Center for Middle East Studies, no. 45, November 2010: 2-3.

<sup>33</sup> Kayhan Barzegar, “Iran’s Foreign Policy Strategy after Saddam,” *The Washington Quarterly* 33 no. 1: 173.

## Syria, Hezbollah, and Hamas

Iran's ties to Syria and Hezbollah have been its most strategically valuable and enduring. Iranian revolutionaries formed ties with the Assad regime in Damascus and Shiite activists in Lebanon during their long struggle to topple the Shah. For example, important IRGC commanders such as Yahya Rahim Safavi (who served as the Guards' top officer from 1997 to 2007), spent time training alongside the PLO and Shiite militants in Syria and Lebanon prior to the revolution.<sup>34</sup> Similarly, Iranian clerical activists, such as Ali Akbar Mohtashami, cultivated ties with counterparts in Syria and Lebanon, which were later harnessed after the revolution in the establishment of close ties between the fledgling Islamic Republic, Damascus, and an emerging Lebanese Shia political network that culminated in the establishment of Hezbollah. (Mohtashami, for one, served a vital role in establishing Hezbollah and served as Tehran's ambassador to Damascus from 1981 to 1985.)<sup>35</sup>

The revolution and the subsequent war with Iraq led to Iran's political alienation from both foreign powers and neighboring Arab states. An exception was Syria under Hafez al-Assad, who shared a common enemy with Iran in Saddam Hussein. In spite of their divergent political ideologies, Syria was Iran's most vital ally during the war years. Although Syria and Iran were at times in competition with one another in the Lebanese civil war (especially during periods of tension and fighting between Hezbollah and Amal, which was closer to Damascus at the time), and in the years following the Taif accords, by the late 1990s and early 2000s their political allegiance had grown tight. Because both countries were invested in the Palestinian-Israeli conflict, and had come to see Hezbollah as their primary client in Lebanon, Tehran and Damascus were able to work closely on countering Israeli and later American influence in the

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<sup>34</sup> Yahya Rahim Safavi, *Az jonub-e lobnan ta jonub-e iran: khaterat-e sardar-e Sayyed Rahim Safavi*, Majid Najafpour, ed. (Tehran: Markaz-e Asnad-e Enqelab-e Eslami, 2004): 95-107.

<sup>35</sup> Some of Mohtashami's experiences in Lebanon and Syria are described in his memoir, Sayyed Ali Akbar Mohtashami, *Khaterat-e siyasi-e Sayyed Ali Akbar Mohtashami*, vol. 2 (Tehran: Khaneh-ye Andisheh-ye Javan, 2000).

Levant.<sup>36</sup> Antipathy to and tension with the Bush government galvanized this relationship and helped it coalesce into a more united front against Washington.

Beyond the primary benefit of having a close allegiance with an Arab neighbor, Iran's relationship with Syria has served a strategic purpose in Tehran's support for Hezbollah. Damascus has been the main logistical hub for Iranian assistance to Hezbollah, from arms transfers to planning, intelligence, and information operations.<sup>37</sup> Through Syria, which (given its proximity to, historical ties with, and decades-long military occupation of its western neighbor) has had a robust political and covert network in Lebanon, Iran has been able to build Hezbollah into a formidable regional actor and domestic power in Lebanon. Its relative success in the 2006 war with Israel, and its subsequent emergence as the leading domestic political movement in Lebanon, gave Hezbollah a ballooning reputation as a political-military force. Iran has shared in these spoils, becoming widely perceived as one of the most influential foreign players in the Israeli-Palestinian issue largely due to its patronage of Hezbollah and, to a lesser extent, of Palestinian groups such as Hamas.

Through Hezbollah, Iran has gained a vital stake in the broader Palestinian-Israeli conflict. While its activities in the Levant have increased Tehran's regional and international alienation, and have transformed its nuclear program into an global issue taken up by the United Nation's Security Council and of vital importance to the United States, European Union, Israel, and the GCC, they have nonetheless given Iran a seat at the table for one of the region's most enduring conflicts and an issue of deep concern to Washington. For this reason, Hezbollah has been Tehran's most valuable strategic investment as well as its closest ally. It is a vital piece of Iran's long-term strategic agenda regarding both Israel and the United States, and (along with Iran's ties to other Palestinian groups), is likely considered a bargaining chip by Tehran that could someday be

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<sup>36</sup> For a historical overview of Iran-Syria relations, see Nadia von Malzahn, *The Syria-Iran Axis: Cultural Diplomacy and International Relations in the Middle East* (London and New York: I.B. Tauris, 2013):17-57.

<sup>37</sup> Bill Samii, "A Stable Structure on Shifting Sands: Assessing the Hizbullah-Iran-Syria Relationship," *Middle East Journal* 62, no. 1, winter 2008.

parlayed into concessions from Washington and Tel Aviv in a future grand bargain between the Islamic Republic and its chief foes.

Iran's ties to Hamas have until recently been similarly aided by shared ties to Damascus. Iran's relations with Hamas were never as close as its relations with Hezbollah or Damascus, but since Iran began to court Hamas' leadership in the 1990s the group has been a growing part of its deterrence efforts against Israel.<sup>38</sup> Iran was able to increase its role as patron for Hamas after the latter won elections in 2006 and formed a separate Palestinian government in Gaza.<sup>39</sup> Hamas' victory led to a drastic decline in external financial support for the group and its government activities in Gaza, which gave Iran the opportunity to emerge as one of the Hamas government's main financial backers.<sup>40</sup> Additionally, Iran helped arm with organization through complex smuggling networks.<sup>41</sup> Prior to the Syrian civil war, Iran-Hamas relations had been growing—and, with them, the perception of Iran's ability to impact the situation in Gaza. This enhanced Iran's deterrent strategy against Israel, and gave Iran a foothold in Gaza and the Occupied Territories more broadly.

## Iraq

The toppling of Saddam Hussein radically changed the strategic landscape of the Middle East. For Iran's leaders, Iraq was transformed

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<sup>38</sup> "Middle East: Analyst Discusses Relations between Iran and Hamas," RFE/RL, 27 January 2006, <http://www.rferl.org/content/article/1065130.html>.

<sup>39</sup> Scott Wilson, "Hamas, Fatah Launch Separate Governments," *Washington Post*, 16 June 2007, <http://www.washingtonpost.com/wp-dyn/content/article/2007/06/15/AR2007061500249.html>.

<sup>40</sup> Ibid. Also, "Iran Supports Hamas, but Hamas Is No Iranian 'Puppet,'" Council on Foreign Relations, 8 January 2009, <http://www.cfr.org/israel/iran-supports-hamas-but-hamas-no-iranian-puppet/p18159>.

<sup>41</sup> Evidence for this has emerged from the seizure of Iranian weapons shipments in Africa. See, for instance, Con Coughlin, "Iran arms smuggling details to be disclosed," *The Telegraph* (London), 13 January 2011, <http://www.telegraph.co.uk/news/worldnews/middleeast/iran/8258166/Iran-arms-smuggling-details-to-be-disclosed.html>.

from a hostile enemy, to an opportunity to enlarge Iran's regional footprint and more actively counter U.S. interests. Due to its geographic proximity and its longstanding association with Iraqi opposition parties, Tehran was well placed to take advantage of this situation. Prior to the revolution, many Iranian clerics had spent time studying or teaching in Najaf. Khomeini famously spent part of his exile there, where he was accompanied by some of his chief lieutenants, such as Akbar Hashemi Rafsanjani. After the revolution, the clerical network that had developed in Najaf between Iranian, Iraqi, and Lebanese clergy, became a mechanism through which Tehran was able to aid and support sympathetic Shia political organizations outside Iran.

Saddam's crackdown on the Shia in Iraq, and the subsequent war with Iran, gave Tehran the context in which to strengthen ties with Shia groups in Iraq. Iran aided Iraq's Dawa party and hosted some of its exiled leadership, including Nuri al-Maliki, Iraq's current prime minister, who resided in Iran for a couple of years before moving to Syria. While Dawa activists worked with Iran, the organization had ideological differences with the Khomeinist regime; these differences created a split in the organization. The portion of Dawa leadership willing to adhere to Khomeinist ideology—primarily the concept of *velayat-e faqih*, or clerical political rule—split to create the Supreme Council of Islamic Revolution in Iraq (SCIRI), which recognized Khomeini as their supreme guide (*faqih*).<sup>42</sup> SCIRI's armed wing, the Badr Corps, was established and trained by the IRGC, and operated as an all-Iraqi division of the organization until 2003.

The fall of Saddam enabled Iraq's Shia opposition groups to return to Iraq for the first time since the 1980s. Having been based in Iran for two decades, SCIRI and Badr gave Iran a crucial entry into a new political paradigm in Iraq. These organizations (which eventually split and were renamed the Supreme Islamic Council of Iraq (SICI) and the Badr Organization) became the main conduits for Iranian influence in Iraq and later enabled Tehran to have deep reach into Iraq's government and security forces.

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<sup>42</sup> On the roots of Dawa and SCIRI, see Faleh A. Jabar, *The Shi'ite Movement in Iraq* (London: Saqi, 2003).

Even though it had strong ties with major Shia political constituencies SICI and Badr, Iran broadened its ties with Iraqi groups in order to expand its zone of influence in Iraqi domestic politics. Iran had already established relations with Jalal Talabani's Patriotic Union of Kurdistan (PUK), which gave it strong contacts in the Kurdish north. Through the IRGC's Quds Force and Iranian intelligence, Tehran became the leading patron for certain armed groups such as the Hezbollah Brigades (Kata'ib Hezbollah) and other militant elements within Moqtada al-Sadr's network.<sup>43</sup> Moqtada al-Sadr himself, while vocally critical of Iranian influence in Iraq early in the post-Saddam era, came to be aligned with Tehran, and eventually relocated to Qom under the auspices of completing his clerical training there.<sup>44</sup>

It's unclear to what extent Iran's ties with these various factions enabled Iran to influence state-level decision-making; however, Iran's ability to play spoiler through its Iraqi clients during the U.S. occupation of Iraq is less in doubt (a subject discussed more below). Iran utilized its contacts in Iraq to advance its strategic agenda in that country, which primarily meant harassing U.S. forces via Shia proxies; facilitating the expansion of Iranian trade, business investment, and pilgrimage activities, particularly in the shrine cities of Najaf and Karbala; discouraging the possibility of a long-term status of forces agreement between Baghdad and Washington; and securing Iranian borders. With its complex network of clients, and its strong ties to a wide spectrum of primarily Shiite and Kurdish allies, Iran's investment in Iraq has enabled it to turn a once hostile enemy into a key regional partner. Its success with its Shia partners not only provides Iran with certain benefits in Iraq but also helps Tehran outmaneuver its Arab rivals, particularly Saudi Arabia, for influence in a key regional state.

## Covert operations

To support its interests and objectives in the Middle East, Iran engages in a wide array of covert operations, ranging from violence

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<sup>43</sup> See, Joseph Felter and Brian Fishman, *Iranian Strategy in Iraq: Politics and 'Other Means'* (West Point: Combating Terrorism Center, October 2008).

<sup>44</sup> Ibid.

and political subversion, to arms trafficking and illicit procurement. As discussed, Tehran uses client organizations such as Hamas to gain influence in strategically important issues (e.g., the Palestinian-Israeli conflict), to foster its influence among sympathetic populations, and to expand its equities in the region. Iran also leverages its capacity to engage in unconventional warfare, as well as its ties with groups such as Hezbollah, as a means of power projection and deterrence.<sup>45</sup> As one prominent Lebanese scholar has noted, “The U.S. parks aircraft carriers in the Gulf next to Iran; Iran parks its own aircraft carrier in Lebanon—Hezbollah—which can wreak great destruction on Israel at a moment’s notice.”<sup>46</sup>

The regime’s tendency to support proxies and engage in other covert activities dovetails nicely with its general preference to avoid pitched battles and decisive engagements in favor of “Fabian” strategies that slowly wear down its opponents by attrition.<sup>47</sup> The deniable aspect of covert operations (i.e., those undertaken in secret or by third parties) also suits the regime’s penchant for flexibility, while avoiding the unnecessary risk that more overt, direct means of pressuring its adversaries would entail.

Two organizations are responsible for conducting covert activities outside of Iran: the Ministry of Intelligence and Security (MOIS), and the Qods Force, a branch of the Islamic Revolutionary Guard Corps (IRGC). The latter is the regime’s primary mechanism for leveraging foreign militant groups and proxies abroad, including Hezbollah, Hamas, Palestinian Islamic Jihad (PIJ), and the various Shia militias

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<sup>45</sup> Many of Iran’s surrogates have been innovators in the field of unconventional tactics. Hezbollah, for instance, used suicide bombers to attack U.S. and Israeli targets in the early 1980s, well before the tactic had become the preferred method of other Islamist militant groups. Iranian-affiliated Shiite “special groups” in Iraq perfected the use of explosively formed projectiles (EFPs) and Improvised Rocket Assisted Munitions (IRAMs) against U.S. forces, a tactic that has since been copied by militant groups in Afghanistan and elsewhere.

<sup>46</sup> Hugh Sykes, “Iran’s Lebanese ‘aircraft carrier,’” *BBC World News*, 5 June 2008, <http://news.bbc.co.uk/2/hi/7438553.stm>.

<sup>47</sup> See Michael Eisenstadt, *The Strategic Culture of the Islamic Republic of Iran: Operational and Policy Implications* (Quantico, VA: Marine Corps University Press, August 2011): 12.

in Iraq. Its operatives engage in various activities, including providing training, arms, and logistical support to surrogates; gathering intelligence; procuring illicit parts for Iran's military and nuclear program; conducting covert diplomacy; and enabling information and humanitarian operations in hostile environments. As an elite branch of the IRGC, the Qods Force exerts a significant degree of influence over Iran's foreign and national security policies, particularly in areas where Iran maintains extensive client networks, such as the Levant, Iraq, and Afghanistan. The current leader of the Qods Force, Major General Qassem Soleimani, is rumored to report directly to Iran's supreme leader, bypassing regular IRGC command and control channels.<sup>48</sup>

The missions and functions of MOIS overlap somewhat with the Qods Force, and there is a degree of institutional rivalry between them.<sup>49</sup> MOIS officers operate out of Iranian embassies and cultural centers, as well as non-governmental organizations, including front companies.<sup>50</sup> According to one assessment, MOIS "is heavily involved in foreign intelligence collection and covert action programs, especially in the Middle East. The MOIS is a key player in Iran's global efforts to export its revolution, second only to the Qods Force."<sup>51</sup>

Although Tehran's underlying strategic motivations for engaging in covert activity have remained more or less constant since the end of the war with Iraq, the scope and scale of its operations have fluctuated over time, subject to a range of geopolitical, domestic, and economic factors. For much of the past decade, the Qods Force and MOIS have focused their operations on the Levant, Iraq, and Afghanistan. In the latter two cases, Tehran opportunistically took

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<sup>48</sup> See Dexter Filkin's political biography of Suleimani, "The Shadow Commander," *The New Yorker*, 30 September 2013.

<sup>49</sup> Frederic Wehrey et al., *The Rise of the Pasdaran: Assessing the Domestic Roles of Iran's Islamic Revolutionary Guards Corps* (Santa Monica, CA: RAND Corporation, 2009): xiii.

<sup>50</sup> Scott Modell and David Asher, *Pushback: Countering the Iran Action Network* (Washington, D.C.: Center for a New American Security, September, 2012): 10.

<sup>51</sup> Ibid.

advantage of the U.S. military interventions to expand their client base and establish new client networks while simultaneously putting pressure on U.S. forces.<sup>52</sup> The Arab Spring—hailed as an “Islamic Awakening” by Iran’s leadership—provided an additional opportunity for the Qods Force and MOIS to expand their regional footprint. By and large, however, they have not been able to take advantage of this opportunity, with the notable exception of Yemen, where the Qods Force has been reportedly supporting Houthi rebels against the Yemeni government and its Saudi allies.<sup>53</sup> More recently, MOIS and Qods Force have been concentrating on the conflict in Syria, where they have been fighting a rear-guard action to preserve the Syrian regime.

Recent Iranian covert activity outside the region suggests that Tehran’s propensity for risk might be growing commensurate with the pressure the regime is facing from the international community over its nuclear program. The assassination attempts in February 2012 on Israeli diplomats in India, Thailand, and Azerbaijan were likely orchestrated by the Qods Force in response to the targeting of Iranian nuclear scientists and other pressures. The foiled Qods Force plot to assassinate Adel al-Jubair, the Saudi ambassador to the United States, in November 2011, suggests an even greater willingness to court risk. If the plot had succeeded, it probably would have resulted in significant U.S. casualties and almost certainly invited a major military response. The failed Washington plot came on the heels of multiple Qods Force attacks on Saudi diplomats around the world, including the successful assassination of a Saudi consular official in Karachi in May 2011.<sup>54</sup> These attacks suggest that Iran’s calculus for risk might be changing in the face of escalating outside pressures and regional challenges brought on by the Arab Spring—issues that will be revisited and explored at more length in a later chapter.

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<sup>52</sup> Filkins, “Shadow Commander.”

<sup>53</sup> International Crisis Group, “Yemen: Enduring Conflicts, Threatened Transition,” *Middle East Report*, no. 125, 3 July 2012.

<sup>54</sup> Matthew Levitt, “Hizballah and the Qods Force in Iran’s Shadow War with the West,” Washington Institute for Near East Policy, *Policy Focus* no. 123, January 2013.

## Religious, cultural, and information operations

The Islamic Republic has engaged in a multitude of cultural, educational, and religious initiatives to promote its ideology and project a positive image of itself in the Middle East and beyond. The goal of these initiatives has been to broaden Iran's appeal among select populations outside of its borders, outflank its adversaries in the information realm, and solidify the Islamic Republic as a leader in the region. Although the tone of the regime's rhetoric has softened since the early days of the revolution, its basic themes and underlying content have remained more or less consistent: hostility to the United States, Israel, and "reactionary" Arab regimes; sympathy for popular regional and Islamic causes, especially that of the Palestinians in their struggle with Israel; and disdain for the current regional and international order. Official Iranian discourse is populist and generally pan-Islamist, eschewing the uniquely Shia or Persian aspects of the Islamic Republic and its ideology.

The Iranian government harnesses a variety of tools to support its efforts at public diplomacy. Arguably the most important of these are its foreign-language media outlets, all of which are affiliated with the state-owned Islamic Republic of Iran Broadcasting (IRIB) corporation. In the international sphere, IRIB serves as Iran's media coordination agency, establishing official guidelines for media content and dissemination. It presides over several Arabic-language satellite television stations, including Al-Alam, an Arabic news channel with bureaus in Tehran, Beirut, and Baghdad; Jam-e Jam, a cultural channel; and al-Kawthar, a channel that promotes Shia Islam. IRIB also operates a number of Arabic-language terrestrial and shortwave radio stations. Iran's leadership has attempted to leverage internet tools—mainly individual websites and blogs—to disseminate information to targeted populations in the region, although this effort appears to be far more decentralized than its media outreach activities. Most of Iran's senior leaders have their own websites, and many of these have pages in Arabic.

Cultural activities outside Iran's borders are overseen by the Islamic Culture and Relations Organization (ICRO), a branch of the Ministry of Culture and Islamic Guidance. ICRO is the de-facto cultural

diplomacy arm of Iran's government.<sup>55</sup> It operates cultural and educational centers in most of the region's capitals where Iran maintains embassies. It also hosts book fairs and other cultural events. ICRO is also responsible for interfaith dialogue and proselytization.

The Iranian government has also attempted to propagate its official version of Islam among the region's Shia, both from the "ground up," through educational institutions and religious charities, and from the "top down," through networks of clerics that are affiliated with Iran's supreme leader. For instance, Sayyid Hasan Nasrallah, the secretary general of Lebanese Hezbollah, and Sheikh Mohamed Yazbek, the head of Hezbollah's Sharia Council, are both recognized as official representatives of Ali Khamenei in Lebanon. As such, they use Hezbollah's various media and educational organs to propagate Khamenei's teachings and occasionally denigrate those of rival clerics.<sup>56</sup> Iran also encourages foreign seminarians to study in Qom, at the Hawzeh's International Center for Islamic Studies.

On the whole, Iran's attempts to engage in public diplomacy have only met with limited success.<sup>57</sup> Pan-Islamist aspirations aside, the fact that Iran is a majority Shia Persian state in a largely Sunni Arab region has been a major constraint on Tehran's outreach activities. The growth of sectarianism, largely stemming from the conflicts in Syria, Iraq, and Bahrain, has also rebounded negatively on Iran. Most of the region's population now has a negative view of Iran, outside of Lebanon, Iraq, Kuwait, and Yemen.<sup>58</sup> Iran has achieved some success in establishing inroads with the region's Shia, but even here, the Iranian government has been stymied by the fact that while many

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<sup>55</sup> Pierre Pahlavi, "Understanding Iran's Media Diplomacy," *Israel Journal of Foreign Affairs* VI: 2 (2012): 23.

<sup>56</sup> See Dominique Avon, Anai's-Trissa Khatchadourian, and Jane Marie Todd, *Hezbollah: A History of the "Party of God"* (Cambridge: Harvard University Press, 2012).

<sup>57</sup> Michael Eisenstadt, "The Limits of Iran's Soft Power," *Iran Primer*, United States Institute of Peace, March 2011, <http://iranprimer.usip.org/blog/2011/mar/22/limits-iran%E2%80%99s-soft-power>.

<sup>58</sup> *Looking at Iran: How 20 Arab and Muslim Nations View Iran and Its Policies*, Zogby Research Services, LLC (2012): iii.

Shia are willing to accept Iran as a benefactor for the sake of expediency, they do not necessarily follow the precepts of the Islamic Republic in matters of religion or ideology. Nor is Khamenei widely regarded as a source of emulation by the region's Shia, most of whom look to Najaf, rather than Qom, for inspiration.<sup>59</sup>

## Regional trade

Iran is a large country with immense petroleum and gas resources. Similar to its Arab Gulf neighbors, Iran has largely relied on the revenue derived from these resources to underwrite its strategic activities. However, unlike these neighbors, international sanctions, a much larger population, and other internal factors (such as corruption and structural inefficiencies) have limited Iran's profits and undermined their strategic potential.<sup>60</sup>

Regional trade is one area that Iran has tried to utilize its economic resources for strategic ends.<sup>61</sup> Iran has pursued legitimate bilateral agreements and trade opportunities to increase its economic connectivity with GCC states in an effort to prevent a consensus anti-Iranian (or pro-U.S.) perspective from taking root in the Gulf. Tehran's approach has been in essence a bet that Arab states would be less inclined to support Washington-sponsored initiatives (such as sanctions) against Iran should it become seen as a valuable trade partner. More idealistically, as Nader Habibi argues, Iran's hope has been that strong economic ties with Gulf neighbors would encourage these "countries to abandon their security arrangements with the United States and enter instead into a regional security alliance with Iran."<sup>62</sup>

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<sup>59</sup> See for instance, Mehdi Khalaji, "The Last Marja: Sistani and the End of Traditional Religious Authority in Shiism," *Policy Focus* no. 59, Washington Institute for Near East Policy, 2006.

<sup>60</sup> This topic is discussed at more length in the next chapter.

<sup>61</sup> Nader Habibi, "The Impact of Sanctions on Iran-GCC Economic Relations," *Middle East Brief*, Crown Center for Middle East Studies, no. 45, November 2010: p. 3.

<sup>62</sup> Ibid.

Unfortunately for Iran, pressure by the U.S. has succeeded in discouraging trade with Iran among GCC states (and particularly the United Arab Emirates), which has resulted in a steep decline in Iran's trade relations with the Gulf. (See Appendix 2 for a more detailed discussion of Iran's trade with the GCC and other regional states.) With decreasing economic ties to its neighbors, Iran's regional influence has also been in decline. Although Iran has tried to ameliorate its economic losses in the Gulf by expanding trade with Iraq, India, and other Asian states, its strategic aim of currying favor with GCC states through economic activities has largely failed. No better testament to Iran's declining influence has been the United Arab Emirates' (Iran's foremost trading partner in the region) support for international sanctions on Iran. While this has hurt Iran strategically, it has also had a negative a negative impact on its economy—a topic discussed further in the following chapter.

# The impact of sanctions on Iran's economy

U.S. and international trade, investment, and banking sanctions have adversely affected the Iranian economy, and, indirectly, Iran's ability to use trade, investment, and other economic means toward strategic ends. Since 2010, when the United States and the European Union began imposing a raft of increasingly severe sanctions, Iran's oil production, oil export revenue, and gross domestic product (GDP) have all declined.<sup>63</sup> Meanwhile, unemployment and inflation are at levels not seen since the Iran-Iraq war, and foreign currency reserves, while not officially reported, are believed to be alarmingly low. Iran has undertaken a variety of efforts—such as creative barter-like trade deals with India and increased economic engagement with Iraq—to try to mitigate the damage done by sanctions, but its economy has still suffered greatly. This chapter explores these issues and examines the broad impact that sanctions have had on Iran. (See this study's appendix for an extended summary of the particular sanctions imposed on Iran by the United States, the European Union, and the United Nations.)

## Damaging effects of sanctions

The International Monetary Fund's (IMF's) 2013 *World Economic Outlook Report* predicts that Iran will be the only country in the Middle East and North Africa region to experience negative growth in 2013.<sup>64</sup> Iran's economic woes are all the more striking when contrasted with the worldwide growth of emerging markets, expanding south-south

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<sup>63</sup> *Iran: U.S. and International Sanctions Have Adversely Affected the Iranian Economy*, Government Accountability Report (GAO-13-326), February 2013: 27.

<sup>64</sup> See the International Monetary Fund's *World Economic Outlook*, April 2013: 154, at <http://www.imf.org/external/pubs/ft/weo/2013/01/pdf/text.pdf>.

trade, and growing commerce between the Middle East and Asia.<sup>65</sup> While it is difficult to apportion Iran's economic problems to a particular source—mismanagement, corruption, and sanctions are all legitimate culprits—other regional countries are plagued with similar levels of corruption and mismanagement, and none of them faces a similar economic crisis.<sup>66</sup>

Since sanctions against Iran ramped up in 2010, the Iranian economy has showed signs of being tightly squeezed. Isolation from the international economy is clearly taking its toll on oil exports. Oil accounts for close to 50 percent of government revenue and 80 percent of hard currency earnings.<sup>67</sup> Since 2011, sales of Iranian oil have been cut in half, depriving Iran upwards of \$50 billion in revenue.<sup>68</sup> Since stopping production from an oil well can cause damage and restarting can be very costly, Iran has continued to produce more oil than it can sell, and the country may have close to 30 million barrels of crude oil in storage.<sup>69</sup> Even so, Iranian oil production is estimated to have fallen by 26 percent in 2012 alone.<sup>70</sup> Compounding these problems, the U.S. Treasury sanctioned the Islamic Republic of Iran Shipping Lines for its involvement in Iranian proliferation activities in 2008.<sup>71</sup> This designation has made it very

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<sup>65</sup> Afshin Molavi, "Iran Missed the Real Revolution," *The Weekly Wonk*, 3 October 2013, at <http://weeklywonk.newamerica.net/articles/iran-missed-the-real-revolution/>.

<sup>66</sup> Evaleila Pesaran, *Iran's Struggle for Economic Independence: Reform and Counter-Reform in the Post-Revolutionary Era* (London and New York: Routledge, 2011).

<sup>67</sup> Kenneth Katzman, *Iran Sanctions*, Congressional Research Service, 26 July 2013, at <http://www.fas.org/sgp/crs/mideast/RS20871.pdf>.

<sup>68</sup> *Ibid.*

<sup>69</sup> *Ibid.*

<sup>70</sup> *Iran: U.S. and International Sanctions* (GAO-13-326).

<sup>71</sup> "Executive Order 13382," U.S. Department of State, at <http://www.state.gov/t/isn/c22080.htm>.

difficult, and in some cases, impossible, for Iran to insure its oil shipments.<sup>72</sup>

In addition to problems producing and exporting its oil, Iran is also having trouble getting paid for the sales it does make. For example, China and India, two top destinations for Iranian oil, pay Iran in local currencies held in domestic accounts. Iran is then able to use that money only to buy local goods, which means that it is essentially restricted to bartering rather than earning hard currency.<sup>73</sup> Further, Iran has had to sell its oil at a discount in order to attract customers. A recent Government Accountability Office report estimates that Iran offers up to 10 percent off the market price for some customers.<sup>74</sup>

Iran's non-oil-manufacturing industries, while only a small part of its economy, are also being negatively impacted by sanctions. These industries depend not only on imports but also on cheap energy, which has been limited since Iranian president Mahmoud Ahmadinejad began to remove the energy subsidies in December 2010.<sup>75</sup> Production of Iranian cars in 2012, for example, fell by 40 percent from 2011 levels.<sup>76</sup>

An analysis of several economic indicators in Iran, such as GDP, unemployment, inflation, and level of foreign reserves, indicates that sanctions have undermined Iran's ability to generate revenue and grow its economy. From March 2012 to March 2013, the Iranian economy reportedly decreased nearly 2 percent—one of the worst growth rates in the region.<sup>77</sup> As GDP decreases, the IMF predicts that

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<sup>72</sup> "U.S. places sanctions on Iranian firms that insure oil shipments," Reuters, 15 March 2013, at <http://www.reuters.com/article/2013/03/15/usa-iran-sanctions-insurance-idUSL1N0C7C4420130315>.

<sup>73</sup> *Spider Web: The Making and Unmaking of Iran Sanctions*, International Crisis Group, 13 February 2013, at <http://www.crisisgroup.org/en/regions/middle-east-north-africa/iraq-iran-gulf/iran/138-spider-web-the-making-and-unmaking-of-iran-sanctions.aspx>.

<sup>74</sup> *Iran: U.S. and International Sanctions* (GAO-13-326).

<sup>75</sup> *Spider Web*, International Crisis Group.

<sup>76</sup> Katzman, *Iran Sanctions*.

<sup>77</sup> *Ibid.*

unemployment in Iran could reach 19 percent by 2016,<sup>78</sup> while other analysts suggest that unemployment is likely already over 20 percent.<sup>79</sup> According to Iran's Central Bank, Iranian inflation is around 39 percent<sup>80</sup> (up from 10 percent in 2010<sup>81</sup>), but these are likely conservative estimates. Lowering inflation has become a top priority for Hassan Rouhani, Iran's newly elected president, whose government has looked to reduce subsidies and raise interest rates in order to constrain inflation and establish more sound fiscal policies.<sup>82</sup>

While there is no official report on the level of foreign reserves in Iran, the IMF estimated that Iran had around \$101 billion at the end of 2011. This led to speculation that Iran would run out of hard currency by July 2013. In April 2013, however, Iran's economic minister told journalists that Iran still had \$100 billion left in reserve. Despite the variation in number, Iran has been restricting the use of hard currency for luxury items, allowing its use for essential imports only. This illustrates that the Islamic Republic is gravely concerned about their current levels of hard currency.

## Coping with sanctions

Iranian officials have tended to downplay the impact of sanctions on Iran's economy, citing structural inefficiencies, corruption, or sabotage as the primary cause of its economic problems. However, there have been increasingly frank admissions that sanctions are having a major effect.<sup>83</sup> In 2012, Ali Khamenei, Iran's Supreme Leader, called on Iran's government to adopt an "economy of

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<sup>78</sup> *Iran: U.S. and International Sanctions* (GAO-13-326).

<sup>79</sup> Interviews with Gulf-based economic analysts in Dubai, April 2013.

<sup>80</sup> "Iran's double-digit inflation woes worsen," *Financial Times*, 16 September 2013, at <http://blogs.ft.com/beyond-brics/2013/09/16/1487172/?#axzz2i6Cecgm8>.

<sup>81</sup> *Iran: U.S. and International Sanctions* (GAO-13-326).

<sup>82</sup> "Iran considers interest hike to fight inflation." *Reuters*,

<sup>83</sup> For example, see "Iran Admits That Oil Sanctions Are Having A Brutal Effect," *Agence France Presse*, 7 January 2013, at <http://www.businessinsider.com/irans-oil-exports-have-dropped-by-forty-percent-in-the-last-nine-months-2013-1>.

resistance” to confront Western pressure.<sup>84</sup> Aside from championing vague concepts such as “self-sufficiency” and “sacrifice,” the government’s approach appears to be mainly aimed at four things: reducing the state budget’s reliance on oil revenue while boosting revenues from taxes and privatization; achieving a degree of balance in its trade by increasing the volume of non-oil exports, or exports of hydrocarbon products other than crude oil, such as gas condensates; maintaining a positive balance of trade through import controls; and, if all else fails, drawing on its foreign exchange reserves.<sup>85</sup>

Iran has also implemented informal banking exchange mechanisms and barter arrangements with some of its trading partners in lieu of using traditional payment methods. For example, Iran has continued to sell oil to India, in exchange for rupees, which it then uses to purchase food, medicine, and commercial products. While the barter approach allows Iran to circumvent sanctions, it has a cost. First, Iran is essentially forced to sell its oil at a steep discount. Second, it is paid in local currencies, which can be used to pay for products only within those countries.

## Impact on regional trade

Another area in which sanctions have had a direct and measurable impact is trade. As most of Iran’s traditional trading partners in the region are now in compliance with U.S., EU, and UN sanctions, Iran has been forced to reevaluate its economic policies. Trade with the UAE—traditionally Iran’s largest trading partner in the region—has experienced a sharp downturn since sanctions began to bite. When the UAE began to compel its banks to comply with UN sanctions in 2010, the Iranian rial dropped 15 percent in value almost instantly;<sup>86</sup> this illustrates the importance of the UAE to the Iranian economy.

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<sup>84</sup> “Iran Leader Calls for ‘Economy of Resistance,’” AFP, 23 August 2012.

<sup>85</sup> Katzman, *Iran Sanctions*.

<sup>86</sup> “Sanctions Begin to Bite,” *Economist*, 7 October 2010, at <http://www.economist.com/node/17204603>.

Trade with Dubai, Iran's principal trading partner in the Gulf, fell from 36 billion dirhams in 2011, to 25 billion dirhams in 2012.<sup>87</sup> Re-exports to Iran from the UAE also dropped by nearly a third in the first half of 2012.<sup>88</sup> In December 2011, Dubai's Noor Islamic Bank, which was once a main conduit for Iranian oil money, ceased doing business with Iran.<sup>89</sup> In March 2012, major money exchange houses in the UAE stopped dealing in rials completely, in part due to the volatility of the currency.<sup>90</sup> UAE government officials contend that Iranian banks still operating within the UAE are only able to conduct transactions in cash, making it much more difficult to do business.<sup>91</sup> In addition, it is reportedly very difficult for Iranian traders to get financing for shipping.<sup>92</sup> UAE companies have claimed that the web of sanctions is so complicated and difficult to understand that many companies have ceased to process any payment from Iran, out of fear of noncompliance.<sup>93</sup> Despite the relatively severe impact that sanctions have had on Iran's trade with the Emirates,<sup>94</sup> the drop in

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<sup>87</sup> Martin Dokoupil, "Dubai's Trade with Iran Shrinks a Third in 2012," Reuters, 25 March 2013, at <http://www.reuters.com/article/2013/03/25/dubai-iran-trade-idUSL5N0CH1SI20130325>.

<sup>88</sup> Tom Arnold, "Dubai traders call for relief on Iran exports," The National (Abu Dhabi), 3 January 2013, at <http://www.thenational.ae/business/industry-insights/economics/dubai-traders-call-for-relief-on-iran-exports>.

<sup>89</sup> Martina Fuchs, "Major UAE Currency Houses Halt Iran Rial Business," Reuters, 15 March 2012, at <http://www.reuters.com/article/2012/03/15/dubai-iran-currency-idUSL5E8EC6RB20120315>.

<sup>90</sup> Ibid.

<sup>91</sup> Katzman, *Iran Sanctions*.

<sup>92</sup> Tom Arnold, "Iran Sanctions Hurt Dubai Trade," The National (Abu Dhabi), 17 February 2012, at <http://www.thenational.ae/business/industry-insights/economics/iran-sanctions-hurt-dubai-trade>.

<sup>93</sup> Colin Simpson, "UAE businesses to feel effect of fresh US sanctions on Iran," The National (Abu Dhabi), 3 July 2013, at <http://www.thenational.ae/news/uae-news/uae-businesses-to-feel-effect-of-fresh-us-sanctions-on-iran>.

<sup>94</sup> While the UAE has certainly made itself much less hospitable to Iranian business, the country is reluctant to cut off Iran outright. The royal

trade had only a minimal effect on Dubai, whose economy grew 4 percent in 2012, compared to 4.3 percent in 2011.<sup>95</sup>

Because Iran has not been able to rely on its traditional trading partners, such as the UAE, it has been pursuing new outlets for trade in the region, particularly with neighboring Iraq. The latter has allowed Iran to skirt progressively severe sanctions. As a result, trade between the one-time rivals is flourishing. According to the International Trade Centre, Iran's exports to Iraq reached \$4 billion in 2011, around 12 percent of Iran's total exports for that year. According to some Iranian news media, trade between the two countries surpassed \$6.5 billion in 2012. The Trade Promotion Organization of Iran also claimed that 72 percent of Iran's exports go to Iraq, and revealed that Iraq's imported goods from Iran increased by nearly 15 percent this year. While these figures are likely exaggerated, they illustrate the upward trajectory of Iran-Iraq trade. And their relationship extends beyond trade: in July 2013, Iraq signed a deal to import natural gas from Iran, which will feed 850 million cubic feet of gas to three power stations in Iraq. An Iranian company, Iran Consulting Group, was awarded the \$365 million contract to build the pipeline.

The United States has imposed sanctions on Iraqi banks—and then lifted those sanctions when the banks have complied—and Iraq has been accused of allowing Iran to use its air space to send weapons to Syria. For Iraq, Iran is a very cheap and convenient trade partner at a time when the country is in need of cash. For Iran, Iraq is a convenient and large market for its overabundance of exportable goods. While to some extent the increased trade with Iraq has helped mitigate the severity of sanctions imposed on Iran, it is more like a

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family seems to want to pursue better relations with the United States by cooperating on sanctions without provoking Iran or fully denying Dubai the economic benefits of doing business with Iran. For example, the UAE refuses to shut down Bank Melli or Bank Saderat, two Iranian banks that are heavily sanctioned by the United States, but it has taken away their ability to do business in rials, rendering the banks essentially inactive. See Kenneth Katzman, *The United Arab Emirates (UAE): Issues for U.S. Policy*, Congressional Research Service, 18 June 2013, at <http://www.fas.org/sgp/crs/mideast/RS21852.pdf>.

<sup>95</sup> Arnold, "Dubai traders call for relief."

band aid on a festering gunshot wound than a cure for Iran's economic ills. Nonetheless, it is likely that both countries will continue to further their trade and economic cooperation to the extent that both sides can earn cash and other tangible benefits from doing so.

## **Indirect strategic impact: decreased military spending**

It is difficult to gauge the broader strategic effects that sanctions are having on Iran outside of general economic activities. However, one area that seems to have suffered from the impact of sanctions is Iran's military spending and investment. Budget shortfalls have probably forced the Iranian government to engage in a series of trade-offs, prioritizing some activities while divesting in other areas. For instance, while sanctions do not appear to have had a material impact on Iran's capacity to fund and arm regional allies and militant groups, such as Syria and Hezbollah, they have forced the Iranian government to make deep cuts to its conventional armed forces. Between 2010 and 2012, Iran's conventional military budget, as reported in official sources, declined by approximately 20 percent.<sup>96</sup> The commander of Iran's regular army, Brigadier General Amir Mohammad Hosayn Dadras, evidently concerned about these cuts, noted that the country's military budget is "not appropriate to the enemies' threats," although he also stated that "passion and zeal" could compensate for these losses.<sup>97</sup> Sanctions might also be hampering Iran's missile and nuclear programs by making it difficult for Iran to obtain foreign components, such as guidance systems and centrifuge technology.

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<sup>96</sup> Iran's conventional military budget for 2010 was 7,957 million, in current (2013) U.S. dollars. The same budget in 2012, the latest period for which such figures are available, was 6,297 million. This figure excludes funds for paramilitary forces, such as the IRGC, and covert programs, including the Qods and Missile Forces. Figures derived from data provided by the Stockholm International Peace Research Institute, at <http://portal.sipri.org/publications/>

<sup>97</sup> "Iran Commander Says Military Budget Not Proportionate to Enemies' Threat," Mehr News Agency in Persian, 5 July 2013, Open Source Center, IML2013070535250013, 5 July 13.

## Under pressure on shifting sands

Sanctions and their economic impact have hit hardest during a difficult period for Iran. Over the last several years, Iran has faced domestic political unrest, a campaign of violence and sabotage aimed at slowing down its nuclear program, and ethno-sectarian insurgencies based in some of its peripheral provinces. Additionally, the entire Middle East has been in flux as the wave of pro-democracy movements associated with the “Arab Spring” has dramatically changed the political orientation of some states and mired others in unrest and conflict. Sectarianism, an ugly outgrowth of hardening regional attitudes and state responses to pro-democracy movements (especially in Bahrain and Syria), has further affected the region and Iran’s place within it. Perhaps most problematic have been heightened tensions between Iran and its neighbors, particularly Saudi Arabia. With all these factors together, Iran has been under significant pressure from both inside and out, just as its strategic environment has begun to shift under its feet.

This chapter explores these issues in two parts. The first focuses on the pressures (apart from sanctions) that Iran has been under during the last few years. These include domestic upheaval and insurgencies as well as external actions taken against Iran’s nuclear program. The second part discusses how pro-democracy movements since 2011 have caused dramatic change in the region, most of which has not benefited Iran.

### Iran under pressure

In addition to sanctions, Iran believes that it has been a constant target of external pressure. Iranian leaders have traditionally spoken of domestic unrest and incidents of violent activity as part of larger foreign plots to destabilize the country and harm the regime. Over the last several years, three issues have been particularly damaging to the Islamic Republic’s sense of security: (1) the protests that erupted after the contested 2009 presidential election; (2) the ongoing ethno-sectarian insurgency in Iran’s Sistan-Baluchistan province; and (3)

sabotage of Iran's nuclear program, including the assassination of Iranian scientists inside Iran. Although the first two of these had largely domestic triggers, Iran's leaders consider them all to be outgrowths of Western aggression and regional rivalries. Western reporting has also established a foreign link to some of the incidents, which, for Iran, has validated its prevailing view.

## Post-election crisis

The domestic upheaval that followed the disputed June 2009 presidential election took Iran's regime by surprise. Mahmoud Ahmadinejad had gained the presidency in the 2005 under similar contested circumstances, but there was no corresponding popular fallout.<sup>98</sup> The regime's heavy-handed repression of protests was a signal of how worried Iran's leaders were about the unrest endangering the regime. Outside criticism of these tactics, particularly by the United States, convinced the regime that Western powers were at the root of the unrest and sought to exploit the situation. In a speech delivered after most of the unrest had been put down, Iran's Supreme Leader claimed: "The leaders of certain Western countries, presidents, prime ministers, foreign ministers, and various other officials explicitly interfered in the Iranian nation's domestic affair." He further warned:

We will calculate the hostile behavior and remarks of these governments. We will write these down in their names. They should know this. These interferences will definitely have a negative effect in their future relations with the Islamic Republic. They should know this and understand this. The Iranian nation is not a nation that would bear bullying. The Iranian nation is a strong nation. The Islamic Republic's system is a deep-rooted and stable system. The officials of the Islamic Republic's system would be united together in safeguarding this country's independence and resistance against enemies despite their differences. The enemies should know this. They should not think that they can create a division among the nation.... The Islamic system will not let some people be subject to the enemy's deception and plots and destroy people's lives and peace, and threaten

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<sup>98</sup> See Kasra Naji, *Ahmadinejad: The Secret History of Iran's Radical Leader* (Berkeley: University of California Press, 2008).

young people. This country's children are dear. Everyone is dear. The system will not let this happen.<sup>99</sup>

The uprisings reawakened a paranoia about foreign plots working to bring down the Islamic Republic from the inside. Iran's security forces, primarily the IRGC and Basij, became tasked with sniffing out and disrupting foreign attempts at instigating a "soft war" inside Iran. The Basij made this one of its central missions,<sup>100</sup> developing a new training protocol that included texts such as 'Obur az Fetneh [Overcoming Sedition], which viewed the protests and the subsequent pro-democracy Green Movement as part of a Western conspiracy against the regime.<sup>101</sup> The IRGC has continued to focus on this effort, despite the election of the more moderate Hassan Rouhani in June 2013, as evinced by the organization's most recent ideological agenda.<sup>102</sup>

## Ethno-sectarian insurgencies

Iran's post-election upheaval was only part of what Iran's leaders saw as external efforts to destabilize the country. Ongoing armed

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<sup>99</sup> Speech by Ayatollah Ali Khamenei on 6 July 2009. See "Supreme Leader: Iran Will React to Western Attempts to Create Internal Divisions." Voice of the Islamic Republic Radio 1 in Persian, Open Source Center, 6 July 2009.

<sup>100</sup> On the Basij, see Afshon Ostovar, "Iran's Basij: Membership in a Militant Islamist Organization," *Middle East Journal* 67, no. 3, summer 2013.

<sup>101</sup> Mohammad Javad Akhvan, 'Obur az Fetneh: Bazkhwani-ye Parvande-ye Yeksal-e Nabard-e Narm [Overcoming Sedition: Reviewing the Record of Year One of the Soft War] (Tehran: Markaz-e Motala'at va Pazhuheshha-ye Sazman-e Basij-e Daneshjuyi, 2010). On the Basij's overall approach to ideological training, see Saeid Golkar, "The Ideological-Political Training of Iran's Basij," *Middle East Brief* (Crown Center for Middle East Studies, Brandeis University), no. 44 (spring 2010).

<sup>102</sup> "Chahar naqsh-e sepah va jonbesh-e daneshju'i dar 4 sal-e ayandeh." *Ya al-Sarat al-Hosayn*, 20 August 2013, <http://www.yalasarat.com/vdcjhaem.uqeavzsffu.html> (Accessed 22 August 2013). Also see Arash Karami, "The Revolutionary Guard's Ideological Plan Under Rouhani," *Al-Monitor*, 20 August 2013, <http://iranpulse.al-monitor.com/index.php/2013/08/2648/the-revolutionary-guards-ideological-plan-under-rouhani/> (accessed 25 August 2013).

insurgencies that operated from ethno-sectarian minority communities along Iran's periphery were another area in which Tehran felt foreign hands at work. Iran experienced intermittent violence from the Kurdish Pjak organization in the west and smaller Sunni-Arab groups in the south,<sup>103</sup> but it was the increasingly bold and escalating operations of the Sunni-Baluch Jondollah ("Army of God") organization in Iran's southwestern Sistan-Baluchistan province that most troubled the regime. (See figure 2.) Jondollah's campaign of violence stretched for seven years, culminating in a string of bombings in 2009 and 2010 that targeted IRGC and provincial security forces. The group appeared to operate largely from across the border in Pakistan, and Iranian authorities accused other foreign powers and groups (ranging from the United States and Israel, to Saudi Arabia and "Wahhabist" organizations) of supporting it.<sup>104</sup> Tehran emphasized that Jondollah had foreign support in the trial of its leader, Abdolmalek Rigi, who was captured, put on trial, and executed in 2010.<sup>105</sup>

Notions of foreign support for Jondollah and other anti-regime elements in Iran were also put forward in the Western press (for example, see Seymour Hersh's article in the 7 July 2008 *New Yorker*).<sup>106</sup> Later, Mark Perry claimed that Israel's Mossad, posing as American intelligence operatives, had actively provided support to the group.<sup>107</sup>

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<sup>103</sup> On Sunni-Arab unrest in Iran's south, see John R. Bradely, "Iran's Ethnic Tinderbox," *Washington Quarterly* 30, no. 1, 2007.

<sup>104</sup> On Jondollah and its ideological and political roots, see Audun Kolstad Wiig, *Islamist opposition in the Islamic Republic: Jundullah and the spread of extremist Deobandism in Iran*, Norwegian Defence Research Establishment, 2 July 2009.

<sup>105</sup> See, for instance, "US offered 'extensive aid' in Iran attacks," *Press TV Tehran*, 25 February 2010, <http://edition.presstv.ir/detail/119481.html> (accessed 15 June 2013).

<sup>106</sup> Seymour M. Hersh, "Preparing the Battlefield: The Bush Administration steps up its secret moves against Iran," 7 July 2008, [http://www.newyorker.com/reporting/2008/07/07/080707fa\\_fact\\_hersh](http://www.newyorker.com/reporting/2008/07/07/080707fa_fact_hersh) (accessed 20 June 2013).

<sup>107</sup> Mark Perry, "False Flag," *Foreign Policy*, 13 January 2012, [http://www.foreignpolicy.com/articles/2012/01/13/false\\_flag](http://www.foreignpolicy.com/articles/2012/01/13/false_flag) (accessed 20 July 2013).

Washington's decision to designate Jondollah as a banned foreign terrorist organization in 2010 made official U.S. policy clear.<sup>108</sup> But, regardless of the facts, the mere presence of these claims in prominent American periodicals no doubt added weight to Iran's suspicions.

Figure 2. Zone of insurgency: Iran's Sistan-Baluchistan province



Iran worries that foreign support has continued to fuel insurgent groups in its southwestern province. The smaller militant groups that have arisen from Jondollah's ashes, such as Harakat-e Ansar-e Iran, Jaysh al-Adl, and Hezb al-Furqan, have taken on a much more pronounced jihadist ideology. Similar to Jondollah, these groups

<sup>108</sup> Laura Rozen, "U.S. designates Jundullah as terrorist group," Politico, 3 November 2010, [http://www.politico.com/blogs/laurarozen/1110/US\\_designates\\_Jundullah\\_as\\_terrorist\\_group.html](http://www.politico.com/blogs/laurarozen/1110/US_designates_Jundullah_as_terrorist_group.html) (accessed 22 June 2013).

have continued to target IRGC and local security forces through bombings and ambushes. Unlike Jondollah, however, these groups have been active on jihadist forums, have adopted the same sectarian (anti-Shia) rhetoric as jihadists, and present themselves in the guise of other jihadists (for example, by flying the Islamic black flag, as shown in figure 3). This outreach to the broader jihadist and Sunni Islamist community likely plays into Tehran's view that support for Baluch insurgents (like jihadist groups in Syria) is in part drawn from Saudi Arabia or other anti-Shia elements in the Gulf. Whether these groups draw support from the Gulf or not, their public relations effort to the jihadist community looks to be aimed at attracting such backing.<sup>109</sup> Indeed, in an April 2013 communiqué that takes credit for an attack on an IRGC weapons convoy near Samsur in Sistan-Baluchistan province, Jaysh al-Adl encourages "wealthy Sunnis" (a not-so-subtle reference to Gulf Arabs) to contribute financial support and "partner" with the group in its "jihad against the infidel (*rafz*) and tyrannical" Iranian regime.<sup>110</sup>

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<sup>109</sup> The Harakat-e Ansar-e Iran organization has been particularly active on popular jihadist forums, and has used its activity on those sites both to advertise its operations and to advocate for support from the broader jihadist community.

<sup>110</sup> Statement posted to Jaysh al-Adl's website:  
<http://jaishuladl.blogspot.com/2013/05/80.html> (accessed 15 August 2013).

Figure 3. Jaysh al-Adl members flying the black flag<sup>111</sup>



## External pressure on Iran's nuclear program

While Iran was dealing with insecurity along its borders, it was also dealing with a dramatic campaign against its nuclear program. The best-known sabotage against Iran's nuclear program was the Stuxnet virus. This malware program intermittently increased the speed of uranium centrifuges, and masked this activity to monitoring systems, thereby causing them to fail. Ultimately, by June 2010, a reported one-third of the centrifuges at the Natanz enrichment facility had been broken or made inoperable by this process.<sup>112</sup>

Additionally, beginning in January 2010, a string of assassination attempts in Tehran targeted five Iranian scientists linked to the

<sup>111</sup> The image was posted to Jaysh al-Adl's official Facebook page: <https://www.facebook.com/jaishuladl/> (accessed 15 August 2013).

<sup>112</sup> See David Albright, Paul Brannan, and Christina Walrond, *Did Stuxnet Take Out 1,000 Centrifuges at the Natanz Enrichment Plant?* ISIS Report, Institute for Science and International Security, 22 December 2010.

country's nuclear program. Four were killed and several innocent civilians were wounded. Masoud Ali Mohammad, a nuclear physicist, was killed by a remote-detonated bomb near his home. Later that year, Majid Shariari, a nuclear engineer at Shahid Beheshti University, was killed when a motorcycle passed by his car in morning traffic and attached a magnetic bomb to the driver's side door. (His wife was also injured in the attack.) The same morning, Fereydoon Abbasi Davani, an IRGC scientist, was targeted in a similar attack but survived. (Davani later became the head of Iran's Atomic Energy Agency.) In the summer of 2011, Darioush Rezaiejad, a professor, was shot dead by motorcycle-borne assailants.<sup>113</sup> In another magnetic bomb attack, a 32-year-old academic, Mostafa Ahmadi Roshan, was killed along with his driver in January 2012.<sup>114</sup>

Iran blamed foreign operatives for the killings. It particularly saw Israel and, to a lesser extent, the United States as being behind the operations.<sup>115</sup> In June and July 2012, Iranian intelligence officers arrested several individuals accused of being involved in the assassinations. Commenting on the investigation, Iran's intelligence minister, Heider Moslehi, directly implicated Mossad of being behind the attacks and claimed that Israel had provided training and logistical support to certain "terrorist networks" in locations "within the territories of one of Iran's western neighbors."<sup>116</sup> It is unclear what "western neighbor" Moslehi was referring to, but his reference was certainly meant to arouse suspicions of possible Saudi or other Arab involvement.

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<sup>113</sup> On these attacks, see David Crist, *The Twilight War: the Secret History of America's Thirty-Year Conflict with Iran* (New York: Penguin Press, 2012): 552.

<sup>114</sup> "Iran car explosion kills nuclear scientist in Tehran," *BBC News*, 11 January 2012, <http://www.bbc.co.uk/news/world-middle-east-16501566> (accessed 22 August 2013).

<sup>115</sup> "US, Israel behind Iran scientist 'killings,'" *Press TV Tehran*, 24 July 2011, <http://edition.presstv.ir/detail/fa/190606.html> (accessed 22 August 2013.)

<sup>116</sup> "Iran Arrests Terrorists behind Assassination of Young Nuclear Scientist," *Fars News Agency*, 22 July 2012, <http://english2.farsnews.com/newstext.php?nn=9104251006> (accessed 15 August 2012).

Much as in the case with Jondollah, Western reporting began to validate Iran's claims. A number of reports in prominent Western media outlets speculated that Israel and possibly the United States were behind the assassinations and the Stuxnet virus. The latter was reportedly confirmed by David E. Sanger of the *New York Times*, who cited anonymous sources in the Obama administration in a report cataloging the United States' and Israel's cyber effort against Iran's nuclear program.<sup>117</sup> Despite some of Iran's claims, a U.S. role in the assassinations did not gain as much credibility in Western reports as an Israeli connection did. David Crist, a senior historian for the U.S. military's Joint Chiefs of Staff, wrote the following description of a meeting between Bush officials and their Israeli counterparts on possible tactics to slow down Iran's nuclear program:

Israeli officials proposed extreme measures such as assassinations of Iranian scientists and supporting armed opposition groups inside Iran. Washington completely rejected these schemes, but within the limits of American legality the two nations developed common plans to derail Iran's nuclear program....<sup>118</sup>

Israel's connection to the assassinations was also put forward by renowned Israeli national security reporters, Dan Raviv and Yossi Melman, in a book on Israel's covert operations.<sup>119</sup> These claims, regardless of their accuracy, no doubt added to Iran's certainty that its enemies and regional rivals were escalating their efforts to disrupt Iran's nuclear program and destabilize its regime.

## A changing strategic environment

As Iran experienced increased pressure at home it also was witnessing extensive changes to its strategic environment. The popular, pro-democracy movements that arose in 2011 and spread across the

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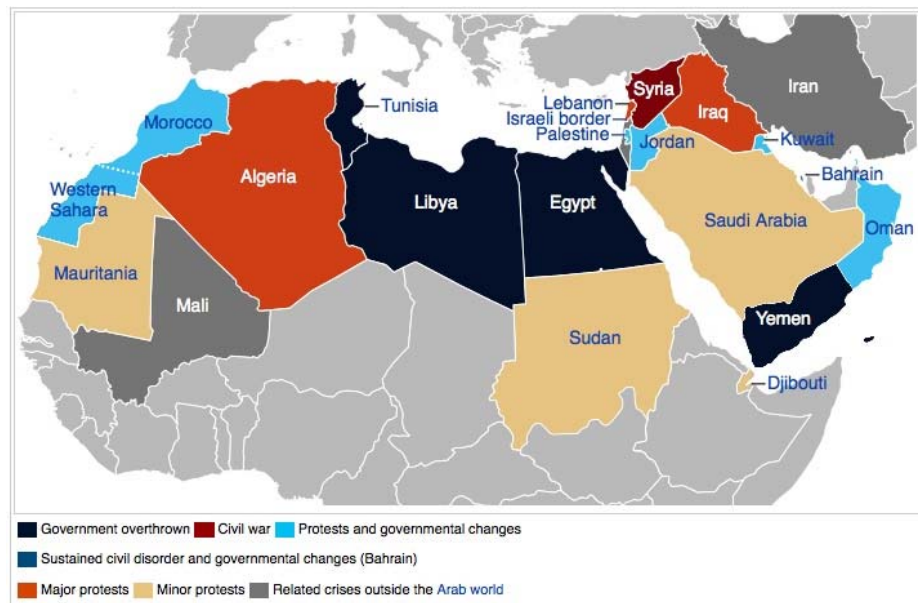
<sup>117</sup> David E. Sanger, "Obama Order Sped Up Wave of Cyberattacks Against Iran," *New York Times*, 1 June 2012, <http://www.nytimes.com/2012/06/01/world/middleeast/obama-ordered-wave-of-cyberattacks-against-iran> (accessed 22 August 2012).

<sup>118</sup> Crist, *Twilight War*: 550.

<sup>119</sup> Dan Raviv and Yossi Melman, *Spies against Armageddon: Inside Israel's Secret Wars* (Sea Cliff, NY: Levant Books, 2012).

Middle East caused a fundamental shift in the region's political dynamics. Despite fear of pro-democratic dissent within its own borders, Iran was initially supportive of the Arab Spring.<sup>120</sup> Tehran saw opportunities in what it perceived to be an "Islamic awakening" in the Arab world, which had toppled longstanding pro-U.S. leaders in Tunisia, Egypt, and Yemen.<sup>121</sup> Even though its ally, Muammar Qaddafi in Libya, was also a victim of the populist surge, Iran hoped that Islamists would achieve power in these countries and perhaps provide new opportunities for Tehran and its relations in the Arab world.

Figure 4. The Arab Spring's impact on the Middle East



But as political unrest spread to Syria and Bahrain, Iran found itself in a complicated position. Iran enthusiastically backed the largely Shia pro-democracy movement in Bahrain just as it vigorously defended the Assad regime against the largely Sunni protest

<sup>120</sup> See for instance, Scott Peterson, "Iran's Khamenei praises Egyptian protesters, declares 'Islamic awakening,'" *Christian Science Monitor*, 4 February 2011, <http://www.csmonitor.com/World/Middle-East/2011/0204/Iran-s-Khamenei-praises-Egyptian-protesters-declares-Islamic-awakening> (accessed 20 August 2013).

<sup>121</sup> Payam Mohseni, "The Islamic Awakening: Iran's Grand Narrative of the Arab Uprisings," Crown Center for Middle East Studies, *Middle East Brief* no. 71, April 2013.

movement in Syria. This apparent hypocrisy was interpreted by much of its Arab neighbors as Iran pushing a pro-Shia, sectarian agenda in the region.<sup>122</sup> Iran's hypocrisy was mirrored by many of its Arab critics, particularly in the GCC, who actively supported the crackdown on Shia protestors in Bahrain just as they decried Assad's crackdown on mostly Sunni protestors in Syria. This caused a growing sectarian divide within the Middle East, which has put Iran at direct odds with its Sunni neighbors over the future of the region.

## Iran's Shia problem

Initially, the toppling of Hosni Mubarak in Egypt was seen as a boon for Iran. Iran and Egypt had not had diplomatic ties since 1981, and remained at odds on a number of issues—ranging from Egypt's relations with the United States and Israel, to Iran's support for Islamist groups across the region. With Mubarak out of the picture, and with Islamists on the rise in Egypt, a major impediment to Iran's influence in the region appeared to be gone.<sup>123</sup> In February 2011 the Iranian navy traversed the Suez Canal for the first time since the Islamic revolution, and then traversed it again in 2012; its doing so seemed to symbolize the changing tide of Iran-Egypt relations.<sup>124</sup>

But the election of Mohammad Morsi and the ongoing crisis in Syria reawakened lingering tensions. Morsi's September 2012 attendance at the Non-Aligned Movement summit in Tehran marked the first time that an Egyptian head of state had visited Iran since the two countries broke relations. Many saw it as a signal that Egypt would

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<sup>122</sup> CNA interviews with GCC officials and regional analysts in Dubai, Abu Dhabi, Manama, and Doha, May 2011.

<sup>123</sup> On Egypt-Iran relations in the Arab Spring context, see Dina Esfandiary, "Iran and Egypt: a complicated tango?" European Institute for Security Studies, 18 October 2012, <http://www.iss.europa.eu/de/publikationen/detail/article/iran-and-egypt-a-complicated-tango/> (accessed 18 August 2013).

<sup>124</sup> "Iran warships sail via Suez Canal amid Israeli concerns," *BBC News*, 22 February 2011, <http://www.bbc.co.uk/news/world-middle-east-12533803> (accessed 19 August 2013).

conduct foreign policy on its own terms and no longer toe the line set by the United States in dealing with Iran.<sup>125</sup>

Morsi's Egypt and the Islamic Republic shared some common interests. Both were the result of revolutionary movements that toppled dictators and reinvigorated religious politics at the state level. The Muslim Brotherhood, the basis of Morsi's power, was historically an ardent critic of Israel and had close ties with Hamas—Iran's chief ally and client in Gaza. Yet, instead of marking a new era of close ties between Tehran and Cairo, Morsi's speech at the summit reflected the great disparity in their ideological perspectives and regional policies. Morsi seized the opportunity to declare Bashar al-Assad's Syria, Iran's primary ally, an "oppressive regime" and advocate outside intervention to help the opposition topple Assad.<sup>126</sup>

This was a political embarrassment for Iran and became the dominant story of the summit. Iran's immediate reaction to Morsi's comments reflected the deep divide between Iran and its featured guest. In translating Morsi's speech, Iran state television replaced all references to "Syria" in the speech with "Bahrain" in an apparent attempt to highlight what Iran considered the more relevant issue and avoid airing criticism of Damascus, Tehran's primary ally. Iran's actions instead magnified the discrepancy; caused backlash from Bahrain, Egypt, and other attendees; and signified the deep differences between Tehran and other Arab states on the Arab Spring.<sup>127</sup>

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<sup>125</sup> Ernesto Lodono, "Visit by Egypt's Morsi to Iran reflects foreign policy shift," *Washington Post*, 27 August 2012, [http://articles.washingtonpost.com/2012-08-27/world/35491859\\_1\\_morsi-nuclear-program-minister-ali-akbar-salehi](http://articles.washingtonpost.com/2012-08-27/world/35491859_1_morsi-nuclear-program-minister-ali-akbar-salehi) (accessed 20 August 2013).

<sup>126</sup> "Selected Excerpts from Morsi's Speech," *New York Times*, 30 August 2012, <http://www.nytimes.com/2012/08/31/world/middleeast/selected-excerpts-of-president-mohamed-morsis-speech.html> (accessed 20 August 2013).

<sup>127</sup> Saeed Kamal Dehghan, "Bahrain attacks Iran over mistranslating Morsi's speech on Syria," *The Guardian*, 3 September 2012, <http://www.theguardian.com/world/iran-blog/2012/sep/03/bahrain-iran-mistranslating-morsi-syria-speech> (accessed 20 August 2013).

The political turbulence in Bahrain emerged as a central issue between Iran and its Arab counterparts in the Persian Gulf. Already wary of Iran's influence within their minority Shia communities, the GCC states saw the pro-democracy movement in Bahrain as an unacceptable political and sectarian challenge. The threat in Bahrain was not simply the immediate danger that the pro-democracy movement posed to the Al Khalifa ruling family, but also the possibility that the political mobilization of Bahrain's majority Shia population could spread to neighboring Shia populations in Saudi Arabia, and to Kuwait and UAE as well.<sup>128</sup> GCC leaders feared that this would shake the bedrock of regional stability and create an environment that Iran could easily exploit to its advantage. When sporadic protests erupted within Shia communities in Saudi Arabia's eastern province in late 2010—events to which Iran seems to have had no significant connection—Riyadh's and the wider GCC's fears of a metastasizing Shia problem in the region seemed to be realized.<sup>129</sup> GCC officials became convinced that Iran not only was behind the unrest in Bahrain and Saudi Arabia but also had similar designs across the region.<sup>130</sup> The GCC states' unified response in helping Bahrain crush the protest movement through military action was a testament to this paranoia, as were its numerous accusations of Iranian involvement in Bahrain and elsewhere in the Gulf.

The GCC's anxieties regarding Iran's willingness to exploit the crisis were not without merit. Although views on Iranian influence in Gulf Shia politics are often exaggerated, the Islamic Republic's history of supporting Shia activism in the region, its reputation for running covert operations in neighboring countries, and its close partnership with Shia parties and militant groups in Iraq are real parts of Tehran's track record. GCC leaders fixate on Iran's reputation in this regard and see the hand of Tehran at work in many regional issues.<sup>131</sup> The

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<sup>128</sup> On sectarianism in the Gulf, see Toby Matthiesen, *Sectarian Gulf: Bahrain, Saudi Arabia, and the Arab Spring that Wasn't* (Palo Alto: Stanford University Press, 2013).

<sup>129</sup> See Frederic Wehrey, *The Forgotten Uprising in Eastern Saudi Arabia*, Carnegie Endowment for International Peace, June 2013.

<sup>130</sup> CNA interviews with GCC officials and regional analysts in Dubai, Abu Dhabi, Manama, and Doha, May 2011.

<sup>131</sup> Ibid.

consequent suspicions of meddling and interference have negatively affected Iran's ties to its Arab neighbors. More recent possible Iranian covert activity in countries such as Kuwait, UAE, and Bahrain has only added to the distrust between most GCC states and the Islamic Republic.<sup>132</sup> The unrest among the Shia in Bahrain and Saudi Arabia, and the conflict between the largely Sunni rebels and the Alawite Assad regime in Syria, erupted in this context, which has come to dominate the GCC's policies regarding Iran in the region.

## Syria fallout

Despite its popular beginnings, the rebellion against the Assad regime in Syria has largely become a sectarian civil war.<sup>133</sup> This has caused a dramatic shift in the relations between the regional stakeholders in the Syrian conflict. (See figure 5.) On one side has emerged a Sunni bloc—composed mostly of Saudi Arabia, Qatar, Jordan, and Turkey—which has actively supported the rebellion against the Assad regime. This bloc also includes non-state actors, such as Hamas, the Muslim Brotherhood, Al Qaeda-linked jihadists, and private funders in the Gulf, who have thrown their support behind Syria's rebels as well. Each of these states and organizations has played a role in arming and supplying the rebels in their fight against Damascus.<sup>134</sup> Counter that bloc is the pro-Assad camp, which, in addition to Russia, mostly comprises Iran, Hezbollah, and various Shiite militant groups from Iraq. This camp has vigorously supported Assad and Syria's military forces in their campaign against the rebellion.

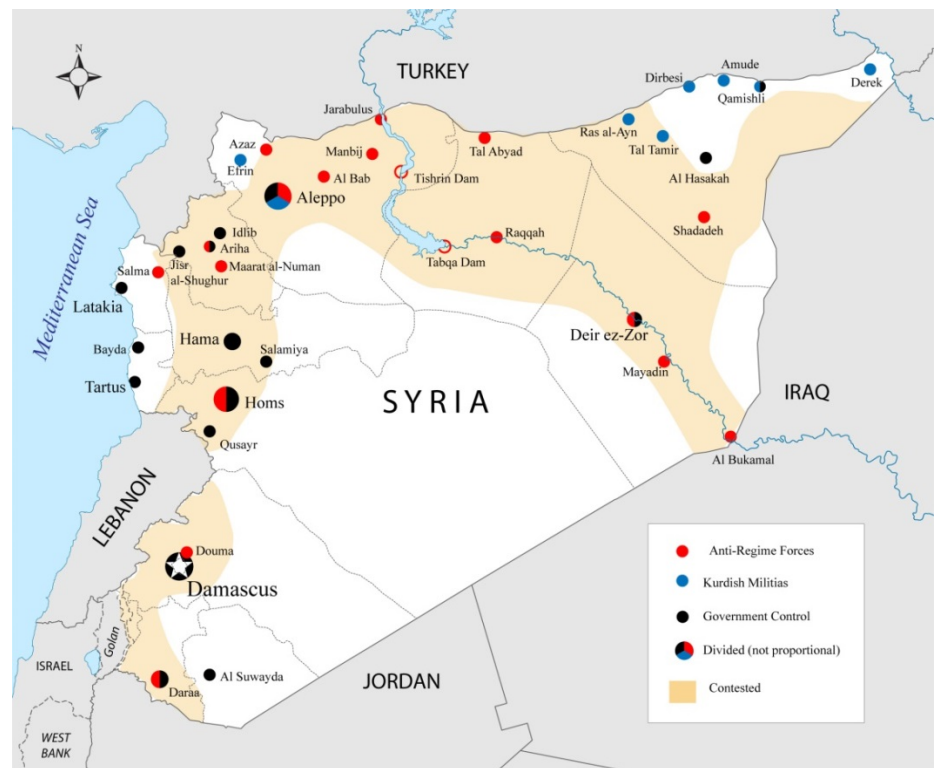
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<sup>132</sup> For instance, see "Kuwait breaks up Iranian 'spy cell,'" *Al-Arabiya*, 1 May 2010, <http://www.alarabiya.net/articles/2010/05/01/107377.html>; "United Arab Emirates 'arrests members of terror cell,'" *BBC News*, 26 December 2012; "Bahrain says Iran's Revolutionary Guard behind 'terror' cell," Reuters, 20 February 2013 (accessed 22 August 2013).

<sup>133</sup> Afshon Ostovar and Will McCants, *The Rebel Alliance: Why Syria's Armed Opposition Has Failed to Unify* (Alexandria, VA: CNA, March 2013).

<sup>134</sup> Ibid.

Figure 5. Syria under civil war



Iran's support for Assad is unsurprising. Damascus has been Tehran's main strategic ally since the Iran-Iraq war, and the two capitals have grown close over their patronage of Hezbollah and shared antipathy for Israel and the United States. The "Resistance Front" partnership of Iran, Syria, Hezbollah, and an assortment of Palestinian groups, has been a pillar of Iran's regional and overall strategic policy. If Assad were to be toppled, Iran would lose its closest state ally and a vital link to Lebanon and Hezbollah. Added to this, Assad could be replaced by Sunni Islamists with stark anti-Shia and anti-Iranian worldviews. Such a change would not only severely weaken the Resistance Front but also put a potentially hostile regime in power of a country once considered Iran's closest friend. As a patron of rebel organizations, Saudi Arabia would also likely gain influence in a new Syria, which would weaken Iran's position in the Levant and possibly erode its credibility as an outside player in the Palestinian-Israeli conflict. The possibility of Al Qaeda-linked groups operating from a new Syria could also pose a threat to Iran, particularly with regard to

Iran's continued problems with jihadist-like organizations in its southeastern Baluchistan region.

These are just some of the potential implications of losing Assad that Tehran faces. It is no surprise then that Iran has thrown its weight behind Assad despite the objections of Arab states and Western powers.<sup>135</sup> Indeed, Iran's actions in support of Assad have come at a price. For instance, the Syrian civil war has put Iran and Turkey on opposing sides of a major regional conflict. Under Recip Erdogan, Ankara had gradually become an important middleman between Iran and the West, particularly on the nuclear issue. Turkey has also become more critical of Israel and more supportive of Palestinian issues. These factors seemed to be bridging Iranian and Turkish interests in the region. However, with the rebellion against Assad, any regional alignment between Tehran and Ankara appears to be over. The two states have had increasingly tense relations since the outbreak of armed conflict in Syria, with Ankara accusing Tehran of supporting Kurdish separatists—an outgrowth of its support for pro-Assad proxies in Syria.<sup>136</sup> While Iran and Turkey were already natural regional competitors because of their comparative economic potentials and geostrategic positions, the Syrian conflict could create more of an ill-tempered rivalry between them, which could have regional ramifications beyond Syria.

In addition to a brewing rivalry with Turkey, the Syrian issue has also been destructive to Iran's ties with Hamas. Although not as close an ally as Hezbollah, Hamas had been Iran's main client in Palestine, and a core component of the Resistance Front. Iran had been Hamas' leading financial backer. This relationship gave Tehran an important foothold in the Palestinian territories and more credibility

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<sup>135</sup> On Iran's support to Assad see, Karim Sadjadpour, "Iran's Unwavering Support to Assad's Syria," *CTC Sentinel* 6, no. 8, August 2013.

<sup>136</sup> Abdullah Bozkurt, "Turkish Minister Sahin slams Iran for providing support to PKK/KCK," *Today's Zaman*, 22 December 2012, <http://www.todayszaman.com/news-302004-turkish-minister-sahin-slams-iran-for-providing-support-to-pkkkck.html>; also see Damien McElroy, "Syria and Iran 'backing Kurdish terrorist group', says Turkey," *The Telegraph*, 3 September 2012, <http://www.telegraph.co.uk/news/worldnews/europe/turkey/9518194/Syria-and-Iran-backing-Kurdish-terrorist-group-says-Turkey.html>.

as a player in the Palestinian-Israeli conflict. But with Hamas declaring support for the rebellion and abandoning Assad, Tehran-Hamas relations quickly cooled.<sup>137</sup> Even though the Assad regime had been a vital political ally and patron, Hamas' ties to Sunni Islamist organizations (especially the Muslim Brotherhood) in Syria and throughout the region made relations with Damascus untenable for Hamas' activist core. Hamas' about-face on Assad was a stunning political defeat for Tehran. It announced to the region and the world that Iran's and Syria's patronage had bought them no actual allegiance from Hamas. Instead, Hamas was willing to abandon its Resistance Front partners and enter into a largely sectarian conflict against them. Iran could not take this apparent betrayal lightly, and seems to have severely curtailed its financial support to the group in response.<sup>138</sup> To this extent, the abandonment of Assad has also harmed Hamas. The group might have been counting on Egypt's Morsi-led government to partially replace Syria and Iran as the group's main political backer, but the ouster of Morsi by the Egyptian military in July 2013, and the subsequent crackdown on the Muslim Brotherhood, has likely eliminated that possibility.<sup>139</sup> Although relations between Hamas and Iran continue, and there have been signs that both parties would like to repair the damage done, the fact remains that the two are on opposite sides of the Syrian civil war and the hot-blooded sectarian environment it has engendered.<sup>140</sup>

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<sup>137</sup> Kevin Flower, "Hamas breaks with Damascus," *CNN*, 24 February 2012, <http://edition.cnn.com/2012/02/24/world/meast/syria-hamas/>.

<sup>138</sup> Robert Tait, "Iran cuts Hamas funding over Syria," *The Telegraph*, 31 May 2013, <http://www.telegraph.co.uk/news/worldnews/middleeast/palestiniana/10091629/Iran-cuts-Hamas-funding-over-Syria.html>.

<sup>139</sup> Benedetta Berti and Zack Gold, "Hamas after Morsi: What Comes Next?" *The Fletcher Forum of World Affairs*, 25 July 2013, <http://www.fletcherforum.org/2013/07/25/berti-gold/>.

<sup>140</sup> Ali Hashem, "Iran-Hamas Rebuild Ties Following Morsi's Ouster," *Al-Monitor*, 12 August 2013, <http://www.al-monitor.com/pulse/originals/2013/08/iran-hamas-rebuild-ties-after-morsi.html>.

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## How Iran has responded

Iran has not been a passive observer over the last few years. It has acted in a number of ways. For instance, as already discussed, Iran has tried to find ways to ameliorate its economic stagnation and the impact of sanctions by working creatively with friendly nations such as Iraq and India. Tehran has also taken a proactive approach toward the Arab Spring, most notably in support of Bashar al-Assad in Syria and as a vocal proponent of Shia protest movements in the Gulf. But the most glaring examples of shifting Iranian behavior have been in the realms of covert operations and diplomacy. In the former, Iran became directly involved in risky plots and attacks against high-level foreign targets, seemingly in response to externally driven sabotage of its nuclear program and other regional factors. It took strides in the latter with the election of Hassan Rouhani, who initiated a sharp turn away from such adventurism in favor of increased diplomatic engagement with the West.

These responses are indicative of the divergent impulses of Iran's top leadership: that of the hardliners, who favor "resistance" measures to fight against Western pressure through forward-leaning covert action and client networks; and that of the pragmatists, who seek to ameliorate Iran's circumstances through diplomatic engagement with its enemies and rivals. This section briefly discusses Iran's actions in these areas. It offers a glimpse into how Iran has chosen to respond, and is suggestive of the very different paths the current Iranian regime could take in the future. We could, for example, see a more pragmatic, diplomatically inclined Iran in the event that a nuclear deal is reached with the United States; or we could see a more aggressive Iran should negotiations fail yet again, pressure continue to build against it, and its regional equities continue to be threatened by a variety of forces.

### Tit-for-tat covert operations

In the face of escalating pressure aimed at degrading its nuclear program, Iran turned to covert operations to respond to its enemies and perhaps discourage further attacks. But instead of tasking its

clients to act on its behalf, Iran's leaders seemingly altered their prevailing strategy of covert action by proxy (which afforded Tehran deniability) and took a direct hand in high-profile kinetic operations. Iran also seems to have engaged in an increasingly aggressive cyber campaign. This apparent strategic shift, which put Iran more at risk, seems to have been driven in part by Iran's deteriorating domestic security and the immense stress put on the regime by cascading internal and external factors.

Matt Levitt argues that after the assassination of Masoud Ali Mohammadi in January 2010, Iranian intelligence decided that it would no longer rely on third parties (such as Hezbollah) to carry out violent covert action abroad and would instead task the IRGC's Qods Force to engage in these operations *directly*. As Levitt explains, "Even more than the loss of its scientists, Tehran sought to address its damaged prestige—the image of an Iran so weak it could not even protect its own scientists at home could not stand."<sup>141</sup> It is unclear whether Iran's calculus was as simple as that. But the number of plots and attacks linked to Iran in 2010–2012 certainly lends credence to such a theory. The direct involvement of Iranian operatives in these cases adds further weight to the idea that a shift in Tehran's strategic thinking and behavior took place.<sup>142</sup>

The most audacious plot, a plan to assassinate Saudi Arabia's ambassador to the United States in Washington, D.C., was disclosed in October 2011 by U.S. Attorney General Eric Holder. The case centered on Mansour Arbabsiar, an Iranian-American former used car salesman from Texas, who was arrested by U.S. federal agents for being the middle man in a scheme that connected Iran's Qods Force with (what Arbabsiar thought were) members of Mexico's Los Zetas cartel. In fact, Arbabsiar's contacts in Mexico were informants for the Drug Enforcement Agency. On a trip to Iran, Arbabsiar reportedly reconnected with a relative who happened to be a Qods Force officer.

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<sup>141</sup> Matthew Levitt, "Hizballah and the Qods Force in Iran's Shadow War with the West," Washington Institute for Near East Policy, *Policy Focus* no. 123, January 2013.

<sup>142</sup> See, Afshon Ostovar, "If Iran Did It," *Foreign Policy*, 23 July 2012, [http://www.foreignpolicy.com/articles/2012/07/23/if\\_iran\\_did\\_it](http://www.foreignpolicy.com/articles/2012/07/23/if_iran_did_it) (accessed 25 August 2013).

The two hatched an idea to hit targets in the United States through Mexican proxies.<sup>143</sup> Another Qods Force officer, Ghulam Shakuri, later took charge of the operation.<sup>144</sup>

After Arbabsiar's arrest, U.S. officials made the story and many of its head-scratching details public.<sup>145</sup> Most analysts were surprised to learn that Iran's Qods Force was involved in such a scheme on U.S. soil, and even U.S. officials acknowledged the odd contours of the case. Secretary of State Hillary Clinton even remarked: "The idea that they would attempt to go to a Mexican drug cartel to solicit murder for hire to kill the Saudi ambassador—nobody could make that up, right?"<sup>146</sup> Working through intermediaries in violent covert activity has been part of Iran's modus operandi. It had used that method to strategic effect through Hezbollah in Lebanon and through allied Shia groups in post-Saddam Iraq. But the U.S. plot seemed to be a far more ambitious, and a somewhat slapdash, effort. It was poorly planned, poorly resourced, and very poorly executed—not the kind of operation the Qods Force was known for. Further, and most disturbingly, it risked escalating tensions with the United States and Saudi Arabia—possibilities that clashed with Iran's overall strategic interests.<sup>147</sup>

But the failure of that plot did not stop Iran from continuing what appeared to be a more forward-leaning and aggressive policy of retaliation. Iran was connected to a number of plots in 2011 and

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<sup>143</sup> For a narrative of the plot, see Crist, *Twilight War*, 562-67.

<sup>144</sup> See the U.S. District Court of Southern New York's indictment of Arbabsiar and Shakuri, "United States of America v. Mannsor Arbabsiar (a/k/a "Mansour Arbabsiar") and Gholam Shakuri (a/k/a "Ali Gholam Shakuri"), Defendants," 2011.

<sup>145</sup> Ibid.

<sup>146</sup> See Clinton's interview with the Associated Press. Matthew Lee, "AP Interview: Plot to kill envoy with hurt Iran," 11 October 2011, "[http://www.boston.com/news/nation/washington/articles/2011/10/11/ap\\_interview\\_plot\\_to\\_kill\\_envoy\\_will\\_hurt\\_iran/](http://www.boston.com/news/nation/washington/articles/2011/10/11/ap_interview_plot_to_kill_envoy_will_hurt_iran/)" (accessed 20 August 2013).

<sup>147</sup> Afshon Ostovar, "Worst. Plot. Ever." *Foreign Policy*, 13 October 2011, [http://www.foreignpolicy.com/articles/2011/10/13/worst\\_plot\\_ever](http://www.foreignpolicy.com/articles/2011/10/13/worst_plot_ever) (accessed 20 August 2013).

2012, including the murder of a Saudi diplomat in Pakistan and a string of failed attacks on Israeli diplomatic officials.<sup>148</sup> On 13 February 2012, assailants targeted two Israeli diplomatic vehicles—one in Tblisi, Georgia, and the other in New Delhi, India—with magnetic explosives, similar to those used in the assassination of Iranian scientists. The Tbilisi bomb was discovered before it exploded, but the attack in India severely injured the wife of an Israeli diplomat. The next day, there was an explosion in an apartment rented and occupied by Iranian nationals in Bangkok, Thailand. Three individuals left the apartment in separate directions; one was carrying an explosive device that he attempted to throw at pursuing Thai police, only for the device to fall nearby and blow off his lower legs. Another suspect was arrested at the airport trying to board a plane to Malaysia, and a third was arrested in Kuala Lumpur.

Although Iran denied involvement in any of these attacks, investigations have connected Iranian nationals—all suspected Qods Force operatives—to each incident.<sup>149</sup> Thai authorities—who convicted two Iranians on explosives charges and are seeking extradition of a third from Malaysia—further concluded that these suspects had been planning to hit Israeli diplomatic targets before the accidental explosion in their apartment forced them to flee. They also claimed that the bombs used in the Bangkok bombing were similar to the magnetic “sticky bombs” used in the Tbilisi and New Delhi attacks.<sup>150</sup>

In addition to these high-profile incidents, Iran was also connected to a surge of cyber-attacks on a variety of targets, including foreign

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<sup>148</sup> David Ignatius, “Intelligence links Iran to Saudi diplomat’s murder,” *Washington Post*, 13 October 2011, [http://www.washingtonpost.com/blogs/post-partisan/post/intelligence-links-iran-to-saudi-diplomats-murder/2011/10/13/gIQAfzCPiL\\_blog.html](http://www.washingtonpost.com/blogs/post-partisan/post/intelligence-links-iran-to-saudi-diplomats-murder/2011/10/13/gIQAfzCPiL_blog.html).

<sup>149</sup> See, Levitt, “Hizbullah and the Quds Force;” also, Crist, *Twilight War*.

<sup>150</sup> Wilawan Watcharasakwet and Warangkana Chomchuen, “Two Iranians Convicted of Botched Bangkok Bomb Plot.” *Wall Street Journal*, 22 August 2013, <http://online.wsj.com/news/articles/SB10001424127887323665504579028401044391862>.

business computer networks.<sup>151</sup> Cyber-attacks connected to Iran had begun to spike in 2009 with the emergence of a shadowy hacker group that called itself the Iran Cyber Army (ICA). The hacking activities associated with this group were relatively unsophisticated and had little impact, though they sometimes affected major Internet sites such as Twitter and Baidu (a Chinese search engine similar to Google) and attracted wide attention.<sup>152</sup> More severe and damaging were attacks on Saudi Aramco in 2012 and on a number of major banks in 2013.<sup>153</sup> These attacks, linked to Iran by industry specialists and U.S. officials, were much more sophisticated operations than those claimed by the ICA, and have been seen broadly as Iranian responses to issues such as Stuxnet, sanctions, and Riyadh's role in Bahrain and Syria.<sup>154</sup>

## A pragmatic turn?

Iran's aggressive covert campaign in 2011 and 2012 resulted in some glaring failures. Although it likely succeeded in communicating to its enemies that attacks against Iran would no longer go unanswered, the poorly executed operations in Tbilisi, New Delhi, and Bombay were likely embarrassments for Tehran. The cyber-attacks against

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<sup>151</sup> Barbara Slavin and Jason Healey, *Iran: How a Third Tier Cyber Power Can Still Threaten the United States*, Atlantic Council (Issue Brief), 29 July 2013.

<sup>152</sup> See, Alex Lukich, *The Iranian Cyber Army*, Center for Strategic and International Studies, 12 July 2011; also, Farvartish Rezvaniyeh, "Pulling the Strings of the Net: Iran's Cyber Army," *Tehran Bureau*, 26 February 2010, <http://www.pbs.org/wgbh/pages/frontline/tehranbureau/2010/02/pulling-the-strings-of-the-net-irans-cyber-army.html>.

<sup>153</sup> On the attack on Saudi Aramco, see Christopher Bronk and Eneken Tikk-Ringas, "The Cyber Attack on Saudi Aramco," *Survival* 55, no. 2, April-May 2013.

<sup>154</sup> Nicole Perloth, "In Cyberattack on Saudi Firm, U.S. Sees Iran Firing Back," *New York Times*, 23 October 2012, <http://www.nytimes.com/2012/10/24/business/global/cyberattack-on-saudi-oil-firm-disquiets-us.html>; also, Nicole Perloth and Quentin Hardy, "Bank Hacking Was the Work of Iranians, Officials Say," *New York Times*, 8 January 2013, <http://www.nytimes.com/2013/01/09/technology/online-banking-attacks-were-work-of-iran-us-officials-say.html>.

Aramco and major banks were more successful in execution but were also potentially risky forms of retaliation which did little to reverse international pressures on Iran or alter its status quo. While such adventurism likely fed the desires of Iran's hardliners, particularly those in the security forces and intelligence services, it did little to alter Iran's predicament. Indeed, these actions provided more fodder to Iran's enemies and hardened Western attitudes already critical of Iran's behavior and activities in the Middle East.

Whether Iran's top leadership arrived at similar conclusions is unknown; however, the presidential election of June 2013 provided them with an opportunity to change course. Given the trend toward more aggressive covert actions and the growing campaign in Syria, most outside observers saw little potential for Iran's next president to change stride. However, the surprising election of Hassan Rouhani—a pragmatic conservative close to both the supreme leader and his chief critic, Akbar Hashemi Rafsanjani—seemed to indicate that regime insiders were open to a new approach to Iran's problems.

The 2013 presidential election was a crossroads for Iran: it could either double-down on its resistance strategy, which would very likely put it on a collision course with the United States; or it could switch strides and seek some sort of accommodation with the West. It is impossible to know the exact process and thinking behind Rouhani's election. Outwardly, Rouhani was elected through a mostly fair democratic contest by an Iranian electorate tired of their country's economic woes and the alienating foreign policies of Mahmoud Ahmadinejad. Yet, given how much the regime appeared to interfere in past elections, the unimpeded result suggests at the very least the supreme leader's tacit support for Rouhani. With Iran's economy in shambles, and its interests threatened in the Middle East, it is likely that the supreme leader and other regime heavyweights correctly understood that the current trajectory was untenable. They also may have feared that the election of another unpopular hardliner could reignite popular protest and—as in Libya and Syria—become a pretext for foreign intervention against the regime.

The election of Rouhani thus provided the regime with both an opportunity and the political cover to address popular domestic concerns and adopt a new approach vis-à-vis the West. The strategic shift towards diplomacy with the West was nearly immediate once

Rouhani took office. Rouhani put together a foreign policy team composed of veteran diplomats—including Foreign Minister Mohammad Javad Zarif, a former ambassador to the United Nations and noted pragmatist regarding relations with the United States—and announced that this team (instead of Iran’s Supreme National Security Council) would take charge of nuclear negotiations with the West.<sup>155</sup> Rouhani’s moves appeared to be supported by the supreme leader, who framed the new push for diplomacy as a “tactical” part of a larger strategic struggle, stating: “I’m not opposed to correct moves. I believe in what was described years ago as heroic flexibility.... A wrestler who exercises flexibility for a tactical reason should not forget who his rival is and what his goal is.”<sup>156</sup>

With the supreme leader’s support, and likely the backing (or at least initial buy-in) of other important regime constituencies, Rouhani planned to restart nuclear negotiations with the West at the United Nations General Assembly session in September.<sup>157</sup> While there, Rouhani’s team took part in high-level meetings with Western officials, including a meeting between Zarif and U.S. Secretary of State John Kerry. These positive interactions culminated in a short phone conversation between Rouhani and President Obama—the highest level interaction ever between the United States and the Islamic Republic. (The action was criticized in Iran’s hardline media

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<sup>155</sup> Farnaz Fassihi, “Iran Shifts Responsibility for Nuclear Talks,” *Wall Street Journal*, 5 September 2013, <http://online.wsj.com/news/articles/SB10001424127887323893004579057231496060624>.

<sup>156</sup> Golnaz Esfandiari, “Famously Inflexible Iranian Leader Advocates Flexibility,” *Radio Free Europe/Radio Liberty*, 17 September 2013.

<sup>157</sup> “Ra’is-e jomhur: naqd ra mi-pazirim/shayad avalin-e mozkerat-e hasteh’i dar New York anjam shavad,” Iranian Students’ News Agency, 10 September 2013, <http://www.isna.ir/fa/news/92061911645/%D8%B1%DB%8C%DB%8C%D8%B3-%D8%AC%D9%85%D9%87%D9%88%D8%B1-%D9%86%D9%82%D8%AF-%D8%B1%D8%A7-%D9%85%DB%8C-%D9%BE%D8%B0%DB%8C%D8%B1%DB%8C%D9%85-%D8%B4%D8%A7%DB%8C%D8%AF-%D8%A7%D9%88%D9%84%DB%8C%D9%86-%D9%85%D8%B0%D8%A7%DA%A9%D8%B1%D8%A7%D8%AA>.

and by the IRGC's top commander, Ali Jafari.)<sup>158</sup> Rouhani's diplomatic push continued through a new round of nuclear talks with the P5+1 in October 2013, which were deemed productive on all sides and set the stage for another round of talks later in the year.<sup>159</sup>

The motivations underlying Iran's new diplomatic track with the West might be many, but its foremost goal appears to be sanctions relief.<sup>160</sup> Although some analysts have argued that sanctions have so far not pressured Iran to change its stated nuclear goals,<sup>161</sup> there is little doubt that the toll of sanctions has motivated the diplomatic efforts under Rouhani. Iran's first nuclear proposal was seen as a serious gesture by P5+1 delegates, but it did not go far enough for the United States.<sup>162</sup> A hardline newspaper close to the IRGC stated that Iran had three areas that it would not compromise on: no cessation of enrichment, no exportation of enriched uranium for storage in another country (e.g., Russia), and no closure of the Fordow enrichment facility.<sup>163</sup> If these issues remain red-lines preventing an

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<sup>158</sup> "Farmandeh-ye kol-e sepah dar goftogu ba khabargozari-ye tasnim," Tasnim News Agency, 30 September 2013, <http://www.tasnimnews.com/Home/Single/154227>.

<sup>159</sup> "Iran deputy FM describes P5+1 talks 'good'," *Al-Alam*, 15 October 2013, <http://en.alalam.ir/news/1524798>; Joby Warrick, "Iran, world powers report progress in nuclear talks, agree to further meetings," *Washington Post*, 16 October 2013, [http://www.washingtonpost.com/world/national-security/iran-nuclear-talks-enter-second-day-western-officials-call-tehrans-proposal-very-useful/2013/10/16/615815f4-364e-11e3-be86-6aeaa439845b\\_story.html](http://www.washingtonpost.com/world/national-security/iran-nuclear-talks-enter-second-day-western-officials-call-tehrans-proposal-very-useful/2013/10/16/615815f4-364e-11e3-be86-6aeaa439845b_story.html).

<sup>160</sup> Thomas Edbrink and Mark Landler, "Iran Said to Seek a Nuclear Accord to End Sanctions," *New York Times*, 19 September 2013, <http://www.nytimes.com/2013/09/20/world/middleeast/iran-said-to-seek-a-nuclear-accord-to-end-sanctions.html>.

<sup>161</sup> See for instance, Bijan Khajepour, Reza Marashi, and Trita Parsi, "Why the Iran Sanctions Don't Work," *The National Interest*, 3 April 2013, <http://nationalinterest.org/commentary/why-the-iran-sanctions-dont-work-8301>.

<sup>162</sup> Barbara Slavin, "Iran's New Nuclear Proposals," *Al-Monitor*, 17 October 2013, <http://www.al-monitor.com/pulse/originals/2013/10/iran-nuclear-freeze-proposal.html>.

<sup>163</sup> "Iran ba 3 khat-e qermez-e hasteh'i beh Geneva mi-ravad," *Javan Online*, 13 October 2013,

Iranian compromise, it is doubtful that a deal with the United States can be made or sanctions removed.<sup>164</sup>

In navigating talks with the United States, Rouhani also has to contend with Iran's hardliners, whose buy-in he will need in order to reach a deal. Though hardliners seemed to have backed the first round of talks, it is unclear to what extent they support the prospect of a détente with Washington. Hardliners have continually reiterated the danger of compromising with the United States. One IRGC official, for example, warned that "heroic flexibility" should not lead to the "surrender" of Iran's rights or the "retreat" of its interests.<sup>165</sup> They have also criticized Rouhani's handling of the talks, arguing that if the United States was pleased with Iran's offer then it must not have been in Iran's favor.<sup>166</sup> All of this suggests that the hardliners'

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[http://www.iranchamber.com/calendar/converter/iranian\\_calendar\\_converter.php](http://www.iranchamber.com/calendar/converter/iranian_calendar_converter.php).

<sup>164</sup> George Jahn, "Iran Nuke Overture: More a Promise Than an Offer," Associated Press, 22 October 2013, <http://abcnews.go.com/International/wireStory/iran-uke-overture-promise-offer-20641802>.

<sup>165</sup> See interview with IRGC commander Hosayn Salami, *Javan Online*, 22 September 2013, <http://www.javanonline.ir/fa/news/613314/%D9%87%DB%8C%DA%86-%D9%86%D8%B1%D9%85%D8%B4%DB%8C-%D8%AF%D8%B1-%D8%AD%D9%82%D9%88%D9%82-%D9%87%D8%B3%D8%AA%D9%87%E2%80%8C%D8%A7%DB%8C-%D9%86%D8%AF%D8%A7%D8%B1%DB%8C%D9%85-%D9%BE%D8%A7%D8%B3%D8%AE%E2%80%8C%D9%85%D8%A7%D9%86-%D8%A8%D9%87-%D8%AA%D9%87%D8%AF%DB%8C%D8%AF%D8%A7%D8%AA-%D9%BE%D8%B4%DB%8C%D9%85%D8%A7%D9%86%E2%80%8C%D8%AE%D9%88%D8%A7%D9%87%D8%AF-%D8%A8%D9%88%D8%AF>; also, Arash Karami, "No 'Flexibility' on Nuclear Rights, Says IRGC Commander," *Al-Monitor*, 22 September 2013, <http://iranpulse.al-monitor.com/index.php/2013/09/2867/no-flexibility-on-nuclear-rights-says-irgc-commander/>.

<sup>166</sup> Scott Peterson, "Nuclear talks secrecy allows Iran's hardliners to argue US has upper hand," *Christian Science Monitor*, 21 October 2013, <http://www.csmonitor.com/World/Middle-East/2013/1021/Nuclear-talks-secrecy-allows-Iran-s-hardliners-to-argue-US-has-upper-hand>.

impulsive resistance of Western pressure could yet return to Iranian foreign policy should Rouhani not be able to achieve a deal with the P5+1 that they can live with.

## Constraints and opportunities for Iranian strategy

In pursuing its strategic agenda, Iran has had to contend with a number of obstacles over the last several years. As previously discussed, sanctions have had a dramatic impact on Iran's economic connectivity strategy with Gulf states and on its economy. This not only has limited Iran's ability to engage productively with its neighbors but also has made Iran less attractive and credible as a potential regional partner. Iran has endured domestic unrest, an active and violent campaign targeting its nuclear program, and ethno-sectarian insurgencies, which brought both embarrassment to regime leaders and a sense of simmering insecurity. The Arab Spring, political activism among Shia populations in Bahrain and Saudi Arabia, and Syria's civil war have severely impacted the political and strategic dynamics of Iran's immediate neighborhood. Iran's support for the Assad regime has harmed its relations with allies such as Hamas and an important interlocutor with the West in Turkey, and has fanned the flames of its on-going rivalry with Saudi Arabia and other Arab states. It has also contributed to a prevailing sectarian mood in the region, placing Iran in an uncomfortable position, while putting in sharp relief the differing regional agendas of Iran and its Sunni neighbors—so much so that Iran now finds itself engaged in a proxy war against Saudi Arabia and other Sunni interests in Syria.

Whereas the previous chapter explored how Iran has already responded to these dynamics, this final chapter looks at how they could impact Iran's future behavior *in the region*. It specifically examines how changes to Iran's strategic environment have created both constraints to and opportunities for Iranian strategic action in the Middle East. We discuss the broad impact this has had on Iranian strategy and examine how the on-going conflicts, sectarianism, and other factors in the region could affect Iran's ability to act and the actions it takes in the future. We also look at how certain outgrowths of this changing environment could benefit or at least be exploited by Iran toward strategic ends.

## A changing strategic landscape

Iran's neighborhood has gone through immense turmoil and change over the last few years. The seismic shifts to the region that the U.S. military invasions of Afghanistan and Iraq brought over a decade ago are in some sense continuing via the Arab Spring. The political and strategic landscape of the Middle East in 2013 is sharply different from what it was in 2008, and it seems destined to change further still in the years to come. Five years ago Iran's regional strategy appeared well suited to its setting. It had promising economic relations with the Gulf, including robust trade with Dubai and the UAE. Its partnerships with Hezbollah and Syria enabled it to maintain a solid position in the Levant. Its patronage for Hamas gave it a foothold in Gaza and more credibility as a player in the Palestinian-Israeli issue. These relationships also helped it keep pressure on Israel as a deterrent against possible Israeli strikes on its nuclear program. Similarly, its ties to Shiite groups in Iraq (and to a lesser extent to groups in Afghanistan) enabled it to keep pressure on U.S. forces in the region. While it was still competing with Saudi Arabia for regional influence, its ties to GCC states in general had been warming.<sup>167</sup>

But in 2013 the picture looks quite different. Iran's trade with the Gulf has steadily declined as has its economic importance to Dubai, the region's foremost commercial hub. Its partners in the Levant are at war with Syria's Sunni opposition. Assad's hold over the Syrian state has crumbled, with large portions of the country controlled by opposition forces. Bleed-over from Syria has caused increasing instability in Lebanon and jeopardized Hezbollah's standing in the country. Alarmed by rising Shia political activism in their own neighborhood, Gulf states have become deeply involved in the Syrian civil war. Saudi Arabia and Qatar are acting as the chief patrons for Syria's armed opposition forces, pitting Iran against its neighbors in an increasingly sectarian proxy war. Iran's actions in Syria, support for Shia movements in the Gulf, and its covert operations targeting Saudi officials and interests, have so tarnished Tehran-Riyadh relations that Saudi Arabia has joined Israel as a leading critic against a possible

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<sup>167</sup> Habibi, "Iran-GCC Economic Relations."

nuclear deal and détente between Washington and Tehran.<sup>168</sup> Also problematic is the loss of Mubarak's Egypt as a counterweight to Saudi influence in the region and the emerging Cairo-Riyadh symbiosis following the toppling of Morsi and his Muslim Brotherhood-led government in June 2013.<sup>169</sup>

## Constraints on Iranian strategy

These changes have likely put constraints on Iran's regional strategy. Firstly, Iran's emphasis on strengthening economic relations with the Gulf—the economic connectivity angle to its broader regional strategy—has withered due to sanctions and pressure from the United States. (This is ironic since economic connectivity was meant to buffer Iran from such Western pressure in the first place.) The sectarian issue, spurred by protest movements in Bahrain and Saudi Arabia and exacerbated by Syria's civil war, has also alienated Iran from much of the Sunni Middle East and made its actions in Syria, which are fueled by strategic objectives, appear to be part of an Iranian pro-Shia (or anti-Sunni) sectarian agenda. This has driven a wedge between Iran and Hamas, which, despite maintaining a semblance of relations, are now opponents in Syria's civil war. It has equally damaged Iranian-Turkish relations, which had begun to warm in recent years under Erdogan's engagement initiatives with the West.<sup>170</sup>

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<sup>168</sup> Ellen Knickmeyer, "Spy Chief Distances Saudis from the U.S." *The Wall Street Journal*, 21 October 2013, <http://online.wsj.com/article/SB10001424052702303902404579150011732240016.html>.

<sup>169</sup> See for instance, Khaled al-Dakhil, "Riyadh and Cairo relations after the toppling of Morsi," *Al-Hayat*, 14 July 2013, <http://alhayat.com/OpinionsDetails/532286>; English translation: "Riyadh Rushes to Support Egypt's New Military Rulers," *Al-Monitor*, July 2013, <http://www.al-monitor.com/pulse/politics/2013/07/relationship-saudi-arabia-cairo-following-morsi-ouster.html>.

<sup>170</sup> Daphne McCurdy and Nick Danforth, "Turkey and Iran: A fraying Relationship or Business as Usual?" *Foreign Policy*, 28 February 2012, [http://mideast.foreignpolicy.com/posts/2012/02/28/turkey\\_and\\_iran\\_a\\_fraying\\_relationship\\_or\\_business\\_as\\_usual](http://mideast.foreignpolicy.com/posts/2012/02/28/turkey_and_iran_a_fraying_relationship_or_business_as_usual).

Iran is therefore left with much of its regional strategic investments in doubt. Tehran's economic role has faded, leaving it with fewer areas of legitimate and fruitful interaction with its neighbors. Its assets in the Levant are threatened by the conflict in Syria, the potential for spillover into Lebanon, and the looming possibility of outside intervention against Assad. With weaker ties to Hamas, Iran's ability to be a credible player in Palestine is also in question. Above all, Iran relies on these relationships as strategic leverage against Israel and, by extension, the United States. If it were to lose its footholds in the Levant and Palestine, its ability to threaten Israel would be less viable and thus less of a deterrent. Iran had relied on the ability to harass U.S. forces in Iraq and Afghanistan as a credible deterrent against the United States, but with the withdrawal of U.S. troops from Iraq and the drawdown of U.S. forces in Afghanistan, Iran's ability to target U.S. forces by proxy has steadily declined. It could suffer an even more critical loss in this context if it became unable to put pressure on Israel through clients such as Hezbollah and Hamas.

Sectarianism has put Iran in an awkward position. Since the revolution, the Islamic Republic has tried to position itself as a leading voice for all Muslims, not just Shiites. Its championing of the Palestinian cause was born partly out of this impulse, as a method to attract broad Arab and Sunni support for both Iran and its campaign against Israel and the West. Even though Iran has never had much success in attracting Sunni support for its ideological conception of Islamic government led by the clergy (*velayat-e faqih*),<sup>171</sup> it has made inroads in Sunni Arab publics through the Palestinian issue, perhaps best exemplified by its partnership with Hamas and Hezbollah.<sup>172</sup> The climate of sectarianism in the region is putting Iran's past efforts at attracting Sunni support at risk.

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<sup>171</sup> Immanuel Sivan, "Sunni Radicalism in the Middle East and the Iranian Revolution," *International Journal of Middle East Studies* 21 (1989).

<sup>172</sup> For instance, according to the Arab Public Opinion Poll, favorability for Iran and its nuclear program among Arab publics was higher in 2010 than in 2011. Iran's decline appears to be the result of the Arab Spring and Iran's support for Assad in the conflict in Syria. See both polls, conducted by Shibley Telhami and Zogby International, <http://sadat.umd.edu/new%20surveys/surveys.htm/>.

As Iran loses goodwill with Sunni allies such as Hamas and interlocutors such as Turkey and Qatar over its activities in Syria, it is forced to rely even more on its core Shia constituency to advance its strategic goals. Hezbollah and other Shia militias from Iraq have been the main backers of Assad aside from Iran and Russia.<sup>173</sup> Iran's reputation is tied to these organizations, which, unlike the Islamic Republic, were formed in hyper-sectarian conflict environments (i.e., the civil wars in Lebanon and Iraq). They lack the pan-Islamist pretensions that Iran has tried to maintain, and, in the polarizing climate of the Syrian civil war, are far more outward about their communalist leanings. Vivid evidence of this can be seen in the numerous Facebook and YouTube pages associated with Shi'ite militant organizations active in Syria, which are just as exclusivist and implicitly as sectarian as comparable accounts run by jihadist groups. These media also link pro-Shia, anti-jihadist (or "takfiri," as jihadists are generally called by Shia activists) rhetoric with Iran and Iranian leadership. The visual propaganda produced by non-Iranian Shia militant groups encapsulates this theme (figures 7 and 8 below). The first, which circulated among mostly Iraqi Shia activists on Facebook, associates the emblems of several Shia militant organizations with a picture of Iran's supreme leader, Ali Khamenei. The image further projects the notion of *rising* Shia dominance over the region and perhaps globally, signified by a picture of the earth highlighting the Arabian peninsula and Persian Gulf. Similarly, the Iraq-based militant group Kata'ib Sayyid al-Shuhada includes pictures of Khamenei (and sometimes of Khomeini) in images honoring the group's "martyrs" killed while fighting along pro-Assad forces in Syria.<sup>174</sup> Even if social media efforts such as these are independent of Iranian influence, they complicate Iran's status as a pan-Islamist actor, and are likely

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<sup>173</sup> On Iraqi groups operating in Syria, primarily in protection of the Sayyida Zaynab shrine in Damascus, see Philip Smyth, "From Karbala to Sayyida Zaynab: Iraqi Fighters in Syria's Shi'a Militias," *CTC Sentinel* 6, no. 8, August 2013.

<sup>174</sup> For more on this organization and its propaganda, see Phillip Smyth, "Kata'ib Sayyid al-Shuhada Emerges: Updates on the New Iraqi Shia Militia Supplying Fighters to Syria," 9 September 2013, <http://jihadology.net/2013/09/09/hizballah-cavalcade-kataib-sayyid-al-shuhada-emerges-updates-on-the-new-iraqi-shia-militia-supplying-fighters-to-syria/>.

seen by Sunni publics as further confirmation of Iran's sectarian role and agenda in the region.

Figure 6. Khamenei with the emblems of Shia militant organizations<sup>175</sup>



Figure 7. Martyr poster by Iraq's Kata'ib Sayyid al-Shuhada organization



<sup>175</sup> These emblems represent the following groups (from left to right): Iraq's Asaib Ahl al-Haq, Lebanon's Hezbollah, Iraq's Badr Organization, Iran's Revolutionary Guards, and Iraq's Hezbollah Brigades.

## Opportunities for Iran

Yet, even as increased external pressure and regional change have created impediments to Iranian strategy, new opportunities have also emerged. For instance, as much as sectarianism might be shrinking Iran's potential partnerships and client base in the Sunni community, it is also hardening Shia identity and could drive previously unreceptive Shia publics toward Iran's orbit. Iran has been the leading critic of the violent repression of Shia protesters in Bahrain and Saudi Arabia. Though Iranian influence appears scant in Saudi Arabia's unrest and is perhaps overstated in Bahrain's,<sup>176</sup> Iran has positioned itself as a willing patron for Shia movements in the region. The more the Shia are violently and politically oppressed in Arab Gulf states, the more Iran, as the only significant critic of such action, is seen in a positive light by Arab Shia communities. If such repression continues, Arab states run the risk of pushing their Shia communities closer to Iran—the precise outcome that their repression is meant to prevent. This would be a shift in orientation for the Arab Shia, who have long found the Islamic Republic's politicized religious ideology less attractive than the more traditional approaches to religion espoused by Arab clergy in Iraq and Lebanon.<sup>177</sup>

The fall of Ali Abdullah Saleh (Yemen's longtime president) in February 2012 and the growing disintegration of the Yemeni state also present opportunities for Tehran. Yemen has been part of Riyadh's sphere of influence for decades. Concerned with instability on their southern border, Saudi leaders have relied on broad patronage networks to prop up the government in Sanaa and enhance stability across Yemen. But with government control collapsing in the face of numerous challenges to state control—e.g., Al Qaeda in the Arabian Peninsula, the Houthi rebels in the north,

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<sup>176</sup> See Geneive Abdo, "The New Sectarianism: The Arab Uprisings and the Rebirth of the Shi'a-Sunni Divide," Saban Center for Middle East Policy at Brookings, Analysis Paper No. 29, April 2013.

<sup>177</sup> See Laurence Louer, *Transnational Shia Politics: Religious and Political Networks in the Gulf* (New York: Columbia University Press, 2008).

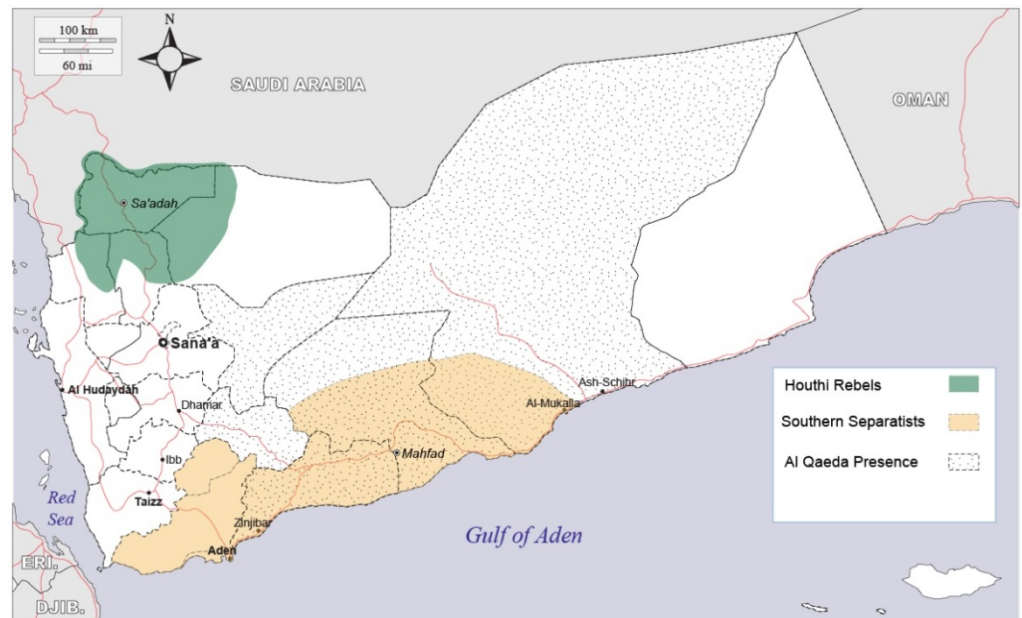
and a resurgent southern separatist movement (Hirak) in the south—Riyadh’s hold over Yemen is no longer a certainty. (See figure 8.) The breakdown of the Yemeni state seems to be providing greater space for Iran to operate in that country. Both Saleh and his successor, Ali Hadi, have been vocal critics of Iran and have regularly highlighted Iranian interference in Yemen in order to garner outside support from Riyadh and Washington.<sup>178</sup> But unlike in previous years, when Iranian influence in Yemen (particularly among the Houthis) seemed overblown, since the departure of Saleh Iran appears to be stepping up its involvement in Yemen, both with the Houthis and also possibly with the southern separatists as well.<sup>179</sup> Iran cannot replace Saudi Arabia as the dominant player in Yemen, but a more stable foothold there (via partnerships with the Houthis and southern Hirak movement) could give Tehran additional leverage in its ongoing and escalating rivalry with Riyadh.

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<sup>178</sup> See Barak A. Salmoni, Bryce Loidolt, and Madeleine Wells, *Regime and Periphery in Northern Yemen: The Huthi Phenomenon* (Santa Monica: RAND, 2010). Also see Silvana Toska, “Building a Yemeni State while losing a nation,” *Foreign Policy*, 28 October 2012, [http://mideast.foreignpolicy.com/posts/2012/10/28/building\\_a\\_yemeni\\_state\\_at\\_the\\_loss\\_of\\_a\\_nation](http://mideast.foreignpolicy.com/posts/2012/10/28/building_a_yemeni_state_at_the_loss_of_a_nation).

<sup>179</sup> International Crisis Group, “Yemen: Enduring Conflicts, Threatened Transition,” *Middle East Report*, no. 125, 3 July 2012. Also see Maria Abi-Habib, “Fears Grow Over Yemenis Ties to Iran,” *Wall Street Journal*, 20 Jun 2013, <http://online.wsj.com/article/SB10001424127887324904004578536884215565420.html>.

Figure 8. Broad look at zones of competition in Yemen



The situation in Syria is a more complex case for Iran. On the one hand, Syria's civil war has seriously damaged Iran's regional strategy and interests. It has embroiled the Assad regime (Iran's primary regional state ally) in a debilitating, bankrupting conflict. Hezbollah's involvement in the fight has undermined its position in Lebanon and threatens to return armed sectarian conflict to that country. Iran's support for Assad has alienated it from most of the region, harmed its relations to Sunni groups and states, and escalated Tehran's competition with Saudi Arabia and other Arab states. All are bad things for Tehran.

But despite these critical strategic losses, Iran could still gain in Syria should Assad's regime survive. Along with Russian support, Iran's backing has been vital for Assad's continued fight against the Sunni rebellion. Iran has provided loans and been a vocal supporter of Assad in international fora. Iran has supplied arms, shared intelligence, provided (via Qods Force units) logistical support and training for Assad's forces, and helped form pro-Assad paramilitary

militias.<sup>180</sup> Tehran has been instrumental in securing Hezbollah's involvement in the conflict, and seems to have similarly encouraged the participation of Iraqi militant groups.<sup>181</sup> Through these efforts it is likely that Iran's influence within the Assad regime has also grown. If Assad's regime survives, Iran's position in it will likely be larger than it was prior to the outbreak of armed conflict.

This will likely be true regardless of whether Syria remains intact as a single country. For example, so long as Assad (or a comparably pro-Tehran figure) remains at the helm of strategically important areas bordering Lebanon and Israel (including greater Damascus, the western coastline, and the mountains), Iran will retain many of the benefits that its partnership with Syria offered previously. However, in such a scenario, Iran would also likely have more influence over Syrian decision-making, and could have a relationship with Syrian pro-Assad militias similar to the one it has with Hezbollah and Iraqi groups such as the Hezbollah Brigades. Thus, even if a future Syria were weaker, Iran could have substantially more influence over it.

Finally, some of Iran's interests in Syria overlap with those of the United States. To be sure, both countries remain far apart in their expressed outcomes for the Syrian conflict. Iran wants the previous status quo of Assad's rule reestablished and the rebels defeated. Washington wants a political solution between the regime and the rebels, but one that likely does not include the Assad clique to remain in power. However, both countries want to prevent jihadists from finding a lasting home in Syria and do not want to see Al Qaeda establish itself as a player in any future Syrian political system. More generally, both Tehran and Washington also want to restore stability to Syria and stop the conflict from spreading beyond Syria's borders. While neither country is in the position to compromise on its current policies, it is possible that this shared goal could provide some

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<sup>180</sup> Sadjadpour, "Iran's Unwavering Support to Assad's Syria." Also see Farnaz Fassihi, Jay Solomon, and Sam Dagher, "Iranians Dial Up Presence in Syria," *Wall Street Journal*, <http://online.wsj.com/article/SB10001424127887323864604579067382861808984.html>.

<sup>181</sup> Smyth, "Iraqi Fighters in Syria."

pretext for diplomacy between Iran and America beyond the nuclear issue, or even play a part in an eventual political solution in Syria

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## Conclusion

The last few years have been difficult for the Islamic Republic. Between internal unrest, external pressure, and regional change, it has experienced perhaps the most turbulent period of its history since its war with Iraq. These factors not only have impacted Iran's sense of national security and economic welfare, they also have challenged Iran's strategy in the Middle East. Tehran has had to adapt to a rapidly changing region even as its sense of security has been compromised by outward attacks and sabotage. Its allies have become wrapped up in an increasingly sectarian war in Syria while its relations with its neighbors have become strained under the weight of political differences and hardening sectarian identities.

Iran has not been a passive observer to all of this. It has acted, at times hastily, in response to this turbulent strategic landscape. But its efforts to navigate the disorder and re-exert its interests have brought Tehran mixed results. Its campaign of bombing attempts against Israeli targets, and the plot to assassinate the Saudi ambassador to the United States, appeared rash and amateurish, and did not seem to enhance Iran's deterrence efforts against Tel Aviv and Washington, or to alter Riyadh's policies in Syria or Bahrain. Moreover, by using its own nationals in these operations, Iran put itself at further risk vis-à-vis its enemies and escalated tensions with its main rival. Iran's cyber-attacks seem to have achieved little but increased scrutiny and condemnation. Far from increasing its deterrence, Iran's actions in the covert realm have only bolstered the West's case against it.

Tehran's support for Assad and its actions in Syria have had less clear-cut results. Iran's backing of Assad has drawn widespread condemnation from its neighbors and most of the international community, with Russia and China the key exceptions. The evolution of the conflict into a largely sectarian war, combined with its vocal support for Shia pro-democracy movements in Bahrain and eastern Saudi Arabia, have cast doubt on Iran's intentions in the region, strained its ties to Hamas and Turkey, and further alienated it from its Arab neighbors. These outgrowths have harmed Iran's position in the

region and put at risk its broader deterrence efforts. Yet, should a semblance of Assad's Syria survive over the long term, Iran's influence in the Levant could grow in importance and value.

None of these actions have helped Iran's case in terms of sanctions relief. Sanctions have undermined one of the chief areas of mutually beneficial interaction between Iran and its neighbors in the Gulf. Just as they have wrought damage to Iran's economy, sanctions have stymied Iran's *strategic* efforts to engage with the region economically. Though Iran possesses great gas and petroleum reserves, sanctions have impeded it from using these resources to garner goodwill from its neighbors. Its actions in Syria, the rise in sectarianism in the region, and its reliance on covert operations have only hardened regional attitudes against Tehran.

Yet, Iran is showing signs of rethinking its approach. Most important, the election of Hassan Rouhani in June 2013 could be seen as a product of Iran's precarious situation. Although the election of Rouhani was outwardly the result of democratic will and the overwhelming desire for change among Iranian citizens, it could also signal a shift in thinking among Iran's top leadership. Because the presidency in Iran has generally not governed major strategic policy—at least not since Akbar Hashemi Rafsanjani held the position—it is not clear how much Rouhani's perspectives will impact Iranian strategic behavior. For one thing, Iran has so far offered no suggestion that its Syrian policy will change under Rouhani. Also, it is likely that Iran will not draw back its covert activities in the region or decrease its support for non-state clients.

The popular backing of Rouhani, however, could give the regime more political space to pursue less confrontational policies with Washington and regionally. If the supreme leader were to get buy-in from hardliner constituencies, particularly the IRGC, Rouhani could be empowered to further bolster its fragile diplomacy with the West and find areas of compromise that could earn sanctions relief for Iran. While Iran's track record, and political dynamics both there and in the West, might make such compromise seem unlikely, it could be that the precariousness of Iran's position is motivating it to seek more tenable solutions to its over-arching strategic problems. Rouhani's diplomatic efforts at the United Nations in September 2013, which culminated in a phone conversation between he and President

Barack Obama, and his reengagement in nuclear negotiations with the P5+1 are vivid testaments to this possibility.

Below are the major takeaways of this study. Our conclusions are not meant to be predictive or prognostications of the future; rather, they represent what we have gleaned from Iran's actions during this period and what these actions might indicate about Iran's strategic trajectory. If the Middle East has taught outside observers anything, it is that its future is far from sure.

- **Sanctions have taken a toll, and Iran is probably serious in its effort to seek sanctions relief.** The election of Hassan Rouhani has given Iran the space and opportunity to change tracks in its engagement with the West. It is quite possible that Rouhani will have suitable backing within the regime to offer some sort of compromise on Iran's enrichment program. But it is not yet clear that Iran is willing to go as far as the West requires. Short of dramatic concessions on its nuclear program, it is difficult to envision circumstances that could lead to the removal of economic sanctions on Iran.
- **Short of a mutually agreed upon political solution to the Syrian conflict, it will be difficult for Iran to regain goodwill from its Arab neighbors.** Economic interaction with GCC states was once an important part of Iran's strategy in the region. But sanctions, outside pressure, sharp political differences over Syria, and rising sectarianism have eroded Iran's ties to the Gulf. Absent areas of legitimate and productive interaction such as trade, the political ramifications of the Syrian conflict and metastasizing sectarianism in the region will continue to impact Iran's relations with its neighbors.
- **Iran will continue to rely on the pillars of its strategic activities to retain deterrent efforts against America and Israel, and will continue to compete with Saudi Arabia for regional influence.** Although Iran might be seeking sanctions relief via warmer political ties and interaction with the West, it remains at odds with Israel, the United States, and its Arab rivals on a number of issues. Thus, even with a constrained budget, Iran is unlikely to drastically change its military investments, posture, or activities in Gulf, particularly those aimed at deterrence. Its religious and information efforts will also likely remain

consistent with their present trajectory. Iran might also continue to expand its client base in places such as Yemen and perhaps in the Gulf in order to retain pressure on its neighbors. Yet, increasing sectarianism could make such activities riskier for Iran to pursue, especially in GCC countries. How Iran chooses to navigate that risk will likely depend on how it perceives external threats to its national security—the more immediate or intense Tehran feels outside threats to be, the more likely it will be to adopt more aggressive policies.

- **Iran will continue to rely on its partnerships with Syria and non-state actors such as Hezbollah to advance its interests in the Levant, challenge the influence of its rivals, and threaten Israel.** Syria is key to Iran's strategic efforts in the Middle East. Iran will not abandon its equities there easily and is likely to expand its role in Syria should the Assad regime survive. Moscow's support for Assad and its joint plan with Washington to secure Assad's chemical weapons arsenal provide cover and a certain degree of legitimacy for Iran's activities in Syria. It is unlikely that Iran will feel enough pressure to draw down its support for Assad as long as such international political cover exists. If the Syrian conflict devolves and begins to cost Iran increasing amounts of blood and treasure, then domestic pressure in Iran could begin to influence Tehran's policies toward Assad. But for the foreseeable future, Iran appears set to stay the course in Syria and is likely committed to supporting Assad even if Western powers (such as the United States) should enter the conflict militarily on the side of the rebels—something that Tehran must surely recognize as a fading possibility.
- **One area that might change is Iran's covert behavior.** The shift toward direct Iranian participation in kinetic activities outside Iran's borders (e.g., assassination attempts on Israeli and Saudi diplomats) was not successful, and continuing such an approach would not help Iran achieve sanctions relief. Therefore, it is possible that Iran might decelerate the type of covert operations that could de-rail diplomatic efforts under Rouhani in the short to mid term.
- **But Iran could return to provocative behavior if its diplomatic efforts fail and pressure increases.** That is, if Iran is unable to strike a deal with the West under Rouhani, sanctions continue,

and Iran's interests are slowly rolled back in the Levant through external support for the rebellion, Iran could resurrect a forward-leaning covert operations strategy that includes both violent activity and increased engagement with clients and partners that harm the interests of its enemies and rivals. Such behavior could also reemerge if hawks within Iran's security establishment (especially within the Qods Force and intelligence services) become hostile to and seek to scuttle any potential compromise between Tehran and Washington.

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# Appendix 1: Economic sanctions on Iran

## Summary of U.S. sanctions on Iran

U.S. sanctions on Iran date back to 1979, when President Jimmy Carter imposed certain sanctions in response to the Iranian hostage crisis.<sup>182</sup> President Reagan imposed additional sanctions after the Islamic Republic was implicated in the attack on the Marine barracks in Beirut in 1984 and Iran's subsequent designation as a state sponsor of terrorism. Congress and the executive branch continued to intensify sanctions against Iran throughout the 1980s with several congressional acts and executive orders.<sup>183</sup>

In 1992, the United States imposed the first sanctions targeting Iran's nuclear proliferation, with the Iran-Iraq Arms Non-Proliferation Act.<sup>184</sup> In 1995, an executive order banned all U.S. trade and investment in Iran.<sup>185</sup> Subsequently, in 1996, Congress passed the comprehensive "Iran Sanctions Act" (ISA),<sup>186</sup> which targeted Iran's energy sector, and authorized penalties against foreign entities that do business with Iran.<sup>187</sup> This act provided the mechanism by which

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<sup>182</sup> "Executive Order 12170—Blocking Iranian Government property," National Archives, <http://www.archives.gov/federal-register/codification/executive-order/12170.html>.

<sup>183</sup> "An overview of O.F.A.C. Regulations involving Sanctions against Iran," U.S. Department of the Treasury, <http://www.treasury.gov/resource-center/sanctions/Programs/Documents/iran.txt>.

<sup>184</sup> "Bill Summary & Status 102nd Congress (1991 - 1992) H.R.5006," The Library of Congress, <http://thomas.loc.gov/cgi-bin/bdquery/z?d102:HR05006>.

<sup>185</sup> "Executive Order 12959—Prohibiting Certain Transactions With Respect to Iran," Federal Register, <http://www.treasury.gov/resource-center/sanctions/Documents/12959.pdf>.

<sup>186</sup> Formerly the "Iran and Libya Sanctions Act."

<sup>187</sup> Text of H.R. 3107, Government Printing Office, <http://www.gpo.gov/fdsys/pkg/BILLS-104hr3107enr/pdf/BILLS-104hr3107enr.pdf>.

the executive branch can bring sanctions against specific firms through the issuing of executive orders.

When Iran's former president Mohamed Khatami was elected in 1997, the United States decreased the pressure, hoping to capitalize on an opportunity for rapprochement with Iran.<sup>188</sup> The failure of the two countries to reconcile, compounded by revelations of covert enrichment activities in Iran the early 2000s, led to a ratcheting up of sanctions under the more hawkish Bush administration. The "Iran Freedom Support Act" of 2006 strengthened ISA by imposing sanctions on any entity that sells WMD technology or materials, or a certain level of conventional weapons, to Iran.<sup>189</sup> Since the mid 2000s, the United States has been blacklisting Iranian banks and financial institutions, has barred U.S. firms from conducting transactions with banks that are doing business on behalf of Iran, and has tried to convince allies to do the same.<sup>190</sup>

The year 2010 brought about another period of increased economic pressure against Iran. Congress passed the Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA), which prohibits the sale of gas and other fuels to Iran worth over \$1 million at one time or \$5 million in a year. It also prohibits the sale of equipment or services that help Iran import gasoline.<sup>191</sup>

After a 2011 IAEA report revealed the possible military dimensions of Iran's nuclear program, congressional support for Iran sanctions grew, and the United States blacklisted the Central Bank of Iran (CBI).<sup>192</sup> An executive order in 2012 applied ISA sanctions to firms

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<sup>188</sup> Kenneth Katzman, *Iran Sanctions*, Congressional Research Service, <http://www.fas.org/sgp/crs/mideast/RS20871.pdf>.

<sup>189</sup> "Iran Freedom Support Act," U.S. Department of the Treasury, [http://www.treasury.gov/resource-center/sanctions/Documents/pl109\\_293.pdf](http://www.treasury.gov/resource-center/sanctions/Documents/pl109_293.pdf).

<sup>190</sup> Katzman, *Iran Sanctions*.

<sup>191</sup> "The Comprehensive Iran Sanctions, Accountability, and Divestment Act," U.S. Department of the Treasury, <http://www.treasury.gov/resource-center/sanctions/Documents/hr2194.pdf>.

<sup>192</sup> "U.S. Targets Iran's Central Bank," Wall Street Journal, 4 January 2012, <http://online.wsj.com/article/SB10001424052970204720204577132923798499772.html>.

that purchase oil or other petroleum or petrochemical products from Iran, or conduct business with either the National Iranian Oil Company (NIOC), or Naftiran Intertrade Company (NICO). However, foreign companies can earn an exemption waiver from the United States if they prove that over a specific period of time they have decreased their oil purchases from Iran. The same executive order also blocked transactions with Iran in precious metals.<sup>193</sup>

The “Iran Threat Reduction and Syria Human Rights Act,” passed in 2012, prohibits the sale of equipment to Iran that can be used to develop its energy sector. The act also imposes sanctions on owners of vessels used to transport Iranian oil;<sup>194</sup> prohibits new joint energy/resource ventures; places sanctions on insurance or reinsurance companies which serve NIOC or National Iranian Tanker Company or any vessel transporting WMD-related equipment or materials; prohibits anyone from purchasing debt from Iran; prohibits the provision of financial messaging services to blacklisted Iranian banks; and prohibits “significant transactions” by any entity with the Iranian Revolutionary Guard Corps (IRGC).<sup>195</sup>

The “Iran Freedom and Counter-Proliferation Act” (IFCA) of 2012 significantly intensified existing sanctions by targeting the entirety of Iran’s energy sector, its shipping and shipbuilding industry, ports, and any transfer of precious and semi-finished metals that can be used in connection with nuclear or ballistic missile programs. The act also prohibits the insurance or reinsurance of blacklisted Iranian entities; imposes sanctions on the state-run media; and imposes sanctions on those who impede the delivery of humanitarian goods to the Iranian people.<sup>196</sup>

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<sup>193</sup> “Executive Order 13622—Authorizing Additional Sanctions With Respect to Iran,” Government Printing Office, <http://www.gpo.gov/fdsys/pkg/DCPD-201200607/pdf/DCPD-201200607.pdf>.

<sup>194</sup> Except for those who have earned waivers.

<sup>195</sup> “H.R. 1905,” Government Printing Office, [http://www.treasury.gov/resource-center/sanctions/Documents/hr\\_1905\\_pl\\_112\\_158.pdf](http://www.treasury.gov/resource-center/sanctions/Documents/hr_1905_pl_112_158.pdf).

<sup>196</sup> “NDAA Bill (2012): Subtitle D,” U.S. Department of State, <http://www.state.gov/documents/organization/204023.pdf>.

In July 2013, Executive Order 13645 implemented the IFCA sanctions, but also introduced sanctions on firms that support Iran's automotive industry; prohibits firms from dealing in rials; and blocks the U.S. assets of any person who conducts transactions with blacklisted entities.<sup>197</sup> Later that month, just days before the inauguration of Iranian president Hassan Rouhani, the U.S. House of Representatives passed a bill which again intensified sanctions on Iran, this time targeting any transaction with the Central Bank of Iran and calling for sanctions on any individual who conducts a significant financial transaction with any entity directly or indirectly controlled by a blacklisted individual. The bill also called for further coordination with the European Union in order to restrict Iran's access to the euro.<sup>198</sup> The bill easily passed the House with a vote of 400 to 20,<sup>199</sup> but, at the time of writing, has yet to be voted on by the Senate.<sup>200</sup>

## UN Sanctions on Iran

While U.S. unilateral sanctions have been harmful to Iran, multilateral sanctions have generally been more effective in restricting Iran's economic activity. The United States has been a big supporter of UN sanctions, which all UN members are required to uphold. But despite U.S. pressure to bring harsh multilateral sanctions against Iran, the UN Security Council (UNSC) has passed only five resolutions concerning Iran's nuclear program.

The first resolution, UNSC Resolution 1696, passed in 2006, "demanded that Iran suspend all enrichment-related and reprocessing activities, including research and development, and gave it one month to do so or face the possibility of economic and

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<sup>197</sup> "Executive Order 13645 of June 3, 2013," Federal Register, <http://www.treasury.gov/resource-center/sanctions/Programs/Documents/13645.pdf>.

<sup>198</sup> "H.R.850 - Nuclear Iran Prevention Act of 2013," Congress.gov, <http://beta.congress.gov/bill/113th/house-bill/850>.

<sup>199</sup> "Final Vote Results for Roll Call 427," House Clerk, <http://clerk.house.gov/evs/2013/roll427.xml>.

<sup>200</sup> "H.R.850 - Nuclear Iran Prevention Act of 2013," Congress.gov.

diplomatic sanctions.”<sup>201</sup> The resolution was passed by a vote of 14-1, with Qatar voting against the resolution.

Resolution 1737, which the UNSC passed later that same year after Iran failed to comply, bans the sale of nuclear-related technology and supplies to Iran. It also imposed a travel ban and froze the assets of specific individuals suspected of involvement with Iran’s nuclear and ballistic missile programs.<sup>202</sup>

In 2007, the UNSC blacklisted more individuals and entities through Resolution 1747. The resolution also stipulates that no loans or financial assistance could be extended to Iran, aside from humanitarian and developmental aid. Further, the resolution bans Iranian arms exports and imposes a conventional arms embargo.<sup>203</sup>

In 2008, additional individuals and entities were blacklisted in Resolution 1803, which also called on states to inspect cargo coming to or from Iran, and called upon “all States to exercise vigilance in entering into new commitments for public provided financial support for trade with Iran.... in order to avoid such financial support contributing to the proliferation sensitive nuclear activities, or to the development of nuclear weapon delivery systems.”<sup>204</sup>

The strictest sanctions imposed by the United Nations came in 2010 with the passing of Resolution 1929. The resolution bans Iranian investment in certain foreign nuclear and missile projects; imposes a conventional arms ban, as well as a ban on ballistic missile activities;

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<sup>201</sup> “Security Council Demands Iran Suspend Uranium Enrichment By 31 August, Or Face Possible Economic, Diplomatic Sanctions,” Department of Public Information, United Nations, 31 July 2006, <http://www.un.org/News/Press/docs/2006/sc8792.doc.htm>.

<sup>202</sup> “Resolution 1737 (2006),” United Nations, 26 December 2006, [http://www.un.org/ga/search/view\\_doc.asp?symbol=S/RES/1737\(2006\)](http://www.un.org/ga/search/view_doc.asp?symbol=S/RES/1737(2006)).

<sup>203</sup> “Resolution 1747 (2007),” United Nations, 24 March 2007, [http://www.iaea.org/newscenter/focus/iaeaيران/unsc\\_res1747-2007.pdf](http://www.iaea.org/newscenter/focus/iaeaيران/unsc_res1747-2007.pdf).

<sup>204</sup> “Resolution 1803 (2008),” United Nations, 3 March 2008, [http://www.iaea.org/newscenter/focus/iaeaيران/unsc\\_res1803-2008.pdf](http://www.iaea.org/newscenter/focus/iaeaيران/unsc_res1803-2008.pdf).

bans additional nuclear-related equipment; tightens cargo inspection system and laws concerning seizure of banned goods; freezes Iranian assets that could contribute to proliferation; and limits banking relations and transactions with the Islamic Revolutionary Guards Corps (IRGC).<sup>205</sup>

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<sup>205</sup> “Resolution 1929 (2010),” United Nations, 9 June 2010, [http://www.iaea.org/newscenter/focus/iaecairan/unsc\\_res1929-2010.pdf](http://www.iaea.org/newscenter/focus/iaecairan/unsc_res1929-2010.pdf).

## Appendix 2: Iran's regional trade

### Trade with GCC countries

The United Arab Emirates (UAE), and particularly the emirate of Dubai, and Iran have a long history of trade. The UAE is home to hundreds of thousands of Iranian nationals and people of Iranian origin, many of whom reside in Dubai.<sup>206</sup> While Iran makes up only a very small percentage of the UAE's overall trade (only 3.1% of documented exports and 0.6% of imports in 2008),<sup>207</sup> the UAE has, over the past decade, served as a base from which to skirt sanctions and re-export goods to and from Iran, and therefore plays a large role in the Iranian economy. Further, small boats known as "dhows" park in Dubai's ports at night, smuggling goods to and from Iran relatively undeterred.<sup>208</sup> When the UAE compelled its banks to comply with United Nations sanctions in 2010, the Iranian rial experienced a nearly instant 15-percent drop in value,<sup>209</sup> illustrating the importance of the UAE to the Iranian economy.

Dubai's relatively close economic relationship with Iran stands in contrast to Abu Dhabi's relationship. Abu Dhabi, the seat of the

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<sup>206</sup> Leila Hatoum, "U.A.E. Seeks Ways to Fund Iran Trade," *Wall Street Journal*, 19 March 2012, <http://online.wsj.com/article/SB10001424052702304636404577291603135859254.html>.

<sup>207</sup> Most of the statistical information cited in this study is from the International Trade Centre, a United Nations-associated organization. Its data can be accessed online via the organization's website: <http://legacy.intracen.org/marketanalysis/Default.aspx>.

<sup>208</sup> Kambiz Foroohar, "Dubai Helps Iran Evade Sanctions as Smugglers Ignore U.S. Laws," *Bloomberg*, 25 January 2010, [http://www.bloomberg.com/apps/news?pid=newsarchive&sid=av5smtYe\\_DDA](http://www.bloomberg.com/apps/news?pid=newsarchive&sid=av5smtYe_DDA).

<sup>209</sup> "Sanctions Begin to Bite," *Economist*, 7 October 2010, <http://www.economist.com/node/17204603>.

government of the UAE, has long feared a nuclear Iran and has pursued a closer relationship with the United States. Until 2009, Abu Dhabi and Dubai had a tenuous power-sharing dynamic. However, since Abu Dhabi bailed Dubai out of a disastrous economic crisis in 2009, Abu Dhabi has had the upper hand.<sup>210</sup> The result is an increasingly anti-Iran policy and further compliance with United Nations sanctions.

The year 2010 appears to have been a turning point for trade between the UAE and Iran. With intensified international sanctions against Iran, a weakened Dubai, and an Emirati economy that wanted to be able to do business with the United States, interactions between the UAE and Iran seemed to be rapidly deteriorating.<sup>211</sup> In December 2011, Dubai's Noor Islamic Bank, which was once a main conduit for Iranian oil money, ceased doing business with Iran.<sup>212</sup> In March 2012, major money exchange houses in the UAE stopped dealing in rials completely, in part due to the volatility of the currency.<sup>213</sup> UAE government officials contend that Iranian banks still operating within the UAE are only able to conduct transactions in cash, making it much more difficult to do business.<sup>214</sup> In addition, it is reportedly very difficult for Iranian traders to get financing for shipping.<sup>215</sup> UAE

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<sup>210</sup> Mohammed Assadi, "Dubai crisis over, UAE united – Formin," Reuters, 17 December 2009, <http://in.reuters.com/article/2009/12/17/idINIndia-44809320091217>.

<sup>211</sup> While UAE-Iran trade has certainly been declining, UN Comtrade statistics depict a significant increase in trade from 2010 to 2011. Michael Singh, Senior Fellow at the Washington Institute for Near East Policy, suggested in a September 2013 conversation with the authors that the growth is likely due to an increase in the price of exports (and re-exports) and not an increase in the volume of trade.

<sup>212</sup> Martina Fuchs, "Major UAE currency houses halt Iran rial business," Reuters, 15 March 2012, <http://www.reuters.com/article/2012/03/15/dubai-iran-currency-idUSL5E8EC6RB20120315>.

<sup>213</sup> Ibid.

<sup>214</sup> Kenneth Katzman, *Iran Sanctions*.

<sup>215</sup> Tom Arnold, "Iran Sanctions Hurt Dubai Trade," *The National*, 17 February 2012, <http://www.thenational.ae/business/industry-insights/economics/iran-sanctions-hurt-dubai-trade>.

companies have claimed that the web of sanctions is so complicated and difficult to understand that many companies have ceased to process any payment from Iran, out of fear of noncompliance.<sup>216</sup>

Trade between Dubai and Iran fell from 36 billion dirhams in 2011 to 25 billion dirhams in 2012.<sup>217</sup> Re-exports to Iran from the UAE also dropped by nearly a third in the first half of 2012.<sup>218</sup> However, this drop in trade had only a minimal effect on Dubai, whose economy grew 4 percent in 2012, compared to 4.3 percent in 2011.<sup>219</sup>

Several Emirati companies continue to do business with Iran. Emirates National Oil Company is accused of importing oil from Iran and refining it into jet fuel for use in the UAE's rapidly expanding aviation industry.<sup>220</sup> Two Emirati companies, Al Hilal Exchange and Al Fida International General Trading, have recently been sanctioned by the United States for doing business with Iran, and are therefore barred from doing business with the United States.<sup>221</sup> Other, smaller firms have also been sanctioned by the United States for selling gas to Iran.<sup>222</sup>

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<sup>216</sup> Colin Simpson, "UAE businesses to feel effect of fresh US sanctions on Iran," *The National*, 3 July 2013, <http://www.thenational.ae/news/uae-news/uae-businesses-to-feel-effect-of-fresh-us-sanctions-on-iran>.

<sup>217</sup> Martin Dokoupil, "Dubai's trade with Iran shrinks a third in 2012," Reuters, 25 March 2013, <http://www.reuters.com/article/2013/03/25/dubai-iran-trade-idUSL5N0CH1SI20130325>.

<sup>218</sup> Tom Arnold, "Dubai traders call for relief on Iran exports," *The National*, 3 January 2013, <http://www.thenational.ae/business/industry-insights/economics/dubai-traders-call-for-relief-on-iran-exports>.

<sup>219</sup> Ibid.

<sup>220</sup> Katzman, *Iran Sanctions*.

<sup>221</sup> Julian Hattem, "UAE financial firms hit with sanctions for aiding Iranian banks," *The Hill*, 15 May 2013, <http://thehill.com/blogs/regwatch/finance/299873-uae-financial-firms-hit-with-sanctions-for-aiding-iranian-banks>.

<sup>222</sup> Kenneth Katzman, *The United Arab Emirates (UAE): Issues for U.S. Policy*, Congressional Research Service, 18 June 2013, <http://www.fas.org/sgp/crs/mideast/RS21852.pdf>.

While the UAE has certainly made itself much less hospitable to Iranian business, the country is reluctant to cut off Iran outright. The royal family seems to want to pursue better relations with the United States by cooperating on sanctions without provoking Iran or fully denying Dubai the economic benefits of doing business with Iran. For example, the UAE refuses to shut down Bank Melli or Bank Saderat, two Iranian banks that are heavily sanctioned by the United States, but the UAE has taken away their ability to do business in rials, rendering the banks essentially inactive.<sup>223</sup>

While trade with Iran was increasing through 2011, it was increasing at a slower pace than in the early 2000s, and likely decreased into 2012 and 2013. Even so, Abu Dhabi will likely continue to walk a fine line between cooperating with the West and allowing Dubai to pursue the economic benefits of doing business with Iran.

The other GCC countries also conduct a small portion of their overall trade with Iran. Saudi Arabia, with which Iran has always had a tenuous relationship, imported only \$74 million in goods from Iran in 2011, out of a total of \$131 billion in imports.<sup>224</sup> Saudi Arabia has cooperated with the United States and its sanctions on Iran, and has played a critical role by agreeing to fill the void in production left by Iran, assuring countries that are decreasing their consumption of Iranian oil that they will be able to meet their consumption needs by other means.<sup>225</sup>

Kuwait has also decreased its trade with Iran. In 2010, trade between the two countries was around \$213 million, and, while Iran claimed that bilateral trade with Kuwait had the potential of exceeding \$500

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<sup>223</sup> Ibid.

<sup>224</sup> International Trade Centre data.

<sup>225</sup> Kenneth Katzman, *Iran: U.S. Concerns and Policy Responses*, Congressional Research Service, 17 June 2013, <http://www.fas.org/sgp/crs/mideast/RL32048.pdf>.

million in the succeeding years,<sup>226</sup> trade dropped to \$200 million in 2011.<sup>227</sup>

Bahrain has a problematic relationship with Iran, as it accuses the Islamic Republic of fomenting revolution within Bahrain through its support of Shia opposition groups. However, some trade between the two countries continues, as Bahrain does not want to antagonize Iran.<sup>228</sup> Iranian exports to Bahrain rose steadily from \$22 million in 2004 to \$70 million in 2006, but then dropped to \$11 million by 2011.<sup>229</sup> This may in part be due to Iran's role, or perceived role, in Bahrain's domestic crisis, in addition to cooperation with sanctions.

There are few areas in which Bahrain seems to be cooperating with Iran. Bahrain's Future Bank is partially owned by Bank Melli and is therefore subject to U.S. sanctions.<sup>230</sup> Further, in 2007 the two countries discussed building a shared gas pipeline, and only a diplomatic row (after an Iranian official claimed Bahrain as Iran's "14<sup>th</sup> province") caused the suspension of the deal.<sup>231</sup> However, Bahrain does seem to be decreasing its trade with Iran overall, and in 2012 even confiscated carbon fiber it found on a ship bound for Iran,<sup>232</sup> proving that the kingdom is somewhat willing to comply with sanctions even if it means antagonizing Iran to some degree.

Of all the GCC states, Oman boasts the closest relationship to Iran. Oman has thus far maintained a normal trade relationship with Iran,

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<sup>226</sup> Geoffrey Kemp, *War with Iran: Political, Military, and Economic Consequences* (Lanham: Rowman and Littlefield Publishers, 2013).

<sup>227</sup> International Trade Centre data.

<sup>228</sup> Kenneth Katzman, *Bahrain: Reform, Security, and U.S. Policy*, Congressional Research Service, 16 July 2013, <http://www.fas.org/sgp/crs/mideast/95-1013.pdf>.

<sup>229</sup> International Trade Centre data.

<sup>230</sup> Katzman, *Bahrain: Reform, Security, and U.S. Policy*.

<sup>231</sup> Tamsin Carlisle, "Iran-Bahrain Project Off Again," *The National*, 23 May 2011, <http://www.thenational.ae/business/energy/iran-bahrain-gas-project-off-again>.

<sup>232</sup> "UAE, Bahrain Confiscate Items Bound for Iran," *CBS News*, 19 September 2012, [http://www.cbsnews.com/8301-202\\_162-57516065/uae-bahrain-confiscate-items-bound-for-iran/](http://www.cbsnews.com/8301-202_162-57516065/uae-bahrain-confiscate-items-bound-for-iran/).

and the United States has repeatedly accused Oman of turning a blind eye to the smuggling of goods in and out of Iran.<sup>233</sup> Various interviews with Omani businessmen indicate that Iranians are regularly travelling to the UAE, placing orders, and having their orders shipped to the Omani port of Khasab, from which point they are forwarded on “duty free” to Iran, just 30 miles away.<sup>234</sup> Oman and Iran have also jointly developed the Hengham oil field in the Persian Gulf, which was officially completed in July 2013 and produces 30,000 barrels of oil a day.<sup>235</sup>

While Omani news outlets report booming Iran-Oman trade in 2012, there are signs that sanctions are also taking their toll. The Omani government claims to comply with UN sanctions, but it has not mandated the U.S. ban on bank financing of trade. Even so, many Omani banks are choosing not to extend line of credits to Iranian businessmen because they feel they are unlikely to be paid back. Iranian traders are reportedly relying on private loans from Omani businessmen in order to finance their shipments.<sup>236</sup> Omani exports to Iran, however, make up only 2 percent of its total exports. Trade between the two countries increased heavily in 2010, but decreased slightly in 2011<sup>237</sup>—and these are only official, reported exports. The *Muscat Daily* reported that bilateral trade reached \$250 million

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<sup>233</sup> Kenneth Katzman, *Oman: Security, Reform, and U.S. Policy*, Congressional Research Service, 12 July 2013, <http://www.fas.org/sgp/crs/mideast/RS21534.pdf>.

<sup>234</sup> Juliane von Mittelstaedt, “Smuggler's Paradise: Iran Sanctions Good for Business in Tiny Omani Port,” *Der Spiegel*, 20 January 2012, <http://www.spiegel.de/international/world/smuggler-s-paradise-iran-sanctions-good-for-business-in-tiny-omani-port-a-810165.html>.

<sup>235</sup> “Hengam Oil and Gas Field, Persian Gulf, Iran,” *Offshore Technology*, <http://www.offshore-technology.com/projects/-hengam-oil-gas-field-persian-gulf/>.

<sup>236</sup> Saleh Al-Shaibany, “Even in Oman, Iran traders feel sanctions pinch,” Reuters, 16 February 2012, <http://www.reuters.com/article/2012/02/16/oman-iran-trade-idUSL5E8DG09R20120216>.

<sup>237</sup> International Trade Centre data.

between the two countries in the fiscal year ending March 2013,<sup>238</sup> almost double the amount reported in 2011.<sup>239</sup> Oman and Iran are likely to maintain a close trade relationship, but it may become even more informal and even illegal as Omani financial institutions find the cost of doing business with Iranians to be very high.

While Iranians are finding the Gulf a much less hospitable place to do business, trade with the GCC countries continues, much of it informally. GCC countries are hesitant to antagonize or provoke Iran, but financial institutions are realizing that there is high risk and an increasing cost to doing business with Iran. While trade is not likely to decrease significantly between these traditional partners in the near term, it is also not growing significantly, even as Iran seeks to make deals and offer discounts. Rather, Iran has had to seek out new strategic partners with which to trade, and Iranians are no longer able to rely on their Gulf neighbors as stable economic partners.

## Trade with the Levant

Lebanon and Syria are both important strategic partners for Iran. Although the trade volume between Iran and each of those two countries is small relative to Iran's total trade, both countries still play an important role in Iran's economic position.

As of 2012, Syria ranked 42<sup>nd</sup> of all Iran's import partners and 10<sup>th</sup> of all its export partners.<sup>240</sup> In 2011, Iran imported less than \$26 million from Syria and exported \$400 million to Syria (total Iranian exports were \$130 billion that same year).<sup>241</sup> These numbers make up just a small part of Iranian trade. Nonetheless, discussions of economic cooperation and joint ventures play an important role in bolstering

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<sup>238</sup> "Oman-Iran Bilateral Trade Reaches \$250 Million," *Muscat Daily*, 23 June 2013, <http://www.muscatdaily.com/Archive/Business/Oman-Iran-bilateral-trade-reaches-250mn-2cv8>.

<sup>239</sup> International Trade Centre data.

<sup>240</sup> "Iran: EU Bilateral Trade and Trade with the World," The European Commission, 5 July 2013, [http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc\\_113392.pdf](http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113392.pdf).

<sup>241</sup> International Trade Centre data.

the image of Syria and Iran's strategic partnership. Syria and Iran signed a Free Trade Agreement in 2011,<sup>242</sup> and the head of the Syrian Investment Agency (a government body) was quoted as saying, "It's logical why we have been working much closer with the Iranians, we're both under the American blockade."<sup>243</sup> The Iranians and Syrians take their economic partnership very seriously, as they see it as a form of resisting Western pressure.

Additionally, Iran has invested very heavily in Syria. In 2006, its direct investment in Syria totaled \$400 million.<sup>244</sup> The crisis in Syria, which began in March 2011, has not deterred Iranian investment, and has actually bolstered it. Iran has twice extended lines of credit to Syria worth \$1 billion and \$3.6 billion with which to purchase Iranian goods.<sup>245</sup> In return, Iran hopes to lay claim to equity, which it hopes will pay out after the war in Syria ends.

Lebanon has a similar economic relationship with Iran. While trade volume between the two countries is relatively small (Iran's exports to Lebanon totaled only \$38 million in 2012),<sup>246</sup> the economic partnership between the two countries is strategically significant. The two countries set up a joint economic commission in 2003 and have

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<sup>242</sup> See "Iran-Syria free trade agreement takes effect," *Tehran Times*, 28 April 2012, <http://www.tehrantimes.com/economy-and-business/97320-iran-syria-free-trade-agreement-takes-effect>; also, "Iranian lawmakers pass Syria free trade bill in show of support," *Daily Star*, 14 December 2011, <http://www.dailystar.com.lb/Business/Middle-East/2011/Dec-14/156821-iranian-lawmakers-pass-syria-free-trade-bill-in-show-of-support.ashx#axzz2bihaEJ5T>.

<sup>243</sup> Hugh Naylor, "Syria, Seeking Investors, Turns Cautiously to Iran," *New York Times*, 4 October 2007, <http://www.nytimes.com/2007/10/04/world/middleeast/04syria.html>.

<sup>244</sup> Ibid.

<sup>245</sup> See Michael Peel, "Iran gives Syria \$1bn import credit line," *Financial Times*, 16 January 2013, <http://www.ft.com/cms/s/0/c0266202-600c-11e2-b657-00144feab49a.html#axzz2bijRZxTV>; also, Suleiman Al-Khalidi, "Iran grants Syria \$3.6 billion credit to buy oil products," Reuters, 31 July 2013, <http://www.reuters.com/article/2013/07/31/us-syria-crisis-iran-idUSBRE96U0XN20130731>.

<sup>246</sup> International Trade Centre data.

issued dozens of memoranda of understanding.<sup>247</sup> However, as in Syria, Iran has gone to great lengths to invest in infrastructure with the intent of maintaining a close strategic partnership. To that end, Iran reportedly gives \$200 million in aid annually to the Lebanese Shiite group Hezbollah.<sup>248</sup>

While trade with the two countries may not be large, and is even decreasing over time, both Syria and Lebanon play an important strategic role for Iran. By investing large amounts of money in both countries, Iran is hoping to wield influence and invest in strategic partnerships, even though the Islamic Republic knows the investments are not likely to bring them cash in the near term.

## Trade with Iraq

Iraq plays a very important economic role for Iran and helps it skirt energy and banking sections as a trade partner. According to the International Trade Centre, Iran's exports to Iraq reached \$4 billion in 2011, around 12 percent of Iran's total exports for that year.<sup>249</sup> According to some Iranian news media, trade between the two countries surpassed \$6.5 billion in 2012.<sup>250</sup> The Trade Promotion Organization of Iran also claimed that 72 percent of Iran's exports go to Iraq, and revealed that Iraq's imported goods from Iran increased by nearly 15 percent this year.<sup>251</sup> While these figures are likely exaggerated, they illustrate the upward trajectory of Iran-Iraq trade.

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<sup>247</sup> "Iran-Lebanon joint economic commission slated for October: envoy," *Tehran Times*, 20 September 2011, <http://www.tehrantimes.com/economy-and-business/2766-iranlebanon-joint-economic-commission-slated-for-october-envoy>.

<sup>248</sup> Viola Gienger, "Iran Gives Weapons, \$200 Million a Year to Help Lebanese Hezbollah Re-Arm," *Bloomberg*, 20 April 2010, <http://www.bloomberg.com/news/2010-04-19/iran-helps-lebanese-hezbollah-rebuild-its-arsenal-pentagon-says-in-report.html>.

<sup>249</sup> International Trade Centre data.

<sup>250</sup> "Iran-Iraq Trade Hits \$6.3b," *Tehran Times*, 24 June 2013, <http://www.tehrantimes.com/economy-and-business/108739-iran-iraq-trade-hits-63b->.

<sup>251</sup> Omar al-Shaher, "Iraq: Iran's Economic Gateway to the World," *Al Monitor*, 28 June 2013, <http://www.al->

And their relationship extends beyond trade: in July 2013, Iraq signed a deal to import natural gas from Iran, which will feed 850 million cubic feet of gas to three power stations in Iraq. An Iranian company, Iran Consulting Group, was awarded the \$365 million contract to build the pipeline.<sup>252</sup>

Iraqi banks have been sanctioned by the United States—and then unsanctioned when they have complied<sup>253</sup>—and Iraq has been accused of allowing Iran to use its air space to send weapons to Syria. For Iraq, Iran is a very cheap and convenient trade partner at a time when the country is in need of cash. For Iran, Iraq is a convenient and large market for its overabundance of exportable goods. While economic cooperation will be limited by the two countries' historical and continuing fight for regional hegemony, it is likely that both countries will continue to further their trade and economic cooperation to the extent that both sides can earn cash and other tangible benefits from doing so.

## Trade with Afghanistan

In 2004 Iranian trade with Afghanistan exceeded \$235 million; in 2011, the value had climbed to over \$1.8 billion—almost all from Iranian exports to Afghanistan.<sup>254</sup> And the cooperation isn't limited to trade. In July 2013, the Afghan government announced that it was working on a deal to use one of Iran's ports to export goods.<sup>255</sup> The next month, Iran announced that it would be holding a three-day

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monitor.com/pulse/originals/2013/06/iraq-iran-economic-gateway-sanctions-tehran.html.

<sup>252</sup> "Iraq signs deal to import Iranian gas for power," Reuters, 22 July 2013, <http://www.reuters.com/article/2013/07/22/iraq-iran-gas-idUSL6N0FS14F20130722>.

<sup>253</sup> Katzman, *Iran: U.S. Concerns and Policy Responses*.

<sup>254</sup> International Trade Centre data.

<sup>255</sup> "Afghanistan eyes Iran deal to boost trade to Europe, India," Reuters, 29 July 2013, <http://in.reuters.com/article/2013/07/29/afghanistan-exports-india-iran-idINDEE96R04Z20130729>.

expo in Afghanistan to showcase its goods.<sup>256</sup> The Afghan ambassador in Tehran claimed that 500 Iranian companies are now operating in Afghanistan, while other analysts put the number much higher.<sup>257</sup>

Illustrating just how intertwined these two economies are, Afghanistan has suffered from unintended consequences of Iranian sanctions in two crucial ways. First, the remittances that Afghanistan once heavily relied on from expats in Iran are no longer worth very much. Further, as unemployment in Iran increases, Afghan workers are being sent back to Afghanistan after 10, 20, or even 30 years of living and working in Iran. Second, Iranian companies, hurting under the pressure of sanctions, are flooding the Afghan market with cheap goods that undermine local businesses.<sup>258</sup>

Iranian influence is especially felt in the Afghan city of Herat, just an hour from the Iranian border. There, Iran has funded the electricity grid, and built roads, schools, industrial parks, and other critical infrastructure<sup>259</sup>—just one part of the \$500 million in aid it has given to Afghanistan to date.<sup>260</sup> In fact, the United States set up an “Iran watch” office in Herat to counter the Iranian influence being spread there.<sup>261</sup>

However, there are signs that Iranian influence is beginning to wane as local Afghan communities push back. In December 2012, Iranian

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<sup>256</sup> “Iran to hold food and goods expo in Afghanistan,” *Tehran Times*, 17 August 2013, <http://tehrantimes.com/economy-and-business/110053-iran-to-hold-foods-and-goods-expo-in-afghanistan>.

<sup>257</sup> *Ibid.*

<sup>258</sup> Maria Abi-Habib, “Iran Sanctions Take Toll on Afghans,” *Wall Street Journal*, 22 July 2012, <http://online.wsj.com/article/SB10000872396390444330904577539000025751884.html>.

<sup>259</sup> Laura King, “In western Afghan city, Iran makes itself felt,” *Los Angeles Times*, 13 November 2010, <http://articles.latimes.com/2010/nov/13/world/la-fg-afghanistan-iran-20101114>.

<sup>260</sup> Kenneth Katzman, *Afghanistan: Post-Taliban Governance, Security, and U.S. Policy*, Congressional Research Service, 25 June 2013, <http://www.fas.org/sgp/crs/row/RL30588.pdf>.

<sup>261</sup> *Ibid.*

news media reported that Iran had to close its consulate in Herat after anti-Iranian protestors attacked it.<sup>262</sup> Further, Afghans are complaining that Iran has failed to maintain much of the infrastructure that it has built, leaving it dilapidated and unusable. Afghans have increasingly perceived Iran as meddling in their domestic affairs, playing both sides of the internal conflict, and using Afghanistan as a tool.<sup>263</sup>

## Trade with China, India, and Turkey

As trade with neighboring countries and traditional economic partners has decreased or stalled altogether, Iran has had to seek out other destinations for its exports. Its traditional trading partners in the Gulf are not eager to increase trade, and doing business in those countries is becoming increasingly difficult: Syria, Iran's main regional ally, is in the midst of civil war that has lasted two and a half years; Lebanon's economy, in which Iran heavily invests, is not productive enough to pay significant cash dividends (although it may pay strategic dividends); Iraq, while willing to cooperate with Iran, faces increasing pressure from the international community to stop doing so; and Afghanistan, long an economic partner for Iran, is beginning to push back against Iran's meddling and is hedging between the two competing sides.

Strapped for cash in such an adverse climate, Iran has had to rely increasingly on partners that are less dependent on the United States and can be tempted by offers of discounts and bartering deals. In addition to domestic economic policy reform and a new focus on non-oil goods, Iran has reoriented its international trade to rely on

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<sup>262</sup> "Iran shuts consulate in Herat until further notice," *Press TV*, 11 December 2012, <http://www.presstv.com/detail/2012/12/11/277452/iran-shuts-consulate-in-herat/>.

<sup>263</sup> Scott Peterson, "How much influence will Iran have in post-US Afghanistan?" *Christian Science Monitor*, 5 August 2013, <http://www.csmonitor.com/World/Asia-South-Central/2013/0805/How-much-influence-will-Iran-have-in-post-US-Afghanistan>.

South and Central Asia—specifically, China, India, Turkey, Turkmenistan, and Kazakhstan.

In 2006, Iran exports to China were worth \$992 million. Just five years later, they were worth over \$5 billion—more than a five-fold increase.<sup>264</sup> Iran exported \$320 million to Turkey in 2006, but just five years later surpassed \$1.4 billion in exports to the same market.<sup>265</sup> According to Iranian news media, Iran increased bilateral trade with Turkmenistan from \$1.3 billion in 2006 to \$5 billion in 2013. Iran is now Turkmenistan's second largest trade partner after Russia.<sup>266</sup> India's imports from Iran increased from \$177 million in 2002, to \$895 million in 2006, to \$2.6 billion in 2011.<sup>267</sup> In 2002, India made up less than half of 1 percent of Iran's exports; in 2011, it made up about 2 percent.<sup>268</sup> While this may not seem like a lot, there are signs that it will increase.

China and India have both agreed on a discounted price for Iranian oil, and have set up domestic accounts at state-owned banks that will house the payments for oil, to be used by Iran to buy domestic goods. This barter system may entice countries such as India and China to keep buying from Iran, but only if Iran can cease its inflammatory behavior. In August 2013, Iran seized an Indian ship in the Gulf's international waters and coerced it back to an Iranian port, claiming that it was polluting the waters and asking for payment for the damage done. Some suspect that the ship was detained because it carried oil from Iraq.<sup>269</sup> Provocations such as this could hinder future India or China future cooperation with Iran—thereby further limiting the destinations to which Iran can send its oil.

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<sup>264</sup> International Trade Centre data.

<sup>265</sup> Ibid.

<sup>266</sup> "Iran, Turkmenistan trade transactions to rise to \$10 billion," *Press TV*, 19 July 2013, <http://www.presstv.ir/detail/2013/07/19/314616/iran-turkmenistan-eye-10bn-trade-volume/>

<sup>267</sup> International Trade Centre data.

<sup>268</sup> Ibid.

<sup>269</sup> Sachin Parashar, "Iran seizes Indian ship carrying oil from Iraq," *Times of India*, 15 August 2013, [http://articles.timesofindia.indiatimes.com/2013-08-15/india/41412731\\_1\\_hormuz-indian-ocean-irgc](http://articles.timesofindia.indiatimes.com/2013-08-15/india/41412731_1_hormuz-indian-ocean-irgc).

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