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TURQUOISE PARTNERS

Nader Shah's Tomb and Museum, Mashhad

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Following the exceptional performance and unprecedented growth of the Tehran Stock Exchange (TSE) over the past few months, January marked a change to this positive trend and the TSE All-Share Index lost 3.4% of its value in Rial terms. This proved to be TSE's lowest performance in the past six months. The rapid increase in stock prices, relative stability in the prices of metal and petrochemical products on the Iran Mercantile Exchange (IME), as well as the implementation of controlling policies by the Securities and Exchange Organization (SEO) authorities were the three main factors behind the reversal of the market's bullish sentiment. However, by considering the fundamental factors supporting stock prices (particularly the continuation of foreign currency appreciation), the recent price corrections cannot necessarily be viewed as a sustainable change in the growing trend of stock prices. Therefore, the persistence of positive parameters affecting the profitability of companies such as further increases in the value of foreign currency, and consequently further growth in the sale prices of mineral, metal and petrochemical producers on the IME, would encourage investors to inject fresh liquidity into the stock market.

Some of the key events and sectors of the stock market will be examined below:

TSE's recent actions

TSE's outstanding performance in recent months which resulted in an average growth of 55% in 2012, stabilized through undergoing some corrections. In January, the Securities and Exchange Organization (SEO) stepped in and suspended the tickers of six companies in the petrochemical and refinery sector. The SEO announced that the suspension was due to further financial clarifications being required by these companies. Many however believe that this action was aimed at controlling the unprecedented jump in the stock prices. According to some analysts, the SEO's direct intervention in suspension of tickers is not considered a sustainable approach. Instead, developing professional market makers who can stabilize the supply and demand when market fever runs high, is perceived to be a more effective approach. As its second step to manage the stock markets' continuous soaring trend, the SEO authorities began strict supervision of the bank credits granted to clients by brokerage firms. During recent months, brokerage firms received bank credits exceeding twice their capital. According to unofficial reports, following the SEO's interference, the amount of credit offered to brokerage firms was limited by 50% in January. The aggregated result of these events was that the market rally lost its momentum and the demand for stocks fell sharply during this month. The market has now stagnated and prices are readjusting to levels some analysts would deem more appropriate to current market conditions.

Nine month reports of leading sectors

In January, TSE investors were presented with nine month corporate earnings announcements. These reports are scrutinized and taken very seriously by investors as they are mandatorily audited prior to publishing and seen as being a reliable source of information. The reports shown different results in various sectors of the market. In the base metals sector, the two largest players, National Iranian Copper Company (NICIC) and Mobarakeh Steel's reports were rather disappointing in the view of many analysts. As a result, in January, stocks of these companies suffered a 10% fall in their value. Relatively high production costs along with a fall in sales volumes were the main reasons behind their weak performance. As a result, investor confidence took a knock, leaving the base metal sector index down 8.4% overall for the month. However, according to some industry experts, if both companies increase their product sales (mainly NICIC's exports) during the winter, positive earnings adjustments of up to 10% can be expected in their next quarter reports. Zinc producers also reported unimpressive earnings and stocks of companies in this sector experienced modest price declines. Zinc producers are still suffering from limited availability of some of their raw materials such as mineral soil. Iron ore companies on the other hand announced an earnings growth of around 40% in their autumn figures compared to those of the summer and the sector index rose by 4.4%. The reports also indicated that the profitability of petrochemical companies in this quarter was heavily dependent on the exchange rate. However, prior price rallies prevented further price increases in this sector during January and the sector index fell by 6% on the TSE. Many analysts believe that current reports show that companies will continue to take a cautious approach in releasing next years' earning forecasts.

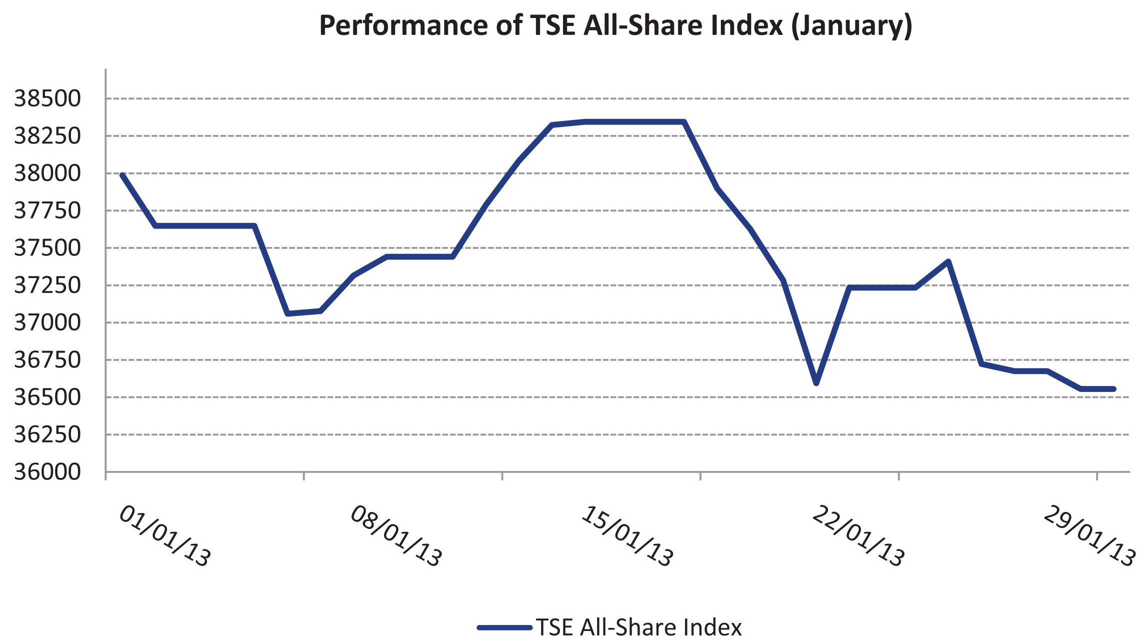
Refinery Sector

In January, the SEO suspended trading of all five refining companies on both the Tehran Stock Exchange and the Iranian OTC market (Farabourse). Companies in this sector have prospered from an approximate 100% increase in their share value over the past five months. The SEO explained that the ambiguity in the profit and loss of these companies is such that the suspension will remain until further notice. Given the strong presence of the government in the refineries' ownership structure, these companies have historically been reliant on governmental policies regarding their feedstock and sales prices and hence sufficient focus has not been placed on the quality of their financial reporting. Even after entering the stock market, refineries are still using their traditional financial reporting mechanisms which are not in line with the TSE's standards. In addition, according to some analysts, the insufficient free-float of around 5% in this sector can result in stock price manipulation and irrational price leaps in this sector. Therefore, the SEO may only consider lifting the suspension of tickers only if major shareholders of these companies commit to an increase in the free-float.

IPO

Initial public offerings (IPO) have always influenced the TSE's short term performance. These offerings attract significant investor interest mainly due to their favorable short term returns. Savvy investors tend to temporarily sell their current holdings in order to purchase shares of newly listed companies. According to a number of analysts, the IPO of Iran's largest petrochemical holding company (named the Persian Gulf Holding Company) potentially in February will have a considerable impact on stock market performance. This holding company is valued at 5 billion dollars and consists of 15 government-owned petrochemical companies which are the core strategic suppliers of feedstock and supplementary equipment for the Iranian petrochemical industry. The 5% offering of the company's shares is expected to raise up to USD 250 million. This would be the largest offering in the history of the Iranian capital market and investors are eagerly waiting for the offering to take place.

Overall, the month of January saw a fall in the market. The main index dropped by 3.4% and trade volumes fell steeply by 44% compared to the previous month, amounting to USD 1.9 billion.



Market Statistics	
Average P/E	5.0
Trade Volume ($ Billion)	1.8
Trade Value Monthly Change (%)	- 44
Market Cap ($ Billion)	135

Top 5 Traded by Value

Rank	Company Name	Turnover Value ($Million)	% of Total Turnover
1	Persian Oil and Gas Co.	27	10
2	National Iranian Copper Industries Co.	14	7
3	Isfahan Mobarakeh Steel Co.	10	6
4	Pardis Petrochemical Co.	10	5
5	Metals and Mining Investment Co.	8	5

Top 5 Companies by Market Cap

Rank	Company Name	Market Cap ($Million)	% of Total MC
1	National Iranian Copper Industries Co.	9,731	8
2	Isfahan Mobarakeh Steel Co.	9,442	7
3	Telecommunications Co. of Iran	8,595	7
4	Gol-e-Gohar Iron Ore Co.	6,634	5
5	Chadormalu Mining and Industrial Co.	6,294	5

All figures quoted in USD in this Newsletter are calculated based on the Central Bank of Iran's official USD/IRR exchange rate of 12260, as at 31 January 2013

President's Speech to the Parliament:

In January, President Ahmadinejad spoke to the Parliament in regards to the Iranian economy and the implementation of the second phase of the subsidies reform plan.

The President had requested to speak to the MPs after the Parliament had blocked the government's efforts to implement the second phase of the subsidies removal plan. Due to recent differences of opinion between the legislative and executive branches of power in regards to Iran's economic status, the members of the Parliament were reported to be concerned that the President may use this opportunity to criticize the Parliament for its stance against his cabinet's economic policies. However, President Ahmadinejad chose to address the Parliament in a fairly conciliatory tone in comparison to his previous speeches. He began by defending his government and said that he considers the sanctions to be the main cause of the economic problems Iran has been faced with. He said that sanctions are the reason behind slow growth, increases in prices and why transactions with foreign countries have been limited.

The President suggested that in order to defuse sanctions, activities such as buying gold and hard currency should decrease. He recommended that the country use its human resources more and focus on domestic capabilities. The subsidies reform plan he argued is one way to help that the economy become more people oriented.

The President said that for the amelioration of the economy and better use of unused economic capacity, the people should be given more resources. He stated that for example giving land to farmers would not only help production but it would also help towards job creation.

The President said in his speech that his government has performed well and gave a number of examples as to why he believed this to be the case. He stated that the production of steel has doubled in the time that his government has been in power and the production of cement has gone from 32 Million Tonnes to 86 Million Tonnes. He said that non-oil exports have increased from US$ 7 Billion to US$ 43 Billion. The President's main premise was that the management of the economy should be in the government's hand and that the Parliament should assist. He said that in order for significant projects to be processed, the government and the Parliament need to be supportive of each other and coordinated in their actions.

After President Ahmadinejad's speech, a few MPs addressed the Parliament and criticized the President's speech and mentioned that the government should not undertake large projects as such activities will disturb the economy further.

The head of the Parliament stated that Iran should focus on domestic production as the Supreme Leader has recommended. This he said, will lead to more stability in the economy and eventually add to prosperity.

President Ahmadinejad left after his hour and a half long speech and did not remain in the Parliament to listen to MP's takes on his proposals.

Iran's space program and the launch and retrieval of a monkey to and from orbit

In January, Iranian state TV announced that Iran has successfully sent a primate into space and retrieved it alive as a test and a step forward towards the goal of Iran sending humans into space.

According to experts, this shows that Iran has taken a strong step in developing their technology to produce advanced rockets, capable of controlled acceleration and deceleration, that would one day be able to send astronauts into space. Iran's state TV, said the monkey had been launched in a space capsule codenamed Pishgam (Persian for Pioneer) and reached an altitude of about 120km which is considered as a sub-orbital space flight. The director of Iran's Space Agency said this month that the reason a monkey was chosen to undertake this mission is because of biological similarities which exist between humans and monkeys. He also mentioned that Iran is planning to send a human into space within the next five years. Another state news agency stated that the space capsule was assembled on a Kavoshgar (Explorer) rocket and returned its shipment intact after the space flight. Pictures showed the monkey strapped to a harness sitting inside a white plastic capsule.

Monday's launch was the sixth known firing of the Kavoshgar rocket, where the first instance was a successful test launch in February 2008. Iran has so far successfully placed three domestically built satellites in orbit, Omid in 2009, Rasad in 2011 and Navid in 2012.

The West has expressed concern that Iran may use the technology from its space programme for implementation in long-range missile applications. Nevertheless, experts have concluded that the recent experiment does not seem to have any new military implications, as it does not add to missile technology Iran has already showcased to have in its possession in the past.

So far only Russia, the United States and China have put men into orbit. However, three other countries have scheduled manned space flight programs coming up with target dates of 2015 for India, 2021 for Iran and 2025 for Japan.

Banks' Resource Management Improves in 2012

A study of historical statistical data published by the Central Bank of Iran (CBI) from 2010-2012 suggests that, after years of battling with mounting loans-to-deposits ratios, the Iranian banking system might have finally found an applicable resource management strategy to alleviate the inflated ratio. According to this study, in 2010 the ratio in question had reached to 112%, implying that the value of loans issued by banks in that year was approximately 1.12 times more than what their deposit reserves permitted. But in the two years that followed, this ratio dropped down to 110% and 100% respectively. The ideal figure would be 80%.

Part of this accomplishment results from the CBI's new policy that restricts the CBI from granting further credit lines to other banks in what the head of the CBI calls "excess credit". Previously, these other banks would compensate the shortages resulting from loans-to-deposits imbalances through excess borrowings from the Central Bank. This not only added further liabilities to the Central Bank's balance sheet, but also fueled Iran's liquidity problem further.

According to the CBI, the new policy is not just limited to the credit lines between the CBI and other banks; it even requires the banks to limit or fully suspend their lines of credit to customers until their accounts are balanced. In addition, banks are obliged to recollect all of their receivables outstanding within a reasonable period of time.

Mahmood Bahmani, the head of the CBI, claims that his monetary organization is satisfied with the outcome of this approach so far. Based on the published report, the amount of bank's debt to the Central Bank has declined by IRR 108 trillion since August 2012. It is anticipated that persisting with this policy will reduce the point-to-point inflation rate and liquidity over time. However, government authorities believe that the positive changes in bank's loan to deposit ratios will not impact the county's liquidity in the short term.

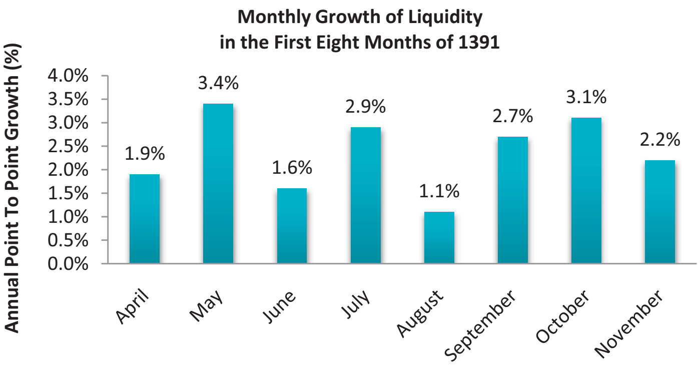
Iran's Liquidity Woes Continue

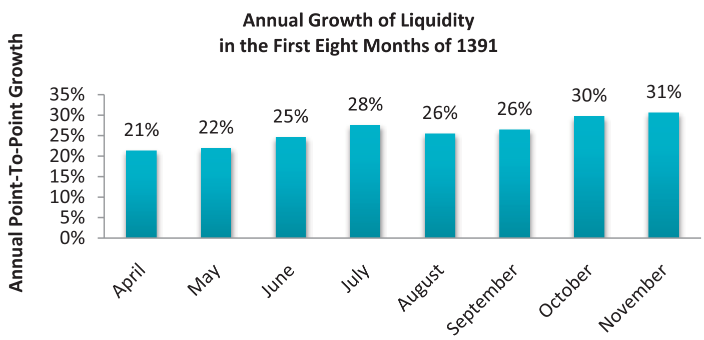
Monthly statistical assessments conducted by the Central Bank of Iran (CBI) for November 2012 continue to show increases in liquidity levels in Iran's economy. From a monthly point-to-point perspective, the CBI assessment sees a 2.2% jump in November 2012's cash levels compared to the preceding month. This implies an IRR 90 trillion increase in liquidity since October, and an IRR 720 trillion growth since April 2012. In other words, during November 2012, this monetary variable grew by IRR 12.5 billion in each hour and IRR 3 trillion in each day. By the end of November, total liquidity had approximately climbed to IRR 4,240 trillion.

One of the most important factors that triggered Iran's liquidity problem is the significant amounts of borrowing from the CBI by other banks, as discussed earlier in Economy Overview. The banking system in Iran has constantly been under pressure from the government to loan out large sums of money to industries in order to promote production and development in the country. The amount of these loans often exceeded the banks' reserves, and banks would in turn borrow the shortage from the CBI. The CBI itself was also under pressure from the authorities to credit these banks in order to support the government's plans to promote domestic production.

In addition, the introduction of the subsidy reform program, and the monthly cash handouts to Iranian citizens as a substitute for eliminating food and energy subsidies, has also impacted liquidity levels in the country. The Iranian government has encountered many difficulties in making these payments, mainly due to an unprecedented cash crunch resulting from the drop in its oil sales and challenges in repatriating oil money. Therefore, a substantial portion of these payments were generated through hefty borrowings from the Central Bank. The persistence of the banking debt, the government's budgetary woes, its diminishing foreign reserves and the devaluation of the Rial, as well as the government's mounting debt to the CBI for making these subsidy payments, have all worsened Iran's liquidity position in the past few years.

However, the CBI claims that it has taken some actions to control the current situation. According to the latest statistical report by the CBI, for the first time since August 2012 the monthly growth of liquidity in November was less than that of the preceding month. As shown in the figure below, in November 2012 cash levels grew only 2.2%, whereas September and October 2012 experienced some of the highest increases in this monetary variable since April 2012, by jumping 2.7% and 3.1% respectively. Additionally, the 8-month growth rate of cash levels stood substantially lower than that of the 7-month data.

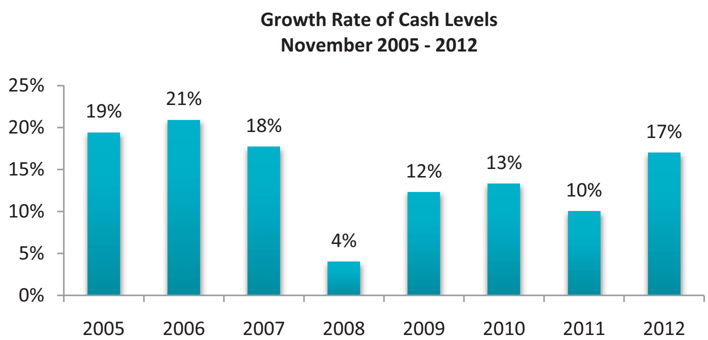




Analysts argue that these developments are largely ascribed to the stricter liquidity regulations imposed by the Central Bank since June 2012. The new regulation has introduced new policies such as restricting the CBI's line of credit to other banks and issuing IRR 100 trillion worth of one-year bonds that offer a yield of 20%. The former prohibits excess credit payouts to other banks and mandates these banks to develop a sound resource management policy. In other words, banks are expected to balance their accounts by collecting all receivables outstanding, instead of borrowing from the CBI. The bond policy has also been successfully launched under two phases in September and November.

Nevertheless, these developments have not stopped economists from expressing their concerns about the current cash levels in Iran's economy, and the CBI's inefficient strategies to control this monetary variable. As shown in the bar chart below, the 8-month point-to-point cash levels in November 2012 stood higher than any other value recorded for this month (November) in the past four years. November 2012's cash level growth was also the fourth highest monthly jump for this variable since Mahmood Ahmadinejad's presidency commenced in 2005.

According to some economists, the bond policy mentioned earlier can also be criticized for returning relatively high yields (20%) over a relatively short period of time (one year). In addition, some experts argue that this course of action only alleviates the problem in the short-term. When the CBI pays out the bonds' returns next year, IRR 120 trillion will be injected back in to the market, and the economy will be driven back to the current status quo.



Iran to Change its Price Base Year

Iran is planning to change the base year used to compute its inflation rate. The current base year is 2004, but the CBI has announced that from March 2013, the base year will move to the year 2011. This would be the eighth time that the CBI has revised the base year for calculating the inflation rate since 1936. The other points in history where such a revision have been made were in 1959, 1969, 1974, 1982, 1990, 1997, and finally 2004.

The reason behind these changes is the use of Laspeyres index in computing Iran's inflation rate. As commonly accepted by economists, the Laspeyres index tends to overstate the inflation rate. This is because the index does not account for the fact that consumers react to price changes by adjusting the quantities they purchase.

In addition, as markets grow and reach out to a larger group of consumers, the range of goods and services that are available and consumed by an average household, changes as well. For example, the CBI states that in the 2004 base year, the number of goods and services included in Iranians' basket of goods was 359. But in the 1997 base year, this number was 310. With this in mind, it is important that the basket of goods for Iranian households should be revised frequently and at least every 7 years, in order to address this. Otherwise the computations made using this index will be misleading.

By changing the base year to 2011, the CBI aims to reduce the current inflation level by 2%. Readjusting inflation by changing the base year has been attempted in Iran before. In 2006, the CBI computed the inflation rate in two phases. First, it utilized 1997 as the base year, where an inflation rate of 13.6% was reached. But the same procedure using 2004 as the base year came to a lower inflation rate of 11.9%.

Iran, the 19th Largest Auto Manufacturer in 2012

A recent study by the Iranian Students' News Agency (ISNA) estimates that, in 2012, the number of vehicles manufactured in the country had slipped below its recorded amount in 2011. Under the most optimistic circumstances, the number of vehicles manufactured in 2012 is estimated to be approximately 1,058,850, whereas the official figure for 2011 was 1,648,505 units.

It is expected that the production cut in 2012 will downgrade Iran's position on the 2012 OICA list of the largest global auto manufacturers. In 2011, Iran's auto manufacturing volume jumped 3.1%, a development that awarded the country the 13th spot on the above mentioned list. While the 2012 ranking has not been officially published yet, a rough data comparison between Iran's 2012 performance with the data available from other countries indicates that Iran will have the 19th spot in 2012, after England, Czech Republic, Turkey, Thailand and Indonesia. Previously, these nations stood behind Iran on OICA's 2011 ranking.

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Turquoise publishes this electronic newsletter, *Iran Investment Monthly*, with the aim of keeping its recipients updated on the latest macroeconomic developments in Iran, providing an in-depth analysis of the Tehran Stock Exchange as well as introducing new financial products and private equity opportunities to potential investors.

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