



Karoon Dam, South Western Province of Khuzestan

THIS MONTH

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In December, the Tehran Stock Exchange (TSE) experienced a downturn and a sharp decline in trade volumes. The price rallies of the first half of the current Iranian calendar year (which ends on 20th March) had, in the view of many analysts, created price bubbles and price corrections had been expected for several months. In the past 2 to 3 months, signals of price corrections had been observed. However, due to an inflow of new funds and strong buying demand, the corrections were modest and short-lived. However, selling queues in December outpaced the demand for shares, and stock prices in several sectors tumbled. In addition, the political turbulence during December and the widespread unrest on the Shi'a holy day of Ashura (see Country Overview) exacerbated the selling pressure in the market.

An analysis of market prices at the end of December shows that the majority of stock prices are at levels 20 – 30% lower than two months ago. The market main index has also lost over 10% of its value over the past two months. Investors are divided in their opinions about the current price levels. The bearish view is that the current price levels reflect the increased systematic risks due to a slowdown in economic growth and political instability this year. On the other hand, the market bulls believe that the recent price falls have brought about many attractive buying opportunities. The latter view seemed to be winning out towards the end of the month, resulting in stability returning to the market.

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

IPO of Asia Insurance

On 30th December, 10% of the shares in Asia Insurance were offered on the market, as part of the ongoing privatisation programme. This IPO attracted huge investor interest, such that according to the listing authorities, the entire offering was bought within 35 seconds. The offering took place at a price of 1,486 Rials per share, putting the market capitalisation of Asia at \$67 million, and the price/earnings ratio at 7.7. Further stakes in Asia are expected to be offered shortly, both as blocks and on the market.

With a 14% market share, Asia is Iran's second largest insurance company. Last year, Asia had total revenues of \$945 million from insurance premiums. Its total reserves amounted to \$476 million. However, due to a payout ratio that is higher than the industry average, Asia's operating margin is considerably below industry average. This is due to the concentration of its portfolio of products on third party car insurance (75%), a loss making business stream for Asia and many other insurance companies. Asia's net earnings for the financial year ended 20th March 2009 were \$6 million.

Oil and Gas Extraction

Haffari Shomal (North Drilling Co.) once again made the headlines in December. 20% of the shares of Haffari was offered on the TSE as one block. Several interested parties competed fiercely for the block for 9 days. Finally, Mehr Eghtesad, a quasi-government investment company, bought the block at a 40% premium to market value of the stock, for the sum of \$153 million.

Haffari was privatised in July 2009 through an offering of 15% of its shares on the TSE. Its key business is design, construction, management and leasing of oil and gas platforms in the Caspian Sea, to both Iranian and also foreign customers. It currently manages Iran's first semi-floating drilling platform, Alborz, in the Caspian Sea.

Steel and Iron Ore

Companies in these two sectors were among the biggest fallers in December and weighed the most on the market index. Every year, determination of the price of iron ore results in considerable debate between steel

and iron ore producers. In November, the two sides agreed that the price of iron ore would become a function of steel price. This meant that iron ore companies had to reduce their earnings forecast for the existing year by approximately 30%. Nevertheless, the decision to liberalise the price of iron ore was perceived as a positive development for the future prospects of the iron ore sector.

The iron ore sector index lost 15% of its value upon the adjustment of earnings forecasts. Mobarakeh, the largest listed steel manufacturer, also re-opened 14% lower.

Fixed Income Market

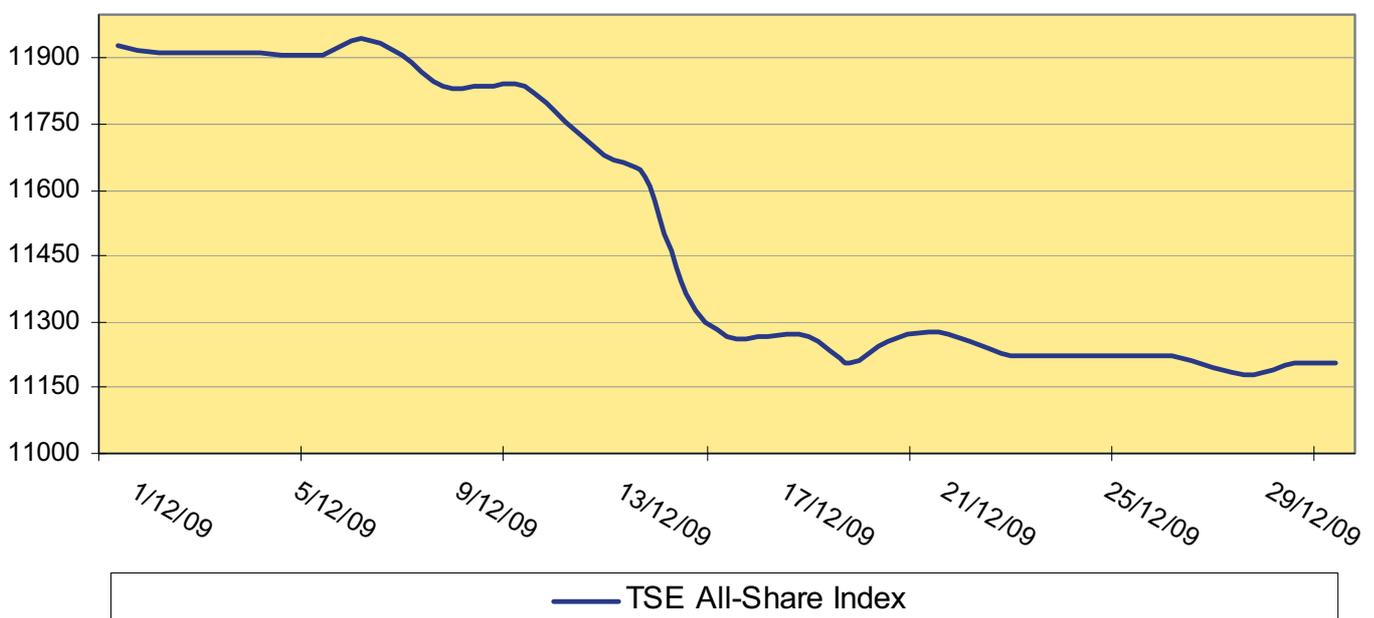
This year has been one of the most active for the issuance of fixed income products. Almost all banks active in the Iranian market have issued deposit certificates. Earlier this year, EN and Keshavarzi became the first two banks to list their term deposit certificates on the Iranian Over-The Counter (OTC) market.

Various state-owned and private entities have also successfully issued Participation Papers (an Islamic form of bond) in the money market. In December, Abadan Refinery issued \$250 million worth of Participation Papers at an attractive annual coupon rate of 16.5%. Not surprisingly, this issuance attracted huge interest. The government also announced its plans to issue \$500 million of papers next month to fund the construction of 8 steel manufacturing plants.

Analysts believe that a sharp fall in the inflation rate over the past year means that yields on fixed income products have become more attractive. This, together with a slowdown in other investment markets such as real estate, is the key reason for the increased investor interest in fixed income products.

Overall, the Tehran Stock Exchange experienced a downturn in December, with the TSE All-Share Index losing 6.3% of its value. Trade volumes also declined sharply to \$377 million, a 60% decline from the previous month.

Performance of TSE All-Share Index (December 2009)



Investment Objective – The Turquoise Equity Investments seeks superior long-term capital growth by investing in the consumer and commodity potential of Iran, one of the most undervalued emerging markets in the world. Turquoise combines international experience with local expertise in investing in equities listed on the Tehran Stock Exchange (TSE) and other Iranian-based securities. The goal is to provide superior returns, with greater diversification and lower volatility.

Portfolio One (Closed)

NAV = 154.5

Vehicle Domicile
Iran

Launch Date
30 May 2006

Currency
Iranian Rial (IRR)

Portfolio One Performance (Iranian Rial) - As at 31st December 2009



Period	Portfolio Return
Last Month	- 7.3 %
Last 3 Months	- 1.7 %
Last 6 Months	10.6 %
Last 12 Months	15.3 %
Since Inception (30 May 06)	54.5%

Portfolio Two (Open)

NAV = 110.8

Vehicle Domicile
British Virgin Islands

Management Fee
2.0% p.a

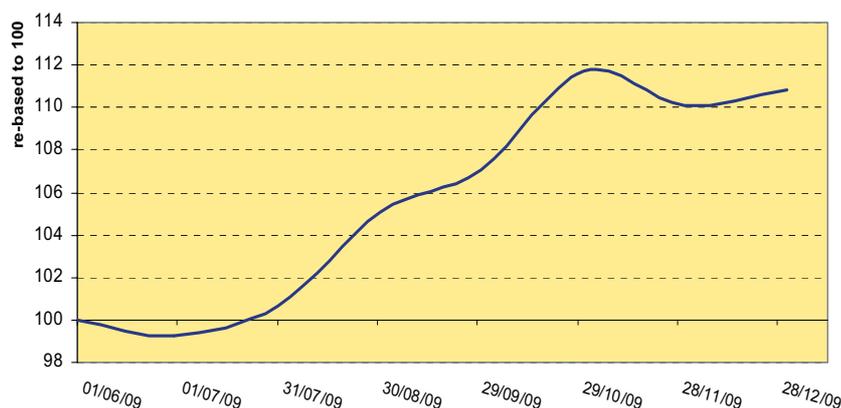
Currency
Euro (€)

Launch Date
01 June 2009

Carried Interest
20% (High Water Mark Applies)

Minimum Investment
€100,000

Portfolio Two Performance (Euro) - As at 31st December 2009



Period	Portfolio Return
Last Month	0.6 %
Last 3 Months	3.5 %
Last 6 Months	11.7 %
Last 12 Months	N/A
Since Inception (01 June 09)	10.8 %

Class C (Closed)

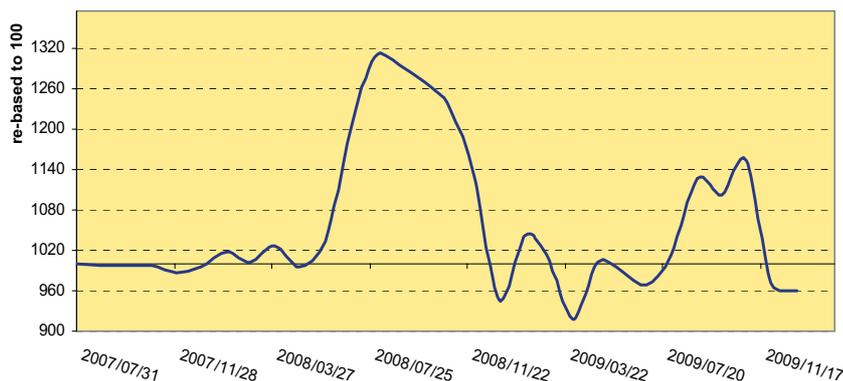
NAV = 960.0

Vehicle Domicile
British Virgin Islands

Launch Date
10 July 2007

Currency
Euro (€)

Class C Performance (Euro) - As at 31st December 2009



Period	Portfolio Return
Last Month	- 1.2 %
Last 3 Months	- 4.2 %
Last 6 Months	10.6 %
Last 12 Months	13.5 %
Since Inception (10 July 07)	6.0 %

Class D (Closed)

NAV = 925.0

Vehicle Domicile
British Virgin Islands

Launch Date
30 June 2008

Currency
Euro (€)

Class D Performance (Euro) - As at 31st December 2009



Period	Portfolio Return
Last Month	- 1.7 %
Last 3 Months	- 4.6 %
Last 6 Months	5.8 %
Last 12 Months	5.9 %
Since Inception (30 June 08)	- 7.5 %

For subscription and further information on our investment products please contact Eddie Kerman on (+44) 20 74 93 04 12 or email eddie.kerman@turquoisepartners.com. For more information about Turquoise Partners please visit our website at: www.turquoisepartners.com

A review of the latest developments on the Iranian nuclear dossier and the domestic political turmoil during the month of Ashura will be discussed in this edition of Country Overview.

There has been a longstanding dispute between Iran and the West over its nuclear programme. The US and its Western allies have repeatedly accused Iran of attempting to build nuclear weapons. These allegations have been dismissed by Iran, with the country arguing that the nuclear programme is designed only for power generation purposes. Iran has continued its uranium enrichment despite the three rounds of sanctions imposed on it by the UN Security Council.

In October, Iranian officials met with the representatives of the 5+1 group in Geneva, Switzerland, to discuss and formulate an agreement over Iran's uranium enrichment. This followed a preliminary meeting in September, in which both sides expressed their willingness for further negotiations. A proposal put forward by the International Atomic Energy Agency (IAEA) formed the basis of discussions in Geneva. The proposal called for Iran to send 75% of its low enriched uranium to Russia. In Russia, it would be further enriched and then sent to France to be manufactured into fuel assemblies. These would then be shipped back to Iran for use in its nuclear power plants. However, the proposal was rejected by Iran. The reason given by Iran was that France cannot be trusted as a partner in the nuclear exchange deal. Iranian officials argued that France has failed to fulfil its previous commitments on delivering enriched uranium to Iran. (In the 1970's Iran and France entered into an agreement whereby France would provide Iran with enriched uranium for its power stations. This was in exchange for a \$1 billion investment that was made by Iran into an enrichment site in Europe. However, no fuel has been delivered to Iran up until now). Iran replied with a counter proposal, offering a simultaneous exchange of its low enriched uranium with fuel in Kish, an Iranian island in the Persian Gulf. This counter proposal was swiftly rejected by the West. Subsequently, the Iranian Foreign Minister expressed Iran's willingness to conditionally accept the exchange taking place in a neutral foreign country, such as Turkey. However, Ahmadinejad stated that unless the West accepts that the exchange takes place on Iranian soil, Iran will begin the process of further enrichment by itself. This, in the view of experts, reflects the differing views on the nuclear issue that exist within the Iranian political system.

With the backing of several Western powers, the IAEA passed a resolution in November, condemning Iran's nuclear programme and demanding an immediate suspension of the enrichment. In response, and in an unprecedented move, Iran issued its own ultimatum to the West, warning that unless the West accepts Iran's proposal for the exchange by the end of January 2010, Iran will begin the process of developing its own nuclear fuel.

Experts believe that both the existing political turmoil in Iran and also the divided viewpoints of influential figures on the nuclear issue are exacerbating the difficulties that Ahmadinejad's government faces in negotiating with the West. Any breakthrough in the negotiations will require a significant improvement in relations between Iran and the West, particularly the US. While the general consensus is for a solution to this issue and better relations with the US, there is still considerable resistance within a segment of the reformist party and the more hardline group of the conservative party. The view of the experts is that any meaningful steps taken by Ahmadinejad in either direction will carry a political cost.

Since the tenth presidential election in Iran in June 2009, the country has been experiencing a great deal of political turbulence. The unrest began following the announcement of Ahmadinejad's victory and lasted for several weeks, with the opposition questioning the legitimacy of the elections.

Despite a period of relative calm, the opposition gained momentum after the death of an influential cleric in December, which coincided with the Shi'a holy month of Moharram. Grand Ayatollah Hossein-Ali Montazeri

was a well-respected theologian and human rights activist. He was the deputy leader at the time of Ayatollah Khomeini's leadership. However, prior to the death of Ayatollah Khomeini, he had a falling out with the regime due to his condemnation and disapproval of various aspects of state operations. He was placed under house arrest between 1997 and 2003. Also, since the first election of Ahmadinejad as president in 2005, he voiced his discontent with Ahmadinejad's domestic and foreign policies on numerous occasions.

Ayatollah Montazeri's funeral is said to have marked a new chapter in the opposition movement. Thousands of mourners, along with opposition supporters, went to the holy city of Qom where Grand Ayatollah Montazeri lived, and turned the funeral into a series of protests. Following the funeral, demonstrations took place in Tehran and other major cities around the country in support of Ayatollah Montazeri. The height of tensions was on the day of Ashura, the most holy day for Shi'as. On 27th December, thousands of opposition protesters demonstrated in conjunction with Ashura. This led to violent clashes with anti-riot police. Reports of deaths were released the next day. Among the casualties was Ali Mousavi, the nephew of Iran's opposition leader Mir Hossein Mousavi. The Chief of Police announced that these deaths were suspicious and blamed them on anti-regime groups.

Three days after Ashura, a large group of government supporters responded to a call from the government and took to the streets of Tehran. These government supporters chanted slogans against Khatami, the ex-president of Iran, Karroubi, a defeated candidate in the June election, and Mousavi. It is believed that these demonstrations were in retaliation for the opposition protests on Ashura. Confrontations also spread among senior political figures and clerics, with various accusations and heated words being exchanged.

After these demonstrations, stability returned to the country. There are, however, fears of a re-emergence of the opposition protests and further clashes, with the approach of the 31st anniversary of the Islamic Revolution, on 11th February.

Anti-Money Laundering (AML) Regulations

In December, the Central Bank of Iran issued a mandate. This outlined specific rules and regulations to prevent the occurrence of money laundering in Iran. The AML law was passed by the parliament in February 2008. This mandate is aimed at banks and other active participants in financial markets. The mandate states that in order to comply with AML law, financial institutions are obligated to formulate and implement strategies, systems and procedures for conducting detailed observations over all related transactions in domestic and international markets. There is also a requirement to identify and report all suspicious transactions to the relevant authorities. In addition, all cross currency transactions should only take place through certified exchange bureaus or banks. According to this mandate, from the start of the next Iranian calendar month this year (Bahman), the maximum daily cash withdrawal for each bank customer will be \$15,000.

In 2007, the Financial Action Task Force (FATF) issued a statement, expressing concerns regarding the lack of robust AML regulations in Iran. In this statement, the FATF urged Iran to address this shortcoming and to take the necessary steps in order to implement AML laws as well as combating the financing of terrorism. The FATF called for Iran to address these deficiencies in order to contribute better to the global financial markets. The Iranian AML law of 2008 and the subsequent regulations put in place by the Central Bank aim to address the issues raised by the FATF, and also to improve the transparency and integrity of the financial markets in Iran.

Inflation Rate in Iran

The latest statistics published by the Central Bank of Iran reveal that in December, the Consumer Price Index (CPI) grew by 1.3% in comparison to the previous month. This means that the annual inflation rate stood at 7.6%. The inflation rate has been on a downward trajectory since the summer of 2008, when it peaked at approximately 30%. The windfall oil revenues of the 2 to 3 years prior to the global economic crisis, and subsequently, the excessive injection of liquidity into the economy as part of the government's aggressive expansionist policies, were assessed as the key reasons for the previous high inflation rate. However, due to a sharp fall in the liquidity growth within the economy and a series of measures taken by the Central Bank, the inflation rate has fallen to its current level.

The Central Bank governor predicts further falls in the inflation rate. However, analysts are sceptical about this assessment. This is due to the growth in excess liquidity in conjunction with a slowdown in economic growth this year. Liquidity growth, which stood at 15.9% at the end of the Iranian calendar year 1387 (which ended 20th March 2009), rose to 27% in September 2009.

Islamic Banking in Iran

A recent publication by the "Banker" ranks Iran at the top of the list of countries with Islamic banking assets, at a total value of \$154 billion. After Iran, Saudi Arabia and Malaysia are in second and third place with \$69 billion and \$65 billion worth of Islamic assets respectively. Also, among the top 20 Islamic banks in the world, 6 are Iranian. Bank Melli of Iran stands at the top of this list with \$35 billion of Islamic assets. Parsian Bank, Iran's largest privately owned bank, is ranked 9th.

Over the past decade, Iran has taken significant steps towards developing and expanding Islamic finance. Last month, the parliament approved the details of a new legislation to develop and expand Islamic financial instruments and institutions. The Securities & Exchange Organization of Iran (SEO) actively promotes innovation in Islamic products and has formed a specific Sharia committee to assess the compatibility of new products with Islamic law (Sharia).

Islamic finance has enjoyed tremendous growth (estimated at 10-15% per annum) over the past decade. This has been not only in Islamic countries, but also in several Western markets. The UK has taken a leading role in promoting Islamic finance. There are currently over 20 financial institutions in the UK that are either wholly Islamic or are conventional institutions with a so-called “Islamic window”.

About Turquoise

Turquoise is a boutique investment bank based in Iran with offices in Tehran and London. Turquoise creates financial products and offers financial services to select clients and investors who are interested in the Iranian market. Having a qualified and diverse management team based both in Europe and in Iran enables Turquoise to benefit from coupling local knowledge and presence with global expertise.

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.

Iran Investment Monthly is distributed exclusively amongst Iran analysts and potential investors who have worked closely or have been in contact with Turquoise Partners. Subscription to this newsletter is by referral only or through an online request sent to: ramin.rabii@turquoisepartners.com

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