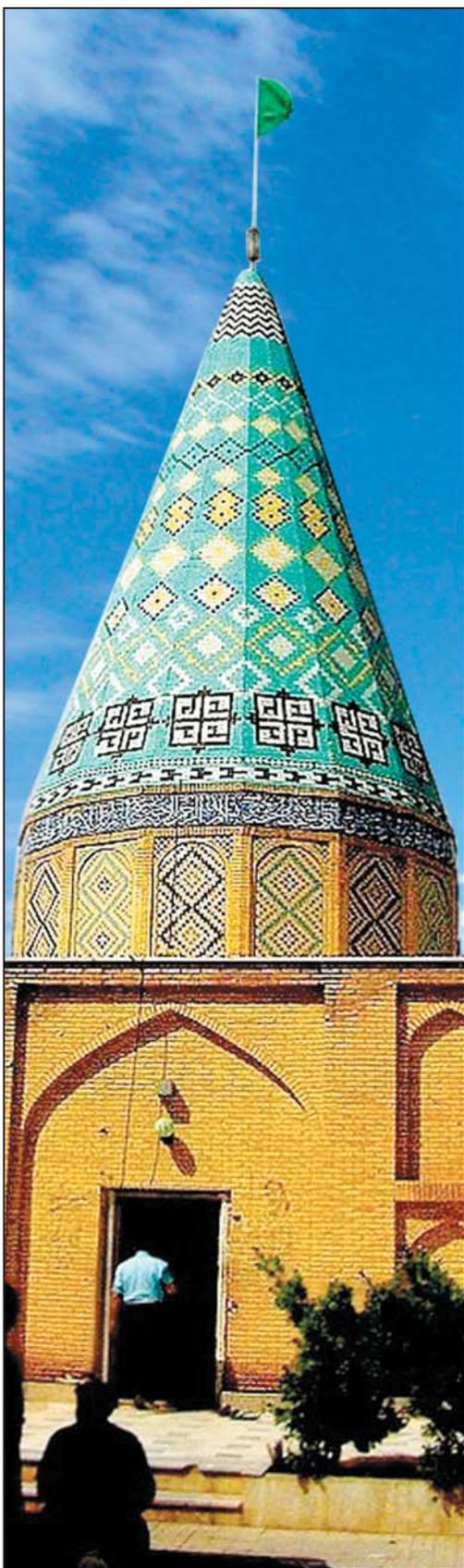


Turquoise Dome of Emamzadeh Davood, Town of Ghamsar , Isfahan Province , Central Iran



## THIS MONTH

### Market Overview 2

The market in June showed some signs of recovery with investor confidence improving evidenced by sell-off queues being replaced by balanced supply and demand. The market witnessed the IPO of an aluminium producing company during this month while the best and the worst performing sectors were metals and petrochemicals respectively.

### Turquoise Iran Equity Fund 4

Turquoise outperformed the market indices in June with the Fund's NAV rising by approximately 2%. The Investment Committee met regularly in Tehran and new holdings were added to the Fund's portfolio.

### Privatization & IPOs 6

IRALCO had a successful IPO with its share price rising following the offering. In contrast in mid-July the IPO of a cement company was met with some resistance. A steel manufacturing company is expected to be offered in the near future.

### Country Overview 7

Positive signals are emerging from the first one-to-one meeting between Iran and the US as well as the continuing Iran-EU negotiations. In addition, the impact of gasoline rationing through the end of June is briefly discussed in this section.

### Economy 8

In this edition of the Economy section, several topics such as the production of hybrid cars, Iran's increasing gas consumption and energy subsidies as well as the privatization schemes for petrochemical companies are briefly covered.

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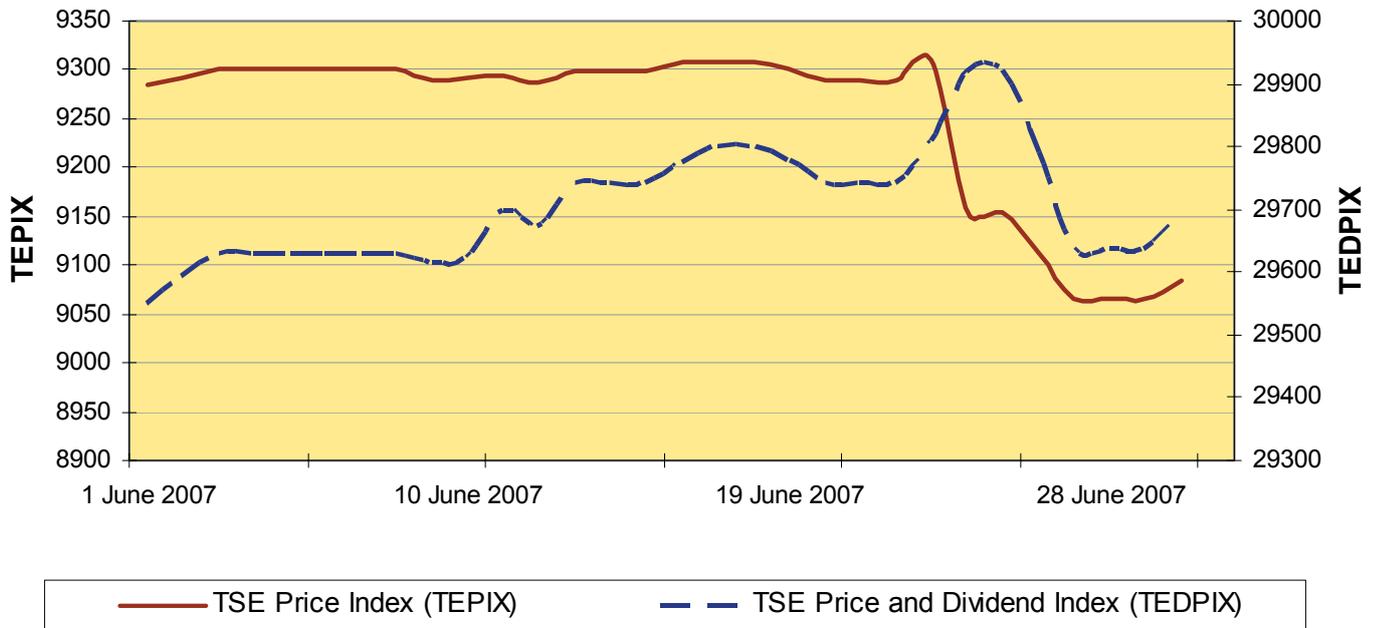
The investment mood in the market has changed positively in the month of June following political developments of recent weeks. Although the first one-to-one meeting between Iranian and US officials in almost three decades as well as a meeting between Iran's top nuclear negotiator, Ali Larijani, and the EU's foreign policy chief Javier Solana did not produce a tangible solution to Iran's nuclear dossier, the willingness to continue with the negotiations in both sides has resulted in more stability and optimism in the Tehran Stock Exchange. This optimism resulted in more balance in supply and demand of stocks and got rid of some of the heavy sell-off queues formed in the previous month. However, it fell short of attracting new liquidity into the market as the volume of trade remained low averaging around \$20 million and mainly limited to large institutional investors.

One of the major events of the TSE during June was the Initial Public Offering (IPO) of Iran's largest aluminium producing company, IRALCO, in accordance with the new wave of privatization that began in early 2007. IRALCO was valued at around \$220 million on the day of listing (11 June). However, only 5% of the company was offered in the first stage. In terms of size, IRALCO was much smaller than the previous two companies that went public which meant that its offering had less impact on the overall market and drained less liquidity from the market than the other IPOs. An analysis of the company and the IPO can be found in the IPO and Privatization section of the newsletter.

Another significant event was the decision by the regulatory body of the Bourse to lower some of the pricing regulations imposed on listed companies. All listed companies on TSE observe a cap on their daily share price change ( $\pm 2\%$ ) and a minimum trade volume threshold which means a certain number of shares need to be traded for the price to observe any change at the closing. This minimum number of stock, called "base volume", is a percentage of total outstanding shares. This means that for a large company to observe any significant share price change, a large number of shares need to be traded daily and in a slow market, it could take days and even weeks for a share price to reach its balanced value. In June, the TSE Corporation which regulates the bourse decided to lower the Base Volume of large companies by 50% which has significantly increased their manoeuvrability and liquidity. Market analysts and experts believe that this move was a first step to gradually rid the exchange of the many limiting regulations that have occasionally locked the trading of some of the listed companies and reduced overall liquidity on the market.

The best and worst performing sectors of the market during the month of June were Metals and Petrochemicals respectively. The total value of the petrochemical sector dropped by 0.6 percent to stand at around \$4 billion. This was mainly due to the government plan to stop raw material subsidies which used to be provided to petrochemical complexes. The government provides the raw material to the petrochemical companies at a 30% discount compared to Persian Gulf FOB prices. Although the plan to stop these subsidies has not been implemented yet, the market is expecting it to materialize within the next few months which could significantly impact earnings of the listed companies which use these subsidies (mainly Isfahan and Arak Petrochemical Companies). The rise in share prices of metal producing companies was mainly driven by gains of the two largest listed companies, National Iranian Copper Industries Company (NICIC) and Mobarakeh Steel Complex (MSC). NICIC distributed 20% dividend without observing a share price loss during June which was mainly due to the rise in international copper prices while MSC saw its share price grow by 14% in the same month. The gain of these giant companies resulted in a 2.3% increase in the index of the metals sector, which made it the best-performing sector of the market. The chart below illustrates the performance of the market indices during June. The TSE Price Index (TEPIX) fell by around 2% while the TSE Price and Dividend Index (TEDPIX) grew by around 0.7%. This is due to the fact that it is now the Annual General Meeting (AGM) season for most listed companies at which usually high dividend payouts are announced.

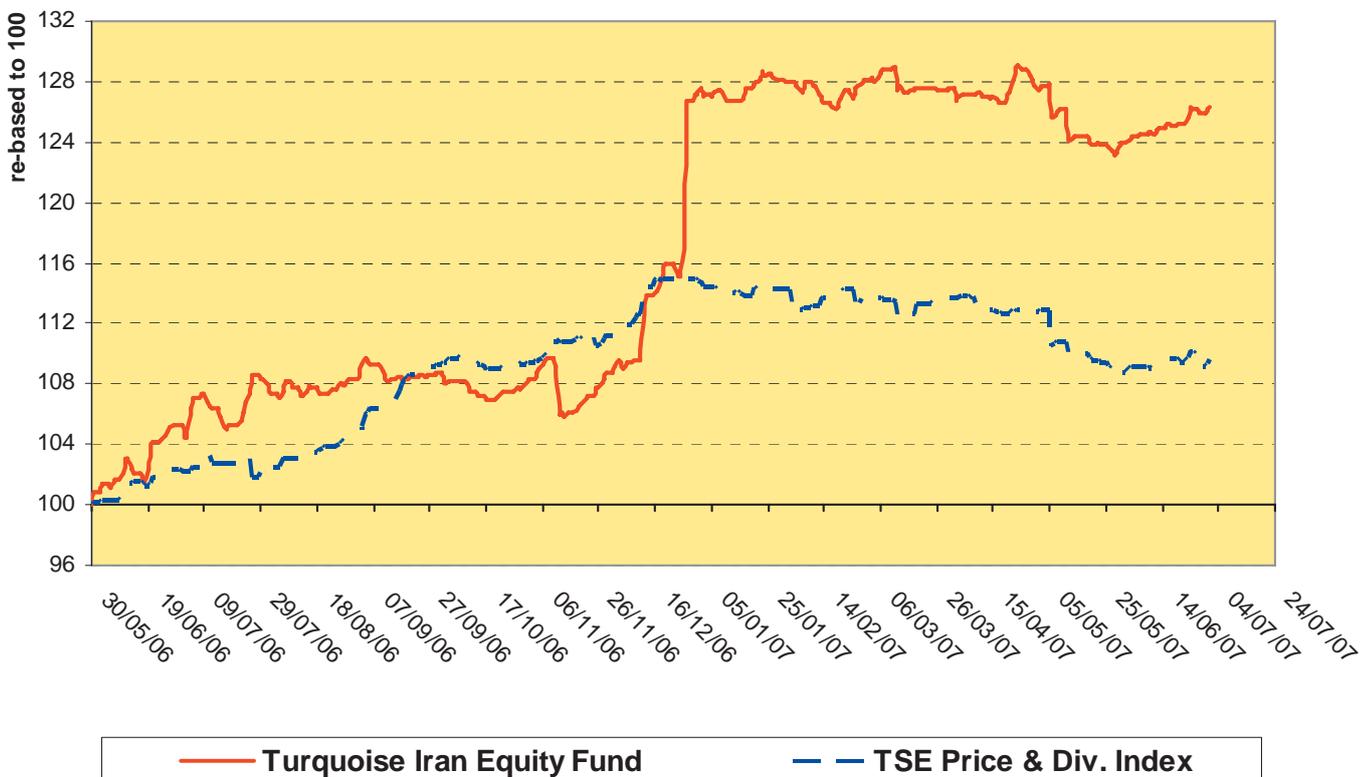
### Performance of TSE Indices (Jun 2007)



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

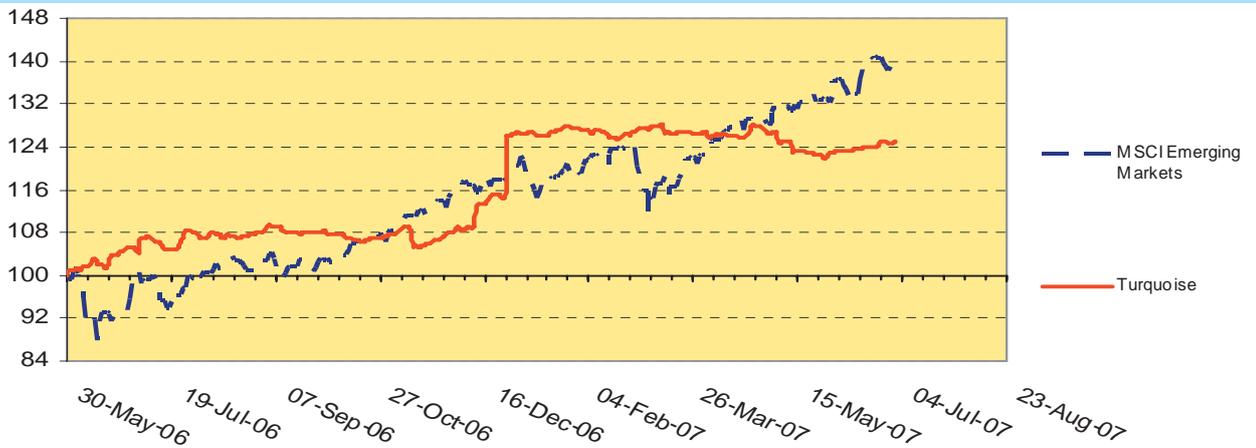
**Monthly Report** – The Net Asset Value (NAV) of the Turquoise Fund grew by approximately 2% during the month of June. The Fund outperformed the market indices with a number of the holdings performing well following their AGM and dividend announcements. The Fund’s unit index grew from 123.9 to 126.3 during June while TEPIX dropped by 2% and TEDPIX grew by only 0.7% during the same period.. The charts below demonstrate the performance of the Fund against the TEDPIX in local currency, and the Emerging Market index in USD as well as the overall performance of the Fund in USD, Euro and GBP:

**Turquoise Portfolio vs. TSE Price & Div Index (TEDPIX)  
(YEAR TO DATE)**



	1 May 07	1 Jun 07	1 Jul 07
<b>Turquoise Fund</b>	27.41%	23.93 %	26.29 %
<b>TEDPIX</b>	12.81 %	8.79 %	9.56 %

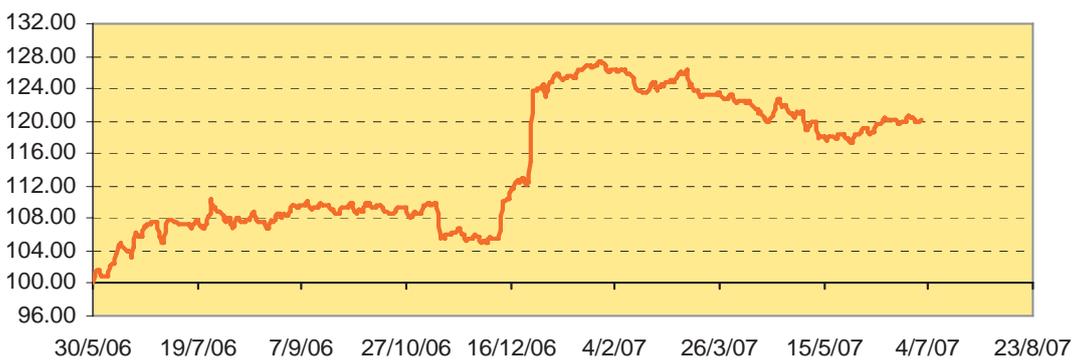
## Turquoise Performance vs. MSCI Emerging Markets



## Turquoise Performance in US Dollar (US\$)



## Turquoise Performance in Euro (€)



## Turquoise Performance in British Pound Sterling (£)



## IRALCO

On June 11<sup>th</sup> 5% of the shares of Iran's largest aluminium producing company, IRALCO, were offered on the Tehran Stock Exchange. The IPO was successful with around \$11 million of shares being sold, giving IRALCO an overall valuation of \$220 million and a PE ratio of 4.8. This is the third successful IPO from the mining and metals sector which seems to be amongst the government's most profitable assets. The previous two IPO's were a copper production company and a steel production company.

IRALCO is one of only two aluminium producing complexes in the country. There is a solid domestic and export market. The company currently has a production capacity of over 120,000 tons of aluminium ingot and products and has over 50% share of the domestic market. The standard of products, with purities of over 99.7%, meets the requirements of the London Metal Exchange. In the domestic market, the products of the company are sold on the Tehran Metal Exchange with prices closely linked to international aluminium prices. Therefore the level of the company's earnings is very much linked to global aluminium prices.

In 2001, the company undertook a large expansion plan to add another 110,000 tons to its production capacity for a total investment of around \$365 million. The project faced some financing difficulties and was delayed several times. According to the latest reports, the project is two third's through and its first phase, with a capacity of 25,000 tons, is expected to come on stream by the end of 2007.

## Dashtestan Cement

For the first time since the new wave of privatization has begun, the government has offered shares in one of its cement companies on the TSE. Shares of Dashtestan Cement were listed on 15 July and the market gave the company a total valuation of around \$83 million and a PE ratio of 7 on the first day of trading. However, this IPO was not as successful as previous offerings. The government was planning to offer 5% of the company on the market but only 1% of the shares were successfully sold. Analysts considered that the initial offering price was too high. The sector as a whole is going through difficult times due to the cement pricing scheme that has been imposed by the government. Even the small number of shares that were sold during the IPO were being sold in early trading. Unless the current pricing scheme is lifted and cement is sold at a free market price, it is not expected that any of the cement companies, including Dashtestan, will experience a significant rise in their share price.

## *IPOs in the Pipeline*

### Khuzestan Steel

Another company whose shares will be offered on the market in early August 2007 is Khuzestan Steel Company. This is the second largest steel producing company in Iran after Mobarakeh Steel Complex (MSC). The MSC was successfully listed with a share price rise of over 25% following its IPO. This has made investors and analysts hopeful that this pattern will be repeated with the IPO of Khuzestan Steel.

Khuzestan Steel was able to increase its profitability by 14% over the last Iranian year with only 1% increase in production, showing a solid growth in its profit margin. The company is expected to produce around 4 million tons of steel products in the Iranian year of 1386 (ending March 2008). It should be noted, one of the operational risks of the company is power shortages in its region with occasional black-outs that could hurt its production levels.

There were some positive signals emerging from the new rounds of negotiations separately between the US and Iran and the European Union and Iran.

Iran and the US had their first one-to-one meeting in almost three decades on 28 May which was held in Baghdad and covered issues of mutual interest concerning Iraq. Although the talks were limited to each country's role in Iraq, the fact that the two rivals chose dialogue rather than confrontation and the fact that the meeting took place on a one-to-one and equal basis and without preconditions sent a positive signal and raised hopes of an eventual rapprochement between the two nations. Both Iranian and US officials showed a willingness to continue on the negotiation path and both emphasized a mutual interest in seeing a stable and secure Iraq.

In another development, Iran's top nuclear negotiator Ali Larijani met with the EU foreign policy chief, Javier Solana to discuss Iran's nuclear program. Both gentlemen stressed that the meeting was positive and constructive and emphasized the need for further dialogue to resolve the impasse created over the nuclear issue. The results of these discussions were observed in the following weeks when the representatives of the International Atomic Energy Agency (IAEA) travelled to Iran and met with Iranian officials to draft modalities for resolving the outstanding issues, and also when rumours of a "time-out" of additional UN sanctions began to circulate in the Western diplomatic circles.

Another important development in the month of June was the introduction of gasoline rationing in Iran. Due to low prices, the consumption of gasoline recently surpassed production by 75%, forcing the government to import \$5 billion worth of gasoline per annum. Low gasoline prices not only encouraged high domestic consumption but also led to alarming gasoline smuggling figures (around 10 million litres a day). Additionally, high domestic consumption was causing serious side-effects such as heavy traffic in large cities, and serious air pollution in metropolitan areas.

Over the years there have been many discussions on ways to curb gasoline consumption levels and to lower subsidies without causing a sudden rise in gasoline prices thus creating further inflation. The solution proposed by both the Parliament and the government was the introduction of a monthly consumption cap which is enforced through the mandatory use of smart-cards tracking the consumption level of each vehicle. The gasoline smart-cards were distributed amongst Iran's 7 million vehicle owners in the past few months and the rationing officially began on 29 June. Early results from the first few days illustrate a 30% drop in daily gasoline consumption, 20% decrease in Tehran traffic, 30% improvement in air quality in Tehran and an 8% rise in the number of public transportation passengers. More analysis on the positive and negative impacts of this plan will be provided in future editions of this newsletter.

- **Hybrid Cars:** Iran's largest auto manufacturing company, Iran Khodro, will start production of hybrid cars, which run on both gasoline and compressed natural gas (CNG), in early August. Iran's auto manufacturers are obligated by a government plan to switch to hybrid cars over the next few years as a way to curb rising domestic gasoline consumption and also reduce air pollution by encouraging the use of clean energy. The main hurdle faced by the auto-manufacturers has been securing enough CNG tanks for their hybrid vehicles. Iran produces over one million vehicles a year while domestic production of CNG tanks has been lower than 100,000 units per annum. Iran Khodro, therefore, is in the process of setting up its own CNG tank producing company with a capacity of 250,000 units per year which will be operational by mid-2008.
- **Natural Gas Consumption:** Iran is the third largest consumer of natural gas in the world, after Russia and the US, with over 109 billion cubic meters of consumption per year. This figure has risen by over 11% compared to the previous year. Iran's strategy is to gradually shift its domestic energy consumption from oil and its derivatives to natural gas by extending its natural gas network across the country to all cities and also encouraging CNG fuelling of vehicles. This is to free more crude oil surplus for exports which are valued higher and could be exported more easily. Iran holds the second largest reserves of crude oil and natural gas in the world.
- **Soaring Energy Subsidies:** Iran paid a total of \$42 billion in energy subsidies during 2006 which included subsidies on electricity, gasoline, diesel, and natural gas prices. From a total of \$49 billion in annual subsidies allocated for energy, basic goods and services, agriculture, medicine, publication and paper, more than 85% was spent to meet the energy needs of the country. It is worth noting that this figure almost equals the country's revenue from its main source of income, exporting oil!
- **Privatization of Petrochem Firms:** many of the subsidiaries of Iran's National Petrochemical Company (NPC) will be privatized during the current Iranian year. While NPC keeps 20% of its holdings in these companies, 40% of the shares of the firms will be allocated to underprivileged citizens under the Justice Shares scheme adopted by the government. Another 35% of the shares will be offered for the first time on the Tehran Stock Exchange, and the remaining 5% will be distributed amongst the personnel of each company.
- **Iranian Power Plant for Iraq:** a consortium of Iranian companies has been able to win an international tender for construction of a gas-based power plant in the Iraqi city of Sadr. The power plant will have two gas-based units each producing 157MW of electricity per annum and will take around two years to complete. Iranian consortium consisted of Saneer, Ameran Ofogh and MAPNA (Iran's Power Plant Project Management Company).
- **Foreign Assets:** According to the figures published by the Central Bank of Iran (CBI), the value of Iran's foreign assets grew by around 30% to over \$62 billion during the past Iranian year (ended 20 March 2007).

## 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.

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