

THIS MONTH

Market Overview **2**

July has been an extraordinary month for the Tehran Stock Exchange since the beginning of the year. All market indicators improved as there was a significant rise in trade volume and the indices closed in positive territory. The reasons for this upsurge as well as sector by sector analysis are provided in this section of the newsletter.

Turquoise Iran Equity Fund **4**

The Turquoise Fund also had a good month with its NAV rising by around 2.9%. The Fund's unit index at the beginning of August stood at 129.9. New investments were made in the Fund during the month of July, notably from international investors with significant asset management experience in Asian markets.

Country Overview **6**

Two separate sets of negotiations were conducted in July between Iranian officials and IAEA representatives to discuss Iran's nuclear program. A further meeting also took place between Iranian and American ambassadors to Iraq to jointly explore potential solutions for the country's security problems. The latest MENA report from the World Bank which includes interesting statistics on Iran is also discussed in this section.

Economy **7**

Iran's path to secure full membership at the World Trade Organization and the potential impact that it can have on Iranian industries are discussed in this edition of the Economy section.

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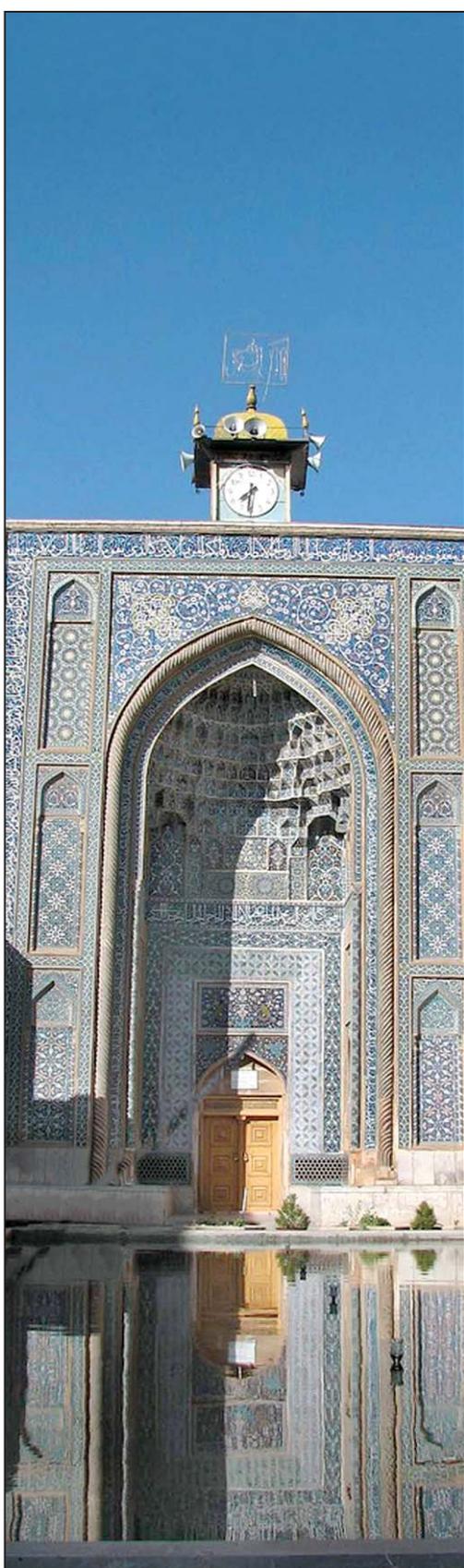
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Further information and detailed analysis of reports in this publication can be purchased directly from Turquoise Tehran office.



July has been an exceptional month for the Tehran Stock Exchange (TSE) since the beginning of 2007. All market indicators including the performance indices, the volume of trade, and the number of traders witnessed significant and sharp rises during the month. The main driving forces behind the recent growth were:

- Relative calm in international developments surrounding Iran's nuclear program.
- Market hype and dynamism created by successful Initial Public Offerings (IPO) and the consistent share price rise of recently privatized companies
- The diversion of funds from bank deposits to the stock exchange following the recent interest rate cut.

A brief analysis of some of the significant sectors on the market is provided below.

Recently Privatized Companies

The selection of these companies as a distinct group on the market has to do with their outstanding performance and liquidity over the past few months since their initial offerings. The National Iranian Copper Industries Company (NICIC) produced an overall gain of over 100% since its IPO six months ago, while shares of Mobarakeh Steel and IRALCO witnessed over 50% and 20% gains since their IPOs respectively four and two months ago. Out of the four companies offered in recent months, only one was faced with little interest in the market due to its overly regulated and restricted sector (Dashtestan Cement Company). The three above-mentioned companies however witnessed enormous demand in the market since their offerings. Their consistent share price rise and increasing demand have given the market a unipolar mode in the past few months with investors selling other holding to acquire these shares. In July, however, the growth spread to other sectors and companies supplemented by fresh funds injected into the market by institutional and private investors.

The rapid gains of the recently privatized companies created hype and dynamism in the market given the fact that many more state-owned companies are in line to be privatized and their shares slated to be offered to the market in coming months.

Petrochemical

Following the decline of petrochemical share prices in the month of June, during which this sector was the worst-performing, the demand for the shares of four listed company in this sector has increased significantly with the recent resurgence of the market. These companies experienced heavy demand queues throughout July which continued until the end of the month. The share prices and the sector index however could not gain significantly since the demand queues coupled with an imposed price fluctuation cap have locked trading. These companies are therefore expected to witness a significant share price increase once their share price is freed to rise without limitation on a *Free Trading* day, when they announce new earnings figures.

Real Estate and Construction

After months of slow movements, there has been an upsurge in trade volume figures for companies in this sector. Two of the largest companies in this sector elevated their forecasted earnings for the year by around 50% after they sold some properties with significant gains. This news however had a limited positive impact on their share prices since this was just a one-time gain.

Iron Ore Mining

Following the price rise of Iron Ore by 10%, the two listed companies in this sector (Chadormaloo and Golegozar) halted their share trading for a recalculation of their earnings. Once reopened, they announced a

20% rise in their forecasted earnings which resulted in a rise in their share price by the same margin. Generally, companies in this sector have shown strong resistance to occasional market declines in the past and as a result have secured the confidence of investors for long term investment. Both of these companies have also had plans to double their production capacity by the end of this year but in the case of Goleghar this has now been postponed to next July. These expansion plans however have raised investors' expectations and increased the PE ratio of these companies to over the market average.

Leasing

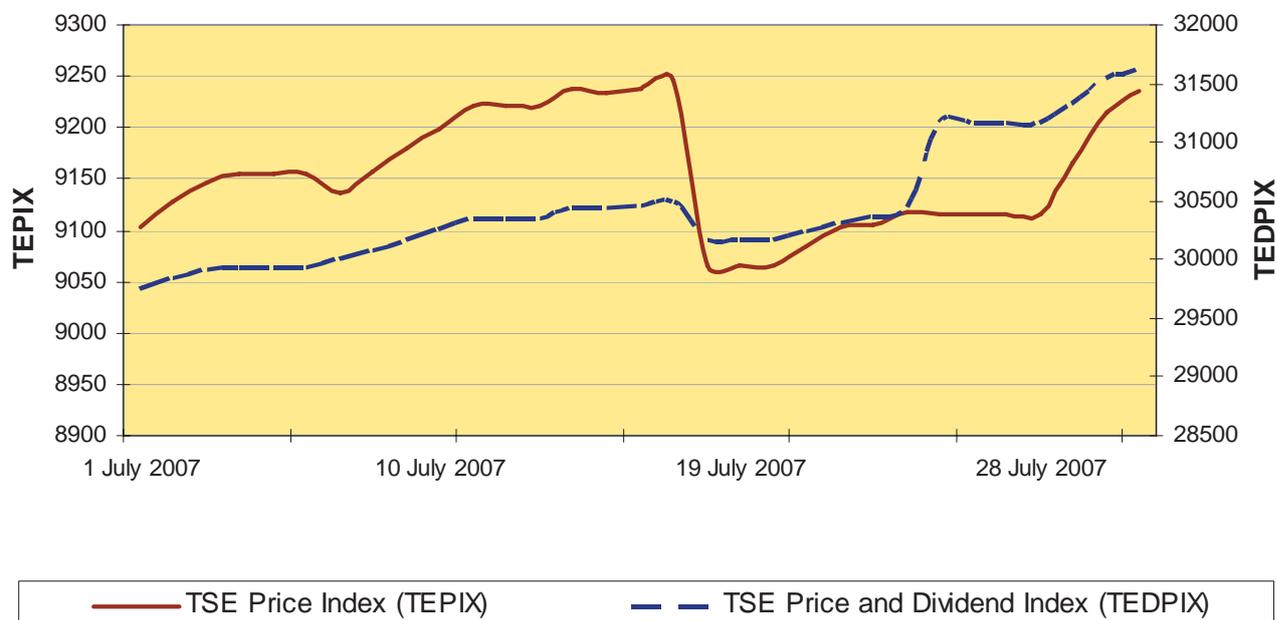
Since the approval of the interest rate cut from 17 to 12 percent by the government, there has been a heavy sell off and supply queues for the Leasing stocks. On average, the Leasing companies are trading at PE ratios of only 2.3. However, the decline of the sector has continued during July. Experts believe that the 12% interest rate of the state-owned banks and the lack of access to foreign financing sources has made it unfeasible to continue with leasing services at current interest rates.

Automotives and Parts

This was one of the only sectors that witnessed an overall decline during July. Even at PE ratios of around 2, there was little interest in stocks from this sector. Analysts believe that the automobile and parts manufacturing sector is facing some fundamental problems such as lack of competitiveness, market saturation, difficulties surrounding part imports following the two sets of UN-imposed sanctions as well as gasoline rationing that was recently put in place by the government.

The recent upward trend of the market made up for the slow and declining market during the first few months of the Iranian year (began March 2007). During July, the TSE Price and Dividend Index (TEDPIX) grew by 6.3% to stand at 31621. This performance represented a record increase for a single month in over three years. The trade volume also witnessed a significant rise of 20% to stand at \$505 million for the same month. The following chart demonstrates the performance of two of the TSE indices during July.

Performance of TSE Indices (Jul 2007)

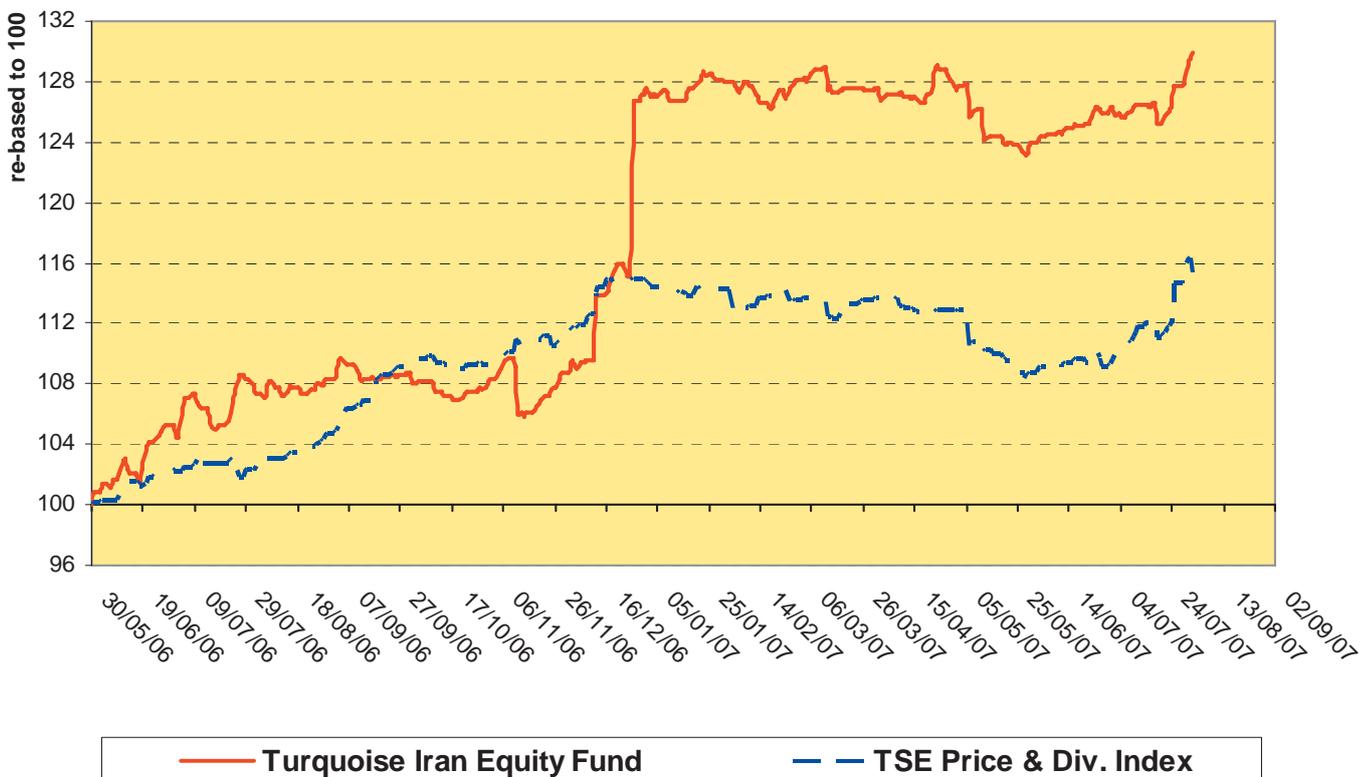


Investment Objective – The Turquoise Equity Fund seeks superior long-term capital growth by investing in the consumer and commodity potential of Iran, one of the most under-valued emerging markets in the world. Combining international experience with local expertise allows Turquoise to provide superior 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 2.9% during the month of July. The Fund outperformed the TSE Price Index (TEPIX) which gained 1.4%. However, due to the AGM season and dividend announcements, the TSE Price and Dividend Index (TEDPIX) grew by around 5% in the same period. The Fund’s unit index grew from 126.3 to 129.9 during July. The Fund attracted new investment in July including the entrance of a highly experienced Asset Manager focused on Asian securities.

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. The performance table also shows the performance of the Fund in different time frames.

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

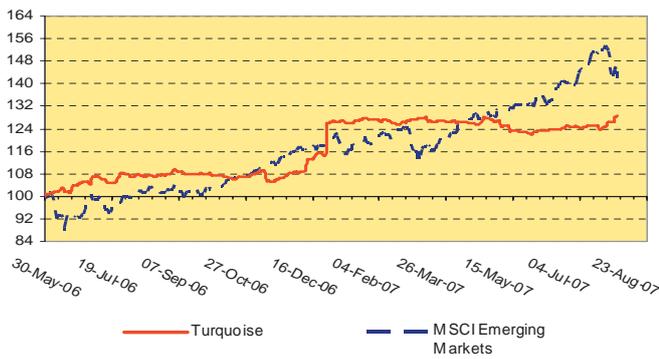


	1 Jun 07	1 Jul 07	1 Aug 07
Turquoise Fund	23.93 %	26.29 %	29.91 %
TEDPIX	8.79 %	9.56 %	15.37 %

Performance

Period	Fund Return
Jul-07	2.86%
Last 3 Months	1.96%
Last 6 Months	1.50%
Last 12 Months	20.67%
Since Inception (30 May 06)	29.91%

Turquoise Performance vs. MSCI Emerging Markets



Turquoise Performance in US Dollar (US\$)



Turquoise Performance in Euro (€)



Turquoise Performance in British Pound Sterling (£)



During the month of July, Iran's negotiating teams were involved in two separate sets of discussions with representatives of the International Atomic Energy Agency (IAEA) in Vienna regarding a possible framework to resolve the remaining issues concerning Iran's nuclear program and also with representatives of the United States in Iraq regarding mutual interests in seeing a secure and stable Iraq. The result of both negotiations looked promising.

In Vienna, both parties confirmed that the negotiations were constructive. This was more apparent when Iran allowed inspectors of the IAEA to visit its heavy water plant in Arak after months of denying them access. Generally, there was a positive view in Tehran that the Iranian nuclear dossier, which was referred to the UN Security Council, is being discussed again at the IAEA which is more of a specialist body.

In discussions with the US over Iraq, both parties continued with their old rhetoric in public, but during private discussions they agreed to set up a trilateral committee consisting of experts from Iran, Iraq and the US to look into possible cooperation in improving the deteriorating security situation in Iraq. Formation of this committee was the first tangible result of the US-Iran negotiations which had some significance. On the one hand, the US seems to have recognized Iran's ability to strongly influence events in Iraq while Iran has recognized the need to have direct negotiations with the US over regional issues that concern the national interests of both countries.

The publication of the MENA (Middle East and North Africa) Report by the World Bank, in which some of the positive and negative aspects of the Iranian economy were discussed, was another noteworthy development in July. According to this Report, the rising figures of non-oil exports and foreign currency deposits are the positive elements of the Iranian economy while the high inflation rate and increased government expenditure figures are problematic indicators. This report puts Iran's annual growth rate at 4.4% and 5.8% in 2005 and 2006 respectively.

Some of the more interesting figures in this report are:

- Women's participation in economic affairs up from 33% in 2001 to 41% in 2006
- Number of female graduates starting a career has risen by 10% every year between 2000 to 2005
- Export of goods and services grew by 280% from \$18.7 billion (20% of the GDP) in 1999 to \$70.5 billion (36% of the GDP) in 2006
- Foreign currency deposits of the country grew by 450% from \$9 billion in 1999 to \$49.6 billion in 2006

Iran is currently preparing for negotiations with the World Trade Organization (WTO) for full membership status. In this edition of the Economy section, a brief study of opportunities and threats posed by Iran's membership in the WTO is provided for some of country's main industries and sectors.

Automobile and Auto Parts

Currently there is a 90% tariff on import of all foreign-made vehicles. This is while the profit margin of Iran's auto manufacturers is only around 9.5%. This margin has dropped in recent years from 28% in 2002 due to the government's policy of keeping the price of domestically produced vehicles unchanged while inflation has been running at over 12% annually in recent years. This situation will make any future competition hard for this industry as the tariffs will have to decrease over time while the Iranian auto manufacturers have only a 9% range of manoeuvre with their current prices. It is worth noting that imports of foreign-made cars were totally banned in Iran from 1995 to 2003. In 2003, the ban on imports was lifted but a 170% tariff was introduced. The tariff was later reduced to 130% in 2004, 100% in 2005, and 90% in 2006 and 2007.

Steel

From early 2006, the tariffs for steel ingot and sheets were reduced first to four and then later to zero percent. This is why Iranian steel products (mostly produced by Mobarakeh Steel and Khuzestan Steel Companies) are currently competing with their foreign rivals in global prices and on the Tehran Metal Exchange. The cost of production of each ton of steel ingot in Iran with subsidised raw material and energy is currently at \$400 which, given the global price of around \$550, produces a safe and significant profit margin. It is worth noting that in other parts of the world where energy is not subsidised, the production costs are around \$450 per ton. The no tariff policy on steel imports and Iran's competitive advantage in the energy sector means that the steel industry could stay competitive even after Iran's membership in the WTO.

Iron Ore

Iran is rich in iron ore resources. Currently the price of iron ore for use at steel production facilities in Iran is set by the government, which has recently increased it from \$40 to \$50 per ton. This is significantly lower than the global prices of \$68 for the Persian Gulf FOB. Adding the transportation cost, which is quite high considering the size and weight of the materials, Iranian steel producers have to pay around \$90 for each ton of iron ore to be imported and transferred to their manufacturing complexes. This provides a unique opportunity for Iranian iron ore producers which are very competitive in Iran and can even look at export opportunities once their production capacities grow. In this sector too, WTO membership will not impact the industry negatively.

Sugar

Iran has dropped the tariffs on sugar from 190% in 2005 to 10% for white sugar and 4% for raw sugar in 2007. This has caused serious difficulties for domestic sugar producers and beetroot farmers who can not compete with global producers. Producing a ton of sugar in Iran costs around \$500; this is while global sugar prices after recent declines are currently settling at around \$400. This means that most probably, the Iranian sugar industry will not be able to compete internationally and will lose out to foreign producers in the long run.

Cement

The cost of production of cement in Iran is currently very low at the extraordinary level of \$25 per ton. This is because of the cheap and heavily subsidized energy that is required in large amounts for the production of cement. The sell price of cement in Iran is currently set and fixed by the government at \$30 per ton which is very cheap even in comparison to India (\$70 per ton) that offers one of the lowest prices in the world. These facts coupled with the high transportation cost of cement means that not only does Iran have absolute domestic competitiveness, but it can potentially capture foreign markets once the domestic market

is saturated, This sector is therefore safe from shock waves created by WTO membership and in fact could even benefit from it to enter new global markets.

Household Goods and Textile

There had been a few years when the domestic textile and household goods producing companies were on the verge of bankruptcy due to the lifting of all tariffs on these products in the late 1990s. This is why the share of these two sectors together in the country's GDP was only about 0.1% in 2006. Recently, there have been new tariff rates for Household and White Goods (around 60%) but analysts believe that it was too little too late. These two sectors are also suffering heavily from the rising smuggling of goods from countries like China. Since most of the companies active in these sectors have already lost out to their foreign competitors, it is not expected for WTO membership to significantly impact figures of the remaining operating companies.

Petrochemical

Petrochemical complexes could be divided into two categories: gas-based and naphtha-based. The government, as the sole producer of naphtha and natural gas, is currently selling these two commodities with discounts of 30% and 90% respectively which makes the production of petrochemical goods very competitive in Iran. Naphtha-based companies are now experiencing a profit margin of around 30% while the gas-based companies are enjoying profit margins of around 70%. Companies from both groups are selling large portions of their products in global markets which means that not only is this sector competitive domestically, it can also secure good market share at the global level. In fact, for the petrochemical sector, WTO membership could help significantly increase its presence in global markets and secure foreign currency income for the country.

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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