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## Trump unlikely to grant sanctions waivers for EU banks/oil traders

*Greg Priddy – DaMina Senior Fellow, Oil Geopolitics*

The May 8 decision by President Trump to unilaterally pull out of the Iran nuclear deal reached in 2015 was widely anticipated by capital markets, but not completely priced into the crude oil market by the time it was announced yesterday. While the assumption that Iranian exports will decrease in an already tightening physical market is largely priced in, the heightened risk of interstate military conflict in the Middle East. Looking forward, the summer months are likely to witness heightened UK Brent price volatility as there are still many unresolved questions about exactly how the US decision will impact other key actors.

|   | Country/Region                      | bpd              | % of total |
|---|-------------------------------------|------------------|------------|
| 1 | China                               | 622,000          | 28%        |
| 2 | India                               | 470,000          | 21%        |
| 3 | South Korea                         | 361,000          | 16%        |
| 4 | Turkey                              | 240,000          | 11%        |
| 5 | Italy                               | 200,000          | 9%         |
| 6 | Japan                               | 170,000          | 8%         |
| 7 | France                              | 100,000          | 4%         |
| 8 | Spain                               | 80,000           | 4%         |
|   | <b>EU total Iranian oil imports</b> | <b>620,000</b>   | <b>28%</b> |
|   | <b>Total exports</b>                | <b>2,243,000</b> |            |

Source: Middle East Economic Survey

### US sanctions to bite after 180-day grace period

The most important US sanctions being restored are the secondary banking sanctions under the National Defense Authorization Act of 2011 (“the NDAA sanctions”) which threaten to cut off US ties to banks and oil trading firms which provide clearing services for Iranian oil payments. These sanctions were amended to also target oil marketing companies that buy Iranian oil (including indirect resales), as well as exporters of services and equipment to be used in Iran’s oil industry. The sanctions on upstream investment under the Iran Sanctions Act (ISA) of 1996 also will come back into force. The US Treasury Department, which administers the sanctions, has clarified that there will be a 180-day implementation period prior to the imposition of sanctions, but also advising companies to begin curtailment of their purchases now. As before when US secondary sanctions were implemented in 2012, US law allows for the issuance of waivers which would allow continued purchases of Iranian crude oil for countries which “substantially” reduce their purchases. The reductions in purchases of Iranian crude oil will begin right as the market reaches peak seasonal tightness in the early summer.

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### ABOUT DAMINA

DaMina Advisors is a preeminent Africa-Asia focused independent frontier markets political risk research, due diligence, M&A transactions consulting and strategic geopolitical risks advisory firm.

DaMina Advisors is legally registered and has offices in the US, Canada, The UK and Ghana. DaMina is headquartered in Toronto.

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## **Efforts of EU/China/Russia to maintain the deal will not negate impact of US sanctions**

Trump did not just passively let the US sanctions waivers lapse – he definitively pulled the US out of the deal and slammed the door shut. There was no talk of future efforts to “improve” or “fix” the deal. Trump also alluded at the end of his remarks to the view that the Iranian people aspire to a better system of government, implying that US policy has shifted toward regime change – undermining Iran’s government economically rather than seeking to use that as pressure to force them back to the negotiating table to make further concessions. This is a very important point.

All of the other signatories to the JCPOA, including the EU-3 (UK, Germany, France), Russia, China, and Iran have put out statements denouncing the US move and taking the position that the agreement is still in force. Iranian President Rouhani also has indicated that Iran considers the deal to still be in force, preferring to avoid immediate action to restart nuclear activities curtailed under the JCPOA, and let the US be the one which is isolated diplomatically. In the case of Europe, there is talk of taking actions to insulate European businesses from the impact of US sanctions. In practice, however, there is no way that European banks or oil companies are going to take the risk of being sanctioned by the US. Their exposure to the US is simply too large to take this risk, and even in the more than two years since Obama approved the waivers in January 2016, most European banks have not wanted to get involved in oil transactions with Iran. For the companies involved, even those with minority state ownership, this is a business decision, and their governments’ diplomatic stance will not be the deciding factor. Given the availability of alternative supplies, most European buyers will want to steer clear of Iranian supplies altogether, and their purchases will drop off well before the 180-day mark. Japan and South Korea, while unhappy with the move by Trump, will at least substantially reduce their purchases, and would have to go back to the escrow accounts used for payments under sanctions, in which Iran is unable to repatriate the yen/won it receives for the oil, and has to use the funds on deposit for purchases of goods from those countries.

China almost certainly will not comply with this sort of diktat by the US, though the Chinese government may not explicitly state this intention. India also has a very independent foreign policy, despite its growing security ties to the US and Japan, and probably will not comply. Turkey, which is heavily dependent on Iranian oil and has strained ties with the US, also may not comply. This will create a market in “distressed” barrels, in which Chinese and Indian buyers will offset some but not all of the decrease in purchases elsewhere. The net loss of Iranian supply will not be half of the total, therefore, but more like the range of 300,000-500,000 bpd.

## **Lingering sanctions questions to drive crude price volatility**

While the assumed loss of this volume of Iranian oil is mostly priced in at this point, there is immense potential for volatility driven by all of the unanswered questions about the medium-

term impacts later this year. There is a significant range of uncertainty around exactly how much volume will be lost, and precisely how all of the relevant governments will respond.

Provocations in regional hotspots like Syria and Yemen also will drive volatility, with the Israeli strike on Iran-linked targets in Syria yesterday and today's missile launches against the Saudi capital by Iran-aligned Houthi rebels in Yemen driving some of the recent price move. Both of these conflicts have the potential to escalate into direct Israel-Iran or Saudi-Iran clashes, even though that remains the less likely outcome in the near future. If Iran chooses to resume its halted nuclear activities after its initial forbearance, this will sharply increase the risk of interstate conflict.

Lastly, the Trump administration will feel free to put pressure on the Saudis and other Gulf Arab producers with spare capacity to offset the loss of Iranian barrels. Saudi Crown Prince Mohammed bin Salman would clearly like to see prices higher for his own short-term ends including the upcoming Saudi Aramco IPO, but US Treasury Secretary Steven Mnuchin already has alluded to the need for this. Unlike 2012, it is not clear how the Saudis will respond, as the Saudi/OPEC (Russia) deal on production ceiling may limit Saudi flexibility, but US pressure on them could escalate given that Trump believes they now owe him a big favor.

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to schedule any in-depth Q&A's with Greg Priddy

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