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TURQUOISE PARTNERS

Taagh Bostan, City of Kermanshah , Western Iran

THIS MONTH

Market Overview 2

In October, the Tehran Stock Exchange (TSE) experienced another month of price rallies and high trade volumes. This was principally driven by the commodity, engineering and automotive sectors. In this month, Alborz and Day insurance companies were listed on the TSE and the Iranian OTC respectively.

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The Turquoise Iran Equity Investments portfolios had another positive month in October. Portfolio One NAV gained 6.5% in value and Portfolio Two NAV gained 4.3%. This section provides data and charts on the performance of the portfolios.

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Following a month of price corrections and market volatility in October, the Tehran Stock Exchange (TSE) once again returned to the bullish trend and large trade volumes of the past few months. By the end of October, the TSE market main index was up 53% since the beginning of the Iranian calendar year (21st March). This was the highest gain for this period in 6 years. Stocks of many commodity-related companies, which experienced price corrections in September, returned to positive territory in October. Among these, zinc and lead producers were once again among the top gainers. This was mainly due to the resilience of global commodity markets.

Historically, October is an important month for the TSE, as first half earnings results are published. This year, in most cases, results were in line with or exceeded analysts' expectations. Despite the positive short-term sentiments towards the market, some analysts have a more bearish longer-term view. They argue that both the domestic business and economic environment in the second half of the year will not be as benign as the first, and that earnings performances will not be as strong. They also add that the uncertainties surrounding the implementation of the economic reform plan (see Country Overview) pose risks to the equity market as a whole, particularly stocks of companies with high energy consumption.

Looking ahead, a combination of profit taking, short-term speculation, the economic reform plan and political developments, are expected to result in increased market volatility over the next few months.

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

IPO of Alborz Insurance

On 7th October, a 10% stake in Alborz Insurance was offered on the TSE, as part of the ongoing privatisation programme. This was the first insurance company to be listed on the TSE and also the first state-owned insurance firm to undergo privatisation. This IPO attracted significant interest on the market and the government sold off a further 20% of the company's shares on subsequent days. Investors purchased the shares at an earnings multiple of 7.5 at the IPO. This was approximately two multiples higher than the financial services sector average. This put the market capitalisation of Alborz Insurance at $160 million. Alborz Insurance shares were up 40% by the end of the month.

Last year, Alborz Insurance had a 5.9% share of the total insurance market premiums and a 6.2% share of the market's total payout. Its payout ratio stood at 73%, lower than the market average of 85%. The net earnings forecast for the current financial year (which ends on 20th March 2010) is $21.1 million.

Engineering services

This was the best performing sector in October. MAPNA Group, the largest company in this sector, was the leading stock. MAPNA is a power plant management and engineering services group with electricity production capacity in excess of 5,000 Mega Watts. News about the disposal of a 20% block in MAPNA by the government has been driving up the share price. In addition, analysts expect MAPNA to benefit from the removal of subsidies on electricity, as part of the economic reform plan.

The sector index gained 27% in value in October.

Automotive Manufacturing

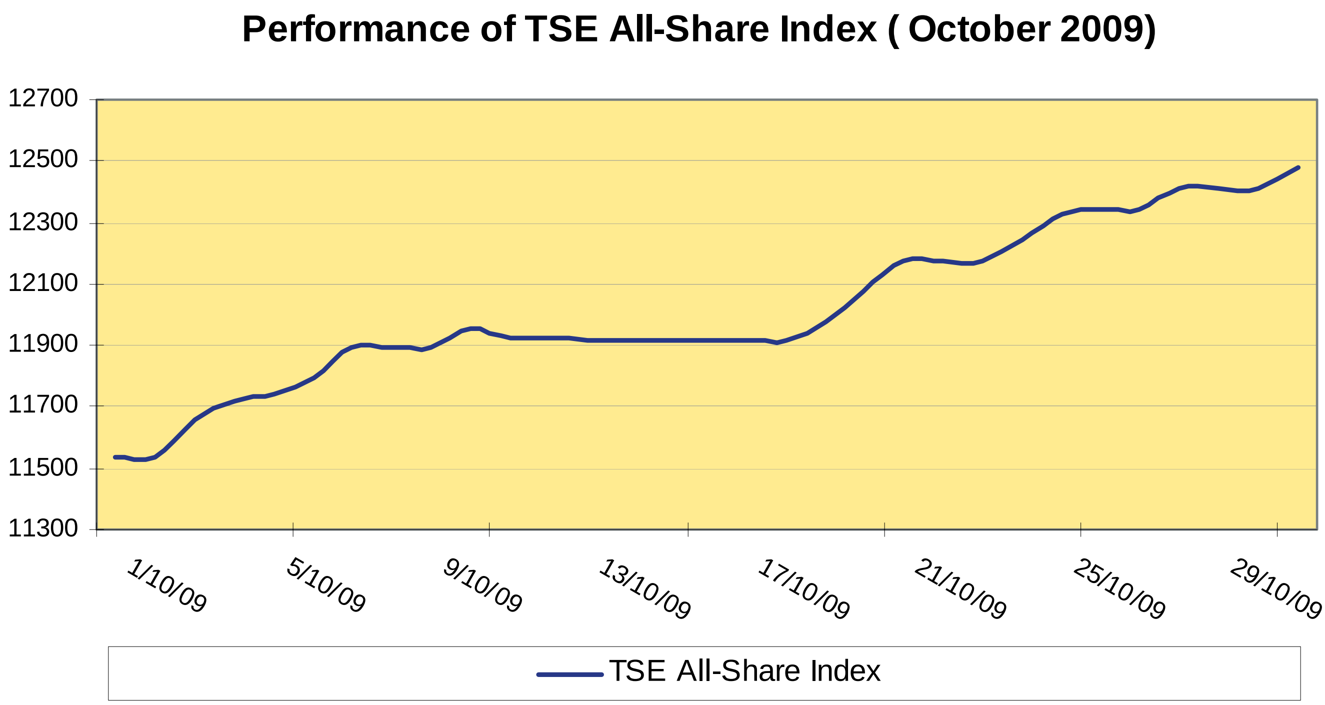
Recent rallies in these stocks have taken many analysts by surprise. The sector index gained 22% in October. Speculation about a possible disposal by the government of shares in Saipa and Iran Khodro, Iran's two largest car manufacturers, is viewed as a possible reason for the recent gains. However, most experts argue that there is little fundamental rationale behind the gains and the sector as a whole continues to face difficult business conditions. Iran Khodro was recently bailed out by the government and its stock has been closed to trading for over 6 months.

Latest Developments in OTC

The Iranian Over-The Counter (OTC) market officially commenced its operations in September. On 21st October, a 2.5% stake in Day Insurance was sold on the OTC at a total market capitalisation of $45 million. Day Insurance was founded in 2004 and has a diversified portfolio of insurance products, ranging from life products through to general contracts such as car insurance.

The second fixed income instrument was listed on the OTC this past month. On 13th October, Keshavarzi Bank successfully issued $50 million of tradable term deposit papers. These papers have a tenure of 1 year and pay a coupon of 15% per annum on a monthly basis. Last month, EN Bank listed $5 million of term deposits on the OTC.

Overall, the Tehran Stock Exchange had a positive month in October, with the TSE All-Share Index gaining 8.2% in value. Trade volumes stood at $1.1 billion, a 51% increase from the previous month.

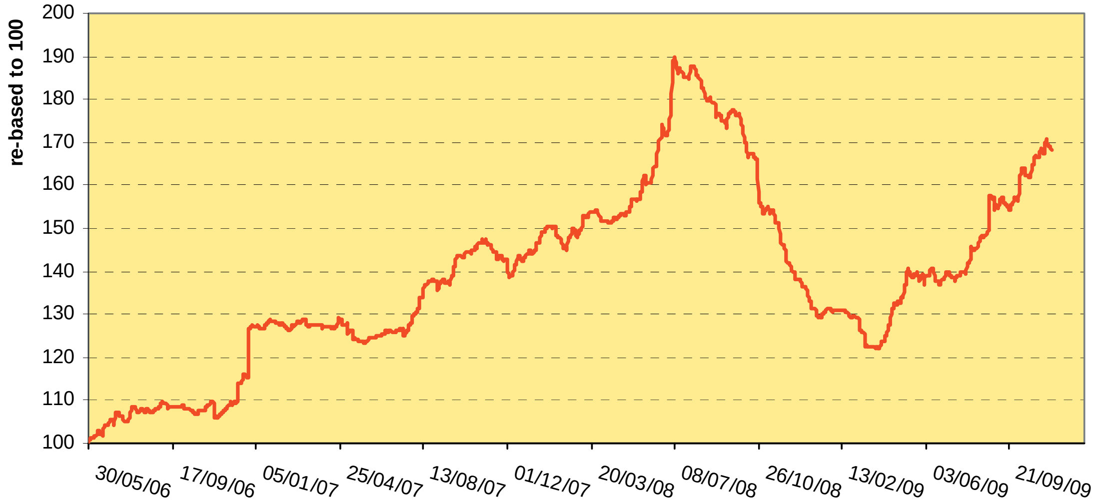


Investment Objective – The Turquoise Equity Investments seeks superior long-term capital growth by investing in the consumer and commodity potential of Iran, one of the most undervalued emerging markets in the world. Turquoise combines international experience with local expertise in investing in equities 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

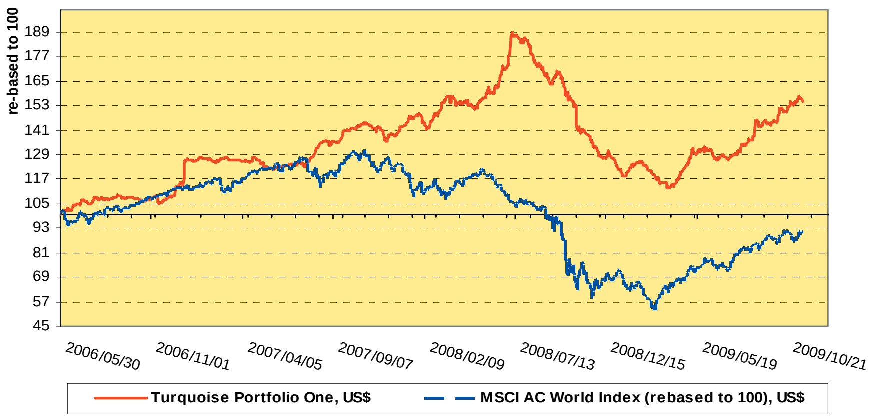
Investment Vehicle Pars Pelican Firouzeh	**Currency** Iranian Rial (IRR)	**Management Fee** 2.5% p.a	**NAV Calculation** Daily
Vehicle Domicile Iran			**Liquidity** Quarterly
Launch Date 30 May 2006	**Benchmark** MSCI All Countries (AC) World Index, US$	**Carried Interest and Hurdle** 20% - 8%	**Minimum Investment** US$100,000

Turquoise Portfolio One, Iranian Rial - As of 15th November 2009



	Aug 09	Sep 09	Oct 09
Turquoise Portfolio One	⬆ 10.8 %	⬇ 0.2 %	⬆ 6.5 %

Turquoise Portfolio One vs. MSCI AC World Index, US Dollar As of 15th November 2009



Portfolio One Performance, IRR

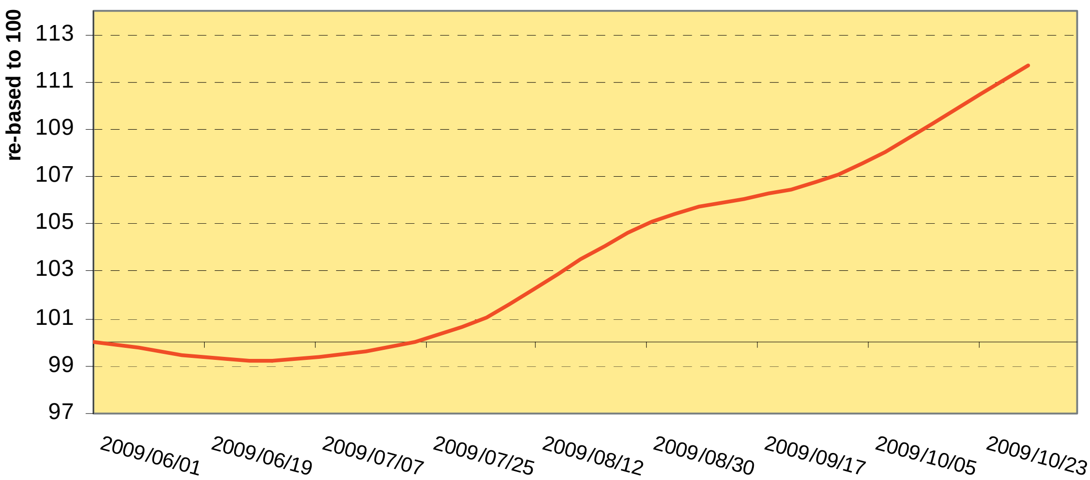
As of 15 November 2009

Period	Portfolio Return
Last Month	⬆ 3.5 %
Last 3 Months	⬆ 13.5 %
Last 6 Months	⬆ 20.9 %
Last 12 Months	⬆ 9.3 %
Since Inception (30 May 06)	⬆ 68.0 %

Portfolio Two

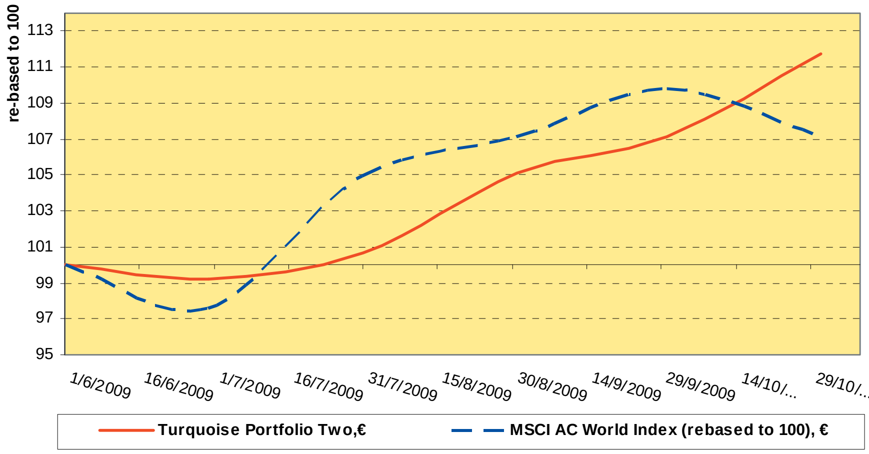
Investment Vehicle Turquoise Partners Ltd.	**Currency** Euro (€)	**Management Fee** 2.0% p.a	**Liquidity** 3 years lock-up with annual liquidity provisions
Vehicle Domicile British Virgin Islands	**Benchmark** MSCI All Countries (AC) World Index, €	**Carried Interest and Hurdle** 20% (High Water Mark Applies)	
Launch Date 01 June 2009		**NAV Calculation** Monthly – by Administrator	**Minimum Investment** €200,000

Turquoise Portfolio Two, Euro - As of 31th October 2009



	Aug 09	Sep 09	Oct 09
Turquoise Portfolio Two	⬆ 4.4 %	⬆ 1.9 %	⬆ 4.3 %

Turquoise Portfolio Two vs. MSCI AC World Index, Euro As of 31th October 2009



Portfolio Two Performance, €

As of 31 October 2009

Period	Portfolio Return
Last Month	⬆ **4.3 %**
Last 3 Months	⬆ **11.0 %**
Last 6 Months	**N/A**
Last 12 Months	**N/A**
Since Inception (01 June 09)	⬆ **11.7 %**

The latest developments on the economic reform plan will be discussed in this edition of Country Overview.

In June 2008, Ahmadinejad announced details of a plan called the “economic reform plan”. This plan proposes reforms in seven key parts of the economy, including the taxation, banking and customs systems. However, plans for a major restructuring in the subsidies regime, known as the “targeted subsidies plan”, has proven to be by far the most controversial element of the economic reform plan. According to the government, approximately $100 billion is spent on subsidising the prices of fuel, energy and many consumable goods each year. The government argues that this has put a huge burden on its budget and is slowing down economic growth. The government believes that subsidies need to be targeted towards lower income social classes and the most vulnerable sectors and industries in the economy.

The government recently submitted its first proposal to the parliament for approval, but it was rejected. After numerous revisions to the original proposal by the government and the parliament’s economic reform specialist committee, the proposed bill finally made it to parliamentary open sessions. After two weeks of heated debate between the parliament and government representatives, the main terms of the proposal were finally approved. However, disputes between the parliament and government over the operational details and the implementation mechanism have brought the process to a halt.

The targeted subsidies bill, as approved by the parliament, obliges the government to remove subsidies currently paid on electricity, fuel, gas, water and most consumable goods - mainly sugar, rice, cooking oil and bread – gradually and over a period of 5 years. The government will continue to subsidise medicine and agricultural seeds. The bill defines price targets to be achieved by the end of the 5th year. For example, at the end of year 5, the consumer price of gasoline and diesel will be 90% of that of the Persian Gulf Freight On Board (FOB) price. For natural gas, the price will be 75% of the average export price, and for water and electricity, the price will be at production cost. The plan will commence with energy, fuel and utilities in the first year and consumable goods will start in the second year.

In the first year of the plan, proceeds from the removal of subsidies must be no less than $10 billion and no more than $20 billion. Estimates indicate that the government has to increase existing prices by an average of 2.5 times to achieve the lower target and by 4 times for the maximum target. Of the proceeds, 20% will be allocated to the government to compensate for increased costs. 30% will go to industries and to improving the efficiency of the utility, fuel and energy production infrastructure. The remaining 50% will be distributed among targeted social classes, either as cash payments or as non-cash assistance. In addition, preferential pricing will be in place for certain industries and regions in the country. For example, petrochemical companies, which use natural gas as their feedstock (rather than fuel), will pay no more than 65% of the average export price (rather than 75%) for a period of 10 years.

This plan has its supporters and critics among senior economic and political figures. However, two aspects of the plan have brought about the biggest divide among experts. Firstly, opinions vary significantly about the inflationary effects of the plan and the ways to tackle it. The government estimates that the excess inflation that will be caused by the plan in the first year will be approximately 15%. At the other end of the spectrum, the parliament’s economic committee puts this figure at 40%. Secondly, the plan delegates power to the government to define eligible social groups and distribute the proceeds among them. The opposition warns that this mechanism is likely to lead to discrimination and corruption, and will have serious social consequences. The government is required to present its strategy for the identification of target groups and the distribution of funds, to the parliament later this year.

The dispute reached its peak when operational aspects of the plan were discussed in the parliament. In its plan, the government proposed that proceeds from the removal of subsidies go into a designated account, over which the government would have full control. However, the parliament opposed this, arguing that it violates the Iranian Constitution. Instead, they argued that funds should go into the national treasury account and that the plan itself should become a part of the state budget. This would be so that the parliament would have oversight on the plan's progress. On 3rd November, Ahmadinejad unexpectedly attended the parliamentary open session in order to defend the government's position. He reasoned that the government would not be able to successfully implement the plan unless the parliament approved the proposal, and threatened to retract the bill if the parliament made any amendments. The parliament also took a firm stance against the government, and progress came to a halt. According to media reports, a special committee, consisting of representatives of the parliament and the government, has been formed in order to resolve the dispute. If this committee does not come up with a workable solution, then intervention from higher supervisory bodies may become necessary.

Iran's Insurance Industry

Although insurance services have been offered in Iran by foreign companies since the nineteenth century, an insurance industry was first established in Iran in 1935, when the first domestic insurance company, Iran Insurance Ltd, was founded. With the approval of the first insurance law by the parliament in 1937, the insurance industry expanded and several other private and state-owned companies were formed. In 1971, the government of the time established the Central Insurance Co. of Iran in order to regulate insurance activities. This entity remains the regulatory body for this industry in Iran today. After the 1979 Islamic Revolution and the consequent nationalisation of the insurance industry, several firms lost their operating licenses and others were consolidated. The result was that the 12 active firms were reduced to 3 state-owned entities.

Despite a sharp growth over the past two decades, insurance remains one of the least developed sectors of the financial services industry in Iran. In 2008, the total insurance premiums generated in Iran were $4.3 billion. This is less than 0.1% of the world's total, while Iran has approximately 1% of the world's population. The insurance penetration rate is approximately 1.4%, significantly below the global average of 7.5%. This underdevelopment is also evident in product diversity. Approximately 60% of all insurance premiums are generated from car insurance. Also, 95% of all premiums come from general insurance contracts and only 5% relate to life products. Payout ratios have shown consistent growth over the years. Last year, the industry average payout ratio was 86%. Restrictive regulations on the premiums of certain general insurance products, mainly car insurance, mean that profit margins are thinning out in these business streams. As a result, firms have begun to diversify their businesses into new products such as home and building insurance and life assurance.

Up until 2001, the Iranian insurance industry was completely state-owned. Experts believe that this was the main reason for the slow development of the industry. In that year, the parliament approved a by-law, allowing for privately-owned firms to enter the market. At the end of 2008, there were 20 insurance firms active in the market, only 4 of which were state-owned. With a 75% market share, state-owned firms still dominate the Iranian insurance industry. Nevertheless, the private sector's market share has been growing consistently year-on-year. The ongoing privatisation programme includes insurance companies. In October, Alborz became the first state-owned insurance firm to undergo privatisation through an exchange listing (see Market Overview). Dena and Asia insurance are also expected to be privatised in the near future. Re-insurance is in its infancy in Iran. For many years, Iranian insurance companies have had to rely on foreign firms and markets, such as Lloyds of London, to obtain re-insurance. However, with the implementation of new regulations regarding re-insurance and the establishment of 2 re-insurance firms, there are signs that this business stream will expand domestically in years to come.

Analysts have a bullish long-term view on the Iranian insurance sector. There is not only tremendous scope for growth and expansion in the industry, but also emphasis on the promotion and development of the insurance industry in the Iranian 20 year outlook plan. There is a need for deregulation within the industry, something that is fully recognised by the authorities. The Central Insurance of Iran, along with the Insurance High Council (a high level supervisory body) is taking steps towards liberalising contract premium pricing mechanisms, something that is vital for keeping the industry competitive. Regulations are also under review in order to move towards international standards such as the Solvency capital adequacy regime. However, limitations on expertise will be the biggest challenge along the way.

Iran's Foreign Currency Reserves

In October, the Trade Promotion Organization of Iran (TPOI) announced that the government has begun the process of converting all national reserves and the country's trade currency from the US Dollar into other currencies, mainly Euro. According to the government, this switch is purely for financial reasons. It argues that the Dollar is becoming increasingly weak and that it is in Iran's best interests to replace its Dollar reserves with other currencies. However, many experts believe that there are also political motives behind this change.

In December 2007, the Central Bank announced that it had sold off its petrodollar reserves and pegged the Iranian Rial to a basket of currencies consisting mainly of the Euro, but also Japanese Yen, the UAE Dirham and other currencies. However, examination of the Rial exchange rate to date reveals that the Iranian Rial has had a relatively stable exchange rate against the Dollar, while the Rial/Euro rate has fluctuated considerably. Experts also assert that, although Iran is now receiving 85% its oil revenues from currencies other than the US Dollar, a complete shift in trade from the Dollar is not achievable. The US Dollar remains the main currency for cross-country trades and it is not always feasible to trade in other currencies.

Iranian Petroleum Exchange

With the completion of the second and final phase in October, the Iranian International Petroleum Exchange (IIPE) became fully operational. The exchange was inaugurated in February 2008 at Kish Island in the Persian Gulf, which is an off-shore centre. In the first phase, only petrochemical products such as polyethylene and methanol were traded on a spot basis and in Iranian Rial. However, with the completion of the second phase, crude and by-products of oil can also be traded on the exchange in both Iranian Rial and Euro. According to the Oil Ministry, Iran is viewing the IIPE as a platform for exporting its oil and petrochemical products in the future.

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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