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TURQUOISE PARTNERS


A View of the Tehran Stock Exchange Trading Floor

## THIS MONTH




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Following a strong performance since the beginning of the Iranian calendar year (21st March), the Tehran Stock Exchange (TSE) had a relatively calm month in May. Sharp falls in the global prices of metals, crude oil and other commodities in May resulted in a sudden change of sentiment in the market. Speculative trading also decreased significantly this past month, resulting in lower price volatility.

The resilience of the market against any significant price falls was notable. The TSE main index was unchanged this past month. The buying appetite of the past few months dissipated quickly in May, but most stocks did not experience any selling pressure either. However, analysts believe that if global prices continue to fall, the TSE will also suffer a downturn.

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

### Telecom

Telecommunications Company of Iran (TCI) has undoubtedly been the most controversial case of privatisation, especially after the transfer of its control from the government to a quasi-governmental consortium.

This year's AGM, which took place in May, also witnessed a dispute between Tose'e Etemad Mobin, the majority shareholder on the one side, and the government as a shareholder and the Securities and Exchange Organisation (SEO) on the other side. TCI's annual results showed a net profit of $1.5 billion for the year and the Board of Directors declared a total dividend of $1.4 billion. The latter parties strongly objected to the dividend, arguing that some of this profit is due to changes in accounting and reporting procedures and that a dividend payout ratio of over 90% could jeopardise the company's expansion plans. Nevertheless, the majority of votes were in favour of this dividend payout.

Tose'e Etemad Mobin consortium acquired the 50% plus one share block last year on an instalment basis. Analysts are of the view that the consortium is planning to use the dividend to fund the instalment payments and has therefore pushed for an unusually high payout at the AGM.

### Automotive

This sector has experienced much volatility over the past few months. For some time, the government has intended to sell blocks of shares in Iran Khodro and Saipa, Iran's two largest car manufacturers, as part of the ongoing privatisation programme. However, the offering has been postponed several times for a variety of reasons. Speculation and contradictory news over the past few months has meant that these two stocks have either had significant buying demand or selling pressure.

In the 3rd week of May, the Iranian Privatisation Organisation announced final plans for the government to offer the blocks. Accordingly, an 18% stake in each company will be offered in the third week of June at a 50% to 80% premium to market price.

In this month, the government successfully sold a 17% block of shares in Rena Investment Co. for the sum of $68 million. Rena has approximately 85% of its portfolio invested in the automotive sector. An interesting fact about this deal is that the block was bought by Saipa. Rena owns a 9% stake in Saipa. Analysts believe that by purchasing this block, Saipa is attempting to indirectly retain control of itself.

### Metals

This sector experienced the greatest price decline this past month, due to falls in global prices of metals. In May, the National Iranian Copper Industries Company (NICIC) and Mobarakeh Steel, the second and third largest listed companies on the TSE, released an earnings update for the financial year ended 20th March. Both companies out-performed their latest earnings forecasts by 18% and 12% respectively. Despite the out-performance, both stocks re-opened lower. This reflects investor concerns about the falls in the price of metals.

The metals sector index lost 7.5% of its value in May.

## Pharmaceuticals

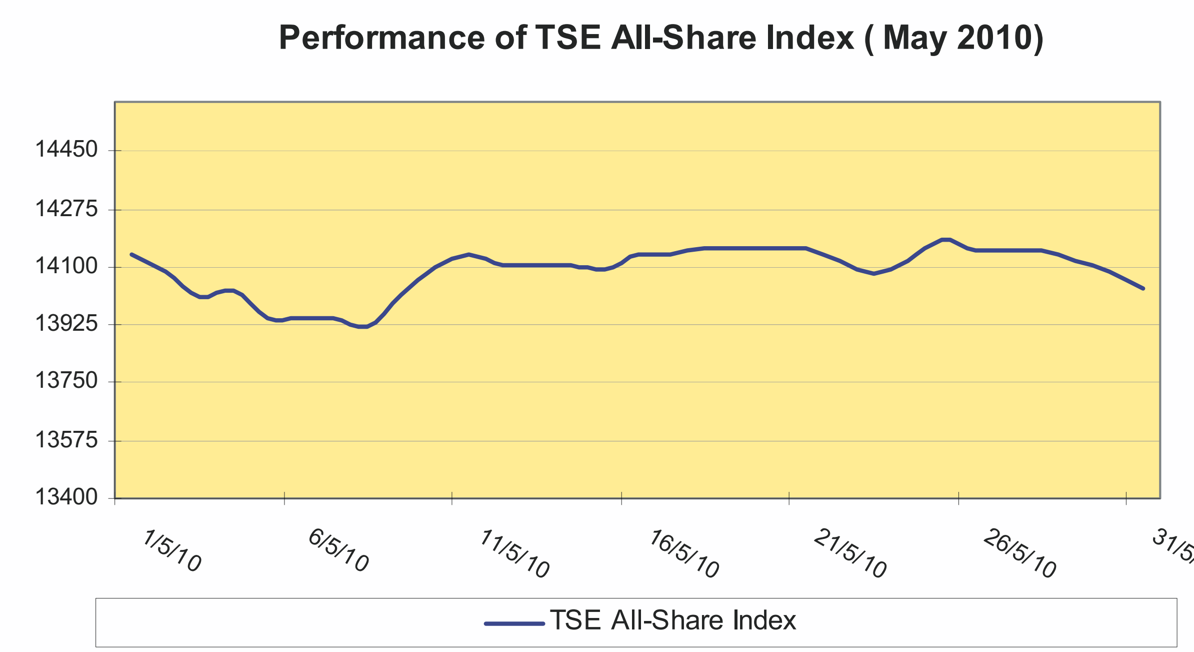
Since the beginning of the Iranian year (21st March), the Euro has lost over 5% of its value against the Iranian Rial. The pharmaceutical sector is one which benefits from the devaluation of the Euro against the Rial. This is because over 50% of raw materials and chemicals used in the drug manufacturing sector are imported, the vast majority of which are procured in Euro. The sector index gained 5.8% in value over the course of May.

## Engineering & Services

In this sector, Iran Marine Industries Co. (SADRA), which specialises in building ships, docks and floating oil rigs, once again hit the headlines. At the beginning of the year, the company announced that it had been awarded contracts worth $7 billion by the government, as well as receiving financial assistance from the government. This led to the stock gaining almost 100% in value within 2 months.

SADRA's annual results, which were released this past month, were disappointing. The company reported a net loss of $25 million. In addition, in a public statement SADRA dismissed the claims that the new contracts and the financial assistance have been finalised. Not surprisingly, the share price slumped and ended the month 10% lower than the previous month. In the first week of June, SADRA finally confirmed that it has been awarded contracts in the South Pars oil and gas field, but declined to comment on the impact of these contracts on the profitability of the company.

Overall, the TSE had a slow month, with the TSE All-Share Index gaining 0.2% in value. Trade volumes stood at $2.77 billion, although over 70% of trades were block trades.



**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 = 192.9

| Vehicle Domicile | Launch Date | Currency |
|---|---|---|
| Iran | 30 May 2006 | Iranian Rial (IRR) |

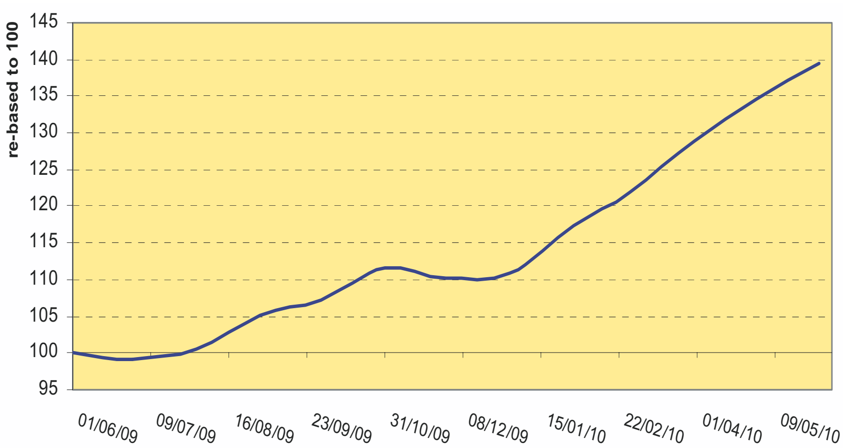
### Portfolio One Performance (Iranian Rial) - As at 31th May 2010


| Period | Portfolio Return |
|---|---|
| Last Month | - 2.5 % |
| Last 3 Months | 10.9 % |
| Last 6 Months | 15.7 % |
| Last 12 Months | 38.8 % |
| Since Inception (30 May 06) | 92.9 % |

## Portfolio Two (Open) NAV = 139.6

| Vehicle Domicile | Management Fee | Currency |
|---|---|---|
| British Virgin Islands | 2.0% p.a | Euro (€) |
| **Launch Date** | **Carried Interest** | **Minimum Investment** |
| 01 June 2009 | 20% (High Water Mark Applies) | €100,000 |

### Portfolio Two Performance (Euro) - As at 31th May 2010

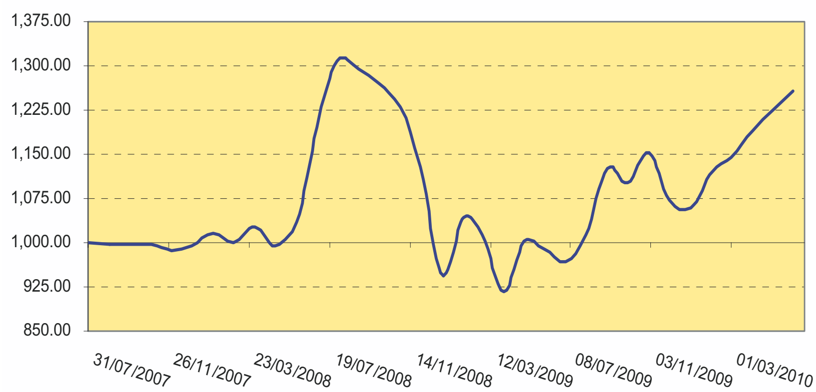



| Period | Portfolio Return |
|---|---|
| Last Month | 3.6 % |
| Last 3 Months | 14.5 % |
| Last 6 Months | 26.8 % |
| Last 12 Months | 39.6 % |
| Since Inception (01 June 09) | 39.6 % |

## Class C (Closed) — NAV = 1077.7

| Vehicle Domicile | Launch Date | Currency |
|---|---|---|
| British Virgin Islands | 10 July 2007 | Euro (€) |

### Class C Performance (Euro, Inc. Dividend) - As at 31th May 2010

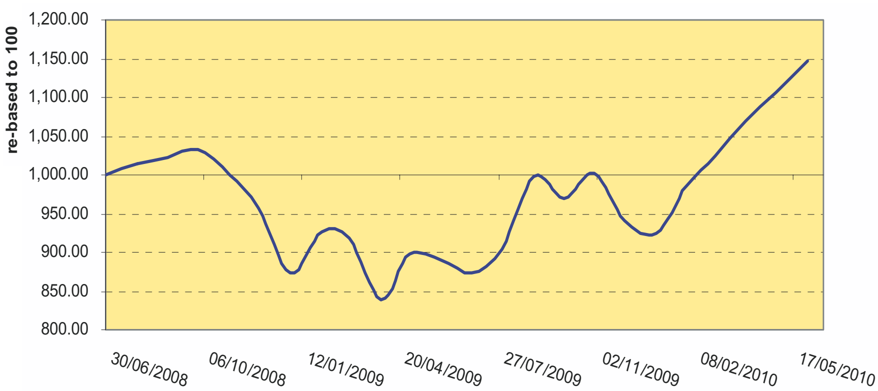



| Period | Portfolio Return |
|---|---|
| Last Month | 3.2 % |
| Last 3 Months | 10.9 % |
| Last 6 Months | 19.2 % |
| Last 12 Months | 30.2 % |
| Since Inception (10 July 07) | 25.8 % |

## Class D (Closed) — NAV = 1067.2

| Vehicle Domicile | Launch Date | Currency |
|---|---|---|
| British Virgin Islands | 30 June 2008 | Euro (€) |

### Class D Performance (Euro, Inc. Dividend) - As at 31th May 2010




| Period | Portfolio Return |
|---|---|
| Last Month | 4.0 % |
| Last 3 Months | 12.9 % |
| Last 6 Months | 22.0 % |
| Last 12 Months | 28.9 % |
| Since Inception (30 June 08) | 14.7 % |

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

In May 2010, Turquoise Partners hosted a conference attended by a large group of existing and prospective foreign investors in Iran. These investors traveled from Switzerland, Finland, Italy, UK, France and other countries. The aim of the conference was to provide an opportunity for the investors to become acquainted with the Iranian capital market and the unique investment opportunities that exist in Iran.

Since 2006, Turquoise Partners has attracted substantial foreign interest to the Iranian market and currently has approximately $150 million of assets under management. Turquoise Partners controls around 90% of the total value of foreign investments on the Tehran Stock Exchange, and has become a leading and respected player within the Iranian equity sphere.

The conference lasted four days from Monday 10th of May until the evening of Thursday 13th.

## Day 1

The first day began by speeches given by the Chairman of Turquoise, the Chairman of Atieh Consultancy Group and the President of Ravand Institute for Economic and International Studies. These speeches covered a broad spectrum of issues ranging from Iran’s macroeconomic indicators and growth potential, to strategic considerations when focusing on the Iranian capital market. The day was then followed by two panel discussions, focusing on equity and private equity investment opportunities and also the ongoing privatisation programme in Iran. In the evening, investors were invited to a dinner, which was also attended by a large number of Iranian senior managers and leading industry players.

## Day 2

On the second day, investors visited Rana Agriculture, the first privately owned plant biotechnology company in Iran. Rana specialises in the micro-propagation of date palms. Following this, the investors visited Butane Industries Group, situated approximately 120 kilometers south west of Tehran. Butane is the largest producer of household gas boilers, gas cylinders and burning appliances in Iran. The investors spent the afternoon at Karafarin Bank, where they had the opportunity to meet the CEO and a group of senior managers of the bank. Karafarin is among the oldest privately owned banks in Iran.

## Day 3

On the third day, the investors visited the Tehran Stock Exchange, where they were given a tour of the trading floor and were introduced to the trading platform and the ways in which trading takes place. They then attended a meeting, hosted by the Managing Director of the Tehran Stock Exchange Corporation and a number of financial experts. An interesting fact about this visit was that it attracted significant interest from the media, including coverage from all major newspapers, and a special TV report, broadcasted on national television. Later in the afternoon, investors were flown to the city of Isfahan.

## Day 4

On day 4, the investors visited the Mobarakeh Steel Complex, just outside Isfahan. Mobarakeh Steel was privatised in 2007. It is the largest producer of raw steel in Iran and is a company which has aroused a great deal of investor interest. The remaining time in Isfahan was spent on a tour of some of the spectacular historical and cultural sites in the city.

Iran's most recent nuclear agreement with Brazil and Turkey, and the West's reaction to this agreement will be discussed in this edition of Country Overview.

In May, Iran, while hosting the G15 summit in Tehran, signed an agreement with Brazil and Turkey for the exchange of its low enriched uranium with nuclear fuel on Turkish territory. The G15, which was founded in 1989, includes developing states from Asia, Africa and South America. In this summit, the Presidents of Iran, Turkey and Brazil signed an agreement which stated that Iran would send 1,200 kilograms of uranium with a concentration of 3.5% to Turkey and in return would receive 120 kilograms of uranium with a concentration of 20% which would be used for Tehran's nuclear reactors. All containment and the exchange of uranium would take place under the direct supervision of the International Atomic Energy Agency (IAEA).

Initially, the deal was deemed as a major breakthrough in Iran's prolonged nuclear stand-off with the West. Previously, there have been a number of unsuccessful attempts made by Iran and the IAEA to reach an agreement on an exchange of uranium. Back in October 2009, a proposal was made by the IAEA which called for Iran to send 75% of its low enriched uranium to Russia to be further enriched and then sent to France to be made into fuel assemblies. However, Iran did not accept this proposal, arguing that France has failed to uphold its previous commitments to deliver nuclear fuel to Iran. Iran gave a counter offer which called for a simultaneous exchange of low enriched uranium with fuel on the island of Kish. This proposal was rejected by the West. At the time, Iran asserted that it would only accept an exchange offer if the physical exchange took place on Iranian territory. Experts believe that the recent agreement reflects an important change of stance by Iranian officials.

The reaction of the West was fundamentally different to those countries involved in the deal and, perhaps, to what Iranian officials had expected. While some of the Western powers regarded the deal as a positive development, they all expressed their skepticism about the deal. A concern shared across the Western world was that even though the initial offer by the IAEA in 2009 had called for Iran to give up the same amount of uranium as agreed in the recent deal, Iran has continued to produce enriched uranium since that offer. Consequently, the 1,200 kilograms, as stated in the deal, was now less than 50% of Iran's total enriched uranium reserves, as opposed to 75% at the time of the initial offer.

Two days after the agreement, the US presented a draft resolution for the fourth round of sanctions against Iran to the UN Security Council, a move that was criticised by Brazil and Turkey. On 9th June, the resolution was passed by the UN Security Council, with 12 out of 15 member states voting in favour of the resolution. Brazil and Turkey voted against the sanctions and Lebanon abstained.

The new resolution bans Iran from investing in uranium mining and the construction of new enrichment sites. It forbids the sales of tanks, combat vehicles, fighter jets, attack helicopters, artillery, warships and missiles to Iran. It also targets the Islamic Republic of Iran Shipping Lines Company and its subsidiaries. In addition, financial transactions which are suspected of being connected to the nuclear programme have also been forbidden. As with the previous three rounds, Iranian officials called the new sanctions ineffective and asserted that Iran would continue with its enrichment programme.

## Iran's Petrochemical Industry

The Iranian petrochemical industry dates back to 1963, when Shiraz Petrochemical was established in order to produce fertilisers. One year later, the National Iranian Petrochemical Industries Co. was founded and 7 more plants were built prior to the 1979 Islamic Revolution. During the Iran – Iraq war, petrochemical production was halted and several plants suffered damage. However, production and the expansion of the industry resumed in 1989 and it has grown significantly since then. As at end of 2009, Iran's total annual petrochemical production capacity stood at 34 million tonnes.

Currently, Iran's petrochemical production comprises 12% of production in the Middle East. This puts Iran in second place, behind Saudi Arabia. Iran has a diversified basket of products with more than 70 products. However, the focus over the past few years has been on products which use natural gas as feedstock; in particular, methanol, ethylene, propane and butane. This is because the profit margins for crude oil and naphtha-consuming petrochemicals are continuously eroding due to the competitiveness of the market and the high price of feedstock. In addition, Iran has a competitive advantage in the gas consuming stream of the petrochemical industry due to its vast reserves of natural gas. In the Assalouyeh region near the South Pars gas field in the Persian Gulf, Iran is able to convert raw gas to ethane (a raw material for the petrochemical industry) and then to petrochemical products at a gross margin of up to 88%. For several years, Iranian petrochemical companies have enjoyed significant discounts from the government on their natural gas feedstock, in comparison to global prices. Even with the partial removal of governmental subsidies on natural gas as part of the economic reform plan, these companies remain highly profitable and retain their global competitive advantage.

Iran is a key player in supplying the world's methanol demand. Currently, Iran has the capacity to produce more than 5 million tonnes of methanol, which constitutes 10% of the world's methanol production. Of this amount, approximately 90% is exported. Zagros Petrochemical is Iran's largest methanol producer. It has a production capacity of 3 million tonnes per annum. Iran also has the capacity to produce 4 million tonnes of ethylene per annum. Ethylene is a mid-stream product, which is used in the production of PVC.

Iran has very ambitious plans for the expansion of its petrochemical industry. According to the 20 year outlook plan, Iran is to become the Middle East's number one producer of petrochemical products by 2015, by increasing its annual production capacity to 126 million tonnes. It is estimated that $50 billion worth of investment is required to achieve this target, something that may prove challenging. Another challenge in reaching this goal for Iran is the availability of feedstock. Despite its vast reserves, Iran's natural gas production is very much underdeveloped. Last year, Iran consumed domestically over 95% of the natural gas that was produced. It is evident that significant developments in the natural gas industry are needed, not just for the petrochemical industry, but also for household consumption and Iran's industry base as a whole.

The petrochemical industry is also a key industry on the privatisation list. Fanavaran Petrochemical, Iran's second largest methanol producer, was the first to be privatised. It was floated on the Tehran Stock Exchange in 2007. At least 5 more petrochemical companies are expected to undergo privatisation over the next 3 years.

## Iran to Build a Dam in Afghanistan

In May, Iran won a contract to build a dam in Afghanistan. This dam is to be built in Shekardarreh, which is situated in the central part of Kabul province. The project is estimated to cost $40 million. The capacity of the dam will be 7.5 million cubic meters. The "Shah and Aroos" dam is expected to take 3.5 years to be built. After the project is completed, 700 hectares of land in Kabul can be irrigated by the dam. In addition, 1 megawatt of electricity will be produced which will be used by the inhabitants of Shekardarreh. According to officials, 25% of the labour force is to be provided by Iran and the remainder from the local area.

## Real Estate Construction and Permits

According to a report by the Tehran Municipality, in the first month of the Iranian calendar year (which commenced on 21st March), more than 5,600 construction permits for Tehran were issued. This showed a 77% increase from the same period last year. In addition, estimates show a 50% increase in actual construction this past month, in comparison to the previous month.

Following an extraordinary boom in the Iranian real estate market between 2004 and 2008, activity in this market suddenly stalled. Over the past two years, the Iranian real estate market had experienced its worst slow-down for nearly a decade. Statistics from the Urban Development Organisation of Tehran indicate that construction activity in 2009 was 50% lower than the previous year, and was at its lowest level for the past 8 years.

Experts believe that the recent rebound in activity is a good indication of a recovery in the real estate market. The Iranian real estate market is very much dominated by Tehran and a recovery in Tehran is likely to spur across other major cities.

Recent data published by the Statistical Centre of Iran reveals a modest increase in prices. Accordingly, real estate prices have increased by 4.7% in the winter of 2009 in comparison to the winter of 2008. However, there has been a substantial increase in rental prices. Rents in Tehran show a 13.8% increase in the winter of 2009 in comparison to the same period last year.

## Iran to Build a Power Plant in Syria

In May, Iran began building a thermal power plant in the port of Jondar in Syria. Iran Power Plant Project Management Co. (MAPNA) was awarded the contract in late 2009. The plant will have a capacity of 450 megawatts. Construction is expected to take 28 months to be completed and come at a total cost of $330 million. MAPNA is currently building another power plant in Syria. The “Tashrin” power plant is estimated to be 75% complete. Jondar is the third power plant to build by an Iranian company in Syria.

**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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