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Sanctions against Iran

Options, Problems, Perspectives

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If Iran does not "re-establish full suspension of all enrichment related activities" as called upon by the International Atomic Energy Agency (IAEA), then the US can be expected to push for sanctions. But what kinds of sanctions are available? What are the problems involved with them? How effective can they be? How could they be usefully implemented as part of a coherent strategy?

The EU-3—Great Britain, France and Germany—and Javier Solana, as the representative of the EU, have repeatedly warned Iran that if it resumes the enrichment of uranium there would be "no other option but to pursue other courses of action." That means if Iran continues its intransigence, the EU-3 will have to support referring the Iranian case to the UN Security Council, which could then impose sanctions. The discussion in Iran might—if things get that far—be influenced by the passing of a resolution, pursuant to which the Security Council might call on Iran to permanently renounce uranium enrichment and the reprocessing of plutonium—or might even declare the Iranian nuclear program to be a threat to international peace and security. At least, such a resolution could be interpreted by the US and other countries as a legitimation for more severe measures.

If there is no vote for economic sanctions in the Security Council, European countries could then come under pressure from the US to impose their own sanctions on Iran. The US itself cannot tighten its already comprehensive sanctions against Iran.

Germany in particular, as Iran's most significant import partner, could be affected by a restriction of economic transactions as a result of sanctions. In the past few years, German-Iranian economic relations have grown considerably: German companies exported goods worth 3.57 billion euros to Iran last year.

Trade and investment sanctions

In the sense of the "classical" model of sanctions, economic sanctions—understood as the restriction of normal economic transactions—achieve the desired political effect if they cause as large an economic damage in the sanctioned country as possible: the supply of goods becomes scarce; consumer prices rise; the business community suffers from the costs of interrupted economic transactions; and unemployment increases.

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These developments will change the political cost-benefit calculation of the government given that every regime needs domestic support in order to ensure its authority. The political leadership—according to the logic of sanctions—will at some point in time give in to the external pressure because of its rational interest in preserving its own power.

An oil embargo imposed by the Security Council, which could be effectively implemented by means of a naval blockade, and the prevention of new foreign investment in the energy sector would hit Iran where it is most vulnerable. Approximately 80 percent to 90 percent of Iran's export earnings and 40 percent to 50 percent of annual government revenues stem from exporting oil. Iran wants to significantly expand its oil production and is therefore interested in massive foreign investment in the energy sector.

An oil embargo and the prohibition of investments in the oil and gas sector would undoubtedly have massive impact on the Iranian economy, even if, due to sharply rising oil prices, there has been an increase in the reserves of the Oil Stabilization Fund (OSF), which was established in March 2000. In the short term, Iran could cushion the losses from decreased exports. But, in spite of increased oil income and a period of growth in the last few years, Iran still finds itself in difficult economic circumstances. Above all, the job situation for young Iranians is especially severe.

Experiences from earlier sanctions show that authoritarian regimes with a functioning repression and propaganda apparatus do not necessarily have to fear the loss of power, despite a drastic decline in economic conditions. Even if there is room to maneuver for government critics and organizations as it is the case in Iran, one cannot necessarily expect that in tense economic times there will be a massive mobilization against the government. To the contrary: in the event of pronounced nationalism, comprehensive sanctions could possibly encourage national unity and produce a "rally round the flag" effect.

Regardless of this, sanctions can be effective over a longer period of time, as in the case of Yugoslavia in the nineties: for a while the Milošević regime could blame the sanctions for a lot of problems and use the "rally round the flag" effect. Unfortunately, the sanctions also helped a mafia class gain influence and motivated members of the politically active middle class to migrate. But in the end, the costs brought about by the sanctions became so high that the political leadership in Belgrade put pressure on the Bosnian Serbs.

Nobody can reliably predict whether, in the event of tough sanctions and the accompanying international confrontation, the Iranian regime would lose support and legitimacy to such an extent that it would have to relent in order to maintain power. It is also unclear whether the question of the unrestricted civilian use of nuclear energy has become such a question of national pride that drastic sanctions would actually stabilize the regime.

One thing is certain: in the event of an oil embargo oil prices would rise considerably causing negative economic consequences on a global scale. At the moment Iran is the fourth largest oil producer and has such a strong position on the international energy market that, under present conditions, the above-described trade and investment sanctions seem to be politically hopeless. The veto power of China could play a key role when it comes to the implementation of an oil embargo. Since 1993 China, as the second largest oil consumer, has pursued an ambitious energy policy, which is also reflected in its closer engagement with Iran. In 2003, the People's Republic of China obtained nearly 13 percent of its oil from Iran and signed an agreement for gas worth 100 billion dollars. Commentators described this as the "deal of the century."

Even among the Western industrialized countries the potential threat from a nuclear-armed Iran would have to command so much enough attention that economic interests would be pushed to the background. Unless Iran withdraws from the Nuclear Non-proliferation Treaty or has an as-yet-undiscovered secret nuclear weapons program, this currently seems rather unlikely considering the most recent, though not undisputed, assessments of the American intelligence services, which found that Iran is eight to ten years away from being able to produce enough fissile material for atomic bombs.

Financial sanctions and other "smart sanctions"

Financial sanctions could be less controversial for the international community. In addition to freezing the assets of the government, companies and individuals of the target country, financial sanctions include, most significantly, the prevention of access to loans; tightened conditions for debt service; the suspension of export credits; and the termination of the convertibility of the country's currency. State-imposed financial sanctions have a "multiplier effect" as both public and private financial institutions adjust their lending policies accordingly.

These kinds of sanctions could also be implemented by the leading Western Industrialized nations. Between 1993 and 2000 the G-7 countries blocked World Bank loans to Iran. However, this measure, because of the rather insignificant volume of the loans, had a mostly symbolic function. The Islamic Republic of Iran never made any effort to get support from the International Monetary Fund.

In light of the currently high oil prices and the building up of currency reserves, financial sanctions will not be able to achieve a drastic economic impact. But used in a targeted, "intelligent" way, they might nevertheless be politically effective. The aim of such "smart" sanctions is to change the cost-benefit calculus of specific groups within the elite of the affected country and by doing so create pressure to change course. At least initially, these kinds of sanctions do not affect the broader population and cannot be manipulated, like extensive drastic sanctions, to such an extent that they end up fostering national unity.

Financial sanctions could both directly hit the policymakers and undermine the support of regime-supporting groups, who have capital invested abroad. The massive capital flight of—according to the estimates of Iranian economists up to three billion dollars each year—provides a starting point for such an approach. The freezing of assets could potentially put regime-supporting groups under pressure. Advocates of such an approach argue that the Iranian merchant class, and not the clergy, is the pivotal power factor in the country.

Financial sanctions require a considerable measure of political and technical cooperation. This cooperation would naturally be made easier if such sanctions were mandated by the Security Council.

In addition, a travel ban for certain people could be part of an "smart" sanctions approach. That would send a clear political signal to Iran that its present course of action will lead to isolation. With respect to Iran's population as a whole, such a message could be highlighted by excluding Iranian participants from international sporting events—a proposal that recently was put forward in the US debate, with the Soccer World Cup in mind.

Sanctions are no substitute for strategy

Considering the problematic alternatives—extensive sanctions, military strikes, "regime change"—"smart" sanctions most likely offer a realistic option to put Iran under some pressure. But even the most intelligent sanctions are only a tool of foreign and security policy, not a substitute for a broader strategy.

Typically, in the debate about whether sanctions work, little or no consideration is given to the question of how a comprehensive political strategy -in which sanctions are or should be embedded as a tool—impinges on their effectiveness. The threat of sanctions alone can be effective if it results in more bargaining power. To this end, lessons learned from earlier instances when sanctions were imposed should be taken into account when future coercive measures against Iran are being considered: such a threat has to be credible, the related demands should be aimed at very specific changes in behavior, and sanctions should be part of a “carrot and stick” strategy.

Until now the Bush administration has not followed an approach that reflects the understanding that sanctions best be an element of a bargaining strategy. If that had been the case, the Bush administration would have offered the possibility of relaxing American sanctions as a bargaining chip—sanctions, which, by the way, have had some impact on Iran: the estimates of the economic costs on Iran range—depending on the methodology applied—from 1 percent to 3.6 percent of the gross domestic product from 1998 to 2001.

What conclusions can be drawn from this discussion? The German/European readiness to implement substantial sanctions should be linked to the clear expectation directed at the US that sanctions are to be employed as a bargaining chip. Only with a common strategy such a wide range of incentives and sanctions can be established, which would change the international context for the nuclear debate within Iran. Ideally, such a strategy should integrate Russia because it is Iran’s most important supplier of conventional arms and nuclear technology. This is presumably the most likely way, if at all, to influence the Iranian cost-benefit analysis with respect to the nuclear question.

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