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IRAN

AUTOS REPORT

INCLUDES 5-YEAR FORECASTS TO 2019

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Iran Autos Report Q2 2015

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BMI Industry View

Iranian vehicle production rose by 67.5% in 2014, to 1,090,846 units, according to statistics from the International Organization of Motor Vehicle Manufacturers (OICA). Breaking down the headline figure, Iran produced 925,975 passenger cars and 164,871 commercial vehicles. This makes Iran the 18th largest auto producer in the world.

At the present time, sentiment towards the Iranian auto industry remains dominated by the progress of ongoing negotiations between Iran and the P5+1 countries (the US, Russia, China, France, Britain and Germany) over Iran's nuclear programme. The two sides have until June 30 2015 to reach a permanent agreement. During this time, Iran will continue to receive around USD700mn a month from its frozen accounts, although key international sanctions on its energy and banking sector will remain in place.

In January 2015, **BMI**'s Country Risk team reaffirmed its belief that the talks will be protracted, with risks tilted slightly to the downside. Overall, we believe that a solution to the nuclear issue will not be found by June 30, as political constraints will prevent both Iranian and US negotiators from making the significant concessions necessary to bridge existing technical obstacles to a deal. That said, a complete breakdown in talks is also unlikely in June, as the costs would be immense. Our core view therefore remains that talks will continue over the next two years through a series of partial deals and extensions. Following June 2015, we believe that a form of face-saving, partial agreement will be reached, which will allow for further talks.

It is clear that there remains strong demand for new vehicles from the Iranian population at present. As such, the potential for improved foreign relations between Iran and the West over the short to medium term has generated considerable interest from carmakers, none more so than French brands Renault and Peugeot, which controlled around a third of the market's output before they withdrew in early 2012 in line with Western sanctions. Indeed, it appears likely that Peugeot will seek some sort of deal with previous partner **Iran Khodro Company** (IKCO), while Renault is presently in talks with **Saipa** about buying an equity stake in its **Pars Khodro** subsidiary.

Iranian carmakers are also looking to expand their operations within the Middle East region. In this context, in January 2015, The Times of Oman reported that IKCO was considering Oman as a potential market for the exports and re-export of its products. IKCO participated in an exhibition of Iranian products held in Muscat during early January 2015, which included its Dena, Runna, Samand and Soren passenger cars as well as its Aryan minibus, Arya Truck and C1230 city bus. According to Iran's Minister of Industry, Mining, and Trade, Mohammad Reza Nematzadeh, there is huge untapped potential for collaboration with Oman on the export and re-export of Iranian-manufactured cars.

Meanwhile, **Iran Khodro Diesel** (IKD) export manager Mohammad Hazrati said that it would be economically viable for Oman to export cars from Iran considering the close distance between the two countries, adding that IKD could be interested in setting up a commercial vehicle assembly unit in Oman via a joint venture (JV) with a local partner. Were Iranian carmakers to establish a local production facility, then this could prove transformative in terms of developing an indigenous Omani auto production and supply chain. **BMI** will monitor events and report on any future developments as they occur.

Iraq is another country where Iranian carmakers are looking to boost output. According to an October 2014 report in the Iran Daily, IKCO is now producing some 50 cars a day in Iraq, with the company set to boost output to 100 cars a day amid signs of stronger demand for cars within Iraq. IKCO's Deputy CEO for exports, Ali Elmi was quoted by the Fars news agency as saying that IKCO produces a variety of cars within Iraq, including the Runna, Samand, Soren, Peugeot Pars and Peugeot 405. The company also has several experienced engineers based at the Iskandariya factory to monitor the build quality of Iraqi-produced cars.

As well as the possibility of higher auto exports, Iran has also witnessed a rising trend in imports over the past calendar year, as the domestic political and economic backdrop improved slightly. Speaking to the Iran Daily in February 2015, the vice president of the Majlis Economic Commission, Iraj Nadimi**,** stated that car imports have increased since mid-March 2014.

However, Nadimi noted that imported cars cannot meet the country's new vehicle requirements, and hence pose little threat to the domestic auto industry. 'Auto manufacturers are not permitted to set prices for their products the way they want. They are required to observe the models set by the government. To bring car prices down, the first strategy is to do away with the monopoly in production and distribution, and prepare the ground for importing more cars,' he said. The main obstacle to foreign carmakers seeking to export cars to Iran remains the 100% tariff levied on all vehicle imports.

Looking forward, electric cars could start to play an increasing role within the Iranian auto sector. In this context, in January 2015, the Fars news agency reported that Iranian carmaker **Diyar Khodro** had unveiled the country's first domestically manufactured electric car, named Sabrina. According to the Tehran Times, the carmaker has begun trial production of the Sabrina and expects large-scale manufacturing to begin in the next Iranian calendar year, starting March 21. It plans to manufacture 42,500 units a year. According to managing director Mohammad-Taqi Khanlou, the Iranian government is negotiating a deal to deploy the Sabrina in the public transportation fleet.

SWOT

Iran Auto Industry SWOT

Strengths	▪ The largest car-producing nation in the Middle East. ▪ Domestically developed engines, as well as vehicles, reduce the country's reliance on imports. ▪ Growing middle class should provide high demand for new cars over the medium term. ▪ New car sales and production both look set for strong growth over the current year. ▪ BMI is forecasting steady growth in new car sales over our newly-extended forecast period to 2019.
Weaknesses	▪ Local parts and components manufacturers face capacity constraints, which will mean greater reliance on foreign imports in car assembly. ▪ Iran is insisting on tough new preconditions before allowing foreign carmakers back into the country, which could deter some inward investment. ▪ Sales growth may slow slightly over 2015/16.
Opportunities	▪ Should a permanent deal on Iran's nuclear programme be reached and sanctions ended, then we would expect the domestic economy to grow rapidly over the medium term, which in turn would boost demand for new cars. Moreover, any permanent deal would increase Iran's attractiveness to foreign manufacturers, as it potentially offers a significant new market. ▪ As Iran's car sector grows, it will increasingly rely on outsourcing for parts and components. ▪ Agreements with Chinese manufacturers bring new business partnerships and uses for capacity. ▪ Domestic manufacturers are also looking to boost exports over the coming years.

Iran Auto Industry SWOT - Continued	
	▪ Electric vehicle production could be a growth area over the long term.
Threats	▪ Should talks between Iran and the West collapse in 2015, then the country would remain subject to US trade sanctions, which would continue to cut the country off from international investment. ▪ Political instability remains a key concern for the whole Iranian economy.

Political

Political SWOT Analysis

Strengths	▪ Since the overthrow of the Pahlavi family in 1979, there has been some reduction in the level of political corruption, while wealth distribution has improved marginally. ▪ The Revolutionary Guard and Basij militia are fiercely loyal to the supreme leader, helping to maintain social stability.
Weaknesses	▪ The country has one of the poorest human rights records in the region, and authorities do not hesitate to quell dissidents. A number of journalists and anti-government protesters are being held in custody. ▪ While decision-making ultimately rests with the supreme leader, the regime is heavily fragmented, and consensus is hard to reach. ▪ Widespread perceptions of electoral fraud during the course of June 2009's presidential elections have damaged the regime's legitimacy in the eyes of many Iranians.
Opportunities	▪ The Majlis (parliament) is more than just a rubber stamp; the move by 150 parliamentarians (out of 290) to hold former president Mahmoud Ahmadinejad accountable for his handling of the economy in March 2012 is a positive indication that checks exist. ▪ The victory of moderate cleric Hassan Rouhani in Presidential elections in June 2013 is leading to a significant improvement in relations with the West.
Threats	▪ Despite progress in nuclear talks, the prospect of further US and EU sanctions and the possibility of a military strike by the US or Israel cannot be dismissed. ▪ Youth unemployment is high. ▪ The strong influence of the Revolutionary Guards within the political and economic arena will continue to present a challenge to reform.

Economic

Economic SWOT Analysis

Strengths	▪ Iran has the world's second largest proven oil reserves after Saudi Arabia, and the world's second largest proven gas reserves after Russia. ▪ Oil and gas aside, Iran is rich in other resources and has a strong agricultural sector.
Weaknesses	▪ Local consumption of hydrocarbons is rising rapidly; this, coupled with ageing technology in the sector, will have a negative impact on its oil and gas exporting capacity. ▪ International sanctions discourage foreign oil companies from bringing much-needed technical knowledge and equipment to maintain oil output levels.
Opportunities	▪ The gas sector remains underdeveloped despite significant improvements in recent quarters, and there is considerable room to maximise this source of revenue. ▪ A shortage of housing, provides opportunities for investment in residential construction.
Threats	▪ Lower oil prices will have a marked impact on the economy. Although an Oil Stabilisation Fund exists to protect the economy at times of weaker oil prices, it has increasingly been used to fund government overspending and could be close to empty. ▪ Capital flight could accelerate should negotiations on the nuclear programme fail.

Operational Risk

SWOT Analysis

Strengths	▪ Iran boasts high numbers of skilled graduates in technical fields such as engineering, construction and science. ▪ The transport network offers good internal and cross-border connections, and is currently able to meet the country's supply chain needs. ▪ The banking sector is relatively well developed, allowing extension of finance and credit to citizens. ▪ A well established intelligence agency and robust counter-terrorist capabilities deter attacks in most areas of the country.
Weaknesses	▪ Costs of employment are increases because the Iranian Labour Code affords workers a high level of protection and generous benefits. ▪ The costs of inland transportation, as well as the risk of congestion and traffic accidents disrupting supply chains, is raised due to reliance on the road network as the dominant freight mode. ▪ There is widespread corruption and heavy handed censorship, which will pose unforeseeable operational costs and limit business activities. ▪ The expansion of IS in Iraq poses a significant risk to Iran's security.
Opportunities	▪ The literacy rate of the labour force is increasing as the benefits of investment in primary school education are filtering through. ▪ The development of road and rail connections with Iran's neighbours highlights the country's potential to develop into key transit point for East-West trade. ▪ Lack of external demand means that those who can invest in Iran are rewarded with cheap resources. ▪ Relaxing of sanctions is resulting in greater foreign direct investment inflows.

SWOT Analysis - Continued	
	▪ There is potential to combat the drug supply into Europe through programmes in Iran.
Threats	▪ The availability of highly skilled labour is restricted as the brain drain results in an exodus of technically qualified workers. ▪ The risk of electricity and water shortages will be enhanced due to growth in energy- and water-intensive agricultural, mining and manufacturing industries. ▪ Lax intellectual property protection carries the threat of patent theft, fraud or infringement, leading to profit losses. ▪ There is a risk of domestic hostility towards Westerners, triggered by international political events.

Industry Forecast

Table: Autos Total Market - Historical Data And Forecasts (Iran 2013-2019)

	2013	2014e	2015f	2016f	2017f	2018f	2019f
Vehicle production, units	651,211	1,090,846	1,290,658	1,583,054	1,739,623	1,896,802	2,080,142
Vehicle production, units, % y-o-y	-35.9	67.5	18.3	22.7	9.9	9.0	9.7
Vehicle sales, units	737,000	1,153,300	1,337,828	1,538,502	1,676,967	1,844,664	2,047,577
Vehicle sales, units, % y-o-y	-28.5	56.5	16.0	15.0	9.0	10.0	11.0
Vehicle trade balance, units	-198,830	-227,325	-226,658	-149,539	-149,108	-179,298	-220,426
Vehicle trade balance, units, % y-o-y	25.1	14.3	-0.3	-34.0	-0.3	20.2	22.9
Vehicle fleet, units	11,366,919	11,568,669	11,739,707	11,995,555	12,261,808	12,564,586	12,864,132
Vehicle fleet, % y-o-y	-10.2	1.8	1.5	2.2	2.2	2.5	2.4
Vehicles per 1,000 of population	146.8	147.4	147.7	149.1	150.6	152.6	154.5

e/f = BMI estimate/forecast. Source: National sources, BMI

Production

Iranian vehicle production rose by 67.5% in 2014, to 1,090,846 units, according to statistics from the International Organization of Motor Vehicle Manufacturers (OICA). Breaking down the headline figure, Iran produced 925,975 passenger cars and 164,871 commercial vehicles in 2014. This makes Iran the 18th largest auto producer in the world.

At the present time, sentiment towards the Iranian auto industry remains dominated by the progress of ongoing negotiations between Iran and the P5+1 countries (the US, Russia, China, France, Britain and Germany) over Iran's nuclear programme. The two sides have until June 30 2015 to reach a permanent agreement. During this time, Iran will continue to receive approximately USD700mn a month from its frozen accounts, although key international sanctions on its energy and banking sector will remain in place.

In January 2015, **BMI**'s Country Risk team reaffirmed its belief that the talks will be protracted, with risks tilted slightly to the downside. Overall, we believe that a solution to the nuclear issue will not be found by June 30, as political constraints will prevent both Iranian and US negotiators from making the significant concessions necessary to bridge existing technical obstacles to a deal. In the US, Republicans won a majority in the US Senate in mid-term elections at the beginning of November. The Republican-controlled Congress convened in January, and lawmakers are already promising an aggressive package of sanctions. As a result, room for concessions to the Iranians will be limited for US negotiators.

In Iran, hardliners have in recent months regained some of the influence they lost following moderate cleric Hassan Rouhani's victory in presidential elections in June 2013. In a sign that the current administration is increasingly under fire by the conservatives, parliament rejected Rouhani's fourth nominee for the sensitive Minister of Higher Education on November 18, with the post being held by a caretaker since August 2014. Lower oil prices in 2015 also pose a challenge to nuclear talks. Support for Rouhani, whose popularity rests on his ability to improve the economic situation, will in our view decline as low crude prices hit Iran's economy, reducing his ability to resist pressure for a more hawkish posturing vis-a-vis the West.

That said, a complete breakdown in talks is unlikely in June, as the costs would be immense. The US would have to face another major crisis in the Middle East at a time when it is grappling with the Islamic State's takeover of much of Syria and Iraq, and risks of terrorist attack on domestic soil have increased. A failure in diplomacy would also result in a significant intensification of international sanctions against Iran, leading to a dramatic worsening of the economic situation. This would prove highly risky for the ruling elite, and Iranian conservatives would prefer to see a continuation of talks rather than an abrupt end to diplomacy. In taking an incremental approach, the Iranians would still get partial sanctions relief, while preserving the long-term option of ramping up the nuclear programme.

Our core view remains that talks will continue over the next two years through a series of partial deals and extensions. Following June 2015, we believe that a form of face-saving, partial agreement will be reached, which will allow for further talks. Sanctions will be somewhat eased, but key measures targeting Iran's oil and banking sector will remain in place. Beyond a two-year timeframe, talks will be influenced by decisions of future political leaders, and their direction is harder to decipher. Political obstacles to a final agreement will remain substantial, and we believe that risks of reaching a final agreement over the coming decade are tilted slightly to the downside.

Turning away from the political backdrop, it is clear that there is strong demand for new vehicles from the Iranian population at present. As such, the potential for improved foreign relations between Iran and the West over the short to medium term has generated considerable interest from carmakers, none more so than French brands Renault and Peugeot, which controlled around a third of the market's output before they withdrew in early 2012 in line with Western sanctions. Indeed, it appears likely that Peugeot will seek some sort of deal with previous partner **Iran Khodro,** while Renault is presently in talks with **Saipa** about buying an equity stake in its **Pars Khodro** subsidiary (*see Saipa company profile for more information*).

In this context, shortly after the news that the deadline for a permanent deal had been extended, AFP reported that French carmaker **PSA Peugeot Citroën** is engaged in talks to resume production in Iran, according to the company's operations director for the Middle East, Jean Christophe Quemard. Speaking in Tehran on December 1, Quemard said: 'We are in intense discussions. We have a long relationship with Iran. We have the strong will to create a joint venture (JV) covering the entire automotive chain as soon as possible.'

However, since the withdrawal of foreign carmakers in 2012, the Iranians have changed the parameters for proposed joint ventures. In November 2014, media reports cited comments from deputy industry minister Mohammed Reza Norouzzadeh, who stated that 40% of any JV auto production must be undertaken by domestic manufacturers, rising to 85% over five years. There are also reported that foreign cars are no longer to be imported on a completely built up (CBU) basis.

As well as the interest from France, Austria also appears ready to invest in the Iranian auto sector. In August 2014, the Fars News Agency reported that Austria intends to establish a car manufacturing plant as well as assembly lines in the Iranian city of Tabriz, according to a statement by Austrian Ambassador in Tehran Friedrich Stift. 'We have had talks with auto parts manufacturers on launching complete production lines to manufacture cars in Tabriz,' said Stift, adding that the move is in line with the Austrian government's readiness to collaborate with Iranian enterprises in different sectors.

In May 2014, IKCO reportedly set out a number of conditions for returning to a partnership with French carmaker **Peugeot**, following a meeting between the bosses of the two companies, which BMI believes shows mutual needs within the industry. Peugeot and its compatriot Renault have both racked up significant losses following their withdrawal from Iran, thereby reflecting the significance of the Iranian market. However, IKCO's demands for greater investment in technology transfer and research and development (R&D) facilities show where the national industry is lacking.

IKCO managing director Hashem Yekkeh Zare said that Peugeot should end its own assembly operations and focus on joint production with the Iranian carmaker, including transferring its technology and setting up local R&D facilities. Zare said IKCO will only consider resuming its relationship if these conditions are met.

While these are significant demands, IKCO also knows how much the market means to Peugeot. After withdrawing from Iran, **PSA Peugeot Citroen** CFO Jean-Baptiste de Chatillon said the company had been losing EUR10mn (USD153mn) a month. Iran is the Middle East's biggest car market in sales volume-terms and stood at 1.6mn units in 2011 before the decline began and sanctions were stepped up. At that time, Peugeot and Renault combined accounted for one-third of total output.

Also in June 2014, ISNA reported that Japanese automaker Suzuki Motor is in discussions with Iranian carmaker **Iran Khodro** to launch a new car production line in Iran, according to Abdollah Babaee, director of marketing and sales at Iran Khodro. The discussions come after Iran, the US, France and four other countries entered an agreement in late 2013, under which the Iranian government will decrease its nuclear activities in exchange for some sanctions relief. Iran's Industry Minister Mohammad Reza Nematzadeh said: 'The foreign firms are very eager to establish ties with Iranian auto manufacturers and we intend to help further develop the country's auto industry through such interactions,' reports Trend News Agency.

Looking forward, electric cars could start to play an increasing role within the Iranian auto sector. In this context, in January 2015, the Fars news agency reported that Iranian carmaker **Diyar Khodro** had unveiled the country's first domestically-manufactured electric car, named Sabrina. According to the Tehran Times, the carmaker has begun trial production of the Sabrina and expects large-scale manufacturing to begin in the next Iranian calendar year, starting March 21. It plans to manufacture 42,500 units a year. According to managing director Mohammad-Taqi Khanlou, the Iranian government is negotiating a deal to deploy the Sabrina in the public transportation fleet.

Sales

Iranian new vehicle sales have been racing ahead over 2014 year-to-date, with the Focus2Move website reporting that new vehicle sales were up by 23% over H114, at 394,463 units. For the full 2014/15 calendar year, **BMI** is targeting further growth, of 56.5%. Beyond the current year, we target further growth, of 77.5%, which should take annual sales over the 2mn unit mark by the end of our newly-extended forecast period in 2019.

Much will depend on how the talks between Iran and the major powers progress over H115. Should sanctions be permanently eased, then there is scope for more rapid growth in new car sales as the Iranian economy - especially its key oil sector - regains access to the world's markets. However, if the talks fail and new sanctions are imposed, then the future of the few remaining international carmakers - such as Renault - still operating in Iran would be called into question.

Turning to the macroeconomic backdrop within the country, **BMI** has become slightly more bearish, now targeting 1.4% growth for 2015, down from 2.1% previously. Overall, we believe that the Iranian economy will expand slowly in 2015 compared to 2014, as oil prices remain low and talks on the nuclear programme fail to reach a breakthrough. Declining oil prices will force the government to cut current spending and investment in the country's infrastructure sector, which will result in slow expansion of private consumption and fixed investment. Key international sanctions on Iran's banking and energy industry will also continue to damage the country's economic outlook.

Looking at private consumption - a key indicator of demand for new vehicles - we are forecasting a decline to 3% in 2015, from 4.5% in 2014. The government will cut current spending this year in a bid to reduce a widening fiscal deficit, a result of falling oil revenues, and will be unable to prop up consumer spending. The inflationary environment will also deteriorate slightly. We project consumer price index (CPI) inflation to average 23.0% in FY2015/16 (fiscal year running from March 21 2014 to March 20 2015) up from 21% in FY2014/15.

One further threat to new vehicle sales over the near term is posed by the mid-2014 decision by the Iranian authorities to increase domestic car prices by 30%. According to a July 2014 report by Iran Daily, three parliamentarians, Issa Emama, Mohammad Ali Madadi and Nader Qazipour, criticised the council responsible for setting domestic car prices, and urged it to reconsider its decision. Behrouz Nemati, a member of the Majlis Mines and Industries Committee highlighted mismanagement in the auto industry as the main reason for the hike.

Against this worsening economic backdrop, **BMI** is forecasting a slowdown in sales growth to 16% for 2015/16, down from 56.5% growth estimated for 2014/15.

Iranian new vehicle sales totalled 737,000 units in 2013, according to information from the Focus2Move website.

Trade

BMI's improved forecasts for production also mean that Iranian auto exports should also increase over the current fiscal year. In August 2014, the Fars News Agency reported that **Iran Khodro** (IKCO) plans to export 10,000 vehicles to Russia. According to CEO Hashem Yekehzare, the move is in line with the company's efforts to raise its world market share. IKCO intends to sell one-third of its cars in international markets, according to Yekehzare. He said: 'Meeting Russian standards is the first step to enter this market. But what is important is to provide suitable after-sales services to our customers in this market.'

Iran is also looking to boost its exports elsewhere in the world. In this regard, in June 2014, Ahmad Nematbakhsh, the secretary of the Association of Iranian Car Manufacturers, stated that 90% of cars produced in the country meet Euro-4 standards. Nematbakhsh added that Euro-4 standards integrated into car components cut fuel consumption and assist in environmental protection. **Peugeot** 206, L-90, Samand and Tiba are some of the vehicles conforming to the Euro-4 standards.

In January 2015, The Times of Oman reported that IKCO was considering Oman as a potential market for the exports and re-export of its products. IKCO participated in an exhibition of Iranian products held in Muscat during early January 2015, which included its Dena, Runna, Samand and Soren passenger cars as well as its Aryan minibus, Arya Truck and C1230 city bus. According to Iran's Minister of Industry, Mining, and Trade, Mohammad Reza Nematzadeh, there is huge untapped potential for collaboration with Oman on the export and re-export of Iranian-manufactured cars.

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Were Iranian carmakers to establish a local production facility, then this could prove transformative in terms of developing an indigenous Omani auto production and supply chain. **BMI** will monitor events on the ground and report on any future developments as they occur.

As well as rising exports, Iran has also witnessed a rising trend in imports over the past calendar year, as the political and economic backdrop has improved slightly. Speaking to the Iran Daily in February 2015, the vice president of the Majlis Economic Commission, Iraj Nadimi**,** stated that car imports have increased since mid-March 2014.

However, Nadimi noted that imported cars cannot meet the country's new vehicle requirements, and hence pose little threat to the domestic auto industry. 'Auto manufacturers are not permitted to set prices for their products the way they want. They are required to observe the models set by the government. To bring car prices down, the first strategy is to do away with the monopoly in production and distribution, and prepare the ground for importing more cars,' he said. The main obstacle to foreign carmakers seeking to export cars to Iran remains the 100% tariff levied on all vehicle imports.

Passenger Vehicles

Table: Passenger Car Market - Historical Data And Forecasts (Iran 2013-2019)

	2013	2014e	2015f	2016f	2017f	2018f	2019f
Passenger car production, units	538,170	925,975	1,111,170	1,388,962	1,527,858	1,665,366	1,827,150
Passenger car production, units, % y-o-y	-38.3	72.1	20.0	25.0	10.0	9.0	9.7
Passenger car sales, units	737,000	1,153,300	1,337,828	1,538,502	1,676,967	1,844,664	2,047,577
Passenger car sales, units, % y-o-y	-28.5	56.5	16.0	15.0	9.0	10.0	11.0
Passenger car trade balance, units	-198,830	-227,325	-226,658	-149,539	-149,108	-179,298	-220,426
Passenger car trade balance, units, % y-o-y	25.1	14.3	-0.3	-34.0	-0.3	20.2	22.9
Passenger car fleet, units	9,713,484	9,864,720	9,995,876	10,197,420	10,398,537	10,623,813	10,840,437
Passenger car fleet, % y-o-y	-8.5	1.6	1.3	2.0	2.0	2.2	2.0
Passenger cars per 1,000 of population	125.4	125.7	125.8	126.7	127.7	129.0	130.2

e/f = BMI estimate/forecast. Source: National sources, BMI

Looking at the most recent sales data by brand (for H114), **Saipa** remains the dominant player on the Iranian new car sales market, although second-placed **Peugeot** is closing the gap.

Over H114, Saipa sold 138,577 units for a share of 35.1%, according to information on the Focus2Move website. Peugeot sold 121,176 units for a share of 30.7%, with **Iran Khodro** in third place on 54,887 units (13.9% share). All told the Top 3 carmakers account for almost 80% of the new car sales market.

Further down the Top 10 chart, of note is the increasing market share being taken by the two Korean carmakers **Hyundai** and **Kia,** as well as the presence of three Chinese carmakers (**Chery**, **Geely** and **Lifan**).

Lastly, Toyota's 10th position within Iran is a far cry from its No 1 position in many of the world's markets and **BMI** would expect the Japanese giant to continue making inroads into the Iranian market over the coming years.

US carmakers remain forbidden from entering the Iranian market, which will put them at a competitive disadvantage should Iran be welcomed back into the international fold over the coming years.

Table: Iran - Top 10 Best-Selling Manufacturers, H114

Manufacturer	Sales	% Share
Saipa	138,577	35.1
Peugeot	121,176	30.7
Iran Khodro	54,887	13.9
Hyundai	20,265	5.1
Renault	19,629	5
Kia	8,946	2.3
Chery	8,162	2.1
Geely	5,764	1.5
Lifan	4,741	1.2
Toyota	4,634	1

Source: Focus2Move

Looking at the best-selling models in Iran, Saipa's Pride is currently the top seller within Iran, followed by Peugeot's Pars, 405 and 206 models. The Saipa Tiba and the Iran Khodro Samand are also reportedly popular within Iran at the present time.

In 2013, local car producer Saipa remained the dominant player on the Iranian new car sales market, selling 237,724 units, according to figures on the Focus2Move website. This equated to a market share of nearly 40%. Saipa manufactures Iran's most popular car, the Pride.

In second place was French carmaker Peugeot, on 181,051 units (30% share), followed by Iran Khodro Company on 102,051 (17%).

In fourth and fifth place were **Renault** (45,221; 7.5%) and Chinese automaker Chery (23,610; 3.9%).

Macroeconomic Forecast

Economic Analysis

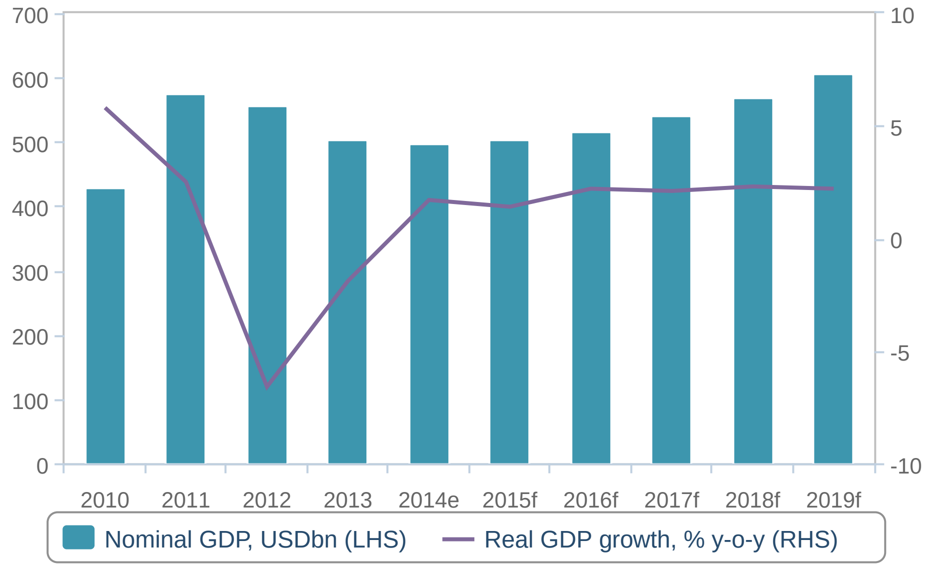
BMI View: *Real GDP growth in Iran will slow in 2015. Lower oil prices will force the government to cut spending, and a failure to reach a breakthrough in nuclear talks will ensure that foreign investment remains low. We have revised downward our real GDP growth forecast for the Iranian economy at 1.4% in 2015 and 2.2% in 2016, from 2.1% and 3.0% previously.*

The Iranian economy will expand slowly in 2015 compared to 2014, as oil prices are low and talks on the nuclear programme fail to reach a breakthrough. We have revised downward our real GDP growth forecast at 1.4% in 2015 and 2.2% in 2016, respectively, from 2.1% and 3.0% previously. The pace of growth will be marginally higher than demographic expansion, implying small productivity gains over the coming quarters.

Declining oil prices will force the government to cut current spending and investment in the country's infrastructure sector, which will result in slow expansion of private consumption and fixed investment. We forecast Brent crude prices to average USD55 per barrel (bbl) and USD58/bbl in 2015 and 2016, respectively, compared to an average of USD106.6/bbl over the 2012-2014 period, a result of oversupply in the market, dwindling global demand and OPEC inaction (*see 'More Pain Ahead, But H115 To Provide A Base', January 8*).

Low Oil Prices A Key Constraint To Growth

Iran - GDP



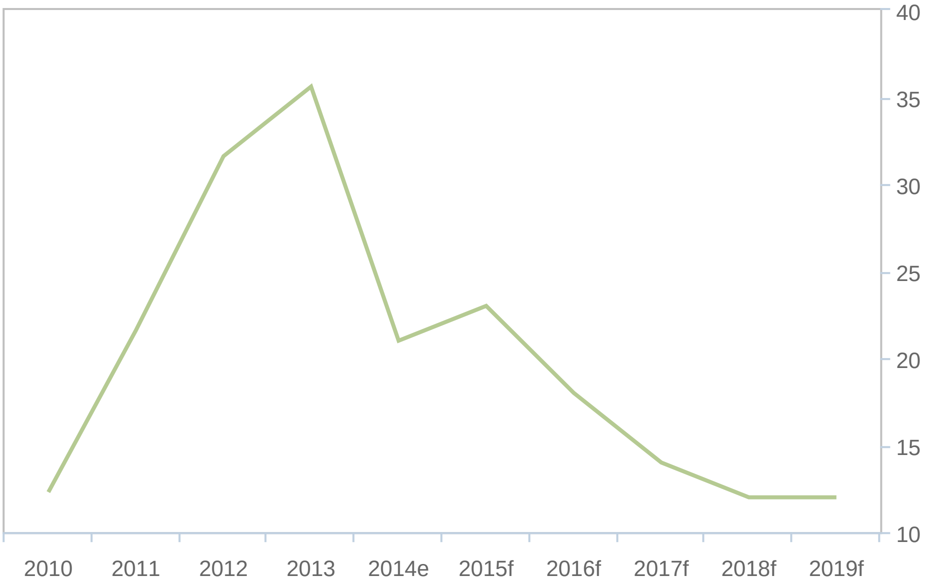
f = BMI forecast. Source: UN, BMI

Key international sanctions on Iran's banking and energy industry will also continue to damage the country's economic outlook. We do not foresee a breakthrough in talks between the P5+1 countries (United States, Russia, China, United Kingdom, France and Germany) and Iran over the next two years, and risks to talks are tilted slightly to the downside (*see 'Nuclear Talks: Breakthrough Unlikely Following Extension', 25 November 2014*). As a result, oil exports and foreign direct investment inflows will remain low.

Private Consumption Outlook: Consumer spending will remain modest over the coming quarters, and we expect expansion of 3.0% and 3.5% in 2015 and 2016 respectively, from 4.5% in 2014. The government will cut current spending this year in a bid to reduce a widening fiscal deficit, a result of falling oil revenues, and will be unable to prop up consumer spending. Elevated price pressures will also hit purchasing power as the government cuts energy and food subsidies. We project consumer price index (CPI) inflation to average 23.0% in FY2015/16 (fiscal year running from March 21 2015 to March 20 2016), from 21.0% in FY2014/15. The failure to reach a breakthrough in nuclear talks will also temper consumer and investor confidence, which had significantly improved since the election of moderate Iranian President Hassan Rouhani in June 2013 lead to an amelioration of relations with the West.

Elevated Inflation To Hinder Consumer Spending

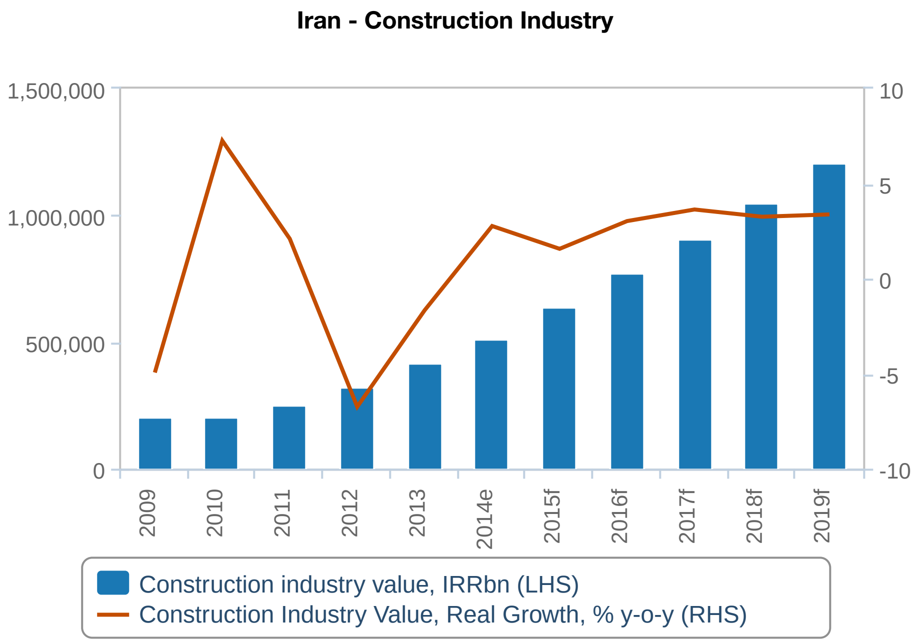
Iran - Consumer Price Index Inflation, % chg, ave



f= BMI forecast. Source: BMI, Central Bank of Iran, Bloomberg

Government Spending Outlook: Government Spending will remain in negative territory over the coming quarters. On December 7, Iranian President Hassan Rouhani proposed a 6.0% hike in nominal terms to the FY2015/16 budget; discounted by inflation, this means that the government plans significant cuts to spending. Spending on the healthcare, education and services sectors will thus be subdued over the coming quarters. We project government consumption contracting by 3.0% in 2015 and 1.0% in 2016, from 4.0% growth in 2014.

Declining Government Spending Hitting Industry In 2015

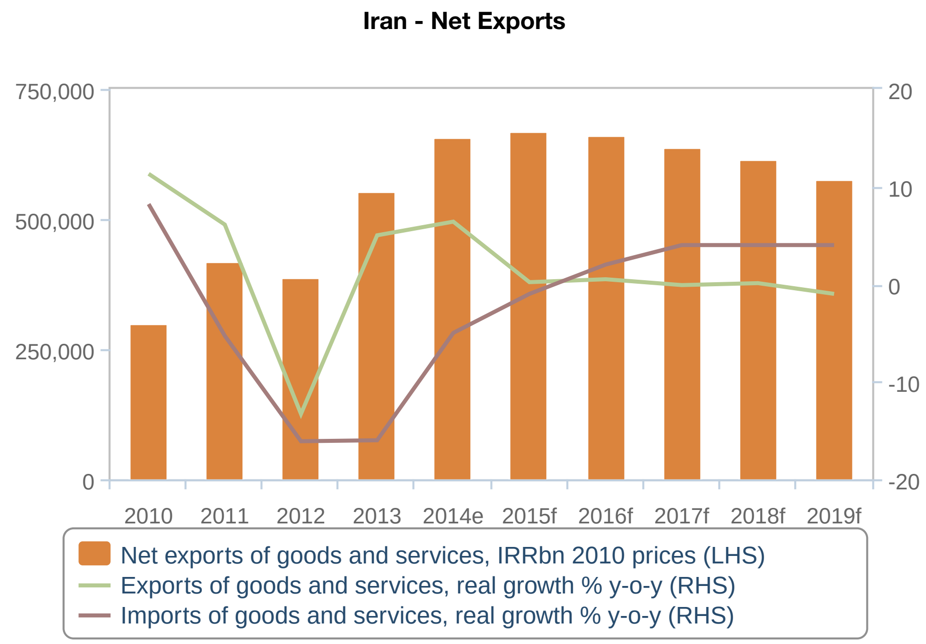


e/f = BMI estmate/forecast. Source: BMI, National sources

Fixed Investment Outlook: Capital formation growth will slow this year, and we project it to expand by 1.0% in 2015, from 3.0% in 2014. **BMI**'s Infrastructure research team holds a relatively bearish outlook for the construction sector in 2015; we project real growth of 1.6%, from 2.8% in 2014, as the government's ability to finance projects is limited by falling oil revenues, and private sector investment remains low. The situation will gradually improve from 2016 as oil prices stabilise, and we project industry growth to average 2.9% over 2015-19.

A host of factors will also hinder foreign direct investment. Foreign companies in nearly every sector have recently expressed interest in returning to the Iranian market, but we believe that Western companies will be unable to undertake major investment in the country due to the sanctions regime. Involvement by firms less exposed to the US market will increase. Some companies are able to avoid the obstacles posed by sanctions by arranging payments in oil or financing in currencies other than the US dollar. That said, the complexity of arrangements to avoid sanctions will result in higher costs and delays in the completion of projects (*see 'Current Account In Deficit From 2015', January 6, 2015*). A further impediment will be Iran's difficult operational environment; Iran scores poorly in **BMI**'s Operational Risks Index, with 41.5 out of 100 ranking the country 13th out of 18 states in the MENA region.

Surplus Narrowing As Energy Exports Stay Low



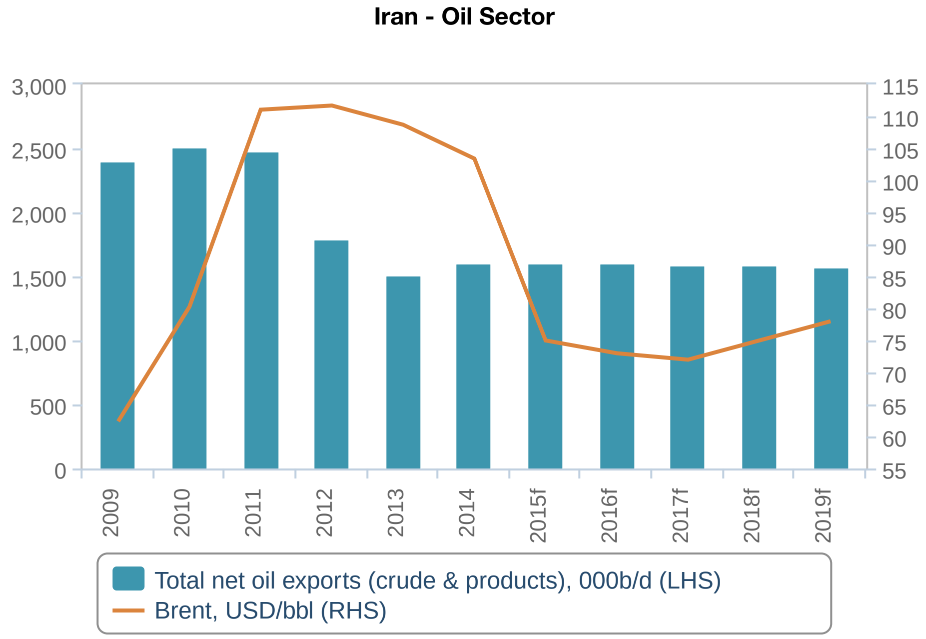
e/f = BMI estimate/forecast. Source: BMI, UN

Net Exports: Iran's net exports surplus will narrow over the next five years. Export growth will slow in 2015 owing to a deceleration in energy production - oil exports accounted for 70.0% of total exports in 2013 - and we project total exports to expand by 0.5% in 2015, from growth of 6.4% in 2014. Low base effects and an uptick in condensates exports - which are not subject to international sanctions - lead to an acceleration of energy export growth in 2014. That said, we are pessimistic that large-scale projects which could boost oil and gas supply will come online in 2015, and energy production will expand slower than consumption.

Growth of exports other than oil will accelerate gradually in 2015, partially compensating for low energy exports. This will result from a weaker rial - which we project to average IRR30,000/USD in 2015 in the official market, from IRR25,800/USD in 2014 - and the government's efforts to increase regional trade. As an illustration, Iran and Iraq recently planned to establish a joint bank, the Islamic Regional Cooperation

Bank for Development and Investment, with a view to increase trade transactions and facilitate bilateral trade.

Low Prices Detrimental To Oil Industry



f = BMI forecast. Source: EIA, BMI

A weak rial will lead to a continued decline of imports in 2015, in line with a trend in place since 2011. Slow economic growth will also contribute to subdued imports, which we forecast to decline by 1.0% in 2015, before returning to growth of 2.0% in 2016.

Table: Economic Activity (Iran 2010-2019)	2010	2011	2012	2013	2014e	2015f	2016f	2017f	2018f	2019f
Nominal GDP, USDbn	429.4	575.4	555.8	504.7	496.3	503.2	514.9	542.2	570.4	606.7
Real GDP growth, % y-o-y	5.8	2.5	-6.6	-1.9	1.7	1.4	2.2	2.1	2.3	2.2
GDP per capita, USD	5,766	7,628	7,272	6,516	6,324	6,331	6,398	6,659	6,925	7,286
Population, mn	74.5	75.4	76.4	77.4	78.5	79.5	80.5	81.4	82.4	83.3
Unemployment, % of labour force, eop	13.5	13.3	13.1	13.0	11.0	10.0	10.0	10.0	10.0	9.0

e/f = BMI estimate/forecast. Source: UN, National Sources, BMI

Industry Risk/Reward Ratings

Middle East - Risk/Reward Index

The aim of **BMI**'s Risk/Reward Index for the automotive industry is to show the rewards and risks that carmakers operating in a particular region - in this case Middle East and North Africa (MENA) - may face. The unique system assesses crucial factors, such as sales and output growth, international trade, market size and location, and the level of market competition, in addition to taking into account a country's economic and political backdrop. The system allows analysts to fully expound the potential advantages and disadvantages of investing in MENA car markets, and offers an overall comparison of the key markets in the region.

Lower oil prices will be a major influence on the economies of many of the countries in our ranking, either as net oil exporters or importers. However, with the top three spots occupied by Gulf Co-operation Council (GCC) states, this supports the view of our Country Risk team that many of these states have sufficient reserves to survive the lower prices.

GCC Still Dominates

Qatar leads the table, up from fourth in the last round-up. Its score is slightly lower than previously, however, reflecting even bigger declines for some of the countries it has overtaken. Its Autos Market score has increased, as robust demand in the market looks set to remain strong over the five-year forecast period. The score for the country-based categories are also relatively high, reflecting its relatively open and well-regulated market.

It is followed by previous leader Kuwait, which has seen its Country Risk scores slip slightly. We do expect the country to lag behind other GCC states in terms of economic growth as its hydrocarbons sector continues to dominate. However, the relative ease of doing business and autos market growth on offer help to support its attractiveness.

Saudi Arabia has moved down one spot to third, although the outlook for demand is still favourable. We expect Saudi Arabia's economic performance to remain strong heading into 2015, on the back of high levels of private consumption, supporting demand for passenger vehicles and fixed investment, which should boost demand for commercial vehicles. We still believe there is potential for Saudi Arabia to move into the lead as its developing production industry gains momentum.

Israel has also dropped one place to fourth on the back of a reduction in its Auto Market score. Higher taxes and depressed private consumption will weigh on car demand and mean much weaker growth than that recorded in 2014. However, in terms of doing business, while it is lacking large-scale production, it scores highly for its business environment and is also gaining a reputation for innovation in the industry.

Little Change Mid-Table

Iran keeps fifth place as the sector fulfilling its potential continues to hang on the country securing a permanent nuclear deal. The growth in production and sales created by the temporary deal has seen its Auto Market score increase, but making long-term investments is still off the cards for Western firms until a deal is in place. The amount of interest from foreign firms in returning to the market could see Iran climb the rankings as soon as a deal is reached.

The UAE stays in sixth. Like rankings leader Qatar, it enjoys transparency and stability, with the GCC determining customs regulations. Coupled with robust sales forecasts, this market openness keeps the UAE among the top GCC states.

Bahrain and Oman stay in seventh and eighth respectively slightly lower overall scores. We have a bullish outlook for Bahrain's sales over the five-year forecast period. We still believe, however, that high levels of car ownership mean it is likely to enjoy lower levels of growth than some of the other markets that are coming from a lower base. That said, while the market is relatively small, it is open and highly competitive. Oman's autos market is also reasonably attractive. Like other GCC states, it offers strong demand and relative stability but no domestic production.

Morocco has made considerable progress to rise from 15th to ninth place. Although its Autos Market score is slightly lower, its Country Structure score has received a boost. One development of note is the plan to recognise European patents in the country from March 1 2015, which will improve its prospects as a destination for investment, particularly for European companies.

Conflicts Take Their Toll

Jordan and Lebanon have swapped places in 10th and 11th places, but with lower scores as events in neighbouring Syria continue to pose a risk. That said, major brands have opened new showrooms in both countries in the latter months of 2014 and we continue to see opportunities in Jordan for low-cost brands in the market and trade talks with the Indian government could encourage new market entrants.

Iraq has climbed to 12th with an increase in its Autos Market score. Although the IS conflict and lower oil prices will be key determinants of vehicle sales in the immediate term, we have raised our forecasts for 2016 and 2017 as we expect sales to start regaining some momentum. In the longer term, therefore, the market still holds potential, depending on the security situation.

Tunisia has slipped to 13th with a reduction in its Country Structure score. However, the longer-term picture could be more favourable as we expect to see an investor-friendly cabinet to be formed in Q115 and the effects of economic reform to be felt from 2016 onward. On the Autos side, however, we expect the parallel market to provide an ongoing threat to new car sales in the immediate term.

Algeria has moved up to 14th with an increase in its Autos Market score. As a production base, it is still a burgeoning hub with investment flowing in from the likes of **Renault** and parts supplier **Lear Corp**. However, its reliance on the hydrocarbons sector will leave the economy vulnerable to lower oil prices and increase macroeconomic risks.

Egypt is now in 15th with a reduced Autos Market score. This is not necessarily a reflection of a poor market, however, more that after an incredibly strong comeback in 2014, such growth levels are unlikely to be replicated over the remainder of the forecast period. In investment terms, we expect an uptick across the board and particularly in the Autos sector in 2015 as political stability returns.

Libya and Syria are in 16th and 17th, marred by instability. In Libya this will result in oil exports declining further, which, along with lower prices, will be detrimental to the economy. In Syria, the ongoing civil war provides no prospect of an improvement in the country's ratings in the foreseeable future.

Table: MENA Autos Risk/Reward Index

	Rewards			Risks				
	Autos Market	Country Structure	Industry Rewards	Market Risks	Country Risks	Industry Risks	Autos Rating	Rank
Qatar	31.67	81.57	49.13	75.00	63.08	69.04	55.11	**1**
Kuwait	31.67	74.09	46.52	75.00	57.54	66.27	52.44	**2**
Saudi Arabia	31.67	69.49	44.91	75.00	62.14	68.57	52.01	**3**
Israel	25.00	77.19	43.27	75.00	67.74	71.37	51.70	**4**
Iran	55.00	39.52	49.58	75.00	35.36	55.18	51.26	**5**
UAE	23.33	79.00	42.82	75.00	64.53	69.77	50.90	**6**
Bahrain	25.00	76.38	42.98	75.00	61.01	68.01	50.49	**7**
Oman	23.33	60.78	36.44	85.00	57.85	71.42	46.93	**8**
Morocco	28.33	40.18	32.48	75.00	53.35	64.17	41.99	**9**
Jordan	18.33	51.41	29.91	70.00	58.01	64.00	40.14	**10**
Lebanon	13.33	54.04	27.58	80.00	58.70	69.35	40.11	**11**
Iraq	25.00	53.61	35.01	60.00	42.92	51.46	39.95	**12**
Tunisia	13.33	50.36	26.29	85.00	52.33	68.66	39.00	**13**
Algeria	23.33	41.69	29.76	65.00	49.23	57.11	37.97	**14**
Egypt	18.33	28.28	21.82	75.00	47.17	61.08	33.60	**15**
Libya	8.33	55.07	24.69	65.00	32.17	48.59	31.86	**16**
Syria	25.00	36.70	29.10	10.00	24.67	17.34	25.57	**17**

Scores out of 100, with 100 highest. Source: BMI

Company Profile

Company Monitor

***BMI View:** The addition of a sport utility vehicle (SUV) to Maserati's product range will enable it to build on its momentum in the MENA region, where SUVs will again be a growth market. Expansion into areas such as North Africa will also create opportunities as increased stability in markets such as Egypt supports sales growth.*

The Middle East and North Africa (MENA) has become one of Italian luxury marque **Maserati**'s leading growth markets and the launch of its first sport utility vehicle (SUV) within the next year will help to consolidate its performance. Having grown its global sales by 136% in 2014, Maserati's MENA division posted growth of 155%, to become the company's fifth largest region by volume, with 2,050 units sold.

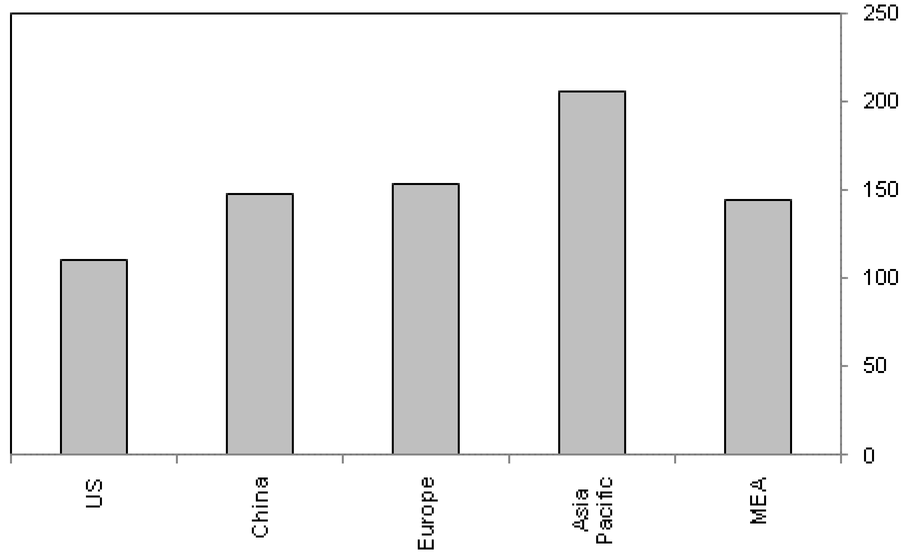
Much of this growth was down to the launch of the new Ghibli, the company's first four-door sedan, and a new engine for the Quattroporte. However, we believe there will be an even bigger reception for the Levante SUV when it is launched toward the end of the year, given the combined popularity of the SUV and premium segments in the region, particularly in the Gulf Co-operation Council (GCC) states. It aligns with our view that 2015 will be a big year for SUVs in general (*see 'Global Autos: Key Trends for 2015', December 8 2014*).

It was the GCC states contributing the majority of the region's growth, led by a 209% increase in the UAE which accounts for 43% of the region's sales. It was followed by Saudi Arabia with 178% growth and Kuwait with sales up 166%. The performance of the UAE and Saudi Arabia underscores our view that these are the two safe havens for growth in a turbulent region and that despite the growth of the volume segment in both markets, the luxury segment will continue to flourish.

Indeed, Maserati's investment in its expansion in these markets also contributed to its record sales performance. New service facilities opened up in Sharjah and Oman, bringing value-added after-sales services to its business, while more new dealerships are being built in Sharjah and Qatar and a combined sales and service facility is planned for Dammam, Saudi Arabia.

MENA Among The Leaders

Maserati Global Sales Growth By Region 2014 (% chg y-o-y)



Source: Maserati

Outside of the GCC, Maserati has also expanded its presence in the Levant states, opening new outlets in Jordan and Lebanon in 2014. The luxury market in these countries is relatively small, with the Lebanese vehicle importers' association reporting that over 90% of new sales are small cars valued at less than USD15,000, but there is room to grow from a small base. The risk to these markets is the close proximity to the violence in Syria, but so far this has not deterred carmakers from opening new showrooms.

North Africa has been another area of expansion, with the company's first Moroccan showroom opening in Casablanca in February 2014. Expansion in some areas, including Morocco, Egypt (where Maserati has one showroom) and Syria, was put on hold during the Arab Spring period, and is just being implemented now. While Syria remains off limits, the rest of the region is now more accommodating of expansion, particularly in Egypt where increased stability bodes well for the Autos sector (*see 'Increased Stability Supports Car Sales Growth', January 2*).

Iran Khodro Company (IKCO)

Strengths	▪ Iran's largest auto manufacturer. ▪ Third-largest seller of cars in the domestic market over 2013. ▪ Samand and Peugeot Pars models remain popular.
Weaknesses	▪ Company needs investment in its facilities and R&D. ▪ Company is primarily focused on one country.
Opportunities	▪ Should sanctions be permanently eased, then there is scope for more rapid growth in new car sales as the Iranian economy - especially its key oil sector - regains access to the world's markets. ▪ Company is looking to increase exports. ▪ Future tie-up with Peugeot could be beneficial to both companies. ▪ Peugeot 206 and 405 models have been selling well. ▪ Local production facilities give the company a competitive edge within Iraq.
Threats	▪ If nuclear talks between Iran and the Western powers fail and new sanctions are imposed, then this would be devastating for the local auto industry. ▪ Political instability remains a key concern for the whole Iranian economy and, by extension, new car sales. ▪ Increased foreign imports could eat into IKCO's market share over time.

Company Overview

IKCO is the largest auto manufacturer in Iran and was established in 1963. The firm also has foreign production facilities, including sites in Azerbaijan, Belarus and Venezuela.

In recent years, IKCO has concentrated on expanding its own ranges, as opposed to those it produces under license to other manufacturers. These models include the

Dena, Runna, Soren, Sarir, Samand and Bardo. In addition, the company still produces variants of the Peugeot 405, 206 and 207 models, according to its website.

Strategy

In January 2015, the IRNA reported that IKCO had expanded its after-sale services in various Iraqi cities, with the country also looking to increase its market share in the Persian Gulf littoral countries, according to managing director Hashem Yekke-Zare'a. The governor of the Iraqi city of Karbala, Aqil al-Tarihi said: 'Foreign vehicles manufactured in various countries, including Russia, are present in Iraq but most of them do not match the geographical conditions of Iraq. They are appropriate for use in the winter season, but do not match the summer season perfectly, while the Iran Khodro products do not have that deficiency'.

According to an October 2014 report in the Iran Daily, IKCO is now producing some 50 cars a day in Iraq, with the company set to boost output to 100 cars a day amid signs of stronger demand for cars within Iraq. IKCO's Deputy CEO for exports, Ali Elmi was quoted by the Fars news agency as saying that IKCO produces a variety of cars within Iraq, including the Runna, Samand, Soren, Peugeot Pars and Peugeot 405. The company also has several experienced engineers based at the Iskandariya factory to monitor the build quality of Iraqi-produced cars.

In August 2014, the Fars News Agency reported that **Iran Khodro Industrial Group** (IKCO) plans to export 10,000 vehicles to Russia. According to CEO Hashem Yekehzare, the move is in line with the company's efforts to raise its world market share. IKCO intends to sell one-third of its cars in international markets, according to Yekehzare. He said: 'Meeting Russian standards is the first step to enter this market. But what is important is to provide suitable after-sales services to our customers in this market.'

Over the first seven months of the Iranian calendar year, IKCO reported an annual export increase of over 100%, to 1,400 vehicles. According to IKCO's deputy head of exports and international affairs, Ali Elmi, only 600 cars were sold abroad by the company in the corresponding period of 2013. Traditional destination markets for Iranian cars are Iraq, Venezuela and Azerbaijan; however, the company expects the Russian market to be opened for Iranian cars by 2015.

In October 2014, IKCO announced plans to commence production of the new PU1 pick-up truck, to be on the market by the start of the next Iranian calendar year (March 21 2015). The Tasnim news agency reports that the PU1 will be based on the Iranian-assembled Peugeot 405 platform, which features a dual-fuel 1700cc engine. Gholamreza Sadeghian, managing director of ICKO's Tabriz plant, said that production is scheduled to begin in late autumn, with a target of 5,000 units by the end of the Iranian calendar year.

In July 2014, the ISNA news agency stated that IKCO is to form a joint venture with French automaker **PSA Peugeot Citroën.** The move is in line with Peugeot's efforts to expand its services, products and exports, according to the report, which cited

Khodro's managing director, Hashem Yekkeh Zare. Under the joint venture, the two companies are expected to manufacture Peugeot 301 and 2008 models using parts provided by IKCO. In May, IKCO set out certain conditions to Peugeot for a joint venture, including the closure of assembly units. 'We want them to transfer technology to us and establish research and development centres in Iran,' said Zare at the time.

In June 2014, ISNA reported that Japanese automaker **Suzuki Motor** is in discussions with Iranian carmaker **IKCO** to launch a new car production line in Iran, according to Abdollah Babaee, director of marketing and sales at IKCO.

In May 2014, IKCO reportedly set out a number of conditions for returning to a partnership with French carmaker **Peugeot**, following a meeting between the bosses of the two companies, which **BMI** believes shows mutual needs within the industry. Peugeot and its compatriot Renault have both racked up significant losses following their withdrawal from Iran, thereby reflecting the significance of the Iranian market. However, IKCO's demands for greater investment in technology transfer and research and development (R&D) facilities show where the national industry is lacking.

IKCO managing director Hashem Yekkeh Zare said that Peugeot should end its own assembly operations and focus on joint production with the Iranian carmaker, including transferring its technology and setting up local R&D facilities. Zare said IKCO will only consider resuming its relationship if these conditions are met.

Societe Annonyme Iranienne de Production Automobile (Saipa)

Strengths

- Second-largest car manufacturer in Iran.
- No 1 seller on the domestic market.
- Company's Pride model is the most popular in Iran.
- Strong increases in sales and production reported for 2014.

Weaknesses

- Company needs investment in its facilities and R&D.
- Company is primarily focused on one country.

Opportunities

- Should sanctions be permanently eased, then there is scope for more rapid growth in new car sales as the Iranian economy - especially its key oil sector - regains access to the world's markets.
- Company is looking to increase exports.
- Future tie-up with Renault could be beneficial to both companies.
- Tiba model has been selling well across 2014.
- Local production facilities give the company a competitive edge within Iraq.

Threats

- If nuclear talks between Iran and the Western powers fail and new sanctions are imposed, then this would be devastating for the local auto industry.
- Political instability remains a key concern for the whole Iranian economy and, by extension, new car sales.
- Increased foreign imports could eat into Saipa's dominant market share over time.

Company Overview Saipa is the second-largest auto manufacturer in Iran. The company produces a wide range of passenger and commercial vehicles, some of which are based on models previously developed by Kia (Pride) and Renault (Logan). The company is also looking to develop its own models, such as the Tiba, which is reportedly selling well at present.

The Iranian government has control over the company through IDRO, an agency of the Ministry of Industry and Mines. In 1998, Saipa listed on the Tehran Stock Exchange as a first step towards privatisation. The majority 14.3% stake in private hands belongs to the Bahman Group, which is also engaged in autos manufacturing, under licence from Mazda, through Bahman Auto.

Speaking to Press TV in February 2015, Saipa's head of commerce and sales office, Mohammad Reza Abbasi, stated that Saipa saw production and sales both rise by 32% during 2014. Looking forward, Abbasi said that Saipa will start to produce a low-cost car, known as the Saina, during the first half of the new Iranian calendar year, with the company also set to launch more than 10 models at the next motor show to be held in Isfahan.

In the same month, Press TV reported on comments from Saipa's CEO, Saied Madani, that the company would soon launch three new models onto the Iraqi market. Madani said that his company is looking to boost its market share within Iraq, saying that 'Saipa products are always highly received in Iraq thanks to their competitive prices, cheap spare parts and low fuel consumption'. Saipa operates one auto plant in Iraq that primarily produces Tiba and X100 models.

In November 2014, The Tehran Times reported that French carmaker Renault was in talks with Saipa about buying a stake in its Pars Khodro subsidiary, according to comments from Majid Souri, Saipa's investment management director. However, there has yet to be any definitive agreement between the two companies, according to Souri, with much depending on the final outcome of the ongoing nuclear talks between Tehran and the P5+1 group of nations.

In June 2014, Renault's Chief Performance Officer Jerome Stoll said that his company is looking for a financial partner to resume full operations in Iran, where it had enjoyed a strong market position before the imposition of international sanctions against Iran in 2011.

In March 2014, Saipa signed a deal with Chinese automaker **C**hongqing Changan Automobile Co. to manufacture cars jointly, according to a report by ISNA. Under the agreement, two models of car will be manufactured by Saipa's subsidiary Saipa Kashan. This subsidiary has the capacity to make 180,000 cars on a yearly basis.

Regional Overview

Middle East Overview

In **BMI**'s regular round-up of production investments, we track the latest projects from the production side of the industry and analyse trends that we see developing on a regional basis. In doing so, we hope to build a picture of any potential hubs that may be developing, as well as company strategy in terms of production bases and export programmes.

Table: MENA Autos Production Investments

Date Announced	Country	City/State/ Region	Company	Brief Description	Date On Stream
Jun-14	Saudi Arabia	n/a	BYD Auto	Joint venture to locally produce BYD cars	In feasibility study phase
Aug-14	Iran	Tabriz	Austrian government	Plans to establish a full production line served by local suppliers	n/a
Oct-14	Iraq	Iskandariya	IKCO	Increasing daily output of passenger cars to 50, with plans to double to 100	2014
Oct-14	Iran	Tabriz	IKCO	Production of new pick-up truck	2015

n/a = not available. Source: BMI

It is most notable in this latest round-up of autos investment in the Middle East and North Africa region that the number of confirmed projects does not reflect the amount of interest shown in the region by the autos sector. In some cases, companies are waiting for the sector to become more developed, or in the case of Iran especially, foreign carmakers are awaiting a finalised nuclear deal with the P5+1 countries.

For that reason, the confirmed investment in Iran so far comes from domestic giant **Iran Khodro Industrial Group** (IKCO), which is adding new products to its production line. Its latest addition is the PU1 pick-up truck, which will enter production in autumn 2015, but it also has more long-term plans to introduce new or revamped models every six months, plus a new engine every three years starting from October 2105. It has also been expanding its operations in Iraq, which has traditionally been one of its biggest export markets, but is now a growing production base.

The bigger boost to its operations will come, however, if a permanent nuclear deal is signed. The company has reached an agreement with French carmakers **PSA Peugeot Citroen** and **Renault** to establish joint ventures for domestic production. At least two new Peugeot models, the 301 and 2008, would be produced under the deals, as well as the Renault Clio4 and Captur. **Suzuki Motor** has also met with the company regarding a production deal. The deadline for a permanent nuclear deal is November 24, which would give the green light for many of these projects to go ahead.

Other areas of potential not covered in the table include Egypt, where the country's domestic producer **Nasr Automotive** is in talks with Russia's **AvtoVAZ** regarding a production joint venture. We see this as a win-win for both sides if it goes ahead, as Nasr has been looking to ramp up volume production since being given a reprieve from liquidation by the government in 2013, and AvtoVAZ needs new markets to focus on outside of Russia (*see 'AvtoVAZ-Nasr Deal Is A Boost For Both Sides', October 2*).

In another positive sign for North Africa, Renault is considering an engine plant in Morocco to support its vehicle production plants in Tangier and Casablanca, which have a combined annual capacity of 400,000 units. However, Renault's chief competitive officer, Thierry Bollore, said the company would need a better supply chain on the ground in Morocco before embarking on such a project. It would align with our long-held view of Morocco as a developing autos production and export hub, particularly for Renault (*see 'Second Production Line Gives Renault Options', October 9 2013*).

Global Industry Overview

In 2015, the autos sector faces considerable opportunities and risks on both the sales and manufacturing side. In addition to the industry specific factors such as growing R&D costs in a period of increasing innovation, the industry will also need to take into account lower oil prices as fact rather than a risk scenario, following OPEC's decision to maintain output at its current level. We have focused on what we think will be the key themes to look for in 2015 and where the risks and opportunities lie for autos firms and outside investors alike.

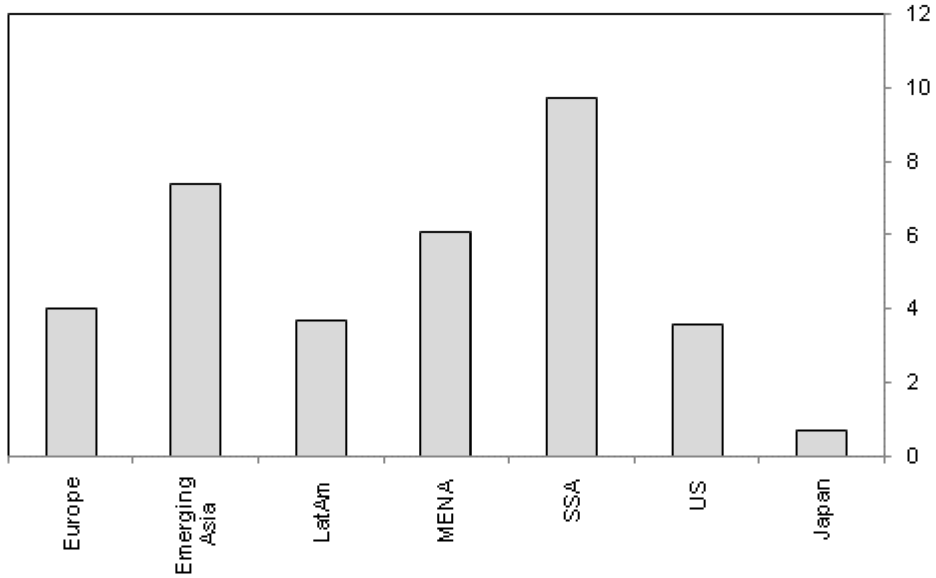
Africa Still The Growth Driver

In terms of vehicle sales, the overriding theme is one of moderation in comparison to previous years. Markets that enjoyed a period of recovery in 2013 and 2014 will begin to stabilise in 2015, which is particularly true of Europe. It has been our long-held view that the European market as a whole will see a slowdown in sales growth in 2015 as the eurozone recovery falters and consumer sentiment dampens as a result. Our aggregate forecast is for total vehicle sales growth of 4.0% in 2015, down from an estimated 5.3% in 2014.

The US will also register slower growth in 2015, although we see this as more of a return to the mature market's natural level, rather than a negative development. Indeed, 3.6% is still relatively robust compared with pre-crisis growth levels when the light vehicle market was last at 16mn units. Lower oil prices also offer upside potential given the popularity of the light truck and sport utility vehicle (SUV) segment.

More Moderate Outlook All Round

Vehicle Sales Growth By Region (% chg y-o-y), 2015f



f = BMI forecast. Source: BMI

We will also look at the Middle East and North Africa (MENA) and Latin America in more detail in relation to oil prices, as they are home to some of the countries that are most likely to be impacted. Between the two, however, we see MENA as the better performer with growth of 6.1% forecast, compared with just 3.7% for Latin America, the lowest of the emerging regions.

This leaves Emerging Asia and Sub-Saharan Africa (SSA) as the outperformers. Within Emerging Asia, where sales are forecast to grow 7.4%, we expect to see the strongest growth coming from South East Asia, particularly as the ASEAN Economic Community integration enables the existing outperformers to consolidate their position. SSA, meanwhile, still benefits from a low base, with growth of 9.7% forecast for 2015.

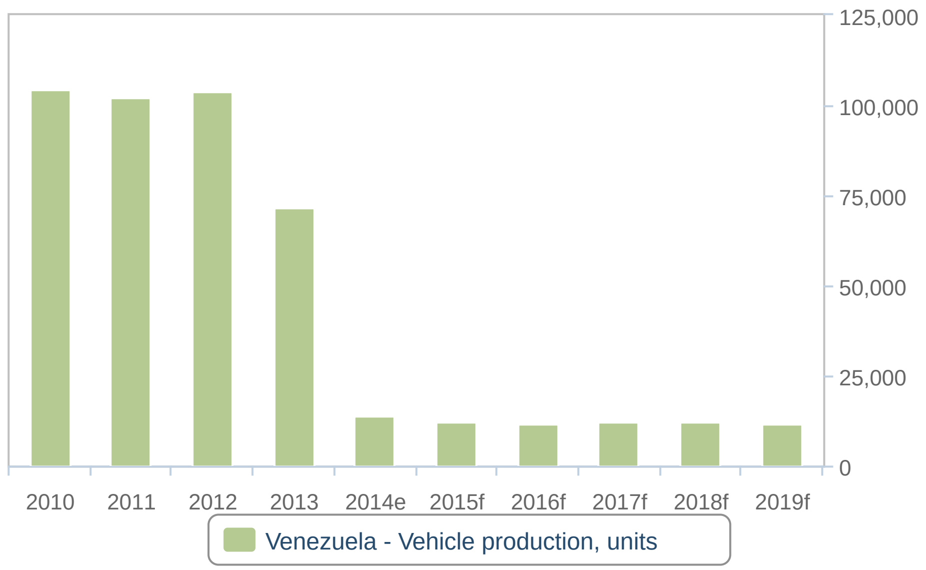
Oil Prices A Boon For Importers

Following OPEC's decision to maintain its current production levels and the resulting revision to our oil price outlook (*see 'Oil Below USD80/bbl To 2020', December 1*) we will see varying effects on the autos sector, depending on whether countries are net exporters or importers. This is not just related to fuel prices and whether consumers are influenced to buy vehicles or not by the prices at the pump. In some cases, a government's reliance on oil income for foreign currency can have a domino effect for the whole manufacturing sector.

This is the case in Venezuela, where vehicle manufacturing has already been decimated by a lack of foreign currency needed to import components. We see the country being one of the hardest hit by lower oil prices, based on its higher fiscal breakeven price per barrel, which will limit income of foreign currency even further. As vehicle production is hit, demand will also see a more prominent decline as locally produced inventories run low and the increasingly weak currency makes imported cars prohibitively expensive.

Even Minimum Output At Risk

Venezuela Vehicle Production



e/f = BMI estimate/forecast. Source: OICA, BMI

MENA will see mixed reactions based on the region's split of oil importers and exporters. Despite concerns from major carmakers such as **Toyota Motor** that lower oil prices will be one of the biggest threats to growth in the region, we see the UAE, Saudi Arabia and Kuwait as best placed among net exporters to offset lower oil prices with substantial reserves. As such, their position as the largest vehicle markets in the region should also be safe.

Regulation Driving Innovation

The link between the automotive and technology sectors will continue to strengthen in 2015, and to a large extent this will be driven by tightening regulations in a number of areas. Increasingly stringent fuel economy standards in particular will see advances in the use of different lightweight materials, such as aluminium, as well as further development work on alternative fuel types, including fuel cells and different types of batteries for electric cars.

Table: Fuel Economy Targets By Geography

Region	Fuel Economy Targets
South Korea	Target of 40.0mpg by 2015
	Target of 47.0mpg by 2020
Europe	Target of 43.0mpg for petrol and 48mpg for diesel by 2015.
	Target of 59.0mpg for petrol and 65mpg for diesel by 2021
US	Target of 34.1mpg by 2016
	Target of 54.5 mpg by 2025
China	Target of 34.0mpg by 2015
	Target of 47.0mpg by 2020
India	Target of 42.8 mpg by 2016
	Target of 51.7mpg by 2021

Source: BMI

Safety standards will also be a key driver of innovation, mostly for suppliers, which we expect to result in increased M&A activity in the supplier segment as a lower cost route to research and development in these areas. Much of the new technology required will be linked to another trend for 2015 - connected cars. While the growth of Telematics and in-car technology is not a new thing, the closer the industry moves to autonomous driving, using other cars for information, the more requirements for safety features will grow in tandem.

Outside of the cars themselves, we see one of the biggest areas of innovation being in the way cars are sold. Growth in e-commerce globally means that online retail in the sector will become more prominent and we are already seeing major dealer groups stepping up their online activity to move beyond just providing information to more sales-based services, while **Tesla** is selling its Model S on Alibaba in China.

SUVs To Be Segment Of Choice

In terms of vehicle segments, we expect the SUV market to be an outperformer in 2015, led by the growth of the subcompact SUV segment. In major emerging markets such as China and India, this will be driven by the rise of the middle class consumer looking to upgrade (*see 'SUVs: The Next Big Thing For Asia', October 15*), while in more-developed states such as the US, it will be the continuation of a preference for vehicles with more space and robust characteristics. Globally, the trend will be supported by lower oil prices.

Based on the fuel economy standards mentioned previously, however, we will see subcompact SUVs coming to prominence, which will provide better fuel economy while fulfilling consumer requirements (*see 'Rising Prominence Of Subcompact SUVs', October 31*). There will be a raft of new launches from several carmakers in 2015, as they add these smaller models to improve the fuel economy of their overall vehicle fleet.

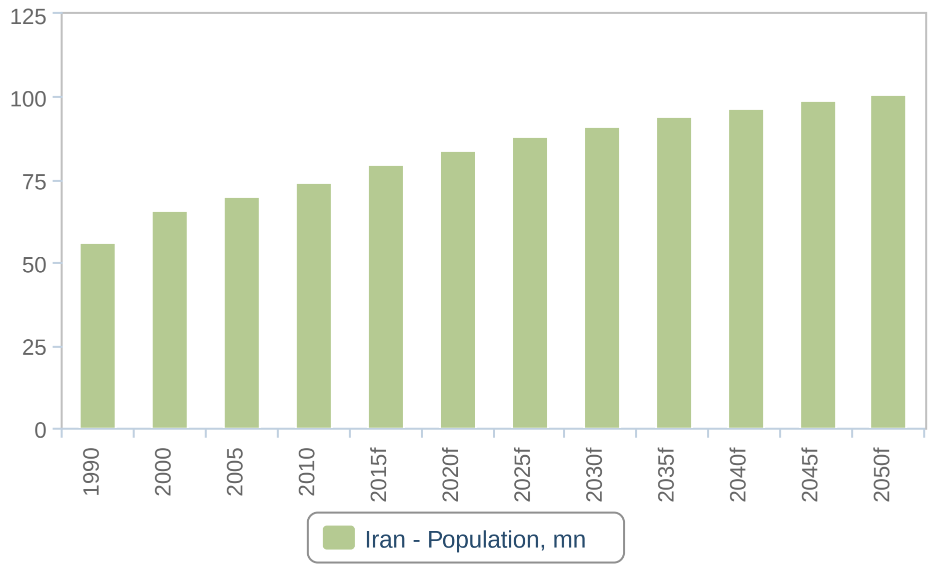
Demographic Forecast

Demographic analysis is a key pillar of **BMI**'s macroeconomic and industry forecasting model. Not only is the total population of a country a key variable in consumer demand, but an understanding of the demographic profile is essential to understanding issues ranging from future population trends to productivity growth and government spending requirements.

The accompanying charts detail the population pyramid for 2015, the change in the structure of the population between 2015 and 2050 and the total population between 1990 and 2050. The tables show indicators from all of these charts, in addition to key metrics such as population ratios, the urban/rural split and life expectancy.

Population

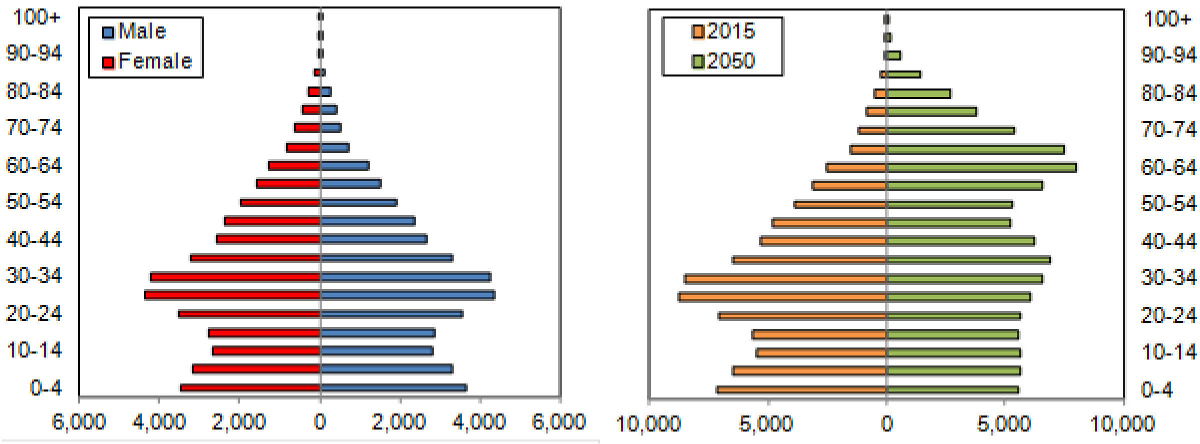
(1990-2050)



f = BMI forecast. Source: World Bank, UN, BMI

Iran Population Pyramid

2015 (LHS) & 2015 Versus 2050 (RHS)



Source: World Bank, UN, BMI

Table: Population Headline Indicators (Iran 1990-2025)

	1990	2000	2005	2010	2015f	2020f	2025f
Population, total, '000	56,361	65,911	70,152	74,462	79,476	84,148	88,064
Population, % change y-o-y	na	1.6	1.2	1.3	1.3	1.1	0.8
Population, total, male, '000	28,807	33,504	35,917	37,656	39,915	42,307	44,213
Population, total, female, '000	27,554	32,406	34,235	36,805	39,560	41,840	43,850
Population ratio, male/female	1.05	1.03	1.05	1.02	1.01	1.01	1.01

na = not available; f = BMI forecast. Source: World Bank, UN, BMI

Table: Key Population Ratios (Iran 1990-2025)

	1990	2000	2005	2010	2015f	2020f	2025f
Active population, total, '000	28,945	40,290	48,583	53,034	55,945	58,184	60,945
Active population, % of total population	51.4	61.1	69.3	71.2	70.4	69.1	69.2
Dependent population, total, '000	27,415	25,620	21,569	21,427	23,530	25,964	27,118
Dependent ratio, % of total working age	94.7	63.6	44.4	40.4	42.1	44.6	44.5

Key Population Ratios (Iran 1990-2025) - Continued	1990	2000	2005	2010	2015f	2020f	2025f
Youth population, total, '000	25,543	22,850	18,115	17,585	19,140	20,362	19,984
Youth population, % of total working age	88.2	56.7	37.3	33.2	34.2	35.0	32.8
Pensionable population, '000	1,872	2,770	3,453	3,841	4,389	5,601	7,134
Pensionable population, % of total working age	6.5	6.9	7.1	7.2	7.8	9.6	11.7

f = BMI forecast. Source: World Bank, UN, BMI

Table: Urban/Rural Population And Life Expectancy (Iran 1990-2025)	1990	2000	2005	2010e	2015f	2020f	2025f
Urban population, '000	31,748.6	42,210.8	47,393.5	51,332.8	55,362.4	59,374.4	63,078.7
Urban population, % of total	56.3	64.0	67.6	68.9	69.7	70.6	71.6
Rural population, '000	24,613.2	23,700.3	22,758.8	23,129.5	24,113.9	24,774.2	24,985.6
Rural population, % of total	43.7	36.0	32.4	31.1	30.3	29.4	28.4
Life expectancy at birth, male, years	61.2	68.7	70.0	71.3	72.8	74.2	75.5
Life expectancy at birth, female, years	65.8	70.6	73.1	75.1	76.6	78.0	79.2
Life expectancy at birth, average, years	63.4	69.6	71.5	73.1	74.6	76.0	77.3

e/f = BMI estimate/forecast. Source: World Bank, UN, BMI

Table: Population By Age Group (Iran 1990-2025)	1990	2000	2005	2010	2015f	2020f	2025f
Population, 0-4 yrs, total, '000	9,312	6,316	5,483	6,555	7,146	6,751	6,148
Population, 5-9 yrs, total, '000	8,905	7,552	5,476	5,416	6,507	7,116	6,729
Population, 10-14 yrs, total, '000	7,324	8,981	7,154	5,613	5,487	6,494	7,105
Population, 15-19 yrs, total, '000	5,822	8,800	9,247	7,215	5,643	5,466	6,474
Population, 20-24 yrs, total, '000	4,697	6,932	9,143	8,993	7,067	5,595	5,424
Population, 25-29 yrs, total, '000	4,054	5,315	6,859	8,704	8,726	6,997	5,541
Population, 30-34 yrs, total, '000	3,535	4,442	5,202	6,521	8,484	8,649	6,937
Population, 35-39 yrs, total, '000	3,030	3,886	4,693	5,210	6,497	8,410	8,579
Population, 40-44 yrs, total, '000	2,123	3,372	4,112	4,833	5,262	6,431	8,333
Population, 45-49 yrs, total, '000	1,620	2,857	3,421	4,032	4,757	5,193	6,353

Population By Age Group (Iran 1990-2025) - Continued							
	1990	**2000**	**2005**	**2010**	**2015f**	**2020f**	**2025f**
Population, 50-54 yrs, total, '000	1,526	1,929	2,800	3,244	3,895	4,665	5,101
Population, 55-59 yrs, total, '000	1,393	1,431	1,766	2,637	3,109	3,788	4,548
Population, 60-64 yrs, total, '000	1,140	1,322	1,336	1,639	2,500	2,985	3,652
Population, 65-69 yrs, total, '000	898	1,145	1,257	1,279	1,550	2,340	2,813
Population, 70-74 yrs, total, '000	507	825	1,055	1,129	1,143	1,369	2,090
Population, 75-79 yrs, total, '000	269	508	654	802	876	902	1,105
Population, 80-84 yrs, total, '000	135	203	347	413	528	598	637
Population, 85-89 yrs, total, '000	48	66	112	172	216	290	343
Population, 90-94 yrs, total, '000	10	17	21	38	63	84	119
Population, 95-99 yrs, total, '000	1	2	3	4	8	15	22
Population, 100+ yrs, total, '000	0	0	0	0	0	1	2

f = BMI forecast. Source: World Bank, UN, BMI

Table: Population By Age Group % (Iran 1990-2025)							
	1990	**2000**	**2005**	**2010**	**2015f**	**2020f**	**2025f**
Population, 0-4 yrs, % total	16.52	9.58	7.82	8.80	8.99	8.02	6.98
Population, 5-9 yrs, % total	15.80	11.46	7.81	7.27	8.19	8.46	7.64
Population, 10-14 yrs, % total	13.00	13.63	10.20	7.54	6.90	7.72	8.07
Population, 15-19 yrs, % total	10.33	13.35	13.18	9.69	7.10	6.50	7.35
Population, 20-24 yrs, % total	8.34	10.52	13.03	12.08	8.89	6.65	6.16
Population, 25-29 yrs, % total	7.19	8.06	9.78	11.69	10.98	8.32	6.29
Population, 30-34 yrs, % total	6.27	6.74	7.42	8.76	10.68	10.28	7.88
Population, 35-39 yrs, % total	5.38	5.90	6.69	7.00	8.18	9.99	9.74
Population, 40-44 yrs, % total	3.77	5.12	5.86	6.49	6.62	7.64	9.46
Population, 45-49 yrs, % total	2.88	4.33	4.88	5.42	5.99	6.17	7.22
Population, 50-54 yrs, % total	2.71	2.93	3.99	4.36	4.90	5.54	5.79
Population, 55-59 yrs, % total	2.47	2.17	2.52	3.54	3.91	4.50	5.17
Population, 60-64 yrs, % total	2.02	2.01	1.90	2.20	3.15	3.55	4.15
Population, 65-69 yrs, % total	1.59	1.74	1.79	1.72	1.95	2.78	3.19
Population, 70-74 yrs, % total	0.90	1.25	1.50	1.52	1.44	1.63	2.37
Population, 75-79 yrs, % total	0.48	0.77	0.93	1.08	1.10	1.07	1.26
Population, 80-84 yrs, % total	0.24	0.31	0.50	0.55	0.66	0.71	0.72

Population By Age Group % (Iran 1990-2025) - Continued							
	1990	**2000**	**2005**	**2010**	**2015f**	**2020f**	**2025f**
Population, 85-89 yrs, % total	0.09	0.10	0.16	0.23	0.27	0.34	0.39
Population, 90-94 yrs, % total	0.02	0.03	0.03	0.05	0.08	0.10	0.14
Population, 95-99 yrs, % total	0.00	0.00	0.00	0.01	0.01	0.02	0.03
Population, 100+ yrs, % total	0.00	0.00	0.00	0.00	0.00	0.00	0.00

f = BMI forecast. Source: World Bank, UN, BMI

Methodology

Industry Forecasts

BMI's industry forecasts are generated using the best-practice techniques of time-series modelling and causal/econometric modelling. The precise form of model we use varies from industry to industry, in each case being determined, as per standard practice, by the prevailing features of the industry data being examined.

Common to our analysis of every industry is the use of vector autoregressions. Vector autoregressions allow us to forecast a variable using more than the variable's own history as explanatory information. For example, when forecasting oil prices, we can include information about oil consumption, supply and capacity.

When forecasting for some of our industry sub-component variables, however, using a variable's own history is often the most desirable method of analysis. Such single-variable analysis is called univariate modelling. We use the most common and versatile form of univariate models: the autoregressive moving average model (ARMA).

In some cases, ARMA techniques are inappropriate because there is insufficient historic data or data quality is poor. In such cases, we use either traditional decomposition methods or smoothing methods as a basis for analysis and forecasting.

BMI mainly uses OLS estimators and in order to avoid relying on subjective views and encourage the use of objective views, **BMI** uses a 'general-to-specific' method. **BMI** mainly mainly uses a linear model, but simple non-linear models, such as the log-linear model, are used when necessary. During periods of 'industry shock', for example poor weather conditions impeding agricultural output, dummy variables are used to determine the level of impact.

Effective forecasting depends on appropriately selected regression models. **BMI** selects the best model according to various different criteria and tests, including but not exclusive to:

- R^2 tests explanatory power; adjusted R^2 takes degree of freedom into account;
- Testing the directional movement and magnitude of coefficients;
- Hypothesis testing to ensure coefficients are significant (normally t-test and/or P-value);
- All results are assessed to alleviate issues related to auto-correlation and multi-collinearity.

BMI uses the selected best model to perform forecasting.

Human intervention plays a necessary and desirable role in all of **BMI**'s industry forecasting. Experience, expertise and knowledge of industry data and trends ensure that analysts spot structural breaks, anomalous data, turning points and seasonal features where a purely mechanical forecasting process would not.

Sector-Specific Methodology

A number of principal criteria drive our extrapolations and forecasts for each autos variable.

- **Production And Sales**

At a general level, we approach our forecasting from both a micro and a macro perspective, assessing the expansion plans of relevant multinationals/indigenous firms, while also taking account of the prevailing economic outlook. In this latter respect, our projections for macro variables such as industrial output, private consumption, government investment, monetary policy and GDP growth play a key role.

Figures for production are derived from a generic source (thereby ensuring maximum comparability between country data-sets), and include all vehicles with four wheels or more. For sales, we rely on data from government agencies and national automobile associations. Unless otherwise stated, sales numbers include domestically produced and imported vehicles, but not exports. The sector's contribution to GDP is projected by taking the US dollar production value as a proportion of nominal GDP, using our own macroeconomic and demographic forecasts.

- **Auto Imports And Exports**

These variables are mainly calculated at the micro level, using individual company reports. Changes in government policy, particularly with regard to tariffs and quotas, also have a significant bearing.

Sources

Aside from government departments and official company reports, we rely on the International Organization of Motor Vehicle Manufacturers (OICA), other established think tanks, institutes, and international and national news agencies.

Risk/Reward Index Methodology

BMI's Risk/Reward Index (RRI) provides a comparative regional ranking system evaluating the ease of doing business and the industry-specific opportunities and limitations for potential investors in a given market. The RRI system divides into two distinct areas.

Rewards

Evaluation of sector's size and growth potential in each state, and also broader industry/state characteristics that may inhibit its development. This is further broken down into two sub categories:

- Industry Rewards. This is an industry-specific category taking into account current industry size and growth forecasts, the openness of market to new entrants and foreign investors, to provide an overall score for potential returns for investors.
- Country Rewards. This is a country-specific category, and the score factors in favourable political and economic conditions for the industry.

Risks

Evaluation of industry-specific dangers and those emanating from a state's political/economic profile that call into question the likelihood of anticipated returns being realised over the assessed time period. This is further broken down into two sub categories:

- Industry Risks. This is an industry-specific category whose score covers potential operational risks to investors, regulatory issues inhibiting the industry, and the relative maturity of a market.
- Country Risks. This is a country-specific category in which political and economic instability, unfavourable legislation and a poor overall business environment are evaluated to provide an overall score.

We take a weighted average, combining industry and country risks, or industry and country rewards. These two results provide an overall Risk/Reward Index, which is used to create our regional ranking system for the risks and rewards of involvement in the autos industry in a particular country.

For each category and sub-category, each state is scored out of 100 (100 being the best), with the overall Risk/Reward Index a weighted average of the total score. As most of the countries and territories evaluated are considered by **BMI** to be 'emerging markets', our index is revised on a quarterly basis. This ensures that the score draws on the latest information and data across our broad range of sources, and the expertise of our analysts.

In constructing these ratings, the indicators in the table below have been used. Almost all indicators are objectively based. Given the number of indicators/datasets used, it would be inappropriate to give all sub-components equal weight. The weighting given is described in the table.

Table: Automotive Risk/Reward Index Indicators And Weighting Of Indicators

	Weighting, %
Rewards	70, of which
Industry Rewards	65, of which
Vehicle ownership, % of population	10
Total vehicle stock, mn	10
Total production	10
Production growth, five-year forecast average	10
Total vehicle sales	10
Sales growth, five-year forecast average	10
Country Rewards	35, of which
Urban/rural split	10
Rigidity of employment	10
Labour costs	10
GDP per capita, USD	10
Risks	30, of which
Industry Risks	50, of which
Regulatory environment	10
Competitive landscape	10
Country Risks	50, of which
Corruption	10
Bureaucracy	10
Market orientation - openness	10
Legal framework	10
Long-term monetary risks	10
Long-term external risks	10
Long-term financial risks	10
Long-term policy continuity	10

Source: BMI

