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Iran cuts oil prices as sanctions bite

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As international sanctions mount, Iran is finding it increasingly hard to find buyers for its oil, forcing the hardline nation to offer discounts in order to shift as much as it can to a declining number of customers.

Though Iranian officials are increasingly voicing their concerns in public, many seem optimistic about finding ways around the trade blockade.

The latest set of sanctions approved by the United Nations Security Council on June 9 includes restrictions on banking and other financial transactions that could further Iran's nuclear ambitions.

The UN measures came eight days after United States President Barack Obama signed off on legislation imposing new unilateral sanctions, which will penalize companies and banks dealing with Iran and block sales of petrol and other petroleum products to the country. Iran lacks an adequate refining capacity despite being a major oil producer.

The sanctions effectively increase the risk of buying oil from Iran.

"It's unfair competition," Hossein Noghrekar Shirazi, the deputy oil minister responsible for trade and international links, said when he was interviewed by the Khabar newspaper following the approval of the latest UN sanctions.

The result of the growing number of restrictions on trade is that long-term customers like India, China and Japan are now looking elsewhere for oil suppliers, such as Saudi Arabia.

For a country in which over 85% of trade revenues are generated by oil, this tougher export environment is a big threat.

Iran has responded by offering customers bigger discounts on crude sales.

There are no precise figures, but the discounts are believed to be running at between US$3 and $7 per barrel. It also depends on the market - prices listed in the Oil Ministry's daily bulletin show that the remaining few European customers buying Iranian crude are paying at least $3 less than those in Asia.

According to Akbar Torkan, formerly a senior Oil Ministry official now at Iran's Center for Strategic Studies, "Our current concern is selling oil, not the price."

Tehran is actively looking for new customers. In mid-June, Iran's ambassador in Minsk said his country was prepared to sell oil to Belarus.

Hojatollah Ghanimifard, who is deputy-managing director of the National Iranian Oil Company and is responsible for investment and development, says marketing tactics have changed so that prospective buyers are offered one-off deliveries. If customers are satisfied, the Iranians will seek to conclude long-term contracts with them.

The difficulties do not stop with finding customers and retaining their loyalty. According to deputy minister Shirazi, the international banking restrictions mean that sales contracts are now concluded without opening letters of credit.

International insurers are also less prepared to provide cover for shipments from Iran, so these costs have gone up. Finally, the new Security Council sanctions will make it harder to ship oil and transfer the proceeds back to Iran.

Thus, at a time when Iran has to charge customers less, the costs of getting the oil to market are mounting. In the past, Iran sold its crude to credible oil companies, refineries or well-known businessmen. These days, middlemen are playing a much greater role.

"Sometimes even old customers prefer to use trade intermediaries to purchase Iranian oil," said an inside source in the Oil Ministry. "They lease oil tankers at random and ship the oil from Iranian ports covertly."

A member of the Iranian Association for Energy Economics, who did not want to be named, said, "It's quite clear. When reputable firms refuse to buy, sales will definitely go to less-credible customers. The government has also taken advice on using Iranian intermediary firms in its efforts to sell oil as fast as possible."

Shirazi recognizes that the economics of exporting under present conditions are less than advantageous but says Iran has few alternatives to the tactics it is forced to employ to sell its oil.

"If we look at it from the point of view of politics and security, it is the best and most logical approach we could have adopted," he said in the newspaper interview.

The lack of customers has dented crude oil production, which has already been hit by worn-out extraction equipment and falling oil well pressure.

Ahmad Ghalehbani, managing director of the national oil company, said recently that daily production stood at 3.9 million barrels per day. That figure is 100,000 barrels higher than permitted under its quota as an Organization of Petroluem Exporting Countries member.

However, insider sources in the Oil Ministry say daily production since the beginning of 2010 has averaged less than 3.6 million barrels a day. Subtracting 1.7 million barrels for domestic consumption, that leaves a mere 1.9 million barrels a day for export.

Even if we take the higher figure cited by Ghalehbani, the implication is that current production levels are some 300,000 barrels a day lower than last year, when daily export levels averaged 2.5 million barrels.
As Iran struggles to balance the books, one has to ask what would happen if even tougher sanctions made it still harder to export oil. Emad Hosseini, spokesman for the Iranian parliament's energy affairs committee, seems unconcerned at the prospect.

He believes there is still room to drop prices to levels where Iran can attract more customers and remain competitive on the international market. It is a formula he calls "Iranian oil diplomacy".