

MIDDLE EAST

Iran-Turkey Partnership: Energy, Trade, and Sanctions Evasion

AUGUST 28, 2024

Iran-Turkish relations undermine U.S. foreign policy objectives in the Middle East. Turkey and Iran have mutually beneficial ties despite their regional rivalries and competition. Their partnership encompasses three objectives: [energy security](#), [international trade](#), and [sanctions evasion](#). In 1934, the Shah of Iran and the Turkish President met to discuss an economic and trade partnership that is still in effect. Iran and Turkey's partnership is more complicated than its mutual benefits; each country uses the other to help their foreign policy and trade goals elsewhere, such as the European Union (EU), Russia, the United States, and the Arab kingdoms. Iran has abundant natural resources and goods that Turkey seeks to import.

Turkey is a primary exporter of manufactured goods for Iran and is used as a trade route for Iranian goods to Europe. Due to Iran's isolation from the outside world, including the United Nations, Iran's economy is in desperate shape. The United States government has campaigned against Iran since the 1979 Islamic Revolution using economic sanctions and multilateralism to isolate its geopolitical influence and limit its regional threats against Israel and other U.S. allies in the Middle East, such as the Arab nations.

The campaign against Iran hinders economic relations between the two countries. Iran needs Turkey because not many large and developing economies are willing to trade with Iran due to financial repercussions and international banking law. Turkey is the bridge between the EU and the Middle East, Central Asia, and the Indo-Pacific. The EU needs Turkey for most of its Asian market imports, including energy and goods, especially since the sanctions placed on Russia for the invasion of Ukraine, plus all of the resources and goods that flow through Turkey from Asia. Turkey's economic growth has been slow due to currency issues. Since Turkey is a NATO

ally, the United States gave Turkey waivers so it could import oil and gas from [Iran to minimize damage](#). The United States and the United Nations sanction many Iranian entities. Turkish entities that wish to engage in transactions with these sanctioned entities prohibit Turkey from engaging with them legally, resulting in these entities evading U.S. sanctions. And risk legal repercussions.

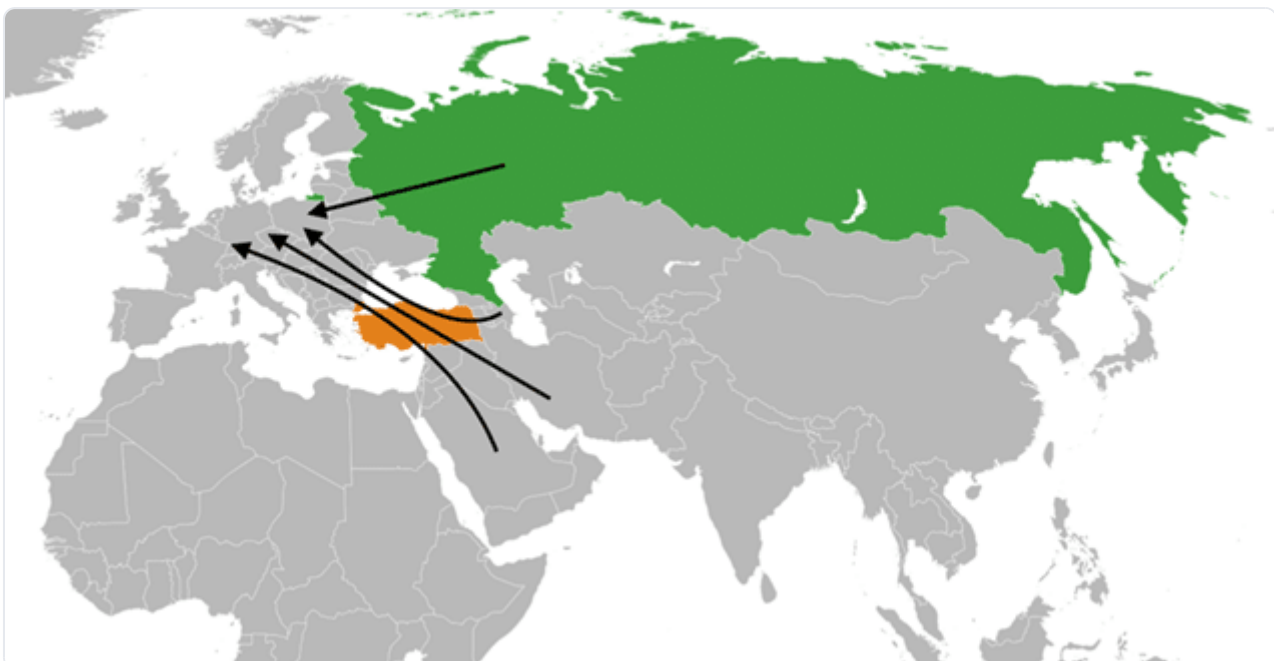
Energy and Trade:

Russia and Turkey historically competed as primary land routes that businesses and merchants would use to ship goods from Asia to Europe. With Russia causing war and geopolitical tension in Eastern Europe, Turkey is the primary bridge between the West and the East. Iran is a crucial player for East Asian merchants because it connects Central and South Asia with the Middle East. Besides using Iran as a transit route, trade routes through Central Asia and the Caucasus or the Arabian Peninsula and Israel are two more land routes merchants can use to ship their goods (maritime trade is irrelevant in this scenario because all maritime trade transpires from Asia to Europe through the Suez Canal or the Cape of Good Hope). The maps below show the potential trade routes countries could use to transport goods. In the top map, the arrows start in East Asia, the Middle East, or in Russia and end in Europe. Countries in East Asia, the Middle East, and Russia are producers, while European countries are consumers, so goods while flow from east to west. The bottom map shows the different routes for oil and gas pipelines heading to Europe. Due to georpgraphy and geopolitics, Turkey is the main transit route for most petroleum to European markets.

Turkey and Russia's strategic geographical location for international trade



Oil and natural gas pipelines from Asia to Europe



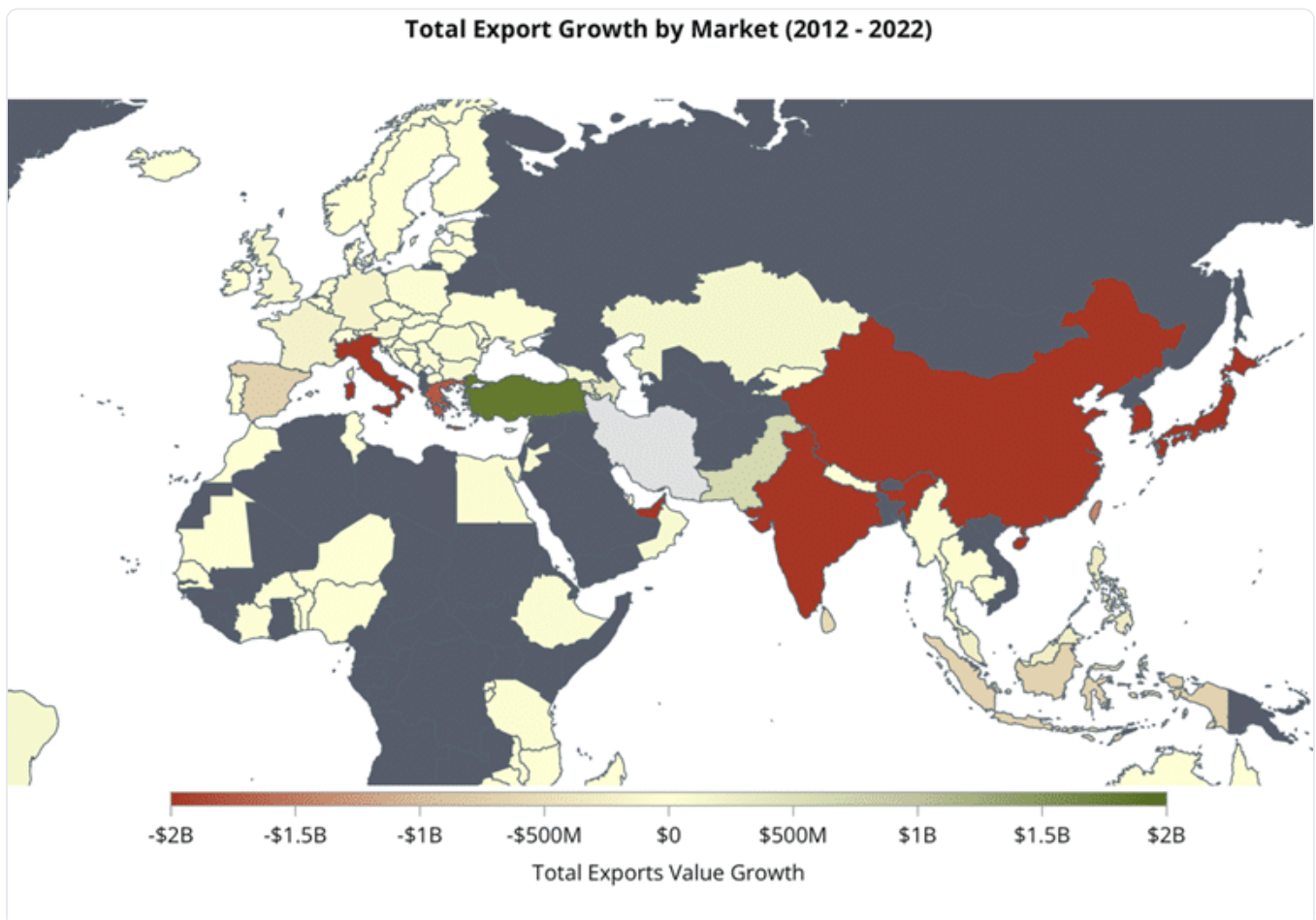
Turkey currently relies on the U.S., Azerbaijan, and North Africa for petroleum gas and Kazakhstan and Nigeria for crude petroleum to supplement its domestic needs. Iran exports

99% of its crude oil to [China](#), and most of its petroleum gas exports go to Pakistan, Armenia, and India. Turkey imports roughly [\\$30 billion](#) of petroleum, and Iran relies solely on a few countries for energy revenue. Turkey has identified Iran's market as a strategic necessity to diversify its energy imports and increase [energy security](#), while Iran seeks Turkey as a primary importer of its energy resources.

Due to the Russian invasion of Ukraine, the EU and the UN placed severe economic sanctions on Russia. In response, EU consumers are seeking to supplement the trade losses from Russia with imports from manufacturers and producers from the Middle East and Asia. Turkey, in this context, is actively seeking to supplement Russia and become the primary transit energy route to Europe. This strategic move not only aims to connect the Middle East and Central Asia gas and oil producers with European consumers but also holds the potential to reshape the energy trade dynamics in the region, offering new opportunities for all involved.

Though the sanctions regimes in place against Iran disincentive Turkey from dealing with Iranian entities, Turkey seeks to expand its energy and trade footprint in Central Asia as another means to diversify its imports because Iran's economy and political situation are unstable. Iran is barely a natural gas supplier to Turkey, with only \$13 million in exports compared to Russia as the primary source of [crude oil](#), with \$6.5 billion in exports to Turkey. Turkish gas imports [declined](#) from 21 percent in 2010 to 15.61 percent in 2018 because Turkey [diversified oil and gas](#) from mainly the Middle East to now including the United States, Europe, and Asia. Iran and Turkey's international trade is tiny compared to other large economies, but as the map below shows, from 2012-2022, Iran's exports to Turkey increased by 133%. Iran's closest economic partner is Turkey (Iran's second largest exporting country is Pakistan, which accounts for about a third as much international trade).

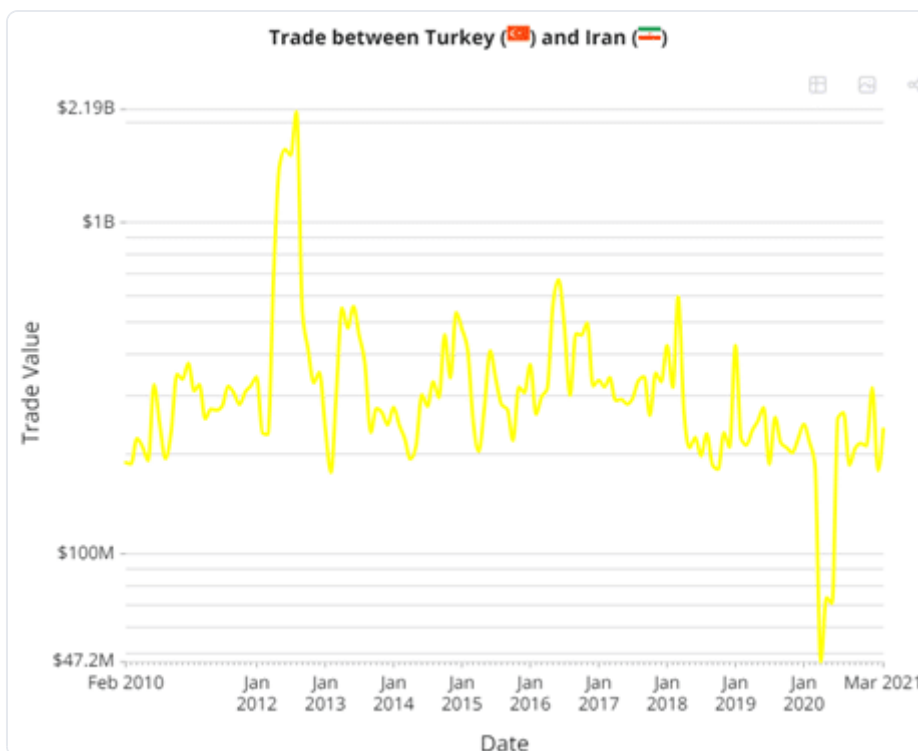
Iran's exporting destinations



Iran and Turkey have mutual economic objectives. As a result, the two countries hold the [Iran-Turkey Joint Economic Cooperation Committee](#) to increase bilateral trade and diplomacy. Iran and Turkey started negotiating plans to build a new pipeline between the two countries. There used to be the Tabriz-Ankara pipeline constructed in [1996](#), but due to terrorist attacks and acts of God, such as severe storms, the National Iranian Oil Company decommissioned the pipeline in 2008. [Turkey](#) imports most of their gas and oil from Algeria, Qatar, and the United States, so Turkey demands fair and competitive prices with Iran.

Iran has a limited economic output due to international isolation, and Turkey's economy has increasing inflation rates and a weakening currency (lira). Iran and Turkey plan to increase international trade and bilateral economic ties. Iran's sizable population makes it an essential market for non-oil exports to Turkey. Investors in Iran also make significant investments in Turkey's [real estate sector](#)—the increase in trade from 2021 to 2022 results from trade

normalizing between [Turkey and Iran](#) after [COVID-19](#). As shown in the graph, the pandemic is the main reason for a decrease in trade from \$200 million to \$47.2 million in 2020. Turkish President Erdoğan stated that sanctions and COVID-19 are the main issues that have caused the decreased trade volumes with Iran. After [trade normalized](#), the Turkish Institute of Statistics reported around a 20% increase in exports to Iran in 2022 compared to 2021 and a 49% increase in non-oil and gas imports from Iran in 2022 compared to 2021.



Erdoğan stressed the crucial role of a preferential trade agreement between [Iran and Turkey](#) in boosting trade. This agreement, to which both countries are committed, addresses critical issues such as fuel prices and [airline frequency limits](#). The economic growth of both Turkey and Iran is a top priority, and their geographical proximity is leveraged for mutual benefit. Both countries strategically use this partnership for economic development: Turkey primarily uses Iran as a resource supplier and a means to diversify its energy imports, while Iran sees Turkey as a key player in boosting its trade balance and as a gateway to [European markets](#).

Sanctions Evasion:

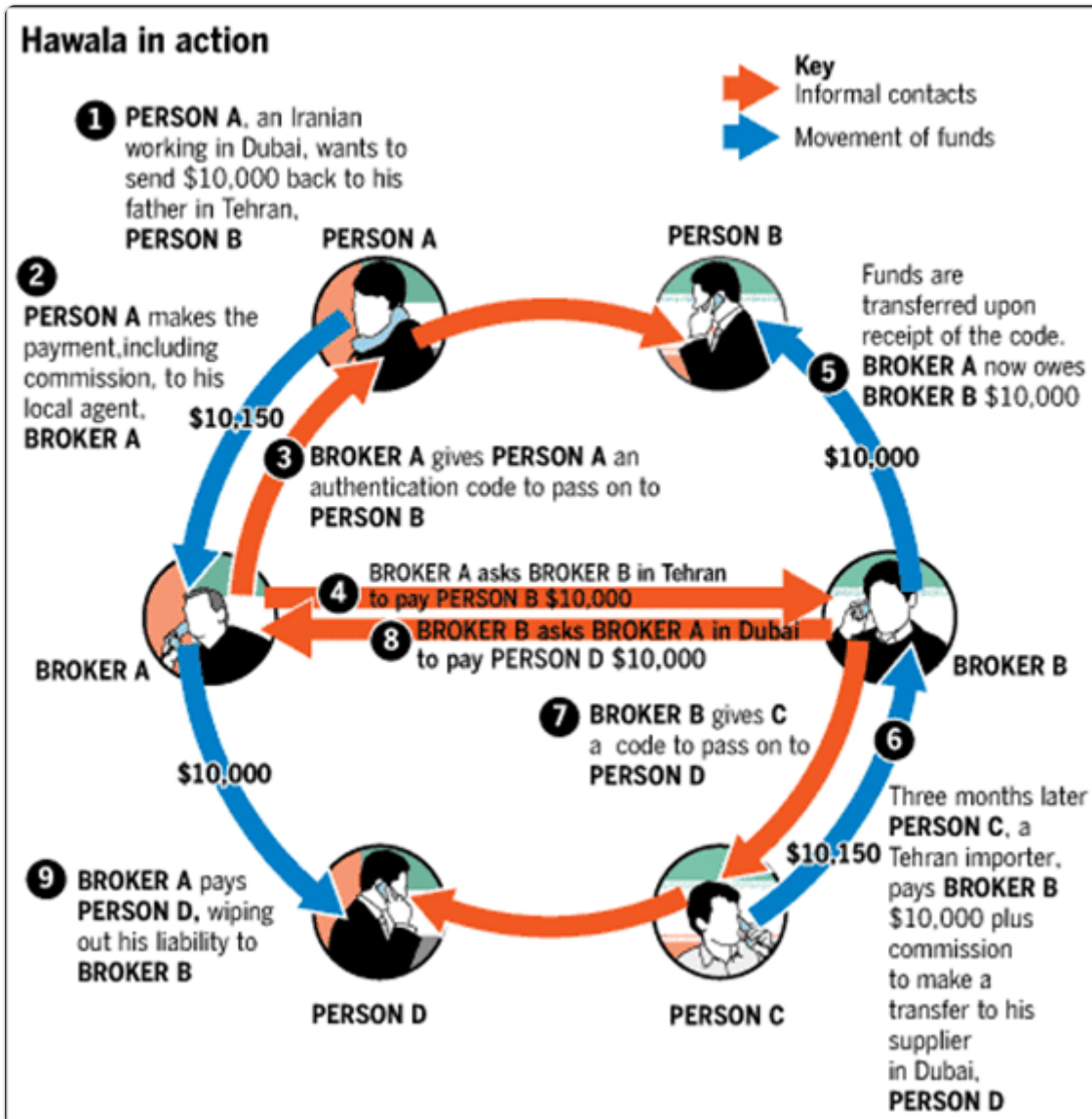
The United Nations and the United States imposed multiple extensive sanction programs on Iran. In 2010, former President Obama signed the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA). [CISADA](#) strengthened U.S. sanctions on Iran's energy sector and increased penalties for foreign financial institutions if they violated sanction prohibitions on Iran. In 2018, after former President Donald Trump withdrew from the Joint Comprehensive Plan of Action ([JCPOA](#)), the United States reinstated a complex series of sanctions on Iran. Initially, these sanctions regimes targeted Iran's ballistic missile and nuclear weapons programs but later included Iran's energy sector and natural resources. Withdrawing from the JCPOA supported [U.S. foreign policy goals](#) by negatively affecting Iran's economic growth, terrorist financing, and defense industry. Due to the damaging effect of the sanctions on Iran's economy, Iran fostered multifaceted sanctions evasion networks with entities worldwide, including foreign governments, companies, and individuals. Iran developed a variety of [illicit financial systems](#) and methods to fund and support its defense and foreign policy objectives, such as financing terrorist organizations (Hamas, [Hezbollah](#), and the Houthis), supporting the Assad regime in Syria, and increasing ballistic missile and nuclear weapons development. Turkey has no sanctions directly placed on them; the [Countering America's Adversaries through Sanctions Act](#) is placed on Russia but indirectly applies to Turkey because of air defense purchases in 2019, which is irrelevant to Iran's sanctions evasion.

Any entity not using the U.S. financial institution or the U.S. dollar can evade U.S. sanctions. Most sanctions evasion schemes between Iran and Turkey do not involve the U.S. financial institution or the U.S. dollar. For example, these two countries' entities evade sanctions through shell companies, hawala, swaps, illicit gold transactions, and other hard currency transfers. Iran and Turkey share a border of over 300 miles. Entities within both countries can travel to each other's country and conduct business unofficially. These parties conduct illegal transactions with ease.

Firstly, hawala "is an [informal method of transferring money](#) without any physical money actually moving. It is a method that takes place outside of the traditional banking system. Unlike the conventional method of transferring money across borders through bank wire

transfers, hawala dealers transfer money to other hawala dealers within their network. Hawala dealers keep an informal journal to record all credit and debit transactions on their accounts. Cash, property, or services are forms of settled debt between hawala dealers. The hawala network excommunicates a hawaladar who doesn't keep their end of the deal in the implied contractual system.”^[1] Hawala is challenging to track because it is usually anonymous and does not leave a paper trail. Some of the [largest hawala centers](#) outside of Iran are in the UAE and Turkey. Iran receives most of its goods from Europe, the U.S., and Asia from Iranian hawala dealers in other countries. So, merchants and businesses that send goods to Turkey do not know whether Iran will import these products.

An example of the [hawala process](#)



Secondly, criminal entities within Iran and Turkey use [gold](#), hard currency like cash, and swaps (oil or rugs) to evade sanctions. The Financial Action Task Force and the U.S. financial enforcement systems struggle to combat illicit gold or hard currency transfers used for illicit financing. A high volume of gold purchases indicates an illicit gold transaction between Iran and other countries close to [Turkey](#). The serial numbers of U.S. dollars are complicated to track even if used through a reputable bank. Swaps of goods, such as oil or foodstuffs, cannot be tracked as well. Entities will use these forms of payments as collateral to traditional payments with money. Iran and Turkey share a border of over 300 miles. Driving or flying these physical payments over the border to the respective parties is nearly impossible to track.

Thirdly, the use of [shell companies](#) by Iranian and Turkish entities for illicit transactions, money laundering, and sanctions evasion is a cause for concern. Shell companies, essentially fake entities with only a name attached to them, are being used as fronts for money laundering schemes. Iranian and Turkish entities have established shell companies in either country to bypass U.S. sanctions. When used strategically, these shell companies can exploit the U.S. financial system by posing as companies in industries that the U.S. has waived, such as the [airline](#) or [maritime](#) sector. Iran and Turkey have been found to use shell companies that appear to be software for the internet or communications, certain food businesses, and the [medical industry](#). For instance, in 2018, the Department of Treasury designated Turkish shell companies that had acquired U.S. parts for Iranian commercial airlines.

Iran and Turkey stand to benefit from their partnership. Turkish relations undermine U.S. foreign policy objectives in the Middle East. Iran and Turkey's economic hardships encourage stronger relations to promote energy security, international trade, and sanctions evasion. Due to Iran's isolation from multilateral organizations and an abundant amount of countries around the world, Turkey has a lot to lose diplomatically, economically, and strategically from its relations with sanctioned entities in Iran and the government itself. With Turkish President Erdoğan continually pushing his boundaries with his allies in NATO and the United States between Russia and Iran, Erdoğan might push Turkey into isolation due to a lack of trust and cooperation. Turkey's geography is the primary reason the West seeks to continue its alliance and waives much of Turkey's disruptive behavior. The EU needs Turkey for most of its Asian market imports, especially since the sanctions placed on Russia for the invasion of Ukraine, plus all of the resources and goods that flow through Turkey from Asia. Erdoğan's ambition to regain Turkey's strategic power will guide his foreign policy over the current world order, and we can expect Turkish entities to continue to engage with sanctioned Iranian entities.

Since the Islamic Revolution in 1979, the United States and most of the international community ostracized Iran from the world stage and sanctioned Iran's economy. Iran's economy and defense industry struggle with the current international restrictions. Iran looks to anyone who wants to partner with them. Iran's closest and most significant economic partner is Turkey due to historic relations since the 1930s, geography, and similar foreign policy goals.

Iran's dependence on Turkey for exports and energy security will continue to have a substantial stake in Iran's policy toward Turkey and their partnership will balance their competing interests in the region.

[1] The reason why I quoted the entire paragraph is because the economists at Investopedia described hawala in the most simplest form that is easily understood; paraphrasing would only take away from the reader.

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