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Dealing with Iran: Finally, a Stick

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LONDON—In the carrot-and-stick world of international diplomacy, Iran and its controversial nuclear program seem impervious to both.

The theocrats of Tehran have dismissed every economic and trade carrot that Europe has dangled before them. And knowing that the stick of a U.S. or Israeli military strike against its nuclear facilities would rally Iranians behind their discredited regime, hardliners like President Mahmoud Ahmadinejad practically invite an attack.

So even as American and Iranian officials meet again in Baghdad to address their deepening proxy war in Iraq, Tehran refuses to halt its controversial nuclear activities and Washington refuses any direct nuclear talks until it does.

"There's really nothing the Iranians want from us," explained Secretary of Defense Robert Gates earlier this year. "We need some leverage, it seems to me, before we engage the Iranians."

Recent months, however, reveal that the West does have an economic stick that could yet change Tehran's calculations. Despite widespread portrayals of Iran Rising—its historic rivals the Taliban and Saddam Hussein ousted, Tehran bolstered by record oil prices and Iranian allies ascendant from Iraq to Lebanon to Gaza—today's Islamic Republic is actually Iran Slipping.

Unemployment and inflation are soaring, and oil production, which generates more than 80 percent of export revenues, is steadily dropping due to decades of neglected infrastructure. Recent riots that followed gasoline rationing may be a sign of bigger troubles to come.

But while average Iranians suffer, nearly three decades of unilateral U.S. trade sanctions have ironically perpetuated the mullah's grip on power by helping prop up the business monopolies of key pillars of the regime—the conservative *bazaari* merchant class and the brutal Revolutionary Guards. Through *bonyads*, corrupt Islamic "charities," Tehran's klepto-clerics control the vast majority of the Iranian economy.

Now, the U.S. may have found a way to exploit Iran's economic Achilles heel by hitting the regime where it hurts—the wallet. Alongside recent UN resolutions freezing the assets of Iranian organizations and individuals involved in the country's nuclear and missile programs, Washington has launched a full-scale financial assault on the mullahs. Since last year, the Bush administration has blacklisted two

major state-owned Iranian banks and warned foreign governments and financial institutions against doing business with Tehran.

"As a result, the Iranians are beginning to feel that pinch," according to Under Secretary of State Nicholas Burns. Fearing a third round of UN sanctions, the regime is reportedly withdrawing millions of dollars from European banks. France, Germany, Italy and Japan have reduced export credits and lending to Tehran.

Dozens of financial institutions, many in Europe and Asia, have either halted or curbed their business with Iran. Companies like British Gas, Japan's Inpex Holdings and South Africa's Sasol have abandoned billions of dollars in energy projects.

A growing movement in the U.S. aims to tighten the financial screws on Tehran even further. Modeled after the 1980s anti-apartheid divestment campaign against South Africa, the effort aims to force the \$1 trillion pension-fund industry to divest from multinational corporations with business in Iran. In particular, divestment advocates hope to deprive Tehran of the nearly \$100 billion it needs to modernize its oil and gas infrastructure and keep its petrodollars flowing.

Some public employee pension funds—in Missouri, Florida and Ohio—are already divesting from hundreds of foreign firms, including energy giants with Iranian operations such as Royal Dutch-Shell, France's Total, Russia's Gazprom and Malaysia's Petronas. More than a dozen other states—including California and Texas—may follow suit.

It's not certain that divestment will persuade these firms to end lucrative deals with oil-rich Iran. Moreover, divestment is opposed by the Bush administration, which argues that targeting foreign firms risks undermining the fragile international coalition against Iran.

Still, after years of fruitless diplomatic engagement with the Islamic Republic over its nuclear ambitions, targeted financial sanctions and divestment offer a road not yet traveled.

Until now, Tehran's theocrats have thumbed their nose at the world, knowing their petrodollars have been beyond reach. Depriving the mullahs of their money could change that old assumption and maybe, just maybe, force them to rethink their nuclear calculations.