



INDIA'S IRAN CONUNDRUM

A LITMUS TEST FOR
INDIA'S FOREIGN POLICY

A Report



ASPEN INSTITUTE INDIA

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Aspen Institute India promotes values-based leadership, open dialogue and cross-sector outreach by engaging the civil society, government, private sector, and other key stakeholders on issues related to India's development. It invites industrial, economic, financial, political, social and cultural leaders to discuss these issues in settings that encourage frank and open dialogue.

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Foreword

As part of Aspen Institute India's efforts to focus on India's relations with other countries, we brought together a group of eminent persons, under the Chairmanship of Ambassador Naresh Chandra to a Round Table on 8th June, 2012 to discuss India-Iran relations and strategy, specifically in the context of the recent US sanctions.

With the third round of negotiations between the Islamic Republic of Iran and the UN Security Council members and Germany reaching an impasse, it is evident that Iran will come under increasing spotlight. In light of these developments, it is inevitable that we need to take stock of India's foreign policy on Iran.

This document is a non-consensus summary of the principal points which emerged from the Round Table. We believe that action is needed on many fronts: by the Government, private sector, the public sector. We also

feel that think tanks should engage in a continued dialogue to keep this issue in focus. However, this is not going to be an easy task as there are a number of key players involved particularly the United States. The recent India-US Track II Dialogue sponsored by the Aspen Institute, India dealt at great length with the complexity of India-US relations with regard to Iran. It is for this reason that the Aspen Institute was encouraged to hold the Round Table. It will test the limits of India's diplomatic initiatives. As a country, it is imperative that India has a framework and strategy for what should and should not be done.

Aspen India is grateful to Ambassador Rajendra Abhyankar for preparing the background paper and trusts that this document will be a contribution to the literature on this subject and to policy formulation by government and industry.

India's Iran Conundrum:

A Litmus Test *for* India's Foreign Policy

Introduction

With the third round of negotiations between the Islamic Republic of Iran and the UN Security Council members and Germany reaching an impasse, it is becoming increasingly evident that Iran will be subject to stricter sanctions in the coming weeks. In light of these developments, it is inevitable that India's position on Iran and its foreign policy underpinnings could be seriously challenged. At the same time, Indian aspirations for a stronger bilateral relationship with the United States must be leveraged against the economic realities at home – a less than optimistic growth forecast and India's spiraling energy demands; all of which necessitate the continuation of bilateral ties with Iran.

Relations between India and the US have steadily deepened in recent years, with the civil nuclear agreement marking a watershed in bilateral ties between the two countries. However, with India taking positions at variance with the US in the UN Security Council on Libya and then Syria, and its difficulty to cap oil imports from Iran beyond a point, the euphoria on Indo-US relations seems to have dulled. Secretary of State Hillary Clinton arrived in India in May 2012 hoping to impress on the government the need to diversify its oil imports and reduce its dependence on Iranian oil. India, which imports approximately 80% of its oil, continues to import around 11% crude oil requirements from Iran despite some reductions.

The present state of affairs highlights the realpolitik of the situation, with the US, India and China all trying to manage their own national interests without disrupting the balance of relations. A pro-Iran posi-

tion would seriously jeopardize the mutually beneficial relationship that India holds with the US and Israel. Close ties with these two nations has allowed India to be not only the beneficiary of defense technology transfers and intelligence sharing, but has also provided India with necessary bipartisan support in Washington political circles. The subsequent US decision to exempt India from the oil embargo against Iran provides some much needed breathing space; India must now adjust its strategy and ensure that it meets the national interest without compromising relations with the US, and West Asia.

The triangulation of relations between a Shia Iran, a Sunni GCC and India further complicates India's position in the region. Dealings between Iran and a GCC backed Saudi Arabia have always been marked by rivalry and competition. The situation is further threatened by renewed violence stemming from Syria which threatens to spillover in the region. Ideological rivalry aside, Iran and the GCC continue to clash over territorial disputes. Iranian occupation of the three islands – Abu Musa, Greater Tunb and Lesser Tunb – is a major source of contention between the GCC countries and Iran. Furthermore, Iran's nuclear program will result in an unstable bipolar competition with Saudi Arabia which has stated that should Iran acquire nuclear weapons it will have no choice but to do the same. For India, its relationship with the GCC represents varied economic and strategic interests in the region. The GCC accounts for over two thirds of India's oil imports and is also a huge importer of In-



dian manufactured goods. Additionally, with over 6 million Indians working in the Gulf region and sending considerable remittances back home, any conflict between the GCC and Iran will have grave immediate and medium-term consequences for the Indian government.

Keeping these realities in mind, international developments surrounding Iran pose a number of challenges for India. Firstly, India is heavily dependent on Iranian crude oil. Many of the Indian oil refineries are configured in a manner to process only heavy crude oil of which Iran is a major supplier; and since there are not any substitute volumes readily available in the global market, India's dependence on Iranian crude shall remain for the near future. This is a problem that India does not face alone, China and various EU countries are facing similar hurdles. While there might be added costs involved in diversifying oil imports, the strategic benefit that we will gain from maintaining current sources will not be enough to balance the additional diplomatic costs that India will incur by continuing to import oil from Iran. Secondly, Indian considerations in Afghanistan lend strategic significance to our relationship with Iran. The US withdrawal from Afghanistan in 2014 will provide the Taliban and Pakistan with an opportunity to once again establish a foothold in the country and under-

mine Indian influence. Having already invested large sums of money in Afghanistan's development program and with huge stakes in several infrastructure and financial projects, India must protect its assets in the region. Since access to Afghanistan and Central Asia through Pakistan is not an option, India has helped finance the Chabahar port in Southeastern Iran so that it can remain connected to Afghanistan. In order to enhance trade with Afghanistan and retain its influence there beyond 2014, India must rely on Iran's cooperation.

It has been argued by some that India is not doing enough to cooperate with the US in light of its global strategic partnership. Provided Saudi Arabia agrees to meet the shortfall in demand for India's oil imports and if both the US and India agree that it is imperative that Iran does not acquire nuclear weapons, then what is staying India's hand and preventing it from going along with the US? The key policy determinant that can be discerned from India's reaction to the Iran issue is "strategic autonomy". A relic of Nehru's legacy, this term has acquired a talismanic status among policy makers and is critical to how India as an emerging global power wants to engage with the international system. While it is crucial that India maintains a sufficient degree of autonomy in its strategic endeavors, a policy of strategic autonomy necessitates autonomous and impartial foreign policy decision making. It is as yet unclear whether India's increasingly assertive position on Iran had to do with the Uttar Pradesh elections and its large Muslim population or strategic autonomy. Is it truly possible for India to maintain a strict policy of strategic autonomy within an interconnected and globalized environment? Clearly, India is in a difficult position wherein it has to balance increasingly diverse foreign policy interests that often conflict with one another, and it is becoming progressively difficult for New Delhi to continue walking the diplomatic tightrope without setting back its relations with one or other of its partners.

Another hurdle involves payment to Iran for its oil. Iran has agreed to allow India to pay for 45% of its imports in Indian rupees. This payment would be used by Iran to purchase Indian goods directly. While wheat has been identified as a potential export item, problems abound on this front as well. Iran had stopped importing wheat from India because of a fungus that was found in Indian wheat. A team of Iranian scientists visited India and have taken back samples of wheat to test. Once this is cleared, Iran will be able to resume its wheat purchases.

The precarious nature of India's energy security, exemplified by its reliance on Iran despite the logistical challenges, has put a spotlight on the TAPI (Trans-Afghanistan Pipeline) project, a project that allows India to acquire natural gas from Central Asia. The TAPI project, expected to be operational by 2018, has progressed considerably after India and Turkmenistan signed a sales agreement in May this year, paving the way for the actual development of the pipeline. While this is a welcome development, investors are still wary of investing in a pipeline that passes through Afghanistan and other unstable areas. India is expected to receive only 38 million cubic meters of natural gas while its demand is projected to go up to 473 million cubic meters. This pipeline will change the dynamics of the region as it brings together India and Pakistan on a common pursuit and inserts Indian interests further into the Central Asian region. At the same time, the pipeline also pits together China and India in their quest for energy. China considers Central Asia to be a key supplier of energy reserves. Turkmenistan will be in a difficult position to honor commitments if its gas fields do not yield the expected amount of gas.

The Iran sanctions and developments of the TAPI project have raised questions on the viability of the Iran Pakistan India (IPI) pipeline. This pipeline would transfer gas from Iran's South Pars fields in the Persian

Gulf to India via Pakistan.

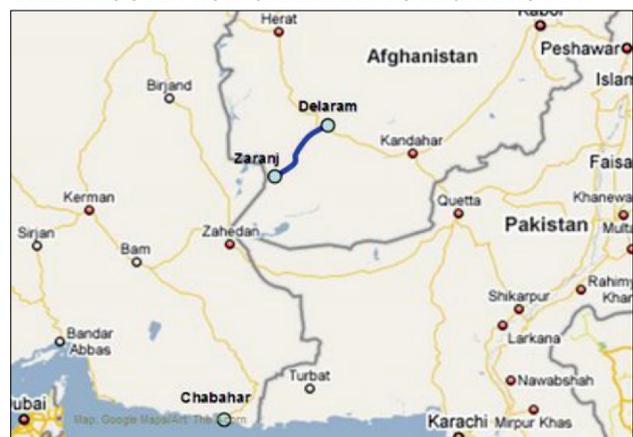
As India takes a closer look at its energy needs, it is expanding its relations with Gulf countries and other resource rich states. India's balancing act of pursuing its own interests while respecting sensitivities of strategic partners like the United States will determine the trajectory of India's energy supplies and relations with its Central Asian neighbours.

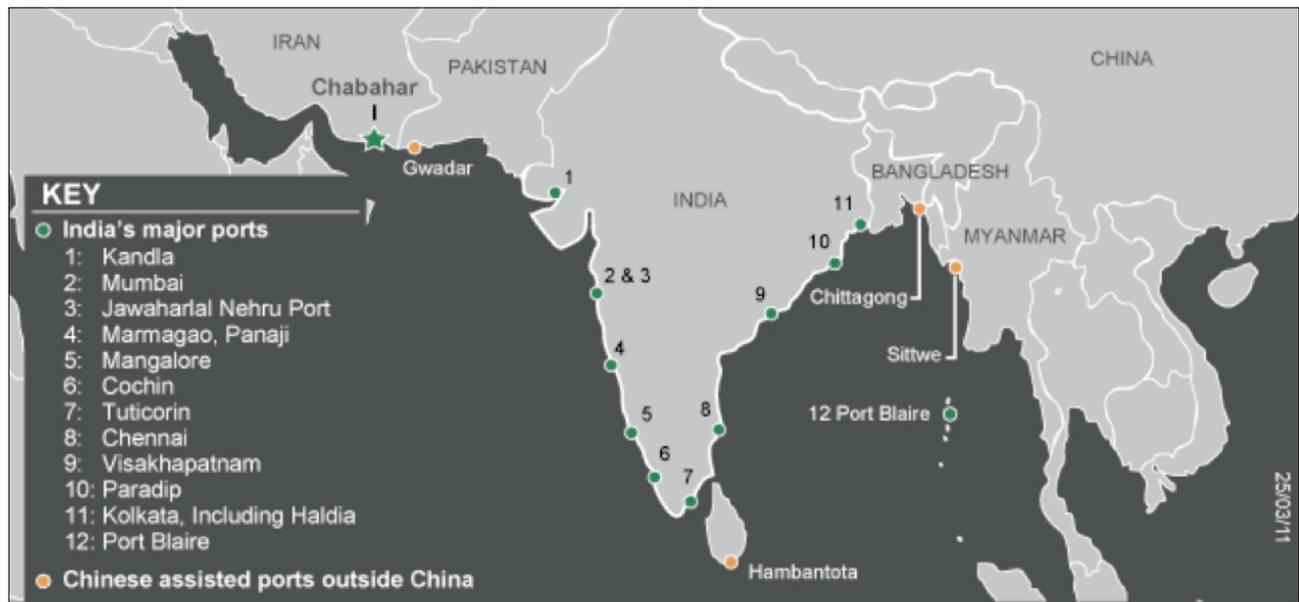
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Chabahar: Key to Afghanistan and Beyond

On 28th June 2012, the Indian government hosted the Delhi Investment Summit on Afghanistan. The basic goal of the summit was to encourage foreign direct investment into Afghanistan and invite the private sector to play a greater role in developing the war torn country. Thus far, Indian investments in Afghanistan have been largely PSU (Public Sector Undertaking) driven. The Indian government is increasingly looking at avenues through which it can promote private sector participation in Afghanistan. While this summit has won strong approval from the Afghan government it is

TRADE ROUTE FROM CHABAHAR TO AFGHANISTAN





TWIN PORTS OF CHABAHAR AND GWADAR

entirely an Indian initiative and is indicative of India's ambitions for (and in) Afghanistan.

In order for India to develop its interests and profit from the investments that it has made in mineral rich Afghanistan, it is crucial that India has land access to the region to conveniently transport goods to and from the country. Cognizant of Pakistan's belligerent attitude and coupled with the requirement for an alternate route into Afghanistan through which it could independently conduct trade, India helped finance the Chabahar port in Iran.

The Chabahar port, Iran's closest and best access point to the Indian Ocean, will significantly reduce Afghanistan's trade related problems and will likely boost trade relations with India. Indeed, the port has already been used by India to transport 100,000 metric tons of wheat to Afghanistan as part of its humanitarian assistance program.

With the Chabahar region being assigned a free trade zone status, its importance for international trade has significantly increased. India proposes to exploit this situation and has already reached an agreement with Iran and Afghanistan which will allow Indian goods heading

for Afghanistan and Central Asia to obtain preferential treatment and tariff reductions at the port of Chabahar. As New Delhi examines various ways and means to step up trade with Iran amidst growing difficulty in transferring of funds for oil imports, Chabahar represents massive potential for Indian products and commodities. India has already constructed a 230 km road from Zaranj to Dilaram in Afghanistan's Nimroz province which will connect to the Chabahar port via Milak. Serious negotiations are also underway with Iran to build a 900 km highway between Chabahar and Zahedan which will provide India access to the Hajigak mines where it has recently won a bid (under Steel Authority of India) for exploitation of the 1.8-million tone Hajigak iron ore mine in Bamiyan province. With pressure from US sanctions increasing and very limited room to handle trade and oil imports, the Chabahar project will ease pressure on both India and Iran and boost India's trade and strategic presence in Central Asia.

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Recommendations for an Emerging Landscape

- India's Middle East policy will have to come to grips with the changing balance of power caused by an increasingly assertive Iran and weakened Gulf Arab regimes. Stepping up India's engagement with the Arab Gulf will require dedicated political effort to assiduously pursue India's strategic interest in the region. India's policy will have to create the economic space for our trade and industry to increase its profile in the Gulf and foster inward and *in situ* projects based on their hydrocarbon and financial resources and India's skills and market.
- India must pursue its interests in the region while displaying sensitivity to American concerns. Independent decision-making is a key element of a strategic partnership. In the long term, a far more consequential scenario will remain a conflict between Iran and Saudi Arabia. India will need to pay attention to all of the dimensions of the possible conflict going beyond its Shiite-Sunni characterization.
- India will continue to rely on Iranian oil imports. Even if India is able to upgrade the technology of the refineries to suit oil imports from other countries, high sulfur crude from Iran and Iraq will remain a part of our product mix. India will have to assess the extent to which it should diversify its energy imports portfolio. India has increased oil imports from Iraq but it is still not back up to the levels of 1990 when it comprised of 50% of India's requirements. Facilitation for the private sector to import oil supplies from other suppliers like Venezuela should be considered. It is suggested that Ministry of Commerce appoint a group comprising the public oil marketing companies, private importers and refiners and representatives of CII and government ministries concerned to work out import portfolio scenarios under different security conditions in the Gulf.
- India will have to find ways to manage sanctions. Indian exports to Iran total around US\$ 2.6 billion while imports are approximately US\$ 10 billion. This major imbalance is a key challenge to getting around the sanctions on Iran through the rupee payment scheme as the significant shortfall in Indian exports will not be sufficient to pay for Iran's oil on a barter basis. India will have to increase its exports to sustain the current level of oil imports from Iran. The Ministry of Commerce & the Ministry of Finance should consider ways in which Indian entities and banks trading with Iran can be immunized and kept out of the scope of US sanctions.
- As the United States begins its troop withdrawal from Afghanistan and pursues its strategy of pivoting to the Pacific, India will also face the challenge of maintaining stability in the Afghanistan-Pakistan region. Iran is an important partner in this process and will remain essential to any strategy. The recent decision to engage in tripartite discussions between India, US and Afghanistan needs to be leveraged to attain this goal.
- India will need to be prepared with contingency plans in case the Gulf is destabilized due to political or military developments involving Israel, Iran or Syria. Six million migrant workers from India are currently in the Gulf. Based on our experience of the Iran-Iraq War, the two Gulf Wars and the recent evacuation of Indian nationals from Lebanon and Arab countries beset with democracy uprisings, we feel that Ministry of External Affairs should be ready with operational plans to minimize displacement and harm to the Indian population in the Gulf. These plans should be kept operational for at least a year given that the situation could become more dynamic after the US Presidential election.

- In the long term, India will also have to devise a strategy to increase the value added component of its migrant workers as the Gulf countries will begin to come under pressure following democracy protests in the region to provide employment to their own nationals. A number of Gulf countries have already put in place plans to indigenise jobs. It is suggested that the Ministry of External Affairs or Ministry of Overseas Indian Affairs should take up this task on a priority basis.
- As India faces strategic choices on how to best handle Iran, there is a need to de-romanticize the civilizational links with Iran. A balance with India's domestic constituents can be achieved by shifting the perception of India siding with the West against Muslims to an issue that is fundamentally about India pursuing its independent interests amidst a deteriorating relationship between the United States and Iran.
- Iran is aware of the strength of the Indian position in Afghanistan. India enjoys tremendous goodwill, largely thanks to the development projects that it has been carrying out. However, this position does not necessarily give India leverage over the United States that Iran can take advantage of. India must continue to eschew any role in the ongoing P5+1/Iran talks. Not only is India's ability to change things on the ground in Iran limited, but it is also unlikely that either side will regard India as a genuinely full participant in the dialogue.
- The United States is gradually decreasing its dependence on oil from the Gulf and increasing imports from other sources like Canada and possibly Brazil. As a result, some projections estimate that the United States may not require oil from the Gulf by 2020. This sets a notional limit both to curtailing our imports from Iran and of reducing our capacity to process high sulphur crude from Iran and Iraq. The shift in US's energy imports will require India

to be swift and methodical in mobilizing its resources to take advantage of the situation.

- Development of the Chabahar port is critical. This port would offer many logistical advantages as it would be linked to Central Asia by rail and would provide expanded access to Central Asian markets. As the Indian Ocean emerges as a new theater for great power competition, the strategic importance of this port is also high, particularly in light of the China assisted Gwadar port next door in Pakistan.
- Whether Israel could view the American election in November as a window of opportunity to initiate hostilities against Iran is debatable. President Obama will be at his weakest point in terms of political resolve and India will have to be prepared to handle such contingencies.
- The concept of strategic independence may offer the cushion of not taking positions on a case by case basis and provides the political leadership an easy way to market foreign policy decisions to domestic constituents.



Annexure

List of Participants

1. **Naresh Chandra** (Chair)
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Founding Trustee, Aspen Institute India
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