

THE BATTLE OF DUBAI

**The United Arab Emirates
and the U.S.-Iran Cold War**

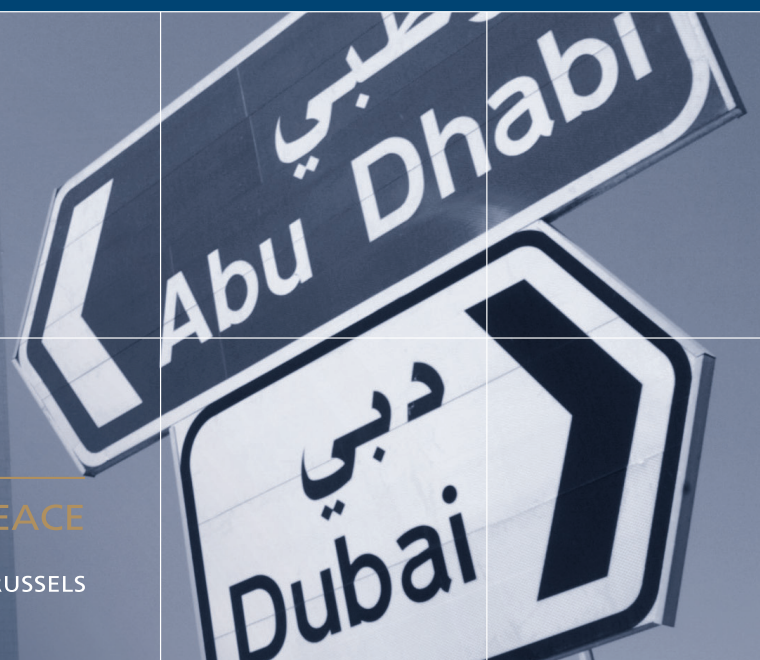
Karim Sadjadpour

MIDDLE EAST | JULY 2011

CARNEGIE ENDOWMENT

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Contents

Summary	1
Introduction	3
Too Close for Comfort: The UAE and Iran	4
Iranians in the UAE	5
Iran-UAE Economic Ties	7
Sources of Iran-UAE Tension and Mistrust	9
Balancing Iran: The UAE and the United States	14
Origins of a Strategic Partnership	14
The Iranian Threat and U.S. Assistance	15
Growing Trade Ties	17
Watching Iran in the UAE	18
Lingering Mistrust	20
The UAE and Sanctions Against Iran	20
Dubai: Iran's Hong Kong?	21
Emirati Acquiescence	23
A New Turn for Sanctions Enforcement	24
Boom Times for Middlemen: The Role of Hawala and Seafarers	26
Tough Times for Businesspeople	27
Conclusion	28
Notes	33
About the Author	39
Carnegie Endowment for International Peace	40

Summary

As the United States seeks to contain Iran's nuclear ambitions through economic sanctions and diplomatic isolation, the United Arab Emirates (UAE) has come to play a critical yet often ambiguous role. The UAE, namely the emirate of Dubai, is a top source of Iranian imports and a key transshipment point for goods—legal and illegal—destined for the Islamic Republic. Dubai's bustling and loosely regulated ports have repeatedly frustrated international sanctions against Iran.

At the same time, the government in Abu Dhabi feels acutely threatened by Iran and has consequently forged a strategic alliance with the United States. The UAE spends billions of dollars on U.S. arms and Emirati officials have privately urged the United States to consider all possible options—including military intervention—to stop Iran's nuclear program. Additionally, the UAE has allowed the United States to use Dubai—home to the world's second-largest Iranian diaspora community—as a perch to gather information on Iran.

A combination of U.S. pressure and Abu Dhabi's newfound economic and political clout over Dubai has led the UAE to significantly enhance the enforcement of sanctions in recent years. Yet both the United States and the UAE face serious obstacles in distinguishing between legal and illegal commerce and have felt a backlash from legitimate merchants who feel unfairly targeted.

Few policymakers in Washington or Abu Dhabi believe that sanctions alone will modify Iran's external behavior or curtail its nuclear ambitions. But if the United States and the UAE seek to move beyond sanctions and military containment to address the deeper roots of the Iranian threat—namely the character of the Iranian regime—they may find they have differing long-term interests.

Introduction

With the Middle East in the throes of momentous popular uprisings and its future up for grabs, America's long-standing concerns about the Islamic Republic of Iran have only grown more acute. American officials, as well as their Arab and Israeli counterparts, now worry not only about Tehran's continued nuclear defiance but also its efforts to enhance its standing by shaping the popular unrest that has unsettled and unseated Arab regimes throughout the region.

Up until now, Washington has focused on two methods, broadly speaking, to contain Iran's regional influence and check its nuclear ambitions. First, it has focused on political and economic coercion, in the form of numerous unilateral, multilateral, and United Nations sanctions resolutions. Second, it has focused on providing significant military aid to Iran's Arab neighbors. In Palestine, Lebanon, Iraq, and the Persian Gulf, Tehran and Washington have been engaged, sometimes directly but more often via proxies and allies, in an often-violent struggle for regional power and influence.

In the tiny United Arab Emirates (UAE), a quieter, but no less fateful, battle between the United States and Iran has long been underway in the spheres of commerce, diplomacy, and intelligence. Located just 35 miles from Iran across the Strait of Hormuz, the UAE is unique in that it combines vast networks of trade and personal relations with Iran with a close strategic relationship with Washington. Consequently, it has come to play a critical, albeit often ambiguous, role in the U.S.-Iran rivalry.

At first glance, the relationship among the three parties resembles an asymmetric triangle: A superpower (Washington) and a smaller power (the UAE) cooperate to check the ambitions of an aspiring regional power (Tehran). Their rivalries are at once geopolitical, civilizational, and ideological. A closer look, however, reveals that the UAE is often torn between the interests of the security-focused emirate of Abu Dhabi and the business-oriented emirate of Dubai. The UAE, furthermore, is not the only party with divided interests. Iran is often pulled in one direction by the ideological ambitions of its regime and in another by the pragmatic aspirations of its private merchants.

Dubai, the UAE's second-largest emirate after Abu Dhabi, is home to one of the largest Iranian diaspora communities in the world. UN sanction resolutions, coupled with Iran's highly regulated and inhospitable business environment, have discouraged international traders and investors from dealing directly with Iran. Dubai's orderly and loosely regulated ports provide an

The UAE is often torn between the interests of the security-focused emirate of Abu Dhabi and the business-oriented emirate of Dubai.

attractive alternative for both licit and illicit traders wishing to do business with Iran. As a result, a sizeable portion of both Iranian exports and imports flow through Dubai. Though U.S. pressure and UN sanctions have succeeded in curtailing Iran-UAE economic ties in recent months, the Emirates remain one of Tehran's primary sources of imports.

Despite its role in enabling Iran to subvert international sanctions, the UAE federal government in Abu Dhabi harbors tremendous suspicions of Iran's "hegemonic" ambitions and feels acutely threatened by its nuclear program. It

has consequently forged a strong strategic alliance with the United States and in recent years has attempted to exercise restraint over neighboring Dubai's ties with Iran.

Given its conflicted relationship with Iran, the UAE has served as a kind of petri dish in which to test American policies toward Tehran. The UAE is a prime target of international sanctions enforcement, and U.S. officials have invested considerable time and resources trying to rein in Dubai's thriving illicit trade with Iran. The UAE is

also one of the largest U.S. arms export markets. Abu Dhabi has bought some of the most sophisticated—and expensive—weaponry available. Furthermore, in the absence of an official U.S. diplomatic presence in Tehran, Washington uses the UAE as a vantage point from which to observe and interpret Iran's internal political and popular dynamics.

As Tehran inches closer to nuclear weapons capability and the U.S.-Iran rivalry for regional power intensifies, the UAE finds it increasingly difficult to reconcile its internal contradictions. While U.S. pressure and international sanctions have made trade with Iran more difficult, considerable illegal commerce persists, and strong domestic constituencies, particularly in Dubai, are beginning to speak out against the adverse impact of sanctions during a time of economic uncertainty.

Moreover, there are serious doubts in both Washington and Abu Dhabi about the efficacy of sanctions in curtailing Iran's nuclear ambitions. The UAE has become an increasingly reliable partner for the United States, but both fear and economic expediency prevent it from taking a stronger public stand against Iran. It has thus tried to walk a fine line between satisfying its ally and protector, the United States, and accommodating its looming neighbor, Iran. A close study of U.S.-UAE-Iran dynamics offers important insights into the progress and continued challenges of efforts to contain Iran.

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Too Close for Comfort: The UAE and Iran

The UAE was born in 1971 when the seven tribal sheikhdoms previously known as the Trucial States—Abu Dhabi, Ajman, Dubai, Fujairah, Sharjah, Ras al-Khaimah, and Umm al-Quwain—received their independence from

the United Kingdom and united to form a common nation. Formal independence aside, however, the tyranny of geography has prevented the UAE from escaping the shadow of its much larger neighbor to the north, Iran.

Iran's ties with the Trucial States go back a millennium. From those early beginnings to the present, many Iranians, both official and civilian, have looked condescendingly at their southern neighbors and seen their lands as falling within Iran's sphere of influence, if not constituting a quasi-extension of Iran. For this reason, the UAE's concerns about Iran's nuclear and regional ambitions have largely fallen on deaf ears in Tehran. In 2007, Mahmoud Ahmadinejad was the first Iranian president to take the trouble to visit the UAE since the 1979 revolution.

Iran's hegemonic assumptions are due in part to Tehran's belief that the modern-day UAE was built by merchants, architects, and artisans of Iranian origin. Iranians have migrated to the UAE, and especially to Dubai, in large numbers and now make up more than 10 percent of the total population. Some 450,000 Iranians or persons of Iranian origin reside in the Emirates, making it the largest Iranian diaspora community in the world after the United States. In contrast to this latter diaspora community, Iranians living in Dubai come and go from their country far more frequently: There are more than 200 flights per week between the UAE and various Iranian cities.

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Due to these cultural ties and geographic proximity, Iran and the UAE have developed a close and multifaceted trade relationship. While the United States has had success curtailing Iran-UAE ties in recent years, the Emirates remain one of Tehran's largest trading partners and a primary source of imports, with official annual trade topping \$10 billion and unofficial (often illicit) trade estimated to be several billion dollars per year. In fact, despite Iran's pretensions of hegemony, the Islamic Republic now relies on the tiny UAE and its Dubai port as an indispensable economic lifeline, not vice versa.

Iranians in the UAE

There is a popular joke among Iranians in Dubai: The ruler of Dubai, worried by drought, implores UAE residents to pray for rain in their "beloved country." The next day, monsoon rains hit Pakistan and India (the UAE has large Pakistani and Indian expatriate communities). The ruler then adjusts his decree and asks all UAE *nationals* to pray for rain in their "beloved homeland." The next day, it rains in Iran.

The joke is usually told by more recent émigrés who still hold Iranian passports, rather than the proud UAE passport holders who migrated from Iran generations ago. Regardless, this anecdote is meant to underscore

the deep and organic ties between Iran and the UAE—ties that have grown dramatically over the past 150 years, and especially since the 1979 Iranian Revolution.

For much of its history, Dubai was Iran's forgotten backwater. It wasn't until the early twentieth century that merchants from southern Iran, upset by the increased centralization of power in Tehran, emigrated to Dubai. These merchants quickly assimilated and in short order helped form the backbone of Dubai's merchant and professional class. Indeed, several Iranian families of that generation—Gargash, Gergawi, and Shirawi to name a few—are among the wealthiest and most influential families in the UAE today.

Ever since those Iranian merchants first began to arrive, Dubai has increasingly played host to economically and politically disaffected Iranians. As author Afshin Molavi noted, “elements of Dubai's success were increasingly tied to Iran's failure, a pattern that continues to play out today.”

In the 1960s and 1970s, a new class of Iranian migrants began landing on the shores of Dubai and Abu Dhabi: the working class. These migrants sought jobs in the new boomtowns of the Gulf, but many became petty traders and

shopkeepers rather than laborers. Iranians of this generation living in Dubai and the UAE were liberally granted UAE passports after 1971 if they chose to accept them. However, Iran did not allow dual citizenship, so many people opted to keep their Iranian passports—a source of great regret to them today, given the notorious difficulty of getting foreign visas with Iranian passports.

By 1979, Iran was in the throes of revolutionary chaos, which sparked another huge wave of Iranian emigration to Dubai. As Dubai solidified its position as a burgeoning trade hub for the region and built a reputation as a stable,

comfortable environment for merchants, Iran plunged into even more chaos in the wake of Saddam Hussein's invasion. All across the southern cities of Iran, families sought safe harbor with relatives in the UAE. Others who had little or no history on the other side of the Persian Gulf also made their way to the security and stability of the UAE. Most notable among these newer migrants to Dubai were residents of Khoramshahr, the southern Iranian city that received the brunt of the devastation by Saddam's bombs and guns.

Over the course of the 1980–1988 Iran-Iraq War, the UAE developed a split personality. While the Emirates officially remained neutral, Abu Dhabi, which frequently took its foreign policy cues from Saudi Arabia, sided with Saddam, whereas Dubai was eager to continue trading with Iran and fearful of antagonizing it. Abu Dhabi, along with other Gulf Cooperation Council (GCC) and Arab nations, bankrolled Saddam's war against Tehran; Dubai served as a key transit point for war material destined for Iran. The “tanker war” of the late 1980s, in which the United States reflagged Kuwaiti tankers to protect them

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from Iranian attack and implemented Operation Staunch to prevent arms sales to Iran, turned the Persian Gulf into a significant theater of operation.

Many Gulf leaders expressed relief at the end of the war in 1988, followed shortly thereafter by the death of Ayatollah Khomeini and the rise of Hashemi Rafsanjani to the presidency of Iran in 1989. They viewed Rafsanjani as a more pragmatic leader who favored trade and reconciliation with Iran's Gulf neighbors over conflict. To be sure, Iran may not have shunted aside its regional ambitions, but revolutionary fervor had begun to wane, opening up room for Iran and the UAE to resume their trade relationship.

In 2003, Dubai's famously pro-business ruler Sheikh Mohammad decided to open up Dubai's restricted real estate market to foreign nationals. Iranian merchants immediately seized on this opportunity and poured money into property, land, and retail space in Dubai. Middle-class Iranians also soon flocked to Dubai to buy studios and one-bedroom apartments, as the purchase of an apartment also guaranteed the buyer a residence permit, a useful document given Iran's internal repression and external conflicts.

The 2005 presidential election of Ahmadinejad on a platform of class warfare and economic populism spurred a new wave of interest in Dubai real estate. Popular Persian language magazines carried exhaustive listings of purchasing opportunities in the UAE. Persian-language satellite television broadcasts from abroad were peppered with advertisements for the hottest deals in Ras Al Khaimah, Dubai, or Abu Dhabi. Thousands of Iranian real estate agents set up shop in Dubai to cater to this burgeoning market.

Furthermore, Ahmadinejad's poor economic management and the resulting inflation, unemployment, and underemployment in Iran sent a wave of job-seeking, white-collar Iranian migrants to Dubai, mostly from Tehran. This latest group of migrants accounts for the largest non-southern Iranian influx to Dubai. Many of them are transient, dividing their time between Iran and the UAE. Dubai has also come to be seen as a convenient place for diaspora families to meet with Iranian relatives without the hassle or potential political difficulties of going to Iran.

Iran-UAE Economic Ties

Over the past decade, the Emirates have become Tehran's most important connection to the global economy, as sanctions and other legal barriers have increased the difficulty of dealing directly with Iran. The UAE-Iran trade relationship brings important benefits for both countries. Iran gets the imported goods it needs, while the UAE profits handsomely from the billions of dollars of trade flowing through its ports.

Iran-UAE trade ties rose steadily throughout the last decade, by most estimates peaking at some \$12 billion in 2007. The UAE eclipsed Iran's traditional European trade partners such as Germany and Italy. Countries such as China—whose commercial and energy relations with Iran are estimated to be

upward of \$15 billion—have begun to conduct much of their bilateral trade with Iran through the Emirates.

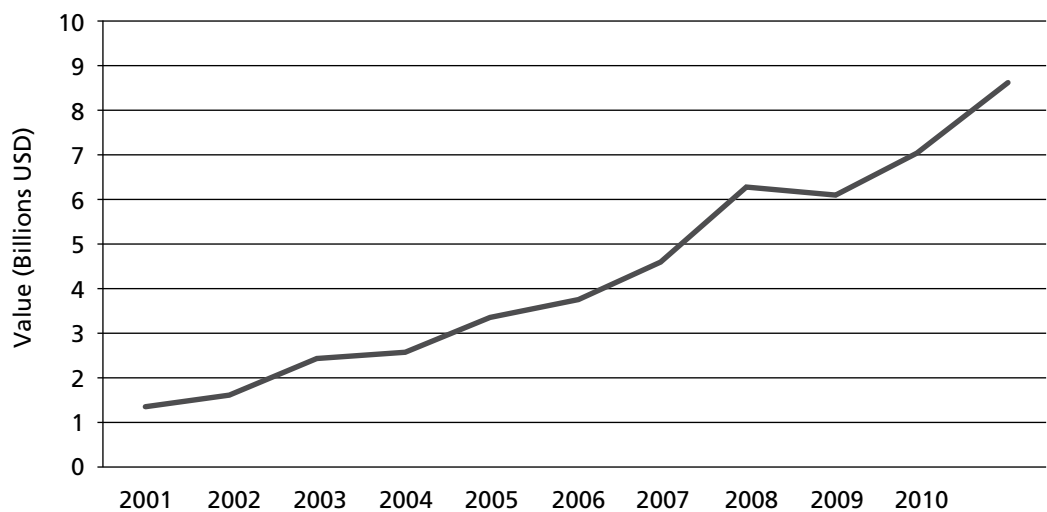
Indeed, the overwhelming majority of UAE trade with Iran involves the simple re-exportation of goods received from other countries, ranging from everyday foodstuffs to industrial equipment. This re-export trade has grown steadily over the past decade and was officially worth over \$8.5 billion in 2010, though unofficial estimates are much higher. Iran is the UAE’s second-largest re-export market, accounting for about 17 percent of total re-export volume, and the UAE in turn is one of Iran’s top sources of imports, accounting for more than 15 percent of its total. As a result, the trade relationship is heavily weighted in the UAE’s favor. In 2010 the UAE exported or re-exported over \$9 billion worth of goods to Iran, and only imported \$1.12 billion worth.¹ Iran’s trade deficit with the UAE is its largest.

Table 1. Top Re-export Partners for the UAE in 2010 (in millions of USD)

Country	Value of Re-exports	Percentage of Total Re-exports
India	\$14,224.52	28.11%
Iran	\$8,581.57	16.96%
Iraq	\$4,131.94	8.17%
Afghanistan	\$2,119.82	4.19%
Bahrain	\$1,604.29	3.17%
Total	\$50,599.12	100%

Source: Ministry of Foreign Trade, United Arab Emirates

Figure 1. UAE Re-exports to Iran in Billions



Source: Ministry of Foreign Trade, United Arab Emirates

Dubai is particularly attractive as a re-export hub for goods to Iran; it re-exported about \$5.8 billion worth of goods there in 2009.² In contrast to Iran's notoriously unruly, corrupt, and inefficient ports, Dubai's ports have modern infrastructure and are governed by a laissez-faire approach.

U.S. officials estimate that several thousand Iranians make a profitable living by simply facilitating this re-export trade with Iran. Dubai has made out very well under this arrangement, too. In addition to reaping benefits from being a re-exporter, it has increasingly become the first stop for Iran's non-oil exports abroad. Rather than sending their goods on more costly long-haul journeys to Europe or Asia, Iranian businesspeople send them to Dubai, where they are placed on larger ships bound for global markets. Due in part to these cross-currents of trade, Dubai has emerged as the third-largest re-exporter in the world after Hong Kong and Singapore.

Dubai still overshadows its fellow emirates in attracting some of the world's most influential companies, but small Iranian businesses are increasingly flocking to free-trade zones in the emirates of Sharjah, Ajman, and Ras al-Khaimah, given their cheaper fees and start-up costs. Indeed, Iran was Sharjah's second-most important export partner in 2009, with re-exports worth more than \$780 million in 2009.³ The annual Iranian Trade and Tourism Week Expo in Sharjah has become a well-attended event for businesses and individuals looking to invest in Iran.

As UAE-Iran trade has flourished, several organizations have formed to promote the interests of Iranian businesses in the UAE. The Iranian Business Council of Dubai (IBC) was established in 1982 to represent the thousands of legitimate private companies with Iranian ownership and management. It seeks to provide its members with the kind of associational support enjoyed by most business groupings: trade delegations, dispute arbitration advice, and networking opportunities. Two other organizations have a more official flavor than the Iranian Business Council: the Iranian Trade Council, formed in 1995 to provide facilities to strengthen Iran-UAE trade, and the joint UAE-Iran Trade Committee, founded in 1991 to broker trade agreements.

Smaller Gulf nations are not merely concerned about Tehran's current theocratic government; they fear the "imperialist" ambitions of the Iranian nation writ large.

Sources of Iran-UAE Tension and Mistrust

While close trade and cultural ties have enhanced UAE-Iran dependency, they have not diminished the UAE's suspicions of its powerful northern neighbor. In private and increasingly even public statements, Emirati officials consistently assert that Tehran poses the single greatest threat to their national security.

In contrast to the United States, smaller Gulf nations are not merely concerned about Tehran's current theocratic government; they fear the "imperialist" ambitions of the Iranian nation writ large. As Anwar Gargash, current UAE

minister of state for foreign affairs, noted more than a decade ago, “Despite the great shift from a monarchic to a revolutionary republican system, Iran’s [hegemonic] goals in the area have neither shifted nor changed.”⁴

Until recently, Abu Dhabi and Dubai have differed about how to deal with Tehran. Dubai preferred a more accommodating, business-first approach; Abu Dhabi had a much more alarmist view of Iran’s nuclear program, its “imperialist” ambitions in the Persian Gulf, and the growing population of Iranians residing in the UAE. Leaked State Department cables reveal that Abu Dhabi officials consistently pressured Washington to exert more pressure on Tehran, while Dubai officials often argued for more dialogue and understanding.

This dynamic began to change after the 2008 global economic collapse, which caused a major economic and financial crisis in Dubai. Cash-rich Abu Dhabi bailed out heavily indebted Dubai to the tune of \$10 billion, giving Abu Dhabi both economic and political clout over Dubai. In the words of a senior Western diplomat who served in the UAE for several years, Abu Dhabi Crown Prince “Mohammed bin Zayed effectively runs Dubai now.”⁵ As a result, the UAE is increasingly speaking with one voice, that of Abu Dhabi, in its dealings and disputes with Tehran.

The Islands Dispute

Emirati suspicion of Iran goes back to well before the Islamic Revolution, even before the UAE’s founding. Iran has long tried to establish its primacy over the Persian Gulf, an ambition that makes smaller Arab states very nervous. One of the most persistent sources of bilateral tension between the UAE and Iran has been over ownership of the islands of Greater Tunb, Lesser Tunb, and Abu Musa. These islands are strategically important to both countries because of their proximity to key shipping lanes.

Tehran believes the islands long belonged to Iran but were taken over by the British in the nineteenth century. The UAE argues that the islands have been mostly ruled by Arab leaders since the fourteenth century, specifically by the Al Qawasim dynasty, whose descendants have ruled Sharjah and Ras al-Khaimah since the mid-1700s. In the 1920s, Iran staked a claim to the islands, but the British opposed it and Sharjah (which then encompassed Ras al-Khaimah) retained control over them.

After the British formally left the Gulf in 1971, Tehran moved quickly to “reclaim” (or, according to the UAE, “seize”) the islands. The late Shah of Iran believed he had a gentleman’s agreement with the United Kingdom: In exchange for Iran’s acquiescing to Bahrain’s independence (another territory it believed it had an historic claim to), Britain tacitly agreed not to interfere if Tehran were to make a move for the three islands.

In November 1971, Iran and Sharjah signed a “Memorandum of Understanding” that allowed both sides to share control of Abu Musa and split

any oil profits, but neither side renounced its claim to full sovereignty. The ruler of Ras al-Khaimah refused a similar agreement on Greater and Lesser Tunb, and Iran invaded these two islands on November 30, 1971.

Tensions escalated in 1992, when the UAE accused Iran of violating the Memorandum of Understanding and illegally increasing its presence in Abu Musa. In 2008, Iran built maritime offices on Abu Musa, prompting further UAE protests. The UAE claims that Iran has taken over all access to the island and encouraged settlement of Iranians there. Sharjah still receives oil revenue from Abu Musa under the 1971 agreement, though it wants more access to the oil underneath the island.

The renewal of heated rhetoric from both governments underscores the re-emergence of tensions over the islands. In April 2010, UAE Foreign Minister Sheikh Abdullah bin Zayed compared the Iranian occupation to the Israeli occupation of the West Bank, Gaza, and the Golan Heights, prompting an angry Iranian response. In September 2010, the GCC reiterated its support for the UAE's claim to the islands. In response, the Iranian foreign minister called the islands an "indispensable" part of Iran and accused the GCC of interfering in its internal affairs.

The islands dispute is a constant irritant in UAE-Iran relations and undermines efforts to strengthen cross-strait ties, but the threat has never escalated to the level of armed conflict. Instead, the UAE and the GCC have called for a settlement brokered either by international arbitration or by the International Court of Justice, both of which Iran has refused.

Iran's Nuclear Program

Iran's nuclear ambitions are the greatest source of bilateral tension. In July 2010, the UAE's ambassador to the United States, Youssef al-Otaiba, made headlines when an interviewer asked him whether he would like the United States to stop Iran's nuclear program by force. He replied:

Absolutely, absolutely. I think we are at risk of an Iranian nuclear program far more than you are at risk. At 7,000 miles away, and with two oceans bordering you, an Iranian nuclear threat does not threaten the continental United States.... I think out of every country in the region, the UAE is most vulnerable to Iran. Our military, who has existed for the past 40 years, wake up, dream, breathe, eat, sleep the Iranian threat. It's the only conventional military threat our military plans for, trains for, equips for, that's it, there's no other threat, there's no country in the region that is a threat to the UAE, it's only Iran. So yes, it's very much in our interest that Iran does not gain nuclear technology.⁶

While the UAE foreign ministry later retracted al-Otaiba's statement, saying that it was taken out of context, leaked State Department cables provided additional evidence that, from the UAE's vantage point, Iran sees itself as an

imperial power and its nuclear ambitions represent an existential threat that must be stopped or delayed, “by all means available.”⁷

In numerous leaked cables, UAE Crown Prince Mohammed bin Zayed and Foreign Minister Shaikh Abdullah are quoted telling American officials that engagement with Iran is futile, economic sanctions are insufficient, and a near-term conventional war with Iran is preferable to the long-term consequences of a nuclear-armed Iran.⁸ When U.S. officials ask them to make stronger statements against Iran, however, UAE officials demur, not wanting to confront Tehran publicly.

Sectarian Unease

In addition to Iran’s territorial and nuclear ambitions, Emirati federal officials are increasingly concerned that Iran is trying to challenge the UAE’s sectarian balance and agitate Shi’i political sentiment. The UAE ruling families are Sunni, and while Sunni Muslims constitute approximately 85 percent of UAE citizenry, concerns about growing Shi’i Muslim emigration—from Lebanon, Saudi Arabia, and especially Iran—as well as alleged Hizbollah “sleepers,” have prompted UAE authorities to make it more difficult for Iranians to reside there.

Previously, anyone who bought property in Dubai was automatically granted a residency permit; now, new regulations require non-UAE nationals to register with UAE authorities every six months. Though the regulations apply to all foreigners, many Iranians in the UAE believe they are being singled out. Numerous Iranians who bought property in Dubai several years ago for the sole purpose of establishing residency stated in interviews that they feel “duped” by the change in policy.

A 28-year-old Iranian saffron business owner complained about Iranians’ increasing sense of insecurity in Dubai as a result of harassment from UAE police. “It’s tough to run a business here when you’re living month to month, worried that your residency permit may suddenly be revoked. We are trying to move our business to Canada.”⁹ Dubai authorities have criticized the Abu Dhabi government on this issue, claiming that the “demonization” of Iranians is “unhelpful,” given Iranians’ political moderation and contributions to the local economy.¹⁰

The Arab Uprisings of 2011

The most recent source of UAE-Iran tension is over allegations that Tehran is supporting Shi’i co-religionists against the Sunni monarchy in Bahrain. Bahraini Shi’a, who constitute a majority of the country’s inhabitants, staged large demonstrations against the ruling Khalifa family earlier this year, demanding political freedoms and an end to sectarian discrimination. GCC

countries, including the UAE, sent forces to support the regime and quell protests. In response, Iranian officials and state media lashed out at the council, and especially at Saudi Arabia, for helping to violently crush peaceful demonstrations in Bahrain. A senior Iranian legislator even threatened to mount a campaign to push Iran to reconsider relations with the Emirates over the issue.

Gulf countries claim that Iran is the one that is guilty of interfering in their internal affairs. They allege that Tehran is providing direct assistance to the protesters in Bahrain, a charge both Iran and Bahraini Shi'a deny. Kuwait has also accused Iran of operating a spy network on its territory, and both Kuwait and Bahrain have expelled Iranian diplomats they suspect of espionage, once again increasing GCC-Iran tensions. In a move that further heightened Arab suspicions of Iranian intentions, the chief of staff of Iran's armed forces said on April 30 that the "Persian Gulf has always, is and shall always belong to Iran." He criticized Gulf Arab regimes as dictatorial and said they should relinquish power to their people.¹¹

While the UAE has not faced significant internal unrest itself, it has demonstrated solidarity with its Gulf allies. Foreign Minister Sheikh Abdullah bin Zayed Al-Nahayan implored Iran to "reconsider its policies in the region ... and respect the unity and sovereignty of Gulf countries."¹²

Cultural Subversion

While the UAE frets over Iranian plots to foment sedition in the Gulf, Iran has its own worries about cultural subversion from the UAE. The Dubai-based Farsi1 television network is a prime example of the inherent tension between UAE permissiveness and Iranian political sensitivity. Farsi1 is a partnership between Rupert Murdoch's News Corporation and the Dubai-based Moby Group, which is run by the prominent Afghan Mohseni media family. The network strictly eschews news and political programs, sticking to broadcasts of dubbed popular foreign soap operas and Western television series like *24*. In little more than a year, Farsi1 has emerged as one of the most popular television networks in Iran. One Iranian woman who splits her time between Dubai and Tehran quipped that all of her friends had become "Farsi1 addicts."¹³

Iranian officials see Farsi1 as part of a larger U.S. strategy of cultural subversion and have pressured UAE officials to shut it down. According to Farsi1's senior management, Tehran has managed to undermine Farsi1 by pressuring the UAE to deny residency permits to its employees, by interrogating and threatening Farsi1 employees who visit their families in Iran, and even by issuing veiled death threats against the Mohseni family. This campaign of intimidation has prompted Farsi1's management to consider relocating to a place well outside Tehran's sphere of influence.

Balancing Iran: The UAE and the United States

At the heart of the Iran-UAE-U.S. dynamic lies a simple irony: Iranian officials want the United States out of the Gulf because they fear and mistrust it, yet the Gulf Arab nations want the United States to stay because they fear and mistrust Iran.

Indeed, the United States and the United Arab Emirates have a multifaceted relationship based on a simple principle: They are critical to one another's national security. The UAE is a small, rich country in a volatile neighborhood; over the years, the United States has served as a consistent ally and protector. For the United States, the Emirates have evolved from a strategically negligible peripheral state to an increasingly crucial partner in Washington's efforts

to maintain stability in the Middle East and contain the Islamic Republic of Iran.

The importance of the friendship to both powers is clear. The UAE relies on the United States to provide it with advanced weaponry and to protect it from regional bullies, particularly Iran; the United States relies on the UAE for military bases, regional support, and intelligence on Iran. Furthermore, the absence of U.S. diplomatic representation in Tehran means that the U.S. consulate in Dubai has become the State Department's most important source for insight and analysis on Iran.

As the U.S.-UAE alliance has grown stronger, both countries have expanded economic ties and cooperation on intelligence, education, energy, and other areas. Trade has increased sharply since the 1990s, and both countries have pledged to increase nuclear and renewable energy cooperation. And the UAE's cooperation has become crucial as U.S. and international sanctions against Iran have intensified. While the relationship is not free from tension, particularly over the UAE's tolerance of illicit trading and money laundering, these issues have not undermined the strategic basis of the partnership.

Origins of a Strategic Partnership

When the United Arab Emirates declared its independence from Britain in 1971, the United States was the third country to recognize the new state. Yet the tiny UAE was far from a major focus of Washington's Middle East strategy. At the time, that strategy rested on strong alliances with the "twin pillars of the Gulf," Iran and Saudi Arabia. The nascent UAE was wary of U.S. support for the Shah of Iran's regional ambitions and opposed the idea of foreign troops in the Persian Gulf.

At the heart of the Iran-UAE-U.S. dynamic lies a simple irony: Iranian officials want the United States out of the Gulf because they fear and mistrust it, yet the Gulf Arab nations want the United States to stay because they fear and mistrust Iran.

The 1979 Iranian Revolution began to alter these dynamics. Washington suddenly needed new regional allies, and the UAE had additional concerns about its security situation. In 1981, the UAE and other Gulf states created the GCC, which aligned itself with the United States and supported Iraq in the Iran-Iraq War. Although the UAE remained officially neutral during the conflict, Abu Dhabi was sympathetic to Baghdad. The necessity of keeping Persian Gulf shipping routes open during the war also led to increased cooperation between the UAE and the U.S. navy.

However, the real turning point in the U.S.-UAE relationship came in 1990. The UAE watched Saddam's increasingly aggressive behavior toward his Arab neighbors with alarm. In July 1990, the UAE conducted joint operations with the U.S. military as a show of strength. When Iraq invaded Kuwait, the UAE was one of the first Arab countries to call for an international military intervention. It made the fateful decision to support Operation Desert Storm militarily and financially, opening bases to coalition forces and contributing more than \$6 billion to the war effort.

After the Gulf War, the United States and the UAE cemented a military cooperation pact giving Washington access to UAE bases and ports and allowing it to pre-position military equipment on UAE soil. (These bases later became crucial to the U.S. military campaigns in Iraq and Afghanistan.) Iraq remained an important consideration throughout the 1990s, but the threat from Iran now looms larger and larger in the U.S.-UAE security relationship, particularly after revelations of Iran's clandestine nuclear activities.

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The Iranian Threat and U.S. Assistance

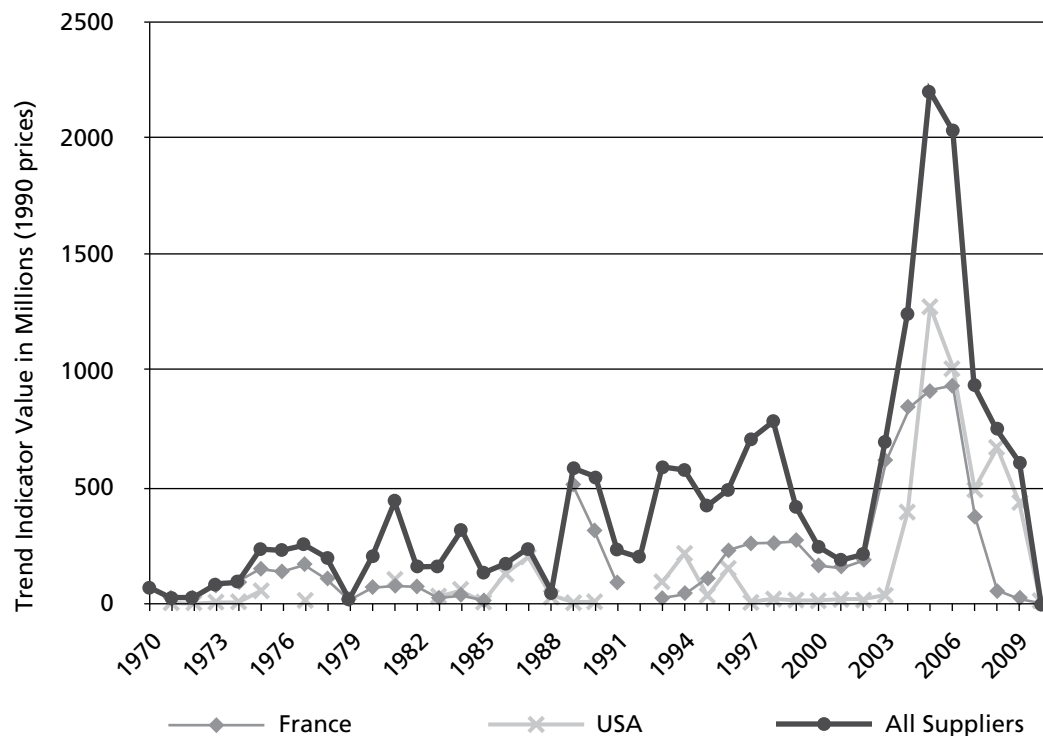
Mutual concerns about Tehran's nuclear ambitions have helped to intensify U.S.-UAE strategic cooperation, but the two countries often differ about how to deal with the Iranian challenge. The UAE, in particular Abu Dhabi, considers a nuclear-armed Iran an acute military threat and has pressed the United States to consider military solutions; the United States, meanwhile, has pushed the UAE to do more to enforce international sanctions. Leaked State Department cables reveal that Abu Dhabi Crown Prince Mohammed bin Zayed has warned U.S. officials that sanctions will never stop Iran from acquiring a nuclear weapon.¹⁴

The UAE's concerns about Iran are clearly reflected by its dramatic increase in weapons imports. The United States has become the Emirates' largest arms supplier, and arms transfers have increased in both quantity and sophistication over time (see figure 2). According to the Defense Department's reports to Congress, the UAE bought over \$3 billion worth of U.S. military equipment in 2009 and over \$5 billion in 2010. The UAE has invested heavily in missile

and radar technology, and in 2008 it became the first foreign nation to receive clearance to buy America's most advanced air defense system, the Terminal High Altitude Air Defense System. As a result of the UAE's superior, U.S.-made planes, General David Petraeus claimed in 2009 that "the Emirati Air Force itself could take out the entire Iranian Air Force."

Nonetheless, UAE officials have repeatedly pressed Washington to provide more weapons technology. In 2007, Abu Dhabi Crown Prince Mohammad bin Zayed warned General John Abizaid that Iran was acquiring advanced weapons and told him "that's why we [the UAE] need it first...give me Predator B."¹⁵ The United States, however, does not have a monopoly on arms sales to the UAE; it competes with other suppliers, particularly France, for contracts on aircraft and other weaponry.

Figure 2. Arms Deliveries to the United Arab Emirates by Supplier



Source: Stockholm International Peace Research Institute

The United States has acceded to UAE requests for weapons, and its companies have profited handsomely from doing so. One former senior U.S. official who consults with the UAE government quipped that the arms deals were "part of the domestic [U.S.] economic stimulus package."¹⁶ However, the United States has also pressed Emirati officials to more strictly enforce sanctions

against Iran. For the UAE, however, doing this would mean incurring a serious economic cost in lost trade, as well as a diplomatic cost in relations with Iran, without any guarantee that this would improve the UAE's security situation.

Thus, even as the UAE has pressed the United States to protect it from Iran, it has in the past been hesitant to aggressively impose sanctions and undermine its role as a major hub for re-exporting prohibited goods to Iran. This dynamic, along with the UAE's status as a base for terrorist financing, has been the main source of tension in the U.S.-UAE relationship.

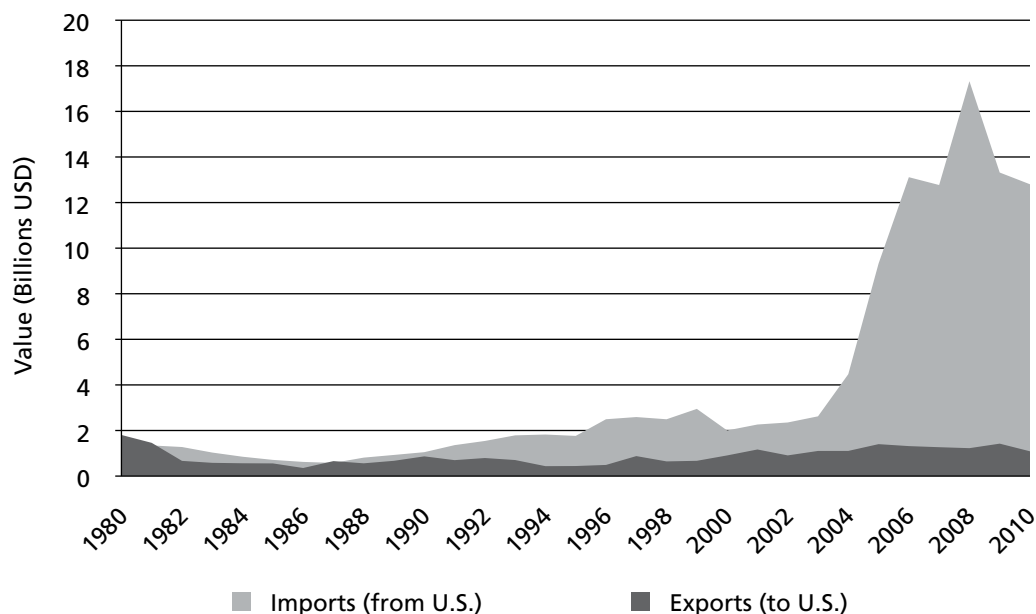
U.S. support for the UAE has expanded beyond arms sales to include nuclear energy. In 2009, the George W. Bush administration signed a peaceful nuclear cooperation agreement with the United Arab Emirates, under which the United States agreed to help the Emirates develop its nuclear energy program, on the condition that it neither enriches nor reprocesses nuclear material. The deal was meant to stand as a model for other nuclear agreements in the Middle East, as well as demonstrate an alternative path for Iran's nuclear program. As one senior U.S. official put it, "If you cooperate with us and are transparent about your intentions you can get the Cadillac of nuclear programs, and if you want to pursue it brazenly and clandestinely you'll get the Yugo of nuclear programs."¹⁷

Even as the UAE has pressed the United States to protect it from Iran, it has been hesitant about aggressively imposing sanctions and injuring its role as a major hub for re-exporting prohibited goods to Iran.

Growing Trade Ties

The budding strategic alliance between the United States and the UAE has brought about expanded trade ties. In contrast to other Gulf countries, the UAE is not a major U.S. oil supplier, and furthermore, as a result of its arms purchases, it consistently runs a substantial trade deficit with the United States (see figure 3). Economic growth and a construction boom led to a rapid increase in UAE imports over the past decade. Driven by arms sales, construction materials, and electronics, UAE imports from the United States have increased dramatically in the past decade, from \$2 billion in 2000 to \$12.8 billion in 2010.¹⁸ Today, the UAE is the largest export market in the Middle East for U.S. goods.¹⁹ UAE exports to the United States are relatively small in comparison but have also risen—from \$900 million in 2000 to \$1.1 billion in 2010.²⁰

While the U.S.-UAE trade relationship is dominated by arms sales and closely related to security cooperation, the two countries have also expanded their investment relationship. U.S. direct investment in the UAE has increased from \$2.3 billion in 2005 to \$3.4 billion in 2009.²¹ UAE foreign direct investment in the United States has risen from \$906 million in 2007 to \$2.6 billion in 2009 (data are not available before 2007).²² The Bush administration initiated negotiations for a free-trade agreement with the UAE in 2004, but these negotiations have yet to be completed.

Figure 3. UAE Trade With the United States

Source: International Monetary Fund

Watching Iran in the UAE

Just as the United States provides critical support to the UAE, the UAE also helps the United States gain a better understanding of Iran.

The Dubai World Trade Center Tower on Sheikh Zayed Road embodies the curiously intimate nature of the U.S.-Iran rivalry in Dubai. Located on the fourteenth floor of the tower are the offices of the Iranian Petrochemical Commercial Company (IPCC), an affiliate of the National Iranian Oil Company. In the same building, ten floors up, is the U.S. consulate and Office of Iranian Affairs in Dubai, which devotes a great deal of energy to monitoring the activities of companies such as the IPCC. “We probably walk past each other in the lobby each day,” said one U.S. official in Dubai, “but we don’t speak to each other.”²³

Absent diplomatic representation in Iran, Dubai is the best location for the U.S. government to try to gauge the political, economic, and social winds blowing from Iran. And given the diaspora community’s large size, relative socioeconomic diversity, and frequent trips to the homeland, no place offers a greater reflection of contemporary Iranian society than Dubai (outside of Iran, of course). Hundreds of Iranians visit the U.S. consulate in Dubai each week to apply for visas to the United States.

For this reason, in 2006 the U.S. State Department set up an “Iran Regional Presence Office” (IRPO) in Dubai. The office employs half a dozen U.S.

diplomats whose primary focus is to better understand Iran. Former George W. Bush administration undersecretary of state Nicholas Burns articulated the logic behind the creation of the IRPO in a 2006 speech at the Council on Foreign Relations:

Secretary Rice and I had an idea...that we might try to replicate what the United States did so effectively in the 1920s in a somewhat similar situation where we didn't have diplomatic relations in the early years with the Soviet Union. We established in Riga what they called back then Riga Station, and we put some of the best young American diplomats, people like George Kennan and Chip Bohlen, into Riga. And we said, "You're going to learn Russian, and your job is going to be to watch the Soviet Union, to understand it, to talk to people coming out."

We have established in Dubai our 21st century version of Riga Station. In the past year we've built up an office in Dubai solely dedicated to watching Iran and understanding Iran and talking to the thousands of Iranians who come out of Iran into Dubai itself so that we might better communicate with Iranians from all walks of life, understand them, and they'll have a little better understanding of what the United States believes about their own country.²⁴

The ability of IRPO officials to interact with a broad range of Iranians has been somewhat compromised due to the controversy surrounding the office. Since Burns's 2006 announcement, hard-line newspapers in Iran have frequently referred to the IRPO as a CIA regime-change hub staffed by dangerous spies. During the Bush administration, several Dubai-based Iran watchers complained that invoking a Cold War paradigm cast their mission in a nefarious light, when in reality their job description was simply to try to understand Iran and Iranians better. In the words of a former Dubai-based IRPO official, the office's mandate is "to get a sense of what's going on in Iran. It is not some recruiting office and is not organizing the next revolution in Iran.... It doesn't do [us] any good to give a lot of publicity to what we're doing, or if these people get too scared and don't want to come talk to us. We try to be discreet."²⁵

More recently, the office has had to weather the WikiLeaks storm. Several Dubai-based Iranians who had previously interacted with IRPO officials expressed concern that their conversations would be leaked, or at any rate could no longer be trusted to be kept confidential.

Nonetheless, given the sheer volume of Iranians who are either based in Dubai or pass through every week, often in search of U.S. visas, there is no shortage of Iranians for U.S. officials in Dubai to interact with. Indeed, IRPO officials report that visa applications have increased considerably in the aftermath of the June 2009 elections in Iran and the ensuing internal repression. Among the applicants are senior opposition activists and even former Iranian officials.

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Still, despite Iran's continued importance to U.S. foreign policy, the IRPO appears understaffed and poorly utilized. Due to the difficulty of acquiring security clearances for Iranian nationals and dual nationals, senior U.S. diplomats who are fluent in Persian often spend their days translating and analyzing the Iranian media (work usually performed by local hires in U.S. embassies elsewhere), instead of cultivating primary sources. Some IRPO staffers suggested one way to rectify this would be to increase investment in "open source" intelligence, in order to hire full-time Persian-language media analysts.²⁶

The fact that the UAE is willing to risk Iran's wrath by allowing the United States to operate the IRPO is a testament to the importance of the relationship to both parties, as well as the concerns they share about Iran.

Lingering Mistrust

Despite the UAE's widespread political, economic, and military cooperation with the United States, UAE officials continue to question the depth of Washington's commitment. In particular, UAE officials fear that Washington is interested in "making a deal" with Tehran, which would undermine the UAE's importance to the United States, as well as the basis for strategic cooperation.

One senior UAE official claimed that Rahim Mashai, President Ahmadinejad's closest adviser, asserted in high-level meetings with both the UAE and other Gulf officials that Tehran and Washington were on the verge of a diplomatic breakthrough that would lead to a normalization of their relationship. "Mashai was trying to tell us that we should no longer rely on the United States for security," said a senior UAE official. "After the U.S. and Iran make nice, Washington will leave Tehran in charge of regional security."²⁷ Another senior UAE official acknowledged that the likelihood of such a U.S.-Iran diplomatic breakthrough was slim, but he also argued that "America needs to do a better job reassuring its allies that it's not going to abandon them."²⁸

The UAE and Sanctions Against Iran

Despite the close U.S.-UAE relationship and the two countries' shared fear of a rising Iran, the Emirates have long been known as Iran's chief means of evading international sanctions. Dubai's role in facilitating Iran's connection to the global economy has increased in importance with each successive round of sanctions imposed by the United States and its allies. Everything from foodstuffs to U.S.-made consumer goods to sophisticated arms have found their way to Tehran through UAE ports.

In the past two years, three factors—Abu Dhabi's enhanced influence over Dubai, the June 2010 United Nations Security Council sanctions against Iran, and the unilateral U.S. and EU sanctions that followed—have led the UAE to noticeably step up sanctions enforcement. This move has angered Iranian

private businesspeople, many of whom are staunch critics of the Islamic Republic but argue that sanctions have the unintended effect of punishing the law-abiding and aiding the lawless. Indeed, one of the most vexing challenges of sanctions enforcement is distinguishing licit Iranian traders from illicit ones.

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Dubai: Iran's Hong Kong?

Dubai has long been considered the biggest hole in the so-called “Swiss cheese” sanctions regime against the Islamic Republic. Its proximity to Iran, limited regulatory regime, vast port, and large numbers of Iranian residents combine to make it akin to what Hong Kong once was to China: a socially lax *entrepôt* for both business and pleasure.

For years, foreign companies and traders nervous about dealing directly with Iran have found eager go-betweens in Dubai. As one Iranian ship captain told this author in 2009, “We can transport whatever you need. Things have actually gotten busier for us now that countries aren’t dealing with Iran directly. Everything is going through Dubai.”²⁹

Much of the trade between Dubai and Tehran appears to be licit, but the volume of re-exports and the lack of export regulations make it very difficult to distinguish legal trade from contraband. What is more, the Iranian government’s strong grip on the country’s economy (according to some estimates, about 80 percent of the economy is state-owned) makes it hard to distinguish independent private traders from those serving official Iranian interests. The Iranian Revolutionary Guard Corps (IRGC) have particularly extensive business ties and use their military status to circumvent Iranian government regulation. Ahmadinejad himself implied that the Guards use private wharves in Iran to avoid paying customs duties on commercial goods.³⁰

In dozens of interviews over a two-year period, numerous private Iranian merchants complained that sanctions had unwittingly strengthened the hand of businessmen affiliated with the IRGC. In the words of one Iranian professional who commutes between Tehran and Dubai, “the sanctions hurt those of us who actually respect the law. The IRGC guys who are already breaking the rules are going to continue to subvert any new restrictions and legislations.” Another Dubai-based Iranian merchant spoke more bluntly:

The Sepah (IRGC) and other government entities have much larger “sweets” (bribes) to give than we do. They can adapt and even prosper in an environment of heavy sanctions.... It is the private businessmen without the government connections who are being squeezed by the current sanctions. And they didn’t like the regime to begin with.³¹

Rumors abound about the IRGC’s vast business network in Dubai, but it is often difficult to discover which companies are in fact IRGC-affiliated. The

scion of a powerful Iranian clerical family who now resides in Dubai has said that IRGC-affiliated companies remain very active in Dubai and frequently change their company names in order to maintain anonymity. For example, Kish Oriental is an IRGC-affiliated oil-services company whose menacing business practices in Dubai have included extensive bribery and physical intimidation. Despite the fact that the *Wall Street Journal* famously chronicled the company's illicit enterprises, it continues to operate in Dubai, albeit under a different name.³²

Furthermore, IRGC-affiliated companies don't partner exclusively with Iranian businesspeople who share their ideology or are knowingly engaged in violating UN sanctions. For example, the Iranian Business Council (IBC) of Dubai was created to represent legitimate Iranian private companies, but, according to one IBC official, "we cannot always know if our members are purely private or government-linked. When someone applies to become a member, as long as they have the proper paperwork and will pay their dues, we will accept them."³³

As another IBC member added, "So much of business in Iran today is intertwined with government agencies. It's hard to tell who is government-linked or private or who derives most of their income from government contracts."

The stories of two Dubai-based traders, Mehdi and Bahman, serve in many ways as examples of the complicated relationship between business and government in dealing with Iran.

*Mehdi*³⁴

Mehdi was once a prominent 33-year-old Dubai-based Iranian steel trader. Though privately critical of Iran's "dictatorial regime," Mehdi comes from a prominent *bazaari* (merchant) family with strong links to the Iranian government. While still a teenager, he began trading in commodities with what he described as "the Russian mafia." Tehran's international isolation meant that Dubai would become the center of his family's business activities, which also included speculation in the UAE's booming real-estate market.

Mehdi's business operation was fairly straightforward. Using his family's high-level connections with the Iranian government, he would purchase discounted steel from IRGC-controlled companies that preferred to stay under the radar. He would then re-sell the steel at the international market rate, offering a healthy kickback to his government contacts in Iran. In Mehdi's words, there were hundreds, if not thousands, of Dubai-based Iranian traders in various industries with similar business models.

During the boom years, Mehdi made millions. When steel prices contracted and Dubai's real-estate bubble burst, however, Mehdi, along with many other Iranian traders, was overleveraged and forced to flee Dubai.

*Bahman*³⁵

Bahman, a 36-year-old Iranian businessman in Dubai, described a somewhat similar partnership of convenience. A decade ago, after earning business degrees in Canada and Europe, he was eager to put his entrepreneurial skills and Western business practices of transparency and accountability to use in Iran. He started a business in Tehran importing security equipment (home and car alarms) via Dubai. Despite a low markup, his sales were undercut by competitors who somehow managed to sell the same products at significantly lower prices.

After struggling for two years, he was summoned to appear at a nondescript government office building in Tehran. “There were a few men dressed in civilian clothes who essentially told me I was making things unnecessarily difficult for myself,” he said. “Instead of paying a 40 percent or sometimes higher tariff for my imports from Dubai, I could partner with them and they would remove the tariffs altogether.” His aspiring partners, he would soon find out, were former Revolutionary Guardsmen who were exempt from import duties.

“In exchange, I would give them a 10 percent kickback,” he said. “If I didn’t take their offer I would basically go out of business. You are forced to become corrupt if you want to survive in this system.” In addition to kickbacks, Bahman described being frequently “asked” to install security equipment inside the homes and cars of senior Iranian officials. The advantage of being based in Dubai, he said, was that it allowed you to continue doing business in Iran while keeping a healthy distance from Iranian officialdom. “Nobody likes the system,” he said. “Even the people in the system don’t like it.”

Bahman was skeptical of Washington’s ability to clamp down on IRGC businesses in Dubai. “It’s very difficult for even me to discern which businesses are being controlled by whom, let alone the U.S. government.... Either you have to intimidate them with overwhelming force, or you have to open up the country to trade. The U.S. seems unwilling to do either.”

Emirati Acquiescence

Estimates of Iranian assets in Dubai vary dramatically, but they are thought to compose a significant portion of Iran’s overseas assets. While Iranian companies based in the UAE’s various free-trade zones are allowed full foreign ownership, local law requires that companies outside the free zones have at least 50 percent UAE ownership.³⁶ In many cases, this means getting a local Emirati “silent sponsor” to lend his name to a company either for a fixed fee or on a profit-sharing basis.

This kind of ownership structure makes it difficult to isolate Iranian companies from their UAE sponsors, who often come from old and established Emirati families. For this reason, the UAE government is sometimes reluctant to clamp down on Iranian business in Dubai. As one senior UAE official told this author, “We would be hurting our own people as well.”³⁷

Sanctions have always put the UAE in a difficult position. UAE officials, to be sure, are terrified of the prospect of a nuclear Iran, and they are eager to do as much as they can to prevent it. However, the very factors that have made Dubai and the UAE as a whole so economically successful—namely free trade and light regulation—have also made them an inhospitable environment for enforcing sanctions.

A New Turn for Sanctions Enforcement

Despite these obstacles, the UAE has recently taken a much bolder stand on sanctions enforcement. New UN, European, and U.S. sanctions have increased the UAE's international obligations and the risks to its companies of trading with Iran. Additionally, increasing alarm about Iran's nuclear program has made the UAE susceptible to U.S. pressure on this issue. Finally, the financial crisis has given Abu Dhabi more leverage over Dubai, increasing the UAE federal government's willingness to confront pro-Iran interests there.

In June 2010, the United Nations Security Council passed its strictest sanctions to date on Iran. Resolution 1929 restricted the sale of arms and technology to Iran and called on all states to inspect suspicious cargo going to and from Iran. It also warned states to exercise vigilance in their relations and financial dealings with Iran to ensure they are not assisting its nuclear program. The sanctions target specific entities and individuals, such as the IRGC and its subsidiaries, which are believed to be involved in Iran's nuclear program. Shortly after the Security Council passed this resolution, the European Union and the United States passed additional unilateral sanctions against Iran. Most significantly for the UAE, the U.S. sanctions penalize foreign financial institutions that do business with Iran.

The United States has long pressed the UAE to improve its sanctions enforcement, but it has particularly ratcheted up the pressure in recent years and has achieved some successes. In 2007, the United States, in a move targeted at the UAE, threatened to increase restrictions on countries that serve as transshipment points for illegal goods. In response, the UAE government passed a new export control law and claimed to have closed dozens of companies that were suspected of selling dual-use goods to Iran. In September 2010, former undersecretary of the treasury for terrorism and financial intelligence Stuart Levey warned UAE bankers that they could be denied access to the U.S. financial system if they do business with Iran.

As a result of U.S. pressure, the UAE's banking sector moved to restrict its ties to Iran. The UAE Central Bank announced it will no longer deal with Iranian banks sanctioned by the United States, and it has provided an explanation of the new U.S. sanctions law to financial institutions in the UAE. The central bank has also stepped up monitoring of all transactions with Iran, rendering UAE banks increasingly wary of any dealings with the Islamic

Republic. The Dubai Financial Services Authority has reportedly told local banks to treat all Iranian clients as high risk. Reports indicate that most UAE banks have stopped money transfers to Iran, with some banning transfers in euros and dollars and others banning all transfers.

Today's more risk-averse banking sector has made it more difficult for Iranian businesspeople to secure loans and insurance. Morteza Masoumzadeh, a representative of the Iranian Business Council in Dubai, reports that UAE banks are refusing to open letters of credit for Iranian businesses, forcing them to conduct transactions in cash.³⁸ As a result, many people have had to turn to Chinese, Indian, and Russian banks. UAE banks are also less willing to accept property in Iran as collateral for loans. These measures are hurting small- and medium-size Iranian firms that rely on UAE banks for financing.

Mohammad Rayees, the managing director of an insurance company in Abu Dhabi, said that insurers are not willing to take the risk of underwriting Iranian interests affected by sanctions.³⁹

The growing reluctance of insurance companies to do business with Iran has also impacted shipping companies. The world's largest container firm, Denmark-based Maersk, has suspended operations at several Iranian ports due to sanctions. One North America-based Iranian businessman who imports agricultural goods from Iran asserted that his trade with Iran has been "seriously disrupted" as a result of the sanctions:

We have two containers of goods that have been sitting in Bandar Abbas for three weeks now and our freight forwarder does not know when they are going to be shipped. We have a booking with Senator Line but they can't tell us when they would be able to pick up our container as they don't know when the next feeder is going to call on Bandar Abbas. It could be next week, it could be another couple of weeks, before our containers are on the water.

In the past we have used big shipping companies such as Maersk, P&O, or Ned Lloyd. A feeder from these companies would come to Bandar Abbas, pick up the container and load them in the mother vessel in Dubai. But over the last six years one shipping line after another suspended service to Iran and we were left with fewer choices for shipment of our products to the West.

Mediterranean Shipping Company was one of the few remaining options for shipment to Canada. Now we are left with one choice, Senator Line, and they don't know when their feeder will come to Bandar Abbas and how big that feeder is going to be. Plus the transit time from Bandar Abbas to Canada will be over 60 days. That is a huge financing cost on us.⁴⁰

While sanctions have affected Dubai more directly than other emirates, all of them have felt the sting. Ras al-Khaimah, which has aggressively promoted trade through its tax-free RAK Free Trade Zone, appears to be enforcing the new sanctions and has stopped issuing licenses to new Iranian companies.

Today's more risk-averse banking sector has made it more difficult for Iranian businesspeople to secure loans and insurance.

The emirate is sensitive to the accusation that it is helping Iran get around sanctions. Sheikh Khalid al-Qassimi, the deposed former crown prince, has attempted to discredit his brother and the current heir, Sheikh Saud, by accusing him of fostering trade with Iran, a claim Saud denies.

Boom Times for Middlemen: The Role of Hawala and Seafarers

As most formal trading and banking links with Iran have been either restricted or rendered illicit as a result of international sanctions, informal trade and capital flows to and from Iran have mushroomed. Operators of the informal system of money exchange known as hawala (or *havala* in Persian) have confidently reassured potential clients of the increasing indispensability of their services.

The hawala system is authorized by Islamic law and was originally designed in the Middle Ages to enable Muslim traders to circumvent restrictions on lending in the Roman Empire. Its central tenets are trust, oral communication, and anonymity.⁴¹ Customers give a sum of money to a hawala broker (known as a *hawaladar*) in one city, to be transferred to a recipient in another, usually foreign, city. The hawaladar in the sender's city then calls another hawaladar in the recipient's city in order to provide the cash (minus the standard 2 percent commission) to the intended recipient. There is often no physical or even electronic transfer of money. The hawaladar who made the payment is reimbursed when the funds flow in the reverse direction, sometimes within minutes.

The Deira district of Dubai, previously the city's financial hub, is dotted with numerous non-descript but bustling offices of Iranian hawala brokers. These brokers boast of being able to transfer large sums of money to and from various Iranian cities within a short period of time. Still, several Iranian hawala brokers in Dubai said they had begun taking additional precautionary measures in an environment of increasing watchfulness over their actions. They frequently change the names of their businesses and have advised potential clients that larger transfers of money (that is, upward of \$1 million) should be carried out in multiple installments, so as not to attract undue attention. "Once we get the money out of Iran," said one hawaladar, "you simply transfer it to a big international bank in Dubai and you're all set. You can then transfer it to Europe or North America."⁴²

Much like Iran's financial middlemen, Iranian shipmen, who pilot the wooden dhows that line the Dubai creek, agree that their services (transporting goods to Iran, usually to the southwestern Iranian port of Bushehr) are in greater demand than ever. "We can transport anything," boasted one seaman. "We simply cover the goods in canvas bags." One shipman quipped that Iranian port authorities are particularly enthusiastic about American goods, which, due to sanctions, are considered contraband. "Tehranis are willing to pay a premium for American products."⁴³

Several people complained, however, about the increased scrutiny of their trade. "The police used to never bother us," said one *Bushehri* shipmen, "but

now they come around much more frequently trying to inspect our goods and asking for our papers.”⁴⁴ Due to pressure they attributed to both the U.S. government and Abu Dhabi, the authorities now require additional permits for them to continue operating legally in Dubai. One Iranian shipman complained that, despite the Iranian regime’s blustery public posture toward the UAE, it has made no effort to protect them from the harassment of UAE officialdom. “If you have a problem and go to the embassy, they tell you you’re on your own. They don’t defend you.”

U.S. officials in the UAE expressed less concern about “contraband” American foodstuffs and household items flowing from Deira to Bushehr. They focus instead on the more ominous illicit trade in dual-use goods, clandestinely conducted by individuals and entities that either have a shadowy background or are positively linked to the IRGC.

Tough Times for Businesspeople

While middlemen operating in the underground economy are currently enjoying booming business, Iranian businesspeople who operate in the open or are unwilling to partner with the Iranian regime are now feeling squeezed from two sides. Iran’s internal political repression and the growing economic appetite of the Revolutionary Guards have caused many businesses to move to Dubai or go out of business. And sanctions are increasingly limiting their ability to do business even in Dubai.

As a result, much of the independent Iranian business community in Dubai—few of whom sympathize with the Tehran regime—is critical of the current U.S.-led international sanctions regime, which they decry as “collective punishment.” Stuart Levey, former U.S. undersecretary of the treasury for terrorism and financial intelligence, became a household name among Iranian businesspeople in Dubai as a result of his aggressive push for stronger sanctions enforcement. “Mr. Levey is endangering the livelihoods of many in order to try and punish a few,” said one Iranian banker associated with the Iranian Business Council of Dubai. “We should be America’s allies but instead we are being punished by them.”⁴⁵

A U.S.-educated Iranian private practice lawyer who operates between Tehran and Dubai argued that sanctions rewarded the “corrupt” at the expense of the innocent. “It is those of us who adhere to the law that get hurt most by sanctions. The people who don’t respect the law or operate in the black market are going to continue to try to work above the law.”⁴⁶

Several Iranian merchants also asserted that heightened U.S. pressure has made the UAE an increasingly inhospitable place for them. “If they decide they don’t like you, they can order you to leave, just like that,” said an Iranian

Much of the independent Iranian business community in Dubai is critical of the current U.S.-led international sanctions regime, which they decry as “collective punishment.”

importer/exporter. “You could lose everything.”⁴⁷ Several Iranian merchants in Dubai talked about the possibility of moving their operations to Canada. Businesspeople have taken their complaints to the government of Dubai, increasing domestic pressure against sanctions.

The most common policy-related suggestion from independent Iranian businesspeople, most of whom are also critics of the Iranian government, is not for the U.S. government to abolish sanctions altogether but for it to target them against specific individuals and entities of concern—namely, senior Iranian officials and Revolutionary Guardsmen. “Freeze their bank accounts and prevent them from traveling abroad,” suggested one Iranian banker in Dubai.⁴⁸

A U.S. official in the UAE said he agreed with the idea in principle but claimed that the U.S. government does not currently have the type of human intelligence necessary to carry out such a policy.

Iranian businesspeople found this explanation dubious. “Given all the resources the U.S. government has—the billions of dollars it spends on weaponry—I cannot believe that they are incapable of targeting specific individuals. There are not that many of these *sepah* [IRGC] bigwigs. They are well known.”⁴⁹ Several Iranian businesspeople expressed the belief that Washington’s strategy—which they criticized as “counterproductive”—was to make life as difficult as possible for all Iranians in order to compel them to rise up against their government.

A U.S. official in the UAE dismissed this assertion but acknowledged that Washington understood that sanctions are “a blunt sledgehammer.” “It’s not our goal to punish honest Iranian merchants. But are officials in Washington tossing and turning at night worrying that the sanctions are harming innocent Iranian businessmen in Dubai? No, they’re not.”⁵⁰

Conclusion

In contrast to what prevailed several years ago, the balance of power in the Iran-UAE-U.S. triangle now tilts toward Washington and Abu Dhabi rather than Tehran and Dubai. Stricter international sanctions, intense U.S. pressure, and the increased clout of the UAE’s anti-Iran federal government have contributed to a sanctions regime whose strength exceeds all expectations. Iranian traders who once enjoyed almost complete freedom to trade in and out of Dubai and other emirates find that they can no longer easily secure residency, credit, or permits. Major shipping lines are refusing to transport goods to and from Iran because they can no longer secure insurance. Iranians who relied on UAE banks for foreign exchange have found their access to currency severely restricted.

The sanctions battle, however, is far from won. While the United States has secured greater political will for enforcement in Abu Dhabi, both the United States and the UAE are now faced with the more complex challenge

of effectively targeting and enforcing these sanctions in a way that will have a real impact on Iran's nuclear program. Goods continue to flow across the Strait of Hormuz, and customs authorities still lack the ability to thoroughly inspect shipments to and from Iran.

Sanctions have hurt legal and illegal traders alike, and they will always run the risk of missing their targets, thus undermining domestic support for sanctions within the UAE. Companies associated with the IRGC continue to enjoy important advantages in circumventing sanctions, and it remains difficult to distinguish them from licit traders. If the United States wants to work toward a more effective sanctions regime, it must improve its human and financial intelligence assets and task them with distinguishing legitimate traders from those closely connected to the IRGC.

More fundamentally, the United States must recognize the limitations of sanctions as a mechanism for changing Iran's behavior. The recent sanctions do appear to have played a role in slowing down Iran's nuclear progress, and indeed their effectiveness has exceeded most expectations. Yet very few people believe that sanctions will prevent or dissuade Iran from moving forward with its nuclear program, especially with oil prices hovering above \$100 per barrel. While anti-government unrest throughout the Middle East has caused Iran political consternation, it has simultaneously helped the Iranian economy by increasing the risk premium of oil prices.

While today's unprecedented U.S.-UAE cooperation on sanctions demonstrates the urgency of both states' concerns about Iran's nuclear program, the two countries still differ about how to deal with Tehran. The UAE continues to retain strong economic and cultural ties with Iran, and a significant diminution of that relationship is unlikely. The UAE's efforts to enforce sanctions exact a domestic cost, and cash-strapped Dubai in particular cannot be relied on to maintain strict sanctions indefinitely. For its part, the United States is not willing to go as far as the UAE would like—either in militarily preempting Iran's nuclear program or in guaranteeing the UAE's security against an Iranian attack.

Beyond these immediate strategic differences, the two countries also have divergent long-term strategic interests with respect to Iran. U.S. officials, both Democrat and Republican, have consistently argued that it is in Washington's interests to see a representative government in Tehran that puts the interests of its citizens over ideology and consequently drags Iran out of its largely self-inflicted international isolation. As former secretary of state Henry Kissinger once said, if Tehran were to pursue its own national interests, "there are few nations in the world with which the United States has less reason to quarrel or more compatible interests."⁵¹

Stricter international sanctions, intense U.S. pressure, and the increased clout of the UAE's anti-Iran federal government have contributed to a sanctions regime whose strength exceeds all expectations.

The UAE and other Persian Gulf states, on the other hand, are not merely concerned about the character of the Iranian regime; they are also concerned about the size and “imperial” tenor of the ambitions of the Iranian nation writ large. These concerns will remain regardless of whom is governing the country. Indeed, while Persian Gulf countries may have little affection for the Islamic Republic, they (particularly the UAE) would still be left with serious security questions if a more moderate or democratic Iranian government were to emerge and restore relations with Washington.

One of the strongest bases for Washington’s alliance with the Gulf states is Iran: Would the United States still covet this friendship with nuclear, economic, and military cooperation if that basis were to disappear? A sizable percentage of the UAE’s economic activity is based on Tehran’s need for a trade lifeline to the rest of the world: Would Iran’s economic re-integration into the global community undermine the UAE’s standing as the region’s primary trade hub? And would the tens of thousands of Iranians who spend hundreds of millions of dollars on UAE real estate, hotels, and restaurants continue to visit Dubai in droves if they could instead dispose of their income at home?

Prospects for U.S.-Iran rapprochement are still a long way off. Nevertheless, the UAE and its Persian Gulf neighbors have a strong interest in preventing movement in that direction. The UAE’s ideal scenario, arguably, is an Iran that is weakened domestically, isolated regionally, and at continuous odds with the United States; this scenario is at best unsustainable and at worst destructive. Hence, even as it cooperates with the UAE to address common concerns, the United States must recognize that its goals with respect to Iran differ.

In light of the Obama administration’s unprecedented and unreciprocated overtures to Tehran, many U.S. officials have come to understand that Iran’s external policies, particularly its opposition to the United States and Israel, are unlikely to change as long as Tehran’s current leadership remains in power. Nonetheless, Washington’s Iran strategy has rested almost exclusively on policies (sanctions and arms sales to Iran’s neighbor) that are intended to modify Tehran’s external behavior, rather than its internal dynamics.

Washington’s ability to facilitate political reform in Iran is limited, to be sure, but there are important measures the U.S. government can take to constrain Tehran’s ability to control information and repress its population. These include: dramatically improving the quality and reception of Persian-language satellite television (including the Voice of America’s Persian News Network, which is estimated to reach more than 25 million Iranians); combating the regime’s ability to control and block communications; and implementing further targeted sanctions, such as travel bans and asset freezes, against human rights abusers. The UAE’s role as a media and technology hub and the vast numbers of Iranian officials who continue to travel to the UAE make it an important player in facilitating all of these measures.

The United States has shown it can effectively leverage its influence in the UAE to increase economic and military pressure on Iran. Yet the ultimate success of its Iran policy may be determined by how well it can apply those same resources to support the cause of democracy and open society in Iran.

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