Iran's 2016 Human Capital Conundrum

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Iran's 2016 Human Capital Conundrum - is your executive leadership team ready to rise to the long-term challenges of doing business and thriving in the re-emerging Iran?

Around boardroom tables and across business wires globally, business leaders and economic commentators are currently considering the new potential opportunity and risk associated with reigniting business ties with Iran. With Asia's 'tiger economies' in slow-down, and the 'green shoots' of global economic recovery only just starting to break the surface, some regard Iran's emergence from crippling economic sanctions as a timely 'business bonanza' not to be ignored. Others are more circumspect, and view the Iranian authorities targeted levels of producing over 5 billion barrels of oil per day by 2016, and generating economic growth of up to 8% annually by 2017, as dangerous and unrealistic hype, shrouded in all manner of opaque complexity.

However, against this current global backdrop of challenging and uncertain economic conditions, Iran has continued to emerge as a country with a truly promising medium-term economic outlook having completed all the requisite steps to reach 'Implementation Day' on 16th January 2016. Iranian authorities continue to devise and implement much needed market-based reforms to encourage private-sector led job creation and growth. Assuming that Iran's government complies with the measures agreed in the recent nuclear deal, and that no 'clawback mechanism' is triggered as a return to sanctions and that political stability ensues, then real GDP could rise to around 6.7% in 2017. The successful, rapid re-emergence of Iran as a trustworthy and stable trade partner will radically change the regional economic landscape across the Middle East and North Africa (MENA). To put this growth into perspective, in 2014 Iran's trade with the EU amounted to around Euro7.6bn, and by 2018 it is predicted to grow by up to 400%.

Despite two years of recession, the Iranian economy began a steady recovery in mid-2014 as President Rouhani's administration gained some traction. In July 2014, the partial lifting of sanctions that had occurred under the Joint Plan of Action (JPOA), a negotiated agreement between the United States, France, the United Kingdom, Russia, China, Germany, the European Union and Iran, in which Iran agrees to suspend or alter its nuclear activities for six months in exchange for limited relief from economic sanctions, initiated a draw-down on diverse economic restrictions. This draw-down saw a relaxing of restrictions on oil exports, on the supply chain to Iran's domestic automotive OEMs, and on international and domestic banks' global transactions. Inflation had declined from 45.1% in 2012 to 15.6% in June 2015.

IRAN TODAY

Today, Iran already boasts the second largest economy in the MENA region, behind Saudi Arabia, with an estimated nominal GDP of US$397bn in 2015, and a single-digit rate of inflation. Iran also has the second largest population in the region, behind Egypt, with just fewer than 80 million people. The economy has been heavily geared into the hydrocarbon, agriculture and services sectors, alongside a significant state sponsored presence in the industrial and financial services markets. Continued reforms to the business environment to encourage sector diversification, promoting competition, optimising licensing procedures and

reducing the over-emphasis of State-owned- Enterprises on the economy will be key to securing further Foreign Direct Investment (FDI), and thus ensuring long-term, sustainable growth. Indeed, Iran's government recognises that FDI is needed across all sectors to truly position the country as a low-cost, quality and technology focused manufacturing hub for MENA.

The current lifting of economic sanctions is expected to unlock significant spending in the oil and gas industry (especially for enhanced oil recovery projects and the construction of LNG export facilities), and other sectors looking to benefit from increased FDI and access to new technology alongside more efficient operating practices. Iran's government plans to make significant investment upgrading many of the countries' 54 airports and expanding the rail network to 25,000km by 2025, to cater both for the marked increase in visitor numbers and demands placed on logistic networks as the international community commercially re-engages with the country.

THE INTERVIEWS

Since Implementation Day, we have interviewed a broad spectrum of industry leaders and their advisers with strong current links and interests within Iran, to gain some clear insights into the potential Human Capital related 'snakes and ladders' when shaping up a leadership team for market entry and growth in Iran. In this article we summarise the comments of four such interviewees, of which several asked to remain anonymous:

THE LAWYER

Hamid Mojtahedi is Head of the 'Iran Group' and Senior Lawyer for Al Tamimi & Company. He is Iranian born and was subsequently raised and educated between Switzerland and Canada. Like so many members of Iran's diaspora, Hamid talks with real passion and pride about his Iranian heritage, and is particularly well placed to offer some thoughts and advice from 'both sides of the cultural divide'. The bulk of Hamid's time is now spent leading his cross-sector client base through the 'minefield' of due-diligence relating to potential business partners or targets for acquisition, and advising them on the optimal manner to set up a business in Iran. He conveys a considered and balanced view of the current opportunity versus risk equation facing organisation's looking to gain a foothold in Iran at this critical juncture.

Hamid firstly focuses on the demographics of Iran because, he says, the development and availability of nascent Human Capital is key to attracting FDI in any emerging market, "the population of Iran has more than doubled since the 1980s and, of the 80 million plus Iranians still residing in Iran, 60% are aged 40 or below."

The Iranian population is highly-educated, with a specific emphasis placed on science, maths and engineering related topics, but unemployment has remained high, rising further in the last 2 years. Today the total unemployment rate stands at around 12%, with around twice as many women unemployed compared to their male counterparts. Unemployment is especially rife amongst the youth population and, whilst over 77% of Iranians aged over 15 can read and write, only around 11% of the 1.5 million school exam-takers are successful in attaining college places annually. Many observers believe that too much emphasis is placed on producing quantity and not quality when it comes to graduate numbers. Today, being a graduate in Iran is no guarantee of suitable employment. Of the 270,000 graduated entering the job market annually, it is estimated that only 75,000 will find employment.

He also draws attention to the 'brain drain' of over 150,000 highly-educated Iranians moving abroad every year in the 1990s. A further IMF report from 2009 suggests that Iran was losing between 150,000 to 180,000 specialists from their academic elite annually. Today over 500,000 Iranians are studying abroad, with Canada, Turkey, UK, US, Germany and Malaysia all playing host to over 100,000 members of the Iranian diaspora. The combined effect of these various demographic factors, combined with low rates of staff turnover in the over 50s, means that there is, at face-value, a ready-made pool of locally available talent at all executive levels for those looking to make key hires.

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However, as Hamid stresses, it is not quite so straightforward in reality, "the years of draconian sanctions and absence of FDI have led to a real lack of international business practices and behaviours amongst large swathes of the working population which in turn has led to a certain commercial complacency and potential stubbornness to accommodate change once FDI increases."

He is both positive but also cautionary when describing the ease of starting up and doing business in Iran, "new market entrants must manage their own expectations and those of their board management. Whilst certain sectors such as IT and broader Technology have kept pace with the global market, others such as FMCG, Automotive and Hospitality have been working to local standards of quality and service delivery with often autocratic management and little scope for original innovation or process improvement. The ownership structures of many such organisations, along with their procurement practices and vendor selection, are often opaque and convoluted, requiring deep due-diligence by specialist service providers."

Finally, Hamid issues a stark warning against an over-reliance on hiring returning talent from Iran's diaspora, "as is the case with China's 'sea turtles', those Mandarin speaking China born professionals returning to China from Western countries having lived, grown up, studied and worked abroad, one must not presume that Iran's returning talent will be able to assimilate and re-adjust quickly, despite speaking Farsi. Of course, such returnees will be welcomed back by Iran's endemic population, but they will be viewed with suspicion by some in a country where trust, network and 'face-time' are often decisive factors in successful business."

THE MANAGEMENT CONSULTANT

Like Hamid, another interviewee we spoke to, CEO of a prominent global professional services firm active in Iran, highlights the potential up-sides and pitfalls for companies looking to enter the promising Iranian market. He says, "We are advising clients not to get side-swiped by the initial hype, and to recognise that some caution is needed until it becomes clear how, when and by whom Iran's frozen assets will emerge back into circulation. Ownership structures, intermeshed with historical relationships amongst key stakeholders, are extremely complex and lack transparency – researching, investigating and choosing the right partner or adviser is crucial. It may well suit many businesses to initially set up operations in Dubai for example, and use this as a springboard into Iran until solid business partners are found, and the Western banks become a little less cautious of being first-movers."

He is very enthusiastic though about the opportunities for Iran itself and other committed Western manufacturers and service providers as the government courts FDI and technology transfer from abroad, with the objective of establishing Iran as the low cost manufacturing centre for the Middle East, "there is indeed a huge opportunity, but the same issues will remain around the quality of the supply chain services, raw materials and manufacturing processes which have not advanced fast enough during the period of sanctions. Organisations must also protect their IP and technology, particularly if entering into a JV or other type of partnership."

THE SENIOR COMMERCIAL ADVISER

A different interviewee, who is currently acting as a Senior Commercial Adviser on behalf of a foreign government with interests in Iran, again highlighted the countries' likely emergence as a low-cost manufacturing hub for MENA. He believes that, "Iran is rich in raw materials, people and energy. There is a mature but technologically underdeveloped local manufacturing base that forms a solid foundation for growth. Foreign governments are actively competing to ensure a 'slice of the action' for their respective MNC players, and Iran is creating a very favourable environment for increased FDI and sustainable business initiatives via tax relief and very relaxed partnering regulations. Despite favourable Unionisation conditions and relaxed requirements towards joint ownership and partnerships, today Iran ranks 118 out of 190 in the World Bank Group's 'Ease of doing business rankings'. The lifting of sanctions and recent elections and political changes will indeed encourage a more liberal approach to economic reform and business regulations."

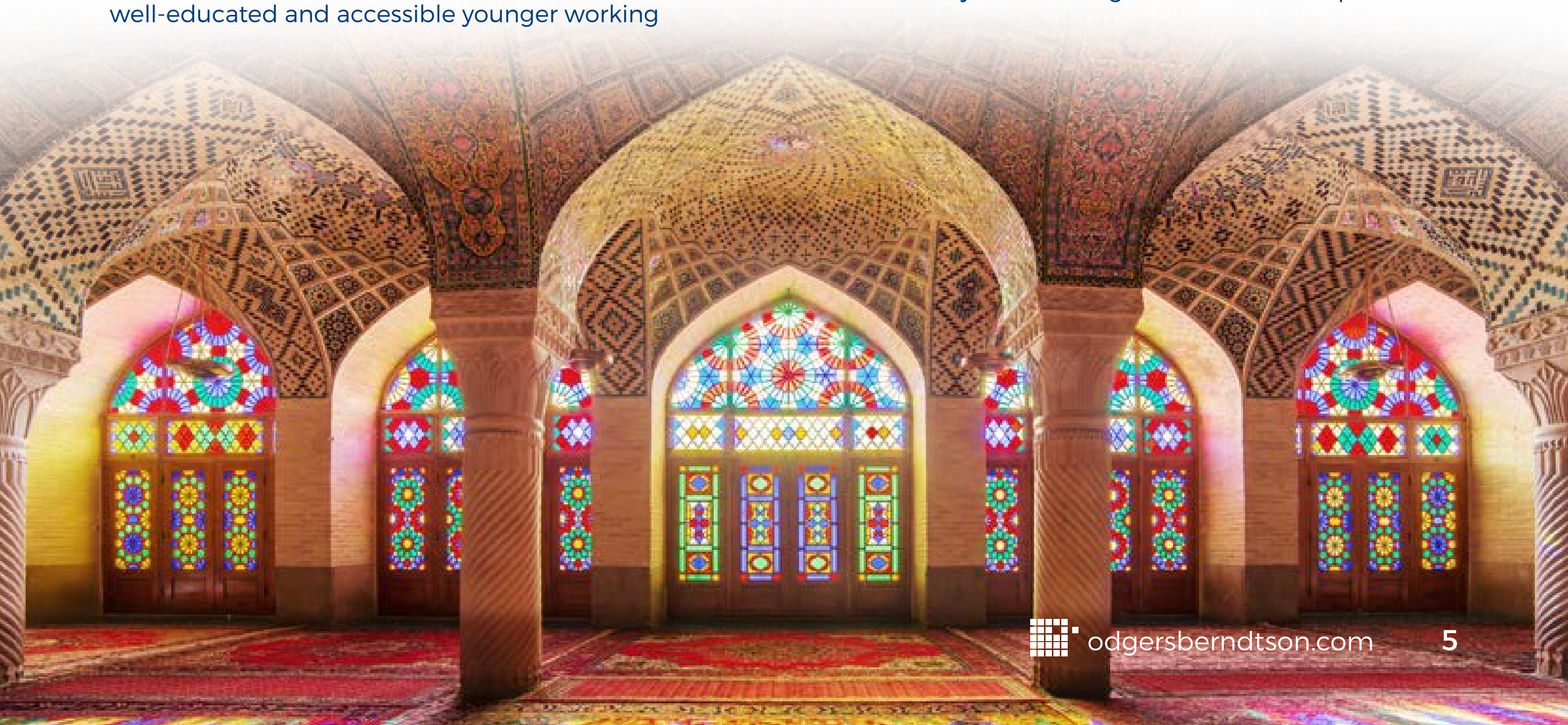
He continues, "Human Resources considerations, especially finding and retaining talent, are pivotal to success in Iran. It may well be difficult to find the ideal managers to champion these new ventures or to form these partnerships. The existing Iranian management will want to see new leaders that understand Iran's cultural nuances and manage in a robust fashion whilst being people-focused and able to develop teams. New managers will need to show commitment to Iran, not simply operate on a commuting basis, establishing trust and speaking the same language. English is just not widely spoken in Iranian executive leadership teams, and relying on an interpreter is fraught with potential issues for many. There is no clear, mature and sustainable talent pool for C and C-1 level executives in Iran and so, organisations will also have to tap the pockets of Iranian specialists and experienced managers currently living abroad but willing to return to their roots."

Furthermore, "Iran has very high job mobility. The younger middle-managers jump roles quickly and often simply for better pay and titles, so retention is key. These ambitious individuals, especially those with good English language skills and stronger vocational degree qualifications, want to work for best-in-class, respected employer brands where there is a visible way forward career-wise, with no glass-ceiling created by the long-serving senior managers."

THE MNC BOARD DIRECTOR

Our final interviewee, an Iranian-born and Western educated board member of a leading MNC with manufacturing and sales operations in Iran, provides some candid commentary on these experiences, "At face value, Iran has a rich talent pool. There is a huge, well-educated and accessible younger working population who are eager to learn, with open and eyes and ears. However, many of them have been raised in an environment with often limited freedom of action, and this factor also affects behaviours in the work place – for some there is a tendency to try to cut corners and to bypass procedures in an attempt to achieve the aim quickly and without restriction. The absence of any significant level of FDI in recent years has left the bulk of organisations ignorant to what best-practice across all functions of a business really looks like. The upcoming challenge facing employers and their staff alike in achieving a transformation of work practices and culture is huge."

He therefore believes that 'tapping Iran's diaspora' to identify and attract robust and experienced leaders back to Iran will be pivotal to ensuring successful business transformation and success in this evolving period of new business growth. He says, "the majority of Iran's top-tier management have historically adopted a very authoritarian management approach that has not allowed executive leadership teams much room-for-manoeuvre. Such executives have also had limited exposure to rapid business growth and the associated ramp-up of systems and procedures required to allow an organisation to flourish when more capacity is required. Organisations may well need to look abroad to find suitable leaders who can bridge the cultural gap between Iran's traditional business practices and those found in more developed, mature markets. In a country where trust and relationships are vastly important, and where a strong yet culturally sensitive leadership style is required, the selection criteria will need to be very tight and without compromise, also appreciating that what works in Tehran may not work in Tabriz, Shiraz, or elsewhere across the diverse Iranian landscape, where around twenty different regional dialects are spoken."



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CONCLUSIONS AND CONSIDERATIONS

The consensus of opinion of those executives that we have interviewed, combined with key advice given by the myriad of professional services organisations and independent consultants focused on Iran market-entry for their clients, tells us that it is crucial to ensure deep due diligence across all external factors/stakeholders relating to business planning for Iran. It is imperative to take the time and professional advice to truly know your customer, potential partner, key vendors and other influential external stakeholders. Such knowledge will ensure that your business can flourish in this culturally complex, bureaucratic and opaque re-emerging market, where business had previously been done largely through personal relationships, and often under the patronage of Iran's security services.

As part of a market-entry strategy for Iran, thorough and comprehensive Human Capital due diligence is also required. Business leaders will need to quickly understand the inherent capabilities, skill-gaps and scalability of the management that they look to recruit, inherit or integrate as part of any joint or new venture. The importance of historical internal and external working relationships cannot be ignored but, at the same time, it cannot take precedence over the need for complete transparency and ethical business practices, aligned to the values and practices of the parent company. It is acknowledged that simply 'importing' managerial talent in the early stages will be expensive, may well set the wrong precedent to encourage local staff development and retention, whilst also being simply impractical in terms of cultural integration and language restrictions. With such a large, ambitious and well-educated talent pool already existing in Iran, middle-management recruiters would do well to focus on identifying, attracting, developing and retaining individuals who show the potential to adjust to new, progressive working practices.

However, when organisations ponder their senior leadership choices and organisation structure for their new or re-vitalised Iran entity, the solution is more complex. Today, as more clarity gradually emerges around the ease of doing business in Iran, many organisations choose to base their Iran top management outside of Iran as the planning, due diligence and commercial framework for market-entry evolves. Tehran, for example, is not an easy place to live in. Infrastructure and lines of communication are under-developed and pollution levels are dangerously high. Consequently, in the short term, having the country leadership team working on a rotation-basis into Iran may work well. But, once the commercial groundwork is complete and the entity is up and running, the leader needs to be on the ground, highly-visible and leading the way in developing relationships with key stakeholders.

The newly appointed leaders of Iran's re-emerging commercial entities will need to immediately exude a tangible sense of credibility, gravitas and a cultural affinity to both external and internal stakeholders. Such leaders will need experience of driving success in emerging markets, managing business process optimisation and transformation in a multi-cultural, challenging environment, whilst ensuring absolute integrity at every level of the business. Whether such candidates are identified internally for secondment to Iran, externally from the Iran's existing internal talent pool, or from within the over 5 million members of the Iranian diaspora abroad, the requirement for sound Human Capital due diligence is real and essential.

ABOUT ODGERS BERNDTSON

Odgers Berndtson is one of the leading, international executive search and leadership assessment firms. Our reputation for excellence and integrity has been established over 50 years. We act as trusted advisors to clients who need help recruiting for important positions and assessing the development needs of their top talent.

A truly global brand, Odgers Berndtson delivers worldwide executive search and leadership assessment solutions from more than 50 offices in 30 countries.

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