



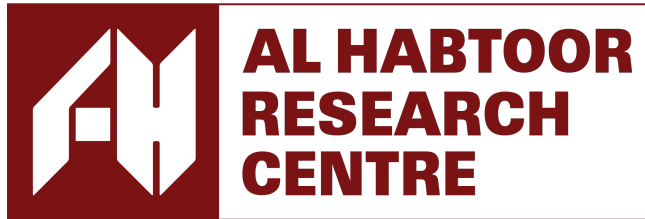
PART THREE

The Regional Proxy Dilemma:

Diverging Perspectives and
Their Implications for the
Settlement Process

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Dr. Azza Hashem

Managing Director

Prepared by

Mostafa Ahmed

Head of Political and Security Studies

Farah Aburaya

Political and Security Studies Researcher

Designed by

Abdelazem Mohamed

Senior Graphic Designer

ANALYTICAL SERIES

Negotiation Deadlocks: How Washington and Tehran Navigate the Tug-of-War Across Every Issue?

This analytical series examines the deep transformations unfolding behind the scenes of US–Iran negotiations, using the "Sixty-Day Agreement" as its point of departure to unpack some of the most complex and contentious files. Rather than merely offering a conventional narrative of events, this analysis probes the strategic roots of the crisis to examine how these disputes are reshaping the global balance of power. Tracing the network of actors and key influencers across both the domestic and external arenas reveals the hidden mechanisms of confrontation and negotiation that drive the strategic game. In doing so, it seeks to anticipate the potentially decisive consequences of the technical negotiations currently underway in Switzerland. These consequences are likely to shape the contours of regional and international security in the period ahead.

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Negotiations between Washington and Tehran are entering an increasingly complex strategic juncture, with most of the 60-day timeframe established under the "Islamabad Truce" having elapsed without a decisive agreement. This has been accompanied by renewed hostilities and the Strait of Hormuz once again closing to international shipping.

These developments on the ground coincide with intensive international diplomatic efforts to contain the repercussions of an open military conflict that has clearly weighed on regional and global economic growth.

At the heart of this negotiating landscape is the conspicuous absence of the regional proxy issue from both the draft preliminary agreement and the current talks. Rather than signalling that the issue has been sidelined, this absence raises fundamental questions about the future of the complex network that has for decades formed a central pillar of Iran's deterrence doctrine.

Current political dynamics suggest the proxy issue is no longer a secondary matter that can be deferred or ignored. Instead, it has become a structural fault line that cuts across each side's conception of security and stability, as well as the limits of any viable settlement.

Its exclusion from the initial formulations reflects a clear recognition of how difficult it would be to incorporate the issue without directly confronting red lines at the intersection of Iran's deterrence doctrine, the US vision of regional security, and Israel's efforts to translate military pressure into irreversible negotiating gains.

The dilemma takes on even greater significance in light of recent macroeconomic analyses indicating that the costs of proxy involvement have extended well beyond direct military losses, striking at the heart of the global economy. Proxy-related operations along critical maritime corridors, particularly in the Red Sea, have severely disrupted supply chains and inflicted tens of billions of dollars in losses on international trade through unprecedented surges in shipping and insurance costs. They have also created unconventional threats to the security of digital infrastructure, most notably subsea fibre-optic cable networks.

Security experts emphasise that the structural attrition the Axis of Resistance suffered during the intense confrontations of 2024 and 2025 prompted Tehran's leadership to reassess its tactics and instruments, but not to abandon them.

The crisis stems from a fundamental divergence in the actors' perspectives. Iran regards its network of proxies as a forward line of defence and an integral component of its national security, integrating these groups with its missile and drone capabilities. Washington and Tel Aviv, backed by regional powers, by contrast, view dismantling and disarming these groups as a mandatory precondition for any new regional security architecture.

This reality places the proxy issue at a critical intersection between three complex levels: Iran's pursuit of strategic depth for its defence; US efforts to neutralise sources of asymmetric threat; and regional and international concerns that link market stability and freedom of navigation to ending the activities of these groups around maritime chokepoints and in the Eastern Mediterranean. Any settlement that fails to define the place and functions of these proxies would therefore amount to little more than a fragile truce vulnerable to rapid erosion.

This section examines the divergent perspectives of the key actors on the regional proxy crisis. It assesses how these competing positions may clash or converge behind closed doors at the negotiating table. The paper asks a central question: will these discussions translate into strategic trade-offs that underpin a comprehensive and sustainable settlement, or will divergence between the parties' red lines reduce the anticipated agreement to little more than a temporary tactical freeze before an even more violent round of conflict?

Iran's Perspective: Proxies between Deterrence Doctrine and Cost Considerations

Iran's military and security doctrine is structurally rooted in the principle of Forward Defence, or what strategic literature conceptualises as Defence in Depth. This military philosophy seeks to shift confrontation to theatres beyond Iran's borders, dispersing adversaries' offensive capabilities and creating invisible buffer zones that insulate the Iranian homeland from external threats.

Non-state actors, from Hezbollah in Lebanon and resistance factions in Iraq and Syria to the Houthi movement in Yemen, form the backbone and operational arm of this strategy. Decision-making circles in Tehran do not regard these armed groups as tactical bargaining chips that can be traded for short-term economic gains. Rather, they view them as the first vital line of defence for regime survival and as a strategic investment on which Iran has spent billions of dollars over decades to secure an asymmetric military advantage in the region.

This view is even more firmly entrenched within the Islamic Revolutionary Guard Corps and the Quds Force, where any US or Israeli attempt to dismantle or disarm these networks is regarded as a direct existential threat and an assault on the foundations of national security, placing the issue firmly beyond the scope of negotiation.

This reality was further underscored by the profound political changes within Iran's leadership in July 2026, following the official funeral of Supreme Leader Ali Khamenei and the succession of Mojtaba Khamenei as the country's new Supreme Leader.

In his first official address, Mojtaba Khamenei delivered an unequivocal message endorsing the armed resistance of the Revolutionary Guard militias and stressing that revenge was a demand of the Iranian people.

These uncompromising directives immediately foreclosed the prospect of concessions at the negotiating table, effectively removing the proxy issue from the understandings set out in the Islamabad Memorandum and rendering those understandings null and void. Iranian foreign policy thus became fully aligned with the defence establishment's hard-line position, underscoring that Tehran's ties to its proxies constitute a deeply entrenched doctrinal and ideological bond, resistant to political shifts or economic inducements.

Iran's evolving approach has moved beyond the conventional frameworks that prevailed before the Gaza war, with its proxy network undergoing a comprehensive restructuring that has taken it beyond the confines of traditional strategies.

Field-level military assessments indicate that Tehran no longer relies solely on the model of Deterrence by Denial, which previously centred on tying down its adversaries by opening multiple fronts simultaneously. Instead, it has shifted toward a highly complex hybrid model.

This new model directly integrates the capabilities of armed factions into Iran's centralised military systems, including precision ballistic missile technology, loitering munitions, and reconnaissance and early-warning systems.

Transformations of Iran's Proxy Network (1979-2026)

Phase	Strategic Logic	Key Features
Phase One: Horizontal Expansion through Proxies (1979-2010s)	Building a regional network of influence	Revolutionary ideology, establishing proxies, Low-cost deterrence, conflict management through proxies, Expansion of regional influence.
Phase Two: Network Consolidation (2010-2023)	Institutionalising the "Axis of Resistance"	Unification of fronts, governance of militias, integrated financing, cross-border supply networks, Deterrence through proxies.
Phase Three: Structural Erosion (7 October 2023-2025)	Declining effectiveness of the proxy system	Military attrition, financial pressure, intelligence penetrations, elimination of leadership figures, erosion of legitimacy, Fragmentation of networks.
Phase Four: Strategic Transformation (2026-)	Restructuring instruments of influence	Security vacuums, fragmentation of alliances, pressure on the Iranian state, Competition over governance, Structural restructuring of the proxy model.

Table: Al Habtoor Research Centre • Source: Belfer Center for Science and International Affairs • Created with Datawrapper

This evolution reflects a fundamental redefinition of the proxies' role, transforming them from relatively autonomous forces of deterrence and denial into critical nodes within an integrated operational network spanning multiple theatres. Their primary function is now to sustain long-term attrition, disperse Western defensive capabilities, and contain adversaries' firepower through effective, real-time coordination.

Iran's military leadership has also adopted an advanced strategy designed to ensure the sustained flow of arms to this network while shielding it from the effects of crippling Western sanctions and pre-emptive air strikes targeting traditional supply lines.

This strategy marks a fundamental shift away from direct logistical transfers, which have proved vulnerable to maritime and aerial interdiction, toward decentralised manufacturing and, ultimately, Fabrication at the Tactical Edge.

This approach relies on providing proxies with advanced technologies that integrate guidance algorithms and 3D printing capabilities, enabling them to produce weapons components, assemble drones, and manufacture munitions locally within the relevant theatres of operation.

Field evidence and international monitoring indicate that Tehran continues to channel sensitive technical expertise into supporting these alternative systems. In mid-July 2026, Mahan Air reportedly operated a series of intensive flights carrying senior Islamic Revolutionary Guard Corps field commanders and highly sophisticated military equipment to Yemen, to strengthen the Houthis' indigenous manufacturing capabilities and train their personnel to operate new missile and guidance systems. This was clearly demonstrated on 26 July 2026, when the Houthi movement announced that it had shot down a Saudi Bayraktar Akıncı drone while it was conducting military operations in Al-Jawf Governorate in northern Yemen. Such developments pose a complex challenge to US and Israeli efforts to cut off the sources of arms supplies to these factions.

From a strategic perspective, Tehran regards negotiations over its proxy network as fundamentally different from bargaining over the nuclear programme or uranium enrichment levels. The issue touches on the very core of the regime's conception of itself and the legitimacy of the geopolitical project it has pursued since the revolution through:

- **Strategic Red Lines and the Credibility of Regional Influence**

The security elite, particularly within the Islamic Revolutionary Guard Corps, places the proxy network among its "Strategic Taboos", on which it categorically refuses to make any substantive concessions behind closed doors.

This rigidity stems from a deeply held conviction among Iranian decision-makers that any display of flexibility on this issue would be interpreted in Washington and Tel Aviv as an unequivocal sign of weakness and a first step towards dismantling Iran's broader deterrence architecture, including its advanced missile capabilities and drone technology.

Iran's concerns extend beyond the loss of any particular faction or specific sphere of influence to the potential collapse of the credibility of its entire network of influence.

The Iranian leadership recognises that merely accepting, even in principle, the inclusion of Hezbollah, Iraqi factions or the Houthi movement in negotiations would send a disastrous signal to its other allies that Tehran's commitments are open to bargaining under international pressure.

Such a signal would impose substantial strategic costs on Tehran, striking at the core of the ideological loyalty cultivated over decades and pushing local actors to seek greater autonomy to protect themselves. This, in turn, would erode Iran's crucial ability to manage regional crises through relatively low-cost instruments rather than direct military confrontation.

- **Decentralised Restructuring of the Factions**

Iran's leadership is moving swiftly to absorb the structural losses sustained by its regional network in 2024 and 2025, not by abandoning or sidelining these proxies, but by restructuring the network from excessive centralisation to flexible decentralisation.

Tehran is gradually moving away from traditional organisational structures in favour of an operational model that places greater emphasis on local manufacturing, the transfer of tactical know-how, and the expanded battlefield use of low-cost drones, while geographically dispersing supply chains to reduce their vulnerability to air strikes.

This strategy rests on a carefully calibrated calculation that rebuilding the network along these hybrid lines remains far less costly than the existential price of losing its forward deterrence architecture.

Field evidence from the Red Sea theatre demonstrates the effectiveness of this approach, with actors operating outside absolute Iranian command and control proving capable of generating global strategic and economic effects at minimal cost.

World Bank data document more than 300 conflict-related incidents involving the Houthi movement between October 2023 and December 2024, including 201 attacks on commercial vessels. These operations disrupted maritime trade through regional ports, with Jordanian seaborne exports falling by 38 per cent and Omani exports by 28 per cent. At the same time, the Egyptian treasury lost an estimated \$7 billion in Suez Canal revenues in 2024 alone.

These figures demonstrate to Iranian decision-makers that a proxy's value is no longer assessed solely by its organisational discipline or numerical strength, but by its ability to impose asymmetric costs and generate negotiating leverage that shifts the balance in Iran's favour on the international stage.

• **The Cost-Benefit Dilemma**

Iran's senior leadership faces a stark dilemma, requiring it to strike a careful balance between severe domestic macroeconomic pressures and the vital strategic imperatives of regime survival.

The renewal of stringent US sanctions, the revocation of oil export waivers in response to violations of the Islamabad understandings, and the continuation of the maximum pressure campaign have fuelled a dramatic surge in inflation and a rapid erosion of the local currency's value.

These deteriorating economic conditions are generating intense social and political discontent, placing mounting pressure on President Masoud Pezeshkian's government and driving it to seek immediate avenues to ease Iran's financial isolation and recover frozen assets to preserve domestic stability.

The military establishment, particularly the Islamic Revolutionary Guard Corps, which the new Supreme Leader has entrusted with shaping Iran's strategic direction, stands in stark contrast to this economic pragmatism, assessing the cost-benefit equation through an exclusively security-driven lens.

The military elite calculates that the strategic cost of abandoning Iran's proxies would far outweigh any temporary financial gains. Dismantling these networks would deprive the country of its defensive depth and expose its infrastructure to the overwhelming technological and air superiority of the United States and Israel, making economic resistance preferable to geopolitical capitulation.

Tactical freezes and manoeuvring become increasingly attractive options for Tehran when its negotiating calculus accounts for the international community's limited capacity to enforce agreements rigorously.

Any diplomatic agreement to constrain Iran's proxies would therefore remain largely on paper unless it succeeds in restricting formal and informal financial channels, hawala networks, cryptocurrencies and proceeds from oil smuggling, while also dismantling technical support networks and joint cells.

This highly complex enforcement process would require a binding, supportive UN Security Council resolution, along with high-level security and financial coordination among key regional states. The wide gap between diplomatic commitments and effective enforcement also gives Tehran considerable scope to avoid making structural concessions, limiting itself instead to reversible tactical measures such as reducing the overt visibility of its support or temporarily suspending certain activities, while exploiting vulnerabilities in the international financial system to sustain its deterrence network beyond the effective reach of Western monitoring.

The US Perspective: Between the Imperative of Dismantlement and Cutting Off Funding Sources

The US strategic approach, particularly under the Trump administration, rests on a firmly held geopolitical conviction that Iran's regional proxies are not merely a source of tactical disruption or a transient threat. Rather, they constitute the primary structural threat to US strategic interests in the Middle East, Israel's existential security, and freedom of navigation and global trade.

• **Dual Pressures**

The US push to resolve the proxy issue is driven not merely by the imperative to protect its allies, but by a recognition that these networks are now striking at the heart of the global economy by disrupting trade and energy routes.

Repeated attacks on vessels in the Red Sea and Bab el-Mandeb, coupled with risks in the Strait of Hormuz, have sharply increased shipping and insurance costs, forcing many Asia-Europe shipping routes to divert around the Cape of Good Hope. This has lengthened transit times, increased fuel consumption, and placed additional strain on available fleet capacity.

This rerouting has directly driven up freight rates, disrupted supply-chain stability, and injected considerable uncertainty into the 2026 outlook for global shipping companies.

These disruptions have also affected energy markets and the aviation sector. Fears of attacks on infrastructure and tankers have triggered surges in oil prices. At the same time, disruptions to air and maritime corridors have raised fuel, insurance, and transit costs for the aviation industry, affecting both ticket prices and airline profit margins.

This equation is particularly sensitive in the Gulf and the Strait of Hormuz, through which a significant share of raw materials critical to global food supply chains, such as urea and ammonia, are exported. Any prolonged disruption to these routes would therefore pose a structural threat to food security in Africa and Asia by driving up fertiliser and essential commodity prices.

In this broader context, proxy activity has become a direct factor in inflation and the growth outlook of both advanced and emerging economies, placing the US administration under mounting political and economic pressure to constrain or halt the capabilities of these networks to keep the vital arteries of the global economy flowing.

- **Sovereignty Architecture and the Monopoly on the Use of Force**

The US strategy extends beyond imposing terms on Tehran behind closed doors to exerting sustained structural pressure on the central governments in Beirut and Baghdad, aiming to restore the state's legitimate monopoly on the use of force and strip armed factions of their political and operational cover.

In Lebanon, Washington is leveraging its diplomatic and financial weight to press the government to fully and rigorously implement UN Security Council Resolution 1701. It is linking military and logistical assistance packages to the Lebanese Armed Forces, whose cumulative value has exceeded \$3 billion since 2006, alongside additional emergency funding provided more recently, to the military's ability to deploy effectively south of the Litani River and dismantle Hezbollah's infrastructure.

Policymakers in Washington view the arming and funding of the Lebanese Armed Forces (LAF) not as unconditional assistance, but as a strategic instrument for building a domestic counterweight capable of filling the security vacuum and transforming Hezbollah from a regional deterrent force into an isolated domestic organisation subject to the rule of law and the authority of the state.

This stringent approach extends to Iraq, where the US administration is exerting mounting pressure on the government in Baghdad on two fronts: to curb the Popular Mobilisation Forces (PMF) factions and sever their structural ties to Iran's Islamic Revolutionary Guard Corps.

In Iraq, US pressure extends beyond the military sphere to strike directly at the financial system, with the Federal Reserve using financial compliance measures to restrict the Central Bank of Iraq's access to its US dollar reserves.

This coercive mechanism has resulted in sanctions and transaction bans being imposed on more than 14 Iraqi banks found to have been involved in money laundering and the illicit transfer of hard currency to Iran-aligned militias.

Washington is confronting Baghdad with a stark zero-sum choice: either make a serious effort to integrate these factions under the unified command of the regular armed forces and strip them of their financial and military autonomy or face crippling financial isolation that could threaten the collapse of an Iraqi economy wholly dependent on oil revenues denominated in US dollars.

At its core, this US strategy seeks to shift the burden of dismantling Iran's proxies away from direct and costly military confrontation with the United States and towards an internal contest of wills and state-building.

Through this systematic approach, Washington seeks to draw Tehran into a direct war of attrition with the national institutions of the states in which its proxies operate, gradually transforming these proxies from low-cost strategic assets that advance Iranian influence into political and economic liabilities that deepen the vulnerability and isolation of Tehran's local allies while eroding their popular support and constitutional legitimacy.

• **Implementation Challenges**

At the operational and enforcement levels, the United States faces an exceptionally complex challenge in its efforts to impose stringent oversight mechanisms capable of cutting off funding to the Islamic Revolutionary Guard Corps and its proxies.

Iranian networks and their allies have shown remarkable resilience and a strong capacity for rapid adaptation, circumventing the traditional dollar-based financial system and the SWIFT network by increasingly turning to cryptocurrencies and decentralised digital assets as key channels for transferring funds and financing military activities.

Intelligence investigations and blockchain analysis have shown that the IRGC's Quds Force relies heavily on the TRON network to transfer Tether (USDT), a US dollar-pegged stablecoin, exploiting the network's high transaction speeds and low fees to evade detection by the US Treasury Department and the Office of Foreign Assets Control (OFAC), while preserving the currency's value and concealing the identities of those involved in the transactions.

Iran's digital financing mechanisms rely on a complex interplay between modern technology and informal money brokers operating through hawala networks. Financial intermediaries are used to provide digital wallets and facilitate transfers worth tens of millions of dollars to Hezbollah and Houthi leaders. Cryptocurrency exchange platforms operating under humanitarian or commercial fronts are also exploited to channel funding to these factions under the guise of donations, with the funds subsequently integrated into complex money-laundering networks and temporary wallets.

Despite the Israeli authorities' success in freezing millions of dollars and dozens of digital wallets linked to these factions, such efforts remain tactical and limited in impact. The structural obstacle hampering US efforts is the absence of a comprehensive and unified terrorist designation by the UN Security Council covering all of Iran's proxies without exception.

The absence of such an international legal mandate constrains Washington's ability to mobilise a binding global consensus that would compel decentralised platforms, virtual asset service providers (VASPs), and major technology companies worldwide to comply and freeze these assets swiftly and effectively. Tehran has adeptly exploited this legal vacuum to move hundreds of millions of dollars with considerable ease to finance its regional military apparatus.

The Israeli Perspective: Between Military Degradation and Tactical Exploitation

Israel's security and political establishment views the regional proxy issue as the core of the direct existential threat it faces and categorically rejects any path towards de-escalation that does not lead to the degradation of Hezbollah's military infrastructure and that of the other components of the "Axis of Resistance".

Tel Aviv regards the current negotiations between Washington and Tehran as little more than a tactical respite in a protracted conflict unless they are accompanied by the structural dismantling of these factions' capabilities and the removal of Iran's forward-deployed proxies from its strategic arsenal.

- **Absolute Rejection of Partial De-escalation and the Imperative of Disarmament**

Israel's perspective is rooted in a strategic assessment that places Hezbollah at the top of the list of imminent existential threats on its northern front, not only because of its vast arsenal, but also because it represents the most successful and tangible embodiment of Iran's Forward Defence doctrine.

Israeli and Western intelligence and research circles estimate that Hezbollah possesses tens of thousands of missiles and rockets, as well as hundreds of precision-guided missiles capable of disabling strategic and sensitive targets deep inside Israel.

In Iran's strategic calculus, this advanced arsenal represents its most important insurance policy against any military campaign targeting Iranian territory. On this basis, Tel Aviv rejects any diplomatic formula that would leave the arsenal intact while imposing only nominal restrictions or a temporary suspension of operations.

Israel's military leadership views Hezbollah's continued possession of arms as subjecting Israel to a state of "Permanent Security Blackmail". Experts in this context argue that diplomacy alone cannot eliminate the threat, making it necessary to consolidate operational successes and targeted killings through fundamental structural and legal change that ends this exceptional status and ultimately dismantles the axis.

- **Fracturing the Axis and Severing Its Logistical Lifelines**

The Israeli military establishment has adopted a comprehensive offensive strategy known as "Fracturing the Axis", moving beyond a passive defence doctrine to conduct simultaneous strikes aimed at degrading and disrupting proxy networks across multiple theatres.

Israel exploited the outbreak of what became known as the "Twelve-Day War" in 2025 to carry out direct surgical strikes against ballistic missile programmes inside Iran, capitalising on the proxies' tactical retreat and limited response amid domestic pressures and fears of overwhelming US retaliation.

This relative absence reinforced Tel Aviv's conviction that the axis was undergoing unprecedented fragmentation and decline, opening a historic window of opportunity to impose new security parameters.

This strategy is inseparable from the Syrian theatre, which for decades served as Iran's logistical corridor and strategic depth. Israel regards the fall of the Assad regime, and Tehran's resulting loss of control over these routes, as a crippling blow to its supply lines.

Tel Aviv insists that any future regional settlement include decisive provisions and measures to prevent the re-establishment of the supply bridge between Tehran and Beirut through Syria and Iraq, whether by tightening surveillance of air traffic or destroying overland supply routes, thereby denying Hezbollah any opportunity to replenish its depleted arsenal.

- **Leveraging the Negotiating Moment and Imposing Security Annexes**

Israel is leveraging ongoing negotiations and periods of temporary ceasefire to impose hard facts on the ground, using diplomacy to consolidate its military gains. This is clearly reflected in the Security Annex to the anticipated trilateral agreement between Lebanon, Israel and the United States.

This detailed annex sets out a stringent roadmap for disarming irregular armed groups south of the Litani River through the establishment of pilot zones cleared entirely of Hezbollah's military infrastructure and subject to joint US-Israeli verification mechanisms.

The agreement requires the Lebanese Armed Forces to take active steps to disarm these groups in return for a gradual Israeli withdrawal with no fixed timetable, while Tel Aviv retains the right to conduct air strikes or pre-emptive operations deep inside Lebanon whenever it perceives an imminent threat.

This landscape reveals a profound divergence between Israel's logic of "Maximum Military Degradation" and Washington's preference for "Gradual Dismantlement" or "Containment", driven by its desire to preserve the broader negotiating track with Tehran.

This divergence places the proxy issue at the heart of tensions within the Western camp. While the US administration at times seeks to restrain Israel for fear of triggering an all-out regional war and large-scale displacement, the leadership in Tel Aviv views any failure to seize this strategic window to eliminate the proxies' heavy arsenals once and for all as a catastrophic mistake.

This hard-line Israeli position makes the future of any US-Iranian agreement contingent on a dual test: the extent to which Iran is willing to relinquish its proxies in practice, and the extent to which Israel is prepared to accept arrangements that do not guarantee the complete dismantling of the pillars of the threat surrounding it.

The Regional and International Perspective

In the strategic assessments of Arab and regional capitals, the regional proxy dilemma extends well beyond the bilateral conflict between Tehran and Washington or direct confrontation with Tel Aviv. It constitutes a structural threat to the foundations of economic security, freedom of navigation, and the legitimacy of the nation-state across the Middle East.

The Gulf and broader Arab position are rooted in deep concerns over sovereignty and categorically rejects any international arrangements that could legitimise irregular armed factions and entrench their presence as a *fait accompli*.

These concerns are rooted in the bitter experience of the past two decades in countries such as Iraq, Syria, Lebanon and Yemen, where developments have shown that the expansion of these militias has consistently come at the expense of the state's legitimate monopoly on the use of force. These groups have gradually evolved into "states within the state", with parallel sources of funding and their own social welfare networks, while appropriating sovereign decision-making in the service of external agendas.

Gulf strategic circles view these networks as a dual threat. They possess both the capability and the willingness to target critical energy infrastructure, ports and pipelines, while also playing a central role in weakening neighbouring fragile states and turning them into open arenas for proxy conflict, creating persistent belts of instability around the Arabian Gulf and the Red Sea.

Accordingly, regional capitals are pressing for any US-Iranian agreement to incorporate stringent guarantees preventing Arab territories from being used as forward operating platforms for the IRGC and prohibiting the reconstitution of these factions under political fronts or new legal designations, with the aim of ensuring their compulsory and gradual integration into accountable state institutions.

Vital maritime corridors, foremost among them the Strait of Hormuz and the Red Sea, occupy a central place in shaping regional and international approaches to this issue. The Gulf states depend almost entirely on the Strait of Hormuz to ensure the flow of their oil and gas exports to Asian markets, while the Red Sea-Suez Canal route serves as the principal artery for trade between Asia and Europe.

Macroeconomic data from international financial institutions document the unprecedented disruption caused by Houthi military operations since late 2023. By the end of 2024, shipping traffic through the Bab el-Mandeb Strait and the Suez Canal had fallen by approximately three-quarters, accompanied by a 15 per cent decline in shipping traffic through the Strait of Hormuz as the disruption spilled over into neighbouring maritime corridors.

This dynamic has placed the Gulf states, Egypt and the countries of the Horn of Africa on the front line of a severe global shipping crisis. Egypt's treasury alone suffered an estimated \$7 billion in lost Suez Canal revenues in 2024, equivalent to nearly 5 per cent of the country's GDP, while most Red Sea ports recorded an average decline of 8 per cent in cargo throughput.

These mounting economic pressures have prompted regional states to adopt a dual strategy that combines tactical participation in international maritime coalitions to safeguard freedom of navigation with the accelerated development of alternative logistics routes, including overland corridors linking Gulf ports to the Eastern Mediterranean, thereby reducing their dependence on maritime routes vulnerable to persistent coercion.

International concerns extend beyond surface navigation and trade security to the very backbone of the global digital economy, as the international community closely monitors the growing capacity of proxy groups to threaten transnational infrastructure.

Specialised supply-chain security studies indicate that sustained attacks in the Red Sea region have generated more than 2,300 conflict-related incidents since the onset of the crisis, triggering dramatic surges in shipping costs.

Drewry's World Container Index recorded a sustained increase, settling at levels 141 per cent above those prevailing before the crisis, while freight rates on the critical Shanghai-Rotterdam and Shanghai-Genoa routes surged by 230 per cent. The disruption was not confined to the surface. Its most acute manifestation emerged with the growing involvement of these groups in the cyber-physical security domain.

In this context, the sinking of the *Rubymar* in February 2024 stands out as a watershed event. As the vessel sank and dragged its anchor along the seabed, four of the 15 strategic submarine cables crossing the Red Sea were severed.

Whether accidental or deliberate, this disruption forced internet service providers to reroute 25 per cent of global data traffic between Asia, Europe and the Middle East, disrupting digital financial communications and propelling the proxy issue to the top of Europe's national security agenda amid growing concerns that the persistence of these complex threats could slow economic growth.

Conversely, the Iranian leadership is leveraging geopolitical shifts and the rise of Global South blocs to expand its diplomatic and economic room for manoeuvre, with the aim of cushioning the impact of Western pressure and easing the burden of sanctions imposed on its regional network.

Iran's formal accession to BRICS+ in early 2024 marked the culmination of its "Look East" strategy, with Tehran betting that integration into a bloc comprising major powers such as China, Russia, India and Brazil would provide it with a measure of strategic insulation.

This positioning provides Tehran with vital channels for its oil exports and facilitates intra-bloc trade using local currencies and non-dollar settlement mechanisms, complicating the US Treasury's efforts to trace assets and cut off funding streams to Iran's proxies.

Beyond the economic benefits, Iran enjoys robust political cover within the UN Security Council and multilateral forums through Russian and Chinese support, helping it break through the ring of isolation Washington seeks to impose. Although policymakers in Tehran recognise that these eastern alliances are no complete substitute for integration into the Western financial system, they provide Iranian negotiators with strategic leverage by demonstrating the country's ability to sustain the financing of its regional project and dispelling Washington's belief that it possesses an absolute capacity to strangle the Iranian economy.

Countries across the broader Global South, from Africa to Latin America, view this conflict through a combination of pragmatic and principled lenses. On principle, they reject foreign intervention and proxy wars that drain the resources of nation-states and prolong civil conflicts, while explicitly condemning any threats to shipping lanes and energy carriers.

From a purely pragmatic standpoint, however, they favour keeping their distance from the stringent Western sanction's regime against Tehran, seeking instead to capitalise on economic opportunities, benefit from preferential energy arrangements, and strengthen partnerships within the BRICS framework.

This diplomatic distance maintained by Global South countries gives Iran additional room for manoeuvre but remains conditional and constrained by considerations of economic stability. These emerging powers recognise that continued proxy-warfare tactics and disruption of international waterways will inevitably rebound on their developing economies, which depend fundamentally on the smooth flow of global trade. This places clear limits on how far the international community is prepared to tolerate a deterrence model that imposes such heavy costs on the global economy.

Trajectories of the Proxy Issue in the Negotiations

The current negotiations between Washington and Tehran are moving into an exceptionally complex diplomatic space, crowded with conflicting red lines that push a final settlement further out of reach and steer the parties toward a fragile, reversible truce rather than a sustainable solution.

Behind closed doors, negotiators confront two fundamentally opposed conceptions of security and stability. The United States insists on a comprehensive halt to the financing and arming of Iran's proxies as a non-negotiable cornerstone, viewing the severing of financial and military support to Hezbollah, the Houthis and Iraqi militias as an indispensable prerequisite for safeguarding regional security and the free flow of global trade.

By contrast, the Iranian leadership remains firmly committed to its network of allies as its first line of deterrence and an ideological extension of its geopolitical project, rejecting any attempt to undermine the core of this network, which, in its strategic doctrine, would constitute a direct blow to the regime's legitimacy and national security.

These sharply polarised positions are pushing international and regional mediators to devise deliberately ambiguous formulations, replacing definitive terms such as "dismantlement" with broader expressions such as "regional de-escalation" and "behavioural restraint", thereby enabling each side to sell the agreement domestically without appearing to have compromised its strategic principles.

Against this backdrop of diplomatic deadlock, the contours of potential trade-offs are emerging, laying the groundwork for a pragmatic path based on limited tactical concessions rather than outright victories.

Under severe domestic macroeconomic pressure, Tehran is considering a temporary suspension of operations deemed most provocative by the international community, such as attacks on commercial shipping lanes in the Red Sea and missile strikes against US bases, in exchange for immediate financial gains, including the release of billions of dollars in frozen assets and an easing of crippling restrictions on its banking system and oil exports.

This Iranian pragmatism is matched by US flexibility driven by disruptions to global supply chains and the resulting economic losses. Washington has shown a cautious willingness to accept an "interim settlement" that recalibrates the rules of engagement rather than dismantling the proxies' organisational structures and physical presence.

This approach would entail freezing cross-border attacks and requiring Tehran to halt the supply of game-changing weapons to its allies, such as precision-guided missiles and offensive drones, in return for temporarily tolerating these factions' domestic activities and less sensitive forms of logistical support. In practical terms, this would transform the proxies' weapons from effective instruments of offensive power into largely symbolic arms carried under the banner of resistance.

The dilemma of competing narratives stands out as one of the most complex challenges facing the implementation of any potential agreement, with each side striving to construct a public narrative that justifies entering into a settlement to its allies and domestic constituencies.

Armed factions, foremost among them Hezbollah and the Houthis, are beginning to frame their political discourse around a strategy of "strategic patience", portraying de-escalation and security annexes as a tactical necessity to regroup and rebuild degraded capabilities, rather than as acquiescence to their adversaries' terms or the abandonment of their deterrent arsenal.

The proxies portray any economic gains Tehran secures through sanctions relief as conclusive evidence of the "Axis's" resilience and its refusal to be broken, facilitating renewed ideological and military mobilisation should the understandings subsequently collapse. This duality of narratives places any future agreement under a permanent cloud of doubt, as both the public and the international community recognise that the parties are presenting the truce domestically as a temporary respite to regroup, rather than as a genuine and lasting end to a conflict that has severely strained the region's economies.

The outcome of these fraught negotiations could follow several possible trajectories, confronting the Middle East with highly sensitive and potentially dangerous scenarios. The first envisages a slide towards a "deferred confrontation", in which diplomacy fails to incorporate the proxy issue structurally into the agreement. This would result in an ostensible freezing of the fronts while funding and arms continue to flow covertly, reducing the agreement to little more than a repetition of past arrangements that merely postpones the inevitable eruption until the next regional crisis.

The second trajectory emerges as a scenario of a "fragile settlement", under which the international community succeeds in imposing stringent but partial restrictions on Iran's allies, particularly in sensitive theatres such as the Red Sea and Israel's northern front. This would create a genuine test of Tehran's ability to rein in its proxies and Washington's capacity to activate deterrence mechanisms and automatic sanctions in response to any detected violations, without being drawn into an all-out war.

These competing scenarios underscore that the proxy dilemma extends far beyond a technical provision in a diplomatic agreement. Rather, it represents the clearest manifestation of a profound geopolitical struggle that is redefining the concepts of national security, sovereignty, and freedom of navigation across a rapidly changing region.

In conclusion, an initial assessment of the positions of the various parties reveals that the regional proxy dilemma is not merely an "additional issue" or a secondary item on the negotiating table between Washington and Tehran. Rather, it lies at the very heart of the enduring struggle over how security, sovereignty and influence are defined in the Middle East and across the global economy.

This issue reveals a profound gulf between the strategic perspectives of the parties concerned. Iran views its proxy networks as a vital layer of deterrent depth and an organic extension of its revolutionary and geopolitical project, treating them as a strategic asset that cannot be relinquished or dismantled without incurring an exorbitant cost that would threaten the regime's legitimacy and survival. Tehran therefore consistently favours strategies of "retention and restructuring" over acquiescence to demands for dismantlement.

By stark contrast, the United States views this proxy model as the central structural threat posed by Iranian behaviour, as it gives Tehran an asymmetric capability to strike US forces, threaten allies and disrupt maritime corridors without becoming embroiled in direct conventional warfare.

This reality imposes tangible costs on the global economy through disruptions to shipping and energy security and threats to digital infrastructure, making the "dismantling of these networks and the severing of their resource flows" an indispensable prerequisite for any long-term stability from the US perspective.

This negotiating equation becomes considerably more complex once the Israeli dimension is factored in, with the core dilemma centring on the perception of Hezbollah as the most immediate and existentially threatening danger on Israel's northern front.

The leadership in Tel Aviv believes that any de-escalation agreement that does not culminate in the complete dismantling of Hezbollah's missile infrastructure and the definitive severing of its logistical supply lines from Iran through Syria and Iraq would amount to little more than a tactical pause in a longer and more violent conflict.

This assessment drives Israel to exploit the negotiating moment and temporary ceasefires to establish new and irreversible security realities, such as its insistence on the trilateral security annex in Lebanon, with the aim of converting temporary military gains into permanent arrangements that reshape the balance of deterrence and constrain any efforts to rebuild the proxies' capabilities.

Nevertheless, this offensive strategy carries significant risks. Excessive military escalation and attempts to impose a new reality of "security zones" could trigger a broader regional confrontation, erode international support and add another layer of complexity and strain to coordination between Tel Aviv and Washington.

This complexity extends beyond the bilateral and regional dimensions to become an international concern centred on economic and maritime security. The Gulf states, Egypt and the countries of the Red Sea basin view the persistence of the armed-militia model as an existential threat to energy corridors, freedom of trade and the legitimacy of the nation-state, and are pressing diplomatically for stringent guarantees to prevent these factions from being legitimised or Arab territories from being used as forward operating platforms for the IRGC.

These concerns converge with broader European and international anxieties over the substantial economic costs of Houthi attacks and proxy activities, as well as their damaging effects on energy prices and the security of submarine cables. From this perspective, safeguarding trade and data flows is an integral part of any comprehensive solution to the proxy issue.

In an attempt to break through this multifaceted pressure, Iran is manoeuvring by leveraging its membership in groupings of emerging powers, such as BRICS and the Shanghai Cooperation Organisation, seeking to turn them into a measure of strategic insulation and diplomatic backing that enables it to sustain its regional project and absorb the impact of Western sanctions.

These conflicting visions at the negotiating table underscore that the dispute extends far beyond technical details, reflecting a profound clash between the underlying strategic logics of the parties: Iran's logic of "retention and restructuring" collides with the US approach of "dismantlement and cutting off funding streams", while both confront Israel's logic of "maximum military degradation", all against the backdrop of mounting regional and international pressure to safeguard economic stability and freedom of navigation.

Accordingly, a strategic consensus is emerging that the most far-reaching settlement realistically attainable would amount to no more than a "fragile and interim" arrangement, centred on a partial freeze of proxy activities and a recalibration of their rules of engagement, in return for giving Tehran some breathing space through economic and diplomatic gains, without fundamentally altering the proxy model itself.

Such a reversible truce would remain little more than an instrument for each side to advance its domestic narrative, rather than a decisive endpoint to the conflict.

Ultimately, any agreement reached in this complex landscape will test the international system's ability to rein in non-state actors and safeguard the vital arteries of the global economy. It will not, however, provide a definitive solution to the proxy dilemma, which will undoubtedly remain the principal and most dangerous driver of stability and instability in the Middle East for decades to come.

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