Russia Sanctions: Diving into the Details

Elina Ribakova
IIF

14. April 2022
Markus Brunnermeier
On Russian Sanctions: Earlier webinars

- Sergei Guriev
  Russian Macroeconomy

- Jim Hamilton
  Oil shocks

- Baqee-Moll:
  Impact on Germany
Sanctions

- Trade sanctions
  - Export control (technology)
  - Import restrictions (coal, oil, natural gas)

- Financial sanctions
  - Activities: capital account restrictions
  - Holdings: Freezing of reserves
  - Forced currency conversion

- Individual
  - How to target?
  - Travel restrictions, …
Resilience and Sanctions

- Offensive: sustain sanctions
- Defensive: withstand others’ sanctions
  - Prepare: build-up reserves, autarky
  - React, agility/flexibility
Resilience and Sanctions

- Offensive: sustain sanctions
- Defensive: withstand others’ sanctions
- Secondary sanctions on

Europe ➔ Russia ➔ Middle East ➔ China
Resilience and Sanctions

- Offensive: sustain sanctions
- Defensive: withstand others’ sanctions
- Secondary sanctions on
  - China
  - Shipping
  - Payment

Map showing regions:
- Europe
- Russia
- Middle East
- China
Why does Russia want to pay in Ruble instead of Dollar/Ruble?
- Let energy importers swap currency
- Easier to follow pay trail

Why doesn’t Russia want to default on $-debt, while US wants Russia to (even to US banks)?
- Downgrade of Russia has many implications
- Existing debt becomes illiquid
- Difficult to issue new debt (even after conflict)

Role of Cryptoassets (Bitcoin et al.)
Sanctions and International Monetary System

- Freezing of dollar reserves
- VoxEU with Harold James and Jean-Pierre Landau
- No serious alternative currency to US $
  - Crypto, Australian $, commodities, …
  - US improves store of value (medium of exchange)
- Alternative to reserves holdings
  - More frequent imposition of capital controls
  - Hurts globalization
Poll

1. Does Ruble strengthening mean sanctions are not working?
   a. Yes
   b. No

2. Do you think a full embargo is preferable to a more gradual approach?
   a. Yes
   b. No

3. Would you pay for sanctions on Russia or a stronger EU armament? What fraction of your annual income?
   a. None
   b. 2%
   c. 5%
   d. 10%
   e. 25%
   f. 50%
Russia Sanctions

Markus Brunnermeier
14. April 2022
It is all “geopolitical” now

Putin says Western sanctions are akin to declaration of war

Meet von der Leyen’s ‘geopolitical Commission’

The impact of throwing Russia out of Swift


The United States cannot get grand strategy right if it gets economic policy wrong.
Russia sanctions: are they working?

1. Sanctions are having an impact
2. We focused on financial sanctions since 2014
3. Time to move to smart sanctions on energy?

   • Escrow accounts for payments for Russia's exports
   • Limitations on oil and gas purchases
   • Wavers vs secondary sanctions on countries like China/India
What is Russia: in one chart

Russia: Reserve dynamics
Balance of payments, in $ bn (4q moving sum)

Current account balance
Non-resident FDI
Non-resident portfolio investment
Non-resident other investment
Other flows, net
Reserves (+ = increase)

Source: CBR, IIF
Financial sanctions from 2014 until now

2014
1. Access to capital markets

2022
1. Central bank sanctions
2. Russian banks (incl. SWIFT)
3. Export controls
4. Commodity bans
5. Individuals
6. “Self-sanctioning”

Source: banki.ru, IIF
What happened in 2014?
Russia lost its access to global markets
What did Russia do in response? Built a Fortress

**Pivot away from the USD**

Currency composition of reserve assets, in %

- **EUR**: March 2014 - 40%, December 2021 - 10%
- **USD**: March 2014 - 30%, December 2021 - 20%
- **Gold**: March 2014 - 30%, December 2021 - 15%
- **GBP**: March 2014 - 10%, December 2021 - 5%
- **CNY**: March 2014 - 5%, December 2021 - 10%
- **Other**: March 2014 - 5%, December 2021 - 15%

*Source: Central Bank of Russia, IIF*

**Nearly complete divestment from UST**

Total U.S. Treasury holdings by Russian residents/entities, in $ bn

*Source: U.S. Treasury Department, IIF*
Are sanctions having an impact?

**Russia’s economy to contract by 15% in 2022**

Contributions to change in real GDP, in pp (q/q (sa) and y/y, respectively)

Source: Rosstat, IIF

**Inflation has picked up sharply**

Inflation and policy rate

Source: CBR, Rosstat, Eurostat, IIF

Inflation has picked up sharply.
However, Ruble has strengthened...

### Ruble back to pre-war levels

- **Exchange rate, in RUB/$**
- **Source:** Haver, IIF

### With shallow market liquidity

- **CBR FX market turnover, RUB to $/€, in $ bn**
- **w/ residents, spot**
- **w/ residents, swap**
- **Source:** CBR, IIF

**Key Events:**
- **Feb. 21:** Recognition of separatist rep.
- **Feb. 24:** Invasion
- **Feb. 26-28:** Sanctions
... and financial system is stabilizing

**Bank runs following sanctions**

Banking system structural liquidity surplus, in RUB bn

30-day moving average

**Drop starting Feb. 28**

**Source:** CBR, IIF

**Skilled CBR response**

Composition of the banking system’s structural liquidity surplus, in RUB bn

- Claims on CBR, standing facilities
- Claims on CBR, deposits, auction-based operations
- Liabilities to CBR, auction-based operations
- Liabilities to CBR, standing facilities, secured loans
- Liabilities to CBR, standing facilities, REPOs/FX swaps
- Non-stand. monetary pol. instruments

**Source:** CBR, IIF

*7-day moving average*
What is happening? FX from CA is flowing in

1. Exporters are required to surrender 80% of their export proceeds
2. Banking system, oil, and gas sectors are dominated by SOEs
3. Gas used for geopolitical objectives
4. Energy for Rubles via Gazprombank
Ruble payments for gas proposal

Transactions executed by Gazprombank

Buyer’s Remitting Account (EUR) → EUR → Buyer’s Special K Account (EUR)

Buyer’s Special K Account (EUR) → EUR → Moscow Exchange MICEX-RTS → RUB → Buyer’s Special K Account (RUB)

Buyer’s Special K Account (RUB) → RUB → Seller’s Receiving Account (RUB)

Source: The Bank of Russia
https://cbr.ru/press/event/?id=12782
Sanctions have to address current account

Historically high current accounts

Composition of current account, in $ bn

Oil and gas exports
Other goods exports
Goods imports
Services bal.
Income & transf. bal.
Current account bal.

Source: CBR, IIF

Driven by commodities

Composition of exports (2017-21)

Crude oil
Petroleum products
Natural gas
Ferrous metals
Coal
Wheat
Wood
Aluminum
Copper
Nickel
Other

Source: Federal Customs Service, IIF
Which countries buy Russian energy?

**Largest trade partners**

Composition of exports (2017-21)
- Netherlands
- Germany
- Other EU
- Japan
- United States
- United Kingdom
- Belarus
- Turkey
- China
- Other

**Source:** Federal Customs Service, IIF

**Purchases of oil and gas**

Imports of Russian energy by EU, UK, and US (volumes & shares of respective Russian exports)

- Oil & petr. products, in tn th
- Natural gas, in bcm
- Oil & petr. products, in % (rhs)
- Natural gas, in % (rhs)

**Source:** CBR, EIA, Eurostat, IIF
The EU most reliant on Russian energy

**Russian imports critical for EU**

- EU27 imports of Russian oil and natural gas
- Oil & petr. products, volume, in toe mn
- Natural gas, volume, in toe mn
- Oil & petr. products, share of total, in % (rhs)
- Natural gas, share of total, in % (rhs)

**Source:** Eurostat, IIF

**Gas supply is less diversified**

- Share of energy imports accounted for by Russia, in % (2016-20 avg.)

**Higher share for**
- Natural gas
- Oil & petr. products

**Source:** Eurostat, IIF
Including due to lack of LNG infrastructure

Source: Entsog, IIF

LNG terminals have capacity

<table>
<thead>
<tr>
<th>Country</th>
<th>LNG import capacity, in bcm/year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Spain</td>
<td>60</td>
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<tr>
<td>UK</td>
<td>40</td>
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<td>France</td>
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<td>Italy</td>
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<td>Belgium</td>
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<td>Lithuania</td>
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<td>Croatia</td>
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</tbody>
</table>

Source: Entsog, IIF

But geographical distribution is challenge

European LNG import terminals

Source: Entsog, IIF
Oil is much more important for Russia’s BOP.

Source: CBR, IIF

But price dynamics may change that.

Source: Haver, IIF
## Oil scenarios for bop

<table>
<thead>
<tr>
<th>Brent oil price, in $/bbl</th>
<th>Change in value of oil and petroleum product exports (2022 vs. 2021), in $ bn</th>
</tr>
</thead>
<tbody>
<tr>
<td>50</td>
<td>0%  5%  10%  20%  30%  40%  50%  60%  70%  80%</td>
</tr>
<tr>
<td>75</td>
<td>-113  -117  -120  -127</td>
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<tr>
<td>100</td>
<td>-47  -54  -60  -73  -87</td>
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<td>193  140  86  33  -20  -73</td>
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</table>

Notes: Urals discount assumed to be $25/bbl.
Oil and gas critical for the budget

1. Oil and gas account for ~ 40% of federal budget revenues
2. Non-oil budget has been consistently in deficit
3. Extraction tax has become more important vs. export duties
4. Other sources of revenues could contract sharply as well
Oil and gas are important sources of revenue

**Oil and gas revenues are significant**

Federal budget oil and gas revenue, in % GDP

- Oil and gas revenue, in % total revenue
- Mining and quarrying taxes
- Export duties

Source: Ministry of Finance, Rosstat, IIF

**Non-oil balance is in large deficits**

Federal government balance, in % GDP

- Overall balance
- Non-oil/gas balance

Source: Federal Treasury, Ministry of Finance, IIF
Oil is also more important for the budget

**Oil is more important for revenues**

- Federal government revenue
  - Total revenue, in RUB bn (3mma, SA)
  - Share of oil revenue, in % (rhs, 3mma)
  - Share of gas revenue, in % (rhs, 3mma)

**Consolidated vs. federal budget**

- Consolidated government revenue and expenditure (2021), in RUB bn
  (frames = federal government)

Source: Federal Treasury, Ministry of Finance, IIF
Other revenues will fall substantially

Source: Federal Treasury, IIF
# Oil scenarios for the budget

## Change in fiscal revenues, in % 2021 GDP

<table>
<thead>
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<th>Brent oil price, in $/bbl</th>
<th>75 RUB/$</th>
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<th>5%</th>
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<th>20%</th>
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Notes: Urals discount assumed to be $25/bbl.

## Change in fiscal revenues, in % 2021 GDP

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Domestic financial system is not very deep

Banking system is of medium depth

Banking system assets (2020), in % GDP

Source: Haver, IIF

Banks are financing most of the deficit

Banks' OFZ holdings, in RUB bn
- Banks' OFZ holdings, in % total (rhs)
- Banks' OFZ holdings, in % total assets (rhs)

Source: CBR, IIF
Can oil be diverted to other countries?

1. Russia’s oil infrastructure is geared towards the West
2. Pipeline to China does not have adequate capacity to divert
3. China and India can be threatened with secondary sanctions (Iran)
4. Some diversion is ok as it would help cushion market impact
China and India import of oil

**EU27**

EU27: crude oil imports (2020), in million tons (lhs) and % of total (rhs)

**China**

China: crude oil imports (2020), in million tons (lhs) and % of total (rhs)

**India**

India: crude oil imports (2020), in million tons (lhs) and % of total (rhs)

Source: BP, IIF
Russia’s oil infrastructure geared towards West

Russian crude oil exports (2020): 260 million tons

- China (83)
- Europe (138)
- Other (39)

~½ via pipeline

~59 mn tons

42% of exp. to Europe

Pipeline cap.: ~100 million tons/year

Source: S&P Global
Counter-sanctions and spillovers

Other commodities could be affected

- Palladium
- Wheat
- Iron (basic forms)
- Vegetable fats/oils
- Barley
- Fertilizers (mineral)
- Nickel
- Coal
- Maize
- Oil/petrol. prod.
- Wood (basic forms)
- Silver/platinum
- Natural gas
- Uranium/thor. ores
- Nickel ores
- Synthetic rubber
- Aluminum
- Copper
- Lead
- Iron ore
- Aluminum ores
- Gold
- Zinc

Share of world imports by product/product group, in %

Source: Unctad, IIF

Correlation with price change

Share of world imports accounted for by BL, RU, and UA vs. price change

- Coal (S. Africa)
- Natural gas (Europe)
- Nickel
- Wheat (avg.)
- Oil/petrol. prod. (Brent)
- Fertilizers (DAP, U.S.)
- Palladium
- Iron ore
- Aluminum
- Silver/platinum (avg.)

Source: Unctad, World Bank, IIF
Sanctions: what happens next?

• Russia’s currency and financial system have stabilized

• Energy exports are the key issue now:
  
  • 1. Escrow accounts for payments for Russian exports (oil products).
  • 2. Limitations on oil and gas purchases.
  • 3. Wavers vs. secondary sanctions on countries like China/India.

• Beware of unintended consequences
References

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