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Major banks and traders react as Russian sanctions mount

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Banks across the world are reviewing all trade and commodities transactions involving Russia as the nation's economy moves into the crosshairs of sanctions enforcers in the US, Asia and Europe.

Governments, including those of the US, UK, EU, Japan, Singapore, South Korea and Australia, have now imposed, or vowed to impose, some form of sanctions on the Russian economy, including against the Central Bank of Russia and **state-owned banking giants** (https://www.gtreview.com/news/global/us-and-europe-unveil-sanctions-targeting-russian-trade-banking/) such as Sberbank and VTB.

Banks – together with less risk-averse commodity traders – are reluctant to enter any new Russian-related transactions, even if they involve companies not subject to sanctions, because they expect further controls if Russia's President Vladimir Putin intensifies his assault on Ukraine, legal and banking sources tell **GTR**.

"There are both actual legal concerns based on what's in place now, but also theoretical concerns based on what may come in the coming days," says Omar Al-Ali, a partner in the energy and resources practice of Reed Smith in Singapore.

"Right now, it's just a moving target," he tells **GTR**. "So there is a risk with doing anything, because you don't know if next week, you might find that the transaction you just signed can no longer operate in the way you thought it was going to operate, because further sanctions have been imposed."

According to trade finance industry figures, reputational damage is a mounting concern for banks, as a steady stream of Western companies abandon Russia amid a groundswell of popular support for Ukraine in the US and Europe.

Contained within the US measures is a provision allowing lenders – including those active in trade finance – to continue conducting short-term transactions of less than 14-days with targeted entities, such as Sberbank and Gazprombank.

"But the question is whether you would actually want to do that; there is a huge reputational risk about financing any Russia-related deals," says Sean Edwards, chairman of the International Trade & Forfaiting Association (ITFA).

Compliance teams at banks, which have grown in recent years as regulators tightened scrutiny of sanctions and anti-money laundering, are working furiously to keep tabs on and interpret new rules and guidance issued by governments, sources say.

The European Bank for Reconstruction and Development yesterday said its board of directors had proposed to suspend access to its financing and expertise by Russia and its ally, Belarus, "open-endedly". The bank's governors have 30 days to vote on the proposal.

A spokesperson for Rabobank tells **GTR** it is "closely monitoring the situation with regard to the Russia-Ukraine conflict" and says its exposure in both Russia and Ukraine is limited.

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Société Générale, ING and Credit Suisse all declined to comment when asked how Western sanctions are impacting their trade finance business.

Citi, which put its Russian retail banking unit up for sale last year, said on February 28 that it "continues to monitor the current Russia-Ukraine geopolitical situation and economic conditions and will mitigate its exposures and risks as appropriate".

Kicked out of Swift

Today, the EU said it would exclude seven Russian banks from Swift, the payment messaging system that underpins global trade, a move widely backed by allies including the US, UK and Canada.

The banks, which will be given 10 days to wind-down their Swift operations, are VTB Bank – Russia's second-largest bank in term of assets held – along with Bank Otrkitie, Novikombank, Promsvyazbank, Bank Rossiya, Sovcombank and VEB.

Omitted from the list are Sberbank and Gazprombank, both of which play a key role in processing payments for Russian oil and gas.

With Russia supplying about 40% of Europe's gas, Germany had previously voiced concern about the measure and warned it could hamper its ability to import gas from Russia. Already, gas prices had reached historic highs on the continent amid a global squeeze in supplies.

When contacted by **GTR**, an EU spokesperson said the banks targeted by today's measure were chosen as they are already subject to sanctions by the EU and other G7 member countries.

Russian Swift users sent and received 278.1 million messages on the platform in 2020, according to Bank of International Settlement (BIS) figures, roughly the same number as Singapore but far fewer than big European economies such as Germany and France.

4.2 million of those were messages sent between financial institutions, known as category two messages. Other categories, such as those for messages relating to documentary credits and guarantees, are not included in the data.

China and Russia have both established alternatives to Belgium-based Swift. Russia moved to set up its SPFS system after the US first threatened to disconnect Russian banks from Swift in response to its annexation of Crimea in 2014. It is mainly used for domestic transactions, although the BIS data show that domestic use of Swift in Russia has more than doubled since 2015.

Commodities impact

While the west has refrained from specifically sanctioning exports of Russian oil, gas and metals, the banks who finance the trade flows of these commodities are increasingly assessing their risk appetite.

As reported by *Bloomberg,* Société Générale and Credit Suisse have halted the financing of Russian commodities entirely, while Dutch lenders ING and Rabobank are restricting support for transactions backing the flow of goods from the region.

ITFA's Edwards says some banks are still financing the flow of Russian goods, including oil and gas, but the picture is "mixed globally".

"A dwindling number of banks globally are issuing import LCs and many are running off existing business," Edwards tells **GTR**. "Lenders are having to be very careful about the source of the goods. As was seen after Crimea, a lot of banks start retrenching to core clients."

For financiers with strong networks in the region, the reputational risk of doing business in Russia is becoming "unbearable", says Jean-François Lambert, founder and managing partner of Lambert Commodities.

"Commodity banks are already significantly diminishing their exposure to Russia," he tells **GTR**. "Eventually they will be in a position where they can no longer finance Russian freight."

Dutch and German lenders are historically some of the most active in Russia's commodities finance sector, he says.

Russian banks have increasingly embraced commodities finance in recent years as European and other lenders reduced their exposure to Russia, with Sberbank and VTB both owning subsidiaries in Switzerland focused on commodities.

Neither responded to requests for comment about the impact of sanctions on their ability to finance commodity transactions.

But in a post on LinkedIn yesterday, Mikhail Ovoshchnikov, head of products at Sberbank Switzerland, wrote: "Wars must never be tolerated and could never be justified. This war should be immediately stopped!"

Western sanctions on Russia are also leading to tough questions for commodity traders active in the region, such as Trafigura and Vitol, which have long-term supply contracts for Russian oil.

Trafigura holds a 10% share in the giant Vostok Arctic oil project, led by Russian company Rosneft, a contract signed in late 2020 to secure millions of barrels of oil for the commodity trader.

As reported by *Reuters*, Vitol agreed to buy 9 million barrels of oil from Rosneft annually as part of a long-term supply contract signed in September. The deal was the first signed between the companies in nearly a decade.

For now, Western governments have not imposed an embargo on Russian oil and gas exports directly. Citing banking sources, the *Financial Times* reports commodity traders will continue to lift Russian crude until they're expressly forbidden.

But there are signs commodity traders could face greater scrutiny from banks over their operations in the region.

"Pretty much everyone is now saying that they don't want to touch Rosneft cargo," a banking source says, because of the energy giant's reported role as a fuel supplier to the Russian military and the prospect that it may soon be subject to sanctions.

Commodity traders offering extended payment terms to certain sanctioned entities could also be ensnared under some US sanctions rules which may apply to trade debt greater than 14 days, Reed Smith's Al-Ali says.

Vitol was not immediately available for comment. But Glencore, another trading giant, said in a statement this week that it has "no operational footprint in Russia" and its trading exposure is "not material".

Trafigura says in a statement that it does not operate any assets in Russia and has no directors or corporate officers in any external Russian entity. The trader adds it has frozen investments in the country, and is "now reviewing the options in respect of our passive shareholding in Vostok Oil in which we have no operational or managerial input".

Navigating shipping sanctions

The impact has also been felt in shipping. The US has slapped sanctions on the entire fleet of shipping company Sovcomflot, which according to maritime intelligence firm Windward owns 229 tankers. The US sanctions on Russian bank PSB also include several vessels owned by the lender.

But as US sanctions also apply to any entity that is at least 50% owned by a sanctioned company, compliance teams are scrambling to ascertain details of the ownership of vessels.

Of the roughly 44,000 tankers and cargo ships operational globally in the last two years, around 2,000 are Russian-owned or Russian-flagged, according to Windward. A banking source says: "It's going to be very, very challenging for banks to determine which vessels they are or aren't allowed to finance."

"Russian vessels belonging to sanctioned actors are likely to avoid visiting EU or US ports in the near term, and we will probably see the beginning of a deceptive AIS [automatic identification system] campaign in short order," David Tannenbaum, a former US sanctions enforcement officer and now director of Blackstone Compliance Services, wrote on LinkedIn. Turning off AIS makes it more difficult for vessels to be tracked.

"We also predict they will use known vessels for intra-Russian trade or offshore storage and will try to charter other ships to move goods," Tannenbaum wrote.

Shipping giants AP Moller-Maersk and MSC have halted all bookings for cargo to and from Russia, except for food, medicine and humanitarian supplies.

A bulk carrier chartered by commodity trader Cargill was hit by a "projectile" on February 24, while waiting to load grain at Odessa, the same day a Moldovan oil tanker was hit and caught fire. Ukraine's maritime authority told *Reuters* yesterday that all the country's Black Sea ports will remain closed "until the end of Russian aggression on our territory".

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