



Russian companies face mounting payment issues as sanctions bite

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Russian President Vladimir Putin is bucking Western efforts to isolate him internationally, meeting with more than 20 world leaders just since May. Russian businesses aren't so lucky.

New US restrictions imposed in June to stem support for the Kremlin's war on Ukraine have put local banks in countries that trade with Russia at a higher risk of so-called secondary penalties, increasingly delaying or disrupting payments to and from places like China and Turkey. That's making it difficult, and sometimes impossible, to execute transactions, particularly with China, arguably Russia's most important economic partner since the start of the 2022 war.

While issues with transferring profits out of another key trading partner, India, have eased from the first years of the war, they haven't been completely resolved because the rupee isn't fully convertible and transacting through third countries is expensive, a person close to Russia's government said, declining to be identified because the information isn't public.

The difficulties threaten to disrupt Russia's trade with economic partners it has relied on since the European Union and the US imposed unprecedented sanctions that significantly diminished business links following the invasion of Ukraine. Trade with China hit a record \$240 billion in 2023.

In June, the US widened the parameters for determining whether to impose secondary sanctions by broadening the definition of Russia's military-industrial base. Imports into Russia from China had started growing again after volumes collapsed when the US initially threatened overseas banks with penalties in December, but the latest move threatens to seriously complicate the situation.

In many cases, transactions with China are only possible through agents in former Soviet republics, said top executives at four commodities exporters, declining to be identified as the information is sensitive. For these deals, foreign currency, including yuan, doesn't end up reaching Russia. While Chinese clients pay in yuan to agents in third countries, exporters often receive rubles in Moscow, people familiar said, noting many intermediary countries have their own restrictions on currency moves.

Cryptocurrency settlements through Hong Kong are also becoming more popular, but even in those cases, Russians are forced to use intermediaries in countries like Uzbekistan or Kazakhstan, two of the exporters and a person involved with crypto payments said. Russian companies have even tried to use barter deals or currency swaps with importers at the same banks, three of the people said.

To be sure, some exporters say they haven't experienced issues executing payments, and at least one major energy exporter has said its yuan-denominated transaction from China this month went smoothly.

While payments with China present the biggest problem for Moscow, Russians have faced similar difficulties in Turkey, people familiar said. The situation there is much less dire because only some banks stopped operations with Russia, they said. Trade with Turkey also is mostly happening in rubles, people said. The share of Turkish exports in rubles grew 50% from January to May, the country's statistics show.

Rupee Accounts

With India, pressure on banks from the threat of sanctions is complicated by the fact that the rupee is not fully convertible. As trade between the countries jumped after Russia invaded Ukraine, Russia accumulated billions of dollars in rupees in India.

To enable Russia to use the accumulated rupees, the Reserve Bank of India came up with rules in July 2022 that said funds can be invested into projects or Indian securities, as well as to adjust for purchases of goods and services at a future date, said officials directly aware of the details. Russia typically buys smartphones and other electronic goods, chemicals and pharmaceuticals, food products, agricultural tools and textiles from India.

The RBI stressed that those investments would be subject to guidelines and limits, indicating it wasn't willing to carve out special rules for Russia. Senior Indian officials have repeated numerous times that India won't do anything to violate Western sanctions. The investments also are subject to lock-in periods and are non-transferable, making it difficult for Russia to liquidate them, people familiar with the rules said.

Following the clarification, the RBI approved at least 34 applications from Russian banks to open accounts in India, and at least nine special "vostro" accounts were opened to facilitate the trade.

Oil, Russia's main export to India, is mostly being paid for with the United Arab Emirates dirham, which is fixed against the US dollar. Still, dollars and euros are also being used, according to people familiar. Those people said some private refiners also use yuan. Russian fertilizer makers and coal producers also prefer convertible currencies and do not trade for rupee, executives at several companies said.

Russia's state-controlled diamond-miner Alrosa PJSC declined to comment on the currency used for their operations in India, and state arms exporter Rosoboronexport didn't immediately respond. The trade with India quite often goes through intermediate countries like the UAE and in currencies other than the rupee, which makes trade costly, a person close to the Russian government said.

'Key Challenge'

"The problem of cross-border payments in 2024 has become a key challenge for Russian business," said Alexander Potavin, an analyst with Finam in Moscow. "In the vast majority of cases, businesses face significant delays in making payments. Now they average about 10-16 days."

Potavin said the Bank of Russia was "now encouraging the use of cryptocurrency" to bypass Western sanctions and facilitate transferring currency abroad.

Payment issues were at the top of the agenda when Putin recently met with Chinese President Xi Jinping, Turkish President Recep Tayyip Erdogan and Indian Prime Minister Narendra Modi. While Russia has made proposals for developing alternative payment methods, they would take time to get up and running.

The effect of all this is yet to be reflected in statistics about exports and imports, but a report on the economic situation in the second quarter from Russia's central bank published July 18 highlights the problem. Imports fell in the second quarter, according to the report, and while the total value of exports rose, physical volumes declined due to restrictions from the West on Russian metals, the report said.

"Difficulties with payments between countries is making the situation worse, primarily with imports," said Natalya Zubarevich, a specialist on Russian regions at Moscow State University. "The consumer market in Russia is getting worse, and will get worse," while imports of components will gradually deteriorate, she said.

“You have to do everything to keep the wheels turning,” even methods that were previously seen as unpopular — like swaps or the use of crypto, Russian central bank First Deputy Governor Vladimir Chistyukhin said at a forum in June.

Without “normal payments” for goods, “it will mean death for our export- and import-dependent country,” he said.



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