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U.S.

U.S., Allies Roll Out Fresh Sanctions on Russia Amid Debate Over How Hard to Hit

Britain pushes for blocking Russia from Swift payment system, while U.S. and Germany resist move

President Biden at the White House, after speaking about the response of the U.S. and its allies to the Russian invasion of Ukraine on Thursday.

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By Ian Talley Follow *and Max Colchester* Follow

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Russia's overnight assault on Ukraine triggered a surge of calls Thursday for Western allies to completely cut Russia off from the global financial system, but fear of collateral damage is quashing the idea for now.

U.K. Prime Minister Boris Johnson, at a virtual meeting of leaders from the Group of Seven largest economies, advocated disconnecting Russia from Swift, the financial-messaging infrastructure that links the world's banks. He joined a chorus of other senior officials, including Ukraine's top officials, the foreign ministers of Estonia, Latvia and Lithuania, and senior U.S. lawmakers.

President Biden joined other allies including Germany and Italy in ruling out the move—at least for now. Instead, the U.S. rolled out fresh sanctions on Russian banks, including two of the country's biggest. Those actions hit 80% of the banking sector, action the U.S. says will cause equivalent pain.

The Biden administration has said that while it isn't something it planned to push, the Swift option is still in its arsenal of possible moves. European Union officials have described it as a last-resort measure. "It would be a huge political lift and have massive ripples," said one U.S. official familiar with the administration's thinking.

The threat of the action is intended to bolster the allies' diplomatic leverage, but some former U.S. Treasury officials say there are a number of reasons why the West is unlikely to press for it.

Chief among them is the potential economic blowback, not just in Europe, but also for the global economy. Cutting off the banking system isn't only about prohibiting cross-border financial transactions: It can essentially sever the entire economy. At an estimated $1.7 trillion last year, Russia's gross domestic product makes it the 12th-largest economy in the world. Even if the global economy weren't hobbled by a two-plus-year pandemic, rising inflation, supply-chain disruptions and escalating East-West political tensions, the potential loss of 2% of global GDP and hobbling of the world's top oil exporter could inflict severe damage to the rest of world.

Some former Treasury officials say cutting Russia off from Swift would likely significantly hit Russia's economy, but also severely harm Western business interests and encourage a shift away from dollar-denominated transactions and Western financial markets. Some economists say China would be a key beneficiary.

Eswar Prasad, the International Monetary Fund's former top China economist and now a professor of trade policy at Cornell University, said any major financial sanctions would facilitate trade with China, the world's second-largest economy, and erode the dollar-dominated global financial system.

Russia and China have been trying to establish their own payment systems as an alternative to the Western-established Swift. While Moscow's version hasn't seen much take-up by banks, Mr. Prasad said, China's Cross-Border Inter-Bank Payments System would allow the two neighboring powers to bypass the Swift system.

That is one of the concerns held by major U.S. banks, whose officials have discussed the matter with the U.S. Treasury Department, according to a person familiar with the matter.

Transactions moving through the Chinese payments system hinders the ability of the U.S. and its allies to monitor transactions, and to therefore disrupt them. It also reduces the need for dollars, because Russia and China's trade can be settled in yuan directly, Mr. Prasad said. Countries often use intermediary currencies such as the dollar to reduce the cost of exchange-rate conversions when trading internationally.

Another reason to avoid using Swift as part of its economic warfare is because there are other weapons that create similar pressure, but with far more flexibility for policy makers.

The so-called blocking sanctions the U.S. and its allies are applying against Russia's largest banks cuts those institutions off from the global financial system. By selecting which banks to block, however, the West has much better control of the flow of international finance, raising or lowering the pressure as officials believe is merited. Such sanctions also raise the cost for the economy, but limit the unintended fallout on allies, especially because governments can carve out exemptions. Western oil companies, for example, could ostensibly be allowed some narrow set of transactions.

Additionally, there are legal constraints on using Swift, a Belgian-based cooperative owned and run by its member banks, as a diplomatic tool. Since Swift operates under European law, getting Russian banks disconnected would be something the bloc of 27 nations would impose, not the U.S., a much more challenging political lift.

Explosions, Airstrikes, Disbelief: Day One of Russia's Attack on Ukraine

Explosions were heard soon after Russian President Vladimir Putin announced a military operation in Ukraine, while inhabitants of Kyiv and other cities rushed to leave

Smoke hung in the air in Kyiv late Thursday, after Russian airstrikes began in the Ukrainian capital and dozens of other cities. VALENTYN OGIRENKO/REUTERS

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U.K. officials have been working on sanctions measures for months. An initial round of Russian restrictions announced earlier this week—which focused on freezing assets of five midsize lenders and three oligarchs—met private criticism from European diplomats for being too weak.

Mr. Johnson convened a group of bankers in Downing Street on Wednesday to pick their brains on how the package could be toughened up. Several people at the meeting said the sanctions package that had been announced so far had very little effect at all, according to people familiar with the meeting.

They discussed banning Russia from raising sovereign debt in Britain among other measures. But during the meeting Mr. Johnson himself raised a more extreme idea: cut off Russia from Swift. After the meeting some executives felt that the prime minister didn't have a clear understanding of how Swift worked or the impact it would have on Russia, according to people there.

A Downing Street spokesperson wasn't immediately available to comment. UK Finance, a finance lobby group, was instructed to pull together a primer on Swift for the government.

Instead of the Swift option, the U.S. Treasury said Thursday it was sanctioning almost 90 Russian financial institutions, including big lenders VTB and Sberbank. It also sanctioned several of President Putin's oligarch allies and expanded bans on new sovereign debt to include a prohibition on trading equity in several of the country's largest companies. The U.S. Commerce Department also unveiled a set of sweeping export controls targeting Russia's defense, aerospace and maritime industries—part of a package of punitive economic measures the Biden administration is imposing.

VTB said it has been and remains a reliable partner for millions of customers, investors and shareholders. "We have had time to learn the lessons and prepare for the most severe scenario," it said. Sberbank said it is closely studying "new working conditions amid the sanctions related to correspondent accounts. The adopted restrictions do not affect the safety and availability of client funds."

The U.K. government also presented a wide-ranging package of new restrictions, saying it would place sanctions on more than 100 Russian entities, and restrict certain high-tech exports. It said it would pass legislation to bar the Russian government and several major state-linked companies from issuing debt in the U.K. In an effort to punish rich Russians, the U.K. said it would limit Russian national's deposits in U.K. banks to £50,000, or about $67,000, and would ban Russian national carrier Aeroflot's aircraft from landing in Britain's airports, which include international hubs like Heathrow.

EU leaders on Thursday agreed to measures that would make it harder for Russians to come to the bloc by scrapping a visa facilitation the country has until now enjoyed. They also agreed to a broad export ban on Russia's aviation sector, including planes, helicopters, spare parts and maintenance which could over time seriously degrade the Russian aviation sector, officials said.

European Union leaders had given the green light to a broad package of sanctions intended to inflict "massive and severe consequences on Russia" on Thursday evening, they said in a statement. They also gave the green light for a new package of economic measures against Belarus.

EU officials hope the sanctions package can be formally approved and published on Friday after the bloc's foreign ministers meet in the afternoon.

The leaders said they had agreed on sanctions on Russia's energy and financial sector, with measures to lock new Russian banks out of international markets. They said there would also be sanctions on the provision of dual-use goods to Russia as well as export control and export financing, and that there would be new targeted listings of Russian individuals.

—Laurence Norman, Dustin Volz, Lindsay Wise and David Benoit contributed to this article.

Write to Ian Talley at ian.talley@wsj.com and Max Colchester at max.colchester@wsj.com

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