

Ukraine – Quick Skirmish or Something More?

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There is much that can be written about the historical and political causes of the war in Ukraine, but this commentary will focus on the potential economic impact. John Mearsheimer gave a good presentation about the causes of conflict in Ukraine at a presentation at the University of Chicago in 2015.

<https://www.youtube.com/watch?v=JrMiSQAGOS4&t=5s>

More recently, Paul Craig Roberts had an interview with Greg Hunter two days before the invasion of Ukraine. In my opinion, it was an objective assessment of the situation in Ukraine. You can view it here: <https://usawatchdog.com/no-shooting-war-in-ukraine-dr-paul-craig-roberts/> Roberts has since posted several updates on his website.

<https://www.paulcraigroberts.org/>

On February 26, the European Commission, France, Germany, Italy, the UK, Canada, and the US announced a joint statement that condemned “Putin’s war of choice” and banned select Russian banks from the SWIFT messaging system (Society of Worldwide Interbank Financial Telecommunication used for international transfers). While the SWIFT ban currently includes seven Russian banks, it excludes its largest bank, Sberbank, and Gazprombank, which are the main conduits for payment for Russian oil and gas.

Economic sanctions against Russia are problematic. Many European countries currently depend on Russia for their natural gas supplies. So far, natural gas supplies to Europe from Russia have continued to flow but if economic sanctions are expanded further or Russia retaliates by withholding exports, a severe recession in Europe is unavoidable. The table below shows the percentage of natural gas supplies for selected countries that come from Russia.

Natural gas is not the only critical export from Russia and Ukraine. According to Gro-Intelligence, Russia and Ukraine collectively produce 14% of global wheat production and 29% of all wheat exports. They also provide one-third of global exports of barley exports and 17% of global corn exports.

The restriction on trade of grains has an impact on other countries as well. Hungary announced that it will ban all grain exports to ensure adequate domestic supplies and to limit the impact of higher prices for its consumers. Bulgaria announced that it would

purchase at least half of three million tonnes of wheat still in its country's silos for its own domestic food supplies.

**Selected European Countries
2020 or latest available**

Country	% of gas supply from Russia
Bosnia and Herzegovina	100
Moldova	100
North Macedonia	100
Finland	94
Latvia	93
Bulgaria	77
Slovakia	70
Croatia	68
Czech Republic	66
Greece	51
Germany	49
Italy	46
Lithuania	41
Poland	40
Hungary	40
Slovenia	40
France	24
Netherlands	11
Romania	10

Source: ZeroHedge, Statista, and European Union Agency for the Cooperation of Energy Regulators

<https://aegis.acer.europa.eu/chest/dataitems/214/view>

Russia is also one of the largest exporters of three major groups of crop fertilizers – nitrogen, phosphorous, and potassium. Fertilizer prices have increased dramatically in the last six months. So, we can expect higher grain prices due to higher costs of production and lower crop yields in many countries.

Steve Erlanger, chief diplomatic correspondent in Europe for the New York Times, reported on March 2 that about 20 countries – most members of NATO and the European Union, are funneling arms into Ukraine to fight Russian military forces and arm an insurgency. How long will Russia tolerate this before it cuts off natural gas exports to many European countries?

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SWIFT is the dominant system used for cross-border payments, but there are alternatives. More than 11,000 financial institutions in 200 countries and territories use SWIFT. After the threat of sanctions in 2014, Russia developed its own financial messaging system, SPFS (System for Transfer of Financial Messages). SPFS had 400 members as of February 2021, including institutions in Germany and Switzerland. China, which has opposed sanctions against Russia, also uses its own system, CIPS (Cross-Border Interbank Payment System).

Reuters has reported that 200 to 300 Russian companies have approached Chinese Banks in Moscow to open new accounts to facilitate international transactions. The news report quoted one Chinese businessman who works with several Russian firms that plan to open accounts denominated in yuan. "It's pretty simple logic. If you cannot use US dollars, or euros, and the US and Europe stop selling you many products, you have no other options but to turn to China. The trend is inevitable."

If you have any questions or comments, please contact me.

Sincerely,
Robert G. Kahl
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