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Russian Banks Exposed in Ukraine's Political Crisis

By The Moscow Times

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Protesters in Kiev are not planning to allow a return to business as normal. **Gleb Garanich**

VIENNA/MOSCOW — The political crisis in Ukraine, sparked by an East-West power struggle in which Moscow has gained the upper hand, is increasing the risk to the country's financial system and creating a particularly acute headache for Russian banks.

As crowds took to the streets to protest after Ukrainian President Viktor Yanukovych rejected a trade and cooperation deal with the European Union last week in favor of closer ties with Russia, Ukraine's rattled central bank, low on reserves, appealed to people not to pull their deposits from the banks.

Ukraine has a "systemic" problem with bad loans, but its interbank money market is functioning normally despite the upheaval of the past week, Russia's state development bank VEB said Wednesday.

Ukraine seems to have little immediate prospect of additional financial help to meet its big external deficits and financing needs, making it even less attractive to the foreign banks that flocked there before the 2008 collapse of Lehman Brothers triggered the worst of the global financial crisis.

While other foreign lenders have cut their Ukraine exposure in the five years since — to 20 percent of Ukraine banking sector assets in 2012 from 40 percent in 2008, according to a Raiffeisen Research survey — Russian banks have maintained a strong market presence, still accounting for 12 percent.

Among foreign banks, the Russians have easily the biggest exposure, more than twice that of Austrian lenders, the next biggest.

In a credit outlook note this week, ratings agency Moody's cited President Vladimir Putin as saying Ukrainian borrowers owed about $28 billion to four Russian banks and named Gazprombank, VEB, Sberbank and VTB as creditors.

"We estimate that these banks' exposure to Ukrainian risk is $20 billion to $30 billion, a sizable amount indeed, considering that their combined Tier 1 capital was $105 billion in June," Moody's said.

Moody's, which estimated that 35 percent of all bank loans in Ukraine were problem loans, said the country's severe economic problems would keep local borrowers under pressure and could result in higher loan losses for the Russian lenders.

In the absence of the Association Agreement with the EU, Russian-Ukrainian trade is likely to rise, and the four big Russian banks may well increase their exposure to Ukraine, it added.

Yekaterina Trofimova, a Gazprombank board member, played down the concerns.

"Gazprombank is the least exposed to Ukrainian risk among major Russian banks. Gazprombank has no subsidiary in Ukraine. Gazprombank does not lend locally [and] has no retail lending in Ukraine. All credit exposure is contract-based secured lending," she said.

A spokesman for VEB said its own loan exposure in Ukraine was nearly $4 billion, mostly through subsidiary Prominvestbank, which it said had a corporate loan book of $3.5 billion and interbank lending of about $250 million.

"It is indeed the case that one of the systemic problems that Prominvestbank encounters is the low quality of debt servicing," the VEB spokeswoman said in e-mailed comments, saying the bank held more than $1 billion in problem loans. Prominvestbank was working flat out to recover these loans and had won $287 million in repayments through the courts in the form of money and property, the spokesman said, adding that no risks had materialized on the interbank markets following last weekend's protests, in which 350,000 people rallied in Kiev to demand Yanukovych's resignation.

Sberbank, Russia's largest bank, declined to detail its exposure to Ukraine when it announced third-quarter results last week. VTB declined to comment.

Eyeing The Exit

Foreign banks have $28.2 billion in cross-border claims and local loans in foreign currency, according to the Bank for International Settlements, whose figures cover 31 countries excluding Russia.

Gianni Franco Papa, head of Italian bank UniCredit's market-leading central and eastern European business, said the bank was not being put off by the drama playing out on Kiev's streets. The country has handled crises in the past. "Whether they are able to cope this time or not we will know in a few days."

An executive at Greece's Piraeus Bank, whose Ukraine unit has 60 branches, said: "There is no panic and no deposit outflows. Ukrainians are used to political crises. But what does happen — with us and at other banks, too — is that there is increased interest to buy foreign currency, mainly U.S. dollars."

Some European banks have already pulled out of Ukraine since 2008, including Commerzbank, Erste Bank and Swedbank. Emerging Europe's second-biggest lender Raiffeisen Bank International has said it would not rule out an exit from Ukraine as it sharpens its focus.

Dimitry Sologoub, head of research at Raiffeisen in Kiev, said the banks had learned lessons from the 2008 crisis, so were much less exposed to credit risk, liquidity risk and forex risk, and the central bank was calming matters by providing liquidity and foreign exchange.

"The question is how long it will go? The reserve cushion of the national bank is not so big."

In the meantime, Ukraine might secure short-term benefits from its closer ties with Russia, enough perhaps to stave off the kind of currency crisis that nearby Belarus suffered in 2011, said Charles Robertson, chief global economist at Renaissance Capital in London.

"In the long run, it will probably keep Ukraine poor. This is bad for Ukrainians and bad for Russia," he added.

"Instead of being a strong, successful economy on Russia's borders, able to buy plenty of Russian exports, Ukraine risks becoming another Belarus."

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