Fallout from Russian Debt Default

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That last time that Russia defaulted on its debts to foreign creditors was during the First World War and the Bolshevik Revolution that led to the creation of the Soviet Union. Now at the time of another war Russia is heading toward default as half of its $640 billion in foreign currency reserves are under sanctions by the US, EU, and UK. Why is this happening? How will it progress? What will be the broader fallout from Russian debt default?

Who Will Determine If Russia Has Defaulted on Its Debts?

Russia's inability to pay its debts will result in a low (junk) credit rating. Creditors will seek payment by going after other Russian assets outside of Russia. That will mean going to court in various countries or jurisdictions and arguing their case. Russia is already arguing that their default is artificial because their money is unavailable due to sanctions by the West. An investor panel called the Credit Derivatives Determination Committee makes decisions in matters of credit-swap markets and default insurance. If they determine that Russia is in default creditors can start the process to get insurance payouts. This happened already with the default of Russian Railways JSC that missed an interest payment.

Results of Russia's Defaults

The end result of debt default by Russia is that no one will lend to them in the future unless they can find a way to receive payment outside of the Western banking and payment systems. We already wrote about Russia using cryptocurrencies to avoid the effects of sanctions. This could work in the future with payments for gas, oil, coal, fertilizers, and other Russian exports. But it would do nothing to free up the money currently under sanctions. Because Russia cannot use much of its stash of money held in the West it will have to default or make payments from money generated as it goes forward. The point of sanctions by the US, EU, UK and others is to deny Russia the use of its money for pursuing its war in Ukraine which is costing an estimated $20 billion a day! In the longer term this will choke off Russia's economic growth as it has benefited over the years from a ready source of capital from the West due to its exports of energy products, strategic minerals, fertilizers, agricultural products, and more. Russia will especially be hurt by losing access to advanced technologies produced in Germany and elsewhere on which they rely for advanced weaponry for their military.

Driving Russia Further into the Arms of China

As the US, UK, EU and their allies trade less and less with Russia and as they cease to be a source of capital for business, Russia will be forced to rely more and more on China for trade, technology, and money transfers. This version of the Sino Soviet Axis will have Russia as the junior partner and increasingly tied to and obliged to the Chinese. With this view of the future in mind we can see that China's support of Russia's war in Ukraine is really China using Russia as a proxy to attack and weaken the West.

Are Sanctions on Russia's Assets Legal?

Sanctions against Russia are the result of and part of the war in Ukraine. Any determination about the legality of Russian debt default will not begin until Russia is actually in default. This will be after May when payments and grace periods have expired and America's temporary exemption for US bond holders accepting Russian payments expires. A failure to pay judgment by the Credit Derivatives Determination Committee would allow bond holders to collect on insurance on their bonds. That determination is a practical one and not a legal determination which would have to be carried out in the various jurisdictions where bonds are held.

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The fallout from all of this will be that Russia will not be able to obtain credit in Western markets or will only be able to secure credit at exorbitant rates. The world will be partially cut off from Russian exports of grains, petroleum products, coal, fertilizers, and strategic minerals which has already affected commodity markets and will possibly lead to civil and political unrest in Africa and Asia as Ukrainian and Russian grain does not arrive. The IMF has already downgraded their projections for global growth by a half for the coming years. And countries like India that trade with Russia anyway will get sweetheart deals for their oil and natural gas.

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