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U.S. Sanctions Can't Keep China from Buying Russian Oil

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China has proven with Iran that it has much practice and great skill in working around sanctions, and the U.S. has made it even easier to do so in the case of Russia in several ways, including leaving gaping loopholes in its sanctions that China and Russia can exploit.

The current ambiguity surrounding these mechanisms suits China perfectly, as until it believes that it is militarily, technologically, and economically able to directly challenge the U.S. as the world's number one superpower its strategy will remain to gradually build up its economic power through the multi-generational power-grab project, 'One Belt One Road' (OBOR), as analysed in depth in in my new book on the global oil markets. This project contains within it a corollary colonialist element by dint of its land and sea routes secured through chequebook diplomacy. Given this, China cannot afford at this stage of its strategy to be seen to back Russia fully in President Vladimir Putin's apparently ill-considered invasion of Ukraine and this was clearly evidenced in China's abstentions – unwanted and unexpected by the Kremlin – in the United Nations Security Council's votes last Friday firstly to condemn the war and secondly on whether to open the special emergency session of the General Assembly the next day.

One basic factor that has worked in China's favour in circumventing sanctions on continuing to do business, especially oil and gas business, with Iran – and will equally apply to its doing the same with Russia – is the lack of exposure of China's firms to the U.S. financial infrastructure – particularly to the U.S. dollar – and the ease with which companies can set up new special purpose vehicles to handle ring-fenced areas of their businesses to allow for special situations, such as sanctions.

As a corollary of this operational independence, China made no secret at the time of the pre-2016 sanctions against Iran or the post-2018 sanctions against it that it was going to use its Bank of Kunlun as the main funding and clearing vehicle for its dealings with Iran. The Bank of Kunlun has considerable operational experience in this regard, as it was used to settle tens of billions of dollars' worth of oil imports during the U.N. sanctions against Tehran between 2012 and 2015. Most of the bank's settlements during that time were in Euros and

Chinese renminbi and in 2012 it was sanctioned by the U.S. Treasury for conducting business with Iran. Rather like Iran – whose Foreign Minister, Mohammad Zarif, infamously stated back in December 2018 at the Doha Forum, that: 'If there is an art that we have perfected in Iran, [that] we can teach to others for a price, it is the art of evading sanctions' – China has always regarded any U.S. sanctions as a fun puzzle to solve.

Washington learned early on – when it sanctioned Zhuhai Zhenrong Corp, the massive state-owned oil trading firm founded by the man who started oil trading between Beijing and Tehran in 1995 as a means by which Iran could pay for arms supplied by China to be used in the Iran-Iraq War – that Beijing would not be playing the sanctions game according to anyone's rules but its own. Indeed, at a time when according to the U.S. 'there is clear evidence that China did not import any crude oil from Iran in June [2020] for the first time since January 2007', OilPrice.com showed that over a period of only 51 days just before the U.S. statement, China imported at least 8.1 million barrels of crude oil (158,823 barrels per day) from Iran.

In the case of Russian oil and gas exports, though, there is no need for China to go through all the trouble it took to circumvent the sanctions on Iran, for three key reasons. Firstly, there are currently no direct sanctions in place from either the U.S. or the E.U. on Russian oil or gas energy exports. A statement was released over the weekend that both are discussing a ban on Russian oil imports but this has not been approved yet and can still be worked around by China in the same way it did for Iran. In fact, despite several announcements last week of various types of sanctions being placed on a slew of Russian banks, one bank that was notably absent from all of the U.S.'s lists was Russia's third biggest lender, Gazprombank, which serves Russian state gas giant (with huge oil interests as well) Gazprom. Indeed, Gazprombank and Russian state-owned banking giant, Sberbank, are also not on the list of the seven institutions that the E.U. wants banned from the Society for Worldwide Interbank Financial Telecommunication (SWIFT) messaging and payments system.

The second reason why Russia and China are untroubled that their oil and gas trade will be affected is that, in addition to the de facto exemptions so far granted to the aforementioned institutions, the U.S. issued on 24 February the 'General License 8A' waiver. Although this sounds as sexy to many as a cold haddock, to would-be sanctions evaders it is the waiver equivalent of Scarlett Johansson or Brad Pitt. Just in case any potential sanctions evaders may have missed the signal being given by the U.S., the U.S. Treasury Department went to great trouble to explain the nub of the point: "Treasury is reiterating … that energy payments can and should continue." In its further detailed guidance, just in case any would-be sanctions evader thought that they would have to engage in any tricky manoeuvring to circumvent the wrath of the U.S., the Treasury explained how to use the waiver to continue to deal with a Russian oil or gas company: "For example, a company purchasing oil from a Russian company would be able to route the payment through a non-sanctioned third-country financial institution as an intermediary for credit to a sanctioned financial institution's customer in settlement of the transaction." The Treasury concluded: "Treasury remains committed to permitting energy-related payments – ranging from production to consumption for a wide array of energy sources – involving specified sanctioned Russian banks."

Even in the unlikely event that this extraordinary free-for-all waiver is stopped, the third reason why China and Russia will continue to go about their oil and gas trade – and all other trades – relatively unhindered is that over the past few years they have been securing their own bilateral infrastructural and financial structures for years, as also analysed in-depth in [my new book on the global oil markets](). China has long seen increased internationalisation of its renminbi currency as a fitting reflection of its growing status in the world and the chief executive officer of Russia's Novatek, Leonid Mikhelson, said in September 2018 that Russia had been discussing [switching way from US$-centric trading]() with its largest trading partners such as India and China, and that even Arab countries were thinking about it. "If they [the U.S.] do create difficulties for our Russian banks then all we have to do is replace dollars," he added. At around the same time, China launched its now extremely successful Shanghai Futures Exchange with oil contracts denominated in yuan (the trading unit of the renminbi currency). Such a strategy was tested initially at scale in 2014 when Gazpromneft tried trading cargoes of crude oil in Chinese yuan and roubles with China and Europe.

Infrastructural development for oil and gas trading between China and Russia has also been extremely extensive in recent years, as examined [several times in depth by OilPrice.com](). The most recent examples of this was, in the oil sector, Rosneft signing an US$80 billion 10-year deal to supply the China National Petroleum Corporation (CNPC) with 100 million metric tonnes of oil over the period (slightly over 200,000 barrels per day). In the gas sector, at almost exactly the same time, Gazprom signed a 10 billion cubic metres per year (bcm/y) deal to supply gas to CNPC, adding to another supply contract between the two companies signed in 2014 – a 30-year deal for 38 bcm/y to go from Russia to China. This, in turn, is part of, and augments, the 'Power of Siberia' pipeline project – managed on the Russian side by Gazprom and on the China side by CNPC – that was launched in December 2019. And just in case there were any doubts on where China stands – in practical terms – on Russia in light of its invasion of Ukraine, Beijing's foreign ministry spokesperson, Wang Wenbin, said in a press conference on 28 February: "China and Russia will continue to conduct normal trade cooperation in the spirit of mutual respect, equality and mutual benefit." For good measure, over the weekend [China warned the U.S.]() against any moves that "adds fuel to the flames" in Ukraine and its Foreign Minister, Wang Yi, called on the West to take account of Moscow's concerns about NATO expansion.

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