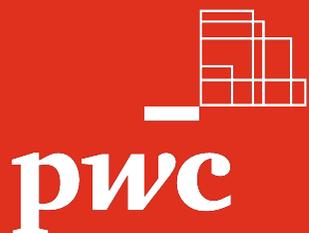


War in Ukraine

— Situational Awareness Briefing

23 August 2022



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Situational Awareness – Briefing as of 23 August 2022 (Summary)

Ukraine Crisis

The current geopolitical developments in Eastern Europe and the unprecedented attack on Ukraine are also an attack on our way of living and doing business together.

At the moment, no one can foresee all the consequences of this aggression. This is why urgent questions are now being asked in all areas of our social life. Also for companies this means far-reaching cuts and changes.

This Situation Awareness Briefing is provided for information purposes only by PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft and will be updated regularly.

The overview to the right represents a summary of points along the following five dimensions:

- Overall Geopolitical Assessment
- Industry Special
- Forecast
- People
- Operations
- Finance



Overall Geopolitical Assessment

A major Ukrainian push into the Iziurm salient was reversed by Russian counter attacks after initial success. Russian breakthroughs in the northern Donbas endanger the Ukrainian defensive positions. It is likely that both sides are currently preparing for a major offensive push in order to achieve strategic objectives before the onset of the fall thaw.



Forecast

German households will have to pay almost EUR 500 more a year for gas after a levy was set to help utility provider to cover the costs for replacing Russian gas providers. China will optimize policies for a long-term economic recovery and that macro policies should actively increase demand in a strong, reasonable, and moderate way. The United States and Taiwan have agreed to begin trade talks that could lead to free trade agreements.



Operations (Focus: Cyber)

Head of Ukraine's cybersecurity agency visited one of the largest hacking conferences in the world and proposed that Russian that the International Criminal Court should prosecute Russia's cyber attacks as war crimes. Ukrainian state-owned energy corporation Energoatom reported that in the evening of August 16 it was subjected to the largest-scale hacker attack on its official website since February 24. The Security Service of Ukraine has exposed an underground server center in Kiev used by Russian hackers for cyber attacks against Ukraine.



Industry Special: Banking & Capital markets - update

According to Russian banking association there is almost no difference in conducting business for sanctioned and non-sanctioned banks in Russia due to the overall pressure on Russian economy and financial sector. Only a handful of banks were able to maintain correspondent banks relationships in Europe and therefore working with foreign currencies. Russia considers purchasing the currencies of "friendly" nations like China, India, and Turkey to hold in its National Wealth Fund..



People

Ukrainian president Vladimir Zelenskyy said that US intelligence warned Ukraine of a Russian invasion as early as September 2021. Governments of European Union are discussing visa restrictions for Russians: on August 31 in Prague they will start a process of decision making. Russians have increased the amount of foreign currency deposits in foreign banks by withdrawing them abroad.



Finance (Focus: Sanctions)

The Federal Bureau of Investigation (FBI) and the Securities and Exchange Commission (SEC) have started to review how Russian oligarch Roman Abramovich's investment company "Concord Management" allegedly has used multiple shell companies to invest in dozens of US hedge funds and private equity firms in the last 20 years. Associates of Abramovich's company may have invested up to USD 8 bln from offshore entities in havens like the British Virgin Islands and the Isle of Jersey in funds managed by BlackRock, Millennium Management, Paulson and others.

For questions, comments or details, please contact Joint Crisis Center team: de_ukraine-crisis@pwc.com



Key takeaways

- Russian forces continue to push along the entire Seversk-Soledar-Bakhmut line in the direction of Sloviansk. Battles are waged in Soledar and Bakhmut. The Ukrainian push into the Izium salient was reversed by Russian counterattacks.

Current topics

Current situation in the Russo-Ukrainian War

The Kharkiv front continues to remain static. Due to shelling the number civilian victims in the Oblast has risen once more. A large Ukrainian counterattack occurred at Izium pushing into the salient from multiple sides and achieving strategic surprise and gaining large areas. After the initial shock, Russian forces regrouped and eliminated all penetrations within a week by pushing Ukrainian forces back to their starting positions. The tip of the salient has transformed into a meat grinder for both sides characterized by high attrition and casualty rates. The Ukrainian push momentarily stalled Russian efforts towards Sloviansk but failed to achieve its goal to plant the Russian spearhead heading south. Moreover, valuable reserves were used to disturb Russian preparations with limited success. In the east, Russian forces continue to push along the entire Seversk-Soledar-Bakhmut line and have advanced further in the direction of Sloviansk and Kramatorsk. Russian forces occupied Berestove and achieved several minor breakthroughs. In addition, a Popasna-like breakthrough is in development between Seversk and Soledar, threatening a deeper penetration in the rear area of Ukrainian defenses. Heavy fighting is raging within Soledar, while Russian forces have entered the outskirts of Bakhmut. At Horlivka and Donezk Russian forces advance on the entire front and are met with stiff resistance by Ukrainian forces along the former contact line. Only limited gains were recorded in these sectors. In the southeastern and southern area of operations currently minor Russian and Ukrainian attacks have led to the exchange of territory. The situation is similar along most of the front line in the Zaporizhzhia and Kherson Oblasts. At the Zaporizhzhia nuclear power plant, Russian forces use the factory complex to store and camouflage heavy equipment and ammunition as Ukrainian forces are unlikely to endanger the nuclear power plant by artillery shelling. The current focus of Ukrainian efforts remains directed towards Kherson, but no major success was achieved in the last two weeks. Even though Ukrainian forces are lacking in reserves and materiel to conduct a strategic counter push, major operations are still expected to commence at the end of the summer campaign season as both sides will seek to achieve some strategic success before the onset of the fall thaw.

Escalation of US-Chinese relations over Taiwan

After the visit Nancy Pelosi to Taiwan, another congressional delegation led by Massachusetts Senator Ed Markey visited Taiwan on August 12, causing further enragement within China. In response, China carried out additional military exercises near Taiwan. This was followed by the arrival of a trade delegation on August 21. With US-China relations already having becoming increasingly strained over the past years, the current tensions could send bilateral relations on a further downward spiral and mark the beginning of an era of increasingly dangerous hostilities. China has becoming increasingly assertive in the efforts to expand its global influence, which the US seeks to contain. Both parties have begun to undermine the status quo over Taiwan and are unlikely to backtrack on this issue. At the same time, pro-independence sentiment in Taiwan has reached a new height. A couple of trajectories regarding how relations between the US and China could evolve in the mid- to long-term are conceivable: (1) Several factors could entice the Chinese leadership to eventually take military action against Taiwan. China faces increasing domestic difficulties. Major issues include its crumbling real estate bubble as well as the economic fallout caused by the zero-COVID policy. China may instigate conflict with Taiwan to distract from these issues. China's unsustainable demography may also signify a closing window of opportunity to China's leadership to act against Taiwan. Finally, China's political system has become increasingly totalitarian and hypernationalist in recent years. In consequence, it may lack internal feedback loops, causing it to miscalculate its odds of success against Taiwan or underestimate the international consequences. (2) A more likely scenario may be a successful US deterrence of major military action by China against Taiwan. In this case, a continuing gradual political and economic decoupling between the US and China accompanied by frequent military provocations against Taiwan that however fail to cross the threshold that would lead towards war are likely. (3) While rapprochement between China and the US is impossible to imagine in the short-term, in the mid- to long-term, severe economic difficulties in conjunction with a hypothetical change of leadership in China may also cause China to (momentarily) revert cause and seek closer relations with the US to maximize mutual economic gains.



Key takeaways

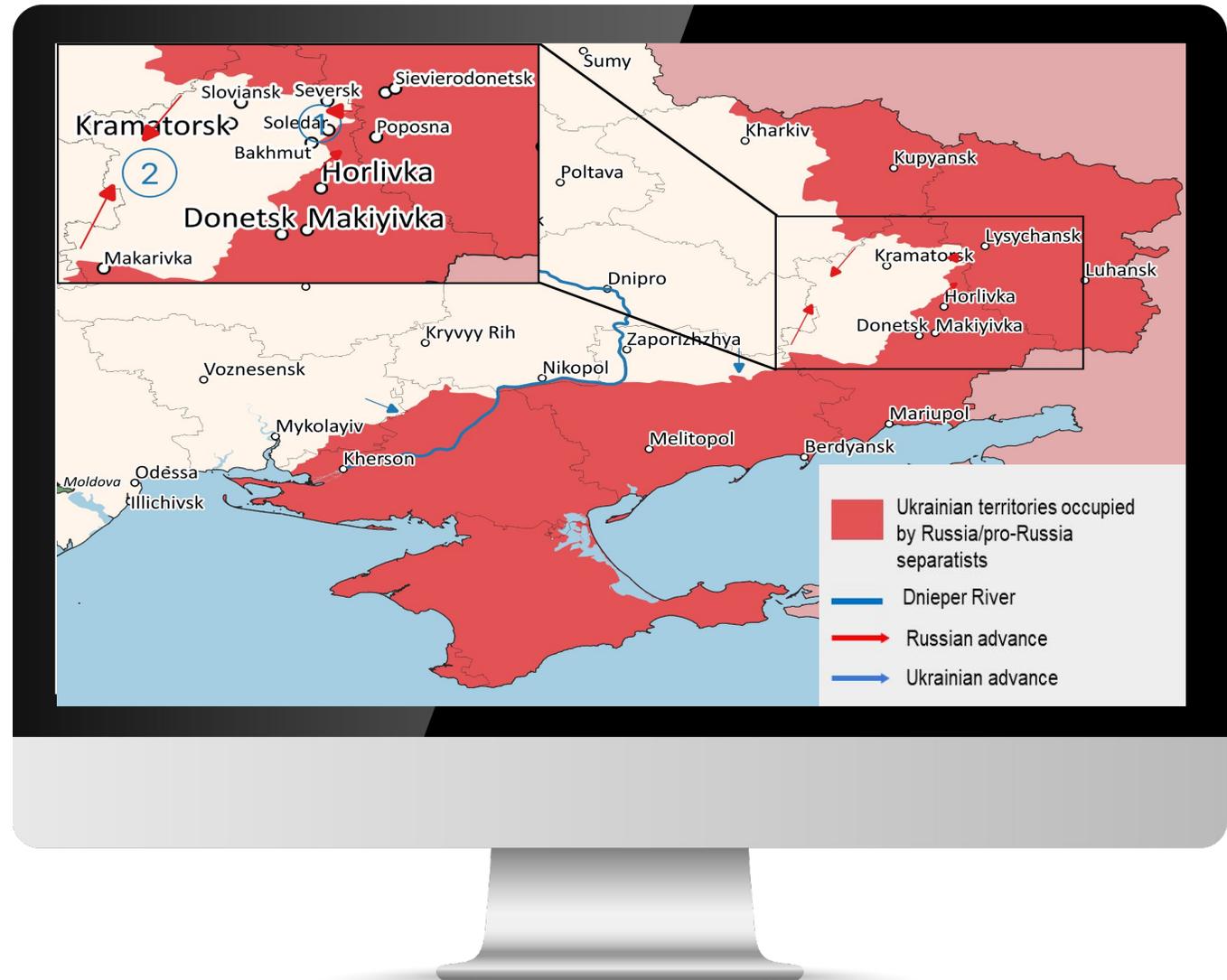
- Ukrainian efforts to eliminate the Iziurm salient have failed, while Russian forces are seeking a decisive breakout in the Donbas.

Selected upcoming events

- 29-30 August:** (EU) Informal meeting of defence ministers
- 31 August:** (EU) Informal meeting of foreign affairs ministers
- 9-10 September:** (EU) Informal meeting of economic and financial affairs ministers

Current Military Situation in Ukraine

(arrows indicate potential future Russian operations in the coming weeks)





General context

Following Russia's invasion of Ukraine, the country's financial system has been crippled by financial sanctions from a broad range of reserve-currency-issuing jurisdictions.

Current topics

Report of the Russian Central Bank on the development of the financial market under sanctions

The Bank of Russia released a report on the development of the financial market under sanctions earlier this month. Among the main priorities: restoring the stability of financial institutions and their participation in the structural transformation of the economy. The regulator intends to accelerate devaluation and will introduce additional measures to reduce bank operations in dollars and euros (it recommends that non-financial organizations convert dollars and euros into yuan and other "friendly currencies"). The regulator plans to supplement the existing system of premiums on risk ratios for foreign currency loans and securities with new premiums, including differentiated ones taking into account the issuer of the currency. The Central Bank will assess the feasibility of establishing increased norms of required reserves for bank liabilities in "toxic currencies".

Russian banks are losing correspondent banks relationships

According to Russian banking association there is almost no difference in conducting business for sanctioned and non-sanctioned banks in Russia due to the overall pressure on Russian economy and financial sector. Only a handful of banks were able to maintain correspondent banks relationships in Europe and therefore working with foreign currencies.

New foreign currencies for Russia

Central Bank of Russia reported that after being unable to purchase dollars or euros due to sanctions, Russia is considering purchasing the currencies of "friendly" nations like China, India, and Turkey to hold in its national wealth fund (NWF). Russia previously purchased dollars and euros for the NWF under the budget regulation, but not the other currencies. It ceased daily FX purchases for the fund in early 2022 due to heightened rouble volatility. Economic contraction in Russia will bottom out in the first half of 2023 Central Bank said. The central bank will be able to lower the main rate from its current level of 8% to the 5%-6% range in 2025 because inflation will decelerate to the 4% objective in 2024, according to the bank. The central bank also stated that it sees no compelling reason to maintain capital controls after the concerns to the country's financial stability have passed.

China launches new probe into banks' property loans

As the real estate crisis develops and places a significant burden on the economy, China's banks regulator is closely examining the property loan portfolios of some domestic and foreign lenders to evaluate systemic risks, f.e. whether those lending decisions were made in accordance with the rules. The inquiry highlights Beijing's difficulties in encouraging banks to provide new loans to troubled developers while managing credit risks.

Preliminary Assessment

- The Bank of Russia is considering different approaches to dealing with blocked assets of Russian residents and liabilities to residents of "unfriendly countries" (including EU countries, the USA, Canada, etc.). As a solution, the option of buying out blocked assets is not considered, since this is fraught with large-scale money emission.
- The Bank of Russia intends to promote the development of mechanisms that promote a more even distribution of credit risk within the banking sector and create conditions for the transition to the use of national currencies in cross-border settlements.
- Experts have expressed concern about the potential hazards and the lack of liquidity in the currencies of "friendly" countries. Turkey's inflation, for instance, increased to a 24-year high of about 80% in June.
- The central bank first deputy governor pointed out that liquidity in yuan-rouble trading has approached the levels of the euro-rouble currency pair on the Moscow Exchange.



General context

Considerations on implications for businesses along the PESTEL framework

P Political	New negotiation round between US and Taiwan
E Economic	China to increase economic demand and accelerate infrastructure. German households to face rise in gas bills
S Social	Social related implications: e.g. refugee streams, labour market developments
T Techno-logical	Technology related implications: e.g. cyber threats and disinformation, IT infrastructure disruptions
E Environ-mental	Environment related implications: e.g. Resource scarcity, energy embargo
L Legal	Legal implications: Compliance with changing regulations, contractual obligations, etc.

Current topics

German households to face EUR 480 rise in gas bills

German households will have to pay almost EUR 500 more a year for gas after a levy was set to help utility provider to cover the costs for replacing Russian gas providers. The charge has been set at 2.419 euro cents per kilowatt hour (kWh). As a consequence of the high dependency of the German energy model on Russia, corresponding measures were taken to prevent a collapse of the German energy market and likely also the European energy market as German Economy Minister Robert Habeck stated. Meanwhile Germany's request for a VAT exemption for the levy had been denied by Brussels.

China will increase economic demand and accelerate infrastructure

An NDRC representative said at a news conference that China will optimize policies for a long-term economic recovery and that macro policies should actively increase demand in a strong, reasonable, and moderate way. China will use new financing, provided by policy banks and special local government bonds more frequently. China had already issued the majority of the 3.45 trillion yuan in special bonds intended for infrastructure as of July 31.

In comparison to the same period last year, infrastructure spending increased 7.4% in the first seven months of this year.

The state of the labor market remained precarious. According to official figures, the overall survey-based unemployment rate slightly decreased from June to July, but youth unemployment remained persistently high and hit a record high of 19.9% in July. China will also implement useful measures to encourage young people to create their own businesses and find jobs.

US and Taiwan are to start formal trade talks

As part of a new attempt to negotiate with "economically substantial outcomes," the United States and Taiwan have agreed to begin trade talks.

They plan to pursue an ambitious schedule for achieving high-standard commitments and meaningful outcomes covering the eleven trade areas in the negotiating mandate that will help build a fairer, more prosperous and resilient 21st-century economy," Deputy United States Trade Representative said. The first round of negotiations is anticipated to begin early this fall, and that this could one day lead to a free trade deal the island has long sought with the United States.

According to the office of the U.S. Trade Representative, which stated that the two parties had "reached consensus on the negotiating mandate."

Preliminary Assessment

- China NDRC in July approved eight fixed-asset investment projects worth CNY 236.8 bln (USD 34.89 bln).
- In June, just days after the Biden administration removed the Chinese-claimed island from its Asia-focused economic strategy intended to challenge China's expanding influence, Washington and Taipei presented the US-Taiwan Initiative on 21st-Century Trade.



Key Considerations

Response measures may include the following:

- Scenario planning sessions to explore how the escalating situation could impact the organization and identify the risks and mitigating actions.
- “Table-top exercising” can be used to validate response structures if they are not already in operation.
- Ensuring that playbooks are in place for extreme but plausible scenarios such as loss of IT for an extended period and disruption to critical suppliers.
- Ensuring the ability to locate all personnel based in, or travelling to, regions of conflict and ensure appropriate steps are taken for their protection.

Current topics

Zelensky explained why the authorities did not warn the Ukrainians about the Russian invasion

In an interview with The Washington Post, Ukrainian President Vladimir Zelenskyy said that US intelligence warned Ukraine of a Russian invasion as early as September 2021. However, he said that the partners did not provide specific data. He also stated that if people were told about the war earlier, it would lead to widespread panic, men fleeing abroad, closing businesses, and withdrawing funds from accounts. Zelensky suggested that by reporting, Ukraine would have been losing USD 7 bln a month since last October, and the moment the Russia did attack, it would have taken over the country in three days.

The heads of foreign affairs of the European Union are discussing visa restrictions for Russians

Among the first states to call for a complete ban on Russians from entering Europe was Estonia, where the head of the Ministry for Foreign Affairs said that “sanctions against Russia should be universal and consistent across Europe. If only the Baltic states and Poland act, the effect will be less.” Lithuania and Latvia joined the calls. Denmark, which is going to reduce the number of tourist visas for Russians, has joined the supporters of restrictions on issuing visas to Russians, and also calls for a corresponding decision at the EU level. The Deputy Foreign Minister of Poland said that Warsaw is currently working on the concept, which will completely stop issuing visas to Russians.

So far, only German Chancellor Olaf Scholz has spoken out clearly among those who disagree, saying that “if sanctions were directed against everyone, including the innocent, this would weaken their effectiveness.”

The EU foreign ministers will discuss visa restrictions for Russians with the background of the war in Ukraine at a meeting on August 31 in Prague.

Russians withdraw funds abroad

Citizens of the Russian Federation in June increased the amount of foreign currency deposits in foreign banks to RUB 266.1 bln, follows from the data of the Central Bank. In dollar terms, this is USD 4.7 bln, which was the maximum since the beginning of 2018.

In March, the Central Bank limited transfers abroad to individuals in the amount of USD 5,000 due to the unstable ruble exchange rate. After that, the regulator increased this threshold several times. In June, it was first raised to USD 150,000, and at the end of the month to USD 1 mln. Against this background, Russian banks began to introduce additional commissions for citizens for servicing foreign currency accounts.

Preliminary Assessment

- On February 23, Joe Biden's administration informed Ukrainian President Volodymyr Zelenskyy of intelligence assessing that Russia is preparing to conduct a full-scale invasion of the neighboring country within the next 48 hours.
- The number of applications for Schengen visas — which give access to most EU countries — submitted by Russians has risen rapidly in recent weeks.



Russian hackers attacked Polish police and hospitals

The Russian hacker group Killnet announced an attack on Poland's law enforcement and health care system in response to aid to Ukraine. Killnet claimed to have attacked all of Poland's law enforcement portals, including the main portal, the website of the Warsaw police headquarters and the police of major cities.

Killnet later claimed that Polish hospitals had problems with the electronic system for securing and monitoring patients in cardiology departments. According to the attackers, they staged cyberattacks to "influence Russophobia ideology" and "for the glory of Russia's future".

Killnet had previously attacked other government agencies in Poland, including the tax service and the "My Governor" service. The hackers said they no longer have any filtering on the target. According to them, the DDOS will also hit the health care system."

The pro-Russian Killnet had in the past declared war on Anonymous and 10 countries they believed were pursuing anti-Russian policies. They included the United States, Germany, Italy, Great Britain, Latvia, Romania, Lithuania, Estonia, Poland, and Ukraine. The hackers assured that their actions were directed only at the authorities of the states, not at civilians.

Current topics

Head of Ukraine's cybersecurity agency visited one of the largest hacking conferences in the world

Victor Zhora, head of Ukraine's defensive cybersecurity agency, visited Black Hat, one of the biggest hacking conferences in the world on August 10-11. He said he was there to rally international support to his country's on the cyber front. He also seized the moment to share Ukraine's experience in cyberdefense, including deflecting a Russian attack that had the goal of turning off the power grid. In total, according to him, since the beginning of the year, more than 1,600 major cyber incidents have been recorded in Ukraine.

Zhora further proposed that the International Criminal Court should prosecute Russia's cyber attacks as war crimes, in particular those that support real-world operations, and those that hit civilian internet infrastructure.

Russian hackers attacked Ukraine's state-owned nuclear power operator

Ukrainian state-owned energy corporation Energoatom reported that in the evening of August 16 it was subjected to the largest-scale hacker attack on its official website since February 24. The attack was carried out from the territory of Russia, the company claims. Energoatom has been regularly subjected to cyberattacks since the start of the war.

"The People's Cyber Army," a small pro-Russian group whose Telegram channel has just over 8,000 subscribers, carried out a DDoS attack using 7.25 million bot-users, which simulated hundreds of millions of views of the company's main page over the course of three hours. However, Energoatom pointed out that the attack did not significantly affect the site's performance and remained invisible to users.

An underground server center of Russian hackers exposed in Kiev

The Security Service of Ukraine has exposed an underground server center in Kiev used by Russian hackers for cyber attacks against Ukraine. The attackers were renting out more than 100 dedicated servers located in Kiev and abroad. Later they were used to hack computers, steal passwords and perform DDoS attacks, including on websites of state authorities.

Dealers served more than 100 "subscribers", the vast majority of which are hackers from the Russian Federation. Some of them were controlled by the Russian secret services and worked to the detriment of the information security of Ukraine.

Preliminary Assessment

- Zhora attributed his country's success in part to because Ukraine has constantly been under attack for the last eight years. This has given his cybersecurity agency the opportunity to learn and improve the country's defenses, both in the public and private sectors.
- On August 15, the Ukrainian parliament appealed to world organizations and governments to condemn the act of nuclear terrorism carried out by Russia at the Zaporizhzhia nuclear power plant in occupied Energodar. The UN is trying to encourage experts from the International Atomic Energy Agency to visit the Zaporizhzhya NPP, but Russia is blocking their visit. Because of such actions of Russian troops at the station, Ukrainian President Zelensky accuses Russia of "nuclear blackmail".
- In the course of the searches, computer equipment, cell phones with evidence of illegal activities, bank cards used to make payments to "clients," and server equipment were found and seized.



Key Considerations

Sanctions Screening Activities

- Screening solutions generate increasing number of alerts (especially banks must deal with the increased workload)
- Appropriateness and effectiveness of sanctions screening measures in identifying sanctioned parties and activities must be ensured. Complex ownership structures complicate the proper identification of involved parties (OFAC 50% rule)
- Trade transactions with Russia and Belarus must be reviewed

Sanctions Compliance Governance

- Sanctions Compliance Governance as a key requirement increasingly in the focus of regulatory authorities
- Robustness of Sanctions Compliance Management System and sanctions controls to counter the current and new sanctions regulations
- Adequateness of internal safeguards to prevent sanctions circumvention activities

Current topics

Siemens to post its first quarterly loss in 12 years

As a consequence of Siemens Energy's decision to leaving Russia the company posted its first quarterly loss since 2010. The company's net profits took a hit of more than half a billion euros resulting from EUR 2.7 bln non-cash write downs for its stake in Siemens Energy. However, despite major turbulences in the market environment caused by sanctions on Russia, high inflation and ongoing impairments of the pandemic, Siemens reported higher revenue and orders within the last quarter.

US federal authorities to investigate investment firm of Russian oligarch Roman Abramovich

The Federal Bureau of Investigation (FBI) and the Securities and Exchange Commission (SEC) have started to review how Russian oligarch Roman Abramovich's investment company "Concord Management" allegedly has used multiple shell companies to invest in dozens of U.S. hedge funds and private equity firms in the last 20 years. Associates of Abramovich's company may have invested up to USD 8 bln from offshore entities in havens like the British Virgin Islands and the Isle of Jersey in funds managed by BlackRock, Millennium Management, Paulson, Carlyle Group and D.E. Shaw as well as many other yet unknown hedge funds. The investigations currently intend to find out whether the identity of Concord's ultimate beneficial owner had been concealed. A loophole in the U.S. legislation allowed hedge funds and private equity firms in some cases to avoid anti-money-laundering and know-your-customer checks, which are mandatory for banks and mutual funds.

Wall Street starting to revive Russian bond trading

Several major banks, including JPMorgan Chase & Co, Deutsche Bank AG and Citigroup Inc. have begun to facilitate disposing Russian debt. After banning US investor from purchasing any Russian security as part of economic sanctions in June, U.S. Treasury Department allowed in July U.S. holders to wind down their positions to mitigate their Russia risk exposure.

Preliminary Assessment

- Multinational retail conglomerate IKEA announced to further scale back its operations in Russia by liquidating its local business unit. With H&M, Nike and IKEA, scores of consumer brands announced their plans for permanent exit from the Russian market.
- After halting business operations in March, Swiss chocolatier company Lindt & Sprüngli AG decided to withdraw from the Russian market completely. The company declared to have no intentions to reopen stores in future. The Ukrainian and Russian market accounts for less than 1% of Lindt's total revenue.
- Following up on the last situational awareness briefing, German economy ministry stated that it had no new information on whether the turbine needed for the Nord Stream 1 gas pipeline is on its way to Russia. Russian state-owned energy company Gazprom stated earlier that Western sanctions prevent the equipment from its shipment, which had been refused by the German government.

General remarks



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