Collateralising Russian Reserves: Short-, Medium- and Long-Term Implications for the Euro's Standing as a Reserve Currency

October 2025
Discussion Paper

Sven Behrendt, Karina Luchinkina, Rachel Ziemba, Paul O'Brien, Udaibir Saran Das, Massimiliano Castelli, Seema A. Khan, Philipp Schoeller, Kristian Flyvholm

Abstract

Europe's immobilisation of roughly €260–300 billion in Russian central bank reserves following Moscow's invasion of Ukraine has become a defining experiment in the use of financial power under international law. What began as a coordinated G7 sanctions measure now tests the euro's dual identity—as a market instrument and as a pillar of the rules-based order. Building on the proposal to use these frozen reserves as collateral for a €140 billion interest-free loan to Ukraine, this short note examines the economic, legal, and geopolitical consequences of such a mechanism for the euro's standing as a reserve currency.

It argues that while collateralisation appears legally cautious, it is politically irreversible: once pledged, the assets cannot credibly be returned to Russia without compensation. The mechanism functions as a contractual path toward asset transfer, blurring the boundary between financial engineering and geopolitical sanction. In the short term, such an approach preserves stability; in the medium term, it embeds conditionality into the euro's governance framework; and in the long term, it would position the euro as an anchor of the rules-based international order, enhancing the European Union's credibility and geopolitical standing.

Shifting Perspectives

The decision by European and G7 partners to immobilise approximately €260 billion in Russian central-bank reserves (appr. €300 billion total worldwide) following the full-scale invasion of Ukraine in 2022[1] has created an unprecedented test case in international finance. Never before have the reserves of a major economy been frozen on this scale. The measure, initially conceived as a sanction to constrain Moscow's war effort, has gradually become a laboratory for re-examining how international law, sovereign immunity, and financial interdependence interact in times of geopolitical rupture. This debate now serves as a stimulus for the evolution of both international financial governance and the legal norms that underpin it, forcing policymakers to confront how sovereignty, responsibility, and monetary trust should be balanced in a conflict-driven global order. What began as a defensive step to uphold international law now raises a larger question: how far can Europe deploy its monetary and financial infrastructure as a strategic instrument while allowing the euro's international role—and the reach of EU jurisdiction that underpins it—to evolve from a neutral store of value into a framework that reinforces lawful order?

A proposal gaining momentum in Europe would transform frozen Russian central-bank reserves into collateral for an interest-free €140 billion loan to Ukraine, repayable once Moscow compensates Kyiv for war damages. The idea, recently advanced by Chancellor Friedrich Merz in a *Financial Times* op-ed, marks a potential turning point in Europe's handling of immobilised sovereign assets. The plan explicitly rejects outright confiscation of the assets, seeking instead to mobilise their financial potential through collateralisation—a mechanism designed to unlock liquidity while formally preserving Russian ownership. In the plan's conception, member states would initially guarantee the loan under national budgets until the next Multiannual Financial Framework in 2028, at which point the guarantees would migrate to the EU budget. By linking Ukraine's long-term defence financing to the EU's collective fiscal credibility, the proposal positions Europe as both the guarantor of Ukraine's resilience and the custodian of a new instrument that could reconcile legal caution with strategic purpose.

While earlier discussions on the use of frozen Russian reserves focused on moral obligation or punitive justice, the current debate reaches deeper into the architecture of the international financial system. Collateralising these assets does more than finance Ukraine's defence: it tests whether the European Union can transform immobilised sovereign wealth into an instrument that both preserves the integrity of international law and projects strategic deterrence. The issue thus bridges two domains that have rarely interacted directly—monetary governance and international accountability—and in doing so provides an opportunity to examine how economic instruments can acquire normative significance. And it adds another case in the complex discussion regarding the doctrine of sovereign asset immunity, monetary authority representing a substantial pillar of a state's ability to conduct its own monetary policy insulated from external interference.

Scale and Structure of Frozen Russian Reserves

The freezing of Russian central-bank reserves in early 2022 represents the largest immobilisation of sovereign assets in modern history. Approximately €260–300 billion in Russian reserves are blocked worldwide, the vast majority within the European Union. It is important to note that the bulk of Russian reserves were held in the EU because of Russia's perceived confiscation risk in the U.S. starting in 2014/15. Public estimates suggest that of the roughly €210 billion in Russian sovereign assets immobilised in Europe, a dominant portion—approximately €191 billion—resides in Euroclear (Belgium), with smaller quantities held in Clearstream (Luxembourg) and other European custodians. Another €80 billion are distributed among the United States, the United Kingdom, Canada, Japan and Switzerland. These assets consist largely of cash balances and high-grade sovereign or supranational securities previously managed by the Central Bank of Russia as part of its official reserves. Other Russian sovereign assets, including new funds since 2022, are outside the reach of western jurisdictions, especially in countries such as China

The immobilisation is grounded in a series of EU Council Regulations adopted under the Common Foreign and Security Policy (CFSP),[2] coordinated with equivalent measures by the other G7 partners.

The decisions restrict all transactions with the Russian central bank and prohibit the disposal, transfer, or use of its assets held in participating jurisdictions. The measures do not, however, alter ownership: the assets remain legally the property of the Russian Federation. This distinction between *freezing* and *confiscation* preserves compliance with long-standing principles of sovereign immunity, which protect central-bank assets from enforcement actions in foreign jurisdictions.

Most of the immobilised reserves lodged in the European clearing systems Euroclear and Clearstream take the form of short-term deposits and high-quality liquid securities. As Russian securities have matured, the proceeds have been converted into cash, which these institutions reinvest in low-risk European government instruments. This process has gradually shifted the composition of the frozen assets from a diversified securities portfolio to predominantly cash-based holdings, creating a stable base from which investment income accrues.

The blocked assets continue to generate interest income, commonly referred to as *extraordinary revenues*. In 2024, interest arising on cash balances from Russian-sanctioned assets was approximately €6.9 billion[3]; during the first half of 2025, it recorded €2.7 billion, implying a full-year figure in the mid-single-digit billions depending on monetary-policy conditions. Following decisions by the EU and G7 in 2024, extraordinary revenues have been used to support Ukraine, including via the G7's Extraordinary Revenue Acceleration (ERA) facility.[4] The frozen principal remains off-limits — it cannot be accessed or redirected without fresh legal authority under the sanctions regime.

The Securitization Proposal

By September 2025, a proposal gaining traction in European policy circles sought to move beyond the existing regime of mere immobilisation toward a structured use of Russia's frozen reserves. The initiative represented the most serious effort yet to translate political intent into a viable financial mechanism. Writing in the *Financial Times* – supporting earlier proposals – Merz called on the European Union to transform these assets into the foundation for an interest-free loan of €140 billion to Ukraine. The plan, discussed with EU heads of state and government in advance of the October European Council, is designed to mobilise substantial resources for Ukraine's long-term defence and reconstruction while formally preserving Russia's legal ownership of the assets.

As publicly outlined, the proposal envisions the creation of a loan facility guaranteed by EU member states, with the frozen Russian central-bank reserves serving as collateral. Under this model, the loan would be disbursed to Ukraine, providing predictable multi-year financing, while repayment obligations would arise only once Russia has paid compensation for the damage caused by its war of aggression. Until that time, the Russian assets would remain frozen, acting as security for the facility. To manage fiscal risk, national guarantees would be issued in the first phase; once the next Multiannual Financial Framework (MFF) takes effect in 2028, the facility would be integrated into the EU's long-term budget, converting the national guarantees into a collective EU liability.[5]

The core innovation of the proposal lies in its effort to reconcile financial mobilisation with legal restraint. It explicitly rejects outright confiscation or appropriation of Russian assets, instead treating them as collateral against future reparations. This design preserves the formal distinction between ownership and use, maintaining consistency with international legal norms on sovereign immunity. At the same time, it seeks to ensure that Russia's reserves cannot be returned unconditionally, anchoring the assets in a framework that connects their eventual release to accountability for wartime damage.

The proposal also carries a broader strategic intent. By linking Ukraine's financial resilience to Europe's own fiscal capacity, it seeks to demonstrate that the EU can act with coherence and scale comparable to major powers. It also aims to signal to both Russia and global markets that aggression entails durable financial consequences and that Europe is willing to use its jurisdictional reach to enforce accountability within the bounds of law. In this sense, the proposal is not only a financial instrument but a statement of strategic credibility.

Transforming frozen Russian central-bank assets into collateral for a loan facility would require a carefully sequenced process balancing legal certainty, operational feasibility, and political legitimacy. The following table outlines an illustrative and hypothetical institutional pathway.

The Collateralization Process: Hypothetical Pathway

Phase	Key Actors	Main Steps	Outcome
1. Political Mandate	European Council, Council of the EU, G7 coordination	• EU leaders agree politically to mobilize frozen assets as collateral for Ukraine. • Joint G7 statement affirms alignment. • Confidential consultations with ECB, Eurogroup, Euroclear.	High-level political mandate to design a collateralization framework.
2. Legal & Institutional Design	European Commission, Council Legal Service, ECB Legal Service, Member States, Euroclear/Clearstream	• Draft Council Regulation establishing the collateralization instrument. • Create an SPV – the *Ukraine Reconstruction Facility* • Define legal provisions for segregated escrow accounts holding the frozen reserves. • Secure unanimous Council adoption.	EU-level legal and institutional architecture in place.
3. Operational Setup	SPV, Euroclear/Clearstream, ECB oversight, investors, rating agencies	• Transfer frozen reserves into ring-fenced escrow accounts. • Conclude collateral contracts between the EU and SPV. • Ensure integration with ECB systems.	SPV fully operational; first collateralized bond issuance prepared.
4. Deployment of Funds	SPV → Government of Ukraine (with EU/IMF monitoring)	• Issue first bond tranche (€30–50 bn). • Disburse proceeds to Ukraine for budget support and reconstruction. • Service interest using Euroclear "windfall profits" or EU budget contributions.	Ukraine receives multi-year financing backed by frozen Russian assets.
5. Endgame / Enforcement	SPV, EU, G7, international courts	• Scenario A – Russia pays reparations: assets released to settle bonds. • Scenario B – No reparations: collateral enforced to repay bondholders (*de facto* confiscation). • Scenario C – EU reversal: EU budget assumes repayment.	Final settlement of Russian assets; burden distributed by scenario.

The process would begin with a political mandate from the European Council and the G7, establishing intent and initiating discreet consultations with the ECB and Euroclear. A subsequent legal-design phase would create the Council Regulation and a Special Purpose Vehicle (SPV), defining the relationship between the frozen assets, the collateral accounts, and the possible issuance of *Ukraine Reconstruction Bonds* (if so executed).

During the operational setup, the reserves could be moved into ring-fenced escrow accounts under EU supervision, while the SPV structures its first bond issuance. Once launched, funds could be deployed immediately, transferring proceeds to Ukraine in tranches monitored by the EU and the IMF. Interest servicing would be covered by the extraordinary revenues generated from the immobilised assets, supplemented by EU-budget contributions if needed.

That said, at the time of writing, discussions on the legal design and operational structure of the transaction remain fluid, with further details expected to emerge as negotiations progress and official documentation becomes public.

The Endgame Logic

Once the European Union transforms the frozen Russian reserves into collateral, it is obvious that the nature of those assets changes irreversibly. What began as a temporary sanction to impede the war effort becomes a structural feature of Europe's financial architecture. From that point, the reserves are no longer inert balances held in escrow; they are the backing for a loan to Ukraine and, by extension, a statement of political purpose. Europe has, in effect, assigned them a new function: to guarantee Ukraine's recovery and to link Russia's financial power to the consequences of its aggression.

This transformation creates obligations that cannot easily be unwound. Once debt has been issued against the collateral, creditors acquire contractual rights, Ukraine obtains long-term financing commitments, and the EU assumes reputational and fiscal responsibility for the scheme's integrity. To dismantle it later would require either Russia's cooperation or a major fiscal outlay by the Union. From that moment, the arrangement acquires its own path dependency; the assets are no longer simply frozen, but politically and financially committed. **The future of the frozen reserves can now unfold along only a few plausible paths.**

The first outcome would emerge if Russia accepted responsibility for wartime damages as part of a negotiated peace. In such a scenario, reparations payments would flow into a *Ukraine Reconstruction Facility*, redeeming the collateralised debt. Once those obligations were met, the immobilised reserves could, in principle, be released to Russia. This path presupposes a broader political realignment: a recognised Ukrainian government, a Russia seeking at least limited normalisation with Europe, and a diplomatic framework that ties sanctions relief to verified compliance. In this version of the endgame, Europe achieves both legal discipline and political closure: the assets return to their owner, but only after accountability has been enforced through reparations.

The second outcome would follow if Russia refused any form of reparation. In that case, debt instruments issued by the EU or its Special Purpose Vehicle would still need to be repaid when they mature. The legally challenging step would be to enforce the collateral—that is, to use the frozen reserves themselves to settle the debt. Formally, this would be an act of payment enforcement, not confiscation, but in practice the difference would be largely semantic. The reserves would be permanently transferred, closing the financial chapter of the war without a political settlement. Such a scenario assumes a prolonged confrontation between Russia and the West, continuing sanctions, and a hardened division of the international financial system into Western and revisionist spheres. Europe would emerge as a geopolitical creditor; its jurisdictional reach having been used to impose economic accountability where diplomacy failed.

The third outcome would result from a reversal within Europe itself. If political fatigue, economic strain, or changing leadership were to erode unity, member states might opt to unwind the mechanism before reparations are secured. The bonds would still have to be honoured, forcing the EU budget to absorb the repayment. Note that €140bn represents roughly 0.8 percent of EU GDP or 1.0 percent of the EU's public debt. This course would not only impose heavy fiscal costs but also undermine the credibility of the sanctions regime and the euro's reputation as a dependable reserve asset. Its underlying assumptions are domestic rather than geopolitical: a decline in public support for Ukraine, a weakening of transatlantic coordination, and a renewed search for accommodation with Moscow. Such an outcome would signal Europe's retreat from the principle that aggression carries lasting financial consequences and not least generate potential eurozone fiscal stress.

Taken together, these three pathways describe the full spectrum of potential outcomes of the collateralization process. A reparations settlement would anchor the mechanism in law and legitimacy; a default and enforcement outcome would consolidate Europe's use of financial power as a strategic instrument; and a reversal would expose internal division and strategic fatigue. Whatever the trajectory, once collateralization begins, the system becomes self-sustaining. The reserves are no longer merely immobilized—they are woven into Europe's fiscal and geopolitical fabric, their ultimate fate inseparable from the shape of the post-war order.

Endgame Scenarios for Collateralized Russian Reserves

Scenario	Core Logic	Underlying Geopolitical / Political Assumptions	Financial & Legal Consequences	Strategic Meaning
A – Reparations Settlement	Russia pays reparations that redeem the collateralized bonds; reserves are released.	• Negotiated peace and partial Western–Russian détente. • Recognized Ukrainian government; sanctions relief linked to compliance. • G7 and EU cohesion (mostly) maintained.	• Bonds redeemed with reparations payments. • Frozen assets legally returned; no precedent of confiscation. • Mechanism validated as lawful.	Confirms Europe's ability to enforce international law through finance; restores stability without eroding legal norms.
B – Refusal and Default	Russia refuses reparations; EU/G7 enforce collateral to repay bondholders.	• Prolonged confrontation; sanctions persist. • Russia isolated from Western finance; deepened global bifurcation. • Western political will remains maintained.	• Collateral executed; reserves permanently transferred. • *De facto* confiscation via enforcement. • Establishes enforceable precedent.	Demonstrates EU's use of financial power as deterrent; redefines euro-area assets as instruments of strategic accountability.
C – Policy Reversal	EU unwinds scheme and repays bonds from its own budget; reserves returned to Russia.	• Political fatigue within EU. • Transatlantic coordination weakens; economic pressures rise. • Desire for détente overrides deterrence.	• EU assumes full fiscal cost (~€140 bn). • Credibility of euro and sanctions regime damaged. • Legal clarity preserved but trust eroded.	Signals European retreat from strategic coherence; undermines deterrence and global confidence in EU resolve.

Strategic Implications: the Euro as a Normative Reserve Currency

The collateralisation of Russian sovereign assets could mark a decisive moment in the euro's evolution as an international currency. For the first time, yet in a narrowly defined case, the European Union is about to link the privileges of access to its financial system to the behaviour of sovereign states. What began as a sanctions measure begins to function as a normative boundary: states that violate fundamental rules of international order risk losing the protection traditionally granted to their reserves. **This represents a tentative transformation in the euro's identity—from a neutral transactional medium to an instrument that expresses Europe's collective understanding of lawful international conduct – and over time, reinforcing the euro's role as anchor for the rules-based international order, thereby building out the geopolitical status of the EU.**

At the centre of this transformation lies a profound legal question: can a state that violates another's sovereignty still invoke the immunity of its own sovereign assets? Russia's invasion of Ukraine exposes the contradiction. The same principle that protects the central-bank assets of a peaceful state has been used by an aggressor to shield itself from accountability. The European response—immobilising and subsequently collateralizing Russian reserves while respecting formal ownership—signals an emerging doctrine of conditional sovereignty: the right to asset protection is inseparable from the obligation to respect international law.

This shift does not necessarily abolish sovereign-asset immunity; it redefines it as conditional. Immunity remains the default for law-abiding states, but it no longer applies unconditionally to violators of fundamental norms that define international relations norms such as the prohibition of aggression. The collateralisation framework operationalises this principle: protection persists in form but is suspended in use. In effect, the euro area's legal order might become the first jurisdiction to treat access to its reserve assets as contingent on adherence to the international rule of law. Clearly, the legal basis of this action is based on an emerging interpretation being tested rather than an established principle of international law.

What then could be the future consequences of the application of this evolving doctrine?

A higher risk premium for revisionist states. In the immediate term, this development increases the political-risk premium for states seen as revisionist or sanction-prone. Holding large euro-denominated reserves now entails an implicit exposure to Europe's normative choices. Also, central banks in non-aligned or "neutral" states may view this as precedent-setting and diversify from euro assets not only for political reasons but to avoid "reclassification risk", generating wider reserve rebalancing, also accelerating the debate about the viability of crypto-based alternatives. The euro's global share may decline, but the commitment of its holders—states committed to stable and lawful relations—will improve.

Deeper trust among rule-abiding holders. Over time, this normative filtering could strengthen the euro's credibility among partners who value legal predictability and principled governance. For the EU and its allies, collateralisation reinforces confidence that Europe defends the integrity of its financial system, not merely its balance sheet. The euro becomes the currency of a rules-based community: smaller in reach but higher in trust. The ability to mobilise frozen sovereign assets without breaching due process demonstrates that Europe can exercise power through law, not outside it.

The euro as a rules-based reserve currency. If this trajectory continues, the euro's long-term identity will diverge from that of the U.S. dollar. The dollar remains the universal transactional currency—accepted everywhere, constrained mainly by U.S. domestic law and global demand for liquidity. The euro, by contrast, evolves into a rules-based reserve currency, one that embeds legal conditionality into access and protection. Its global footprint may remain smaller, but its normative density increases: to hold euros is to signal participation in a lawful order.

This evolution carries both risks and opportunities. It may deter some economies from holding euros, perceiving conditionality as political exposure. Yet it also gives Europe something it has long lacked: a distinctive monetary identity grounded in principle rather than scale. By connecting financial privilege to international responsibility, the euro area begins to project a form of legal power—the capacity to define what constitutes legitimate sovereignty in economic relations.

Collateralising Russian reserves thus becomes more than a financing tool for Ukraine; it is a catalyst for redefining how the European Union links law, finance, and power. The euro's strength will no longer depend solely on the size of Europe's economy, but on the credibility of its commitment to order. In this sense, the euro's future as a reserve currency lies not in neutrality but in normativity: a currency that rewards compliance with the foundations of international law, penalises aggression, and binds sovereignty to responsibility.

[1] See for background information: European Parliament Briefing. Confiscation of Immobilised Russian Sovereign Assets. September 2025. https://www.europarl.europa.eu/RegData/etudes/BRIE/2025/775908/EPRS_BRI(2025)775908_EN.pdf
[2] Council Regulation (EU) No 269/2014, Council Regulation (EU) 2022/334, and Council Decision (CFSP) 2022/327, as published in the Official Journal of the EU.
[3] Euroclear. Euroclear Continues to Deliver String Results in 2024. 2 February 2025. https://www.euroclear.com/newsandinsights/en/press/2025/mr-05-euroclear-delivers-strong-results-in-2024.html?utm_source=chatgpt.com
[4] See also Daniel Franchini. Immobilised Assets, Extraordinary Profits: The EU Council Decision on Russia's Central Bank Reserves and its Legal Challenges. EJIL : Talk !, 1 March 2024. https://www.ejiltalk.org/immobilised-assets-extraordinary-profits-the-eu-council-decision-on-russias-central-bank-reserves-and-its-legal-challenges/
[5] Friedrich Merz. A New Financial Impetus for Peace in Ukraine. Financial Times. 25 September 2025. https://www.ft.com/content/3aacc930-9f5e-4558-90f1-62bf47a31cd5. About possible retaliation: Timothy Ash. Kremlin Financial Retaliation? Empty Threats. CEPA. 6 October 2025. https://cepa.org/article/kremlin-financial-retaliation-empty-threats/

This analysis and all associated assessments, data, and commentary are produced for informational and analytical purposes only. They do not constitute political endorsements, investment advice, policy prescriptions, or predictive forecasts. They are based on publicly available data, government and institutional sources, and structured expert assessments, including the use of AI-enabled analytics to support indicator standardization and comparative analysis.

While artificial intelligence tools assist in processing large datasets and identifying patterns, final judgements are subject to human expert validation to ensure methodological rigor and contextual accuracy. No warranty is made regarding the completeness, timeliness, or accuracy of the information contained herein.

The publishing entity accepts no liability for any direct, indirect, incidental, or consequential losses arising from the use or reliance upon this material. Any reproduction or redistribution of this document must retain this disclaimer and cite the original source.

Use of this analysis constitutes acceptance of these terms.

Contacts:

kf@sovereign-investors.com
behrendt@geoeconomica.com