The impact of Western sanctions on Russia and how they can be made even more effective

REPORT

By Anders Åslund and Maria Snegovaya

While Western sanctions have not succeeded in forcing the Kremlin to fully reverse its actions and end aggression in Ukraine, the economic impact of financial sanctions on Russia has been greater than previously understood.

Dr. Anders Åslund is a resident senior fellow in the Eurasia Center at the Atlantic Council. He also teaches at Georgetown University. He is a leading specialist on economic policy in Russia, Ukraine, and East Europe.

Dr. Maria Snegovaya is a non-resident fellow at the Eurasia Center, a visiting scholar with the Institute for European, Russian, and Eurasian Studies at the George Washington University; and a postdoctoral scholar with the Kellogg Center for Philosophy, Politics, and Economics at the Virginia Polytechnic Institute and State University.

Key points

- While Western sanctions have not succeeded in forcing the Kremlin to fully reverse its actions and end aggression in Ukraine, the economic impact of financial sanctions on Russia has been greater than previously understood.
- Western sanctions on Russia have been quite effective in two regards. First, they stopped Vladimir Putin's preannounced military offensive into Ukraine in the summer of 2014.
- Second, sanctions have hit the Russian economy badly. Since 2014, it has grown by an average of 0.3 percent per year, while the global average was 2.3 percent per year. They have slashed foreign credits and foreign direct investment, and may have reduced Russia's economic growth by 2.5–3 percent a year; that is, about $50 billion per year. The Russian economy is not likely to grow significantly again until the Kremlin has persuaded the West to ease the sanctions.

Acknowledgements

The authors want to thank the following people for discussions or comments on drafts of this paper: Blaise Antin, Timothy Ash, Daniel Fried, Julia Friedlander, Daniel Gros, Gary Hufbauer, Iikka Korhonen, Brian O'Toole, and Elina Ribakova. The responsibility for any mistake remains with the authors.

When analyzing a Western policy on Russia, one must first assess the nature of Russia's government.[1] The authors call it "kleptocratic" or "neopatrimonial" autocracy, as such regimes sustain loyalty of elites and population through the redistribution of benefits and spoils. The two main objectives of Vladimir Putin's system are to maintain power and to enrich a narrow elite. The Kremlin's foreign policy should be seen from this perspective. It is designed to promote the interests of the current Kremlin elite, not the Russian nation. One means of doing so has been small victorious wars, as described by a century-old Russian term. As the Russian economy has barely grown since 2014, the Kremlin has become more cautious with major real warfare. Instead, it pursues cheaper, so-called hybrid warfare, such as cyberattacks and assassinations.

For the West, a real war with Russia has been out of question. But, since Russia's aggression in Ukraine in 2014, the West has felt a need to do something substantial to impede Russian foreign aggression. Its natural choice has been sanctions. The West has focused on two kinds of sanctions: financial sanctions and personal sanctions on human-rights violators and corrupt businessmen working for the Kremlin. In addition, the West has introduced some restrictions on the export of technology, while it has abstained from the previously common trade sanctions. In general, sanctions are becoming more diverse, with the share of trade sanctions falling, while financial and visa sanctions are becoming more popular.[2]

This report aims to assess how effective Western sanctions on Russia have been in macroeconomic terms, and what could be done to render them more effective. Its focus is the impact of sanctions on gross domestic product (GDP). The authors argue that while Western sanctions have not succeeded in forcing the Kremlin to fully reverse its actions and end aggression in Ukraine, their effect has been quite substantial with regard to the weakening of the Russian economy and stopping further military aggression. The financial sanctions had the greatest impact on Russian GDP, by restricting Russia's access to foreign capital, including credits to both the government and the private sector, as well as foreign direct investment (FDI). A secondary impact of the financial sanctions was enticing the Kremlin to pursue a more restrictive fiscal and monetary policy than would have been ideal for economic growth.

This report distinguishes microeconomic effects of sanctions as well, but does not try to quantify them. When passing judgment on the effect of sanctions, the authors make the following distinctions: Did the sanctions roll back objectionable policies, contain them, or deter Russia from further objectionable policies? First, however, it is important to assess the real problem with Putin's regime and its international repercussions.

What is the problem with Putin's regime?

Putin has proven himself a skillful politician. In his first term, 2000–2004, he was everything to everybody, and successfully consolidated power. In his second term, 2004–2008, he extended his control to the big state companies by appointing his loyalists as their chief executives. He has continuously stripped massive amounts of assets from the big state companies, to the benefit of his cronies. Since 2009, he has ignored economic growth, and the standard of living has fallen since 2014. When Putin returned as president in 2012, he rendered his regime more repressive, and its repression is rising further.

Putin's way to power was marked by a series of controversies including dubious explosions of buildings that cost a few hundred Russian citizens their lives[3], a war in Chechnya, and a row of serious human-rights violations.[4]

Russia's political stability under Putin must not be exaggerated. The country has experienced several waves of popular unrest. In 2005, senior citizens protested against a pension reform. And, in 2011–2012, a

1 This report follows the line of Daniel Fried and Alexander Vershbow, How the West Should Deal with Russia, Atlantic Council, November 23, 2020, https://www.atlanticcouncil.org/in-depth-research-reports/report/russia-in-the-world/.

2 Gabriel Felbermayr, et al. "The Global Sanctions Data Base," European Economic Review, October 2020, 129, https://voxeu.org/article/global-sanctions-data-base.

3 Alexander Litvinenko and Yuri Felshtinsky, Blowing Up Russia: The Secret Plot to Bring Back KGB Terror (London: Gibson, 2007); John Dunlop, The Moscow Bombings of September 1999: Examinations of Russian Terrorist Attacks at the Onset of Vladimir Putin's Rule, second edition (New York: Columbia University Press, 2014).

4 Peter Baker and Susan Glasser, Kremlin Rising: Vladimir Putin's Russia and the End of Revolution (New York: Scribner, 2005); Luke Harding, Ma a State (London: Guardian, 2011); Masha Gessen, The Man Without a Face: The Unlikely Rise of Vladimir Putin (New York: Riverhead Books, 2012); Karen Dawisha, Putin's Kleptocracy: Who Owns Russia? (New York: Simon & Schuster, 2014).

A man holds a portrait of the killed journalist Anna Politkovskaya as a woman lays flowers during a commemorative rally in St.Petersburg, October 7, 2009. REUTERS/Alexander Demianchuk

series of protests shaked Moscow and several regions in response to an obviously fraudulent election in which Putin returned to the presidency after a brief stint as prime minister. Since 2019 another series of country-wide protests have taken place across the multiple Russia's regions. But, nothing seemed to seriously shake Putin. He has responded by gradually turning his regime more repressive.

His presidency has been marked by numerous murders seemingly initiated by the Kremlin, such as those of investigative journalist Anna Politkovskaya in Moscow in 2006, Federal Security Service (FSB) defector Alexander Litvinenko in London in 2006, and opposition leader Boris Nemtsov outside of the Kremlin in 2015—and many other completed or failed attempts at people's lives.[5] Such murders have also been revealed or suspected abroad, in Qatar, London, Washington, Berlin, and Vienna.[6] Bellingcat has uncovered that the FSB maintains a murder squad.[7] Assassinations at home and abroad appear to be Putin's standard procedures.

To understand how Putin's regime works, one needs to first understand its neopatrimonial nature. In regimes like Putin's, personalistic rulers hold on to

5 Luke Harding, A Very Expensive Poison: The Assassination of Alexander Litvinenko and Putin's War with the West (London: Vintage, 2017). Harding's Ma a State is possibly the best presentation of Putin's violence, but there are many others. John Dunlop wrote an excellent book on Boris Nemtsov's assassination: John Dunlop, The February 2015 Assassination of Boris Nemtsov and the Flawed Trial of His Alleged Killers (Stuttgart: Ibidem, 2019).

6 Steven Lee Myers, "Qatar Court Convicts 2 Russians in Top Chechen's Death," New York Times, July 1, 2004, https://www.nytimes.com/2004/07/01/world/qatar-court-convicts-2-russians-in-top-chechen-s-death.html; Heidi Blake, et al., "From Russia With Blood," Buzzfeed, June 15, 2017, https://www.buzzfeed.com/heidiblake/from-russia-with-blood-14-suspected-hits-on-british-soil; Jason Leopold, et al., "The US Death of Putin's Media Czar Was Murder, Trump Dossier Author Christopher Steele Tells the FBI," Buzzfeed, March 27, 2018, https://www.buzzfeednews.com/article/jasonleopold/christopher-steele-mikhail-lesin-murder-putin-fbi; "Germany Accuses Russia of Berlin Park Assassination," BBC, June 18, 2020, https://www.bbc.com/news/world-europe-53091298; Andrew Kramer, "In a Death, Details of More Russian Murder-for-Hire Plots," New York Times, July 9, 2020, https://www.nytimes.com/2020/07/09/world/europe/chechnya-russian-murder-vienna.html.

7 "Navalny Poison Squad Implicated in Murders of Three Russian Activists," Bellingcat, January 27, 2021, https://www.bellingcat.com/news/uk-and-europe/2021/01/27/navalny-poison-squad-implicated-in-murders-of-three-russian-activists/.