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**International Business**



**Sanctions and Counter-sanctions – What  
was the effect of Crimean crisis on Russian  
economy?**

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**Declaration**

I hereby declare that I am the sole author of the thesis entitled “Thesis Title “. I duly marked out all quotations. The used literature and sources are stated in the attached list of references.

In Prague on: 10.04.20

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### **Acknowledgement**

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# Abstract

In this thesis it will be briefly looked at reasons of imposing sanctions on the first place and looking at current sanctions imposed by EU, USA and other countries as well as Russian countersanction imposed as a response towards Western countries. Main assumption is that countersanctions had a higher impact on Russian economy compared to sanctions that were enforced on Russian Federation on the first place. Most of information shows that first and second round of sanctions from Western countries had very specific impact whereas Russia's own counter-sanctions had a clear negative effect on the welfare of the average Russian household, all that in mind it could have had a different effect on Russian economy however Russian Federation also faced the decrease in crude oil price. One of the main reasons of picking this topic is because Russia is still facing consequences of its decisions and I had to find out what is the exact effect of Crimean Crisis. And in order to understand what happened to Russian Economy I had to analyze different resources in order to compare them and compile the data. In this paper we will closely look at EU sanctions on Russia and Russian countersanctions. The reason why we are looking closer at EU sanctions is because most sanctions towards Russia were implemented by EU members and other countries either matched them or didn't implement. Therefore USA, Canadian, Australian sanctions will still be mentioned in the future text, however it will be mainly focused on EU sanctions towards Russia and other way round, when we talk about Russian countersanctions we will look on it's impact on EU as EU had faced the most consequences from it.

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# 1. Introduction

18<sup>th</sup> of March of 2014 Crimea was officially annexed by Russian Federation. Following the annexation of Crimea and Sevastopol as well as all hostile operations in Ukraine by Russian soldiers, sanctions were imposed on Russian individuals and certain government owned companies by United States, European Union, Canada and other countries.<sup>1</sup> There were two waves of sanctions towards Russia. The first wave of sanctions was very limited and was aimed mainly at government body and Russian oligarchs who had a close connection to the government. The main reason for those sanctions is to freeze any assets that were owned by those individuals outside Russia and impose a movement restriction. In the sense sanctions and countersanctions were very asymmetrical due as European Union, USA and other countries had the intention of limiting Russian entities towards international finance market, technology exports, movements of assets etc. Whereas countersanctions were specifically aimed at banning specific imports. Primarily those products were agricultural such as but not limited to dairy, fish, meat etc. It's fair to say that it could be considered as "import-substitution" scheme which was aimed to increase competitiveness of domestic producers however at a time Russian agriculture was incredibly underdeveloped and had very short range of economy of scale which caused scarcity of production.

It is very hard to calculate the exact impact of sanctions and counter sanctions on Russian economy due to the reasons that Russian economy suffered at exact same time due to the decrease in crude oil price. Due to the specificity of sanctions it's fair to say that they've had lower impact on Russian economy compared to plunged oil prices as oil and gas are responsible for more than 60% of Russia's exports and provide more than 30% of the country's gross domestic product (GDP). Even though countersanctions had an agricultural incline, due to inability for local producers to fill in the gap for consumers as well as oil price, those sanctions had an additive effect on Russian economy and especially consumers. The food sector in Russia clearly suffered from 2014-2015

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<sup>1</sup> (U.S. DEPARTMENT OF THE TREASURY, 2018)

as prices skyrocketed and there were not enough products on the market available and inability to produce more in a short time.

In this thesis I am not evaluating the effectiveness of sanctions, imposed by EU, USA and other countries towards Russia nor countersanctions imposed by Russian Federation towards banning product imports, but rather looking at the effect those sanctions had on the economies and trade. As sanctions imposed on Russia were rather based on certain entities, we will more closely look at countersanctions and what effect those had on Russia and other countries. Therefore the aim of this thesis is analyze the effect and the difference of it between sanctions that were imposed by Western countries and counter sanctions from Russia. And to see what exact impact it had on macroeconomics of Russia and the spillover towards Russian consumers.

## 2. Chronology of EU, Western and Russian economic sanctions

As a reaction to Russian illegal actions EU and Western countries took defensive measures towards Russia. In the spring of 2014 decisions were made concerning travel restrictions and asset freezes for selected individuals, an import ban on goods that were produced in Crimea or Sevastopol followed later, before a more in depth package of targeted economic sanctions was implemented July 2014. It includes:

- measures to restrict Russia's access to EU capital markets,
- an embargo on the imports and exports of arms and related material from/to Russia,
- a prohibition of exports of dual use goods and technology for military use in Russia as well as
- of products that are destined for deep water oil exploration and production, arctic oil exploration or production and shale oil projects in Russia.<sup>2</sup>

Responding to the sanctions, Russia banned imports of wide arrange of agricultural products from countries that imposed sanctions on Russia, in particular the USA, EU, Canada, Australia and Norway. This import ban includes, milk and milk products including raw milk and all food related products containing milk as well as fish, vegetables and fruits. Any kind of meat including sausages, smoked meet, beef, pork, etc. It is needed to note that the EU sanctions concern only a very small group of products, exhibiting a minor share in total EU exports to Russia. The Russian ban or better be called embargo on products, on the other hand, seems more impactful both for the EU, with Russia being the second most important destination market for agri-food goods, and Russia since the EU is its largest supplier of agri-food products.

The EU sanctions on the other hand affected many sectors. Export and import of military equipment and arms were banned. Export of certain types of goods related to oil exploration and

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<sup>2</sup> (EU Council, 2020)

production was also banned. Most important one was probably the curtailing of long-term financing of Russian companies that had no direct involvement with the fighting in Donetsk and LNR regions. Investors in the EU were forbidden to provide long-term financing to Sberbank, VTB, Gazprom bank, and several other biggest banks in Russia.

Over the past six years, Russia has been developing under the conditions of sanctions imposed on it by Western countries in connection with the situation in Ukraine and for several other reasons such as Russian Middle East politics. The number of reasons for the introduction of sanctions is expanding against Russian companies. For example, in April 2018, restrictions due to “trade with the DPRK authorities” and “long-term relations” with Pyongyang were imposed on Agrosoyuz. According to the official position of the Russian authorities, unilateral sanctions against Russia are unlawful measures of a restrictive nature, since they have no international legal justification<sup>3</sup>. In addition to personal sanctions, the first of which were introduced in December 2012 and a list was periodically expanding since July. In 2014, strict sectoral sanctions began to enforce in relation to financial, energy, defense and mining and metallurgical industries. These included restrictions on loans and investment services (prohibition of operations with new debt with a maturity of more than 90 days or shares of the banks) oil and gas companies with state participation), a ban on the supply of weapons, military equipment and dual-use technologies, high-tech equipment and technologies. In September 2014, the sanctions from the USA extended to energy companies, as well as from EU side - on energy companies and banks. In December 2014, the United States imposed sanctions on the Republic of Crimea, which were subsequently supported by EU countries and other individual states. These sanctions included a ban on the import and export of goods, services or technologies to and from the Crimea, a ban on investments in this region, and termination of VISA and MASTERCARD bank cards. Note that after changing the working conditions of payment systems in Russia and closing payments to the domestic Russian center, the operation of VISA and MASTERCARD cards of Russian production in Crimea was restored. As of 2020, the cards of these payment systems of foreign banks are not functioning on the peninsula, and contactless payment technologies Android Pay, and Apple Pay are not available. In August 2017, the USA introduced second wave of sanctions against

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<sup>3</sup> (RIA news, 2014)

individuals and legal entities of third countries cooperating with companies from Russia or investing in projects with Russian participation more than 33%. In April 2018, toughening of sectoral sanctions took place: a number of Russian companies were included in the list of the US Treasury Specially Designated Nationals (SDN), which meant for Russia not just a ban on funding from US nationals, but also the freezing of assets in the US and the ban for any operations with persons involved in the SDN list for US residents and the threat of secondary sanctions for non-residents.

The next wave of sanctions against the Russian Federation took place in August, when the United States introduced a ban on the supply of military and dual-use products also on any help to the Russian Federation (except urgent humanitarian aid, food supplies products or agricultural goods) and the provision of loans and financial support to the Russian authorities.

Thus, in general terms, the current sanctions against the Russian Federation by the US and the EU are as follows.

## 1. Personal sanctions

- I. From the U.S. side (Specially Designated Nationals and Blocked Persons List, SDN) - visa restrictions, freezing the property and accounts, a ban on the export / re-export of goods and services, transfer of technology and materials, a ban on cooperation and business relations with individuals and legal entities from the list, as well as with companies in which physical or legal entities from the list own 50 or more percent of particular company.
- II. On the EU side — visa restrictions, blocking of all assets in the EU, a ban on any transactions related to blocked assets (after 18<sup>th</sup> of March) in relation to individuals and companies, including subsidiary companies with a holding of more than 50% (except registered in the EU).

## 2. Sectoral Sanctions

- I. From the USA (Sectoral Sanctions Identifications, SSI):

- i. in the financial sector: a ban on the provision of financing to financial institutions of the Russian Federation, on any operations with property and assets <sup>4</sup>;
- ii. in the energy sector: a ban on the provision of financing for operations with valuable property securities with a maturity of more than 60 days<sup>5</sup>, a ban on the export / re-export of goods, technologies, and the provision of non-financial intelligence services and oil production on the Arctic shelf, deep-sea oil production, shale gas production (for projects initiated after 29 January 2018, the ban valid regardless of location) <sup>6</sup>;
- iii. in the defense sector: ban on export / import of weapons and related materials, goods and services purpose, a ban on the provision of debt financing for a period of more than 30 days, any kind of transactions involving property (applies to a number of strategic companies) <sup>7</sup>
- iv. Secondary sanctions: against non-US individuals and legal entities cooperating with Russian companies in the intelligence and defense industries and investing in projects in which Russian involvement is more than 33% (mainly in the oil and gas sector) <sup>8</sup>

II. From the EU:

- i. in the financial sector: the prohibition to individuals and legal entities of the EU of the purchase / sale, the provision of brokerage services and the provision of any kind of assistance in relation to securities and money market instruments with a maturity of more than 90 / 30 days to a number of Russian credit organizations or other credit organizations, 50% of the

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<sup>4</sup> ( US Department of the Treasury, 2017)

<sup>5</sup> ( US Department of the Treasury, 2017)

<sup>6</sup> ( US Department of the Treasury, 2014)

<sup>7</sup> ( US Department of the Treasury, 2017)

<sup>8</sup> (Congress, 2017)

shares of which belong to persons from the sanctions list (Sberbank, VTB, Gazprom bank, VEB, Russian Agricultural Bank)<sup>9</sup>

- ii. in the energy sector: the prohibition of individuals / legal entities from the EU buying / selling, providing brokerage services and any kind of assistance regarding securities and monetary instruments the market with a maturity of more than 30 days the largest oil companies (Rosneft, Transnet, Gazprom); transaction licensing procedure introduced by goods and technologies in the field of mining and exploration oil and other minerals<sup>10</sup>
- iii. in the defense sector: a ban on the purchase / sale / transfer of weapons and ammunition, dual-use goods, technology for military use<sup>11</sup>

### 3. Crimean sanctions

- I. From the USA: ban on the import and export of goods, services or technologies in the Crimea and from the Crimea, a ban on investment in this region, ban on banking services in the region<sup>12</sup>
- II. From the EU: a ban on the import of products from the Crimea, for export to Crimea of some goods and technologies in the fields of transport, telecommunications and energy, to invest in Crimea, to conduct tourism business, to enter to ports and use of the airport of Crimea, with the exception of emergency cases<sup>13</sup>

### 4. Additional set of sanctions

- I. On the part of the United States — freezing deals with the FSB and the Main Directorate of the General Staff of the RF Armed Forces, ban on any assistance (except urgent humanitarian aid, food supplies products or agricultural goods), to provide loans and financial support to state authorities, limiting funding through

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<sup>9</sup> ( European Union, 2014)

<sup>10</sup> ( European Union, 2014)

<sup>11</sup> ( European Union, 2014)

<sup>12</sup> (US Treasury, 2014)

<sup>13</sup> (European Council, 2020)

privatization or investment in the amount of 10 million dollars, expansion of personal sanctions, the creation of additional sanctions lists for Syria, North Korea (for the export of goods and services), actions in the Crimea and Donbass, undermining cybersecurity etc.

- II. On the EU side, suspension of financing of projects in Russia by the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD)

## 5. Exceptions

- I. From the USA: general and special licenses may be issued by the Office for Foreign Control Assets (OFAC) to take certain transactions out of sanctions, for example, on the export / re-export of agricultural goods, medicines, medical equipment, spare parts, separate services and software in Crimea, personal non-profit transfers.
- II. From the EU: lifting the ban on goods that were provided for verification and controlled by Ukrainian<sup>14</sup>

It is important to note that export control is also a sanction tool, although it is, according to classification The WTO is a non-tariff measure of foreign economic regulation and is generally prohibited. However, the provisions of the WTO do not cover trade in arms and military products, as well as goods related to national security issues, which the United States has successfully used, licensing not only the export of goods, but also the transfer of technology. Pressure was also exerted on Russia through procedural (suspension of forms of cooperation with international economic organizations) and diplomatic sanctions (several waves of expulsion of Russian diplomats). Of the companies on the U.S. sanctions list, the largest share is held by companies in the fuel industry and financial sector (Fig. 4). Currently under US sanctions there are 427 Russian organizations and companies (including subsidiaries) and 335 of individuals<sup>15</sup>; under EU sanctions—21 organization and company; and 85 individuals.<sup>16</sup> Also the US sanctions list

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<sup>14</sup> (European Council, 2014)

<sup>15</sup> (CSIS.ORG, 2020)

<sup>16</sup> (European Council, 2014)

includes eight Russian courts and 47 foreign companies punished for cooperation with Russia, the largest share of which are companies of Cyprus (offshore zone), Ukraine and Finland.

Of all sanctioned Russian companies, 82 conducted foreign economic activity. From out of which 56 companies are importers, the volume of their imports in 2017 was 4,25 billion dollars. 58 companies are exporting with a total export volume of 107, 68 billion dollars. Moreover 43 of them carry out export activities through intermediaries (for 32 companies, the share of exports through intermediaries exceeds 96%). Obviously, the sanctions are directed primarily against companies exporting the oil and gas sector, while out of 23 companies exporting the oil and gas sector, seven carried out deliveries to the USA in 2017.

Exports of other sanctioned companies include goods groups TN VED (Commodity nomenclature of foreign economic activity

- “Nuclear reactors, boilers, equipment and mechanical devices; parts thereof”,
- 85 “Electrical machinery and equipment, their parts ”,
- 73 "Products from black metals",
- 90 “Tools”,
- 93 “Weapons and ammunition”,
- 87 "Ground transportation means, except for railway and tram"

In 2017 the products listed above, were delivered mainly to China, India, Turkey, Algeria, Peru. For example, the company Izhora Plants in 2017 total export volume was 619,6 million dollars and included mainly supplies of equipment for nuclear reactors, capacities from ferrous metals, electric heating devices to Bulgaria, China, India. The main purchaser of measuring and control instruments, information carriers and fiberglass products by AO VPK "NGO Engineering" is currently India. The import products of sanctioned companies are mainly related to procurement of equipment and components from European countries to produce machinery, equipment, electronics, ships and aircraft. Largest volume import is observed at OJSC “Surgutneftegas” (2,1 billion dollars), which purchases special mechanical equipment (8479 TN VED) seamless steel pipes (7304 VED TN VED), special motor vehicles (8705 TN VED) mainly imported from the USA and Singapore. In second place in terms of import— Power Machines PJSC (368 million dollars), purchasing liquid pumps (8413 TN VED), special mechanical equipment (8479 HS) and

hydraulic turbines (8410 VED) mainly from Germany, Netherlands and China. From the number of subsidiary companies, only five procured in the United States in 2017. From the companies involved in foreign economic activity, 32 are both exporters and importers. For example, OOO Kinef exported in 2017 oil, oil products, natural gas mainly to the Netherlands, Denmark and the USA, despite the fact that they purchased catalysts, air pumps, transmission equipment in France, the USA, and the British Virgin Islands.

In general, there is a tendency towards an increasing commercialization of sanctions especially from the side of the United States, that is, in fact application of restrictive business practices, unfair competition for the largest and successful Russian companies. Due to sanctions, American corporations, for example, have gained benefits and additional opportunities in the markets of aluminum and weapons. There is a combination of sanctions with traditional trade restrictions, since in both cases the interests of American business are promoted by non-competitive methods. On aluminum, the United States increased import customs duties and at the same time they have imposed sanctions against the owner of RUSAL and RUSAL itself. In this case RUSAL was not chosen as a target by chance. At first, compared to other major metallurgical companies, the RUSAL: aluminum and steel exporting company have significant weight in US imports, they have exported about 7% aluminum and about 9% of iron and steel from Russia into USA in 2017. At the same time, the import volume of US aluminum from Russia, and its share in total US imports since 2013 was significantly increasing.

It is important that companies such as NLMK and EVRAZ have production facilities in the United States, to which only primary raw materials are being imported. For example, NLMK's North American division produces 2,3 million tons of rolled steel using 450 thousand tons of cast iron produced at NLMK's Russian division. EVRAZ supplies from Russia 500 thousand tons of slabs for further processing in the United States. This allows companies to use their bargaining power, for example, due to threats of closure of production and reduction jobs that the US Presidential Administration usually considers and takes into account. From this point of view, the highest chance not to get sanctioned is for those companies that are in cooperation with US corporations or individuals that have the great interest. This, for Russian companies, indicates the need to aggressively build up cooperation with American companies in order to make the process of introducing new sanctions as difficult as possible. If we confine ourselves to considering sectors

of the economy, producing “tradable” goods (agriculture, forestry, hunting, fishing and fish farming; mining fossils; manufacturing industries), then in these sectors in alone, approximately 5500 companies whose global ultimate owner located in countries in USA and EU; of which 1523 companies (28%) - EU (excluding Cyprus, Luxembourg and the Netherlands, representing a large number of offshore companies), 362 companies - USA (6,7 %). Largest number American companies represented in the Russian sector food production (101 company), and EU companies - in agriculture and hunting (273 companies), production of rubber, plastic products and other non-metal products (202 companies), metallurgical production and manufacture of finished metal products (172 companies), the food industry (151 company) and the production of machinery and equipment (150 companies). Companies in these sectors can be seen as potential withdrawal lobbyists of softening sanction measures or at least non-tightening of anti-Russian sanctions by the EU and the US, respectively. On the other hand, the share of American companies, especially in comparison with a share of European companies, it is extremely low in agriculture, fisheries and fish farming, the production of rubber, plastic products and other non-metal products, the metallurgical industry, manufacturing computers and electrical equipment, printing, which indicates the weak security of these sectors from US sanctions pressure. Ultimately sanctions and other restrictive measures of the USA, EU countries, Canada, Australia and other countries against Russia simultaneously with the declaration of political goals have a pronounced economic dimension. One way or another, sanctions are detrimental to the Russian economy, the defense industry, energy and others. complexes, financial and political systems, international image, and undermining Russian position in the world economy and political space. It should also be noted that the United States is forming a system of measures and tools for US interaction and their allies, the positions of third countries and their possible reaction (primarily China). Mostly very specific and targeted sanctions are being applied towards certain individuals and companies, then situation is being monitored by how countries going to reply on those sanctions. Most important reactions that USA is interested are from Russia, allies of the USA and then the world community. Over the years, sanctions seem to strengthen, diversify in a direction that more and more individuals and companies that are of Russian origin are getting sanctioned. In particular, the United States initiated consideration of the second round of sanctions against Russia, which may include a ban on loans to The Government of the Russian Federation( with the exception of loans for food and

agricultural products, mutual trade but excluding the exports of agricultural products to the US), for air travel provision to Russian companies with state participation, freezing diplomatic relations, as well as a ban on the import of products and services by companies from the sanctions list . In addition, the U.S. Congress is considering a bill banning operations and freezing assets of seven largest Russian banks (VEB, Sberbank, VTB, Gazprom bank, Bank of Moscow, Russian Agricultural Bank, Promsvyazbank). At the same time, the EU announced an expansion anti-Russian sanctions in December, regarding restrictions for the defense, banking and energy sectors of the Russian Federation. The risks of further expansion of sanctions remain very high. Areas for potential sanctions include tightening restrictions on already sanctioned companies, expanding personal and sectoral sanctions, restrictions by other countries, prohibition operations with Russian government debt, disconnection from SWIFT, limitation of the liquidity of reserves of the Central Bank of the Russian Federation. Thus, to create a lobby among American and European companies, in the long term counteracting the expansion and tightening of anti-Russian sanctions, it is necessary to identify point-to-point mutual interests with American and European companies, especially those working in sectors that are most vulnerable to sanction pressure. It is about American companies in agriculture, fisheries and fish farming, the production of rubber, plastic products and other non-metallic products, metallurgical industry, computer manufacturing and electrical equipment, printing activities. Promising identification of beneficiaries and losers appears from sanctions at the level of individual companies (corporations), located under US and EU jurisdictions. For beneficiaries it is necessary to create additional opportunities in the Russian market, the loss of which could be critical for their business, and with the losers, one should work as lobbyists for easing the sanctions regime or as lobbyists for stabilizing the level of sanction pressure.

### 3. Russian policies prior and after sanctions.

In this part we will talk closely at the relationship of Russian countersanction and their attempt to implement the import substitution program and policies. Russian government previously already had an agenda to boost the domestic production therefore it wasn't just a reaction to banning agriculture related food products. In yearly 2000's and 2005 we can see radical changes in import policies that are aiming at economical independence of Russia <sup>17</sup>. Another important factor in the development of the agricultural sector is that the import substitution program in the industry was officially adopted back in 2012, when in the message of the President of the Russian Federation The Federal Assembly has been tasked over the coming years fully provide the country with domestic food. Then Vladimir Putin noted that global food demand is steadily growing, especially in developing countries, and Russia accounts for 55% fertile land of the planet. Therefore, with the involvement of all its resources, the country is capable of not only ensuring its own independence in this area, but also enter the foreign market and become the largest supplier nutrition. We can see that Russian economical agenda was striving to become more and more independent and become self-sufficient however by the beginning of Crimean Crisis and implementation of counter sanctions, Russian economy was nowhere near to being self sufficient as well as domestic producers couldn't possibly produce in the volume that it would fill in the gap of import.

After the introduction of sanctions and anti-sanctions, the Russian government began adopting legal acts aimed at implementing policies import substitution. The first of these was the RF program on "Development industry and increase its competitiveness ", approved By the Cabinet of Ministers in April 2014. This program has proclaimed the main method of implementing the import substitution policy in the country is to reduce the share of imports of products, both finished and used for further processing by manufacturers in Russia. Later, in May 2014 Russian President Vladimir Putin signed a list of instructions on additional measures to stimulate economic growth.

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<sup>17</sup> (Russian government website, 2005)

The Government of the Russian Federation has prepared an import substitution assistance plan in industry, and at the end of 2014 a new program was approved import substitution in agriculture, food embargo.<sup>18</sup> The government also began to implement a set of measures to financial support for the development of import substitution policies. The main instruments of financial assistance are subsidies, and co-financing of research, the provision of grants and preferences for public procurement. In addition, to increase volumes lending to organizations of the real sector of the economy for long-term and preferential terms, an investment support program was adopted projects in which the production stage is implemented in Russia

Overall, we could see the pattern in which Russia was gradually preparing and making steps in direction of autonomy it could have seen a different impact of Crisis if there wouldn't been any other external factors affecting Russian economy.

### 3.1 Factors assisting, the weakening of Russian economy

As it was mentioned before it's rather hard to assess the whole impact of sanctions on Russia by Western countries and Russia's reciprocated measures since at the same time as sanctions came into effect - the oil prices, a big part of GDP and exports, considerably dropped resulting a big drop in GDP throughout 2014-2015 as Figure 1. Depicts. This negative oil price shock adversely affected output growth and exchange rates. Ruble exchange rate skyrocketed as it went up from 31.1RUB per 1 USD way up to 69.2 and at some point, reached 82.1 RUB for 1 USD. (Figure 2) It is argued that these multiple hits are what caused massive economic problems that Russia was inevitably faced in 2014-2015. Since 2007 Russian economy already has been experiencing a recession as well as economic crisis of 2008/2009 which caused the deterioration in health care, education and culture but having price oil plunging as well as sanctions with countersanctions just made the situation much more unstable.

Here is the summary of what Russian economy faced at the time of 2014-2015:

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<sup>18</sup> (Tymoshenko, 2015)

- an economic slowdown, with GDP growth slowing to 0.7 % in 2014, before contracting by 2.8 % in 2015.
  - a massive depreciation of the ruble by more than 50 % against the US dollar in 2015.
  - a substantial increase in the inflation rate, especially with respect to food prices
  - budgetary pressure.
- a substantial outflow of capital, deteriorating Russia's capital and financial account balance.<sup>19</sup>



Figure 1 GDP of Russia (Source: Trade economics)

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<sup>19</sup> (Monaghan, 2014)



Figure 2 Ruble exchange rate (Source: XE Currency Charts)

## 4. Macroeconomics effect of sanctions on the economy

Overlooking the impact of other factors, all sanctions potentially bringing out the serious economic consequences both for Russia and EU, accounting the fact that before Crisis for past couple of years the volume of trade kept steadily rising: Russia was 4th biggest trade partner with EU with a share of 7.8% of all exported goods from EU. As of for Russia EU was the biggest exporter, with all goods being imported in Russia, EU had the highest share with 42.5%. Although just before sanctions trade relationship between Russia and EU had a downfall that was resulted by economic downfall in Russian economy. The exportation level experienced the stall, while they have had seen a massive increase in each previous consecutive year, and as a consequence of sanctions as well as other significant factors weakening Russian economy, Russian imports from EU decreased by 20.6% per year from 2014-2016 as before that on average they've increased by 20% from 2009-2013. Looking at Figure 3, which is based on statistics from UN COMTRADE , it shows the significant decrease in total exports to Russia over the 2014-2016. We can see that at the 1st half of 2014 the decrease in exports didn't suffer too much, however coming in late 2014 and early 2015 we can see drastic changes in export volume. Through out all EU countries we can see that trend of decrease in exportation to Russia. Just in early 2014 trade declined by 17.8% resulting a fall of export value of USD 66bn. In the first half of 2015 total Russian importation from EU fell by 42 %, similar downside impacts on exports can be seen for the Great Britain and Austria. However, countries like Czech Republic, France and Estonia experienced even higher reductions in exports to Russia in the first half of the year.

The decline in EU exports to Russia, as can be seen from these official statistics, is certainly the most crucial economic impact that has a connection to the sanctions. On the other hand, for at least two reasons it may be not a very clear indicator for the total sanction related economic loss. First one is that total economic costs need to include negative spillover effects on firms which are part

of the supply chain for the companies exporting to Russia. Since they cannot be observed directly, they must be calculated by models considering the linkages within the European economy.

	2013			2014			2015			2016		
	1.HY	2.HY	Year	1.HY	2.HY	Year	1.HY	2.HY	Year	1.HY	2.HY	Year
Percentage changes against the previous year												
AUT	16.9	2.4	9.1	- 6.5	- 8.8	- 7.7	- 46.3	- 43.7	- 45.0	- 29.9	- 22.6	- 26.2
BEL	- 3.5	- 1.0	- 2.3	- 17.0	- 23.4	- 20.1	- 43.3	- 31.3	- 37.7	9.3	13.4	11.4
BGR	4.5	4.7	4.6	- 2.1	- 12.8	- 7.8	- 39.1	- 31.1	- 35.1	- 19.6	- 12.5	- 15.8
CYP	36.5	39.0	37.2	- 39.3	- 41.7	- 40.0	- 51.1	3.2	- 37.0	- 16.0	- 1.9	- 10.0
CZE	- 3.4	- 3.5	- 3.4	- 1.3	- 11.8	- 6.7	- 45.0	- 40.4	- 42.8	- 10.5	3.3	- 3.5
DEU	- 1.6	- 7.0	- 4.4	- 11.9	- 23.8	- 17.9	- 42.9	- 30.7	- 37.2	- 2.2	- 0.1	- 1.1
DNK	21.8	4.5	12.6	- 26.3	- 35.1	- 30.6	- 49.4	- 43.5	- 46.7	- 6.3	0.7	- 2.9
ESP	5.1	- 6.0	- 0.7	- 3.3	- 15.3	- 9.2	- 52.1	- 37.4	- 45.3	- 2.6	- 5.9	- 4.3
EST	6.5	- 9.6	- 2.8	45.3	20.0	31.7	- 52.4	- 38.3	- 45.5	- 9.7	- 2.7	- 5.8
FIN	7.1	- 7.4	- 0.8	- 8.3	- 17.0	- 12.8	- 46.8	- 39.5	- 43.3	- 10.5	- 1.9	- 6.1
FRA	- 12.5	- 11.7	- 12.1	- 10.1	- 13.8	- 11.8	- 49.3	- 38.1	- 44.2	0.6	15.2	8.0
GBR	- 14.9	1.0	- 7.3	- 10.7	- 24.3	- 17.9	- 45.1	- 37.5	- 41.4	- 1.1	- 19.2	- 10.4
GRC	- 2.5	- 3.5	- 3.0	- 12.3	- 12.2	- 12.2	- 51.0	- 49.6	- 50.2	- 14.1	14.5	1.1
HRV	- 21.1	- 3.4	- 10.6	12.2	- 11.9	- 3.2	- 41.2	- 40.6	- 40.8	- 0.9	- 4.5	- 3.0
HUN	18.4	- 1.6	7.7	- 16.2	- 17.8	- 17.0	- 40.8	- 37.2	- 39.0	- 8.8	- 3.7	- 6.2
IRL	22.1	1.8	11.5	16.5	10.9	13.8	- 60.3	- 53.8	- 57.3	- 3.9	1.1	- 1.4
ITA	11.9	12.1	12.0	- 6.1	- 17.0	- 11.9	- 42.4	- 33.4	- 37.8	- 6.6	- 4.4	- 5.4
LTU	18.2	13.3	15.5	8.1	1.3	4.4	- 49.4	- 47.6	- 48.5	- 6.7	0.6	- 2.8
LUX	- 7.5	- 24.6	- 15.9	- 26.2	- 16.1	- 21.7	- 43.2	- 19.2	- 31.8	- 5.6	18.1	7.7
LVA	9.2	4.0	6.2	- 3.0	- 7.3	- 5.4	- 34.3	- 37.8	- 36.2	- 13.9	0.4	- 6.2
MLT	4 595.1	- 77.6	1.9	- 97.2	- 66.6	- 90.6	42.2	- 38.8	- 19.9	94.8	- 66.1	0.5
NLD	17.7	- 13.7	0.3	- 20.9	- 14.7	- 18.0	- 46.5	- 31.3	- 38.9	2.4	- 22.7	- 11.6
POL	13.5	6.3	9.6	- 7.0	- 19.0	- 13.3	- 42.7	- 35.8	- 39.3	0.0	2.7	1.4
PRT	43.6	54.4	49.2	- 12.5	- 30.2	- 22.0	- 40.0	- 31.1	- 35.8	- 12.0	- 6.6	- 9.2
ROU	35.3	36.8	36.1	21.0	- 7.9	6.0	- 41.4	- 45.4	- 43.2	- 15.5	13.5	- 2.9
SVK	11.5	- 8.2	0.5	- 3.1	- 32.8	- 18.3	- 47.0	- 34.0	- 41.6	- 25.7	18.8	- 4.7
SVN	29.2	14.3	21.3	- 2.2	- 1.6	- 1.9	- 37.1	- 31.8	- 34.4	- 17.5	11.9	- 2.2
SWE	1.9	7.4	4.7	- 4.7	- 17.2	- 11.2	- 49.3	- 41.9	- 45.7	- 4.9	- 0.5	- 2.6
<b>EU</b>	<b>3.3</b>	<b>- 2.2</b>	<b>0.4</b>	<b>- 8.6</b>	<b>- 17.8</b>	<b>- 13.3</b>	<b>- 44.9</b>	<b>- 35.8</b>	<b>- 40.5</b>	<b>- 4.9</b>	<b>- 1.7</b>	<b>- 3.2</b>
CHE	2.6	11.4	7.4	- 1.5	- 16.0	- 9.7	- 27.6	- 16.6	- 21.8	- 4.3	- 21.3	- 13.9
USA	4.0	5.2	4.6	11.7	- 17.4	- 3.6	- 33.7	- 34.8	- 34.2	- 28.7	- 5.1	- 18.2
ARM	18.9	19.8	19.4	- 7.3	- 8.9	- 8.2	- 34.2	- 19.5	- 25.8	92.5	38.4	59.2
BLR	5.6	1.2	3.3	- 7.6	- 11.8	- 9.7	- 33.9	- 30.2	- 32.1	- 3.3	12.0	4.6
KAZ	-	-	-	-	-	-	- 9.7	- 14.8	- 12.2	-	-	-
MKD	2.4	- 8.5	- 4.7	17.6	42.4	33.2	1.5	- 25.4	- 16.6	62.1	24.6	39.5
SRB	28.0	18.3	22.5	2.0	- 6.7	- 2.8	- 69.2	- 51.8	- 60.0	152.6	8.0	60.6
TUR	4.7	4.0	4.3	- 11.3	- 17.9	- 14.7	- 38.0	- 41.2	- 39.6	- 59.8	- 43.2	- 51.7

Figure 3 EU exportation to Russia (Source: UN Monthly COMTRADE)

While it is rather hard to calculate the impact of the sanctions for the EU and Russian economy in taking away other factors that were mentioned above, several studies nevertheless attempted to estimate the economic costs taking into account economy-wide multiplier effects. The European Commission summarizes the damage to Europe's economy as "managed" and puts the overall costs of the sanctions and countersanctions at EUR 40 bn (-0.3 % of EU GDP) in 2014 and EUR

50 bn (-0.4 %) in 2015. Forecasting) estimates the potential impact of the sanctions for the Russian economy at 8 % to 10 % of GDP and the impact for the EU at 0.5 % of GDP. A study by (Havlik, P.)<sup>20</sup> concludes that Ukraine's economy is hit strongest by the conflict with GDP contracting by up to 10 % in 2014, while the loss in Russian GDP is predicted to amount to EUR 20 bn and more than EUR 30 bn and EUR 50 bn in 2015 and 2016, respectively. Assuming a 10 % loss in exports of goods and services to Russia, he estimates a GDP loss for the EU of around EUR 11 bn (-0.1 % of GDP), while in a more extreme scenario with a decline in value added exports by 50 %, the predicted losses may account for EUR 55 bn (-0.4 % of GDP).

Russia on the other hand had a way bigger impact again partially due to oil price fall in Figure 4. Even though they've rebound as of 2016-2017 the impact on Russian economy was still immense due to the reason that Russian economy is mostly oil based. By the end of 2013 GDP of Russia stagnated and went negative by almost 2% in first quarter of 2014. Overall, throughout 2014-2016 GDP contracted by 3.5 % Which can be seen in Figure 5. Economic sanctions are more effective in relation to countries that are traditionally were business partners rather than against long-standing rivals. For Russia, US sanctions were less painful than from the EU member states that are considered Russian strategic partner. At the end of 2013, the volume of accumulated Russian investments in the US economy amounted to \$ 4.1 billion when in the Netherlands it was \$ 23.3 billion. Investments from USA were measured just in 10.3 billion whereas from the Netherlands - 68.2 billion dollars.

Economic sanctions that adversely affect opportunity obtaining by Russian banks of affordable loans, provoke investment decline in the country's economy and weaken the ruble. This situation leads to a complication and cost of external maintenance debt of domestic companies. According to estimates of the chief economist for Russia and the CIS of the investment bank Renaissance Capital Russian companies must repay loans worth about \$ 160 billion. Of these, the public sector accounting for about 65 billion, in the coming year, Russian state-owned companies in the non-financial sector will to pay 41 billion dollars, to state banks - another 33 billion. In addition to this, private banks need to pay off 20 billion dollars. Private non-financial companies account for external debt \$ 67 billion According to the Bank of Russia, the external debt of the Russian

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<sup>20</sup> (Havlik, 2014)

Federation amounted to in the middle 2014 731.2 billion dollars, of which the public sector accounted for more than half<sup>5</sup>. The most serious problem is sanctions against state-controlled major banks. According to Bloomberg, VTB, Sberbank, Gazprom bank and VEB in the upcoming three years should buy bonds for about \$ 15 billion. But dollar loans from foreign banks declined in the first six months of 2014 to 7.9 billion compared with 25 billion a year earlier<sup>5</sup>. The external debt of the public sector in an expanded definition covers the external debt of government, the Central Bank, as well as banks and non-banking corporations, in which the government and the Central Bank directly or indirectly own 50% or more of participation in capital or control them in another way. Without access to long-term financing paying off debts will be difficult. Russian companies with state participation in capital (over 50%), including Gazprom and Rosneft, are deprived of the opportunity place securities in European markets. Due to sanctions, the head Rosneft asked the government to buy new ones Rosneft bonds at the expense of the National Wealth Fund 2.4 trillion rubles.<sup>6</sup> Sberbank, VTB, Gazprom bank, Russian Agricultural Bank and VEB is forbidden to sell shares and bonds with maturities of more than 30 days issued after September 12, 2014 to Europeans. The European Commission (EC) has proposed to close the syndicated loan market for them and other state-owned companies.

There are studies that came out based of sanctions are stating that they do bring a negative impact. Citibank found out that out of all decline within Russian economy during the period of 2014-2016 is 85-90% could be explained by that massive drop in oil price, thus leaving 10-15% for everything else including the sanctions with counter sanctions. Study by Gurvich and Prilepsky in 2015 is taking a closer look at the consequences of financial sanctions on companies that has Russian origin. Even though financial sanctions curtailed the financial opportunities, companies were still able to gain access to their own assets outside Russia, therefore it negated the negative impact of sanctions. Gurvich and Prilepsiy came up with four different cases for various combinations of sanctions policies and oil price. They found out that the total effect withing those scenarios during the 2014-2017 would be 2.4% which means that by their calculations the GDP would be just 2.4%

higher in 2017 compared to what it actually was. Whereas the impact of oil price fall was at least 3 times higher than the sanctions effect.<sup>21</sup>

The IMF (International Monetary Fund) looked at potential effects of sanctions and Russia's counter sanctions. In the model that was created, the initial Russian GDP reduction was 1-2% whereas total impact and loss could have been as high as 9%.<sup>22</sup> This large loss in GDP, however, assumes a lower level of investment and lower level of productivity. According to the available data, Russia's GDP declined initially some 2.5%, of which one percentage point, or almost half, could be explained by sanctions and countersanctions.

A different study run by the World bank<sup>23</sup> calculated the different areas in which sanctions and counter sanctions might possibly influence Russian economy. They came up with a result that the impact of counter sanctions is negative but didn't quantify the exact impact in their research. Their study concludes that investments are most likely to experience the biggest impact due to sanctions. Dreger research, which focused on the effect of sanctions as well as oil price on Russian markets, came up with that the fact that oil had a much bigger role in development of Russian ruble course compared to sanctions. They said "Due to its relative openness, the Russian economy is heavily exposed to exchange rate fluctuations. Since January 2014, the Ruble strongly depreciated against the US Dollar. The fall of the currency started with the conflict between Russia and Ukraine. The impact of the conflict on Russia may be amplified by the sanctions imposed by Western countries. However, oil price also declined since Summer 2014. As Russia is heavily dependent on exports of natural resources, the oil price decline can be another factor behind the deterioration"<sup>24</sup>. This clearly states the trend of current researches that even though the main reason why Russia

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<sup>21</sup> (Gurvich, 2015)

<sup>22</sup> (International Monetary Fund, 2015)

<sup>23</sup> (World Bank, 2015)

<sup>24</sup> (Dreger, 2016)

experienced trouble is because oil price plunged, however the sanctions made situation only worse for the stability of Russian economy and Ruble exchange rate.



Figure 4 Urals Crude oil price (Source: Reuters)

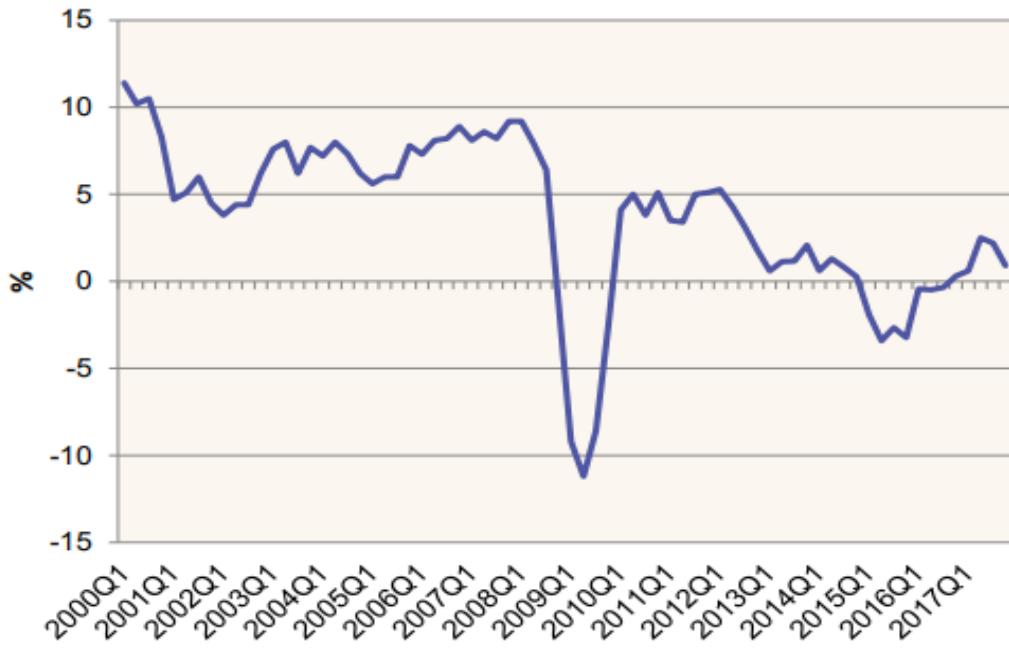


Figure 5 GDP change in percentage (Source: Rosstat)

At the end of 2016, estimates of American experts on the impact of sanctions on companies in 2014 were published. Sanctioned firms lost about a third of their profits, more than half of their capital and were forced to lay off about a third of their employees. It was emphasized that the sanctions had a lesser impact on the Russian economy than the fall in oil prices, internal problems and “political uncertainty”. The effect of these sanctions amounted to no more than \$ 3 billion. In 2016, the United States had a new reason for expanding sanctions against Russia - accusations of cyber-attacks and interference in the presidential election. In 2017, under these conditions, the Countering America’s Adversaries Through Sanctions Act, CAATSA, was passed. CAATSA is notable for the consolidated codification of US restrictive measures against Russia, Iran, and North Korea. For Russia, areas have been defined that have not yet been affected by sanctions, but that are potentially at risk. In particular, the main areas that we discussed about the possibility of imposing sanctions against companies of third countries cooperating with the Russian military-industrial complex. In accordance with CAATSA, the United States in April 2018 introduced another package of sanctions against the Russian Federation. In August 2018, an unprecedented

104-page draft of the next US sanctions was published<sup>25</sup>. The motivation part has expanded, highlighting Russia's accusations of cyber-attacks and the use of chemical weapons (the Salisbury incident). The list of banks subject to sanctions has been expanded: The Bank of Moscow and Promsvyazbank have been added to the five available. VEB is mentioned even twice<sup>26</sup>. A complete ban is imposed on the supply of dual-use products (before each transaction was to be approved by the competent authorities of the United States), calibration equipment, equipment for the fuel and energy sector, and the volume of purchases of uranium in Russia is being reduced. The Department of State estimated the potential effect of these sanctions on trade at hundreds of millions of dollars<sup>27</sup>. The second “wave” of sanctions, designed to be introduced 90 days after the first wave and is supposedly is the toughest on Russia since 2014, offers the US President a wide range of economic options to choose from - a ban on operations with the Russian public debt until personal sanctions are extended up to freezing accounts. It is important to note the proposal which is to create on a permanent basis the new structures in the field of security, including economic. This is the National Fusion Center to Respond to Hybrid Threats, aimed specifically against Russia. The tasks of that Center include countering “the use of energy resources or infrastructure to influence on sovereign states”<sup>28</sup>. Within the framework of the State Department, it was proposed to create the Office of Cyberspace and the Digital Economy - Office of Cyberspace and the Digital Economy, which would deal with issues of cybersecurity, the Internet, etc. The Countering Russian Influence Fund in Europe and Eurasia on fiscal 2020- 2021 it was proposed to allocate more than \$ 250 million with a possible expansion of funding<sup>29</sup>. It is planned to upgrade the status and strengthen the role of the Office of Sanctions Coordination within the Department of State. Its tasks, in particular, will include the analysis of sanctions imposed by the United States without the EU; sanctions imposed by the EU, but without the US, and an explanation of the reasons for the discrepancies in each case<sup>30</sup>. In order to maximize the effect of sanctions, in order

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<sup>25</sup> (US Congress, 2018)

<sup>26</sup> (US Congress, 2018, p. 56)

<sup>27</sup> (The NY Times, 2018)

<sup>28</sup> (US Congress, 2018, p. 84)

<sup>29</sup> (US Congress, 2018, p. 53)

<sup>30</sup> (US Congress, 2018, pp. 63-65)

to avoid duplication of efforts in this direction, the US Secretary of State is called upon to ensure coordination with the EU and its structures, the governments of NATO or EU member states and international organizations.<sup>31</sup> Western Economic Sanctions against Russia: Developing the Situation Forecasting Problems. The EU sanctions did not concern contracts signed before the decision of the EU Council in 2014.



Figure 6 SWOT Analysis of Sanctions

Given the “unpredictability” of Russian policy, even the sections “Benefits” and “Opportunities” include sanctions that could turn against the sanctioning countries themselves. This concerns cooperation between the EU and the USA, which has turned into a source of mutual irritation for these strategic partners. The total export losses of Western countries from December 2013 to June 2015 exceeded \$ 60 billion, but the vast majority (more than 82%) fell on manufacturing goods, which were not affected by the Russian response (dual-use products, equipment for fuel and energy complex, etc.). Out of the total export losses, more than ¾ suffered EU countries. Later,

<sup>31</sup> (US Congress, 2018, pp. 7, 91)

the numbers were adjusted upward. Most of the losses for the West are directly related to their own restrictive measures, and not to the Russian food embargo. According to a NATO expert<sup>32</sup>, "the main task of the sanctions - to harm the Russian economy - can be considered successfully completed." At the same time, he sees the "value" of economic sanctions not only and not so much in the amount of actual damage, but in the symbolic value common to Western countries - a demonstration of the unity of coordinated actions. Sanctions are directed against strategic state-owned enterprises, thus causing targeted economic damage. At the same time, Western countries imposing restrictions take upon themselves the risks associated with the negative economic consequences for themselves (an illustration of their determination). Damage to the sanctioning countries of the West occurs in three cases. Direct damage - if they ban the export of equipment for the fuel and energy complex, defense industry, dual-use products; and due to reciprocal Russian restrictions on food imports. Indirect damage is associated with the recession of the Russian economy and the depreciation of the ruble. Sanctions prevent Russia from carrying out strategic economic planning; the planning horizon has been reduced to a year. Which together leads to a decrease in demand for imports of products. The latter is the most significant, but it is impossible to blame solely on Western sanctions. As of 2015 alone, 7 out of 28 EU countries suffered net losses. This "unlucky sevens" includes two groups of countries: those that were able to partially reorient to other markets, and those that were unable to adapt to new conditions at all. The first group included Belgium, the Baltic countries and Finland, the second - Greece and Sweden. In March 2018, the EU Council extended sanctions against 150 individuals and 38 legal entities "associated with actions that undermine or threaten the territorial integrity, sovereignty and independence of Ukraine" until September 15, 2018. The EU sanctions list included new individuals and legal entities responsible for the construction of the Kerch Bridge. Thus, the total number of those subject to EU restrictions amounted to 44 legal entities and 155 individuals as of July 31, 2018. A list of over 400 pages has been published, indicating the reasons for inclusion in the list in accordance with recognized international agreements<sup>7</sup>. It is noteworthy that during the exchange of restrictive measures, officials on both sides alleged a violation of the rules and principles of the WTO by sanctions, but neither side carried out a formal dispute settlement

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<sup>32</sup> (Christie, 2015)

procedure within this organization. Russian economy adjusts to new reality including sanctions, the abolition of which is not visible in the foreseeable future.

At present, the losses from Western sanctions on the Russian economy are about from 1 to 1.5 % of total GDP accumulated per year according to IMF estimates <sup>33</sup>. According to the estimates of the Economic Expert Group, the accumulated growth losses from sanctions for the period 2014 – 2017 years is amounted to 8.4%. Bloomberg estimates that Russia has lost 6% of GDP over the past four years. <sup>34</sup>. Moreover, the impact of sanctions has direct and indirect effects, expressed in the reduction of bilateral trade between Russia and Western countries, the refusal to cooperate not only with Western investors, but also with third-country companies due to the spread of “toxicity” of Russian companies and the risk of introducing secondary sanctions, a decrease in foreign direct investment inflows and capital outflows from Russia, growing uncertainty, expressed in high ruble volatility and fluctuations in the financial market, and other aspects.

## 4.1 Decrease in bilateral trade with Western countries

The value of exports to the EU decreased by 117 billion dollars, and imports from the EU by 53 billion dollars, in connection with that the EU's share in Russia's foreign trade decreased from 47,6% in 2013 to 39,3% in 2017. This reduction in trade was caused not only by sanctions in relation to Russia, but rather the food embargo of Russia on several European goods. To the greatest extent the value export to the EU of mineral fuels, inorganic chemistry products, iron and steel, fats and oils of animal origin, and organic chemical compounds has decreased since 2013. The largest decline in imports from the EU occurred in nuclear reactors, boilers, land vehicles, electric machines and equipment, and pharmaceutical products. Nevertheless, in 2017 there was a slight recovery in bilateral trade with the EU. As for trade with the United States, its volume was also low in 2013, so its decrease was insignificant: Russia's share in the US foreign trade decreased

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<sup>33</sup> (Gurvich E., 2016)

<sup>34</sup> (Doff, 2018)

from 1,1 to 0,8%, and the US share in Russia's foreign trade on the contrary, it increased from 2 to 2,1% in 2017. In general, there was a reorientation of trade from Western countries to APEC and EAEU countries, however, trade volumes have not yet been reached before the imposition of sanctions.

## 4.2 Refusal of partnership

In some areas of the oil and gas industry, technical sanctions had a very strong effect. However, the investors' refusal to finance or the complete refusal to implement these projects was influenced not only by the sanction pressure, but also by a significant reduction in the price of fuel (oil and natural gas), since the profitability of some projects was estimated only when the oil price was above 80 USD per barrel. Nevertheless, a fine of 2 million dollars was imposed on the US oil company ExxonMobil for cooperation with Rosneft. "Toxicity" of Russian companies leads to the abandonment of transactions with foreign partners. Therefore, a lot of companies and investors backed down in the fear of getting fined.

## 4.3 Decrease of FDI towards Russia and capital loss

The action of sanctions also entails an outflow of capital from the country, which in 2017 amounted to about 20 billion US dollars (approximately 1,5% of GDP). Even though there is no direct restriction on foreign direct investment (except for the Republic of Crimea), the influx of FDI into Russia is extremely sensitive to tougher sanctions. In particular, the periods of active imposition of sanctions and maintenance of sanction uncertainty from March 2014 to January 2016 and from April 2017 lead to a sharp drop (and even negative values) in FDI inflows, while the relative stabilization of the sanctions regime from February 2016 to March 2017 is characterized by a recovery in FDI inflows to Russia . Therefore, it is stabilization of the sanctions regime that is the most acceptable strategy for foreign policy and foreign economic positioning in modern conditions, since only in this case (due to the extremely low probability of easing the

sanctions regime) can the economy adapt to stable external constraints — the so-called second best will be achieved. The outflow of capital from Russia is due to both a reduction in investments of Western investors in Russian debt and the sale of their assets. For example, it is estimated that in 2017 the sale of commercial real estate by foreign investors amounted to 1,54 billion dollars, while its purchase was only 502 million dollars<sup>35</sup>.

## 4.4 Rise of uncertainty in financial market

The decrease in FDI and other macroeconomic indicators is caused not so much by the introduction of new sanctions, but rather by the discussion of the USA and the EU of this possibility, since it creates market uncertainty for both domestic producers and foreign investors. The United States strongly supports this uncertainty, constantly threatening to impose new sanctions or tighten existing ones. After all, the ruble and stock exchange indices react to any announcements of American discussions of anti-Russian sanctions. For example, after the April sanctions were introduced in 2018, the ruble exchange rate fell sharply: on 11 April, the official euro exchange rate grew by almost 5 rubles. and reached 76,85 rubles., and the dollar exchange rate - by 3,8 rubles. to 62,36 rubs. Sellers and distributors of household appliances immediately announced a price increase of 5-10%<sup>36</sup>. On 6<sup>th</sup> of April, En +'s capitalization fell by 30%, and RUSAL announced a technical default risk, after which its share price collapsed by more than 50%. Sanctions led to a drop in quotations of metallurgical companies. In April , on the Moscow Exchange , Nornickel fell by 16,5% (up to 29,1 billion dollars' worth of drop), Polyus by 14,8% (around 9,6 billion loss ), Severstal - by 9,4% (equated to around 12,4 billion dollars), NLMK - by 8,7 % (to 15,8 billion dollars)<sup>37</sup>. After the announcement of new US sanctions in August 2018, American media reported that the ban in the second package of Aeroflot flights to the United

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<sup>35</sup> (Filatov, 2017)

<sup>36</sup> (Sichkar, 2018)

<sup>37</sup> (Trifonova, 2018)

States would deprive the company of 5% of revenue. The next day, the company's shares fell by 12%, then the quotes corrected (-8%) and became 1,5% lower than the initial value.

## 4.5 Effect from Russian measures

In connection with the sanctions, the Government of the Russian Federation implemented a number of forced measures, in particular, introduced the requirement for data storage on the territory of the Russian Federation and software localization in government institutions<sup>38</sup>, which led to an increase in costs of technology and telecommunications companies. To reduce dependence on Western financial services, analogs of payment systems, credit ratings, and an analogue of SWIFT — Financial Message Transmission System (SPFS) were developed and introduced. There was a significant increase in Russia's international reserves, because as a result of the sanction uncertainty, there could be a threat of forced repayment of Russian external debt obligations: from 1<sup>st</sup> of April 2016 to 26<sup>th</sup> of October 2018 by 73,7 billion dollars.<sup>39</sup>, with a decrease in external debt over the same period — by 53 billion dollars. The most serious restrictive measure taken by Russia after the introduction of sanctions against it was the food embargo imposed on 7 August 2014 for a number of food products moat (meat and dairy products, fish, vegetables, fruits, nuts) from the USA, EU, Norway, Australia, Canada, and later from Albania, Montenegro, Iceland, Liechtenstein and Ukraine. However, these measures caused damage to the Russian economy, as their negative effect, expressed in rising prices and lower consumption of the population, was not offset by the expected increase in production of the domestic food and agricultural sectors and a decrease in imports. The estimated negative effect of Russian countersanctions over four years amounted to 0.2 % of a decline in GDP and 2-3 % of a decrease

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<sup>38</sup> (Ministry of Digital Development , 2016)

<sup>39</sup> (Central Bank of Russian Federation, 2016)

in real incomes of the population<sup>40</sup>. According to other estimates, the average increase in annual inflation due to the introduction of countersanctions amounted to 3,1%.

Also, in Russia, a framework law was adopted on 4<sup>th</sup> of June “On Measures of Impact (Counteraction) on Unfriendly Actions of the United States of America and (or) Other Foreign States”, which facilitates the introduction of restrictive measures by Russia<sup>41</sup>. Nevertheless, the negative effect of anti-Russian sanctions is felt by the European Union. According to estimates, Germany’s losses in the first year after the imposition of sanctions are the biggest in comparison with other countries and amounted to 830 million dollars per month. According to other estimates, Germany loses \$ 727 million a month, and it accounts for 40% of Western countries' losses<sup>42</sup>. Such statements by the Western press and scholars undoubtedly make it possible to soften the rhetoric of the authorities on the introduction of new sanctions. Therefore, it is necessary to increase the tendency to disseminate this information in the EU countries, as well as cooperation with European companies in areas of mutual interest. This will provide a lobby for Russian interests in the EU countries, as, for example, this happened during the construction of the Nord Stream. Currently, the Government of the Russian Federation is working to overcome the sanction pressure, however, the costs of implementing such a policy are at a fairly level. A positive decision was the creation of the Department of External Control at the Ministry of Finance, an analogue of the American Office for Foreign Assets Control (OFAC). Russia and China are discussing the creation of a cross-border settlement system in national currencies to de-dollarize bilateral trade and reduce sanctions risks. The possibility of creating a SWIFT analogue system is being discussed with Switzerland, while Russia is proposing the use of its own development — SPFS, but today its coverage is only about 400 participants. In addition, the Government is implementing several measures to help victims of sanctions. For example, it is planned to purchase armored vehicles for the Russian Guard in the amount of 2 billion rubles.(from the reserve fund) from the companies Ural and Arzamas Engineering Plant, which are part of the GAZ and Russian Machines group of companies included in the sanctions US list. Also, subsidies in 1,5 billion rubles. will be

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<sup>40</sup> (Ekaterina Ponamareva, 2017)

<sup>41</sup> (Russian Federation, 2018)

<sup>42</sup> (Yandex News, 2018)

directed producers of natural gas appliances that will allow additional loading of production capacities of enterprises that have fallen under sanctions. Earlier, the Ministry of Industry and Trade proposed to provide preferences to 11 Russian Machines enterprises for purchases at the regional and municipal levels. Thus, the negative effect of sanctions on the Russian economy is not so much in their level as in the uncertainty of the sanctions parameters, which is expressed in significant fluctuations in the financial markets the ruble's volatility, the refusal of foreign investors to cooperate with Russian companies, the outflow from the capital of Russia and others. Therefore, the efforts of the state should be focused in the short and medium term on stabilizing the current level of sanctions to reduce uncertainty, and not on their complete lifting. To reduce the risks of foreign companies, it is advisable to create favorable conditions for investors, especially in the "non-sanctioned" sectors, increasing the transparency of the ownership structure. But from what we can see most of those measures to minimize the impact are addressed towards the companies rather than Russian citizens. When it comes to looking at everyday consumers there is an important research that was concluded in 2018 by Volochkova is that the countersanctions had a clear negative impact of welfare-level of the average Russian household. The main impact was that every Russian on average had to decrease consumption of banned items by 3000 rubles a year. It shows that even though the real income has decreased by 2-3% between 2014-2016 which had a very significant impact on low income class that it most of the Russian population. By talking about the household income and consumption we move to our next topic which is price comparison and household consumption in Russia before and after Crimea crisis.

## 5. Impact on Russian household

The burden of economic sanctions against Russia for the average consumer affects the change in prices for both essential and non-essential goods. As a result, the subsistence minimum increased sharply both among the able-bodied population as a whole and among pensioners (Figure 8)

Indicators	Abbreviation	2014	2015	Δ
Gross domestic product, bln. RUB.	GDP	63049,2	60687,1	↓
Investments, mln. RUB.	I	13527683,7	13450238,2	↓
Government spending on goods and services	G	13932,4	15513,0	↑
Export, mln. RUB.	Ex	497763	340349	↓
Import, mln. RUB.	Z	308026	194088	↓

Figure 7 (Change in the main indicators affecting the IS curve)

If in the 1st quarter of 2014 the cost of living increased by just 650 rubles compared to the 1<sup>st</sup> quarter of 2013, then in the 1st quarter of 2015 the cost of living increased by 1974 rubles compared to the 1st quarter of 2014, ( more than 3 times). In the 3rd quarter of 2014, the cost of living increased by 657 rubles compared to the 3rd quarter of 2013, and in the 3rd quarter of 2015 the cost of living increased by 1,587 rubles compared to the 3rd quarter of 2014 (i.e. more than 2.4 times). At the same time, the cost of living growth accelerated sharply in 2015 (see Figure 7).

	All citizens	by demographic		
		Working citizens	pensioners	children
2013	7306	7871	5998	7022
Q1	7095	7633	5828	6859
Q2	7372	7941	6043	7104
Q3	7429	8014	6097	7105
Q4	7326	7896	6023	7021
2014	8050	8683	6617	7752
Q1	7688	8283	6308	7452
Q2	8192	8834	6717	7920
Q3	8086	8731	6656	7738
Q4	8234	8885	6785	7899
2015				
Q1	9662	10404	7916	9489
Q2	10017	10792	8210	9806
Q3	9673	9673	9673	9673

Figure 8 Minimum subsistence level (Source:  
[http://www.gks.ru/free\\_doc/new\\_site/population/urov/urov\\_41kv.doc](http://www.gks.ru/free_doc/new_site/population/urov/urov_41kv.doc))

The structure of the consumer basket in the I quarter of 2015 is presented in Figure 9: 47.2% accounted for food, 23.0% for non-food products, 22.8% for services and 7% for expenses on mandatory payments and fees. For pensioners and children, the share of food products was higher and exceeded 50% (see Fig.9). Today in Russia the composition and volume of the food basket is in effect, established by the Federal Law of December 3, 2012 No. 227-FL "On the consumer basket as a whole in the Russian Federation" and put into effect on January 1, 2013. The structure of the living wage was approved in kind expressed in terms of food and non-food goods and services and will be valid until 2018. Consumption is calculated on average per person for each of the main socio-demographic groups of the population: working age laziness, senior citizens and

children.

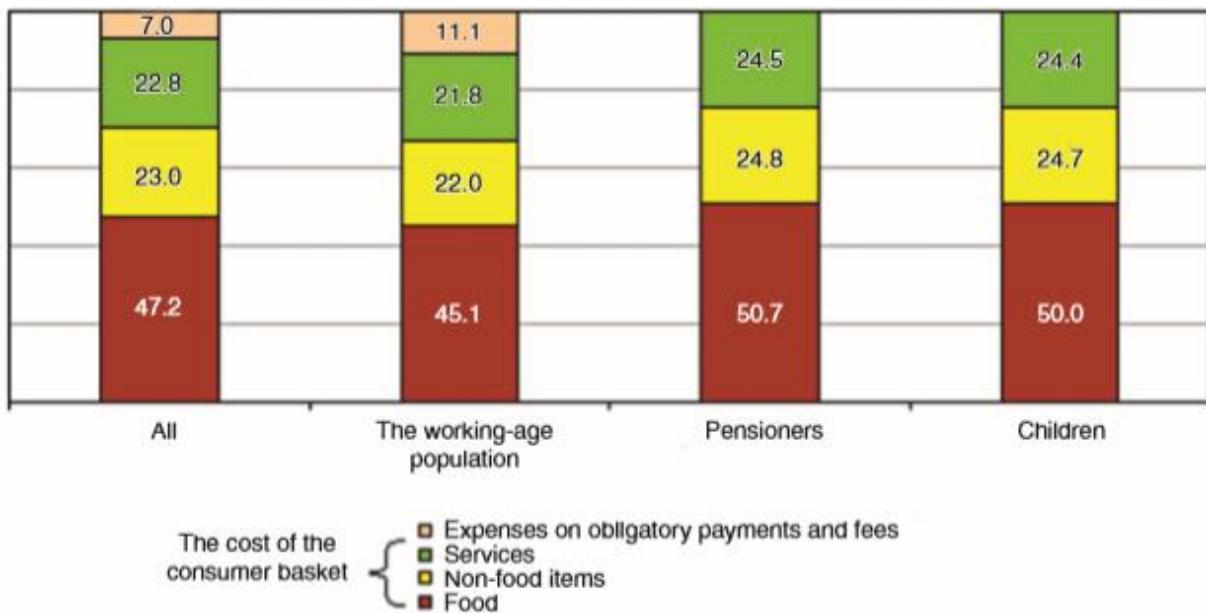


Figure 9 The structure of minimum subsistence level by groups in Q1 of 2015

Source:

[http://www.gks.ru/bgd/free/b04\\_03/IssWWW.exe/Stg/d05/image5115.gif](http://www.gks.ru/bgd/free/b04_03/IssWWW.exe/Stg/d05/image5115.gif)

Monitoring is carried out regularly for 40 main types of food and prices are regularly monitored at fairs and markets. The ratio of the average per capita cash income of the population with the cost of living is presented in Figure 10. It is seen that as a result of inflation, this ratio decreases. Since the largest item in the structure of the consumer basket is food products, we first consider the dynamics of prices for food products, and then for electronic goods, cars, real estate and the cost of leisure within the country and abroad. The increase in food prices is shown in Figure 10. Food prices skyrocketed already in the fall of 2014, peaking towards the new 2015. They made the largest contribution to inflation, as can be clearly seen in Figure 10. The largest contributor to inflation was the increase in food prices. The increase in prices for non-food products even lagged the average inflation rate. The effect of price increases on food products from January 2013 to June 2015 on inflation in the Russian Federation is shown in Fig. 11.

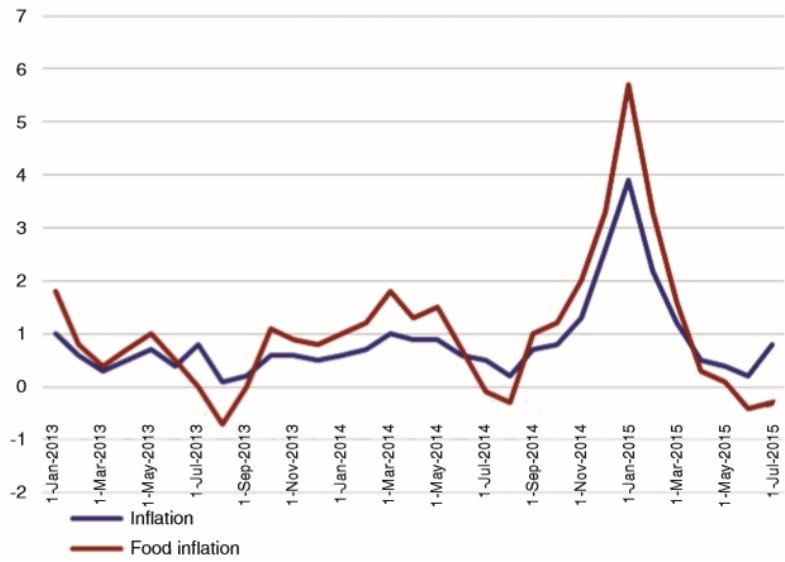


Figure 10 The growth rate of food prices and inflation in 2013—2015 Source:  
[http://www.cbr.ru/statistics/infl/Infl\\_01072015.pdf](http://www.cbr.ru/statistics/infl/Infl_01072015.pdf))

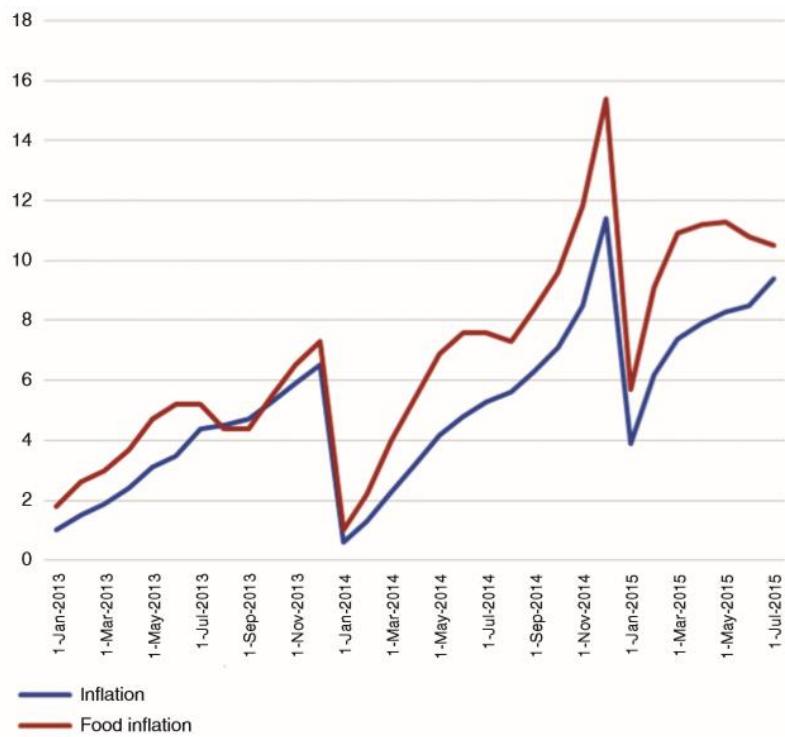


Figure 11 Dynamics of Inflation in 2013-2015 (cumulatively) Source:  
[http://www.cbr.ru/statistics/infl/Infl\\_01072015.pdf](http://www.cbr.ru/statistics/infl/Infl_01072015.pdf))

Russian countersanctions resulted in an embargo on imports of certain groups of food products: meat, fish, dairy products, vegetables and fruits, which were previously exported from the EU and North America. Overall, for some positions, the share of Russian countersanctions fell in 2013 from 4 to 30%. Particularly significant were restrictions on cheese (29.5%), pork (20.4%), fruits and berries (17.7%).

However, various essential commodities had a different effect on inflation. Although price increases were typical of all consumer goods, their growth rates were not uniform. If prices for vegetables and fruits experienced traditional seasonal fluctuations and their growth was not so noticeable, then prices for meat and fish increased significantly. Due to the imposition of sanctions and a rise in the dollar and the euro, imports of meat and poultry, including offal, fell by 30% in 2014 compared to 2013, pork imports fell by 2 times, cheese imports decreased by 20%, and cereal flour and leguminous crops - by 40%. The trends that were outlined at the end of 2014 continued into 2015. Let us compare Russia's imports of the most important goods in January - June 2015 with January - June 2014. In value terms, imports decreased from \$ 141,603.1 million. up to 87 728.0 million dollars, i.e. by 38%. This was mainly due to a reduction in imports from non-CIS countries. If in the first 6 months of 2014 goods were imported in the amount of 125,431.3 million dollars, in the first half of 2015 only 76,642.7 million dollars were imported. The largest reduction affected meat and dairy products. Import of butter decreased by 8.9 times. Import of milk and condensed cream - 6.1 times, import of poultry meat - 3.7 times, meat and fish - more than 2 times. The reduction did not concern only coffee, tea and cocoa beans. As a result of economic sanctions, the share of imports from the EU countries decreased from 48.8% in January - October 2014 to 45.3% in January - October 2015, the share of automatic telephone exchange countries increased from 26.6% in January - October 2014. up to 27.9% in January - October 2015. It is interesting to note that the share of the CIS countries has not changed over this period, it remained at the level of 12.5%. However, a noticeable redistribution took place inside: the share of Ukraine during this period decreased from 3.7% to 2.8%, while the share of other countries, and especially Belarus, increased markedly. Economic sanctions against Russia objectively divided the whole world into friends and enemies of our country. With a general reduction in foreign trade, the BRICS countries (South Africa, India, Brazil, China) and the CIS countries (Armenia, Tajikistan, Turkmenistan, Kyrgyzstan, Kazakhstan, Belarus, Uzbekistan) increased the volume of foreign trade with the

Russian Federation. Among Latin American countries, growth dynamics are especially noticeable in countries such as Peru, Chile, Cuba, Brazil, Mexico, Argentina. From Asian countries, Vietnam, Georgia, Iran, Indonesia, Mongolia, and Hong Kong should be singled out. Imports from Indonesia, Malaysia, Vietnam, Brazil, Taiwan, India, Belarus, China, and Kazakhstan grew especially significantly. Of the EU countries, sanctions have less affected Spain, Portugal and Italy. As a result, there was an increase in demand for goods that are produced within Russia. There was an increase in the consumer basket of domestic essentials. Natural products began to displace artificial ones. Figuratively speaking, the Russians began to consume more honey and less "Bounty", which could be very good in certain cases however the quality of products in Russia is not set to a high standard.

## 5.1 Dynamics of demand for non-food products

Rising prices for Apple's electronic products led to the Giffen paradox at the end of 2014, the higher the price, the greater the sales volume. Despite the rapid increase in prices for the company's products (the price of Apple products rose by 25% on November 25, and another 35% on December 22), sales grew by 80%. This is because Russian consumers were afraid of an even higher price increase for the product and were afraid of losing the product, which for many of them became a matter of prime necessity. As a result, despite the rise in price of household appliances, demand for it did not decrease to Q2, but increased to Q3. Thus, there was a shift in the demand curve D1 to position D2 (Figure 12) and the demand curve in the long term acquired a positive slope (D). As a result of the reduction in imports in the market of goods not necessary, there was also a significant decrease in supply. Furniture imports in January - June 2015 compared with January - June 2014 decreased 1.9 times, imports of cotton fabrics - 1.8 times, clothes - 1.5 times, medicines - 1.5 times, shoes - 1.6 times, trucks - 4.9 times, cars - 2.1. Let us dwell on the car market in more detail.

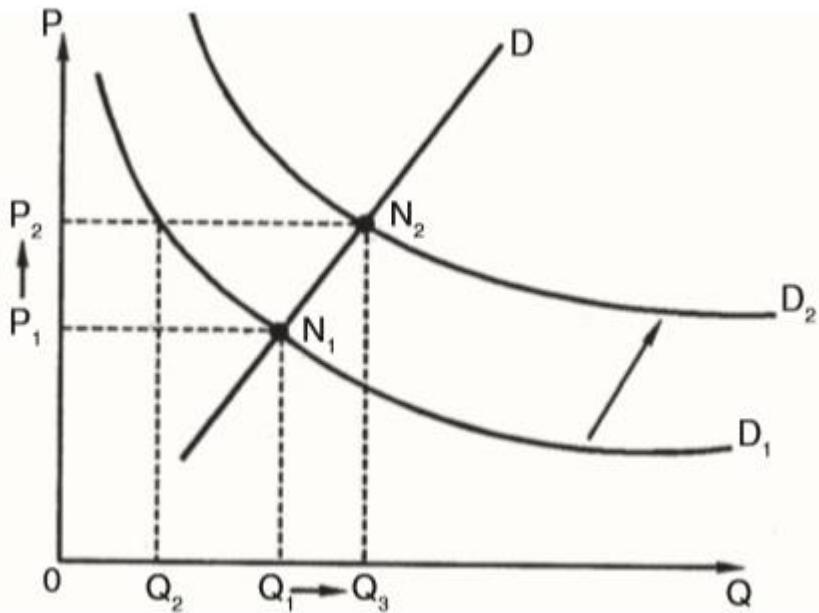


Figure 12 The dynamics of demand for the goods of Apple Inc. in 2014 (in comparison to 2013).

A major blow to the Russian market was the departure of General Motors. March 18, 2015 General Motors decided to close production cars in St. Petersburg in the middle of the year, and completely abandoned the sale of Opel cars in Russia starting in December 2015. Coarse assembly continued until June 30; from July 1, the plant is mothballed, only a small part of the employees who will be to ensure the functioning of the plant under conservation conditions.

Car loans in the I quarter of 2015 compared with the I quarter 2014 decreased by 4 times, sales fell by 2 times, imports cars from abroad amounted to half of the previous level. The dynamics of the issuance of new car loans from Q1 2014 to Q1 2015 is presented in Figure 14 and the dynamics of sales of cars for the same period - in table 13. The dynamics of the share of cars sold on credit is presented in table 15. Starting from the first quarter of 2014, a systematic reduction of cars bought on credit. Biggest changes started in late 2014 - early 2015. As a result, the share of sales new cars on credit in January 2015 amounted to about 8%. This was reflected primarily in the Top 10 most imported brands. cars (table. 16). The largest reductions were made by such popular brands as Nissan (whose sales fell 10 times) Daewoo, Volvo, Mitsubishi, whose sales fell by almost 2 times. The car market in the regions has also changed. Virtually all regions there was a

market reduction of almost 2 times. If in January - February 2014, 339.7 thousand new cars were sold, then in January - February 2015 - only 174.9 thousand (a decrease of 48.5%)

<b>Period</b>	<b>Issues in thousands</b>	<b>% changes. (from year to year)</b>
Q1 2014	194,1	-10,1
Q2 2014	205,7	-23,0
Q3 2014	206,1	-27,9
Q4 2014	217,5	-25,2
Q1 2015	50,3	-74,1

Figure 13 The dynamics of new car loans issue (Source: National Bureau of Credit Histories (NBCH) according to 3000 creditors except the bank «Sberbank of Russia»)

<b>Period</b>	<b>Sales in thousands</b>	<b>% changes (from year to year)</b>
Q1 2014	555,5	1,33
Q2 2014	553,3	-17,48
Q3 2014	524,3	-18,33
Q4 2014	704,4	4,28
Q1 2015 r.	275,4	-50,4

Figure 14 The dynamics of the sales of passenger cars (Source: «AVTOSTAT» agency)

<b>Period</b>	<b>Share, in %</b>	<b>Changes from year to year in percentage</b>
2014	48,0	
Q1 2014	40,2	-5,1
Q3 2014	42,7	-3,1
Q3 2014	45,2	-5,9
Q4 2014	35,5	-14,0
2015	40,5	-7,5
Q1 2015	20,1	-20,1

Figure 15 The dynamics of the share of cars sold on credit (Source: In general, on the market of RF, the calculations of NBCH and «AVTOSTAT»)

Nº	Brand	January — March of 2014 in thousands	January — March of 2015 in thousands	Changes, %
1	TOYOTA	23,6	24,0	1,6
2	HYUNDAI	15,9	11,0	-31,1
3	MERCEDES	10,9	9,6	-12,5
4	LEXUS	4,4	7,2	63,2
5	MITSUBISHI	10,7	6,3	-40,6
6	AUDI	6,1	6,1	0,7
7	LAND ROVER	5,9	3,6	-40,1
8	DAEWOO	5,6	2,3	-58,7
9	VOLVO	4,1	2,2	-45,5
10	NISSAN	16,1	1,6	-90,0
	TOTAL	159,9	87,3	-45,4

Figure 16 Top—10 most imported brands of passenger cars in January — March of 2015 (Source: <http://avtosreda.ru/news-common/Importlegkovushekupalna45TOP10modeleyizzarubehza/>)

The decline in incomes could not but affect the real estate market. If earlier the prices for elite housing grew at a rather high pace, now prices are rising in the secondary apartment market in Russia slowed down a lot. This affected the cost of one square. m of housing. In 2014, its value increased from 60 598 rubles. in December 2013 up to 63 635 rubs. in December 2014, i.e. only 5%. 2014 data are presented in Figure 17.

Month	12.13	01.14	02.14	03.14	04.14	05.14	06.14	07.14	08.14	09.14	10.14	11.14	12.14
Price, rub/ sq.	60 598	61 847	61 159	61 576	62 994	62 327	62 406	62 477	62 709	62 858	63 192	63 538	63 635
Changes to 12.2013		0,4%	0,9%	1,6%	2,3%	2,9%	3,0%	3,1%	3,5%	3,7%	4,3%	4,9%	5,0%
Changes compared to previous		0,4%	0,5%	0,7%	0,7%	0,5%	0,1%	0,1%	0,4%	0,2%	0,5%	0,5%	0,2%

Figure 17 - The dynamics of the average price on the market of pre-owned apartment in Russia, rub/sq. in 2014. ( Source: : <http://www.domofond.ru/pricearchive/downloads/2/price-realty-report-2014>)

Although at the beginning of 2015, prices in the secondary market of apartments increased slightly, already in the 2<sup>nd</sup> quarter there was a decline, which continued until August 2015. The decline also touched the dynamics of the average price of offers in the rental market. However, here the situation began to improve noticeably faster. In July, growth was outlined and after the recession in August continued in September. Thus, the situation in the real estate market already stabilized and some prerequisites have been created for the start of growth.

## 5.2 Tourism

The economic crisis hit tourism hard. The cost of traveling abroad increased by 50% or more. The main flows have changed - domestic tourism in general and in southern Russia has greatly increased. The result was a reduction in travel abroad and revitalization of domestic tourism. In conditions when the service on domestic routes lags significantly behind international standards, there has been a deterioration in the price-quality ratio. Foreign trips of Russian citizens in 2014 decreased compared with 2013 by 15% (from 54.1 million to 45.9 million), and demand for

domestic tourism in 2014 increased by 30-40%, and this trend preserved in 2015. In the CIS countries, on the contrary, the number of Russian tourists has increased sharply: in Kazakhstan - by 99%, in Georgia - by 38%, in Armenia - by 16%. At the same time, the volume of purchases increased significantly in these countries<sup>1</sup>. The depreciation of the ruble created objective prerequisites for attracting foreign tourists to rest in Russia. True in the past the year the total number of tourists decreased by 3%, but the number of people Arriving in Russia for business reasons, on the contrary, increased by 8%. Especially noticeable is the entry from South Korea, Israel, Poland, Finland and China.

In 2013, Ukraine was the most popular country among Russians, but in 2014 she moved from the 1st place she occupied in 2013, the 6th (by 7.3 million people, or 73.2% of Russians, less than a year earlier, tab. 4.7). The most popular countries to travel abroad in 2015 were Abkhazia, Turkey, Kazakhstan, Finland, Egypt, Estonia, Poland, China and Germany. In each of these countries, more 1,000,000 trips (tab. 4.8). However, after a series of political events (the attack on board the A321 and the military incident with the SU-24) at the end of 2015, the situation changed dramatically, which created the prerequisites to increase the role of domestic tourism. According to a Citibank study, for 5 months of 2015, demand Russian citizens on purchases abroad fell sharply, then how domestically grew by 21%<sup>1</sup>. Russians, according to Citibank, still have the most money spend in the USA, Italy, Great Britain, Finland and France. However, in all these countries there was a significant decrease in the number of Russian tourists: in Italy by 37% (compared with the same period in 2014), in Finland by 43%, in France by 39%, in the UK by 17%, in the USA by 26%. At the same time, the volume of purchases in these countries declined even more. The depreciation of the ruble created objective prerequisites for attracting foreign tourists to rest in Russia. The number of foreign tourists visiting Russia increased from 2244.6 thousand in January - September 2014 to 2539.5 thousand in January - September 2015, i.e. by 13%. Particularly noticeable increase in tourists from Asian countries: China (increase by 63%), South Korea (an increase of 41%), Iran (an increase 111%), India (an increase of 66%), Taiwan (an increase of 35%) and Hong Kong (by 25.5%, tab. 4.9). As a result of the southeast country Asia and Israel are ahead of Europe in the number of tourists coming to Russia. China came first, ahead of Germany and the United States.

## 5.3 Small Business crisis

Small businesses have been hit hard. If in 2013 in Russia 490.7 thousand legal entities were opened, and 419 thousand were closed, then for 11 months of 2014, 417.5 thousand legal entities were opened, and 483.6 thousand were closed. This means that if in 2013 the number of legal entities opened was 70 thousand more than those closed, then in 2014, the opposite situation was observed: almost 70 thousand legal entities closed more than they opened. In Moscow, for example, in 2014 it was filed 14.5 times more ads for the sale of business than in 2013, in the Moscow region - 11.7 times, in St. Petersburg - 15.8 times, in Krasnodar Krai - 11.1 times<sup>1</sup>. In order to support small and medium-sized businesses, the State the Duma adopted a law that will last for three years, effective January 1, 2016, on exempting small businesses from unnecessary inspections. However, looking at current years the support of small business was very weak and had barely any impact in following years.

## 6. What is next?

The purpose of the sanctions against Russia is not only a change in the political course of the country, but also the realization of the economic interests of the Western countries, the initiators of the sanctions, the increase of political support for the establishment by their citizens, as well as the demonstration of their position regarding Russian policy to third countries. It is possible to formulate considerations and recommendations regarding the sanctions policy in the form of the following set of theses.

- Firstly, empirical studies do not provide unambiguous assessments of the effectiveness of sanctions in terms of achieving their goals. Success from the imposition of sanctions is achieved only in a third of cases. According to available estimates, the average negative effect of sanctions for the recipient country is 5% of GDP, although not considering their long-term impact. Economic sanctions also lead to increased uncertainty in the economic system, which results in a reorientation of national economies to domestic markets and, as a result, a decrease in development potential. Assessment of the negative impact of sanctions on the Russian economy is approximately 6 percentage from GDP per year (that is how much Russia is losing in terms of economic growth).
- Secondly, the successful experience of countries that have come under different sanctions at different times has shown that the most effective anti-sanctions policy is not the introduction of symmetrical measures and the closure of markets for goods / services / capital, and the policy of “aggressive” openness of markets for cooperation, including with countries that apply sanctions, the so-called liberalization in response to sanctions. Examples of this are China’s liberalization policy and active participation in the global economic system as a contrast to trade and political sanctions introduced in b; South African policy, namely, the path to counteracting trade and political sanctions through an emphasis on diversifying the commodity structure of exports, searching for new markets and sources of supply of necessary goods. The opposite vivid example is Iran’s anti-sanction tactics: abandoning the dollar; building close relations with countries included in the SDN sanctions list; adaptation of the mechanism for circumventing sanctions through

“intermediaries” and special-purpose companies; mutual settlements with a limited circle of solvent partners in the national currency of the buyer; barter agreements.

- Thirdly, the main negative channel for the impact of sanctions on the Russian economy is not so much in the level of sanctions, but in maintaining uncertainty about future sanctions parameters. The main consequence of the announcement and introduction of new sanctions is the growth of uncertainty, expressed in significant fluctuations in the financial markets, ruble volatility, the refusal of foreign investors to cooperate with Russian companies, the outflow of capital from Russia, etc. In this regard, it is advisable to direct efforts in the short and medium term to stabilize the current level of sanctions for reduction of uncertainty, and not their complete abolition.
- Fourth, in order to reduce the risks of foreign companies, it is advisable to create favorable conditions for investors, especially in the “non-sanctioned” sectors, and to increase the transparency of the ownership structure. In the medium term, for beneficiaries and those who lose from sanctions at the level of individual companies (corporations) located in the jurisdiction of the United States and the EU. Beneficiaries should create additional opportunities in the Russian market, the loss of which could be critical for their business. It is already possible to work with losers as lobbyists for easing the sanctions regime or as lobbyists for stabilizing the level of sanction pressure.
- Fifth, assistance is needed in disseminating information to foreign companies, especially European ones, about the benefits, security and transparent conditions for investing in Russia, as well as about the damage caused to EU and US entities by anti-Russian sanctions. In order to mitigate the negative consequences of existing and the risks of introducing new sanctions, along with the development of the manufacturing sector, human capital, science, innovations, strengthening of national institutions, a wide diversification of trading partners, commodity export items, an increase in the share of foreign economic settlements in rubles, and the creation of our own financial infrastructure involving its use by other countries.

The European Union chooses as a target industry, on the income of which the state budget of the Russian Federation largely depends. The history of the Cold War period repeats itself in more complex globalization conditions for Russia. At the same time, the country's economy, as well as

a decade ago, retains its raw material specialization, which leads to the instability of its economy. Russia has practically nothing to oppose to the EU countries in the war of economic sanctions. And the issue is not only the size of economies. During the period of high hydrocarbon prices, the opportunity was missed to modernize an archaic sectoral structure unacceptable for a country that claims to be a member of the OECD (however, the process of Russia's admission to this international organization has been suspended). Sanctions are also directed against the Russian military-industrial complex, which further increases the burden of military spending for the country. The history of the USSR shows that, combined with a drop in hydrocarbon revenues, an increase in military spending can have disastrous consequences. The legitimacy of the measures taken by Russia, as well as the EU sanctions, can be disputed and defended within the framework of the WTO. However, it is necessary to consider what grounds for imposing sanctions are recognized as justified in this organization. In our opinion, it is wrong to underestimate the cumulative effect of economic sanctions. The USA, Canada, Australia, as well as the EU countries, Russia's main economic partners, have resorted to this policy tool. Under the pressure of geopolitics, economic interests fade into the background. However, they can become decisive if continued sanctions lead to negative growth dynamics. Russia will fully experience the delayed effect of economic sanctions by the EU in a year or a half. We emphasize that sanctions that worsen the situation in the Russian economy are not the primary cause of its current state. The previous economic model has exhausted itself, but the way out of the current situation, in our opinion, is not in the mobilization, but in the market model, using fiscal and monetary policy tools, state-private partnership mechanisms.

## 7. Conclusion

In this bachelor thesis, we have looked at the sanctions and counter-sanctions measures that were imposed by the Western countries and also by Russia itself all due to Russia's illegal actions towards Ukraine such as but not limited to annexation of Crimea and military actions in eastern regions of Ukraine. The existing researches, articles and literature on economic effects suggests that sanctions did have and continue to have a negative effect on Russian economy. Although it is worth mentioning again that the available information consistently implies that between 2014 and 2016 the decline in the price of oil had a much larger negative effect on the Russian economy than sanctions. Although, it is possible that if sanctions on both sides remain in place for an extended period, especially if Russia intensifies its import-substitution policy then Russia's long-term growth potential will be decreased. Exports to Russia from the Western and other countries that had an involvement with sanctions have declined in recent years. We can see that the direct effect from sanctions on export decline was limited, however, the main factors behind this development were the contraction in demand in Russia and substantial depreciation of the ruble. In Russia's banking sector, large state-owned banks such as Sberbank and VTB dominate. As they have been targeted by the ban on long-term financing, it is no wonder that the foreign debt of Russian banks has decreased dramatically. Many EU sanctions are explicitly linked to the Minsk peace process and its implementation, which currently seems quite distant. At the same time, Russia's food import bans seem to have become parts of its overall import substitution policy. These two facts in themselves are enough to imply that various sanctions on bilateral economic activities between the EU, US and other countries, as well as Russia on the other side, will be in place for a good while. The latest round of US sanctions in April 2018, illustrates how further sanctions can add to the uncertainty concerning Russian economy.

Summing up the results of four years of the sanctions war, we can state the following. At the time of the imposition of sanctions, none of the parties had a clear assessment of the future cumulative consequences for their own economy. Such estimates were received only recently and showed that certain amount of damage was caused not only towards direct participants in the economic conflict, but also to the countries that are not involved in it. Regional sanctions wars in fact have a global dimension in the form of a rupture of links in the GCCS.

For the Russian population and consumers, there is very little causal relationship established by experts between sanctions but a way stronger impact due to countersanctions. It is the average consumer who felt the burden of economic counter sanctions. During the Crimean Crisis the cost of living in Russia dramatically increased. Most elders were not able to reach new minimal cost of living resulting more and more people to move below poverty line. During 2014-2015 Russian government kept increasing taxes, kept the government spending rising on military costs. By increasing military spending, they had to lowered education and healthcare costs. During that time almost zero help was given towards population of Russia thus leaving all the economic burden on shoulders of Russians. That trend is not new. Even before Crimean Crisis and after it, from what we can see, Russian government always placed it's citizens at the lowest priority, it is the middle class that barely saw any assistance from its country during tough periods and struggled a lot. And things don't change for Russia. Even nowadays during the fall of Russian ruble in 2020 with combination of novel coronavirus Covid-19, Russia increased the income taxes and instead of setting the quarantine they've set the "unpaid holidays" the only thing government doesn't take into consideration is that vast majority of Russian's do not have savings and live from paycheck to paycheck and by introducing the unpaid holidays, they've let firms and companies to let people go. Already millions of people are unemployed, and cost of living is rising because of Covid-19. In the result all we can say about it is either Russian government can't or what's most probable is that they just don't want to help its citizens as they've consistently showed that government doesn't care.

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