



# russian analytical digest

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## SANCTIONS AGAINST RUSSIA RUSSIA'S WAR IN UKRAINE ON SOCIAL MEDIA

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## ANALYSIS

## Fortress Russia: Completely Lost in (Financial) Sanctions Warfare, A Deep Economic Crisis Is Unavoidable

By Gunter Deuber (Raiffeisen Bank International AG)

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### Abstract

Russia has been preparing for years for measured Western economic and financial sanctions as part of its so-called Fortress Russia strategy. With the invasion of Ukraine, an unpredicted and extraordinarily broad-based spiral of sanctions has been unleashed by the Western world. Tools of economic warfare—specifically the freezing of substantial public and private funds—were deployed quickly, while “private” voluntary sanctioning (company withdrawals, supply stops in non-sanctioned sectors, etc.) has been unexpectedly comprehensive. The bulk of sanctions and company withdrawals will likely remain in place for a long time. Russia’s economic crisis management has so far appeared eclectic and defensive; stronger countermeasures may yet follow. In the West, a clear strategy is needed to use the hundreds of billions of dollars/euros in frozen Russia-related funds as reparations for the reconstruction of Ukraine.

In 2022 and 2023, Russia faces the most severe and self-inflicted economic crisis since the deep and multi-year transition crisis of the early 1990s. The complex interplay of deep official Western economic and financial-market sanctions and a withdrawal of large and medium-sized foreign companies, investors, and trading partners from Russia (private sanctions) that is unprecedented in modern economic history will lead to a very deep recession and probably a long-lasting economic stagnation. When it comes to financial markets, Russia is already close to collapse in some areas due to the extremely quickly established and very far-reaching Western financial sanctions, which go far beyond mere sanctioning by the US, UK, and EU and G7 countries.

The GDP slump in 2022 should be significantly more pronounced than during previous crises such as the global financial crisis and the occupation of Crimea. In addition, unlike during previous crises, a further GDP slump can also be expected in 2023. As such, economic output could collapse by at least 10–15 percent over the next 12–24 months, with downside risks. This time, the rapid recovery and rebound otherwise characteristic of emerging markets is very unlikely. A probably still strong first quarter and hoarding purchases will likely provide a buffer in terms of the GDP recession number in the 2022 economic slump. A concrete point forecast for GDP growth and the depth of the upcoming recession is hardly feasible to be made in a clear-headed way. Currently, it is not possible to clearly assess how drastically Russian imports will collapse in the coming weeks and months or how much exporting will still be possible, for how long, and to where, making it difficult to elucidate how high the positive external contribution to Russian growth will be. Currently, it seems likely that imports will drop by

40–50% in 2022, while export is set to drop by at least 10–15%. It is also not possible to predict how drastically domestic consumption and overall economic plus investment confidence in Russia will suffer as a result of the unseen sanctions and to what extent local support programs will be able to compensate for this. Financing conditions have already tightened drastically, as exemplified by the rise in the key interest rate to 20%. Inflation is expected to average at least 20 to 25% this year and will most likely remain in double digits in 2023, producing further declines in real wages. The Russian Central Bank (CBR) does not expect to reach its inflation target of 4% before 2024. In view of its economic isolation, Russia will also not be able to benefit in the foreseeable future from growth effects in foreign trade resulting from the drastic devaluation of the ruble. This is often a channel from which rapid recoveries in emerging markets emanate and one from which Russia benefited in the aftermath of the 1998 economic and financial crisis (J-curve effect).

However, Russia is not facing a GDP collapse, as Iran did following the 1979/1980 revolution (–10% and –27%). For one thing, Russia has more of its own resources, in some subsectors consolidated economic structures that have been oriented toward self-sufficiency for some time, and a functioning economic and financial bureaucracy. In addition, certain export activities will continue to be possible, especially by land and on a selective basis by air and sea. Nevertheless, the coming economic slump will be dramatic in terms of the country’s economic strength or GDP in foreign currency terms and the general level of prosperity. Russian GDP will, in foreign currency terms, fall to just over \$1,300 billion in 2022/2023—where the country was in 2007 and 2015. At the beginning of the 2010s,

Russia's GDP in foreign currency terms amounted to over \$2,000 billion. Thus, the last decade or so has been economically lost when it comes to GDP levels. For years, Russia's economic policy has been focused not on increasing prosperity or investments, but on building up reserves plus financial shielding (Fortress Russia strategy) and a retreat from the process of globalization. Also, in the very long term, Russia is lagging far behind the global average in terms of prosperity: Russia's nominal GDP (in foreign currency) as of 2022/2023 will be about 2.5 times higher than at the end of the 1980s, while world economic output has increased by a factor of 4.5 during that period of time. This shows Russia's relative loss of economic importance, which can be expected to continue. The interplay of deep economic and financial sanctions and the emerging brain drain will cause the already low potential growth of the Russian economy to drop further. Whereas potential growth in the Russian economy was estimated at 1.5% before the Ukraine war, it is now estimated to fall well below 1%.

### **Complete Underestimation of Private Sanctions and the Global Environment**

The impending economic collapse will, in all likelihood, be much more severe than the Russian leadership might have anticipated during its cynical preparation for the war in Ukraine. This is because the Western and internationally coordinated financial and economic sanctions have been implemented much more quickly and with much further reach than the Russian side probably anticipated—perhaps also because they expected faster “creation of facts” in the Ukraine war on the ground. However, the West quickly drew battle lines in what both sides agree is “economic warfare”; the Russian side is currently even talking about an “irresponsible Western economic blitzkrieg.” The very far-reaching sanctioning of the Russian CBR is exemplary here. In addition, the Western financial sanctions—which have been imposed with particular severity by the US and the UK, leading to the virtual exclusion of Russia from these global financial centers—are having a significant impact on Russia's financial and logistical ability to conduct large-volume foreign trade even in areas that have not yet been sanctioned. For example, even without a broad-based Western oil embargo, 50–80% of Russian crude oil exports can no longer be processed by ship, and there are hardly any processing possibilities in the air freight business (which restricts palladium exports, for example). Trade financing, the hedging of Russia-related risks, and logistical processing are no longer commercially viable, while traditional customers no longer want to buy Russian products, including oil. This is why the price discount of Russian oil (Urals) from the world market price, for

example, is currently at an unprecedented \$10 to \$30. Furthermore, the exclusion of Russia from WTO regulations, which is being pursued by the US and the EU, would allow for substantial punitive tariffs to be imposed on Russian products that are still tradable.

In addition to the Western government-led sanctions on Russia, there is massive (voluntary) private-sector sanctioning going on, which the Russian leadership had probably not anticipated. Western corporations that are cutting their Russian operations are doing so in view of the reputational risks of continuing operations, as well as the expected difficult economic situation this year and in the coming years. Already, more than 400 major international companies have put their Russian business on hold, sold their operations or no longer supply the Russian market (or do so only on a very limited scale). These include not “only” the consumer and luxury goods manufacturers found on the shopping streets of Moscow and St. Petersburg, but also many international industrial, capital goods, and machinery manufacturers (including of construction machinery, electronics, and tires). Here, the Russian side obviously completely underestimated the global (social) media impact of the invasion of Ukraine; the increasing focus in international business on social aspects and governance issues; and the current “termination culture,” which has combined with management techniques pushing for swift adaptation to fast-changing circumstances. Moreover, given Russia's limited economic power (its GDP in Euros is just three times higher than the Austrian GDP!), Russian business and/or turnover is not of systemic importance to most international corporations with larger Russian operations. In addition to many large companies and export bans, significant private sanctions are also evident and expected in the small and medium-sized business sector; here, of course, financial sanctions also have a significant impact. The lack of supplies and technological imports should lead to considerable tensions in the Russian economic cycle this year and in the medium term that are not yet easy to project and will not be easy to substitute in a “centrally planned” way. Especially in the technology sector, it will be difficult to find suitable replacements on the world market. For instance, Russian producer Avtovaz has already had to announce that it will move up its scheduled summer operating vacations to April. Furthermore, the far-reaching Western financial market sanctions make it very difficult for large non-Western companies to actively pursue substantial business in Russia. Major Chinese (state-owned) banks have also switched to very restrictive foreign trade financing practices. Even the joint development bank (NDB) established by the BRICS—Brazil, Russia, India, China, and South Africa—put all new Russia financing or projects on hold in early March.

### **Naiveté in the Area of Financial Sanctions— Or Were the Relevant Bodies Not Thoroughly Involved in the Escalation Action Plans?**

In recent weeks, there have been unprecedented financial sanctions against Russia, a large, trade-open, and heretofore internationally integrated state. Countries that have faced such heavy sanctions in the past have had much more limited financial links to foreign countries than Russia: Iran's and Venezuela's financial exposure to the outside world amounted to \$15–20 billion and North Korea's to \$2 billion, compared to Russia's \$250–500 billion. These figures highlight how economically irresponsible the Russian escalation in Ukraine is.

The rapid Western action in the area of financial sanctions was possible because the West's meticulous and internationally coordinated sanction preparation behind closed doors in the pre-war weeks, based on close exchange between public and private actors. Russia's brutal actions in Ukraine also justified the quick imposition of the most hard-hitting financial sanctions, which clearly went beyond previously publicly discussed options such as exclusion from the SWIFT payment system. Chief among these were the possible freezing of foreign exchange reserves and the comprehensive sanctioning of the CBR. This also shows that Russian authorities apparently did not expect such a measure to be implemented quickly. After all, in terms of economic warfare, it seems downright naïve of Russia to hold a large part of its foreign exchange reserves in French and German securities or in account balances in Western national central banks or the Eurosystem. The decisive reaction of the US, the EU, and the G7 countries has also led to countries or financial centers such as Switzerland and Singapore, which have historically not implemented financial sanctions in lockstep with the West, joining the financial sanctions train. As a side effect, Russia's financial leeway to support "allied" states (eg., Venezuela) going forward has been restricted.

The harsh sanctioning of the CBR has put this formerly reputable institution on par with the central banks of countries like Iran, Venezuela, Myanmar, and Afghanistan. The imposition of the harshest possible sanctions—which may have come as something of a surprise to the Russian authorities—was necessary because Russia has been meticulously preparing for moderate or so-called "cosmetic" financial market sanctions in recent years as part of its appropriately named "Fortress Russia" strategy. The latter has entailed accumulating foreign exchange reserves, cautious fiscal policy, and external deleveraging, all at the expense of economic development.

On the local financial market and also in terms of international investor perception, the comprehensive Western financial sanctions have had a devastatingly fast impact. In the space of a week, 20–30 years

of work to rebuild the country's financial sector and capital market reputation have been wiped out. Within days, Russia's country risk rating moved into the realm of insolvent and/or unwilling-to-pay countries (such as Sri Lanka, Congo or Argentina). There have also been noticeable private sanctions in the financial sector, with the withdrawal of global payment providers (eg., Visa, Mastercard, American Express, Apple Pay, and PayPal) from Russia or from Russia-related business abroad. In the coming days and weeks, Russian assets will be completely excluded from the relevant international benchmark indices. Extensive public and private Western financial sanctions have necessitated harsh foreign exchange market restrictions for local companies and individuals, while local financial markets are de facto dysfunctional. The Moscow Stock Exchange has been closed for weeks, making securities sales and active divestment by foreigners impossible. (Foreigners currently hold about \$29 billion in local government securities, for example.) The freeze on market transactions is currently providing some support to the ruble exchange rate, yet the ruble has nevertheless lost 50% of its external value in recent weeks. Russian exporters are currently being forced to exchange 80% of their foreign exchange earnings in order to rudimentarily stabilize the ruble exchange rate. Russian citizens without foreign currency accounts are now unable to obtain foreign currency until September, while the withdrawal limit for citizens with foreign currency accounts is limited to \$10,000. Small companies are allowed to withdraw foreign currency only in \$5,000 amounts until September. Considering that private depositors in Russia have accumulated foreign currency savings of \$90 billion deposited at Russian banks and companies have at least \$150 billion in deposits, these are significant restrictions. Thus, unlike in 2014/2015, the Western financial sanctions are reaching the breadth of economic life and the population. Of course, with this there are more and more signs of a black market; the foreign or world market price (offshore) for the ruble on the international financial market is also still above the local and administered exchange rate (onshore). Russia's authorities no longer believe in a quick recovery either. Foreign exchange controls are set to continue into the fall; market prices for Russian assets in bank and balance sheet valuations will also be frozen at pre-war levels until then. There will also be separate and regulated onshore and offshore markets for shares and bonds on March 21, a clear expression of the "wartime economy" in the financial sector.

### **Technical and/or De Facto State Bankruptcy as a Symbol of the Changing Times**

In the coming days and weeks, a discussion about a technical or de facto sovereign default by Russia (or



its major corporates) on its foreign debt will in all likelihood become prominent among the public, financial market experts, and lawyers alike. In the spirit of economic warfare, Russia has defined a list of unfriendly states to which foreign currency payments will be possibly made only in rubles in accordance with a presidential decree. In certain financing and sovereign bond contracts, Russia has even cynically prepared for Western sanctions since 2014, adding clauses that allow repayment in a different way (rubles) than in the original currency or foreign currency if sanctions are in place. But in financing structures issued before 2014, Russia does not have this right. De facto, a ruble transfer—as required by the presidential decree—would therefore constitute a payment default or unilateral contract breach. Interestingly, the decree has not been applied in practice in recent days and weeks. Larger Russian companies (such as Gazprom, Rosneft, Russian Railways, Norilsk Nickel, and Severstal) still made payments in foreign currency in March, partly with the exceptional approval of the Ministry of Finance, and thus implicitly undermined the decree (albeit in complex offshore payment structures). The state itself also avoided a technical sovereign default on March 16; at least for the time being. Dollar interest payments on a sovereign bond apparently did reach international investors. Although some market participants already expected an escalation, i.e., a unilaterally driven payment in rubles, sanctions on the CBR still allowed for a dollar transfer during a grace period. In particular, the License 9A of the OFAC authorizes transactions necessary for the receipt of interest or maturity payments for the debt of the Russian Ministry of Finance issued before 1 March 2022 through 25 May 2022. Essentially, this means that all payments up until then might be still transacted in an orderly way. At the moment, it looks as if Russia or the relevant competent institutions, like the CBR and the Ministry of Finance—in a surprisingly risk-strategic consideration—do not want to cut all financial ties to the international capital markets prematurely.

The balance between Russia's ability and willingness to pay after 25 May remains unclear. Without unlikely changes to the sanctions regime, there could be more clarity about the looming (technical) sovereign default on external debt by then at the latest. Russia will probably blame this on the Western sanctions and deny a technical state of bankruptcy. However, the question of who triggered this looming technical state bankruptcy is secondary. The outlined facts show that Russia has been trying to prepare for sanctions for years, with the result that the West's only option was to impose extremely severe financial sanctions, including a technical sovereign default. Given the financial sanction escalation and questions about Russia's current willingness

and ability to honor external payments, there is no way for the Western side to do business with Russia and to insure business with Russia with a certain predictability and financial hedging possibilities.

In 2022, about \$60 billion in foreign debt is still due and it remains to be seen what will be serviced and in what currency. However, tough financial market sanctioning of Russia was possible because the weak performance of the Russian economy—combined with its rather moderate level of financial development and active pursuit of deleveraging—meant that Russia was very easy to sanction without incurring substantial global systemic risk. The Russia exposure of international banks and on international financial markets is at roughly the level of Greece in 2008–2010. In the latter case, investors were possibly not prepared for a shock or default at that time; Greece was also not seen as a risk exposure before its debt crisis. The situation is different in the case of Russia, where a certain degree of risk awareness had existed for years in view of longstanding financial market sanctions.

The dramatic currency collapse already outlined; the financial isolation of Russia to a level similar to Iran, North Korea, Myanmar or Afghanistan; and the threat of technical or de facto state bankruptcy show that the current Russian leadership is no longer concerned with longer-term-oriented economic-rational considerations. Indeed, it has more or less consciously accepted leading the country into a worse economic and financial crisis than in the late 1990s—a traumatic period in Russian collective memory. Unfortunately, it is therefore reasonable to assume that further economic and financial sanctions, including those already implemented, will not per se lead to a departure from (foreign) policy objectives. After all, Russia is not necessarily dependent on foreign currency income for short-term warfare (except to provide the relevant raw materials), can continue to finance the war in local currency, and will possibly accept substantial short- and medium-term inflationary risks.

Nevertheless, it is important to consider further sanctions steps to limit Russia's potential to cushion the economic crisis. Considering that forced foreign currency income conversions are continuing to provide some stability to local financial markets, income streams in foreign currency would probably have to be further limited. Furthermore, it must be accepted that an entire institutional system has prepared itself for cultural and civilizational rupture, and thus the bulk of the sanctions will probably have to be maintained for years (or decades) in order to limit the country's medium- and long-term ability to act to the maximum—in the absence of comprehensive systemic changes that go beyond "personnel reshufflings." Currently, we are "only" in the eighth year of sanctioning Russia—rather moderate sanctions

began in 2014—while sanctions regimes may well be necessary for decades.

### **Russian Emergency Measures: Counter-Sanctions to Come**

As economic and financial sanctions bite, it is leading to the hoarding of goods that are expected to be sanctioned, followed by their substitution with goods that are still available. For example, Western smartphones that were still available in early March quickly sold out; since then, Chinese models have been in demand. Russia has already switched to crisis mode in the economic sphere. Of course, the budget rule for 2022 was immediately suspended in order to pursue an expansionary fiscal policy and deviate from the otherwise dominant austerity course that characterized the “Fortress Russia” strategy. There are plans, for example, to set tariffs on key imports (vegetables, grain, critical parts for manufacturing, as well as baby food and goods for the manufacture of pharmaceutical products) at zero for at least six months, thus facilitating customs clearance. In the export sector, Russia has imposed export restrictions for several months on such goods as wheat, semolina, rye, barley, corn, and sugar (with the exception of its economic partners in the EAEU) in order to keep such products in the country for the time being. The fact that Russia’s leadership was completely surprised by the Western public and private sanction dynamics is also shown by the fact that now apparently not officially approved imports of Western companies are somehow to be sold on the world market.

On top of the defensive freeze of local financial markets, funds from the National Wealth Fund are now being used to buy or repurchase Russian government bonds and shares on a large scale. COVID restrictions on public life are also being lifted quickly to provide some support for the economy, while measures are being initiated to take over foreign companies or assets (those with more than 25% foreign ownership) from unfriendly states or companies withdrawing from the Russian market. Technical-administrative measures cannot be ruled out either; for example, the regulatory closure of Sberbank’s European subsidiary (in Vienna) was due not only to an order by the European Central Bank (ECB), but also to observed customer and liquidity outflows. Such processes, in conjunction with social media and/or propaganda campaigns, are quite conceivable in Russia as well. In the coming days and weeks, we can also expect export restrictions from the Russian side that will inflict certain shortages and price pressure on global commodity markets and global manufacturing. To date, however, there is no comprehensive plan to support the domestic economy, which, in conjunction with the rationing measures outlined above, is a further indi-

cation that the current deep financial and sanctions situation was probably not planned for. Rather, there are desperate political appeals for private (and small) companies—which have long struggled in Russia’s state-centric business climate—to play a decisive role in stabilization, as regulatory and administrative hurdles are to be quickly removed. A certain amount of scepticism is appropriate here in light of the institutional structures in the country. At the same time, technical-operational steps are being taken to strengthen China–Russia trade, as demonstrated, for example, by the linking of the two national payment systems.

### **Economic Reconsideration of the Ukraine Invasion and Reparations**

The accumulation of (now-frozen) foreign currency reserves was an important part of this cynical preparation for war, and here a lot of thinkers and practitioners in the state administration were certainly involved—even if they were perhaps unaware that such a devastating war of aggression was being planned. The following figures suffice to illustrate the extent of Russia’s preparation: whereas it is standard practice to hold foreign exchange reserves in the range of 6–12 months of import cover, Russia recently hit 30 months. This exuberant accumulation of foreign exchange reserves as part of the “Fortress Russia” strategy has taken place at the expense of the domestic population and represents a departure from a sound and prosperity-enhancing economic policy.

It is precisely these foreign exchange reserves that must now be used to hold Russia and its state apparatus economically responsible for the humanitarian catastrophe and alleged war crimes in Ukraine. In all likelihood, Russia will unfortunately dominate some of the (peace) negotiations in the interest of conflict resolution, and official reparations from Russia to Ukraine can hardly be expected. It will therefore be all the more important to draw on the currently frozen Russian foreign currency reserves. However, it is also important to proceed moderately and to cut Russia down to a realistic level. According to relevant import ratios, Russia probably needs foreign exchange reserves no greater than 200–300 billion euros. Taking into account its domestic gold reserves and those located in China, about 250–350 billion euros of Russia’s frozen foreign exchange reserves should be available to build up Ukraine. Nor would this be an entirely novel approach: the US intends to use some of the frozen funds of the central bank of Afghanistan to compensate the families of 9/11 victims.

In the case of Russian public assets and/or assets of individual actors in the military and security apparatus, there are different grounds for confiscation than in the case of private assets of oligarchs. For public assets

it will most likely be possible to establish a clear link between the Ukraine war and state actions. In order to justify an infringement on Russia's assets, some political and legal safeguards are necessary. To this end, it is important to pursue a further formal-legal clean isolation and condemnation of Russia and relevant key figures, including for war crimes. This applies above all to the International Criminal Court (ICC) in the Hague, where Moscow currently refuses to play a constructive role, and to the documentation of war crimes. On the economic level, too, further sanctioning and isolation will certainly be necessary to prepare Russia's reparation payments. Attempts to withdraw Russia's voting rights in the IMF, to terminate Russia's membership in international development banks, etc., could be considered as well—for only if Russia is successfully positioned as a "pariah state" at all levels can the outlined reparations strategy work. Nevertheless, in the context of the current economic warfare, the West and the international community of states must take steps to uphold the rule of law and to differentiate sufficiently between frozen assets and any expropriation of (state) assets that may be necessary. In the coming days and weeks, a joint task force of the EU, the US, and the UK will track down the assets of Russian oligarchs and actors of the security establishment in more detail and block or freeze them. The latter is certainly not an easy factual and legal undertaking given complex holding and offshore structures and assets, such as yachts, real estate, cars, and football

clubs. Going forward, there could also be legal challenges arising from this exercise.

Interestingly, some oligarchs are trying to distance themselves somewhat from the Putin-Russia regime, whether out of conviction or as a hedge for legal disputes. The private assets of Russian citizens can certainly not be used simply or completely as compensation for misconduct or war crimes on the part of the Russian state. To justify confiscating these assets to such ends, a very clear connection to the war machine—that is, to representatives of the bureaucracy and the security apparatus—would have to be proven, especially since the West long tolerated this influx of Russian money, at least silently, and the consulting and legal industries made a good living from it. However, one could still consider a significant tax on pure oligarch money, as demanded by renowned economists like Thomas Piketty. Even a tax that is not particularly high could yield substantial sums here. After all, the assets of Russian oligarchs abroad could amount to between 50 and 100% of Russia's GDP. The taxation solution is also preferable to outright appropriation in the sense that it avoids playing into Russian propaganda claims that the West is engaging in banditry. However, it has long been Putin-Russia's strategy to harness the economic elites strongly to its nationalistic policy. If they fear expropriation in the West, this could even succeed. Of course, the foreign assets of the members of the Russian military and security apparatus must be treated differently.

The views presented and opinions expressed in this article are those of the author and do not necessarily reflect the official policy or position of Raiffeisen Bank International AG.

#### *About the Author*

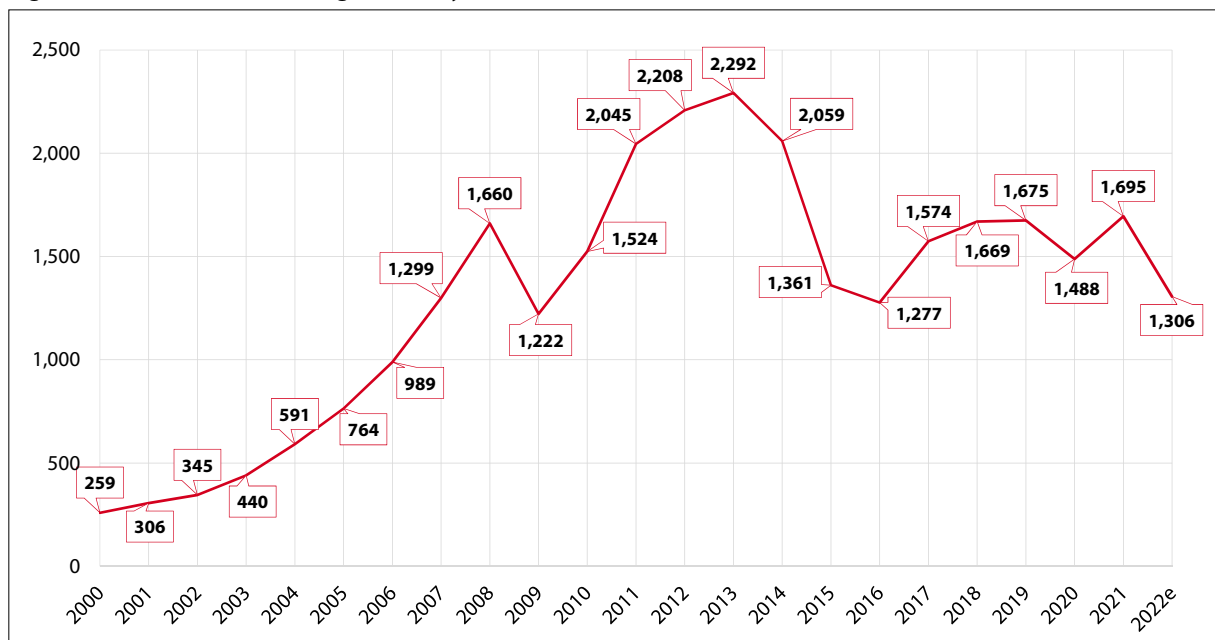
*Gunter Deuber* is Managing Director and Chief Economist of Raiffeisen Bank International AG in Vienna, one of the largest foreign banks and investors in Russia, Ukraine, and Central and Eastern Europe. In his day-to-day business, he collaborates closely with a team of local economists based in 14 countries in CEE, for whom he performs a steering and coordination function. He regularly publishes in professional journals, edited volumes, and industry magazines. In addition to his analytical work, he supports RBI's top management in discussions with stakeholders, regulators, rating agencies, etc. In 2019, he participated in the U.S. State Department's International Visitor Leadership Program, which enabled him to strengthen his network in the area of international financial markets (governance).

The unprecedented situation in Ukraine and Russia has led RBI to consider its position in Russia. The bank, which has been present in Russia for 26 years and has significant crisis management experience, is assessing all strategic options for its future in Russia, up to and including a carefully managed exit from Russia.

## STATISTICS

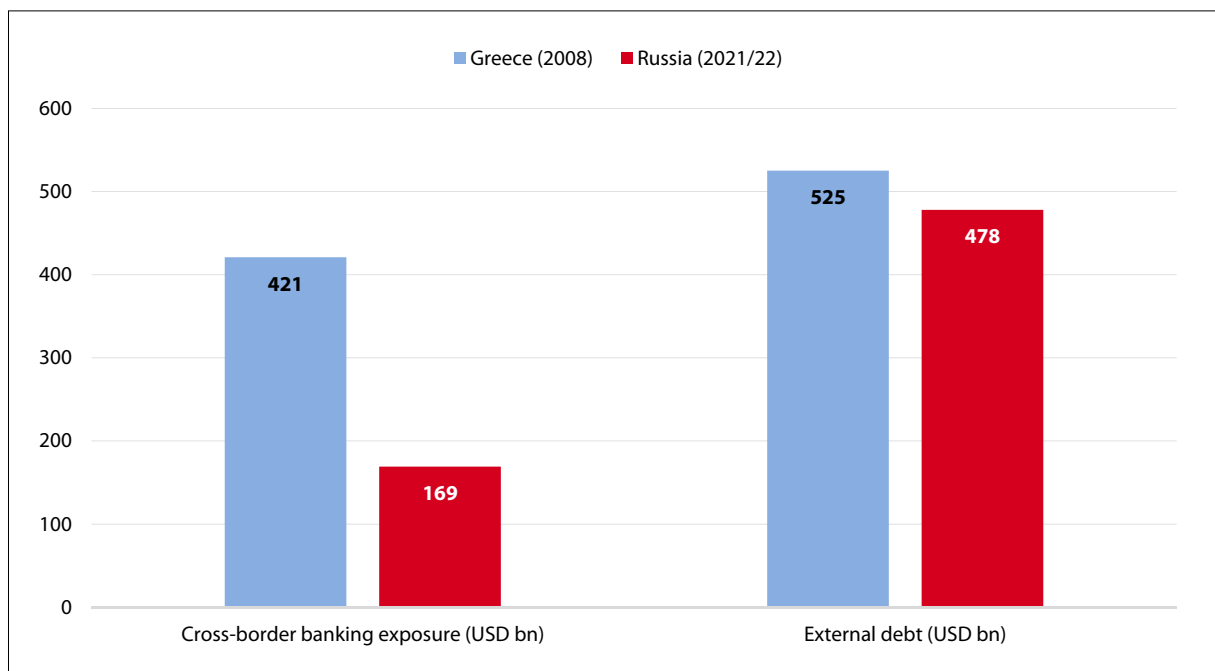
## Russian Financial and Economic Indicators

Figure 1: GDP Russia in Foreign Currency (USD bn)



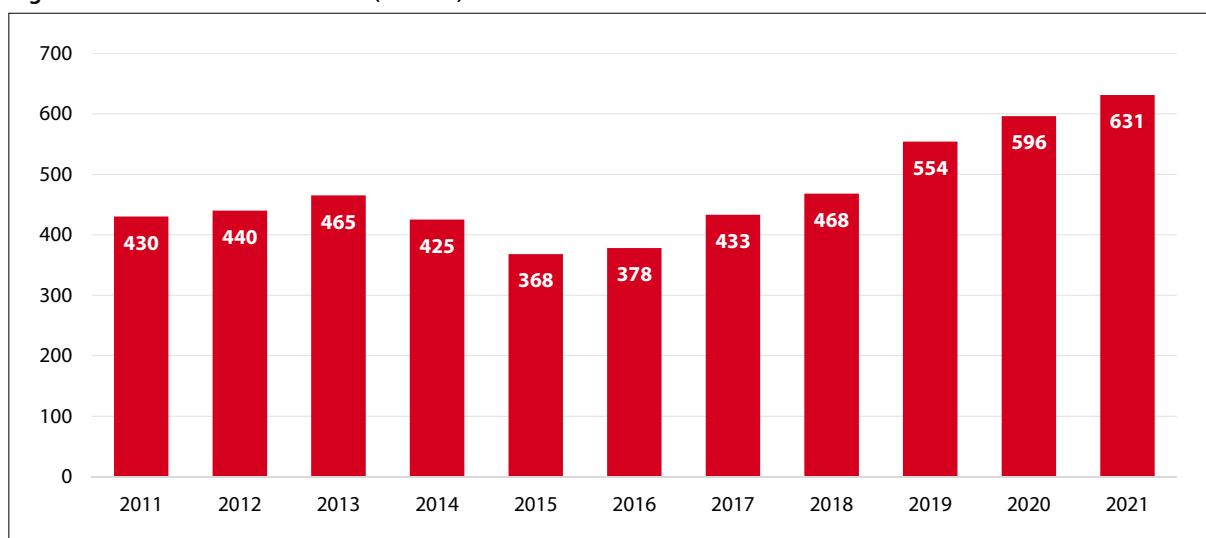
Source: World Bank, IMF, RBI/Raiffeisen Research

Figure 2: International Banking Exposure and External Debt: Russia vs Greece

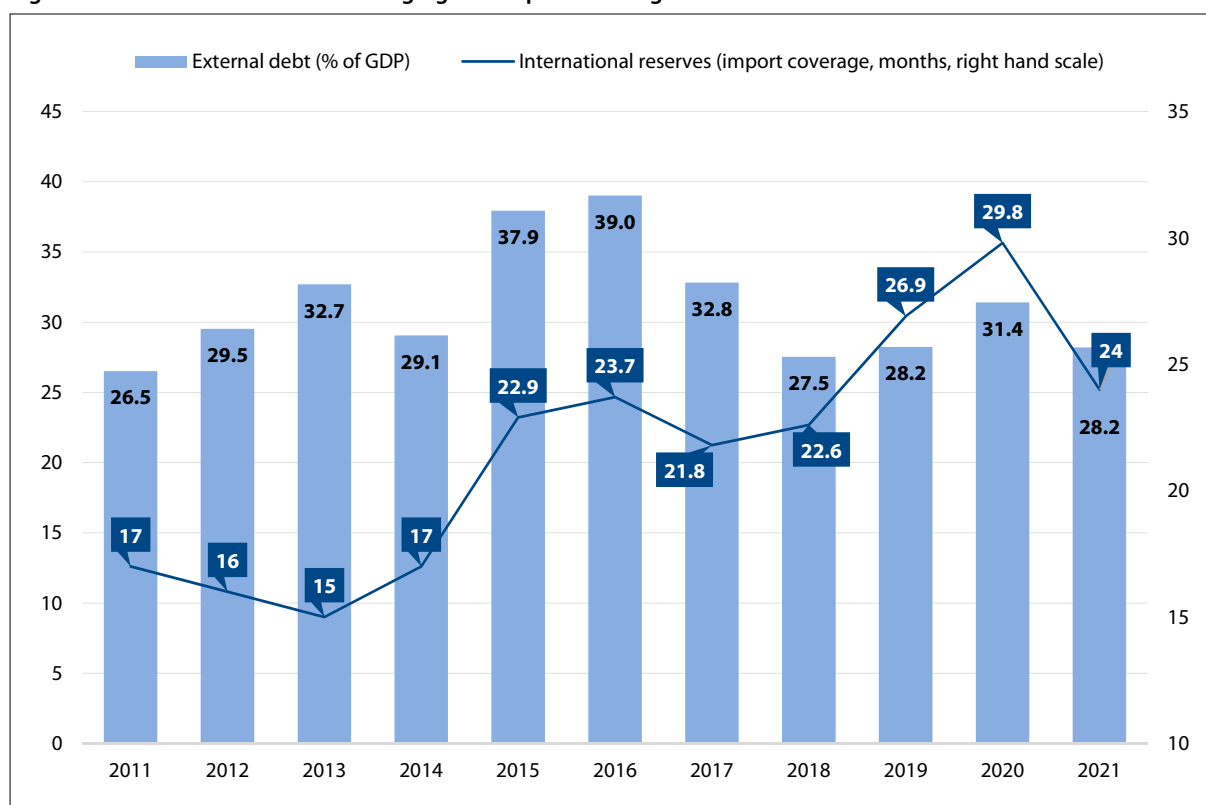


Source: BIS, World Bank, RBI/Raiffeisen Research

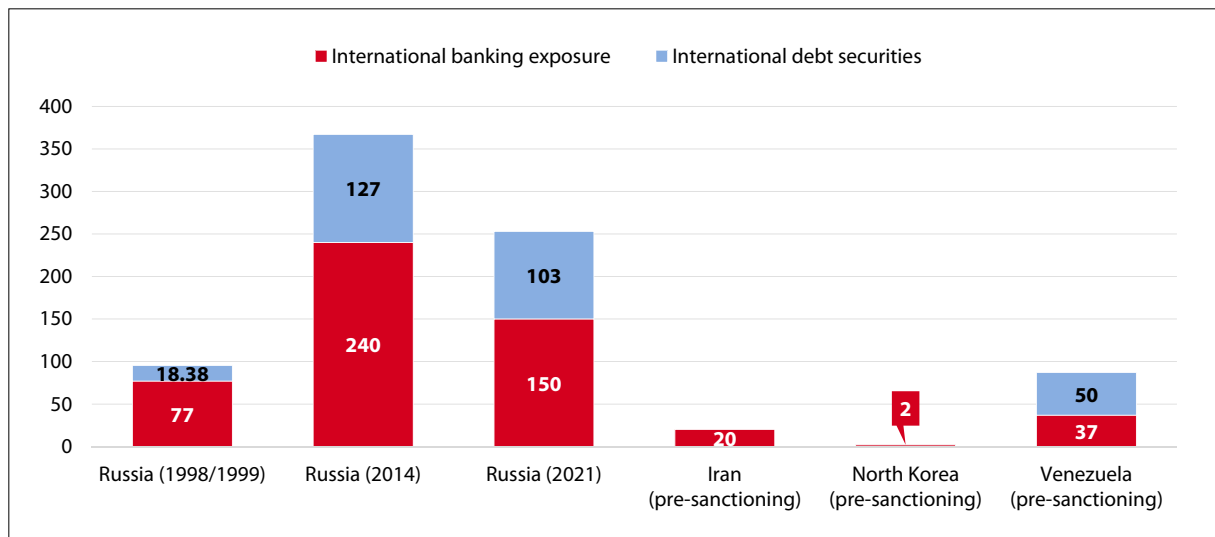


**Figure 3: Russia: Reserve Assets (USD bn)**

Source: CBR, Rosstat, RBI/Raiffeisen Research

**Figure 4: Russia: External Debt and Import Coverage Ratio**

Source: CBR, Rosstat, RBI/Raiffeisen Research

**Figure 5: International Financial Linkages to Sanctioned Countries (USD bn)**

\* Consolidated banking statistics (Claims plus other potential exposures) & International debt securities statistics (resident issuers); for Iran and North Korea no int. debt securities data available/no int. debt outstanding

Source: BIS, RBI/Raiffeisen Research

## ANALYSIS

### Is Russia Becoming a Second North Korea?

By Michael Rochlitz (University of Bremen)

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On 24 February 2022, Russian president Vladimir Putin ordered a full-scale military invasion of Ukraine. The decision was based on a series of fatally flawed situational assessments, including an overestimation of the fighting abilities of the Russian army, an underestimation of the determination of the Ukrainian army and people, and a faulty evaluation of the West's willingness to impose serious economic sanctions.

The massive sanctions that have since been imposed on Russia's economy have led to a freeze on half of the central bank's reserves, a fall of more than 40 percent in the value of the ruble, and an exodus of most Western companies from Russia. Increasing political repression and a fear of border closures have caused several hundred thousand Russians—a significant part of the country's intellectual elite—to flee abroad.

The economic consequences of these developments will be disastrous. At the moment, neither the Russian government nor most Russian people seem to realize the extent of the economic catastrophe that is sure

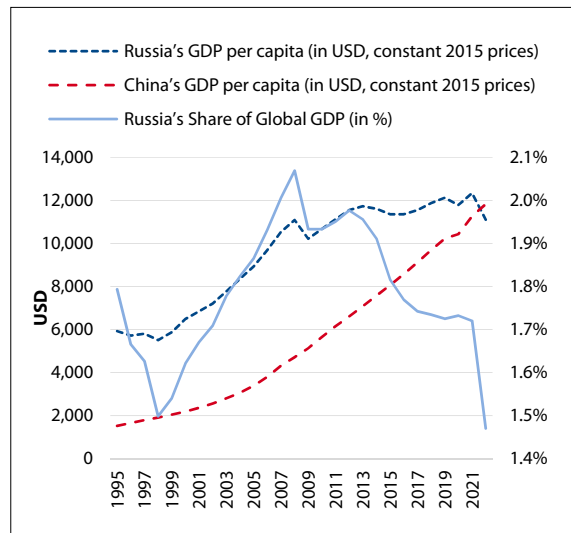
to happen. In the best-case scenario, Russia's economy will shrink by 10 to 20 percent this year, a somewhat worse decline than during the 2008 financial crisis. As a consequence, Russia's relative economic importance in the world—as measured by its share of global GDP—will reach its lowest point in recent history, and Russia's GDP per capita will be overtaken for the first time in several centuries by the GDP per capita of China (see Figure 1). But if the war continues, and new war crimes lead to additional sanctions, the economic disaster might be even worse than that occasioned by the collapse of the Soviet Union in the early 1990s, causing the country to be left even further behind.

#### Hitting an Already Weak Economy

The economic fallout of the war will hit an already stagnating economy. Russia's GDP per capita in early 2022 was only slightly higher than before the onset of the financial crisis in 2008. Since 2009, Russia's economy has grown at an average rate of less than 1 per-

cent per year, a growth rate far too low for a country of Russia's economic potential.

**Figure 1: Russia's Economic Development Compared**



Data for 1995 – 2020: World Bank; from 2021: projections, based on GDP growth of 4.7% in 2021 and –10% in 2022 in Russia (see also Table 1 on p. 13).

Russia has a well-educated population, still relatively low salaries, an excellent strategic position between China and Europe—soon to be the world's two largest economies—and abundant natural resources. Yet since Putin came to power 22 years ago, and in particular since his return to the presidency in 2012, the Russian government has lacked a strategy to diversify its economy and make it independent from oil and gas (Yakovlev 2021). While other authoritarian oil-producing countries, such as the United Arab Emirates and Saudi Arabia, have long been preparing for a future without natural resources by investing in science, technology or tourism, Russia has instead focused on an increasingly aggressive foreign policy agenda.

The negative economic consequences of this confrontational agenda have been amplified by increasingly neo-feudalist institutions, with an array of different security services harassing entrepreneurs and investors in the country. Putin's control over domestic politics is more and more based on a quid pro quo between him and the security services, with the latter suppressing protests and guaranteeing Putin's hold on power in exchange for the ability to expropriate successful businesses and plunder the country's economy (Rochlitz 2014, Kazun 2020).

Yet despite all these difficulties, Russia in early 2022 was still a middle-income country well integrated into the global economy. A large part of its population was better off than ever before and able to enjoy a living standard comparable to that of some European states. Russians could choose from a similar range of consumer

goods as people elsewhere in the world, occasionally travel abroad for a holiday, and expect to lead a relatively stable and peaceful life.

### A Self-Inflicted Catastrophe

Within less than a month, and as a result of the delusional ideas of a single person, all this has changed. Today, Russia has become an almost completely isolated pariah state. Belarus, Eritrea, North Korea, and Syria were the only countries that voted against a UN resolution condemning the Russian war in Ukraine. According to a list compiled by researchers at Yale University, by 20 March over 400 foreign companies had ceased or curtailed their operations in Russia, with only 37 overseas firms continuing to operate normally. As both Airbus and Boeing are no longer servicing Russian planes, Russia's airlines have been forced to stop international flights and might soon be compelled to stop domestic flights as well. Travel within the country will be pushed back to where it was in the early twentieth century.

It is unlikely that any of these companies will return to Russia if the current situation continues or deteriorates. As a consequence, the country will be deprived of many of the high-technology and consumer goods it has been importing. As Russia produces very few hi-tech goods, this will seriously affect the Russian economy, disrupting supply chains and making the country's situation similar to that of Iran during the last 30 years.

A similarly heavy blow will be the brain drain caused by the recent wave of repression. Most of the hundreds of thousands of people who have fled Russia in recent weeks are highly qualified specialists and researchers who are difficult to replace. The remaining scientists in Russia will be cut off from international networks, as academic institutions around the world have cut all ties with Russian universities. The consequences for science, research, and innovation in Russia will be devastating.

An additional tragedy is that, because of the government's control over the media and its ensuing monopoly over information, most Russians are not yet aware of what is happening to them. Yet as the economist Maxim Mironov has outlined in a recent post (Mironov 2022), both white- and blue-collar workers in Russia will suffer substantially as a result of current developments. The exodus of international financial, consulting, and accounting firms will force tens of thousands of accountants to seek employment in other, less well-paid professions. However, because of the overall contraction of the economy and their narrow specialization, they will encounter major difficulties in finding alternative employment. Entrepreneurs who had built their business models on digital platforms such as Instagram or Facebook, which have recently been banned by the Russian government, will be similarly affected.

Blue-collar workers will also be hit hard. Both Russia's automobile and aviation industries rely on foreign supplies and have already been forced to shut down production. It is only a question of time until they will be forced to lay off workers on a large scale. Several hundred thousand employees in the restaurant business will also be threatened by unemployment, both because many foreign chains have left the country and because remaining restaurants will be hit hard by the crisis, as a much smaller percentage of Russians will be able to afford to eat out. By comparison, state employees—the so-called *biudzhethniki*—will suffer relatively less. Their incomes might decrease in relative terms as a consequence of the fall of the ruble, but they will most likely keep their jobs. The only group that are likely to profit from the current crisis will be people working in the security services and for state media corporations, as they are necessary for the survival of the regime. To ensure their loyalty to the state, their salaries will likely be indexed to the dollar, and might even increase in relative terms.

### Dysfunctional Institutions

Few, if any, politicians in recent history have inflicted such massive harm on their own country in such a short period of time as Putin has done during the last month. How could one person cause such a disaster? The answer lies—most probably—in the increasing concentration of power around Putin and the deterioration of Russia's political institutions.

Since 2012, a number of influential heavyweights within Russia's security services have been purged and replaced by less influential technocrats, who are arguably much less able to keep their leader from making dangerous decisions (Petrov and Rochlitz 2019). This problem has also affected other branches of the Russian government, with more and more positions being occupied by loyal but not necessarily competent officials, a problem faced by many authoritarian regimes (Egorov and Sonin 2011). As the threat of being arrested now looms over most Russian government officials (see, e.g., Buckley et al. 2021 on the arrests of Russian mayors), they are unlikely to take responsibility and pass unfa-

vorable news on to higher levels of the government and to the head of state.

As almost all opposition media have been shut down, this contributes to an informational dilemma where key decision-makers in the country no longer have any reliable information upon which to act. As a result, they might find themselves in a parallel reality without much connection to what is actually happening in their country and the world. Although we do not know for sure, this could be a reasonable explanation for why the decision to invade Ukraine was made by Putin, as well as for the dismal performance of the Russian armed forces since then and the deterioration of Russian governance institutions more generally.

### Dark Prospects for the Future

How are things going to evolve from here? Even in the best possible scenario of immediate peace, it would take several years to repair the damage already caused. Such a scenario would probably require the fall of the Putin regime, and a new government that ends the war and takes responsibility for Russia's actions, to open up the possibility of returning the country to the international community. Even in this highly unlikely scenario, however, Russia's population will have suffered substantial economic harm, and the horrors already committed in Ukraine will leave deep scars for Ukrainians and Russians alike.

In what is unfortunately a more likely scenario, the war will drag on for a considerable time, potentially leading to a complete end of Western oil and gas imports from Russia. Although China might be willing to jump in, Russia will not be able to significantly increase its oil and gas exports in the near future, as the existing infrastructure in the Far East is already operating at full capacity. Moscow will thus have to rely on Chinese loans to import Chinese consumer goods. As a result, Russia might turn into a large-scale version of North Korea: economically dependent on China and with a government that through tight control of travel and information will try to prevent its population from finding out the true reasons for the disaster that has befallen it.

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Table 1: Russia's Economic Development Compared

	1995	1996	1997	1998	1999	2000	2001	2002
Russia's Share of Global GDP (in %)	1.8	1.7	1.6	1.5	1.5	1.6	1.7	1.7
Russia's GDP per capita (in USD, constant 2015 prices)	5,928.96	5,714.63	5,804.21	5,505.70	5,876.20	6,491.07	6,851.11	7,206.19
China's GDP per capita (in USD, constant 2015 prices)	1,520.03	1,653.43	1,787.76	1,909.62	2,038.20	2,193.89	2,359.57	2,557.89

	2003	2004	2005	2006	2007	2008	2009	2010
Russia's Share of Global GDP (in %)	1.8	1.8	1.9	1.9	2.0	2.1	1.9	1.9
Russia's GDP per capita (in USD, constant 2015 prices)	7,767.41	8,360.25	8,929.30	9,693.20	10,535.13	11,087.82	10,219.89	10,675.00
China's GDP per capita (in USD, constant 2015 prices)	2,797.17	3,061.83	3,390.71	3,800.76	4,319.02	4,711.64	5,128.90	5,647.06

	2011	2012	2013	2014	2015	2016	2017	2018
Russia's Share of Global GDP (in %)	2.0	2.0	2.0	1.9	1.8	1.8	1.7	1.7
Russia's GDP per capita (in USD, constant 2015 prices)	11,125.34	11,553.58	11,731.38	11,608.76	11,355.24	11,356.40	11,550.53	11,875.73
China's GDP per capita (in USD, constant 2015 prices)	6,156.83	6,608.71	7,086.87	7,574.68	8,066.94	8,572.88	9,117.34	9,688.47

	2019	2020	2021	2022
Russia's Share of Global GDP (in %)	1.7	1.7	1.7	1.5
Russia's GDP per capita (in USD, constant 2015 prices)	12,122.61	11,786.62	12,340.00	11,106.00
China's GDP per capita (in USD, constant 2015 prices)	10,228.29	10,430.73	11,264.00	11,827.00


Data for 1995 – 2020: World Bank; from 2021: projections, based on a GDP growth of 4.7% in 2021 and –10% in 2022 in Russia.



## DOCUMENTATION
















## How the 50 Biggest Foreign Companies in Russia Are Reacting to International Sanctions

Table 1: How the 50 Biggest Foreign Companies in Russia Are Reacting to International Sanctions (as of 15 March 2022)

Company name (country)	Business sector	Earnings 2020 (Euro)	Plan for business in Russia (date of announcement)	Source
Philip Morris International (USA)	Tobacco	4.33 bn.	Partial closure / withdrawal (09 March 2022) 	<a href="https://www.pmi.com/media-center/press-releases/press-details/?newsId=24966">https://www.pmi.com/media-center/press-releases/press-details/?newsId=24966</a>
Leroy Merlin (France)	Trade	4.18 bn.	Continuation (02 March 2022) 	<a href="https://tass.com/economy/1415495">https://tass.com/economy/1415495</a>
Volkswagen Group (Germany)	Car industry	3.85 bn.	Closure / withdrawal (03 March 2022) 	<a href="https://www.volkswagenag.com/en/news/2022/03/volkswagen-stops-production-of-vehicles-in-russia-and-suspends-e.html">https://www.volkswagenag.com/en/news/2022/03/volkswagen-stops-production-of-vehicles-in-russia-and-suspends-e.html</a>
Japan Tobacco International (Switzerland)	Tobacco	3.76 bn.	Continuation (10 March 2022) 	<a href="https://www.jti.com/jti-suspends-investments-russia-and-continues-prioritize-safety-its-employees-and-their-families">https://www.jti.com/jti-suspends-investments-russia-and-continues-prioritize-safety-its-employees-and-their-families</a>
Groupe Renault (France)	Car industry	3.73 bn.	Partial closure / withdrawal (25.02.2022) 	<a href="https://tass.ru/ekonomika/13860687">https://tass.ru/ekonomika/13860687</a>
Groupe Auchan (France)	Trade	3.30 bn.	Continuation (10 March 2022) 	<a href="https://www.kommersant.ru/doc/5251119">https://www.kommersant.ru/doc/5251119</a>
Apple (USA)	Consumer electronics	3.21 bn.	Closure / withdrawal (01 March 2022) 	<a href="https://eu.usatoday.com/story/tech/2022/03/01/apple-russia-sanctions-ukraine/6983755001/">https://eu.usatoday.com/story/tech/2022/03/01/apple-russia-sanctions-ukraine/6983755001/</a>
Toyota Motor (Japan)	Car industry	3.18 bn.	Closure / withdrawal (03 March 2022) 	<a href="https://global.toyota/en/newsroom/corporate/36979255.html">https://global.toyota/en/newsroom/corporate/36979255.html</a>
Samsung Electronics (South Korea)	Consumer electronics	2.96 bn.	Partial closure / withdrawal (05 March 2022) 	<a href="http://www.koreaherald.com/view.php?ud=20220306000101">http://www.koreaherald.com/view.php?ud=20220306000101</a>
IKEA (Netherlands)	Trade	2.96 bn.	Closure / withdrawal (03 March 2022) 	<a href="https://about.ikea.com/en/newsroom/2022/03/03/ikea-pauses-operations-in-russia-and-belarus">https://about.ikea.com/en/newsroom/2022/03/03/ikea-pauses-operations-in-russia-and-belarus</a>
Metro Group (Germany)	Trade	2.78 bn.	Continuation (11 March 2022) 	<a href="https://newsroom.metroag.de/news/2022/03/11/statement-zum-krieg-in-der-ukraine">https://newsroom.metroag.de/news/2022/03/11/statement-zum-krieg-in-der-ukraine</a>
KIA Motors (South Korea)	Car industry	2.67 bn.	No statement found	
PepsiCo (USA)	Food	2.62 bn.	Partial closure / withdrawal (08 March 2022) 	<a href="https://www.pepsico.com/news/press-release/pepsico-suspends-production-and-sale-of-pepsi-cola-and-other-global-beverage-brands-in-russia">https://www.pepsico.com/news/press-release/pepsico-suspends-production-and-sale-of-pepsi-cola-and-other-global-beverage-brands-in-russia</a>
British American Tobacco (UK)	Tobacco	2.37 bn.	Partial closure / withdrawal (09 March 2022); withdrawal and sale (11 March 2022)  	<a href="https://www.bat.com/group/sites/UK__9D9KCY.nsf/vwPagesWebLive/DOCCGBH">https://www.bat.com/group/sites/UK__9D9KCY.nsf/vwPagesWebLive/DOCCGBH</a> ; <a href="https://www.bat.com/group/sites/UK__9D9KCY.nsf/vwPagesWebLive/DOCCEKV9">https://www.bat.com/group/sites/UK__9D9KCY.nsf/vwPagesWebLive/DOCCEKV9</a>
Daimler (Germany)	Car industry	2.31 bn.	Closure / withdrawal (03 March 2022) 	<a href="https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-03/card/mercedes-benz-to-halt-exports-to-russia-XTjNaEX7POOKUUNE7Q8d">https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-03/card/mercedes-benz-to-halt-exports-to-russia-XTjNaEX7POOKUUNE7Q8d</a>
Nestlé (Switzerland)	Food	2.25 bn.	Continuation (09 March 2022) 	<a href="https://www.nestle.com/ask-nestle/our-company/answers/update-russia-ukraine">https://www.nestle.com/ask-nestle/our-company/answers/update-russia-ukraine</a>
BMW Group (Germany)	Car industry	2.17 bn.	Closure / withdrawal (01 March 2022) 	<a href="https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-01/card/bmw-halts-production-in-russia-and-stops-exports-to-the-country-T36AO5SxgtXwEfXJBsZ8">https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-01/card/bmw-halts-production-in-russia-and-stops-exports-to-the-country-T36AO5SxgtXwEfXJBsZ8</a>















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**Table 1: How the 50 Biggest Foreign Companies in Russia Are Reacting to International Sanctions (as of 15 March 2022) (continued)**

Company name (country)	Business sector	Earnings 2020 (Euro)	Plan for business in Russia (date of announcement)		Source
Hyundai Motor (South Korea)	Car industry	2.12 bn.	Partial closure / withdrawal (08 March 2022)		<a href="http://www.koreaherald.com/view.php?ud=20220308000924">http://www.koreaherald.com/view.php?ud=20220308000924</a>
Mars (USA)	Food	1.73 bn.	Continuation (01 March 2022); partial closure / withdrawal (10 March 2022)	 	<a href="https://www.mars.com/news-and-stories/press-releases-statements/mars-ceo-outlines-support-for-ukraine-and-calls-for">https://www.mars.com/news-and-stories/press-releases-statements/mars-ceo-outlines-support-for-ukraine-and-calls-for</a> ; <a href="https://www.mars.com/news-and-stories/press-releases-statements/mars-update-russia-and-ukraine">https://www.mars.com/news-and-stories/press-releases-statements/mars-update-russia-and-ukraine</a>
Huawei Technologies (China)	Consumer electronics	1.54 bn.	No statement found		
Danone (France)	Food	1.33 bn.	Continuation (06 March 2022)		<a href="https://www.danone.com/content/dam/danone-corp/danone-com/homepage/Danone-statement-Ukraine-PDF-EN.pdf">https://www.danone.com/content/dam/danone-corp/danone-com/homepage/Danone-statement-Ukraine-PDF-EN.pdf</a>
Cargill (USA)	Trade	1.32 bn.	Continuation (11 March 2022)		<a href="https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-11/card/cargill-to-maintain-some-russia-business-halts-further-investments-TRcELUg4MJ-PULRGmyVp">https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-03-11/card/cargill-to-maintain-some-russia-business-halts-further-investments-TRcELUg4MJ-PULRGmyVp</a>
Procter&Gamble (USA)	Consumer goods	1.31 bn.	Partial closure / withdrawal (08 March 2022)		<a href="https://us.pg.com/blogs/pg-european-operations-update/">https://us.pg.com/blogs/pg-european-operations-update/</a>
Globus Group (Germany)	Trade	1.28 bn.	Continuation (09 March 2022)		<a href="https://www.handelsblatt.com/unternehmen/handel-konsumgueter/matthias-bruch-globus-chef-will-die-maerkte-in-russland-gegen-alle-widerstaende-offen-halten/28142512.html">https://www.handelsblatt.com/unternehmen/handel-konsumgueter/matthias-bruch-globus-chef-will-die-maerkte-in-russland-gegen-alle-widerstaende-offen-halten/28142512.html</a>
Royal Dutch Shell (UK)	Oil and gas	1.23 bn.	Continuation (short term), withdrawal and sale (long term) (08 March 2022)		<a href="https://www.shell.com/media/news-and-media-releases/2022/shell-announces-intent-to-withdraw-from-russian-oil-and-gas.html">https://www.shell.com/media/news-and-media-releases/2022/shell-announces-intent-to-withdraw-from-russian-oil-and-gas.html</a>
McDonald's (USA)	Food	1.21 bn.	Closure / withdrawal (08 March 2022)		<a href="https://corporate.mcdonalds.com/corpmcd/en-us/our-stories/article/ourstories.Russia-update.html">https://corporate.mcdonalds.com/corpmcd/en-us/our-stories/article/ourstories.Russia-update.html</a>
Nissan (Japan)	Car industry	1.19 bn.	Partial closure / withdrawal (07 March 2022)		<a href="https://global.nissannews.com/en/releases/release-4454c7eb99daae98b9a1ec98f118161d-220307-00-e">https://global.nissannews.com/en/releases/release-4454c7eb99daae98b9a1ec98f118161d-220307-00-e</a>
LG Electronics (South Korea)	Consumer electronics	1.15 bn.	No statement found		
Robert Bosch (Germany)	Engineering + technology	1.05 bn.	Partial closure / withdrawal (09 March 2022)		<a href="https://europe.autonews.com/suppliers/bosch-closes-ukraine-site-continuously-assesses-volatile-situation">https://europe.autonews.com/suppliers/bosch-closes-ukraine-site-continuously-assesses-volatile-situation</a>
Google (USA)	Internet + technology	1.03 bn.	Continuation		<a href="https://www.bbc.com/news/technology-60579641">https://www.bbc.com/news/technology-60579641</a>
Henkel Group (Germany)	Chemical industry	1.01 bn.	Continuation (04 March 2022)		<a href="https://www.henkel.de/presse-und-medien/presseinformationen-und-pressemappen/2022-03-04-henkel-stoppt-investitionen-in-russland-1626158">https://www.henkel.de/presse-und-medien/presseinformationen-und-pressemappen/2022-03-04-henkel-stoppt-investitionen-in-russland-1626158</a>
Inditex (Spain)	Trade	0.99 bn.	Closure / withdrawal (05 March 2022)		<a href="https://www.theguardian.com/world/2022/mar/05/zara-owner-inditex-ceases-trading-in-russia-temporarily-ukraine-sanctions">https://www.theguardian.com/world/2022/mar/05/zara-owner-inditex-ceases-trading-in-russia-temporarily-ukraine-sanctions</a>
Unilever (UK)	Consumer goods	0.98 bn.	Partial closure / withdrawal (08 March 2022)		<a href="https://www.unilever.com/news/news-search/2022/updated-unilever-statement-on-the-war-in-ukraine/">https://www.unilever.com/news/news-search/2022/updated-unilever-statement-on-the-war-in-ukraine/</a>

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**Table 1: How the 50 Biggest Foreign Companies in Russia Are Reacting to International Sanctions (as of 15 March 2022) (continued)**

Company name (country)	Business sector	Earnings 2020 (Euro)	Plan for business in Russia (date of announcement)	Source
Uniper (Germany)	Energy	0.97 bn.	Continuation (short term), withdrawal and sale (long term) (07 March 2022) 	<a href="https://www.uniper.energy/news/de/update-zu-unipers-russlandaktivitaeten-und-weiteren-schritten">https://www.uniper.energy/news/de/update-zu-unipers-russlandaktivitaeten-und-weiteren-schritten</a>
Bayer (Germany)	Pharmaceuticals	0.92 bn.	Continuation (14 March 2022) 	<a href="https://www.bayer.com/de/ukraine">https://www.bayer.com/de/ukraine</a>
Carlsberg Group (Denmark)	Food	0.91 bn.	Partial closure / withdrawal (09 March 2022) 	<a href="https://www.carlsberggroup.com/newsroom/update-on-ukraine-and-russia-suspension-of-2022-guidance/">https://www.carlsberggroup.com/newsroom/update-on-ukraine-and-russia-suspension-of-2022-guidance/</a>
Mitsubishi Motors (Japan)	Car industry	0.91 bn.	Continuation (01 March 2022) 	<a href="https://www.reuters.com/business/autos-transportation/mitsubishi-motors-may-suspend-car-sales-russia-due-sanctions-jiji-2022-03-01/">https://www.reuters.com/business/autos-transportation/mitsubishi-motors-may-suspend-car-sales-russia-due-sanctions-jiji-2022-03-01/</a>
Fortum (Finland)	Energy	0.90 bn.	Continuation (03 March 2022) 	<a href="https://www.fortum.com/media/2022/03/fortum-ceo-markus-rauramos-statement-groups-russian-businesses">https://www.fortum.com/media/2022/03/fortum-ceo-markus-rauramos-statement-groups-russian-businesses</a>
Coca-Cola Hellenic Bottling (Switzerland)	Food	0.88 bn.	No statement found (09 March 2022)	<a href="https://www.coca-colahellenic.com/en/media/news/corporate_news/2022/ukraine-and-russia-update">https://www.coca-colahellenic.com/en/media/news/corporate_news/2022/ukraine-and-russia-update</a>
ELKO Grupa (Latvia)	Trade	0.87 bn.	Closure / withdrawal (10 March 2022) 	<a href="https://www.elkogroup.com/news/elko-group-is-considering-exiting-the-russian-market">https://www.elkogroup.com/news/elko-group-is-considering-exiting-the-russian-market</a>
Imperial Tobacco Group (UK)	Tobacco	0.85 bn.	Closure / withdrawal (09 March 2022) 	<a href="https://www.imperialbrandsplc.com/media/key-announcements/2022/update-on-russia---ukraine.html">https://www.imperialbrandsplc.com/media/key-announcements/2022/update-on-russia---ukraine.html</a>
Volvo (Sweden)	Car industry	0.79 bn.	Closure / withdrawal (28 February 2022) 	<a href="https://www.nytimes.com/2022/02/28/business/volvo-russia-ukraine.html">https://www.nytimes.com/2022/02/28/business/volvo-russia-ukraine.html</a>
Johnson & Johnson (USA)	Pharmaceuticals, consumer good	0.78 bn.	Continuation (04 March 2022) 	<a href="https://www.jnj.com/johnson-johnson-statement-on-conflict-in-ukraine">https://www.jnj.com/johnson-johnson-statement-on-conflict-in-ukraine</a>
Mondi Group (UK)	Paper + cartonnage	0.74 bn.	Continuation (10 March 2022) 	<a href="https://www.mondigroup.com/en/newsroom/market-update/2022/update-on-russian-business-activities/">https://www.mondigroup.com/en/newsroom/market-update/2022/update-on-russian-business-activities/</a>
KOMATSU (Japan)	Machine building	0.73 bn.	Closure / withdrawal (07 March 2022) 	<a href="https://www.komatsu.eu/de/news/komatsu-shipments-to-russia">https://www.komatsu.eu/de/news/komatsu-shipments-to-russia</a>
Novartis (Switzerland)	Pharmaceuticals	0.72 bn.	Continuation (04 March 2022) 	<a href="https://www.novartis.com/news/novartis-condemns-war-ukraine-and-commits-supporting-humanitarian-efforts">https://www.novartis.com/news/novartis-condemns-war-ukraine-and-commits-supporting-humanitarian-efforts</a>
Mondelez International (USA)	Food	0.72 bn.	Continuation (09 March 2022) 	<a href="https://www.mondelezinternational.com/News/Statement-on-War-in-Ukraine">https://www.mondelezinternational.com/News/Statement-on-War-in-Ukraine</a>
Sanofi (France)	Pharmaceuticals	0.70 bn.	Continuation (14 March 2022) 	<a href="https://www.sanofi.com/en/media-room/our-response-to-the-situation-in-ukraine?utm_campaign=corp_2022_responseukraine&amp;utm_medium=social_corp&amp;utm_source=twitter">https://www.sanofi.com/en/media-room/our-response-to-the-situation-in-ukraine?utm_campaign=corp_2022_responseukraine&amp;utm_medium=social_corp&amp;utm_source=twitter</a>
Enel (Italy)	Energy	0.69 bn.	No statement found	
Schneider Electric (France)	Consumer electronics	0.65 bn.	No statement found	

Note: The table covers all companies included in the list of Russia's 50 biggest foreign companies compiled by Forbes Russia as of 04 October 2021, available online at <https://www.forbes.ru/biznes/441733-50-krupnejsih-inostrannyh-kompanij-v-rossii-2021-rejting-forbes>

Compiled by Olivia Faust (Research Centre for East European Studies at the University of Bremen)

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## ANALYSIS

## War in the Age of TikTok

By Jacqueline Evans (George Washington University)

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### Abstract

The rise of social media has revolutionized information-sharing and the way in which people learn about important events. As evidenced by the use of TikTok in the ongoing Russian invasion of Ukraine, social media has the ability to connect people from conflict zones to individuals around the world. Although dramatic video clips can be critical for our understanding of real-time developments and for pressuring policy-makers to act, they also open the door to misinformation that creates confusion and division.

### A Social Media Revolution

Approximately a decade ago, social media changed the world by connecting individuals from across the globe. Similar to the impact of television and live reporting in war zones during the Vietnam War, the social media revolution has dramatically changed how people obtain and process information from conflict zones in the twenty-first century.

Today, the popular social media platform TikTok is once again transforming how people interact with news by providing users with short video clips from the war in Ukraine. These videos portray in dramatic fashion the destruction of urban infrastructure, life in bomb shelters, and the successes and failures of both the Russian and Ukrainian armies, as well as the responses of millions of global users. The relatively user-friendly nature of TikTok makes it easy to create and share videos from the conflict in real time and reach an audience of nearly a billion people. The platform provides an online space where people can become more educated and advocate for change.

Yet for all the good that TikTok brings, bad actors have been using the platform to spread misinformation and construct a false narrative that creates division and sows confusion regarding the war. This phenomenon is not new to TikTok: the Russian state has frequently deployed such techniques to generate infighting and hinder a unified response. These techniques pose a particular danger because they create an environment where people like, share, and absorb information that may not necessarily be accurate.

With Russia's invasion of Ukraine, dubbed the first TikTok war, the platform is being used to spread infor-

mation and misinformation regarding the conflict. In connecting a younger generation with videos of the devastation, it may also be fostering a dangerous situation where misinformation flourishes and results in division amongst Ukrainians, Europeans, and Americans.

### TikTok's Reach and Influence

TikTok's rise to global prominence began in 2018 after the China-based company ByteDance purchased Musical.ly and rebranded under the name TikTok. The app allows users to create short videos and use various songs and voiceovers to lip-sync viral content. The platform's specific and personalized algorithm facilitates users watching clips similar to videos they have previously made or liked. TikTok's success can be measured by its nearly 1 billion active monthly users worldwide, including an estimated 50 million daily users in the United States.<sup>1</sup>

Approximately 70% of American teenagers use TikTok, with the majority of users being members of Generation Z, or individuals born between 1997 and 2012.<sup>2</sup> In fact, of the nearly 100 million monthly users in the United States, 37.3 million are between the ages of 10 and 25.<sup>3</sup> Studies have shown that almost a quarter of American adults get their news from TikTok, a figure that rises to almost half among Millennials and Generation Z adults.<sup>4</sup>

These statistics are critical because Generation Z and Millennials will soon be the largest political voting bloc. By 2028, an estimated 49% of American voters will be either Millennials or Generation Z, meaning that future voters will largely be accustomed to obtaining information from social media rather than traditional

1 Dean, B. (2022). How Many People Use TikTok? 80+ TikTok Statistics. Backlinko. Available at: <https://backlinko.com/tiktok-users>

2 Galaskas, T. (2021). How Gen Z is Turning TikTok into the next Google. Available at: <https://www.abc27.com/national/how-gen-z-is-turning-tik-tok-into-the-next-google/>

3 Insider Intelligence Editors. (2021). More Gen Zers now use TikTok than Instagram in the US. Available at: <https://www.emarketer.com/content/more-us-gen-zers-now-use-tiktok-than-instagram>

4 Mimo, D. & Farah, H. (2022). War as seen on TikTok: Ukraine clips get views whether true or not. The Guardian. Available at: <https://www.theguardian.com/technology/2022/mar/05/tiktok-ukraine-russia-invasion-clips-get-views-whether-true-or-not>

mainstream media.<sup>5</sup> In the context of the current crisis, although members of Generation Z only comprise about 10% of eligible voters, they still have a voice, and their opinions and views impact the kind of legislation that policymakers support.<sup>6</sup>

Taken together, these statistics regarding TikTok's reach and its users' influence show how important the social media platform is, demonstrating that it is critical to monitor how people are using the app and what news they receive. With this in mind, let us turn to examine how Ukrainians and Russians are using TikTok to spread their respective messages.

### How Ukrainians and Russians Use TikTok

Both Ukrainians and Russians are engaging in the creation and sharing of videos. Many of these videos have gone viral and have been liked by people outside the conflict.

Within Ukraine, users have been producing videos that let viewers around the world see the deprivation they are experiencing. Some show life in bomb shelters. Others highlight the damage and destruction of buildings or display destroyed military equipment, including tanks, missiles, and planes. Some clips are aimed at the domestic Ukrainian audience, such as informational videos to help citizens survive the onslaught.

In contrast, Russians have been posting TikToks that show support for Russian troops, as well as videos that spread propagandistic government claims that Ukraine is attacking its own civilians, faking deaths, and committing aggressive acts.

The differences between the two sides are significant and highlight the potential risk of the spread of misinformation. Information is being weaponized, with supporters of both Ukraine and Russia spreading misinformation to promote their causes.

#### *Ukraine*

Ukrainian videos show both the horror of the conflict and moments of hope. One of the most viral videos includes a post by the user Valerishh, who posts videos depicting a typical day in a Ukrainian bomb shelter. The video has over 40 million views, 5.7 million likes, and 29,000 comments. In this specific post, she shows the struggles that ordinary civilians face, as well as the destruction that has been inflicted on her city. This TikTok enables viewers to see the human face of war, as well as demonstrating the reach that a post can have.

Another video that has received a lot of attention is a clip posted by the user yutsyartis showing a Ukrain-

ian soldier launching a rocket-propelled grenade against a Russian target. The post has over 51 million views, 3.3 million likes, and 47,000 comments. In 8 seconds, this TikTok gives viewers a glimpse of the ongoing battle.

Lastly, a TikTok posted by CBS News shows the damage to physical infrastructure and human life that a Russian missile strike inflicted on a children's and maternity hospital. In the 28-second clip, viewers see injured civilians, including pregnant women; children in shock; and a blood-stained bed. The images horrified people around the world by showing the brutal devastation facing innocent civilians. The TikTok has nearly 9 million views, 900,000 likes, and 26,000 comments. Once again, viewers are witnessing the violence that everyone in Ukraine faces.

Together, these three TikToks show different angles from Ukraine: life in a bomb shelter, a battle scene, and injured civilians. By depicting various facets of the war in short yet powerful snippets, they allow TikTok users from around the globe to share in Ukrainians' experiences and learn about what is happening on the ground. The Ukrainian videos contrast strongly with those coming from Russia.

#### *Russia*

The Kremlin is using TikTok to promote its military activities in Ukraine. Its propaganda videos include posts claiming to show Ukrainians pretending to be dead or injured in an effort to blame Russia. Although many fact-checkers have shown these videos to be false or taken out of context, they remain viewable and shared on TikTok, meaning misinformation is actively being spread to millions of people.

One of the most viewed videos being used to spread misinformation includes a news segment of a reporter in front of rows of "body bags." During the piece, an individual in one of the body bags moves. Pro-Russian social media users claim this video is from Ukraine and proves that people are not actually dying but rather the Ukrainian government is faking deaths to make the West target Russia. The video has been debunked as misleading, as it is actually from a climate protest in Vienna, Austria. The Kremlin likely shared this video to make people question what is really happening in Ukraine and whether or not the media and/or politicians are telling the truth.

A similar video that has been used to claim that Ukrainians are only pretending to be under threat includes a clip of a large crowd being told by a director to run and scream. Russia claims this is recent footage and shows Ukrainian officials telling civilians to act like

5 Griffin R., Frey W., & Teixeira, R., 2019. America's electoral future. American Progress. Available at: <https://www.americanprogress.org/article/americas-electoral-future-3/>

6 See Griffin et. Al, 2019.



they are in danger. In reality, however, the recording is from a movie set in London in 2013; the clip has absolutely nothing to do with Ukraine. Nevertheless, this video has been viewed thousands of times on various TikTok pages that claim it is related to the war.

Finally, there are also videos from Russian influencers supporting the operation being promoted by Russia and questioning the authenticity of images of injured civilians. Although most of these posts have been flagged as propaganda, they nevertheless reflect an effort by Russia to spread misinformation regarding the invasion. In the first such TikTok under study, a user repeats the false claim that one of the women injured during the attack on the Mariupol maternity hospital is actually an actress pretending to be injured. This TikTok is completely false and has been debunked numerous times. Nevertheless, the video, posted by the user *furrygrisy*, has over 13,000 views.

The second such TikTok is a montage of clips of Russian influencers seemingly reading from a script while stating their support for military action. Although as of the writing of this article it cannot be confirmed if the influencers were paid or forced to make these statements, the video posted by *realraywilliams* shows that some TikTokers have flagged these clips to highlight the risks of misinformation.

In sum, although they post different content, users in both countries comprehend the TikTok's reach and the importance of using it.

### The Danger of Getting News from TikTok

As demonstrated in the previous section, there are both real and misleading videos on TikTok. Although some videos get debunked and removed, there are millions of posts on the platform and it would be impossible to catch every single fake video. As such, many users frequently come into contact with inaccurate content.

Additionally, TikTok's algorithm is designed in such a way that once a user likes a video, the user will see more videos with similar content. As a result, once someone likes a misleading post, it becomes more difficult for them to differentiate between real and fake information.

Two examples that highlight this phenomenon are a TikTok that claimed to show Russian nuclear weapons entering Ukraine and a video that depicts a battle scene. Both of these TikToks reached millions of people before they were flagged as misinformation.

The original video claiming to show Russian nukes entering Ukraine received 18 million views before TikTok removed the post for violating its guidelines. However, the video continues to be reposted, including by

the user *radewnnn* (linked above), meaning users are still coming into contact with misinformation intended to create panic.

The second clip claims to show footage of the "Ghost of Kyiv" shooting down two Russian planes in 30 seconds. However, the post is inaccurate: it was taken from a video game called *Digital Combat Simulator*. This clip has been spread numerous times in various videos on TikTok and other social media platforms. The misleading video has even been shared by the Ukrainian government. This TikTok demonstrates that it is critical to factcheck all content prior to sharing it, since such fake videos feed into the Russian misinformation campaign that claims the West and Ukraine are making propaganda pieces.

These two examples reveal the danger of getting news from TikTok, as it would be impossible to monitor videos and fact-check millions of posts. This is not to say that all videos on TikTok are misleading—but by sharing fake videos, the platform not only enables pro-Russian individuals to claim the war is Western propaganda, but also allows deniers around the world to declare all information coming from Ukraine to be misinformation.

### Conclusion

This article has demonstrated the ways in which Ukrainians and Russians are using TikTok during the ongoing war and the risk of getting one's news from the platform. What lessons can we draw from this? First, through this mode of information-sharing, a younger segment of society is engaging directly with videos and images from the war and is becoming more educated about the situation. Second, this growing awareness matters politically, as most Western viewers are current or soon-to-be voters, meaning they have the ability to push policymakers to respond and hold accountable those who do not act, thus directly impacting the responses of Western countries, whether with regard to the provision of military support or humanitarian aid. Finally, users must be cautious and continue to flag content that is misleading, as failing to do so will aid Russian misinformation campaigns and sow division.

While the outcome of the conflict remains difficult to predict, social media platforms such as TikTok have enabled people from all over the world to witness the immense devastation the war has wrought. As this war continues and other conflicts arise, it will be vital to monitor all social media platforms and understand how individuals are engaging with the content, as this will directly impact how political leaders react.

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## Russian Social Network VK Gains Carte Blanche Following the Closure of Instagram and Facebook in the Country

By Daria Zakharova (Research Centre for East European Studies at the University of Bremen)

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### Abstract

As the Russian invasion of Ukraine erupted, the country's authorities declared a war on Western social media as well. In March, such social media giants as Facebook, Twitter, and Instagram were blocked in Russia, giving their local competitor—named VK—a virtual monopoly in the country. Millions of Russian Facebook and Instagram users have flocked to this social network. Though VK may seem similar to Facebook, it is drastically different due to its proximity to the Russian government. The article examines the core peculiarities of VK and the risks its users may face, especially, in the context of war.

### Capture of VK by the Russian Government

VK is a popular Russian social network that has more than 100 million visitors per month. It was created in 2006 by Russian software developer Pavel Durov, who later gained fame as the architect of Telegram. In 2014 Durov was forced to leave Russia due to his refusal to disclose users' personal data at the request of Russian intelligence (the FSB). On March 7, 2022, Durov wrote on Telegram: "Nine years ago I was the CEO of VK, which was the largest social network in Russia and Ukraine. In 2013, the Russian security agency, the FSB, demanded that I provide them with the private data of the Ukrainian users of VK who were protesting against a pro-Russian president. I refused to comply with these demands, because it would have meant a betrayal of our Ukrainian users. After that, I was fired from the company I founded and was forced to leave Russia."

Following Durov's dismissal, VK became closely connected to the Russian government. In 2021 Vladimir Kirienko, an official linked to the Presidential Administration, was appointed CEO of VK. Simultaneously, Alisher Usmanov, who held the controlling stake in VK, sold it to Sogaz. The latter is owned by Yury Kovalchuk, a businessman closely allied with Vladimir Putin.

VK thus became a social network that—unlike Instagram, Facebook, and Twitter—easily and instantly cooperates with the government and is controlled by pro-Putin parties. What are its core peculiarities?

### War vs. "Special Military Operation"

If foreign social networks are guided by their policies and international law, VK relies on Russian law. And Russian law changes rapidly, especially in the context of war. On March 4, the Russian authorities hastily passed a law that imposes serious criminal penalties on media, public figures, and private individuals alike for spreading "fakes" about the Russian armed forces. The definition of fakes and the application of the law is still

quite vague, but it has become clear that publicly using such common terminology as "war" or "intervention" to describe Russia's actions in Ukraine amounts to a violation thereof. According to a letter from the Federal Service for Supervision of Communications, Information Technology, and Mass Media (Roskomnadzor) received by multiple media and public actors, only official Russian sources can be cited and only the term "special military operation" can be used to describe Russia's actions.

Facebook, Instagram, and Twitter faced the same demands from Russian regulatory bodies and were de facto instructed to censor all content that referred to a "war" in Ukraine instead of a "special military operation." Facebook not only refused to do so, but also banned Russian state media pages from advertising on the site. Following hundreds of thousands of Euro of fines issued by the Russian government, Facebook, Twitter, and Instagram were ultimately blocked in the country.

VK, unlike its Western counterparts, instantly implemented the demands of Roskomnadzor and rapidly deleted any content violating the new Russian law about fakes. It blocked the pages of a range of media—such as the BBC, Radio Free Europe, and Deutsche Welle—for not complying with the new law. The same procedure has been applied to many other pages and private VK users that post content at odds with the new law.

Moreover, VK has blocked a range of groups opposing war, the biggest of which is called "No War." The site reported on March 9 that by order of the public prosecutor's office, the group's page is no longer available to Russian users.

### Cooperation with Russian Law Enforcement

VK is notorious for disclosing users' personal data at the request of Russian law enforcement. As the founder of VK, Pavel Durov, stated, this was the main stumbling block that forced him to leave Russia in 2014. Since the

ousting of Durov and the installation of pro-Kremlin management, VK has disclosed hundreds of users' personal data to the government. Many of them are allies of Alexey Navalny.

Since the adoption of the law "on spreading fakes about the Russian armed forces," VK has been transferring the data of any users who post comments that are not in line with the current legislation (i.e., calling it a war, invasion or attack instead of a special military operation) to the law enforcement and intelligence bodies daily. Russian courts have already handed down hundreds of fines, ranging from 30,000 to 100,000 rubles (~250–800 Euro). People across Russia—in Siberia, in southern Russia, and in the North—have been accused of posting or reposting "fakes" about the war in Ukraine on VK.

At the same time, Facebook, despite its spotty reputation when it comes to the protection of users' personal data, refused to localize the data of its Russian users in Russia, as the authorities had demanded, fearing that doing so would make the data more vulnerable to the interested state bodies.

### Growing Militarization of VK

VK not only bans and deletes information about the Russian invasion of Ukraine in accordance with the new law "on spreading fakes about the Russian armed forces," but also promotes a strong pro-Russian military agenda.

In some Russian regions, public sector employees are reportedly being forced to post diverse content supporting the Russian invasion of Ukraine. Some teachers received instructions from the municipal administration to post a range of hashtags, such as #ЗаПутина (for Putin) and #Своихнебросаем (we don't abandon our people), on their VK pages. The instruction also included a link to materials that they were encouraged to post.

#### *About the Author*

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In an anonymous interview, a teacher from the Russian Far East said that she was ordered to support the Russian invasion of Ukraine on her VK page or risk dismissal. "They called on February 26 and said that it is necessary to post materials on social networks. They asked me to make my VK page visible. I know that the order came 'from above,' from the regional ministry of education. They sent me the pictures and a reporting form via WhatsApp," she explained. Similar anonymous statements were made by a range of state employees—doctors, teachers, and employees of state media outlets—as well as students.

At the same time, students and teachers at Russian universities are reported to have faced problems for attending anti-war meetings and posting anti-military content on their VK pages. Some insist that they were expelled from their universities as a consequence.

It follows that VK is also exploited by the Russian authorities as a platform for the promotion of pro-war content.

### Conclusion

The blocking of Western social networks in Russia and the virtual monopoly consequently gained by Facebook's Russian analogue, VK, represents a disturbing trend. Since 2014, VK has been closely allied with the Russian government and does not ensure the safety of users' data. Instead, it instantly cooperates with the Russian censorship (Roskomnadzor) and intelligence (FSB, MVD) bodies and blocks any content they find objectionable. In the context of war and the range of repressive laws passed by the Russian government against freedom of speech, it is especially crucial for local social network users that the only platform left available is VK.

## ABOUT THE RUSSIAN ANALYTICAL DIGEST

Editors: Stephen Aris, Matthias Neumann, Robert Orttung, Jeronim Perović, Heiko Pleines, Hans-Henning Schröder, Aglaya Snetkov

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