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The Economic Impact of Russia Sanctions

In response to Russia's 2022 war on Ukraine, a broad, multilateral coalition, including the United States, the European Union (EU), the United Kingdom, Canada, Australia, Japan, and others, imposed sweeping new sanctions on Russia. The sanctions—unprecedented in terms of scope, coordination, and speed—target the overseas wealth and economic activity of Russia's elites and decision makers. The sanctions also target Russia's financial and energy sectors and access to western technology, among other financial and trade tools. The sanctions have created challenges for Russia but to date, have not delivered the economic "knock out" that many predicted. New sanctions on Russian oil exports implemented in December 2022 may increase economic pressure on the government.

Although sanctions are a foreign policy tool deployed in several contexts, the coordinated sanctions on Russia are significant to the global economy due to the size of Russia's economy—before the war, the 11th largest in 2021—and Russia's integration in the global economy. In addition to its oil and natural gas exports, Russia has been a key global supplier of several metals (titanium, aluminum, and nickel), chemical gases used in semiconductor production, wheat, and fertilizers, among other commodities. Many U.S. and international firms had also established factories, joint ventures, and retail operations in Russia, and face losses as they exit the Russian market.

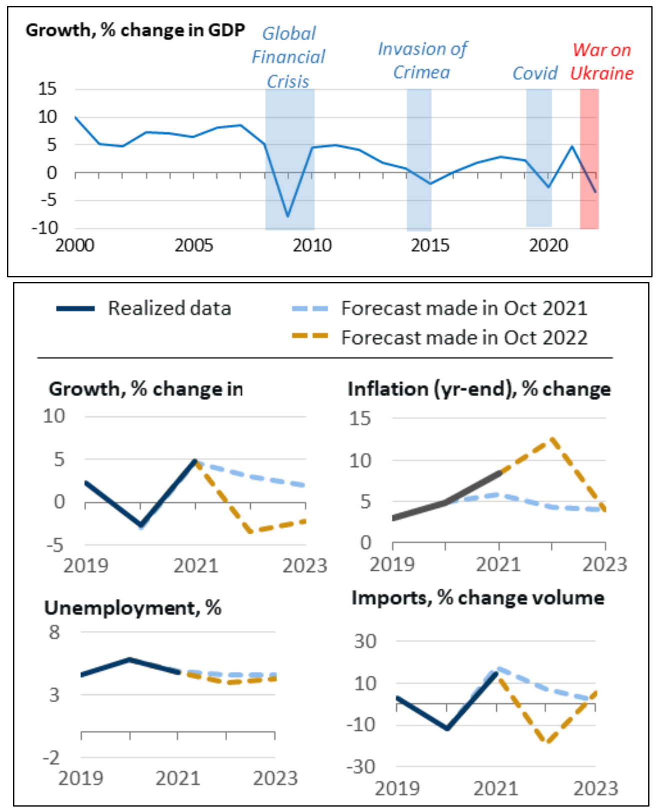
Impact on Russia's Economy

Early in the war, the broad consensus was that the new sanctions could devastate the Russian economy. Since the start of the war In February 2022, sanctions have created numerous economic challenges in Russia. For example:

- Russia's financial sector faces losses of hundreds of billions of dollars;
- the Russian military is having difficulties procuring key components for its war effort;
- many Russian factories have suspended production because they cannot access foreign-made parts;
- many affected companies are placing employees on part-time schedules or furlough;
- hundreds of U.S. and international companies have exited the Russian market; and
- Russian oil is selling below market prices.

By other metrics, however, the Russian economy has weathered the sanctions better than many expected. In October 2022, the International Monetary Fund (IMF) estimated that in 2022 Russia's economy would contract by 3%, less than half of its economic disruption during the global financial crisis of 2008-2010 (**Figure 1**). Additionally, IMF forecasts suggest that the 2022 uptick of inflation in Russia, and its decline in imports, will be temporary (**Figure 1**). Russia's oil exports to non-U.S. destinations, largely exempt from sanctions until December 5, 2022, have been an important source of government revenues.

Figure 1. Economic Trends in Russia



Source: Created by CRS from IMF World Economic Outlook Database.

There is some evidence that economic conditions in Russia are starting to deteriorate at a faster rate. In November, the Russian central bank estimated a faster economic contraction in Q4 2022 (7.1%) relative to previous quarters in 2022 (around 4%). Sanctions may be a contributing factor—it often takes time for the full effect of sanctions to materialize—but other factors are likely contributing as well. Most notably, the war effort itself—including the mobilization of civilian production for military purposes, workers drafted to military service, and deferred domestic infrastructure projects—has created economic disruptions.

The recent expansion of oil-sector sanctions is expected to increase pressure on Russia. In December 2022, the EU banned imports of most Russian crude oil and the G7 implemented a global price cap on Russian oil purchases. These new oil sanctions could reduce government revenues, exacerbating budgetary pressures resulting from higher war expenditures.

Economic Impact Outside of Russia

Sanctions that isolate Russia are a shock to the global economy, which is still struggling to recover from the COVID-19 pandemic. The sanctions have likely contributed to disruptions in global supply chains, higher global commodity prices, and a slowdown in global economic growth. The IMF forecasts that global economic growth will slow from 6.0% in 2021 to 3.2% in 2022 and 2.7% in 2023, but it is difficult to assess the effect of sanctions separate from other contemporaneous factors, including the war, tighter monetary policy (higher interest rates) in many advanced economies, and COVID-19 related supply disruptions primarily in China.

United States

The United States has never had a substantial economic relationship with Russia; Russia (and the USSR prior to 1992) has accounted for less than 3% of annual U.S. exports and imports since World War II. However, sanctions may have significant effects on specific U.S. companies and sectors engaged with Russia. For example, there may be concerns about the exposure of particular U.S. financial institutions to Russia, the availability of raw materials from markets outside of Russia, and the competitiveness of U.S. firms. Concerns also focus on whether reduced Russian energy supplies could lead to higher gas prices and exacerbate inflation.

Europe and Energy

Among the coalition imposing sanctions, the EU has been Russia's strongest economic partner and faces the greatest economic disruption. Europe has been dependent on energy imports from Russia, especially natural gas, and EU sanctions on Russia exempted certain energy-related exemptions through December 5, 2022. Natural gas from Russia to the EU has have fallen by more than half since the war started. European governments are stockpiling fuel and providing emergency financial assistance to households and businesses. The expansion of oil sanctions could further destabilize global energy markets.

Food Security

The sanctions include exemptions to minimize humanitarian costs. For example, the war has disrupted global grain and fertilizer markets, increasing concerns about global food insecurity. U.S. and EU sanctions do not prohibit the exportation of agricultural commodities from, to, or involving Russia. Transactions involving agricultural trade are exempt from financial sanctions.

Countries Outside the Sanctions Coalition

Current sanctions on Russia are multilateral but not global, and Russia is seeking deeper economic relationships with countries outside the sanctions coalition. For example, Russia's exports to Brazil, China, India, and Turkey have increased by at least 50% since the 2022 war started, relative to the previous year.

However, Russia's ability to engage in cross-border transactions remains hindered by the sanctions. The extent to which countries outside the sanctions coalition are willing to risk potential fallout with the United States, the EU, and others by significantly increasing economic engagement with Russia is also unclear.

Impact on the Structure of the Global Economy?

The new sanctions responding to Russia's aggression could have lasting effects on the structure of the global economy. The sanctions could create (or deepen) fractures in the global economy, resulting in disparate economic blocs and schisms that could undermine the international rules-based economic order that the United States has prioritized since World War II. On the other hand, a coalition of like-minded economies, led by the United States and Europe, could create opportunities for significant new economic agreements.

Sanctions also could accelerate efforts by various countries, particularly China, to reduce their reliance on the U.S. dollar in international transactions, and Western cross-border payments infrastructure more generally. The freeze of Russia's central bank assets, in particular, could make countries reconsider their holdings of and use of the dollar. If de-dollarization efforts gain traction on a broader scale, U.S. borrowing costs could increase and sanctions could become a less effective policy tool.

Policy Questions for Congress

Sanctions have imposed some costs on Russia, disrupted global energy markets, and created economic opportunities for countries outside the sanctions coalition, including China. Most U.S. sanctions imposed on Russia in 2022 were implemented by the Biden Administration through executive orders.

As Congress exercises oversight of U.S. sanctions on Russia and considers the role of the legislature in formulating U.S. sanctions policy, possible policy questions include:

- What is the ultimate goal of sanctions on Russia?
- Are the sanctions advancing the United States and allies towards these goals?
- Are decision-makers in Russia responsive to economic pressure?
- Are more sanctions needed?
- Under what conditions should sanctions be lifted?
- How long can the United States sustain multilateral cooperation on sanctions? What would be the consequences of weakened cooperation?
- Should the United States provide economic support to U.S. companies and industries affected by sanctions?
- How should the United States engage with countries increasing economic engagement with Russia?
- Should Congress codify sanctions implemented through executive orders?

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