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How will Russia respond to Western sanctions ?



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By Swann Collins, investor, writer and consultant in international affairs. Eurasia Business news, March 7, 2022



The House of the government of the Russian Federation, Moscow. Photo credits : Eurasia Business News.

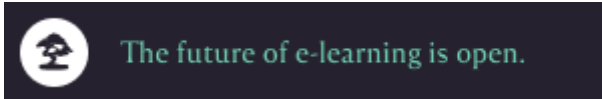
The United States, the European Union and the other members of the G7 have imposed strong economic and financial sanctions against Russian banks, state officials, the Russia's central bank, individuals and legal entities, after the launch of a military operation in Ukraine by Moscow in early morning on February 24. Western leaders see it as an invasion of Ukraine.

The European Union, together with the US, UK and Canada, has even decided to freeze the assets of the central bank of Russia and to exclude the main Russian banks from the international payment system SWIFT.

As the war in Ukraine is underway for already 12 days and that markets are worried by a further deterioration of the conflict in Eastern Europe, we can think now about the possible retaliation of the Kremlin to the Western sanctions. In order to succeed, any political or diplomatic move over settlement of the conflict in Ukraine must take into account the economic factors.

Is Russia in an economic and financial state now that will allow it to resist without suffering too much from the Western sanctions ? How will Russia respond to sanctions ?

The Russian state relies on a budget surplus since 2020, which can give financial resources to support the national economy against Western sanctions. In November 2021, the Russian Duma (lower house of parliament) adopted and published on its website the 2022-2024 budget, forecasting a budget surplus of 1.327 billion rubles in 2022 (15.8 billion euros at the rate in November), or 1% of GDP. The Russian authorities also expect the share of hydrocarbon revenues to decline from 38% in 2022 to 33% in 2024.



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Moreover, the Russian public debt is relatively low (between 16% and 17% of GDP in 2021-2022), absolutely not comparable to amounts of the public debt of European states. Russian public debt was about 13.5 trillion rubles in 2019, or 12.3% of GDP.

In 2020, despite the coronavirus pandemic and the oil crisis, Russia managed to limit the federal deficit to 3.8% of GDP. And in 2021, the Russian federal budget was expected to be slightly in surplus, if oil prices were remaining at least \$75 a barrel until January 2022. Coming to power more than two decades ago, shortly after a Russian default on its debt in 1998, Russian President Vladimir Putin has made maintaining financial stability a priority, despite difficult consequences for the population.

The Russian state now hold only \$3.7 billion in US debt compared to \$177 billion in 2010. That means that Russian public finance does not depend on the US Treasury bond.

Since 2014 Russia has more than doubled the amount of gold in its centrak bank reserves. Also, the Bank of Russia was the largest consumer of gold in the country in 2021. Russia was the second largest producer in the world in 2020 and accounted for 9.88 per cent of total global production, with 331.1t of mined gold. Russia's international monetary reserves rose by \$3.6 billion from February 21 to 24, reaching a new all-time high of \$643.2 billion.

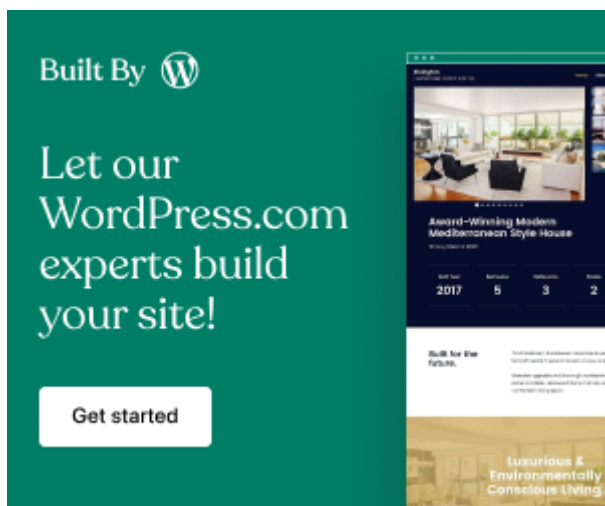
Russia can now retaliate in **four ways** against the West :

1/ Firstly, Moscow can take measures to **restrict imports of certain Western products**, as it did in 2014, in response to the economic sanctions imposed by the European Union and the United States at the time. For semiconductors, the volume of imports to Russia, which falls under restrictions, is estimated at about \$ 470 million. These imports can be reoriented to Asian partners.

2/ Secondly, Russian government can also adopt a much stronger, symmetrical response to the measures taken by Western countries to freeze Russian assets in recent days. Russian may consider **freezing the assets of Western companies that are present in Russia**. European companies are greatly exposed. Thus, there are more than 700 French companies that have direct investments in Russia, for an amount estimated by Paris to 20 billion euros. In Europe, Italian and French banks have the largest exposure in the Russian market, representing just over \$25 billion each at the end of September, followed by Austrian banks with \$17.5 billion, according to data from the international bank of settlements. The US banks have exposure in Russia amounting to \$ 14.673 billion.

3/ Thirdly, Russian authorities can decide to **reduce the exports of strategic metals** to Western markets, such as Palladium, aluminium, platinum, steel, copper, nickel or gold.

4/ Fourthly, the Russian government could decide to **nationalize some assets owned in Russia by Western companies and investors**.



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The Russian Central Bank has already announced the implementation of a ban on the outflow of foreign capital by Russian companies. If this measure had been taken a few days ago, companies like Shell or BP would not have been able to get their assets out of Russia. This is already a form of nationalization.

The coming weeks will be difficult for stock markets and European economies.

We must admit that Western sanctions pressure on Russia has led to serious problems within the Western economies themselves. The sharp rise in oil and gas prices, problems with fertilizers and wheat, titanium and palladium caused enormous disproportions in the world economy. And if each specific one could still be solved, then together they become absolutely critical for Western economies.

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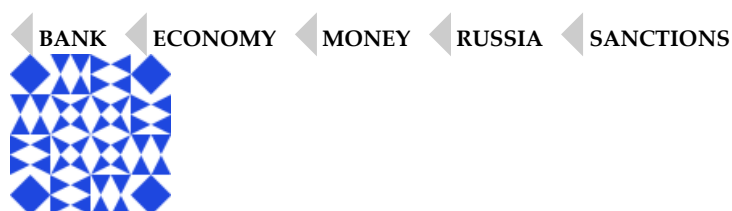
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