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SNAPSHOT

Get Ready for More Russian Belligerence

Why the Sanctions Might be Too Effective

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This week, the European Union and the United States announced additional economic sanctions aimed at punishing Russia for its increasingly direct military involvement in eastern Ukraine. These and the previous rounds are beginning to bite; the already anemic Russian economy may be headed toward recession, and inflation is rising. And in the long term, Russia's ability to develop its energy sector and restructure its massive debt is now in serious doubt.

And therein lies the problem: these sanctions may prove too effective, as serious short- and long-term damage to the Russian economy could lead to further instability in eastern Europe and Central Asia. A Russia with a sophisticated and effective military but a cratered economy would pose a substantial threat to its neighbors, especially since many of those neighbors possess large amounts of valuable natural resources. In other words, although sanctions may be intended to deter Russia from adventurism in its near abroad, they could end up doing just the opposite.

LOSING ENERGY

Even before Russia annexed Crimea and loaned its support to separatist rebels in Ukraine, the country's economy was struggling. Analysts considered a forecast of a two percent increase in GDP in 2014 highly optimistic. In fact, many suggested, the economy was on the brink of recession. Sanctions -- as even Russian officials have admitted -- are making those gloomy prospects far worse. They have significantly increased inflation and the price of household goods. But there is bad news still to come. Indeed, the real bite of sanctions will be felt in the medium and long term. In addition to targeting Russian oligarchs and Russian President Vladimir Putin's inner circle, the U.S. and EU sanctions will put significant pressure on Russia's financial and energy sectors.

On the financial side, Russian banks and companies owe more than $600 billion in debt to foreign lenders. According to Russia's central bank, over $150 billion of that debt will come due in 2014. Since Western financial institutions are now blocked from making new loans to certain Russian ones (including many of Russia's most important banks), Russian firms will have an extremely difficult time refinancing. Over the next few years, as these firms struggle, they will likely need government bailouts or face failure. And that will further dim Russia's medium- and long-term economic outlook.

On the energy side, current sanctions do not ban the import from Russia of key energy resources such as liquefied natural gas, but they do forbid the export of key technologies from the United States and the EU that would assist

Russia in developing its ability to extract and process oil from deep-water, arctic, and shale deposits. Given the decline in Russia's oil production since its peak in the 1980s -- and expected additional decreases to come, since it is getting harder and more costly for Russia to tap current fields -- making it more difficult for Russia to exploit new resources seriously threatens the long-term health of the country's energy sector.

ARMED AND READY

Although the Russian economy may be weak and getting weaker, the Russian military continues to grow in sophistication and effectiveness. As recent analysts suggest, Russian operations supporting separatists in Crimea and Ukraine have been extremely effective. They married cyber-capabilities and highly trained special operations forces to help Russia quickly establish control over Crimea and parts of eastern Ukraine. And that was no accident. Russia focused on developing these capabilities following the 2008 war with Georgia, during which its military had an unexpectedly tough time against a much smaller foe.

This concerted effort -- coupled with increases in the defense budget -- created a Russian military that is particularly adept at engaging in limited operations to ensure that neighboring countries either remain sympathetic to Moscow's goals or suffer the loss of territory. The strategy is at its best where there are significant ethnic Russian populations and where Russian special operations forces can work closely with separatist elements to foment instability and control territory.

Russia certainly has the opportunity and incentive to make use of its forces. Large ethnic Russian populations reside in many of the Baltic states, as well as in other pockets of Ukraine and Belarus. What's more, many of these areas possess significant natural resources. In Ukraine, for example, the annexation of Crimea provided Russia with control over potentially trillions of dollars of underwater energy resources [1] in the Black Sea. Additional westward territorial acquisitions would provide Russia with increased access to industrial facilities and resources in the Donbas region in eastern Ukraine and potentially greater control over maritime resources in the Black Sea. Likewise, in Central Asia, countries such as Kazakhstan have both substantial ethnic Russian populations and lots of oil, which, given the deteriorating state of the Russian economy, may prove enticing. In particular, the Karachaganak oil field -- one of Kazakhstan's largest -- is located in a region with a significant ethnic Russian population.

And although a militarily strong but economically weak regional power invading a smaller country for wealth may seem like a strategy right out of the nineteenth century, one should remember Iraq's decision to invade Kuwait in 1990. Iraq's occupation of its neighbor partly stemmed from the fact that it was in dire financial straits following the Iran-Iraq War and capturing Kuwait offered it the opportunity to control significant oil holdings.

SAFER SANCTIONS

The sanctions meant to punish Russia for its activities in Ukraine and deter it from further regional aggression may make Russia more set on such adventurism. Overeffectiveness is a problem rarely encountered by U.S. policymakers; usually the United States is trying to convince its allies in Europe and Asia to go along with its strategy in order to ensure that the sanctions are even minimally biting. Indeed, so much political energy is spent ratcheting up pressure that policymakers often ignore fundamental questions about the long-term implications of these sanctions [2].

Policymakers would be well served to more fully consider how to hold Russia's feet to the fire while also avoiding significant instability in Russia's near abroad. To do that, instead of relying on sector-based sanctions aimed at slowing Russia's economic development in the coming years, U.S. and EU policymakers could redouble efforts to target a wider swath of Russian elites close to Putin. Such a strategy, although it would have a more limited effect on the Russian economy, could put additional pressure on Putin's inner circle while avoiding significant damage to the Russian economy.

Likewise, although economic sanctions have become the go-to tool of coercive diplomacy in the past ten years, other tools could potentially be more effective. In particular, the United States and the EU should consider providing additional military aid to Ukraine -- and other threatened countries -- so that they can better defend themselves from Russian aggression. Although this policy has its own risks, it would surely decrease Russia's incentives to seize economic resources and increase the costs of trying.

Over the past few years, U.S. and EU policymakers have honed their ability to use economic sanctions to put great pressure on countries such as Iran, Syria, and Russia. But these policymakers need to temper discussions of ratcheting up pressure with consideration of the medium- and long-term consequences of that pressure. Only then will they be in a position to ensure that their attempts at coercive diplomacy do not backfire.

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