

Russia: Freezing for Freedom?

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The ramifications of an EU energy embargo for the Russian economy

“We can freeze now and again for freedom” and endure “less happiness and *joie de vivre*” for a couple of years. With this comment on the ARD talk show *Maischberger* on 9 March, former German president Joachim Gauck reiterated his demand for an immediate halt to Russian energy imports. Ever since the beginning of the Russian invasion of Ukraine, there has been ongoing discussion in Germany as to which effective steps could be taken to move the Russian government to cease fighting and enter into peace negotiations. The two most important demands being debated are an increase in arms shipments to Ukraine and a ban on Russian energy imports.

So far the German government has blocked an embargo on Russian energy imports in the European Union. Germany sources 55 percent of its imported natural gas and around a third of its imported oil from Russia. For the EU as a whole, these figures are around 40 percent for natural gas and almost 30 percent for oil respectively. Despite repeated statements about “achieving energy independence from Russia”, German economics minister Robert Habeck has sought to [dampen expectations](#) that this could take place within a few weeks or months.

Until now, this interweaving of energy and politics has followed a political calculus, as it has been perceived across the political spectrum as providing stability in Germany’s relationship with Russia, and something that should help keep exclusive channels of communication to Moscow open in times of increasing conflicts. In keeping with the slogan *Wandel durch Handel* (“change through trade”), for years supporters of Nord Stream 2 brushed off any concerns about the project with the argument that the construction of the gas pipeline did not primarily serve economic interests but rather cemented Germany’s special status in the eyes of Russia. The pipeline’s suspension and the debate around a possible embargo on Russian energy providers thus mark a watershed moment, for according to Habeck both enable the transition to renewable energy to be discussed not only with respect to the environment but also “finally from a national security perspective”.

What are the arguments in favour of a ban on Russian energy imports? Going beyond the issue of security risks, proponents of a ban point to the significance of oil and gas exports for Russia’s budget. A drastic reduction of imports or even their suspension would deprive the Russian government of the means with which they finance their belligerent foreign policy.

That said, there is disagreement on the extent to which a boycott would impact not only Russia’s ruling class, but also broad swathes of the wider population, which could result in increased support for the government. There is also disagreement as to what the political consequences of a Western embargo would be. Would it facilitate a further strengthening of ties between China and Russia? What effects would a comprehensive economic decoupling between the EU and Russia have on the post-Soviet sphere?

Russia’s Dependence on Fossil Fuels

Russia has occupied the role of raw materials provider for the capitalist centre states in the

international division of labour since the 1990s, and in recent years for China as well. The pillars of the Russian economy are raw materials extraction and (partial) processing, the aluminium, metallurgy, and steel industries, and the finance sector. The proportion of GDP constituted by the fossil fuel sector (oil, natural gas, and coal) over the past ten years has remained constant at 20 percent and is thus of central importance to the Russian economy.

Raw materials dominate Russian exports, with oil, gas, and metals representing between 65 and 70 percent. If commodities that can partially be ascribed to the extractive sector (chemical products, foodstuffs, and wood) are included, this figure exceeds 80 percent. Machinery and equipment account for only 7 to 12 percent of total exports — these are almost exclusively military equipment and components for nuclear power plants, along with a smaller proportion of agricultural machinery. [1]

The EU is by far the most important export market for Russian energy products. In 2019, it accounted for 55 percent of energy exports, followed by China (15 percent), Turkey, and South Korea (6 percent each). In contrast, Russia primarily imports high-value commodities, with machinery and equipment accounting for between 40 and 50 percent of total imports. Chemical products and processed raw materials make up another significant proportion of imports (between 14 and 18 percent).

In comparison to the 1990s, only the import of foodstuffs and agricultural products has been significantly reduced, which suggests that the state's attempts to bolster the country's agricultural production are beginning to bear fruit. Yet there is no evidence that the manufacturing base has been modernized. While the share of fixed capital invested in repairs and modernization averaged 21 percent between 2005 and 2008 (the peak phase of the economic boom), this figure fell to 17.4 percent in 2014 and 16.1 percent three years later. Accordingly, the average age of machinery and equipment rose slightly from 11.2 years to 11.4 years over the same time period.

A modernization of manufacturing plants is a central requirement for Russia to be able to overcome its dependence on raw materials. Measured as a proportion of GDP, state expenditure for research and development has remained at a very low level, only increasing from 1.07 percent in 2014 to 1.11 percent in 2017.

Although the Russian Federation regularly achieves trade surpluses, this is almost exclusively due to oil and gas exports. These exports have allowed the government to amass the fourth-largest foreign currency reserves in the world, behind China, Japan, and Switzerland. Yet these funds have hardly been used to diversify the economy or develop infrastructure, serving instead as a lifeline in times of crisis. The EU, the UK, the US, and Canada froze Russian assets in response to Russia's attack on Ukraine. As a result, the Russian central bank can no longer access half of its foreign currency reserves, which amount to 630 billion US dollars.

Due to the low levels of diversification in its economy, Russia's budget is largely dependent on income derived from raw materials exports. The oil and gas sector alone contributes one third of the total federal budget. The extent to which the state is directly dependent on the fossil fuel sector is illustrated by a [statement](#) made by then-prime minister Dmitry Medvedev in February 2016: the low price of oil led to a massive decline in state revenue, he said, necessitating a 10 percent cut to the state budget. A further drop in the oil price or a decline in exports, as would be the case in the event of an EU embargo, would thus have wide-ranging repercussions for the Russian economy.

Returning to the Periphery

Since the dissolution of the Soviet Union and its transition to capitalism in the 1990s, Russia has

become increasingly oriented towards raw materials exports. That development must be analyzed in the context of this profound transformation and accompanying formation of new power structures. Otherwise, the contradictions of Russia's raw materials economy (peripheral integration into the global market, the social polarization of Russian society) will remain largely unexamined.

The disentangling of party and state initiated under *perestroika* created a power vacuum in the Soviet republics that greatly enhanced the scope of activity for national elites (state bureaucrats, factory directors, and high-ranking party officials). This often facilitated an alliance between nascent national independence movements and elements of the state bureaucracy, with the latter assuming that they would be able to more strongly influence political developments and the distribution of state wealth in a future successor state (such as Ukraine) than they would in a reformed Soviet Union under president Mikhail Gorbachev.

The relevant sections of the Russian elite took advantage of these divisions. As the economic crisis of the late 1980s threatened to escalate and state control over production decreased, a heterogeneous alliance of neoliberal economists, members of the salariat, and large sections of the liberal dissident movement pushed for an immediate transition to a market economy. Owing to the comparatively advanced internationalization of Russian commodity firms, the high degree of industrialization, and the size of the country, this alliance, represented by Boris Yeltsin, believed that conditions were ripe for an independent, capitalist Russia.

In the Russian Federation that emerged in the wake of the Soviet Union, the Yeltsin government pursued its goal of making its market-based reforms "irreversible" from the outset. By means of "shock therapy", it sought to execute a radical break with the Soviet planned economy. Yet this neoliberal economic policy was not a therapeutic programme of modernization, instead ushering in a decade of economic decline that continues to shape Russia today. The extent of this impact is illustrated by the view of economist [Joseph Stiglitz](#), according to whom Russia's economic losses during this time period (measured in relation to GDP) were even worse than those the country experienced during the second world war.

The shock therapy applied comprised four key components: the removal of state price controls, the liberalization of foreign trade, the cultivation of a private finance sector, and the privatization of state assets. The government under Yeltsin did not follow the path taken by China, that of holding on to state assets — at least in key sectors — and supporting the emergence of private capital in parallel. Through a state-directed process of privatization, a group of national business owners, the so-called "oligarchs", were able to bring the most profitable sectors of the Russian economy — the fuel, iron, and steel industries, non-ferrous metallurgy, and the chemical and petrochemical industries — under their control — essentially, the sectors of the Soviet planned economy that fulfilled a central supply function through the delivery of cheap resources in large quantities. Their international competitiveness is based on the exploitation of relatively cheap labour power, relatively modern production facilities, and large transport capacities.

In contrast, production sectors (mechanical engineering, consumer goods) were left defenceless against international competition by the forced integration of the Russian economy into the global market. By 1998 industrial production had fallen by 45.8 percent relative to 1990 levels, while the number of those employed by the industrial sector fell by a third. The industrial sector's loss of significance is also reflected in absolute terms: from 1990 to 2014, the proportion of GDP constituted by industrially produced commodities fell from 65.5 percent to 41 percent.

A New Relationship between Capital and the State

Vladimir Putin's assumption of the presidency in 2000 symbolized a new stage in the development of

Russian capitalism. Increased economic *dirigisme* and the centralization of decision-making processes in the executive are a reaction to the specific dysfunctionalities of the unregulated neoliberal capitalism of 1990s Russia, and aim to improve the conditions for the reproduction of the capitalist mode of production. In this altered configuration, the state has increasingly adopted a mediating role between the individual factions of the ruling bloc while taking up the task of disciplining the different social classes and their organizations (the workforce and unions).

The consolidation of power relations under Putin established a new form of regulation that could be called an oligarchic-statist order. The government declared itself willing to legalize the structures of ownership that emerged from the process of privatization in return for the oligarchs' political support. Above all, however, the new order was based on an intensified extraction and export of raw materials (mainly oil and gas) — a lucrative business model that became increasingly controlled by state firms.

Oligarchs who cooperated had their share in the oil companies bought out by the state. Roman Abramovich, long-time owner of the English football club Chelsea FC, received 13 billion dollars for the sale of his company Sibneft to Gazprom. The same thing happened with Russian shareholders of the TNK-BP consortium when it was taken over by state-owned oil company Rosneft.

At the same time, the Putin government was clear from the beginning that resistance to these changes would not be tolerated. This was evident in the serious proceedings against Mikhail Khodorkovsky and the liquidation of his oil company Yukos, the majority of whose assets were transferred to Rosneft. Despite conflict between a portion of the oligarchy and the state, the majority supported this new course. On the one hand, they favoured a strong state that could support and help drive the internationalization of Russian firms. For this reason, admittance to the World Trade Organization became one of the key projects undertaken by the Putin and Medvedev governments. On the other hand, only a functioning state would be able to prevent Russia collapsing again.

Putin's first two presidential terms (2000–2008) coincided with a period of economic growth that had a markedly positive effect on socio-economic conditions for the general population, with real disposable incomes increasing by 7.9 percent. In the same timeframe, the fraction of the population living below the poverty line decreased from 43.8 million (30 percent of the total population) to 19 million (13.5 percent). This resulted in the emergence of an urban middle class who have proved important in propping up the oligarchic-statist order. This is also true of a certain fraction of those who lost out from the transformation (workers, retirees, and state employees in the education and healthcare sectors). While these sectors of the population suffered drastic pay cuts in the 1990s, they now profited from increases in wages and pensions, a measure that economist [Stanislav Menshikov](#) believes contributed to a 20 percent increase in consumption.

The clientelist integration of certain social classes should not be confused with an active policy of wealth redistribution, however. Although the state's social expenditure grew 126 percent from 2005 to 2009, this figure looks less impressive when the fact that total state expenditure [increased by 132 percent](#) across the same time period is taken into consideration.

Conversely the number of (US dollar) billionaires in Russia went from zero in 2000 to 87 in 2008. The social policies funded by oil revenues did not conflict with the interests of large-scale capital — instead, they pacified the social conflicts that had raged in the 1990s. The growing economic importance of the raw materials sector is also reflected in its above-average wages, which had a particularly stabilizing effect in regions beyond the main centres of Moscow and St. Petersburg. Although by the mid-2000s [Norilsk Nickel](#) had shed almost half of the 160,000 employees that it had in 1990, it paid an average wage 2.6 times higher than the national average.

Failed Alignment with the West

The consolidation of the oligarchic-statist order was largely achieved through the intensified extraction of fossil resources. This led to criticism of the Russian economy's dependence on the oil and gas sector and demands that steps be taken to strengthen production-oriented sectors.

Since its beginning, the Putin government had endeavoured to initiate the modernization of the Russian economy through new international alliances. Central to this strategy was the EU, by far Russia's largest trading partner. Within the EU, Germany played a key role in Russia's foreign policy strategy. Germany had risen to the position of Russia's most important trading partner and creditor as early as the 1990s. Additionally, German companies (particularly those in the plant construction, engineering, automobile, and chemical sectors) expanded their presence in Russia through the founding of local subsidiaries.

In the 2000s, the scope of trade in the energy sector was expanded further through a joint venture between Gazprom, Wintershall, and E.ON established to exploit new gas fields. Although the German partners (Wintershall and E.ON) had to accept the controlling interest being held by Russian energy companies, their role as providers of technical equipment meant they still occupied a significant position.

The construction of the Nord Stream gas pipeline strengthened economic relations between the two countries, with German capital increasingly playing a "[leading role](#)". The Western-oriented trade policy (particularly towards the EU) pursued under Putin cemented Russia's semi-peripheral status as raw materials supplier to the capitalist centre states. From 1998 to 2008, fossil fuels increased from 40 percent to 73.5 percent of all exports, while machinery and equipment fell from almost ten to three percent.

Pivoting to China

Russia's economic consolidation also exacerbated competition between sections of the Russian bourgeoisie and Western capital interests. These first came to public attention at the Munich Security Conference in 2007, when Putin criticized the way he believed Russian concessions in the process of German reunification had been used to strengthen NATO's position in Europe, which he said [placed limits on cooperation](#). The efforts of Russian capital to internationalize were also met with stiff resistance in the West. One instance of this was the discussions over the potential danger of direct Russian investment, for example by Gazprom, and the associated loss of political control. This was also criticised by Putin in his Munich speech, where he lamented the barriers that Russian capital faced in key economic sectors in Western countries, despite the fact that the Russian economy was largely open to foreign capital.

By contrast, the strengthening of the stature of the G20 during the economic and financial crisis of 2008 made plain the increased political and economic significance of emerging countries, particularly the BRICS states. [2] This bolstered certain forces within Russia's ruling bloc, which urged a political and economic turn towards Asia and (to a more limited extent) Africa. They believed such a focus would offer the domestic economy, especially the productive sectors, new possibilities for expansion and would create a political counterweight to global Western hegemony, in which Russia would take a leading role thanks to its size and military potential.

As a result of the first Ukraine conflict in 2014 and the ensuing sanctions imposed by the West, the regional orientation of Russian foreign policy shifted significantly. The importance of countries in the OECD and the EU diminished. Instead, the flow of Russian commodities was redirected towards Asia and in particular China, which superseded Germany as Russia's most important trading partner

in 2021.

While Germany remains an important supplier of machinery and facilities and a buyer of Russian natural resources (oil and gas), China has replaced German manufacturers in many areas. Through the construction of new pipelines China has also become a more significant purchaser of fossil fuels. Despite this geographical shift in trade, Russia's typical foreign trade structure (raw materials for machinery) remains the same, thereby solidifying Russia's semi-peripheral position in the global capitalist system.

Ways Out of the Raw Materials Trap

Russia's orientation towards the global market expedited the real-economic disintegration of the post-Soviet sphere. At the end of the 1980s, Soviet member states completed an average of almost 72 percent of their trade with each other — Russia being the exception at almost 58 percent. From 1991 to 1993 the [trade volume between CIS member states](#) [3] halved, which further exacerbated the process of deindustrialization.

The post-Soviet sphere's diminished importance for Russian trade becomes particularly clear from a long-term perspective. In 2004, Russia still exported 16 percent of its commodities to CIS states and sourced 23.5 percent of its imports from them. By 2017, these numbers had dropped considerably: only 13.4 percent of Russian exports flowed into the CIS region, while the share of imports had shrunk to 10.9 percent.

One exception to this trend is found in the member states of the Eurasian Economic Union (EAEU), the most successful integration project in the post-Soviet sphere under Russian leadership. Russian trade with the rest of the bloc even increased slightly in recent years, although it is starkly asymmetrical. At 30 percent, mineral products dominate trade in the union. Of this, 80 percent flows from Russia to the other members. Machinery and equipment come in second at 21.5 percent of trade, which is almost entirely accounted for by Russia (62.4 percent) and Belarus (35.3 percent). When economic crisis returned in 2015, trade amongst EAEU member states decreased considerably, most significantly in the machinery and equipment market segment (-39.7 percent), metals (-30.9 percent), and mineral oil products (-23.2 percent) (Ustyuzhanina, 2016, p. 39).

From Russia's perspective, the EAEU was originally planned as an alliance with Belarus, Kazakhstan, and Ukraine — the most industrially and financially developed countries in the region. Ninety percent of Russia's foreign trade within the CIS is conducted with these three countries, which also constitutes 13 percent of its overall trade. Belarus, Ukraine, and Russia have the highest amount of industrial diversification among CIS member states. This creates favourable conditions for intensified economic cooperation as part of an international integration project. [Fyodor Lukyanov](#), chief editor of *Russia in Global Affairs* magazine, saw Kyiv's participation as the "most important unspoken goal of Eurasian integration". Only with Ukraine, Lukyanov believed, could the EAEU achieve real global importance.

With the beginning of the Ukraine conflict in 2014, the country's accession to the EAEU is now permanently off the table, putting a dampener on its success as an integration project. It remains to be seen whether Russia's push to integrate Armenia, Kyrgyzstan, and Tajikistan will prove to be "more of a burden than a benefit", since the economic costs increase with the admission of these crisis-ridden states. Support for the integration project among the Russian population may also diminish due to widespread hostility to migrants from the Caucasus and Central Asia.

New Conflicts on the Horizon

Oil, gas, and coal constitute over 60 percent of Russian exports, half of which end up in the EU. An immediate Western energy embargo would thus plunge Russia into a deep economic crisis, especially as long-term supply contracts mean it would hardly be possible to fall back on alternative export markets.

In addition, a halt to Russian energy imports would accelerate the realignment of Russian foreign trade relations towards China and the post-Soviet sphere that has been an apparent trend since 2014. While Russia also plays the role of raw materials supplier in its dealings with China, the situation in the post-Soviet sphere is different. There are indications that Russia integrates member states as suppliers into the supply chains of selected flagship projects (in weapons technology, nuclear technology, agriculture, and engineering), but without them having a broader impact. This may have reduced the attractiveness of the Eurasian integration project for other countries.

A fundamental shift away from a dependence on raw materials exports is thus not to be expected, which will only exacerbate the inherent contradictions of the Russian developmental model. New conflicts thus appear unavoidable.

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Footnotes

[1] Unless otherwise indicated, figures concerning Russian economic development are based on statistics provided by the Russian Federal State Statistics Office, while export figures are sourced from data made publicly available by the Federal Customs Service.

[2] BRICS is an acronym for Brazil, Russia, India, China, and South Africa.

[3] The Commonwealth of Independent States came into being in the course of the dissolution of the Soviet Union as an attempt to coordinate a common economic and security policy between the successor states. Apart from the Baltic states, through to the 2000s all former Soviet states were CIS members. Since 2005, Turkmenistan has been an associate member, while in 2008 Georgia announced its withdrawal from the organization. In 2018, then Ukrainian president Petro Poroshenko signed a decree resolving to end his country's participation in the CIS, although Ukraine formally remains a member.