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• Author: [Wojciech Jakóbiak](#)

## [Change through rapprochement vs. change through sanctions](#)



Following Russia's aggression in Ukraine, the two models of cooperation with Russia in Europe are on a collision course and only one is proving effective.

The Ukrainian crisis resulted in the introduction of economic sanctions by the European Union against Russia. With the situation in Ukraine apparently relatively calm at present, the temptation to bring Russia closer to Europe arises once again. Rapprochement by means of economic cooperation is intended to prevent future examples of unpredictable Kremlin policy. However, the policy of 'change through rapprochement' is on a collision course with the policy of 'change through sanctions'.

The oil market conditions Russia faces today bring into question the sustainability of the model of power shaped throughout Putin's tenure. President Putin has recently pointed out that it is low oil prices which are most costly to Russians. The statement was meant to disavow the sanctions as ineffective but it rather serves to expose real concerns.

### **The crisis of the petro-state**

Countries dependent on the sale of crude oil now have to revise their budgetary spending. Crude, which cost more than 115 dollars a barrel in June 2014, is now oscillating around 30 dollars. The downward trend persists despite periodic fluctuations. Two other petro-states will become reference points in the discussion about the impact of this on Russia: Saudi Arabia and Venezuela.

Saudi Arabia announced a record budget deficit of 98 billion dollars in 2015. Revenue was expected to reach 608 billion riyals (162 billion dollars) which is a far cry from 2014 projections thanks to the slide in oil prices.

Revenue from the sale of oil in 2015 was forecasted at 118 billion dollars, 23 per cent less than in the previous year. Revenues from the non-oil sector, however, increased by 29 per cent to 43.5 billion dollars.

The Saudis [planned for a budget deficit of 87 billion dollars in 2016](#) with revenues expected to drop to 137 billion dollars. The budget was produced on the basis of the assumption that the average price per barrel will be 29 dollars. In the case of Saudi Arabia, the implications are mainly financial in nature, whereas a political dimension has also developed in Venezuela. Cheap crude and the budget crisis associated with it could have been the reason behind the loss suffered by the ruling party of President Nicolas Maduro in the parliamentary elections of December 6. The Socialist Party relinquished its parliamentary majority for the first time in 16 years. Opposition parties won 112 out of 167 seats in the National Assembly and the Socialist Party won 55 seats.

The drop in the price of a barrel of oil deprived the government of significant resources, leading to fractures in the social welfare system which provided legitimacy for the Venezuela authorities. The Venezuelan social order, funded by petrodollars, faces an existential threat. Despite an appeal by Caracas to limit oil extraction in member states in a bid to prompt a rise in prices, OPEC chose not to intervene. It was argued that the surplus of the commodity affecting revaluation on the markets does not flow from OPEC states, hence,

measures taken by the cartel would prove ineffective. Although Maduro's term expires in 2019, an element of the opposition is already calling for his early resignation, should he fail to introduce reforms. Maduro speaks of a counter-revolution aimed at undermining the fundamental principles of the Venezuelan revolution.

### **If cheap oil doesn't kill you, it will make you stronger**

What options have emerged for another commodity power – Russia – under these circumstances? Further isolation, lying to society and providing distractions in the form of entertainment such as further military campaigns in the Middle East or Eastern Europe serve as alternatives to reforms.

Russia was in recession in 2015 due to the concomitance of falling oil prices, the weakening of the ruble, sanctions and graver structural problems. In October 2015, Russians' real wages [dropped](#) by about 10 percent on the same period of the previous year. Russian media propaganda fingers the guilty party: the West. Opposition is not a real option. An internal dispute as to how to deal with the threat to the main revenue source rumbles on without any input from society. The authorities ensure social support through aggressive foreign policy as well as steps aimed at maintaining a stable social policy which benefits both citizens and the elite.

Here is a case in point: Gazprom CEO Alexey Miller earned 25 million dollars in 2014 according to *Forbes* magazine. The company's management earned 40.3 million dollars. According to *Forbes'* estimates, all of the 17 managers of Gazprom were paid an average of almost 2.3 million dollars, roughly 198 thousand dollars a month.

Regular employees can also count on significant social assistance; they receive bonuses on Oil and Gas Industry Workers' Day, Defender of the Fatherland Day and – in the case of women – on March 8. A bonus for continued service exceeding 15 years is also paid. The cost of holidays at Gazprom's resort are also reimbursed up to the value of 92 thousand rubles and employees of the company can access free services at its health resorts. The company's activity also includes unofficial support 'for its own people'.

Stroygazmontazh – the company of Arkady Rotenberg, widely regarded as one of Putin's friends, was awarded a no-bid contract for the construction of a gas pipeline from Russia to China named 'The Power of Siberia' worth 155.9 billion rubles, a record sum.

One can conclude that the corrupt system, which links business and politics in Russia, guarantees a good life for its affiliates. Putin has signaled that he intends to take care of "his own people" in the face of the oil price crisis.

The rhetoric of the besieged fortress is developed with the ordinary citizen of the Russian Federation in mind. Russians consolidate around their chieftain – Vladimir Putin – in the face of an 'attack' in the form of oil price gouging which the Kremlin attributed to undefined ['political forces'](#) since November of 2014. However, evolution of the rhetoric was observed as the downturn continued. When Igor Sechin, the president of Rosneft, became agitated over Saudi plans to supply Poland with oil – a traditional market for his company – his statement had to be toned down by Russia's Minister of Finance Anton Sulianov who conceded that competition for business is a typical feature of the market game and that it is something that one has to accept. Petro-states are engaged in a battle for customers in a sluggish market plagued by oversupply.

### **Sanctions do work**

The policy of sanctions threatens Russia more so than plummeting oil prices. Vladimir Putin has wasted petrodollars mainly on 'bread and entertainment' for the Russian people, in return for increased support. I am speaking of the ventures into Ukraine and Syria and, in particular, the Olympics of 2014 in Sochi. At a cost of nearly 50 billion dollars, the games were one of the most expensive in history. According to estimates by [Bloomberg](#), Vnesheconombank (VEB) took it upon itself to put the infrastructure in place for the Sochi Olympics, investing over 200 billion rubles in assets such as hotels and ski resorts. According to Standards and Poor's, VEB became a financial tool for Moscow's interventions in the economy. With its help, Putin financed special-purpose projects which flew in the face of market logic. The jaunt into Ukraine resulted in EU and US sanctions against the regime which cut off VEB's access to mid-term and long-term loans.

The restrictions introduced by the West arrest indispensable support for the Kremlin from Western business for Russian endeavors and threaten the existence of social giants. Rosneft and Novatek - targeted by the sanctions - were forced to discontinue their investment programs. They have been seeking capital and partners in Asia, thus far with minimal success.

Gazprom has not been directly targeted by sanctions for good reason: Unlike competitors, this company has strong business ties with customers from the European Union. These ties often go beyond business as they often take the form of personal ties as evidenced by the example of former German Chancellor Gerhard Schroeder, a member of the management board of Nord Stream. The Western European support for Nord Stream 2 illustrates that [Europe will not allow Russian business to become completely isolated.](#)

Parliamentary elections will be held in September 2016 in Russia. As the Western media wait with bated breath for political changes brought about by the difficult economic situation and the actions of society it prompts, business circles can act to initiate change. For it is they who should advocate change in Russia as it is they who are equipped with the tools required to apply pressure to the Kremlin. The policy of sanctions should be continued in order to provide encouragement to them. 'Change through rapprochement', popular in Germany, is decidedly ineffective juxtaposed against the policy of 'change through sanctions'.

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