‘Sanctions Are a Failure…Let’s Admit That’

With Europe debating re-opening economic ties to Russia, have U.S. sanctions on Moscow lost their teeth?

David Francis and Lara Jakes

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From Iran to Russia, Africa, and North Korea, the Obama administration has long relied on financial sanctions as a preferred weapon against U.S. adversaries. But over the past year, it’s America’s allies that are increasingly feeling the pinch, leading Washington to wonder whether its favorite economic power tool has been so overused it’s becoming ineffective and, in some cases, even counterproductive.

The U.S. financial system is the engine of all global trade. Sanctions that are prohibitive or otherwise too restrictive to foster trade risks driving business to foreign markets — and, in doing so, broker new alliances between longtime American friends and foes.

“It is important to make sure our sanctions tools remain effective and are not overused,” acting U.S. Treasury Undersecretary Adam Szubin said this month. “We must continue to balance the costs and benefits of our sanctions regime in our favor.”

Szubin oversees the Treasury Department’s counterterrorism and financial intelligence arm. His boss, Treasury Secretary Jack Lew, warned Congress in March that financial transactions may bypass the United States if sanctions “make the business environment too complicated or unpredictable, or if they excessively interfere with the flow of funds worldwide.

“We must be conscious of the risk that overuse of sanctions could undermine our leadership position within the global economy, and the effectiveness of the sanctions themselves,” Lew said.

Tensions wrought by U.S. sanctions against Russia and Ukrainian separatists, for example, have divided U.S. allies in Europe that were already financially struggling before being hit with the economic penalties’ knock-on effects. On Thursday, the lower house of France’s parliament voted in a nonbinding agreement to lift EU sanctions against Russia.

“Sanctions have been a success? No. It’s a true failure,” Italian lawmaker Deborah Bergamini, who is also a delegate to the Parliamentary Assembly of the Council of Europe, told a Rome forum in February that pondered the West’s relations with Russia. She said Italy has lost at least 1.25 billion euros in exports since U.S. and European Union sanctions were imposed in 2014.

The U.S. State Department’s chief sanctions policy coordinator, Ambassador Daniel Fried, rejected her argument, saying sanctions were the only thing that helped broker the 2014 cease-fire known as the Minsk agreement, which since has all but fallen to the wayside in the Donbass region in eastern Ukraine.

“I do not agree that sanctions are a failure,” Fried said at the conference, held at the Center for American Studies in Rome. “If not for sanctions, we would not have the prospect of a Minsk agreement at all — we would have more war. Sanctions have brought about the possibility of a diplomatic solution.”

Bergamini shot back: “Sanctions are a failure; I insist on that. … Europe is paying a big price. Let’s admit that.”

Meanwhile, Kremlin consultant Dmitry V. Suslov, deputy director of the Council on Foreign and Defense Policy in Russia, sat back with a slight smile on his ruddy face.

“Sanctions are harming both sides,” Suslov said, adding that the economic penalties have had little sway on Russia’s military actions in Donbass: “They are proving unable to change the Russian cause.”

New research from the Cato Institute and the Center for a New American Security (CNAS) has raised questions about how effective sanctions actually are — and shows mounting evidence of their negative ripple effect.

Cato research fellow Emma Ashford, an expert on the politics of energy, called the sanctions against Russia an “outright failure” that have led to food shortages and credit crunches for ordinary Russians, and ultimately “are harming U.S. economic and geopolitical interests.”

A Treasury Department statement, e-mailed Thursday to Foreign Policy, disputed that.

“It’s clear that our sanctions, coupled with the dramatic fall in oil prices, have imposed great costs on Russia’s leadership with only a limited macroeconomic effect on the U.S. and European economies,” the statement said. It went on to say the transatlantic economic penalties “have already contributed to tighter financial conditions, weaker confidence, and lower investment in Russia.”

Russia’s economy has been in recession since its financial power base was hit by U.S. and EU sanctions in 2014 as punishment for invading Ukraine. This year, the value of the ruble hit an all-time low against the U.S. dollar, and Moscow is reeling from low global oil prices that have sent its projected budget revenues into a tailspin. A Reuters poll released Thursday predicts Russia’s economy will further contract by 1.5 percent in 2016 and the International Monetary Fund believes it will remain in recession until next year.

The one sanctions success story that is widely acknowledged is Iran.

In the mid-2000s, the United States, the United Nations, and the European Union imposed a slew of sanctions on Tehran to force the Islamic Republic to abide by international treaties prohibiting it from building a nuclear weapon. The sanctions were ratcheted up in 2012 amid sagging negotiations between world powers and Tehran; as a result, Iran's economy cratered as the value of the rial plummeted and daily oil exports more than halved, from 2.5 million barrels in 2011 to 1.1 million barrels in 2013.

The financial fallout, combined with the 2013 election of relatively moderate Iran President Hassan Rouhani, injected new urgency into the nuclear negotiations. In July 2015, world powers agreed to lift sanctions in exchange for Iran limiting its nuclear program — a goal that had long proven elusive.

"Our sanctions against Iran's nuclear program are the most powerful example of how a broad-based effort, coupled with serious diplomacy, can succeed," Lew told a Washington audience last month.

But the sanctions-driven nuclear deal also spawned a political backlash against the United States from Israel and Saudi Arabia — two key Mideast allies — that Washington has yet to smooth over. In Congress, Republicans and some Democrats are trying to roll back the deal, in part by increasing sanctions against Iran. GOP lawmakers also have resisted Obama administration efforts to give Tehran greater access to the global financial system, including conducting transactions in dollars.

And even Iran isn't happy: Tehran's Central Bank chief Valiollah Seif this month accused the United States and Europe of not living up to the terms of the nuclear deal by keeping the Islamic Republic locked out of the international financial system.

Widely overlooked in the story line of sanctions' impact on Iran is what the CNAS study described as much of the source — if not predominantly so — of Iran's financial straits: "the 2014 collapse in oil prices and significant domestic economic mismanagement." CNAS said that was true for Russia, too.

Worldwide, the Treasury Department has imposed ongoing sanctions in 28 programs. Some are broadly splayed against geographic regions and countries, while others are limited to specific individuals and business entities. Though the vast majority go unnoticed — except by the people, businesses, and governments they directly impact — more than a few have notably fallen far short of reversing aggressions by bad actors.

In North Korea, a U.S. trade embargo to punish Pyongyang for its nuclear weapons and ballistic missile programs has not stopped the Hermit kingdom from launching frequent rocket tests, including one as recently as Thursday.

In South Sudan, the Obama administration has long threatened — including again this week — to impose sanctions on President Salva Kiir and rebel leader Riek Machar for failing to uphold an admittedly loose peace agreement or even tone down a bloody power struggle in its third year.

But Washington has held off on directly penalizing Kiir and Machar, although it has issued broad sanctions against people guilty of threatening South Sudan's stability, including through war crimes and human rights abuses.

The U.S. is also warning that it may finally ask the U.N. Security Council to impose an arms embargo against South Sudan — a move the Obama administration has resisted for years.

U.S. sanctions in Somalia have produced unintended — and devastating — consequences. Experts said restrictions on money sent to Somalia have stunted funding streams to the terror group al-Shabab, which is based there. But a 2015 report by the Center for Global Development concluded that legitimate money transfers — whether to nonprofit aid groups or impoverished relatives — also were curbed.

"A major source of income, as acknowledged by everyone in Somalia, is remittances," said Elizabeth Rosenberg, senior fellow and director of the energy, economics, and security program at CNAS. "You shut off a major source of income for the country."

But most of the consternation over U.S. sanctions centers on those imposed against oligarchs in Russia and warring separatists in eastern Ukraine — and whether Europe will continue to support the penalties.

Beyond France and Italy, there's also growing momentum in Germany to lift the sanctions. Last month, German Economy Minister Sigmar Gabriel called for the European Union to try to create conditions by this summer to eliminate the penalties. Trade between Moscow and Berlin has dropped by nearly 12 billion euros ($13.6 billion) — a quarter of the total value between 2014 and 2015, said Michael Harms, chairman of the Russian-German Chamber of Commerce.

EU leaders are expected to decide whether to extend their sanctions by June. Treasury officials said Thursday that they believe the sanctions will hold, based on conversations President Barack Obama had last week with several European leaders.

Direct foreign investment in Russia has plunged from $69 billion in 2013 to $23 billion in 2014, after Moscow invaded Crimea. Anders Åslund, an economic policy expert at the Atlantic Council, said that's exactly what the sanctions were designed to do — proving they do have some bite.

"International finance in Russia is a one-way street out of Russia. There's no possibility to get alternative financing," he said.

But the flip side of that coin is the economic impact the sanctions have had on Europe.

The European Commission estimates sanctions cut EU growth by 0.3 percent of GDP in 2015 at a time when economic expansion was desperately needed. The Austrian Institute of Economic Research found that continuing penalties against Russia could cost more than 92 billion euros, or $104 billion, in export revenue and more than 2.2 million jobs over the next few years. The financial pain is especially acute in Germany, which stands to lose nearly 400,000 jobs due to the sanctions.

And adding insult to the EU's economic injury, the CNAS report this month concluded that modern-day sanctions "do not have a significant effect on the GDP of target countries."

Sanctions "do, however, have a powerful impact on foreign investment, corruption, ease of doing business, governance, and other measures of a country's hospitality to engagement with the international financial community," the report found.

This is probably why many Western officials are re-thinking sanctions' power in lieu of other means to stare down adversaries. In February, U.S. Undersecretary of Defense Christine Wormuth admitted that the sanctions had "not changed so far what Russia has been doing on the ground, and that is the great concern."

Rosenberg, the CNAS fellow, said "it's not the case" that sanctions directly cause GDPs to plummet. She said there is no single, simple way to measure the effectiveness of sanctions, which have also hurt the U.S. economy — although there's no way of knowing how much.

"It's appalling that we've used this set of economic tools so aggressively to go after Russia, a huge global economy, without doing robust modeling of effects and consequences," Rosenberg said.

"There are clearly costs, it's just a matter of if we're willing to pay them."