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Economic Sanctions as a Tool of Foreign Policy: A Critical Analysis of Sanctions on Russia

Dr. Pritam Raj*

Associate Professor, Political Science, LBS Government College Kotputli.

*Corresponding Author: pritamraj.8121983@gmail.com

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ABSTRACT

After Russia invaded Ukraine in February 2022, the United States, the European Union, the United Kingdom, and their allies enacted the most severe sanctions regime ever implemented against any major economy. This paper examines the effectiveness of sanctions as an instrument of foreign policy in this case. A mixed-methods secondary-data approach is used, which includes three methods: a chronology of events based on the main sanctions, a comparison of before-and-after data on macroeconomic variables and forecasts in Russia, and a goal-attainment rubric based on Hufbauer et al. (2007). The findings show that the sanctions exacted costs and affected finance, technology, and energy trades, but the level of resilience of the Russian economy was unexpectedly high, and the political goal to change its course has not been accomplished. Sanctions are thus a means of attrition and signalling, rather than a coercive measure, and their success relies on enforcement and time.

***Keywords**: Economic Sanctions, Economic Statecraft, Russia, Ukraine, Coercion, Weaponised Interdependence.*

Introduction

Sanctions have emerged as the go-to approach used by democracies in reaction to acts of aggression without an outbreak of armed conflict. Sanctions are less costly than war, more powerful than protests, and easier to undertake politically than military action (Baldwin, 1985). The Russian invasion of Ukraine in February 2022 has provided the biggest example of this tool in contemporary times. In just a matter of weeks, Western powers had managed to freeze the foreign currency reserves of the Russian Central Bank, exclude banks from global payment networks, control the export of high-tech goods, and sanction individuals and firms tied to the state (Bown, 2022; Mulder, 2022).

Considering the scale of the action taken, the following question arises: have the sanctions been effective? This depends entirely on what the sanctions were supposed to accomplish. If the objective was forcing Russia out of Ukraine, thus far there are no indications that it has been accomplished. In case the purpose was to make the cost of the war for Russia higher and weaken Russian capabilities while showing determination to act as a unified force, then the picture becomes somewhat different. The aim of this paper is to analyze the matter in light of three main objectives, namely: to explain the logic of sanctions in general and its possible effects.

The case is also theoretically interesting because while earlier cases targeted smaller and isolated nations such as Rhodesia, Iraq, or Iran, Russia is a permanent member state of the United Nations Security Council that possesses nuclear capabilities, is one of the largest exporters of energy and grain, and has been highly integrated into international markets. Whether or not sanctions can be used to compel this kind of economy is thus a question with repercussions far greater than just this particular conflict. The rest of the paper is structured as follows: Section 2 discusses the literature, Section 3 presents the methodology, Section 4 covers the regime, Section 5 covers the economic consequences, Section 6 discusses goal achievement, and Sections 7 to 9 discuss and conclude.

Conceptual Background

Sanctions literature has traditionally split into optimists and sceptics. Galtung (1967) challenged the 'naïve theory' suggesting that economic suffering necessarily leads to political change, because external pressure could consolidate the target government by unifying people against the common enemy. Pape (1997) suggested even wider perspective – sanctions hardly ever accomplish their objectives and early optimism concerning success rate of sanctions was overstated. In contrast, Hufbauer et al. (2007) found that sanctions reached their objective partially in about one-third of all cases from history, and the probability of success increases when the objective is moderate, target is weak, and coalition of senders is wide.

Subsequent research has been concerned less with whether sanctions work, and more with why and under what circumstances. For example, Drezner (1999) found that sanctions are more likely to be successful when applied to an ally or trading partner, rather than a hostile state, because the former is less afraid that concessions may lead to further demands. Drezner (2011), in his later work, suggested that "smart" or targeted sanctions are more politically appealing than comprehensive embargoes but do not necessarily prove to be more effective. Targeted sanctions were presented by Ahn and Ludema (2020) as a means of punishing elites and minimizing damage done to regular people. Baldwin (1985) warned researchers about multiple goals of sanctions, including signalling, deterrence, and symbolism.

Three hypotheses can be formulated based on the existing literature and tested in the following sections. The first hypothesis is that sanctions become more costly for the target because of a broad coalition and economic network control. Second, a big, resource-rich target with other possible trading partners should be adaptable. Third, political objectives concerning a target's security issues should be the most difficult to achieve. All this provides a framework for the examination of the Russian case.

There is, lastly, the question of the architecture of the international economy itself. As Farrell and Newman (2019) point out, the key nodes within networks of finance and technology – which are dominated by the U.S. and its allies – have the ability to weaponize interdependence via denial of access to the network. This is put to the test in the Russian example, as it is a sanctions regime heavily reliant upon control of payment systems, reserve currencies, and advanced components.

Research Methodology

This study employs a mixed secondary-data approach with three analytical pieces, each addressing one aspect of the research question. The first component consists of a chronological content analysis of the principal sanctions measures. Measures were identified using the timeline of the Council of the European Union (2022) and the sanctions chronology provided by Bown (2022). Four types of measures were distinguished: financial measures, measures involving trade and technology, energy measures, and individual designation measures. This piece illustrates the evolution of the sanctions regime.

The second component consists of a descriptive before-and-after time series comparison. Real annual GDP growth rates for Russia and the euro area are compared in the years between 2019 and 2022 using the World Bank (2022) and Eurostat (2022) data, while the initial estimates are compared against the actual outcome using projections prepared shortly after the invasion (International Monetary Fund, 2022). This design cannot estimate causal effect, as there were many other influencing factors besides the sanctions measures. It is employed to check whether the initial predictions of a large negative impact were realized.

Thirdly, there is a rubric assessing the achievement of certain goals according to Hufbauer et al. (2007). Five objectives are evaluated according to their achievement, partial achievement, or non-achievement on the basis of the information collected in the first and second components and secondary materials. All the materials used are publicly available, and no primary data were collected. It is necessary to note the limitations of this research. Official statistics in Russia have become less reliable after 2022, they may be corrected, growth rates are rounded, and the data used are for up to 2022 only.

Evolution of the Sanctions Regime

Analysis of the content indicates that the system has been formed through different stages. The first stage, between the end of February and March 2022, involved the financial sector. The Western countries paralyzed a significant amount of the resources belonging to Russia's central bank in foreign territory, which is normally estimated at around 300 billion US dollars, and also cut off some Russian banks from the SWIFT payment system (Bown, 2022). In turn, the central bank hiked up its policy rate to 20 per cent and imposed capital controls (Itskhoki & Mukhin, 2022).

Phase Two, lasting until 2022, expanded the programme to include trade and technology. Export controls were placed on advanced items such as semiconductors, aviation parts, and other goods in order to limit Russia's industrial-military complex. Phase Three focused on energy exports, which form the core of Russian export income. In December 2022, the EU banned maritime shipments of Russian crude oil and, in February 2022, of refined products; and the G7 countries along with their partners imposed a price cap of $60 per barrel for oil shipped using their transport and insurance services (Council of the European Union, 2022). Individual sanctions against officials, businesspeople, and companies were increasing steadily throughout.

Beginning 2022, emphasis was on implementation and plug loopholes. The EU enacted consecutive packages, making their fourteen up to June 2022, with many of them aiming at third country facilitators and shipping lines to bypass the sanctions (Council of the European Union, 2022). In 2022, G7 also agreed to give loan to Ukraine worth fifty billion dollars from profits of immobilized Russian assets. This is what happens in sanctions regime; once the shock wears off, the battle moves to the target adapting to sanctions and the senders tightening them (Nephew, 2018).

As a result, Russia was the most widely sanctioned major economy, and the number of sanctions in this instance is what sets this instance apart from previous instances. Coordination between the United States, the European Union, the United Kingdom, Japan, Canada, and other allies was another extraordinary aspect of this regime, as it decreased the possibility of the target taking advantage of the divisions between senders. Finally, while the regime depended on national enforcement, the capacity for enforcement varied across jurisdictions. In the end, it is administrative details that determined the effectiveness of any single sanction.

Economic Outcomes

Immediate Impact of Events: Immediate impact was quite hard. In early March 2022, there was sharp depreciation in Rouble, higher inflation and several foreign firms exited from the market. There were predictions for an economic recession, where in April 2022, International Monetary Fund predicted that output in Russia would decline by 8.5 per cent in 2022 and a further decline by 2.3 per cent in 2022.

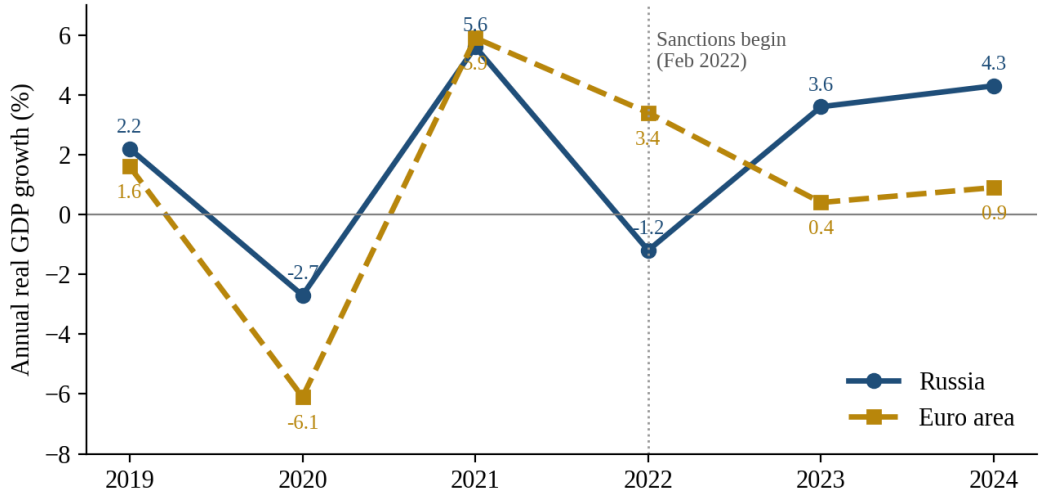


Figure 1: Real GDP Growth, Russia and the Euro Area, 2019 to 2022 (Per cent, Rounded; Initial Official Estimates, Subject to Revision)

Sources: World Bank (2022); Eurostat (2022).

The Russian economy contracted by about 1.2 per cent in 2022, but that was not a significant contraction, and in the following year the economy resumed growing at 3.6 per cent and 4.3 per cent in 2022. Over the same two years, the euro zone, which had been imposing sanctions on Russia and had been facing supply disruptions, had grown relatively slowly. Figure 2 shows a comparison of the early forecasts and actual results.

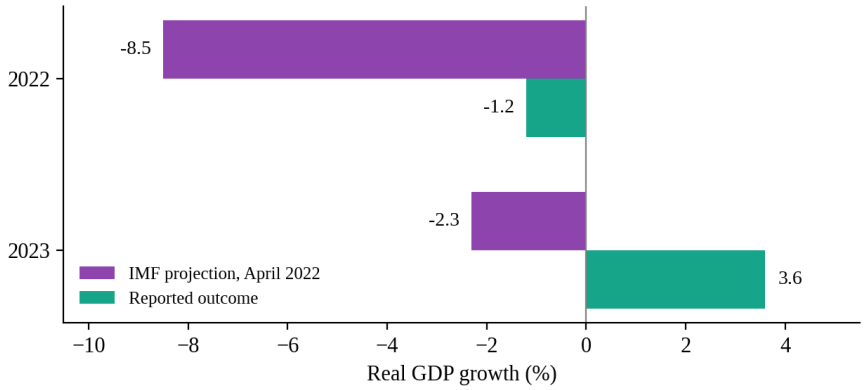


Figure 2: IMF Projections of April 2022 Compared with Reported Russian GDP Growth (per cent).

Sources: International Monetary Fund (2022); World Bank (2022).

The discrepancy between the forecast and results is significant in both years. This can be explained by several reasons. First, Russia's central bank responded rapidly to stabilize the financial sector, the energy exports were diverted to Asian customers instead of being halted, and government spending on defense increased drastically: military expenditures increased by around 24% in real terms in 2022, reaching 109 billion dollars (Tian et al., 2022). Growth based on military production and state orders cannot be considered healthy economic growth and may bring negative consequences in terms of higher inflation, lack of workforce, and underinvestment in the civilian economy. Therefore, the figures presented overestimate the health of the Russian economy, but they prove that sanctions did not lead to a complete collapse.

However, the costs to the citizens and businesses of Russia were very real, and included high inflation, historically high interest rates, and more costly and unreliable access to foreign technology. Worker shortages and decreased investment in non-military industries indicated structural stress underneath the surface numbers. This is the sort of longer-term impact that can be masked by aggregate growth figures, and indicates that the full impact of the sanctions may not come all at once, but gradually.

Goal Attainment

There have been a number of goals for the sanctions imposed on Russia, some of which are not mentioned directly. These are ranked in Table 1, based on the rubric in the methodology. Each cell is colour-coded: green means largely accomplished, amber partially accomplished, and red means not accomplished.

Table 1: Goal-Attainment Rubric for Sanctions on Russia

Objective	Evidence	Assessment
Weaken Russian growth and finance	Output fell about 1.2% in 2022 but recovered in 2022 and 2022	Partially achieved
Restrict military-industrial inputs	Export controls and technology curbs imposed; military spending still rose	Partially achieved
Reduce energy revenue	EU embargo and price cap introduced; exports redirected to Asia	Partially achieved
Compel change in Russian policy	War continued; no withdrawal	Not achieved
Maintain unity and signal resolve	Successive packages adopted by the coalition	Largely achieved

Source: Author's assessment adapted from Hufbauer et al. (2007).

The rubric clearly shows that sanctions were most effective in terms of their ability to maintain cohesion between senders and demonstrate resolve, as well as impose costs on finances, trade, and technology. They were least effective as a means of political pressure that could lead to altering Russian behavior. It fits into Pape's (1997) view that threats and coercion cannot be effective in case of a determined adversary who pursues security objectives and Drezner's (1999) assumption that sanctions fail because targets resist.

There are limitations to the rubric itself. The ratings are subjective assessments rather than objective measurements, and people tend to interpret the evidence differently. Objectives that have never been stated explicitly should be inferred from the evidence provided. Therefore, the rubric is best used as a summary of evidence that can be structured using the criteria provided above.

Evasion, Third Countries, and Costs to Senders

Sanctions are effective only up to the point where the coalition that imposed them is big enough, and the implementation of those sanctions is effective. Large economies such as China, India, and Turkey have not joined the programme of the Western coalition. For instance, India started buying cheap Russian oil which covered much of their total oil imports, and intermediaries in several countries bought restricted items using alternative channels. This makes sanctions less effective and illustrates the inefficiency of weaponised interdependence when there are alternative networks available (Farrell & Newman, 2019).

There are also costs associated with sanctions for senders. The European economies experienced a dramatic increase in energy prices in 2022, while the absence of Russian gas led to swift restructuring of the energy supply system. Sanctions can also encourage the recipient to build more connections with other economies which will result in the development of parallel payment systems and other trade relations that will reduce the leverage of the sanctioning coalition over time. According to Dreger et al. (2016), oil prices and sanctions have had an effect on the rouble in 2014.

Russia adapted in multiple ways that became obvious. The transportation of oil through export was done via a shadow fleet of ships that worked outside the jurisdiction of the Western insurance and shipping industry, which became a target for the European Union from 2022 onwards (Council of the European Union, 2022). Parallel import of goods through third countries helped to overcome the restrictions on export, and there were also changes in the form of currency that could be used for the payment. Each of the mentioned adaptations cost more to Russia than regular transactions.

Discussion

The data suggest three things. First, sanctions are slow tools. The shock at the start was strong, but the target adjusted in months, and its impact requires persistence over many years rather than in one stroke. Second, to evaluate sanctions based on the policy reversal alone is not sufficient. Following Baldwin (1985), sanctions are also meant to restrain capabilities, convey values, and solidify coalitions, where the track record is more favorable. Third, effectiveness is conditional on structure. Control over finance networks provided Western governments the power to sanction, but the presence of large non-participants constrained it.

For policy-makers, this means that expectations need to be set. Sanctions need to go hand-in-hand with military and diplomatic policy as opposed to being a replacement, there is a need to give equal consideration to enforcement versus new designations, and there is a need to recognize the humanitarian and economic impact on the sender and the bystander countries. For scholars, this means that future research needs to make use of micro-data, such as firm and trade flow data.

Conclusion

Since 2022, sanctions levied against Russia have been some of the most extensive imposed against any big economy and they have disrupted the financing, technology, and energy sectors greatly. However, they have not resulted in the economic failure that many had foreseen and have not altered the strategic course followed by Russia. Instead, the lessons to be learned should be viewed from a perspective of limited success. They have been effective in sending signals and ensuring coalition unity, moderately successful at limiting capabilities, and unsuccessful in pressuring an obstinate opponent. Sanctions can be used effectively in diplomacy, but as part of a larger plan with clear objectives and cooperation.

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