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Sanctions, cooperation, and innovation: Insights into Russian economy and implications for Russian firms

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Abstract

The aim of this paper is to reveal the effects of sanctions at the firm level, with the special attention to cooperation and innovation activity of sanctioned firms. Specifically, the differences between domestic and international companies in their ability to adapt to the sanctions in terms of their cooperation with partners and capability to innovate are discussed.

The study argues that firms operating in international markets tend to prioritize product innovation and entering new markets to overcome negative consequences of sanctions. In addition, they are more likely to improve their products and to find new markets to compensate for losses and fill their unused capacities.

An important finding having both managerial and political value is that operating in the international market may not necessarily provide an advantage in terms of new partners in the local market but rather facilitate the search for new foreign markets. Inviting the government to provide assistance for Russian domestic and international firms on an equal basis, we admit that with varying degrees of control and interest in national firms, the Russian government can help sanctioned companies in different ways, regardless the scale of their internationalization.

The study contributes to the literature on the impact of economic sanctions at the firm-level and in the context of the domestic market of the sanctioned country.

Keywords: economic sanctions, international firms, cooperation, innovation, Russia.

JEL: F02, F23, F42.

Introduction

Economic sanctions are a foreign policy instrument commonly used by governments to influence the decision-making process of other countries (Oxenstierna & Olsson, 2015).

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There are consolidated studies on the effects of sanctions on the macro level, but with the new realities of the last decade of the 21st century, the impact of sanctions on organizations attracts more attention. In the context of the transition from global economic sanctions deteriorating the living conditions of innocent citizens to "smart" sanctions targeted at selected individuals, organizations, and sectors (Ahn & Ludema, 2020), the importance of understanding their consequences for companies has increased significantly.

Companies operating under sanctions seek to mitigate their negative effects. Understanding the impact of sanctions on different types of companies would shed light on how companies should react to sanctions and how they can leverage their international operations, which were not profoundly studied before in the business and management literature.

In order to fill the respective research gap, this paper aims to discuss the consequences of sanctions at the firm level, with special attention to the implications for cooperation and innovation of sanctioned firms. Specifically, the differences between domestic and international companies in their ability to adapt to sanctions in terms of their cooperation with partners and attitude to innovations are discussed. The study argues that firms operating in international markets tend to prioritize product innovation and entering new markets to overcome the negative consequences of sanctions. In addition, they are more likely to improve their offers to clients and find new markets to compensate for losses and fill their unused capacities.

1. Impact of economic sanctions on countries and organizations

Economic sanctions are a foreign policy instrument commonly used by the West to express disapproval of countries that violate international law (Oxenstierna & Olsson, 2015). Sanctions usually lead to a country's withdrawal from customary trade and financial relations for the purposes of foreign and security policy.[1] They can also be used by countries to penalize nation states, institutions, or individuals who do not follow the rules or agreements between the nations (Lin, 2016). Economic sanctions may include all measures that do not involve the use of armed forces and that are applied to give effect to decision-making. Specific measures are chosen according to the pursued goal and can range from comprehensive economic and trade sanctions to more targeted measures, such as travel bans and arms embargoes. Economic sanctions can also be divided into two major groups — individual sanctions and sectoral sanctions (Milutina, 2018). Individual sanctions are restrictive measures that are imposed on certain groups of people or companies, while sectoral sanctions are imposed on certain sectors of a country's economy.

The effect of sanctions can be analyzed at the organizational (firm) and global (country) level. The major studies devoted to the analysis of sanctions' effects are conducted at the global level. This is due to the difficulties of selecting and extracting data sufficient to

[1] https://www.cfr.org/backgrounder/what-are-economic-sanctions

conduct an analysis at the firm level, mitigate the impact of other factors, and generalize the results due to the very individual nature of each case. Additionally, the major focus of the economic sanctions of the previous decades was on global measures.

In addition to the fact that economic sanctions lead to unfavorable economic circumstances for the targeted country, they can also result in serious conflicts and wars. The most discussed examples of economic sanctions include those against Cuba in 1960, Iran in 1979 and 2003, Iraq in 1990, North Korea in 2006, Russia in 2014, and Venezuela in 2018. A common trait of imposing economic sanctions is a comprehensive trade embargo. However, the goal pursued and results are different in each case.

The following examples present the evolution of measures applied by some countries to sanction others and prove the current trend on using *smart sanctions* (Ahn & Ludema, 2020). The significant deterioration of the impact of previous methods of sanctioning on the population as a whole and the lack of successful results in achieving the primary goal have led to the popularity of smart sanctions targeting individuals, entities and sectors while minimizing collateral damage. The nature of sanctions at the entity level (individuals and organizations) has emerged as a leading policy in the last two decades, but has not received due attention among scholars.

2. Retrospective and specifics of economic sanctions imposed on Russia

The geopolitical conflict between Russia and Ukraine triggered the condemnation of the international community, which later led to the imposition of a range of sanctions against Russian individuals, entities, and sectors by the United States (US), the European Union (EU), and several other states. Although the actions were imposed after Russia's annexation of Crimea, the US authorities claim that the reason for sanctions is Russia's international behavior, specifically, interference in elections, malicious activities in cyberspace, human rights violations, the use of chemical weapons, proliferation of weapons, illicit trade with North Korea, and support for Syria.[2]

Since March 2014, the US, the EU and their allies have been progressively introducing restrictive measures against Russia. One way to look at these sanctions is to consider them in accordance with the implied measures (Christie, 2016). Firstly, the sanctions limit access to foreign capital for designated Russian companies in the banking, defense, and energy fields. Secondly, they restrict the import of high technologies in the oil explorations and production sectors. Finally, they are imposed in the form of an embargo on the export of certain military and dual-use goods to Russia.

The sanctions against Russia can also be analyzed by splitting them into two groups: sanctions against individuals and entities, and sectoral sanctions (Milutina, 2018). The first group is characterized by sanctioning people who threaten the political stability and

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2 https://crsreports.congress.gov/product/pdf/R/R45415?__cf_chl_jschl_tk__=pmd_xm3E5aXoYwSF5CxIWK5VCjQKdVjIfK291dHJVkEyApM-1632391569-0-gqNtZGzNAiWjcnBszQhR

integrity of Ukraine. This group implies a restriction on entry for persons included in the above-mentioned list, freezing of their assets, and a ban on business relations. The second group is sectoral sanctions, which limit the ability of major banks and companies in Russia to receive foreign financing. This group is mainly aimed at jeopardizing the sectors of the Russian economy. Key figures and industries in Russia are facing much more stringent and unpredictable conditions than ever before (Gould-Davies, 2018).

Companies directly or indirectly owned by people who were involved in the conflict in Ukraine faced limited access to capital markets, export bans and restriction on certain technologies and services. If a person subject to sanctions owns more than 50% of the entity, the company also becomes the target of sanctions. The US Department of the Treasury's Office of Foreign Assets Control (OFAC) prohibits any transactions with persons (state officials, heads of key state companies and major private companies) and entities designated in the Specially Designated Nationals and Blocked Persons List (SDN List). The EU also imposed different types of restrictive measures on individuals and companies, which began with the first travel bans and asset freezes on March 3, 2014.[3] However, in contrast to the US, which targets foreign entities that violate US sanctions against Russia, the EU sanctions against Russia apply only to EU citizens and EU-registered companies. The EU imposed restrictions on economic relations with Crimea and Sevastopol through bans on import and export of goods, restrictions on trade and investments, as well as a prohibition on providing tourist services in these locations. The negative effect of the economic sanctions on trade depends on the level of involvement of countries as a whole (Caruso, 2005). That is why the countries imposing sanctions are trying to engage more countries to participate. For example, the United Nations (UN) sanctions are considered to have a stronger adverse effect than the unilateral US sanctions (Neuenkirch & Neumeier, 2015). Given the US persistence in increasing the severity of the sanctions against Russia, a long-term and constantly growing scope of sanctions was expected.

The second group of economic restrictions is sectoral sanctions. On July 16, 2014, OFAC created a new Sectoral Sanctions Identifications (SSI) List, which authorized sanctions against certain sectors of the Russian economy, including financial services, energy, mining, as well as defense and related materiel sectors.[4] It restricts short-term financing to the financial services and energy sectors (and has since further tightened the permissible loan maturity to 14 days for financial services and 30 days for energy). The sectoral sanctions imposed by the US and the EU include limited access to the EU's primary and secondary capital markets for certain Russian banks and companies, as well as some sensitive technologies and services that can be used for oil production and exploration, a ban on the export and import of arms trade, and a ban on the export of dual-use goods for military use or military end users in Russia. In 2017, the sectoral sanctions

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[3] ttps://eeas.europa.eu/sites/default/files/eu_restrictive_measures_in_response_to_crisis_in_ukraine_eng_web.doc.pdf

[4] https://www.skadden.com/insights/publications/2015/01/sectoral-sanctions-add-new-layer-of-complexity-to

against the railway, metallurgical and mining sectors were imposed in accordance with the Countering America's Adversaries Through Sanctions Act (CAATSA).

In addition to direct sanctions against individuals, organizations and sectors, there are measures that deteriorate international cooperation. Countries introduce various diplomatic measures and restrictions on economic cooperation with Russia and its entities. For example, the EU-Russia summit in 2014 was canceled and a G7 meeting was held in Brussels instead. New agreements between the EU and Russia, as well as negotiations on Russia's joining the Organization for Economic Cooperation and Development (OECD) and the International Energy Agency (IEA) were suspended (Council of the European Union, 2019).

According to numerous experts and policy-makers, sanctions will continue to strengthen. While the EU states that Russia must fully implement the Minsk agreements in order to lift the sanctions, the US demands are less obvious. On April 6, 2018, the US launched another wave of sanctions, designating the reason as "in response to worldwide malign activity."[5] The Treasury Department added that "Russian oligarchs and elites who profit from corrupt system will no longer be insulated from the consequences of their government's destabilizing activities."[6] Thus, it is unclear what actions Russia can take, in particular, in order for the sanctions to be lifted. Moreover, while the EU needs to unanimously extend the sanctions every six months, the US has passed the law named Countering Russian Influence in Europe and Eurasia Act of 2017 (CRIEEA) which transfers substantial powers to impose, ease and lift sanctions from the President to Congress. Russia was exempt from the Jackson-Vanik amendment, which affected the US trade relations with countries with non-market economies which restricted freedom of emigration and other human rights, only for 38 years (Gould-Davies, 2018). The cases of the US sanctions against Cuba and Iraq show that economic restrictions can remain imposed for decades if the targeted country resists meeting the requirements. Potential negative harm to Cuba was mitigated with the help of the Soviet Union. The confrontation and the lack of interaction between the market and planned economies also reduced the effect of sanctions imposed by the US against Cuba. In the current context of globalization, economies are more connected and negative effects of isolation are much stronger. Given the high complexity of the process of lifting sanctions by the US authorities, no changes can be expected in the short run.

While sanctions are popular restrictive measures and are commonly applied against post-socialist countries, the sanctions imposed in 2014 represent the first such case since the Cold War and the collapse of the USSR in 1991 (Oxenstierna & Olsson, 2015). The example of the introduction of the current economic sanctions against Russia is comparable to other comprehensive sanctions programs, e.g. as in the cases of Iran and Cuba, although there are certain complexities that should be emphasized in the case of Russia, for instance, turning sanctions against Russia into a law, introducing a new type of

[5] https://crsreports.congress.gov/product/pdf/R/R45415?__cf_chl_jschl_tk__=pmd_xm3E5aXoYwSF5CxIWK5VCjQKdVjIfK291dHJVkEyApM-1632391569-0-gqNtZGzNAiWjcnBszQhR

[6] Ibid.

sectoral sanctions that were not frequently used before, and stating unclear conditions for lifting the sanctions. It is also obvious that the United States limit the options for Russian companies to perform successfully on the global arena. However, being a more significant partner for Russia, the EU is in no hurry to terminate all economic contacts with Russian entities. Still, while the EU lost less than 0.2% of its value added and employment from 2014 to 2017, Russia's GDP fell by 2.4 percentage points (Gurvich & Prilepskiy, 2015). The situation is unlikely to change in the near future, and Russian companies need to be ready to respond to the intensified economic sanctions.

The economic sanctions against Russia could not remain unanswered. It is interesting that the groundwork for Russia's *countersanctions* was laid in January 2010 when the food security doctrine was signed (Korhonen et al., 2018). This program sets targets for domestic production of basic foodstuffs, such as potatoes, dairy products, grain, and meat. It was formulated in the action plan, Agricultural Development Program 2013–2020, in 2012, and also extended to other sectors within the framework of the "Government Program on Industries and Competitiveness" in April 2014. The first trade restrictions with the US were introduced in December 2012, after the Sergei Magnitsky Act, limiting the maximum possible amount of imported beef, pork, and poultry.[7] Later, when the act became the law, the Russian parliament also voted to ban the adoptions of Russian children to the United States and extended sanctions to travel prohibitions for certain citizens. After the Ukrainian crisis, the economic countersanctions intensified against more individuals and banned the import of agricultural products from countries imposing sanctions on Russia, starting with the EU, the US, and Turkey in July 2014. The Russian government began to introduce different measures to decrease the import-dependence in different fields, for example, in the mining industry (Vorotnikov et al., 2019).

Since the introduction of Western sanctions, Russia has started investing in the upgrading of its sanctions defenses (Kluge, 2019). The government develops its sanctions policy in such a way as to minimize costs for domestic interest groups, including organizations (Bělín & Hanousek, 2021). In addition to the import substitution policy, it has established a national payment system and a respective credit card "Mir." A specialized bank without the US exposure was created to serve sanctioned firms — Promsvyazbank, which removes "toxic" assets from the balance sheets of banks with the extensive international operations. The introduction of a floating exchange rate of the Russian ruble in November 2014 served as a buffer against sanctions related risks, and the devaluation of the currency helped the Central Bank to replenish its reserves. In addition, sanctions and strained relations with the US led to mutually expelling mission personnel and closing of consulates and chanceries. In April 2018, President Putin signed a law authorizing restrictions related to trade with the US and other unfriendly countries, as well as banning foreign access to Russian public procurement and privatization.[8]

The effect of economic sanctions is a complicated indicator to measure. It is very difficult to disentangle the impact of sanctions from other factors influencing the ultimate

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7 Ibid.

8 Ibid.

socio-economic environment. The cumulative effect of fluctuations in oil prices, which is the main export product and a source of revenue for the Russian government, as well as underperformance of the Russian economy, political uncertainty, and economic sanctions led to a deep recession in 2014–2015 and a number of serious problems, such as the depreciation of the Russian ruble, inflation, collapse of investor sentiment, falling of foreign exchange reserves and an increase in the budget deficit.[9] Several studies even claim that the negative impact of low oil prices on the Russian economy is three times greater than the effect of sanctions (Stout, 2017; Korhonen et al., 2018; Kholodilin & Netsunajev, 2019). It also significantly reduced the purchasing power of the population (Christie, 2016). However, the rise in oil prices in 2016 helped the economy to exit its two-year recession.

Therefore, even with many other factors determining the unfortunate situation in the Russia's economy, the effect of sanctions cannot be neglected. First, there is a significant negative effect of economic sanctions in the long run (Mirkina, 2018). This decreases the trade flows and deteriorates other economic outcomes, such as policy indicators or consumer welfare (Bělín & Hanousek, 2021). Secondly, sanctions create new realities in which companies need to operate. For example, it is expected that restrictions on access to Western technologies will impede the modernization of Russian oil companies.[10] According to policy-makers, Western sanctions will dry up foreign investment and credit, hitting large and small businesses in the short run, and will cost Russia's economy 0.2% of annual economic growth in the long run due to lost business opportunities, underinvestment in infrastructure, and a slowdown in modernization.[11] Thirdly, the analysis of various cases of sanctions imposition and the opinions of experts raise concerns about the possibility of lifting the sanctions in the short term. The head of the International Department of the Russian Energy Ministry, Roman Marshavin, said at the Fort Ross Dialogue conference in May 2018 that "US sanctions against Russia, Iran and Venezuela have an economic subtext, and are, in essence, part of a struggle for the global gas market" (Interfax, 2018 May 23). All the above supposes that the sanctions can last for a long time. Finally, given the fact that sanctions are most likely to be effective when they are multilateral, comprehensive, and target a regime that is economically vulnerable (Hufbauer et al., 2007), it is expected that tougher measures will be applied by different players, and more industries will be subject to sanctions.

3. General consequences of sanctions

Smart sanctions, which are currently a very popular tool of international policy, led to a strong negative effect on individuals and entities of the Russian economy. One fifths

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[9] Ibid.

[10] Ibid.

[11] https://www.washingtonpost.com/world/europe/russia-keeps-getting-hit-with-sanctions-do-they-make-a-difference/2018/08/21/f466db1c-a3ec-11e8-ad6f-080770dcddc2_story.html

of the 100 largest firms in Russia are direct subjects of the US sanctions. They have already lost on average about a quarter of their operating revenues, more than half of their asset values, and about a third of their employees compared to their non-sanctioned counterparts (Ahn & Ludema, 2020; Stout, 2017). In this context, it is very important not only to analyze the global effects of sanctions, but also to consider the consequences for the country's domestic and international firms.

Given the evidence that domestic companies lag behind their international counterparts in terms of performance and competitiveness (Shukla, 2015), it would be worthwhile to compare the two groups of firms' ability to resist the negative impact of sanctions. For example, exporters are more capital-intensive, productive, and able to survive downturns in the economy than non-exporters (Cassiman & Golovko, 2010; Fernandes & Isgut, 2015; Puig et al., 2014). They have easier access to knowledge and information from foreign markets, which, in turn, may result in enhanced innovations, reduction of costs and improved quality of products (De Loecker, 2007; Ermolaeva et al., 2018). By contrast, domestic corporations may have better risk-adjusted market performances than multinational corporations (Michel & Shaked, 1986).

By choosing the method of product innovations within or outside the company, the organization can significantly reduce the costs of operations, thus improving its market position. Additionally, business model innovations are crucial for success in unsettled markets where traditional revenue and pricing models are not applicable (Teece, 2010). Business model innovations are tightly coupled with the opportunities that exist for the companies and can assist them in finding new partnerships.

Russian sanctioned firms experience significant limitations in access to suppliers, financial resources, customers, and technologies. They are also restricted in creating new partnerships, which, in turn, pushes them to accept the assistance of the government (Panibratov & Michailova, 2019). Previous collaborations enhance the adaptability of alliances: companies foster their own current cooperation with established partners (Bělín & Hanousek, 2021). Moreover, companies that operate in foreign markets are expected to have less difficulties in overcoming obstacles stated above and, therefore, experience fewer negative effects from the sanctions compared to companies operating only in the domestic market. Access to international markets increases their chances of finding a substitution for the no longer available resources and partnerships, thus improving their resistance to the unfavorable economic situation in the country.

The main consequences of sanctions can be grouped into two clusters: cooperation and innovations. The first group, cooperation, can be viewed through relations with suppliers, customers, financial institutions, and the government. The loss of certain partnerships is expected to push the company to look for new agreements in Russia and abroad. The government also plays a significant role in mitigating the effects of economic sanctions. It can provide direct support to the company (e.g. governmental orders, subsidies and loans), as well as create an environment in which the company compensates for losses through entering new agreements. The deterioration of international cooperation is expected to have a long-term effect on the performance of the company and lead to entering a new agreement.

The second group, innovations, is represented by changes that happen to the company in the field of innovations: product innovations, business process innovations, and the internal environment of the company influencing the creativity of employees. This aspect of Russian companies' activities is significantly influenced by sanctions due to restrictions on the import of technologies and concurrent import substitutions policies. Innovations are globally recognized as one of the main tools for improving competitiveness of the company. During economic sanctions, innovations can become a source of mitigating negative effects and increasing productivity. In turn, employees make a significant contribution to the company's success, and their creativity can become a source of future improvements. These two groups of changes are discussed in the latter part of the paper on the example of Russian firms.

4. Prospects of cooperation

One of the most affected aspects of a company's activities during sanctions is cooperation with foreign partners: suppliers, customers (Ahn & Ludema, 2020), and investors (Mirkina, 2018). The role of the government is also subject to changes during sanctions, as it starts to play a significant role in mitigating the effects of the sanctions on companies (Gibson, 1999). Since 2014, Russian companies have also been facing new realities that force them to quit partnerships. Companies are entering new local and foreign markets to mitigate the negative effect of lost agreements (Golikova & Kuznetsov, 2017). They also need to look for new partnerships in the field of supplying good and services in Russia and abroad (Vorotnikov et al., 2019). In addition, the economic sanctions have cut off Russian companies from the global economic and financial system (Gould-Davies, 2018). Companies are isolated from global payment systems and have difficulties obtaining credit lines. In its turn, the government is introducing new mechanisms to help companies overcome the consequences of the sanctions, such as facilitation of the issuance of loans or tax reduction. Companies often turn to the government for help in acquiring and managing resources (Panibratov, 2016), stimulating innovations (Chandran et al., 2013), and creating an environment that allows them to build new partnerships. During the period of sanctions, the role of the government increases dramatically.

The reverse effect of economic sanctions encourages companies to find new suppliers, customers and investors and to form new agreements (Milutina, 2018). New partnerships can be established both within the state border and in other markets. Moreover, previous collaborations can enhance network adaptability (Bělín & Hanousek, 2021). Companies are trying to mitigate the negative effect of the sanctions on alliancing capacity via indirect exports through the nearest neighboring countries (Crozet et al., 2021). The priority markets for Russian companies during the sanctions are the BRICS countries, the EAEU, as well as Central and Southeast Asia (Babkin & Baikov, 2017). Government agreements between Russia and other countries that are "neutral" in relation to sanctions or a part of "neutral" states facilitate the process of building new or alternative business relationships.

Although partnerships can become a reliable alternative to a deteriorated business relationship and bring high potential gains, Russian firms face additional costs and risks. The potential problem is the increase in direct and indirect costs (Stout, 2017) and transaction costs (Hennart, 2010; Williamson, 1993). A company that is subject to economic sanctions may lose negotiating leverage due to the lack of available options for alternative partnerships, which, in turn, leads to less favorable conditions of agreements. Geographic distance can increase logistics costs, while difficulties in doing business in a new country can lead to additional spending on marketing and related activities. Additionally, new suppliers may provide products and services of lower quality or request a higher price for the same supply. Failure to find a proper substitution can increase the costs of production, reduce the consumption of the company's goods or services, and even contribute to displacing the company from the market (Ahn & Ludema, 2020). At the same time, the previous experience of firms in the sanctioned country significantly mitigates the impact of sanctions (Crozet et al., 2021).

Sanctioned companies may experience a loss of opportunity cost. This effect works not only for the sanctioned country, but also for those that imposed the sanctions. For example, between 1975 and 1989, when the US imposed sanctions against the USSR, American companies could earn approximately USD 5.5 billion (USD 15.4 billion in 2019 dollars) by maintaining trade relations with the USSR (Stout, 2017). Due to the US embargo on Russian oil equipment (1975–1989), losses of the US companies were estimated in the range of USD 1,54–2,0 billion (USD 4,6–6,0 billion in 2021 dollars). Economic sanctions can also force the company to withdraw from certain joint ventures. For example, ExxonMobil, the world's largest energy company originated in the US, slowed down and then terminated working on many projects with a Russian counterpart.[12] The economic sanctions against Russia also put GAZ at risk in a way that affects contracts with German carmakers Volkswagen and Daimler, as well as the US based firm Cummins, Inc.[13]

Economic sanctions can also lead to changes in the cost of capital, production capacity, equity prices and employment (Stout, 2017). The effect of economic sanctions on organizations leads to a loss of production opportunities, which, in turn, can result in unused capacity, increased cost due to reduced economies of scale, increased cost of capital due to sales losses and lowered rates of return, as well as higher borrowing costs. The economic sanctions against Russia also affect companies established in other countries (Abramova & Garanina, 2018). ExxonMobil experienced a significant decrease in stock valuation of the company.[14] The effect on other indicators was not that obvious, but was expected due to the limited time frame available at the time of the investigation (Stout, 2017). Another example is the overall impact of economic sanctions on American companies in connection with the introduction of sanctions against the USSR following

[12] https://www.reuters.com/article/us-exxon-mobil-russia-rosneft-oil/exxon-quits-some-russian-joint-ventures-citing-sanctions-idUSKCN1GC39B

[13] Ibid.

[14] Ibid.

the invasion of Afghanistan (1980–1981). The harm to the US business was estimated at USD 80 million in annual revenue from technology and USD 200 million from other chemical related items.

Another consequence of the introduction of sanctions for business is damage to the brand image. For example, 12 McDonalds restaurants in Russia were accused of violating sanitary standards and temporary closed in 2014. It was viewed by some experts as retaliation for the economic sanctions and tarnished the image of the company (Stout, 2017). Foregone profit due to the lack of presence in the business leads to the loss of the company's visibility in the country and competitive advantages. Owing to the unfavorable economic environment in Russia, the soft drinks producers' brands Pepsi-Cola and Coca-Cola closed or partially suspended their operations in the Russian market. For the US firms, this can lead to the loss of not only the revenue stream, but also the market share that can be seized by a competitors' business.

One of the major negative effects of sanctions is the loss of access to foreign inputs (Abramova & Garanina, 2018). Companies are forced to look for new suppliers of goods and services in other markets to compensate for losses. It is expected that companies operating in global markets experience less difficulties in getting an access to new foreign resources than those operating only domestically as they have wide external network and experience in forming new partnerships (Wang & Lam, 2019). They also possess practical knowledge and experience of operating in different markets and have an advantage in organizing the logistics process in different countries. On the contrary, companies that do not operate in various international markets are less competitive and more vulnerable to changes in the supply of goods (Panibratov, 2016). Competitiveness and ability to adjust to a changing environment can help the sanctioned companies to conclude new supply contracts with foreign partners. However, the companies have equal chances to find new suppliers in the local market. Thus, it is expected that companies operating internationally are more flexible when shifting to other foreign markets than those operating only domestically. However, they have no advantages in entering into new agreements in local markets.

The economic sanctions against Russia also influence the relations of Russian companies with their foreign partners in the supply sector. Companies face bans in trade relations with different countries and are not able to procure technologically advanced products. Companies operating internationally are more flexible to enter onto new agreements in foreign markets, but they are not at the forefront in terms of entering into new agreements with local partners. However, it is important to emphasize that, on average, companies admit that it is challenging to find a proper substitute in the Russian market (Vorotnikov et al., 2019). Despite the fact that import replacement opened up new opportunities for finding a substitution in the local market, this policy had its limits, since some equipment had never been produced in Russia before, and it requires some time to launch manufacturing. Thus, due to the difficulties in finding suppliers in the local market, companies are forced to look for new markets abroad (Panibratov & Michailova, 2019).

Based on the above considerations, we can assume that differences in the conditions of doing business for Russian firms operating in Russia are minor, and therefore we suggest:

Proposition 1a: Russian sanctioned companies operating domestically experience the same difficulty in replacing suppliers at home as Russian sanctioned companies operating internationally.

Emphasizing the importance of international experience and the ability to adjust to changes in uncertain market conditions, the second proposition is:

Proposition 1b: Russian sanctioned companies operating domestically experience more difficulties in replacing suppliers in foreign markets than Russian sanctioned companies operating internationally.

Sanctioned firms experience difficulties while operating in countries that have imposed sanctions which changed relationships with customers. To utilize unused capacities and maintain production, companies may decide to enter new domestic markets. Although it is important for companies to focus on enhancing sales on domestic markets, they can also benefit from expanding operations in foreign markets (Milutina, 2018). Companies that already operate abroad possess knowledge and reputation, have developed value chains and can adapt to external changes faster than firms operating only domestically (Hennart, 2010). This provides them with an advantage in performing in foreign markets and increases their chances of successfully entering new markets, mitigating risks and protecting the company from sanctions. International experience gives companies an advantage in the speed of adapting logistics processes and increasing brand awareness in other markets. Even if a company is forced to leave certain markets and stop supplying its products or services to certain countries, it still has a structured supply chain and knowledge to do business internationally. Given these advantages and higher competitiveness, international companies are more likely to apply their unused capabilities in other foreign markets than domestic companies.

The economic sanctions imposed against Russian firms lead to a ban on operations with many important markets. Although international and domestic Russian companies have equal chances to expand domestically, the decrease in purchasing power and shrinking demand in Russia create difficulties in compensating for losses locally (Ahn & Ludema, 2020). Instead, companies may seek to enter new foreign markets, such as BRICS, the EAEU, as well as the countries of Central and Southeast Asia (Babkin & Baikov, 2017). Companies with experience of working in other markets have an advantage when entering new markets because of their experience and obtained knowledge.

Following this logic, here are the next two propositions:

Proposition 2a: Russian sanctioned companies operating domestically experience the same difficulty in finding a replacement for consumer markets in Russia as Russian sanctioned companies operating internationally.

Proposition 2b: Russian sanctioned companies operating only domestically experience more difficulties in finding a replacement for consumer markets in foreign markets than Russian sanctioned companies operating internationally.

One of the main direct effects of economic sanctions on companies is the restriction of access to foreign capital. The impact of sanctions on foreign investment may change over time, depending on the cost of sanctions and the initiator of sanctions (Mirkina, 2018). Interestingly, although sanctions have a negative effect on some firms' indicators in the long run, cross-border financial flows suffer a strong and immediate negative effect. However, in any case, this limits the ability of companies to receive financing. Turning to other markets in search of new sources of financing, firms may face higher costs, unfavorable transaction terms and increased dependence on fewer investors. Better credibility in the global market, experience in attracting financing and higher transparency of their financial activities allow international companies to have more favorable conditions for entering foreign financial markets via reducing the indirect costs of creating new partnerships.[15] However, international and domestic companies of the same nationality can equally benefit from financing in local markets.

For many Russian firms, access to external financing from the US, the EU, and their allies has been limited since the third quarter of 2014, while the gross foreign debt, especially the banks' foreign debt, decreased by about USD 210 billion in the period 2013–2017 (Korhonen et al., 2018). The cross-border bank lending declined by just over 50%, and the average FDI flow dropped from USD 54.5 billion per year in 2013 to USD 7 billion per year in 2015. In 2016, the FDI flow began to increase, but the FDI net inflow was still much lower than the pre-sanctions level. FDI strategy makes firms more competitive in the market and helps maintaining higher effectiveness (Fedorova et al., 2018). Thus, an increase in inward FDI from new markets can diversify risks and help companies to withstand negative consequences of sanctions. Accordingly, Russian firms operating abroad may have better chances to attract foreign capital as they have experience of operating abroad, a stronger brand and image, and transparency in their operations.

Financial sanctions against Russian state-owned and state-controlled banks adjust their international and domestic risks (Mamonov et al., 2021). First, banks that are anticipating debt sanctions are raising international borrowings (especially in Moscow). Accordingly, they are decreasing their foreign assets (especially if they are located farther from Moscow). Second, banks that could have expected asset sanctions cut own international borrowing and sold foreign assets in advance (Mamonov et al., 2021). Sanctions stimulate the return of capital to Russia as leverage to reduce investments of foreign firms.[16] The government introduces new initiatives aimed at encouraging local businesses to repatriate their capital and creating a favorable investment climate, e.g. tax breaks for Russian citizens who become local tax residents. Companies operating locally are expected to have the same leverage and conditions of receiving financing in home markets as companies operating internationally. Based on the above observations, the next two propositions are as follows:

Proposition 3a: Russian sanctioned companies operating domestically experience the same difficulties in finding a replacement for financing in Russia as Russian sanctioned companies operating internationally.

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15 https://www.americanexpress.com/en-us/business/trends-and-insights/articles/advantages-international-trade/

16 https://www.themoscowtimes.com/2017/12/27/putin-tries-to-lure-1-trillion-home-as-sanctions-fear-grows-a60061

Proposition 3b: Russian sanctioned companies operating domestically experience more difficulties in finding a replacement for financing in foreign markets than Russian sanctioned companies operating internationally.

The government not only plays a key role for firms in emerging economies in general, but may also be of critical importance in mitigating the negative effects of economic sanctions on national firms (Panibratov & Michailova, 2019). It can either assist them directly through subsidies, loans, and governmental contracts, or create conditions in the market that would provide firms with new opportunities. Companies that have lost their access to Western markets and have not found a replacement are seeking for government money, partnerships with the state, and other types of assistance that the government can provide them.[17]

The government can help companies to offset losses by offering them governmental contracts. On the one hand, it helps businesses that experience difficulties to realize their potential. On the other hand, it can ruin the competitive climate in the country. For example, in order to "shield" (Ahn & Ludema, 2020) the sanctioned Bank Rossiya, the Russian government granted the bank an exclusive contract for servicing the domestic wholesale electricity market amounting USD 36 billion.

The lack of access to financial resources in the foreign market can cause auxiliary flows from the government in the form of subsidies and loans (Mirkina, 2018). Although this practice is very popular due to its simplicity and high speed of implementation, it shifts the negative impact of sanctions on the government and leads to the depletion of state financial resources. For example, from 2015 to 2017, the Industrial Development Fund allocated loans totaling about RUB 250 billion (around USD 4 billion) in various projects, primarily in the automotive industry, agricultural, special and mining machinery (Vorotnikov et al., 2019). To offset the losses from the sanctions, VTB Bank received USD 5,4 billion in state financial assistance.[18]

The government can not only directly help companies but also create an "ecosystem" in which firms can find their own way to mitigate or overcome sanctions. Simplifying the process of creating partnerships with other countries, signing framework agreements that facilitate the process of doing business in other countries, or lowering taxes on certain factors can foster companies to find new partnerships in other countries. It was also found that governments of developing countries play a significant role in creating incentives for companies to innovate, since markets are not effective distributors of resources (Chandran et al., 2013). During the economic sanctions, when innovations give companies an opportunity to overcome their negative consequences, the government is expected to focus on creating conditions for product and process innovation. A favorable legal and institutional context in the country can also enhance the willingness of companies to introduce innovations (Trott, 2012).

In July 2018, the Russian government worked out a comprehensive plan to provide "systemic support to victims of sanctions" (Gould-Davies, 2018). It included, in particular,

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[17] https://www.bnnbloomberg.ca/large-russian-companies-are-turning-inward-1.1112107

[18] https://dlib.eastview.com/browse/doc/42659672

initiatives to reduce the use of the dollar in foreign trade payments, to support the access of sanctioned companies to the domestic financial market, and to reduce dependence on foreign patent holders. In turn, the countries that introduced the economic sanctions began to look for ways to limit the access of Russian firms to replacing partnerships. For example, the Ukraine Freedom Support Act of 2014 allowed the US to impose secondary sanctions against entities that violate the US sanctions on Russia. The Russian government established the Industry Development Fund that allocates money from the federal budget as soft loans to Russian companies that have expressed interest in designing, developing, or manufacturing any kind of equipment or technology that were primarily imported before the sanctions. Since 2017, companies can also sign a Special Investment Contract (SPIC) with the Ministry of Economic Development of Russia that started allocating investments for localization of production in Russia.

The majority of sanctioned Russian companies (both international and domestic) are those that play a significant role in the national economy. The underperforming of these companies can lead to negative consequences for the Russian economy and for the socio-economic environment of the country. The government is expected to take equally strong measures to assist both groups of companies — domestic and international. Thus, the next proposition is:

Proposition 4: Russian sanctioned companies operating only domestically receive the same level of government support as Russian sanctioned companies operating internationally.

4. Prospects for innovations

One of the important aspects of economic sanctions is a change in the attitude to innovation at the country and firm level. Innovations have direct and indirect effects on firms' performance and can become a strategic factor that ensures the growth and wealth of the company (Bolivar-Ramos et al., 2012). Companies that use the latest achievements and technologies have more chances to survive in conditions of uncertainty and sustain competition (Kim & Pae, 2007). During economic sanctions, innovations can become a source of overcoming the corresponding negative consequences. Product and process innovations lead to higher sales and growth rate (Goedhuys & Veugelers, 2012). Referring to the endogenous growth theory, it can also be argued that the economic growth of a company is highly dependent on internal forces, mainly innovations (Solow, 1956). Economic sanctions most often entail blocking technologies that pushes companies to look for other means to compensate for lost opportunities and find new ways to maintain economic growth (Afesorgbor, 2019). It is interesting that the more complex and dynamic the regulatory business environment, the more likely an organization will pay special attention to training and innovation in its products and processes development (Milutina, 2018).

There are differences in the attitude and capability to innovate between domestic and international firms. First, companies that operate abroad are more productive and innovative, because they have better access to international contacts, accumulated knowledge and advanced technologies (Sharma, 2018). Secondly, even in the case of limited access to external resources, which may occur during economic sanctions, firms operating abroad have more initiatives to innovate, since they compete in global markets and must be more efficient to survive (Chandran et al., 2013). International openness is very important for stimulating innovativeness and productivity, which are achieved through competition and access to different markets (Goedhuys & Veugelers, 2012). In contrast, domestic companies are less exposed to international markets and thus, are less likely to use knowledge from other countries.

According to a survey of 603 Russian domestic enterprises conducted by the Skolkovo Innovation Center (known as the Russian Silicon Valley), about half of the firms (50%) declared their interest in going abroad, especially to Asian markets (Skolkovo & TusPark, 2016). One of the main challenges these firms are facing is the lack of knowledge about doing business abroad and the lack of special capacities, such as innovations and others (Neparko & Frolova, 2019). These problems are addressed to a greater extent to domestic firms and are less critical for internationally operated ones, since they have better access to knowledge due to global experience and networks (Davidson et al., 2018). There is a low level of participation in innovation activities of domestic Russian firms (about 20–30%); whereas, large international companies demonstrate a relatively high level (about 75%).[19] Thus, sanctioned Russian domestic firms show less initiative in introducing innovative capacities than international ones: the larger the company, the more it is inclined to innovate (Davidson et al., 2018).

The economic sanctions limited the access of Russian firms to foreign technologies. To encourage companies to innovate, the Russian government started offering various lowered tax duties on the import of certain components for the production of innovative equipment and products (Vorotnikov et al., 2019). Russia pursues an active innovation policy; one of its goals is to expand participation of businesses in research, technologies and innovations (Davidson et al., 2018). It facilitates innovation in companies through loans, subsidies, and tax breaks. Import substitution initiatives are intensely introduced in different industries, thus boosting the development of technologies at the organizational level. In order to be more competitive in the home and foreign markets, companies need to focus on being more technologically advanced (Milutina, 2018). While international companies demonstrate great initiative in the field of innovation due to their international exposure and experience, domestic Russian firms do not possess the same technological achievements, resources, and a global network to maintain innovation in the company (Vorotnikov et al., 2019). Taking all the above into account, the next two propositions are as follows:

Proposition 5a: Russian sanctioned companies operating domestically show less initiative in introducing innovations into business processes than Russian sanctioned companies operating internationally.

Proposition 5b: Russian sanctioned companies operating domestically show less initiative in introducing product innovations than Russian sanctioned companies operating internationally.

[19] https://www.fbacs.com/upload/Report_RUS.pdf

The resilience of the company in the conditions of fierce competition and market uncertainty can be explained by better manageability of human resources in organizations (Melnikov & Yaremchuk, 2018). Sanctioned firms are expected to emphasize the creativity of the employees to generate ideas for new markets, develop new partnerships, improve products and processes. The task of the top management is to improve the firm's efficiency by creating an innovative environment, encouraging product development and business processes, and promoting new ideas among employees (Ridge et al., 2017). This allows the company to maintain the level of performance despite external factors, such as economic sanctions. For example, high-tech projects, such as the Crimean Bridge project and Nord Stream-2, require special innovative solutions. Despite the fact that the US has imposed sanctions on Russian companies, the pipeline will be completed with the collaboration of West-European partners.[20] Thus, the experience of working in the least favored conditions is extremely useful for domestic companies.

In order to sustain or develop competitive advantages in the marketplace, companies should facilitate implementation of new technologies (Kim & Pae, 2007). Advances in technology can increase the viability of a company by lowering production costs, entering new markets and developing innovative strategies, solutions or products. Given the link between talent management practices and performance of a company (Latukha, 2015), it is expected that companies affected by economic sanctions should emphasize the innovativeness of their culture and encourage employees to develop new ideas to enhance their competitiveness in rigorous conditions.

To maintain the level of competitiveness and innovativeness of the firm, employees and managers of the organization need to develop skills and competencies that help them acquire, develop and apply resources. This process can take a considerable time, but signals that the company is changing the focus in human practices can be observed in a short time and perceived by the employees as an encouragement of innovations. Since there is a positive relationship between the innovativeness of the company and its performance, the development of talent management practices can become a cornerstone in adapting to economic sanctions. Due to the undeveloped talent management practices in Russia, there is a long road in front of Russian companies in terms of attracting and retaining employees (Latukha, 2015). It can be expected that a firm that faces external difficulties in the market will be forced to develop these practices faster than domestic ones. The diversity and tenure of managers can improve the innovativeness at the company (Guo et al., 2018), and the experience and abilities can help the firm to cope more successfully with international expansion and improve its performance in foreign markets (Hutzschenreuter & Horstkotte, 2013; Latukha & Panibratov, 2015).

Russian companies are aware of the positive impact of talent management practices and the importance of encouraging and stimulating employees, but they lack interest in applying these techniques (Latukha, 2015). Additionally, the speed of applying new practices in Russian companies is lower than that of their foreign competitors. In turn, foreign companies demonstrate a more mature approach and a serious attitude to talent

[20] https://www.reuters.com/world/us-issues-nord-stream-2-related-sanctions-russians-blinken-2021-08-20/

management. Due to a wider access to the foreign market, the experience in dealing with international companies and the need to compete in the global market, Russian companies operating abroad are expected to have more intentions to implement advanced talent management practices and promote innovativeness of employees. A tough competitive environment, labor mobility of management and international exposure can lead to the fact that international companies will pay more attention to creating an environment in which employees feel opportunities for innovation and exchange of new ideas, compared to companies operating only in Russia. Thus, the next proposition is:

Proposition 6: Russian sanctioned companies operating domestically pay less attention to the innovativeness of employees than Russian sanctioned companies operating internationally.

5. Discussion

This study emphasizes the differences between Russian international and domestic firms in their ways of adapting to the economic sanctions. Companies operating in foreign markets possess the advantages of international experience, global network and competitiveness, which can potentially lead to simplification of the process of finding new suppliers and financial resources abroad, entering new foreign markets, introducing product and process innovation, and creating an environment facilitating innovations within the company. However, government support and the possibility to enter new agreements in their home country are equally available for both groups of companies.

Using the example of Russia, the paper answers the question whether there is in reality an advantage of internationalization for Russian firms during the sanctions. It is assumed that national firms operating in foreign markets can find new foreign partners and introduce innovations easier than those operating domestically. Despite the initiatives introduced by the Russian government in the field of import substitution and shielding the sanctioned companies, the Russian market is not sufficiently developed to provide companies with all the necessary resources locally. That is why internationalization can bring significant benefits to companies in overcoming the negative effects of economic sanctions.

Two important and specific implications of this paper are the impact of sanctions on cooperation and innovation, and both are subject for future studies. While remaining critical of the proposed insights without their empirical confirmation, we assume that there may be a contradiction between the propositions we made and the anecdotal evidence of Russian firms.

Thus, although the propositions state that Russian firms with international operations may have easier access to foreign suppliers and financial resources, we still need to find evidence to prove this, otherwise internationalization cannot be considered as a "helping hand" for sanctioned firms in finding new suppliers and capitals in either of the two markets.

Despite the literature-based argumentation of the advantages of Russian international firms over domestic ones in their access to foreign suppliers and financial resources, both groups of companies may face difficulties in finding financing and procurement in foreign markets, as sanctions severely restrict lending to Russia by EU and US banks (Russell, 2018). Despite the variety of markets where Russian firms might expand, the restrictions imposed by a foreign government apply equally to all firms originating from Russia. The economic sanctions against Russia created an environment in which all companies are experiencing difficulties in finding partners in local markets and abroad (Vorotnikov et al., 2019).

Operating in the international market may not necessarily provide an advantage in terms of new partners in the local market but will rather facilitate the search for new foreign markets. The proposal that the government should provide the same level of assistance to both types of companies equally regardless of their international activities would also require further justification, since, having different control and interest in national firms, the Russian government can help sanctioned firms differently, regardless of the scale of their internationalization.

Although it was suggested that there were differences between international and domestic firms in their intent to invest into innovations during the sanctions, the significance of these differences may vary. The specifics of Russian companies can be explained by the fact that all of them share a cautious attitude to the changes introduced in their process: only 8.4% of Russian companies were engaged in organizational innovations in 2016 (Russell, 2018). Additionally, innovations in business processes require time and resources that are limited during sanctions, and companies may prioritize other initiatives.

As expected, internationally active firms are more focused on product innovation. Given the fact that companies resort to manufacturing new products to the same extent as they resort to product modification, it can be argued that they see prospects and opportunities in introducing new products or improving old ones to overcome the consequences of sanctions (Singh & Subrahmanya, 2018). Coupling with easier access to new markets in Russia and abroad, internationalized firms can mitigate the negative effects of sanctions faster than domestic ones. The higher degree of product innovation of international companies compared to domestic companies can be explained by a wider network of international contacts and familiarity with foreign talents, resources, and ideas, which leads to lower operation costs. In addition, the import substitutions policy pursued by the Russian government can become a driver for the product innovations (Vartanova & Osadchaya, 2018).

Finally, although it was stated that Russian sanctioned firms operating internationally explore the employees' innovativeness more than domestic companies, international companies may attach more value to the creativity of employees and emphasize it during the period of sanctions. This may also be connected to their diverse experience and familiarity with international practices that are less popular among Russian organizations.

Conclusion

Although the paper contributes to the study of the consequences of sanctions, some limitations should be mentioned. Firstly, the specifics of the Russian case complicate the generalization of the results. The analysis provides an opportunity to consider the impact of sanctions on other developing countries, but the results should be confirmed using other cases. The attitude of Russian companies to business process and product innovation, as well as state support for local firms and Russian counter-sanctions can distort the overall applicability of the results, while it is an undisputed fact that heterogeneity does exist among firms at the regional and country levels. Secondly, it is important to mention that, even though economic sanctions target specific companies, their negative consequences apply to a much larger number of firms than only to the direct targets of the sanctions, as well as to foreign companies operating in the sanctioned country. To a certain extent, all companies need to adapt to the changing environment and use new approaches to operate in the domestic and foreign markets. Although this research focuses only on companies that are direct subjects of economic sanctions, the scope of analysis can be extended to all organizations that are affected by them.

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