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A reality check on divestment from Russia

While most Western corporations with ties to Russia announced plans to exit the country, recent data has shown that very few have followed through

The fallout from Russia's invasion of Ukraine is still reverberating in corporate boardrooms around the world. Since continuing peace and geopolitical stability can no longer be assumed, two implicit pillars of many businesses' international strategies have begun to fracture. Western governments – swayed more by national security officials now than in the recent past – are demanding that domestic firms decouple from autocratic regimes.

Russia's appalling, unprovoked war is a test case of businesses' willingness to unwind the cross-border ties that have been deepening since the fall of the Berlin Wall. European Union and G7 countries were the first to impose sanctions on Russia and Western companies with subsidiaries in Russia have been under significant pressure to divest. But what matters is how much they have actually pulled up stakes.

How common is divestment from Russia?

In recently published research, we set out to answer the following empirical questions: in the nine months after the invasion, to what extent did Western businesses actually divest from their Russian subsidiaries? What was the commercial footprint of exiting firms compared to those that stayed? And were companies headquartered in certain Western countries more likely to leave than others?

We didn't know what to expect. On one hand, the media narrative of a mass exodus from Russia led us to think that we would find widespread Western divestment. On the other hand, precedents like the campaign to persuade Western firms to leave apartheid-era South Africa tempered our expectations.

By the end of November 2022, only 8.5 per cent of EU- and G7-registered firms had completed a divestment from at least one Russian subsidiary.

To establish a clear definition of foreign companies operating in Russia around the time of the invasion, we used the highly regarded ORBIS database to identify those subsidiaries in Russia owned by firms that are registered in countries leading the sanctions campaign. We then focused our analysis on completed exits, rather than on temporary suspensions of activity or mere announcements of an intention to leave. After all, many such promises might ultimately be broken, and suspending operations implies that a firm still has important obligations to local stakeholders such as tax payments, employment contracts, or relationships with suppliers.

Our headline finding is that by the end of November 2022, only 8.5 per cent of EU- and G7-registered firms had completed a divestment from at least one Russian subsidiary. But, depending on how companies' public evidence is used and interpreted, estimates within the range of 5-13 per cent are defensible. We also found that exiting firms tended to have lower profitability than firms that remained and that exiting firms had larger workforces (which may make them easier targets for divestment campaigners). Exit rates varied across countries. For example, while 15.8 per cent of US firms had quit by the end of November 2022, only 5.3 per cent of German firms had done so.

Why is it taking so long to withdraw?

These findings raise profound questions for business executives, policymakers and analysts. The first concerns Western businesses' appetite to sever ties with Russia's $ 1.7 trillion economy. Though Russia is an international pariah now, it will not necessarily remain in the global doghouse forever. The temptation to do business in the world's eleventh-largest economy is not going away.

Why is it taking so long for Western firms to withdraw? Before condemning any firms for foot-dragging, it is worth remembering that divestments are fraught with pitfalls and delays even in the best of times. In this case, the Russian government has taken active steps to discourage or even prevent divestment by foreign companies. For example, presidential decrees issued between August and October 2022 make it technically impossible for several foreign companies to complete their divestments. The October decree prohibits 45 foreign banks from disposing of their Russian assets without President Vladimir Putin's

personal approval. Any fair assessment must account for these complications.

This raises the biggest question of all: to what extent are senior corporate executives really aligned with Western policymakers who are determined to decouple from autocratic regimes?

At the same time, the fact that more firms have not divested suggests that, alongside the compelling moral argument for doing so, their boards are weighing other salient considerations that bear on their fiduciary responsibilities. Whether the moral argument could be strengthened to override these considerations remains to be seen.

Again, there are strong echoes to the debate over divesting from South Africa in the 1970s and 1980s. Then as now, many worried that too few firms would quit voluntarily. While there was no invasion in this instance, there certainly was an active clampdown by Western countries.

All of this raises the biggest question of all: to what extent are senior corporate executives really aligned with Western policymakers who are determined to decouple from autocratic regimes? If they are as aligned as they say they are, there seems to be a mismatch between what policymakers want and what businesses can actually do when it comes to divesting rapidly without taking massive losses.

As Russian aggression enters its second year and the human and economic toll continues to climb, all eyes will remain on Eastern Europe. But the commercial and moral ramifications of the war, and the entrenched geopolitical rivalry it portends, will be felt much more widely.

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Simon Evenett

Simon Evenett is Professor of Economics at the University of St. Gallen.



Niccolò Pisani

Niccolò Pisani is Professor of Strategy and International Business at the International Institute for Management Development in Lausanne, Switzerland.