

## **THE SHORT-TERM EFFECTS OF ECONOMIC SANCTIONS ON TRADE ACTIVITY. CASE STUDY: MOLDOVA'S EXPORTS OF WINE**

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### **Abstract**

*For the Republic of Moldova winemaking is of great importance, not only culturally, but also from an economic point of view. The aim of this paper is to submit to the analysis the effects of the recent economic sanctions imposed by the Russian authorities on Moldovan exports of wine. As a result, we intend to better understand how the 2009 and 2013 embargoes have affected Moldova's trade potential and if they have determined any change of direction in terms of new partnerships and access to new markets.*

**Keywords:** *Economic Sanctions, Embargo, Trade Policy*

**JEL classification:** *F13*

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### **1. Introduction**

Although the tariff policy is the most commonly used one for regulating trade activity and it is a very important part of any country's commercial policy, the non-tariff policy is still widely practised by most of the states and can provide the desired results when it comes to targeting specific areas and relations one might have with other economies. Even if the subject of economic sanctions and specifically embargos seems to be a more recent one, it does actually date to ancient times and have been implemented ever since.

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Towards the 19<sup>th</sup> century and the beginning of the 20<sup>th</sup> century these sanctions were primarily used in order to replace military hostilities, while in the period after the Second World War they were an important tool in limiting other countries' potential to create and use weapons of mass destruction and sometimes try and produce a shift in the tug of war between the Western and the Eastern blocs (Hufbauer et al., 2007).

In the more modern times, towards the end of the 20<sup>th</sup> century and the beginning of the new millennium, due to a decrease in military activity around the globe, the economic sanctions have become an important tool for challenging various internal and external problems (Lektzian & Souva, 2003), but also for trying and changing the targeted country's foreign and in some cases internal policies (Afesorghor & Mahadevan, 2016; Allen, 2005). Whatever the goal might be, economic sanctions are also considered to be a much better alternative to armed interventions, while most of the time they lead to greater economic and social costs for the targeted country rather than the country that imposes them (Dashti-Gibson et al., 1997; Kaempfer & Lowenberg, 2007).

## **2. Recent Russia's sanctions on Moldovan exports**

The territory situated between the Prut and Dniester rivers has always represented a great deal of interest to the great powers of the region. In the recent history those two powers are the European Union and the Russian Federation. While the first one aspires to secure its border by creating a common economic European space, the latter has always considered that most Eastern European countries should always stay under its geopolitical sphere of influence.

The recent trends which have led to a deepening economic integration process with the EU have put Moldovan economy to the test. Although it meant that Moldovan producers gained access to new markets and could now explore new opportunities, the following several sanctions imposed by the Russian Federation lead to the loss of a great number of ties they had with the Russian partners. The signing of the Association Agreement with the European Union in 2013 was seen by the Kremlin as an attempt to diminish Russian influence in the area. Euro-integralist aspirations were also seen very negatively by the Russian government and the response came swiftly.

The Russian authorities have imposed a series of embargoes on Moldovan wines in the fall of 2013, reminiscent of the 2006 and 2009 sanctions, which also affected Georgia as well, as a result of the two countries

expressing their will to adopt the EU integration vector. Apart from wines, other goods were affected by the Russia's policies in particular fruits and processed meats. While the possibility of these mentioned goods being potentially harmful for consumers existed, the timing of the sanctions suggests a political incentive.

The European Union on the other hand hasn't really imposed any sanctions on Moldovan goods and services apart from quotas on agri-food imports from outside of the Union. In an attempt to protect its own primary sector, the EU restrictions are part of the common policy and affects all states that are not EU members.

### **3. Sanctions' effects on Moldovan economic growth and structure**

Being an economy that still relies a lot on the agri-food sector, the embargoes on wine and other agricultural products caused major damage to the Moldovan economic situation as a whole. The wine branch is rightfully considered a pillar of the economy of the Republic of Moldova (Table 1). Thus, the main question that surfaces is: "did the embargoes actually affect the economy as a whole?"

**Table 1: The evolution of Moldova's wine exports**

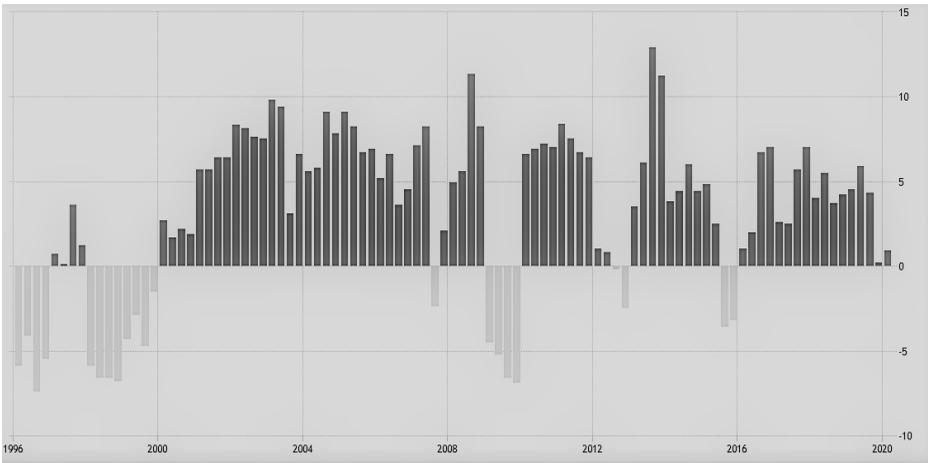
<b>Year</b>	<b>Total exports (thousands \$)</b>	<b>Wine exports (thousands \$)</b>	<b>Share in total exports (%)</b>
<b>2009</b>	780006.002	128819.159	16.52%
<b>2010</b>	935389.782	138458.458	14.80%
<b>2011</b>	1215190.558	132432.048	10.90%
<b>2012</b>	1389561.933	141545.959	10.19%
<b>2013</b>	1619833.3	149457.063	9.23%
<b>2014</b>	1529632.454	111870.362	7.31%
<b>2015</b>	1303995.43	97779.529	7.50%
<b>2016</b>	1350204.363	107715.491	7.98%
<b>2017</b>	1640755.73	128425.966	7.83%
<b>2018</b>	1852384.655	137825.058	7.44%

Source: UN Comtrade

In the last decade, we could observe a downward shift in importance of the wine exports for the Republic of Moldova (Table 1). Although the total

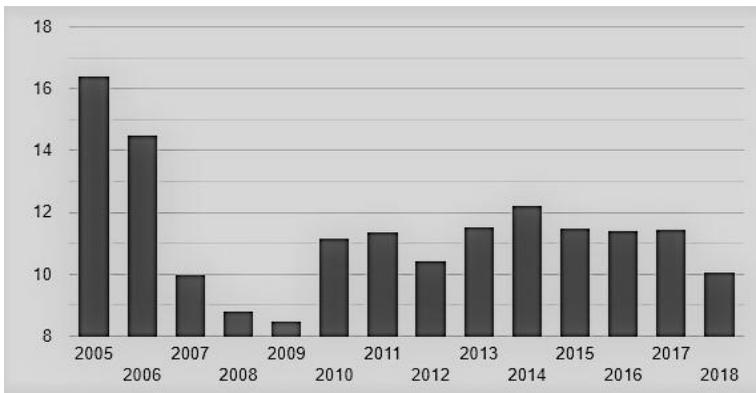
value of the wine exported in 2018 slowly reached the levels of 2010, the share in total exports has reduced to a half of what it was 9 years prior. At the same time, while the total exports have steadily grown, this was not always the case for Moldovan wineries. After a high of almost 150 million USD worth of wine exported in 2013, the value has fallen to 111 million in 2014 and 97 million in 2015, returning to a growing trend in 2016-2018.

**Figure 1. Moldova's GDP growth rate**



Source: World Bank

**Figure 2. Primary sector's contribution to Moldova's GDP**



Source: World Bank

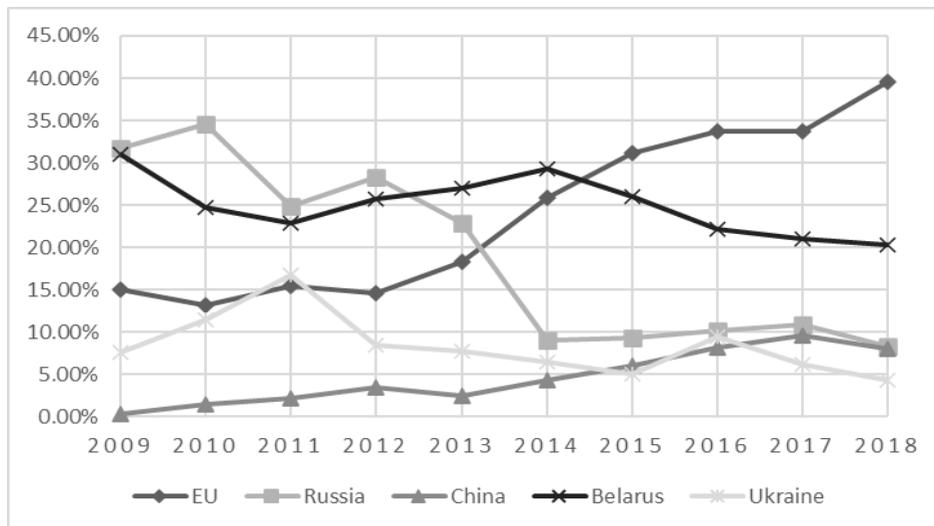
Even if the dynamics of the wine exports has changed quite a bit in the last decade, it is still difficult to estimate its effects on the economy as a whole. As seen in Figure 1., the GDP growth rate was negative during 2010-2011 and 2015, following the most recent sanctions imposed by Russia, but it is not enough to consider the embargos the main reason for that. It is also important to understand that these trends actually emulate the global ones and might be the result of the global financial crisis of 2008-2009 and the national banking crisis from 2014. At the same time, the 2006-2007 GDP growth rates seem to have been positive, despite the Kremlin sanctions.

A similar picture emerges in relation to the primary sector's contribution to the country's GDP. The agri-food branch was on a downward trend from 2006 to 2009 and 2015 onwards (Figure 2), while the wine production and export were actually increasing in the same timeframe, once again making it difficult to claim that the economic sanctions on wine exports had a significant impact on Moldovan productivity right away. The primary sector might have decreased in importance, but that could happen due to changes in Moldova's economic structures and business environment.

#### **4. Moldova's change of direction amid Russia's economic sanctions**

In the last 10-15 years, the Republic of Moldova has faced at least 3 embargos imposed by the Moscow authorities on wine of Moldovan origin, many times, in order to put political pressure on Moldova authorities. In this context, it is quite difficult to imagine Moldovan wine producers not taking any actions accordingly and probably seeking new ways to sell their goods on other markets. The insecurities of Moldovan producers and their skepticism about a constructive cooperation with their Russian partners might have increased during the last 10 years as a result of the harsh reactions to Moldova's geopolitical aspirations.

#### **Figure 3. The distribution of Moldova's wine exports**



Source: UN Comtrade

When it comes to wine export distribution, it is clear that the tides have shifted quite a bit in the last decade (Figure 3). The immediate effect of the Russian sanctions has shown a dramatic decrease in wine exports towards Russia. While Russia's share has plummeted to a little over 25% in the years following the 2009 restrictions, it has further decreased ever since. In 2014 only 9.08% of Moldovan wine exports reached Russian markets in comparison to 22.95% the year prior. In 2018, Russia's share was only 8.29%. At the same time, Belarus' share has also decreased in the last decade by around a third of its 2009 value. In 2018, only a little over 20% of the Moldovan wine was exported to Belarus, thus still making it one of the biggest partners in terms of wine trading. It is worth mentioning that neither Belarusian or Ukrainian markets seem to have mitigated the effects of the sanctions, the exports to the Commonwealth of Independent States (CIS) decreasing all-together as a result.

Meanwhile, amid the Russian embargos the wine producers have turned to the European Union markets. Following the CEED II project, as well as the cancellation by the European Parliament of the export quotas for Moldovan wines, the share of Moldovan wine exports to EU countries increased from 15.1% in 2009 to 25.9% in 2014 and to almost 40% in 2018, making the European Union the biggest foreign market for Moldovan wine. The Union's friendly policy towards Moldova has led to an increase in overall

trade activities between the two. Following the sanctions imposed by the Kremlin in 2013, the Moldovan wine exports towards the EU almost doubled in the next 4 years.

At the same time, it is worth mentioning that China's importance for Moldovan winemakers has also increased in the last decade. From importing almost no Moldovan wine in 2009, China's share in 2018 was almost on par with Russia's. In 2018, a little over 8% of the Moldovan exported wine reached the Chinese market.

Overall, it seems like the Moldovan winemakers have found ways to gradually replace the lost Russian partnerships with others, more lucrative ones, specifically in the West, increasing their exports towards the EU countries. However, the issue of embargos is much more complex than it seems. Even if we are talking about economic recovery and reorientation of exports to other markets, this is not as easy to achieve. Many of the EU trade regulations have export quotas applied for countries like Moldova, which are not members of the Community. On the other hand, entering new markets requires new investments and transitions to higher quality standards, which could be an engine for more competitive goods being produced by the developing economies, as long as they can keep up with the additional costs.

Finally, we can't deny that the economic sanctions proved to be very costly for the Moldovan wine industry and the effects of those measures took a lot of effort to overturn successfully. But even so, taking into consideration that the total exports have grown in the last decade, while the wine sector had to recover, it is only natural to speculate what could have happened if the sanctions were never applied. Apart from the economic dimension of the sanctions there is still a lot to discuss regarding the geopolitical dynamic as well. As long as Moldova chooses to follow the Western vector, the Kremlin might feel the need to act with further sanctions. There is also the Transnistria problem, which seems to put Moldova's EU Accession on hold and affect its commercial ties with the latter.

## **5. Conclusions**

The economic sanctions have become a powerful tool used not only to shift trade activities, but also influence the behaviour of the targeted country. Although, the Kremlin will never openly admit it, the recent embargos imposed on Moldovan wines and in some instances on fruits and meat seem to have a political character, the main reason being the recent deepening of the relations between Brussels and Chisinau.

It is safe to say that these sanctions have dealt a huge blow to the Moldovan winemaking branch, reducing wine exports drastically in the years following them. Wines' share in total trade has also fallen in the last decade, while the values have increased relatively slowly in comparison with other products, in 2018 only slightly surpassing the levels registered in 2009.

Even if the effects of the Russian sanction on Moldovan economy are difficult to quantify and there might not even be a direct relationship, it has definitely produced a change of direction when it comes to trading abroad. The EU markets seem to demand more and more Moldovan wine, while Russia's importance for Moldova's winemakers have ultimately reduced. Thus, the recent policies applied by the Kremlin might have determined the Moldovan businessmen to look for new opportunities in the West or further East, in order to be prepared for possible future challenges.

## **6. Acknowledgement**

This work was co-financed from the European Social Fund through Operational Programme Human Capital 2014-2020, project number POCU/380/6/13/125015 "Development of entrepreneurial skills for doctoral students and postdoctoral researchers in the field of economic sciences"

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