

POSSIBLE SCENARIOS FOR DEVELOPING EU TRADE RELATIONS WITH RUSSIA

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Abstract: The study presents general scenarios for the future development of EU trade relations with Russia, which are conditionally marked as 'stagnation', 'optimistic' and 'pessimistic'. The dynamics of the sanctions regime is used as a key indicator for distinguishing these scenarios. We associate the first scenario, called 'stagnation', with the expectations of a serious slowdown in the economic growth of the EU and Russia. The second, described as 'optimistic', is based on expectations for a gradual recovery and development of the trade relations between the two countries over a long period of time. The third scenario is defined as 'pessimistic', given the consolidated tightening of anti-Russian sanctions within the transatlantic alliance and the expansion of Russia's countermeasures.

Keywords: trade relations, European Union, Russia

JEL: F14, N74, O24, P45, P52.

Introduction

The strategic importance of EU trade relations with Russia provoke economic thought to seek options for their future development, based on key indicators which allow identifying factors that have a significant impact on trade and expectations for its development in the short and long run.

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The purpose of the study is to present possible scenarios for developing bilateral relations in the field of trade, conditionally referred to as 'stagnation', 'optimistic' and 'pessimistic'.

The scenarios are outlined on the basis of in-depth studies of the historical development of EU trade relations with Russia in the 1992–2020 period (Zhelyazkova, D., S. Piddubrivnyy, 2021).

The topic is relevant due to the divergence of the geopolitical attitudes of the EU and Russia and the reciprocal restrictive measures, which have not severed their relations in foreign trade. However, the current crisis phase in their trade relations continues. In the event of any significant change in the geopolitical environment, both a further escalation of tension and its gradual easing can be expected, which must be taken into account when forecasting future trends in the development of trade relations.

1. The first scenario: Stagnation

We associate the first scenario, called 'stagnation', with expectations of a slowdown in economic growth in the EU and Russia. In Russia, this decline is the result of a reduction in the intensity of financial flows in the form of loans and foreign investment amid rising levels of uncertainty and risk, accompanied by technological fall of key sectors of the Russian economy, such as oil production. Both the EU and Russia are in the process of intensively seeking opportunities to reduce economic interdependence, which requires diversification of the portfolio of suppliers and search for customers in new markets.

This scenario is based on four key indicators:

- Maintaining the status quo, which preserves the current geopolitical differences and reciprocal restrictive measures, whereas in the event of an escalation of the sanctions regime by the United States, the EU will not support them. This attitude of the EU is based on pragmatic considerations and is mainly related to the potential negative consequences of the new package of anti-Russian sanctions for its own economy.

- The complementarity of the EU and Russian economies still plays a stabilizing role. However, a gradual and mutual diversification of foreign trade flows is observed, which is most noticeable in the energy sector.

- Opportunities remain for active bilateral trade and the implementation of joint business projects in various sectors of the economy, including the energy sector. At the same time, participants are forced to adapt both to the existing restrictive measures and to the possible tightening of sanctions by the United States.

- With the EU's attitude of condemnation of the new US measures and the existing threat of their negative impact on European businesses, a historic possibility emerges for resuming bilateral dialogue on strategic trade issues in the context of ensuring the economic security of partners.

For Russia, the main problems in this scenario are related to the growing negative effects of the current restrictive measures in the medium and long run. These restrictions on a number of strategically important sectors of the Russian economy worsen the forecast for overall economic growth due to the slowdown in modernizing production and reducing the competitiveness of the companies on the world market. This is to a large extent due to the ban on lending extended to a number of large Russian companies in Western banks, which limits access to the resources needed to invest in future business development.

Asian financial markets are not always a suitable alternative, since they offer loans on strict and unfavorable terms, while the search for the necessary funds within the country is hampered by the fact that access to capital in European financial markets is also closed to a number of leading banks.

Sanctions will also be a major obstacle to the inflow of foreign investment, which is an important driving force for economic development and a source of know-how. The main problem is that the sanctions regime itself and the hypothetical possibility of its extension significantly increase the degree of uncertainty and risk. This strongly affects the decisions of potential new investors due to the inability to adequately plan and organize key business processes in Russia.

The negative effects of restricting access to new technologies for the oil sector, where high-tech imported goods are predominant, will also gradually emerge. Restrictions affect drilling rigs, marine equipment for Arctic use, engines and compressors, high-pressure pumps, seismic equipment and other industry-critical products, as well as hydraulic

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fracturing software. Without lifting the sanctions, Russia will not have access to the necessary equipment, since some of the technologies in the oil and gas sector are currently owned by only two countries in the world – the United States and Norway.

Satisfying the demand for oil will be ensured mainly by increasing its production in already developed locations, which will compensate for the problems in the development of more complex fields associated with technological constraints in the short run. Their initial manifestation will be expressed in technical problems related to maintaining and modernizing the production capacity. In the future this may lead to a reduction in oil production.

The results of a study by the Energy Center of the Moscow School of Management “Skolkovo” show that a serious vulnerability of the Russian oil and gas sector to sanctions will emerge by 2025, when the increase in the share of deep wells and the lack of new equipment will have a significant impact on the industry. Given the investment cycle which takes at least 5-7 years, investments in the most important technologies for oil production must be made today in order to protect its production from a rapid decline in the future. (Pertsova, 2018).

In view of the above mentioned, the start of their own or joint projects for developing technological equipment for oil production should be one of the key short-run tasks facing Russia in implementing this scenario.

As a whole, Russia’s announced programme of import substitution continues to perform best in agriculture and the food industry, while the ongoing food embargo provides a forecast for further growth in domestic Russian production and a decrease in food imports.

In the short run, the dependence of the Russian agricultural sector on imports of a number of commodity items (for example, high-quality seeds, young fish, etc.) is expected to remain, as evidenced by their exclusion from the sanctions list.

In the context of the geographical structure of Russia’s foreign trade, the EU’s role as a leading trading partner and the intensification of trade turnover diversification measures can be envisaged by expanding cooperation with countries that do not support the introduction of the sanctions regime, mainly with developing Asian economies.

The most active development of bilateral trade will continue with China. However, the role of a number of other Asian countries will gradually grow – South Korea, India, Singapore and Vietnam, which according to statistics from the Federal Customs Service of Russia is a leader in trade turnover growth rate and the share of Russia's foreign trade in the 2013 – 2019 period. At the same time, one of the most significant negative factors in the development of Russia's trade and economic cooperation with key foreign partners may be the expansion of the US sanctions regime. The risk of extraterritorial implementation of these sanctions against third countries and the companies involved in trade and in joint projects with sanctioned Russian businesses will put serious pressure on the decisions of the existing and potential partners.

Russia's real ability to create effective trade mechanisms, circumventing sanctions and preventing negative effects on its foreign business partners is limited due to the significantly weaker economic potential of the United States and its dominant role in the global financial system. This situation could lead to a further deterioration of Russia's domestic investment climate, increased foreign capital outflows and serious difficulties in foreign trade.

The main problems facing the EU in implementing this scenario are maintaining a rational balance between geopolitical objectives and economic interests, reducing the negative effects of existing and counter-sanctions, and stepping up energy security measures.

The current dimensions of EU trade relations with Russia suggest that, if the status quo is maintained, the current restrictive measures on the EU's economic development indicators will continue to have a rather limited impact while their maximum damage, *ceteris paribus*, can only be calculated as part of the percentage of the total GDP. At the same time, the varying degrees of trade interaction with Russia among EU member states in the short run will predetermine the ongoing uneven impact of sanctions on them, and EU solidarity will increasingly be tested due to internal disagreements regarding the appropriateness of their extension or expansion.

The resource interconnectedness of the economies and the upward trend in the EU trade with Russia after 2017, despite the sanctions, allow

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for a moderate increase in the volume of trade turnover and the relative stability of its structure in the short run.

Just as before, mineral products will have a dominant role in the structure of EU imports from Russia. A more noticeable increase in the value indicators of metal imports can be envisaged, given the rising prices in response to the ongoing trade disputes between the leading players in the world market.

The larger share of EU exports will continue to be occupied by industrial goods with a leading role of the machinery industry, electronics and the automotive sector, while due to Russia's ban on imports of European agricultural products, a future decline in their share in the structure of EU exports to Russia can be expected.

Russia's current food embargo and the relatively slow pace of diversification of export flows from Eastern European countries, which are more affected by its negative impact, will predetermine the need to continue implementing measures to support the agricultural sector by The European Commission, at least in the short run.

Among the main factors that can affect the dynamics of bilateral trade and reduce the asymmetry of its commodity structure in the long run, we can point out the following:

- Implementing the EU strategy for energy security and the relative slowdown in the overall pace of global economic growth, accompanied by a reduction in demand for Russian mineral resources. At the same time, the extent of the projected decline will largely depend on the situation on the world energy markets (OPEC quotas, sanctions against leading exporting countries, etc.).

- Russia's declining demand for European machinery and equipment as a result of the weakening ruble (rising prices of imports), slowing economic growth and limited investment opportunities in modernizing production. Decline in exports may be partly due to the ongoing technological constraints on Russian businesses' access to specific oil production equipment, and to an even lesser degree to Russia's import substitution strategy.

The gradual diversification of mineral imports will be the EU's most important source of energy security and the most important challenge in implementing this scenario in the medium and long run.

Based on the analysis of the situation and the main trends in the development of the world energy market, it can be assumed that the main component of this strategy will be the expansion of the geographical structure of imports and the increasing share of liquefied natural gas (LNG) in its total volume. Qatar will remain the largest LNG exporter, although US imports will also grow. It should be noted that an important feature of the American LNG, from the point of view of its competitive position, is the high price, which will be a constraint on significant import growth, *ceteris paribus*.

Saudi Arabia, which has relatively recently entered the global LNG market, is also interested in expanding the geography of exports in the medium run. It can be expected that their price offer will also be more advantageous for the EU.

Despite these circumstances, it can be assumed with a high degree of probability that, regardless of the significant price differences, US LNG imports will continue since they provide the EU with an additional channel to overcome the monopolization of the energy market. In addition, the strategy to increase US gas imports will partially improve the existing asymmetry in EU-US foreign trade, which will reduce trade disputes and tension with the EU's most important strategic partner.

The new gas pipelines will be an additional source of diversification of the EU energy system:

- The "Southern Gas Corridor", through which natural gas from Azerbaijan will reach Greece, Bulgaria and Italy, passing through Turkey with a design capacity of 10 billion cubic meters per year (Toshkova, 2018).

- The EastMed pipeline, which supplies gas from Israel to Cyprus, Greece and Italy. Its construction must be completed by the end of 2025. The project capacity is also 10 billion cubic meters per year (Bulgartransgaz, 2019).

Thanks to regasification terminals built in recent years, Spain can also contribute to expanding LNG supply to the EU. Six existing terminals enable imports from different parts of the world. In addition, the EU's

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energy security can be facilitated by the more active construction of new cross-border interconnectors connecting gas pipeline systems of different countries and enabling the transport of additional LNG volumes from Polish and Lithuanian terminals, as well as reverse gas supplies in case of force majeure circumstances.

In general, it should be noted that the implementation of this scenario for developing trade relations allows the EU to gradually and smoothly build the necessary additional infrastructure, which allows reducing costs and the risk of possible crises in the Member States energy supply.

A serious problem that the EU may face in implementing the so-called stagnation scenario is the disagreement within the transatlantic alliance on anti-Russian sanctions. Removing these contradictions can be one of the key tasks of US foreign policy, since the EU's refusal to support new sanctions significantly reduces their effectiveness and potential consequences for Russia, as well as runs counter to long-run energy interests. This situation poses a potential risk to a number of EU companies involved in and investing in joint projects with Russian businesses, since in the event of a unilateral tightening of US sanctions, there is a possibility of their extraterritorial (secondary) impositions on European companies. At the same time, the measures that the EU must take to protect its own economic interests will further exacerbate the controversy within the alliance.

The new sanctions could affect a wide range of trade and economic relations. However a general look at the information available on the draft bills to expand the US sanctions list suggests the most likely spread to joint energy projects, which are currently of a strategic interest to a number of EU Member States.

Secondary sanctions threaten businesses with a ban on receiving any financial services in the United States, a ban on lending by US banks, restrictions on exports of US goods, as well as restrictions on the acquisition of property and a ban on managers and shareholders of sanctioned companies to enter the USA. In addition, the United States effectively controls the international financial sector. Therefore, a threat of sanctions exists against European organizations making non-cash

payments in US dollars with counterparties on the sanctions list. All similar transactions go through their correspondent accounts with US banks and can have negative consequences for financial institutions.

An example of this is the fines of over \$ 10 billion imposed on a number of EU banks in the 2013-2017 period for violating the sanctions regime against Iran, Cuba and others. These include such large financial institutions as BNP Paribas (France), Credit Agricole (France), Deutsche Bank (Germany), Commerzbank (Germany), Barclays (the United Kingdom) and Intesa Sanpaolo SpA (Italy). All fines have been paid, because otherwise banks are threatened with blocking dollar accounts.

Based on the abovementioned, it can be concluded that the implementation of this scenario will require the use of additional measures to protect the economic interests of the EU and Russia from external influences, aimed at preventing the negative impact of possible US sanctions on joint activities of European and Russian businesses.

One of the important preconditions for the success of this protection strategy can be the coordination of the reciprocal actions of the partners, which will create an opportunity for the resumption of a constructive dialogue in the field of bilateral trade and economic cooperation.

2. The second scenario: Optimistic

We define the second scenario as 'optimistic' in the long run, when expectations exist for a gradual restoration and development of EU trade relations with Russia under conditions of relative security for the business partners, as a result of renewed dialogue and a clearly regulated legal framework.

The key indicators for this scenario are as follows:

- Complete abolition or significant weakening of reciprocal restrictive measures against the background of the positive dynamics of geopolitical factors that caused their introduction.
- Strengthening the dialogue for future development of trade and economic cooperation and its legal framework under the new conditions.
- Gradual upward development of bilateral trade.

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- Completing existing projects in various areas of the economy and planning new joint initiatives.
- Strengthening the potential risks of extraterritorial implementation of US sanctions.
- Implementing coordinated measures to protect business, economic security and independence of trading partners.

In general, the abolition of reciprocal restrictive measures is certainly an important positive factor for developing EU trade relations with Russia. However, we cannot expect a rapid growth of bilateral trade indicators and a significant increase in investment activity in the short run.

One of the reasons for this inertia in the short run is the very nature of the existing reciprocal sanctions, which do not lead to the complete suspension of the economic cooperation, yet are limited to its individual areas. The other reason is related to the lack of trust and security, which inevitably emerges in critical periods of the bilateral relations and continues for some time after their regularization. Another important factor is the need to establish new economic relations or restore lost international contacts, which also requires a lot of time and effort.

In the field of bilateral trade we can expect a lasting moderate growth of the main indicators of trade turnover and maintenance of its commodity structure.

A positive aspect of the scenario is the expansion of the foreign market for the European agricultural one after lifting the Russian food embargo, yet a significant increase in exports in the short run will be hampered by the need to create new distribution channels against the background of strengthening local producers in the context of Russia's import substitution strategy.

Certain foodstuffs and agricultural raw materials, in the production of which European manufacturers have an absolute advantage, are generally not prohibited during the sanction period, as a result of which the export of these items cannot significantly change the dynamics of exports. The positive aspects of lifting the food embargo for Russian consumers will be related to expanding the range and improving the quality of food offered, as well as a gradual reduction in prices, which for some goods have been significantly increased during sanctions due to reduced competition and

rising costs for imported raw materials. At the same time, the lifting of the embargo is an unfavorable factor for Russian farmers due to the threat of weakening state support measures for the agricultural sector and a weaker competitive position compared to a number of European producers.

The elimination of technological constraints can serve as a stimulus for the growth of exports of European machinery and equipment, which is of particular importance to manufacturers of special oil products.

For Russia, restoring access to technology is the most important stimulus for modernizing production facilities and business processes in strategic industries and for improving the long-run forecast for the development of the oil sector.

For its part, the volume of EU imports from Russia in the short run is also likely to continue to grow at a moderate pace, and energy resources will remain a key element of this growth.

The stability of pipeline natural gas imports, the significant increase in Russian LNG imports and the construction of new pipelines serve as an indicator of Russia's ongoing role in the EU energy system in the medium run. The main prerequisite for this lasting trend is the developed combined infrastructure for the supply of relatively cheap gas.

A gradual reduction in Russia's share is expected in the long run with the successful implementation of the EU strategy for diversifying mineral imports.

A significant positive aspect of the scenario for the Russian economy is the elimination of restrictions on access to the European financial system. The fact itself is a positive signal for the financial markets, which may cause the growth of major stock indexes in Russia and the strengthening of the ruble.

Restoration of access to borrowed capital, which is provided by European banks on relatively favorable terms is of great importance for the Russian business and financial sector. This will significantly expand the opportunities for modernizing production, which in turn is the basis for the gradual development of the economy in the future. Increasing demand for financial services also benefits the EU banking sector.

We should note the positive impact of lifting the sanctions on Russia's overall investment climate, yet it is in this area that the strongest

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crisis of trust and security can be expected, hence a significant increase in investment activity of foreign investors is unlikely to become a reality in the short run. The indisputable positive aspect with implementing this scenario is the possibility to get out of the so-called 'gray schemes' for the current European investors.

The resumption of the open dialogue between the EU and Russia on strategic issues of trade and economic relations, based on pragmatism, respect for the mutual attitudes and the search for compromise solutions, can help intensify investment activity. After the period of crisis in relationships, a new programme of particular actions and joint initiatives is needed, aimed at restoring constructive cooperation in the field of international trade, financial and investment activities, economic security and independence, as well as increasing the resilience of partners to the negative impact of global external factors.

One of the key problems in implementing this scenario is the sharp deterioration of geopolitical and trade disputes within the transatlantic alliance, because the probability of lifting sanctions against Russia by the United States can be assessed as low even in the medium run, and further tightening is very likely in the short run.

The nature of the negative impact of these sanctions on the development of trade and economic cooperation between the EU and Russia is generally similar to the previous scenario, yet the risk of their extraterritorial implementation extends to a larger number of European companies. European banks lending to Russian companies, as well as manufacturers of equipment for the energy sector are exposed to risk the most.

Additional factors determining the low probability of implementing this scenario of bilateral trade relations, can be as follows:

- Potential EU foreign trade losses in the event of a deepening conflict with the US (key trading partner and net importer of European goods).
- The procedure for making a decision on lifting sanctions against Russia (the need for a unanimous decision made by all EU member states).

3. The third scenario: pessimistic

The main indicator of this scenario is the consolidated tightening of anti-Russian sanctions within the framework of the transatlantic alliance and the expansion of Russia's countermeasures. Strengthening the reciprocal sanction policy may include a wide variety of options from soft to full-scale, which will be determined by the degree of deterioration of the geopolitical situation. Soft options mean introducing additional personal restrictions and including a number of new companies or sectors of the economy, which do not affect the strategic areas of bilateral trade and economic relations, in the sanctions regime.

Stricter options may involve significantly deepening of restrictive measures and extending them to the most important areas of bilateral trade, financial and investment cooperation, in order to cause more significant economic damage in the medium and long run. The full-scale sanctions regime is, in fact, a contraction in trade and economic relations and includes the most radical measures to minimize government revenues and block financial activities, which poses a critical threat to economic security in the short run.

Essentially, this is the so-called Iranian scenario, which includes severing contacts at official level, blocking state bank accounts, banning financial transactions, including operations with alternative financial instruments (government debt, precious metals), total ban on investments in the country and large-scale trade restrictions, including the energy embargo (ban on the import of mineral resources).

It is impossible to present all possible scenarios for the possible tightening of reciprocal sanctions in the framework of the study, given the wide variety of options, therefore the consequences of the extension of the restrictive measures in the strategic areas of bilateral trade and economic cooperation are considered in more detail.

The expansion of sanctions in the financial sphere may be related to limiting the interaction between a wider range of Russian companies from different sectors of the economy and all banks with state participation of the Russian Federation, with the European financial institutions. The ban could include lending to businesses and individuals, opening accounts in

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European banks, securities transactions with Russian companies, and restricting the technical capacity to directly invest in Russian economy.

Significant damage could be caused by excluding Russian financial institutions from international payment systems, as well as blocking their accounts with European banks and the ban on operations with Russia's debt financial instruments.

One of the serious restrictions could be excluding Russia from the SWIFT interbank system for international currency transfers. This measure is not expected to stop, yet it will significantly complicate international trade and investment, as the use of alternative payment mechanisms will involve greater operational risks, time and transaction costs. Russia currently has an alternative payment system, although it cannot force foreign banks to use it.

The EU's accession to the US financial sanctions could lead to blocking a larger volume of assets of Russia's state-owned banks (over \$ 100 billion), which will further increase the destructive effect on Russia's financial system.

Due to possible restrictions on operations with Russia's bonds (public debt), which are an important tool for maintaining the exchange rate, they can be expected to sell off quickly by foreign investors. This could lead to a devaluation of the Russian ruble, rising inflation and a reduction in the purchasing power of the population. At the same time, the implementation of these measures will have negative consequences for the EU economy.

The ban on foreign exchange transactions will make it impossible to pay off Russia's public debt, which will bring losses to bondholders, including central banks in various countries mainly.

Due to the global financial market sensitivity to changes in external environment and the high degree of integration of the Russian economy, the so-called 'domino effect' is possible, which could seriously damage the stability of the European and global financial system. It should be borne in mind that these effects can be further exacerbated by the use of countermeasures by Russia, which is also a holder of public debt and assets of the EU member states.

In the context of the impact of the restrictive measures on the real sector of the Russian economy, it should be noted that the consequences of tightening the sanctions may be even more significant, yet this will become more noticeable in the medium and long run.

The general negative effects of the limited access to borrowed capital and new technologies were considered in the first scenario, after the example of Russia's oil and gas sector. In this scenario, the effect of the sanctions covers an even wider range of sectors of the Russian economy, which will lead to much stronger negative consequences for its state and future growth. The main potential damages will be suffered by the industries that use imported high-tech equipment and components, which determine the prospects for the innovative development of the industry, namely. The limited access to new technologies and the weak success of the programme to replace imports in mechanical engineering, radio electronics and other high-tech industries in the long run could lead to a significant economic lagging of Russia and its development under the formula 'mining + agricultural + military industry'.

An option to partially offset the losses from the extension of sanctions is to further strengthen Russia's trade, investment and financial cooperation with the BRICS countries and other developing economies in Asia, South America and Africa. However, the significant deterioration of the investment climate and the high risks of the secondary implementation of EU and US sanctions are factors limiting the possible scale of cooperation and repelling these partners.

Predicting the impact of possible Russian counter-sanctions on the real sector of the EU economy, it can be assumed that the direct negative effects on key industries will be quite limited throughout the Union. The more significant negative effects may be related to the potential extension of trade restrictions on imports of goods from a wide range of industries, which will greatly affect the industry of Central and Eastern European countries and will require more active diversification of export flows and measures for state support.

In view of the commodity structure of bilateral trade, it can be concluded that the most radical measure among all options for implementing this scenario is the energy embargo. The predominant share

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of mineral resources in Russia's exports and its dominant role in the EU's energy supply system predetermine the strongest potential consequences of this restrictive measure for both the Russian economy and the economies of most EU member states. In the context of the impact of the energy embargo on Russia, it can be assumed that it will not stop exports, yet will lead to a significant reduction in its volume.

A significant problem for diversification is the logistics factor. A significant share of oil exports is made through pipelines, so a change in the way of transportation and the creation of additional infrastructure will take time and significantly increase costs.

The increase in import volumes by current Asian consumers who do not support anti-Russian sanctions (China, South Korea, Philippines, Singapore, Malaysia, Taiwan), as well as Russia's partners from BRICS, which are interested in expanding trade cooperation (India and Brazil) can be considered to be the potential for diversifying exports in the short run. However, even the successful implementation of these opportunities will not allow for compensating more than 50% of the lost volumes of oil exports.

Major problems exist with compensating for losses related to the suspension of natural gas exports (about 200 billion cubic meters per year). Opportunities for export reorientation are significantly limited, as they depend not only on the willingness of other trading partners to increase Russian gas imports in the complex geopolitical situation, but also on the transport infrastructure for its supply to new markets. The situation is further complicated by the fact that most of the current exports are also made through the system of main gas pipelines, most of which are oriented to the European market. The main alternative for diversification can be considered the growth of exports to China, where demand for gas is constantly growing against the background of government policy to replace coal in urban agglomerations. However, even after the completion of the construction of the Power of Siberia and Power of Siberia-2 gas pipelines, the additional export volumes to China will amount to no more than 75 million cubic meters per year (Barsukov, Yur., 2019). Losses can be partially reduced by strengthening and expanding the geography of LNG exports, yet even taking into account Russia's successful efforts to implement these options, the total offset is likely to be no more than 40% of

current exports to the EU in the mid-run plan. On this basis, it can be concluded that the energy embargo will lead to a significant reduction in Russia's export earnings, which is likely to deal the strongest blow to the stability of the Russian economy and its financial system. In addition, the embargo leads to the loss of such an important trade resource as the positive balance, which in this situation could lead to an increase in external debt. On the other hand, the imposition of the embargo poses a real threat to the economic security of the EU itself, which is related to the large lacking volumes of mineral resources and the logistical problems of diversification, especially in the short run.

Energy security is the basis for the normal functioning of all types of production, so the main task of the EU in implementing this scenario will be to find alternative sources as soon as possible. The main sources of oil in this situation may be the existing suppliers from the OPEC member countries. In addition, a significant increase in US imports can be expected due to increased production and the high interest in maintaining the Euro-Atlantic unity on anti-Russian sanctions.

The main problems for the operational diversification of oil imports are as follows:

- Limited unused capacity for oil production of the OPEC countries and the inability to compensate for the required volumes by increasing production only. In a situation like this, serious diplomatic efforts can be stepped up to divert supplies to the EU from existing consumers (mainly Asian countries).

- Rise in oil prices, which increases EU spending. The embargo against Russia, which accounts for more than 10% of the world oil market, in addition to the sanctions against several major exporters and instability in a number of other oil-producing countries, leads to a significant imbalance between supply and demand, causing oil prices to rise. This situation may also have a positive effect on the growth rate of shale fuel imports from the United States, since rising world prices will ensure profitability.

- Serious logistical problems for imports. Central European countries have no access to the sea, and significant quantities of oil are delivered to the EU via pipelines from Russia. The embargo necessitated the construction of

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new pipelines and infrastructure, while the expansion of maritime supplies is associated with increased costs and congestion in ports.

- Problems with oil refining. Refineries in a number of countries (Hungary, Slovakia, the Czech Republic) are technologically oriented towards the so-called heavy oil grades, to which the Russian Urals variety belongs, and the most important alternative exporters of oil with a similar composition (Iran and Venezuela) are also under the effects of the US sanctions regime. Reconstruction of the processing facilities requires additional time and costs.

An even more challenging task for the EU, in the event of an embargo, is to compensate for the lacking volume of natural gas, the consumption of which, due to price and environmental factors, is showing a steady upward trend. The seriousness of the problem is also related to Russia's almost 40% share in total EU imports. However, in a number of EU member states it is from 70 to 100% (Austria, Bulgaria, the Czech Republic, Estonia, Latvia and Slovakia). It is impossible to compensate for even part of the lost volumes of imports through increasing their own production, given the persistent downward dynamics of production. Norway, the EU's second-largest supplier of natural gas, is unlikely to be able to double its production. Additional supplies through the Southern Gas Corridor pipeline could offset no more than 5% of Russian imports. In this situation, the only real possibility to compensate for the missing volumes can be considered a significant increase in LNG imports from the United States and the Middle East (mainly Qatar in the case of diversion of exports from East Asian countries that do not support sanctions regime against Russia).

The main factor, complicating large-scale diversification is the lack of infrastructure needed to start such large LNG supplies, while the construction of additional regasification terminals and gas pump interconnectors between pipelines also requires significant financial and time costs. Thus, insufficient compensation for the lacking volumes of natural gas as a result of the embargo in the short run could lead to a serious energy crisis in the EU itself. In addition, higher EU financial costs can also be associated with a number of additional factors:

- the significant price difference between Russian pipeline gas and the US LNG;

- the long-run contractual obligations of European oil and gas corporations to pay a penalty to Russia's Gazprom under the so-called "take it or pay it" clause (about \$ 50 billion a year);
- losses due to terminating joint projects in which funds have been invested (eg. Nord Stream-2).

In general, the analysis of this scenario for developing EU trade relations with Russia allows us to assume that its implementation can be caused only by some critical negative changes in the geopolitical situation. Otherwise, the potential risks to the EU economy as a whole, to its individual member states and to big European businesses are important factors hindering the escalation of sanctions against Russia.

Russia's restrictive measures against the EU, since their introduction, have the nature of counter-sanctions and therefore this trend can be expected to continue in the future, while the likelihood of unilateral tightening of sanctions by Russia can be assessed as low.

Conclusion

In conclusion, it should be noted that the scenario envisaging the abolition of reciprocal restrictive measures, according to its cumulative effect, is the most positive from the point of view of the main issues discussed in the study.

The most negative, from the point of view of the development of bilateral trade, is the third scenario, which carries a high risk for the economic security of both partners. It can also become a serious factor for further deepening economic and political instability throughout world.

The most realistic scenario in the short and medium run, according to the authors, would be to maintain the status quo between the EU and Russia in their reciprocal sanctions policy. This option will allow the EU to maintain a rational balance between its geopolitical and economic interests and avoid the additional negative effects of Russia's new counter-sanctions.

The real political and economic environment in which the trading partners interact is characterized by high dynamics and unpredictability,

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and any new factor from the external or internal environment can have a significant impact on the dynamics of the trade relations. This necessitates noting the fact that the presented scenarios do not exhaust the possible options for the development of cooperation between the EU and Russia in the future, yet lay the foundation for future scientific research.

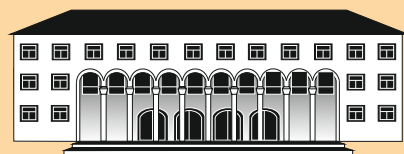
It can definitely be said that the current crisis period in the development of the relations between the EU and Russia is one of the most serious in their history. Due to disagreements on geopolitical issues, a regime of reciprocal sanctions has been introduced, which has a negative impact on the macroeconomic indicators of Russia and the EU member states. According to expert forecasts, the long-run negative economic effects of sanctions could be even more pronounced and dangerous.

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