



ECONOMISTS
FOR UKRAINE

WORKING PAPER SERIES

WORKING PAPER No. 44

SEPTEMBER 2026

CUT OFF FROM CAPITAL: THE IMPACTS OF SANCTIONS ON PORTFOLIO INVESTMENTS

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We would like to thank Oleksandr Talavera and Zuzana Fungáčová as well as participants of BOFIT seminar and Conference on “Global Governance in Transition” for their insightful comments on this paper.

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ABSTRACT

Cut off from capital: the impacts of sanctions on portfolio investments

We examine the impact from sanctions on global capital flows. Sanctions can be understood as an extreme version of geopolitical decoupling that affects economic relations, including trade and foreign direct investment. Specifically, we look at how the introduction of wide-ranging financial sanctions has affected foreign portfolio investment, treating Western sanctions packages on Russia in 2014 and 2022 as a natural experiment. Applying a triple-difference setup and using annual portfolio investment data collected by the IMF, our results show that portfolio investment flows into Russia sharply declined from both sanctioning and non-sanctioning countries particularly after 2022. The decline in investment from sanctioning countries was much more severe, however. Unlike with trade, we find little evidence of investment diversion for Russia after imposition of sanctions.

JEL CLASSIFICATION: F02, F2, F51

KEYWORDS: sanctions, portfolio investment, Russia

Non-technical summary

Focus

The paper examines how Western financial sanctions against Russia have affected foreign portfolio investment (investments in stocks, bonds, and other securities). The paper uses the sanctions imposed after Russia's annexation of Crimea in 2014 and especially after the full-scale invasion of Ukraine in 2022 as a natural experiment to study the impact of sanctions on international capital flows.

Contribution

This paper contributes to the broader literature on geopolitical tensions, and to the sanctions literature specifically, by providing, to the authors' knowledge, the first comprehensive analysis of how financial sanctions affect foreign portfolio investment. Most existing research on sanctions and international investment has so far focused on trade or foreign direct investment

Findings

The 2022 sanctions caused a dramatic collapse in foreign investment in Russian securities. Investment from sanctioning countries fell by roughly 90%, while investment from non-sanctioning countries declined by about 58%, suggesting both direct sanction effects as well as indirect effects such as heightened risk and concerns about secondary sanctions. Unlike trade flows, there is little evidence that investors circumvent sanctions by redirecting investments through third countries. The findings indicate that sanctions have been highly effective in isolating Russia from global capital markets.

1. Introduction

In recent years effects of geopolitical events and risks have been felt throughout the world economy. Correspondingly, economic research has turned to analyzing the effects of geopolitics, decoupling of economies and – as a more extreme version of decoupling – sanctions. Literature on the trade effects of sanctions is already relatively extensive, see for example Morgan et al. (2023) and – in the context of sanctions against Russia – Egorov et al. (2025) as well as Korhonen and Simola (2026).

However, the literature on the effects of sanctions on financial flows is fairly sparse, particularly on the topic of foreign portfolio investment. We take an initial step in filling this gap by studying the impacts of Western sanctions packages introduced against Russia in 2014 and 2022 as a natural experiment. Many countries have introduced sanctions against Russia, and many have not. While portfolio investment to Russia is not absolutely prohibited by sanctions, sanctions limit investment possibilities in a number of ways, for example by prohibiting financing of several Russian large corporations and banks (Korhonen, 2019). We would therefore expect from the outset that sanctions have curtailed foreign portfolio investment flows into Russia to some extent.

Applying a triple-difference setup to annual portfolio investment data collected by the IMF, we find that portfolio investment in Russia from both sanctioning and non-sanctioning countries declined sharply after 2022. The decline in investment from sanctioning countries was much more severe, suggesting an added effect of sanctions. Unlike with trade, we find little evidence of investment diversion for Russia after the imposition of sanctions. This result is quite striking given that sanctions do not explicitly forbid many forms of portfolio investment.

Our study contributes to the growing body of sanctions literature in several ways. It is the first attempt to our knowledge at examining the effects of financial sanctions on portfolio investment, which is more flexible in reacting to uncertainty than foreign direct investment (FDI). We further distinguish between sanctioning and non-sanctioning countries to examine potential diversion of financial flows from sanctioning to non-sanctioning countries. Finally, this paper contributes to the

growing literature on the economic effects of sanctions on Russia, which in themselves are unprecedented in many respects.

The paper is structured as follows. The second section provides a literature survey, the third section introduces the data and its main features, while the fourth section presents our main econometric analysis. The fifth section presents robustness checks and the sixth section concludes.

2. Previous literature

With the massive increase in interest in the effects of geopolitical and geoeconomic factors on international economic relations in recent years, the literature now offers substantial evidence on importance of geopolitical and geoeconomic trends and events for FDI (International Monetary Fund, 2023; Aiyar et al. 2024; Gopinath et al. 2025) and portfolio investment (Kempf et al., 2023; Lugo and Montone, 2026). Broadly speaking, increasing geopolitical distance between countries or groups of countries decreases their bilateral trade and capital flows. Our contribution differs from the previous contributions concerning portfolio investments in that we are looking at macro-level data from a large number of countries instead of e.g. funds or banks operating in the United States.

The specific discussion of sanctions, which are closely linked to wider geoeconomic conflicts, has also emerged. Sanctions can be treated as an extreme manifestation of general political and economic decoupling between countries and country groups. Our contribution speaks to both of these strands of literature. Much of the sanctions literature focuses, however, on macroeconomic or trade effects, whereas financial flows have received little attention. Sanctions have a clear, sometimes sizeable effect on trade flows, and also negative macroeconomic effects especially on the target countries of sanctions (Morgan et al. 2023). However, we are not aware of any studies that examine the effects of sanctions on portfolio investment to the target country.

Research on the effects of sanctions on international investment flows mainly focuses on FDI. Such studies typically find a substantial and relatively persistent negative effect of sanctions on FDI from the sanctioning countries to the tar-

get countries. Gutmann et al. (2021) and Mirkina (2018) examine the effects of sanctions on FDI in a multi-country panel setup. Both studies find a substantial decline in FDI to sanctioned economies especially in the short-run, but the effect is substantial also in longer term. There is also evidence of sanction circumvention through third countries. For example, Lektzian and Biglaiser (2013), who consider sanctions imposed by the United States, find that US FDI to target countries declined sharply after the imposition of sanctions. At the same time, however, FDI to target countries from rest of the world increased, undermining the effectiveness of US sanctions.

Only a handful of studies look at effects of sanctions on financial flows other than FDI. Besedes et al. (2017), who apply detailed data on German cross-border financial flows, find that financial sanctions had a strong and immediate negative effect on German direct financial flows with the sanctioned country. They also uncover evidence of sanction evasion as flows with major trading partners of sanctioned countries increase. Efung et al. (2023) find that domestic banks in Germany reduced lending in sanctioned countries, while their foreign bank affiliates outside Germany increased lending. Berkowitz et al. (2026) look at the evolution of lending via syndicated loans to entities in countries sanctioned by the US. They show that lending to sanctioned countries from G7 countries declined, while Chinese banks, particularly their Hong Kong subsidiary banks, increased their lending. Companies borrowing more from Chinese banks also become more opaque. Ongena et al. (2022) look at financial sanctions and their effects on the foreign borrowing and assets of Russian banks. Not only have sanctions and the anticipation of sanctions had clear effects on these variables, but targets of sanctions also cut their loan supply.

The bulk of research related to recent sanctions packages imposed on Russia focus on the effects of restrictions imposed on exports to Russia. These studies typically find a substantial decline in the sanctioning country exports of sanctioned products to Russia (Chupilkin et al. 2026; Egorov et al., 2025; Korhonen and Simola, 2026). These results further suggest an increase at the same time in exports of non-sanctioning countries to Russia, particularly the export of sanctioned goods. Despite a certain amount of rerouting of exports, most studies conclude that Russia has been unable to compensate fully for the diminution of exports of sanctioned goods from

sanctioning countries. In the specific context of sanctions on Russia, we are unaware of any studies focusing on the effects of sanctions on portfolio financial flows.

3. Data

3.1. Sanctions imposed on Russia

The financial sanctions imposed on Russia by Western countries in 2014 were the consequence of Russia's illegal annexation of Crimea and related events. These sanctions were narrowly focused on a few entities and sectors. They were robustly extended in spring 2022 after Russia's full-scale invasion of Ukraine.

Korhonen (2019) provides a summary of sanctions, including financial sanctions, prior to Russia's invasion of Ukraine. The first set of sanctions imposed in spring 2014 following the annexation of Crimea were quite limited. They included travel restrictions and asset freezes on Russian individuals and organizations, but did not apply to Russia's large state-owned enterprises or the Russian government itself. The second set of sanctions came with the downing of Malaysian Airlines flight MH-17 in July 2014. They included such financial sanctions as prohibitions on providing long-term financing to certain large Russian state-owned companies. Sanctioned entities in the banking sector included Sberbank, VTB, Gazprombank, Rosselkhozbank (Russian Agricultural Bank) and VEB (Russia's state-owned development finance institution, which, strictly speaking, is not a bank). For Sberbank and VTB, which together controlled approximately 60% of the Russian banking market, this was clearly a significant step towards banishing Russian participation in global financial markets. Similar financial sanctions were also imposed on large Russian companies in the energy sector, specifically the oil giant Rosneft, the oil pipeline operator Transneft, the oil company Gazpromneft, as well as many companies involved in the defense sector.

The much tighter and wider sanctions imposed on Russia in the wake of the invasion of Ukraine on February 24, 2022, included financial sanctions. The introduction of specific measures was staggered over time, but the European Union, the United States, the United Kingdom, Canada, Japan, and other allies, coordinated their sanctions. Financing of the Russian government was forbidden, and a large

number of Russian banks were banished from the global financial messaging system SWIFT. Transactions with the Central Bank of Russia (CBR) were also forbidden, effectively freezing Russia's international reserves invested by the CBR in the EU and elsewhere. The net effect was a sharp decoupling of the Russian financial system from investors in the EU, US, UK, and allied countries.

3.2. Data description

Russia has ceased the release of detailed information on foreign investment, so we rely on mirror data collected by the IMF. The Portfolio Investment Positions by Counterpart Economy (PIP) dataset is a voluntary data collection effort conducted under the auspices of the IMF. Participating economies provide data on their holdings of portfolio investment securities by counterpart economies.

Our sample includes annual data for 49 reporting economies and 75 recipient economies,¹ including all major advanced and emerging economies, for the years 2002–2024. The reporting for some economies does not cover the entire observation period. Reporting economies consist of 37 sanctioning economies and 12 non-sanctioning economies.² The combined value of the portfolio investment of the reporting economies accounted for 80% of the portfolio investment recorded by the CBR in 2021. The share of sanctioning countries with respect to the CBR figure was 68%. Among the destination economies included in the sample, Russia is the sole country subject to financial sanctions during the observation period.

The total value of the reporting country portfolio investment to Russia tracks quite closely trends in the official Russian data reported by the CBR (Figure 1). The level is, however, constantly lower suggesting that all investor countries present in Russia are not reporting to the IMF. Both the CBR and IMF data show a sharp drop in the value of portfolio investment in Russia in 2022 with no recovery in the following years. While the trends are similar, the ratio of the combined sum

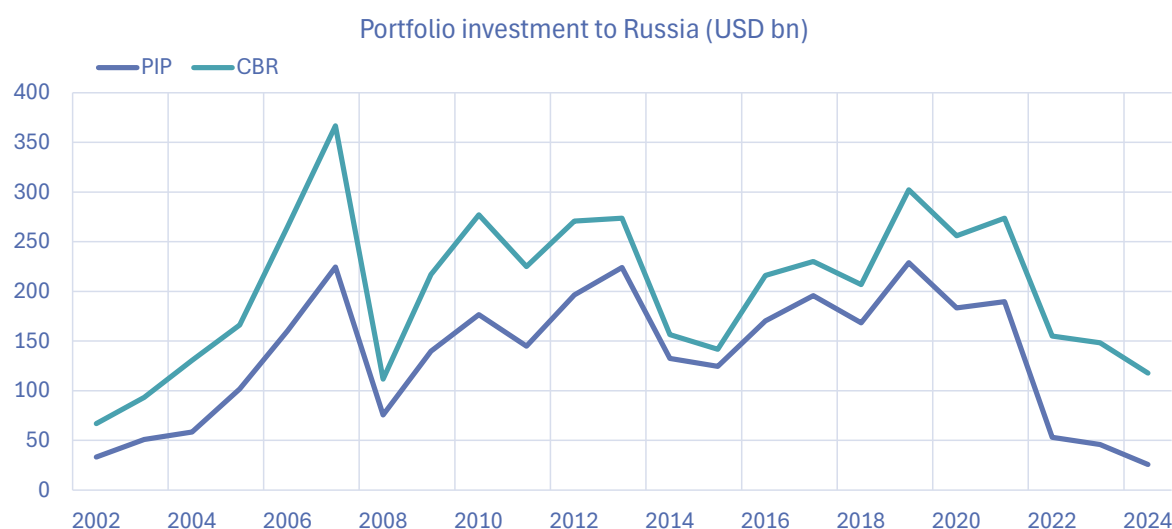
¹ We exclude certain economies from the sample due to large amount of missing observations or large amount of very small investment values.

² The UK overseas territories (Bermuda and Cayman Islands) are included as sanctioning economies. Sanctioning and non-sanctioning investor countries and territories included in the sample are presented in the Appendix.

of mirror investments to the total value reported by the CBR declined sharply in 2022.

In 2012–2021 on average, the total sum of investment reported to the IMF was nearly 80% of the sum reported by the CBR. In 2022–2024, the ratio dropped to just below 30%. In value terms, the declines shown in the CBR data and IMF data are roughly similar for recent years. The CBR data show the value of foreign portfolio investment in Russia declined by \$156 bn between 2021 and 2024, while the IMF data show a drop of \$164 bn. This discrepancy suggests that the IMF data cover at least the majority of those countries that reduced their investment in Russia, while those not reporting to the IMF retained their investment positions in Russia to some degree.

Figure 1. Stock of portfolio investment to Russia in 2002–2024.



Sources: CBR, IMF PIP.

We only have yearly data on the portfolio investment stock, not the portfolio investment flows. In principle, a decrease in the investment stock might reflect divestment or negative valuation effects. Various analyses suggest foreign investors exited the Russian market on a mass scale (BOFIT, 2023). The CBR data further show that the share of foreign investors in the government bond (OFZ) market declined from 20% in 2021 to 3% in early 2026. The ruble's exchange rate also strengthened in 2022, which would imply an increase in bond valuation in USD terms. The USD-based Moscow Stock Exchange index RTS declined approximately 32% from

the end of 2021 to the end of 2023. Thus, we find it plausible that the decline in portfolio investment stock primarily reflects divestment of foreign investors from Russian assets, even if valuation effects are also present.

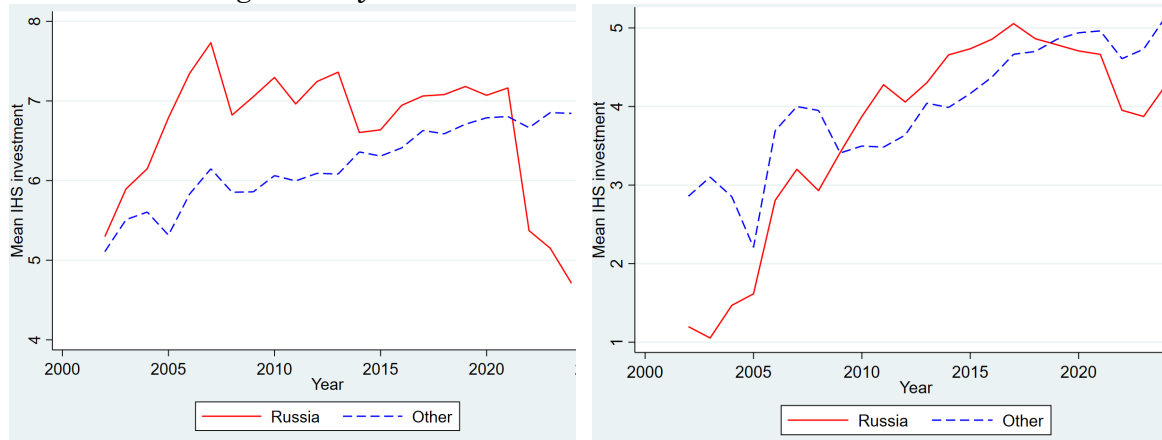
3.3. Preliminary analysis of the data

Preliminary inspection of the data suggests that the trends in portfolio investment from sanctioning countries to Russia and other destination countries were not substantially different for most years before 2022 (Figure 2.A). Following the exceptional drop in investment to Russia in 2014, the trend in investment flows into Russia follows a pattern similar to other countries up to 2022. In that year, we see a sharp drop in investment flows into Russia dissimilar to trends for other countries. Moreover, we see no recovery in subsequent years.

Regarding non-sanctioning countries, the investment trends for Russia and other countries are very similar up to 2022 (Figure 2.B). For non-sanctioning countries, there appears to be no particular effect on investment to Russia in 2014. In 2022, investment to Russia from non-sanctioning countries declines, but the drop is milder than for sanctioning countries. For non-sanctioning country investment there is modest recovery in investment during the most recent years, but not to the pre-sanctions level.

This suggests that Russia has been a special case as an investment target in recent years, with investment in Russia from both sanctioning and non-sanctioning countries declining. This drop could reflect perceived increased risk associated with Russian markets due to the war, but it could also reflect the effect of sanctions – *directly* for sanctioning countries and *indirectly* for the non-sanctioning countries due to the risk of secondary sanctions. Focusing on sanctioning and non-sanctioning country investment to Russia shows that the drop in sanctioning country investment has been much stronger, however, emphasizing the role of sanctions. Combined investment from sanctioning countries was 87% lower in 2024 than in 2021, while investment from non-sanctioning countries fell by only 24%.

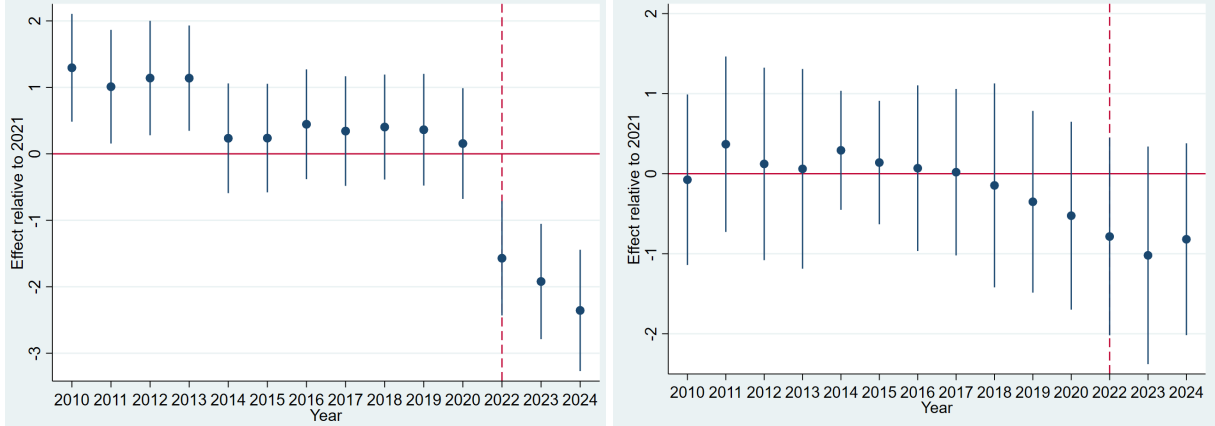
Figure 2. A) Sanctioning country investment to Russia and other destinations B) Non-sanctioning country investment to Russia and other destinations.



We next apply an event-study setup to examine the development of investment flows in greater detail and formally validate our assumption of parallel trends. We first compare the evolution of sanctioning country investment to Russia. Investment flows clearly drop in 2014 and remain thereafter somewhat steadily at a lower level until 2022 (Figure 3.A). The data then show a sharp and statistically significant drop in investment flows from sanctioning countries to Russia. There is no recovery in the following years, and the effect becomes even more pronounced. Regarding non-sanctioning countries, the development is quite stable until 2022 (Figure 3.B). There is a drop in investment from non-sanctioning countries in 2022–2023, but it is not statistically significant. Thus, the formal tests support the assumption of parallel trends.³ The coefficients for the years preceding imposition of sanctions are not statistically significantly different from zero.

³ If we regress the IHS of investment value with the interaction of year dummies and Russia as the destination country, the individual year coefficients preceding the imposition of sanctions are small and statistically not significant. The joint test for the most recent years preceding the imposition of sanctions also fails to reject the hypothesis that the pre-treatment coefficients are jointly zero.

Figure 3. Event study for the impact of sanctions imposed in 2022 on portfolio investment flows to Russia from A) sanctioning countries and B) non-sanctioning countries.



Note. Investor, destination and year-specific fixed effects included. Robust standard errors clustered by investor-destination pairs.

4. Empirical estimation

4.1. Baseline estimation

For a more formal empirical examination, we estimate a triple-difference setup with three dummy variables. Our time dummy gets a value of 1 from 2014 or 2022 onwards, and zero otherwise. The dummy variable for Russia is assigned 1 when Russia is the destination country of investment, and zero otherwise. Our final dummy depicts whether the investor country has imposed sanctions on Russia. The baseline regression is as follows:

$$PI_{ijt} = \text{SanctioningCountry} \times \text{Russia} \times \text{SanctionTime} + FE_i + FE_j + FE_t + FE_{ij} \quad (1)$$

The dependent variable, PI_{ijt} , is the value of portfolio investment from country i to country j in year t . It is regressed on the interaction term of dummies depicting the sanctioning position of the investor country, Russia as the target country, and the time period when sanctions are implemented. We include a rich set of fixed effects to control for other variables.

Since the sample includes many zero observations, we cannot readily estimate equation (1) in log terms. We first use inverse hyperbolic sine (IHS) transformation that can handle the zeros.⁴ As a robustness check we also use the PPML estimation in line with the literature on gravity models of international trade.

We first focus only on sanctioning countries. In these estimations we include two interaction terms separately for sanctions imposed in 2014 and 2022. The main variables of interest are the interaction terms of sanctioning countries, Russia as the investment destination and the time period sanctions are effective. In the second specification we construct separately corresponding interaction terms for non-sanctioning countries to examine the effects of sanctions on their investment to Russia.

The results are qualitatively quite similar in both specifications (Table 1). For sanctioning countries, the sanctions imposed in 2014 already had a notable negative effect on investment which is also statistically highly significant. The effect of 2022 sanctions is even much more substantial and also highly statistically significant. For non-sanctioning countries, we find statistically significant effect only for the 2022 sanctions. The effect is quite large and statistically highly significant in both specifications.

We also test if the coefficients differ statistically significantly. As could be expected, the impact of 2022 sanctions is much stronger than the effect of 2014 sanctions on the sanctioning countries investment in both specifications. Comparing the coefficients of sanctioning and non-sanctioning countries shows that the coefficients for both 2014 and 2022 sanctions are substantially higher in absolute terms for sanctioning countries and the difference is statistically significant.

In terms of economic significance, the effect is also substantial. In the case of relatively large variable values, the IHS approximately describes the semi-elasticity, similar to the PPML coefficient⁵. Therefore, our results suggest that the sanctions imposed in 2014 reduced sanctioning country portfolio investment in Russia by about 60 % and the sanctions imposed in 2022 by 90 %. In addition, the 2022

⁴ More formally, inverse hyperbolic sine function can be written as $\text{arshinh}(x) = \ln(x + \sqrt{x^2 + 1})$.

⁵ Therefore the effect in percentage change terms is calculated as $(\exp(\beta) - 1) * 100$.

sanctions reduced portfolio investment from non-sanctioning countries to Russia by 58 %.

Table 1. Regressions on the impact of sanctions on foreign portfolio investment to Russia.

	Dependent variable: IHS investment	
	Specification 1	Specification 2
Sanctioning country x Russia x Post-2014	−0.8383*** (0.1782)	−0.8378*** (0.1783)
Sanctioning country x Russia x Post-2022	−2.1656*** (0.1902)	−2.1684*** (0.1902)
Non-sanctioning country x Russia x Post-2014		0.1400 (0.4480)
Non-sanctioning country x Russia x Post-2022		−0.8602*** (0.3455)
N	71,417	71,417
R ²	0.89	0.90

Note. Constant term included, but not reported. All specifications include investor, target, year and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

4.2. Equity and debt investment

We now split portfolio investment into equity and debt categories and estimate the same regressions for both investment types separately. The overall results are quite similar (Table 2). For sanctioning countries, both 2014 and 2022 sanctions have a substantial negative effect on both equity and debt investment to Russia. The effect is highly statistically significant in various specifications. For both investment types the effect is also much more pronounced in 2022.

For non-sanctioning countries, the 2014 sanctions have no statistically significant effect on either equity or debt investment. The effect of 2022 sanctions is negative for both equity and debt investment, but statistically significant only for debt investment. The effect is also quantitatively quite large, although smaller than for sanctioning countries. This suggests that the indirect effect of sanctions (i.e. effect on non-sanctioning country investment) was particularly strong for debt instruments.

Table 2. Regressions on the impact of sanctions on foreign portfolio investment to Russia separately for equity and debt investment.

	Dependent variable: IHS equity		Dependent variable: IHS debt	
	Specification 1	Specification 2	Specification 3	Specification 4
Sanctioning country x Russia x Post-2014	−0.6524*** (0.1875)	−0.6513*** (0.1875)	−0.7368*** (0.2146)	−0.7365*** (0.2147)
Sanctioning country x Russia x Post-2022	−2.1128*** (0.2135)	−2.1158*** (0.2134)	−2.1819*** (0.2714)	−2.1846*** (0.2714)
Non-sanctioning country x Russia x Post-2014		0.3641 (0.3498)		0.0655 (0.4500)
Non-sanctioning country x Russia x Post-2022		−0.8801 (0.7234)		−1.1234*** (0.3532)
N	66,131	66,131	66,761	66,761
R ²	0.91	0.91	0.87	0.87

Note: Constant term included, but not reported. All specifications include investor, target, year, and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

4.3. Offshore financial centers and other economies

Our data include several offshore financial hubs (e.g. Eurostat, 2021). Among these hubs in our sample (i.e. Bahrain, Barbados, Bermuda, Cayman Islands, Guernsey, and Jersey), Bahrain and Barbados have not imposed sanctions on Russia. The other offshore hubs are subjects of the UK and thus assumed to abide by UK sanctions. Next we examine if the results differ for offshore financial centers and other economies. We perform the same regressions as above, but for offshore financial centers and other economies separately.

Our results suggest that the effects of sanctions on portfolio investment to Russia have been somewhat different for offshore financial centers than other economies. Regarding sanctioning countries, the effects of both 2014 and 2022 sanctions are negative, but statistically significant, only for 2022 (Table 3). Among non-sanctioning countries, the effect of 2014 sanctions was *positive*, as well as quantitatively large and statistically significant. The effect of 2022 sanctions was negative for non-sanctioning offshore financial centers, but not statistically significant. These results

indicate that there could have been circumvention of sanctions or reducing risks of secondary sanctions by steering investment to Russia via offshore financial centers following the initial rounds of sanctions in 2014.

Table 3. Regressions on the impact of sanctions on foreign portfolio investment to Russia separately for offshore financial centers and other economies.

Dependent variable: IHS investment				
	Offshore financial centers		Other economies	
	Specification 1	Specification 2	Specification 3	Specification 4
Sanctioning country x Russia x Post-2014	−0.6089 (1.0470)	−0.6071 (1.0472)	−0.8668*** (0.1504)	−0.8665*** (0.1504)
Sanctioning country x Russia x Post-2022	−2.5974*** (0.5557)	−2.6010*** (0.5558)	−2.1092*** (0.1987)	−2.1119*** (0.1987)
Non-sanctioning country x Russia x Post-2014		0.5970*** (0.2133)		0.0661 (0.5141)
Non-sanctioning country x Russia x Post-2022		−1.0420 (0.9807)		−0.8571** (0.3647)
N	8,603	8,603	62,814	62,814
R ²	0.75	0.75	0.91	0.91

Note: Constant term included, but not reported. All specifications include investor, target, year, and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

5. Robustness checks

First we check that the results are robust to the estimation methodology that we have chosen. Another common estimation approach in the presence of large amount of zero flows is the PPML estimation that is applied particularly for gravity models of international trade. The PPML estimation results are qualitatively and largely also quantitatively similar to our baseline estimations. The effect of sanctions is quite strongly negative and statistically highly significant both in 2014 and 2022, both for sanctioning and non-sanctioning countries (Table 4). Comparing the coefficients of sanctioning and non-sanctioning countries shows that the effect of sanctions imposed in 2022 is substantially higher in absolute terms for sanctioning countries and also statistically significant.

Table 4. Regressions on the impact of sanctions on foreign portfolio investment to Russia with PPML

	Dependent variable: Investment	
	Specification 1	Specification 2
Sanctioning country x Russia x Post-2014	−1.0024*** (0.1341)	−1.0024*** (0.1341)
Sanctioning country x Russia x Post-2022	−1.8895*** (0.3030)	−1.8895*** (0.3030)
Non-sanctioning country x Russia x Post-2014		−0.9633*** (0.2905)
Non-sanctioning country x Russia x Post-2022		−0.8229*** (0.2406)
N	70,697	70,697
R ²	0.99	0.99

Note. Constant term included, but not reported. All specifications include investor, target, year and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

Then we examine if the negative effect on sanctioning country investment is specific to Russia or applies also to other emerging economies. In a placebo-style experiment we perform the same regressions as above for India, Kazakhstan, Mexico and Serbia. We find no negative effects on the investment from sanctioning countries to any of these economies (Table 5). For Kazakhstan, the coefficients are small and not statistically significant. For India, Mexico and Serbia, the coefficients are actually positive, although not always statistically significant. These findings support our hypothesis that the negative effect on sanctioning country portfolio investment is related particularly to Russia. The positive result for India can reflect the rapidly increasing weight of India in various emerging market stock indices (e.g. the MSCI EM index) in the past years.

Table 5. Regressions on effects of sanctions on other countries than Russia.

Dependent variable: IHS investment				
	India	Kazakhstan	Mexico	Serbia
Sanctioning country x Target x Post-2014	0.4507** (0.1906)	0.1209 (0.2251)	0.5278*** (0.2029)	0.3752 (0.3618)
Sanctioning country x Target x Post-2022	0.5562** (0.2493)	0.0180 (0.2691)	0.3357 (0.2419)	0.7808** (0.3802)
N	71,417	71,417	71,417	71,417
R ²	0.89	0.89	0.89	0.89

Note. Constant term included, but not reported. All specifications include investor, target, year and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

To emphasize the individual role of sanctions beyond general geopolitical risks related to Russia's war against Ukraine, we check whether our results hold if we control for the destination country geopolitical risk. We employ the commonly used country-specific geopolitical risk indices constructed by Caldara and Iacoviello (2022). As the authors note, the indices capture the U.S. perspective on risks involving the country in question, so we consider it highly relevant for the decisions of foreign portfolio investors. The data covers 41 of our destination countries, including Russia. We aggregate the data to annual averages for our estimations and use log deviation from the country average across 2002–2024. Our results show that geopolitical risk has a negative and statistically significant effect on portfolio flows (Table 6). Nevertheless, the results for sanction effects remain very similar both qualitatively and quantitatively and are still highly statistically significant.

Table 6. Regressions controlling for geopolitical risk

Dependent variable: IHS investment		
	Specification 1	Specification 2
Sanctioning country x Russia x Post-2014	−0.8220*** (0.1795)	−0.8217*** (0.1795)
Sanctioning country x Russia x Post-2022	−2.1725*** (0.1910)	−2.1785*** (0.1910)
Non-sanctioning country x Russia x Post-2014		0.1537 (0.4482)
Non-sanctioning country x Russia x Post-2022		−0.8710** (0.33462)
Geopolitical Risk Index	−0.0007** (0.0003)	−0.0007** (0.0003)
N	38,467	38,467
R ²	0.91	0.91

Note. Constant term included, but not reported. All specifications include investor, target, year and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

To further examine the robustness of the results, we limit the sample to those investor-destination pairs that exist in the data throughout 2015–2024 in every year. Now we also have to limit the analysis to the sanctions imposed in 2022. The results are both qualitatively and quantitatively very similar to the baseline estimations and remain highly statistically significant (Table 7). This provides support that our results are not driven simply by the exit of certain specific investor-target pairs.

Table 7. Regressions on the impact of sanctions on foreign portfolio investment to Russia for a sample limited to those investor-destination pairs that are present in the data for the whole period of 2015–2024.

Dependent variable: IHS investment		
	Specification 1	Specification 2
Sanctioning country x Russia x Post-2022	−2.1532*** (0.1855)	−2.1558*** (0.1855)
Non-sanctioning country x Russia x Post-2022		−0.9000** (0.3747)
N	31,428	31,428
R ²	0.95	0.95

Note. Constant term included, but not reported. All specifications include investor, target, year and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

Portfolio investment flows can fluctuate sharply across individual years. To address this concern, we perform the baseline regressions for three-year non-overlapping moving averages for 2016–2024, as well as 2011–2013 versus 2022–2024. The results are again quite similar for sanctioning countries both qualitatively and quantitatively (Table 8).

For non-sanctioning countries, the coefficient is also negative, but statistically significant only in the specification with more time periods. These results support our main findings that the sanctions have substantially reduced portfolio investment from sanctioning countries to Russia. There are no signs of investment diversion to non-sanctioning countries. The results point to an indirect negative effect from sanctions to investment from non-sanctioning countries, although this result is less compelling.

Table 8. Regressions on the impact of sanctions on portfolio investment to Russia over longer periods.

Dependent variable: IHS investment				
	2016–2024 3Y-ma		2011–2013 vs. 2022–2024	
	Specification 1	Specification 2	Specification 3	Specification 4
Sanctioning country x Russia x Post-2022	–2.1964*** (0.1798)	–2.1987*** (0.1798)	–2.0890*** (0.2912)	–2.0890*** (0.2913)
Non-sanctioning country x Russia x Post-2022		–0.7569** (0.3582)		–0.4731 (0.5415)
N	10,131	10,131	6,448	6,448
R ²	0.96	0.96	0.84	0.84

Note. Constant term included, but not reported. All specifications include investor, target, year, and investor-target fixed effects. Robust standard errors clustered by investor-target pairs in all specifications.

6. Conclusions

In this paper, we assessed the effects of financial sanctions on portfolio investment flows into Russia, a topic which to our knowledge has not been analyzed in the previous literature. The imposition of sanctions on Russia, a country deeply integrated with the global markets, provides a natural experiment for estimating sanction effects. Moreover, many countries have embraced financial and non-financial sanctions regimes on Russia, but many other countries have not.

We find that the sanctions packages introduced in 2022 had a very strong negative effect on portfolio investment in Russia. This negative effect extends to countries that have not officially sanctioned Russia or Russian entities, but its absolute size is smaller for investors in these countries. Moreover, we find no evidence of investment diversion, that is, investors in sanctioning countries redirecting their investments to Russia via non-sanctioning third countries.

It is easy to understand why investors in countries imposing sanctions are reluctant to invest in Russian assets, even if investing in particular asset classes is legal. What is interesting is that many investors in countries not imposing sanctions have also become reluctant about investing in Russian assets. One can speculate that since sanctioning countries in this instance are the largest OECD countries with the largest and the most liquid capital markets, investors in non-sanctioning third countries do not want risk access to these markets. If true, this tells us about

the efficacy of financial sanctions when imposed by the largest countries or countries with the largest capital markets.

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Appendix. Investor countries and territories included in the data sample.

Sanctioning countries and territories	Non-sanctioning countries and territories
Australia	Bahrain
Austria	Barbados
Belgium	Brazil
Bermuda	China
Bulgaria	Hong Kong
Canada	Israel
Cayman Islands	Kazakhstan
Cyprus	Mexico
Czech Republic	Saudi Arabia
Denmark	South Africa
Estonia	Thailand
Finland	Türkiye
France	
Germany	
Greece	
Guernsey	
Hungary	
Ireland	
Italy	
Japan	
Jersey	
Korea	
Latvia	
Lithuania	
Luxembourg	
Netherlands	
Norway	
Poland	
Portugal	
Romania	
Slovak Republic	
Slovenia	
Spain	
Sweden	
Switzerland	
United Kingdom	
United States	

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