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CSD CENTER FOR THE STUDY OF DEMOCRACY

STRATEGIC DECOUPLING

Phasing out Russian economic influence in Germany

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ANALYSIS

Imprint

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Content

Executive Summary

Russia's war of aggression in Ukraine upended European peace and security and intensified global power competition. The Kremlin overturned decades of accommodating German Ostpolitik as it chose to weaponize Germany and Europe's decision to opt for Russian gas as a transition fuel for achieving green transformation. Russia's most potent tool in this global rivalry has been **state capture** – the use of military or law enforcement coercion to weaponize state, oligarchic or private sector economic resources for achieving foreign policy goals. **Decoupling and/or de-risking** from the corrosive impact of this state capture model is paramount for democratic Europe's economic security.

There are a range of **tools of Russian influence** in Germany: the promotion of large-scale energy projects as well as the support of political parties with anti-Western agendas; the locking of companies and assets in long-term deals, and the flooding of the cyber and media space with disinformation and propaganda.

The following report is an assessment of the magnitude of Russia's **direct and indirect economic footprint** in Germany, with a focus on energy intensive industries, which form the backbone of the country's economic might.

Despite Moscow's increasingly authoritarian posture, and even after the annexation of Crimea in 2014, Germany continued deepening its trade and investment relations with Russia, ensuring uninterrupted influx of capital and technology. The largest Russian companies, many of which state-owned, struck successful cooperation agreements with German firms. Such links have undermined the timely and effective **enforcement of sanctions** and **goods control**, dampening EU and Germany's response to Kremlin's aggression.

Most notably, German companies, together with European peers, teamed up with Gazprom to jointly develop the **Russian geopolitical gas pipeline projects** Nord Stream 1 and 2, which weakened considerably the economic security of Ukraine and Central European EU countries.

The cornerstone of the Russian-German economic ties has been the import of cheap Russian energy for powering German heavy manufacturing, which then exports back high added-value products and sophisticated technology. While the bilateral trade turnover had been on the decline already before the Russian invasion of Ukraine, German companies had invested more than EUR 21 billion by the end of 2021, making the country the third biggest investor in Russia following Cyprus and the Netherlands. Although Russian Foreign Direct Investment (FDI) in Germany is comparatively miniscule, it has been concentrated in a few strategic economic sectors such as energy supply (mostly oil refining, natural gas transmission, storage and distribution).

Many German companies continue operating in Russia and there are still several thousand Russian firms active in different German markets. Given Russia's proven track record in abusing corporate networks for foreign policy goals, including through deploying **strategic corruption**, these company networks pose economic and investment security risks. These risks are likely to increase as the Kremlin seeks to evade sanctions by further obfuscating final beneficial ownership of its companies.

There were 1713 companies with Russian ultimate beneficial ownership in Germany at the end of 2022. The **Russian corporate presence in Germany is highly concentrated** in around 40 larger firms, which specialize in oil refining, natural gas supply and distribution, metal and plastic products manufacturing, glass production, and transport. These firms employ thousands of personnel and possess strategic assets worth billions. EU sanctions have limited the capacity of these firms from gaining further strategic edge and from acquiring more assets in certain industries in Europe. Yet, their potential for malign influence through the abuse of their local corporate networks and/or covert operations remains high.

The **geopolitical risks to the energy and climate security** of Germany have markedly increased after Russia's annexation of Crimea in 2014. The share of Russian gas increased to 49% of total German gas imports by 2019, compared to 34% in 2009. As a result of this short-sighted policy bet, at the time of Moscow's invasion in Ukraine in February 2022, Germany was one of the most vulnerable EU countries in terms of security of supply and overall energy and climate security vis-à-vis Russia. In the first weeks of the invasion, German businesses were one of the most vocal prophets of an impending geoeconomic Armageddon for Europe, disorienting and delaying EU and Germany's strategic policy response. The decade-long delay in responding to Russia's aggressive authoritarianism led to a painful tradeoff for Germany. According to CSD's Energy and Climate Security Risk Index (ECSRI), the significant improvement of the security of German energy supply on the back of measures to almost completely phase out Russian oil, gas and coal imports came at an enormous costs in the form of higher energy poverty and diminished industrial competitiveness.[1]

The Kremlin's war in Ukraine has disenchanted decades of German foreign policy towards Russia. The scale and brutality of the Russian invasion have summoned a decisive

1 According to the ECSRI, the affordability risks to energy and climate security rose in Germany by more than 100% in 2022. More details about the energy security/affordability tradeoff can be found in the sections below.

response from the German society and the German government, following the initial shock. As a result, **Germany has quickly inaugurated emergency economic security and decoupling polices** in the energy sector, and has upheld unprecedented EU and G-7 sanctions and technology and goods control on Russia. Next, Germany needs to work on strengthening further its national and the European economic security institutions.

As a first line of defense, Germany needs to complete its decoupling from Russia to make sure Moscow would not be able to deploy any of its Kremlin Playbook instruments in the future. The German government needs to develop capacity to design and implement a **well calibrated economic de-risking strategy**, as a major dress-rehearsal for addressing China's rising global assertiveness. Germany should spearhead and support EU efforts to design and kick start a common economic security strategy with its respective instruments on risk assessment, investment screening, customs and financial intelligence coordination, anti-money laundering, etc. Economic security needs to be counterbalanced with a comprehensive European nearshoring and investment strategy built around leadership in green and digital technologies.

The next steps of Germany's decoupling and de-risking of its economic relationship with Russia should see the German businesses continuously and gradually **phase out their exposure to the Russian market** by closing their operations in Russia and by letting joint ventures and corporate partnerships with Russian companies expire. There is also an urgent need to continuously map the **informal Russian economic and political networks active in Germany** and dismantle their influence. Germany and the EU need to build up institutional defenses to fend off strategic corruption attempts and raids on Europe's technological base.

Germany's economic security strategy requires sophisticated mechanisms for **screening and halting** of overt and covert Russian strategic investments in Europe linked to state-owned companies and oligarchic networks close to the Kremlin. Such screening needs to be complemented by measures for ensuring intra-EU corporate ownership transparency and the **strengthening of the European anti-money laundering infrastructure** and efforts on reducing the Kremlin's hidden economic footprint in Europe.

On the EU level, a **common EU mechanism for sanctions enforcement** is needed that prescribes specific requirements for national customs officials to investigate the ultimate beneficial ownership of the EU companies selling sanctioned and dual use goods and that of buyers in third countries.

1. Introduction

Russia's war of aggression in Ukraine has upended European peace and security, challenged the international rule-based order that has persisted for over seventy years, and intensified global power competition. With the start of its full-scale invasion, the Kremlin also undermined decades of accommodating German Ostpolitik. **Moscow chose to weaponize** the controversial decision of Germany and many other European nations to rely on Russian gas as a transition fuel during their green transformation. China's continued support for the Kremlin, albeit more muted and couched in diplomatic language, has helped divide the global community into opposing camps, leading to a rise in transactional diplomacy on a global level, mostly at the expense of Russia and the European Union (EU). Moscow and Beijing's most potent tool in this new period of global rivalry has been state capture – the use of corrosive capital or other forms of economic or geopolitical coercion to direct state, oligarchic or private sector economic resources to achieve desired foreign policy goals, while still benefiting from international free market rules.[2] **Decoupling and/or de-risking** from the corrosive impact of this state capture model is paramount for the survival and prosperity of a democratic Europe.

The EU and Germany, as its most powerful economy and most populous democracy, aim to strengthen their global standing by upholding common transatlantic defence and security efforts, bolstering their internal democratic resilience, and safeguarding their economic and investment security.[3] **Accommodating Russia** even when its foreign policy actively undermines European security, as the EU did after the annexation of Crimea, **is no longer defensible**. Almost a decade later, in the wake of last year's full-scale invasion of Ukraine, both the EU collectively and many member-states individually have moved to reduce and eventually end their economic dependence on Russia by imposing a series of economic sanctions on the Kremlin and its network of state-controlled corporations, as well as discontinuing the import of Russian gas and oil.

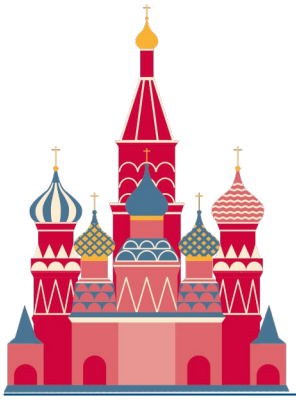
While **sanctions** have been effective in cutting some financial ties between Europe and Russian businesses and impeding the Kremlin's weaponization of energy, their **enforcement** has been alarmingly inconsistent. This has proven especially concerning with regard to control of sensitive technologies and dual-use goods, as well as the disruption of overt and covert corporate networks of influence. The German government has implemented a number of measures aimed at almost fully eliminating its dependence on Russian fossil fuel imports and discontinuing Gazprom's corrosive corporate presence in the German economy. However, **vulnerabilities in key sectors persist**, and the need remains for more comprehensive policy action to fully decouple Germany from the Russian state capture networks which fuel the Kremlin's war machine and continue to threaten the economic security and democratic institutions of both Germany and the EU. Complicating matters, these attempts at decoupling from Russia have been constrained by increasing dependence on China. The German government has acknowledged the problematic nature of this dependence in its first ever National Security Strategy which aims to de-risk and friend-shore its economy. Yet, calling China a "partner, competitor, and systemic rival"[4] at the same time also shows the country's hesitant approach on taking action to counter China's growing economic and political assertiveness and coercion globally. More specific de-risking measures have been agreed under the proposal of the European Commission for a European Economic Security Strategy, including the introduction of an Anti-Coercion Instrument to "deter countries from restricting or threatening to restrict trade or investment to bring about a change of legitimate policy in the EU"[5], and the creation of a Critical Raw Materials Club to build long-term partnerships with resource-rich countries for fair and sustainable trade that benefits all countries involved.

The Russian economic influence in Germany is the result of Moscow's usage of a variety of **instruments from the Kremlin Playbook toolbox**. These tools replicate the Kremlin's domestic state capture power in Russia, where the two defining characteristics of the political regime in Moscow, **autocracy and corruption, blur the boundary between state and private capital**. The concentration of economic and political power in the hands of a small number of current or former security service officials cemented the Kremlin's grip on Russian society and allowed it to pursue its revisionist foreign policy. Russia replicates its domestic fusion between business and political interests via its foreign and strategic policy in Europe; this malign influence campaign exploits and thrives on social, economic, and political polarization, as well as democratic deficits and governance gaps, which provide important entry points for the Kremlin and other authoritarian influences.

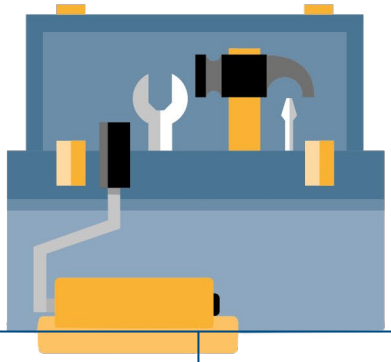
In Germany, the Kremlin has relied on both institutional enablers and governance gaps, such as corruption and bias in politics and government, ineffective enforcement of existing laws, and media polarization, among others.[6] The Kremlin utilizes four recurrent **tools of Russian state capture influence** in Germany: the promotion of large-scale energy projects involving Russian participation, the support of political parties with anti-Western agendas, the entangling of

2 Shentov, O., Stefanov, R. and Vladimirov, M. (eds.), *The Kremlin Playbook in Europe*, Sofia: Center for the Study of Democracy, 2020.
3 Center for the Study of Democracy, *Countering the Kremlin Playbook in Europe after Russia's Invasion of Ukraine*, Policy Brief No. 115, October 2022.
4 Die Bundesregierung, *Integrierte Sicherheit für Deutschland – Nationale Sicherheitsstrategie*, June 2023.
5 European Commission, *European Economic Security Strategy*, June 2023, p. 8.
6 Galev, T., Gerganov, A. und Todorov, B. (Hrsg.), *State Capture Deconstructed: Risk Measurement in Vulnerable Economic Sectors in Europe*, Sofia: Center for the Study of Democracy, 2021.

Fig. 1 | The Kremlin's instruments for weaponizing its state capture power for foreign policy goals



Toolbox instruments



The Kremlin's state capture power

blurs the boundary between state and private sectors in Russia through the abuse of law enforcement and media for achieving foreign policy goals.

The Kremlin's hard power:

military, political and economic threats ←→ fusion of political and economic power controlled through security networks.

The Kremlin's soft power:

common ethnic, religious, linguistic, historical bonds, cultural, educational, etc., exchanges, civil society financing, ownership of sports clubs, establishing networks of pro-Russian cultural, sports, hunting, etc., organizations.

The Kremlin's sharp power:

controlled media in Russia, which beams distorted facts and realities, including through international state-owned or commercially controlled media and telecom channels; glorifying the illiberal, nationalist, state-controled market economy; propagating Russia's military supremacy and might; divisive messaging on any issues of conflict in Europe.

- → Socio-political divisions; lack of strategic clarity; political extremism; institutional deficiencies, in particular rule of law, anti-money laundering, anti-corruption, regulatory bodies.
- → Corruption and governance deficits; unreformed, state-owned, centralized markets; lack of access to deep capital markets.
- → Powerful [former communist] security and oligarchic networks; para-military establishments, light clubs, gun clubs.

- → Civil society capture through ownership and funding; lack of local civil society development mechanism.
- → Lack of public debate culture; lack of societal agreement on the division of politics and history; lack of local initiatives and traditions in supporting and moderating Russian cultural, educational, sports ties.

- → Media capture, lack of mechanism for disclosing final beneficial ownership of media, media market concentration and oligarchization through ownership and advertising.
- → Unclear EU perspective, deficiencies of EU decision-making process and democratic credentials; lass of transformative pull from the EU.

Local governance and state capture vulnerabilities provide fertile ground for Russian influence operations.

Source: Center for the Study of Democracy (CSD)

strategic companies and assets in long-term deals with Russian or Russian-aligned firms, and the flooding of the cyber and media space with disinformation and propaganda.[7] Russia's oligarchs, often appointed by the state, need access to the government to preserve and enlarge their wealth. In return, the Kremlin avails itself of their wealth to further its foreign policy purposes.

The following report is a strategic assessment of the scale and magnitude of the Kremlin's economic influence in Germany. The analysis focuses specifically on the direct and indirect Russian economic footprint in Germany's energy-intensive industries, which form the backbone of the country's economy.

2. Mapping Russia's economic footprint in Germany

Despite Russia's increasingly aggressive and revanchist rhetoric towards Ukraine, which openly challenged international laws and norms, Germany continued to follow its "Wandel durch Handel" (change through trade) doctrine, assuming that economic interdependence would be sufficient to quell any Russian plans for further military aggression.

Germany deepened further its economic ties to Moscow, forging stronger trade relations, financing large-scale joint projects, and allowing a significant flow of German capital and technology into Russia. Many of Russia's largest companies, a majority of which are either state-owned or closely state-affiliated via networks of oligarchs, struck successful cooperation agreements with German firms.

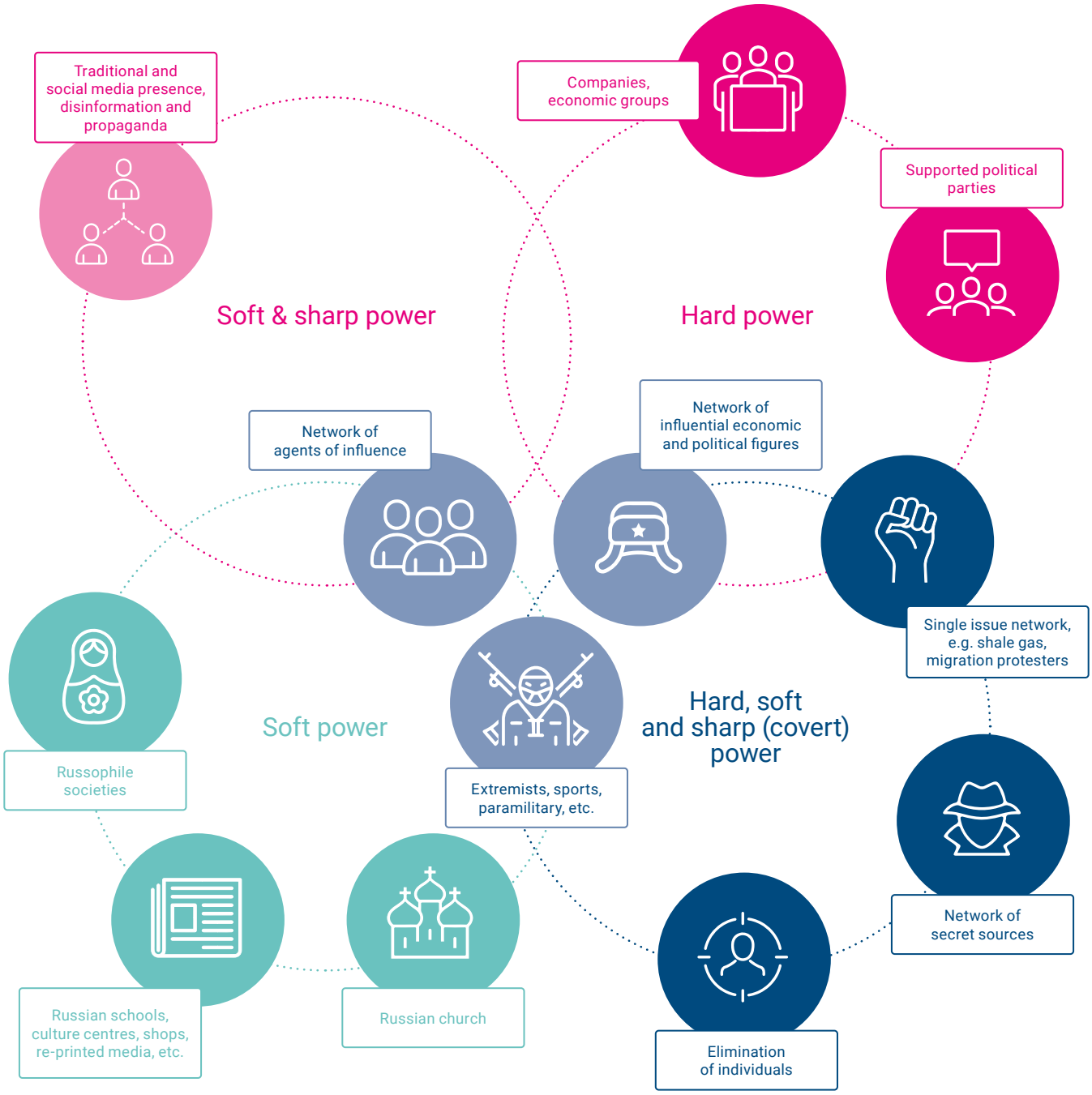
Most notably, in what has now become an infamous example of Berlin's short-sighted Ostpolitik, German companies, together with European peers, teamed up with Russian state oil giant Gazprom to jointly develop the **Russian undersea gas pipeline projects Nord Stream 1 and 2**, which circumvented land transit routes and severely undermined both the security of Europe's natural gas supply and the transit revenues of Ukraine and Central European EU member-states.

For years, a majority of the the German political and business elite defended the importance of Nord Stream 2 for Germany's energy security and its green transition. Ultimately, however, many pipeline's most ardent supporters were revealed to be personally and financially tied to the success of the project through an intricate web of forums, organisations and lobby groups. These connected backers leveraged their political and economic influence to fight for the completion of the project.[8] North Stream 2 exemplified how state capture at home allowed the **Kremlin to weaponize different combinations of hard, soft, and sharp power** instruments for furthering its foreign policy goals and subverting European security and democracy. This toolbox, while cantered on extracting economic rent and around state-run and oligarchic corporate networks, included, among others, lucrative positions of former political heavyweights at Russian state-owned companies' boards, constant media propaganda and disinformation, support for non-systemic political parties, creation of front charitable organisations, and the continuous fearmongering of strings of brutal killings across Europe, including in Germany. Those tools have all been backed up by increasingly aggressive rhetoric and display of military might from the Kremlin against the EU and NATO.

7 Filipova, R., Stefanov, R., *Countering Kremlin's Media Influence in Europe: Patterns of Anti-Democratic Messaging, Disinformation Responses, and Resilience Assets*, Sofia: Center for the Study of Democracy, 2021.

8 Nitzov, B., and Rangelova, K., *How to Deal with Kremlin's Desire to Starve Europe of Energy: The Case of Nord Stream 1 and Beyond*, CSD Working paper, August 2022.

Fig. 2 | Kremlin's instruments for weaponizing its state capture power for foreign policy goals

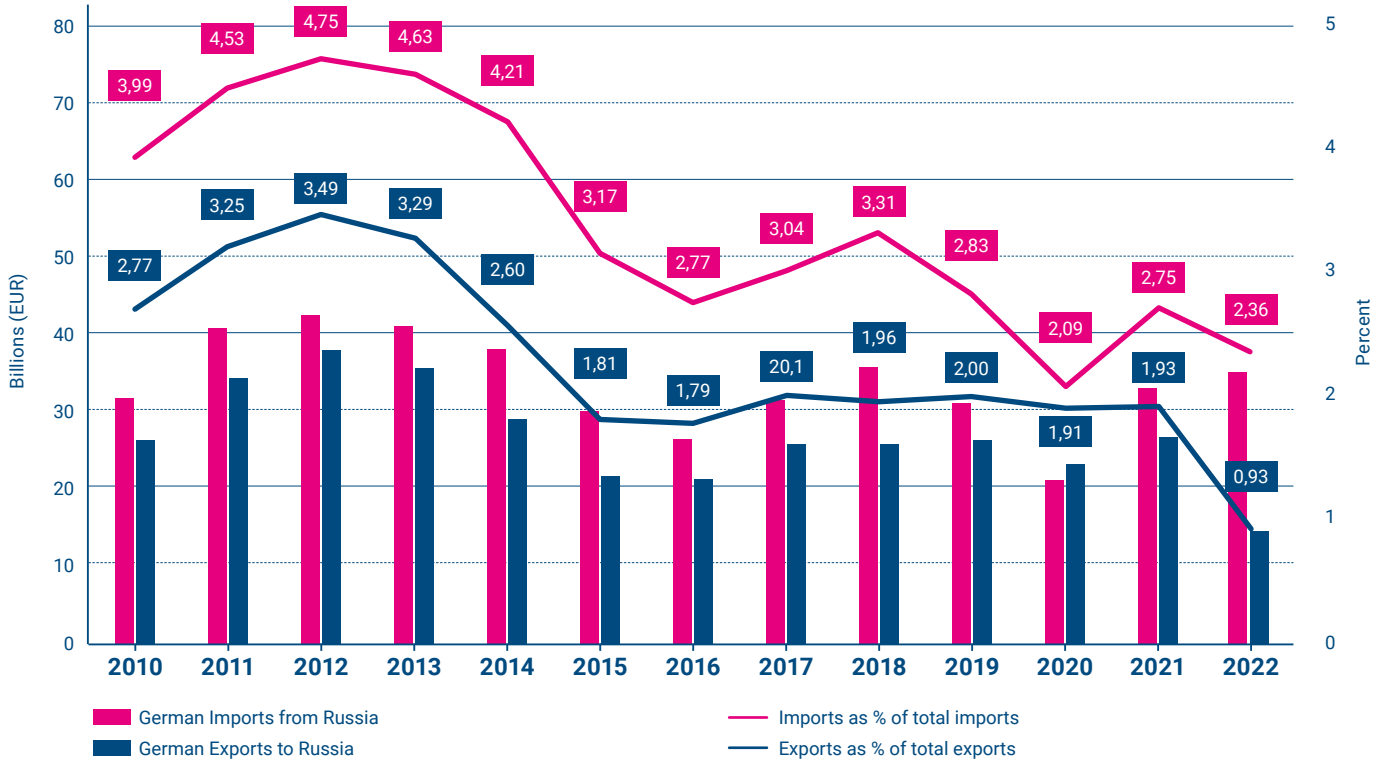


Source: Center for the Study of Democracy (CSD)

Structural Trade Ties

Since the early 2000s, Germany has steadily deepened its economic relations with Russia. Germany is Russia's second largest trading partner, exporting machinery, vehicles and vehicle parts to Russia.[9] Until the fall of 2022, Russia was the main energy supplier of Germany delivering between 35 and 40% of Germany's total oil, gas and coal imports. Russia's share in Germany's foreign purchases differs significantly between the energy sector, where Russia used to play a key role, and other sectors of the economy where its presence remained mostly negligible.

Fig. 3 | Total trade between Germany and Russia in nominal and relative terms.



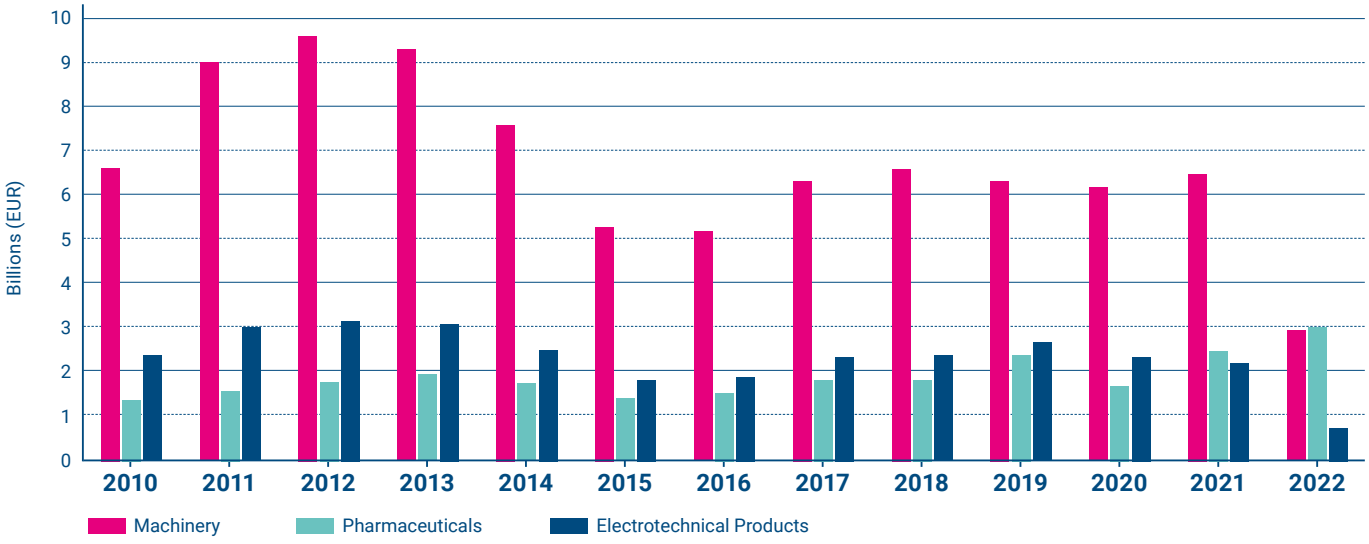
Source: CSD based on data from the Federal Statistical Office of Germany (Destatis).

The cornerstone of the Russian-German economic relationship has been the **symbiosis between energy trade and heavy manufacturing**. Russia's vast energy resources have powered the German industrial heartland, which then supplied the Russian market with high added-value products and sophisticated technology. However, the trade ties between the two countries have never comprised a significant part of the German economy, and the trade turnover has actually gone down after the annexation of Crimea. However, the Russian invasion of Ukraine sharply reduced the trade turnover by around 50% in 2022 (mostly due to the cutback in German exports), in comparison to the average values in the past decade. The data for 2023 would likely reveal a much sharper drop in bilateral trade, as for most of 2022, Germany was still importing large volumes of Russian oil and natural gas.

While most of the German imports of Russian goods consisted of fossil fuels and raw materials, the **German export structure for the Russian market is more varied**. Heavy machinery, electrotechnical equipment, and pharmaceuticals have traditionally been some of the most important export items. As with the general picture of the trade flows above, German exports have gone down by 70% vis-à-vis 2012 with the notable exception of pharmaceutical sales, which have seen a double-digit growth in the past three years. Medicines have been excluded from the EU and US sanctions lists.

9 German Ministry of Foreign Affairs, *Germany and Russian Federation: Bilateral Relations*, as of 2021.

Fig. 4 | Export of staple goods from Germany to Russia in nominal terms



Source: CSD based on data from the Federal Statistical Office of Germany (Destatis).

A set of exports that are of particular interest are the so-called **"dual-use goods"** – products, which have both civilian and military applications. The three largest categories, which potentially contribute to the Russian war effort in Ukraine are semiconductors, printed circuit boards (PCBs) and explosives & detonators (E&Ds). Up until 2018, the export value of German PCBs and E&Ds was insignificant. This changed in 2019 when Russian PCB demand increased tenfold and stayed relatively constant up until the introduction of sanctions. In 2022, with the exception of semiconductors, most of the rest of German military-grade exports have dried up.

Investment Relations

While the bilateral trade turnover has been on the decline, German companies have invested more than EUR 21 billion at the end of 2021, making the country the third biggest investor in Russia following Cyprus and the Netherlands.[10] Even today, many German companies continue operating in Russia and there are still several thousand Russian firms active in different German markets. Given Russia's proven track record in abusing corporate networks for foreign policy goals, including through deploying strategic corruption, **these company networks pose economic and investment security risks**. These risks are likely to increase further as the Kremlin seeks to evade sanctions by further obfuscating final beneficial ownership of its companies.

Russian foreign direct investments (FDIs) in Germany almost tripled from 2012 to 2020 reaching around EUR 9.5 billion before falling to EUR 5.5 billion at the end of 2021 (still 75% higher than a decade ago). Although **Russian FDI in Germany** is miniscule compared to the country's GDP or even the overall investment stock, it has been **concentrated** in a few strategic economic sectors such as energy supply (mostly oil refining, natural gas transmission, storage and distribution).

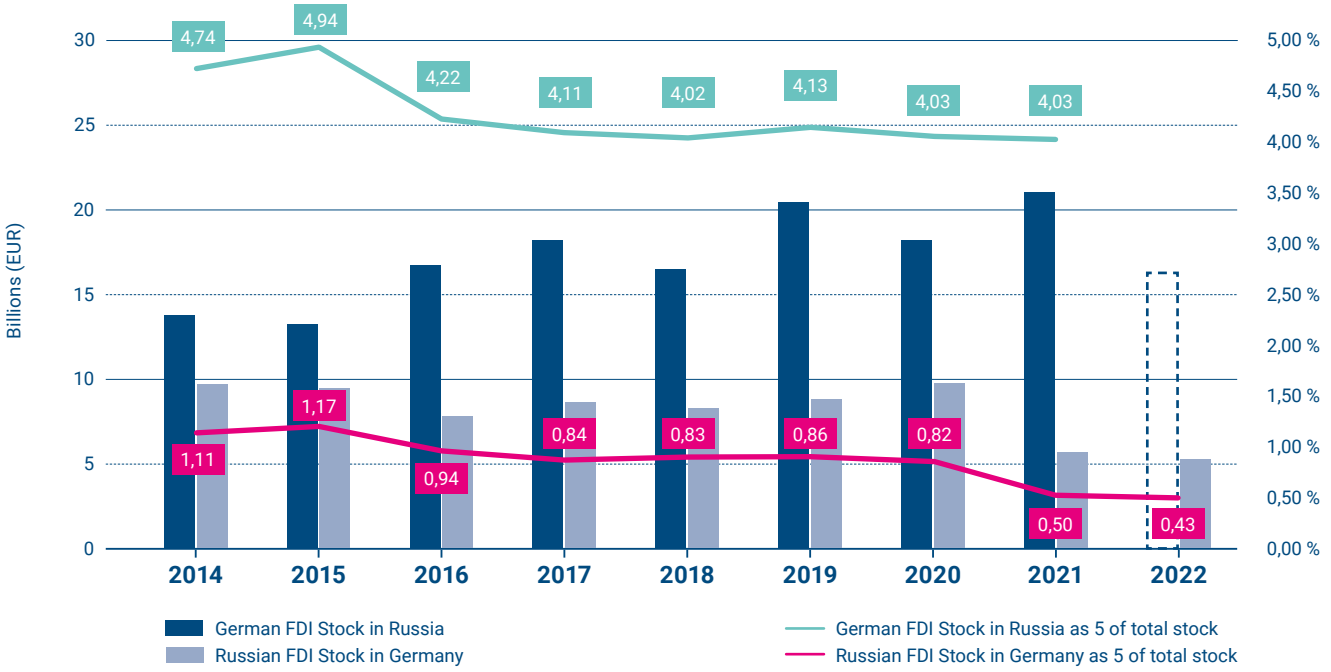
German FDI in Russia represents 4% of the total foreign investment in Russia. If roundtripping investments linked to Russian entities from offshore destinations such as the BVI, Cyprus, Netherlands and Luxembourg are excluded, German FDI in Russia could go as high as 10% of the total stocks. It can be estimated that the German investments declined by at least 25% in 2022 as sanctions came into effect and big investors withdrew.[11] However, the massive corporate exodus was "cushioned" by Russian countermeasures, which included imposing restrictions on capital outflows for "unfriendly" countries, complicating the procedures of pulling out capital.[12] As a result, many German and Western companies have been stranded on the Russian market, and have not sought active measured to actually end their exposure to Russia.

10 Investments from Cyprus and the Netherlands have very often been essentially Russian investments, as Russian companies have used the two countries' laxer corporate registration and tax regimes to park profits. This makes Germany the likely number one European investor in Russia. For more detailed analysis, see Shentov, O., Stefanov, R. and Vladimirov, M. (eds.), *The Kremlin Playbook in Europe*, Sofia: CSD, 2020.

11 A conservative CSD estimate, based on the assumption that German divestment was proportional to the latter's FDI share of total stock and based on the overall shrinking of foreign direct investment in Russia after the start of the war in Ukraine.

12 Simola, H., *Can Russia reorient its trade and financial flows?*, Bank of Finland Policy Brief 2022 No.7, December 2022.

Fig. 5 | German FDI stock in Russia in nominal and relative terms



Quelle: CSD based on data from the Russian Central Bank

Corporate Footprint

Although there were 1713 companies with Russian ultimate beneficial ownership identified by the end of 2022, the **Russian corporate presence in Germany is small and highly concentrated in around 40 larger firms**, which specialize in oil refining, natural gas supply and distribution, metal and plastic products manufacturing, glass factories, raw materials trading, banking and consultancy services.

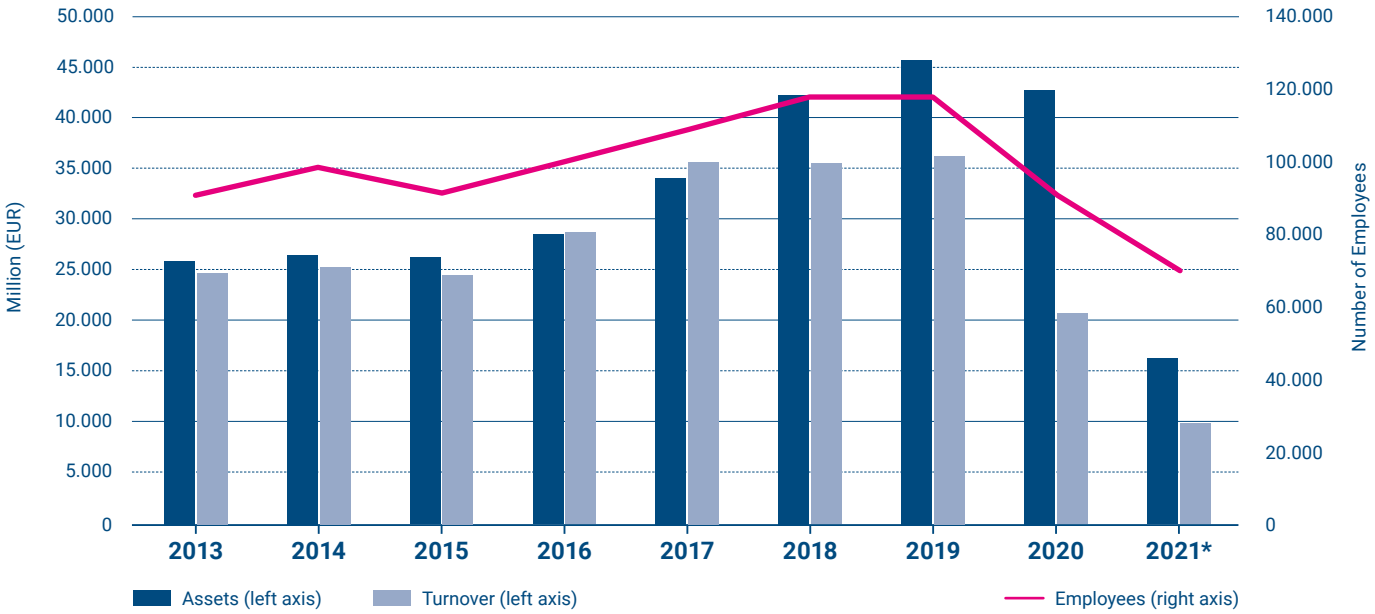
Over the past decade, Russia-controlled businesses have held assets worth between EUR 25 and 45 billion and have employed roughly 100,000 workers across the country – a tiny fraction of the German economy and labor force. Only 1.9% of the turnover of all foreign-controlled companies in Germany was generated by firms with Russian owners in 2019.[13] After the introduction of EU sanctions against a number of Russian banks (including VTB Europe) and the German government's measures to take the main assets owned by Rosneft and Gazprom under state control, the **Russian corporate footprint in Germany has lost its strategic edge**. Yet, its potential to conduct malign Russian influence in the country should not be underestimated, given that some of the decline is likely only accounting-based and the deep corporate networks the Kremlin has spun around Europe. These are likely to also be more and more linked to covert operations for delivering dual-use goods for keeping Russia's war machine running.

Much of the Kremlin's leverage vis-à-vis Germany in the past two decades can be explained by the **growing exposure of German businesses to the Russian market**. Large German companies, such as Siemens, Bayer, Henkel, BMW, Mercedes-Benz, Volkswagen and UNIPRO all have major manufacturing and sales operations in Russia. According to the Russian-German Chamber of Commerce, around **4,500 German companies operated in Russia** on the eve of the Russian full-scale invasion in Ukraine in 2022 with total revenues hovering between EUR 50 and 60 billion per annum over the last decade, and employing around 200,000 people in Russia. In addition, a number of German energy companies had long-term gas import contracts and jointly developed exploration and production projects with Gazprom in Siberia. German firms were regular winners of large-scale infrastructure and engineering contracts across different Russian sectors taking part in the construction of power plants, electrical grids, highways and other public facilities.

The deep and long-term ties European and German companies have with the Russian market, and **the ambiguity of some of the previous rounds of sanctions**, most notably after the annexation of Crimea, have left many of them stranded with the onset of the invasion in 2022. Only 8.5% of the about 2,405 firms owned by EU and G7 companies have divested some or all of their business from Russia after the invasion.[14] Of the 375 largest German companies making business in Russia, 25% have announced they have left the country but just 6% have effectively exited, including brands such as Aldi, Deutsche Bank, Lufthansa, and Mercedes-Benz.[15]

13 Dierig, C., Direct investment: *That's why Russian companies are reluctant to invest in Germany*, WELT, Februar 2022.
14 Evenett, S., & Pisani, N., *Less than Nine Percent of Western Firms Have Divested from Russia.* SSRN Electronic Journal, January 2023.
15 The Leave Russia project divided international companies into 4 categories (statuses): "stay" – companies that continue to operate in Russia; "wait" - companies that have reduced current operations and suspended new investments; "leave" - companies that have curtailed Russian operations; "exited" – companies that completed the exit from Russia. *International Businesses Leaving Russian Market: Is There Progress?*

Fig. 6 | Russian Corporate Presence in Germany



Top 10 by Turnover in million euros

* 2022 corporate data is still not available while 2021 firm statistics is incomplete.

Source: CSD based on corporate database data

Box 1 | German business activities in Russia after the Invasion

To understand better the forces and motivations which German companies operating in Russia face after the start of the war in 2022, it is important to spotlight some of the known cases so far.

Volkswagen AG has decided to stop the production of vehicles in and export of cars to Russia until further notice. The company is expected to announce the liquidation of the production site in Nizhny Novgorod while buyers have expressed interest in its Russian plant in Kaluga.[16]

The retailer, Metro AG, continued doing business in Russia on a large scale. The CEO of the Metro supermarket chain confirmed plans to continue operating arguing that the firm has responsibility for more than 15,000 employees and for their customers. Ukraine's National Agency for the Prevention of Corruption has added Metro to its list of "international sponsors of war" after the key shareholder Daniel Kretinsky (Czech businessman who holds a 29.99% stake in METRO) was accused of ties to the Russian oil, gas, and banking sectors.[17] METRO is in a partnership with the Russian state-owned bank Sberbank (currently under EU and U.S. sanctions with exception to energy trade servicing) to develop a franchise project of chain grocery shops in Russia that uses the Russia-based *Mir* payment system.

Bosch, producing refrigerators and washing machines in two Russian plants until the invasion, is one of the companies on the "waiting" list looking for buyers. Production has been stopped due to the sanctions over exports to Russia.[18] However, no divestment has yet occurred.

Bayer, although having announced the shut-down of all non-essential business operations in Russia and Belarus, decided to ensure continued access to health and agriculture products for the Russian farmers under ethical concerns.[19]

Similar to Metro AG, Knauf keeps operations across 14 sites in Russia, although new investments have been suspended. Early in March, 2022,[20] the company again quoted their responsibility for its more than 4.000 employees and decided to continue business-as-usual while the political and commercial situation allows it. In December 2022, the Russian subsidiary of Knauf allegedly assisted the Kremlin in the soldier recruitment campaign, although the company argued it was simply following local requirements for providing lists of military eligible employees that should be temporarily directed to the military service[21].

Claas Group, the largest German manufacturer of agricultural machinery, has kept its Krasnodar plant open.[22] Although the firm has not made any public statements, it has ordered an internal audit to determine whether the company has violated the sanctions against Russia. A formal request[23] in the European Parliament demanded for an investigation of the "Claas case" to specifically acknowledge if the company was assembling prohibited goods with the intention to reclassify them, or was smuggling prohibited goods into Russia by hiding them inside permitted goods. The company was also accused of using loopholes to export sanctioned goods to Russia.

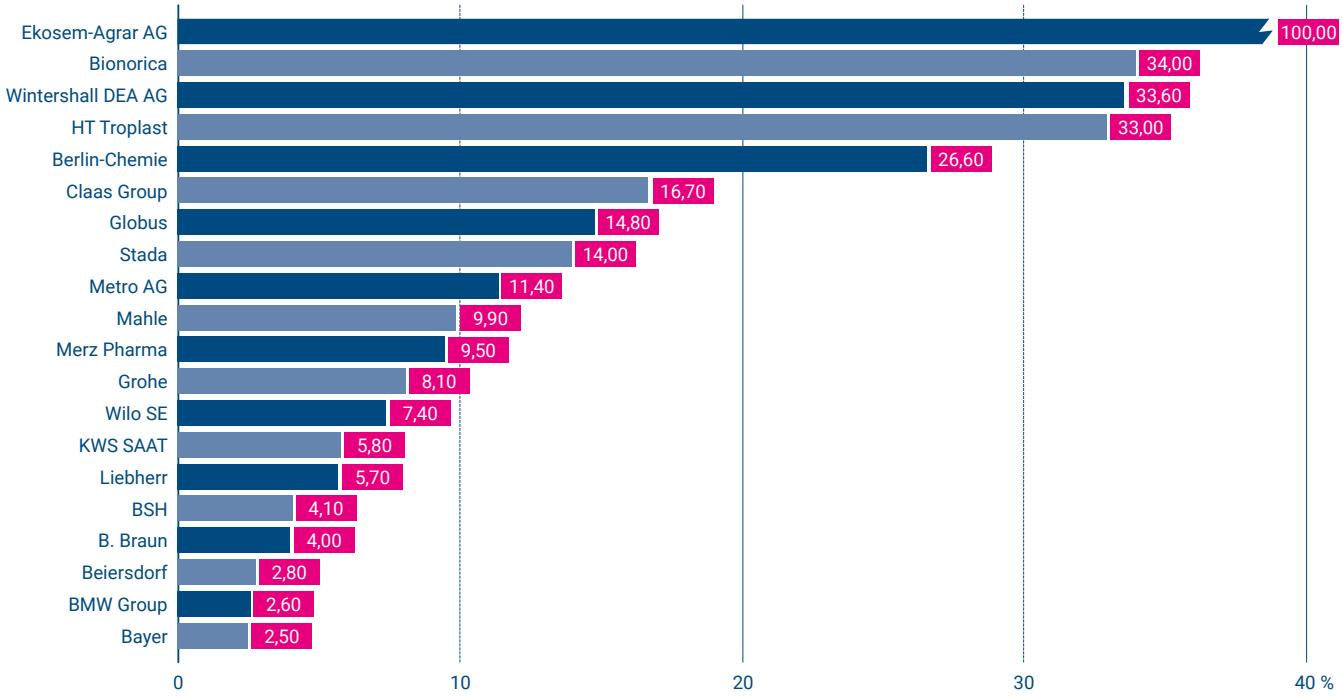
Liebherr, the manufacturer of fridges, has been a significant investor in Russia since 1965 and today Russia is one of the company's largest sales markets. The Liebherr Group operates through two factories at Dzerzhinsk (Nizhny Novgorod region) and in Moscow. The company has kept business-as-usual after the war, even though it has announced publicly that it supports and implements the sanctions imposed on Russia.[24]

The German headquartered Ekosem-Agrar, one of Russia's largest agricultural companies continues to openly run its business and has actually increased profits. The company has faced a financial crisis after the imposition of sanctions against Russia, which prompted the start of a bond restructuring program. Nonetheless, preliminary figures as of 30 September 2022 revealed that the company has doubled revenues year-on-year reaching EUR 613 million in the first 9 months of the year.[25]

16 Reuters, No decision on sale of Volkswagen's last Russian factory, says govt, Reuters, March 2023.
17 Krantz, P., Ukraine labels German wholesaler Metro as 'sponsor of war', DW, March 2023.
18 Kornev, T., Вендоры толпятся у плиты, Kommersant, February 2023.
19 Bayer, *Bayer-Statement zur Ukraine*, Bayer, May 2023.
20 KNAUF, Кнауф остается в России, KNAUF Press Release, March 2022.
Available at: https://www.knauf.ru/about/pressroom/current-press-infos/2022/3/11/knauf-ostaetsja-v-rossii.html (Last accessed: 26.06.2023)
21 Business & Human Rights Resource Centre, *Knauf subsidiary allegedly assisted Russian authorities in recruiting new soldiers, according to media reports; incl. company response*, Business & Human Rights Resource Centre, December 2022.
22 Marx, U., *Claas entkräftet Vorwurf der Sanktionstrickserei*, Frankfurter Allgemeine Zeitung, March 2023.
23 European Parliament, *Loopholes in the sanctions regime imposed on Russia and the case of CLAAS KGaA mbH*, Priority question for written answer P-003914/2022 to the Commission, December 2022.
24 Liebherr, *On the current situation in Ukraine*, Liebherr Press Release, March 2022.
25 Ekosem-Agrar, Ekosem-Agrar AG publishes preliminary figures as of 30 September 2022, Ekosem-Agrar, January 2023.

In contrast, more than half (55%) of the companies have decided to continue operations in Russia or have put business on hold waiting for regulatory or political clarity. Of the Top 50 companies that remain on Russian soil, 12 of them belong to the Top 100 largest companies in Russia by revenue (including Volkswagen Group, Metro AG, BMW Group, Wintershall Dea AG, Bosch, Bayer, Havi, Knauf, Claas Group, BSH, Liebherr, and SAP). A number of these German businesses make up between 5 and 40% of their revenues in Russia. This strong **dependence on a single market has led many German companies to hesitate** leaving Russia, and to lobby heavily Berlin to soften its stance on sanctions.

Fig. 7 | The share of the Russian market versus their global operations of the top 20 German investors in Russia (2021)



Source: CSD based on the Leave Russia database 2021

Although EU and German sanctions against Russia have been unprecedented in terms of depth and reach, ensuring their effective implementation and enforcements has been problematic. For starters, the EU and Germany do not possess the comprehensive institutional infrastructure capable of ensuring the enforcement of sanctions of such depth and breadth. The EU introduced a sanctions coordinator, pushed forward with establishing the European Anti-Money Laundering Authority, adopted an investment screening mechanism, and is about to come up with a comprehensive economic security strategy. Germany has gone a step further, by upgrading its energy security law and moving fast to cut Russian control of strategic energy assets in the country.

In the meantime, many EU companies have been exploiting **gaps in the restrictions regime** or the lack of adequate controls from national regulators to evade sanctions, especially on Russian crude oil and oil products and on dual use goods that Russia needs to sustain its war effort in Ukraine. After tumbling down in March 2022, Russian imports have climbed up again, as Russia has been able to develop alternative supply chains for key products such as spare parts, semiconductors and oil and gas production equipment.

While some products previously imported from the U.S. or EU members may be relatively easy to replace by alternative supply sources, other items are harder to obtain, forcing **Russian importers to rely on third countries as intermediaries.** Trade data from 2022/2023 reveals that **Armenia, Kazakhstan** and **Kyrgyzstan** that are part of the customs-free Eurasian Economic Union (EEU) with Russia, as well as **China** and **Turkey** are shipping sanctioned goods that were originally destined for them, on to Russia.

From March 2022 onwards, EU/UK exports of fully or partially sanctioned goods to Armenia, Kazakhstan and Kyrgyzstan steadily increased by between 15 and 90% depending on the product reaching more than $1 billion between March and June 2022.[26] The increase in exports of such products relative to all other goods has been around 22%. Meanwhile, the Chinese shipments of fully or partially sanctioned goods to Russia and the named Central Asian countries increased by 8

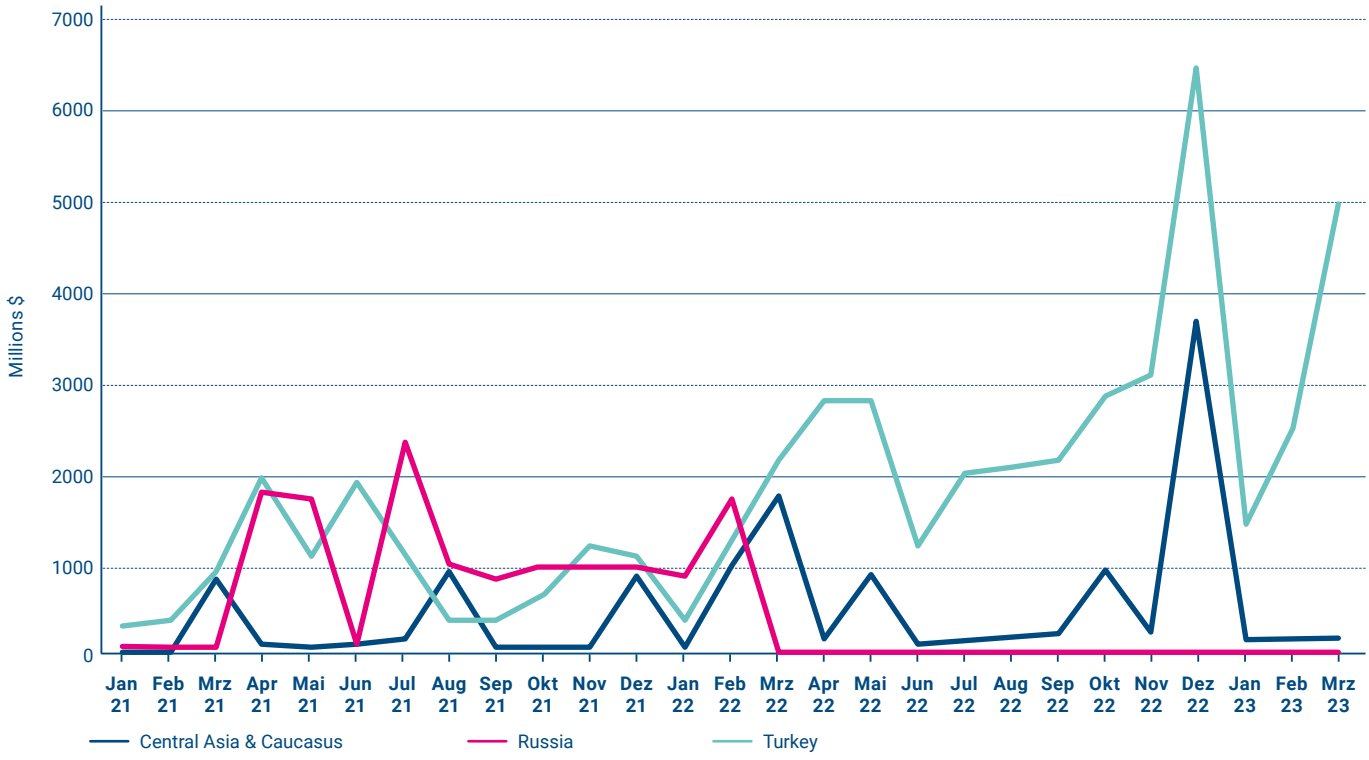
26 Chupilkin, Maxim and Javorcik, Beata and Plekhanov, Alexander, The Eurasian Roundabout: Trade Flows Into Russia Through the Caucasus and Central Asia (February 23, 2023). EBRD Working Paper No. 276.

to 15 percent compared with trade in other goods. While the increase in exports to Central Asian countries by the EU, UK and USA corresponds to only 4% of the decline in the direct exports of fully or partially sanctioned goods to Russia, the substitution ratio varies widely between product categories. For example, for automatic data processing machines, or computers, track-laying tractors and combine harvesters the ratio exceeds 100 per cent. Double-digit growth can be seen also for internal-combustion vehicles, paints, washing machines and pumps and compressors.

German exports to Russia and possible intermediary countries show similar patterns. While exports to Russia have collapsed after March 2022, exports to EEU countries have skyrocketed across most goods categories. This is especially true for foreign sales of vehicles and vehicle parts, electrotechnical products, optical and photographic products, inorganic and organic chemicals, as well as tools of all sorts. The total value of the exports of some goods to those countries in March 2023 stood at 100% and sometimes at more than 1000% higher than it was in March 2022. Some of these goods include sanctioned products such as semiconductors which are a dual use technology, as they can serve both civil and military purposes. Since March 2022, German semiconductor exports to most Central Asian countries have increased significantly relative to pre-war levels. Yet in absolute numbers they correspond to only a fraction of what Germany used to export to Russia before the war.[27]

German exports of dual-use goods that can be linked to the production of sanctioned items to Turkey and many countries in the Southern Caucasus and Central Asia have surged on a monthly basis by around 170% year-on-year in 2022. The peak in exports can be observed in December 2022 when the sale of sanctioned-related goods make up 36% of total German exports to the region.[28] This peak is most likely a result of two factors: First, it probably took some time to set up new intermediaries in third countries. Second, Russian companies may have placed larger orders for sanctioned goods in December 2022, fearing that new sanctions coming into force in 2023 would make it more difficult to import German goods via third countries.

Fig. 8 | Exports from Germany of sanctions-related goods to Central Asia, the Caucasus and Turkey



Source: CSD based on the German national statistic

27 For reference, in March 2021, Germany exported roughly $16.82 million worth of semiconductors to Russia, whereas exports to Central Asia in March 2023 stood at $1.35 million.

28 China and the UAE, which have been previously suspected of enabling Russian sanctions evasion, have not seen their imports from Germany of sanctions-related goods increase after the invasion.

Reselling products made in Germany for which there is high demand in Russia is a lucrative business. Individual investigations show how tools produced in Germany that fall in the dual use category found their way to Russian arms companies via resellers located in Germany and Turkey.[29] The evasion of sanctions by German companies is not necessarily the result of malicious intent, but rather very often because of **insufficient due diligence on clients in third countries.** There is currently no legal framework to regulate the export of sanctioned goods, which puts the whole **responsibility for sanctions enforcement on firms themselves** instead of requiring the third country to observe the sanction regime.

There are many different ways, in which German manufacturers intentionally can evade sanctions. They can **obfuscate the origin and final destination of traded goods** by using foreign-owned but German-registered firms that can tranship the goods through third countries on the way to Russia. German firms are required to demand a so-called **"end-use declaration" from customers in third countries** that ensure the items are not going to be resold to Russia. Yet, in practice, these declarations are voluntary commitments rather than binding legal documents, with no immediate downside for the company if it fails to rigorously check compliance, making them ineffective. In addition, German producers or resellers can also purposefully declare falsely the shipments that are going directly to Russia, taking advantage of the limited capacity of customs authorities to identify and stop these shipments.

It is likely that sanctions evasion will continue at a higher rate before stabilizing with improved enforcement, as **evasion tactics tend to evolve with new regulations**. Russia may be able to exploit regulatory loopholes and alternative trade routes to get its hands on products from Western producers that are crucial to its economy. Yet, the volumes that Russian companies can obtain through these practices are unlikely to come even close to meeting the industrial needs of the whole economy. The growth rate for German exports to Central Asia and the Caucasus may be high due to sanctions evasion practices, yet despite this steep growth, trade volumes in absolute terms are remain comparatively small.

The steep drop in Russian budget revenues in the second half of 2022 and in the first half of 2023 shows that Western **sanctions have taken hold and have hurt the ability of Russian firms to access international finance and trade**. The scale of the Russian economy makes it difficult to fully compensate for lost business through evasion. Still, even if the exported electronic components are not compensating for the fall in industrial production and imports, Russia has been able to extract and repurpose them for military applications, including from household appliances like refrigerators and dishwashers.[30]

Tackling sanctions evasion is challenging. Closing one loophole leads to the creation of new schemes. Hence, it requires concerted institution building efforts on European level to redefine and support a new economic security strategy, balancing carefully between decoupling and de-risking on the one side, and preserving economic and technological agility, on the other. Germany and the EU would need to continue their joint efforts with the G7 to convince third countries, in particular large democracies and economies from the Global South, not to tolerate evasion and **to enforce secondary sanctions** to close the existing governance gaps. One possible way forward is to complement or build upon US initiatives in this area, which has longer experience and bigger institutional capacity. The US has launched the Disruptive Technology Strike Force, an initiative by the Departments of Commerce and Justice, to prevent Russia and other adversarial states from illicitly acquiring advanced US technology. The Strike Force recently announced criminal charges against individuals supplying stolen software and hardware source codes to China.[31] Moreover, the US Department of Commerce and Treasury's Financial Crimes Enforcement Network (FinCEN) have published a joint supplemental alert outlining red flags for potential Russian export controls evasion that financial institutions should watch out for and report on.

The EU, in general, and Germany, in particular, should introduce similar strict coordination, **reporting and compliance mechanisms to enforce export controls**. This includes the development of special systems for identifying controlled goods and the network of intermediaries that have enabled this trade using a comprehensive mapping of their ultimate beneficial ownership. The large-scale sanctions evasion cases will likely rely on Kremlin-built financial and corporate networks in countries across the EU, such as Cyprus, involving also European companies. These enablers help Russia exert its malign economic influence by channelling illicit funds into Europe, exploiting governance gaps and corruption. The complexity of this ecosystem and the scale of Russian capital outflows make it almost impossible to distinguish between legitimate and illicit capital flows.[32]

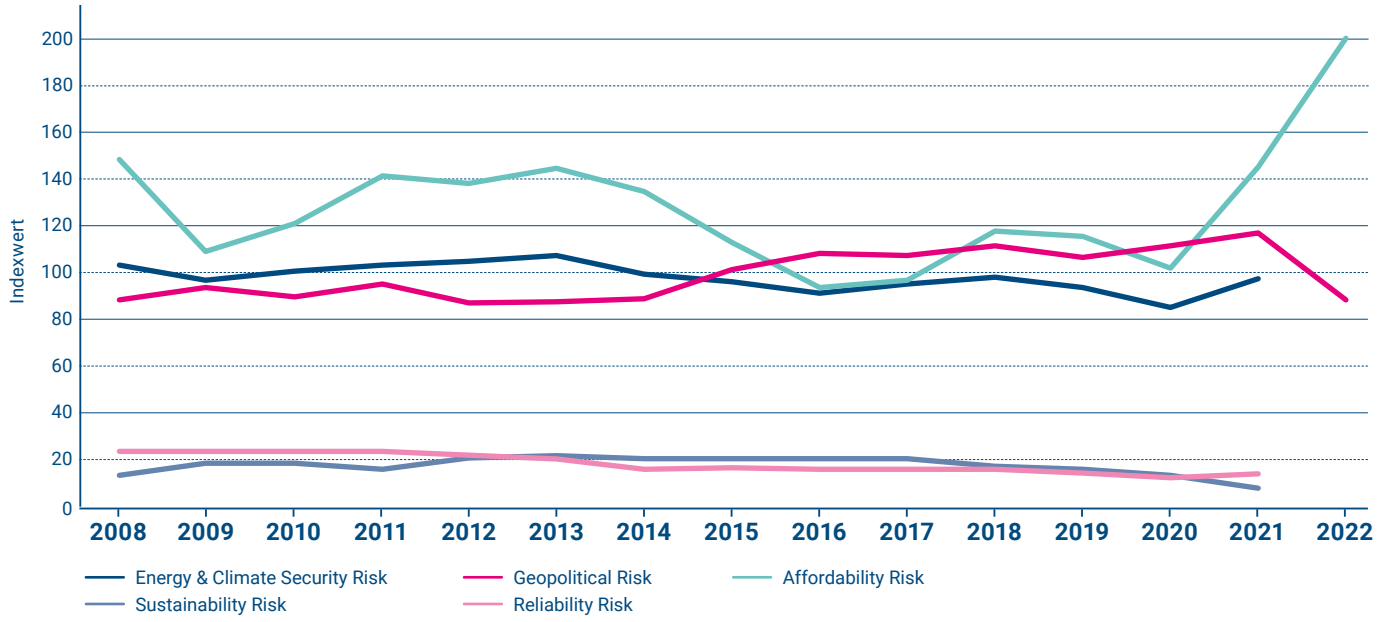
29 Malcher, I., Rudzio, K., *Deutsche Wertarbeit für Putins Raketen*, Zeit Online, April 2023.
30 Tagesspiegel, *Munitions-Not in Russland: „Sie holen Mikrochips aus Waschmaschinen und bauen sie in Raketen ein"*, Tagesspiegel, February 2023.
31 Donovan, K., Nikoladze, M. and Mossberg, B. *Global Sanctions Dashboard: US and G7 allies target Russia's evasion and procurement networks*. Atlantic Council, May 25, 2023.
32 Center for the Study of Democracy, *Kremlin Playbook 2: The Enablers*, March 2019.

3. Energy and climate security before and after Ukraine

The geopolitical risks to energy and climate security in Germany have markedly increased since Russia's annexation of Crimea in 2014.[33] The share of Russian gas increased to 49% of total German gas imports by 2019, compared to 34% in 2009. Germany has emerged as one of the most vulnerable EU countries in terms of security of supply and overall energy and climate security vis-à-vis Russia, according to the Energy and Climate Security Risk Index (ECSRI). The ECSRI includes 42 risk indicators that are distinct yet interconnected, enabling a comprehensive analysis of energy and climate policy trends. Moreover, Gazprom's ownership of gas storage infrastructure in the country has undermined the reliability of gas supply on the eve of the war in Ukraine as Russia took advantage of its position to keep storage levels below the normal average for the winter season.

The spike in fossil fuel prices since the fall of 2021 has contributed to a steep increase in the affordability risks. At the same time, a return to higher coal and natural gas-based power generation has **reversed some of the decline in the sustainability risks**, leading to a rebound in energy-related emissions. Without a significant acceleration of the uptake of renewable energy, the slow-down of decarbonization efforts is bound to continue even though Germany has been among the leaders in Europe in this domain.

Fig. 9 | The Energy and Climate Security Risk Profile for Germany before and after the Russian invasion*



* The higher the Index score, the higher the energy and climate security risk level.
There is no sufficient data for 2022 to estimate the reliability and sustainability risks

Source: CSD.

Ultimately, Germany and Europe's bets on gas as a transition fuel for the green transformation and on Gazprom as the leading supplier have allowed the Kremlin to blackmail its European customers, before and after the start of the war in Ukraine, by reducing unilaterally gas supplies while keeping the level of revenues as prices soared in mid-2022. These revenues have flowed directly into Kremlin's war machine.

The import share in Germany's total gas consumption has increased from 87.9% in 2015 to almost 100% in 2021 and the share of Russian gas in total imports has increased from 41.7% to 48.8% during the same period. While import volumes of Russian gas in Germany have only increased by 24% compared to 46% for the total EU gas imports increase, **Germany alone is responsible for 17% of that expansion of gas**

33 Center for the Study of Democracy, *Energy Security Risks and Russian Economic Influence in Germany: Towards Economic Decoupling*, Policy Brief No. 113, June 2022.

imports in the EU. Germany has become more vulnerable by deepening its reliance on Russia while simultaneously failing to develop alternative supply sources. Over the past three decades, many European energy champions have dragged their feet on diversifying their natural gas supply and have instead decided to work exclusively with Gazprom. The German energy shareholders in both phases of the Nord Stream pipeline project unsurprisingly initially opposed the idea for an EU embargo against Russian gas while they have simultaneously demanded compensation for the suspension of the project.[34]

The energy crisis was a rude wakeup call for Germany to begin a massive transformation of the structure of its energy supply. Germany has acknowledged its dependence on oil and gas imports from Russia as the main energy and climate security risk in the country's energy strategy. **The government's emergency actions reduced geopolitical risks by a third in less than a year** on the back of reducing Russian energy imports and accelerating key security of supply projects such as LNG regasification facilities. However, the emergency diversification exposed Germany to an overheated spot market. The large share of Russian gas in its import mix and the sizeable volumes that needed to be replaced with spot supply contributed to skyrocketing gas prices. Similarly, replacing Russian crude came at a high cost, ultimately contributing to 80% higher oil and gas import expenditures per capita vs 2021 (the German government spent EUR 270 billion to reduce the impact of higher energy prices on consumers – a third of the total European spending on the crisis).[35] The decades-long delay in implementing energy security measures led to a painful tradeoff, in which the affordability of the energy supply expressed in industrial competitiveness and energy poverty deteriorated by almost 100% since 2020.

To improve energy security, the German government has implemented a number of measures to lessen the country's dependence on Russian oil and gas. **On the demand side**, both households and business consumers cut their gas consumption by more than 20% in 2022 without hurting economic output. Despite the moderate economic slowdown, the apocalyptic scenario about an industrial meltdown in case of Russian supply cut, painted by many pro-Russian voices in Germany and elsewhere in Europe at the onset of the invasion, turned out to be deeply flawed.

On the supply side, the speed and ease at which full independence from Russian suppliers can be achieved varies widely. In the case of coal, the transition has been fairly successful already, as the share of Russian imports has declined from 50% to 8% and new sales contracts have been banned since 9 April 2022. Oil imports from Russia were reduced from 35% to 12% after the start of the war with the two refineries Leuna and Schwedt having been the only remaining importers of Russian crude. After the EU embargo on Russian crude oil and oil products imports came into force on 5 December 2022 and 5 February 2023, respectively, Germany should have in principle stopped buying Russian crude. However, Russian crude in the form of a Kazakh blend, as well as gasoline and diesel produced by Indian refiners using Russia oil inputs could still be making its way on the German market.

Although the share of Russian gas imports has dropped from 55% to almost a trickle since the start of the war, the German government estimated that at the end of 2022, 30% of gas imports still came from Russia. The government foresees a **full Russian gas phase out by the end of 2024** if there is significant progress in facilitating diversification projects, energy efficiency and the use of hydrogen and renewables.[36] The key issue for the success of this deep diversification strategy would be the ability of German companies to rid themselves from the take-or-pay clauses in the existing contracts that extend beyond 2024.

By putting Gazprom Germania under state trusteeship and ordering mandatory gas storage levels, the **German government took decisive measures to regain control over Germany's natural gas storages** and ease the pressure on natural gas prices. Likewise, Germany's decision to install its first ever LNG terminals has enabled it to diversify its natural gas imports. Germany has begun working on the construction of 8 floating (FSRUs) and 3 fixed LNG regasification terminals. Two FSRUs have already been commissioned and another two are expected to come online in 2024. These four terminals are estimated to replace approx. 72% of current gas imports from Russia.

Large German gas importers have also signed supply contracts with alternative companies. EnBW agreed on a new 20-year contract with American company Venture Global for 1.5 million tonnes per annum, starting in 2026, that will be imported through the new fixed terminal in Stade. RWE signed a 15-year contract with American company Sempra Infrastructure for 2.25 million tonnes per year of LNG, starting in 2027, and will most likely use the planned fixed terminal in Brunsbüttel to feed the natural gas into the German market. Similarly, a new deal with Qatar will see Germany importing 2 million tonnes per year, starting in 2026, for a minimum of 15 years.

The German Parliament also passed a *Gas Storage Act* that requires gas storages to adhere to certain filling levels over the winter. The unusually empty storages have been a major concern since the start of the winter in 2021/2022. The fact that the storages owned by a Gazprom subsidiary were even emptier than the national average gave rise to the suspicion that Gazprom was using its power over the German gas supply to artificially drive-up gas prices and deter German support for Ukraine.

34 Financial Times, *Nord Stream 2 backer Wintershall Dea says it expects compensation for investment*, FT, February 2022.
35 Sgaravatti, G. et al., *National fiscal policy responses to the energy crisis*. Bruegel, March 2023.
36 BMWK, *Zweiter Fortschrittsbericht Energiesicherheit*, May 2022.

4. Assessing vulnerable sectors to Russian economic influence

Germany's **manufacturing and heavy industry sector** has become heavily dependent on Russian energy sources, making it vulnerable to Russian indirect economic influence. In addition, Russia has also established a web of informal business and political ties with German companies and politicians, creating a network that allows for the exertion of influence beyond the traditional channels of diplomacy and trade. The following assessment zooms in on the extent of this dependence and the potential risks it poses to Germany's economic security and strategic autonomy.

Self-inflicted damage: Russia's networks of influence in the energy sector

The deepening of energy ties between Russia and Germany has been facilitated by a vast network of German and Russian politicians, businessmen, oligarchs, and lobbyists, as well as the alluring prospect of substantial profit margins through long-term contracts with Russian suppliers. Russia has managed to acquire some of Germany's critical energy infrastructure, and how German companies have deepened their reliance on and collaboration with Russia in the areas of natural gas, oil, and nuclear power. This trend continued even after Russia's annexation of Crimea in 2014 and despite the imposition of EU and U.S. sanctions on Russia.

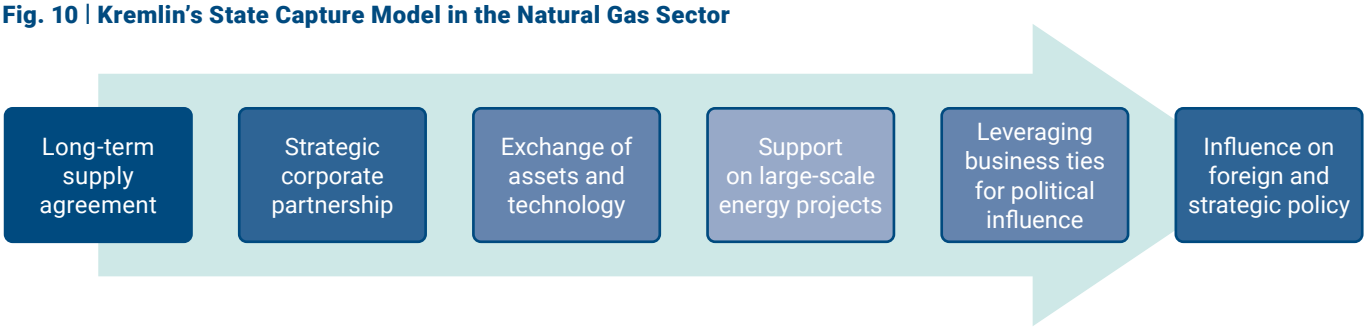
Natural gas

While Germany's heavy reliance on relatively cheaper Russian pipeline gas had been previously seen as a competitive advantage, it turned out to be a strategic vulnerability for the national economy with the onset of the full-scale invasion. Germany found itself in a position where **some of its critical energy infrastructure was owned by a country waging war** in central Europe. This long-term lock-in on Russian gas was supported for years by some of the largest German companies, which were lobbying the German government to strengthen political and economic ties with the Kremlin. One of the strongest proponents of this special gas relationship has been Wintershall Dea, which was created through a fusion of the companies Wintershall and Dea in 2019, both of which had been involved in different joint ventures with Russian companies after the Crimean annexation in 2014. Dea was formerly owned by one of the largest German utilities, RWE, until it was sold in early 2015 to the investment firm LetterOne, whose ultimate owner Mikhail Fridman is a Russian oligarch, placed on the EU sanctions list in February 2022, where he was described as "a leading Russian financier and promoter of Putin's inner circle".[37] Despite the sanctions, LetterOne still holds 33% of the shares of the joint company.

At the same time, VNG AG and Gazprom Germania were working on the construction of a new gas storage site in Peissen, which they own in equal parts and which ended up being the fourth largest gas storage site in Europe upon its completion. The gas storage facility, named after the Russian Empress Catherine the Great, is directly connected to the Yamal pipeline, which pumps natural gas from Russia via Belarus and Poland to Germany.

In 2015, Wintershall and Gazprom signed one of the most strategic gas asset swap agreements in Europe, in which the German company gave up its ownership of three gas storage sites in Germany and Austria, including the largest gas storage in Western Europe (Rehden), as well as its ownership of the gas trading company Wingas, and in return received a 25% stake in two blocks of a Gazprom-owned gas field in Russia.[38]

Fig. 10 | Kremlin's State Capture Model in the Natural Gas Sector



Source: Center for the Study of Democracy (CSD)

37 Publications Office of the European Council, *Council implementing Regulation (EU) 2022/336 of 28 February 2022*, Official Journal of the European Union, February 2022.
38 Socor, V., *Nord Stream Expansion Agreed, Wintershall Swapped to Gazprom*, ICSD, September 2015.

Wintershall has been also among the strongest backers of Nord Stream. Just a year after the Crimean annexation, it led a consortium together with another German utility, E.ON (later replaced by Uniper), the French ENGIE, OMV and Shell to build the second leg of the pipeline, which would have allowed Russia to completely bypass Ukraine for its natural gas deliveries to Europe. Both the U.S. and Eastern European governments protested against the project warning of its negative impact on German, but also on European energy security. Many of the supporters of the project turned out to be personally connected to its success through an intricate network of forums, organizations and lobby groups and were able to leverage their political and economic influence to make their voices heard.

Box 2 | Russian Politically-Driven Investments in German Regions

To enable the development of Nord Stream, Russia concentrated its political and economic activities in the federal state of Mecklenburg-Vorpommern, the landing point for the Gazprom-led project. Russian companies linked to senior Gazprom and Nord Stream officials made investments in the region including by buying the Wismar shipyards in 2018.[39]

Another example is the development of the production facility of Deutsche Großwälzlager GmbH in Rostock's fishing port, which was opened in May 2016 by the-then Prime Minister of the province Erwin Sellering (SPD) and Russia's Minister of Industry Denis Manturow. The majority shareholder of the company that became the owner is the Russian investor Georgi Semenenko (55%), who is also the Chairman of the Board of the engineering conglomerate Kirovsky Zavod in St. Petersburg.

Russia's largest timber company Ilim Timber also made a major investment in Mecklenburg- Vorpommern when it bought a sawmill in Wismar in 2009. Ilim Timber has direct links to the Kremlin. Dmitry Medvedev is a co-founder of a predecessor company and used to be its Director of Legal Affairs before going into politics. Therefore, it comes as no surprise that Ilim Timber, as well as Kirovsky Zavod, have sponsored the controversial Russia Days, a central propaganda format of the Kremlin in Germany in support of Nord Stream 2.

This apparent focus of Russian investments in Mecklenburg-Vorpommern raises the question whether the vehement support on both federal and state level in Germany for Nord Stream 2 against all odds could be an indication of corresponding politically-driven business agreements: hundreds of millions of euros and the creation of local jobs for the ailing economy in the Northeast in exchange for the assurance of a permanent green light for the pipeline project that is so important to the Kremlin. These connections have taken on a different meaning following Russia's invasion in Ukraine in February 2022, as they have made Europe and its leading economy, Germany, more vulnerable to Russian extortion.

This **political-business network to promote the construction of Nord Stream 2** has been particularly active in Mecklenburg-Vorpommern, where a number of lobby organisations, most notably the so-called *Ostinstitut*, managed to blur the lines between public and private interests to such an extent that the state government eventually set up a climate foundation in an attempt to circumvent US sanctions and hired a special vessel to complete the pipeline using the charitable organization as a front. Shortly after the start of the war, this foundation was liquidated by the state government which is now facing a parliamentary committee of inquiry.

Representatives of German energy companies, like the CEO of Wintershall Dea, have spoken out repeatedly against new sanctions on the Kremlin even just a few days before the start of the invasion, when Russia was already amassing troops at the Ukrainian border.[40] Then after the invasion, the long-term gas supply contracts and joint ventures with Gazprom suddenly became an existential threat for those companies, pushing them to the brink of bankruptcy. EnBW still had a contract for 6.5 billion cubic meters per year until 2030, RWE had a short-term contract for 15 TWh of natural gas until 2023, and Uniper was bound to a take-or-pay contract for about 24 billion cubic meters per year until 2036.

Russia's unilateral natural gas supply cuts via Nord Stream 1 led the same German companies that used to be making enormous profits on their agreements with Gazprom to face bankruptcy, as they were still obliged to supply households and businesses with natural gas at the cheaper prices previously agreed. As a result, VNG lost EUR 337 million in 2022 alone, Wintershall Dea lost EUR 4.8 billion and Uniper the whopping EUR 19.1 billion, forcing it to seek a government bailout. Ultimately, the German government nationalized Uniper in September 2022 to prevent wider contagion and market panic as industrial consumers depending on Uniper could have also faced an existential financial crisis.

39 Kirilenko, A., Köpke, J., Tonev, N., *Wismar im Schatten der Russenmafia*, HAZ, March 2018.
40 Theurer, M., *Wintershall-Chef Mehren über Sanktionen und Nord Stream 2*, Frankfurter Allgemeine Zeitung, February 2022.

Crude oil and petroleum products

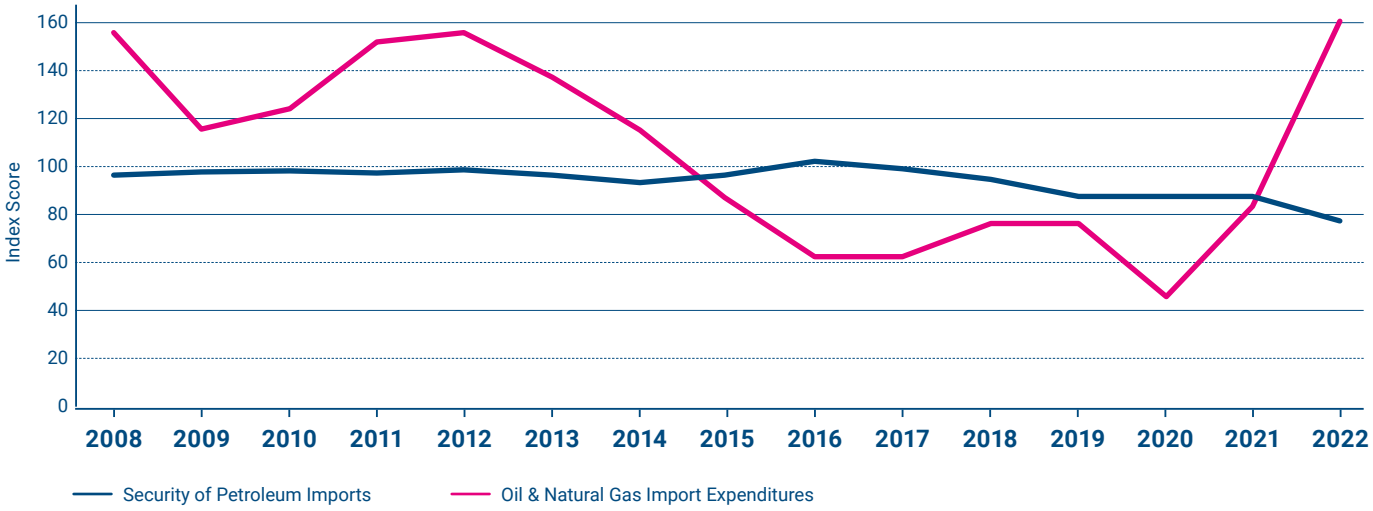
Unlike the security of natural gas imports, **Germany's oil import risk level has remained stable after the Russian annexation of Crimea**. Oil imports from Russia have declined by 7% from 2014 to 2021. Still, before the EU embargo on oil imports from Russia came into force, Germany used to be the largest buyer of Russian crude in the EU by volume, and the share of Russian oil in its total imports used to be above the EU average.

Similar to the gas sector, the Kremlin has sought to leverage for strategic gains the **investment strategy of the largest Russian state-owned oil company**. Rosneft has acquired key assets in the German oil sector. Rosneft completed the gradual takeover of the Schwedt oil refinery from Total, Shell and BP in 2021. Not only is the refinery a crucial supplier of gasoline, diesel and heating oil in East Germany, but it is also the endpoint of the Druzhba pipeline through which 25% of Germany's oil demand is satisfied.[41] The deal was approved by the Federal Anti-Trust Office only three days before the invasion, which raises the suspicion that the Kremlin was planning to use the control over the refinery as a strategy to paralyze the German economy and more specifically the Berlin/Brandenburg region, which are supplied entirely by the Schwedt refinery.[42] The supply of the Schwedt refinery remains a key challenge. To keep up its usual production levels, the Schwedt refinery needs around 12 million tonnes of crude oil per year. As of now, 5 to 6.8 million tonnes can be delivered via the port in Rostock, resulting in a utilisation rate of 50-60%. The German federal government aims to achieve a 70% utilisation by modernising the pipeline between Rostock and Schwedt, and by securing additional deliveries from Poland and Kazakhstan via the Druzhba pipeline.

While Kazakh crude oil has the advantage of being very similar to Russian crude oil and is therefore more suitable as a substitute for certain production processes in Schwedt, it has the disadvantage that Russia will also benefit from this deal due to the transition fees for the use of the Russian part of the Druzhba pipeline. Another danger consists in the possibility for Russian oil inadvertently being imported in Germany if Russian and Kazakh oil is mixed in the Druzhba pipeline system.

The ownership of the refinery became a key obstacle for Germany's decision to phase out Russian fossil fuel imports after the invasion. Rosneft continued importing Russian Urals light crude oil, which began trading at a discount of between $20 and $30 per barrel vis-à-vis the other global benchmarks. This meant that the Russian state-owned major was generating high profits out of its strategic position on the German downstream market that were used to finance the Russian military. The Schwedt refinery could not, however, find alternative crude supply as Poland refused to deliver crude to the facility from the Baltic Sea port of Gdansk via the Druzhba pipeline as long as the ownership is in Russian hands. To resolve this conundrum, the German government decided to place Rosneft's German subsidiary under state trusteeship in a similar manner to how it took control over the operation of Gazprom Germania.

Fig. 11 | Improving the Security of Crude Oil Supply after the German Decision to cut Russian oil imports



*The compared indicators have been turned into Index scores as to ensure comparability.
The higher the Index score, the higher the level of risks in the particular factor examined.

Source: CSD based on its Energy and Climate Security Risk Index.

41 Spiegel, *Wirtschaftsministerium prüft Anteilskauf an deutscher Raffinerie durch Rosneft*, Spiegel, February 2022.
42 A last-minute intervention from the Federal Economy Ministry that ordered an investment audit delayed the actual transfer of the remaining shares in the hands of Rosneft.

By becoming the trustee of Rosneft's business in Germany, the government took over control of all Rosneft assets in the country. Since 2010, Rosneft has held stakes in the MiRO refinery in Baden-Württemberg and the Bayernoil refinery in Bavaria, which it increased to 24% and 28.57% respectively in 2017. As Rosneft remained a minority shareholder and as these two refineries are not directly connected to the Russian pipeline network, Russian crude oil never exceeded 15% at either facility and could be replaced more easily when the war started. The Leuna refinery, the other major refinery in eastern Germany, owned by Total was willing to immediately reduce Russian oil imports in 2022 despite its connection to the Druzhba pipeline and its previous dependence on Russian oil.

Nuclear energy

On 15 April 2023, Germany completed its nuclear phaseout after decades of heated public debates. This trend has differed from the rest of Europe, as many EU countries - proponents of the nuclear energy have seen it as a possible solution to meeting their climate targets and the challenge of fully eliminating the use of Russian fossil fuels. Yet, the **European nuclear sector is similarly heavily dependent on Russia** in terms of reactor fuel, technical maintenance and nuclear waste storage and disposal, as gas and oil supplies. Around 20% of EU uranium imports comes from Russia, 26% of uranium enrichment is done by the Russian state-owned nuclear monopoly, Rosatom, and 21 EU-based nuclear reactors are receiving their fuel rods directly from Rosatom.[43] For decades, European companies, including several German firms, have developed strong nuclear cooperation with Russia on a number of projects.

Rosatom is also responsible for the storage and operation of Russia's nuclear weapons. Rosatom's close alignment with Russia's military has been further proven by its recent involvement in the war in Ukraine. After initial denials by Rosatom, it is now clear that the company has effectively taken over the management of the Zaporizhzhia nuclear power plant in Ukraine which Russian troops took by force in March 2022 and is planning to connect the plant to the Russian power grid. While Rosatom is taking care of the smooth operation of the power plant, Russian troops are using the site to launch artillery attacks on Ukrainian forces across the river.[44] Despite this, and despite Ukrainian President Zelenskyy's call for **Rosatom to be sanctioned** for its obvious involvement in the war, EU policymakers have so far been reluctant to do so. This comes as no surprise, given Europe's dependence on Rosatom as a partner in the nuclear sector and the ongoing dealings between Rosatom and European companies. Here, German companies are no exception.

RWE and E.On each hold one sixth of Urenco which, among others, runs a uranium enrichment facility in North Rhine-Westphalia and covers 71% of enrichment services in the EU together with the French company Orano-GBII. Although Rosatom's subsidiary TVEL is considered a competitor of Urenco in the uranium enrichment market, Urenco actually relies on TVEL for large parts of its nuclear waste management.[45] According to Greenpeace, Urenco has delivered 45,000 tonnes of depleted uranium to Russia over the course of the past 25 years[46]. As it is illegal under German law for companies to export nuclear waste, the depleted uranium was officially sent to Russia for re-enrichment, but in reality, the barrels with radioactive waste are often stored under unsafe conditions.[47] Both sides profited from this deal. Rosatom received a substantial payment for disposing of the nuclear waste, while for Urenco it was less of a burden than storing the waste in Germany. However, the war in Ukraine seems to have tipped the scales in a less favorable position for Urenco, as the company declared in March 2022 that it would terminate contracts in both directions until further notice.

Another noteworthy example of a German company engaging in business with Rosatom is Siemens Energy, which for years has been a trusted partner to a number of Russian energy companies delivering equipment to power plants and pipelines (including evading sanctions in the process as with the delivery of turbines to a Crimean gas plant in 2015). Siemens Energy has cooperated with Rosatom on the construction of new nuclear power plants, in particular by supplying so-called I&C systems (instrumentation and control) which ensure the safe and reliable operation of the nuclear facilities. Siemens' equipment was installed in the Novovoronezh II nuclear plant, commissioned in 2017, and in the newly built reactors at the Leningrad II plant, the first of which started operating in 2018.[48] More recently, Rosatom, Siemens Energy and the French company Framatome have been working together on the expansion of the Paks II nuclear power plant in Hungary, a Russia-financed project.[49] Despite the imposition of a wide range of sanctions in the aftermath of the Russian invasion, Siemens has continued the works on the Paks II expansion although the German Federal Office for Economic Affairs and Export Control (BAFA) has delayed granting an export license for the shipment of the I&C equipment.

Rosatom also owns the German company, Nukem Technologies (formerly owned by RWE), which specializes in the dismantling of nuclear power plants and the management of radioactive waste. Nukem has built interim storage facilities and waste treatment centers in a number of countries, including Russia, Lithuania, Bulgaria, Ukraine, Germany and France. One of the two Managing Directors, Thomas Seipolt, is also Chairman of the board of KernD, the central German

43 Gufler, K., Meister, F., *Analyse der Rosatom-Aktivitäten bzw. Rosatom-Verflechtungen mit der EU*, Report REP-0814, Umweltbundesamt, 2022..
44 Melkozerova, V., *Running Europe's largest nuclear power plant under the barrel of a Russian rifle*, POLITICO, April 2023.
45 Gufler, K., Meister, F., *Analyse der Rosatom-Aktivitäten bzw. Rosatom-Verflechtungen mit der EU*, Report REP-0814, Umweltbundesamt, 2022.
46 Weiland, M., *EU-Taxonomie nach russischem Wunsch*, Greenpeace, May 2022.
47 Deutsche Welle (DW) *Weltweite Geschäfte mit strahlendem Müll*, 04.03.2020.
48 urgewald, *Der nukleare Pakt mit dem Teufel - Siemens Energy muss seine Geschäftsbeziehungen mit ROSATOM sofort beenden*, urgewald e.V., Februar 2023.
49 Nuclear Engineering International, *Russia amends loan agreement for Paks II*, NEI Magazine, November 2021.

nuclear lobby organization.[50] In an open letter to Chancellor Olaf Scholz in March 2022, KernD called on the government to reverse its nuclear phase-out strategy, arguing that nuclear power plants could play a vital role in improving Germany's energy security by reducing the need for fossil fuel imports from Russia.[51]

Russia's indirect economic footprint

Russia nurtures the development of informal **private-public networks of influence** based on the mutual partnership between Russian and domestic business groups. They act together to acquire strategic and lucrative assets or to ensure a dominant position in key markets. Local power brokers benefit from Russian political and financial support in engineering the deals. In this context, the extensive ties between Russian and German energy companies have been thoroughly documented. Yet, Russia's indirect economic footprint in the country's most productive industrial segments has been less visible.

Understanding Germany's Russia-friendly stance requires an examination of the informal business and political networks that Russia has established within the country. These networks have enabled Russian influence to extend beyond traditional channels of diplomacy and trade, and have allowed German companies to leverage the relatively cheaper Russian gas to boost their global market positions. However, the decision to lock themselves into a long-term dependence on Gazprom has proven to be a double-edged sword. As Russia gradually reduced gas exports to Europe in 2022, energy prices skyrocketed and fears of supply disruptions mounted. In the following section, we will explore some of the most striking cases of German companies that have developed such networks, which have enabled the Russian influence over Germany's foreign and strategic policies.

Chemical industry

The growth of the German-Russian bilateral business ties has come largely on the back of the German industry's demand for relatively cheap Russian gas as a tool to preserve its global competitiveness. However, achieving this strategic level of partnership between Russian energy suppliers and German business majors has been buttressed by the simultaneous creation of an **intricate web of umbrella forums and organizations**, which have brought together influential Russian and German business representatives and politicians. In turn, they have allowed privileged access of Kremlin-linked entities to the highest policy-making circles of the German government.

The most obvious case of this confluence of political and economic relations is the German chemical industry, which is by far the single biggest industrial gas consumer in Germany. Global leaders such as BASF utilize natural gas both for electricity production and as the main input in manufacturing. BASF's natural gas consumption in Europe in 2021 was 48 terawatt hours (TWh), with the Ludwigshafen site, its main production facility, alone consuming 37 TWh (roughly equal to the total final gas demand of Bulgaria, for example). BASF relies heavily on natural gas to generate its own electricity. In 2021, natural gas accounted for more than 80% of BASF's own electricity generation. At Ludwigshafen, BASF currently operates three natural gas power plants, which together cover 65% of the site's electricity needs. Given this excessive dependence on - mainly Russian - natural gas, it is not surprising that when Russia invaded Ukraine, BASF's CEO, Martin Brudermüller, went so far as to warn of 'the destruction of the entire German economy'[52] if the government decided to block Russian oil and gas imports.

BASF is the main shareholder of Wintershall, which as described above, developed a strategic partnership with Gazprom on developing upstream gas fields and swapping gas transmission and storage assets in Germany. Gazprom benefitted from Wintershall's expertise and technology in increasing gas exploration and production from Western Siberian fields, while BASF received Russian natural gas directly to its production facilities at preferential prices that allowed the chemical giant to become one of Germany's largest businesses.

Despite the dire warnings from BASF's CEO at the onset of Russia's war in Ukraine, in reality the chemical company did not suffer an insurmountable financial blow. In its annual report for 2022, BASF claims that the additional costs for natural gas at its European sites amounted to EUR 2 billion compared to 2021. Yet, BASF avoided the worst-case scenario by implementing a number of demand reduction measures that cut natural gas consumption by a third.[53]

50 Green Planet Energy, *Wie deutsche Atomlobby und russische Atomwirtschaft verflochten sind*, Magazin von Green Planet Energy, September 2022.
51 Behringer, T., *Offener Brief an den Bundeskanzler der Bundesrepublik Deutschland, Herrn Olaf Scholz, zum Weiterbetrieb deutscher Kernkraftwerke*, Kernd, March 2022.
52 Spiegel, *BASF-Chef warnt in Embargo-Debatte vor Zerstörung der gesamten Volkswirtschaft*, Spiegel, April 2022.
53 BASF-Gruppe, *BASF-Bericht 2022*, 2022.

Box 3 | German-Russian Networks of Influence

Since the early 1990s, Russian and German civil society organizations have developed umbrella forums, which have served to strengthen bilateral economic and political ties. The most prominent among them is the **German-Russian Forum**, which started off as a platform for intercultural dialogue but then saw its decision-making bodies being increasingly populated by representatives of German and Russian energy companies and people with ties to the Kremlin. Its activities in supporting the access of Kremlin-linked entities and intermediaries in the highest policy-making circles of German government earned the Forum its reputation as a Russian 'Trojan horse' in Germany.[54]

Another influential enabler of the Russian influence in Germany is the **Petersburg Dialogue**, which was founded in 2001 by German Chancellor Gerhard Schröder and Russian President Vladimir Putin. This organization used to be institutionally tied to the German-Russian Forum, and gathered annually German and Russian policy-makers and business leaders to discuss contemporary issues in German-Russian relations. Additionally, organizations that support German-Russian bilateral economic ties include the **German-Russian Chamber of Commerce and the Association of Russian Businesses in Germany**. These entities bring together businesses from a diverse range of sectors, and their events provide mutual updates on new regulations and the economic climate, as well as plenty of opportunities for networking.

There are also other forums, conferences and organizations with similar intents which operate mainly at state level. In 2009, two years before Nord Stream 1 began pumping gas from Russia to Germany, former SPD North Rhine-Westphalia Minister President Wolfgang Clement founded the Ostinstitut together with Andrey Zverev (then Commercial Counsellor at the Russian Embassy), Peter W. Schulze (co-founder of the pro-Russian think tank DOC) and others.[55] In 2014, the Ostinstitut organised the first Russia Day in Mecklenburg-Vorpommern with the participation of Erwin Sellering, Prime Minister of Mecklenburg-Vorpommern, Wolfgang Clement, Gerhard Schröder and the Russian Ambassador Grinin. The event was sponsored among others by Nord Stream, Gazprom and Gascade. The entanglement of Russian lobby interests and the state government of Mecklenburg-Vorpommern did not stop there. After the end of his tenure as Prime Minister, Erwin Sellering joined the board of the Ostinstitut and founded his own organization named **German-Russian Partnership**.

In Saxony, the two oldest mining universities in the world, the TU Bergakademie Freiberg and the St. Petersburg State Mining Institute, agreed in 2006 to establish a permanent German-Russian forum on the use of raw materials resources (**German-Russian Raw Materials Forum**) in the presence of Angela Merkel and Vladimir Putin. The forum's main sponsors are Gazprom on the Russian side, and Gazprom Germania and VNG on the German side. Each year, the forum organizes a multi-day conference that brings together representatives of material-intensive companies, universities, energy companies, as well as local and national politicians.

In Baden-Württemberg, Klaus Mangold founded the **'German-Russian Conversations'** in 2008, when he was Chairman of the German Eastern Business Association (GEBA). At the first gathering in 2008, Gerhard Schröder was one of the speakers. Other participants were Matthias Warnig (former spy for the East German Ministry for State Security (Stasi), close friend of Putin's and CEO of NordStream) and Eggert Voscherau (BASF). Klaus Mangold, is one of the three Russian honorary consuls in Germany (the others being Heino Wiese and Nikolaus Knauf) and therefore an official representative of the Kremlin's interests in Germany.[56] As former head of the GEBA, Mangold maintains good ties with Russian businesses, oligarchs and Putin himself and has been called 'Mister Russia' in German media.[57] Mangold also has close ties to the Orbán government in Hungary (he facilitated a deal with Rosatom) and facilitated the business of a Russian oligarch in Germany.[58] Mangold also sits on the board of trustees of the German-Russian Forum. The German-Russian Conversations are organized by the GEBA and the BMW Foundation. Previous participants include former German President Wulff, Mr. Mangold himself, former Chancellor and Chairman of Nord Stream 2 and Rosneft Gerhard Schröder, and representatives of BASF, VNG, Gazprom Germania, Rosatom, Siemens Energy, Heidelberg Materials, the Knauf Group, and other companies related to energy and natural resources. Employees of ADVANT Beiten (former BeitenBurkhardt), which is a law and lobby firm known for its pro-Russian engagements, also make regular appearances.

54 Atlantic Council, *The Kremlin's Trojan Horses 3.0*, Atlantic Council, December 2018.
55 Ostinstitut Wismar, *Gründungsmitglieder*, December 2009.
56 Bingener, R. & Wehner, M. (2023) *Die Moskau Connection. Das Schröder-Netzwerk und Deutschlands Weg in die Abhängigkeit.* München: C.H. Beck, p.138.
57 Meck, G., *Mister Russland der Deutschen Wirtschaft*, Frankfurter Allgemeine Zeitung, February 2016.
58 Szabó, A., *The Mysterious German Behind Viktor Orban's Russian Deals*, Direkt36, October 2017.

Food processing

The German food and feed sector has also been affected by the activities of informal Kremlin-linked networks operating in Germany. It is the second largest industrial sector in terms of consumption of Russian natural gas, accounting for around 11% of the total gas demand of the German industry. The negative impact of the crisis on the sector has been enormous, with companies facing skyrocketing prices not only for energy, but also for logistics services and agricultural products. As a result, food prices were 22.3% higher in March 2023 than in the previous year, far outstripping the increase in energy prices (+3.5%).[59]

Tönnies Holding, which is Germany's largest company in the sector, is no exception to the trend. At the start of the Russian invasion, Tönnies sent an urgent letter to its customers[60] in the food retail industry, asking them to increase their prices for meat, as Tönnies did not see itself being able to produce meat at such low prices for much longer. As the largest company in a highly energy-intensive industry, Tönnies Holding also benefitted from the preferential prices at which Gazprom was selling natural gas to Germany via Nord Stream I.

Box 4 | Old habits die hard

Tönnies Holding and Gazprom first came into contact not through direct business dealings, but indirectly through Clemens Tönnies' position as chairman of the board of the football club Schalke 04, where Gazprom became the main sponsor in 2007. The contract was allegedly facilitated by Gerhard Schröder himself, who at the time was already working for Gazprom as a lobbyist and who organised a meeting between Tönnies and Putin in the Kremlin.[61] The agreement between Schalke 04 and Gazprom also gave the Russian gas company, a seat on the board of the team; a position that was held by Schröder's and Putin's friend Matthias Warnig from 2019 until his resignation in February 2022.

Warnig is a former Stasi agent, a member of the board of directors of both Rosneft and Transneft, and the CEO of Nord Stream II AG. In the years following their meeting in Moscow, Tönnies publicly declared himself a friend of Putin's. Pictures taken at the Vladivostok Economic Forum in 2010[62] show Putin laughing and speaking with him, along with two of the three honorary consuls in Germany, Klaus Mangold and Nikolaus Knauf. Angela Merkel and several other German politicians and businessmen were also present.

Tönnies's friendship with Putin benefited his company, as it expanded its business on the Russian market in the past decade. At the peak of its activities, Tönnies generated up to 10% of its export revenues in Russia and held numerous assets such as thousands of hectares of land for grain and beet cultivation, its own feed plant and around a dozen pig farms. Tönnies saw no reason to cut business ties with Russia after the annexation of Crimea, but when the profitability of the company's activities started declining, he decided to sell its Russian assets to a competitor from Thailand in 2021. The move came just at the right time to save the company from deciding on an exit strategy from Russia after the invasion. It was also easier for Tönnies to then condemn Russia's aggression. Meanwhile, Matthias Warnig retired from his position at Schalke 04, and the club officially buried its sponsorship contract with Gazprom.

Cement and building materials production

The production of cement and building materials has also become enmeshed in corporate ties with Russian entities. The perfect examples are two German companies that are both highly competitive on the global market and very active in German-Russian networks: Heidelberg Materials, one of the world's largest building materials companies, and the Knauf Group, the world market leader in gypsum. These cases highlight the importance of how the corporate activities and dependencies of German companies have been used for leverage by Kremlin-led informal networks, and the potential consequences for German economic security and strategic autonomy.

Heidelberg Materials manages cement plants worldwide, including three production facilities in Russia that service the local market only. Nonetheless, the company's exposure to Russia is minimal as these plants generate only around 1% of the firm's global revenues. Still, the company has not left Russia even after the invasion and despite rising production costs linked to surging energy prices. In its annual report, the company states that natural gas made up roughly 11% of the fuel mix for clinker production.[63] Energy expenses jumped by 50% year-on-year to €2.98 billion in 2022 while sales plummeted by 6.1 %. Heidelberg Materials took advantage of the discounted rates at which Russia supplied Germany with natural gas until Gazprom's unilateral gas cuts. The company has been hesitant to transfer the higher energy and raw materials costs

59 Verbraucherzentrale, *Steigende Lebensmittelpreise: Fakten, Ursachen, Tipps*, Verbraucherzentrale, May 2023.
60 Terpitz, K., *Fleischbranche sieht Existenz bedroht - Tönnies & Co. Rufen nach höheren Preisen*, Handelsblatt, March 2022.
61 Kopp, J., *Schalke 04 und sein russischer Sponsor: Schauriger Partner*, taz.de, February 2022.
62 Sputnik Mediabank, *Vladimir Putin visits Germany*, Sputnik Mediabank Gallery, November 2010.
63 Heidelberg Materials, *Berichte und Präsentationen*, HM: 2023.

onto its clients, as demand for its products is highly elastic. Even though the energy crisis was exacerbated by Gazprom's actions, Heidelberg's annual report in 2022 did not blame Russia for the difficult financial situation, but 'the sanctions against Russia in the financial and energy sectors'.[64]

Heidelberg also has proven links to the extensive network of German and Russian politicians, business and civil society enablers of the Russian influence in Germany. One of its former board members also had a seat on the board of the German-Russian Forum during his term of office.[65] In 2014, Heidelberg Materials organized the "Young-Leader Seminar" for the German-Russian Forum, which was an invitation for 30 German and Russian young leaders to explore the production sites of Heidelberg Materials, SAP, BASF and John Deere.[66] Furthermore, at least two representatives of the company participated in Klaus Mangold's German-Russian Conversations in 2015 and 2021. Heidelberg Materials has condemned the war in Ukraine

Box 5 | The Knauf Group Case

The Knauf Group, along with BASF, are among the most compelling illustrations of how a dominant German corporation can become an instrument of Russian interests within Germany. Nikolaus Knauf, former CEO and chairman of the shareholders' committee and son of the original founder, has a central role. In the 1990s, Knauf and his brother spearheaded a bold expansion into the Russian market, resulting in the establishment of 14 production sites in Russia, with 4,000 workers, making the Knauf Group the leader in drywall and interior construction building materials. This significant contribution to the Russian economy earned Knauf recognition from Vladimir Putin, who appointed him as the first Honorary Consul of the Russian Federation in Germany in 1998, and later bestowed upon him the Order of Friendship in 2006 for fostering Russian-German friendship relations.

As Honorary Consul of the Russian Federation in Germany, Knauf became an official representative of Russian interests within Germany. He leveraged his position to facilitate German-Russian business deals and served as a board member of the German-Russian Forum for several years. Knauf also hosted the Club of the German-Russian Forum in Nuremberg in 2018, where he spoke to Sputnik News about the impact of sanctions on Knauf's business in Russia. In the interview, Knauf lamented that the Knauf Group was losing 1.2% growth each year in Russia, which he claimed they would have achieved under normal circumstances, were it not for the sanctions.[67]

Similarly, like his fellow Honorary Consul, Klaus Mangold, Knauf also had a role in GEBA, where the Knauf Group finances the Contact Point for Small and Medium-Sized Enterprises for Russia (KSM). The purpose of the KSM is to support German SMEs who are active in the Russian market or who intend to enter it, by facilitating business contacts. The close collaboration of the two Honorary Consuls is further evident through the participation of Knauf Group representatives in almost every edition of Mangold's German-Russian Conversations since 2008.[68] Furthermore, the Knauf Group is also among the primary sponsors of 'Germany-Russia – The New Generation,' an organization whose stated objective is to bring together young talents from the two countries. However, in reality, the organization is reportedly infiltrated by representatives of energy companies and Kremlin associates, similar to the other organizations mentioned earlier.[69]

Obtaining reliable information on the extent to which the Knauf Group depends on natural gas for its production processes and the potential impacts of rising energy prices and supply risks on its competitiveness can be challenging. However, a document from 2014 sheds some light on the matter, indicating that natural gas accounted for 16% of Knauf's production costs at that time, twice as much as the costs for electricity.[70] If the Knauf Group still relies significantly on natural gas for its production processes, it may face considerable pressure on the prices of its products. This conclusion is supported by letters the company sent to its business partners in 2022. In a letter from July of that year, the Knauf Group announced that price increases have become necessary once again due to unfavorable developments in the prices of energy, raw materials, and logistics. The letter noted that price increases would vary between the different types of products, ranging from 2% to 26%.

This is not the first time the Knauf Group has had to raise prices due to Russia's war on Ukraine. Such reliance on Russia may have previously helped safeguard the company's competitiveness, but it may now pose a threat to its ability to compete in the global marketplace. Yet, it seems that the recent resignation of Nikolaus Knauf as Honorary Consul of the Russian Federation in Germany shows the company may have recognised the risks of its dependence on Russia and may lead the firm to cease production in Russia.

64 Heidelberg Materials, *Geschäfts- und Nachhaltigkeitsbericht 2022*, HM:2022.
65 German-Russian Forum, *Mitgliederliste Deutsch-Russisches Forum e.V, Deutsch-Russisches Forum e.V.*, June 2016.
66 German-Russian Forum, *Info-Bulletin Special 42. Young-Leader Seminar Walldorf*, Deutsch-Russisches Forum e.V., September 2014.
67 German-Russian Forum, *45. Club Forum Konferenz-Broschüre*, Club FORUM, October 2018
68 German-Russian Dialogues Baden-Baden (Deutsch-Russische Gespräche Baden-Baden), *Gespräche 2008*, DRGBB, October 2008.
69 German-Russian Forum, *Our sponsors and supporters*, Leaders Conference, 2016.
70 Wintrich, H., *Energieeffizienz, ein wichtiger Schritt zur Standortsicherung bei Knauf*, 2. Energiedialog Mainfranken, 2014.

5. Towards strategic decoupling from Russia

The Kremlin's war in Ukraine has disenchanted decades of German foreign policy towards Russia. It has also put Europe at its most difficult test so far undermining the EU unity and the ability to defend its common democratic values and strategic objectives. In addition, the war has upset Europe's global standing and has hurt its economic recovery and outlook. The scale and brutality of the Russian invasion have summoned a decisive response from the German society and the German government, following the initial shock. As a result, **Germany has quickly inaugurated emergency economic security and decoupling polices** in the energy sector, and has upheld unprecedented EU and G-7 sanctions and technology and goods control on Russia. These policies have come at a considerable cost for the German business and households. China's (muted) support of Russia's invasion of Ukraine has put further strain on the German government to re-think its long-term strategy for geoeconomic and geopolitical positioning vis-à-vis countries with considerable state capture power.

As a first line of defense, Germany needs to complete its decoupling from Russia to make sure Moscow would not be able to deploy any of its Kremlin Playbook instruments in the future. Germany's first ever National Security Strategy has been a major step in this direction while also acting as a dress rehearsal for addressing China's rising global coercive power.

Germany needs to spearhead and support EU efforts to design and kick start a common economic security strategy with its respective instruments on risk assessment, investment screening, customs and financial intelligence coordination, anti-money laundering, etc. Similarly, Germany should act as a voice for environmental protection and human rights in EU negotiations with resource-rich third countries on the establishment of the Critical Raw Materials Club foreseen in the European Economic Security Strategy[71], to ensure that European access to a reliable flow of raw materials does not come at the expense of the well-being of people in partner countries. Economic security, needs to be counterbalanced with a comprehensive European nearshoring and investment strategy built around leadership in green and digital technologies.

The assessment of the Russian economic influence in Germany has shown that the long-term dependence on Russian fossil fuel has also contributed to the entrenching of **powerful corporate networks of influence** linked to Russian oligarchic and/or state-owned companies, which the Kremlin can use to sway specific German decisions. Germany needs to completely eliminate its dependence on Russian fossil fuel imports and nuclear cooperation in other European markets in order to strengthen its energy and economic security, and undermine the basis of the Russian economic and political power.

Decisive action by the German government can deal a severe blow to Russia's revenues and thus weaken its war potential. Furthermore, the price that households and businesses had to pay for the government's short-term measures to reduce energy demand and put energy prices under control is worth the long-term positive implications for Germany's economic security and its European leadership. In the end, the emergency measures will contribute the EU and German long-term energy and climate security strategy.

The next steps of Germany's decoupling and derisking of its economic relationship with Russia should see the German businesses continuously and gradually phase out their **exposure to the Russian market** by closing their operations in Russia and by letting joint ventures and corporate partnerships with Russian companies expire. There is also an urgent need to continuously map the informal Russian economic and political networks active in Germany and dismantle their influence. Germany and the EU need to build up defense to fend off strategic corruption attempts and raids on Europe's technological base.

Germany's economic security and strategy for the new global realities require sophisticated mechanisms for **screening and halting of overt and covert Russian strategic investments** in Europe linked to state-owned companies and oligarchic networks close to the Kremlin. Such screening needs to be complemented by measures for ensuring intra-EU corporate ownership transparency and the **strengthening of the European anti-money laundering infrastructure** and efforts on reducing the Kremlin's hidden economic footprint in Europe. Germany needs to strengthen the national laws on the **transparency of ultimate beneficial ownership** of companies and other legal entities such as civil society organizations, foundations and charities. In addition, Germany should **build up the capacity of regional governments to implement economic and investment security instrument**, in particular in strategic sectors such as energy, manufacturing, banking, defense and real estate.

The German government, in cooperation with the US and fellow EU countries, needs to prioritize the **stopping of Russian illicit financial flows** to Germany and the **closing of governance gaps** that have allowed Russian companies to evade sanctions before, and the tracking and seizing of the assets of Russian oligarchs across Europe. For example, Germany should make sure that Russian oil and natural resources companies do not bypass the oil embargo by utilizing intermediaries like Turkey and the UAE or businesses that have strong connections to the Kremlin to sell Russian crude oil or oil products in Germany and other parts of the European market.

71 European Commission, *European economic security strategy*, June 2023, p.13.

To facilitate the ultimate exit of German business from Russia, the government should strongly disincentivize German companies from entering **joint ventures and starting common projects with Russian state-owned companies** or with (sanctioned) Russian businesses/ oligarchic networks linked to the Kremlin. German entities should pay particular attention to avoiding participation in Russian public procurement tenders or the delivery of dual-use goods to Russia via third countries.

The German government should **incentivize German majors to leave the Russian market** by imposing higher taxes on the repatriation of profits generated there. The higher taxes should be combined with fiscal and other financial stimuli for German majors to relocate their investments in other neighborhood regions such as the Western Balkans, the Black Sea and North Africa where the German, and generally, the EU economic footprint could be strengthened as a way to counter the rising influence from authoritarian states.

There is a need for a **common EU mechanism for sanctions enforcement** that prescribes specific requirements for national customs officials to investigate the ultimate beneficial ownership of the EU companies selling sanctioned and dual use goods and that of buyers in third countries. To ensure compliance strict destination clauses for sanctioned items should be placed in supply contracts backed by a mechanism for cooperation with customs authorities in third countries in joint investigation of suspicious trade deals.

On the domestic front, German politicians should be required to make public any involvement in civil society organizations or events organized by NGOs, supported by non-EU and non-OECD entities. This requires the strengthening of the oversight on the collaboration between domestic political parties and both state and non-state entities from Russia, with a particular emphasis on **political actors who publicly oppose sanctions against Russia** or promote Russia's strategic objectives. On societal level, Germany needs to increase the awareness of Russian influence operations and their corrosive impact on the public debate, which would help people identify and resist such campaigns.

Probably the most potent long-term derisking strategy of the German government is the attainment of the **EU's energy and climate security objectives and ambitions** for 2030 and 2050. The existing strategic documents in this domain still contain unattainable targets and disjointed measures that could contradict the priorities of the EU. Strengthening energy and climate security would also require taking a number of additional strategic decisions including:

→ Mandate all German companies to discontinue their long-term natural gas supply contracts with Gazprom after their expiration in 2024.

→ Set up a strategic natural gas reserve stock following the example of the strategic oil reserve and implement strictly a mandatory 90% target for natural gas storage injection by 1 December of each year.

→ In line with its net-zero ambitions, Germany should continue to seek ways to accelerate the development and deployment of cutting-edge green technologies, such as new heating solutions and take measures to fully realize the country's offshore wind energy potential.

→ German companies should be careful when considering new long-term LNG supply contracts, including by implementing more viable corporate net zero strategies.

→ Roll out demand response tenders for industrial gas consumers to further reduce natural gas demand and prevent large-scale losses in case natural gas prices skyrocket again in the autumn of 2023.

→ In the industrial sector, accelerate the uptake of renewable energy-based electrification and alternative fuels that would reduce the German economy's excessive dependence on the import of fossil fuels.

→ Germany should strengthen efforts to friendshore supply chains and increase cooperation with countries sharing the West's strategic objectives. This is especially true if Germany, and by extension, Europe is to accelerate the green transition of its economy and to simultaneously lower its dependence on critical raw materials.

Germany's urgent need for strategic decoupling from Russia has become increasingly evident after the invasion of Ukraine and the subsequent paradigm shift for European geopolitics. Germany has implemented emergency economic security policies, including sanctions and trade controls on Russia, in order to strengthen its energy and economic security. In addition to these measures, however, it remains crucial for Berlin to eliminate its dependence on Russian fossil fuel imports, weaken Russian economic and political power, and contribute to Europe's long-term energy and climate security strategy. Germany should gradually phase out its exposure to the Russian market, dismantle Russian influence networks, and establish screening mechanisms for Russian investments. Collaboration with the U.S. and EU is vital to prevent illicit financial flows and incentivize German companies to redirect investments. Transparency, public awareness, and achieving EU energy objectives are essential steps toward a resilient and sustainable Europe.

About the Authors

Center for the Study of Democracy (CSD)

Founded in late 1989, the Center for the Study of Democracy (CSD) is a public policy institute fostering the reform process in Europe through impact on policy and civil society. CSD's mission is "building bridges between scholars and policy-makers" and as an independent, interdisciplinary think tank it combines a broad range of capacities.

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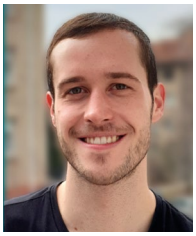

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