

**BRIEFING NOTE**

# Investors and the Russian Invasion of Ukraine

April 29, 2022





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**T**here can be no peace without equitable development and no development without sustainable management of the environment in a democratic and peaceful space.”

**Wangari Maathai**, Nobel Peace Prize recipient, 2004



Nations, international institutions, the private sector and civil society are responding to the Russian invasion of Ukraine that began in February 2022, seeking an end to the conflict and addressing the resulting humanitarian crisis. The Russian invasion and occupation of Ukraine is contrary to international law and to widely recognized human rights standards.

**The primary responses have been support for territorial defence by Ukraine, economic sanctions against Russia, refugee assistance and diplomatic initiatives.**

The war in the Ukraine raises important short- and long-term humanitarian, human rights and economic issues for investors. In the short term, companies with operations or business relationships in Russia that are not restricted by sanctions must decide how they will respond. Some within the energy sector are pressing for investments to increase alternate fossil fuel supplies that conflict with long-term sustainability and climate change mitigation goals. The millions of displaced women and children increase the danger of human trafficking and forced labour, with consequent challenges for business.

In the long term, the conflict demonstrates again the enormously destructive power of war in the 21<sup>st</sup> century, and the wide negative economic footprint of conflict. Infrastructure valued at \$100 billion has been destroyed in less than eight weeks in Ukraine, in addition to the immediate human toll;<sup>1</sup> and Ukraine's GDP is expected to contract by more than 45% this year, with expected regional impacts.<sup>2</sup> In countries dependent on food grains and fertilizers from Ukraine and Russia, shortages and price increases resulting from supply disruption are expected to increase food insecurity and political instability. Globally, more than 10% of GDP is spent on police, military and other responses to violence and security.<sup>3</sup> The Russian invasion of Ukraine is leading some countries to consider increases in national military budgets, risking further competition for the resources needed to achieve Sustainable Development Goals.

**This briefing note discusses six questions for investors, both short-term and long-term, raised by the Russian invasion of Ukraine.**

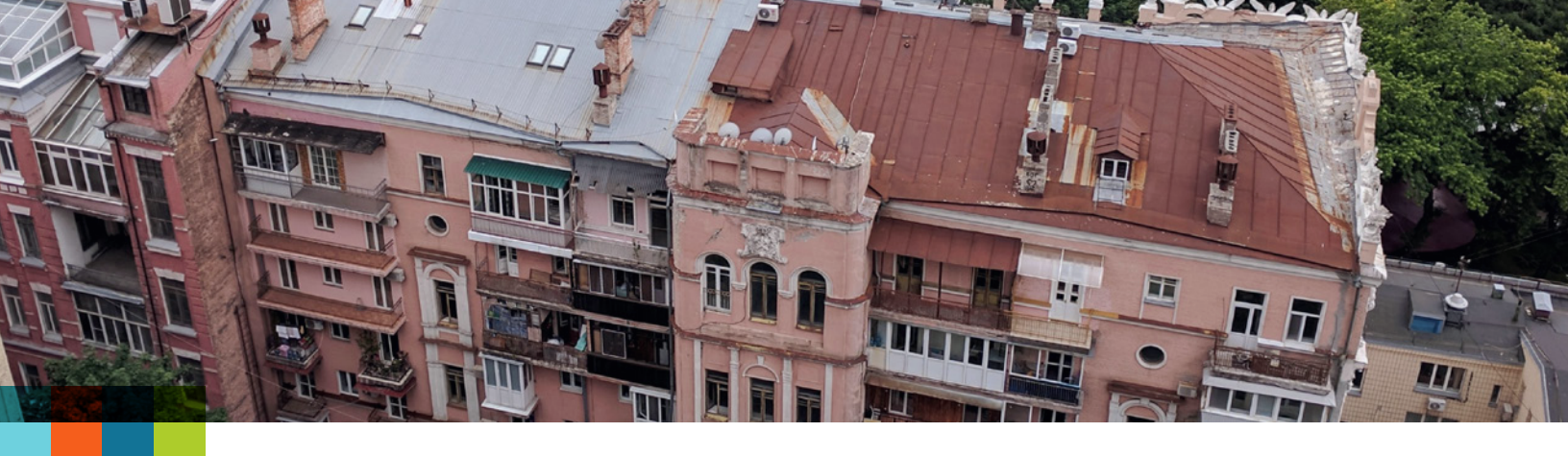
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1 Pavel Polityuk, "Russian invasion damaged up to 30% of Ukraine's infrastructure, says minister" *Reuters*, April 18, 2022.

2 World Bank, "Russian Invasion to Shrink Ukraine Economy by 45 Percent this Year". Press Release. April 10, 2022.

3 Institute for Economics and Peace. *Economic Value of Peace 2021; Measuring the Global Economic Impact of Violence and Conflict*. 2021. Page 2.





# 01

## What can investors do to facilitate an end to the Russian invasion of Ukraine?

Investors should comply with sanctions, and undertake due diligence to ensure that their investments do not cause or contribute to the conflict.

- The primary step investors are taking is to remove direct investment in Russian sovereign debt and Russian equities from their portfolios. This is hampered by market closures and sanctions.
- Complying with sanctions is required, but insufficient. The human rights responsibilities and obligations of business go beyond legal compliance, and include acting in a manner consistent with the UN Guiding Principles on Business and Human Rights.
- Investment in conflict-affected and high-risk areas carries financial risks tied to international standards and norms, and international humanitarian and human rights law. Unresolved, the invasion and occupation of Ukraine represents a risk to financial markets, as well as to vulnerable populations. The legal, ethical, financial and fiduciary issues raised by the invasion are not easily separated.
- Enhanced due diligence appropriate to a conflict zone should be undertaken to ensure that investments throughout the whole value chain, including direct and indirect ties to Russian state enterprises, are not causing or contributing to human rights abuses or the conflict.
- The Investor Alliance for Human Rights has called for investors to “identify business and investment ties to the Russian state, their affiliated companies, and other entities or individuals that are arming, financing, resourcing, or otherwise contributing to Russian violations of humanitarian and human rights laws.”
- Roger Beauchemin, President and CEO of Addenda Capital and Chair of the Responsible Investment Association, urged investors to “use your portfolio as a weapon”.<sup>4</sup> However, caution should be exercised to ensure that the impact of investor actions on all parties, including vulnerable populations, are considered.
- Investors should review their response to this and similar events (e.g., the 2008 Russian military action in Georgia or the Russian occupation of Crimea in 2014) to identify weaknesses in investment risk management; and protect against conflict-stranded assets and complacency in the face of military aggression, anti-democratic activity, and violations of international humanitarian and human rights law.

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<sup>4</sup> Melissa Shin, “No need to redefine ESG for wartime, RIA chair says”, *Investment Executive*. March 18, 2022.

# 02

## What should investors expect of portfolio companies?

All companies should engage in heightened due diligence to ensure that they comply with sanctions, and are not complicit in violations of human rights and international law throughout their value chain.

- Complying with government-imposed sanctions is a legal obligation.<sup>5</sup> In addition, companies with operations in Russia should cease operations unless they produce essential goods or services that cannot be provided locally. Decisions about operations should include considerations for the safety, security and economic welfare of employees.
- Companies operating in Russia should ensure that they are not complicit in undermining those who support the recognition of universally recognized human rights.
- Like investors, companies should undertake heightened due diligence to ensure that their direct and indirect economic relations with Russia, including purchases or sale of goods and services throughout the value chain, do not contribute to violations of human rights.
- Companies should consider whether business relationships provide influence that may be exercised in the interest of peace and the observance of human rights.
- The Yale Chief Executive Leadership Institute has created a list of more than 1,000 companies with operations in Russia, and ranked their responses according to five categories, ranging from Withdrawal (“A”) to Digging in (“F”).<sup>6</sup> According to the Yale database, Canadian companies that have suspended operations in Russia include Alimentation Couche-Tard, Bombardier, Restaurant Brands, Canadian Tire, Kinross and Magna.<sup>7</sup> Oil field services company Calfrac is continuing to operate in Russia, within limits imposed on the company by government sanctions.<sup>8</sup>
- One in four people in the Ukraine have been displaced by the Russian invasion. More than five million Ukrainians have fled the country since late February,<sup>9</sup> and an additional seven million Ukrainians are internally displaced. Ninety percent are women and children. The United Nations High Commissioner for Refugees has warned that this massive dislocation has dramatically raised the risks of human trafficking and modern slavery.<sup>10</sup> Investors should support enhanced due diligence and mandatory disclosure, including new measures announced by the Canadian government.<sup>11</sup>
- Proper human rights due diligence requires knowledge and skill. Companies should ensure that their processes are properly resourced.

5 For example, Government of Canada, [Canadian Sanctions Related to Russia](#) and European Council, [EU restrictive measures against Russia over Ukraine \(since 2014\)](#).

6 <https://www.yalerussianbusinessretreat.com/> Accessed April 22, 2022.

7 [https://som.yale.edu/story/2022/over-750-companies-have-curtailed-operations-russia-some-remain?utm\\_campaign=mb](https://som.yale.edu/story/2022/over-750-companies-have-curtailed-operations-russia-some-remain?utm_campaign=mb) Accessed April 21, 2022.

8 [Calfrac Announces Suspension of Investments in Russia](#), Press Release, March 28, 2022.

9 UN High Commissioner for Refugees, [Ukraine Refugee Situation](#), April 21, 2022.

10 Kristy Siegfried, [“Ukraine crisis creates new trafficking risks](#), United Nations High Commissioner for Refugees”, April 13, 2022.

11 Marie Woolf, [“Law combating modern slavery and child labour a priority: minister”](#), *Toronto Star*, April 20 2022.

# 03

## Can economic sanctions and investor action contribute to the end of the war?

Economic sanctions are an important tool of the international community in response to violations of international laws and norms. The goal of sanctions is to deliver an economic shock sufficient to change behaviour. Continuing “business as usual” can be seen as a tacit acceptance of military aggression. However, improperly applied, sanctions and investor action have the potential to prolong conflict and harm vulnerable populations. Action should be taken to mitigate potential negative impacts on third parties.

- ◉ Woodrow Wilson called sanctions “something more tremendous than war.”
- ◉ Trade is generally seen as promoting peace, but in this acute situation, any form of commerce could be viewed as legitimizing the invasion or contributing to Russia’s military capacity.
- ◉ Russia is the world’s 11th largest economy; a member of the G20; and a major exporter of oil, gas and food grains.
- ◉ As of April 21, more than 750 Western companies have withdrawn or suspended business operations in Russia. After an initial sharp decline, Russian currency has rebounded as sales of oil and gas continue, and currency controls have been imposed. The Russian GDP is expected to contract by 20% in 2022.
- ◉ Sanctions have focused on the financial sector and technology. Europe has not placed sanctions on coal, oil and gas – Russia’s most valuable export commodities. Although doing so would be an enormous shock to the Russian economy, it also risks creating an energy crisis with global consequences.
- ◉ Decisions on sanctions and business relationships need to consider the views of those within Russia who are working for peace. Russian opponents of the invasion of Ukraine have expressed support for stronger sanctions, according to Mary Kaldor, London School of Economics.<sup>12</sup>
- ◉ Assessments of the impact of sanctions and investor action should consider the implications for countries dependent upon Russia, particularly for energy and food. One option would be to ensure that food grain production and export by Russia is not harmed by sanctions.<sup>13</sup>
- ◉ The impact of sanctions and voluntary withdrawals by companies may hurt ordinary Russians, and be less consequential for elite decision-makers.
- ◉ According to academic Nicholas Mulder, sanctions tend to be less effective in authoritarian states, and over time, as countries adjust to new supply chains and customers. Economic sanctions on the scale of those currently imposed on Russia have not been tried before. Mulder believes that the success of sanctions as a tool to end conflict depends on ensuring a clear path to end them.<sup>14</sup>

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12 Mary Kaldor [interview](#), Novara Media, March 2, 2022.

13 Ian Mitchell, Sam Hughes and Samuel Huckstep, “Price Spike Caused by Ukraine War Will Push Over 40 Million into Poverty: How should we respond?”

14 Nicholas Mulder, “Russia’s economic isolation will have dramatic repercussions for the world economy”, *The Economist*. March 4, 2022.



## 04

### Should Canada increase oil and gas production to help reduce European dependence on Russian energy?

European dependence on Russian oil and gas has created short-term challenges to reducing foreign income that Russia may use to fund its war in Ukraine, and to taking steps that might help end the conflict. But while short-term substitution of oil and gas supplies from other sources can help alleviate immediate problems, the Russian invasion of Ukraine is not a reason to delay addressing climate action.

- ⦿ The need for short-term alleviation of supply does not justify capital expenditures that would commit Canada and other countries to higher GHG emissions in the long term; and jeopardize a rapid, orderly and just transition to a low-carbon economy.
- ⦿ The secure energy needs of all countries, particularly low-income countries, must be considered as part of the response to the Russian invasion of Ukraine.
- ⦿ Generation Investment Management has commented, “The West is directly funding this war by buying Russian hydrocarbons. [...] Dependence on fossil fuels creates geopolitical instability, allowing autocratic nations to survive and encouraging conflict.”<sup>15</sup>
- ⦿ The rapid deployment of conservation and renewable energy measures offers a viable alternative to long-term investments in oil and gas infrastructure.
- ⦿ The political consequences of energy dependence in this situation demonstrates the value of speeding the transition to a greater emphasis on conservation and renewable energy.

## 05

### Should armaments be considered a socially responsible investment?

Labelling weapons as “socially responsible investments” is inappropriate. States’ right to defend themselves is recognized in international law, and the production of armaments in some circumstances may be justifiable. But high levels of regional armament generally correspond to lower levels of human security. The production of weapons diverts resources away from social development, and the alleviation of poverty and Sustainable Development Goal 16.

- ⦿ Article 51 of the United Nations Charter guarantees the right of self-defence, and supports the right of other states to provide military assistance to Ukraine.

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<sup>15</sup> Generation Investment Management, “Fossil Fuels, the Economy and Instability: Why the world’s dependence on fossil fuels hurts the economy and creates instability”, March 15, 2022.

- ◉ The Arms Trade Treaty, to which Canada became a party in 2019, obliges states to establish controls over the international sale of weapons, including undertaking risk assessments and putting in place risk mitigation measures.
- ◉ Although the transfer of lethal arms to Ukraine is permitted, it is not without potential risks and consequences, including: (1) the diversion of weapons into private hands for sale globally; and (2) the escalation of post-conflict regional violence as a result of the prevalence of arms and light weapons, including the emergence of armed non-state actors.<sup>16</sup>
- ◉ Hans Christian Atxpodien, head of the German defence industry lobby group BDSV, says, “The invasion of Ukraine shows how important it is to have a strong defense. I appeal to the EU to recognize the defense industry as a positive contribution to ‘social sustainability’ under the ESG taxonomy.”<sup>17</sup> His statement was strongly contradicted by Antje Schneeweiss, Managing Director at German church investors Arbeitskreis Kirchliche Investoren.<sup>18</sup>
- ◉ The purpose of a sustainable finance taxonomy is to create common definitions and terminology about what is meant by “sustainable”. Such a taxonomy may be applied to labelling financial products, identifying required financial market disclosures, and addressing legal and regulatory obligations.
- ◉ The most notable Canadian contribution to weapons systems involved in the war in Ukraine is the L3Harris webcam, part of the targeting system of Turkish Bayraktar TB2 drones, which have been effective in attacking Russian armour. Canada has also sent small arms and ammunition, recently approving an \$80-million military aid package.
- ◉ Increasing small arms and light weapons will have long-term negative consequences for peace and security in the region; and the chaos of war, plus Ukraine’s existing reputation as a source of illicit weapons transfers, increases the danger of diversion of weapons being shipped into the region.

## 06

### Is peace and security a systemic risk that investors should consider?

The Russian invasion of Ukraine highlights the systemic risk that peace and security issues pose for investors and the companies in which they invest. Institutional investors can help build a stable investment environment by supporting democratic rights, strong international institutions, and the protection and enhancement of humanitarian and human rights. Systemic change is required.

- ◉ Sustainable Development Goal 16 (SDG16) is “Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels.”
- ◉ The world currently spends more than 10% of global GDP on “containing, preventing, and dealing with the consequences of violence”.<sup>19</sup> Military expenditures alone surpassed \$2 trillion (US) in 2021.<sup>20</sup>

16 Tomas Hamilton, “Articulating Arms Control Law in the EU’s Lethal Military Assistance to Ukraine” March 30, 2022.

17 Deutsche Welle “Pointing to Ukraine war, arms lobby pushes for ‘sustainable’ label”. n.d., Accessed March 25, 2022.

18 Gina Gambetta, “Armaments ‘cannot be classified as social’ in taxonomy, says rapporteur”, *Responsible Investor*, March 22, 2022.

19 Institute for Economics and Peace, *Global Peace Index 2021: Measuring Peace in a Complex World*. 2021, page 38.

20 Stockholm International Peace Research Institute, “World military expenditure passes \$2 trillion for first time”, April 25, 2022.



- ⦿ These resources could be used for development assistance, and to promote a more peaceful and just world.
- ⦿ In addition to diverting resources away from human needs, conflict also creates negative outcomes for business. As John Ruggie stated, “The message for businesses is that the cost of conflict is not only imposed on the victim; you are also imposing costs on yourselves. This is a lose-lose proposition that you can and should fix.”<sup>21</sup>
- ⦿ Higher military expenditures increase the risks and potential consequences of violence. The international response to the Russian invasion of Ukraine could be an acceleration of arms races regionally and globally, with consequent negative impacts on the broader economy, sustainable development and, ultimately, investment returns.
- ⦿ Corporate reporting, and the development of metrics and performance expectations related to SDG16, remain underdeveloped. Improvements will aid investors in assessing corporate performance and market conditions.<sup>22</sup>
- ⦿ The political power of the military industrial complex creates the risk that military expenditures will increase, and economies and societies will suffer. Bradford University Emeritus Professor of Peace Studies Paul Rogers observes that weapons producers are benefiting from the conflict and are using the efficacy of their weapons in the conflict to boost arms sales globally.<sup>23</sup>
- ⦿ Sanctions are supported by countries representing approximately 55% of global GDP, but these countries are primarily in the Global North.<sup>24</sup> The Global South is not only still recovering from the 2008 global financial crisis, but continues to deal with a lack of access to COVID-19 vaccines. It now faces rising inflation, and the disruption of food and energy flows, because of the war in Ukraine. Continuing sanctions have implications for democracy and social development, as well as international political alignments.

## Resources

- Investor Alliance for Human Rights, Investor Alert: Human Rights Risks Related to the Russian Invasion of Ukraine. <https://investorsforhumanrights.org/news/investor-alert-human-rights-risks-related-russian-invasion-ukraine>
- Principles for Responsible Investment, “Russian invasion of Ukraine” (March 2, 2022). <https://www.unpri.org/news-and-press/russian-invasion-of-ukraine/9587.article>
- Institutional Investors Group on Climate Change. “The impact of Russia’s invasion of Ukraine for the energy transition”. March 17, 2022.
- United Nations Guiding Principles on Business and Human Rights.

21 Quoted in Business & Human Rights Resource Centre, “Advancing business respect for human rights in conflict-affected areas through the UNGPs”, June 9, 2021.

22 PeaceNexus Foundation, *Strengthening Corporate Reporting on Sustainable Development Goal 16 Peace, Justice and Strong Institutions*. Swiss Peace Foundation, PeaceNexus Foundation and UN Global Compact, November 2020.

23 Paul Rogers, “The Ukraine war will hurt people worldwide – no matter who wins”, *Open Democracy*. March 25, 2022.

24 Nicholas Mulder, “Don’t Expect Sanctions to Win the Ukraine War”, *Wall Street Journal*. April 21, 2022.

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