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Cross-Border Economic Cooperation and Market Integration: The Impact of Geopolitics on the Finnish Economy

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Abstract

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Geopolitical events present significant risks of disrupting cooperation between countries. This becomes especially critical when one country develops a dependency on the other one that is directly involved in these events. That was the case of Finland and Russia, when the long-standing economic relationship and Finland's dependency on Russia as a trade partner collapsed following the geopolitical escalation of 2022. This study combines a literature review and statistical analysis to examine trade patterns and economic indicators to address the following research question: "How have the recent geopolitical events affected the economy of Finland, and what opportunities do Russia and Finland face in potential future relations?" The thesis explores the historical relationship between the countries to establish how Finland dealt with geopolitical shifts in the past. The findings show that in 2022, Finland's economy experienced notable setbacks such as high inflation, an energy crisis, and a trade deficit. The loss of access to the Russian market and energy sources exposed Finland's vulnerabilities due to previous dependence. Despite the economic shock, Finland acted swiftly by diversifying trade partners and securing new energy suppliers. This helped to stabilise the economy and reduce future risks by breaking the dependence. The study also emphasises that future cooperation between the countries is possible and even desirable, following resolution of the current conflict.

Keywords: Geopolitics, Finnish economy, Cross-border trade, Sanctions

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Glossary

CCI	Consumer Confidence Indicator
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
INSTC	International North-South Transport Corridor
NATO	North Atlantic Treaty Organisation
OPEC	The Organisation of the Petroleum Exporting Countries
PPP	Purchasing Power Parity
SWIFT	The Society for Worldwide Interbank Financial Telecommunication
TPP	Trans-Pacific Partnership
USSR	The Union of Soviet Socialist Republics
WTO	World Trade Organisation

1 Introduction

In an increasingly interconnected world, the geographical proximity of countries plays an important role in the formation of economic partnerships and trade agreements. It heavily influences the countries' economic strategies, contributing to market integration and the development of cross-border cooperation. This, in turn, allows for resource sharing and smooth cross-border trade, reducing transaction costs and encouraging both economic and cultural exchanges. In the literature of economics, this is conceptualised as “gravity”, whereby the shorter the distance between two countries, the stronger the “pull” of trade relationships (Shahriar et al., 2019: 28).

However, despite the obvious benefits, cross-border cooperation is highly sensitive to geopolitical shifts. Unexpected crises can disrupt all relationships and trade, leaving both countries with significant losses.

As a nation located at the border of Europe and Russia, Finland's economic landscape is deeply influenced by political events beyond its borders. Until recently, Finland had to navigate a position of relative neutrality between the East and West, engaging in trade with both the European Union (EU) and Russia.

Historically, Russia has been Finland's biggest trade partner for many years. Sharing a 1,340 kilometres long border, the countries have also been sharing industries, such as manufacturing and technology. This connection facilitated the development of mutual trade networks, which allowed both countries to benefit from shared resources and trade agreements. The proximity also contributed to the high tourism flow between the countries, which further brought profits to the local businesses.

The events of the past decade have complicated the relationship between the countries and have led to the disruption of their trade. For Finland, these disruptions resulted in significant economic challenges, due to the long-

established dependence on Russian raw materials. EU-wide sanctions imposed on Russia forced Finland to reassess its economic strategies. Businesses had to withdraw from the Russian market, resulting in revenue loss, export reduction, and increased unemployment. Finland was forced to seek alternative options in its supply chain, particularly in regard to energy supply.

This thesis aims to contribute to the topic of geopolitics' influence on the Finnish economy. The topic was chosen with the thought of understanding how the recent geopolitical events have affected the economic interdependencies between Finland and Russia, and what new challenges have emerged for Finnish businesses and regional trade. The thesis aims to analyse both the historical and current state of the economic relationships between the countries. Furthermore, the research also aims to explore how Finland can potentially engage in any future opportunities to establish an economic connection with Russia while also being aware of its risks. Since the geographical position of both Finland and Russia cannot be changed, it is important to consider a situation when their relations improve. Thus, investigating future opportunities becomes vital.

The research question for this topic is as follows: "How have the recent geopolitical events affected the economy of Finland, and what opportunities do Russia and Finland face in potential future relations?"

2 Methodology

The research will rely strongly on secondary data sources to examine the impact of geopolitical tensions on Finnish-Russian economic relations. This includes a comprehensive review of existing literature as well as compilation of relevant statistical data. For this study, a mixed-methods research approach will be applied to provide a comprehensive understanding of Finnish-Russian economic cooperation over the years. To address the research question, a combination of qualitative and quantitative sources will be employed to gather relevant information and statistics.

A systematic review of existing literature forms the foundation of the qualitative analysis. The review focuses on investigating a wide range of sources, including academic journals and historical papers. This approach helps to explore the historical context of the Finnish-Russian economic relations as well as their relationship nowadays. This method captures a broad scope of perspectives on the topic offering a more nuanced understanding of the cooperation between countries. Here, a thematic analysis will be used to identify key themes and insights throughout all relevant literature.

Quantitative analysis includes looking into economic indicators such as gross domestic product (GDP) and inflation rates over the years. These statistics can reveal how the markets have reacted to the geopolitical tensions. Moreover, by analysing statistical data, the research identifies shifts in trade flows, particularly in sectors heavily reliant on Russian exports. Here, comparative and statistical analyses will be used to assess the effects of recent events on the economy. Related patterns and trends will be identified.

The combined research approach ensures a more comprehensive analysis of the economic situation between the countries. It also helps to analyse possible future opportunities for trade, once current difficulties have been resolved.

3 Literature Review

3.1 Cross-Border Economic Cooperation

Cross-border economic cooperation is a part of a much broader process of cross-border cooperation, which refers to a partnership between neighbouring countries. The objective of cross-border cooperation is to promote development in border regions and solve shared problems together (European Commission, n.d.). Cross-border cooperation contributes to the integration between the countries, facilitating exchanges in various sectors.

Cross-border cooperation with a country's neighbours can be influenced by a variety of factors, both external and internal. These include, for example, global geopolitical tensions and countries' responses to them, including sanctions, policies and regulations. The membership of countries in organisations like the EU and NATO can also determine the cooperation. The level to which the neighbouring countries are developed and their willingness for open collaboration further contribute to the establishment of partnerships (Strykiewicz and Tölle, 2009: 19).

Cross-border economic cooperation drives economic growth by providing opportunities for neighbouring countries to access new markets. It also contributes to resource and expertise sharing as well as reduced costs (Nwobi, 2024: 2). Furthermore, it encourages tourism and cultural exchanges between the nations.

3.1.1 Impact of Geopolitics on Cross-Border Cooperation

Although cross-border cooperation provides various opportunities for economic growth, it also comes with certain risks that must be taken into account when establishing cooperation strategies. These risks can negatively affect the cooperation as well as totally disrupt it. Geopolitical events, such as wars, terrorist acts, and foreign policies, are the main threats in terms of the development of cross-border cooperation.

Geopolitics is a critical factor that influences a country's cooperation strategy with other countries, but it is especially important for neighbouring nations. Tensions and unpredictable events can lead to urgent changes in such strategies, in terms of policy frameworks and market access. As such, after the beginning of Russian military operations in Ukraine in 2022, the European Commission has suspended all cross-border cooperation initiatives between the EU and Russia (European Commission, 2022).

One of the main tools related to geopolitics, which can limit the countries' interactions is sanctions. In terms of sanctions, there are always two parties: the sender country, which imposes the sanctions, and the target country, on which the sanctions are imposed (Hufbauer et al., 2009: 43-44).

Sanctions are political and economic measures meant to restrict trade, investment and financial transactions with a targeted country. They are usually used as an influence tool on another country's behaviour and decision-making. Sanctions are primarily imposed with the intention of pressuring the targeted country to change its policies regarding specific concerns. They can be in the form of embargoes on certain goods from the targeted country or limitations on specific industries overall. They can also target individuals, who are associated with the wrongdoings of a country, by freezing assets or introducing travel bans (Kaempfer and Lowenberg, 2007: 869). Imposing sanctions on a country in response to geopolitical tensions can either restrict to some extent or fully disrupt any cooperation between the sender and target countries.

Even though sanctions are meant to hurt the target country, they often have a negative impact on the sender country as well. By imposing sanctions on countries with which the senders previously had trade, the need for alternative supplies with possible higher prices arises (Giumelli, 2017: 1064).

For target countries, the economic costs of sanctions are intended to act as a stimulus for behavioural change. Therefore, when the target country does not

experience any economic losses after the sanctions regime has been introduced, it is unlikely to adjust its policies in response to the measures. As for the countries applying sanctions, the costs of sanctions arise due to disrupted trade flows and increased uncertainty and cost of doing business, particularly abroad (Hufbauer et al., 2009: 101, 108).

Thus, geopolitics must be accounted for when establishing partnerships between countries. Not only can unexpected tensions result in decreased cooperation, but they also might lead to new costs for countries involved. Cross-border cooperation is sensitive to shifts in the geopolitical landscape, so even though it offers great potential for mutual benefit, it needs careful risk assessment in advance.

3.2 Historical Context

Before starting the analysis of the relationship, it is important to understand its historical development by dividing it into four time periods. The first period covers the relationship between Finland and the Soviet Union, from 1950 to 1991. The second time period, following the collapse of the Soviet Union in 1991, indicates the relatively fast recovery of the economic relationship between Finland and Russia until the 2014 sanctions came into force. The third period examines the first wave of sanctions imposed on Russia in 2014 until the escalation of the conflict in Ukraine in 2022. Finally, the last and still current time period marks the escalated conflict between Russia and the EU starting in 2022 and continuing until now.

The background of the Finnish-Russian economic relationship showcases the strong ties the countries had before the events of 2022. It also provides information on how Finland's economy reacted to geopolitical shifts or other obstacles in the past and how the country dealt with challenges.

It is important to mention that the final time period, which covers the events after 2022, will be examined in the sections following the Literature Review as the findings from this time period directly relate to the research question.

3.2.1 First Time Period, 1950-1991

The first time period examined covers the relationship between the countries after the end of the Second World War and until the collapse of the Soviet Union in 1991. This time period is important to investigate as already at that time, the USSR established itself as an important economic partner for Finland. In 1952, Finland paid its last war reparations to the Soviet Union, which consisted mostly of manufactured goods, ships, and natural resources (Erickson, 2024: 9, 13).

The payments, however, did not end; rather, they transitioned into a system of mutual economic cooperation. Just two years before the last reparations were paid, Finland and the Soviet Union concluded the first five-year bilateral trade agreement. This agreement marked the start of a 40-year period of trade between the two countries.

A key feature of the trade between Finland and the Soviet Union was the bilateral clearing trade system. It can be described as a system where both countries exchanged goods without using hard currency. Instead of direct financial transactions, the value of imports and exports was recorded in a clearing account, ensuring that trade remained balanced (Matala, 2020: 88; Laurila, 1995: 19-20).

Under this agreement, Finland exported industrial products such as machinery, ships, and forest products in exchange for mineral products such as gas and oil. The trade agreements between Finland and the USSR ensured a stable supply of materials as their volumes were predetermined in five-year agreements (Ollus and Simola, 2006: 17-18).

While the bilateral clearing trade system provided Finland with stability, it was also highly dependent on market fluctuations and especially on constantly volatile oil prices. This vulnerability can be clearly seen during the 1970-1980s period.

In 1971, with the United States abandoning the gold standard, the USD became a floating currency. Since the oil was priced in USD, and exclusively so following the US-Saudi agreement of 1974, the exchange rate fluctuations affected oil price volatility. The weaker dollar reduced producers' oil revenues, so the prices for oil increased significantly in dollar terms. Finland's oil bill from the USSR tripled and then rose another 2,5 times in the years 1974 and 1978-1980, respectively, while the volumes remained the same. This increase in oil prices contributed to the clearing imbalance, and Finland had to increase its exports to meet the volume of imports (Laurila, 1995: 36; Matala, 2020: 98).

The second oil crisis in 1979-1980, related to the Iranian revolution, resulted in the growing imbalance of trade between the countries. The oil prices doubled, significantly increasing Finland's import costs from the Soviet Union. The industrial production and exports had to be increased once more to compensate for the rising oil bill.

By the early 1980s the Soviet Union accounted for a quarter of Finnish trade. At the same time, the trade deficit began increasing from the USSR side. After the oil prices peaked in the spring of 1980, they started to gradually decline. Since the oil import costs were falling but the exports to the USSR kept growing, the imbalance started to become more and more evident (Oblath and Pete, 1985: 167, 173).

The value of the USD declined again in 1985, further reducing the oil prices, assisted by Saudi-led OPEC production increases. The Soviet Union's debt grew more as the country found it difficult to maintain parity with the volume of Finnish exports. The oil prices crashed even further in 1986, which made Finland cut exports. The trade decline affected the industrial sectors in Finland and resulted in slower economic growth.

As the Soviet economy weakened, Finnish exports started to drop slowly. Despite that, Finland still had trust in the persistence of Finnish-Soviet trade

because the eighth agreement for the next five years of trade was signed in 1989. However, already in December 1990 the Soviet Union terminated the trade agreement for the next five years (Matala, 2020: 101-104).

The 40 years of bilateral trade between Finland and the Soviet Union allowed the countries to benefit from each other. The USSR managed to obtain products that other Western countries did not provide. Finland gained access to a rather stable supply of mineral resources, while also developing its own industries. Even though Finland was profiting from the bilateral trade with the Soviet Union, the effects were somewhat negative in the long term. It created an extreme dependency on the USSR as an economic partner. The collapse of the Soviet Union in 1991 led to Finland losing its major trade partner overnight, triggering a deep recession. Although not the sole reason but certainly a major contributor, the collapse of the USSR influenced the Finnish economic crisis (Sutela, 2001: 13).

3.2.2 Second Time Period, 1991-2014

The second period covers the economic relationship between the countries after the collapse of the USSR and until the first wave of sanctions imposed on Russia, following the integration of the Crimean Peninsula into Russian Federation, which was not recognised by Western countries. This period showcases that, despite an economic crisis related to the loss of Finland's main trade partner, the relationship recovered quite fast and continued to prosper. As mentioned previously, at the beginning of the 1990s, Finland suffered a deep recession, partly due to the loss of the USSR as a trade partner. Another reason for the crisis was the overheating of the economy in the 1980s. Financial deregulation led to excessive lending from banks, which flooded the country's economy with more money resulting in inflation that reached 7%. The devaluation of the markka, Finnish currency at that time, further affected the economic situation since the loans taken in foreign currencies were now harder to pay off. As a result of the recession, the country's GDP declined by almost 15% from 1990 to 1993, and the unemployment rate rose from 3% to 20% (Honkapohj and Koskela, 1999: 401-406; Gulan et al., 2019: 4-7).

For a newly established post-Soviet Russia, these times also brought instability and hyperinflation with the transition to the market economy and the large amount of debt inherited from the former Soviet Union. At the time of the USSR collapse in 1991, its foreign debt amounted to 78,7 billion dollars. Following the collapse, the agreement among the former republics led to Russia taking responsibility for 61% of the debt. However, already in 1994, Russia accepted full responsibility for the entire foreign debt due to many other republics being unable to meet their designated share. The full amount of debt, however, increased by one-third in the four years following the USSR collapse due to accumulating interest and delayed payments. Its total amount by 1995 was around 100 billion dollars (Tikhomirov, 2001: 265-270). Finland's share of the total debt arising from the previous bilateral trade agreements accounted for around \$600 million. Nevertheless, the debt was fully repaid ahead of schedule by 2006 since Russia's financial situation improved due to the increase in profits from oil (Ollus and Simola, 2006: 20-21). However, in the early 1990s, Russia struggled with the economic chaos caused by the abolition of the command economy. The country lacked the institutional foundations needed for the market economy and was not capable of maintaining stability.

After the first effects of the economic crises in both countries dissipated and their economies stabilised, Finland and Russia began to reestablish their economic cooperation under the new conditions. A transition from the command economy in the USSR to the market economy in Russia led to the disappearance of the previous clearing system. Trade was now conducted using hard currency.

At the same time, Finland was shifting its focus towards trade with other Western countries. In 1995 Finland joined the European Union. For Russia this meant that Finland now had to follow the trade regulations established by the EU. The previously lower tariffs would be raised to EU levels. Moreover, Finland was increasing the share of EU countries in its trade turnover to the detriment of Russia (Drobot and Ilyina, 2017: 1448). The membership in the EU was seen

not only as a tool for economic growth but also as an additional security against threats, including those from Russia. This aspect of Finland's security agenda especially increased after 2014 and will be discussed in the following sections.

During the 1990s Russia accounted for around 6% of Finnish trade until the Russian financial crisis of 1998 that happened partly because of another global oil price decline and partly because of the debt default. The Asian financial crisis beginning in 1997 triggered recessions in many major economies and sharply reduced demand for oil, while its supply kept growing. This resulted in the oil prices falling as low as \$10,82 per barrel (Macrotrends, n.d.). As an economy heavily reliant on oil exports, Russia experienced decrease in revenues in addition to debt obligations that the country struggled to meet. The devaluation of the ruble further contributed to the growing financial chaos in the country. The crisis disrupted the trade for some time that it took Russia to recover from the aftermath. The oil prices recovered somewhat already in 1999 and continued to grow with only some occasional and not so critical declines. Even though the initial consequences of the ruble's devaluations were quite negative, it helped stimulate the economy by making Russia's exports cheaper and more competitive.

The early 2000s saw a strong recovery in trade relations between Russia and Finland. As in the previous Soviet-era trade relationship, Finland mostly imported mineral products, with oil being the most essential one. The exports still consisted of machinery, wood, and paper. Moreover, another export group consisted of electrical equipment, a share of which was 20% in 2000 and increased to 36% in the next 5 years. Out of the electrical equipment, the most essential products were mobile phones as in 2005 Russia positioned itself as the largest export market for these (Ollus and Simola, 2006: 25-29).

It is important to mention the significance of re-exports to Russia since their volume was growing fast in the early 2000s. After the collapse of the USSR, the demand for foreign goods in Russia increased, and Finland provided an efficient transport route. Since the volume of re-exports was included in the statistics of

overall volume of exports, it becomes more difficult to analyse the scale of Finland's actual trade with Russia. The main products meant for re-exporting were passenger cars, pharmaceuticals, and electronics. The problem of analysing the exports' scale becomes particularly evident in the electronics sector, specifically mobile phone exports, which were at the time still produced in significant quantities in Finland as well. This problem resulted in a difference in the countries' trade statistics: whereas Finland counted re-exports as Finnish exports, Russian import statistics treated such goods based on the country of their origin. It is stated that about a quarter of Finland's exports to Russia consisted of re-exports in the mid-2000s. Moreover, their annual growth rate was increasing at much higher speed than that of the actual exports from Finland, with 64% compared to 16% on average over the first half of the 2000s respectively. As for the benefits of re-exports to the Finnish economy, the profits were accrued by intermediary trade companies and warehousing services (Lainela et al., 2007: 29-30; Ollus and Simola, 2006: 34-38).

During the 2000s, with the increasing global demand for oil and gas, the countries' interdependence kept growing. Russia ranked among the top trade partners with Finland alongside Germany and Sweden. The year 2008 saw Russia at the first place of Finland's trade partners with turnover of 22,4 billion dollars. This was due to the high global oil prices that were reaching more than 200 USD dollars per barrel in June of 2008 (Macrotrends, n.d.). Trade volumes between Finland and Russia sharply dropped in 2009 following the global financial crisis. Both exports and imports were reported to have fallen by about 40%. After recovering from the crisis, trade resumed and increased, but it failed to reach the same levels as pre-2008 (Volkov, 2021: 177).

In Soviet times, the border between countries was generally closed (Stepanova, 2014: 110-111). Thus, another big sector in the Finnish-Russian relationship during the years following the USSR collapse was tourism, which started to increase already in the 1990s. Russian tourists were the largest group of visitors to Finland, accounting for a third of all travellers. However, compared to most tourists from other countries, a lot of Russians were coming to Finland

only for one day trips due to the countries' proximity. Border towns like Lappeenranta became especially popular among Russian tourists for their shopping opportunities. The number of tourists crossing the border peaked in 2013 at almost 13 million, followed by a drop in the numbers due to the changes in the political climate between Russia and the EU in 2014 (Makkonen et al., 2018: 143).

Finland was also often used as a transit country to another one in the Schengen area. Due to the proximity of the countries, many Russian tourists entered Finland via land routes, primarily by cars, buses or trains. From Finland, they could then continue their journey to other European destinations through the country's well-connected transportation infrastructure. The easier process of obtaining a Schengen visa through Finland instead of other Schengen countries contributed to this trend allowing Russians to use Finland as their initial entry point.

Undoubtedly, Russian tourism generated significant profits for the country due to two factors identified by Ollus and Simola. The first one, as discussed previously, was the high number of Russian travellers, making them the largest tourist group. Secondly, Russian tourists' average daily spending ranked second highest in 2005 at 88 euros per day. This factor can be attributed to the amount of people coming to Finland primarily for shopping opportunities (Ollus and Simola, 2006: 100-101).

Overall, the period of 1991-2014 highlights the resilience of trade between the two countries as it always resumed despite numerous crises. The importance of the Russian market to Finland was evident in 2005 and 2008 when Russia was positioned as Finland's largest trade partner (Ollus and Simola, 2006: 25; WITS, n.d.). Moreover, in times of economic downturn in Russia, Finland started to focus on other markets. Even though by joining the EU, Finland opened new trade opportunities, the country remained highly dependent on Russian energy. Given that, the events of 2014 posed an economic risk to Finland.

3.2.3 Third Time Period, 2014-2022

The third period focuses on how the economic relationship progressed after the first EU-level sanctions were imposed in 2014. It covers the time before the second wave of sanctions in 2022. This period highlights the decline of economic cooperation as a result of geopolitical tensions.

The year 2014 brought new obstacles for the trade between countries in the form of sanctions towards Russia by the EU, including Finland. The sanctions were directed at Russian actions in Ukraine and targeted some economic sectors, as well as specific individuals, involving measures like freezing bank accounts, seizing property, and travel restrictions (Virkkunen, 2020: 102-103; Korhonen et al., 2018: 4). As a response, Russia imposed counter-sanctions, which included bans on imports of food.

New geopolitical tensions changed the landscape for the cooperation between the countries. The overall relationship between Russia and the West worsened in 2014. Russian actions in Ukraine raised concerns in countries of Europe about their security, especially in those countries neighbouring Russia. Finland, previously keeping a position of neutrality, now aligned more closely with the EU. The concern for the country's security kept rising, and the conversation about Finland's national defence became more noteworthy. Several polls showed that the idea of joining NATO was looking more and more appealing to the Finnish citizens. However, no decision on joining the alliance was made at this stage (Järvenpää, 2015: 3).

Total trade turnover between Finland and Russia declined by 40% from 2014 to 2015. The products for trade remained mostly the same as before, with Russia exporting oil (more than 50% of all imports) and other raw materials, and Finland exporting paper, machinery, and electronics (Drobot and Ilyina, 2017: 1450; Drobot, 2017: 821-824). In order to compensate for the losses of trade with Russia, Finland started to expand its share of trade with Germany, Sweden and China. Thus, for example, in 2014, Russia was ranked first among Finnish

import partners with a share of 14,82%, followed by Germany (13,24%) and Sweden (11,25%). In 2015 Russia was moved to the third place with 10,95%, while Germany remained the biggest of Finland's import partners up until 2022 (WITS, n.d.).

The aftermath of Russia's counter-sanctions can be seen, for example, in the decline of the Finnish food exports from 400 million euros in 2013 to approximately 100 million euros in 2015 (Volkov, 2021: 179). The most critical goods from Finland that were sanctioned were meat, fish, milk and other dairy products. At that time, Finnish exports to Russia primarily consisted of dairy products, so the counter-sanctions had a significant impact on certain Finnish companies, such as dairy goods producer Valio, whose products exported to Russia in 2013 had a value of 242 million euros. After the ban on imports of food was introduced, Valio's net sales declined by approximately 20%. The company's profits kept decreasing by around 10% for the next three years until 2016 (Kalyukov, 2016; Lagoyko and Egorova, 2022: 97).

The food embargo also included a ban on meat imports to Russia. With that, the value of meat exported from Finland dropped from 20 million euros in 2013 to 0 in 2018. The Finnish meat company Atria struggled with its operations in the Russian market and experienced a turnover decrease equaling more than 22 million euros in 2014 and around the same in 2015. The financial losses amounted to more than 6 million, which was twice as much as in the previous year. In their annual report, the reason for the losses was stated to be the weakening of the ruble. The number of the company's employees also decreased during the years 2014-2015 with around 600 workers having been laid off (Lagoyko and Egorova, 2022: 98).

For Finnish companies that had business with Russia, the depreciation of the ruble became one of the main problems. Triggered by the sharp drop in oil prices, the ruble's decline significantly reduced the purchasing power of Russian consumers. The cost of imported goods, including those from Finland, increased, lowering the demand.

Sanctions also led to the closure of some subsidiary enterprises in both Finland and Russia. Due to that around 3000 people lost their job places in each country. Among the Finnish companies that started to leave the Russian market after 2014 are Kesko, Stockmann and Ruukki (Krokhin, 2023: 53).

Figure 1 showcases the volume of exports and imports between Finland and Russia in the years 2013-2022. Based on the graph, bilateral trade experienced a significant drop in 2014-2015, and although after some time it increased again, it never reached the pre-2014 volumes.

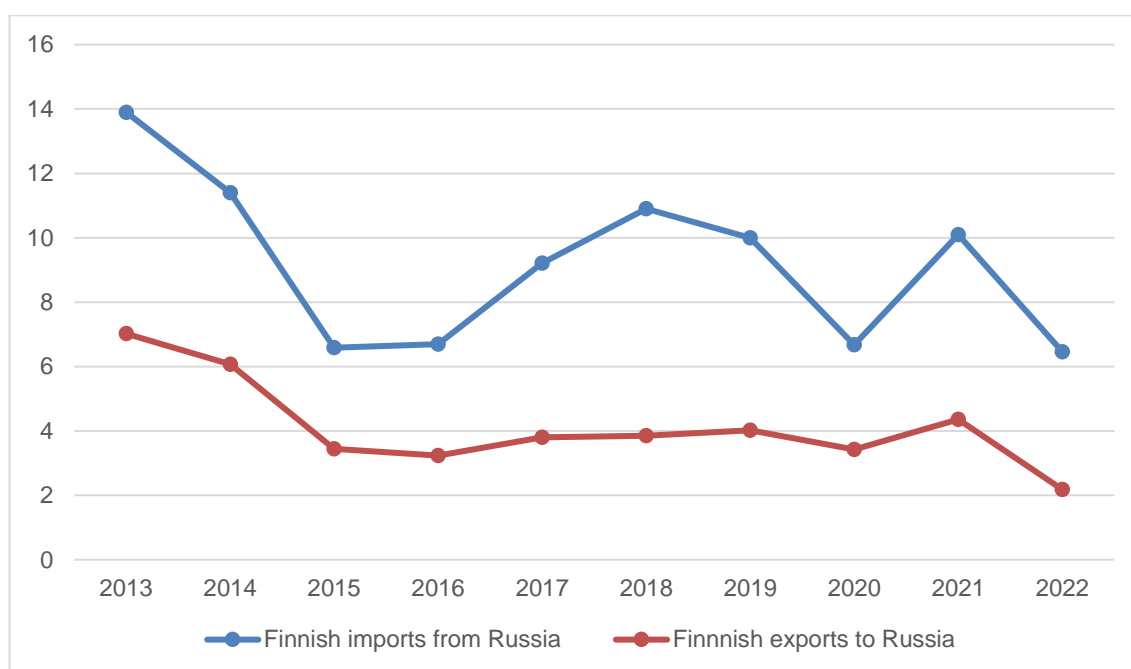


Figure 1. Volume of imports and exports between Finland and Russia, billions USD (Trading Economics, n.d.a; Trading Economics, n.d.b)

The impact of the sanctions and counter-sanctions resulted in halving the volume of trade between the countries. Another reason for the slowdown in the economic relationship and the decline of trade was the overall drop in oil prices in 2014 by almost half. Figure 2 shows the correlation between Russia's exports of oil to Finland and global oil prices.

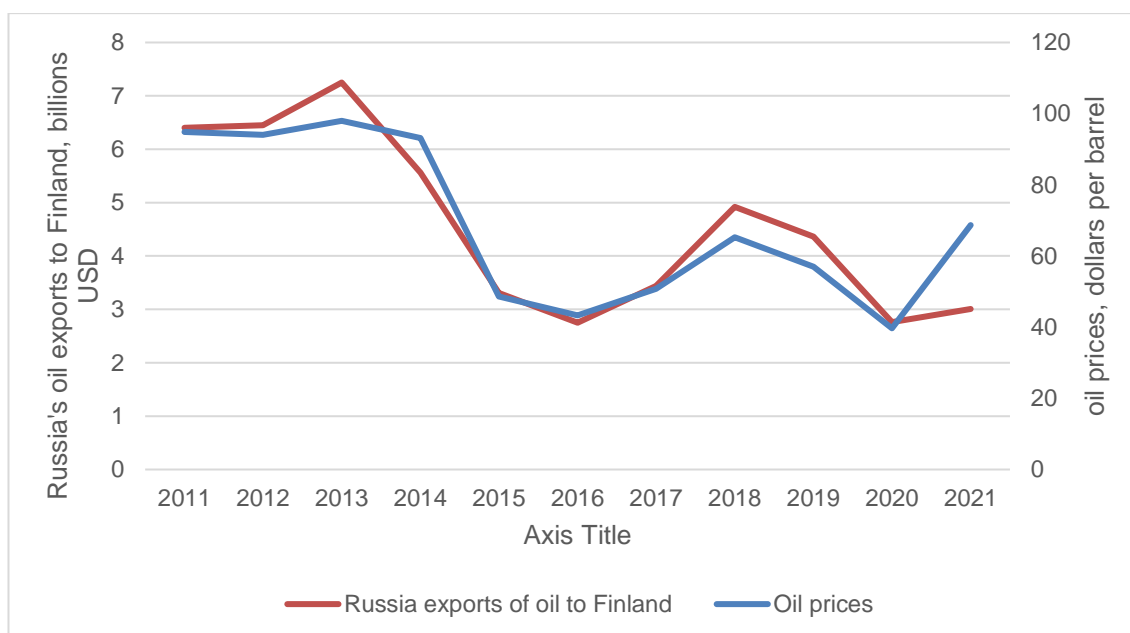


Figure 2. Oil prices in comparison to Russia's oil exports to Finland (Trading Economics, n.d.c; MacroTrends, n.d.)

As shown in Figure 2, after peaking in 2013, oil exports have significantly fallen along with the oil prices. The correlation between them weakened after 2020, presumably because of the impact of the COVID-19 pandemic. Although the oil prices grew higher, the trade of goods and services became restricted due to external economic shock.

Thus, another factor that affected trade in the examined period was the global pandemic COVID-19 and the related restrictions on trade and disruptions to supply chains. As shown in Figure 1, another sharp drop in trade, especially concerning imports from Russia, occurred after 2019.

The pandemic had a negative impact on the global economy, being the first major health crisis in recent history. It revealed vulnerabilities in global supply chains, largely due to an overreliance on certain suppliers and insufficient diversification (Hilmola et al., 2020: 4). Finland was not an exception, and the pandemic severely affected many economic sectors, particularly those reliant on international trade and tourism. The economy slowed down with the GDP decreasing by 2,5% in 2020, reflecting the combined impact of lockdown

measures. Consumer confidence indicator (CCI) fell to as low as -13,9 in April 2020, indicating a sharp decline in public optimism regarding the economy and personal finances (Statistics Finland, n.d.a). The uncertainty contributed to decreases in consumer spending and overall economic activity. The unemployment rate rose to 7,8% in 2020, increasing by 1,1%, and returned to the pre-pandemic level in 2022 (IMF, n.d.a).

The trade between Finland and Russia was largely affected as well. The overall trade turnover fell by almost 27% from 2019 to 2020. Russian exports to Finland fell by 3 billion euros, while Finnish imports to Russia fell by half a billion. More than half of all Russian exports to Finland continued to consist of mineral products (58%). The biggest share of Finnish imports was machinery at around 30% (Ru-Stat, n.d.).

The tourism industry continued to play an important role in the countries' cooperation but it was also experiencing some difficulties during this period. In 2014 the number of Russian visitors fell by approximately 20% (Volkov, 2016: 179). The outflow of Russian tourists arriving in Finland for shopping significantly decreased due to the sharp weakening of the ruble. The previously popular shopping opportunities in Finland became less appealing to Russians. This affected the companies that were reliant on Russian tourists, particularly in the Eastern part of the country.

The luxury fashion department store that had opened in 2013 in Lappeenranta, Grande Orchidée, had to close its operations already in 2015 due to the decreased demand. Supermarkets in the area were also primarily targeting Russian tourists, so their profits more than halved during the mid-2010s (Schönberg, 2015).

The pandemic further affected the decline of tourism with restrictions on travel and the closure of borders. Since 2007, Russia has consistently ranked as the top country in terms of the number of arrivals to Finland, with an exception for 2016, when it was briefly moved to second place. This trend continued until

2021 when the number of Russian visitors suddenly decreased by 7 times compared to 2020 (Statistics Finland, n.d.b). The drop can be explained by the COVID-19 restrictions and the fact that the EU, and thus Finland, did not recognise the Russian Sputnik vaccine. Therefore, Russian travellers generally did not meet entry requirements even when borders reopened.

After the pandemic, tourism's contribution to Finland's GDP dropped from 2,7% to 1,4%. As the economy gradually recovered from the effects of the lockdown, the sector began to improve, reaching 1,8% of GDP in 2022 (Ministry of Economic Affairs and Employment of Finland, n.d.).

Finland's international tourism receipts during this time can be seen in Figure 3. The first decline of approximately one billion happened after 2014 but returned to the previous level already in 2017. Tourism receipts continued to grow and reached a peak in 2019. The pandemic resulted in a severe drop in international receipts, bringing their value down by over 4 billion USD.

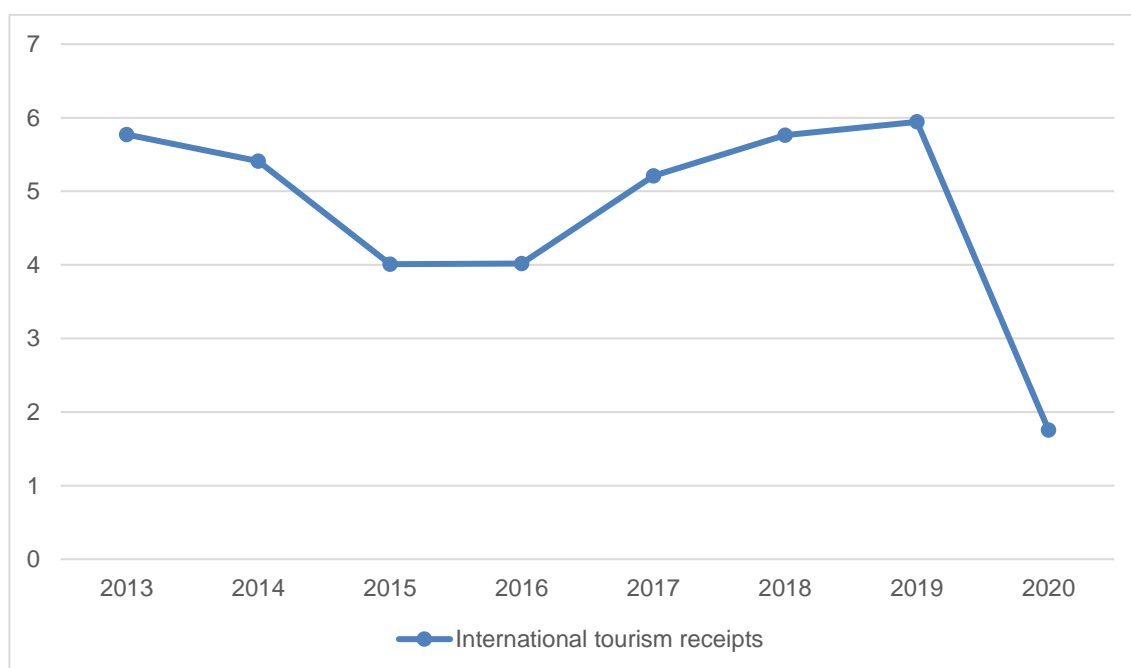


Figure 3. International tourism receipts in Finland for 2013-2020, billions USD (The World Bank, n.d.a)

Moreover, the pandemic affected Finnish businesses in several ways. More money had to be allocated to solving supply problems. New expenses related to the health of employees appeared. Overall purchasing power declined and with this, the product selection preferences changed.

Another important sector in the Finnish-Russian relationship is energy, which has also undergone certain changes during this period. Finland imports most of its primary energy (65%), and Russia accounted for the biggest share (63% for 2016) due to the cheaper price and geographical proximity. Among all energy imports from Russia, oil and natural gas were the main ones. Generally, all the natural gas has been imported to Finland only from Russia, making it the most vulnerable product and contributing to the dependence on Russia (Jääskeläinen et al., 2018: 11; Lyyra et al., 2018: 3). However, since the early 2010s the Finnish consumption of natural gas has been steadily decreasing until 2018 (Statistics Finland, n.d.c). The situation changed even further in 2020 when the opening of the Balticconnector pipeline connected Finland to Estonia and other European gas networks. Thus, the reliance on Russian natural gas was significantly reduced.

The main suppliers of electricity in Finland have historically been Russia and Sweden. Russia's share was the largest until 2012, but even after that, Russia remained a key supplier along with Sweden until 2022. However, the overall share of net imports of electricity has started to decline since 2019, while domestic production increased. The production has also become clearer, indicated by a growing share of renewable sources (Statistics Finland, n.d.d). The shift has been supported by the country's growing focus on renewables in their energy overall. Thus, their share in Finland's total energy consumption kept growing, reaching more than 40% in 2021, which was almost a 10 percentage point increase from 2014 (Statistics Finland, n.d.c).

There was no direct influence on the energy trade between countries after the first wave of sanctions; on the contrary, Russia accounted for the biggest share in primary energy imports. However, during this period, Finland started to

reduce its dependence on Russian energy by diversifying suppliers and investing more in renewables. Nevertheless, some degree of dependence remained.

As can be seen from this section, the events of 2014 have had a negative impact on the Finnish-Russian economic relationship, particularly in terms of trade and tourism. The new geopolitical environment became a challenge for some Finnish businesses, especially the ones specialising in meat and dairy products, which became sanctioned. However, Volkov (2021: 186) identified that EU sanctions and Russia's countermeasures played a less significant role in the changes in economic relations between Russia and Finland. The major factors were the decline in the ruble exchange rate and the change in oil prices. Overall, the effects of the sanctions were not as critical as in the period discussed later.

3.3 Deglobalisation

Before starting the analysis of Finland's current economic situation, it is important to understand the overall global context. Although global economic cooperation brings several benefits, it also comes with certain risks – geopolitical uncertainties, economic fluctuations, cultural diversities, and changing regulatory environments. These risks can become difficult to navigate due to their unpredictability. They can lead to increased costs, trade barriers, and disruptions in supply chains. All of this can make global cooperation less appealing, leading countries to seek more localised strategies. Nations begin reshoring or near-shoring production and seek to reduce exposure to global powers by exploring alternative arrangements.

Over the past decade, the global economic landscape has been transforming due to a series of events. The era of globalisation, marked by interconnectedness and interdependence between countries, has come to an end. Currently, the world is experiencing a shift towards deglobalisation, with countries diversifying their supply chains by “nearshoring” and reducing dependency on foreign markets.

Deglobalisation refers to a shift towards a less interconnected world (Cesluk-Grajewski, 2022). It is characterised by reducing interdependence through the establishment of more localised production networks. Countries start to prioritise domestic industries and regional trade instead of global integration. This shift often arises as a response to economic vulnerabilities or geopolitical tensions.

A key indicator of globalisation was the growing Foreign Direct Investment (FDI) flows (Pekarskiene and Susniene, 2015: 205). Thus, the decline of FDI flows signalled a turn toward deglobalisation. Figure 4 indicates FDI net inflows from 2007-2023, showcasing their downward trend. The highest level appeared in 2007, followed by a major drop due to the financial crisis. Since then, there have been some recoveries in the inflow, but the trend remains mostly negative, with more declines after the years 2016 and 2021. The figures never returned to the peak levels seen in 2007.

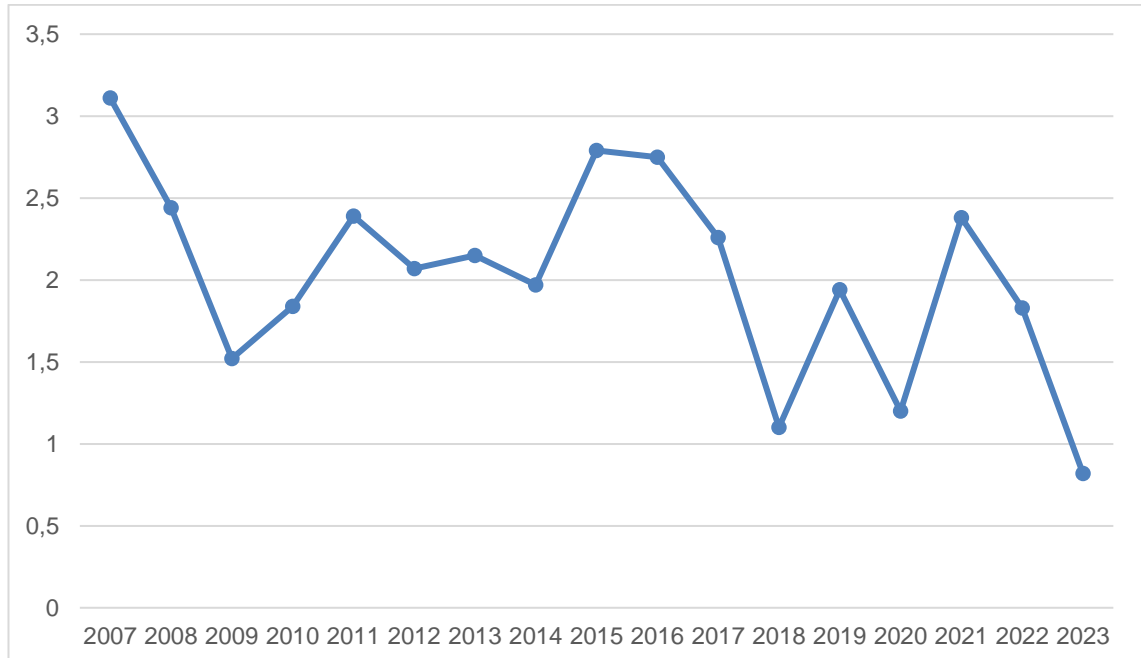


Figure 4. Foreign direct investment, net inflows, trillions USD (The World Bank, n.d.b)

Concerns over the future of globalisation began after the financial crisis of 2008. However, after some time, the markets stabilised, and the situation improved.

Nevertheless, the emerging trend of deglobalisation can be seen in the late 2010s, marked by events such as the Brexit referendum in 2016 and the election of Donald Trump in the same year (Komolov, 2021: 35). These events contributed to and underscored the development of economic nationalism as both the United Kingdom and the United States began prioritising their national interests.

The 2016 Brexit referendum was driven by the desire for sovereignty from the European Union and its regulations. The effects of the decision included increased trade barriers and an overall drop in trade volumes due to the consequently higher costs.

Similarly, Donald Trump's presidential election victory in November 2016 marked a turn towards protectionist economic policies in the world's largest economy. The actions of his presidency signalled a major shift towards rising economic nationalism in the world. His administration prioritised domestic industries and reduced reliance on international trade agreements.

Trump advocating reshoring manufacturing and imposing high tariffs on imports to protect American industries. To achieve this, he started a trade war with China, putting tariffs on a wide range of Chinese goods. He immediately withdrew from the Trans-Pacific Partnership (TPP) and threatened to leave the World Trade Organisation (WTO) while also criticising it and its decisions (Stiglitz, 2018: 516-518).

These examples show the withdrawal from global economic integration in favour of national control of trade. They indicate a decline in global economic cooperation and trade, setting the trend for the deglobalisation shift.

The outbreak of the COVID-19 pandemic even further forced countries to focus on their own stability. It highlighted the risks of relying on global networks and the need for localised solutions. With the pandemic growing rapidly and globally, supply chains were disrupted, especially as COVID-19 originated from

China – a major link in the supply chain with many countries. The closure of borders and the reduction of transport communication between countries significantly limited the movement of goods and services (Komolov, 2021: 42). The Bank of England (2021) reported that global trade dropped by almost 10%, which was the biggest decline since the 2008 financial crisis. The pandemic also hindered tourism and labour migration, further contributing to the deglobalisation trend.

Liedtke (2022: 123-124) considers those events as signals of the move toward deglobalisation, but the Russian military operations in Ukraine in 2022 amplified the trend. This event accelerated the shift as countries struggled with energy crises and disrupted trade networks. The conflict highlighted the increased vulnerability to political events, which made nations reconsider their attitudes towards countries outside their alliances. It affected many countries, particularly those where dependence on Russian raw materials was especially present. Russian actions towards a European country prompted Europe to impose sanctions on Russian companies and seek alternative oil and gas supplies. Moreover, it contributed to a higher rate of inflation as the prices of energy skyrocketed, following reductions of gas and oil supplies from Russia to the West.

The actions of one of the largest military forces in the world also made countries reassess their national security. More funds had to be allocated towards the military sector, especially in countries neighbouring Russia. Finland and Sweden had to reassess their previous position of neutrality by rethinking their military alliances.

3.3.1 Finland in the Context of Deglobalisation

Within the context of deglobalisation, Finland's economic relationship with Russia presents several challenges. For decades, globalisation has been facilitating strong economic ties between Russia and Finland, bringing benefits such as trade efficiency and resource sharing. As neighbouring countries, Finland and Russia contributed to the development of shared infrastructure.

Their proximity also allowed for a massive flow of tourists, which brought huge profits for local businesses.

Despite the benefits brought by globalisation, it also brought a major vulnerability - the interdependence between the countries. As a country with one of the highest energy consumption rates globally, Finland's relationship with Russia has always been hugely characterised by imports of oil and gas (The World Bank, n.d.c). Finland relied heavily on Russian imports of energy and raw materials, while Russia profited from Finland's technology. Over the many years of cooperation, the interdependence based on Russian raw materials grew stronger and stronger. In the context of globalisation, even a decade ago, such interdependency was mostly contributing to the growth of both countries. However, the recent geopolitical tensions and the increasing deglobalisation have disrupted all cooperation. Now the vulnerability can be clearly seen in Finland's supply chain disruptions and increased prices of gas and energy. With sanctions now imposed on Russia, gas and oil must be supplied from elsewhere, creating an urgent need for diversification. Moreover, many Finnish companies were either present in the Russian market or were cooperating with the country on the basis of supply chains so the sudden need to exit the market presented financial losses and greater uncertainty for the future.

4 Impact of the Geopolitical Events of 2022 on Finland

February 2022 saw the immediate escalation of geopolitical tensions with the beginning of Russian military operations in Ukraine. The event affected the world as many countries condemned the actions of Russia. For Finland, which borders Russia, this marked a turning point in its economic and security strategies. Western countries and international organisations like the EU imposed a series of sanctions on Russia in response to its actions. Finland, being among those countries, was directly impacted by the sanctions, which disrupted the long-standing trade relations. As discussed previously, Finland and Russia had developed an interdependence in trade, particularly in the energy sector from the Finnish side. Thus, the ending of cooperation resulted in various challenges for the economy that are going to be discussed in the following sections.

4.1 Sanctions

In response to Russia's actions, the EU has imposed a variety of both individual and economic sanctions on Russia. Economic sanctions targeted sectors like finance, energy, and trade. As of now, the EU has introduced 16 packages of sanctions against Russia. As presented in Figure 5, since 22 February 2022, Russia has become the most sanctioned country in the world.

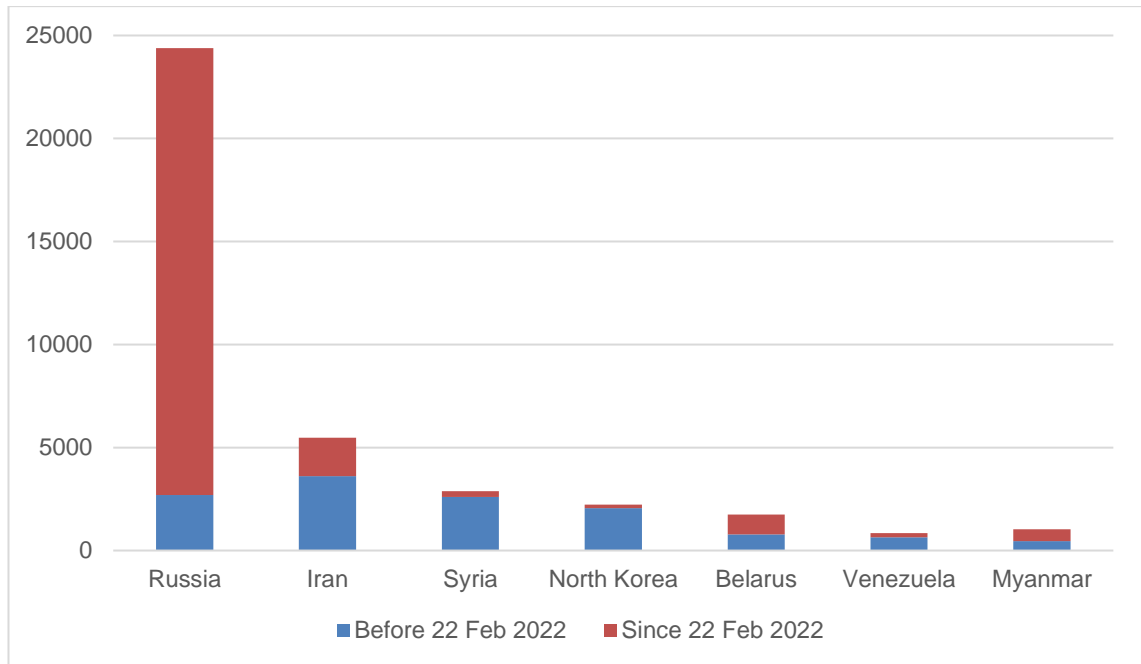


Figure 5. Number of sanctions by target country before and after 22 February 2022 (Castellum.AI, 2025)

The number of sanctions imposed on Russia has increased to nearly eight times the pre-2022 level. Sanctions on individuals and entities included asset freezes and travel restraints. Financial sanctions included a ban on supplying euro-denominated banknotes to Russia as well as disconnection of major Russian banks from the SWIFT payment system. These sanctions significantly limited the ability to conduct international transactions. Export restrictions targeted a wide range of goods, particularly luxury goods, technology and other equipment that would be important to Russia's military sector. The most critical import restrictions on Russia focused on energy products and raw materials. Additionally, the EU imposed bans on the import of other goods, for example, cosmetics and jewellery (European Council, n.d.). In addition, Russia imposed counter-sanctions in response to sanctions from "unfriendly countries", including EU members and, thus, Finland, which, as an EU member, is bound by collective policy in trade. The countermeasures included, for example, trade restrictions and limitations to foreign currency transactions (Haga, 2023).

The imposed sanctions have had negative effects not only on Russia, but also on the sender countries since Russia was an important part of the global

economy and cooperated closely with many countries. Many of the sanctions focused on banning exports and imports of certain goods, making trade more restricted. Thus, for sender countries, these sanctions resulted in increased costs for goods that were previously imported from Russia, such as raw materials and energy. Some supply chains were now disrupted and needed restructuring with alternative options, often at a higher price.

Besides the previously mentioned EU financial sanctions and restrictions on trade, those sanctions included, for example, the prohibition of Russian planes flying over EU territory. In response, Russia closed its airspace to EU aircraft as well, forcing them to take longer and more costly routes. For Finnair, a Finnish airline, this meant replanning its routes from Europe to Asia as Russian airspace could now only be bypassed either to the north or the south. As a result, the longer routes led to increased costs related to fuel, crew and navigation. In addition, the new routes required special permissions and preparations due to new flight conditions (Finnair, 2022a). Finnair's operating expenses increased by 98,1 % in 2022, with fuel costs experiencing the most significant increase of 295%. Overall, Finnair's net result in 2022 was -476,2 million EUR, representing a -2,6% decline compared to 2021, when the net result was -464,3 million EUR (Finnair, 2022b: 12-13).

4.2 Finland's Economic State Overall

Following the pandemic and prior to February 2022, Finland's economy was on the path to recovery. Supply chains began to stabilise, and economic growth had resumed. Therefore, the sudden change in the geopolitical landscape presented a set of new challenges that threatened to undo the economic progress made in the post-pandemic recovery. Most economic indicators fell in 2022 compared to the previous year of stabilisation.

As shown in Figure 6, the GDP of Finland significantly decreased in 2022, following a strong recovery in 2021 after the initial impact of the COVID-19 pandemic. The decrease was likely triggered by the introduction of the sanctions and their effects on various economic sectors. Finland was not fully

prepared for the situation, and the resulting uncertainty for the future further contributed to the economic downturn.

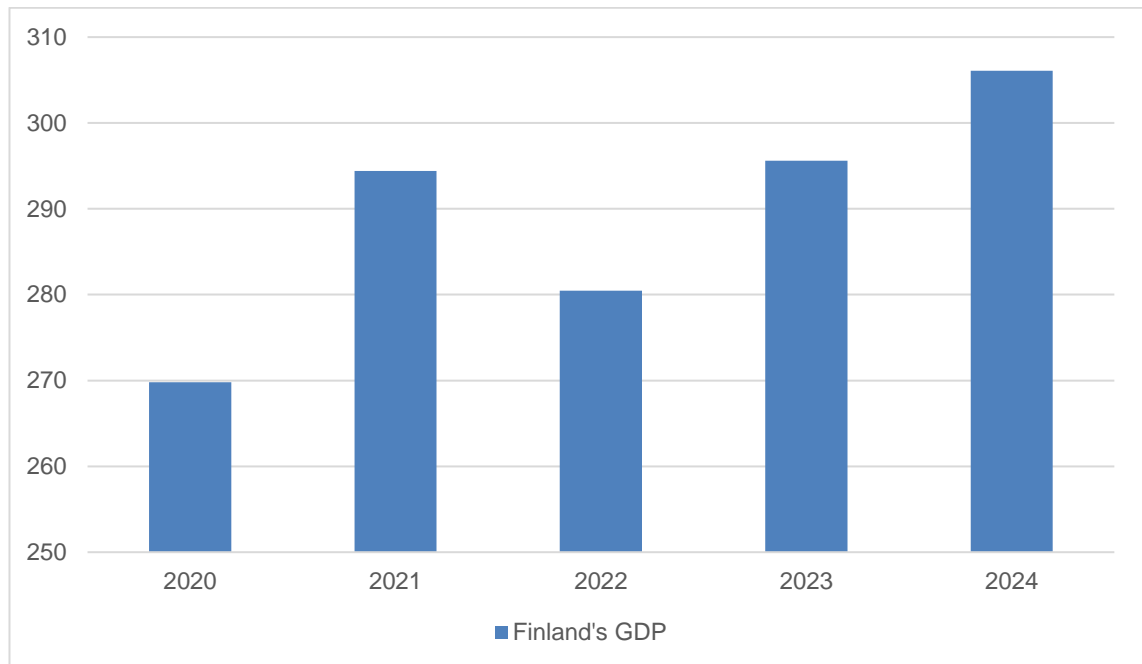


Figure 6. Finland's GDP, billions USD (IMF, n.d.b)

Nevertheless, the post-2022 period marks a steady recovery, as already in 2023, the GDP returned to approximately the same level as in 2021. The economy began to stabilise as Finland adapted to the new economic situation. Furthermore, by 2024, Finland's GDP has reached its highest level and is predicted to keep increasing in the upcoming years – by 0,8% in 2025, 1,8% in 2026 and 1,3% in 2027 (Bank of Finland, 2025).

Despite the growth of the GDP, Finland's national debt relative to GDP indicator has also been growing more since 2022. During the pandemic, the government started to actively borrow funds to support the economy, increasing the national debt. In the following years, the higher public spending further raised government expenditures. Thus, after 2022, the debt kept increasing further and reached 81,4% of the country's GDP by 2024, as seen in Figure 7.

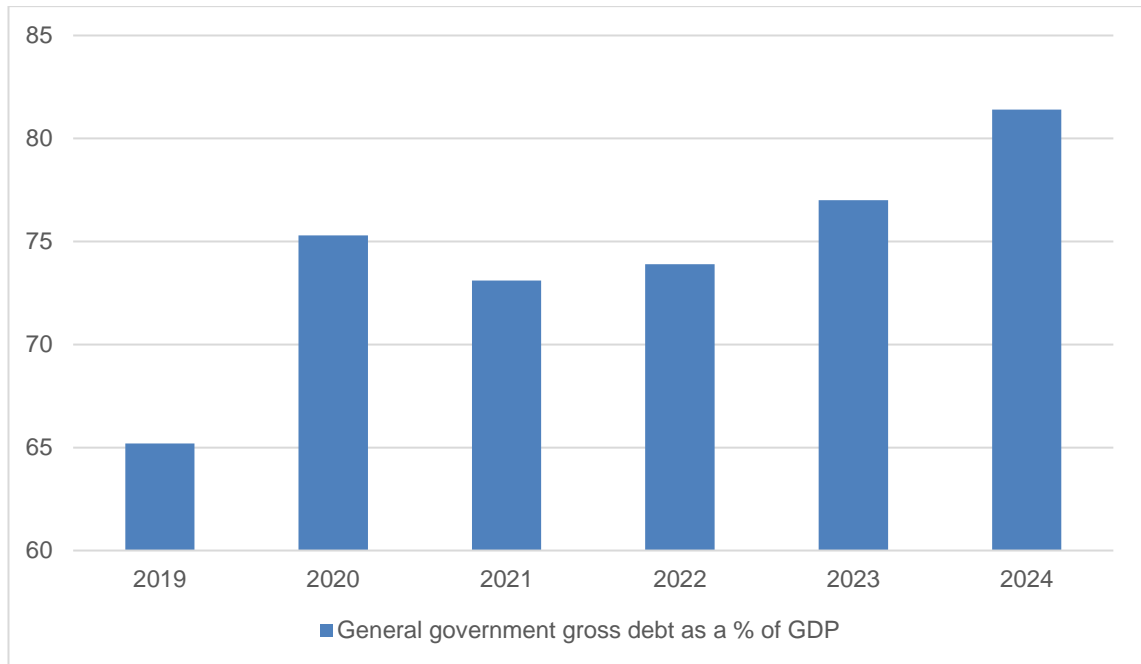


Figure 7. Finland's general government debt relative to GDP (IMF, n.d.c)

Even despite the GDP growth during the past years, it has not been able to offset the higher borrowing. The growth must be further strengthened in order to begin reducing the debt.

Figure 8 showcases Finland's CCI since January 2022 and its development until March 2025. During 2021, the CCI was mostly positive, reflecting post-pandemic improvements in economic stability and confidence in personal finances. This led to better purchasing power among consumers. The country's CCI fell immediately following the events of February 2022, reaching -10,5 in March 2022. This was the weakest it has been since 1995, with the exceptions of 2008 and April 2020 (Official Statistics of Finland, 2022). Since March 2022, it has been mainly decreasing further, hitting the lowest score of -18,5 in December 2022.

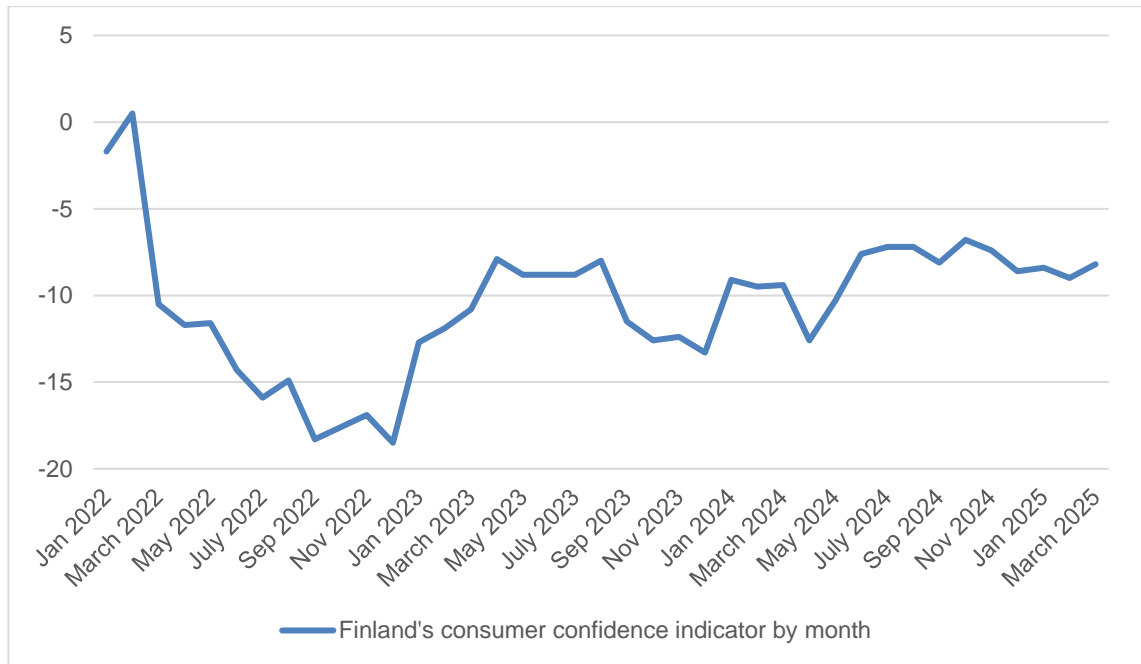


Figure 8. Finland's consumer confidence indicator, 2022-2025 (Statistics Finland, n.d.a)

Although the CCI started to recover slightly after reaching its lowest point, it has remained negative to the present day, indicating ongoing uncertainty among consumers.

In the previous years, the inflation rate in Finland was relatively stable between -0,2% and 2,2%. However, since the start of the conflict, it skyrocketed from 2,07% in 2021 to 7,17% in 2022, which is the highest level in over a decade, as indicated in Figure 9 (IMF, n.d.d). The sharp decline in trade with Russia forced Finland to seek alternative suppliers, which were generally more expensive. The prices for goods and services surged, increasing the inflation rate and reducing purchasing power. Rising energy prices made a particularly big contribution to this. Natural gas saw an especially extreme price surge, reaching around 180 euros per MW in September 2022 compared to only 30 euros in June 2021 (Plyusnin, 2023: 93). In the following year, inflation started to slow down but remained relatively high due to the lingering effects of the previous year's disruptions. Looking at the forecast by the Bank of Finland (2025), inflation is projected to remain moderate and will not exceed 2%. The increase in energy prices is expected to be a one-time event.

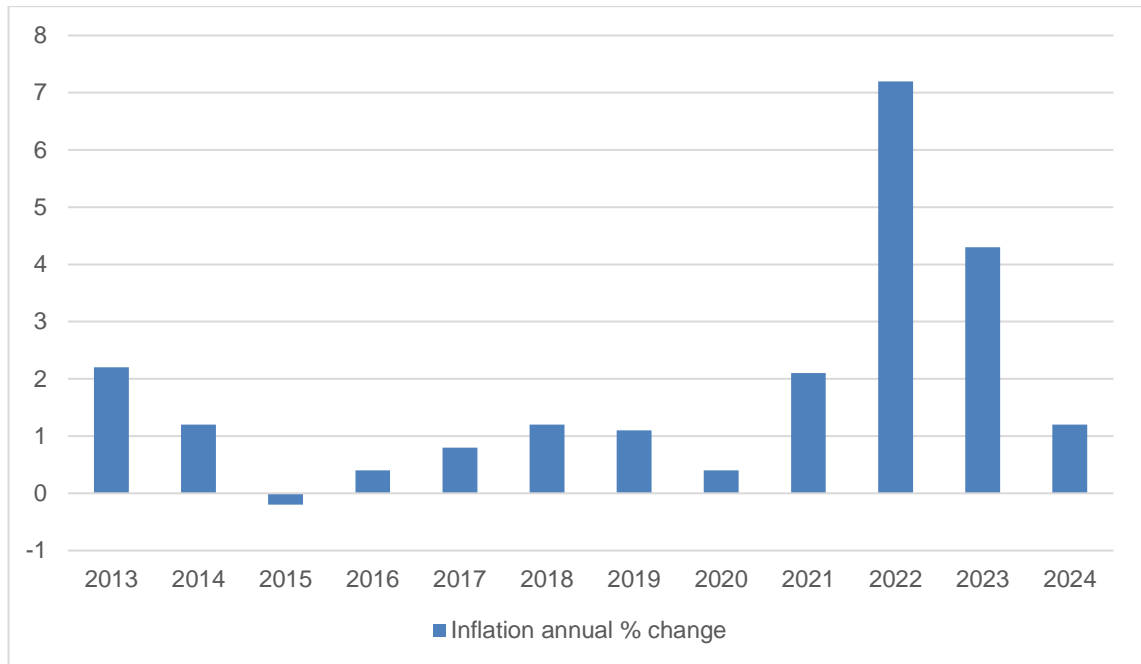


Figure 9. Finland's inflation annual percentage change (IMF, n.d.d)

Figure 10 indicates that the unemployment rate has been increasing since 2022, reaching 8,3% in 2024, which is even larger than during the pandemic time. It is, however, predicted to slow down and decrease in the foreseeable future, but not yet to the same level as in 2022.

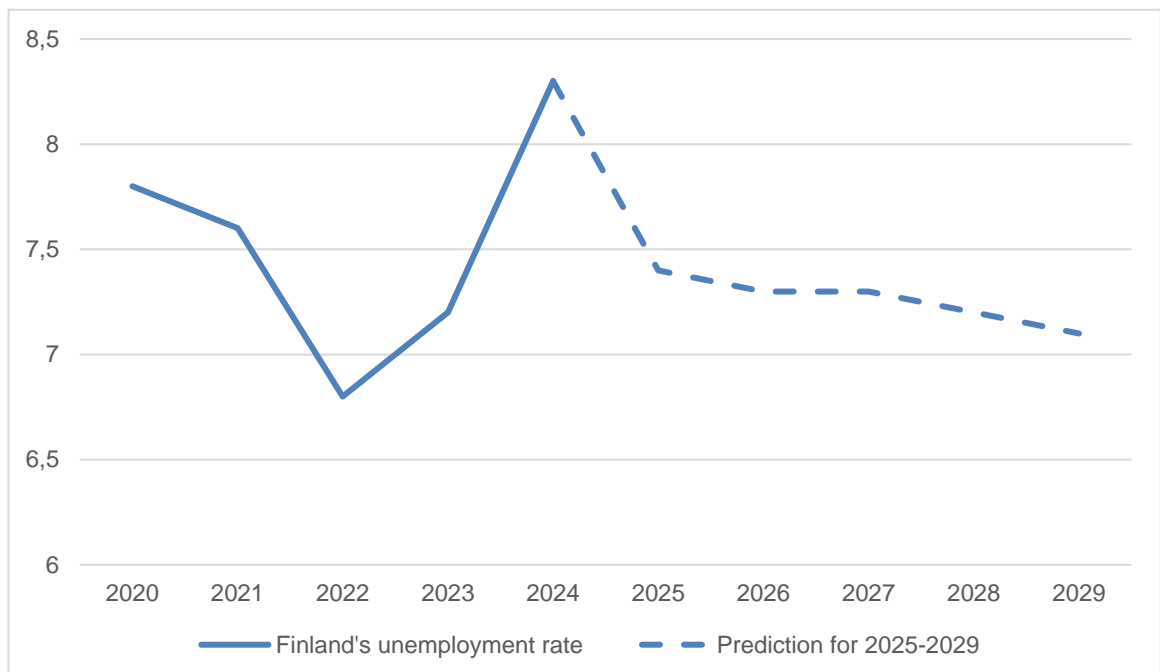


Figure 10. Finland's unemployment rate and its prediction (IMF, n.d.a)

The imposition of sanctions led to a significant decline in trade volumes between Russia and Finland. Previously one of Finland's most important trade partners, Russia's share has decreased to a minimum in the past years. Figure 11 clearly depicts the sharp decrease in trade between the countries at the beginning of 2022. The imports saw an approximately 50% drop from January to May, reflecting the immediate impact of the geopolitical events on trade volumes.

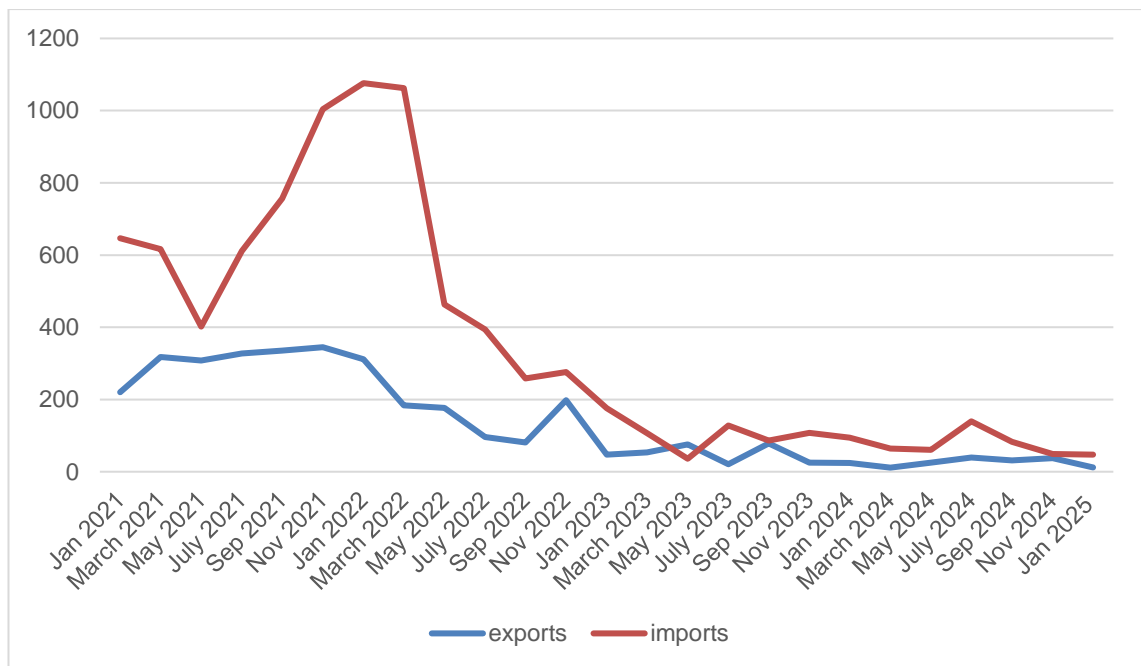


Figure 11. Monthly trade between Russia and Finland 2021-2025, millions of euros (Finnish Customs, n.d.)

Although some trade between Russia and Finland has continued to this day, most of it has stopped completely. Finland's total foreign trade experienced fluctuations in 2022 as well. Figure 12 indicates that both exports and imports exceeded the previous year's values in 2022. When comparing March of 2021 with March of 2022, the value of imports rose by almost 2,5 billion. The value of exports also rose, but did not experience the same sharp increase.

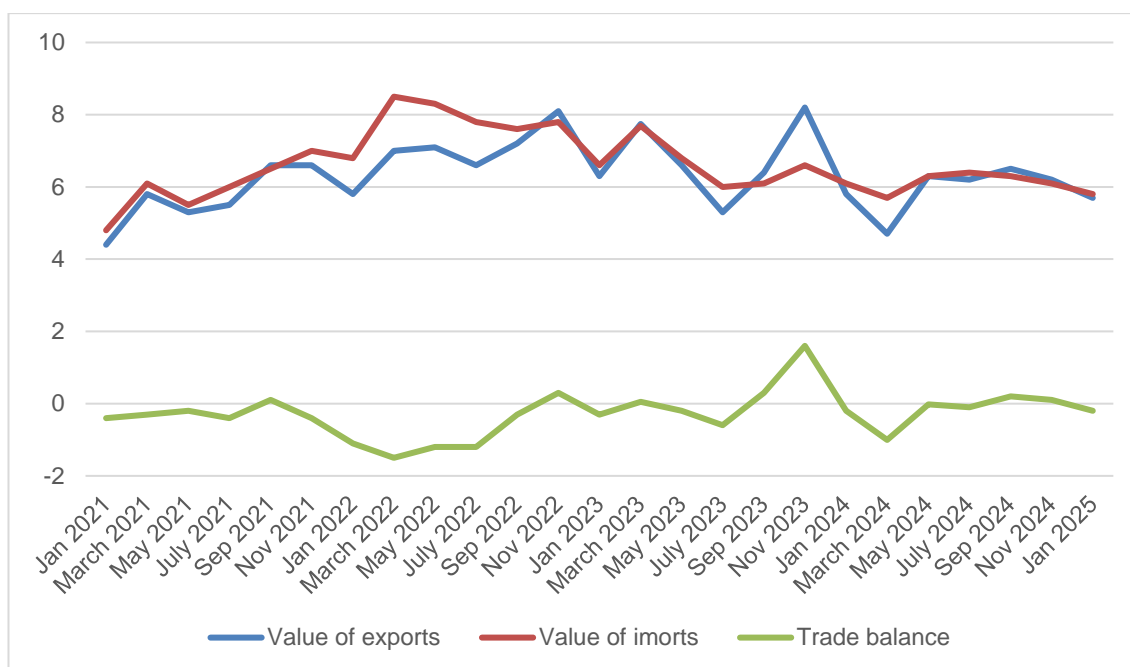


Figure 12. Monthly exports, imports and trade balance 2021-2025, billions of euros (Finnish Customs, n.d.)

Thus, the value of imports was mainly exceeding that of exports in 2022, which resulted in a clear trade deficit. The switch from using Russian energy resources to more expensive suppliers increased the costs of imports, which resulted in a significant worsening of Finland's trade balance in 2022. Figure 13 shows the cumulative trade balance of Finland for the years 2019-2024, clearly indicating the sharp decline in 2022, when the trade deficit reached its lowest point of -10,6 billion euros. Since then, however, the trade balance normalised as the value of imports decreased, with exports sometimes even exceeding the imports.

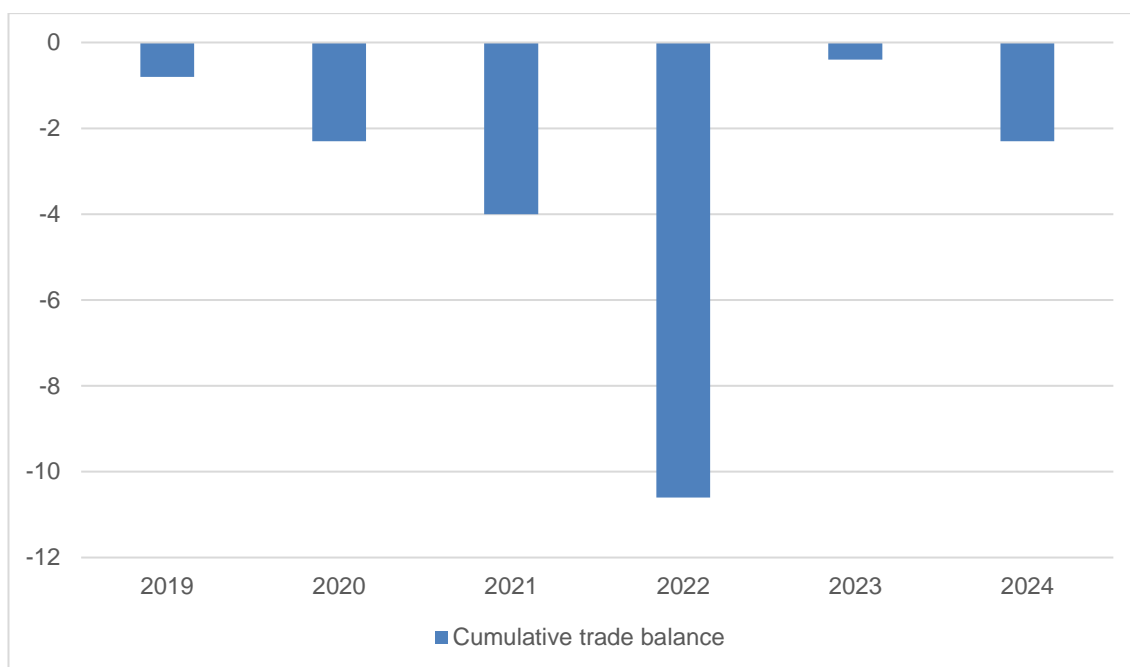


Figure 13. Finland's cumulative trade balance (Finnish Customs, n.d.)

The main sectors of the Finnish economy experienced several obstacles in 2022. Nevertheless, since then, the country showed resilience, with most of the indicators beginning to improve.

4.3 Energy

The energy trade between Russia and Finland has always been one-sided. Since Finland does not have enough resources but has a high energy demand, it has relied heavily on Russian energy imports.

As discussed previously, most imports from Russia consisted of oil and gas, so Finland has developed a dependence on the Russian energy sector over the many years of trade. Therefore, the events of 2022 resulted in a fundamental shift in Finland's energy supplies. The imposition of sanctions, along with Finland's own desire to reduce energy dependence on Russia, led to a diversification of energy sources.

Figure 14 depicts the imports of crude oil from Russia to Finland. The EU's sixth package of sanctions, introduced in June 2022, included a ban on crude oil

imports from Russia as of December 2022 (Eurostat, 2023). However, countries started decreasing the imports even before that, as can be seen from Figure 14, when Finland cut all imports of crude oil from Russia already in August 2022.

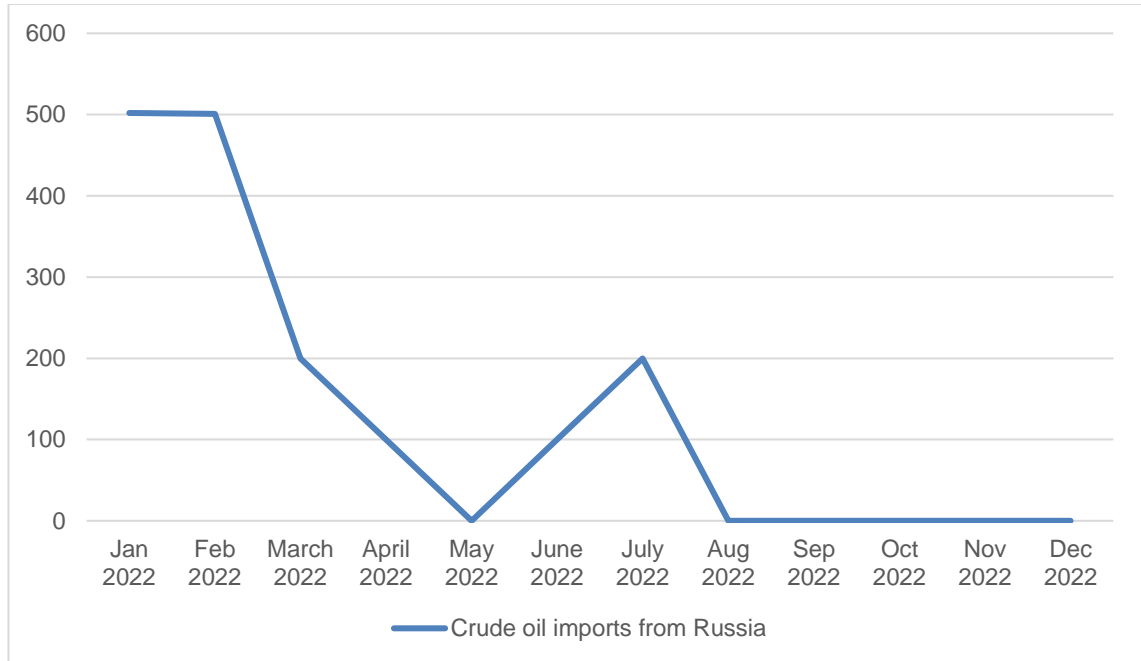


Figure 14. Crude oil imports from Russia in Finland, 2022, thousand tonnes (Eurostat, n.d.a)

Currently, Finland's crude oil imports come primarily from Norway (78,7%), followed by the US (12%) and the UK (7,8%) in 2023 (Tulli, 2024). Figure 15 showcases the gradual decline in oil imports from Russia accompanied by a steady increase in imports from other countries, particularly Norway.

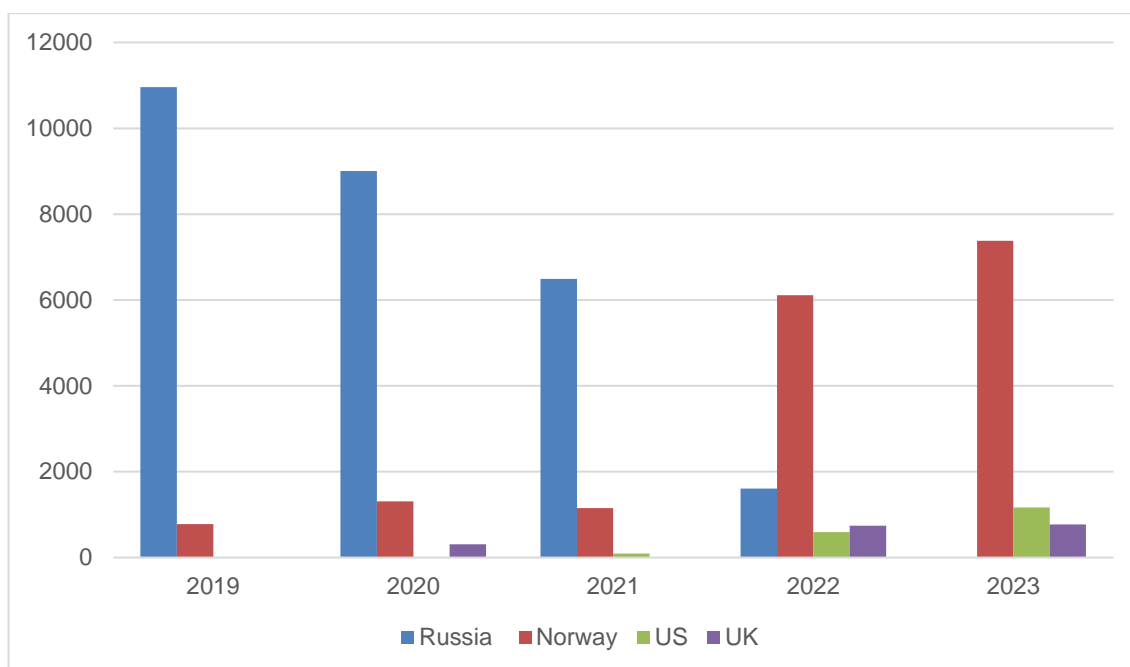


Figure 15. Imports of crude oil to Finland by main partner countries, thousand tonnes (Eurostat, n.d.b)

Figure 16 shows the total import of energy products to Finland, the value of which almost doubled in 2022 compared to the previous year. This sharp increase was driven by the global energy crisis, following the start of the conflict. As mentioned previously, the imports of crude oil from Russia stopped in August 2022. However, the crude oil imports still doubled in 2022 due to the increase in global prices. The higher prices and Finland's continued reliance on it resulted in crude oil imports accounting for more than 50% of all energy product imports in 2023.

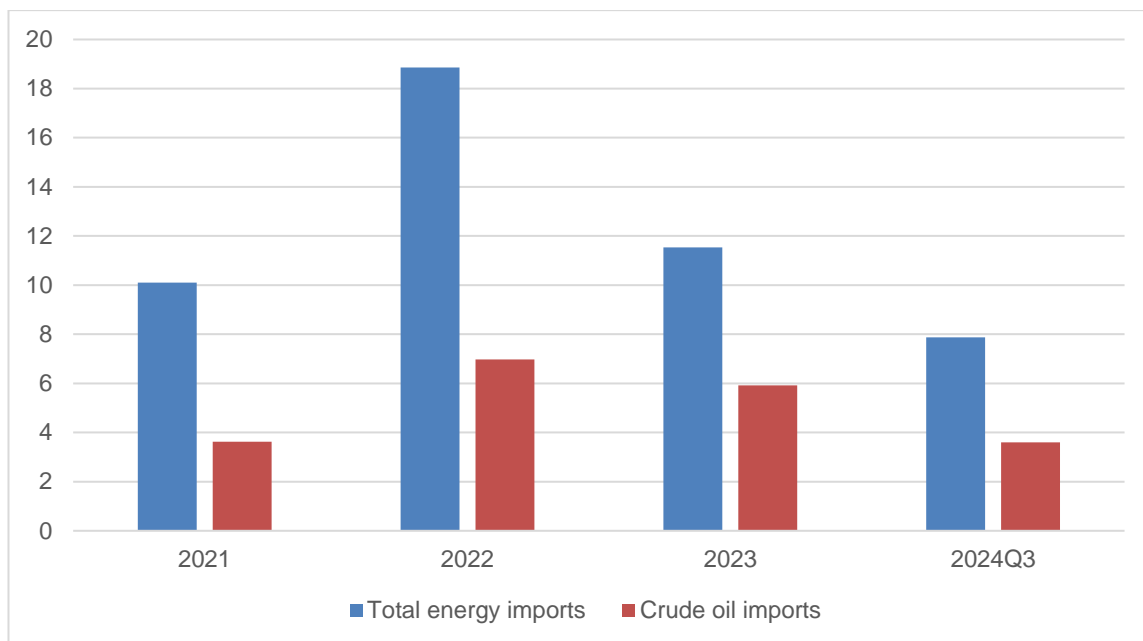


Figure 16. Energy products imports to Finland, 2021-2024Q3, millions of euros
(Statistics Finland, n.d.e)

The quick adaptation to the new situation in the energy market can be seen in Figure 17. Finland started to diversify its energy trade partners to reduce the dependence on Russia already in 2022. From then on, the biggest share of all energy imports came from Norway and Sweden, and already in 2023, the imports from Russia were down to a minimum.

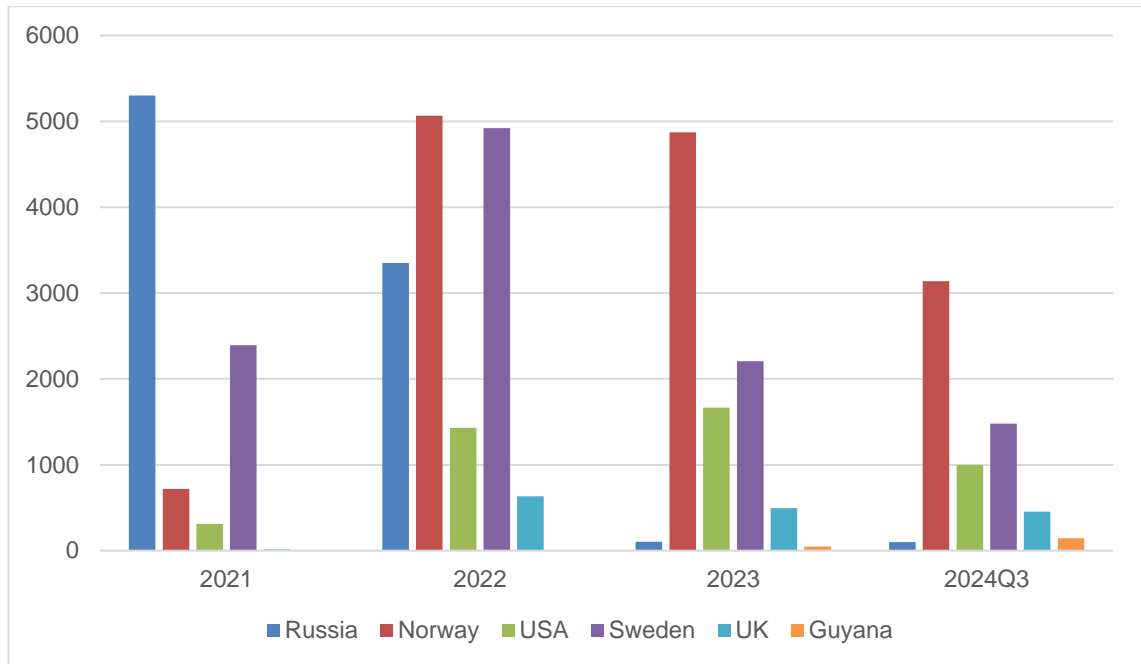


Figure 17. Energy imports by country of origin, 2021-2024Q3, millions of euros (Statistics Finland, n.d.e)

The shift from the Russian energy imports marked a turning point in Finland's energy strategy, which was long reliant on Russian trade. While the transition involved challenges such as rising costs, it also encouraged Finland to diversify. From an economic security perspective, this is highly positive for the country, since the reliance on one partner is too risky.

4.4 National Security

Russian actions posed a serious concern for security worldwide, but especially in the countries of the EU. Considering that Finland shares such a long border with Russia, the country has become especially cautious in addressing security risks. The geographical proximity to Russia made Finland increase defence measures and rethink its military alliances.

As discussed previously, Finland always tried to balance its relationship between Russia and the West. The military conflict in a European country has changed this position almost overnight. During the first days since the Russian military operations in Ukraine in 2022, research organisation Taloustutkimus

conducted a public survey on joining NATO. The results showed a historical switch in public opinion on the matter, with the majority of respondents (53%) supporting the decision (Koivisto, 2022).

Finland's defence spending has also significantly increased since 2022, positioning the country among the leading NATO members in terms of military expenditure. Figure 18 showcases the sharp increase in Finland's defence spending in 2023, which reached 2,5 % of GDP. It remained at a similar level in the following years and is projected to stay consistent in the near future. Furthermore, the national defence expenditure is said to be increased to be at least 3% of GDP by 2029 (Ministry of Defence, 2025).

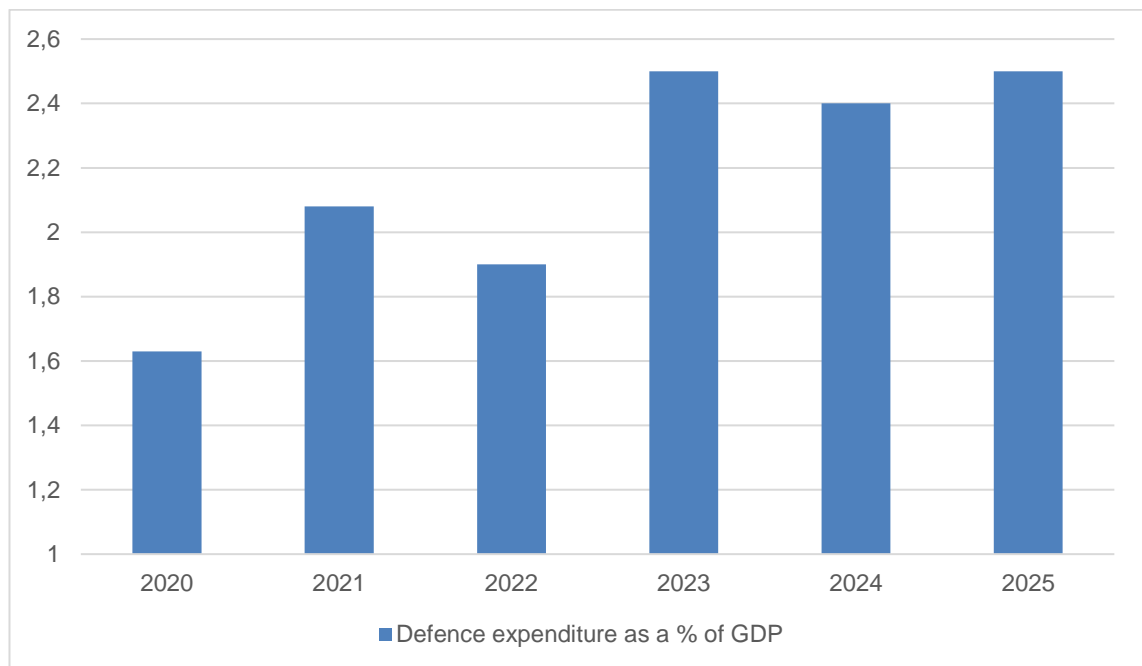


Figure 18. Finland's defence expenditure as a % of GDP (Ministry of Defence, n.d.)

Thus, the events of the past years not only impacted Finland's economy, but also marked a significant shift in its geopolitical stance - from the policy of neutrality to the decision of joining NATO. The shift highlights the impact that the geopolitical situation had on Finland and the increased concerns about the country's security (Das, 2024: 1254-1255).

4.5 Tourism

The tourism industry was largely affected in 2022 as well. Firstly, already in spring 2022 the Allegro train services between Helsinki and Saint Petersburg were suspended. The train had been in service for 12 years and had already been experiencing a decline in passengers due to the recent pandemic restrictions. Later, Finland decided to close its border with Russia fully at the end of 2023. This resulted in more than just an outflow of tourists – many Russians live in Finland, so the closure of borders meant that many families were now separated and needed to find alternative ways to see each other.

Based on Figure 19, 2022 saw a slight increase in Russians arriving in Finland, which can be attributed to the lifting of COVID-19 restrictions as well as people leaving Russia due to geopolitical uncertainties in the country. Based on a press release by the Finnish Government, 2022 saw the historically high quantity of labour migration, which was mainly achieved by the high number of applications from Russia (Finnish Government, 2024). The arrival of the Russian citizens, however, declined again in 2023 and further in 2024. This happened as a result of the full closure of borders between the countries and visa restrictions.

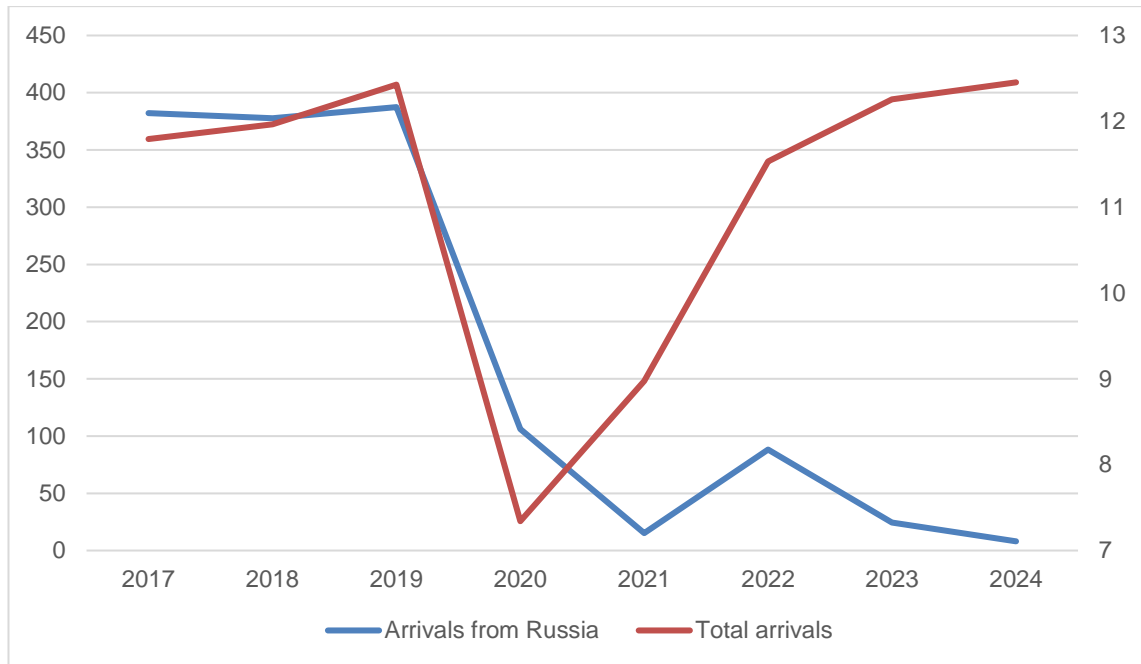


Figure 19. Number of yearly arrivals to Finland, arrivals from Russia in thousands, total arrivals in millions (Statistics Finland, n.d.b)

This decline underlines the broader disruption of not only economic but also cultural exchanges. Russian tourists went from being the largest group of foreign visitors in Finland to one of the smallest.

Nevertheless, total arrivals to Finland have been growing ever since the lifting of COVID-19 restrictions and have exceeded the pre-pandemic levels in 2024. Therefore, the impact of the conflict on the tourism industry has been insignificant, but it has significantly weakened Russian-Finnish tourism ties and cross-border cooperation in this sector.

4.6 Impact on Businesses

Even before 2022, Finnish companies had been reducing their presence in the Russian market since the events of 2014. Nevertheless, cooperation and trade generally continued, and the number of Finnish companies doing business with Russia was more than 3000 in 2020 (Taskinen et al., 2022). Furthermore, the number of Finnish subsidiaries in Russia was around 300 in 2019 (Bank of Finland, 2022).

The new geopolitical landscape forced most Finnish organisations to fully withdraw from the Russian market and end the cooperation. According to a survey by the Finnish Chamber of Commerce, at the start of the 2022 conflict, 78% of companies still had business operations in Russia. However, in the autumn of 2024, most had shut down all operations there and only 0,9% were still finalising the exit (Pohjanheimo, 2024). The decision was partly influenced by the sanctions and restricted operations, but for many countries, the decision has been voluntary.

Before exiting the market, the cooperation between Finnish businesses and Russia was already complicated by the sanctions on the financial sector. Restrictions on SWIFT access for Russian banks, combined with bans on financial transactions with sanctioned entities, complicated and slowed down the payments between the countries. Moreover, Finnish banks were much stricter than other European banks in terms of Russia-related money, which even further complicated the process of companies withdrawing from Russia (Mäkinen, 2022).

The outflow of tourism also affected some Finnish companies, particularly those operating in Eastern Finland. The businesses there relied heavily on Russian visitors as their primary target customer base. They were offering products that were tailored specifically to Russian tourist demand. Thus, the full closure of the border presented difficulties in the form of a decrease in demand and outflow of customers. For example, the store RajaMarket (translating as “border-market”) has been struggling with clients and has had to even rebrand itself to RMarket to attract customers outside its previous target group (Palola, 2024).

For travel company Saimaa Travel the events of 2022 brought critical problems, further complicating its already bad financial state after the pandemic. The company specialised in cruises between Lappeenranta and Vyborg, so the border closures first in 2020 and then again after 2022 severely damaged its

profits. As of 2023, the company has gone bankrupt as its debts greatly exceeded its assets (Pesu, 2023).

Another example is a previously discussed department store Grande Orchidée, which reopened in Autumn 2022 as an interior design store named Interior Centre. The store, however, operated for less than a year when it had to be closed due to financial losses. The demand for interior products decreased with lower purchasing power, while the lack of tourists from Russia further contributed to the losses (Sairanen, 2023).

5 Potential for Future Cooperation

The geographical proximity of Finland and Russia has been playing a major role in Finland's economy before the events of 2022. Although the crisis is still ongoing, it can be assumed that a resolution will be reached in the foreseeable future. The negotiations between Russia and the USA bring some hope for this progress. Should the geopolitical situation improve, it is reasonable to assume that after some time, the global attitude towards Russia may improve, and some sanctions might be lifted from the country. Therefore, cooperation between Russia and the West might become possible again. The improvement in relations with Russia could offer new opportunities for Finland.

According to a recent statement by Finnish President Alexander Stubb, the country should be prepared to restore its relationship with Russia. He also emphasised the fact that the geographical proximity of the countries is unchangeable, highlighting the importance of maintaining a realistic approach regarding the future (Immonen, 2025).

Improvements in countries' cooperation after the agreement is reached would be seen foremost in the areas of tourism and business operations. Since the decision to leave the Russian market among Finnish companies was primarily voluntary, after the conflict is resolved, many companies might consider the possibility to return. In fact, business owners in Eastern Finland have already been thinking of an idea of resuming business operations with Russia even at the current stage. The CEO of Atma Trade Oy, which owns Laplandia Market, has been targeting the Russian market since 2004, so the closure of borders has had a huge negative effect on the store's operations. Not willing to face bankruptcy, the idea of opening a Laplandia store in Saint Petersburg appeared (Seppä, 2024).

5.1 Arctic Ocean Railway

When thinking of more significant cooperation between Russia and Finland, one possible opportunity can be the Arctic Ocean Railway – an idea that was

proposed already in 2018. Since Finland is a quite isolated country and is not as connected as the rest of Europe, the Arctic Ocean Railway would significantly increase Finland's connections and offer new routes for trade (Finnish Transport Agency, 2018: 6).

The five routes proposed to connect Finland to the Arctic Ocean were as follows: Rovaniemi-Kirkenes, Kolari-Narvik, Tornio-Narvik, Kolari-Skibotn-Tromsø, and Kemijärvi-Murmansk. The most favourable route chosen by the Finnish Transport Agency (2018: 8) was from Rovaniemi to Kirkenes. However, this analysis focuses on the Kemijärvi-Murmansk route since it is the only option passing through Russia.

When choosing the best route to connect Finland to the Arctic Ocean, several factors should be considered, such as costs, length, impact on the environment, and broader possibilities brought by the route. The routes Rovaniemi-Kirkenes and Kemijärvi-Murmansk will be compared based on these factors.

When comparing the proposed route of Rovaniemi-Kirkenes with the Kemijärvi-Murmansk one, the first thing to notice is the investment costs. While the route through Russia would only cost 750 million euros, the Rovaniemi-Kirkenes alternative would cost nearly four times more (2,9 billion). Furthermore, in the Murmansk route, Russia would cover most of the costs (649 million euros), with Finland contributing only 101 million. In contrast, for the Kirkenes option, Finland would need to take the financial burden of over 2 billion euros (Finnish Transport Agency, 2018: 11). This makes the Kemijärvi-Murmansk significantly more cost-effective, not only operationally, but especially for Finland since the country would be able to save more than 20 times in investment costs.

In terms of length and infrastructure, the Kemijärvi-Murmansk is considered the "easiest and best" option by the council of eastern border municipalities in Lapland's region. This route leverages the already existing infrastructure, as there is already a railway from Kandalaksha to Murmansk. The existing railway covers about half of the route, leaving a distance of about 220 kilometres, which

is about half of Kirkenes route. Another reason in favour of the Kemijärvi-Murmansk route is that it can provide access to the global Russian railway that is, in turn, connected to China and other Asian destinations (Nilsen, 2017). This connection can open new opportunities for Finland as the country establishes itself as the northern transit centre between Europe and Asia.

Another aspect to consider is the environmental and social impact of the proposed routes. The Ministry of Transport and Communications (2019: 16) mentions that the two main concerns are related to the Sámi people and reindeer husbandry. Since the Sámi are the only Indigenous people in the EU and inhabit the Arctic regions of countries like Finland, Norway, Sweden, and Russia, any project that may affect their traditional lands and life must be approached with sensitivity. Moreover, since reindeer herding is considered a part of the Sámi culture, railway construction must account for its potential impact on this practice (Ministry of Justice Finland, n.d.).

The Rovaniemi-Kirkenes route is expected to pass through the Sámi territories, which has led to strong opposition to its construction from the Sámi community. The way of life of the Sámi people would be highly affected by the railway construction. It would fragment reindeer pastures and disrupt the movement of both reindeer and herders. Besides, the overall environmental consequences in the area of construction would be negative due to the potential exposure of the surrounding ecosystem to contamination through the potential mining developments (Itkonen, 2021: 70). In fact, the Rovaniemi-Kirkenes route was named the most environmentally harmful among all five options (Cepinskyte, 2018: 3). In comparison, the Kemijärvi-Murmansk route has no impact on either Sámi homelands or reindeer husbandry, making it easier to implement from both socio-cultural and environmental perspectives. Among all five proposed routes, the Kemijärvi-Murmansk and the Tornio-Narvik ones are the only ones that do not affect the life of the Sámi people and their activities to any extent. These two routes are also the most cost-effective options and are similar across the other evaluation criteria used by the Finnish Transport Agency (2018), with some differences regarding their strategic impacts.

Thus, after comparing the route chosen by the Finnish Transport Agency and the one connecting Finland to the Arctic Ocean through Russia, the following conclusions can be made. Firstly, the Kemijärvi-Murmansk route offers Finland a much more cost-effective connection. Secondly, it benefits from existing infrastructure on the Russian side, which includes access to the broad Eurasian railway network. Finally, and most importantly, the route through Russia poses no negative effects on either reindeer husbandry or the Sámi people, unlike the Norway alternative.

At the current stage, the implementation of the Arctic Ocean Railway is suspended because of the significant costs of the project as well as the objections from the Sámi Parliament (Kähkönen and Nystén-Haarala, 2022). It is unlikely that the Rovaniemi-Kirkenes route will be implemented in the future because the impact on the Sámi people and their activities is too critical. Regardless of the route alignment, any potential rail connection from Finland to Norway's Arctic coast would inevitably cross Sámi homeland areas and affect the reindeer husbandry. This makes the idea of connecting Finland to the Arctic Ocean through Russia more promising, given that relations between the two countries improve in the future.

6 Discussion

The findings above suggest that the geopolitical events of 2022 had a profound effect on Finland, primarily because of the full disruption of all forms of cooperation with its largest neighbour, Russia. As a member of the EU, Finland joined the sanctions regime aimed at isolating Russia, implementing economic measures to restrict trade between the countries.

By aligning with this decision of the EU, Finland fundamentally changed its economic and security strategies. Previously neutral, even after the beginning of the conflict in 2014, Finland radically shifted its position, resulting in the historical decision of joining NATO. The alignment with the EU measures also meant that the previous historical dependence on Russian energy products and raw materials had to end.

Any dependency relationship between countries in terms of supply chains and trade can present an extreme risk in the modern world. As seen in the example of the Finnish-Russian relationship, countries that are heavily reliant on trade with politically unstable regions are vulnerable to sudden changes in the geopolitical landscape. In order to avoid unwanted losses and economic recession, countries need to be prepared for this by having a diversified supply chain network and alternative trade partners.

Through analysing the existing literature on the Finnish-Russian relationships, recurring patterns were identified. Historically, Finland's economy has encountered several global geopolitical events since the 1950s, some of which were related to Russia to some extent. The ongoing geopolitical conflict is likely the most critical in its effects on the country. Although the economy did not suffer as severely in the long term, the event's impact was seen in a complete termination of cooperation between Russia and Finland, which is a crucial shift in the countries' relations. Despite the previous re-establishment of the relationship after geopolitical crises, the events of 2022 caused a deeper and more lasting disruption that is not as easily reversed. During the previous

geopolitical tensions, the major factors contributing to the economic slowdown were currency fluctuations and changes in oil prices, rather than sanctions.

After analysing Finnish economic indicators and looking into specific sectors important for the country's economy and directly related to cooperation with Russia, the following conclusions can be made. Finland's economy had not yet fully recovered from the impact of the pandemic, so when the new geopolitical crisis occurred, the country experienced some additional complications. Although the initial impact of the geopolitical events of 2022 on the Finnish economy was negative and led to a short-term economic slowdown, the economy recovered quickly, and by 2023, the improvements were already visible as the country demonstrated resilience. The areas that had struggled the most at the start of the conflict were, unsurprisingly, the cost of living and energy supplies. Furthermore, the conflict largely affected local businesses with a primarily Russian customer base.

Due to the geographical location of the countries, a lot of Russian-oriented businesses and industries are located in Finland, especially in the eastern part of the country, close to the border. Therefore, the closure of borders and the restrictions on tourist visa applications for Russian citizens that are in force now have highly affected their operations. With the decrease in arrivals of Russian citizens in Finland to a mere eight thousand in 2024, many businesses were unable to continue their operations due to the decreased demand and faced the threat of bankruptcy.

The energy sector of Finland has been quite dependent on Russian energy imports for a long time, so the sanctions, followed by the decision to cut the imports, affected the country. At the same time, they served as an acceleration for breaking this dependency. Although energy prices rose in 2022, leading to increased inflation, Finland has shown resilience in adapting to the situation. The imports from Russia have been mostly replaced by those from Norway and the ongoing transition to renewable energy, which started already in the 2010s.

Thus, while initially the termination of most energy supplies from Russia led to some economic instability, the long-term impact can be treated as positive, with Finland diversifying its supply chain with other stable markets and increasing the share of renewables. Even if Finland were to resume the energy trade with Russia after the potential lifting of sanctions, it is highly unlikely that the dependence on Russia as a supplier would return.

Finland is still struggling with high unemployment rates and decreased consumer confidence. Another problem for the economy is the increasing government general debt. Dealing with this problem will require Finland to introduce either new financial measures to decrease the debt or to stimulate the GDP growth even further. Despite this, the country's economy has mostly dealt with the obstacles and picked up after the initial effects were over, with most economic indicators having already returned to the pre-conflict levels.

Since, according to Krokhin (2023: 54), the Russian-Finnish economic relations are now in a state of the greatest degradation in their recent history, there is the possibility of gradual improvement over time. Since the geographical proximity of the countries cannot be changed, the potential future cooperation between Finland and Russia becomes an interesting possibility to consider.

It can be said that the cooperation of Russia and Finland is much more necessary for Finland than for Russia. According to the IMF, Russia has become the fourth largest economy in the world based on purchasing power parity (PPP) (IMF, n.d.e). With this in mind, the imposed sanctions did not significantly affect the Russian economy, at least negatively; on the contrary, it even appeared to benefit. The disrupted trade with the Western countries made Russia fully divert its focus to Asian economies such as, for example, China (33,8% of Russia's trade turnover for January-October of 2024) and India (8,8%) (Tkachev and Vinogradova, 2025).

Meanwhile, Finland's economy has experienced several drawbacks in the form of high rates of inflation and unemployment, lower consumer confidence, and

growing government debt. Thus, the anticipated end of the ongoing conflict could provide Finland with new economic opportunities for resumed cooperation with Russia. The idea of connecting Finland to the Arctic Ocean is especially appealing due to the possibility of expanding the country's value in the global supply chain. Since the formerly favourable route was said to be unfeasible, the implementation of the Kemijärvi-Murmansk route could be considered if cooperation resumes after the conflict is resolved. The connection through Russia could offer Finland benefits in terms of costs, accessibility, and reduced cultural disruption. Moreover, this route would enable a connection from Finland to Asia through the extensive Russian railway network. With the economic growth shifting to Asia, Finland could benefit from its strategic position as a country between the East and West.

The potential benefits are even further expanded when considering the possibility of connecting Finland to the INSTC, which was named the most important part of the transport framework of Eurasia, through Russian infrastructure (Roscongress, 2024). This would open new trade corridors to the Middle East and Central Asia, enhancing Finland's logistic value even more.

Even though the current geopolitical situation is making it almost impossible to implement any of this at the present time, the ongoing negotiations offer some hope for future progress.

7 Conclusion

This thesis aimed to investigate the following research question: “How have the recent geopolitical events affected the economy of Finland, and what opportunities do Russia and Finland face in potential future relations?”

The research has shown that the geopolitical events of 2022 have exposed Finland’s vulnerability in trade and energy security. They reduced economic growth, however, only for a short period. Finland quickly adapted its strategies and achieved economic recovery by expanding trade with other countries and diversifying supply chains. Thus, even though the sanctions and the suspension of cooperation with Russia temporarily hindered Finland’s economic growth due to the historical dependence, the country’s effective measures laid the foundation for recovery.

Currently, the geopolitical conflict is at its closest point to resolution since its start in 2022. This fact prompts consideration of the possible form of relations between the countries. The improvements are likely to occur gradually and might take a long time. Nevertheless, it is unlikely that Russia, one of the world’s largest economies, will remain at the same level of isolation from the Western world as it is now. The country’s geographical location and the link to many Asian economies provide logistical and economic benefits.

The isolated country of Finland would greatly benefit from establishing a railway to the Arctic Ocean, which would also grant the country access to Asia through Russia. Since the end of cooperation with Russia, Finland has not been making use of its otherwise valuable strategic location between East and West.

If the geopolitical conditions were to shift, both countries could benefit from carefully redefined economic cooperation. Nevertheless, any such opportunity would clearly require both stability and trust.

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