GCSP
Geneva Centre for Security Policy

NOVEMBER 2022 | ISSUE 26

Strategic Security Analysis

The Impact of the Russia-Ukraine War on the Global Sanctions Landscape

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The Geneva Centre for Security Policy

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ISBN: 978-2-88947-312-0

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Key points

- The Russia-Ukraine conflict will accelerate the global trend towards increasing great power competition that pits the existing West-anchored world order against others, especially Russia and China.
- This new era will have significant implications for the global sanctions landscape as sanctions that have been effective in harming countries with smaller economies are increasingly focused on larger economic powers that are integrated into the global economy. This will carry a far greater risk of diminishing the effectiveness of the sanctions weapon, because larger economies like that of China have a greater capacity to overcome technology export restrictions and the US dollar's centrality in global finance.
- While sanctions campaigns often seek to coerce the target state into policy modification, sanctions may be increasingly used for the purpose of economic containment by attempting to retard the long-term economic development of states. This may result in open-ended sanctions campaigns that will generate a new era of geoeconomics where sanctions risk factors become key to the design of business relationships and supply chains.
- The use of financial sanctions against larger economies will exacerbate already existing trends of de-banking and a decline in corresponding banking relationships.
- Technology sanctions and export controls will be increasingly central as sanction-imposing countries in the West seek to leverage their superiority in key emerging technologies against those they perceive to be their adversaries.

Introduction

Wars and major geopolitical episodes tend to accelerate already existing trends. The Russian attack on Ukraine has shaken the international community and set off a series of reactions that will reshape the global sanctions landscape. Since the end of the Cold War, major sanctions campaigns against countries have been primarily focused on smaller nations that are more peripheral to the global economy. But now, the United States and the European Union (EU) have thus far introduced a series of sanctions against key Russian and Belarussian economic sectors that were designed and implemented at an unprecedently rapid rate. Because the world was already heading towards great power competition, this imposition of broad sanctions against a larger economy like that of Russia demonstrates the West's confidence in its ability to use economic statecraft as a means of influencing international affairs and the centrality of the economic weapon in the context of this new era of competition.[1]

For decades sanctions have been part of what European leaders considered a legitimate repertoire of tools to influence the EU's external relations. The Council of the EU even adopted special programmatic guidance on the issue as far back as 2004.[2] But the aggressiveness of Ukraine-related sanctions imposed on Russia and the speed with which they were imposed have highlighted the extent to which sanctions have been legitimised in European decision-making and how Europe has become increasingly comfortable with broad and sectoral sanctions that affect the whole of the target state's economy and society. Of course, the United States was far ahead of Europe in this trend. Already by 2015 the US Department of the Treasury was being touted as the Obama administration's "favorite noncombatant command".[3] However, currently sanctions have also become central to the EU's common security policy.[4]

Since the end of the Cold War, major sanctions campaigns against countries have mainly been primarily focused on smaller nations that are more peripheral to the global economy.

Underpinning the cooperation of the private sector with US and EU sanctions efforts in the first two decades of this century was the fact that these sanctions were implemented against small countries and under what would often be presented as special circumstances. When sanctioning smaller economies, US sanctions architects argued, Washington leveraged the standard operating culture and behaviours of banks to direct them away from doing business with targets like Iran even in the absence of statutory bans.[5] When larger economies more central to the global economic order are sanctioned, these same factors become risk points. These larger economies have greater capacities to manage sanctions pressure and a larger network of economic partners around the world (businesspeople, firms, institutions and nations) that will be willing to abandon common practices and find new mechanisms with which to carry out basic business activities.

Economic containment

Most of the sanctions regimes that have been implemented in the first two decades of the century have, for the most part, been aimed at achieving the goal of policy modification. This most ubiquitous goal for sanctions campaigns means that the state or coalition of states imposing the sanctions is seeking to strong-arm the target into altering a policy or a set of policies that had triggered some form of tension. Non-nuclear-proliferation-related sanctions against Iran and North Korea are examples of such efforts. But sanctions against Russia and China, while often formally imposed due to specific and real transgressions such as Moscow's invasion of Ukraine, are occurring in the context of great power competition and will, therefore, be underpinned by a different strategic calculus.

In the context of this new era, the goal of sanctions campaigns against these far larger economies will more likely be *economic containment*.[6] This is defined as a feature of the grand strategy of a leading state or a coalition of leading states that seek to maintain the status quo in the international balance of power and mitigate the rise of global competitors by undermining the economic, technological and military capacity of such competitors. Whereas more orthodox economic sanctions campaigns typically lay down clear demands and offer at least a theoretical path for the target state to have the sanctions lifted, a campaign of economic containment is inherently open-ended, and any cessation of economic hostilities can only come about as a result of a substantial change in the assessment of the target's capacities and ambitions.

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The way one detects such a strategy is by examining the formal explanations offered for a particular sanctions campaign. In this respect, US leaders have been the most explicit. In a speech in Warsaw, President Biden called on "freedom-loving nations" to "commit now to be in this fight for the long haul", and added that "We must remain unified today and tomorrow and the day after and for the years and decades to come".[7] Similar statements showing a determination to weaken Russia – especially its military capacity – in the long term have been made by US secretary of defense Lloyd Austin[8] and national security advisor Jake Sullivan.[9] European officials have been far more hesitant to chart such a course, at least publicly. But several officials and former officials have. For example, former NATO secretary general Anders Fogh Rasmussen stated that Putin's assumption would be that the sanctions campaign is aimed at weakening Russia, "So why not speak openly about it?"[10]

Financial sanctions were central to US campaigns against smaller economies like those of Iran, North Korea, Venezuela and Syria in the first two decades of the century. Even sanctions against the hydrocarbon exports of these countries were largely successful due to the dollar-centred nature of global oil and gas markets.[11] The modalities required to impose such sanctions against Russia and China are available both to the United States and the EU. However, as seen in the case involving Russia, while financial sanctions will have a strong role to play here as well, imposing them against larger countries more integrated into the international economy carries greater costs and risks for the sanctioning nations.

The risks are numerous and complex, but they can generally be placed in three distinct categories. The first is that measures taken against larger economies may involve imposing sanctions against major firms that are deeply integrated into the global economy. This may trigger unwanted and/or unintended affects that backfire on the sanctioning countries.

Recent examples include the sanctions imposed on Russian aluminum giant Rusal and Chinese shipping firm COSCO.[12] These measures caused signficant disruptions in global commodity markets and logistics, respectively, that the sanction designers had seemingly not anticipated or prepared for. If firms in these countries were to be targeted at an accelerated rate and over a longer period of time, the potential for disruption will grow significantly.

The second and third categories are the risk of larger economies – and their global partners – working to dilute the power of the economic weapon and the target states' greater retaliatory capacities. These two latter issues will be discussed extensively in the following sections.

Financial sanctions

Many scholars and practitioners have long warned of the prospect of overuse undermining sanctions as a tool of statecraft and possibly leading to the loss of the US dollar's coveted position.

Critical to the success of financial sanctions has been the centrality of the US dollar and a largely Western-based international financial infrastructure in an increasingly globalised world where cross-border transactions are intrinsic to any national development strategy.[13] In the 2010s de-banking or de-risking[14] (i.e. the withdrawal of financial services from jurisdictions under heavy sanctions scrutiny) has become standard practice among global banks.

Bank compliance departments, once considered relatively unimportant middle-level institutional structures, have become increasingly enmeshed in daily operations as the burden of policing global financial transactions has been increasingly shifted onto financial institutions. Their staff sizes and resources have also grown dramatically to manage the new regulatory demands.[15] One study projected that the cost of compliance for banks in the US and Canada alone during the year 2022 at US$56.7 billion, a 13.6% increase from the previous year.[16] This is one major factor driving the retreat of vital correspondent banking relationships around the world that undermines globalisation and global value chains.[17] The exposure of larger economies to sanctions risk will likely expedite this trend and spread it into new areas and regions.

The efforts of countries like China and Russia to produce alternatives to the pillars of the international financial infrastructure like the Belgium-based SWIFT system for international financial transfers between banks and to de-dollarise that infrastructure have been largely unsuccessful up to this point, as indicated by Russia's struggles to facilitate cross-border transactions using its local financial messaging system.[18] These alternative systems have failed to achieve significant traction even in their own markets due to a combination of factors. These include SWIFT's strong global network effects, the weakness of the Russian economy, China's stringent capital controls and the deprioritisation of these systems in favour of the economic convenience of working through more mainstream institutions like SWIFT.[19] That being said, these endeavours could become the focus of increasing government and private sector investment in the new environment that is emerging.

Many scholars and practitioners have long warned of the prospect of overuse undermining sanctions as a tool of statecraft and possibly leading to the loss of the US dollar's coveted position, which would have broad ramifications.[20] Despite the strength the dollar has shown during the recent (and ongoing) period of successive crises, the warnings about US attempts to impose major financial sanctions against great power competitors have become louder.[21] While individual projects to lower the dollar's centrality or erect non-dollar financial infrastructure have yielded limited results, the accumulation and increased resource investment into these measures by a greater number of actors involved in the Russian and Chinese economies may eventually achieve a significant measure of success in wearing away the dollar's usefulness as a weapon.

Highlighting this concern is a new World Bank report warning that "Global trade and financial networks could fragment" if the Russia-Ukraine conflict and its associated embargoes continue, adding that the sanctions' impact on Russia can result in other countries' "self-isolating" with higher trade barriers and alternative financial systems independent of the US dollar. The authors of this report note that the resulting loss of specialisation and competitiveness "could slow output and income growth and add to inflation pressures".[22]

Technology sanctions and export restrictions

Searching for asymmetries, sanctions architects have focused on technology sanctions believing that the U.S. and its allies dominate foundational technologies that Russia and China still lack.

By far the most important likely change caused by the use of sanctions in the context of great power competition will be the increasing presence of technology sanctions and export controls on the Western sanctions agenda, usurping the financial sanctions that have taken centre stage over the last two decades. This is largely due to the abovementioned difficulty in imposing broad sanctions against larger economies. Searching for asymmetries, sanctions architects have focused on technology sanctions believing that the U.S. and its allies dominate foundational technologies that Russia and China still lack.

In the context of Russia's invasion of Ukraine, US officials have indicated both surprise and satisfaction with both the speed and depth with which technology sanctions have impacted Russia and its war effort.[23] According to US officials, this has undermined both Russia's military manufacturing capacity and its economy. As President Biden stated, "We are choking off Russia's access to technology that will sap its economic strength and weaken its military for years to come".[24]

Western officials have publicly argued for a stronger technology export control regime – or an "Economic NATO" – to safeguard the West and its allies and ensure that major countries like Russia and China are "playing by the rules".[25] Already, a new coalition has been formed of countries that are imposing new technology export restrictions on Russia and Belarus. This coalition includes the United States, the EU, many non-EU European states and key East Asian allies such as Japan and South Korea. Countries are incentivised to join this coalition because doing so would exempt them from requiring licences to import the goods and technologies being targeted. These include a host of emerging technologies and items of advanced equipment made with or partially containing US technology, including advanced semiconductors and integrated circuits.[26]

A large set of overlapping efforts have also been put in place to create new mechanisms for technology export controls championed by Washington. The transatlantic Trade and Technology Partnership is the most significant of such efforts between the United States and EU.[27] But these efforts also include the Export Controls and Human Rights Initiative[28] and working groups under the G7 and NATO that are currently only focused on monitoring the implementation of sanctions on Russia. The most significant interstate group regulating technological and dual-use exports, the Wassenaar Arrangement, is unlikely to be particularly helpful in this regard, especially because Russia itself is a member.

There are already calls for the United States and its allies to create a new version of the Coordinating Committee for Multilateral Export Control (CoCom),[29] and legislation calling for it has already passed the US House of Representatives.[30] Established in the early Cold War years, this informal organisation operating out of an annex of the US Embassy in Paris played a vital role in restricting Western exports of important technological items to the Soviet Union and the Eastern bloc.[31] Due to its strong performance in the early years of the Cold War, some sanctions scholars consider CoCom to be one of the most effective economic statecraft endeavours in history.[32]

Critically, CoCom served as a strong vehicle for the United States to impose export limitations on its allies in the Western bloc. As the US Congressional Research Service attests, in almost every case it was the United States that argued for greater restrictions, while its European allies preferred greater East-West trade.[33] Therefore, Europe should consider how the prospect of a resurrected CoCom would impact its interests with some scepticism. While European countries and institutions have had some success regulating US technology firms on such matters as privacy issues specifically involving these firms' operations in Europe, Washington has long held the initiative on strategic export controls pertaining to nations beyond the West on national security grounds.

Countries will increasingly treat the interdependence that global value chains bring as a national security issue and regulate accordingly.

Just as financial sanctions were effective due to the globalisation of finance, technology sanctions are also bolstered by the fact that the global economy is defined by global value chains dispersed around the world. A new era of intensified technology sanctions and export restrictions will result in new challenges. Countries will increasingly treat the interdependence that global value chains bring as a national security issue and regulate accordingly. This securitization effect will cause them to further shift toward indigenisation and economic interaction with countries of shared political orientation – what scholar Henry Gao has called moving from value chains to "values chains".[34] This will also confront sanctions coalitions with a variety of collective action problems, especially regarding the gap between the technology and export control frameworks of Europe and the United States that diverge significantly in many ways in terms of their goals, definitions of dual use and liability structures.[35]

Both the United States and China see technology through the prism of military power and economic competition, and will therefore increasingly implement aggressive measures and mobilise their respective military-industrial complexes to advance their technology goals. Europe, on the other hand, has to this point focused on reducing vulnerabilities and interference rather than trying to shape the future technology order. Currently there is insufficient global governance on issues of technology, which means that there is little international order to ease or regulate competition in this sphere.

Playing defence

This new era, particularly its technology sanctions dimension, will emphasise the importance of anti-coercion tools. Larger economies have significantly greater potential for retaliatory action, and Chinese dominance in various aspects of the global supply chain will present an unprecedented challenge.

Western scholars and sanctions practitioners have long been concerned about China's capacity to deepen its own already significant level of economic statecraft. They argue that there has been a trend toward an increasing willingness to impose economic measures as the importance of the country's economy has provided greater opportunities to use such strategies for its geopolitical ambitions.[36] While China maintains a formal opposition to economic sanctions, it has increasingly weaponised its own economic ties. It has levied a variety of economic restrictions against countries over perceived slights such as their relations with Taiwan and hosting the Dalai Lama, as well as maritime and territorial disputes. As has been extensively discussed in recent months, Russia has also leveraged its key position as a hydrocarbon supplier to Europe to retaliate against the barrage of sanctions imposed upon it by Western countries.

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In addition, European countries – and in particular smaller European nations – need to ensure that undue influence is not exerted on their economic decision-making from across the Atlantic. Europe's inability to challenge US pressure on European firms and institutions to leave Iran after Washington abandoned the Iran nuclear deal weighs on Europe's economic sovereignty and its capacity for independent action.

A credible framework to identify and challenge hostile or arbitrary economic coercion would guarantee the EU's freedom of action and ensures that countries have a seat at the decision-making table proportionate to their technological weight. The Anti-Coercion Instrument[37] that was proposed in response to Beijing's hostile action against Lithuania represents an important first step in this regard. Various European scholars have outlined more comprehensive plans for both defending the continent against economic coercion and retaliating as need be against those who would encroach on EU economic sovereignty; such plans also merit consideration.[38]

Conclusion

While financial and energy sanctions have reshaped the global economic landscape in many ways, the shift of sanctions towards larger economies and the emerging escalation of technological export controls will yield a new era of geoeconomics where economies are more fulsomely instrumentalised for national security purposes. This will have broad implications for how sanctions – or "restrictive measures" in EU parlance – are used and will likely accelerate already existing trends of de-globalisation and economic bifurcation. In many cases increased cross-border economic activity could accompany this trend, but the rate of economic growth will outpace interconnectivity as countries become increasingly guarded with regard to any kind of perceived or real asymmetrical interdependence.

> While sanctions can be very potent in harming the target state's economy, they are not necessarily effective in bringing about policy modification in the target state.

The European Community as a whole and the sanctioning parties involved should be realistic about the fact that sanctions, like many other tools of statecraft, are often not effective. In a particularly influential study of sanctions' effectiveness, Hufbauer et al. have argued that sanctions are effective only 34% of the time.[39] Firstly, this is a relatively rosy assessment compared to those of other studies. Secondly, effectiveness here is defined as contributing to a positive outcome for the sanctioning party or parties, rather than sanctions dictating the outcome of events to these parties' satisfaction.[40]

Sanctioning countries should also consider the impacts that long-term isolation may have on Russia and its decision-makers in Moscow. Scholars broadly believe that economic sanctions tend to reduce the level of democracy in states, expand corruption and undermine human rights.[41] Some have also contended that long-term blockades tend to push sanctioned nations' leaders to adopt riskier strategies by limiting their options even when these strategies face long odds of success.[42] An economically isolated and increasingly authoritarian Russia that sees the achievement of both its foreign and domestic economic goals in terms of leverage seeking and one-upmanship against the West in general and the EU in particular may be more, not less, belligerent in its approach.

While sanctions can be very potent in harming the target state's economy, they are not necessarily effective in bringing about policy modification in the target state. They can also often be somewhat ineffective in undermining that state's war-making capacities. For example, the Trump administration repeatedly claimed that Iran's ability to support its regional allies was severely compromised by the maximum pressure campaign imposed on it by that administration. However, US government experts and even supporters of the hardline approach against Iran in the Washington foreign policy community rejected this claim.[43] As mentioned above, US officials believe that the sanctions imposed on Moscow are degrading Russia's military manufacturing capacity. At this early stage, and because of the opacity of the Russian military industrial base, it is difficult to assess the degree to which this is the case and whether this has meaningfully affected the direction of the conflict in Ukraine.

Sanctions are best used for limited objectives and in concert with other means of statecraft.[44] This is especially the case in major security conflicts where relative gains are critical and the expectation of future conflict looms over the wider decision-making process. A target state would be concerned that any concession made to the sanctioning state or coalition would have a dual effect: not only would it be a concession in its own terms, but it would also change the balance of power against its interests during the expected next round of security competition.[45]

This will certainly be the case in terms of sanctions imposed against larger powers who have strategic ambitions and whose leaders could face severe audience costs at home. Sanctions occupy an intermediate position between war and diplomacy, and are seldom effective on their own.

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ISBN: 978-2-88947-312-0