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Sanctions and Economic Security: The Third-Country Dilemma

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Abstract. G7 states are increasingly using economic sanctions in the conduct of their foreign policies. Such sanctions have serious impacts on third countries, even though they are not directly targeted. The cases of Armenia and South Africa illustrate the challenges that third countries face as they seek to balance competing geopolitical and economic imperatives. Sanctions often penalise such countries if they fail to reduce ties with sanctioned countries and entities. However, a more effective approach would rebalance this relationship through greater engagement.

Keywords: sanctions, G7, Global South, South Africa, Armenia, economic security.

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INTRODUCTION

Since 2022, economic sanctions have become a key component of international relations. In the wake of Russia's full-scale invasion of Ukraine, a G7-led coalition introduced restrictive measures on an unprecedented scale. They aimed to cut off a major global economy from essential financial systems, trade routes and advanced technologies. What were once largely symbolic or narrowly targeted measures have become broad instruments of economic pressure - designed to both weaken Russia's war effort and influence the choices of other states.

Much of the current analysis understandably concentrates on the direct impact of these sanctions on Russia. However, a quieter, yet profound, change is also unfolding: the rising pressure on third countries - those not directly involved in sanctions regimes. Such countries - many of which are non-aligned or strategically cautious - are not formal members of the sanctions coalition but are increasingly indirectly affected. They are facing growing costs and constraints that emerge not from explicit legal obligations, but from the wider enforcement environment shaped by global financial networks. The loss of correspondent banking relationships, restricted access to dollar-based payment systems and an atmosphere of regulatory uncertainty have gradually undermined their ability to sustain economic autonomy.

This article places these developments within the broader framework of economic security, defined here as a state's ability to protect its financial infrastructure, maintain stable trade flows and pursue independent economic policy. The impacts of sanctions on third countries often arise unintentionally, yet they are deeply felt. For many of these governments, sanctions have shifted from distant foreign policy tools to front-of-mind dilemmas that affect domestic economic planning, political stability and external engagement.

This article draws on fieldwork conducted in Armenia and South Africa - two countries with different geopolitical alignments but comparable exposure to sanctions-related disruptions - to offer an in-depth look at how third countries experience and respond to the evolving global sanctions regime. Interviews with G7 policymakers complement these on-the-ground perspectives, revealing a gap between the strategic objectives of sanctions and their real-world effects.

Ultimately, the article argues that the G7's broad application of sanctions has reshaped the landscape of global economic governance. Sanctions today operate less as tools of bilateral confrontation and more as regulatory signals carried through international financial systems. This evolution has left third countries in a difficult position: remain neutral and risk economic isolation or align politically to preserve financial connectivity and market access.

The sections that follow outline the structure and rationale of the G7 sanctions regime, propose an analytical framework for assessing third-country economic security, present detailed case studies, and conclude with policy recommendations for both sanctioning states and those that need to respond to the changing geopolitical and economic landscape.

1. SANCTIONS AND ECONOMIC SECURITY AS A KEY DIMENSION OF MODERN INTERNATIONAL RELATIONS

Sanctions as foreign policy tools have become a central feature of contemporary international relations. They are used to signal disapproval, as well as punish and compel behavioural change in targeted individuals, entities and states. Sanctions - whether mandated by the United Nations (thereby showing broad multilateral consensus), or imposed unilaterally by blocs (such as the G7) or individual countries - serve many functions: they seek to enforce international norms, deter future violations, and show political solidarity. At their core, sanctions serve as instruments of economic statecraft that alter the conduct of the sanctioned party.

In the 2010s, G7 countries have increasingly used unilateral sanctions, demonstrating their growing significance in foreign policy strategies. In the 20th and early 21st centuries, sanctions - notably when used by countries other than the United States - were primarily symbolic and designed to send a signal. They are now applied more frequently and are larger in scope, marking a shift from a messaging tool to mechanisms of coercion with painful economic consequences.

Economic statecraft, of which sanctions are the main tool, has long been a cornerstone of U.S. foreign policy - from the Marshall Plan to the Global Magnitsky Act. The U.S. has consistently leveraged its economic power to influence the behaviour of other states in pursuit of national objectives (Furman & Klein, 2023; Fishman, 2025). The use of sanctions, in particular, has increased dramatically, with a nine-fold surge in designations between 2000 and 2021 (United States Department of the Treasury, 2021). In recent years, sanctions have become a "tool of first resort" for addressing U.S. national security, foreign policy and economic threats. During his first term in office, President Donald Trump emphasised economic coercion as a primary instrument of American foreign policy (Harrell, 2019), and the first 100 days of his current term has shown that the U.S. government will continue to emphasise their use (The Soufan Center, 2025).

In the European Union, sanctions - referred to as "restrictive measures" - are integral to the Common Foreign and Security Policy. They are employed both in response to international crises and as a means of asserting the European Union's role as a normative global actor, committed to the defence of democracy, human rights and the rule of law (European External Action Service, 2025).

The European Union's approach to sanctions has evolved considerably since the early 1990s. Initially, its sanctions were reactive and often aligned with United Nations Security Council resolutions. But with time, EU restrictive measures have grown more autonomous and strategically targeted. Notable examples include the complex regimes imposed on Syria and Iran, which strongly shaped the EU framework for the use of restrictive measures. The sanctions against Syria, initiated in 2011, were at that time the most comprehensive autonomous regime ever adopted by the European Union (Council of the European Union, 2011).

The European Union's response to Russia's full-scale invasion of Ukraine was historic and a step-change in its sanctions policy. In response to Russia's illegal war of aggression, the European Union imposed extensive financial and trade restrictions targeting central bank reserves, oil exports and dual-use goods (European Commission, 2025). These measures signalled a further shift from symbolic gestures to systemic economic warfare, aimed at both penalising Russia and undermining its war economy. The change in the primary purpose of sanctions, from signalling to impact, forced the European Union to confront its enforcement challenges and triggered remodelling of both how sanctions are designed by the European Commission and implemented and enforced by the Member States (European Parliament & Council of the European Union, 2024).

2. SANCTIONS TRANSMISSION TO THIRD COUNTRIES

Sanctions regimes increasingly operate beyond national borders and engage third countries, relying on a range of mechanisms to influence their behaviour. These mechanisms include extraterritorial enforcement via tools such as secondary sanctions, and control of financial system chokepoints (for example, SWIFT and access to U.S. dollar clearing). The strategies deployed by the United States, the European Union and the United Kingdom to ensure effective sanctions implementation illustrate distinct legal and institutional preferences shaped by their respective global leverage.

The United States operates the world's most far-reaching sanctions framework, underpinned by the centrality of the U.S. dollar, the dominance of U.S. financial institutions and the regulatory power of the Office of Foreign Assets Control (OFAC). The mere threat of U.S. secondary sanctions can cause significant market disruption, incentivising compliance even among foreign actors outside formal U.S. jurisdiction. In particular, OFAC's reputation effectively amplifies U.S. sanctions and reinforces compliance throughout international financial networks.

The United States' most potent tool is its secondary sanctions - measures that penalise non-U.S. persons and operators for conducting operations that violate U.S. sanctions. They may be applied regardless of a direct U.S. legal connection and can result in significant repercussions, including loss of access to the U.S. financial system. For many firms, such exclusion is tantamount to commercial isolation. The December 2023 Executive Order (President of the United States) further reinforced the U.S. approach. It announced secondary sanctions targeting foreign banks and businesses facilitating transactions for Russian military-industrial firms - a notable expansion in enforcement scope and a clear signal of intent to deter circumvention by third-country actors.

Traditionally, the European Union has rejected the extraterritorial application of sanctions; Brussels maintains that its measures are legally binding only on EU nationals and operators, and any individual or entity operating on EU territory. Historically, Europeans have vocally opposed unilateral U.S. extraterritorial sanctions, particularly in cases such as Iran, and view such measures as a breach of international law and sovereignty. In 1996, the European Union introduced the Blocking Statute (European Union, 2018). It is a legal mechanism to counteract the extraterritorial application of foreign sanctions, particularly those imposed by the United States. The statute prohibits EU companies from complying with certain non-EU sanctions and nullifies the effect of foreign court rulings based on those sanctions within the European Union. This approach amplified the European Union's commitment to strategic autonomy in sanctions policy and reinforced the bloc's legal framework against the extraterritorial reach of foreign laws. Despite its intent, the Blocking Statute has limited practical impact because EU companies often fear the loss of access to the much-larger U.S. market more than EU penalties for complying with U.S. sanctions.

With time, the European Union has increasingly recognised the need to enhance its strategic autonomy in the financial domain and to strengthen instruments that reinforce its foreign policy objectives. A key turning point came with the European Union's response to Russia's full-scale invasion of Ukraine. To secure effective implementation of its sanctions on Russia, the European Union initially sought to secure broader international implementation through diplomacy rather than exterritorial enforcement. In December 2022, the European Commission established the office of EU Sanctions Envoy and tasked David O'Sullivan, an experienced diplomat, with engaging with third countries to prevent circumvention. It quickly turned out that the diplomatic track had to be supplemented by the European Union's market power and economic incentives, offering a more tangible 'carrot' to complement the 'stick' that the United States often wields.

Gradually, the European Union has advanced mechanisms to exert influence over the behaviour of non-EU operators, such as ancillary listings - targeted sanctions applied to third-country actors who, while not the primary focus of EU measures, materially support or facilitate activities that undermine EU sanctions objectives (Nielsen et al., 2025). These listings allow the EU to reinforce compliance and deterrence without asserting extraterritorial jurisdiction in the manner of traditional secondary sanctions. However, it has not decided to expand the legal basis for imposing true secondary sanctions capabilities; it continues to rely on diplomatic engagement and incentives, rather than coercive enforcement, to ensure third-country compliance.

However, the European Union's leverage, while different from that of the United States, is not negligible. Hypothetical discussions about transatlantic divergence in Russia sanctions policy after Donald Trump won the 2024 presidential election have revealed that the European Union can exert considerable pressure (Sandbu, 2025). It controls key nodes in the global financial infrastructure, notably SWIFT (the main network used to send messages that initiate international payments) and Euroclear (the depositary of the majority of Russian central bank assets), both based in Belgium. The European Union also boosted its capacity to enforce sanctions on EU economic operators by adopting Directive (EU) 2024/1226, establishing minimum criminal penalties for sanctions violations. To complement the Commission's efforts, the Member States have significantly developed and strengthened their domestic sanctions implementation frameworks, as illustrated by a series of country-specific workshop reports published under the SIFMANet project by the Royal United Services Institute (RUSI), which offer detailed insights into financial network vulnerabilities and sanctions implementation challenges across various EU jurisdictions (Royal United Services Institute [RUSI], n.d.). All those efforts mark a critical step towards harmonising enforcement standards and thus effectiveness of the measures.

After Brexit, the UK has charted a sanctions course that largely aligns with its allies while preserving some autonomy. Under the Sanctions and Anti-Money Laundering Act (2018), the United Kingdom enforces primary sanctions and does not maintain a formal secondary sanctions regime comparable to that of the United States. Nonetheless, the United Kingdom may sanction foreign entities involved in activities that violate UK law - such as financing terrorism or breaching international humanitarian norms.

Since the United Kingdom lacks explicit extraterritorial enforcement mechanisms, it predominantly deploys its soft power. The Office of Financial Sanctions Implementation and Office of Trade Sanctions Implementation issue regulatory guidance (HM Treasury, n.d.; Department for International Trade, n.d.), and the Foreign, Commonwealth & Development Office supports these efforts with diplomatic engagement in third countries (Foreign, Commonwealth & Development Office, n.d.). The United Kingdom often acts as a link between the United States' strong stance and Europe's cooperative approach, helping to keep the group united while following its own legal rules. The United Kingdom's February 2024 sanctions strategy reinforces this stance (Foreign, Commonwealth & Development Office, 2024).

To sum up, the United States, the European Union and the United Kingdom share a commitment to using sanctions as a central tool of foreign policy. However, each differs in how global compliance is ensured. The United States relies on legal extraterritoriality and financial dominance; the European Union increasingly pursues diplomatic engagement and institutional innovation; and the United Kingdom balances legal restraint with strategic alignment. These differences reflect broader geopolitical roles, legal cultures and economic structures. Yet all three actors recognise that effective sanctions enforcement increasingly requires engagement beyond their borders - whether by force, law or persuasion.

From the global perspective, the G7's increasingly assertive use of sanctions has reshaped the world's economic governance and brought unintended consequences to third countries. As sanctions aim to change an aggressor's behaviour, their extraterritorial reach and reliance on financial chokepoints impose often heavy burdens on uninvolved states. Countries that decided not to join sanctioning coalitions must manoeuvre compliance demands, bear economic collateral damage and adjust to shifting regulatory landscapes - often with no or limited influence over the sanctions' design or objectives. The asymmetry is clear, and so it raises urgent questions about global economic and financial order and its impact on the economic security of countries across the globe.

3. ECONOMIC SECURITY OF THIRD COUNTRIES

Economic security is a state's ability to sustain its economic resilience and autonomy, especially in the face of an increasingly volatile international economic and security environment. Third countries, in order to preserve their economic security, need to ensure the stability of their financial systems, access to global trade routes and markets, safeguard supply chains and maintain investment flows. This multidimensional nature of economic security reflects the interconnected global economy.

Economic security has gained renewed importance as geopolitical competition, especially between the G7 and China, has escalated. The weaponisation of finance and trade has become an increasingly important dimension of global relations. Sanctions, one of the tools used to project economic pressure, are intended to influence the behaviour of a specific country, individual or entity, but they also have severe consequences for other international actors.

The United States has projected its economic power on global actors for years - and this is accelerating under President Trump's administration. The EU has increasingly sought a coordinated approach. Its June 2023 Economic Security Strategy reflects this shift. The European Union's three-pillar response - enhancing competitiveness, managing risks and partnering with like-minded states - mirrors broader G7 efforts (European Commission, 2023).

All those measures have externalities for third countries, especially in the Global South. The sanctions regime against Russia intensified the impacts of these measures. Third countries also became more aware of their own exposure to coercive economic tools. Many states find themselves caught between competing economic giants. As such, they need to balance the threat of secondary sanctions, the risk of losing access to correspondent banking services, and loosening political alliances, while juggling their own unique geopolitical and security challenges.

In response, third countries have shown a range of behaviours. Some comply under duress, realigning trade and financial relationships to avoid penalties. Other countries choose a silent disengagement, gradually reducing exposure to sanctioned entities without overt political repositioning. Another group, against sanctions, pursues deeper trade relations with sanctioned countries and entities - essentially benefiting when other countries disengage with sanctioned countries and entities. All those types of responses demonstrate that, for third countries, adaptation is a fundamental aspect of their long-term resilience, especially considering increasing geopolitical rivalry.

4. ARMENIA

4.1. Geopolitical Context

Armenia has a distinct set of geopolitical vulnerabilities and constraints that significantly shapes its approach to international sanctions regimes and its own economic security. With only two of four international borders open - those with Georgia and Iran - Armenia remains physically and economically isolated from key regional trade routes. Armenia's highest security priority is the unresolved conflict with Azerbaijan over Nagorno-Karabakh. The war, which reignited in recent years, disrupted economic planning and complicates efforts to forge stable regional economic relations. Additionally, Armenia has a small, trade-dependent economy. All those factors place Armenia in a uniquely challenging position when responding to G7 sanctions on Russia.

Armenia has long pursued a diversified foreign policy strategy aimed at balancing relations among regional powers - Russia, Iran, the West and its neighbours - yet this balancing act is fraught with contradictions and limitations. The protracted conflict with Azerbaijan has resulted in both human and economic insecurity and deepened Armenia's reliance on traditional partners such as Russia and Iran for military and economic support. Another challenge is Armenia's relationship with Türkiye. A closed border and a lack of formal diplomatic ties since the 1990s undermine Armenia's economic resilience. Even though the recent negotiations suggest a cautious willingness to normalise relations, the pace and scope of this rapprochement are vague, hindering its immediate economic benefits.

On Iran, relations have strengthened, especially after the 2020 Nagorno-Karabakh War, with both countries deepening infrastructure and energy cooperation. These developments have bolstered Armenia's resilience but also tether it more closely to actors that are themselves targets of Western sanctions. Such alignment, while strategic, risks complicating Armenia's positioning in relation to Western partners and its obligations under international sanctions regimes.

Russia, historically Armenia's most significant economic and security partner, continues to dominate Armenia's external economic landscape. The surge in bilateral trade, growing from $2.6 billion in 2021 to $12.4 billion in 2024 (Statistical Committee of the Republic of Armenia, 2021), has raised international concern about Armenia's potential role as a transshipment hub, used to circumvent sanctions against Russia. There are very few proved cases of the circumvention of G7 sanctions involving Armenia (Pambukhchyan, 2024), yet reputational risks persist, with disinformation campaigns further undermining investor confidence (Mamulashvili & Redlowska, 2025). Meanwhile, remittance flows and financial interdependence through Russian banking channels - especially important due to the Armenian diaspora in Russia - highlight the enduring depth of this bilateral relationship.

Despite these entanglements, Armenia is looking to strengthen its ties with the West. The signing of a Strategic Partnership Charter with the U.S. and the initiation of EU visa liberalisation talks mark symbolic steps towards greater Western integration. However, a gap between political alignment and economic reality is striking: Western economic engagement lags significantly behind that of Russia and Iran. No comparable investments or infrastructure initiatives have emerged from the European Union or the United States, underscoring Armenia's continued dependence on actors with divergent strategic agendas (Campbell, 2024).

Ultimately, Armenia's foreign policy posture reflects the broader dilemma faced by many third countries manoeuvring between conflicting geopolitical and economic pressures. Its case shows how unresolved conflicts, limited economic diversification and asymmetrical regional ties can constrain the capacity of smaller states to engage meaningfully in sanctions enforcement without jeopardising their own security and economic stability.

4.2. Armenian Sanctions Framework

The legal architecture of Armenia's sanctions regime is rooted in a relatively recent framework that reflects the country's efforts to respond to a dynamic global security landscape, especially in the wake of Russia's full-scale invasion of Ukraine. The base of it is constituted by the Law on Control of Export and Interstate Transit of Dual-Use Goods and Technologies through the Territory of the Republic of Armenia, supported by Government Decree No. 924-N (2010) and No. 1785-N (2011). These legal acts together constitute the primary legal framework for the regulation of trade of dual-use goods that may have both civilian and military applications and are the cornerstone of Armenian sanctions framework.

Under these regulations, any individual or business operator exporting dual-use items must obtain an appropriate licence from the State Revenue Committee. The classification of such items follows the European

Union’s dual-use control list, which Armenia updates periodically to maintain alignment with evolving EU standards. In 2023, Armenia adopted Government Decree 808-N - this decree enhances its export-control mechanisms. It was designed to strengthen screening and compliance processes, particularly in response to concerns about sanctions evasion through re-exportation.

The Ministry of Justice has a lead role in harmonising national legislation with evolving guidance from the European Union and OFAC. In 2023, the government created interagency committee on AML/CFT and PF chaired by the Governor of the CBA. This format coordinates sanctions-related policy implementation, enforcement and diplomatic liaison efforts. It brings together key actors from the Ministry of Economy, Ministry of Foreign Affairs, the Central Bank of Armenia (CBA) and the State Revenue Committee, in an effort to institutionalise a whole-of-government response.

Customs authorities in Armenia are at the forefront in the enforcement of export control regulations. This results in operational challenges, particularly in monitoring dual-use goods and detecting attempts to manipulate Harmonized System (HS) codes - a common tactic used to obfuscate the nature of exports. Both negligent infractions and deliberate schemes have been reported, often involving complex trade chains that exploit Armenia’s membership in the Eurasian Economic Union (EAEU), where intra-union goods movement is not subject to rigorous customs checks.

To address these challenges, customs authorities have adopted electronic invoicing and transit declarations for goods destined for EAEU countries. Nevertheless, enforcement remains inconsistent due to limited capacity, understaffing and a lack of sector-specific knowledge among customs agents and logistics intermediaries (Mamulashvili & Redlowska, 2025). Given these challenges, continued technical assistance is needed, particularly in HS code verification, risk profiling and real-time trade analytics, as well as increased private-sector education and outreach. This should be offered by G7 countries to support the effort of the Armenian government to comply with sanctions on Russia.

4.3. Financial System Architecture and Its Vulnerabilities

Armenia’s financial system has undergone a major recalibration as it attempts to reconcile international compliance obligations with its domestic economic realities and longstanding dependencies. The CBA has played a central role in this effort. It issues internal compliance benchmarks, conducts supervisory audits and promotes the adoption of OFAC-aligned risk management tools. However, systemic risks remain due to Armenia’s deep financial, economic and demographic ties with Russia and Iran.

One example is the presence of VTB Bank (Armenia), the wholly owned Armenian subsidiary of the sanctioned Russian bank VTB. The bank is included on U.S. sanctions screening lists and operates under restrictions linked to its parent company’s designation, while continuing to play a role in facilitating remittance flows between Russia and Armenia. Another example is Bank Mellat, an Iranian bank operating in Armenia that is subject to U.S. sanctions. Due to these sanctions, it is restricted in its access to international financial systems and primarily conducts transactions outside U.S. dollar–based channels, including currency exchange and other non-dollar-denominated operations.

When the G7 sanctions coalition sanctioned major Russian financial institutions, Armenian banks experienced a sudden loss of correspondent banking relationships. This led to an urgent rewiring of the Armenian banks, although no new relationships were offered by G7 banks. While one American bank continues to support a limited channel, Western financial institutions have generally adopted a risk-averse posture, exacerbating the de-risking trend and limiting Armenia’s access to international financial markets.

The financial intelligence unit (FIU) in Armenia plays a key role in identifying and mitigating the risks of sanctions evasion. The main tool used for this purpose is the Suspicious Transaction Report (STR) framework, which is integrated into the broader anti-money laundering (AML) and countering the financing of terrorism (CFT) framework. STRs are triggered by suspicion of criminal activity or concealment of sources of funds. The FIU maintains regular communication with international counterparts via the Egmont Group (Mamulashvili & Redlowska, 2025).

4.4. Unintended Consequences of G7 Russia Sanctions Regime

The Armenian private sector - particularly small and medium-sized enterprises (SMEs) - has been disproportionately affected by sanctions-related enforcement and the overcompliance of global partners. Prior to the war in Ukraine, many Armenian businesses depended on Russian banks and virtual marketplaces such as Wildberries and Ozon to access EAEU consumers. These platforms remain key channels of trade, especially in the absence of comparable Western alternatives.

However, post-sanctions enforcement has made it increasingly difficult for SMEs to conduct international transactions, as Armenian banks are now required to perform enhanced due diligence, including verifying end-users of products, before approving even low-risk transfers. Many SMEs report delays, rejections and increased costs as a result, while larger firms often navigate these hurdles through their global networks(Mamulashvili & Redlowska, 2025).

As already mentioned, sanctioned financial institutions such as VTB and Bank Mellat remain excluded from the international financial system. Increasingly, many problems for Armenian enforcement efforts relate to informal cash flows and cryptocurrency-based payments, which remain under-detected.

Sector-specific impacts have been particularly pronounced in Armenia's technology industry, a pillar of national development policy. Multiple Western technology suppliers - including Digi-Key and Mouser Electronics - have ceased exports to Armenia, because of potential re-exportation to Russia. This development impacted the domestic innovation ecosystem, constrained production capabilities and discouraged venture investment.

Amid these challenges, as well as ahead of the upcoming MONEYVAL evaluation this year, the Armenian government has institutionalised public–private cooperation through the interagency committee, which now includes business associations, financial compliance officers and civil society representatives. It aims to foster dialogue, transparency and regulatory predictability. As in the case of many MONEYVAL member states, the international community (in particular, the European Union which is currently adopting an ambitious AML framework), should further support Armenia in development of typologies and public–private data sharing. The governmental efforts in this field demonstrate intent in sanctions compliance, but the resources and capacities of a relatively small economy are not sufficient to address the complexity of global financial flows. Externally imposed sanctions have evidently intensified Armenia's structural vulnerabilities and placed new pressure on its resources and already-delicate economic-security equation. It is true that Armenian institutions have taken meaningful steps to align with international sanctions enforcement. However, the G7 should view these efforts through the lenses of constrained choices and longstanding regional dependencies. The economic shockwaves - felt most acutely in the financial sector and among SMEs - highlight not just Armenia's exposure, but the insufficiency of external support to offset them.

Crucially, Western partners, particularly the European Union, have yet to offer a compelling economic alternative to Armenia's reliance on Russia and Iran. Political gestures of alignment have not been matched by market access, investment or infrastructure support that could help to reorient Armenia's economy westward and strengthen alignment with G7 financial frameworks. Given Armenia's status as an EU neighbourhood country and its demonstrated willingness to engage, the European Union must act more strategically. A more robust and attractive economic partnership would not only support Armenia's resilience under sanctions pressure but also strengthen the European Union's broader interests in a stable, democratic and economically secure South Caucasus.

5. SOUTH AFRICA

5.1. Geopolitical Context

After the end of Apartheid, South Africa has pursued a foreign policy based on multilateralism, neutrality and balancing between global powers. Economically, it partners with blocs and countries such as the European Union and the United States, but also with emerging powers such as China and India. It has complex relations with Russia - during the Cold War, the Soviet Union supported the African National Congress in its fight against Apartheid. As a result, there is a sense of historical solidarity between Russia and many current South African leaders. Some of them still have longstanding ideological and personal ties with Russia. However, despite strong political ties, economic links are inconsequential.

South Africa is the third-largest African economy. Its main trading partners are China, the United States, Germany, India and the United Kingdom (World Bank, n.d.). Under the African Growth and Opportunity Act, the country benefits from free trade with the United States. Its economy is diversified, and key sectors include mining, manufacturing and finance. South Africa’s strategically significant but modest arms industry is particularly relevant to sanctions discussions. South Africa is not a major global exporter, but it produces advanced systems such as armoured vehicles, artillery, missile systems and electronic warfare technology. Denel SOC Ltd, Paramount Group, Rheinmetall Denel Munition and ARMSCOR are the main South African arms producers. The financial sector is also important in the sanctions discussion. It contributes roughly 20% to GDP and is among the most developed in Africa, with Johannesburg serving as a regional financial hub.

Politically, South Africa positions itself as a promoter of democracy, human rights and peaceful conflict resolution. This policy is rooted in its post-Apartheid identity. The country often takes a lead in cross-African initiatives and supports African Union regional peacekeeping. Outside Africa, the country associates with the Global South, advocating for reform of international institutions, including the United Nations Security Council and the International Monetary Fund. In 2010, to strengthen diversification of its foreign policy, South Africa joined BRICS. Within the organisation, it often positions itself as a gateway to African markets and a voice for African interests, but the size and weight of its economy is small compared with other members.

South Africa's geopolitical stance has direct implications for sanctions implementation. It enforces only UN-mandated sanctions, rejecting unilateral measures, including G7 sanctions on Russia. This has posed a strategic dilemma for Pretoria, which continues to seek a balance in the face of rising geopolitical competition among the main global powers. Furthermore, the practical necessity to implement sanctions by South African financial institutions and the strongly neutral or even pro-Russian stance of political elites has created an internal divergence.

5.2. South African Sanctions Framework

South Africa's sanctions regime is primarily reactive to UN-mandated sanctions and anti-terrorism obligations, but it can also reflect the country's domestic and foreign policy decisions. The President plays a central role in enacting sanctions domestically through the regulations that can be introduced. The legal basis for sanctions implementation lies mainly in the Protection of Constitutional Democracy Against Terrorist and Related Activities Act (2004), which criminalises terrorist financing but does not extend to unilateral or secondary sanctions that are not endorsed by the United Nations Security Council. The United Nations Act 49 of 1947 empowers the President to make regulations to comply with any decision of the United Nations Security Council under Chapter VII of the UN Charter, including economic and arms sanctions. There are also other legal documents that support this domestic framework which regulate the implementation of targeted financial sanctions, especially per the Financial Action Task Force (FATF) recommendations, and to enforce trade-related sanctions (Financial Intelligence Centre Act 38 of 2001) and import and export restrictions related to arms embargoes or dual-use goods (Customs and Excise Act 91 of 1964).

The lack of a legal framework regulating other sanctions regimes results in South African regulators and financial institutions operating in a grey area: they are legally unbound by Western sanctions but must contend with the global dominance of Western-led financial infrastructure, particularly the U.S. dollar system. Some effort has been made by the South African Reserve Bank and the Financial Intelligence Centre (the South African FIU) to provide guidance based on AML/CFT compliance. In practice, this encourages cautious engagement with sanctioned entities - even in the absence of a domestic legal requirement to do so. Overall, this tension creates ambiguity for both public and private actors, as they must navigate between legal permissibility and systemic exposure to foreign regulatory regimes.

5.3. G7 Russia Sanctions in Practice

The de facto extraterritoriality of G7 Russia sanctions has created a multi-layered challenge for South African firms, particularly in banking, insurance and logistics. Several major banks have adopted over-compliance strategies - terminating or limiting transactions involving Russian or other sanctioned entities - not because of domestic legal obligation, but due to fears of losing access to correspondent banking, dollar clearing or being de-risked by international partners. This over-compliance is noticeable especially among institutions with strong links to U.S. and UK financial systems, as the threat of reputational damage has a strong chilling effect on them. The threat of a potential OFAC response has led to de-risking, significantly constraining commercial discretion (Allison, 2024).

Following the government's policy of neutrality on the Russian invasion of Ukraine, South African domestic supervisory and regulatory bodies have not provided specific guidance to domestic financial institutions and operators on how to respond to the extraterritoriality of G7 Russia sanctions. The guidance that is available focuses on AML and CTF measures under the FATF. Following South Africa's grey listing by the FATF in February 2023, the government committed to a 22-point Action Plan to resolve the identified deficiencies. Its implications have limited relevance to Russia sanctions, but grey listing itself is another factor that is part of the G7 sanctions trajectory. The South African financial sector remains concerned that the country's reputation for financial crime control could deteriorate further if a South African bank were subject to secondary sanctions, as this would amplify the threat of losing access to the international financial system.

The increasing link between the circumvention of the G7 Russia sanctions and other sanctions regimes - for example, targeting terrorism financing and proliferation financing - adds an interesting dimension. Russia's deepening relationship with North Korea and Iran - a potential nexus for the proliferation of conventional and nuclear weapons - has also become more frequent concern (Keatinge, 2023) This development challenges South Africa's current sanctions posture and raises the question of whether it should treat Russia-related sanctions circumvention with the same seriousness as violations of United Nations Security Council sanctions - particularly given the growing nexus between the two - and consider this alignment when seeking to ensure compliance with its UN obligations.

It raises questions about whether to approach Russia sanctions in the same way as violations of the United Nations Security Council's North Korea sanctions - and would therefore be acknowledged by the South African government, and vice versa.

Another challenge relates to the production of dual-use goods. Many South African producers lack the sophisticated expertise and resources to apply trade-related sanctions effectively (Keatinge & Redlowska, 2024). As one RUSI workshop participant noted, "a lot of the banking industry does not know how to apply sanctions in a trade environment." This lack of clarity is evident among SMEs, as they are now increasingly exposed to sanctions risks. The increased exposure does not match their resources, institutional knowledge or the support they receive from national regulators. It therefore creates gaps that might lead to South African businesses being involved in circumvention. It also increases tension between financial institutions and their clients. The former prioritises correspondent banking relations; the latter prioritises increased business opportunities and profit making.

5.4. Unintended Consequences and Their Impact on Economic Security

The G7 sanctions on Russia have triggered an economic security challenge for South Africa. Choosing not to align with Western sanctions presents hazards to the private sector, especially financial services. Broad support and application of those sanctions is against its balancing strategy and may also shake the fundamentals of its economic resilience. The dilemma is distinct. At the same time, the country is grappling with urgent economic pressures. The need for job creation and sustainable economic growth is central, particularly for a young and growing population. The impact of sanctions, following closely after the Covid-19 pandemic, has added to inflationary pressures and rising interest rates, worsening the financial situation for many, especially low-income and indebted households.

The private sector in South Africa remains in a difficult position - legally required to follow domestic laws, which do not incorporate G7 sanctions, while also needing to maintain vital international banking relationships. Efforts to strengthen financial crime controls, such as enhancing beneficial ownership transparency, are underway. These are partly driven by the country's attempt to exit the FATF grey list. However, these improvements only offer partial relief. Domestic operators are steering through uncertainty due to an absence of explicit and region-specific guidance from international partners. Most available information on sanctions compliance is designed for European or American contexts and does not adequately reflect African realities (Allison, 2024).

To address these tensions, G7 diplomats must recognise and engage with the economic security priorities of Global South countries. For many of these governments, economic stability is a matter of survival, and as such, their policy decisions - regardless of ideological stance on sanctions - will ultimately be shaped by national interests tied to economic resilience.

It is also important to promote a better understanding among the populations of South Africa and other countries of the Global South about the connection between the implementation of G7 sanctions and their economic stability. By shining a light on the scope and purpose of G7 sanctions, the West can encourage greater engagement from civil society, which in turn can help to foster a more informed dialogue and scrutiny of policymakers' decisions (Keatinge & Redlowska, 2024).

But the sanctions coalition should also incentivise correspondent banks to apply a more fine-tuned approach and transparent, tailored communication to support South African financial institutions - keen supporters of G7 sanctions compliance - as they are the key to effective implementation in their home country.

6. G7 PERSPECTIVES ON THIRD COUNTRIES

The G7 sanctions coalition over the past three years has been fully conscious of the unintended consequences that its Russia sanctions regime has had on third countries. However, these costs are subordinated to the broader geopolitical objectives. Maintaining pressure on Russia, an aggressor country that violated international law and threatens transatlantic security, remains the main concern. The repercussions include disruption in trade and financial flows. Such flows then have an impact on political alignments and choices of states not directly targeted. This decision to accentuate sanctions reflects a deeper tension in the G7's strategy: how to apply coercive economic measures in relation to the stability of the global economic system. In doing so, the G7 walks a tightrope.

This strategic ambiguity extends to how economic security is conceptualised. While G7 countries increasingly frame sanctions as essential tools of economic statecraft, there is limited appreciation for the fact that third countries interpret economic security through fundamentally different lenses - ones shaped by their own economic development, dependency risks and exposure to great-power rivalry. As a result, third countries often perceive the sanctions regime less as a tool for upholding international norms and more as an externally imposed risk that they must navigate with limited institutional capacity and political space.

To address this misalignment, G7 states should consider integrating third-country concerns into the design and implementation of sanctions regimes and offer a more engaged communication on its theory of change. This includes offering technical and financial support to help non-target states to manage compliance risks, and improving coordination across multilateral institutions to reduce the fragmentation of the global financial system. Strategic buy-in also requires political work. The G7 should engage with political elites in countries - such as South Africa - that traditionally align with Russia or express scepticism towards Western policy frameworks by stressing global interests in financial transparency and institutional integrity. Linking unilateral sanctions enforcement with broader UN sanctions circumvention efforts could provide an entry point for cooperation.

Moreover, societies in third countries need to see a clear connection between alignment with sanctions and the long-term resilience of their own economies. Public diplomacy and targeted assistance should highlight how responsible economic governance and sanctions compliance can create conditions for greater investment, market access and integration into diversified global supply chains. Doing so does not dilute the coercive power of sanctions - it strengthens their legitimacy.

7. THE THIRD COUNTRY PERSPECTIVE: A SYNTHESIS

For third countries, dancing (or not) in step with unilateral sanctions of global powers is not merely a question of compliance or resistance. It reflects a structural shift that diminishes the political and economic space for neutrality. In a global economy increasingly shaped by extraterritorial enforcement, non-alignment is becoming economically costly. South Africa's experience - balancing rhetorical neutrality with growing pressure from Western financial institutions and compliance risks - illustrates how difficult it is for third countries to remain on the sidelines.

In the end, "it's the economy, stupid!" For most policymakers, economic security, not ideology, is the principal driver of policy choices. Countries such as Armenia may try to balance Western and non-Western actors. But their ultimate calculus hinges on the stability of trade flows, access to financial infrastructure, and how their populations perceive the impact of sanctions on the domestic economy. Their willingness to align or hedge is often reactive, shaped by which actors are seen as more credible guarantors of economic stability.

Third countries' choices have consequences for the global order. Non-UN mandated sanctions serve to extend the economic governance power of advanced economies. And consequently, they trigger counter-responses. Efforts to build alternative financial systems - from de-dollarisation initiatives to regional payment systems - are partly rooted in the need for third countries to regain agency in a sanctions-dominated environment (Keatinge, 2023). They are signals of systemic shift and are viewed by the West as threats.

In response, third countries should adopt a proactive strategy. Building domestic capacity for sanctions compliance and financial risk assessment is essential. Diversifying trade and financial partnerships can help to reduce over-reliance on exposed channels. At the same time, regional and multilateral forums offer platforms for articulating and defending economic security interests. These venues should be used not just reactively, but as arenas for drawing the contours of future sanctions governance. Where appropriate, third countries can leverage G7 demands to secure improved market access, investment assurances and capacity-building support.

Sanctions are no longer peripheral instruments - they are central to how economic security is defined and contested globally. The experiences of third countries reveal a shifting landscape in which power, vulnerability and alignment are being renegotiated. A more sophisticated sanctions strategy - one that balances coercion with credible engagement - is urgently needed. Without it, there is a real risk of destabilising the very international order sanctions are meant to defend.

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